# Chapter XII

# BROWNFIELDS & BUSINESS TRANSACTIONS

## A. Business Transactions

Since a purchaser of real estate or corporate assets may take on environmental liabilities, it is important to conduct environmental due diligence prior to purchase in order to avoid these liabilities. Further, "innocent purchaser" and other defenses may not be available unless an owner exercises due diligence prior to acquisition.

As a general rule, the present owner of property contaminated with hazardous substances is liable for cleanup under CERCLA §107(a), 42 U.S.C. §9607(a). Further, under the common law, a purchaser may be liable for cleanup of contamination existing at the time of purchase, even if he did not cause the situation, if "upon learning of the nuisance and having a reasonable opportunity to abate it" the purchaser fails to do so. *New York v. Shore Realty Corp.*, 759 F.2d 1032, 1050 (2d Cir. 1985).

At a minimum, a purchaser should comply with the "innocent purchaser" defense under CERCLA by conducting a Phase I environmental site assessment. A Phase I study normally includes a site inspection, research on the site history (including a Freedom of Information search of government authorities, and review of available data bases, abstracts of title and historic maps and aerial photos), and interviews, but usually no testing. If the Phase I identifies recognized environmental conditions of concern, it may recommend Phase II study involving soil or groundwater testing. It is prudent for a site owner to require the purchaser to sign a site access agreement, which requires insurance coverage for persons coming onto the site, an indemnification for any damages, and split samples on request.

A Phase I or II study may also be prudent for the seller to conduct prior to putting their property up to sale. If a purchaser later determines a need for a cleanup, that may open the seller up to claims under environmental statutes. *Channel Master Satellite Systems, Inc. v. JFD Electronics Corp.*, 702 F. Supp. 1229 (E.D.N.C. 1988); *Umbra U.S.A., Inc. v. Niagara Frontier Transportation Authority*, 262 A.D.2d 980, 981, 693 N.Y.S.2d 371, 372 (4th Dep't 1999). However, conducting a study may trigger the obligation to report a spill to an environmental agency, so that some property owners that suspect their property is contaminated would rather "moth ball" their site and not open a Pandora's box. If a buyer relies on the seller's study, the buyer should make sure it gets certified to the buyer so that the buyer can complain to the environmental consultant if an error is made.

Under CERCLA, persons who "did not know and had no reason to know" about hazardous substances at the site can qualify as "innocent purchasers" exempt from liability. CERCLA §101(35)(A)(i), 42 U.S.C. §9601(35)(A)(i). In order to qualify as an "innocent purchaser," it must be shown, among other things, that the purchaser had "carried out all appropriate inquiries… into the previous ownership and uses of the facility in accordance with generally accepted good commercial and customary standards and practices." CERCLA §101(35)(B), 42 U.S.C. §9601(35)(B).

For purchases between May 31, 1997 and November 1, 2005, when EPA promulgated a new standard, a Phase I Environmental Site Assessment complying with ASTM Standard E1527-97, entitled "Standard Practice for Environmental Site Assessment: Phase 1 Environmental Site Assessment Process," was sufficient to meet due diligence requirements under the defense.

EPA promulgated a new standard, effective November 1, 2006, which is set forth at 40 C.F.R. Part 312 setting standards for Phase I ESAs. Beginning on November 1, 2006, either ASTM Standard E1527-05, or the new "All Appropriate Inquiry" standards set forth in the regulations, must be used. The study must be completed within one year of property acquisition, except that certain aspects must be updated within 180 days of closing. 40 C.F.R. §312.20.

Lenders are particularly concerned about giving mortgage loans on contaminated properties, since they may take on CERCLA liability if they foreclose on contaminated property. Under CERCLA §101(20)(A), 42 U.S.C. §9601(20)(A), holding a mortgage does not, in and of itself, make a lender an "owner" subject to CERCLA liability, provided the lender does not "participate in management" of the facility. CERCLA §101(20)(E)(i), 42 U.S.C. §9601(20)(E)(i). Moreover, lenders who take title after foreclosure may also be protected if they seek to sell "at the earliest practicable, commercially reasonable time." CERCLA §101(20)(E)(ii), 42 U.S.C. §9601(20)(E)(ii). A similar defense is provided under the New York State Superfund Law, ECL §27-1323, and New York Oil Spill Law. Navigation Law §181(4)(b).

However, if a bank gives a mortgage loan on contaminated property, it may be left with not collateral. Thus, lenders will typically require a Phase I environmental site assessment (and if necessary a Phase II) prior to giving a mortgage loan, and often prior to bringing a foreclosure action.

Environmental liens are a particular concern. Some states have "superlien" laws, which allow the state to file a lien for environmental cleanup costs that takes priority over earlier mortgages and other liens. Under CERCLA §107(l), 42 U.S.C. §9607(l), EPA can file a lien for

its response costs, but this does not supersede previously filed mortgages. Many states have similar lien provisions, such as the New York Oil Spill Law. *See* New York Navigation Law §181-a.

Generally, "[t]he mere silence of the seller, without some act or conduct which deceived the purchaser, does not amount to a concealment that is actionable as a fraud," so "[t]he buyer has the duty to satisfy himself as to the quality of his bargain pursuant to the doctrine *caveat emptor*." *London v. Courduff*, 141 A.D.2d 803, 804, 529 N.Y.S.2d 874 (2d Dep't 1988), *lv. dis'd* 73 N.Y.2d 809, 537 N.Y.S.2d 494 (1988). That is another reason why environmental due diligence is prudent prior to purchase. Nonetheless, in some situations there is a duty to disclose defects to a buyer, even if no inquiry is made. *See Stambovsky v. Ackley*, 169 A.D.2d 254, 572 N.Y.S.2d 674 (1st Dep't 1991).

Furthermore, after closing on a real estate sale, the doctrine of merger is generally a bar to claims arising out of a purchase and sale contract. *White v. Long*, 204 A.D.2d 892, 612 N.Y.S.2d 482 (3d Dep't 1994), *rev. on other grounds*, 85 N.Y.2d 564, 626 N.Y.S.2d 989 (1995). Thus, it is in the buyer's interest to be sure that their purchase contract includes provisions such as representations and indemnifications with regard to environmental conditions that survive closing. *See, e.g. Avalon Realty, Inc. v. Baumrind*, 203 A.D.2d 185, 610 N.Y.S.2d 269 (1st Dep't 1994), *app. dis'd* 84 N.Y.2d 864, 618 N.Y.S.2d 8 (1994). While an "indemnification, hold harmless or similar agreement" is not effective to absolve a responsible party from CERCLA liability, such an agreement is enforceable to seek contribution between the parties. CERCLA §107(e), 42 U.S.C. §9607(e); *Olin Corp. v. Consolidated Aluminum Corp.*, 5 F.3d 10 (2d Cir. 1993).

It may also be prudent for a buyer or lender to minimize their risk by obtaining environmental impairment liability insurance at the time of closing. If contamination is identified but the purchaser still wants to proceed, options include an indemnification provision, "cost cap" insurance, an escrow for the anticipated remedial costs, and leasing the property with an option to buy once the EPA or other regulatory authorities approve the cleanup, such as by a "no further action" letter.

### B. Brownfields

Brownfields are real property, the expansion, redevelopment, or reuse of which may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant. Cleaning up and reinvesting in these properties takes development pressures off of undeveloped "greenfields," and both improves and protects the environment.

Often, brownfields will be well-located, and available at low prices that provide an opportunity for profitable development. The brownfield developer may be able to utilize incentives available from many states for grants, loans and/or tax credits. In addition, the developer may be able to bring suit to recover remedial costs from former owners and operators.

While EPA has an extensive brownfield program, it chiefly involves spreading information about brownfields, and providing funding to local governments. Many cities use this money to fund studies of potential development sites.

Many states have their own brownfield program. In 2003, the New York State Legislature created the Brownfield Cleanup Program (BCP), which is primarily set forth in Title 14 of New York Environmental Conservation Law Article 27. The law, which is administered by the New York State Department of Environmental Conservation (DEC), provides a process

for voluntary cleanup of sites contaminated with hazardous waste or petroleum, rewarding the applicant with a liability release and tax incentives.

In order to go through the BCP and obtain the liability release and tax benefits, the volunteer or participant must follow a process established by the statute to investigate and remediate the site. Four different tracks are available which set the level of cleanup depending on the intended use of the property. In addition, there are a number of public notice requirements built into the BCP process that essentially force the developer to deal with land use planning issues at the same time as environmental remediation issues.

Generous tax incentives, which have been incorporated into Section 21 of the New York Tax Law, may constitute the best economic development incentives in the country at this time, and are already encouraging development on contaminated property. These tax credits apply to parties (either a true "volunteer" who is not liable under the law, or a responsible party "participant") who complete a cleanup project under the new BCP. Under the law as passed in 2003, the tax credits range from 10% to 22% of (1) site preparation costs, including investigation and cleanup; (2) tangible property costs, including building improvements, rehabilitation, demolition, electrical improvements and even landscaping; and (3) ongoing on-site water treatment costs for five years. In addition, the BCP provides significant real property tax credits, and a 50% credit toward the cost of environmental insurance or $30,000, whichever is less.

The definition of "brownfield site" set forth at ECL §27-1405(2) includes "any real property, the redevelopment or reuse of which may be complicated by the presence or potential presence of a contaminant." The purpose of the BCP is "to encourage persons to voluntarily remediate brownfield sites for reuse and redevelopment" in order to "achieve [] a permanent

cleanup of a contaminated site," eliminate the threat to "the health and vitality of the communities they burden, and avoid "sprawl development," in order to "enhance the health, safety and welfare of the people of the state of New York and their overall economic and social well being." ECL §27-1403.

In December 2006, DEC promulgated revisions to its regulations at 6 N.Y.C.R.R. Part 375. These revisions include the BCP in Subpart 3, as well as soil cleanup standards ("SCOs") in Subpart 6.

ECL §27-1405(2) sets the rules for eligibility for the BCP. Certain sites are ineligible, including sites that are on the NPL or Class 2 sites on the Registry of Inactive Hazardous Waste Disposal Sites, permitted RCRA sites, and sites subject to certain enforcement actions.

DEC interprets these rules in sections 2.1 through 2.5 of the DEC Draft Brownfield Cleanup Guide, revised in March, 2005, available on the DEC web site at http://www.dec.ny.gov/docs/remediation_hudson_pdf/bcp_eligibility.pdf. DEC has interpreted the statute as requiring that two elements are met: (1) the "contamination factor," and (2) the "complication factor." While some courts have upheld the Guidance, *377 Greenwich LLC v. DEC*, 4 Misc. 3d 417, 827 N.Y.S.2d 608 (Sup. Ct. N.Y. Co. 2006), in *Destiny USA Development, LLC v. DEC*, 2009 NY Slip Op. 4504, 2009 WL 1570205 (4th Dep't 2009), the Appellate Division, Fourth Department found that the Guidance "constitutes an impermissible attempt to legislate."

In light of the generous tax credits available under the BCP, DEC has been very slow to process applications, and set the bar very high for admission. Governor Spitzer, and then Governor Patterson, called for amendments to the statute. In June, 2008, the New York State Legislature capped the benefits for tangible property costs to of $35 million (or 45 million for

manufacturing projects), or three times the cost of the site preparation and on-site groundwater remediation costs, whichever is less. However, the site preparation credits were also increased, so they range from 20% to 50%.

Conflicting court decisions have been rendered on eligibility. Some have overturned DEC's interpretations as too restrictive. *Destiny USA Development, LLC v. DEC*, 2009 NY Slip Op. 4504, 2009 WL 1570205 (4th Dep't 2009); *HLP Properties, LLC v. New York State Department of Environmental Conservation*, 21 Misc.3d 658, 864 N.Y.S.2d 285 (Sup. Ct. N.Y. Co. 2008); *East River Realty Company, LLC v. New York State Department of Environmental Conservation*, 22 Misc. 3d 404, 866 N.Y.S.2d 537 (Sup. Ct. N.Y. Co. 2008). Others have deferred to DEC's decisionmaking. *Lighthouse Pointe Property Associates, LLC v. NYSDEC*, 872 N.Y.S.2d 766, 2009 N.Y. Slip Op. 00878 (4th Dep't 2009); *377 Greenwich LLC v. DEC*, 4 Misc. 3d 417, 827 N.Y.S.2d 608 (Sup. Ct. N.Y. Co. 2006). The *Lighthouse* case is under review by the New York Court of Appeals, and should resolve the eligibility issue and the meaning of the term "brownfield site."

Under another brownfield program, New York also provides extensive funding for remediation for municipal "environmental restoration projects," pursuant to Title 5 of ECL Article 56. Under this program, a municipality must take title, and the municipality and any purchaser will be indemnified for environmental liability by the state.