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Foreclosing on Lender Liability: The European Union Launches Environmental, Civil Liability Legislation

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I. INTRODUCTION

In response to the "slow but relentless deterioration" in the state of the environment, the European Union (EU) is considering a system of civil liability to finance the cleanup of environmental damage.[1] During 1993, the EU Commission circulated a discussion document known as the Green Paper[2] on Remedying Environmental Damage (Green Paper).[3] The Green Paper, a communication from the EU Commission to the Council of Ministers and Parliament, discusses the usefulness of civil liability to remedy environmental damage and finance its cleanup.[4] The recommendation, which remained open for discussion through October 1993, is similar to the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) enacted in the United States.[5] CERCLA holds responsible parties strictly liable for environmental damage.[6] Following the enactment of CERCLA in 1980, U.S. lenders faced environmental liability as "owners and operators" of contaminated property.[7] European financial institutions, aware of the liability concerns facing lenders in

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1. EU Environment Commissioner Ioannis Paleokrassas, Address Before the European Parliament Regarding the Green Paper in Brussels, Belgium (Nov. 3, 1993), *in* Reuter Eur. Community Rep., Nov. 3, 1993, *available in* LEXIS, News Library, Reueub File. On November 1, 1993, the former European Community (EC) became known as the European Union (EU). *European Union*, FIN. TIMES, Nov. 1, 1993, at 15. Since the author is uncertain whether the former EC organizations have altered their names to reflect the EU name change, this comment refers to EC organizations by their previously recognized titles.

2. A Green Paper concentrates interest in a particular area and is used in preparing legislation. *EC—EC Environmental Liability Legislation*, MARKET REP., Aug. 17, 1993.

3. Green Paper on Remedying Environmental Damage COM(93) 47, Mar. 1993 [hereinafter Green Paper]; *EC Dives into Environmental Liability Debate*, EC ENERGY MONTHLY, Sept. 16, 1993. The EU Environment Commissioner Ioannis Paleokrassas declared the development of an environmental, civil liability system to be a priority in 1994. *The Week in Europe: Aid for Britain's Jobless*, PRESS ASS'N NEWSFILE, Jan. 20, 1994.

4. Green Paper, *supra* note 3, § 1.0; *Environment*, EC Commentaries (Coopers & Lybrand) (Mar. 3, 1994) *available in* LEXIS, Intlaw Library, Eurscp File (discussing the civil liability proposal in the Green Paper); Chris Napier, *World: Paying Out for Pollution—EC Green Paper Opens Debate with Insurers*, REACTIONS, July 1, 1993 (discussing the community-wide system of civil liability approach of the Green Paper). *See infra* notes 26-29 and accompanying text (explaining the Commission, Parliament, and Council of Ministers).

5. 42 U.S.C. § 9607 (1994); Green Paper, *supra* note 3, § 4.1.2. Similar to the strict liability scheme employed in the United States under CERCLA, the Green Paper examines the advantages of a strict liability system for remedying environmental damage in the EU. Green Paper, *supra* note 3, § 4.1.2.

6. 42 U.S.C. § 9607 (1994). CERCLA consists of environmental legislation in the United States which holds "owner[s] and operator[s]" of "vessel[s] or facilit[ies]" liable for damage to natural resources and cleanup costs as the result of such damage. *Id. See infra* notes 66-98 and accompanying text (discussing the effect of CERCLA on financial institutions); *infra* notes 159-79 and accompanying text (examining the civil liability system expounded in the Green Paper).

7. *See infra* notes 66-98 and accompanying text (discussing lender liability under CERCLA).

the United States, fear being held strictly liable under the proposed environmental legislation in the European Union.[8]

Concerned parties in the European Union, particularly bankers, carefully follow lender liability issues in the United States in order to anticipate events under similar EU legislation.[9] The Banking Federation of the European Community (BFEC) has expressed concern over potential lender liability. The BFEC is particularly apprehensive about acquiring the responsibility of policing borrower behavior in order to prevent their own liability for environmental damage.[10]

European industries have also expressed discontent with the establishment of a civil liability system similar to CERCLA legislation.[11] The European gas and electricity lobbyists and the Union of Industrial and Employers' Confederations of Europe (UNICE) have registered discontent with the U.S. civil liability system under CERCLA.[12] However, European environmental leaders appreciate the value of examining the civil liability system in the United States.[13] The U.K. environmental minister and the American Chamber of Commerce in Belgium advocate reviewing the benefits of CERCLA while averting the repercussions of

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8. *Lender Liability*, FIN. TIMES, Mar. 13, 1992. Banks fear that they will be held liable as owners operators or deemed producers under environmental legislation. *Id. See EC Dives into Environmental Liability Debate*, *supra* note 3 (noting that European policy makers consider the U.S. Superfund experience); *Emerging Issues: A Crisis Looms*, BUS. INT'L MONEY REP., June 14, 1993 (noting that many European entities carefully follow U.S. cleanup expenditures).

9. *Emerging Issues: A Crisis Looms*, *supra* note 8 (noting that many European entities carefully follow environmental spending in the United States).

10. *Environment: First Clash of Swords in Liability Debate*, Multinat'l Serv. (Eur. Info. Serv.), Nov. 20, 1993 available in LEXIS, World Library, Allwld File [hereinafter *First Class*] (announcing the Banking Federation's concern about environmental liability). The Banking Federation wishes to limit lender involvement in environmental cleanup to the general monitoring of client activities. *Id.* The Banking Federation of the European Economic Community (BFEC) represents the interests of banking associations in the EU and the European Free Trade Association (EFTA). ENCYCLOPEDIA OF ASSOCIATIONS: INTERNATIONAL ORGANIZATIONS 25 (Grant J. Eldridge ed., 28th ed. 1993).

11. *First Clash*, *supra* note 10. The chemical industry and the European Federation of Waste Management have expressed discontent specifically with CERCLA's civil liability scheme. *Id.* The International Chamber of Commerce, the insurance industry, and the banking industry have expressed general discontent with a civil liability scheme. *Id.*

12. *Gas, Power Sectors Take Hard Line on Environmental Liability*, FLIGHT INT'L, Oct. 21, 1993; *UNICE Expresses Strong Opposition*, FLIGHT INT'L, Oct. 21, 1993. Gas and electricity lobby groups negatively view Superfund because of the tremendous resources that are expended in identifying polluters. *Gas, Power Sectors Take Hard Line on Environmental Liability*, *supra.* UNICE argues that only the party controlling the activity causing the damage should be held responsible for the damage. *UNICE Expresses Strong Opposition*, *supra.* Additionally, the UNICE believes that financial institutions which do not participate in decisions which lead to environmental damage should not be held liable. *Id.*

13. *AmCham Draws US Lessons*, FLIGHT INT'L, Oct. 1993 (noting the support for an examination of the experience under Superfund by the American Chamber of Commerce in Belgium (AmCham)); *Opening Volleys*, FLIGHT INT'L, Oct. 1993 (quoting U.K. environmental minister's recognition of the positive benefits of Superfund).

sweeping civil liability.[14] Since the Green Paper recognizes the importance of addressing the detrimental effects of civil liability, particularly the consequences facing the lending industry,[15] it is helpful to analyze the effects of civil liability on U.S. lenders under CERCLA.

By examining the experience of lenders and financial institutions under CERCLA, EU lenders can avoid repeating the miscalculations of U.S. lenders.[16] Following a federal appellate court decision which broadly interpreted the security interest exemption under CERCLA, lenders began to confront uncertain environmental liability.[17] In order to alleviate potential liability, the Environmental Protection Agency (EPA) drafted a rule clarifying the security interest exemption under CERCLA.[18] The EPA's clarification has created a safe haven for lenders facing liability under CERCLA.[19]

This comment explores liability issues that EU lending institutions will face if the EU adopts CERCLA-like civil liability legislation. Part II discusses the origins of environmental legislation in the EU and examines the European stimulus for environmental legislation.[20] Part III reviews the U.S. approach to civil liability under CERCLA, the effect of case law, and the administrative response.[21] Part IV previews the forthcoming EU system of civil liability as pronounced in the Green Paper and addresses the detrimental consequences of

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14. *AmCham Draws US Lessons*, *supra* note 13; *Opening Volleys*, *supra* note 13. U.K. Environmental Minister Tim Yeo called for recognition of Superfund success in prevention of environmental damage. *Opening Volleys*, *supra* note 13. The EU Committee of AmCham also notes that it is important to recognize the advantages of comprehensive environmental legislation while avoiding the "overly broad liability system." *AmCham Draws US Lessons*, *supra* note 13.

15. Green Paper, *supra* note 3, § 4.1.2 (recognizing the need to consider how financial institutions will be affected by a system of strict liability).

16. *See AmCham Draws US Lessons*, *supra* note 13. The EU Committee of AmCham examines the EU position on civil liability in light of the U.S. experience under Superfund. *Id.* *See* notes 13-14 (describing AmCham). U.K. Environmental Minister Tim Yeo calls for recognition of the positive benefits of Superfund, including the effectiveness of deterring further contamination. *Opening Volleys*, *supra* note 13.

17. United States v. Fleet Factors Corp., 901 F.2d 1550, 1558 (11th Cir. 1990). Liability for cleanup costs is based on the lender's capacity to influence hazardous waste decisions. *Id.* *See* Peter N. Lavalette, Comment, *The Security Interest Exemption Under CERCLA: Timely Relief from the EPA*, 24 U. TOL. L. REV. 473, 475 (1993) (stating that the lending community faces uncertain and controversial exposure to liability since *Fleet Factors*); Michael I. Greenberg & David M. Shaw, Note, *To Lend or Not to Lend—That Should Not Be the Question: The Uncertainties of Lender Liability Under CERCLA*, 41 DUKE L.J. 1211, 1211-12 (1992) (noting that lender uncertainty is the result of differing interpretations of the security interest exemption under CERCLA); *infra* notes 79-98 and accompanying text (reviewing *United States v. Fleet Factors*).

18. National Oil Hazardous Waste Substance Pollution Contingency Plan; Lender Liability Under CERCLA, 57 Fed. Reg. 18,344 (1992) (codified as 40 C.F.R. §§ 300.1100, 300.1105 (1992)); Lavalette, *supra* note 17, at 508 (noting that the EPA regulations offer guidance to lenders to avoid liability under CERCLA). *See infra* note 103 (noting that the EPA rule has been invalidated by the D.C. Circuit Court).

19. National Oil and Hazardous Waste Substances Pollution Contingency Plan; Lender Liability Under CERCLA, 40 C.F.R. §§ 300.1100, 300.1105 (1992). *See* 57 Fed. Reg. 18,344, 18,348-74 (1992) (discussing the promulgation of the EPA clarification of the secured creditor exemption); Lavalette, *supra* note 17, at 487-92 (reviewing the EPA rule); *infra* notes 99-136 accompanying text (discussing the EPA rule).

20. *See infra* notes 24-65 and accompanying text.

21. *See infra* notes 66-162 and accompanying text.

lender liability.[22] Finally, part V recommends that European lenders undertake certain precautions to reduce the possibility of environmental liability during the uncertain period before and shortly after the enactment of environmental, civil liability legislation.[23]

II. RECENT TRENDS IN EU ENVIRONMENTAL LAW

A. EU Background

In 1957, the Treaty of Rome (EEC Treaty) gave birth to the idea of a common market among European countries.[24] The EEC Treaty remains fundamentally intact, although subsequent legislation has amended it.[25] Three institutions are authorized under the EEC Treaty to participate in the legislative process in the EU: the Commission, Council of Ministers, and European Parliament.[26] The Commission initiates legislative proposals and implements EU law,[27] while the Council of Ministers reviews Commission proposals and prescribes EU law based on these proposals.[28] Additionally, the European Parliament aids in the decision-making authority of the Council by commenting on Commission proposals before a final decision is made by the Council.[29] While the original EEC Treaty contained no provisions regarding the environment, the Single European Act (SEA)[30] amended the EEC Treaty to include environmental legislation.[31]

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22. *See infra* notes 163-91 and accompanying text.

23. *See infra* notes 192-228 and accompanying text.

24. Treaty Establishing the European Economic Community, Mar. 25, 1957, 298 U.N.T.S. 11 [hereinafter EEC Treaty]. Two other treaties were also involved in the establishment of an European Union: the Treaty Establishing the European Coal and Steel Community (ECSC) and the Treaty Establishing the European Atomic Energy Community (Euratom); however, the EEC Treaty was the instrumental device in the move toward a common market. Treaty Establishing the European Atomic Energy Community, Mar. 25, 1957, 295 U.N.T.S. 259; Treaty Establishing the European Coal and Steel Community, Apr. 18, 1951, 261 U.N.T.S. 140.

25. P.S.R.F. MATHIJSEN, A GUIDE TO EUROPEAN COMMUNITY LAW 2 (5th ed. 1990) (noting Single European Act, Merger Treaty, and Act regarding direct elections for European Parliament are among the several acts which have amended the original treaty). A comprehensive list of amending treaties acts may be found in the table of "abbreviations used in footnotes" reproduced prior to the text of the EEC Treaty at 2 B.D.I.E.L. (CCH) 45 (1989).

26. EEC Treaty, *supra* note 24, arts. 137, 145, 157.

27. THE ENVIRONMENTAL LAW INSTITUTE, EUROPEAN COMMUNITY DESKBOOK 4 (1992) [hereinafter DESKBOOK]; JOHN PAXTON, A DICTIONARY OF THE EUROPEAN ECONOMIC COMMUNITY 44 (1977).

28. DESKBOOK, *supra* note 27, at 4; PAXTON, *supra* note 27, at 58.

29. DESKBOOK, *supra* note 27, at 4; PAXTON, *supra* note 27, at 58.

30. Single European Act, July 1, 1987, 30 O.J. Eur. Comm. (No. 169) 1 (1987). *See* Mark L. Jones, *Treaty Establishing the European Economic Community (Treaty of Rome), Introduction and Bibliography*, 2 B.D.I.E.L. (CCH) 3 (1989) (stating that the slow pace of integration led to the adoption of the SEA).

31. EEC Treaty, *supra* note 24, art. 130r; Thomas R. Mounteer, *Proposed European Community Directive for Damage to the Environment Caused by Waste*, 23 ENVTL. L. 107, 111 (1993) (discussing the adoption of environmental provisions in the EU). The EEC Treaty requires that all EU actions "shall be based on principles that preventative action should be taken, that environmental damage should as a priority be rectified at [its]

Similar to the U.S. judicial interpretation of CERCLA, the SEA amendments embodied a "polluter should pay" principle.[32] Following the mandate of the EEC Treaty, the Commission considered the merits of civil liability to implement this principle.[33] The Green Paper evaluates the usefulness of both strict and fault liability regimes to remedy environmental damage.[34] Although the EEC Treaty permits member states to adopt more stringent environmental standards, the Green Paper acknowledges that differing standards among member states may result in "distortions of competition" in the single market.[35] Uniform environmental legislation will alleviate competition distortions between member states.[36] Beyond the need for uniform legislation, the Commission was also motivated by public demand for a system of environmental accountability, a pledge by the Council of Ministers to draft environmental legislation, and a similar draft Convention on environmental liability by the Council of Europe.[37] In March 1993, the Commission delivered the Green Paper to the Council and Parliament.[38] The Commission recommended the adoption of a strict, civil liability standard supplemented with a system of joint compensation.[39]

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source, and the polluter should pay." EEC Treaty, *supra* note 24, art. 130r. *See* MATHIJSEN, *supra* note 25, at 275-76 (reviewing environmental legislation in the EU).

32. EEC Treaty, *supra* note 24, art. 130r; Green Paper, *supra* note 3, § 1.0. CERCLA mandates that parties responsible for environmental damage finance the cost of cleanup. United States v. Bliss, 667 F. Supp. 1298, 1304 (E.D. Mo. 1987).

33. Green Paper, *supra* note 3.

34. *Id.* § 2.1. "[Civil liability] was developed to cover situations where it was more just to make the person responsible for the act or incident causing the damage to bear the consequent costs . . . ." *Id.*

35. EEC Treaty, *supra* note 24, art. 130t; Green Paper, *supra* note 3, § 1.0. "The protective measures adopted . . . shall not prevent any Member State from maintaining or introducing more stringent protective measures compatible with this Treaty." EEC Treaty, *supra* note 24, art. 130t.

36. Green Paper, *supra* note 3, § 1.0. EU Environment Commissioner Ioannis Paleokrassas notes that environmental legislation promulgated at the national level will create differences in extent and amount of liability between member states. *Paleokrassas Outlines Views on Environmental Liability Debate*, EC ENERGY MONTHLY, Nov. 19, 1993 [hereinafter *Paleokrassas Outlines*].

37. Green Paper, *supra* note 3, § 1.0. *See infra* notes 40-53 and accompanying text (discussing the Council of Europe's Convention on Civil Liability for Damage Resulting from Activities Dangerous to the Environment).

38. Green Paper, *supra* note 3. During a five month discussion period, the Commission accepted over 100 comments from interested parties and organizations. Paleokrassas, *supra* note 1. *See infra* notes 159-76 and accompanying text (examining the civil liability system proposed in the Green Paper).

39. Green Paper, *supra* note 3. *See infra* notes 159-76 and accompanying text (examining the Green Paper).

B. European Environmental Legislation

1. Convention on Civil Liability for Damage Resulting from Activities Dangerous to the Environment

Environmental action by the Council of Europe precipitated the development of the Green Paper.[40] The Council of Europe is an entirely distinct body from the EU and should not be confused with any of the EU branches: the Commission, Council of Ministers, or Parliament.[41] Formed in 1948, the Council of Europe promotes political and military integration in Europe.[42] Although many of its economic proposals have been superseded by EU action, the Council of Europe has made advances in the human rights arena.[43] One commentator has noted that the Council of Europe "provides a forum for cultural and political contacts extending beyond membership in the EU and so preserves the concept of European unity."[44]

In June 1993, seven European countries signed the Council of Europe's Convention on Civil Liability for Damage Resulting from Activities Dangerous to the Environment (Convention).[45] The Convention holds operators liable for injury to property, persons, or the environment when the operator conducts activities dangerous to the environment.[46] The Convention exempts operators who can prove a force majeure,[47] intervening third-party acts, or compliance with the public authority regulations.[48]

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40. Green Paper, *supra* note 3, § 1.0. The Commission began to consider an environmental protection system of liability because the Council of Europe and other international organizations are establishing liability schemes. *Id.*

41. Members of the Council of Europe include Austria, Belgium, Cyprus, Denmark, France, Germany, Greece, Iceland, the Republic of Ireland, Italy, Liechtenstein, Luxembourg, Malta, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, and the United Kingdom. Kellee A. Brown & Sophia A. Muirhead, *Extradition: Divergent Trends in International Cooperation*, 33 HARV. INT'L L.J. 223, 234 n.72 (1992). The members of the European Union include Belgium, Denmark, France, Germany, Greece, Italy, Luxembourg, the Netherlands, Portugal, the Republic of Ireland, Spain, and the United Kingdom. ENCYCLOPEDIA OF ASSOCIATIONS: INTERNATIONAL ORGANIZATION *supra* note 10.

42. D. LASOK & J.W. BRIDGE, LAW AND INSTITUTIONS OF THE EUROPEAN ECONOMIC COMMUNITY 9-10 (4th ed. 1987); PAXTON, *supra* note 27, at 55-57 (discussing the Council of Europe).

43. LASOK & BRIDGE, *supra* note 42, at 9-10; PAXTON, *supra* note 27, at 55-57 (discussing the Council of Europe).

44. PAXTON, *supra* note 27, at 55-57 (discussing the Council of Europe).

45. Convention on Civil Liability for Damage Resulting from Activities Dangerous to the Environment, SEC(91) 750 final (adopted on Mar. 8, 1993) [hereinafter Convention]. Cyprus, Greece, Italy, Liechtenstein, Luxembourg, Finland, and the Netherlands signed the Convention on June 21, 1993. *Environment*, *supra* note 4; *Environment: Seven States Sign Civil Liability Convention Europe Energy*, EUR. ENERGY, July 9, 1993, § 405.

46. *See EC—EC Environmental Liability Legislation*, *supra* note 2 (reviewing the Convention by Europe's Convention).

47. If an operator can prove a force majeure, that operator may be fully exonerated from environmental liability. See *Environment*, *supra* note 4.

48. *See EC—EC Environmental Liability Legislation*, *supra* note 2 (reviewing the Convention by the Council of Europe).

Although the Convention is the first international legal document to propose a general principle on environmental liability,[49] at least two and perhaps four members of the EU will not support the Convention endorsed by the Council of Europe.[50] The Commission has criticized the Convention's failure to provide strict guidelines to prevent distortions of competition in the EU.[51] Nevertheless, the Commission is considering using the Convention as a starting point for an EU initiative.[52] In addition to examining the environmental liability schemes of individual member states, the Commission also surveyed the civil liability system of the United States established under CERCLA.[53]

2. *Council Directive on Civil Liability for Damage Caused by Waste*

Notwithstanding the significant acceleration in EU environmental legislation over the past twenty years, recent civil liability developments are elevating concern over potential environmental liability.[54] The Council Directive on Civil Liability for Damage Caused by Waste (Waste Directive)[55] imposes strict, joint and several liability for personal injuries, property damage, and environmental damage.[56] The Waste Directive, which endorses the imposition of strict liability on the producers of waste,[57] has been criticized for its potential impact on lenders.[58]

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49. *Environment, supra* note 4.

50. *Environment: The Council of Europe Convention on Environmental Liability*, EC Commentaries (Coopers & Lybrand) (Oct. 11, 1993) *available in* LEXIS, Intlaw Library, Eurscp File. Denmark and the United Kingdom have announced their intention not to support the Convention. *Id.* Ireland and Germany disagree with the approach to environmental liability taken by the Council of Europe. *Id.*

51. *Environment, supra* note 4 (explaining that the multitude of enforcement options available under the Council's Convention will lead to distortions of competition).

52. Green Paper, *supra* note 3, § 4.1.2. The usefulness of the Convention as a model is limited by the fact that it covers only damage caused by dangerous activities. *Environment Council: Fairly Warm Welcome for the Green Paper on Liability*, EUR. ENERGY, Dec. 17, 1993, § 414 (comments of EU Environment Commissioner Ioannis Paleokrassas).

53. Green Paper, *supra* note 3, § 3.2.2 & annex. In addition to the Convention developed by the Council of Europe, the Commission also analyzed systems of liability in Sweden and France. *Id.* § 3.2.2.

54. Turner T. Smith, Jr. & Roszell D. Hunter, *The European Community Environmental Legal System*, 22 ENVTL. L. REP. (Envtl. L. Inst.) 10,106 (Feb. 1993) [hereinafter Smith & Hunter, *Legal System*].

55. Council Directive on Civil Liability for Damage Caused by Waste, 1991 O.J. (C 192) 6 [hereinafter Waste Directive].

56. Waste Directive, arts. 3, 5; Turner T. Smith, Jr. & Roszell D. Hunter, *The Revised European Civil Liability for Damage from Waste Proposal*, 21 ENVTL. L. REP. (Envtl. L. Inst.) 10,719 (1991) [hereinafter Smith & Hunter, *Waste Proposal*]. The Waste Directive raises liability problems similar to those faced in the United States under CERCLA. Smith & Hunter, *Legal System*, *supra* note 54, at 10,134; Mounteer, *supra* note 31, at 127-28 (discussing lender liability under the Waste Directive).

57. *Environment, supra* note 4. If the producer could not be traced, the holder of waste would be held liable. *Id.*

58. *EC Banks Look Down a 'Bottomless Pit' of Environmental Liability as Rule Nears; Open-Ended Liability and European Banks*, INT'L BANK ACCT., May 11, 1992, at 3 [hereinafter *Bottomless Pit*]. Under the Waste Directive, lenders will be held liable for the environmental damage of their borrowers. *Id.* Hilary Thompson, head of the environmental management unit at Britain's National Westminster Bank, notes that the Waste Directive does not limit the liability exposure faced by lenders. *Id.*

Under the Waste Directive, liability is assigned on the basis of whether or not a person had actual control of the waste at the time of incident.[59] The Waste Directive failed to define "actual control," but some commentators have suggested that actual control may encompass the "ability" to control.[60] This expansive interpretation of actual control draws frightening parallels to the infamous *Fleet Factors*[61] decision which equated the ability to influence hazardous waste decisions with participation in management.[62] The dangerous resemblance that the Waste Directive bears to *Fleet Factors*, the epitome of lender liability in the United States, alerts the transnational practitioner to examine carefully lender liability in the United States.

The Council of Europe's Convention, the Waste Directive, and the Green Paper are additions to the expanding arena of environmental legislation in Europe.[63] These proposals will likely foreshadow the inevitable adoption of civil liability legislation in the EU.[64] All of the proposals embrace strict liability, which is not unfamiliar to U.S. financial institutions operating under the strict, joint and several liability system of CERCLA.[65] Therefore, the U.S. experience will provide valuable insight to EU lenders in assessing and minimizing environmental lender liability.

III. Recent Trends in U.S. Environmental Law

A. *CERCLA*

In response to increasing environmental and health hazards posed by hazardous substances and dump sites,[66] the U.S. Congress enacted CERCLA in

59. *Id.* (discussing the Waste Directive); Smith & Hunter, *Waste Proposal, supra* note 56, at 10,718 (discussing the Waste Directive).

60. Mounteer, *supra* note 31, at 127-28; Smith & Hunter, *Waste Proposal, supra* note 56, at 10,718.

61. *See infra* notes 79-98 and accompanying text.

62. "[A] secured creditor will be liable if its involvement with the management of the facility is sufficiently broad to support the inference that it could affect hazardous waste disposal decision if it so chose." United States v. Fleet Factors Corp. 901 F.2d 1550, 1558 (11th Cir. 1990). *See infra* notes 79-98 and accompanying text (examining *United States v. Fleet Factors Corp.*).

63. Green Paper, *supra* note 3, § 3.2.2 & annex; *1713RD Council Meeting Environment—Brussels, 2 and 3 December 1993 President: Mrs. Magda De Galan, Minister for the Environment in the Kingdom of Belgium*, RAPID, Dec. 8, 1993, available in LEXIS, News-Library, RAPID File (recognizing that the Green Paper is part of a series of measures concerning environmental civil liability); *EC—EC Environmental Liability Legislation, supra* note 2; Smith & Hunter, *Waste Proposal, supra* note 56, at 10,718.

64. *EC—EC Environmental Liability Legislation, supra* note 2.

65. *Id. See supra* notes 40-53 and accompanying text (discussing the Council's Convention); notes 54-62 and accompanying text (discussing the Waste Directive); *infra* notes 163-79 (discussing the Green Paper).

66. S. Rep. No. 848, 96th Cong., 2d Sess. 2 (1980); United States v. Maryland Bank & Trust Co., 632 F. Supp. 573, 576 (1986); Patricia L. Quentel, Comment, *The Liability of Financial Institutions for Hazardous Waste Cleanup Costs Under CERCLA*, 1988 WIS. L. REV. 139 [hereinafter Quentel, *Cleanup Costs*].

1980.[67] CERCLA imposes strict, joint and several liability[68] upon four categories of entities: (1) present owners and operators of hazardous waste sites, (2) owners or operators of a facility at the time of hazardous waste disposal, (3) persons or entities that arranged for the disposal or treatment of hazardous substances at the facility, and (4) persons or entities that transported the hazardous waste to the affected facility.[69] CERCLA aspires to hold those responsible for the creation of hazardous waste also responsible for its cleanup.[70] CERCLA empowers the President of the United States to take necessary action to "remove or arrange for the removal" of hazardous substances.[71] By executive order, the President delegated that power to the EPA.[72] The EPA identifies and remedies hazardous waste sites with federal monies earmarked for cleanup, commonly known as the Superfund.[73] Subsequent to cleanup, the EPA may seek to

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67. Pub. L. No. 96-510, 94 Stat. 2767 (1980), *amended by* Superfund Amendments and Reauthorization Act of 1986 (SARA), Pub. L. No. 99-499, 100 Stat. 1613 (codified at 42 U.S.C. §§ 9601-75 (1994)).

68. *See* City of Philadelphia v. Stepan Chem. Co., 544 F. Supp. 1135, 1140-41 (E.D. Pa. 1982) (holding that legislative history clearly established a strict liability standard under CERCLA); Theodore C. Taub, *Pre-Transaction and Transactional Issues Involving Hazardous Materials/Waste*, ABA-ALI COURSE OF STUDY: LAND USE INSTITUTE 251, 253 (1993) (noting that owners and operators are strictly and jointly and severally liable for the cost of cleanup under CERCLA).

69. 42 U.S.C. § 9607(a) (1994). Persons covered by CERCLA include:

(1) [T]he owner and operator of a vessel or a facility,

(2) any person who at the time of disposal of any hazardous substance owned or operated any facility at which such hazardous substances were disposed of,

(3) any person who by contract, agreement, or otherwise arranged for disposal or treatment, or arranged with a transporter for transport for disposal or treatment, of hazardous substances owned or possessed by such person, by any other party or entity, at any facility or incineration vessel owned or operated by another party or entity and containing such hazardous substances, and

(4) any person who accepts or accepted any hazardous substances for transport to disposal or treatment facilities, incineration vessels or sites selected by such person, from which there is a release, or a threatened release which causes the incurrence of response costs, of a hazardous substance . . . .

Id.

70. *See* United States v. Fleet Factors Corp., 821 F. Supp. 707, 722 (S.D. Ga. 1993) [hereinafter *Fleet Factors II*] (stating that "one of CERCLA's central tenets is to make the polluter pay"); United States v. Fleet Factors Corp., 901 F.2d at 1553 (11th Cir. 1990). "The essential policy underlying CERCLA is to place the ultimate responsibility for cleaning up hazardous waste on 'those responsible for problems caused by the disposal of chemical poison.'" *Id.* (citing Florida Power & Light Co. v. Allis Chalmers Corp., 893 F.2d 1313, 1316 (11th Cir. 1990)). *See also* Green Paper, *supra* note 4, § 1.0 (providing that "a person should rectify damage that he causes"); EEC Treaty, *supra* note 24, art. 130r (providing that the "polluter should pay").

71. 42 U.S.C. § 9604 (1994).

72. Executive Order No. 12,316, 3 C.F.R. 168 (1982); United States v. Maryland Bank & Trust Co., 632 F. Supp. 573, 576 (D. Md. 1986).

73. 26 U.S.C. § 9507 (1993) (establishing Hazardous Substance Superfund); 42 U.S.C. § 9611(a) (1994) (defining the uses of fund). The Hazardous Response Trust Fund is a body of funds which may be tapped by the EPA to be used for the cleanup of environmentally damaged property. *Id.* § 9611 (1994) (listing the activities which may financed); Comment, *Cleaning Up the Debris After Fleet Factors: Lender Liability and CERCLA's Security Interest Exemption*, 104 HARV. L. REV. 1249, 1251 (1991) [hereinafter *Cleaning Up the Debris*] (describing the process of reimbursement of Superfund). "Superfund" is used to refer to the entire act as well as to refer to the Hazardous Substance Superfund.

reimburse the Superfund account by bringing suit against potentially liable parties.[74]

Lending institutions have fallen prey to CERCLA legislation, despite the fact that CERCLA contains a security interest exemption.[75] Courts have found lenders liable for cleanup costs under CERCLA in two instances: (1) when contaminated property has been foreclosed upon,[76] and (2) when lenders become involved in the management operations of a liable facility.[77] Consequently in 1991, the Court of Appeals for the Eleventh Circuit in the *United States v. Fleet Factors Corp.* adopted an expansive standard of liability.[78]

B. United States v. Fleet Factors Corp.

In *United States v. Fleet Factors Corp.*,[79] the U.S. government sued the shareholders of a cloth printing facility, Swainsboro Print Works (SPW), and its creditor, Fleet Factors Corp. (FFC) to recover hazardous waste cleanup costs.[80]

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74. 42 U.S.C. § 9607(a) (1994); *Cleaning Up the Debris*, *supra* note 73, at 1251. The Green Paper notes the existence of the U.S. Superfund as an example of a joint compensation system. Green Paper, *supra* note 73, § 3.2.2.

75. 42 U.S.C. § 9601(20)(A) (1994).

> The 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.

Id. Banks in the EU fear environmental liability in the absence of a secured creditor exemption. *Lender Liability*, WORLD INS. REP., Mar. 13, 1992. The transnational practitioner would be wise to be aware of potential environmental liability even in the presence of a secured creditor exemption. *See* United States v. Fleet Factors Corp., 901 F.2d 1550 (11th Cir. 1990) (indicating that lenders will be liable where the lender has the capacity to influence hazardous waste decisions); Guidice v. BFG Electroplating & Mfg., 732 F. Supp. 556 (W.D. Pa. 1989) (holding that the secured creditor exemption does not survive foreclosure); United States v. Maryland Bank & Trust Co., 632 F. Supp. 573 (D. Md. 1986) (finding that the security interest exemption unavailable when a lender foreclosed on contaminated property); *infra* notes 189-225 and accompanying text (discussing preventive measures for lenders). *But see In re* Bergsoe Metal Corp., 910 F.2d 668 (9th Cir. 1990) (holding that a security interest exemption applies until actual participation in the management of the facility); United States v. Mirabile, [1985] 15 ENVTL. L. REP. (Envtl. L. Inst.) 20,994, 20,996 (E.D. Pa. 1985) (holding that foreclosing lenders become liable only if they exercise control over the day-to-day operations of a site); *In re* T.P. Long Chem., 45 B.R. 278, 288-89 (Bankr. N.D. Ohio 1985) (finding that participation in management of facility was necessary to forfeit the security interest exemption). The Eleventh Circuit rejected the formulation in *United States v. Mirabile. Fleet Factors*, 901 F.2d at 1558. "We, therefore, specifically reject the formulation of the secured creditor exemption suggested by the District Court in *Mirabile*." *Id.*

76. *See* United States v. Maryland Bank and Trust Co., 632 F. Supp. 573 (D. Md. 1986). In *Maryland Bank*, the court ultimately held that a mortgagee who purchased at a foreclosure sale is not entitled to the security interest exemption because the mortgagee purchased at the foreclosure sale, not to protect the security interest, but rather to protect the investment. *Id.* at 579.

77. *Fleet Factors*, 901 F.2d at 1557. "It is not necessary for the secured creditor to involve itself in the day-to-day operations . . . in order to be liable." *Id.*

78. *Id.* at 1558 (holding that a secured creditor's involvement need only support the inference that the creditor could involve itself in waste decisions); Taub, *supra* note 68, at 268 (noting that the court created a "radically expansive standard").

79. *Fleet Factors*, 901 F.2d at 1550.

80. *Id.* at 1553.

FFC loaned money to SPW in return for an assignment of accounts receivable and taking a security interest in the textile facility, its equipment, inventory, and fixtures.[81] Five years later SPW declared bankruptcy and FFC foreclosed on its security interest in SPW's inventory and equipment.[82] A liquidating company sold most of the collateral on behalf of FFC; FFC contracted with another party to remove the remaining equipment.[83]

Subsequent to the liquidation, the EPA discovered 700 drums of toxic waste and a large amount of asbestos on the property.[84] The EPA removed and disposed of the hazardous waste at a cost of $400,000.[85] The cleanup cost became the crux of the litigation.[86] The EPA sued to recover the cleanup expenditures from FFC alleging that FFC was liable either as a present owner or as an owner during the release or threatened release of hazardous waste.[87]

The Eleventh Circuit held that FFC was not liable as a present owner or operator.[88] However, the government also sought to recover under the past owner provision in CERCLA.[89] In response to this charge, FFC sought protection from liability under the security interest exemption, which exempts from liability those owners holding an ownership interest in order to protect a security interest.[90] The court conceded that FFC held the indicia of ownership merely as a security interest, but the court still examined the extent of FFC's liability as a participant in the management of the facility.[91] The court fashioned a new rule which declares secured creditors liable when "involvement with the management of the facility is sufficiently broad to support the inference that it could affect hazardous waste disposal decisions if it so chose."[92]

As a result of this new test, the *Fleet Factors* decision prompted an uproar in the lending community and later prompted the EPA to develop regulations

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81. *Id.* at 1552.
82. *Id.*
83. *Id.* at 1553.
84. *Fleet Factors*, 901 F.2d at 1553.
85. *Id.*
86. *Id.*
87. *Id.* at 1552.
88. *Id.* at 1555. *See supra* note 69 (setting forth the text of 42 U.S.C. § 9607(a)).
89. *Fleet Factors*, 901 F.2d at 1554. *See supra* note 69 (setting forth the text of 42 U.S.C. § 9607(a)(2)). Liable parties include "any person who at the time of disposal of any hazardous substance owned or operated any facility at which such hazardous substances were disposed." *Id.*
90. *Fleet Factors*, 901 F.2d at 1556. *See supra* note 75 (setting forth the text of the security interest exemption).
91. *Fleet Factors*, 901 F.2d at 1556.
92. *Id.* at 1558. *See* Greenberg & Shaw, *supra* note 17, at 1212 (stating that after the *Fleet Factors* decision, lenders in the position to control borrower's hazardous waste decisions may be liable even without exercising control); Michael B. Kupin, *New Alternations of the Lender Liability Landscape: CERCLA After the Fleet Factors Decision*, 19 REAL EST. L. J. 191, 207 (1991) (stating that the standard is whether or not the lender has "capacity to influence" hazardous waste treatment activities); *Cleaning Up the Debris*, *supra* note 73, at 1257 (1991) (stating that after *Fleet Factors* decision, a lender will be liable if its involvement suggests that it could influence hazardous waste disposal decisions).

explaining the security interest exemption in an effort to protect the interests of financial institutions.[93] Today, lending institutions in the United States confront genuine prospects of environmental liability.[94] Moreover their European colleagues fear similar exposure with the advent of the Green Paper.[95] When drafting the Green Paper, the Commission recognized the existence of problems under CERCLA and acknowledged the need to appreciate the effects of environmental civil liability on financial institutions.[96] Since the EPA regulations have been effective in curbing environmental lender liability in the United States,[97] EU law makers should review and utilize the security interest exemption, as clarified by the EPA, in order to protect lenders from the perils of liability experienced under CERCLA.[98]

C. Examining the EPA Regulations

Following the decision announced in *Fleet Factors*,[99] the EPA responded to growing resentment among financial institutions by promulgating a rule explaining the security interest exemption under CERCLA.[100] In April 1992, the EPA issued its explanation and supplementary report.[101] The EPA clarified the security interest exemption by defining CERCLA terminology and identifying actions by lenders that constitute management participation sufficient to render liability.[102] The rule defines the meaning of the phrases "indicia of ownership," "primarily to protect a security interest," and "participating in the management of

93. Brent Nicholson & Todd Zuiderhoek, *The Lender Liability Dilemma: Fleet Factors History & Aftermath*, 38 S.D. L. REV. 22, 38 (1993) (noting that lenders and federal agencies, such as the FDIC and the Resolution Trust Corp., became concerned with lender liability).

94. *Id.* at 38-39. In addition to environmental liability, lenders also risk the loss of the security because contamination will render the property valueless. *Id.*

95. *Lender Liability and How It Effects [sic] Customers' Credit Rating*, BUS. INT'L MONEY REP., July 5, 1993 (noting that banks are focusing attention on lender liability).

96. Green Paper, *supra* note 3, §§ 3.2.2, 4.1.2, annex II (recognizing that credit institutions have become liable upon taking possession of land).

97. Kelley v. Tiscornia, 810 F. Supp. 901, 905 (W.D. Mich. 1993); Ashland Oil, Inc. v. Sonford Products Corp., 810 F. Supp. 1057, 1060 (D. Minn. 1993). *See* Lavalette, *supra* note 17, at 508 (commenting that the EPA rule offers guidance for lenders); *infra* notes 137-58 and accompanying text (discussing the favorable judicial reception to the EPA regulations).

98. *CIC Reviews Lending Liability Policy*, HAZNEWS, Dec. 1992. The French banking group, *Union Europeenne de CIC*, has examined the EPA rule and believes that the EU will follow the U.S. civil liability legislation model. *Id.*

99. United States v. Fleet Factors Corp., 901 F.2d 1550 (11th Cir. 1990).

100. 57 Fed. Reg. 18,344, 18,344-45 (1992) (The EPA rule "clarif[ies] and specif[ies] the range of activities which may be undertaken"). The EPA regulations provide "guidance by synthesizing earlier case law and providing a framework within which the Exemption's coverage may be analyzed." *Fleet Factors II*, 821 F. Supp. 707, 711 (1993); Lavalette, *supra* note 17, at 487 (1993) (stating that the EPA rule sought to identify permissible activities). *See supra* note 75 (setting forth text of the security interest exemption).

101. 57 Fed. Reg. 18,344, 18,348 (1992). *See* Lavalette, *supra* note 17, at 487-92 (1993) (reviewing the introduction of the EPA rule).

102. 40 C.F.R. § 300.1100(c) (1992).

a vessel or facility" and specifies activities permissible upon and after foreclosure.[103] The following sections discuss each of the principle phrases and permissible lender activities as clarified by the EPA rule.

1. Indicia of Ownership

"Indicia of ownership"[104] requires evidence of a security interest, interest in a security interest, or an interest in realty or personalty securing a loan or other obligation.[105] The rule permits the acquisition of legal or equitable title in property incident to foreclosure or its equivalents to qualify as a security interest.[106] Many of those commenting on the EPA proposal supported the preservation of the exemption upon foreclosure because at the point of foreclosure lenders have exhausted all other options available to manage incurable default.[107] The regulations also emphasize that a person does not have to hold title

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103. 40 C.F.R. § 300.1100 (1992). Recall the security interest exemption: "Owner and 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." 42 U.S.C. § 9601(20) (1994). *See supra* note 75 (setting forth text of the security interest exemption). The D.C. Circuit Court of Appeals invalidated the EPA rule because the court determined that the Congress had not delegated the statutory authority to the EPA to promulgate a clarification to the security interest exemption. Kelley v. EPA, No. 92-1312, 1994 WESTLAW 27,881 (D.C. Cir., Feb. 4, 1994). Nevertheless, the invalidation of the rule does not affect its usefulness as a model for drafting environmental legislation in the EU. *See supra* notes 99-162 and accompanying text (discussing the EPA rule). Prior to its invalidation, the EPA rule had successfully safeguarded lenders from environmental liability in the United States. *See supra* notes 150-62 (examining the benefits of the EPA rule). Consequently, lenders were better equipped to anticipate potential liability concerns than under previous conflicting case law. *Id*; *supra* note 75 (recognizing conflicting interpretations of the security interest exemption). The EPA's intrusion on congressional legislative duties should not reflect unfavorably upon the merit of the rule as a prototype for EU lawmakers; its usefulness has not been diminished. *See supra* notes 99-103 and accompanying text; *infra* notes 104-62 and accompanying text (discussing the EPA rule).

104. 42 U.S.C. § 9601(20)(A) (1994); *see supra* note 73 (setting forth the text of security interest exemption).

105. 40 C.F.R. § 300.1100(a) (1992).

> Evidence of such interest include, but are not limited to, . . . deeds of trust, liens, surety bonds and guarantees of obligations, title held pursuant to a lease financing transaction in which the lessor does not select initially the leased property, . . . legal or equitable title obtained pursuant to foreclosure, and their equivalents, . . . assignments, pledges, or other rights to or other forms of encumbrance against property that are held primarily to protect a security interest. A person is not required to hold title or a security interest in order to maintain indicia of ownership.

Id.

106. *Id.*; 57 Fed. Reg. 18,344, 18,347 (1992). *See supra* note 105 (setting forth the text of regulation); *infra* notes 129-32 and accompanying text (discussing foreclosure and postforeclosure activities). The EPA believed that including foreclosing holders within the security interest exemption would prevent the shutdown of an otherwise viable business and the termination of its employees. 57 Fed. Reg. 18,344, 18,347 (1992).

107. 57 Fed. Reg. 18,344, 18361 (1992). The EPA found support for this interpretation in United States v. Maryland Bank & Trust, Inc. *Id.* (citing United States v. Maryland Bank & Trust, Inc., 632 F. Supp. 573, 579 (D. Md. 1986)). In that case, the court held that the security interest exemption does not apply "to former mortgagees currently holding title after purchasing the property at a foreclosure sale, at least when, as here, the former mortgagee has held title for nearly four years." United States v. Maryland Bank & Trust, Co., 632 F. Supp. 573, 579 (D. Md. 1986). The EPA believed that the preservation of the exemption for foreclosing lenders

in order to maintain indicia of ownership.[108] Finally, the EPA rejected the premise that the exemption should only apply to title theory jurisdictions and announced that the purpose of the exemption was to treat holders in all jurisdictions similarly.[109]

2. *Primarily to Protect a Security Interest*

The EPA rule also defines the phrase "primarily as a security interest" to denote an interest created or established in a vessel or facility for the purpose of securing a loan or other obligation.[110] The subdivision contains a nonexhaustive list of transactions traditionally recognized as giving rise to a security interest.[111] The rule does not protect, however, interests held primarily for investment purposes or purposes other than security protection.[112] Nevertheless, protection will be granted so long as the primary reason is the protection of a security interest.[113]

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was consistent because the case did not preclude the application of the exemption; rather, the facts did not warrant the preservation in that case. 57 Fed. Reg. 18,344, 18,360-62 (1992).

108. 40 C.F.R. § 300.1100(a) (1992). *See supra* note 105 (setting forth the text of § 300.1100(a)). One commentator describes this as a deviation from the original meaning under CERCLA, which carved out the security interest exemption to protect mortgagees in title theory jurisdictions. Lavalette, *supra* note 17, at 479. The security interest exemption was introduced to protect from liability titleholders who have not participated in management. *Id.*

109. 57 Fed. Reg. 18,344, 18,351 (1992). Thus, the EPA's interpretation applies equally in both title theory and lien theory jurisdictions, even though the mortgagee does not hold title in a lien theory jurisdiction. *Id.* In a title theory jurisdiction, the mortgagee holds legal title in the security until the mortgage obligation has been satisfied or discharged; whereas in a lien theory jurisdiction, the mortgagor does not hold legal title, but merely holds a security interest and the mortgagor is recognized as the owner of the property until foreclosure. GRANT S. NELSON & DALE H. WHITMAN, REAL ESTATE FINANCE LAW §§ 4.1-4.2 (2nd ed. 1985). *See generally id.* (reviewing the lien and title theories).

110. 40 C.F.R. § 300.1100(b) (1992).

111. *Id.* § 300.1100(b)(1) (1992); 57 Fed. Reg. 18,344, 18,351-52 (1992). Under the EPA rule, mortgages, deeds of trusts, liens, title pursuant to lease financing transactions are security interests. *Id.* The EPA disagreed that lease financing agreements should not be included in the list of transactions creating a security interest; that type of financing arrangement is maintained to secure a loan or other obligation. 57 Fed. Reg. 18,344, 18,352 (1992). Sale and leasebacks, conditional sales, installment sales, trust receipt transactions, certain assignments, factoring agreements, accounts receivable financing arrangements, and consignments which create or establish an interest in the vessel of facility to secure an interest or other obligation also constitute a security interest. 40 C.F.R. § 300.1100(b)(1) (1992).

112. 40 C.F.R. § 300.1100(b)(2) (1992). The motivations of a lender are relevant only to determine whether the indicia of ownership is held primarily for security purposes. *Id. But see* Greenberg & Shaw, *supra* note 17, at 1241 (criticizing the intent test because lending itself is a form of investment).

113. 40 C.F.R. § 300.1100(b)(2) (1992); Lavalette, *supra* note 17, at 488-89 (discussing primarily the protection of a security interest). The rule does not permit nonsecured creditors to claim the security interest exemption. 57 Fed. Reg. 18,344, 18,352 (1992).

3. Participating in the Management of a Vessel or Facility

The EPA rule extensively discusses activities which constitute participation in management.[114] Participation in management refers to actual participation in the management or operational affairs of the vessel or facility by the holder.[115] The EPA developed a two-prong test to determine activities that constitute participation in management by the holder while the debtor is still in possession of the property.[116] The test inquires into the management and decision-making control of the holder. If the holder meets either prong, that holder's actions constitute participation in management.[117]

Under the first prong, the actions constitute participation in management if the holder "exercises decision-making control over the [debtor's] environmental compliance, such that the holder has undertaken a responsibility for the [debtor's] hazardous substance handling or disposal practices."[118] Under the second prong, a holder's action constitutes participation in the management if the holder exercises management level control of the daily decisions with respect to

114. 40 C.F.R. § 300.1100(c)(1) (1992). This section states:

> Participation in the managements of a facility means . . . actual participation in the management or operational affairs of the vessel or facility by the holder, and does not include the mere capacity to influence, or ability to influence, or the unexercised right to control facility operations. A holder is participating in management, while the borrower is still in possession of the vessel or facility encumbered by the security interest, only if the holder either:
> (i) Exercises decision-making control over the borrower's environmental compliance, such that the holder has undertaken responsibility for the borrower's hazardous substance handling or disposal practices; or
> (ii) Exercises control at a level comparable to that of a manager of the borrower's enterprise, such that the holder has assumed or manifested responsibility for the overall management of the enterprise encompassing the day-to-day decision making of the enterprise with the respect to:
> (A) Environmental compliance or
> (B) All, or substantially all, of the operational (as opposed to financial or administrative) aspects of the enterprise other than environmental compliance. Operation aspects of the enterprise include functions such as that of facility or plant manager, operations manager, chief operating officer, or chief executive officer.
>
> Financial or administrative aspects include functions such as that of credit manager, accounts payable/receivable manager, personnel manager, controller, chief financial officer, or similar functions.

Id.

115. *Id. Cf. supra* notes 79-98 and accompanying text (reviewing *United States v. Fleet Factors Corp.*).

116. 40 C.F.R. §§ 300.1100(c)(1)(i)-(ii) (1992). *See* Lavalette, *supra* note 17, at 489-92 (discussing the EPA's two-prong test for determining participation in management).

117. 40 C.F.R. § 300.1100(c)(1) (1992). *See* Lavalette, *supra* note 17, at 489-92 (discussing the EPA's two-prong test for determining participation in management).

118. 40 C.F.R. § 300.1100(c)(1)(i) (1992). Regardless of whether the holder actually caused the waste release or threatened release, the lender may have exercised management control sufficient to render liability. 57 Fed. Reg. 18,344, 18,355, 18,359 (1992); Patricia L. Quentel, *EPA Issues Long-Awaited Lender Liability Rule*, 22 ENVTL. L. REP. (Envtl. L. Inst.) 10,640 (Oct. 1992) [hereinafter Quentel, *Long-Awaited Rule*].

environmental compliance[119] or substantially all of the operational aspects other than environmental compliance.[120] In order to prevent financial institutions from insulating themselves from liability, the EPA included the latter provision to prevent lenders from assuming control over a substantial portion of a vessel's or facility's operation and then claiming the security interest exemption.[121] Thus, financial institutions exerting substantial operational control will be adjudged participants in management even though the control does not extend to environmental compliance.[122]

In addition to expounding a test for management participation, the EPA also incorporated an explanation of activities which do not comprise management participation.[123] During loan negotiations, the rule permits prospective lenders to require environmental inspections or to order cleanup without incurring liability for participating in the management of the facility.[124] Lenders are also entitled to police and engage in workout activities with their borrowers.[125] Permissible policing activities include: requiring the borrower to cleanup the facility or comply with environmental laws, inspecting the facility, monitoring the debtor's financial condition, and requiring borrower compliance with the loan terms.[126] The EPA recognized that troubled loans may necessitate increased lender participation to avert debtor default, and consequently outlined acceptable workout activities.[127] Permissible workout procedures include: restructuring or renegotiating the terms, elevating the rent or interest, exercising forbearance, assigning accounts, and providing financial advice and guidance.[128]

119. 40 C.F.R. § 300.1100(c)(1)(ii)(A) (1992). *See supra* note 114 (setting forth the text of § 300.1100(c)(1)).

120. 40 C.F.R. § 300.1100(c)(1)(ii)(B) (1992). *See supra* note 114 (setting forth the text of § 300.1100(c)(1)). A lender will not be deemed to have participated in management if control exists over the financial or administrative aspects of the enterprise. 57 Fed. Reg. 18,344, 18,360 (1992). Thus, a lender can safely participate as credit manager, chief financial officer, personnel manager, or other financial or administrative activities. *Id.*

121. 57 Fed. Reg. 18,344, 18,360 (1992). *See* Lavalette, *supra* note 17, at 490 (discussing the restriction on carving out environmental control to prevent liability).

122. 40 C.F.R. § 300.1100(c)(1)(ii)(b) (1992); 57 Fed. Reg. 18,344, 18,360 (1992).

123. 40 C.F.R. § 300.1100(c)(2) (1992).

124. *Id.* § 300.1100(c)(2)(i) (1992); 57 Fed. Reg. 18,344, 18,353-54 (1992). *See infra* notes 192-228 and accompanying text (reviewing practical guidelines to avoid environmental lender liability).

125. 40 C.F.R. § 300.1100(c)(2)(ii) (1992); 57 Fed. Reg. 18,344, 18,356-57 (1992). *See infra* notes 192-228 and accompanying text (reviewing practical guidelines to avoid environmental lender liability).

126. 40 C.F.R. § 300.1100(c)(2)(ii)(A) (1992). The list provided by the EPA was not intended to be exhaustive; activities not listed are subject to analysis under the two-prong test for participation in management. 57 Fed. Reg. 18,344, 18,375 (1992).

127. 57 Fed. Reg. 18,344, 18,356-57 (1992).

128. 40 C.F.R. § 300.1100(c)(2)(ii)(B) (1992); 57 Fed. Reg. 18,344, 18,356-57 (1992). *See* 42 U.S.C. § 9607(d)(1) (1994) (providing that a person shall not be liable for activities in accordance with the National Contingency Plan or at the direction of the on-site coordinator).

4. *Foreclosure and Postforeclosure Activities*

The EPA rule also examines foreclosure and postforeclosure activities which may be conducted pursuant to the security interest exemption.[129] A holder will continue to maintain indicia of ownership primarily for protection of its security interest after foreclosure if the holder undertakes to sell, release, or otherwise divest itself of ownership of the contaminated property in a reasonably expeditious and commercially reasonable manner.[130] The holder may further engage in activities related to the sale and release of the property entailing liquidation, protection or preservation of assets, maintenance of business activities, and wrap up operations.[131] Further, in order to maintain the status of a security interest holder, the holder must list or advertise the property within the year following foreclosure and must refrain from outbidding, rejecting, or forgoing any offer of fair consideration for the property.[132]

The EPA regulations enable lenders to engage in activities related to borrower behavior and management of the security with reasonable assurance that they will not be held liable as owners or operators participating in the management of a vessel or facility.[133] Instead of forgoing foreclosure and workout options, several cases have indicated that a lender may safely maneuver around the pitfalls of liability existing prior to the promulgation of the EPA rule and subsequent to the

129. 40 C.F.R. § 300.1100(d) (1992). *See* Quentel, *Long-Awaited Rule*, *supra* note 118, at 10,641 (discussing permissible foreclosure and postforeclosure activities pursuant to the EPA rule).

130. 40 C.F.R. § 300.1100(d)(1) (1992). A holder will lose its status as maintaining indicia of ownership primarily to protect a security interest if the holder outbids, rejects, or fails to act upon a written, bona fide, firm offer of fair consideration. *Id.* The EPA interpreted the security interest exemption to protect holders when foreclosure is undertaken to recover the security. 57 Fed. Reg. 18,344, 18,347 (1992). The crucial issue is whether the lender's behavior indicates an active desire to recover the obligation by making reasonable efforts to sell or otherwise divest itself of ownership of the contaminated property. *Id.*

131. 40 C.F.R. § 300.1100(d)(2) (1992). However, lenders need to limit their postforeclosure activities. Following the promulgation of the EPA rule, the action in *United States v. Fleet Factors Corp.* was reactivated. *Fleet Factors II*, 821 F. Supp. 707, 712 (S.D. Ga. 1993). Relying on the EPA's recently promulgated rule, a Georgia federal district court found that Fleet Factors Corp. (FFC) had lost its security interest exemption as a result of postforeclosure activities. *Id.* at 720. The liquidating company, hired by FFC to sell the secured collateral subsequent to foreclosure, exceeded the level of contact permissible under 40 C.F.R. § 300.1100(d)(2) when it handled environmental waste which was readily identifiable and apparent and present in significant quantities. *Id.* at 719-20. FFC was also held liable for the activities of the contracted cleanup crew, which haphazardly handled hazardous substances aggravating the environmental threat and likewise failed to complete salvage operations in a reasonable amount of time. *Id.* at 720.

132. 40 C.F.R. §§ 300.1100(d)(2)(i)-(ii) (1992). The property must be listed with a broker, dealer, or other agent dealing with the particular type of property or advertised in a newspaper with a general circulation of over 10,000 or other acceptable trade or real estate publication. *Id.* § 300.1100(d)(2)(i) (1992). Unless required by law to make or obtain a higher bid, the holder may not outbid or reject fair offers. *Id.* § 300.1100(d)(2)(ii) (1992).

133. Lavalette, *supra* note 17, at 508.

decision in *Fleet Factors*.[134] Neither this comment nor the EPA regulations suggest that lenders have absolute insulation from environmental liability. The EPA regulations, while quite generous, do not permit financial institutions to freely involve themselves in the debtor-polluter's waste decisions.[135] Nor do the EPA regulations permit lenders, while participating in substantially all of the debtor-polluter's operational activities, to carve out their own exemption by exclusively removing their ability to exercise discretion over waste decisions.[136]

D. Judicial Reception to the EPA Rule

Judicial reception to the EPA rule has been promising. Since its promulgation, the EPA rule has been noted in at least four cases.[137] In January 1993, two federal district courts ruled that lenders were shielded from liability by the security interest exemption as explained by the EPA rule.[138] Likewise, two federal appellate courts have acknowledged the protection afforded by the EPA rule.[139] These cases foreshadow the favorable auspices of avoiding environmental liability.

In *Ashland Oil, Inc. v. Sonford Products Corp.*, a U.S. district court in Minnesota held that the security interest exemption embodied in CERCLA, as

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134. *See* Ashland Oil, Inc. v. Sonford Prods. Corp., 810 F. Supp. 1057, 1060 (D. Minn. 1993) (finding that the lender's activities were within the safe harbor provision of the EPA rule); Kelley v. Tiscornia, 810 F. Supp. 901, 909 (W.D. Mich. 1993) (finding that the lender's activities did not relate to the operational aspects of the enterprise necessary for a finding of liability under the EPA rule). U.S. court decisions have found in favor of lenders without relying on the rule, despite the fact that the legality of the EPA regulations had been challenged. United States v. McLamb, 5 F.3d 69, 71 (4th Cir. 1993); Waterville Indus. Inc. v. Finance Auth. of Maine, 984 F.2d 549, 553 (1st Cir. 1993). *See supra* note 103 (noting that subsequent to the decisions in *McLamb* and *Waterville Indus.*, the EPA rule was invalidated). These courts seem less willing to fuel the blaze of liability by sacrificing deep pocket lenders. *See infra* notes 137-58 and accompanying text (discussing judicial reception to the EPA rule).

135. *See* 40 C.F.R. § 300.1100(c)(1)(i) (1992) (limiting decision-making control by lenders); *supra* notes 114-28 and accompanying text (discussing the permissible lender activities under the EPA rule).

136. *See* 40 C.F.R. § 300.1100(c)(1)(ii) (1992) (limiting management-level control by lenders); *supra* notes 114-28 and accompanying text (discussing the permissible lender activities under the EPA rule).

137. *McLamb*, 5 F.3d at 73; *Waterville*, 984 F.2d at 553; *Fleet Factors Corp.* 821 F. Supp. at 713; *Ashland*, 810 F. Supp. at 1059; *Kelley*, 810 F. Supp. at 905. *See supra* note 103 (noting that the EPA rule has been invalidated by the D.C. Circuit Court of Appeals).

138. *Ashland*, 810 F. Supp. at 1060; *Kelley*, 810 F. Supp. at 909 (relying on the EPA regulations, the court granted summary judgment finding that the bank fell within the security interest exemption under CERCLA). The bank's involvement in the activities of the enterprise were permitted under the EPA regulations. *Kelley*, 810 F. Supp. at 901. *See* 40 C.F.R. § 300.1100(c)(1)(ii)(B) (1992) (limiting permissible lender activities). Actions included in participation of management include exercise of management level control with respect to all, or substantially all, of the operational aspects of the enterprise other than environmental compliance. *Id.* On a motion for summary judgment, the *Ashland* court held that a lender fell within CERCLA's security interest exemption and was not liable for cleanup costs. *Ashland*, 810 F. Supp. at 1057. The lender's activities associated with the property did not constitute actual participation. *Id.* The court also concluded that the EPA regulations were consistent with CERCLA and thus entitled to deference. *Id.*

139. *McLamb*, 5 F.3d at 73; *Waterville*, 984 F.2d at 553.

interpreted by the EPA rule, safeguarded a lender who briefly took title to the assets of an alleged polluter.[140] In that case, a property owner sued its tenant's lender to recover cleanup costs resulting from the tenant's use of the premises for manufacturing wood preservatives.[141] Following the tenant's petition for bankruptcy, the lender foreclosed on the secured assets and briefly held title before transferring the property to a buyer.[142] The court rejected the owner's claim that the lender was liable as an owner of the property at the time hazardous waste was disposed.[143] Holding that the EPA rule applied,[144] the court concluded that the lender's fleeting ownership fell within CERCLA's security interest exemption.[145]

Immediately following *Ashland Oil*, a district court in Michigan applied the EPA interpretation of the security interest exemption and dismissed a liability claim against a lender.[146] In *Kelley v. Tiscornia*, the State of Michigan sued a lending institution to recover expenditures assessed during the cleanup of a site operated and owned by a loan customer.[147] Between 1964 and 1988, the lender made several loans to a manufacturing company.[148] The lender also retained a position on the company's board and monitored the accounts receivable and other financial activities of the corporation.[149] The court examined the bank's activities between 1964 and 1986 and between 1986 and 1988.[150]

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140. *Ashland*, 810 F. Supp. at 1060-61.

141. *Id.* at 1058-59.

142. *Id.* at 1059-60. The lender held the property for approximately four weeks. *Id.* at 1060. The buyer financed the transaction with a loan from the same lender. *Id.* When the buyer defaulted, the lender abandoned its security interest in the assets. *Id.*

143. *Id.* at 1059-60. *See* 42 U.S.C. § 9607(a)(2) (1994) (setting forth prior owner liability).

144. *Ashland*, 810 F. Supp. at 1059-60 n.4.

145. *Id.* at 1060. *See* 42 U.S.C. § 9601(20)(A) (1994) (setting forth the security interest exemption); 40 C.F.R. § 300.1100(a) (1992) (codifying the EPA's clarification of the security interest exemption); Lavalette, *supra* note 17, at 490 (noting that the district court applied the EPA rule to find that the security exemption applied). The district court relied on case law to support the conclusion that the EPA rule is consistent with the security interest exemption embodied in CERCLA. *Ashland*, 810 F. Supp. at 1060 (citing *In re* Bergsoe Metal Corp., 910 F.2d 668 (9th Cir. 1990) and United States v. Mirabile, [1985] 15 ENVTL. L. REP. (Envtl. L. Inst.) 20,992, (E.D. Pa. 1985)). *See In re* Bergsoe Metal Corp., 910 F.2d 668, 672 (9th Cir. 1990) (holding that the security interest exemption is not voided by reservation of right to protect security); United States v. Mirabile, [1985] 15 ENVTL. L. REP. (Envtl. L. Inst.) 20,992, 20,995 (E.D. Pa. 1985) (holding that foreclosure is within the security interest exemption under CERCLA).

146. Kelley v. Tiscornia, 810 F. Supp. 901 (W.D. Mich. 1993) (dismissing on summary judgment a CERCLA claim against a lender for cleanup costs).

147. *Id.* at 902.

148. *Id.* at 902-04.

149. *Id.*

150. *Id.*

The district court relied on the EPA's clarification and found that the lender was entitled to the protection of the security interest exemption.[151] The district court held that bank's participation in semiannual board meetings and other financially related monitoring activities between 1964 and 1986 did not amount to the actual decision making necessary to establish liability.[152] Furthermore, the bank's later insistence for outside management and other financial recommendations did not constitute day-to-day control of the company's operational decisions sufficient to render liability.[153]

Although not relying explicitly on the EPA rule, two federal appellate courts have also found in favor of lenders in recent lender liability cases.[154] The First Circuit found a loan guarantor was entitled to protection under the secured creditor exemption of CERCLA.[155] The court refused to permit "maturation of ownership" to divest the guarantor of its protection under CERCLA's security interest exemption, even though the loan guarantor became the record owner of the property by accepting a deed in lieu of foreclosure.[156] Similarly, the Fourth Circuit permitted a foreclosing lender to claim the protection of the security interest exemption.[157] Relying on the absence of investment or profit motivation, lack of other bidders, and prompt turn around of the property, the Fourth Circuit concluded that the lender acquired title to the property solely to protect its

151. *Kelley*, 810 F. Supp. at 909. Notably, the district court recognized the detrimental consequences of holding banks liable under CERCLA. *Id.* Banks will abstain from workout attempts in favor of accelerating loans which "virtually guarantees an increase in the country's inventory of abandoned and inactive hazardous waste disposal sites." *Id.*

152. *Id.* at 907. The board did not involve itself in the operational decisions or environmental issues of the manufacturing company; those decisions were reserved for the executive committee. *Id.* The EPA rule requires actual participation in the management by the lender, influence is not sufficient. *Id.* at 906-07. Michigan failed to demonstrate the day-to-day actual, operational control of the facility necessary for a finding of liability. *Id.* at 906-07. *See supra* note 114 (providing full text of 40 C.F.R. § 300.1100(c)(1)); Lavalette, *supra* note 17, at 506-07 (noting that the court relied on the EPA rule to interpret the secured creditor exemption).

153. *Kelley*, 810 F. Supp. at 902-04. A person exerting influence over a "facility manager but who has no power to direct or implement operational decisions is not 'participating in management,' even if the level of influence exerted over the borrower is substantial." 57 Fed. Reg. 18,344, 18,359. *See Kelley*, 810 F. Supp. at 908 (discussing the EPA rule).

154. United States v. McLamb, 5 F.3d 69 (4th Cir. 1993); Waterville Indus. Inc. v. Finance Auth. of Maine, 984 F.2d 549 (1st Cir. 1993).

155. *Waterville*, 984 F.2d at 550.

156. *Id.* at 550, 553. The guarantor, on the same day as receiving a deed in lieu of foreclosure, released the property to the defaulting tenant. *Id.* at 551. Hazardous waste was released on the property during the tenure of the second lease. *Id.* The tenant's financial difficulties persisted and the guarantor eventually sold the property within 18 months of being declared titleholder by the tenant's bankruptcy court. *Id.* The court recognized the same policy expounded in the EPA rule—protecting lenders who promptly divest themselves of ownership. *Id.* at 553; *supra* notes 129-32 (discussing foreclosure activities by lenders).

157. *McLamb*, 5 F.3d at 71. *See supra* note 75 (setting forth the text of the security interest exemption).

security interest and acted reasonably and promptly to divest itself of ownership.[158]

In the cases in which it has been tested, the EPA rule has successfully protected lenders from the overly expansive realm of liability announced in *Fleet Factors*.[159] Consequently, lenders in the United States are better able to evaluate the risks associated with participation in borrower activities.[160] Since the advent of the Green Paper, which fails to define liable parties, lenders in the EU face uncertain liability.[161] During the uncertain period prior to the enactment of legislation, lenders need to take preventative measures to limit their exposure to liability.[162] Moreover, lenders should lobby for legislation which, similar to the EPA rule, clearly defines permissible lender behavior.

IV. PREVIEW OF EU ENVIRONMENTAL LAW

A. *The Green Paper on Remedying Environmental Damage*

Enacted by the Commission and presented to the Council of Ministers and Parliament, the Green Paper discusses the various options and alternatives considered by the EU to remedy environmental damage.[163] The Green Paper discusses the adoption of a system of civil liability based on the "polluter should pay" principle first acknowledged in the SEA.[164] The Commission believes that civil liability advances the dual goals of deterring future contamination and compelling responsible parties to clean up existing environmental damage.[165]

158. *McLamb*, 5 F.3d at 72. Roughly 10 months passed between the lender's purchase and resale of the property. *Id.* at 71. The court also noted that the lender had also met the second requirement of the security interest exemption in that it did not participate in the management of the property. *Id.* at 72. The court also noted that an identical conclusion would result under the EPA rule. *Id. See supra* note 75 (setting forth the text of the security interest exemption).

159. *See supra* notes 137-58 and accompanying text (discussing judicial reception to the EPA rule).

160. Lavalette, *supra* note 17, at 508 (noting that the EPA offers predictability for lenders); *supra* notes 137-58 and accompanying text (discussing the favorable judicial reception to the EPA rule).

161. *See supra* notes 5-10 and accompanying text (discussing liability fears in the EU).

162. *See infra* notes 192-228 and accompanying text (suggesting preventative guidelines to be followed by EU lenders).

163. Green Paper, *supra* note 3, § 1.0; *Environment*, *supra* note 4 (noting that the Green Paper discusses the possibility of EU-wide action for restoring environmental damage); Napier, *supra* note 4 (stating that the Green Paper is a discussion on remedying environmental damage).

164. Green Paper, *supra* note 3, § 1.0; EEC Treaty, *supra* note 24, art. 130r. *See Environment*, *supra* note 4 (noting that the Green Paper adopts the "polluter pays principle"); Napier, *supra* note 4 (commenting on the Green Paper's polluter pays policy as the basis of community environmental policy). *See also supra* notes 30-32 and accompanying text (discussing the mandate of the EEC Treaty that the polluter should pay).

165. Green Paper, *supra* note 3, § 1.0. *See Environment*, *supra* note 4 (noting civil liability implements the polluter pays principle and deters future damage); Napier, *supra* note 4 (commenting that the Green Paper's policy of civil liability will create an incentive for the prevention of pollution).

In the Green Paper, the Commission considered both strict and fault-based liability.[166] The Commission seems convinced that a system of strict liability is better suited for remedying environmental damage because strict liability provides legal certainty, increases incentives for better risk management, and assists in implementing the polluter should pay principle.[167] Although the environmental damage must be linked to the activities of the allegedly liable party, strict liability eases the burden of proof by removing the need to prove fault.[168]

In spite of the advantages of a strict liability system, the Commission also identifies the limitations of strict, civil liability.[169] The Commission recognizes that the outrageous costs associated with an overly expansive strict liability scheme may stifle industry.[170] The Commission suggests that such problems may be overcome by an integrated environmental liability scheme, where the limitations of a civil liability scheme are supplemented by a system of joint compensation.[171] The Commission recognizes that the effectiveness of a civil liability scheme is frustrated when environmental damage cannot be attributed to a particular party.[172] Consequently, the Commission has suggested a system of joint compensation, similar to the Superfund in the United States, to make up for the deficiencies of a strict liability scheme.[173]

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166. Green Paper, *supra* note 3, § 2.2.1; *Environment, supra* note 4 (recognizing that the Green Paper discusses both a fault-based liability regime and a strict liability system); Napier, *supra* note 4 (stating that the Green Paper discusses fault-based and strict liability for remedying environmental damage).

167. Green Paper, *supra* note 3, § 4.1.2; Napier, *supra* note 4 (noting that the Green Paper recognizes that strict liability is suited to remedying environmental damage and concludes that strict liability will deter damage). "Strict liability appears to be particularly suited to the specific features of repairing environmental damage." Green Paper, *supra* note 3, § 4.1.2. CERCLA is also a civil liability system based on strict liability of responsible parties. *See supra* note 68 (noting that CERCLA is a strict liability system).

168. Green Paper, *supra* note 3, § 4.1.2. "[S]trict liability eases the burden of attaching liability because fault need not be established. However, the injured party must still prove that the damage was caused by someone's act." *Id.*

169. *Id.* § 2.1 (discussing the limitations of civil liability in remedying environmental damage).

170. *Id.* § 2.1.2. While an overly broad strict liability system will hamper industry, a narrow liability scheme may fail to encompasses all of the potentially threatening activities. *Id.* Napier, *supra* note 4 (stating that a strict liability may be regarded as unjust or become to expensive for targeted sectors).

171. Green Paper, *supra* note 3, § 3.0. *See Environment, supra* note 4 (noting that the Green Paper discusses a compensation system to cover costs when a liable party cannot be located); Napier, *supra* note 4 (stating that the Green Paper considers a compensations scheme to cover costs when not met by civil liability).

172. Green Paper, *supra* note 3, § 4.0 & fig. 1. The effectiveness of a civil liability scheme may be hampered when successive acts of pollution or historical pollution impede the ability to identify a liable party. *Id.* §§ 2.1.5(i), 3.0. A similar problem arises when the type of damage, for example the loss of a species of fauna, makes it difficult to place a monetary value on the damage. *Id.* § 2.1.10. Finally, civil liability requires a party with standing to sue on behalf of the environment. *Id.* § 2.1.9. *See* Napier, *supra* note 4 (reviewing the limitations of strict liability including identifying parties, apportioning liability, and standing to sue).

173. Green Paper, *supra* note 3, § 3.0; 26 U.S.C. § 9507 (1993) (establishing Hazardous Substance Superfund); 42 U.S.C. § 9611(a) (1994) (describing the uses of the fund). "Joint compensation systems sustained by contributions from the economic sectors most closely linked to the type of damage needing restoration would be concrete applications of the polluter pays principle." Green Paper, *supra* note 3, § 3.0. The Hazardous Substance Superfund is financed with environmental taxes, penalties, reimbursement monies, and punitive damages recovered under CERCLA and the Clean Water Act. 26 U.S.C. §§ 9507(b)(1)-(5) (1993) (noting

Presumably, the suggested joint compensation system will not generate lender liability because industries contribute to a general fund based on participation in damage-causing industries.[174] Nevertheless, financial institutions will face liability in the wake of expanding environmental liability in the EU.[175] Lenders may encounter liability by taking possession of waste when enforcing a security interest or by influencing the management or control of waste as a condition of a loan.[176]

Although the Green Paper announced the EU's intention to implement a system of strict, civil liability for environmental damage, the Green Paper left unanswered the most important question: Who will be liable?[177] This question certainly looms heavily on the minds of financial institutions as well as insurance companies and industry leaders.[178] However, the Commission recognizes that any proposal must consider how lenders and financial institutions will be affected.[179]

B. *Detrimental Effects of Lender Liability*

European financial institutions are concerned about the prospect of liability for environmental damage caused by their borrowers.[180] Proponents of holding financial institutions liable for environmental damage note that lender liability will encourage lenders to investigate potential borrowers and their waste related

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amounts to be appropriated to the Hazardous Substance Superfund). *See supra* note 73 (citing and discussing Hazardous Substance Superfund).

174. Green Paper, *supra* note 3, § 3.0. "The cost of damage linked to the aggregate impact of a sector's activities becomes apportioned among the individual enterprises, and thereby internalized." *Id. See* Napier, *supra* note 4 (discussing the Green Paper's version of a joint compensation system).

175. *See The European Community—Environmental Liability and the Risk for Financial Institutions*, EC FIN. SERVS. NEWSL. (Clifford Chance, London), Feb. 1992, at 28-30 [hereinafter Clifford Chance] (discussing direct and indirect lender liability). The newsletter discusses lender liability in regard to the Waste Directive. *Id. See* Waste Directive, *supra* note 55. Discussion on the Waste Directive has been delayed pending the development of a comprehensive environmental liability scheme. Turner T. Smith, Jr. & Roszell D. Hunter, *International Environmental Law Developments: A Focus on Europe*, ALI-ABA COURSE OF STUDY: ENVIRONMENTAL LAW 301 (1993) (stating that the proposed Civil Liability for Waste Liability Directive was held up pending the Green Paper). *See supra* notes 54-65 and accompanying text (discussing the Waste Directive).

176. Clifford Chance, *supra* note 175, at 29 (discussing the dangers of taking possession of land and retaining some power to control the business in the loan agreement). *See supra* notes 66-98 and accompanying text (discussing liability of owners and operators under CERCLA).

177. Green Paper, *supra* note 3, § 4.1.2 (raising the unanswered issue of what shall constitute a liable party).

178. *First Clash, supra* note 10 (recognizing that several industries have expressed discontent with the Green Paper). The European chemical industry refuses to accept liability for the life of its chemical products. *Id.* The BFEC wishes to avoid assuming the role of policemen of borrower activities. *Id.* The European Insurance Committee explains that it cannot offer insurance until it is possible to evaluate the cost of damage. *Id.*

179. Green Paper, *supra* note 3, § 4.1.2.

180. *First Clash, supra* note 10 (noting that the BFEC, which represents the banking industry of the EU, has expressed great concern about lender liability).

activities.[181] In addition, proponents of lender liability argue that it is reasonable to hold lenders liable when they profit on loans to businesses involved in waste disposal, production, or transportation.[182]

Despite these arguments, the BFEC fears that if banks are held liable for the waste related activities of their borrowers, financial institutions will be required to police the activities of potential and present borrowers.[183] Experience under CERCLA dictates that lender liability negatively affects lending transactions.[184] Consequently, businesses shoulder the cost of environmental liability in the form of added fees, environmental property audits, and higher interest rates.[185] The chairman of the EU Parliament's Committee on the Environment, Public Health, and Consumer Protection stresses that lender liability is a concern in the EU.[186]

Essentially, private investors are unwilling to invest more money to cleanup contaminated areas.[187] Unwillingness to reinvest "is a very serious concern because without such capital contaminated land will not be reused and will continue to pose potential risks to [the] environment and public health."[188] Another concern is that lenders will blacklist certain businesses or industries, refusing to lend to parties engaged in environmentally risky activities.[189] As a necessary consequence, even though Europe has not faced a precedent-setting case on the level of *Fleet Factors*, financial institutions remain at risk in the EU.[190] Lenders may be liable for cleanup costs or pay indirectly through loss in the value

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181. Quentel, *Cleanup Costs*, *supra* note 66, at 185.

182. *Id.* at 184. *See* John Gapper, *Banks Face Liability for Pollution*, FIN. TIMES, Oct. 13, 1993 (reporting that the British government believes banks should be responsible along with polluters and landowners).

183. *First Clash*, *supra* note 10.

184. *See Cleaning Up the Debris*, *supra* note 73, at 1257-58 (1991) (noting that lender liability may deter hazardous waste counseling by lenders attempting to avert liability for participation in disposal decisions and may deter entrepreneurs from investing in ventures by the cost of environmental cleanup which banks will require before making loans); Nicholson & Zuiderhoek, *supra* note 93, at 23 (noting several repercussions: Lenders become saddled with unmarketable property because the liability for cleanup is greater than the value of the property; lenders must delay foreclosure for fear of incurring liability as an owner of damaged property; and lenders refrain from workouts for fear of incurring liability as an operator of damaged property). *See generally* Greenberg & Shaw, *supra* note 17, at 1211 (discussing the potential risk of liability for lending institutions).

185. *See* Nicholson & Zuiderhoek, *supra* note 93, at 23 (noting that lender liability leads to lesser availability of loans and higher premiums); *Lender Liability and How It Effects [sic] Customers' Credit Ratings*, *supra* note 95 (noting that businesses face added fees, higher interest rates, and environmental audits).

186. *EP Committee Public Hearing on Environmental Damage*, Reuter Eur. Community Rep., Nov. 4, 1993, *available in* LEXIS, News Library, Reueub File (discussing an address by Chairman Ken Collins at a joint public hearing on preventing and remedying environmental damage).

187. *Id.*

188. *Id.*

189. John Bryne, American Banking Association senior counsel commented, "If Fleet were upheld, [banks] may as well blacklist firms on the EPA National Priority List and never lend to those on that list until they are cleared of liability." *Lender Liability and How it Effects [sic] Customers' Credit Ratings*, *supra* note 95.

190. *Id.*

of the security or by the decreased likelihood that a borrower will make good on the note.[191]

V. LENDING IN AN UNCERTAIN AGE: RECOMMENDATIONS FOR EU LENDERS

The Green Paper is a harbinger to the changing climate in European environmental legislation.[192] Forthcoming environmental legislation will likely impose liability without fault.[193] Consequently, EU lenders must recognize and prepare for the introduction of environmental, civil liability legislation. Respected specialists have developed guidelines to assist prudent lenders and their attorneys in minimizing the risk of environmental liability.[194] In the United States, lenders have a difficult time distinguishing between cautious supervision of borrower activities and supervision sufficient to constitute participation in management activities.[195] Prior to the adoption of the EPA regulations, case law was devoid of consistent and clear rules outlining acceptable lender behavior making it necessary to adhere to prophylactic strictures.[196] These guidelines advise the lender to take precautions prior to the loan, during loan negotiation, and upon workouts and foreclosure.

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191. *Id.* (quoting Chris Napier of Clifford Chance).

192. *This Week in Europe: Aid for Britain's Jobless, supra* note 3. In 1994, EU environmental policy will focus on the development of an environmental, civil liability system. *Id.*

193. *See supra* notes 163-79 and accompanying text (discussing the Green Paper's recommendation of strict environmental liability).

194. *E.g.*, 2 GERALD L. BLANCHARD, LENDER LIABILITY: LAW, PRACTICE AND PREVENTION § 15:15.50 (1989 & Supp. 1993); Jeffrey M. Gaba, Lender Liability for Hazardous Waste Cleanup, *in* LENDER LIABILITY LAW AND LITIGATION § 12.04 (Joseph J. Norton & W. Mike Baggett eds., 1992); Louis C. DeArias & Richard E. McCann, *Financial Institutions, in* ENVIRONMENTAL DISPUTE HANDBOOK: LIABILITY AND CLAIMS §§ 13.1-13.21 (David A. Carpenter et al. eds., 1991); Laura A. Baity & G. Robert Witmer, Jr., *Minimizing Risk to the Lender: Fleet Factors Revisited, in* THE IMPACT OF ENVIRONMENTAL REGULATIONS ON BUSINESS TRANSACTIONS 1990, at 375 (PLI Corp. L. & Prac. Course Handbook Series No. B4-6949, 1991); David R. Berz & Peter M. Gillon, *Lender Liability Under CERCLA: In Search of a New Deep Pocket*, 108 BANKING L.J. 4, 27-29 (1991); Michael B. Kupin, *supra* note 92, at 214; George A. Nation III, *Minimizing Risk of Loss from Environmental Laws*, 108 BANKING L.J. 346, 367-85 (1991); Thomas Redick, *Life After "Fleet Factors,"* CAL. LAW., Apr. 1991, at 72.

195. DeArias & McCann, *supra* note 194, § 13.19.

196. *See In re* Bergsoe Metal Corp., 910 F.2d 668, 672-73 (9th Cir. 1990) (holding that a lender must exercise the right to participate in management in order to lose security interest exemption); United States v. Fleet Factors Corp., 901 F.2d 1550, 1557 (11th Cir. 1990) (establishing that a capacity to influence standard for participation in management); United States v. Maryland Bank & Trust Co., 632 F. Supp. 573, 579 (D. Md. 1986) (holding that a lender's protection under the security interest exemption terminated at foreclosure); United States v. Mirabile, [1985] 15 Envtl. L. Rep. (Envtl. L. Inst.) 20,994, 20,996 (E. Pa. 1985) (holding that a lender did not lose the security interest exemption upon foreclosure).

A. *Investigation of Property*

The most effective way for lenders to elude environmental liability is to reduce exposure prior to loan transactions.[197] The risk of liability necessitates the execution of environmental audits.[198] Lenders should religiously conduct environmental audits of high risk properties prior to the execution of a loan.[199] High risk properties include industrial sites; construction sites; properties handling, using, or storing hazardous waste; and properties located near Superfund sites or landfills.[200] In order to insure against lender liability, financial institutions should take full advantage of audits and refrain from financing environmentally risky enterprises.[201] Lenders should order environmental audits as early as possible during loan negotiation in order to give the lender sufficient time to fully evaluate the environmental risks of the loan.[202]

An environmental audit should begin by examining several sources of information to develop an accurate site history of the secured property.[203] Initially, the lender should conduct a title examination of the property, taking notice of any easements, leases, restrictions, as well as transfers.[204] A review of the named transferees will indicate how the property has been used; for example a lessee known as the *ABC* Chemical Corporation may indicate the need for further investigation.[205] The extent of the title search will vary depending on the location and past uses of the secured property.[206] Real estate located in histori-

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197. BLANCHARD, *supra* note 194, § 15:43; DeArias & McCann, *supra* note 194, § 13.14. Activities undertaken prior to a loan transaction will not constitute participation in management. 40 C.F.R. § 300.1100(c)(2)(i) (1992). A lender may conduct an environmental audit or order the prospective borrower to clean up the property without risking the loss of the security interest exemption. *Id.* Nonetheless, failure to conduct an environmental audit prior to the loan transaction will not affect the lender's liability. *Id. Cf. Long Awaited Rule, supra* note 118, at 10,640 (noting that preloan activities will not constitute participation in management under the EPA rule).

198. Gaba, *supra* note 194, § 12.04.

199. DeArias & McCann, *supra* note 194, § 13.2; Gaba, *supra* note 194, § 12.04; Baity & Witmer, *supra* note 194, at 375; Kupin, *supra* note 92, at 212-13; Redick, *supra* note 194, at 75.

200. DeArias & McCann, *supra* note 194, § 13.12. High risk properties also include existing or former gas stations, automobile repair shops, dry cleaning stores, railroad yards and tracks, underground tanks and pipelines, refuse or waste disposal sites, and improvements containing asbestos. *Id.*

201. Gaba, *supra* note 194, § 12.04.

202. Kupin, *supra* note 92, at 213. Often the environmental audit is received nearing the end of the lending process. *Id.* The enthusiasm for the project may inhibit prudent deliberation of the audit's results. *Id.*

203. BLANCHARD, *supra* note 194, § 15.44; DeArias & McCann, *supra* note 194, § 13.14; Gaba, *supra* note 194, § 12.04; Berz & Gillon, *supra* note 194, at 27-28; Kupin, *supra* note 92, at 212-13; Nation *supra* note 194, at 371-73.

204. BLANCHARD, *supra* note 194, § 15.44; DeArias & McCann, *supra* note 194, § 13.14; Quentel, *Cleanup Costs, supra* note 66, at 183.

205. BLANCHARD, *supra* note 194, § 15.44; DeArias & McCann, *supra* note 194, § 13.14.

206. BLANCHARD, *supra* note 194, § 15.44.

cally industrialized areas will require a more extensive examination, as will property which has been used for environmentally risky activities.[207]

In order to complete a thorough environmental audit, the lender should conduct a visual inspection of the real estate and adjacent properties.[208] The lender should also require the borrower to complete, with the assistance of counsel when possible, an environmental questionnaire.[209] Lenders should employ fact specific inquiries and members of the lending team knowledgeable in environmental law should review the responses, and investigate questionable activities.[210] Finally, if available, the lender should obtain and diligently examine any governmental records which would indicate past or prospective environmental hazards.[211]

B. Negotiation of Loan Agreements

Prudent lenders should review and amend standard loan covenants to reflect their increased awareness of environmental liability. To avoid liability on the basis of capacity to influence, the lender should delete provisions which provide for increased lender participation of a debtor's enterprise upon financial deterioration of the borrower.[212] In addition, lenders should require periodic updates of the original environmental audit.[213] These regular updates may detect environmental problems in time to require cleanup by the borrower, move the loan to another lender, or accelerate the loan and collect from solvent guarantors.[214]

Further, the lender should require that the borrower warrant proper past and future use of the property[215] and likewise indemnify the lender against any environmental liability arising out of such use.[216] The indemnity agreement

207. *Id.*

208. *Id.* § 15.47; DeArias & McCann, *supra* note 194, § 13.14.

209. BLANCHARD, *supra* note 194, § 15.54; Nation, *supra* note 194, at 368-71.

210. Nation, *supra* note 194, at 368-71. Lenders should refrain from using legal terminology in the questionnaires. *Id.* at 370. For example, the question, "Does the corporation use hazardous substances in its manufacturing process?" involves a determination of the legal issue of what is a hazardous substance. *Id.* A better and fact specific question would be, "Has the corporation ever used polychlorinated biphenyls (PCBs) in its manufacturing process?" *Id.* This will enable the potential client to accurately answer the inquiries. *Id.*

211. BLANCHARD, *supra* note 194, § 15.45; DeArias & McCann, *supra* note 194, § 13.14; Quentel, *Cleanup Costs*, *supra* 66, at 183.

212. Kupin, *supra* note 92, at 214. *See* United States v. Fleet Factors Corp. 901 F.2d 1550, 1558 (1990); *infra* notes 79-98 and accompanying discussion. "[A] secured creditor will be liable if its involvement with the management of the facility is sufficiently broad to support the inference that it could affect hazardous waste disposal decision if it so chose." *Fleet Factors*, 901 F.2d at 1558.

213. BLANCHARD, *supra* note 194, § 15.15.50; Redick, *supra* note 194, at 72.

214. BLANCHARD, *supra* note 194, § 15.15.50.

215. DeArias & McCann, *supra* note 194, § 13.19; Gaba, *supra* note 194, § 12.04; Quentel, *Cleanup Costs*, *supra* note 66, at 183-84.

216. DeArias & McCann, *supra* note 194, § 13.17; Gaba, *supra* note 194, § 12.04; Redick, *supra* note 194, at 72; Quentel, *Cleanup Costs*, *supra* 66, at 183-84.

should outlive the loan to shelter the lender from liability claims which arise subsequent to the debtor's obligation but as a result of borrower activities.[217] If the borrower seeks to terminate indemnity upon sale, the lender should order an environmental audit at that time to determine if contamination has taken place.[218]

C. *Workouts and Foreclosure*

After the execution of the loan document, the lender must continue to exercise caution when managing the loan portfolio, specifically during workouts and foreclosure.[219] Whenever possible, lenders should refrain from activities which could be characterized as participation in management.[220] Extra precaution should be taken to abstain from deciding operational issues related to the use, transportation, handling, or disposal of hazardous materials.[221] Lending institutions can guard against liability by establishing and following precepts which restrict the lender's involvement in the management decisions of the borrower.[222] All contact with the debtor should be documented to preserve evidence of the lender's noninterference with the hazardous waste decisions of the borrower.[223] Finally, before increasing involvement in debtor activities, lenders may consider ordering an additional environmental audit report.[224]

If the potential environmental liability will outweigh the value of the obligation, the lender should consider alternatives other than foreclosure when the borrower defaults on loan obligations. A lender may consider acceleration of the debt, partial foreclosure, or loan modification to avoid incurring liability.[225] Ultimately, the lender may have to consider abandoning the security.[226] If title is taken at foreclosure, the lender should restrict involvement at the site and

217. DeArias & McCann, *supra* note 194, § 13.12; Gaba, *supra* note 194, § 12.04. *See* DeArias & McCann, *supra* note 194, § 13.13 (providing a sample indemnity agreement for lenders).

218. Redick, *supra* note 194, at 75.

219. *See supra* notes 114-36 and accompanying text (discussing policing and workout activities which do not constitute participation in management under the EPA rule).

220. Gaba, *supra* note 194, § 12.04. *See supra* notes 114-36 and accompanying text (discussing policing and workout activities which do not constitute participation in management under the EPA rule).

221. Berz & Gillon, *supra* note 194, at 28.

222. Kupin, *supra* note 92, at 213-14; Redick, *supra* note 194, at 76. Loan officers should observe and diligently follow the established lending precepts. *Id.*

223. Redick, *supra* note 194, at 76.

224. Baity & Witmer, *supra* note 194, at 375; Kupin, *supra* note 92, at 214. Lenders should consider abandoning the loan obligation if the risk of environmental liability is greater than the value of the security. Baity & Witmer, *supra* note 194, at 375.

225. DeArias & McCann, *supra* note 194, § 13.20.

226. Kupin, *supra* note 92, at 215; Baity & Witmer, *supra* note 194, at 375; Quentel, *Cleanup Costs*, *supra* note 66, at 183.

transfer the property without delay.[227] Nevertheless, acquisition of the property remains risky because polluted property is less marketable. This extends the time period which the lender retains possession and increases the likelihood of being characterized as participating in the management of the facility.[228]

VI. CONCLUSION

As previously stated, the Commission believes that environmental, civil liability will advance the dual goals of polluter accountability and prevention of environmental damage.[229] Civil liability implements the accountability goal by requiring monetary compensation from polluting parties.[230] Likewise, the threat of tremendous civil liability will deter environmental damage.[231]

The Commission advocates the use of civil liability to finance the restoration of the environment.[232] Understandably, European financial institutions are worried about liability following the rise of lender liability under CERCLA.[233] However, holding lenders liable for the environmental damage of a borrower is not consistent with the polluter should pay principle. Lenders who merely hold a security interest in the realty or personalty of a pollution causing enterprise are not ultimately responsible for the environmental damage. Lenders, who acquire ownership of the property through foreclosure or agreements in lieu of foreclosure, are not responsible for the production of pollution. Similarly, lenders who become involved in management decisions in order to protect their security, without managing hazardous waste, are not generating waste or causing environmental damage.[234] Lenders should not be forced to finance the cleanup

227. Gaba, *supra* note 194, § 12.04; Redick, *supra* note 194, at 76. *See supra* notes 129-36 and accompanying text (discussion foreclosure and postforeclosure activities under the EPA rule).

228. Berz & Gillon, *supra* note 194, at 4. Lenders may incur liability during the removal and relocation of personalty if the process triggers the release of hazardous substances. Redick, *supra* note 194, at 76.

229. Green Paper, *supra* note 3, § 1.0. EU Environment Commissioner Ioannis Paleokrassas identifies EU goals as prevention of environmental damage and the imposition of the polluter pays principle. *Paleokrassas Outlines*, *supra* note 36.

230. Green Paper, *supra* note 3, § 2.1.

231. *Id.* § 1.0. U.K. Environmental Minister Tim Yeo has called for recognition of Superfund achievement in the area of deterrence of further contamination. *Minister on Lenders' Responsibilities*, FLIGHT INT'L, Oct. 1993.

232. Green Paper, *supra* note 3, § 1.0 (stating "a person should rectify damage that he causes"). *See* United States v. Fleet Factors Corp., 821 F. Supp. 707, 722 (S.D. Ga. 1993) (remarking that "one of CERCLA's central tenets is to make the polluter pay"); United States v. Fleet Factors Corp., 901 F.2d 1550, 1553 (11th Cir. 1990) (citing Florida Power & Light Co. v. Allis Chalmers Corp., 893 F.2d 1313, 1316 (11th Cir. 1990)) ("The essential policy underlying CERCLA is to place the ultimate responsibility for cleaning up hazardous waste on 'those responsible for problems caused by the disposal of chemical poison.'"). *See also* EEC Treaty, *supra* note 24, art. 130r (providing that the "polluter should pay").

233. David Lascelles, *Debate Rages on Liability/Review of the Problem of Contaminated Land*, FIN. TIMES, Dec. 22, 1993; John Gapper, *supra* note 182.

234. *Bottomless Pit*, *supra* note 58. Lenders are not polluters and should not have to finance the cleanup of environmental damage caused by their borrowers. *Id.*

of damage caused by defaulting borrowers.[235] The foregoing reasons demonstrate that a civil liability system which does not exclude lending institutions from liability is inconsistent with the goal of requiring the polluter to pay.

While the Green Paper recognizes that civil liability deters environmental damage,[236] it fails to recognize that lender liability is inconsistent with the goal of prevention. Placing the risk of liability on financial institutions which finance environmentally risky industries will not deter pollution; rather, it deters lending institutions from advancing capital to these "tagged" industries. In certain situations this may actually hinder the prevention of environmental damage because lenders are unwilling to finance activities needed to regenerate affected areas. Consequently the areas will remain contaminated and unused by industry.[237] In lieu of incurring the risk of liability, lending institutions may also blacklist industries which pose a liability risk for lenders.[238] In either scenario, holding lenders accountable for the activities of their capital recipients is not consistent with the EU goal of prevention of environmental damage.[239]

Lender liability is inconsistent with both of the goals expounded in the Green Paper. Holding financial institutions liable for environmental damage does not deter pollution. It deters lenders from financing environmentally risky activities, engaging in workouts with troubled businesses, and ultimately it deters lenders from exercising their right to foreclose and recover on their loans. Similarly, holding lenders liable does not compel the polluter to pay, it mandates that deep pocket lending institutions foot the bill for irresponsible, insolvent, or absent borrowers.

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235. *See supra* notes 99-136 and accompanying text (discussing the EPA clarification of the security interest exemption, which delineates permissible management activities).

236. Green Paper, *supra* note 3, § 1.0.

237. Chairman Ken Collins, Address at the Joint Public Hearing on Preventing and Remedying Environmental Damage, *supra* note 186. The restriction of loans to an entire industry will punish low risk borrowers, who in order to cut operating costs may neglect environmental compliance. Nicholson & Zuiderhoek, *supra* note 93, at 39.

238. *See supra* note 189 (stating that banks may blacklist environmentally risky enterprises).

239. National Westminster Bank in Britain accepts the polluter should pay principle, but adamantly refuses to finance environmental cleanup caused by borrowers. *Bottomless Pit*, *supra* note 58.