

**ELEVENTH ANNUAL
NORTHEAST SURETY AND FIDELITY CLAIMS
CONFERENCE**

**THE FINANCING SURETY'S POTENTIAL LIABILITY
FOR ENVIRONMENTAL ISSUES**

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by Robert M. Wright, Esquire

Financing the principal may expose the surety to liability for clean-up costs in cost recovery actions pursuant to the Federal Superfund Law¹ and under State hazardous waste laws as well as by reason of certain state common law actions.² There may also be liability based on a simple negligence action. These actions may claim as damages not only the cost of the clean-up but also emotional distress because of concern about exposure to toxic waste, damages for the financial burden of medical surveillance, and damages for interference with the quality of life.³ In order to properly understand these liabilities, it is important to understand the scheme of the federal superfund statute, hereafter referred to as CERCLA. The discussion which follows assumes that the bonded principal is not a Response Action Contractor specifically hired to clean-up hazardous waste.⁴

Bases of Liability Under CERCLA

Liability exists under CERCLA if the following exists:

A. The site is a "facility" under 42 U.S.C. §9601(9). This means virtually any building structure, equipment or impoundment that could hold hazardous material including a motor vehicle or aircraft.

B. The defendant is a responsible person under 42 U.S.C. §9607(a) as discussed below.

C. A release or threatened release of a hazardous substance has occurred; and;

D. The release or threatened release has caused the plaintiff to incur response costs and other statutory damages.⁵

¹ Comprehensive Environmental Response, Compensation, and Liability Act. 42 U.S.C. §9601 *et seq.*

² Some states have mini Superfund Laws. Common law actions may include the common law doctrine of ultrahazardous or abnormally dangerous activities and liability without fault under the common law doctrines of nuisance and trespass. *See New York v. Shore Realty Corp.*, 759 F.2d 1032 (2nd Cir. 1985); *State v. Ventron Corp.*, 94 N.J. 273, 468 A.2d 150 (1983). *Sterling v. Velsicol Chemical Corp.*, 647 F.Supp. 303 (W.D. Tenn. 1986).

³ *Ayers v. Township of Jackson*, 202 N.J. Super. 106, 493 A.2d 1314 (1985).

⁴ For a detailed discussion regarding the bonding of Response Action Contractors *see* Wright, Robert M. and Ryan, William F., Jr., "Hazardous Waste Liability and the Surety Revisited", 30 Tort and Ins. Law J. 741, 760 (1995).

⁵ Injury to natural resources and costs of any Health Assessment or Health Effects Study.

Liability is retroactive⁶ and the liability scheme is designed so that in all cases private resources pay for the clean-up. When all private responsible parties are not available the Superfund and not the taxpayer bears the cost.

Strict, Joint and Several Liability Under CERCLA – Due Care is No Defense

42 U.S.C. §9607 states that, notwithstanding any other provision or rule of law, and *subject only to the defenses set forth in CERCLA*, the following persons are liable under §9607(a).

A. “Owner” and/or “Operator” of the Facility including, where title has been conveyed to a unit of state or local government by reason of bankruptcy, foreclosure, tax delinquency, abandonment or a similar means, any person who owned, operated or otherwise controlled activities at such facility immediately beforehand. *The term does not include a person who, without participating in the management of a facility holds indicia of ownership primarily to protect their security interest in the facility.*⁷ The term does include any state or local government which has caused or contributed to the release or threatened release of a hazardous substance from the facility and such state or local governmental entity is subject to liability under the provisions of the chapter in the same manner and to the same extent, both procedurally and substantively, as any non-governmental entity. Owner or Operator includes the present property Owner as well as the Owner or Operator of the site at the time the waste was disposed of.

Operator liability only attaches if the defendant had authority to control the cause of contamination at the time the hazardous substances were released into the environment.⁸ A contractor in control of operations on the site is a potentially responsible party not only for placing contamination on the site, or being in control of the site at the time the contamination was placed, but also for exacerbating pre-existing contamination.⁹

B. “Arranger” Liability. Under §9607(a)(3) an Arranger is any person who “arranges” for disposal or transport for disposal or treatment of hazardous waste at any facility whether or not the waste is owned by that person or whether or not the facility is owned by that person. Disposal means placing of any hazardous waste on any land. It includes not only the initial introduction of hazardous material on the property but also exacerbating preexisting contamination. An arranger also includes anyone who accepts the hazardous waste for transport to a disposal or treatment facility selected by such person from which there is a release or threatened release.

⁶ CERCLA has been construed as imposing retroactive liability. *United States v. Olin*, 107 F.3d 1506 (11th Cir. 1997).

⁷ This is known as the Secured Lender Exemption.

⁸ *Nurad v. Hooper*, 972 F.2d 837 (4th Cir. 1992).

⁹ *Kaiser Aluminum v. Catellus*, 976 F.2d 1338 (9th Cir. 1992); *Ganton Technologies, Inc. v. Quadriion Corp., Inc.*, 834 F. Supp. 1018 (M.D. Ill. 1993); *Danella Southwest v. Southwestern Bell Telephone Company*, 775 F. Supp. 1227. (E.D. Mo. 1991).

C. “Transporter” Liability. A Transporter is one who accepts hazardous materials for transport to a site selected by the Transporter. It has been held that it is not required that the Transporter move the materials from one parcel of land to another. Transporter Liability may exist if the material is simply taken from a contaminated area on one parcel and disposed of on an uncontaminated area of the same parcel.¹⁰

Defenses

Other than an act of God or an act of war there is no liability if the Defendant can establish by a preponderance of the evidence that the release or threat of release and damages resulting therefrom were caused solely by an act or omission of a third party if the property was acquired after the hazardous substances were disposed of or placed. However, the Defendant must prove:

A. That it exercised due care with respect to the hazardous substance concerned in light of all the relevant facts and circumstances and;

B. It took precautions against foreseeable acts or omissions by any such third party and the consequences that could foreseeably result from such acts or omissions and;

C. That it had no reason to know that any hazardous substance was disposed of at the facility. To establish a lack of “reason to know” the Defendant must have undertaken at the time of the acquisition appropriate inquiry into the previous ownership and the use of the property consistent with good commercial or customary practice in an effort to minimize liability. The statute provides that the court will take into account that not only any specialized knowledge or experience on the part of the defendant but also the relationship of the purchase price to the value of the property if uncontaminated; commonly known or reasonably ascertainable information about the property; the obviousness of the presence or likely presence of contamination at the property; and the ability to detect such contamination by appropriate inspection.¹¹ As a practical matter, this means that the Defendant must conduct a Phase I environmental audit. This consists of a search of records to determine known environmental conditions on the property plus a physical inspection of the property.¹²

If the third party defense applies, once the Defendant knows of the release or threatened release if it transfers the property to another person without disclosing it then, that person is treated as liable and the innocent landowner defense is unavailable. Additionally,

¹⁰ *Kaiser Aluminum, supra* at 1343.

¹¹ 42 U.S.C. §9607(b)(3); 42 U.S.C. §9601(35)(A-D).

¹² A Phase II audit is a more detailed physical inspection including tests such as bulk asbestos analysis, underground storage tank tightness testing, surface soil sampling and analysis, and inspection of PCB-containing equipment. ASTM released a Phase II standard document in February, 1998 providing a model for these investigations. A Phase III environmental audit is done where the site conditions indicates high likelihood for on-site subsurface contamination. This involves soil borings and test pits for collecting subsurface soil samples as well as installation of ground monitoring network and hydrogeological characterization of ground water monitoring flow and quality.

even if the third party defense applies, the Defendant may remain liable under state law, as well as other federal statutes.¹³

Potential Contractor/Surety Liability – Conventional Construction Sites

There are certain high risk activities where a contractor and a surety can become exposed to hazardous Waste Liabilities if contamination is present. These include:

- A. Excavation and fill operations.
- B. Sediment discharge and stormwater runoff.
- C. Dewatering operations.
- D. Demolition activity.

It is obvious that all of these activities may disturb and exacerbate existing contamination creating potential responsibility for clean-up and liability for consequential losses.

Contract clauses can cause problems for the Contractor and its Surety by requiring them to deal with known contamination issues if there is no contractual exception excluding that responsibility. These clauses are:

A. Change order clauses making the contractor responsible to perform directed changes without notice to the surety.¹⁴

B. Underground conditions or differing site conditions clauses where the issue is not responsibility for a payment but responsibility for performing directed work. Note that in certain state contracts an acknowledgement is set forth where the Contractor acknowledges he has satisfied himself as to surface and subsurface materials including substances classified by the EPA as hazardous materials so he is clearly responsible for their removal if they are found.

C. Scope of Work and Performance Specification clauses. These can also require hazardous waste clean-up. Under the AIA Form 201 1987 Edition of the General Conditions, § 4.3.6 regarding claims for concealed or unknown conditions could be interpreted to require removal of hazardous waste if an equitable adjustment is granted. This is particularly true considering the provisions of Article 10 which excuse the Contractor from performing work related to asbestos or PCBs. It does not excuse the Contractor from work relating to other toxic materials. This defect has been eliminated in the 1997 AIA 201¹⁵ but the 1987 form is still being used by many Owners and Contractors.

¹³ For example, the Resource Conservation and Recovery Act.

¹⁴ *Active Fire Sprinkler Corp.*, 85-1 B.C.A. (CCH) ¶ 17,869 (GSBCA 1988) (where the Contractor was required to remove asbestos under the changes clause).

¹⁵ See, ¶ 10.3.

D. Under the Federal Acquisition Regulations, all fixed price construction contracts contain a "Permits and Responsibilities" clause which requires the contractor to be responsible for all damage to persons or property that occur as a result of the contractor's fault or negligence. The clause requires the contractor to take proper safety and health precautions to protect the work, workers, the public, and property of others. Obviously a broad reading of this clause could require the contractor to remediate hazardous materials thereby creating potential liability.

One ray of hope on all of these issues is the *Danella Southwest Case, supra* which found that a contract should be construed not to include CERCLA liability within the scope of a standard indemnity clause. By analogy, it can be argued that hazardous waste clean-up should not be read into the standard construction contract unless expressly provided for.

Lender Liability: An Analogy for the Contract Bond Surety

It is apparent that there are a number of ways in which a principal may incur environmental liability and cause that liability to be passed to its surety. The financing surety's exposure is analogous to that of a lender and others in the financial services industry. Potential environmental liability causes concerns for these entities including:

A. The risk that property subject to a security interest will require clean-up, which prospect diminishes its value or subjects it to a possible superceding governmental lien for the cost of clean-up;

B. The impact of clean-up costs on the principal's ability to perform or to reimburse the surety or to repay its loans.

C. The risk that an entity foreclosing after default will become an Owner/Operator subject to clean-up costs and;

D. The risk that Lender or Financing Surety which does not foreclose in a work-out situation may unwittingly become subject to CERCLA or state law liability by virtue of its involvement with the Principal/Borrower.

As previously noted, §9607 contains a secured lender's exemption. The term "Owner or Operator" is also defined under §9601(20)(A) and excludes:

"a person, who, without participating in the management of a vessel or facility, holds indicia of ownership primarily to protect his security interest in the vessel or facility."

Unfortunately, the 11th Circuit in an infamous opinion known as *The United States v. Fleet Factors Corp.*, 901 F.2d 1550 (11th Cir. 1990) *cert. denied* 498 U.S. 1046 (1991) generated alarm in the financial services industry because of its low threshold for holding a non-foreclosing secured lender liable under CERCLA. The 11th Circuit stated that a secured creditor could incur Superfund clean-up liability without being an Operator, by participating in the financial management of a facility to a degree indicating a capacity to influence the

borrower corporation's treatment of hazardous waste. The standard dramatically narrowed the scope of the secured lender exemption and broadened the potential liability of lenders, and by analogy contract bond sureties, who participate in the financial decisions of the borrower. While other cases did not necessarily follow *Fleet Factors* even the government became concerned by reason of the large number of properties being held by the FDIC in connection with the collapse of the savings and loan industry.¹⁶

As a result, in April 1992, the Environmental Protection Agency adopted a final rule defining the scope and operation of the CERCLA secured creditor exemption. EPA said the rule was a legislative substantive rule binding in private cost recovery actions brought by third parties as well as those brought by the Agency itself. The rule specifically sought to restrict *Fleet Factors* by defining "participation in management" as actual participation by the security interest holder in the management or operational affairs. It did not include the mere capacity to influence or the ability to influence or the unexercised right to control operations. The rule specified those actions that are not deemed participation in management. They included activities in policing the loan by undertaking a financial workout when the borrower's obligations are in default or a threat of default, or in foreclosing and preparing the facility for sale or liquidation, or in monitoring the borrower's business. The EPA said that to the greatest extent possible, the rule was intended to protect lenders against exposure to CERCLA liability for engaging in the "normal course of business".¹⁷ Unfortunately, in February 1994, the D.C. Circuit vacated the regulation as being beyond the authority granted to EPA under CERCLA.¹⁸ The EPA rule still represents current EPA and Department of Justice enforcement policy.¹⁹

Asset Conservation, Lender Liability and Deposit Insurance Protection Act of 1996

In 1996 the EPA's rule was codified in 42 USC 9601(20)(E) entitled "Exclusion of Lenders Not Participants in Management" which was an extensive addition to CERCLA's definition of "owner or operator." The definition of "owner or operator" excludes a person who, without participating in the management of a vessel or facility, holds indicia of ownership primarily to protect his security interest in the vessel or facility. The added section E is intended to codify the EPA's 1992 Lender Liability Rules rejecting the decision in *U.S. v. Fleet Factors*. This legislation provides the EPA with the statutory basis for the lender liability rules that the D.C. Circuit said was lacking when the regulations were promulgated in 1992. It should be noted that §9601(20)(E) does not by its terms protect the Lender from liability as a "Transporter" or as an "Arranger."

The statute provides that the term "owner or operator" does not include a person that's a lender that, without participating in the management of a vessel or facility, holds indicia

¹⁶ For an example of provisions commonly found in financing agreements between sureties and their principals which could give rise to liability under *Fleet Factors*, see, *James E. McFadden Co. v. Baltimore Contractors, Inc.*, 609 F.Supp. 1102, 1103-04 (E.D. Pa. 1985).

¹⁷ For further detail as to the regulation see Wright, *supra* at 756.

¹⁸ *Kelley v. EPA*, 15 F.3d 1100 (D.C. Cir. 1994).

¹⁹ The effect of Superfund on Lenders that Hold Security Interests in Contaminated Property (issued by the EPA's office of Site Remediation). This document was issued for use by EPA staff and reaffirms that EPA and the Department of Justice will follow the April, 1992 regulation when exercising enforcement discretion to determine whether lenders may be subject to enforcement actions under CERCLA. 27 B.N.A. Environmental Rep. 1059 (9/13/96). EPA's policy on interpreting CERCLA provisions Addressing Lenders states that EPA will consult the Rule as guidance in interpreting the secured lender exemption. 62 Fed. Reg. 36424, 2 (July 7, 1997).

of ownership primarily to protect the security interest of the person in the vessel or facility. “Lender” is defined to mean any person that makes a bona fide extension of credit to or takes or acquires a security interest from a non-affiliated person, or a person that insures or guarantees against the default and the repayment of an extension of credit or acts as a surety with respect to an extension of credit to a non-affiliated person.²⁰ “Security Interest” means any right accruing to a person to secure the repayment of money, the performance of a duty, or any other obligation by a non-affiliated person. The statute also states that “owner or operator” does not include a lender that did not participate in management of a vessel or facility prior to foreclosure. The phrase “Participation in Management” is defined to mean *actually participating in the management or operational affairs of a facility* and expressly does not include merely having the capacity to influence, or the unexercised right to control the facility operations. The statute further states the lender shall be considered to participate in management only if, while the borrower is still in possession of the vessel or facility and covered by the security interest, the lender exercises decision making control over environmental compliance related to the facility such that the Lender has undertaken the responsibility for the hazardous substance handling or disposal practices related to the facility or exercises control at a level comparable to that of a manager of the facility such that the Lender has assumed or manifested responsibility for the overall management encompassing day-to-day decision making with respect to environmental compliance or responsibility for all or substantially all of the operational functions (as distinguished from financial administrative functions) of the facility other than the function of environmental compliance.

Participation in management expressly does not include, among other things, monitoring or enforcing the terms and conditions of the extension of credit or security interest as well as exercising forbearance, or restructuring or agreeing to alter the conditions of the extension of credit, or exercising any other remedies that might be available under applicable law for the breach of a term or condition of the extension of credit or security agreement, all of which would be applicable to a financing agreement between a surety and its principal. After there has been a foreclosure on collateral security, the statute also grants protection similar to the EPA rule as discussed below.²¹

It is important to appreciate that while the Statute and EPA policy provide exemptions from “Owner or Operator” liability the exemptions do not prevent the holder of the security interest from being a “Transporter” or “Arranger” with respect to its actions, nor do they preempt the Holder’s potential liability under any other state or federal law to which the Holder is also subject. The bottom line is that where a surety knows of or suspects the presence of hazardous material on the job site, it must consider potential “Arranger” or “Operator” liability both with respect to its initial decision to finance and, in connection with the terms and conditions of its agreements with its principal and its actions in monitoring the principal’s activities. In certain cases the risk may dictate a rejection of the financing option. This is especially the case if the principal does not have insurance coverage for hazardous waste liability in sufficient amounts. The surety may be forced to consider Owner completion or

²⁰ In this connection, the 1992 EPA Rule defined “indicia of ownership” to mean evidence of a security interest or an interest in the security interest or an interest in real or personal property securing a loan or other obligation. Evidence of such interest included “surety bonds” 40 CFR §300.1100(a)(1)(1994).

²¹42 U.S.C. §9601 (20)(F)(iv)(I-IX).

tender or takeover with the new contractor providing adequate bonding and pollution insurance.²²

Holding and Foreclosing on Collateral Security²³

While it is obvious that mere holding collateral security is not a problem in and of itself under the secured creditors exemption, the difficulty is what happens when the surety executes on real estate either under collateral agreements or upon judgments against the principal and its indemnitors. In this situation, the surety is in the same position as a foreclosing bank. The problem was first illustrated in 1986 when the United States sued a bank that had foreclosed on a hazardous waste site following the default of the debtor.²⁴ The bank had held title for a year and the property was the subject of an EPA clean-up costing in excess of \$500,000. The court granted summary judgment as to liability and ruled that the third party defense did not apply. The third party defense is available if one can show that a release or a threat of release was caused solely by a third party other than an employee or agent of the defendant or one whose act or omission occurs in connection with a contractual relationship existing directly or indirectly with the defendant.²⁵ It is unclear whether the third party defense is available to a financing surety, or a surety not engaged in financing if the bonding relationship (contractual relationship) existed during the period when the act or omission causing the release took place, particularly if the deposit of the hazardous substance was in some fashion connected with the principal's business operation.

The 1992 EPA rule offered significant relief to sureties that found themselves holding a security interest in property containing hazardous waste. This rule provided that the secured lender exemption was not lost by foreclosure on the property and by certain post-foreclosure activities. It also included assignments of title in lieu of foreclosure, termination of a lease, any other repossession or acquisition of a right to title or possession, and agreements in satisfaction of the secured obligation by which the surety acquires title to or possession of the secured property. After foreclosure the exemption was not lost as long as the surety undertook to sell or otherwise divest itself of the property in a reasonably expeditious manner using a commercially reasonable means under all the facts and circumstances.²⁶ The protection of the EPA rule has again been codified in the Asset Conservation, Lender Liability, and Deposit Insurance Protection Act of 1996 as an amendment to 42 USC 9601 (20)(E). The statute states that foreclosure includes purchase at a sale under a judgment or decree, power

²² With respect to contractor's pollution insurance coverage see Answers to the Most Important Questions a Surety Can Ask About the Surety's Environmental Risk, Monograph of the Fidelity and Surety Law Committee, Law Division, Tort and Insurance Practice Section of the American Bar Association, 103 (Gavin and Wright, Eds. (1997).

²³ For an in depth discussion of this issue, see Welge, Mark A., *Environmental Concerns of the Surety Seeking Salvage* in SALVAGE BY THE SURETY (Bachrach, George J., Ed., ABA, Torts and Insurance Practice Section 1998).

²⁴ *United States v. Maryland Bank & Trust Company*, 632 F.Supp. 573 (D. Md. 1986).

²⁵ 42 U.S.C. §9607(b)(3). Moreover, for the defense to apply, the defendant must establish by a preponderance of the evidence that it exercised due care with respect to the hazardous substance concerned, taking into consideration the characteristics of such hazardous substance in light of all the relevant facts and circumstances and that it took precautions against foreseeable acts or omissions of any such third party and the consequences that could foreseeably result from such acts or omissions.

²⁶ 40 CFR §300.1100(d)(2)(j) (1992). The EPA rule provided that within 12 months following foreclosure, property must be listed with a broker, dealer or agent. For further details see Wright *supra* at 759.

of sale or nonjudicial foreclosure sale, as well as a deed in lieu of foreclosure or similar conveyance from a trustee or a repossession or a conveyance pursuant to an extension of credit or any other formal or informal manner by which the person acquires title to or possession of a facility to protect the security interest of the person. There is no owner or operator liability after foreclosure if the Lender sells, liquidates, maintains business activities, winds up operations, or undertakes an appropriate response action or takes other measures to preserve, protect or prepare the facility prior to sale or disposition providing the Lender seeks to sell or divest himself of the facility at the earliest practicable, commercially reasonable time, on commercially reasonable terms taking into account market conditions and legal and regulatory requirements.²⁷

Limitations on §9601(20)(E) and the Impact of the Supreme Court Decision in *United States v. Best Foods, et al.*²⁸

The problem of course is that these amendments apply only where the hazardous waste is on real estate which is subject to the surety's security interest. The statute does not in its terms protect the financing surety for the operations of its principal on third party property including the project site. However, the statute does provide the basis for the surety to argue that it is a statement of legislative intent that a financing party such as a surety should not be constructively deemed to be an "owner or operator" when it has not participated in the management of its principal to any greater extent than allowed by a traditional commercial lender.

In addition, the Supreme Court's decision in *United States v. Best Foods, et al.* indicates that the Court has rejected a "capacity to influence" test for purposes of determining who is a "owner or operator" under CERCLA. In fact, the Court commented that CERCLA's definition of a facility's "operator" as being "any person -- operating" the facility was essentially useless and stated that the terms should be given their "ordinary or natural meaning." The Court went to the dictionary definition and found that::

Under CERCLA, an operator is simply someone who directs the workings of, manages, or conducts the affairs of a facility. To sharpen the definition for purposes of CERCLA's concern with environmental contamination, an operator must manage, direct, or conduct operations specifically related to pollution, that is, operations having to do with the leakage or disposal of hazardous waste, or decisions about the compliance with environmental regulations. 118 S. Ct. at 1887

Best Foods involved an attempt by the government to impose derivative liability for the cost of cleaning up industrial waste upon a parent corporation for the acts of its defunct subsidiary.²⁹

²⁷ The Act does not contain a 12 month provision regarding sale after foreclosure as did the EPA rule.

²⁸ 524 U.S. 51; 118 S. Ct. 1976 (1998).

²⁹ There was a split in the Circuits, with the 4th Circuit indicating that a parent could be liable if it had "authority to control" the hazardous waste facility. *Nurad, Inc. v. William E. Hooper*, 966 F.2d 837 (4th Cir. 1992). The 5th and 6th Circuits indicated that to hold a parent liable the state law standards for piercing the corporate veil would have to be satisfied. *U.S. v. Cordova Chemical Co. of Michigan*, 113 F.2d 532 (6th Cir. 1997); *Joslyn Manufacturing Co. v. T.L. James*, 893 F.2d 80 (5th Cir. 1990). Four other circuits state that a parent corporation should be held liable if it steps beyond its role as stockholder of a subsidiary and participates in the day-to-day operation of a subsidiary and its facility.

The District Court held that liability could be imposed when the parent corporation exerted power or influence over its subsidiary by actively participating in, and exercising control over, the subsidiary's business during a period of hazardous waste disposal. The parent was held liable because officers and directors of the parent were also officers and directors of the subsidiary and an official of the parent had played a significant role in shaping the subsidiary's environmental compliance policy. The 6th Circuit reversed holding that the parent could not be held liable unless the corporate veil could be pierced under state law or unless the parent actually operated the facility in the stead of the subsidiary or alongside it as a joint venturer. Based upon the Supreme Court's view of the definition of "operator," the Court said the 6th Circuit correctly rejected the District Court's analysis of direct liability. The Court explained that the trial court applied the "actual control" test of whether the parent "actually operated the business of its subsidiary." The Court pointed out that the well-taken objection to this test is that it asks a question about the relationship between the two corporations instead of a question about the parent's interaction with the subsidiary's facility saying:

The question is not whether the parent operates the subsidiary, but rather whether it operates the facility, and that operation is evidenced by participation in the activities of the facility, not the subsidiary... . The District Court was therefore mistaken to rest its analysis on [the parent's] relationship with [the subsidiary] premising liability on little more than [the parent's] 100% ownership of [the subsidiary] and [the parent's] active participation in, and at times majority control over, [the subsidiary's] board of directors. The analysis should have instead rested on the relationship between [the parent] and the...facility itself. 118 S. Ct. at 1887-88³⁰

The Court indicated that there is no special CERCLA rule of derivative liability. The Court pointed out that if the trial court's approach was approved:

There would in essence be a relaxed, CERCLA-specific rule of derivative liability that would banish traditional standards and expectations from the law of CERCLA liability. But, as we have said, such a rule does not arise from congressional silence, and CERCLA's silence is dispositive. 118 S. Ct. at 1889

In distinguishing oversight of a subsidiary from operation of a subsidiary's facility, the Court stated it was necessary to focus upon the norms of corporate behavior "undisturbed by any CERCLA provision." The Court pointed out that activities involving the facility which are consistent with investor status such as monitoring of a subsidiary's performance, supervision

³⁰ The Court pointed out that a parent's control of its subsidiary if extensive enough could give rise to indirect derivative liability under traditional veil-piercing doctrines but not direct liability under the language of CERCLA. The Court pointed out that the trial court's findings of fact were flawed. The District Court assumed that any action of joint officers and directors were necessarily attributable to the parent. These facts were that the parent put high level officials on the subsidiary's board and in key management positions. Those individuals made major policy decisions and conducted day-to-day operations at the facility. These positions included the position of president and chief executive officer. The Court stated out that the trial court failed to recognize that it was appropriate for directors of a parent to serve as directors of its subsidiary and that it was "normal" for a parent and subsidiary to have identical directors and officers and it is assumed that these joint directors and joint officers both change hats to represent the two corporations separately. The Court stated that the government would have to show that despite the general presumption to the contrary, the officers and directors were acting in their capacities as parent officers and directors and not as subsidiary officers and directors.

of the subsidiary's finance and Budget decisions, and articulation of general policies and procedures, should not give rise to direct liability. The Court stated that the critical question:

is whether, in degree and detail, actions directed to the facility by an agent of the parent alone are eccentric under accepted norms of parental oversight of a subsidiary's facility. 118 S. Ct. at 1889³¹

The entire thrust of the opinion is a rejection of the type of reasoning employed in *Fleet Factors* and an interpretation of the statutory language in its common and ordinary meaning. The ordinary norms of business behavior are recognized as not imposing derivative liability. Under this approach, a financing surety should not be found liable as either an operator, transporter or arranger for those activities commonly engaged in by sureties in a financing situation. Nonetheless, there is insufficient case law at this time to be totally comfortable in this regard.³²

Conclusion

When there has been a default in a project involving hazardous waste, it remains the case that the surety should attempt to arrange for a completing contractor to contract directly with the owner, with the surety standing aside and agreeing simply to finance progress payments in excess of the contract balance to the extent of the bond penalty. Financing the principal where hazardous waste is present risks serious potential liability and remains a risky proposition for the surety under existing law. Even with the protections currently offered by the Lender Liability Act and the potential applicability of the third party defense, as well as the comfort offered by opinion in *Best Foods*, all of these depend, in part, on factual determinations which present the ever present risk, of an adverse finding on the facts. Additionally, the lender or surety remains exposed under federal statutes other than CERCLA and under state minisuperfund statutes and the common law. For this reason, extreme care should be exercised in considering financing and the taking of collateral when there is reason to suspect environmental contamination on either the job site or on the collateral property being offered by the principal or its indemnitors.

³¹ The Court found there was some evidence that this may have been the case with respect to the activities of an employee of the parent who was not an employee or officer of the subsidiary. As a result, the case was remanded for the trial court to reevaluate the role of the particular individual and any other agent of the parent who might have had a part in operating the facility.

³² For cases which have applied the *Best Foods* analysis to CERCLA see *Commander Royal Corp. v. Barlow Equipment Corp.*, 215 F.2d 321 (2nd Cir. 2000) (under the ordinary meaning of the language, a lessee was not a "owner" nor did it exercise a sufficient actual control of the site to be considered an "operator"); *United States v. Township of Brighton*, 153 F.3d 307 (5th Cir. 1998) (*Best Foods* actual control analysis used in determining Township liability for a portion of third-party owned land used as a dump)..

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Mr. Wright has written numerous papers on fidelity and surety topics, as well as in the area of construction law and alternate dispute resolution, including the following:

Contributing author, *Fifty State Construction Lien and Bond Law*, Aspen Law Publications (2d ed. 2000).

Co-Editor, *Answers to the Most Important Questions a Surety Can Ask About the Surety's Environmental Risks*, Tort and Insurance Practice Section – American Bar Association (1997).

Co-author, *Hazardous Waste Liability and the Surety Revisited*, 30 Torts & Ins. L. J., 139 (1995).

Co-author, *Beyond Study: Environmental Construction Contracting in the 1990s*, Section of Public Contract Law, American Bar Association (1993).

Co-author, *Hazardous Waste Liabilities and the Surety*, 25 Tort & Ins. L. J., 663 (Spring, 1990)