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The Innocent Landowner Defense Under CERCLA Should Be Transferable to Subsequent Purchasers

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Under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA)[1] and the accompanying Superfund Amendments and Reauthorization Act of 1986 (SARA)[1] (collectively the "Act"), landowners are held strictly liable for cleaning up hazardous substances on their property. Purchasers who acquire title to contaminated property become liable for cleanup costs simply by virtue of their status as the current owner.[2] Although liability under the Act is strict, joint, and several, a few limited defenses enable some landowners to avoid liability altogether. One such defense, known as the innocent landowner defense,[3] is the subject of this article.

In order to qualify as an innocent landowner, a purchaser who acquires title to contaminated property must prove that he or she had no reason to know that the property was contaminated at the time it was acquired.[4] Although it is not easy for an innocent landowner to prove "lack of knowledge," Congress has determined that a landowner who satisfies this burden is not responsible for cleanup costs. However, a landowner who cannot meet this bur-

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[1] CERCLA §§ 101-75, 42 U.S.C. §§ 9601-75 (1988).

[1] SARA amends, clarifies, and reauthorizes the CERCLA statutes. 42 U.S.C. §§ 9601-75.

[2] *See, e.g.*, New York v. Shore Realty Corp., 759 F.2d 1032, 1043-44 (2d Cir. 1985) (holding current owner liable for response costs even though current owner did not own site at time of disposal); United States v. Parsons, 723 F. Supp. 757, 761 (N.D. Ga. 1989) (holding the owner of a farm on which hazardous substances were disposed liable for the response costs under CERCLA § 107(a)); FMC Corp. v. Northern Pump Co., 668 F. Supp. 1285, 1289 (D. Minn. 1987) (holding the current owner definitely liable for the response costs under CERCLA § 107(a)).

[3] The innocent landowner defense is codified under CERCLA 42 U.S.C. §§ 9601(35)(A), 9607(b)(3).

[4] 42 U.S.C. § 9601(35)(A)(i).

den, including one who acquires title to contaminated property with actual knowledge of the contamination, is held strictly liable under the Act for the costs of cleanup whether or not the owner had a role in contaminating the property.[5]

This article argues that there should be no lack-of-knowledge prerequisite to the innocent landowner defense under the Act because this prerequisite does not further the goals of the Act and penalizes those landowners who Congress has sought to relieve from liability. Sellers have a legal duty to disclose their knowledge of material facts concerning their property to subsequent purchasers.[6] Contamination of property will always be a material fact of interest to a subsequent purchaser. When combined with the lack-of-knowledge prerequisite to the innocent landowner defense, the duty of disclosure precludes innocent landowners from transferring their innocent landowner status to subsequent purchasers.

Because subsequent purchasers who knowingly acquire title to contaminated property cannot qualify as innocent landowners, there is virtually no market for contaminated property in today's economy. As a result, supposedly innocent landowners are deprived of much of the benefit of their defense, and society is deprived of potentially faster pollution remediation as well as potentially more efficient land use. There is no good reason to deny the innocent landowner defense to subsequent purchasers who acquire title to contaminated property with knowledge of the contamination. Such purchasers, if afforded innocent landowner status, will put contaminated property to higher and better uses, and will potentially facilitate faster and more complete cleanup efforts.

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[5] If the landowner does not clean up the property, the government or another potentially responsible party under the Act will probably clean it up and sue the landowner for contribution.

[6] Certain states, such as California, have adopted disclosure statutes that require landowners to complete a special form when transferring title to their property. *See, e.g.*, CAL. CIV. CODE § 1102.6 (West 1982 & Supp. 1994)(requiring detailed disclosures of many different types of information). However, even in states that do not have such disclosure laws, landowners with knowledge of contamination on their property who do not disclose this information to subsequent purchasers can still be held liable for negligent or intentional misrepresentation under common law principles.

I. THE LACK-OF-KNOWLEDGE PREREQUISITE TO THE INNOCENT LANDOWNER DEFENSE PRECLUDES SUBSEQUENT PURCHASERS FROM QUALIFYING AS INNOCENT LANDOWNERS

The following two sections of the Act combine to create the lack-of-knowledge prerequisite to the innocent landowner defense: (1) section 9607(b)(3), which was part of the original CERCLA legislation, and (2) section 9601(35), which was adopted with SARA. Section 9607(b)(3) denies the innocent landowner defense to those who stand in a contractual relationship with a responsible party,[7] and section 9601(35)(A) defines the term "contractual relationship" to include a purchase and sale agreement.[8]

Even prior to SARA, the courts had interpreted the term "contractual relationship" to include a purchase and sale agreement.[9] Because title to real property is almost always transferred by deed pursuant to a purchase and sale agreement, however, virtually all purchasers of contaminated property stood in a contractual relationships with responsible parties and, therefore, could not qualify as innocent landowners. However, SARA added language to section 9601(35) which allows certain landowners to qualify for the innocent landowner defense despite the fact that they may stand in a contractual relationship with a responsible party.[10] If one of the three conditions quoted below in Section 9601(35) can be proven by a preponderance of the evidence, then a written in-

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[7] CERCLA § 107(b) provides in pertinent part as follows:

> There shall be no liability . . . for a person otherwise liable who can establish by a preponderance of the evidence that the release or threat of release of a hazardous substance and the damages resulting therefrom were caused solely by . . . 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 . . . if the defendant establishes by a preponderance of the evidence that (a) he exercised due care with respect to the hazardous substance concerned, . . . and (b) he took precautions against foreseeable acts or omissions of any such third party . . . .

CERCLA § 107(b), 42 U.S.C. § 9607 (1988).

[8] 42 U.S.C. § 9601(35)(A) provides that the term 'contractual relationship' for purposes of § 9607(b)(3) "includes, but is not limited to, land contracts, deeds or other instruments transferring title or possession . . . ."

[9] *See supra* note 3 and accompanying text.

[10] It is important to note that even when a subsequent purchaser acquires contaminated property from an innocent landowner, the subsequent purchaser still stands indirectly in a contractual relationship with a responsible party so long as a responsible party is in the chain of title. A purchase and sale agreement can serve as a contractual bridge to liability that is several transfers removed in the chain of title.

strument transferring title will not constitute a contractual relationship for purposes of section 9607(b)(3).

Section 9601(35) provides as follows:

> The term "contractual relationship" for the purpose of Section 9607(b)(3) of this title includes, but is not limited to, land contracts, deeds or other instruments transferring title or possession, unless the real property on which the facility concerned is located was acquired by the defendant after the disposal or placement of the hazardous substance on, in, or at the facility, and one or more of the circumstances described in clause (i), (ii), or (iii) is also established by the defendant by a preponderance of the evidence: (i) At the time the defendant acquired the facility the defendant did not know and had no reason to know that any hazardous substance which is the subject of the release or threatened release was disposed of on, in, or at the facility. (ii) The defendant is a government entity which acquired the facility by escheat, or through any other involuntary transfer or acquisition, or through the exercise of eminent domain authority by purchase or condemnation. (iii) The defendant acquired the facility by inheritance or bequest.[11]

These classifications provide defenses for very few landowners.

Most subsequent purchasers are not government entities, and most do not acquire title by inheritance or bequest. Consequently, conditions (ii) and (iii) are usually not applicable. Condition (i), which contains the lack-of-knowledge requirement, is therefore the innocent landowner defense for the majority of qualifying purchasers. For a subsequent purchaser who acquires title to contaminated property by executing and performing on a purchase agreement, the entire innocent landowner defense turns on whether that subsequent purchaser knew or should have known that the acquired property was contaminated.[12] When sellers of contaminated property have knowledge of contamination and discharge

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[11] 42 U.S.C. § 9601(35)(A)(1988).

[12] This inquiry is controlled by CERCLA § 101(35)(B) which provides as follows: To establish that the defendant had no reason to know, as provided in clause (i) of subparagraph (A) of this paragraph, the defendant must have 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. For purposes of the preceding sentence, the court shall take into account any specialized knowledge or experience on the part of the defendant, 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

their legal duty to disclose this information to subsequent purchasers, the subsequent purchasers, by definition, cannot qualify for the innocent landowner defense. Purchasers who acquire title to contaminated property with knowledge of the contamination cannot satisfy the requirements of section 9601(35)(A)(i), quoted above.

Even if a seller does not discharge his or her legal duty of disclosure, the subsequent purchaser may still not be able to prove that he or she had no reason to know that the acquired property was contaminated. Parties who challenge application of the innocent landowner defense often argue that the current owner failed, at the time of acquisition, to undertake "all appropriate inquiry into the previous ownership and uses of the property consistent with good commercial or customary practice," as required by section 9601(35)(B). For example, in *Jersey City Redevelopment Authority v. PPG Industries, Inc.*,[13] the court held that even if the innocent landowner defense applied to off-site property, the defendant could not satisfy the requirement that it did not know of the hazardous waste disposal on the property it had purchased because the purchaser knew that the site had been used for chromium processing and that residue muds were created. The court declined to read into CERCLA an intent to afford landowners a broad lack-of-specific-knowledge defense. Instead, the court understood the appropriate inquiry to be whether the landowner knew at the time of purchase that the substance existed on the property.

This article argues that this lack-of-knowledge requirement contained in section 9601(35)(A)(i) should be deleted from the Act. Deleting the lack-of-knowledge requirement will obviate the need to distinguish actual knowledge from a lack of diligent inquiry and will allow innocent landowners to transfer their status as innocent landowners to subsequent purchasers. Section 9601(35)(A) should be rewritten to provide that the term "contractual relationship" does not include a purchase and sale agreement, deed, or other instrument transferring title. For the reasons discussed below, subsequent purchasers should be able to qualify

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the presence or likely presence of contamination at the property, and the ability to detect such contamination by appropriate inspection.

CERCLA § 101(35)(B), 42 U.S.C. § 9601 (35)(B) (1988).

[13] Jersey City Redevelopment Authority v. PPG Industries, Inc., 28 Env't Rep. Cas. (BNA) 1873 (3d Cir. 1988).

as innocent landowners whether or not they acquire title with knowledge of the contamination.

II. THERE SHOULD BE NO LACK-OF-KNOWLEDGE PREREQUISITE TO THE INNOCENT LANDOWNER DEFENSE

The 1986 addition of Section 9601(35) outlining the requirements for the innocent landowner defense confirms that Congress did not intend to hold landowners who have nothing to do with contaminating a particular site responsible for cleaning up contaminated property.[14] By disallowing the defense to purchasers who acquire title with knowledge of contamination, however, this Congressional purpose is frustrated. The lack-of-knowledge prerequisite forces these innocent landowners to incur cleanup costs despite the fact that they can satisfy all of the elements of section 9607(b)(3). A purchaser interested in a parcel who discovers during an investigation that the property is contaminated will be unable to acquire the parcel without becoming liable for the costs of cleaning it up, which means that the seller, the supposedly innocent landowner, holds title to property which has become devalued by the estimated costs of cleanup. This phenomenon hurts both innocent landowners and society at large. Innocent landowners are not relieved of the costs of cleaning up their contaminated property, which seems inconsistent with Congress's objectives under the CERCLA liability scheme, and society is deprived of faster remediations and more efficient land use.

Assuming that an innocent landowner does not just ignore contamination or defraud a subsequent purchaser, an innocent landowner who discovers contamination on his or her property has two viable options. First, the innocent landowner has a litigation option. The innocent landowner can either sue the responsible parties, forcing them to clean up the contaminated property, or wait until the government or other private parties file suit against the responsible parties. The litigation option, however, is time-consuming and expensive. An innocent landowner must have significant resources available to file a lawsuit.

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[14] *See, e.g.*, United States v. Monsanto Co., 858 F.2d 160 (4th Cir. 1988), *cert. denied*, 490 U.S. 1106 (1989) (holding that landowners may affirmatively avoid liability if they can prove that they did not know and had no reason to know that hazardous substances were disposed of on their land at the time they acquired title or possession and noting that CERCLA § 101(35) signaled Congress' intent to impose liability on landowners who could not satisfy the subsection).

Likewise, waiting for the government or another private party to file a lawsuit against the responsible parties is also time-consuming and expensive. Innocent landowners who elect to take no offensive action are still forced to incur the costs of defending themselves against lawsuits filed by other responsible parties. Additionally, innocent landowners bear the burden of proving the elements of their defense in court. In sum, whether the innocent landowner is the plaintiff or defendant in a civil action, retaining title to contaminated property is expensive because the current owner is inescapably involved in the remediation efforts.

The second alternative available to innocent landowners is a sale-of-property option. An innocent landowner who lacks sufficient resources to pursue a litigation option can attempt to sell the contaminated property and, upon transferring title, escape the liability provisions of the Act.[15] However, this second option similarly denies the innocent landowner the benefits of the defense. Because innocent landowners cannot transfer their status to subsequent purchasers, innocent landowners who sell contaminated property become indirectly liable for the entire remediation effort because the property must be devalued, at a minimum, by the estimated cleanup costs.

Innocent landowners who elect to sell their contaminated property must discount the purchase price by an amount sufficient to compensate the subsequent purchaser for the estimated costs of cleanup. When the subsequent purchaser acquires title to the contaminated property with knowledge of the contamination, the purchaser becomes jointly and severally liable for the entire costs of cleanup despite the fact that the acquisition postdates the contamination. Consequently, a purchaser must add the estimated cleanup costs to the purchase price to determine the true cost of the property.

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[15] CERCLA places liability for cleanup costs on three different groups: (1) individuals who owned the property at the time the property was contaminated; (2) individuals who accepted the hazardous waste for disposal, transport or treatment; and (3) the current owners. CERCLA § 107(a), 42 U.S.C. § 9607(a)(1988). The only theory upon which an innocent landowner can be held liable, absent the defense, is under category three, as a current owner of a contaminated site. Consequently, if such an owner transfers title and thereby drops out of category three, there is no theory by which the now former owner can be held liable. The former owner no longer faces liability under the Act, assuming, of course, that the owner did not exacerbate the contamination during the period of ownership.

Additionally, the subsequent purchaser will charge the innocent landowner a premium to compensate for the risk that the actual cleanup costs might exceed the estimated cleanup costs. After acquiring title, the purchaser will not be able to rescind the sale if he or she discovers that the cleanup will be more expensive than anticipated.[16] Therefore, the price the subsequent purchaser will pay for the contaminated property will equal the fair market value of the property after cleanup, less the estimated costs of cleanup, less an additional premium.

For example, suppose a current owner acquires a small parcel of land for $50,000 on which he or she plans to open a minimarket. Suppose further that before the acquisition the parcel was the former site of a gasoline station and that petroleum products leaked into the soil and onto a neighboring parcel. Assuming that the current owner had no reason to know that the property was contaminated at the time of purchase, the current owner is an innocent landowner under sections 9601(35)(A) and 9607(b)(3). Assume that, after title is transferred to this innocent landowner, the neighboring landowner discovers contamination leaching from the parcel and notifies the innocent landowner of the problem. Further investigation reveals that it will cost approximately $30,000 to clean up the property. If the innocent landowner has no available resources to undertake a cleanup effort, or to pursue a litigation option, or to fund a defense to establish its status as an

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[16] A typical example of the potential harm subsequent purchasers can suffer when actual cleanup costs exceed estimated cleanup costs is illustrated by Schurgin Development Corporation's experience when it acquired the Franciscan Prominade in Los Angeles, California. The Franciscan Prominade was the former site of a ceramics manufacturing plant. Before acquiring the site, Schurgin hired an environmental consultant. The consultant found piles of asbestos on the property along with unacceptable levels of lead and zinc in the soil. The consultant estimated the costs of cleanup to be approximately $3 million. Schurgin negotiated a purchase price reflecting the anticipated cleanup cost and acquired the site. The consultant had estimated the cleanup cost based on a new remediation technique called "waste washing." This process turned out to be an unacceptable method of treatment. Instead of cleansing the soil through waste washing, Schurgin was forced to seal the hazardous materials in layers of concrete and asphalt, a process called "capping." The cleanup costs ultimately exceeded $23 million. In addition to increasing the costs of cleanup, the capping ultimately decreased the fair market value of the property. *See* Lori Grange, *Building a Franciscan Mall Called a Long Shot Development: Because the $23 Million Toxic Cleanup at the Site Costs More Than Expected, the Builder Faces Foreclosure and the City Faces Loss of Funds*, L.A. TIMES, Nov. 15, 1990, at J1; Denise Hamilton, *Toxic Waste Cleanup at Atwater Will Begin Soon*, L.A. TIMES, May 14, 1987, § 9, at 1; Denise Hamilton, *$60 Million Shopping Center Proposed for Franciscan Site*, L.A. TIMES, June 1, 1986, § 9, at 1; Martha L. Willman, *$23 Million Cleanup Ends at Franciscan Site*, L.A. TIMES, Sept. 27, 1990, at J1.

innocent landowner, the innocent landowner will have to sell the property and recoup whatever value remains.

Although the innocent landowner will be able to avoid all of the costs associated with the litigation option by selling the property,[17] the innocent landowner is duty-bound to disclose his or her knowledge of the contamination to a subsequent purchaser, which means that the subsequent purchaser will not qualify for the innocent landowner defense once title is transferred, and will be jointly and severally liable for the estimated $30,000 cleanup costs. Consequently, the price a subsequent purchaser will pay for the property will be discounted accordingly.

In a perfect world, a subsequent purchaser should not discount the purchase price by the estimated costs of cleanup because the subsequent purchaser should be able to recoup the cleanup costs from other responsible parties. However, the subsequent purchaser will certainly not want to take the risk that there will be no solvent, responsible parties available to make a contribution. Additionally, the subsequent purchaser will be unwilling to take the risk that the actual cleanup costs will exceed the estimated $30,000. Consequently, the subsequent purchaser will discount the purchase price by $30,000, plus an additional amount as compensation for the additional risks.

In this hypothetical, suppose a subsequent purchaser will offer $10,000 for a parcel that will be worth $50,000 once $30,000 for cleanup is expended. The innocent landowner who does not have the resources to clean up the contaminated property or to pursue a litigation option must take a $40,000 loss on property that he or she purchased for $50,000. Although these numbers are fabricated, it is clear that the supposedly innocent landowner receives little economic benefit from the innocent landowner defense because of his or her inability to transfer the innocent landowner status to a subsequent purchaser.

The only real economic benefit innocent landowners receive from their defense occurs when the estimated cleanup costs exceed the value of the cleaned property. For example, suppose that in the above hypothetical the estimated cleanup costs for the contaminated property were $75,000. The innocent landowner in such a scenario would receive a real economic benefit from the defense worth $25,000, less the costs of establishing his or her status as an

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[17] *See* sources cited *supra* note 16.

innocent landowner. The innocent landowner will not be able to sell the property to a subsequent purchaser, but his or her liability is capped at the value of the property plus the costs of establishing the defense. No one can sue the innocent landowner for the cleanup costs after the innocent landowner establishes the elements of sections 9601(35)(A) and 9607(b)(3). If the property is cleaned up in the future, either by a responsible party or the government, the innocent landowner will then be able to market it and recoup some economic benefit. Until that date, however, the property will have a negative value, precluding the innocent landowner from selling it on the market.

CONCLUSION

There is no good reason to preclude subsequent purchasers of contaminated property having knowledge of the contamination from qualifying for the innocent landowner defense. If such transfers of the defense were allowed, the pool of responsible parties existing immediately prior to the transfer of title would be identical to the pool of responsible parties existing immediately after the transfer. No responsible parties would be relieved from liability by a transfer of contaminated property from an innocent landowner, who is by definition not responsible, to a subsequent purchaser who has knowledge of the contamination. Modifying the innocent landowner defense as suggested in this article would not relieve any potentially responsible parties from liability. In fact, allowing the transfer of status would probably result in faster remediations and more thorough cleanup efforts.

Innocent landowners who do not have the resources to file lawsuits against potentially responsible parties will theoretically delay a cleanup effort. A subsequent purchaser with greater resources who desires to clean up a parcel and use it for a more efficient purpose should be able to do so with the same protection against liability available to the innocent landowner who sold the property. These subsequent purchasers will speed remediations by filing lawsuits against responsible parties and forcing them to clean up the contaminated property. Alternatively, these subsequent purchasers may elect to clean up the property first, putting the property to a higher use at even an earlier date, and then sue the responsible parties for contribution. In either event, a subsequent purchaser who could qualify for innocent landowner status despite the fact that he or she acquired the property with knowl-

edge of the contamination could accelerate the remediation process. Nothing would be lost by allowing these subsequent purchasers to qualify as innocent landowners, and there is potentially much to gain.