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# Methods To Minimize CERCLA Liability: Part 1

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The Comprehensive Environmental Response, Compensation, and Liability Act, 42 U.S.C. §§ 9601 *et seq*., has now been the law of the land for almost 35 years. It has resulted in the investigation and cleanup of thousands of contaminated sites throughout the nation. Hundreds of billions of dollars have been spent to complete those activities. Most of the money has come from companies held responsible under the statute's strict joint and several liability provisions. Increasingly, however, in an effort to find more funds to pay for the remedial and removal actions undertaken, governments and private companies are investing significant resources in tracking down the alleged successors to companies that owned or contributed hazardous substances to those sites.

When a company is notified that it may be a successor to a company that contributed to a hazardous waste site and therefore may be on the hook for hundreds of thousands or millions of dollars in cleanup costs, it is not only a shock but is often just the beginning of a very long and expensive process.

Although the law on successor liability under CERCLA continues to evolve, certain aspects of the law should be kept in mind when such notices arrive. For example, although the debate continues, one needs to look at state successor liability law for answers. In this article, we review the issue of successor liability under CERCLA in the Ninth Circuit, applying California law.

Under California law a company may be the successor to a prior company's liability if the transaction between the prior company and the new company explicitly transfers the liability in question or the transaction qualifies as a "de facto merger."

With regard to CERCLA successor liability, courts look to the following factors to determine whether a de facto merger has occurred: "(1) there is a continuation of the enterprise of the seller in terms of

continuity of management, personnel, physical location, assets, and operations; (2) there is a continuity of shareholders; (3) the seller ceases operations, liquidates, and dissolves as soon as legally and practically possible; and (4) the purchasing corporation assumes the obligations of the seller necessary for uninterrupted continuation of business operations." *La.-Pac. Corp. v. Asarco Inc.*,909 F.2d 1260, 1264 (9th Cir. 1990), *overruled on other grounds by Atchison, Topeka & Santa Fe Ry. Co. v. Brown & Bryant Inc.*,159 F.3d 358, 362 (9th Cir. 1998) ("*ATSF*"). Courts attempting to determine whether a de facto merger took place should base their decision "on the need for fairness, and conduct a holistic inquiry rather than a rote factor-by-factor analysis." *United States v. Sterling Centrecorp Inc.*, 960 F. Supp. 2d 1025, 1043, (E.D. Cal. 2013).

Where there is little or no continuity of personnel or assets, and no continuity of physical location or operations, successor liability should fail. Even where a company and the predecessor were both engaged in the same *type* of business, "continuity of operations" between the two companies is not a given. In the context of a de facto merger, courts have interpreted "continuity of operations" to mean continuing the prior company's business operations, not operating a new company in the same line of business. *See Sterling Centrecorp*, 960 F. Supp. 2d at 1044 (court found de facto merger where purchaser "continued the general business operations" of seller at same location with same employees); *Marks v. Minn. Mining & Mfg. Co.*, 187 Cal. App. 3d 1429, 1436-37 (1986) (court found de facto merger where purchaser: (1) hired all of seller's employees, including all founders; (2) continued to manufacture same product without alteration; and (3) assumed all of seller's normal operating liabilities).

The Ninth Circuit has definitively stated that a continuity of shareholders is required for a finding of a de facto merger. *Asarco*, 909 F.2d at 1264-1265 ("[t]o find that a *de facto* merger has occurred there must be ... continuity of stockholders," and "continuity of shareholders is [o]ne of the key requirements of the doctrine") (citations and internal quotation marks omitted). Continuity of shareholders, also referred to as continuity of ownership, means a transfer of assets in exchange for the buyer's corporate securities, not just that some of the shareholders have the same identity. *Bud Antle Inc. v. E. Foods Inc.*, 758 F.2d 1451, 1458 (11th Cir. 1985). This is because corporate liability adheres to "the corporate entity itself," and if assets are not transferred for stock, then "no basic fundamental change occurs in the relationship of the stockholders to their respective corporations, ... and absent continuity of shareholder interest, the two corporations are strangers, both before and after the sale." *Id*. (citation and internal quotation marks omitted).

To determine whether an asset purchase should be considered a de facto merger, one of the factors that courts consider is whether "[t]he seller corporation ceases its ordinary business operations, liquidates, and dissolves as soon as legally and practically possible." *Phila. Elec. Co. v. Hercules Inc.*, 762 F.2d 303, 310 (3d Cir. 1985).

An asset transfer that is fraudulently entered into in order to escape liability will not insulate the successor corporation from liability under CERCLA. *ATSF*, 159 F.3d at 361. In determining whether or not a transaction was entered into fraudulently, the sufficiency of consideration given for the assets purchased is a significant factor. *Id*. at 365.[1] However, merely showing that the principal assets were transferred for less than their fair market value will not normally be enough to warrant imposition of successor liability under this exception. Lawrence P. Schnapf, *CERCLA and the Substantial Continuity Test: A Unifying Proposal for Imposing CERCLA Liability on Asset Purchasers*, 4 Envtl. Law. 435, 447 (1998) (citing *Armour-Dial Inc. v. Alkar Eng'g Corp.*, 469 F. Supp. 1198, 1202 (E.D. Wis. 1979)). Further, the intent of the parties to fashion the transaction solely to circumvent CERCLA liability is an important factor. *ATSF*, 159 F.3d at 365. Notably, this exception is rarely, if ever, applied in a CERCLA context. *Id.*

"[C]orporations cannot escape liability by a mere change of name or a shift of assets when and where it is shown that the new corporation is, in reality, but a continuation of the old." *McClellan v. Northridge Park Townhome Owners Ass'n Inc.*, 89 Cal. App. 4th 746, 756 (2001) (citation and internal quotation marks omitted). A company is a mere continuation of another company when only one company remains after the principal asset transfer, and there is an identity of stock, stockholders and directors.*Ferguson v. Arcata Redwood Co. LLC*, No. C03-05632 SI at *5 (N.D. Cal. 2004); *Washington v. United States*, 930 F. Supp. 474, 478 (W.D. Wash. 1996). Factors examined by courts in a mere continuation analysis include the continuation by the buyer of the divesting corporation's business and an inability of the divesting corporation to pay its debts after the asset transfer because no adequate consideration was given for the seller's assets. *K.C.1986 Ltd. P'ship v. Reade Mfg.*, 472 F.3d 1009, 1025 (8th Cir. 2007); *Ray*, 19 Cal. 3d at 29.

In *McClellan*, the Peppertree homeowners association ("HOA") decided to disband and reform as the Northridge Park HOA in order to avoid a debt. *McClellan*, 89 Cal. App. 4th at 749-50. The Northridge Park HOA conducted the same business, collected the same revenues, operated through the same board of directors, had the same management company and presided over the same condominiums as the Peppertree HOA. *Id.* at 750. The *McClellan* court held that the new HOA, Northridge Park, was "nothing more than the continuation of Peppertree under a different name" and that "[d]isregarding the corporate entity by finding successor liability was proper." *Id.* at 755-56.

Defending a successor liability claim can be time-consuming and expensive, but also successful. Going forward, companies need to keep the factors referenced above in mind in shaping purchasing transactions. Where the company allegedly responsible for contamination is already in the corporation's history, investigating the transactional history of the purchase in the context of the applicable successor law and taking appropriate action to ringfence the liability that was not part of the bargain may be well worth the effort.

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[1] Numerous courts have recognized that as long as the seller receives adequate consideration for its assets, the seller's creditors will generally be protected even if the purchaser does not assume liability. *See, e.g.*, *Ray v. Alad Corp.*, 19 Cal. 3d 22, 29 (1977) (Consideration paid for assets was available to meet claims of creditors; therefore, the acquisition of "assets was not in the nature of a merger or consolidation.").

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# Methods To Minimize CERCLA Liability: Part 2

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It is never pleasant for a company to receive a potentially responsible party letter from the U.S. Environmental Protection Agency or a state environmental agency seeking relief under the Comprehensive Environmental Response, Compensation, and Liability Act, 42 U.S.C. §§ 9601 et seq.

This is particularly true when the environmental site in question has been the subject of investigations and cleanup activities for years, but no prior contact has been made with your company. Given the breadth of actions and powers provided to government agencies under CERCLA, most companies that receive these CERCLA 104(e) requests for information, or CERCLA 106 notices of potential liability, believe they have no defense. Often overlooked is a key defense: the statute of limitations. PRPs added late to the process need to consider this defense as soon as such a letter arrives. Raising this issue early might allow your company to cut back on the increasingly expensive process of responding to government demands that ultimately have no merit.

CERCLA actions, like actions under any other statute, are time-limited. See 42 U.S.C. § 9613(g)(2)(B). Statutes of limitations ensure "that the defendant is given the protections of predictability and promptness." United States v. Hagege, 437 F.3d 943, 955 (9th Cir. 2006); see Cal. Dep't of Toxic Substances Control v. Hearthside Residential Corp., 613 F.3d 910, 914 (9th Cir. 2010) (statutes of limitation are intended in part to protect defendants).

A CERCLA cost recovery claim associated with "remedial" actions must be commenced within six years after initiation of physical on-site construction of the remedial action. 42 U.S.C. § 9613(g)(2)(B). The language of CERCLA's statute of limitations "indicates that there will be but one 'removal action' per site or facility, as well as a single 'remedial action' per site or facility." Colorado v. Sunoco Inc., 337 F.3d 1233, 1241 (10th Cir. 2003); see New York State Elec. & Gas Corp. v. FirstEnergy Corp., 766 F.3d 212, 235

(2d Cir. 2014) ("Virtually every court" agrees that "there can only be one remedial action at any given site."); see also California ex rel. Cal. Dep't of Toxic Substances Control v. Hyampom Lumber Co., 903 F. Supp. 1389, 1394 (E.D. Cal. 1995) ("Hyampom") ("There is no authority for the view that each 'remedial' activity undertaken at a site triggers a new cause of action for the cost recovery of that activity.").

The first step in the CERCLA statute of limitations analysis is to determine whether the response action or actions taken at the site constitute one or more remedial actions. Where the facts regarding the response actions at the site are undisputed, the determination of whether an action can be characterized as a removal action or a remedial action "is one of law and is therefore appropriate for resolution on summary judgment." Hyampom, 903 F. Supp. at 1391; see United States v.W.R. Grace & Co., 429 F.3d 1224, 1234 (9th Cir. 2005) ("Whether the ... cleanup activity was a removal action — or, on the other hand, a remedial action in removal action's clothing—is a question of statutory interpretation.").

The term "remedial action" is defined by CERCLA as:

those actions consistent with permanent remedy taken instead of or in addition to removal actions in the event of a release or threatened release of a hazardous substance into the environment, to prevent or minimize the release of hazardous substances so that they do not migrate to cause substantial danger to present or future public health or welfare or the environment. 42 U.S.C. § 9601(24).

Courts addressing the distinction between removal and remedial actions have developed the universally accepted principle that "removal actions generally are immediate or interim responses, and remedial actions generally are permanent responses." Geraghty & Miller Inc. v. Conoco Inc., 234 F.3d 917, 926 (5th Cir. 2002). Consistent with this approach, the Hyampom court has held that "'removal' actions are short-term, temporary responses to an immediate threat as well as actions taken to assess, monitor and evaluate a given site, while 'remedial actions' are those measures taken to achieve a permanent solution." Hyampom, 903 F. Supp. at 1391.

As opposed to remedial actions, removal actions are usually short in duration and occur early in the cleanup "life" of a site. See OBG Tech. Servs. Inc. v. Northrop Grumman Space & Mission Sys. Corp., 503 F. Supp. 2d 490, 523 (D. Conn. 2007) (regarding Congress' motives for different statutes of limitation for removal and remedial actions). Further, removal actions usually precede remedial actions. Id. at 525 (plaintiff could not point to permanent remedial action that followed its so-called removal actions "because the actions it considers to be removal actions were, in fact, the permanent remedial solution envisioned under CERCLA"). Courts also emphasize the circumstances in which the response action is taken, rather than the type of response activity, to determine whether a response action should be characterized as a removal action or a remedial action. Valbruna Slater Steel Corp. v. Joslyn Mfg. Co., No. 1:10-CV-044 JD at *9 (N.D. Ind. March 21, 2013).

In Hyampom, the court set forth several factors to be considered in determining whether a response action at a hazardous waste site is properly characterized as a "removal" action or a "remedial action." These factors, applied on a case-by-case basis with no one factor carrying more weight than any other, are: (1) proximity in time of the response action to disclosure of the final remedial design; (2) whether remedial investigation and feasibility study monitoring and testing are ongoing at the time of the response action; (3) whether the response action falls within the statutory definition of "removal" (or "remedial"); and (4) the response action's role in the implementation of the permanent remedy. Hyampom, 903 F. Supp. at 1392-94. Regarding the fourth factor, the Ninth Circuit has held that whether a given response action is consistent with a permanent remedy "is when the permanent remedy is

actually selected," i.e., when a final remedial action plan is approved. California ex rel. Cal. Dep't of Toxic Substances Control v. Neville Chem. Co., 358 F.3d 661, 667 (9th Cir. 2004).

Given this case law, companies served with PRP notices by the EPA or state agencies threatening action under CERCLA should carefully scrutinize the available public record concerning the site in question to determine whether the statute of limitations has already run on the remedial action involved.

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# Methods To Minimize CERCLA Liability: Part 3

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As of Sept. 1, 2015, there are over 570 hazardous waste and substance sites listed in California alone. Each one of those sites is subject to action by the state under the Comprehensive Environmental Response, Compensation, and Liability Act, 42 U.S.C. § 9601 et seq., as well as state environmental laws. State participation in the enforcement of CERCLA is critical to the statute's success. Niagara Mohawk Power Corp. v. Chevron USA Inc., 596 F.3d 112, 126 (2d Cir. 2010). To encourage potentially responsible parties to assist in the payment of costs for the investigation and cleanup of such sites without extensive litigation, Congress has given the U.S. Environmental Protection Agency and state agencies implementing CERCLA the right to enter into a consent decree that provides protection for the settling PRPs from contribution claims by the nonsettling parties. See 42 U.S.C. § 9613(f)(2). These decrees, however, must be approved by the appropriate federal district court. Id.

The standards for federal court approval of CERCLA consent decrees, although almost identical, are set by each federal circuit. States seeking approval of such decrees face a higher standard, however, in the Ninth Circuit based on Arizona v. City of Tucson, 761 F.3d 1005 (9th Cir. 2014) and its progeny. As a result, PRPs seeking CERCLA contribution protection through the execution of a consent decree with state environmental agencies must be careful to ensure the following two circumstances.

First, that the state presents substantial evidence of the comparative fault involved in "apportioning liability among the settling parties according to rational (if necessarily imprecise) estimates of how much harm each [potentially responsible party] has done." Id. at 1012 (quoting United States v. Charter Int'l Oil Co., 83 F.3d 510, 521 (1st Cir. 1996)). (quoting United States v. Cannons Eng'g Corp., 899 F.2d 79, 87 (1st Cir. 1990); and, second, that the district court has made a record that it carried out its "obligation to independently scrutinize the terms of [such agreements]" by comparing "the proportion of total projected costs to be paid by the [settling parties] with the proportion of liability attributable to them." City of Tucson, 761 F.3d at 1008 (quoting United States v. Montrose Chem. Corp. of Cal., 50 F.3d 741, 747 (9th Cir. 1995)).

To approve a CERCLA consent decree, a district court in the Ninth Circuit must find the agreement to be procedurally and substantively "fair, reasonable, and consistent with CERCLA's objectives." City of Tucson, 761 F.3d at 1009 (quoting Montrose, 50 F.3d at 748). Moreover, in the Ninth Circuit, such

decrees presented by the EPA must be given ”deference.” As the court in Tucson held, however, the court is only required to give state-agency-based proposed decrees “some deference”:

We find the reasoning of the First Circuit on this issue persuasive, and we hold that where state agencies have environmental expertise they are entitled to ‘some deference’ with regard to questions concerning their area of expertise. But ‘[a] state agency's interpretation of federal statutes is not entitled to the deference afforded [to] a federal agency's interpretation of ... statutes’ that it is charged with enforcing. City of Tucson, 761 F.3d at 1014 (quoting Orthopaedic Hosp. v. Belshe, 103 F.3d 1491, 1495 (9th Cir. 1997)).

This standard makes it more difficult in the Ninth Circuit to obtain approval of consent decrees proposed by state environmental agencies versus those proposed by the EPA. In addition, the Ninth Circuit’s standard makes obtaining approval for proposed consent decrees more difficult than in almost all other circuits.

Although this higher standard is a concern, it should not be a bar to approval for several reasons.

In most cases, at least some history about the site and the involvement of PRPs at the site is available. Questions that should be answered in preparing the proposed decree and presenting it to the court include, for example, the following:

- If an owner is involved, how long did that owner own the site?
- If they owned the site, did they also operate a facility at the site? For how long?
- Did others own the site? For how long?
- Did they operate a facility at the site? For how long?
- Compared to the total cleanup bill, what is the PRP's percentage of responsibility for the cleanup based on the ownership, operation or transportation of hazardous substances to the site?
- Did any of the PRPs contribute to the investigation of cleanup of the site?
- If other PRPs contributed but didn’t settle, how much did the contributing PRPs provide versus the nonsettling parties?
- If the settling PRPs transported to the site, how much did they take to the site versus the nonsettling parties?
- What is the financial status of the settling PRPs versus the nonsettling parties?
- How early in the action have the settling PRPs agreed to enter into the decree?
- What defenses do the settling PRPs have?

The last few questions may also be used to justify discounts from the allocation shares calculated by the state. Other factors to consider include whether the PRPs that are settling versus the nonsettling parties were in violation of a cleanup order or other state-based environmental laws and regulations. And, finally, what was the specific methodology used to calculate the allocation and the discount?

The bottom line is that, particularly in the Ninth Circuit, PRPs wishing to obtain the protection provided by a court-approved consent decree should be proactive to ensure that the state agency proposing the decree has a well-documented record to present to the district court regarding a fair allocation formula, the PRPs’ share in that allocation versus the nonsettling parties and the reasonable discounts supporting the settlement amount. Moreover, the parties involved must ensure that the district court is diligent in documenting its independent examination and evaluation of these facts.

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