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Supreme Court Clarifies The Scope of Parent Corporation Liability for Cleanup of a Subsidiary's Contaminated Properties

In the nearly two decades since Congress enacted the Comprehensive Environmental Response, Compensation and Liability Act[1] to clean up the nation's most polluted sites, there has been extensive litigation, controversy and overall confusion regarding the extent to which corporate shareholders, otherwise known as "parents," may be held responsible to clean up their subsidiaries' polluted properties. Much of this confusion has arisen from the conspicuous silence of CERCLA on this subject and the resultant inconsistent interpretations of the statute by numerous federal trial and appellate courts. Now, the U.S. Supreme Court has addressed this issue in a recent unanimous opinion, *United States v. Bestfoods*.[2] While the Supreme Court does not go so far as to create a bright-line test for determining whether, and under what circumstances, CERCLA should compel parents to clean up their subsidiaries' contaminated properties, the Court brings some much-needed clarity to this area of environmental law.

Cases Prior to Bestfoods

With few defenses, CERCLA imposes liability on owners and operators of contaminated property to clean up such contamination without regard to the owners' or operators' fault or participation in the activities that caused the contamination.[3] Liability under CERCLA is joint and several, which means that a person who is liable under the statute can be held singularly responsible to clean up contamination even if there are other liable parties in connection with the same contamination. Under this sweeping liability scheme, a corporation that itself owns or operates contaminated property clearly is considered a liable party. Not long after the statute was enacted, questions arose in the case law as to whether others affiliated with the immediate corporate owner of contaminated property, such as the officers, directors and shareholders (or parents) of the corporation, could also be held liable for cleanup of the property. These questions were based on the fact that under CERCLA, "operation" of a property provides an avenue of liability independent from property "ownership" and, depending on a corporate affiliate's involvement in the corporation or the contaminated property owned by the corporation, the argument could be made that the affiliate is an "operator" of the contaminated property.

This line of argument thus would allow the imposition of cleanup liability on a parent directly under CERCLA, rather than having to resort to traditional common law principles of "piercing the corporate veil" between the parent and its subsidiary. In most jurisdictions courts disregard the presumption that a parent corporation is not responsible for the liabilities of its subsidiary if the extent of the parent's control over, and involvement in, the affairs of its subsidiary amounts to an abuse of the corporate form that will warrant "piercing the corporate veil" and disregarding the separate corporate entities of the parent and the subsidiary.

Given that the standard for "piercing the corporate veil" can be onerous—often requiring fraud or other wrongful purposes—claimants in the environmental arena have looked for alternative theories of liability and, thus, have extensively litigated whether a parent may be held liable directly under CERCLA as an "operator" of its subsidiary's contaminated property. Regrettably, this issue has not been easily or clearly resolved, mostly because of CERCLA's complete lack of guidance as to what the

term "operator" means.[4] Prior to the *Bestfoods* decision, federal courts covered the entire spectrum in their interpretation of this term in the parent-subsidiary context. Some courts, like the Courts of Appeals for the Fifth Circuit (which includes Texas and some of the Gulf states) and the Sixth Circuit (which covers Michigan, Ohio and some other mid-Atlantic states) have held that a parent cannot be liable for cleanup directly under CERCLA as an "operator," but rather only when the corporate veil is pierced.[5] Most federal courts, however, have held that, alternatively to veil-piercing, a parent can be held liable as an "operator" under CERCLA.[6] In this regard, some courts had held that, in order for "operator" liability to be imposed, a parent must actually have exercised control over or actually have become involved in the affairs of its subsidiary,[7] while other courts had held that a parent's authority to control its subsidiary is sufficient.[8]

What has fueled the confusion in this area of case law—other than the varying standards in different jurisdictions—is that in most of the cases, the court's liability analysis is highly fact-specific and balances a variety of factors related to the relationship between the parent and the subsidiary to determine the parent's "actual control" of, or "authority to control," its subsidiary. Because of the multitude of factors considered, the cases collectively do not yield a clear standard as to what would be considered "normal" participation by a parent in its subsidiary's affairs and participation sufficient to incur CERCLA liability. Moreover, the factors considered by the courts sometimes have nothing to do with the subsidiary's environmental matters. They include the percentage of stock ownership by the parent in the subsidiary; the extent of the parent's involvement in the appointment of and control over the subsidiary's directors and officers; the degree of parental control over the subsidiary's budget and finances; and the extent of the parent's oversight of the subsidiary's day-to-day operations. While many of the cases involve parent corporations that played a role in environmental management at the subsidiary's contaminated property, several courts have articulated that parental involvement in the subsidiary's environmental issues is not a prerequisite for incurring CERCLA liability if other factors demonstrate sufficient control by the parent over the subsidiary.[9] The "authority to control" standard articulated by some courts (such as the Fourth Circuit) is particularly troublesome, insofar as most if not all parent corporations, by the very exercise of their normal shareholder rights such as the appointment of the subsidiary's board of directors, have some authority to control their subsidiary.

The *Bestfoods* decision resulted from the appeal to the U.S. Supreme Court of the *Cordova* case, the Sixth Circuit decision noted above. In light of the conflict among the federal appellate courts over the standard for parent liability under CERCLA, the Supreme Court agreed to hear the case.

The Bestfoods Decision

The Lower Court Decisions

The *Bestfoods* case arose from the following circumstances. In 1957, a company called Ott Chemical Co. ("Ott I") began manufacturing chemicals at a plant near Muskegon, Michigan, a process that significantly polluted the soil and groundwater at the site. In 1965, CPC International Inc. ("CPC," subsequently renamed Bestfoods) purchased Ott I's assets, including the plant, through a wholly owned subsidiary (also named Ott Chemical Co., and referred to in the decision as "Ott II"). Ott II continued chemical manufacturing at the site and continued to pollute its surroundings. CPC kept the managers of Ott I on board as officers of Ott II. CPC also gave several such Ott II officers and directors positions at CPC, and these individuals performed duties for both corporations.

In 1972, CPC sold Ott II to Story Chemical Company, which operated the Muskegon plant until its bankruptcy in 1977. Shortly thereafter, the Michigan Department of Natural Resources ("MDNR") examined the site and found the land "littered with thousands of leaking and even exploding drums of waste, and the soil and water saturated with noxious chemicals." After extensive negotiations, MDNR facilitated the sale of the property from the bankruptcy trustee to Aerojet-General Corporation through Cordova Chemical Company of California, a wholly owned subsidiary created by Aerojet for the acquisition. Cordova/California in turn created Cordova Chemical Company of Michigan to operate the site, and the latter company manufactured chemicals at the site until 1986.

By 1981, the federal Environmental Protection Agency ("EPA") had undertaken to oversee the cleanup of the Muskegon property, and its remedial plan called for expenditures into the tens of millions of dollars. To recover some of this money, EPA filed suit under CERCLA in 1989, naming CPC, Aerojet, Cordova/California, Cordova/Michigan and a joint officer of CPC and Ott II as allegedly liable parties (Ott I and Ott II were defunct by that time). In relevant part, CPC was the party whose

defense to liability rested on the notion that a parent cannot be held liable for its subsidiary's (in this case, Ott II's) environmental matters absent piercing the corporate veil, and that the relationship between CPC and Ott II did not warrant such veil-piercing.

The federal trial court deciding the CERCLA action held that, independent from a veil-piercing analysis, a parent corporation can be held liable as an "operator" directly under CERCLA. Based on the facts developed regarding CPC, the court found that CPC in fact was an "operator" within the meaning of CERCLA. Such facts included CPC's selection of Ott II's board of directors and its appointment of several CPC officials to executive positions at Ott II. According to the trial court, these joint officials of CPC and Ott II made major policy decisions and conducted day-to-day operations at the Muskegon property (although without the need for formal approval from CPC). The court also found that certain CPC executives who were not Ott II board members occasionally attended Ott II board meetings. In addition, G.R.D. Williams, CPC's governmental and environmental affairs director, while not appointed to any position at Ott II, played a significant role in shaping Ott II's environmental compliance policy.[10]

On appeal, the Sixth Circuit reversed the trial court's decision on the ground that a parent may not be held liable directly as an "operator" under CERCLA, but rather only upon a piercing of the corporate veil.[11] Applying the veil-piercing law of Michigan, the Sixth Circuit decided that CPC was not liable for controlling the actions of Ott II, since the parent and subsidiary corporations maintained separate personalities and the parent did not utilize the subsidiary corporate form to perpetrate fraud or a wrongful purpose. Because the Sixth Circuit's veil-piercing analysis was not challenged on appeal to the U.S. Supreme Court, the Supreme Court rendered a decision only on the standard to be used to decide CPC's "operator" liability under CERCLA.

The Supreme Court Decision

To a great extent, the *Bestfoods* decision clarifies, and narrows, the scope of a parent corporation's liability for cleanup of its subsidiary's contaminated properties. The *Bestfoods* decision leaves intact the theory of parental liability as an "operator" directly under CERCLA as an alternative theory of liability to "piercing the corporate veil." However, the decision narrows the circumstances under which a parent can be deemed an "operator." As a preliminary matter, the Supreme Court defines an "operator" as someone who directs the workings of, manages, or conducts the affairs of a facility, and further states that "[t]o sharpen the definition for purposes of CERCLA's concern with environmental contamination, an operator must manage, direct, or conduct operations specifically related to pollution, that is, operations having to do with the leakage or disposal of hazardous waste, or decisions about compliance with environmental regulations." As such, the Court holds that it is not enough for the parent simply to interact with or control the subsidiary in ways unrelated to the subsidiary's contaminated property. Rather, to be deemed an "operator" under CERCLA, the parent must operate the contaminated property, evidenced by participation in the activities of the property.

Moreover, the Supreme Court addresses the traditionally problematic situation in which dual employees of the parent and the subsidiary play a significant part in the operations of the subsidiary. On this point, the Supreme Court states that it is entirely appropriate for directors and officers of a parent corporation to serve as directors of, or in key management positions at, the subsidiary, and "it cannot be enough to establish [the parent's] liability here that dual officers and directors made policy decisions and supervised activities at the [subsidiary's contaminated property]." Rather, to establish the parent's "operator" liability, it must be shown that such joint officers or directors were acting in their capacities as the *parent's* officers and directors, and not the subsidiary's, when they committed those acts.

Notwithstanding this fine-tuning of the CERCLA "operator" standard for parent corporations, the Supreme Court did not find the facts developed by the trial court to present an open-and-shut case that CPC was not liable as an "operator." Rather, the Supreme Court found that certain facts, particularly the involvement of Mr. Williams (who was not a joint officer or director) in the affairs of Ott II, warranted remanding the case back to the trial level for a reconsideration based on the principles espoused by the Supreme Court.

The Aftermath of Bestfoods

While the *Bestfoods* decision goes far in clarifying the standard for holding a parent corporation liable for cleanup of its subsidiary's contaminated property, the decision stops short of closely defining examples of "normal" participation by a parent at its subsidiary's contaminated property

and participation sufficient to incur CERCLA liability—even when the parental involvement relates to environmental matters. In the case of joint officers and directors, the Supreme Court simply observes that "a dual officer or director might depart so far from the norms of parental influence exercised through dual officeholding as to serve the parent, even when ostensibly acting on behalf of the subsidiary in operating the facility." And in the case of a parent corporation employee who "wears no hat" at the subsidiary level, the Supreme Court observes that such employee's involvement in the subsidiary's affairs may stay in a "normal," and thus safe, range. Among the few examples of safe involvement given by the Supreme Court are monitoring the subsidiary's performance, supervision of the subsidiary's finance and capital budget decisions and articulation of general policies and procedures.

The Supreme Court does not voice any opinion on the standard to be used under the alternative route for establishing a parent's cleanup liability—piercing the corporate veil. Specifically, the Supreme Court does not speak to a conflict among lower federal courts as to whether state law or a uniform federal law should apply to a veil-piercing analysis in the CERCLA context.

Finally, it should be noted that the *Bestfoods* decision relates only to federal CERCLA liability, and most states have enacted their own statutes dealing with the issue of environmental cleanup liability. Nonetheless, because such liability under state statutes typically is "no-fault" and rests on "owner" or "operator" status as under CERCLA, the *Bestfoods* decision may serve as ample guidance regarding the scope of parent corporation liability even under the state statutes.

Endnotes

1 42 U.S.C. §§ 9601 et seq. (otherwise known as CERCLA or the Superfund law).

2 66 U.S.L.W. 4439 (June 8, 1998).

3 42 U.S.C. § 9607(a)(1) and (2).

4 CERCLA circuitously defines "owner or operator" as "any person owning or operating" the contaminated property. 42 U.S.C. § 9601(20)(A)(ii).

5 *See, e.g.*, *Joslyn Mfg. Co. v. T.L. James & Co.*, 893 F.2d 80, 82-83 (5th Cir. 1990), *cert. denied*, 498 U.S. 1108 (1991); *United States v. Cordova/Michigan*, 113 F.3d 572, 580 (6th Cir. 1997).

6 *See, e.g.*, *United States v. Kayser-Roth Corp.*, 910 F.2d 24 (1st Cir. 1990); *Lansford-Coaldale Joint Water Authority v. Tonolli Corp.*, 4 F.3d 1209 (3rd Cir. 1993); *Nurad, Inc. v. William E. Hooper & Sons Co.*, 966 F.2d 837 (4th Cir. 1992), *cert. denied*, 506 U.S. 940 (1992); *Jacksonville Electric Authority v. Bernuth Corp.*, 996 F.2d 1107 (11th Cir. 1993).

7 *See, e.g.*, *Kayser-Roth*, 910 F.2d at 27; *Jacksonville Electric*, 996 F.2d at 1110.

8 *See, e.g.*, *Nurad*, 966 F.2d at 842; *United States v. Carolina Transformer Co.*, 978 F.2d 832, 837 (4th Cir. 1992).

9 *See, e.g.*, *Lansford-Coaldale*, 4 F.3d at 1209; *United States v. TIC Investment Corp.*, 68 F.3d 1082, 1091-92 (8th Cir. 1995); *Schiavone v. Pearce*, 79 F.3d 248, 255 (2nd Cir. 1996).

10 *CPC International, Inc. v. Aerojet-General Corp.*, 777 F. Supp. 549 (W.D. Mich. 1991).

11 *See* note 5, *supra*.

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