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Sales of Environmentally Contaminated Properties: Is "As Is" Ever Enough?

by Angela M. Demerle

I. INTRODUCTION

When the "as is" clause is utilized in traditional real estate transactions, there is a common perception that the purchaser takes the property in its existing condition, subject to any and all defects. This common perception is very misleading, however, in transactions involving environmentally contaminated properties. In fact, in most cases involving environmental "defects" to the property, the "as is" clause serves no useful purpose other than to spark expensive litigation over the real meaning of the term in the context of environmental cleanups. This article focuses on the effectiveness of "as is" clauses in shielding sellers from liability in lawsuits involving environmental statutes which impose strict liability on the polluters, with specific emphasis on federal and state court decisions in New York State.

II. THE LIMITED SCOPE OF "AS IS" CLAUSES IN GENERAL

Even in the context of a real estate transaction where environmental contamination is not an issue, the "as is" clause is not as expansive in its protection of the seller from future liability as might be expected. For example, while it has been recognized in New York that a provision in a contract for the sale of realty by which the purchaser takes the property "as is" may protect the seller from liability due to physical defects in the property, the same may not hold true when allegations of fraud are involved. Accordingly, the purchaser of an apartment building who alleged a defect in the property (malfunctioning trash compactor) was precluded from recovery because the passing

of title "as is" extinguished any claims for defects discovered after purchase.¹ However, the "as is" purchase did not shield a seller and realtor from judicial inquiry into allegations of fraud in the inducement of a contract.² Thus as a general proposition it may safely be said that in New York an "as is" clause in a contract of sale bars *only* defect in warranty claims against the seller.⁴

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be completed by the end of 2000 will reduce the potential inputs into the river by over 90 percent from 1989 levels. The report, entitled "Reduction of Toxic Loadings to the Niagara River From Hazardous Waste Sites in the United States," is available from EPA's web site at <<http://www.epa.gov/glnpo/lakeont/nrtmp/hwsrpt99.htm>>.

EPA Settles Clean Air Act Case With Brooklyn Printer

A company that runs a flexographic printing facility in Brooklyn will pay a \$40,000 penalty for Clean Air Act violations under a settlement agreement with EPA. EPA cited the company for failing to operate equipment to control VOC emissions. An EPA inspection revealed that a catalytic incinerator used to control VOCs was not operating while equipment was being repaired. The company is required to run this equipment between April 1 and October 31, the months during which VOCs more readily combine with other chemicals and sunlight to form ground-level ozone or smog. EPA also cited the company for storing VOC-containing inks and VOC-soaked rags in open containers. EPA Region 2 Press Release (Jan. 3, 2000).

UPCOMING EVENTS

April 15-19, 2000

"American Planning Association Conference," sponsored by the American Planning Association, New York City. Requested topics include brownfields, takings, open space, and endangered species. Information: (312) 431-9100, or <<http://www.planning.org>>.

April 30 - May 3, 2000

"Conference of Solid Waste Associations," Sagamore, Bolton Landing. Information: Eric Swenson, (516) 677-5790 or ny-waste@erols.com.

WORTH READING

John M. Armentano, "Permit Denials: Substantive Due Process Claims Face Big Barriers," *New York Law Journal*, Jan. 26, 2000, at 5:2.

Paul S. Edelman, "Admiralty Law: Jurisdiction for Federal Navigable Waters," *New York Law Journal*, Jan. 27, 2000, at 3:1.

Michael B. Gerrard, "Consultants' and Lawyers' Duties to Report Contamination," *Trends (ABA Section of Environment, Energy, and Resources Newsletter)*, Jan./Feb. 2000, at 10.

Michael B. Gerrard, "The Swinging Pendulum of Citizen Suit Standing in 'Laidlaw,'" *New York Law Journal*, Jan. 28, 2000.

Michael R. Jung, "The Pine Barrens: A New Model of Land

Use Control For New York," *3 Buffalo Environmental Law Journal* 37 (1995).

Stephen L. Kass and Jean M. McCarroll, "Clean Air Act Enforcement Initiatives," *New York Law Journal*, Jan. 3, 2000, at 3:1.

Robert B. Koegel, "Cell Tower Siting Under Telecommunications Act of 1996," *New York Law Journal*, Jan. 5, 2000, at 1:1.

Peggy Santillo et al., "Panel of Towns (New York State) in Symposium: The Increasing Conflicts of Deer and Human Populations in Suburban Areas," *5 Buffalo Environmental Law Journal* 428 (1998).

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III. "AS IS" AND CERCLA

The use of "as is" clauses in the context of the Federal Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) has a fairly long history. Shortly after CERCLA's enactment, the Ninth Circuit held that an "as is" clause in a sales contract precluded only a breach of warranty action; a CERCLA claim was not precluded. In *Mardan Corporation v. C.G.C. Music, Ltd.*,⁴ plaintiff Mardan bought "as is" an environmentally contaminated property used to manufacture musical instruments. Mardan sued under CERCLA. Defendant, citing to New York law, which controlled the contract, argued that the "as is" clause negated any representations by the sellers as to any particular condition (fitness, type of construction, etc.) of the premises sold. The Ninth Circuit agreed as to the effect of the "as is" clause in New York, but in one bold stroke sided with plaintiff Mardan (without any supporting authority) that a warranty disclaimer such as an "as is" clause is limited to causes of action based upon breach of warranty theory *only*. As Mardan's lawsuit was based on a statutory cause of action created by CERCLA, Mardan's recovery was not defeated.

The ball was quickly rolling in the federal arena with respect to holding former owners liable under CERCLA, and thus, only one year later, a federal court in the Eastern District of Missouri held that a party which owned property at the time of a release cannot shift liability by claiming *caveat emptor*.⁵ One year after this, in 1988, the Third Circuit applied the same ruling but held that the defense is one to be considered in "mitigation of amount due."⁶ The District Court of New Jersey soon followed suit, holding that both the *caveat emptor* doctrine and "as is" clause inapplicable to bar a CERCLA cause of action.⁷ Shortly thereafter, a federal court in New York was confronted with the issue.

IV. THE INTERNATIONAL CLINICAL LABORATORIES (ICL) CASE AND ITS PROGENY

International Clinical Laboratories (ICL) purchased contaminated property and then sued the seller under CERCLA. The

contract of sale stated that ICL purchased the property "as is" and in its "present condition subject to reasonable use." The United States District Court, Eastern District of New York, concluded that the clause prevents a purchaser from recovering on a breach of warranty claim, and went on to explicitly endorse the Ninth Circuit's decision in *Mardan*:

This Court agrees with the *Mardan*'s court's interpretation of New York law. Accordingly, this Court holds that the "as is" clause of the contract cannot be construed to bar the present actions by I.C.L.⁸

Mardan's seminal ruling regarding the efficacy of an "as is" clause to bar a CERCLA claim had nothing to do with that court's interpretation of New York common law, but this does not diminish the *ICL* holding regarding the efficacy of "as is" clauses in the CERCLA context.

One year later, a U.S. District Court in California, facing a similar fact pattern to New York's *ICL* case, reached the same result, but the basis of this court's ruling was more reasoned and supportable. In *Wiegman & Rose Int'l Corp. v. NL Industries*,⁹ the court determined, contrary to *ICL*, that the "as is" clause vis-a-vis CERCLA was to be interpreted by federal law rather than state law. The *Wiegman* court stressed that CERCLA embodied Congress' intent that former owners of contaminated property be liable to current owners for contamination that occurred during the time they owned the property. The court reasoned that to allow an otherwise responsible party to avoid liability under the statute based on an "as is" clause would clearly circumvent both the intent and language of CERCLA. To so circumvent the statute something more than "as is" is required.¹⁰

Other cases from the 1980s which ruled that a seller could not escape liability for cleanup costs even though the property was offered and sold "as is" include *In re Sterling Steel Treating, Inc.*¹¹ and *Channel Master Satellite Systems, Inc. v. JFD Electronics Corp.*¹²

In more recent cases involving the "as is" clauses in the CERCLA context, defendants have had to be more creative given the case history against them. Accordingly, they have coupled the "as is" clause defense with factual patterns such as the buyer was a sophisticated developer, knew the property was an old industrial facility, had the opportunity to inspect, etc. Thus, the argument goes, it must be "assumed" the purchaser took the property subject to all environmental risks. In 1995, the U.S. District Court in New Jersey swept aside these arguments, insisting that to transfer environmental liabilities, the parties must say they are doing so:

[I]n order to preclude recovery of response costs, there must be a clear provision which allocates these rights to one of the parties . . . in order for the Court to interpret a contract as transferring CERCLA liability, the agreement must at least mention that one party is assuming environmental type liabilities.

[H]ad the parties intended such a transfer, it would have been easy to so provide.¹³

*M & M Realty Company v. Eberton Terminal Corp.*¹⁴ is a striking example of another federal court's insistence on explicit language regarding environmental liabilities. In this case, the purchasers took "as is" and had the right to cancel the contract after an environmental investigation. Despite these facts, the court refused to bar plaintiff's claims, stating "there can be no allocation of CERCLA liability without explicit language of indemnification, clearly manifesting the parties' intent to transfer liability."

V. THE UMBRA CASE

The Fourth Department of the New York State Supreme Court, Appellate Division, recently confirmed the general ineffectiveness of "as is" clauses as a shield to the liability of the seller for its environmental contamination of property. In *Umbra, U.S.A., v. NFTA*,¹⁵ the court ruled on Niagara Frontier Transportation Authority's (NFTA's) ability to shift its liability to Umbra under the New York State Oil Spill Prevention, Control and Compensation Act (the "Oil Spill Law"),¹⁶ through the use of an "as is" clause. Since there was no *express* shift of liability in the contract of sale, the court found that NFTA had not successfully shifted its responsibility for cleanup under the Oil Spill Law. As seen above, the *Umbra* decision was preceded by several federal court cases which held that "as is" or similar clauses failed to protect the seller from suit by the purchaser under another strict liability environmental statute, CERCLA.¹⁷ Thus, from one perspective the decision to this effect in *Umbra* was fairly predictable. However, *Umbra* is noteworthy because the contract of sale contained not only an "as is" clause, but additional language whereby Umbra was given the opportunity to undertake an environmental investigation of the property and had the opportunity, as well, to cancel the contract if dissatisfied with what that investigation revealed.

The environmental investigation revealed that there were several underground storage tanks (USTs) currently on the property. Moreover, these tanks had replaced old, leaking USTs that NFTA had removed from the property several years ago. Umbra purchased the property and upon removing the existing USTs discovered severe historical petroleum contamination in the area of the former leaking USTs. The cleanup cost Umbra several hundred thousand dollars.

Umbra sued, and after early skirmishes involving statute of limitation issues, moved for summary judgment seeking indemnification under New York's Oil Spill Law. NFTA cross-moved for dismissal of the action based on the contract of sale of the property "as is." NFTA's motion was denied without discussion by the lower court. On appeal to the Fourth Department, NFTA presented the case as one of first impression in the New York courts and moved away from its emphasis on the "as is" clause as a complete shield to liability. Rather, NFTA argued that the "as is" clause, *coupled* with Umbra's failure to exercise the contingency clause to cancel the contract after environmental issues were identified in its investigation, was sufficient indication that all risk was allocated to Umbra under the contract.

Umbra focused on the issue somewhat differently. It argued

that the case was really about whether there was language in the contract sufficient to protect a seller from the strict liability provisions of environmental protection statutes.

The Fourth Department's answer echoed that of most federal and state courts that have ruled on the question: the contractual language allegedly shifting liability under strict liability statutes from seller to purchaser must be clear, explicit and unambiguous. In the final analysis, the court told NFTA that if it had intended to escape from future liability under the Oil Spill Law its contract with Umbra should have "just said so." It did not, and Umbra prevailed on appeal.

VI. WHEN "AS IS" (WITH IMPORTANT ADDITIONS) IS ENOUGH

There are a few cases where the "as is" clause, coupled with other specific language, did work to shield the seller from liability. In *Niecke v. Enro Mkts. Co.*,¹⁸ purchaser's claims were barred. The contract explicitly stated that the buyer had fully inspected the property and was purchasing "as is," but also included a clause whereby the purchaser explicitly assumed responsibility for any damages caused by conditions on the property at the time of transfer of title.

In the most recent ruling on the matter, a U.S. District Court in Tennessee found that an "as is" clause which provided that the "seller made no representations or warranties to the usability of the above described property under present or future federal, state or local air and water pollution laws, ordinances or regulations," was ambiguous. However, extrinsic evidence of the parties' intentions to relieve the seller of all liability relating to the condition of the property was accepted by the court and resulted in a decision in favor of defendant.¹⁹

Absent explicit contractual language shifting environmental liabilities from seller to purchaser, or ambiguous language and convincing extrinsic evidence of the parties' intent to shift the burden, courts are very unlikely to undo the usual emphasis in environmental statutes of placing responsibility on polluting former owners of property.

VII. WAIVER OF CONTINGENCY IN A PURCHASE CONTRACT

As mentioned above, the *Umbra* case was somewhat unique in the history of "as is" cases because of defendant's arguments coupling the "as is" clause with Umbra's waiving of its right to cancel the contract of sale upon its receipt of the results of an environmental investigation of the property.

In this regard, NFTA argued on appeal that in New York the waiver of a defect in a contract equates to an express assumption of the obligations of the seller by the purchaser, but was unable to cite any cases where this "assumption" could be implied. Further, in the cases cited by NFTA such as *Modular by Design, Inc. v. DBJ Development Corporation*²⁰ and *Marino v. Dwyer Berry Construction Corp.*,²¹ there was explicit language in the contract indicating a waiver of defect would result in a shift of responsibility from buyer to seller. Umbra's contract had no such express language, and none could be implied.

Perhaps the most interesting case cited by NFTA on appeal was *In re Schenk Tours, Inc., Debtor*.²² In that case, Schenk purchased the property in a bankruptcy proceeding knowing it was a former bus garage, and after receiving a report of environmental problems on the property. *Dicta* in the Bankruptcy Court's opinion stated that the contract "strongly suggested that the risk of environmental problems were allocated to the purchaser under the agreement." However, the opinion also noted that Schenk agreed in the contract of sale to "assume responsibility for all violations of law including environmental matters." This is the type of language that courts accept as indicative of reallocation of environmental liabilities. Indeed, in *101 Fleet Place Associates v. New York Telephone Company*,²³ the court interpreted similar language as shifting the burden for environmental cleanup of a property under the Oil Spill Act from the contaminating tenant to the innocent landlord. Since the *Schenk* contract contained language explicit enough to shift environmental burdens to the purchaser, the court's opinion lends no light on when "as is" is ever enough.

VIII. CONCLUSION

The *Umbra* case is but one in a long series evidencing federal and state courts' good intentions to carry out the mandates of remedial environmental statutes. Case after case places the judiciary in the plaintiffs' corner with regard to the shift of environmental liabilities from the polluting seller to the innocent purchaser.

However, one must consider at what cost these plaintiffs' successes have come. The delay in environmental cleanups, the parties' expenses in taking these cases to appeal, and the overall frustration caused by poorly drafted contracts is the untold story of the "as is" saga. As the most recent opinions warn: when shifting environmental liabilities, say you are doing so, *explicitly* (and then say you are doing so a few more times). In cases such as these, "as is" is never enough.

Angela Demerle is an associate at Harter, Secret & Emery (HSE), and has concentrated her practice in environmental law since 1989. She has worked extensively on a broad range of environmental issues including hazardous and solid waste, Superfund litigation, environmental criminal defense, state and

federal permitting, underground storage tanks and spill liability, bankruptcy and environmental law, and land use development. HSE represented Umbra in the appeal before the Fourth Department.

¹ 1845 Ocean Associates v. Stein, 87 A.D.2d 765, 449 N.Y.S.2d 54 (3d Dept. 1982).

² Dygert v. Leonard, 138 A.D.2d 973, 525 N.Y.S.2d 436 (3d Dept. 1988).

³ Approved Properties, Inc. v. City of New York, 52 Misc. 2d 956, 277 N.Y.S.2d 236, 238 (Sup. Ct. Richmond Co. 1966). See also Young v. Keith, 112 A.D.2d 625, 492 N.Y.S.2d 489 (3d Dept. 1985).

⁴ 600 F. Supp. 1049 (D. Ariz. 1984), *aff'd*, 804 F.2d 1454 (9th Cir. 1986).

⁵ Sunnen Prod. Co. v. Chemtech Indus., Inc., 658 F. Supp. 276 (E.D. Mo. 1987).

⁶ Smith Land & Improvement Co. v. Celotex Corp., 851 F.2d 86 (3d Cir. 1988), *cert. denied*, 488 U.S. 1029 (1989).

⁷ Southland Corp. v. Ashland Oil, Inc., 696 F. Supp. 994 (D.N.J. 1988).

⁸ International Clinical Lab. v. Milton S. Stevens, 710 F. Supp. 466, 470 (E.D.N.Y. 1989).

⁹ 735 F. Supp. 957 (N.D. Cal. 1990).

¹⁰ The *Wiegman* court's rationale was at least considered by the Fourth Department in *Umbra*, and although the court did not mention in its opinion the importance of placing the burden for environmental cleanups on the parties responsible, the matter certainly arose during oral argument, with at least one judge expressing an opinion that the context of this case under the Oil Spill Law was a specific factor to take account of in rendering the court's decision.

¹¹ 94 B.R. 924 (Bankr. E.D. Mich. 1989).

¹² 702 F. Supp. 1224 (E.D.N.C. 1988).

¹³ New West Urban Renewal Co. v. Westinghouse Electric Corp., 909 F. Supp. 219, 223 (D.N.J. 1993).

¹⁴ 977 F. Supp. 683, 688 (M.D. Pa. 1997).

¹⁵ 693 N.Y.S.2d 371 (4th Dept. 1999), *leave to appeal denied*, 697 N.Y.S.2d 455 (N.Y. 1999).

¹⁶ Article 12 of the Navigation Law, § 170 *et. seq.*

¹⁷ 42 U.S.C. § 9601 *et. seq.*

¹⁸ 769 F. Supp. 973 (E.D. Mich. 1991), *aff'd*, 973 F.2d 1296 (6th Cir. 1992).

¹⁹ Velsicol Chemical Corp. v. Reilly Industries Inc., 67 F. Supp. 2d 893 (E.D. Tenn. 1999).

²⁰ 174 A.D.2d 885, 571 N.Y.S.2d 168 (3d Dept. 1991).

²¹ 146 A.D.2d 751, 537 N.Y.S.2d 234 (2d Dept. 1989).

²² 69 B.R. 906, 913 (Bankr. E.D.N.Y. 1987).

²³ 197 A.D.2d 27, 607 N.Y.S.2d 896 (1st Dept. 1994).