

SB

154

SENATE COMMITTEE REPORT
FIRST COMMITTEE OF REFERRAL

DATE: 3/1/91

FURTHER: Judiciary

Date of 5-Day Notice: 3/4/91
(in accordance with Uniform Rule 23)

DATE TURNED INTO OFFICE: _____

Resources Committee considered SB 154

Liability for environmental damage and to liens arising from environmental damage.

and recommended:

- replace with _____ CS SB 154 Res same title
- attached amendment(s) new title
- _____ letter of intent adopted

do pass

do not pass

no recommendation

individual recommendations

further referral to _____

ATTACHES NEW FISCAL NOTE(S):

fiscal note(s) Dept/Date _____

zero fiscal note(s) Dept/Date _____
Previous FN DEC 3/18/91

appropriation-no fiscal note

Governor's bill w/fiscal note

SIGNING DO PASS:

[Signature]

OTHER RECOMMENDATIONS:

[Signature] NO Re
[Signature]

[Signature]
 Chair: Signature and Recommendation

CS FOR SENATE BILL NO. 154 ()

IN THE LEGISLATURE OF THE STATE OF ALASKA

SEVENTEENTH LEGISLATURE - FIRST SESSION

BY

Offered:
Referred:

Sponsor(s): SENATOR RODEY

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to the liability of financial institutions for environmental damage or the
2 threat of environmental damage and to liens arising from environmental damage or the
3 threat of environmental damage."

4 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

5 * Section 1. AS 46.03.822(a) is amended to read:

6 (a) Notwithstanding any other provision or rule of law and subject only to AS 46.03.825.
7 the defenses set out in (b) of this section, and the exception set out in (i) of this section, the
8 following persons are strictly liable, jointly and severally, for damages to persons or property,
9 whether public or private, including damage to the natural resources of the state or a
10 municipality, and for the costs of response, containment, removal, or remedial action incurred by
11 the state or a municipality, resulting from an unpermitted release of a hazardous substance or,
12 with respect to response costs, the substantial threat of an unpermitted release of a hazardous
13 substance:

14 (1) the owner of, and the person having control over, the hazardous substance at

1 the time of the release or threatened release; this paragraph does not apply to a consumer product
2 in consumer use;

3 (2) the owner and the operator of a vessel or facility, from which there is a
4 release, or a threatened release that causes the incurrence of response costs, of a hazardous
5 substance;

6 (3) any person who at the time of disposal of any hazardous substance owned or
7 operated any facility or vessel at which the hazardous substances were disposed of, from which
8 there is a release, or a threatened release that causes the incurrence of response costs, of a
9 hazardous substance;

10 (4) any person who by contract, agreement, or otherwise arranged for disposal or
11 treatment, or arranged with a transporter for transport for disposal or treatment, of hazardous
12 substances owned or possessed by the person, other than domestic sewage, or by any other party
13 or entity, at any facility or vessel owned or operated by another party or entity and containing
14 hazardous substances, from which there is a release, or a threatened release that causes the
15 incurrence of response costs, of a hazardous substance;

16 (5) any person who accepts or accepted any hazardous substances, other than
17 refined oil, for transport to disposal or treatment facilities, vessels or sites selected by the person,
18 from which there is a release, or a threatened release that causes the incurrence of response costs,
19 of a hazardous substance.

20 * Sec. 2. AS 46.03 is amended by adding a new section to read:

21 Sec. 46.03.825. FINANCIAL INSTITUTIONS. (a) Except as provided by (b) of this
22 section, a financial institution is not liable under AS 46.03.822 - 46.03.828 for damages or costs
23 resulting from an unpermitted release of a hazardous substance or the substantial threat of an
24 unpermitted release of a hazardous substance at or from a facility or vessel that

25 (1) the institution acquires through foreclosure;

26 (2) the institution holds as a lessor under the terms of an extension of credit;

27 (3) is subject to the financial control or financial oversight of the institution under
28 the terms of an extension of credit, if the institution does not exercise actual, direct, and continual
29 managerial control that materially divests the borrower, debtor, or obligor of control of the
30 facility or vessel; or

31 (4) the institution acquires in a fiduciary capacity.

1 (b) A financial institution may be required to reimburse the state for the actual benefit
2 received by the institution that results from a response, containment, removal, or remedial action
3 undertaken by the state involving a facility or vessel identified under (a)(1) of this section, but
4 the liability for the reimbursement, including the payment of a state lien, may not exceed the fair
5 market value of the facility or vessel.

6 (c) In this section, "financial institution" means

7 (1) a bank, credit union, or savings association if the deposits of the bank, credit
8 union, or savings association are insured in whole or in part by the Federal Deposit Insurance
9 Corporation, by another agency of the United States, or by an agency of the state;

10 (2) a trust company that is owned in whole or in part by a bank or that is subject
11 to regulation by the United States Comptroller of the Currency.

12 * Sec. 3. AS 46.08.075(a) is amended to read:

13 (a) The state has a lien for expenditures by the state from the oil and hazardous substance
14 release response fund or from any other state fund, for the costs of response, containment,
15 removal, or remedial action resulting from an oil or hazardous substance spill, or, with respect
16 to response costs, the substantial threat of a release of oil or a hazardous substance against the
17 facility or vessel that is [ALL PROPERTY] owned by a person who is determined by the
18 commissioner to be liable for the expenditures under this chapter, AS 46.03, AS 46.04, 42 U.S.C.
19 9607, or other state or federal law, and that is subject to the state's response, containment,
20 removal, or remedial action. The lien includes interest, at the maximum rate allowable under
21 AS 45.45.010(a), from the date of the expenditures. The state may file an action in a court of
22 competent jurisdiction in order to foreclose on the lien.

23 * Sec. 4. AS 46.08.075 is amended by adding a new subsection to read:

24 (f) The lien imposed by this section is subject to the rights of a purchaser, holder of a
25 security interest, or judgment lien creditor if the interest of the purchaser, holder, or creditor is
26 perfected under applicable law before notice of the lien is filed in the appropriate recorder's
27 office under (b) of this section. The purchaser, holder of a security interest, or judgment lien
28 creditor shall be afforded the same protections against the lien imposed by this section as are
29 afforded under state law to a purchaser, holder of a security interest, or judgment lien creditor
30 against a judgment lien that arises out of an unsecured obligation and that arises at the same time
31 the notice of the lien created under this section is filed.

- 1 * Sec. 5. AS 46.08.075(e) is repealed.
- 2 * Sec. 6. AS 46.03.825, enacted by sec. 2 of this Act, applies according to its terms to a release or
- 3 threat of a release that occurs after the effective date of this Act even if the facility or vessel was
- 4 acquired or held by the financial institution before the effective date of this Act or was subject to the
- 5 financial control or financial oversight of the institution before the effective date of this Act.

Section 1. AS 46.03.822 (c) is amended to read:

(c) For purposes of (b)(1)(B) of this section, a third party or an agent of a third party is in privity of contract with the person who is otherwise liable, if the third party or its agent and the person are parties to a land contract, deed, or other instrument transferring title or possession of the real property on which the facility in question is located, unless that property was acquired by the person after the disposal or placement of the hazardous substance on, in, or at the facility, and the person establishes that the person has satisfied the requirements of (b)(1)(B) of this section and establishes that

(1) at the time the person acquired the facility the person did not know and had no reason to know that a hazardous substance that is the subject of the release or threatened release was disposed of on, in,, or at the facility;

(2) the person is a governmental entity that acquired the facility by escheat, or through another involuntary transfer or acquisition, or through the exercise of eminent domain authority by purchase or condemnation;

(3) the person is a corporation organized under 43 U.S.C. 1601-1629e (Alaska Native Claims Settlement Act) that acquired the facility under those sections;

(4) the person acquired the facility by inheritance or bequest;

[or]

(5) the person is a state governmental entity and the state acquired the facility under Public Law 85-508 (Alaska Statehood Act)[.]; or

(6) the person's interest in the facility arose as a lender to a person owning or controlling the facility or arose as a security holder in the facility, and the person has not controlled, managed, or influenced the operations at or on the facility, whether or not it had the capacity to do so.

***** F A X T R A N S M I T T A L M E M O *****	
TO: <u>Tim Benintendi</u>	NO. OF PAGES 2
DEPT: _____ FAX #: <u>463-3144</u>	
FROM: <u>Staley D.</u> PHONE: <u>452-1855</u>	
CO: <u>Barbara S.</u> FAX #: <u>452-B154</u>	
Post-It brand fax transmittal memo 7671	

Memo to Dan Mogck
From: Barbara Schuhmann
03-26-91

Re: "Trust Company" definition

There is only one trust company in the state of Alaska, Key Trust, according to Terry Lutz, Division of Banking, 465-2521. He advised that anyone can attempt to form a trust company. Ownership is not limited to banks. Key Trust is wholly owned by Key Bank of Alaska. The Alaska Division of Banking apparently must authorize the formation of a state trust company. There are no other state regulations per se as to state trust companies.

The national banks apparently operate trust departments under regulation of the Comptroller of the Currency. This information came to me from a trust officer at the Trust Department of National Bank of Alaska.

No trust company has "deposits", so the way the first draft was worded, Key Trust might not be construed to be included in the type of financial institution whose liability is limited. I think we should re-work the definition in our proposed bill to state:

"No trust company, and no bank, credit union, or savings association, the deposits of which are insured . . ."

If that is too comprehensive for the legislature, we could limit "trust company", to something like:

"No trust company which is wholly-owned by a bank or subject to regulation by the Comptroller of the Currency, and no bank, credit union, or savings association, the deposits of which are insured . . ."

Also, we might insert the word "which" right before subpart (1) and the word "is" at the beginning of subpart (3). The order of the subparts of (a) could be switched around. I am not sure we need all the language of subpart (3) but because of federal decisions, it would probably be better to retain it all.

After giving subpart (b) more thought, I believe we should make it clear that the limit of liability of an institution is the benefit received. Since third parties (besides the state)

could claim they conferred a benefit, the liability should be restricted to reimbursing the state's funds that confer a benefit. Payment should then release any lien the state may have. The state should not be able to recover the "benefit conferred" and also have a lien on the property benefitted. The state has a lien for its expenditures against property owned by persons liable for such expenditures. AS 46.08.075(a). If the lender has not yet foreclosed, it should be able to remove the state's junior lien but be responsible for any benefit received from the state. If the lender has already foreclosed, the state's lien should be released upon payment of the limited amount the institution may owe to the state.

BLS:695

 FAX TRANSMITTAL MEMO
 TO: Tim Benintendi
 DEPT: _____ FAX #: 463-3144
 FROM: Staley, D. PHONE: 452-1855
 CO: Barbara S. FAX #: 452-8154
 Post-It® brand fax transmittal memo 7671

NO. OF PAGES
2

Draft 2 - definition for "financial institution"

Section 1. AS 46.03. is amended by adding a new section to read:

AS.46.03.910 Limited liability for financial institutions.

(a) No trust company *(which is wholly owned by a bank or subject to regulation by the Comptroller of the Currency,)* and no bank, credit union, or savings association (or trust company), the deposits of which are insured in whole or in part by the Federal Deposit Insurance Corporation or by any agency of the United States, or by the state of Alaska, shall be held or construed to be an "owner", "operator", person "having control" over a hazardous substance, or to be liable under any state law imposing strict liability for, or imposing a duty to discover, to contain or to clean up the release or threatened release of a hazardous substance at or from a facility or vessel which:

- (1) it acquired through foreclosure;
- (2) it held as a lessor pursuant to the terms of an extension of credit;
- (3) is subject to its financial control or financial oversight pursuant to the terms of an extension of credit but as to which it did not exercise actual, direct, and continual managerial control that materially divested the borrower, debtor or obligor of such control; or
- (4) it acquired in a fiduciary capacity.

(b) An institution described in subpart (a), or the estate which it represents in a fiduciary capacity, as the case may be, may be liable to (required to reimburse) the state (a third party), but only for any actual benefit received by such institution or estate, from a removal, remedial, containment, or other response action undertaken by the state (third party), the total liability for which benefit, including payment of any state lien, shall not exceed the fair market value of the affected property following such action.

(c) An institution described in subpart (a), or the estate which it represents in a fiduciary capacity, as the case may be, which causes or exacerbates a release or threatened release of a hazardous substance, through activity and not by omission, shall be liable for response costs to the extent that the release or threatened release is attributable to the person's activities.

Section 2. (Repeat Sec. 3 of SB 154)

Section 3. (Repeat Sec. 4 of SB 154)

Section 4. (Repeat Section 5 of SB 154)

BLS:697



MAIN OFFICE: 3500 EIDE STREET ANCHORAGE, AK 99503 563-3768	DIMOND BRANCH: 300 E. DIMOND BLVD. ANCHORAGE, AK 99515 344-5144	SOLDOTNA BRANCH: 131-A WAREHOUSE SOLDOTNA, AK 99869 282-7600	EAGLE RIVER BRANCH: 16515 CENTERFIELD DRIVE EAGLE RIVER, AK 99577 894-5444	CAMPUS BRANCH: 2801 PROVIDENCE DRIVE ANCHORAGE, AK 99508 581-3161
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April 26, 1991

State Senator Lloyd Jones
Resource Committee
P.O. Box V
Juneau, Alaska 99811

Dear Senator Jones:

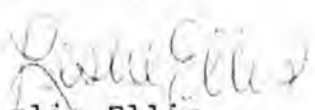
I am writing to express my Credit Union's support of SB 154 sponsored by Senator Rodey. The bill will limit the liability to the lender for the cost of cleaning contaminated properties acquired through foreclosure.

Frontier Alaska State Credit Union is a source of non-investor real estate lending to its 24,000 member/owners. Due to the risk associated with contaminated property, we have had to curtail some types of real estate lending, most notably raw land loans. We also have had to incur additional expense for inspections, certifications and other expenses associated with holding foreclosed properties. Those additional expenses are passed on to our member/owners in the form of increased fees and/or higher loan rates. We have also found that the property can become contaminated during the term of the loan without the Credit Union's knowledge.

Because of the above mentioned risks, combined with the regulators inherent fear of real estate loans and associated losses, many Alaskans cannot find competitive real estate loans when they need them. Passage of this bill will help make competitive real estate loans available to more Alaskans. It will also aid the economic recovery currently taking place in the state. The Board of Directors and Management at Frontier urge swift passage of SB 154, so that affordable real estate loans are available to all qualified Alaskans.

Thank you for your time and attention to this matter. If you have any questions please don't hesitate to contact me.

Sincerely,


Leslie Ellis
President

SB 154

**EPA DRAFT PROPOSAL DEFINING LENDER LIABILITY ISSUES
UNDER THE SECURED CREDITOR EXEMPTION OF CERCLA
(Sept. 14, 1990)**

ENVIRONMENTAL PROTECTION AGENCY
40 CFR Part []

Lender Liability under CERCLA

AGENCY: Environmental Protection Agency

ACTION: Final Interpretative Rule; Proposed Rule and Request for Comments

SUMMARY: The Environmental Protection Agency is issuing this rule to define the meaning of certain statutory elements in the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), which pertain to the liability of both financial institutions that lend money to facilities and governmental loan guarantors or entities that acquire ownership, or some indicia thereof, of contaminated facilities. In this rule, EPA is interpreting the secured creditor exemption in CERCLA section 101(20)(A) so that private and governmental lending institutions and successors-in-interest that hold a security interest in a facility may undertake a variety of activities related to a borrower's facility in the course of protecting the security interest, without voiding the exemption. In addition, EPA is interpreting the terms of CERCLA section 101(35)(A)(ii) so that certain federal government entities (the Resolution Trust Corporation (RTC) and the Federal Deposit Insurance Corporation (FDIC) that obtain a security interest or ownership of a contaminated facility as the result of actions mandated under the Federal Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Pub. L. No. 101-73, 103 Stat. 183 (Aug. 9, 1989), fall within the scope of the innocent landowner defense, as long as the other elements of the defense are met.

EFFECTIVE DATE: (insert publication date)

ADDRESSES: Comments on this final interpretative rule and proposed rule must be submitted by (insert date 30 days from date of publication). Commentors must send an original and two copies of their comments to: [Office], U.S. Environmental Protection Agency, 401 M Street, S.W., Washington, D.C. 20460. Comments should include the docket number []. The public docket is located at EPA Headquarters at the above address in Room [] and is available for viewing from 9:00 a.m. to 4:00 p.m., Monday through Friday, excluding Federal holidays.

I. Background

The Agency is promulgating this rule to interpret the provisions of sections 101(20) and 101(35) of the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), as amended, 42 U.S.C. §9601 et seq., as they affect private lending institutions and governmental entities that hold a secured interest in a facility contaminated by or containing hazardous substances, or that acquire ownership of contaminated property in the course of protecting a secured interest.

Section 107(a) of CERCLA, 42 U.S.C. §9607(a), identified four broad classes of responsible parties that are liable for the costs of cleaning up, among other things, hazardous substances when the federal government, state government, or a private party brings suit. The first two classes include certain owners and operators of facilities contaminated by or containing hazardous substances, 42 U.S.C. §9607(a)(1)-(a)(2). The third class consists of certain persons who arranged for disposal or treatment of hazardous substances. *Id.* §9607(a)(3). Finally, the fourth class includes persons who accepted for transportation hazardous substances and selected the disposal facility. *Id.* §9607(a)(4).

It is now well-settled that each of the four groups of responsible parties is strictly liable under section 107(a). See, e.g., *Tanglewood East Homeowners v. Charles-Thomas, Inc.*, 849 F.2d 1568, 1572 (5th Cir. 1988); *United States v. Monsanto Co.*, 858 F.2d 160, 167 & n.11 (4th Cir. 1988), cert. denied, 109 S.Ct. 3156 (1989). In addition, it is also settled that such parties are jointly and severally liable when the environmental harm is indivisible. *United States v. Monsanto Co.*, 858 F.2d at 171; *United States v. Chem-Dyne Corp.*, 572 F.Supp. 802, 810-11 (S.D. Ohio 1983).

CERCLA defines "owner or operator" in Section 101(20). However, Section 101(20)(A) exempts those persons who, without participating in the management of the facility, hold indicia of ownership primarily to protect a security interest, 42 U.S.C. §9601(20)(A). The issue of how the "secured creditor" exemption is to be interpreted under CERCLA has generated a great deal of uncertainty in the financial and lending communities regarding the extent to which a secured creditor can undertake activities to oversee the affairs of a borrower for the purposes of protecting a security interest and still maintain the exemption.

These uncertainties were heightened by *dicta* in the recent opinion of the United States Court of Appeals for the Eleventh Circuit in *United States v. Fleet Factors Corp.*, 901 F.2d 1550 (11th Cir. 1990). In this opinion, the court suggested that a secured creditor may be liable, without being an operator, if it participated in the management of a facility "to a degree indicating a capacity to influence the corporation's treatment of hazardous wastes." 901 F.2d at 1557. Another court of appeals has indicated that the mere capacity or right to control facility operations is insufficient to void the secured creditor exemption and suggested that the creditor must participate in the operational management of the facility to lose the exemption's liability shield. See *In re: Bergsøe Metal Corp.*, No. 89-35397, slip op. (9th Cir. Aug. 9, 1990) ("What is critical is not what rights the [creditor] had, but what it did . . . [A creditor] cannot have participated in management if it never exercised [its rights].")

TEXT

Further uncertainty has arisen as a result of the role of the Federal Deposit Insurance Corporation and the Resolution Trust Corporation, which act as conservators or receiver of failing or failed lending institutions, and the potential applicability of CERCLA to these governmental entities which have succeeded to the properties and assets owned by the failed lending institutions. In particular, an issue has arisen as to the applicability to these institutions of the so-called "innocent landowner" defense of sections 107(b)(3) and 101(35).

To reduce these uncertainties, EPA is issuing this rule to specify for lenders and these governmental entities what actions they may take and still remain within the bounds of either the secured creditor exemption or the "innocent landowner" defense.

EPA is promulgating this rule as a final interpretative rule which is effective upon publication in the FEDERAL REGISTER in accordance with the provisions of section 553(b) and (d) of the Administrative Procedure Act (APA). These sections of the APA authorize the Agency to issue interpretative rules without providing notice and opportunity to comment and to make today's rule immediately effective rather than wait for the expiration of a 30-day period. Because of the important issues that are raised by this interpretative rule, however, the Agency is accepting public comment for a 60-day period. Upon review of the comments, EPA will formally codify the rule in 40 C.F.R. Part [].

The Agency also believes that judicial review of this rule is governed by the provisions of CERCLA section 113(a). These provisions mandate that any review of a regulation promulgated under CERCLA is confined to the United States Court of Appeals for the District of Columbia Circuit and that any application for such review must be made within ninety days of the rule's date of promulgation. By enacting these provisions, Congress intended that the District of Columbia Circuit Court would have "exclusive" jurisdiction to review regulations and that any petitions for review that were filed after the ninety day period would be barred. S. Rep. No. 848, 96th Cong., 2d Sess. 95 (1980); see *Lubrizol Corp. v. Train*, 547 F.2d 310, 314-16 (6th Cir. 1976) (by centralizing appeals in the D.C. Circuit under the Clean Air Act, congress hoped to avoid needless delays in the implementation of important national programs caused by incessant litigation and inconsistent decisions).

II. Summary

This rule interprets the secured creditor exemption to permit a broad range of lender activity when that activity is conducted primarily to protect a security interest. This rule defines the key terms of CERCLA section 101(20)(A): (1) "indicia of ownership," (2) "primarily to protect a security interest," and (3) "participating in the management of a ... facility." With respect to a government entity acting under FIRREA that may assume ownership, conservatorship, or receivership of financial lending institutions and thereby assume actual ownership of and exercise total control over a contaminated facility, this rule defines those circumstances in which the governmental entity may have a defense available under section 101(53)(A)(ii) of CERCLA.

While section 101(20)(A) provides lenders with a potential exemption from CERCLA liability when the collateral securing the loan is contaminated, it does not otherwise provide protection from the ordinary risk assumed by the lender that the collateral's market value may not be

sufficient to cover the borrower's debt. The CERCLA secured creditor exemption is not a loan guarantee for lending institutions and does not shift to the Superfund the cost of poor loan decisions, but serves only as a shield from CERCLA liability.

From an environmental perspective, the EPA must concern itself first with protection of health and the environment. Following expenditure of public funds to clean up contaminated property, EPA must, as authorized by law, seek to recover the cost expended by the fund from those liable under CERCLA. Accordingly, CERCLA clearly imposes liability on owners of real property where there is a release or threat of release of hazardous substances for the consequences of that release.

This rule seeks to reconcile the lender's need to manage loans with EPA's duty to clean up waste sites and recover public funds spent in remediating these sites. EPA's interpretation of the secured creditor exemption both acknowledges and accommodates these competing interests within the current statutory scheme by protecting the secured creditor that acts in an environmentally responsible manner (which includes requiring environmental audits of the collateral upon making loans) from incurring CERCLA liability.

III. CERCLA Provisions
Protecting a Secured Lender
A. Security Interest Exemption

The section 101(20)(A) security interest exemption is the principal means of avoiding CERCLA liability for a lender or loan guarantor (hereafter referred to as the "lender," "secured lender," "holder of the security interest," or simply "holder"). EPA interprets a security holder as including both the lender and the private or governmental loan guarantor or successor-in-interest. A private successor-in-interest is a subsequent bona fide purchaser of the loan (security interest) in the secondary market. A governmental successor-in-interest is the governmental entity that acquired property involuntarily or by operation of statute through failure, dissolution, or other insolvency of a lending institution (such as the Federal Deposit Insurance Corporation or the Resolution Trust Corporation) acting under FIRREA.

Section 101(2)(A) provides:

"Such term [owner or operator] does not include a person who, without participating in the management of a vessel or facility, holds indicia of ownership primarily to protect his security interest in the vessel or facility." There are three key terms found in the exemption that are not otherwise defined in the CERCLA: (1) "indicia of ownership" (2) the requirement that the indicia be held "primarily to protect the security interest" in the facility, and (3) the prohibition of the security holder from "participating in the management" of the facility.

(a) "Indicia of ownership."

Ownership indicia within the meaning of Section 101(20)(A) are those interests in real or personal property held as security or collateral for a loan, including the real or personal property acquired in the course of protecting the security interest. The nature of the ownership interest may vary under the laws of different states and by the type of secured loan transaction. Examples of such indicia may include, but are not limited to, a mortgage, deed of trust, or legal title obtained pursuant to foreclosure or its equivalents, or an assignment, lien, pledge, or other right to or encumbrance against the facility that is fur-

ished by the borrower as security for the loan. The mortgage, lien, or other encumbrance must be for the purpose of security for a loan, and not for some other purpose, to come within the exemption. Section 101(2)(A) does not cover an interest in the nature of an investment in the contaminated property, or any interest other than as a security. See, e.g., *United States v. Maryland Bank & Trust*, 632 F. Supp. 573 (D. Md. 1986) (actions taken by lending institution indicate property held as an investment rather than security for a loan). "Indicia of ownership" are maintained or acquired by the lender as an assurance of repayment: ownership indicia within the meaning of the exemption are those given as collateral incident to a loan transaction. For purposes of CERCLA, the security holder's ownership "interest" is not the facility itself but the extent to which the facility or inventory represents a guarantee for the debtor's unpaid obligation.

(2) "Primarily to protect the security interest."

The exemption in section 101(2)(A) requires that the lender's ownership interest have been created and held as security for a loan or other obligation. This requires that the lender's ownership interest represent a true security interest in the facility,¹ as opposed to a lease or a consignment which ordinarily would not be considered a secured transaction.² Because the exemption covers only true security interests, Section 101(20)(A) does not exempt from the CERCLA definition of "ownership" a lender's ownership interest in property held for investment purposes. EPA recognizes that lenders typically have revenue interests in the loan transaction. However, when the lender holds its indicia of ownership in the property for investment purposes, as opposed to assuring repayment of the loan, the secured creditor exemption will not apply. Similarly, the CERCLA secured lender exemption has no application where a lending institution acts as a trustee or manager of property or a business, or where a lending institution acts in a non-lending capacity or has any interest other than one created as bona fide security interest in real or personal property.

Consistent with the exemption, the secured creditor may act to protect the interest by policing the loan, by undertaking financial workout with a borrower where the security interest is threatened, and by foreclosing and expeditiously liquidating the assets securing the loan. In general, such actions are not considered to be participation in the management of a facility provided that the actions taken are necessary to protect the security interest.

Accordingly, a secured party is considered to be acting within the scope of the exemption if it regularly or periodically monitors the borrower's business, requires or conducts on-site inspections and audits, requires certification of financial information or compliance with applicable duties, laws or regulations, or requires other similar actions, provided that the borrower remains substantially in possession and control of the operations of the facility. Such oversight and obligations of compliance imposed by a lender are generally considered to be undertaken to protect the security interest and are not considered part of the management and operation of a facility. Although such requirements and oversight may inform the borrower's management of a facility, the lender is not generally considered to be participating in management where the borrower continues to make operational decisions at the facility.

Making a Loan

CERCLA's broad remedial goal of protecting health and the environment from the hazards of improper waste practices (and, by implication, encouraging safer hazardous waste practices), requires that the lender seeking shelter from CERCLA liability act consistently with the statute's purpose to qualify for the statutory secured creditor exemption. Specifically in order to be considered acting primarily to protect a security interest, a lender must undertake certain affirmative obligations, at the time of the loan, with respect to the property (collateral). For purposes of this CERCLA exemption, when making a loan, lenders are acting consistently with CERCLA when an inspection or audit of the collateral securing the loan is undertaken in an effort to minimize environmental liability. Such an inquiry is required by the exemption as an action taken to protect the security interest through assessing and ensuring the value of the collateral in which the lender has taken an indicia of ownership.³

Policing the Loan

Actions consistent with protecting the security interest may include, but are not limited to, requirements for environmental audits prior to making the loan; cleanup of the property during the life of the loan; requirements of assurance of the borrower's compliance with applicable federal, state, and local environmental and other rules and regulations during the life of the loan; permission for the lender to periodically or regularly monitor or inspect both the collateral (including site inspections) or the borrower's business or financial condition; or other requirements or conditions reasonably necessary for the lender to adequately police the loan or to comply with legal requirements.

Such requirements may be contained in lender-imposed requirements for financial, environmental, and other warranties, covenants, and representations or promises from the borrower, as conditions for the loan and included in loan documents. While the exemption requires that a secured creditor undertake actions consistent with CERCLA when protecting the security interest, a lender is not expected to be an insurer or guarantor of environmental safety at a facility in which it has a security interest. The inclusion of environmental warranties and covenants are not considered to be evidence of a lender acting as an insurer or guarantor, and liability cannot be premised on the existence of such terms, or upon the lender acting to ensure the facility is managed in an environmentally sound manner. Neither are these actions or requirements alone considered to be evidence of participation in management.

Loan Work Out

The lender may need to take actions to secure or safeguard real property or other collateral from loss. These actions are usually necessary when the loan is in default or threat of default, and is a situation commonly referred to as "loan work out." These actions will not take a lender outside of the security interest exemption provided that the actions are taken in the course of protecting the security interest. To remain within the exemption from CERCLA liability, all such actions must be structured to protect and preserve the security interest; such measures are taken to protect the security interest when the lender is assisting the debtor in an effort to prevent default of the loan or diminution of the value of the collateral.

Activities that EPA considers to be "primarily to protect the security interest" (and are not evidence of "participation in management") during the work-out period include, but are not limited to, restructuring or renegotiation of the terms of the loan obligation, payment of additional interest, extension of the payment period, specific financial or operational advice, suggestion, counseling, guidance, or any other action reasonably necessary to protect the lender's security interest. The lender's actions must, however, duly consider and account for the hazardous substances known to be present at the facility, and must not cause or contribute by act or omission to the environmental harm at issue. The Agency believes that this position is consistent with the underlying statutory purposes of CERCLA of ensuring the cleanup of hazardous waste sites and that those who cause harm from hazardous substances bear the costs of such cleanups. S.Rep. No. 84B, 96th Cong., 2d Sess. 12-13 (1980). When the lender does undertake work-out activities, it will remain within the exemption only if the borrower remains the ultimate decision maker for operation of the facility. Where the evidence demonstrates that the lender controls the decisionmaking process of the borrower, EPA considers the lender to be "participating in the management of the facility" and therefore to have voided the exemption.

Foreclosure and Liquidation

The process of foreclosure and sale may require or result in the secured lender taking record title to the property under the laws of some states. Foreclosure, purchase at foreclosure sale, acquisition or assignment of title in lieu of foreclosure, acquisition of a right to title, or other agreement in settlement of the loan obligation, or any other formal or informal manner by which the lender acquires possession for disposition of the borrower's collateral, are generally considered to be actions within the scope of the statutory exemption as necessary to protect the security interest. However, the lender's temporary acquisition must be reasonably necessary to ensure satisfaction or performance of the loan obligation. The lender's actions in outbidding or refusing bids from parties offering fair consideration for the property are evidence that the property is no longer being held primarily to protect the security interest. To remain within the exemption after foreclosure, the foreclosing entity must be acting to preserve the assets of the facility for its subsequent sale at the earliest possible time. In general, the lending institution must undertake to wind up operations expeditiously and liquidate all assets, or take other action as appropriate for maximizing the value of the secured asset prior to sale as a means to realize the debtor's unpaid obligation. "Winding up" is construed as including those actions necessary to properly and responsibly close down a facility's operations, secure the site, and otherwise protect the value of the foreclosed assets for subsequent liquidation. The lender should undertake all necessary security measures or take other actions that protect and preserve a facility's assets. A lender's actions while winding up operations that cause or contribute to environmental contamination are not considered to within the meaning of the exemption. Mitigative or preventative measures that are environmentally responsible are considered to be actions that preserve and protect the value of the facility and, hence, the lender's security interest. In addition, such actions are not considered

evidence of a lender's participation in the management" of the facility.

Holding Property for a Reasonable Period

Having foreclosed upon or otherwise acquired the collateral securing a loan, the lending institution remains within the ambit of the secured creditor exemption only if it disposes of the property as expeditiously as possible. For purposes of this rule, a lender holding property after foreclosure for six months or fewer is presumed to be holding to protect the security interest. However, if the lender has not divested itself of the property within this time, the burden shifts to the lender to demonstrate that it continues to hold the property primarily to protect the security interest, taking all relevant facts and circumstances into account.

A secured lender is considered to be acting to dispose of property in an expeditious manner if it seeks to sell, auction or otherwise liquidate or transfer the assets as soon as practicable, taking into account the condition of the property, what is required to property wind up operations, and other facts and circumstances as appropriate. Evidence that the lender is seeking to divest itself expeditiously of the asset includes, but is not limited to, advertising or auctioning the facility for sale, listing property with a realtor or sales agent, or other actions reasonable demonstrating or manifesting an intent to sell or otherwise divest itself of the asset.

In the event that an EPA cleanup of the contaminated property enhances the value of the collateral during the time that the secured lender is holding its indicia of ownership, much that the lender realizes an amount at the foreclosure sale of the cleaned-up property greater than the value of the property in its contaminated condition. EPA may seek equitable reimbursement, under applicable principles of law, of the amount by which the lender has been enriched or has benefited as a result of the EPA cleanup.

Participation in Management

Whether a lender has engaged in management participation sufficient to void the exemption is a fact-sensitive issue. This depends upon all relevant facts, including, but not limited to, the nature of the borrower's business, the areas in which the lender becomes involved, whether the facility is in the possession of the borrower or lender (after foreclosure), the actual control exercised by the lender over the borrower's activities, and whether the lender has caused or contributed to environmental harm at the facility.

"Participation in management" sufficient to void the exemption means actual operational participation by the lender, and does not include the mere capacity or ability to influence facility operations. In all cases, the determination of whether a lender is participating in management depends on a lender's actions and omissions with respect to facility operations. In general, a lender is considered to be participating in management within the meaning of the exemption if, while the borrower is still in possession, the lender has materially divested the borrower of decisionmaking control over facility operations, particularly with respect to the hazardous substance present at the facility. However, a lender is not considered to be participating in management if it undertakes actions that primarily protect the security interest, as discussed in the preceding section. In particular, and consistent with CERCLA's purpose, actions taken by a

lender that are environmentally beneficial are not considered to be participation in the management of a facility within the meaning of the exemption.

B. Innocent Landowner Defense

The third-party/innocent landowner provisions, sections 107(b)(3) and 101(35)(A)-(B), provide a limited and secondary means of protection for the holder of a security interest. Section 107(b)(3) provides a defense where the harm was caused solely by the acts of third parties with which the defendant had no "contractual relationship" and the defendant establishes certain additional elements specified in section 101(35)(A)-(B). The relevant sections of the third-party innocent landowner defense provide:

Section 107(b):

"There shall be no liability under (section 107(2) for a person who can establish ... that the release or threat of release of a hazardous substance and the damages resulting therefrom were caused solely by—

(3) an act or omission of a third party other than ... one whose act or omission occurs in connection with a contractual relationship existing directly or indirectly with the defendant ... if [the defendant] (a) [has] exercised due care with respect to the hazardous substances ...; and (b) he took precautions against the foreseeable acts or omissions of any ... third party...."

Section 101(5):

"(A) The term 'contractual relationship,' for the purpose of section 107(b)(3), 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 placement of hazardous substances, and ...:

(i) At the time the defendant acquired the facility the defendant did not know and had no reason to know that any hazardous substance ... was disposed of on, in or at the facility.

(ii) The defendant is a government entity which acquired the facility ... through any ... involuntary transfer or acquisition,....

In addition, ... the defendant must ... satisf[y] the requirements of section 107(b)(3)(a) and (b).

(B) To establish that the defendant had no reason to know, ... the defendant must have undertaken all appropriate inquiry into the private previous ownership and uses of the property consistent with good commercial or customary practice in an effort to minimize liability." (emphasis added.)

The section 101(35)(A)(i) innocent landowner defense is not intended to serve as the primary means of protection from potential CERCLA liability for secured lenders; EPA believes that the security interest exemption is ordinarily sufficient for this purpose, and the innocent landowner defense is not necessary to protect a lending institution from liability for properties in which it holds indicia of ownership to protect a security interest. In the limited circumstances in which the secured lender is not in a position to claim the security interest exemption for property which it owns, the lender/owner may seek to defend itself as an innocent landowner in the same manner.

Involuntary Acquisition

Different provisions apply to the government-as-innocent owner of contaminated property. EPA interprets

the phrase "a government entity which acquires the facility ... through any ... involuntary transfer or acquisition" in section 101(35)(A)(ii) as including, but not being limited to, acquisition of the property and assets of failed or insolvent banks, credit unions, savings institutions and thrifts by a government agency or government corporation that is obligated under law to act as a conservator or receiver of the lending institution. Such governmental entities are the Federal Deposit Insurance Corporation or Resolution Trust Corporation acting under FIRREA. The range of assets acquired by such entities say include, among others, simple security interests, property for which the depository or thrift institution holds record title or other form of title through foreclosure, or property that has been purchased or acquired as an investment by the failed institution or its subsidiary.

For these assets or properties in which the failed or insolvent institution held a security interest, as a successor-in-interest the government receiver or conservator has the same rights as any private or commercial holder of the secured interest. It may therefore sell or transfer the interest, engage in loan workout, wind up operations, foreclose, and liquidate the assets securing the loan in the same manner as a private or commercial lending institution acting under the protection of section 101(20)(A).

With respect to those properties the government conservator or receiver acquired by operation of law that were owned by the failed or insolvent institution as an investment interest or for other reasons (i.e., those properties for which the failed institution's indicia of ownership is not held as a security interest and for which the section 101(20)(A) does not apply), EPA interprets section 101(35)(A)(ii) as providing a potential defense to liability. For the purposes of CERCLA, property owned by the failed or insolvent institution to which the government entity succeeds by operation of law has been acquired involuntarily within the meaning of section 101(35)(A)(ii). EPA further interprets section 101(35)(A)(ii) to provide a potential defense to CERCLA liability for contaminated property that is owned by a governmental entity as the result of its foreclosure on a security interest originally acquired by the government entity in its capacity as a conservator or receiver. To establish any such defense, the other provisions of section 107(b)(3) (requirements for due care and precautions against the foreseeable acts of third parties) must also be satisfied.

Where the government entity acquires contaminated property in its corporate capacity (e.g., by transfer of non-salable assets from the FDIC as receiver to the FDIC in its corporate capacity), the property remains "involuntarily acquired"; the government entity does not assume CERCLA liability merely because of the transfer of property or assets to it as part of its legally imposed mandate to resolve the affairs of failed or insolvent thrifts and depository institutions.

Part [] — Lender Liability Under CERCLA

(a) Definitions:

(1) *Indicia of ownership* as used in section 101(20)(A) of CERCLA means interests in real or personal property held as security or collateral for a loan, as well as the real or personal property acquired in the course of protecting the security interest. The interest in the property must be held primarily as security for a loan.

(2) *Security interest* for the purposes of section 101(20)(A) of CERCLA means an interest in property acquired for the purpose of securing payment or performance of an obligation. A security interest exists at any time (A) if, at such time, the property is in existence and the interest has become protected under local law against a subsequent judgment lien arising out of an unsecured obligation, and (B) to the extent that, at such time, the holder has parted with money or money's worth. A holder of a security interest within the scope of the section 101(20)(A) exemption is a private or governmental lender or loan guarantor or successor-in-interest, that receives as collateral for a loan an interest in the real or personal property of the borrower, or that is a subsequent bona fide purchaser of or successor to the security interest. A governmental successor-in-interest includes the government entity that acquires property involuntarily by operation of statute through failure, dissolution, or other insolvency of a lending institution.

(1) *Covered Security Interests.* A "security interest" within the scope of section 101(20)(A) of CERCLA are those that have been created and held as a true security for a loan or other obligation, and do not include a lease or a consignment which may not be considered a secured transaction under applicable principles of commercial law. This term does not include an ownership interest in property held for investment purposes (ownership indicia held for purposes other than for assuring repayment of a loan). The term also does not include the interests of a lending institution acting as a trustee or manager of property of a business, or where a lending institution acts in any other non-lending capacity or has any interest other than one created as bona fide security interest in real or personal property.

(3) *Primarily to protect a security interest* means that the lender's interest in the property is created and held as security for a loan or other obligation, and that certain activities undertaken regarding the interest are necessary and required for its protection. The secured creditor may act further to protect the interest by policing the loan, by undertaking financial workout with a borrower where the security interest is threatened, and by foreclosing and expeditiously liquidating the assets securing the loan. Such actions are within the exemption if taken primarily to protect the security interest.

(i) *Requirement of Inquiry Upon Making a Loan.* At the time that the loan is made, an inquiry into the environmental condition of the collateral securing the loan must be undertaken in an effort to minimize environmental liability and to protect the security interest through assessing and ensuring the value of the collateral.

(ii) *Requirements During the Life of a Performing Loan.* A secured lender is acting consistently to protect its security interest if the lender requires cleanup of the property prior to or during the life of the loan; requires assurance of the borrower's compliance with applicable federal, state, and local environmental and other laws, rules and regulations during the life of the loan; obtains permission to periodically or regularly monitor or inspect both the collateral (including site inspections) or the borrower's business or financial condition; or by taking other actions that are necessary for the lender to adequately police the loan or to comply with applicable legal requirements.

(iii) *Loan Workout and Foreclosure.* A lender's actions during workout, foreclosure, and liquidation must: duly

consider and account for any hazardous substances known to be present at the facility, and must not cause, contribute to, or exacerbate the release or threat of release of hazardous substances. Causing or contributing to a release or threat of release of hazardous substances is not considered to be protection of the security interest. Mitigative or preventative measures that are environmentally responsible are considered to be actions that preserve and protect the value of the facility and the lender's security interest.

(A) *Loan Workout.* Loan workout activities are those actions of the lender that are structured to protect and preserve the security interest by assisting the debtor in an effort to prevent default of the loan or diminution of the value of the collateral. Loan workout activities that are primarily to protect the security interest include, but are not limited to, restructuring or renegotiation of the terms of the loan obligation, payment of additional interest, extension of the payment period, forbearance, or providing or taking other actions when the lender does undertake work-out activities, it will remain within the exemption only if the borrower remains the ultimate decision maker for operational management of the facility.

(B) *Loan Formulation.* When the lender forecloses or by any formal or informal manner requires possession of the property for disposition, the temporary acquisition of the property must be necessary to ensure satisfaction or performance of the loan obligation, and the secured party must set to preserve the assets of the facility by winding up operations expeditiously for subsequent sale or other divestment of the assets at the earliest possible time. A lender is not considered to be acting as expeditiously as possible if, in the context of the lender's actions with respect to a non performing loan, the lender never seeks to foreclose or otherwise acquire or otherwise act to protect the collateral securing the loan, or delays foreclosure for an unreasonable length time once the loan is non performing, in light of all relevant facts and circumstances.

(1) *Winding up operations* means those actions necessary to close down a facility's operations in full compliance with all applicable laws and regulations, secure the site, and otherwise protect the value of the foreclosed assets for subsequent liquidation. While winding up operations, a lender's actions or failure to act that cause or contribute to environmental contamination are not considered to be actions taken primarily to protect the value of the collateral within the meaning of the secured creditor exemption.

(2) A secured lender is presumed to have acted expeditiously to sell or otherwise divest itself of property taken by default, foreclosure, or by other similar means if it has sold or otherwise completely divested itself of any indicia of ownership in six months or fewer after it has foreclosed on or by other means acquired possession of property. After the expiration of this six month period, the burden shifts to the lender to demonstrate that it continues to hold the property primarily to protect the security interest, taking all relevant facts and circumstances into account.

(4) *Participation in the management of a facility* means the exercise of operational management control by a security holder over a borrower's activities with respect to the facility securing the loan obligation.

(i) The term does not include the mere capacity to control or influence a facility's operations, but does in-

TEXT

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clude the actual exercise of such operational management control. Whether a lender is participating in management depends on a lender's actions with respect to facility operations.

(ii) A security holder is considered to be participating in management if, while the borrower is still in possession, the security holder has materially divested the borrower of decisionmaking control over facility operations, particularly with respect to any hazardous substances present at the facility.

(iii) A lender is not considered to be participating in management if it undertakes actions that primarily protect the security interest, as defined in 40 C.F.R. [(a)(3)].

(5) *Involuntary Transfer or Acquisition*, as used in section 101(35)(A)(ii) of CERCLA, includes acquisition of property and assets of failed or insolvent banks, credit unions, savings institutions and thrifts by a government entity that is obligated under the Federal Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Pub. L. No. 101-73, 103 Stat. 183 (Aug. 9, 1989), to act as a conservator or receiver of a lending institution. Involuntarily acquired property includes property that is owned by a governmental entity as the result of its foreclosure on a security interest originally acquired by the government entity in its capacity as a conservator or receiver. (b) *Secured Creditor Exemption*

A person holding an indicia of ownership in a facility primarily to protect a security interest and who does not participate in the management of a facility is not an owner or operator" under section 101(20)(A) of CERCLA.

The CERCLA definition of "facility" includes real property as well as any equipment or other articles

contaminated by hazardous substances. See CERCLA §101(9).

² Whether a sale-and-leaseback, conditional sale, installment sales contract, or other similar commercial transaction is within the security interest exemption under CERCLA is determined by the facts of each case.

³ The requirement under section 101(20)(A) to undertake an environmental assessment of the collateral when making a loan is prospective only, and does not apply to loans already made as of the effective date of this rule. This rule in no way affects the obligation of purchasers to undertake "all appropriate inquiry" required for innocent landowner defense of CERCLA §§101(35) and 107(b)(3).

⁴ To the extent that the foreclosing lender is acting "primarily to protect its security interest" and is within the secured creditor exemption, EPA considers that the ownership of the property remains with the borrower for purposes of the CERCLA lien provision. See 42 U.S.C. §9607(1).

⁵ In this context (a secured lender's actions with respect to a non performing loan), a lender is not considered to be acting as expeditiously as possible if the lender never seeks to foreclose or otherwise acquire the collateral securing the loan, or delays foreclosure for an unreasonable length of time once the loan is non performing, in light of all relevant facts and circumstances.

⁶ See Guidance on Landowner Liability Under Section 107(a)(1) of CERCLA, De Minimis Settlements Under Section 122(g)(1)(B) of CERCLA, and Settlements With Prospective Purchasers of Contaminated Property, 54 Fed. Reg. 34235 (Aug. 18, 1989).

DIVISION OF LEGAL SERVICES

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MEMORANDUM

May 1, 1991

SUBJECT: Sectional summary of CSSB 154()
(Work Order No. 7-LS0716\G, 4-23-91)

TO: Senator Pat Rodey
Attn: Tim

FROM: Theresa L. Bannister *TB*
Legislative Counsel

You have requested a sectional summary of the above described bill. As a preliminary matter, note that a sectional summary of a bill should not be considered an authoritative interpretation of the bill and the bill itself is the best statement of its contents.

Section 1. This section amends AS 46.03.822, the section that creates strict liability for releases (and threatened releases) of hazardous substances. The amendment makes AS 46.03.822 subject to the new section (created in bill sec. 2) that exempts certain financial institutions from strict liability with regard to certain property.

Section 2. This section exempts certain qualifying financial institutions from the strict liability provisions of AS 46.03.822 - 46.03.828. Subsection (a) contains the exemption and ties the exemption to certain listed types of facilities and vessels held by the institution. These types of property include property acquired through foreclosure. Subsection (b) creates an exception to the exemption and allows the state to require the institution to reimburse the state for certain benefits received by the institution resulting from state response, containment, removal, or remedial action. Limits the reimbursement to the fair market value of the facility or vessel involved. Subsection (c) describes the financial institutions that qualify for the exemption.

Section 3. This section amends the section that gives the state a lien for its costs of response, containment, removal, or remedial action. The amendment limits the property against which the state has a lien to a facility or vessel that is owned by the liable person and that is subject to the action.

Senator Pat Rodey

May 1, 1991

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Section 4. This section makes the state's lien subject to the rights of certain parties if the parties' interests were perfected before notice of the state's lien was recorded. Gives the parties the same protections against the state's lien that they have under state law against judgment liens that arise out of unsecured obligations and that arise at the same time notice of the state's lien was filed.

Section 5. This section repeals AS 46.08.075(e). That subsection authorizes a person with an ownership interest in property against which a state lien is recorded under AS 46.08.075 to ask a court to release the lien, and gives the court guidelines for releasing the lien.

Section 6. This section states that facilities and vessels are covered by proposed sec. 46.03.825 (bill sec. 2) even if they were acquired or held by, or subject to the financial control or financial oversight of, a financial institution before the effective date of the Act.

If I may be of further assistance, please advise.

TLB:pl:gc
91-326.plm

STATE OF ALASKA

WALTER J. HICKEL, GOVERNOR

DEPT. OF ENVIRONMENTAL CONSERVATION

OFFICE OF THE COMMISSIONER
P.O. BOX 0, JUNEAU, ALASKA 99811-1800

TELEPHONE
(907) 465-2600

POSITION PAPER SB 154

SB 154 would exempt lending institutions and fiduciaries from liability for environmental damage. Even those fiduciaries who have been involved in the control or management of the facility or vessel responsible for the damage would not be liable. Because the potential for liability is believed to lead to better facility management, the Department does not support this limitation. The Department would support both a definition of "management" of a facility or vessel as well as the development of professional standards for environmental audits by the private sector. In that way, just as a structural engineer examines for the lending institution a building's structure, a private environmental engineer would examine the property's environmental condition.

Section Three would limit the responsible party's assets which the State could attach for expenditures from the Oil and Hazardous Substance Release Response Fund. Under this language, the State would only be able to look to the value of the real property which was the subject of the remediation for satisfaction of the responsible party's debt to the State. Currently, the State may look to all assets owned by the responsible party. Without that ability, it is expected that the Department would encounter difficulty in recovering Response Fund costs, and thus the Department does not support this provision.

Section Five in part repeals AS 46.03.822(b)(2) which limits the liability of an owner and operator for damage caused by an unrelated third party or an act of God so long as the owner or operator discovered the hazardous substance and began containment and cleanup within a "reasonable period of time." The Department does support this repeal.



John A. Sandor
Commissioner

WALTER J. HICKEL, GOVERNOR

DEPARTMENT OF LAW

OFFICE OF THE ATTORNEY GENERAL

May 3, 1991

The Hon. Pat Rodey
Alaska State Senator
P. O. Box V
Juneau, AK 99811-3100

Re: CSSB 154

Dear Senator Rodey:

Your office has asked us to review the 4/23/91 work draft of CSSB 154, relating to liability of financial institutions for environmental damage.

As you know, we have reviewed earlier versions of the bill. The 4/23/91 work draft contains virtually all of the problems that existed in prior drafts.

*** Section two would immunize - not merely remove from strict liability - financial institutions in a variety of situations. Even if the policy judgment is made that strict liability should not apply in certain situations involving financial institutions, there is no apparent reason to completely immunize the institutions from liability for their own negligent or intentional acts which caused harm to others or expense to the public.

*** The list of situations (sec. 2) in which financial institutions would receive immunity is so broad that it amounts to a general immunizing of almost all actions regarding land in which the institutions claim a security interest or other interest; it goes far beyond the original rationale for giving relief to such institutions, that they should not have to bear liability for problems which were encountered involuntarily and without fault.

*** The list is stated in the alternative, so that the limitation in proposed AS 46.03.825(a)(3), limiting liability where the institution does not exercise control over the property, does not apply to the other situations listed. For example, an institution may acquire a property through foreclosure; under (a)(1), that fact alone would immunize the institution from liability even if it actively managed the property and even if it knowingly or negligently caused the hazardous substance problem. Likewise, an institution acquiring property as a lessor under an extension of credit arrangement, or acquiring as a fiduciary (an extremely broad category) would be free to manage the property and free to

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cause a hazardous substance problem with no liability whatsoever. Note that these are situations in which the bank would have placed itself freely and voluntarily. There is no apparent justification for permitting a lending institution to immunize itself from all liability for the way in which it itself manages property, when its own actions harm either neighboring properties, neighboring people, or create a situation requiring expenditure of state or local funds to protect the public.

*** Subsection (a)(3) in the list in Section 2 implies that immunity is available to an institution with financial control under an extension of credit, only if it does not exercise managerial control. But the apparent limitation is illusory because the immunity applies unless the institution exercises "actual, direct, and continual managerial control that materially divests the borrower . . . of control..." In effect this means that if the institution's control is not constant, e.g., if it only steps in periodically, even if it actually orders actions which cause hazardous substance releases, it has no liability; and if its control is indirect, i.e., if it acts only through some intermediary such as a contractor, even if it orders the contractor to act in a way that harms others, it would bear no liability. And even if the institution's control were direct and continual, as long as the borrower retained some control itself and were not actually totally divested of it, it would bear no immunity. In short there is unlikely ever to be a situation in which an institution would have to bear the consequences of its own actions regarding such property.

*** Proposed AS 46.03.825(b) would limit the ability of the state to recover its response costs from a financial institution to the "actual benefit received" by the institution. This runs counter to the notion that the measure of damages when a party has caused harm to others is the amount of the harm, i.e., what it would take to make the injured party whole. There is no principle that a responsible party should never have to incur a net loss when the state has to step in to protect the public health. In essence this calls for the public treasury to subsidize the institutions' liabilities. The section goes even further, by limiting the reimbursement to the fair market value of the facility. It is common for a hazardous waste problem to cause property to have a negative value; therefore this section would decree that if the problem for which the institution is responsible is bad enough, it would not have to pay anything when the state steps in to prevent it from doing further harm to the public. This provision is analogous to the provision in federal law which limits liability of vessel owners for damages caused by the vessel to the remaining value of the vessel, even if it is zero. Congress removed this limitation of liability as it applies to oil spills last year in the Oil Pollution Act of 1990. This

The Hon. Pat Rodey
Alaska State Senator

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provision would reinstate, for both vessels and real property, a limitation on liability which has been universally condemned as archaic and unjust.

*** Section 3 would limit the state's existing statutory lien for its response costs to the vessel or property from which the release came. The result would be that the State could not recover its response costs where the property has become valueless or has been destroyed by the responsible party's own actions. When the legislature passed the existing lien law it carefully considered whether the lien should extend to all property of the responsible party, and it concluded that it was only fair to require the party -- not some damaged vessel or land -- to repay the state's costs in responding to the problem for which the party is legally responsible. In short, this provision is another way of immunizing a responsible party from paying for damages even when it is, in a technical sense, liable.

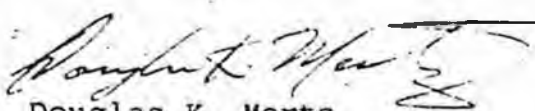
*** Section 5 would repeal the existing provision at AS 46.08.075(e) which permits a property owner, subject to a lien for response costs, to get an adjudication releasing that person's interest from lien upon a showing that the person is not liable. It is not clear why the banks desire this section repealed, but it may be that the banks want all people with an ownership interest in property from which there has been a release to remain subject to the lien along with the bank, so that the bank has leverage against its co-owners. Since this section applies only to persons who can demonstrate lack of liability, a repeal seems particularly unfair.

*** Section 6 would make the provisions limiting liability of institutions retroactive, so that it would apply even when the banks exercised control over the property before the act's effective date; in other words the provision would shift the burden for past situations in which the banks may be liable to other parties or to the taxpayers.

Let us know if we can be of further assistance.

Sincerely yours,

CHARLES E. COLE
ATTORNEY GENERAL

By: 
Douglas K. Mertz
Assistant Attorney General

DKM:tg

Patrick M. Rodey
Senator

Alaska State Legislature



Senate

311 C. St., Suite 510
Anchorage, Alaska 99503
(907) 561-7618

During Session:
P.O. Box V
Juneau, Alaska 99811
(907) 465-3793

SPONSOR SUMMARY

Senate Bill 154

SB 154 relates to the strict liability provisions enacted into the state's environmental laws in the spring of 1989. The bill which the state legislature enacted then, HB 68, was patterned after the strict liability provisions of the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), the law that established the SUPERFUND.

Just as the Congress and EPA are now re-thinking whether the strict liability provisions of federal law should be applied to the lending industry, so should the state be looking at the impact upon local lenders and fiduciary agents, and the availability of credit in Alaska.

The purpose of SB 154 is to eliminate the possibility that a lending institution which forecloses on property that is contaminated with hazardous waste, be liable for the cost of a clean-up, even if the lender in no way caused or contributed to the contamination. Likewise, the trust divisions of banking institutions should not be required to pay for a clean-up of property which it merely holds in trust for beneficiaries of estates and trust funds. Under present law, this is the case.

Sections 1 and 2 of the bill exempt designated lending and fiduciary institutions from the definition of "owner" or "operator", or person in "possession" of contaminated property as those terms are used in the strict liability provision of AS 46.03.822.

Sections 3 and 4 clarify the rights of the state to place a lien on real property which the state has had to clean up with state funds. Present law would allow the state to lien ALL PROPERTY of a liable person, including property in no way subject to or affected by the state's lien to the affected property. Section 4 clarifies that the priority of the state's lien is from the date of recording, which is the interpretation being given to present law despite its lack of clarity.

Section 5 of the bill eliminates the unclear language of the existing state lien provisions contained in AS 46.08.075 (e), which are replaced by Section 4 of the bill. Section 5 would also try to revive the exemption from liability contained in AS 46.03.822(b), by eliminating subpart (2) of that section which contains the requirement that a totally innocent person DISCOVER contamination AND begin operations to clean it up. This subpart (2) is not a requirement of federal law, and destroys the exemption to liability otherwise contained in AS 46.03.822(b) by imposing a duty to clean contamination in no way caused by an innocent party.

SB 154 does not address all the environmental problems facing the lending industry, however, it is a good way for the legislature to begin to study and address the problems created by the sweeping and unclear language contained in the present strict liability provisions of AS 46.03.822.

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MEMORANDUM

DATE: March 9, 1991

TO: Senator Lloyd Jones, Chair
Senate Resources Committee

FROM: Senator Pat Rodey *Pat*

SUBJ: Request for Hearing - SB 154

I respectfully request a hearing in the Senate Resources Committee for SB 154, relating to liability for environmental damage, and to liens arising from environmental damage.

The bill has three main objectives. One is to eliminate a state requirement that an innocent third party take responsibility for containment and cleanup of hazardous substance contamination.

The second is to provide an exemption from liability for lending and fiduciary institutions who take title or control through bankruptcy, foreclosure, tax delinquency or abandonment action.

The third objective is to clarify and limit the state's environmental lien provision.

I would appreciate the earliest possible scheduling of SB 154 before the committee.

PMR/tb/memo03

STATE OF ALASKA

WALTER J. HICKEL, GOVERNOR

DEPT. OF ENVIRONMENTAL CONSERVATION

OFFICE OF THE COMMISSIONER
P.O. BOX 0, JUNEAU, ALASKA 99811-1800

TELEPHONE
(907) 465-2600

POSITION PAPER SB 154

SB 154 would exempt lending institutions and fiduciaries from liability for environmental damage. Even those fiduciaries who have been involved in the control or management of the facility or vessel responsible for the damage would not be liable. Because the potential for liability is believed to lead to better facility management, the Department does not support this limitation. The Department would support both a definition of "management" of a facility or vessel as well as the development of professional standards for environmental audits by the private sector. In that way, just as a structural engineer examines for the lending institution a building's structure, a private environmental engineer would examine the property's environmental condition.

Section Three would limit the responsible party's assets which the State could attach for expenditures from the Oil and Hazardous Substance Release Response Fund. Under this language, the State would only be able to look to the value of the real property which was the subject of the remediation for satisfaction of the responsible party's debt to the State. Currently, the State may look to all assets owned by the responsible party. Without that ability, it is expected that the Department would encounter difficulty in recovering Response Fund costs, and thus the Department does not support this provision.

Section Five in part repeals AS 46.03.822(b)(2) which limits the liability of an owner and operator for damage caused by an unrelated third party or an act of God so long as the owner or operator discovered the hazardous substance and began containment and cleanup within a "reasonable period of time." The Department does support this repeal.



John A. Sandor
Commissioner

Post-It™ brand fax transmittal memo 7671 # of pages 2

To: Tim Rodley	From: Annie
Co.	Co. DEC
Dept.	Phone #
Fax # 463-3144	Fax #

AlaskaUSA

Federal Credit Union

TO: Senator Pat Rodey

DATE: March 18, 1991

FROM: William B. Eckhardt
President

SUBJECT: ~~Senate Bill 154~~

From a lenders standpoint, the factor which creates a greater potential for loss than either market risk or credit risk, is the risk associated with environmental contamination. Under various laws, a lender can be held liable for the cost of cleanup of contaminated properties. While these environmental laws are extremely complex, liability for clean up is very simple. Regardless of who contaminated the property, the current owner of the property, which a lender becomes through the foreclosure process, is financially responsible for cleanup and damages. While there are methods that can be used to limit lender liability when originating a real estate loan, there is no way to guarantee that during the term of the loan the property value will not be impaired by contamination. If an individual property owner is not financially capable of cleaning up a property, the government can clean the property and file a superior lien for their incurred costs.

Both federal and state environmental laws, as currently written, have severely curtailed or eliminated sources of credit for real estate related transactions. In fact, Alaska USA discontinued granting real estate loans in October of 1989 directly as a result of environmental laws. Prior to that time, the credit union granted \$50 million in real estate loans each year. We feel the availability of credit for real estate-related purposes is an essential part of the economy, without which property values will remain depressed and economic development will be adversely affected.

The criticism of Senate Bill 154, and other proposed legislation on the federal level, is that if lenders are not held responsible for cleanup, then widespread lending to potential polluters will occur. This simply will not happen. If a lender were to blindly extend credit to such potential polluters, they risk the borrower defaulting on the loan because of the ultimate cost of cleanup and additionally risk the loss of the collateral's value if the property is left contaminated. Today, the financial services industry and their regulators are ultra-sensitive to real estate loan losses. The potential extension of credit, as the criticism suggests, would be financially irresponsible and certainly invoke regulatory sanctions.

Currently, prudent lending requires not only the traditional appraisal, title insurance, etc., but also site assessments for the detection of environmental contamination. If, through the site assessment, contamination is discovered, then the law requires it to be reported. If the contaminated real estate is to ever have economic value, it must be ultimately cleaned. Without third-party lending and the related requirement for site assessments, contaminated properties could go undetected and unreported, and continue to pollute the environment for years.

The proposed changes to existing laws with regard to lender liability will encourage the active involvement of financial institutions in real estate lending. Through required site assessments, financial institutions can assist in the identification of contaminated properties and in policing of the environment. This participation, however, will not occur if lender liability for cleanup remains as currently written. Consequently, we feel it is in the best interest of the environment, the economy, and the people of Alaska that Senate Bill 154 be passed this session.

Section 1. AS 46.03.822 (c) is amended to read:

(c) For purposes of (b)(1)(B) of this section, a third party or an agent of a third party is in privity of contract with the person who is otherwise liable, if the third party or its agent and the person are parties to a land contract, deed, or other instrument transferring title or possession of the real property on which the facility in question is located, unless that property was acquired by the person after the disposal or placement of the hazardous substance on, in, or at the facility, and the person establishes that the person has satisfied the requirements of (b)(1)(B) of this section and establishes that

(1) at the time the person acquired the facility the person did not know and had no reason to know that a hazardous substance that is the subject of the release or threatened release was disposed of on, in, or at the facility;

(2) the person is a governmental entity that acquired the facility by escheat, or through another involuntary transfer or acquisition, or through the exercise of eminent domain authority by purchase or condemnation;

(3) the person is a corporation organized under 43 U.S.C. 1601-1629e (Alaska Native Claims Settlement Act) that acquired the facility under those sections;

(4) the person acquired the facility by inheritance or bequest;
[or]

(5) the person is a state governmental entity and the state acquired the facility under Public Law 85-508 (Alaska Statehood Act)[.]; or

(6) the person's interest in the facility arose as a lender to a person owning or controlling the facility or arose as a security holder in the facility, and the person has not controlled, managed, or influenced the operations at or on the facility, whether or not it had the capacity to do so.

define lender

Mr. Chairman, I am pleased to introduce S.B. 154 and recommend its passage by the Senate. The bill relates to the strict liability provisions enacted into the state's environmental laws in the spring of 1989, shortly after the Exxon Valdez tragedy.

The bill the state legislature enacted in 1989 (H.B. 68) was patterned after the strict liability provisions of the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), 42 U.S.C. §9601 et seq., known as the law that established the "Superfund". Just as the federal Congress and the Environmental Protection Agency now are re-thinking whether the strict liability provisions of federal law should be applied to the lending industry, I believe it is time for the state legislature to analyze the effect that the state strict liability statute has had and will have upon the lending institutions and the availability of credit in Alaska. It is time for us to address the serious questions and solve the problems that our state law provisions have created, before the effect is to seriously jeopardize the availability of credit.

The purpose of S.B. 154 is to eliminate the possibility that a lending institution, that forecloses upon property which is contaminated with hazardous waste, may be liable for the cost of cleaning up the contamination, even if the lender in no way caused or contributed to the contamination. Likewise, the trust companies of banking institutions should not be required to pay for a cleanup of contaminated properties they merely hold in trust for beneficiaries of estates and trust funds. Under present law, a person merely holding title to contaminated property may be liable for a cleanup, even if that title is held in trust for others.

Sections 1 and 2 of the bill exempt designated lending and fiduciary institutions from the definition of "owner", "operator", or person in "possession" of contaminated property, as those terms are used in the strict liability provision of AS 46.03.822.

Sections 3 and 4 of S.B. 154 clarify the rights of the state to place a lien on real property the state has had to clean up with state funds. Present law would allow the state to lien

all property of a liable person, including property in no way subject to or affected by the state's clean up activities. Section 3 would limit the state's lien to the affected property. Section 4 clarifies that the priority of the state's lien is from the date of recording, which is the interpretation being given to present law despite its lack of clarity.

Section 5 of S.B. 154 eliminates the unclear language of the existing state lien provisions contained in AS 46.08.075(e), which are replaced by Section 4 of the bill.

Section 5 also would try to revive the exemption from liability contained in AS 46.03.822(b), by eliminating subpart (2) of that section which contains the requirement that a totally innocent person discover contamination and begin operations to clean it up. This subpart (2) is not a requirement of federal law, (see 42 USC §9607(b)) and destroys the exemption to liability otherwise contained in AS 46.03.822(b), by imposing a duty to cleanup contamination in no way caused by an innocent party.

Mr. Chairman, S.B. 154 does not address all the environmental problems facing the lending industry. I wish that it did. But S.B. 154 is a good way for the legislature to begin to study and address the problems created by the sweeping and unclear language contained in the present strict liability provisions of AS 46.03.822.

FISCAL NOTE

STATE OF ALASKA
1991 LEGISLATIVE SESSION

BILL NO. SB 154

Revision Date: _____ Department Affected: DEC
 Title: Liability and liens for BRU: Environmental Quality
Environmental Damage
 Sponsor: Senator Rodey Component: EQ Projects
 Requestor: Senator Rodey

COMPONENT SERIAL NO. 1 1 0 1 1 6

EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 92	FY 93	FY 94	FY 95	FY 96	FY 97
PERSONAL SERVICES	0.0	0.0	0.0	0.0	0.0	0.0
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL						
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REVENUE						
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FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

POSITIONS:

FULL-TIME	0.0	0.0	0.0	0.0	0.0	0.0
PART-TIME						
TEMPORARY						

Estimate of current year impact: NONE

ANALYSIS: (Attach a separate page if necessary.)

If SB 154 is enacted into law, the number of sites for which the State would become responsible for cleaning up would be expected to increase. However, estimating those costs to the State at this time is not possible.

Prepared by: Janice Adair
 Division: Commissioner's Office

Phone: 465-2600
 Date: 3-15-91

Approved by Commissioner: *Michael J. Dunbar*
 Agency: Dept. of Environmental Conservation

Date: 3/18/91

Distribution (by preparer): Legislative Finance, Legislative Sponsor, Requestor, OMB, & Impacted Agency(ies).

Environmental Damage
(liability for/liens arising
out of)

SENATE BILL NO. 154, by Senator RODEY. Relates to liability for environmental damage and to liens arising from environmental damage:

-Amends AS 46.03.826(8) (Environmental Conservation. Definitions), the definition of "owner" and "operator" by adding language to read: "(8) 'owner' and 'operator' ... (B) do not include ... (ii) a designated lending institution that acquires ownership or control of the facility or vessel under the terms of a security interest held by the institution in the facility or vessel; (iii) a corporation that in a fiduciary capacity has legal title to a facility or vessel for the purpose of administering an estate or trust of which the facility or vessel is a part or does not have legal title to a facility or vessel but operates or manages the facility or vessel under the terms of an estate or trust of which the facility or vessel is a part; (iv) an individual who in a fiduciary capacity has legal title to a facility or vessel for the purpose of administering an estate or trust of which the facility or vessel is a part; (v) an indenture trustee for debt securities or for a certificate of interest or participation in debt securities that acquires ownership or control of a facility or vessel as the result of a default under the terms of the indenture agreement, or similar financing document, between the trustee and the entity issuing the debt securities or certificates of interest or participation; (vi) a designated lending institution that acquires ownership of a facility or vessel in connection with a lease subject to regulation by federal or state banking authorities."

-Amends AS 46.03.826(14) (Environmental Conservation. Definitions), by adding a definition of "designated lending institution;" and "possessed" or "possession" as those terms apply to the new language added to the definition of "owner" and "operator."

-Amends AS 46.08.075(a) (Oil and Hazardous Substance Releases. Liens Against Property as Security for State Expenditures) to read: "(a) The state has a lien for expenditures by the state from the oil and hazardous substance release response fund or from any other state fund, for the costs of response, containment, removal, or remedial action resulting from an oil or hazardous substance spill, or, with respect to response costs, the substantial threat of a release of oil or a hazardous substance against all real property that is owned by a person who is determined by the commissioner to be liable for the expenditures under this chapter, AS 46.03, AS 46.04, 42 U.S.C. 9607, or other state or federal law, and that is subject to or affected by a removal or remedial action. ..." (underlined language added to current law).

LEGISLATIVE REPORTING SERVICE
REPORT # 6)
MARCH 4, 1991,
Pgs. 297-298

Adds a new subsection to AS 46.08.075 (Oil and Hazardous Substance Releases. Liens Against Property as Security for State Expenditures) to provide: "(f) The lien imposed by this section is subject to the rights of a purchaser, holder of a security interest, or judgment lien creditor if the interest of the purchaser, holder, or creditor is perfected under applicable law before notice of the lien is filed in the appropriate recorder's office under (b) of this section. The purchaser, holder of a security interest, or judgment lien creditor shall be afforded the same protections against the lien imposed by this section as are afforded under state law to a purchaser, holder of a security interest, or judgment lien creditor against a judgment lien that arises out of an unsecured obligation and that arises at the same time the notice of the lien created under this section is filed."

-Repeals AS 46.03.822(b)(2) (Environmental Conservation. Strict Liability for the Release of Hazardous Substances), subsection (b)(2) provides: "(b) In an action to recover damages or costs, a person otherwise liable under this section is relieved from liability under this section if the person proves ... (2) in relation to (1)(B) or (C) of this subsection, that the person, within a reasonable period of time after the act occurred, (A) discovered the release or threatened release of the hazardous substance; and (B) began operations to contain and clean up the hazardous substance."

-Repeals AS 46.08.075(e) (Oil and Hazardous Substance Releases. Liens Against Property as Security for State Expenditures), subsection (e) provides: "(e) A person with an ownership interest in property against which a lien is recorded may bring an action in a court of competent jurisdiction to require that the lien be released. The lien may be released to the extent of that person's ownership interest if the court finds that the person is not liable for the expenses incurred by the state in connection with the costs of response, containment, removal, or remedial action resulting from the oil or hazardous substance release or threat of release of oil or a hazardous substance."

Introduced March 1, 1991 and referred to Resources; Judiciary.

DIVISION OF LEGAL SERVICES

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MEMORANDUM

March 12, 1991

SUBJECT: Sectional analysis of SB 154 (W.O. 7-LS0716\A)

TO: Senator Pat Rodey
Attn: Tim

FROM: Theresa L. Bannister ^{TB}
Legislative Counsel

You have requested a sectional analysis of the above described bill.

As a preliminary matter, note that a sectional analysis of a bill should not be considered an authoritative interpretation of the bill and the bill itself is the best statement of its contents.

Section 1 adds a list of individuals and entities that are not considered "owners" or "operators" under AS 46.03.822 - 46.03.828, the sections addressing strict liability for the release of hazardous substances.

Section 2 defines "designated lending institution", which appears in the description of some of the entities added by sec. 1. Also defines "possessed" and "possession".

Section 3 qualifies the type of property that is subject to a lien by the state for certain oil/hazardous substance response expenditures. States that the property must be real property and that it must be property that is subject to or affected by a removal or remedial action.

Section 4 states that the lien imposed by AS 46.08.075(a) is subject to the rights of certain entities if the rights are perfected before the notice of the lien is filed. Gives these perfected rights the same protection against the lien as would be provided against a judgment lien that arises out of an unsecured obligation and that arises at the same time as the notice of the lien.

Section 5 repeals certain statutory provisions.

If I may be of further assistance, please advise.

TLB:gc:pl
91-139.glc