Legal Trends in Environmental Law
Frank J. Petrino

Index

A. Prospective Purchaser Agreements
- (1) With EPA
  - (a) Advantages/Benefits
  - (b) Disadvantages
  - (c) Impact of 2002 Brownfields Amendments
- (2) With NJDEP
  - (a) Benefits
  - (b) Limitations
- (3) EPA Materials (Appendix A)
- (4) NJDEP Prospective Purchaser Agreement (Appendix B)

B. Natural Resource Damages
- (1) Understanding Natural Resource Damages
- (2) A closer Look at the Injuries
- (3) Questioning the Formula used to calculate the Ground Water Injury Value
- (4) Who is Responsible for NRD?
- (5) Voluntarily Resolving Natural Resource Damage Liability
- (6) The Brownfield Act
- (7) Reimbursement Agreements

C. Environmental Insurance
- (1) Cap Insurance Overview
- (2) Pollution Legal Liability Insurance
- (3) Is there coverage for Natural Resource Damages?

A. Prospective Purchaser Agreements

(1) With EPA.

Prospective Purchaser Agreements (**"PPAs"**) are settlement mechanisms used to provide liability relief to a purchaser of Superfund property prior to acquisition, thus allowing the purchaser to avoid becoming a potentially responsible owner for pre-existing contamination under the Superfund liability scheme. Only prospective purchasers who had nothing to do with the contamination of the site are eligible.

The January 2002 Brownsfields Amendments significantly altered the Superfund liability scheme by providing liability protection to bona fide prospective purchasers (**"BFPP's"**). As a result, EPA believes that, in most cases, the Brownsfields Amendments make PPAs from the federal government unnecessary. However, EPA will still consider providing a prospective purchaser with a covenant not to sue in limited circumstances, where the public interest will be served. More information on EPA's policy regarding prospective purchase agreements is available from Bona Fide Prospective Purchasers and the New Amendments to CERCLA (See Memorandum in **Appendix A**).

a. Advantages/Benefits

i. The protection against contribution claims by third parties.

ii. The covenant of the United States not to sue for civil liability for injunctive relief or response costs.

iii. Negotiation of the PPA, including resolution of the required remedial work, is likely to take considerably

less time than the remedial investigation/feasibility study process required under the Federal Superfund Program and most of its state counterparts.

iv. Purchaser can bet or quantify costs and thus facilitate financing.

v. The Agreement, to the extent that it defines the nature of required remediation, allows a Purchaser to better quantify the costs associated with the purchase and minimize uncertain or unknown liability costs from pre-existing contamination. Moreover, the Purchaser is much more likely to receive financial assistance from lending institutions when the institution can be satisfied that environmental response costs are highly unlikely in the future.

b. Disadvantages

i. Potential liability under state law remains.

ii. The potential Purchaser may not be able to maintain cost recovery actions against responsible parties.

iii. Insurance claims by the prospective Purchaser may be precluded.

iv. At industrial sites, the Purchaser may have to prove that newly discovered contamination was pre-existing.

v. The EPA may assert claims not covered by its covenant not to sue.

vi. Natural resource damage claims are generally not covered by the covenant.

c. Impact of 2002 Brownfields Amendments

EPA's long-standing policy is not to become involved in purely private real estate transactions. The Brownsfields Amendments reinforce the appropriateness of that policy. The Amendments provide a limitation on liability from CERCLA to persons who qualify as BFPPs thereby making a federal covenant not to sue under CERCLA unnecessary. In light of the new Amendments, purchaser should no longer need PPAs with the federal government in order to complete the vast majority of real estate transactions involving contaminated property.

While EPA believes the necessity for PPAs has been largely addressed by congressional action, the Agency recognizes that in limited instances the public interest will be served by entering into PPAs or some other form of agreement. First, where there is likely to be a significant windfall lien, and the purchaser needs to resolve the lien prior to purchasing the property (e.g. to secure financing), EPA may consider entering into an agreement with purchaser.

Second, there may be projects in which a PPA is necessary to ensure that the transaction will be completed and the project will provide substantial public benefits to, for example, the environment, a local community

because of jobs created or revitalization of long blighted, under-utilized property, or promotion of environmental justice.

(2) With NJDEP.*

Under the Tech Regs, as amended in 2003, a "prospective purchaser" is someone who is considering acquiring contaminated property and

- Is not responsible under any federal, state or common law for hazardous substances, hazardous wastes or other pollutants discharged at the contaminated site; and
- Is not a corporate successor to, or capitalized by, any person who is in any way responsible under any federal, state or common law for hazardous substances, hazardous wastes or other pollutants discharged at the contaminated site.

a. Benefits

DEP will consider entering into Prospective Purchaser Agreements (PPAs) in certain cases prior to the purchaser taking title to contaminated property and before the issuance of the NFA/CNTS. The DEP will consider entering into a PPA as long as some party (the seller, the buyer or some other party) is conducting a cleanup under the oversight of the PPA, the DEP and Division of Law (DOL) document preparation costs are paid, and the purchaser agrees to pay a settlement premium. The PPA will offer the purchase liability protection from the DEP (but not from third parties) between the time that the contaminated land is purchased and the time that the NFA/CNTS is issued. Another benefit of a PPA is that it can "lock a purchaser in early at a lower cost,"

referring to the environmental settlement premium sought, as opposed to when the property is clean and more attractive to developers. The purchaser and "qualifying successors" will receives a CNTS from DEP stating that it will not institute civil action or claims for further cleanup under the Spill Act and the Water Pollution Control Act for contamination known to DEP to have been discharged prior to the acquisition of the purchaser's title.

b. Limitations

The PPA will not provide contribution protection against claims by third parties nor claims for natural resource damages. The PPA contains reopeners for fraudulent or false certifications, failure to timely provide the environmental protection premium, failure to timely remit the PPAA administrative preparations costs and failing to take title by the date set forth in the agreement.

There are two important reservations of rights in the PPA. The first provides that if the purchaser commits to perform a cleanup and fails to do so, the PPA will be terminated if the purchaser fails to cure the breach within 30 days notice by DEP of the breach. If the PPA is terminated for failing to properly implement the cleanup, the DEP CNTS will become null and void. However, the PPA provides that the purchaser will not automatically lose the other protections of the PPA.

The second important reservation involves the situation where a party other than the purchaser is performing the cleanup. If the third party fails to timely perform the cleanup, DEP reserves the right to revoke the

PPA after providing written notice to the purchaser and the remediating party. DEP may also revoke the PPA if it determines that the cleanup is not being performed in accordance with the Tech Regs.

Some developers are using PPAs to provide comfort to purchasers of condominium units that are constructed on a contaminated site. Some developers have also entered into PPAs to aid with the disclosure statements that are used in connection with the sale of condominiums.

*Goldshore, Brownfields Law and Practice, §NJ.03 [5]

(3) EPA Materials (Appendix A)

(4) NJDEP Prospective Purchaser Agreement (Appendix B)

Contact Persons at NJDEP

- Phyllis Bross, DAG (609) 984-4863
- Sue Boyle (609) 633-2933

B. Natural Resource Damages

(1) Understanding Natural Resource Damages

In order to understand the theory behind natural resource damages, it is first important to understand what natural resources are. Natural resources are "all land, fish, shellfish, wildlife, biota, air, waters and other such resources owned, managed, held in trust or otherwise controlled by the State." N.J.S.A. 58:10-23.11b; N.J.A.C. 7:26E-1.8; see also 42 U.S.C.A. §9601(16). An injury to natural resources is defined as "any adverse change or impact of a discharge on a natural resource or impairment of natural resource service, whether direct or indirect, long-term or short-term, and includes the partial or

complete destruction or loss of the natural resource." N.J.A.C. 7:26E-1.8. Injuries can be ecological based, such as the contamination of a stream habitat and/or use based, such as the public's inability to use the same stream for fishing.

Restoration is the remedial action that returns a natural resource to its pre-discharge condition. It includes the rehabilitation of an injured resource, replacement, or acquisition of a natural resource and its services, which were lost or impaired. Restoration also includes compensation for the natural resource services lost from the beginning of the injury until the resource is fully recovered.

Natural resource damages, therefore, are the dollar value of the restoration that is necessary to restore the injured resource and to compensate the citizens of the State for the injury to natural resources as a result of a discharge. Natural resource damages are not fines and are not punitive. They are compensatory.

(2) A Closer Look at the Injuries

All of the information that is needed to assess and restore natural resource injuries will be generated as part of the site characterization process, set forth in the Technical Requirements for Site Remediation, N.J.A.C. 7:26E-1 et seq. Generally, there is no need for additional sampling or studies.

Characterization of natural resource injuries falls into two categories: ecological injury, which involves federal co-trustees, and ground water injury, which is the sole responsibility of the State. In evaluating ecological

natural resource injuries, there are two items that must be considered: a baseline ecological evaluation, and if necessary, an ecological risk assessment.

A baseline ecological evaluation is required of each person conducting the remediation of a contaminated site or area of concern to ensure that the resulting remedy is protective of the environment. N.J.A.C. 7:26E-3.11. DEP uses this information to determine whether or not natural resource injuries potentially exist as a result of a discharge at a site. The following criteria are examined: (1) the presence of a contaminant of ecological concern[1] that exists at the site; (2) the presence of an environmentally sensitive natural resource at or near the site; and (3) a pathway that would link the contaminant of ecological concern with the environmentally sensitive natural resource. Id. If all three things are present, then an ecological risk assessment is required. Id., see also N.J.A.C. 7:26E-4.7.

An ecological risk assessment is the process through which the person responsible for conducting the remediation evaluates the likelihood that adverse ecological effects to natural resources have occurred, are occurring, or may occur, as a result of a discharge. In addition to using the ecological risk assessments to ensure that the remedy is protective of the environment, DEP uses the risk assessment to identify and characterize the injuries to natural resources and natural resource services. Often, the results of the risk

---

[1] A contaminant of ecological concern includes a contaminant that exhibits the ability to biomagnify or bioaccumulate, as well as a contaminant with a concentration that exceeds the applicable standards or guidelines recommended by DEP, the United States Environmental Protection Agency, the National Oceanic and Atmospheric Administration, or other federal natural resource agencies. DEP has outlined some of the references that may be used in identifying a contaminant of ecological concern for specific environmental media at N.J.A.C. 7:26E-3.11(a).

assessment can be use to provide the scope of restoration necessary to compensate for the injury.

In evaluating ground water injury, DEP considers ground water to be "injured" when contaminants are above the New Jersey Ground Water Quality Standards. DEP then looks at the delineation of the horizontal and vertical extent of the ground water contamination. DEP utilizes a ground water injury calculation developed and applied by DEP's Office of Natural Resource Restoration ("ONRR"). This formula incorporates plume size, duration of injury, ground water recharge rates and water rates in order to derive a monetary value (damages) for injuries to ground water resources of the State. The resulting surrogate value is then used to determine the appropriate scale of the restoration project.

A copy of the formula used by DEP to calculate the Ground Water Injury Value is attached in **Appendix C**.

(3) Questioning the Formula used to calculate the Ground Water Injury Value

There are certain factors incorporated into the formula that DEP is not willing to modify when doing its calculation. For example, the water rate is derived from both the planning area and projected status and the annual ground water recharge as determined from the New Jersey Statewide Water Supply Plan 1996. (Actually, the water rate is an average for each particular area, as opposed to looking at each individual municipality). A responsible party can, however, ensure that DEP has the most accurate information that exists regarding the aerial extent of the contaminant plume. If a responsible party receives a calculation and determines that the values are not consistent with the

information it has, it should notify DEP and have a revised calculation completed. Likewise, if a responsible party has information that would affect the duration of the contamination, it should be brought to DEP's attention.

There are additional arguments that could be made, however, they have not been successful thus far. These arguments include:

1. if ground water is being remediated, the remedy selected (e.g., active pump and treat vs. natural attenuation) may impact the amount of uncontaminated ground water available for future use;
2. the size of a ground water plume may decrease over time, but the formula does not account for it and therefore, overstates damages;
3. instead of using an average water rate as a measure of the loss resulting from reduced ground water availability, a more appropriate measure would be the difference between the costs of using the contaminated water in an uncontaminated state and the cost of alternative sources to supply replacement water;
4. the formula assumes that 100% of recharge water is available for potential use and is therefore impacted by a contaminated plume, which is almost certainly not the case; and
5. the formula does not account for the quality and quantity of water that would otherwise be available but for the contamination.

(4) Who is Responsible for NRD?

One of the primary sources for the State's authority to seek natural resource damages is the New Jersey Spill Compensation and Control Act ("the Spill Act"), N.J.S.A. 58:10-23.11 et seq. (See also the Water Pollution Control Act, N.J.S.A. 58:10A-1 et seq., the Industrial Site Recovery Act, N.J.S.A. 13:1K-6 et seq., and the Brownfield and Contaminated Site Remediation Act ('the Brownfield Act"), N.J.S.A. 58:10B-1 et seq.) The Spill Act defines cleanup and removal costs as "all costs associated with a discharge, incurred by the State…in the:…(2) taking of reasonable measures to prevent or mitigate damage to the public health, safety, or welfare, including, but not limited to, public and private property, shorelines, beaches, surface waters, water columns and bottom sediments, soils and other affected property, including wildlife and other natural resources…." N.J.S.A. 58:10-23.11b.

Any person who is deemed responsible under the Spill Act for the discharge of hazardous substances, is "strictly liable, jointly and severally, without regard to fault" for cleanup and removal costs. N.J.S.A. 58:10-23.11g(c)(1). Likewise, the Spill Fund is "strictly liable, without regard to fault, for all cleanup and removal costs and for all direct and indirect damages no matter by whom sustained, including but not limited to: (2) the cost of restoration and replacement, where possible, of any natural resource damaged or destroyed by a discharge…." N.J.S.A. 58:10-23.11g(a)(2). DEP, or the Spill Fund, is then given the authority to seek recovery of such costs or damages from a responsible party. N.J.S.A. 58:10-23.11q.

(5) Voluntarily Resolving Natural Resource Damage Liability

DEP has taken the position that if a party approaches DEP and wishes to resolve its natural resource damage liability, ONRR will use its formula (See **Appendix C**) in valuing ground water injury. A non-volunteer, or a party who receives a notice letter regarding its liability, would not be given the option of using that formula and instead, would be subject to a more "rigorous" valuation. The more "rigorous" valuation has not been made public in the form of an actual formula, however, it is my understanding that it may consider both a three-dimensional plume and may look at the duration of injury not only prospectively, but also retroactively back to the date of the original injury.

(6) The Brownfield Act

Redevelopers who acquire property on or after January 6, 1998 (the effective date of the Brownfield Act) may, according to the January 19, 2005 amendment to the Brownfield Act, be afforded liability protection against natural resource damage claims at Brownfield sites, provided the following conditions are met:

(a) the redeveloper acquired the property after the discharge of a hazardous substance took place at the property;

(b) the redeveloper is in no way responsible for the discharge of a hazardous substance at the property, and is not a corporate successor to the responsible party; and

(c) the redeveloper did not contractually agree to assume natural resource damage liability as part of its acquisition or otherwise.

Before the amendment, DEP limited its policy of not pursuing natural resource damages from redevelopers to a limited subset of "innocent purchasers."[2]

The statute of limitations for filing natural resource damage claims was also recently amended. The limitations period for those claims is four years. The amendment provides that the period cannot have begun to run before (a) January 1, 2002, or (b) the completion of the remediation investigation for the

---

[2] The Spill Act provides an affirmative defense to liability, which includes liability for natural resource damages, for innocent property purchasers who perform due diligence investigations. Pursuant to N.J.S.A. 5810-23.11g(d), a person who owns real property acquired on or after September 14, 1993 shall be considered a responsible party for discharged hazardous substances unless he can demonstrate:

1. the property was acquired after the contamination occurred;
2. the purchaser did not know and had no reason to know about preexisting contamination because an appropriate due diligence inquiry was made before the sale;
    a. to establish that a person had no reason to know of the discharged hazardous substances, the person must undertake all appropriate inquiry into the previous ownership and uses of the property, meaning the performance of a preliminary assessment, and site investigation, if the preliminary assessment indicates that a site investigation is necessary.
3. the purchaser was not a discharger or in any way responsible for the hazardous substance and is not a corporate successor to the discharger or responsible party;
4. DEP was notified upon discovery of the discharge; and
5. if contamination is found on the property as a result of an appropriate inquiry, it must be remediated, or the purchaser must rely on a No Further Action ("NFA") letter issued prior to the acquisition (but after January 6, 1998), or the purchaser (or seller) must obtain and comply with a remedial action work plan ("RAWP"), including requirements for engineering and institutional controls. The person who completes the remediation is eligible for an NFA letter.

site, whichever is later. Prior to this statutory change, subsection (b) stated that DEP was given until the performance of the preliminary assessment, site investigation, and remedial investigation, if necessary, of the contaminated site, whichever is later, to bring its natural resource damage claims. See N.J.S.A. 58:10B-17.1. The benefit to the revision for DEP is that a remedial investigation could take years to be complete (meaning there will not be as many lawsuits filed in the near future), and, it provides DEP with what it claims is more complete information with which to perform a natural resource damage assessment.

DEP does not yet have a formal process in place to determine that a developer of a Brownfield Site qualifies under the January 19, 2005 amendment, however, it may implement the following:

(a) In cases where there is a developer conducting the remediation of a contaminated site, who is not responsible for the discharge and is in the process of getting a NFA, the developer would submit a certification to DEP stating that he or she is eligible for the protection provided in the Brownfield Act. DEP will then review that certification along with the final report for the NFA. The NFA will be issued and DEP will make a note to pursue whoever is responsible for the contamination for natural resource damages.

(b) In cases where a developer merely acquires the contaminated property and there is another party conducting the remediation, the process is more problematic. In that case, DEP will not issue an NFA until the other party resolves its natural resource damage liability.

7. Reimbursement Agreements

N.J.S.A. 58:10B-27 permits developers to enter into redevelopment agreements with the State, provided the developer is not liable for the contamination at the site proposed to be the subject of the redevelopment agreement. That developer may then be eligible for reimbursement of up to 75% of the remediation costs. N.J.S.A. 58:10B-28. To qualify for the certification of reimbursement of the remediation costs, the developer must enter into a Memorandum of Agreement (See **Appendix D**) or other oversight document with DEP for remediation of the site of the redevelopment project. N.J.S.A. 58:10B-29.

Given the fact that "cleanup and removal costs" are defined to include natural resource damages, see N.J.S.A. 58:10-23.11b., there is an argument that "remediation costs" should also include natural resource damages. Then, by virtue of a redevelopment agreement, a developer could seek recovery of up to 75% of the natural resource damages that a developer is liable for paying. In light of the recent amendment to the Brownfield Act, however, developers are now explicitly exempt from liability for natural resource damages and no longer have to satisfy the strict requirements of an innocent purchaser.

C. Environmental Insurance

(1) Cap Insurance Overview

It is very difficult to predict the exact quantity of contaminated soil or tainted groundwater within a high degree of certainty. Most contractors' cleanup bids are on a contingency basis, dependent on time and materials. This often leaves owners with a high degree of uncertainty regarding the final cost of a cleanup. Gerrard, Michael B., *Brownfields Law and Practice*, 28.02[5](a), 28-57 (2004).

Consequently, many parties to real estate transaction look to Environmental Impairment Insurance to allocate risk effectively. Witkin, James B., *Environmental Aspects of Real Estate Transactions*, 329 (American Bar Association 1995). This type of insurance comes in a variety of forms including, "off-the-shelf" policies and custom-designed policies. Specifically, you were interested in environmental "cap" insurance. Environmental "cap" insurance combines traditional environmental remediation insurance with self-insurance and is useful for controlling losses at properties with known environmental problems. Id. at 336. Cleanup cost cap (sometimes referred to as "stop loss" insurance) manages the economic risk when environmental remediation projects exceed the projected cost. Gerrard at 28-57. "This form of stop-loss insurance caps the financial exposure of environmental remediation projects for owners and investors alike. In fact, cleanup cost cap insurance can be a key component of an investment strategy…" Id. Typically, the cost cap insurance is based on the cleanup costs associated with a defined remedial implementation. The policy is

triggered when the cleanup costs exceed a self-prescribed "self-insured retention", usually equal to the expected cleanup cost plus a previously agreed upon buffer. Id. at 28-58. The insurer bears the risk of all cleanup costs in excess of the "stop loss" amount, up to the policy limit. Witkin at 336.

For example, a project with an expected cleanup cost of $1 million may carry a contingency of $250,000. When project costs exceed $1,250,000, the cost cap policy is triggered from that point up to the limit of liability. The cost of this type of policy is estimated at an average of six to eight percent of coverage. Id. However, there has been some difficulty for owners in projecting remedial costs, causing confusion as to how much insurance to obtain, which may cause some underwriters to require high coverage with its associated premium cost. Gerrard at 28-59.

This "stop loss' insurance contains an important underwriting option pertaining to control of the actual cleanup. Under the first option, the policyholder retains the right to select and supervise the environmental engineers, subject to the insurer's approval. This option is attractive to informed policyholders with experience in environmental remediation. Under the second option, the insurance company selects and oversees the consultants, which is useful for parties lacking experience in supervision of cleanup activities. Witkin at 336.

Parties should note that cap insurance does not cover the cost to clean up any other contamination discovered during the course of this insured cleanup. Additionally, coverage under this type of policy ends when the project is completed and the insured receives a No Further Action Letter or similar

documentation from the applicable governmental authority having jurisdiction over the cleanup. Waiger, Ann M., *Current Insurance Policies for Insuring Against Environmental Risks* (1999).

If the estimated cost of cleanup is very high, a developer may choose to purchase "finite risk insurance", a type of cost cap insurance that applies to the entire estimated cost of remedy and potential overruns. This funding mechanism mirrors whole life insurance. Under this form of insurance, the insured pays a premium equal to the net present value of the estimated cleanup cost. During the policy period, which can extend for 40 years, the insured is reimbursed by the carrier for its cleanup costs based on an agreed upon schedule. Id. at 28-58. This form has many benefits, including a very long coverage period; a share in the insurance company's return on the invested funds which effectively lowers the costs of coverage; a number of tax advantages; and the opportunity to permanently remove environmental liabilities from the company's balance sheet. Id.

Included in **Appendix E** is a specimen form of Clean-up Cost Cap insurance. The coverage provided is for on-site clean up costs in excess of the Self-Insured Retention for known pollutants and unknown pollutants. Coverage for, inter alia, Bodily Injury, Property Damage and Third-party Liability is excluded.

(2) Pollution Legal Liability Insurance

Coverage under Pollution Legal Liability Insurance (hereinafter "PLL") applies to pollution conditions from or at a specified location. The

pollution condition can be pre-existing or can arise during the policy term; if the condition is pre-existing, it can be either unknown or known (provided that it was disclosed to the insurer during the application process). Generally, a pre-existing condition will be covered if the regulatory agency has issued a No Further Action letter with regarding to the known contamination or where the levels of contamination are low or narrow. Gerrard at 28-60.

This type of policy is useful following the completion of actual environmental remediation and after a cost cap program would be expected to respond. Id. at 28-59. Once remediation is completed, PLL provides coverage options for: onsite cleanup of environmental releases from new site operations; onsite cleanup of undiscovered contamination from prior site operations; government reopener and third-party liability protection for known contaminants from prior operations; and offsite cleanup, bodily injury and third-party liability for environmental releases from new site operations or prior conditions. Id.

The essential damages this type of policy covers are third-party bodily injury and property damage and first and third-party cleanup costs. (Other types of damages, such as business interruption, transportation liability and delayed construction costs can be added at an increased premium). Generally, a claim made and reported during the policy period is a prerequisite to coverage of third-party bodily injury and property damage. Id.

A PLL policy is an effective tool for managing risk in a real estate transaction involving commercial or industrial property where potential contamination may come to light. Id. However, these policies generally have

exclusions for asbestos and lead paint; there is normally no coverage for contamination resulting from intentional noncompliance with environmental regulations; and some policies exclude contamination from leaking of underground storage tanks. Id. See also, Waiger at 502.

Included in **Appendix F** is specimen form of a Pollution Legal Liability policy. In addition to providing clean-up cost cap coverage for on-site pre-existing and new conditions, coverage is also provided for, inter alia, off-site clean up and on-site and off-site bodily injury and property damage. Among the excluded coverage is intentional non-compliance. The coverage is typically on a claims made basis (i.e., occurrence and claim must occur during the time that the policy is in force). The defense costs reduce the "applicable limit of liability". A condominium association could be added as an additional insured and would have coverage for the period of time that the policy is in force.

(3) Is there coverage for Natural Resource Damages?

Nevius and Ellison, You Should Be Covered for **Natural Resource Damages,** New Jersey Law Journal, February 2, 2004.

Contact:

Frank J. Petrino
Sterns & Weinroth, P.C.
Trenton, NJ
(609) 989-5029
fpetrino@sternslaw.com