CLIENT ALERTS & INSIGHTS

Ohio Expands Liability Protection for Brownfield Purchasers, But Reduces Incentives for Voluntary Cleanups

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The federal Comprehensive Environmental Response, Compensation, and Liability Act of 1980 ("CERCLA"), also known as the Superfund law, has been used successfully to clean up abandoned industrial sites across the country. However, the massive costs incurred by parties liable under the law attached such a stigma to real estate with a history of industrial use, known as "brownfields," that risk-averse real estate investors became wary of investing in even lightly contaminated properties and instead fed the phenomenon of urban sprawl by choosing to build on undeveloped "greenfields."

Almost three decades ago, the Ohio General Assembly created the Voluntary Action Program ("VAP") to incentivize property owners to voluntarily investigate and clean up brownfield sites. More recently, the General Assembly passed, and Gov. DeWine signed, legislation (H.B. 168) that further encourages responsible investments in brownfield properties by limiting purchasers' legal liability for pre-existing contamination. Unfortunately, the recent legislation also simultaneously changed existing state environmental law in a way that might discourage some owners of brownfields from proactively cleaning them up through the VAP.

Why Environmental Liability Protection for Brownfield Owners is Necessary

CERCLA was enacted to provide the U.S. Environmental Protection Agency with the means to ensure that sites with unacceptable levels of historic contamination (especially abandoned sites) are cleaned up. Most states, including Ohio, have enacted complimentary state cleanup programs that follow the federal model to varying degrees. The enactment of CERCLA and its state analogs unintentionally led to fundamental changes in how real estate is bought, sold, financed and developed for industrial purposes in the United States.

U.S. EPA has long portrayed CERCLA as an embodiment of the "polluter pays" principle, imposing cleanup liability on those responsible for a site's contamination so American taxpayers will not be stuck with the bill. However, to maximize its effectiveness, CERCLA was designed to retroactively impose strict cleanup liability (*i.e.*, without regard to fault) for sites with historic contamination, including sites whose industrial use may date back to the early days of the industrial revolution. Unfortunately, but not surprising, many contaminated industrial properties are no longer owned or operated by the same companies that did so back in the days when such sites were contaminated by largely unregulated hazardous emissions and waste disposal practices. As a result, many of the actual "polluters" whose historic operations contaminated CERCLA sites disappeared long ago.

In anticipation of the difficulty in imposing retroactive liability on long-defunct or insolvent companies, Congress drafted CERCLA to include the present-day owners and operators of sites among the parties that could be held jointly and severally liable for cleanup costs, along with the actual polluters.[1] Accordingly, those familiar with the Superfund program in practice understand that a more accurate statement of the statute's underlying principle is "polluter pays . . . unless the polluter isn't around anymore, in which case whomever is unlucky enough to own the property (or finds itself in the chain of title) when EPA comes to town pays."

As enacted, CERCLA provided an affirmative defense to defendants who could prove, among other things, that their liability was solely the result of "an act or omission of a third party other than an employee or agent of the defendant, or than one whose act or omission occurs in connection with a contractual relationship, existing directly or indirectly, with the defendant," so long as the defendant "exercised due care with respect to the hazardous substances concerned" and took "precautions against the foreseeable actions or omissions of any such third party" and their consequences. 42 U.S.C. § 9607(b)(3). However, CERCLA's third-party defense proved to be of little value to "innocent" landowners (*i.e.*, owners of property contaminated entirely before their ownership), because the courts deemed the owner's deed to the property to be a disqualifying "contractual relationship" with the prior owners in the chain of title who had caused or allowed the site's contamination to occur.

Once the potentially vast CERCLA liability exposure of property owners became clear in the early 1980s, it did not take long for savvy real estate developers and their lenders to realize that investment in sites that were previously used -- or even *might* have been used -- in a manner that left behind a chemical residue in soil or groundwater carried higher liability and resale risks than investment in property with little or no such history. As a result, brownfields were out and greenfields were in. Manufacturing zones that had constituted many cities' longstanding industrial core were progressively abandoned and replaced with brand new plants constructed on former farmland located beyond city limits.

Efforts to Protect Innocent Landowners

In 1986, Congress made its first attempt to provide CERCLA liability protection for innocent landowners, adding a statutory definition of "contractual relationship" that made CERCLA's third-party defense available to owners of contaminated sites who could prove that (i) the contamination occurred before the owner acquired title, and (ii) the owner "did not know and had no reason to know" of the contamination at the time of acquisition. 42 U.S.C. § 9601(35)(A).

To establish that they "had no reason to know" of a site's preexisting contamination, owners had to prove that they had "undertaken, at the time of acquisition, all appropriate inquiry into the previous ownership and uses of the property consistent with good commercial or customary practice in an effort to minimize liability. . . [taking] into account any specialized knowledge or experience on the part of the [owner], 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." 42 U.S.C. § 9601(35)(A)(i). This multi-faceted, site-specific definition of "all appropriate inquiry" vested judges with broad discretion and made it

practically impossible for prospective purchasers to know with confidence that they would be deemed to have satisfied the law's requirements if sued in the future.

In fact, as the courts implemented the amended defense, they rarely held that a landowner qualified under the facts of the case, because judges often concluded either that the owner effectively "knew" of the contamination based on the owner's sophistication and/or knowledge of the property's past use, or that the owner surely would have known if he or she had truly conducted "all appropriate inquiry" into the condition of the property.

The Bona Fide Prospective Purchaser Defense

The innocent landowner defense added to CERCLA in 1986 failed to significantly reduce real estate purchasers' preference for greenfields over brownfields. Beyond the uncertainty purchasers faced regarding how a future court would assess the sufficiency of their pre-acquisition due diligence, the defense provided no liability protection to purchasers of brownfield properties that were obviously contaminated to some degree. Whatever advantages a brownfield might present in terms of its location and existing infrastructure, those benefits were often outweighed by the possibility of open-ended environmental cleanup liability in the future.

Congress amended CERCLA in 2002 to provide broader and more certain liability protection for innocent purchasers, particularly brownfield purchasers. First, Congress sought to eliminate (or at least reduce) uncertainty regarding the meaning of "all appropriate inquiry" by directing U.S. EPA to draft specific standards for such due diligence. As a result, prospective purchasers can now generally meet their obligations through compliance with environmental site assessment procedures established by the American Society for Testing and Materials. Second, to facilitate the purchase and beneficial redevelopment of sites known to be contaminated, Congress created a new CERCLA defense for "bona fide prospective purchasers" ("BFPPs") of contaminated sites acquired after January 11, 2002. *See* 42 U.S.C. §§ 9601(40) and 9607(r).

The BFPP defense imposes the same "all appropriate inquiry" due diligence standard applicable to the innocent landowner defense, but importantly eliminates the requirement that the owner have no knowledge of the property's contamination when they acquire it. In other words, the BFPP defense makes CERCLA liability protection (and now protection from Ohio EPA enforcement actions) available to owners who knowingly purchased contaminated property after January 11, 2002, so long as they can demonstrate to a court that they satisfied certain requirements before acquiring the property and have satisfied other requirements since acquiring the property.

Pre-acquisition requirements. Would-be BFPPs must prove that:

1. They are not affiliated with any other potentially liable party;
2. All disposal of hazardous substances at the site occurred before they acquired the property; and
3. The owner made "all appropriate inquiry" into the previous ownership and uses of the site in accordance with generally accepted good commercial and customary standards and practices.

Post-acquisition requirements. Would-be BFPPs must also establish that since acquiring title, they have:

1. Provided all legally required notices regarding the discovery or release of any hazardous substances at the site;
2. Exercised "appropriate care" with respect to hazardous substances found at the site by taking reasonable steps to stop any continuing release, prevent any threatened future release, and prevent or limit exposure to such hazardous substances;
3. Provided full cooperation, assistance, and access to persons authorized to conduct cleanups at the site;[2]
4. Complied with any land use restrictions established or relied on in connection with any site cleanup and have not impeded the effectiveness or integrity of any institutional control established in connection with a cleanup; and
5. Complied with any request for information or administrative subpoena issued by U.S. EPA.

Under H.B. 168, owners of Ohio real estate may now assert the BFPP defense in civil actions brought by the state of Ohio to recover the state's costs of investigating contamination and conducting cleanups on the owner's property. Although the new Ohio defense is substantively identical to the CERCLA version, the federal defense has wider application, as it may be raised in litigation brought by private plaintiffs. Moreover, the Ohio defense may only be asserted against claims that are based solely upon the defendant's status as owner or operator of the facility. State causes of action based on other legal grounds are unaffected. The defense may be asserted in any applicable case filed after September 14, 2020, as well as actions pending on that date.

Limitations of Ohio's New BFPP Defense

The primary practical limitation of the BFPP defense is that a prospective purchaser cannot confirm its availability when deciding whether to acquire a property. Whether the criteria have been met will be determined by a future judge only if and when the owner is sued. While ambiguity in the meaning of "all appropriate inquiry" is far less than when the requirement was added to CERCLA in 1986, the BFPP defense is still highly fact-intensive and site-specific, leaving individual judges with a great deal of discretion in determining whether the owner has met the burden of proving each and every element of the affirmative defense. An owner need only fall short on one element to lose the defense.

A prospective purchaser's uncertainty over how a future court would assess its conduct is enhanced by the fact that courts will typically make such assessments with the benefit of facts that were unavailable to the purchaser. The defense will necessarily only be litigated when the need for a site cleanup has become clear, possibly after an extensive governmental investigation of the property has identified significant contamination. The judge assessing the reasonableness of the purchaser's past actions will therefore often be aware of many more facts regarding the condition of the property than were reasonably available to the purchaser. This judicial hindsight will often arm judges with a host of reasons to conclude that the purchaser could (and thus should) have done more to meet the affirmative requirements of the defense.

The Ohio law's restriction of the defense to actions where the state is a plaintiff, leaves owners exposed to at least some state-law contribution claims, as well as to claims by neighbors whose property has been damaged by contamination migrating from the owner's property.

H.B. 168's Partial Elimination of the VAP Enforcement Safe Harbor

One other change made to Ohio law by H.B. 168, which has largely escaped attention, is the partial elimination of an enforcement "safe harbor" for parties that have proactively begun to address their contaminated property under the state's Voluntary Action Program ("VAP"). As the VAP was originally enacted, owners that received written notice of Ohio EPA's intent to take enforcement action regarding contamination at the owner's property could prevent the enforcement action and continue to address their property under the VAP if they provided Ohio EPA with "sufficient evidence" that the contamination was already being expeditiously addressed in accordance with the VAP. *See* Ohio Revised Code § 3746.02 (A)(5) and Ohio Administrative Code Rule 3745-300-02(C)(4).

The opportunity to address a site privately under the VAP, rather than under a government consent order, is one of several VAP incentives to property owners to proactively pursue a cleanup. The reasoning behind the enforcement safe harbor is that if owners face a risk of investing resources in the VAP process only to be forced out of the program at any time by an Ohio EPA enforcement notice, they will be less likely to start the VAP process.

The drafters of H.B. 168 intended to expand the VAP enforcement safe harbor to include BFPPs, meaning that an owner could avoid an enforcement action ***either*** by making a 'sufficient evidence' demonstration or by establishing their BFPP status. However, the textual changes made to the relevant provision instead provide that, upon receipt of an enforcement notice, a property becomes ineligible for cleanup under the VAP if the owner ***either*** cannot make a sufficient evidence demonstration ***or*** if the owner cannot establish BFPP status. Thus, H.B. 168 inadvertently limits the enforcement safe harbor to owners that can satisfy ***both*** requirements.

Unless it is corrected, H.B. 168's drafting error could discourage participation in the VAP by Ohio brownfield owners that wish to clean up their properties under the VAP, but who cannot assert a BFPP defense. The universe of Ohio brownfield owners who meet this description is not insubstantial. For example, the BFPP defense only applies to owners who acquired the property after January 11, 2002. Thus, companies who have owned their facilities for more than 18 years cannot qualify as BFPPs and, under H.B. 168, could be forced out of the VAP upon receipt of a state enforcement notice.

The BFPP defense also excludes owners whose operations contributed to contamination of their property. The VAP contains no such limitation on participation and thus is generally available to owners of facilities that became contaminated over the course of their ownership. Companies who wish to use the VAP to proactively address their own legacy contamination, cannot qualify as BFPPs and, under H.B. 168, could now also be forced out of the VAP upon receipt of a state enforcement notice.[3]

Conclusion: Brownfield Owners and Potential Buyers Should Still Exercise Caution

Ohio's adoption of the federal "bona fide prospective purchaser" defense to state enforcement actions is a useful, though limited, step toward eliminating the legal disincentives to brownfield investment. Prospective purchasers of contaminated property should explicitly address the defense's list of requirements in their due diligence and post-closing plans. Since purchasers lack a mechanism to confirm the defense's applicability at the time a purchase decision must be made, they should view the potential defense as a supplement to, rather than a replacement for, other

means of reducing environmental liability risks, including escrowed cleanup funds, contractual indemnities and insurance. For those sites where it is cost-effective to do so, obtaining a Covenant Not to Sue pursuant to the VAP would ultimately provide more certain liability protection, while also increasing the underlying value of the property.

Ohio property owners who may be considering the VAP, but cannot meet the requirements of the BFPP defense, should weigh the current unavailability of the VAP's enforcement safe harbor when assessing the pros and cons of addressing their site via the VAP. The Ohio General Assembly will likely correct the statutory language and restore the safe harbor for non-BFPPs, but the earliest this could occur is in a "lame duck" session following the Fall elections. One potential complication is that H.B. 168's principle sponsor, Rep. Steve Arndt, is unavailable to sponsor technical correction legislation, as he resigned from the Ohio House at the end of July 2020. Ohio EPA has not indicated whether it will, in the meantime, exercise enforcement discretion to prevent unintended results.

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[1] CERCLA makes four categories of persons at each Superfund site jointly and severally liable for the costs of cleaning up the site: persons who arranged for the disposal or treatment of their hazardous substances at the site, persons who selected and transported hazardous substances to the site, persons who owned or operated the site at the time hazardous substances were disposed there, and persons who presently own or operate the site. *See* 42 U.S.C. § 9607(a). For example, at a former dump site, the parties that generated the wastes disposed at the dump, waste haulers who chose to take wastes to the dump, the owners and/or operators of the dump while it was active, and the current owners and/or operators of the property are all jointly and severally liable under CERCLA for the costs of cleaning up the dump site.

[2] An additional element of the federal BFPP defense, which was not expressly incorporated into the new Ohio defense, is that the BFPP does not impede a cleanup or natural resource restoration at the site. *See* 42 U.S.C. § 9607(r). However, a duty not to impede a cleanup is arguably implicit in this requirement to cooperate with those conducting a cleanup.

[3] H.B. 168 also modified the circumstances under which a party that has completed the VAP process and received a Covenant Not to Sue from Ohio EPA may have their CNS revoked for failing to comply with institutional controls or activity/use limitations imposed on the property under the CNS. Under the new law, the Director ***may*** revoke a CNS for such noncompliance, but revocation is no longer automatic. Since revocation of a CNS is the VAP's equivalent of the death penalty, it makes sense to provide the Director with discretion to ensure the penalty is only applied when it fits the seriousness of the noncompliance.