Federal Case Law Favorable for Lenders Since 1996 CERCLA Amendments

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Nearly a decade has passed since the infamous 1990 Fleet Factors decision, which sent shock waves through the business and lending community. The Fleet Factors holding that a lender could be held liable by virtue of having the "capacity to influence" a company's treatment of hazardous waste was clearly at odds with the intent of the secured creditor exemption under the Comprehensive Environmental Response Compensation and Liability Act ("CERCLA"), also known as the federal Superfund statute. However, by diluting the secured creditor exemption and expanding liability for lenders who merely possessed the "capacity to influence" a borrower's treatment of hazardous waste, Fleet Factors created an environment of considerable uncertainty for lenders. In turn, this unnecessarily increased the cost of loan transactions and reduced the availability of capital.

Fortunately, it appears now that the impact of the Fleet Factors decision is finally behind us. With the ground rules for lender and fiduciary liability defined more fully by the 1996 amendments, the subsequent case law shows that lenders are once again able to move forward to provide loans to borrowers involved in hazardous waste sites without undue fear of being exposed to enormous cleanup costs under CERCLA.

Legislative Victory for Lender Protections:

The 1996 federal legislation was the result of years of perseverance by the lending community. Lenders had initially believed that their liability concerns were addressed in a 1992 EPA regulation that defined the framework for lender liability. Much to their dismay, lenders were once again in a state of limbo after a federal Circuit Court vacated EPA's "lender liability rule" in 1994. Uncertain of environmental liability risks, lenders continued to be haunted by Fleet Factors. Finally, in 1996, the enactment of the CERCLA amendments in essence overruled Fleet Factors and codified the language of EPA's "lender liability rule." The 1996 amendments also provided the necessary certainty for

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lenders by clarifying a number of situations when they can and cannot be held liable for environmental cleanup costs.

Case Law Post-1996 Amendments:

In the last two years, the courts appear to have heard Congress' message and have consistently limited liability for innocent lenders. A summary of the four relevant cases follows.

In Kelly v. Tiscornia, et al., the Sixth Circuit Court of Appeals held that the 1996 amendments "effectively codif[ied] the EPA rule," and affirmed the district court's decision in favor of the lender based on the amended statute. The Kelly court concluded that the lender was qualified to claim the secured creditor exemption because the lender had not "participated in the management" of the borrower within the meaning of EPA's lender liability rule. Based on the facts, the court found that the lender had neither "exercised decisionmaking control" nor "assumed or manifested responsibility for the overall management of the day-to-day decisionmaking" of the borrower "with respect to environmental compliance" or "with respect to all, or substantially all of the company's operational aspects other than environmental compliance."

In Canadyne-Georgia Corp. v. Nationsbank, a District Court in Georgia decided in the lender's favor on the grounds that the plaintiff (the owner of the contaminated site) failed to establish that the defendant (a successor lender) was a covered entity under CERCLA. Although the initial lender held a general partnership interest as well as a fiduciary interest as co-trustee for the facility, the Canadyne court concluded that the successor lender was neither an owner nor an operator of the facility for purposes of CERCLA and, thus, not liable for cleanup costs because the lender did not exercise "substantial" or "pervasive" control over the operations of the facility.

In F.P. Woll & Co. v. Fifth and Mitchell St. Corp., et al., a District Court in Pennsylvania decided a pretrial motion against a defendant/lender in connection with a plaintiff/owner's response cost recovery action because the court found that the lender was the operator of the debtor's business after foreclosure and, thus, liable for cleanup costs. The F.P. Woll court concluded that the lender could not be shielded from cleanup

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cost liability under the secured creditor exemption because the lender's conduct constituted "active management" of the debtor's operation and involved "much more than a mere foreclosure to protect its security interest." Although the analysis is consistent with the framework of EPA's lender liability rule, the F.P. Woll decision is significant because the court recognized that the lender/secured creditor protection is not absolute under CERCLA.

Finally, in United States v. Pesses, et al., a District Court in Pennsylvania denied a pretrial motion against a savings and loan association on the grounds that the lender qualified for the secured creditor exemption under CERCLA. Since the Pesses court concluded that (1) the lender did not participate in the management of the facility while the borrower was still in possession, and (2) the lender divested itself of the facility "at the earliest practicable [time on] commercially reasonable terms," the lender was not liable for cleanup costs as an "owner or operator" of the facility.

Conclusion:

Although only a few cases have been decided on the issue of lender liability since the 1996 CERCLA amendments, lenders and the business community in general have good reason to be pleased with the developing case law. Since all of the decisions have largely been consistent with the new rules, the lending community can make loans to borrowers with some assurance that innocent lenders will not be exposed to cleanup costs. As a result, it appears the Fleet Factors chapter has finally come to an end.

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