LIABILITY OF PARENT CORPORATIONS, OFFICERS, DIRECTORS, AND SUCCESSORS: When Can CERCLA Liability Extend Beyond the Company?

Michelle De Blasi*

INTRODUCTION

The high cost of remediating contaminated sites and the joint and several liability scheme under the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") (42 U.S.C. § 9607), as amended, have led the United States Environmental Protection Agency ("EPA") and CERCLA Potentially Responsible Parties ("PRPs") to pursue every available resource to cover cleanup costs. Litigation seeking reimbursement for remediation expenses from corporate parents, corporate successors, officers, directors, and shareholders has shown that plaintiffs will attempt to cast CERCLA's liability over every possible party with resources, and any such party can be caught under the right circumstances.

United States v. Bestfoods established the standard by which the liability of corporate entities and their subsidiaries is determined.[1] In *Bestfoods*, the Court held that parent corporations can be *directly* liable under CERCLA § 107(a) if they are directly involved in the company's management of hazardous substances, or *indirectly* liable under traditional principles of corporate veil piercing. Courts have found that corporate officers, directors, and shareholders also face similar liability risks.

I. PARENT CORPORATIONS

In *Bestfoods*, the United States sued the parent corporations of liable chemical manufacturers to recover costs incurred for cleaning up contamination caused by chemical plant operations.[2] In considering these claims, the Court first recognized that "[i]t is a general principle of corporate

---

* Michelle De Blasi is senior environmental counsel at Gammage and Burnham, PLC in Phoenix, Arizona. Portions of this article were contributed by Greg Tan at Greenburg Traurig, LLP.

1. 524 U.S. 51, 52 (1998).
2. *Id.* at 51.

law deeply 'ingrained in our economic and legal systems' that a parent corporation (so-called because of control through ownership of another corporation's stock) is not liable for the acts of its subsidiaries."[3] However, the Court found that a parent corporation can be held liable under CERCLA in two ways: (1) a parent corporation can be held directly liable as an operator if it manages, directs or conducts activities relating to the disposal or release of hazardous substances; or (2) a parent corporation can be held indirectly liable for a subsidiary's actions if the corporate veil can be pierced.[4]

The two paths to parent corporation liability are discussed in more detail below. The key difference between them is that direct liability assesses the parent corporation's involvement in, or operation of, the facility which is the subject of the CERCLA cleanup.[5] By contrast, the indirect liability analysis assesses the parent corporation's relationship with, or control over, the subsidiary that is the primary owner or operator of the facility.[6]

A. Direct Liability

The Court in *Bestfoods* found that a company that provides active supervision and control over matters relating to a release of hazardous substances to the environment can be found directly liable as an "operator" of the facility.[7] For direct operator liability, "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."[8]

Certain activities, however, for example "[a]ctivities that involve the facility but which are consistent with the parent's investor status, such as monitoring of the subsidiary's performance, supervision of the subsidiary's finance and capital budget decisions, and articulation of general policies and procedures, should not give rise to direct liability."[9] As such, without further action, merely holding a controlling interest in an entity is insufficient to hold an investor liable, and, conversely, an investor is not automatically immune merely because it holds a minority interest in the company that operates the facility.[10]

---

3. *Id.* at 61.
4. *Id.* at 51–52.
5. *Id.* at 67–68.
6. *Id.* at 68.
7. *Id.* at 52.
8. *Id.* at 66–67.
9. *Id.* at 72.
10. Consol. Edison Co. of N.Y. v. UGI Utils., Inc., 310 F. Supp. 2d 592, 603–06 (S.D.N.Y. 2004); CBS, Inc. v. Henkin, 803 F. Supp. 1426, 1436 (N.D. Ind. 1992) (constructive ownership

In *Bestfoods*, the director of governmental and environmental affairs of the parent corporation actively and directly participated in a variety of environmental matters of the subsidiary company, including issuing directives relating to regulatory inquiries.[11] This individual was not an employee, officer or director of the subsidiary, and his actions were therefore construed as those of the parent corporation.[12] The Court found that these facts could provide the basis for the parent corporation's direct operator liability under CERCLA, and remanded the case for further proceedings.[13]

The *Bestfoods* decision sets forth the law of the land with respect to extending CERCLA liability to various corporate entities. The District of Arizona had occasion to apply *Bestfoods* in a 2005 cost recovery case where plaintiffs alleged direct operator and arranger liability of related corporations.[14] The district court adopted the *Bestfoods* principles as its basis for finding direct parent liability.[15] In ruling on whether the testimony of certain experts would be allowed, the court held that expert testimony addressing the corporate relationship among the defendant companies, and factual information relating to the activities of the parent corporation's agents in relation to the subsidiary, were relevant to determine whether direct operator or arranger liability existed under CERCLA.[16]

B. Indirect Liability: Piercing the Corporate Veil

A parent corporation can be found to have indirect liability when the corporate veil can be pierced. The Court in *Bestfoods* relied upon general principles of corporate law to determine whether veil-piercing would be merited, first recognizing the fundamental principle that "a parent corporation . . . is not liable for the acts of its subsidiaries."[17] The Court also acknowledged that "the corporate veil may be pierced . . . when . . . the corporate form would otherwise be misused to accomplish certain wrongful purposes."[18] Without determining the outcome under the facts of the case, the Court held that a parent may be liable for its subsidiary's CERCLA liabilities

---

of ninety percent of stock insufficient to establish liability); United States v. McGraw-Edison Co., 718 F. Supp. 154, 156–58 (W.D.N.Y. 1989).

11. *Bestfoods*, 524 U.S. at 72.
12. *Id.* at 73.
13. *Id.*
14. Pinal Creek Grp. v. Newmont Mining Corp., 352 F. Supp. 2d 1037, 1040–42 (D. Ariz. 2005).
15. *Id.*
16. *Id.* at 1041–42.
17. *Bestfoods*, 524 U.S. at 52.
18. *Id.*

if standard veil-piercing factors are satisfied.[19] The Court, however, left unresolved the question of whether federal common law or a state law standard should apply to veil-piercing in the context of CERCLA.[20]

Courts of Appeals have reached varying conclusions regarding whether federal or state standards should apply to issues of indirect liability arising under federal environmental laws.[21] Most appellate panels, including the Ninth Circuit,[22] have applied state law when faced with this type of issue, but the Third and Fourth Circuits have reached the opposite conclusion.[23]

C. Veil Piercing Under Arizona Law

In Arizona, a corporation will generally be treated as a separate legal entity unless sufficient evidence exists to disregard the corporate form.[24] While Arizona law states that a member of a limited liability company ("LLC") is not liable solely by reason of being a member of an LLC, it is likely that the same analysis would be applied to LLCs for piercing the corporate veil.[25] Thus, members of Arizona LLCs may be subject to the same direct liability analysis and veil-piercing analysis that courts have applied to corporations. Prudent members of an LLC can protect against this potential liability by taking steps necessary to ensure that the LLC does not become an alter ego and by otherwise observing the formalities of the LLC.[26]

In Arizona, the corporate form will be disregarded when (1) the corporation is the alter ego of another, and (2) observing the corporation would work an injustice.[27] "If a corporation was formed or is employed for fraudulent purposes then clearly the corporate fiction should be disregarded."[28] The corporate veil may be pierced under circumstances where a sole shareholder or parent corporation "not only influenced and governed [the subsidiary] but that there was also such a unity of interest and ownership

---

19. *Id.* at 63–64.

20. *Id.* at 63 n.9.

21. New York v. Nat'l Serv. Indus., Inc., 460 F.3d 201, 207 (2d Cir. 2006) (Sotomayor, J.) ("The choice of law question is a complicated one that has led . . . sister circuits to reach different answers.").

22. *See* Atchison, Topeka & Santa Fe Ry. Co. v. Brown & Bryant, Inc., 159 F.3d 358, 363 (9th Cir. 1998) (applying state law to question of corporate successor liability).

23. *Nat'l Serv. Indus., Inc.*, 460 F.3d at 207–08.

24. Dietel v. Day, 492 P.2d 455, 457–58 (Ariz. Ct. App. 1972).

25. *See* ARIZ. REV. STAT. ANN. § 29-651 (2013).

26. *See*, *e.g.*, Gray v. Shaw, No. 1 CA-CV 06-0298, 2007 WL 5439746, at * 11 (Ariz. Ct. App. Aug. 9, 2007).

27. *See Dietel*, 492 P.2d at 457.

28. *Id.*

that the individuality or separateness of [the subsidiary] and [the parent] had ceased to exist."[29]

Factors that may support a finding of alter ego might include the failure of the entities to observe separate corporate formalities, the commingling of assets or economic integration of the entities, the presentation of the entities to customers or the public as a single business entity and undercapitalization of the entity whose separate existence is challenged.[30] There is not a single factor that is dispositive, but instead a combination of these factors will likely exist where a successful veil-piercing case is made using the alter ego theory.[31]

II. SUCCESSOR LIABILITY

Successor liability is another path by which related corporations might be liable under CERCLA, as ruled by the Third Circuit in *Smith Land v. Celotex*.[32] In *Smith Land*, the purchaser of contaminated land sued to recover cleanup costs from the corporate successors to the seller who operated an asbestos manufacturing facility at the site.[33] The court acknowledged that CERCLA does not directly address successor liability, but found that the congressional intent underlying CERCLA favored a conclusion that successors can be liable under CERCLA.[34] The case was remanded with instructions to the district court to apply the general doctrine of successor liability, applied in most states, that successor liability may be imposed under CERCLA where corporations either have merged with or have consolidated with a corporation that is a responsible party under CERCLA.[35]

The Ninth Circuit has adopted the holding in *Smith Land*.[36] "Preliminarily, we must decide whether there is successor liability under CERCLA. Although Congress failed to address specifically the issue of corporate successor liability in CERCLA we find Third Circuit authority persuasive on this issue and hold that Congress did intend successor liability."[37]

---

29. *Id.* at 457–58 (citing Whipple v. Indus. Comm'n, 121 P.2d 876 (1942)).
30. *Id.*
31. *Id.*
32. 851 F.2d 86, 92 (3d Cir. 1988).
33. *Id.* at 87.
34. *Id.* at 89–90.
35. *Id.* at 92.
36. *See* La.-Pac. Corp. v. Asarco, Inc., 909 F.2d 1260, 1262–65 (9th Cir. 1990).
37. *Id.* at 1262.

III. OFFICER/DIRECTOR/SHAREHOLDER LIABILITY

A. Direct CERCLA Liability

Corporate officers, directors, and even shareholders are also at risk of being held liable under CERCLA as parent corporations under a direct liability analysis. In this context, individuals can acquire personal liability based on their authority over and involvement in waste management or disposal decisions.

1. Corporate Officers and Directors

An individual may be personally liable if he personally conducts operations giving rise to CERCLA liability.[38] Merely being an officer or shareholder of a corporation that operates the facility does not shield an individual from liability for operating a hazardous waste facility.[39] "There is no liability shield at all for an officer. If he commits an act that is outside the scope of his official duties, his employer may not be liable; but he is whether or not the act was within that scope . . . . So if [defendant] operated the [facility] personally, rather than merely directing the business of the corporations of which he was the president and which either formally, or jointly with him . . . , operated it, he is personally liable."[40]

The Eighth Circuit has held that corporate officers and directors can acquire direct CERCLA liability in the context of a case alleging direct arranger liability.[41]

> [CERCLA] imposes direct arranger liability on a corporate officer or director if he or she had the authority to control . . . directly or indirectly, over the arrangement for disposal, or the off-site disposal, of hazardous substances . . . . For arranger liability to attach to a corporate officer or director, there must be some actual exercise of control, *and* it must include the exercise of some control, directly or indirectly, over the arrangement for disposal, or the off-site disposal, of hazardous substances.[42]

38. Browning-Ferris Indus. v. Ter Maat, 195 F.3d 953, 955–57 (7th Cir. 1999).
39. *Id.*
40. *Id.* at 955–56.
41. United States v. TIC Inv. Corp., 68 F.3d 1082, 1089–90 (8th Cir. 1996).
42. *Id.*

2. Shareholders

Principal shareholders and officers of a closely-held corporation can also acquire direct CERCLA liability. While Congress did not include corporate shareholders and officers in the definitions of owner or operator, and "liability may not imposed . . . solely on the basis of an officer's or shareholder's active involvement in the corporation's day-to-day affairs," officers or shareholders may be held liable where the person "actually participated in the liability-creating conduct."[43]

B. Sarbanes-Oxley Act

The Sarbanes-Oxley Act of 2002 imposed new requirements on key executives to certify the accuracy of financial information disclosures.[44] While the Act did not change the fundamental disclosures already required by laws enforced by the SEC, it raised the stakes for executives who are now subject to individual civil and criminal liability for inaccurate financial reporting.

Pertinent disclosures may include those relating to environmental compliance costs and investments that materially affect business, environmental legal proceedings, or known environmental trends and uncertainties that may affect business.[45] It is therefore important for companies to have systems in place to thoroughly vet and accurately quantify their environmental liabilities or risk enforcement under Sarbanes-Oxley.

The SEC has actively sought enforcement against companies relating to inaccurate reporting of environmental remediation reserve accounts. Environmental reserve accounts are required to reflect future remediation costs that the company is likely to incur, including pre-cleanup activities and the performance of remedial actions.[46] The following are some SEC enforcement actions arising from reporting of environmental liabilities:

- **Safety-Kleen** – criminal case in which the SEC alleged that Safety-Kleen's CFO improperly reduced the company's environmental remediation reserve account estimates to overstate the company's income.[47]

---

43. United States v. USX Corp., 68 F.3d 811, 825 (3d Cir. 1995).

44. 15 U.S.C. § 7241 (2012).

45. Andrew N. Davis, *Environmental Disclosures After Sarbanes-Oxley*, PRAC. LAW., June 2004, at 19, 20.

46. ROBERT C. KIRSCH & TINA Y. WU, DISCLOSURE OF ENVIRONMENTAL LIABILITIES: SEC OBLIGATIONS, AUDITING STANDARDS, AND THE EFFECT OF SARBANES-OXLEY 1683, 1689 (2007).

47. Safety-Kleen Corp., Litigation Release No. 18555, 2004 WL 162953 (Jan. 28, 2004).

- **ConAgra** – civil enforcement case in which the SEC alleged that executives improperly reduced the company's environmental reserve estimates in order to offset losses.[48]

- **Ashland, Inc.** – civil enforcement case in which SEC alleged that Ashland's Director of Environmental Remediation inappropriately reduced the cost estimates for remediating several of the company's chemical and refinery sites.[49]

CONCLUSION

The general rule is that the corporate form will be recognized to shield parent corporations, officers, directors, and shareholders from environmental liabilities of the liable corporation. Exceptions have been found, however, where direct liability can be established based upon direct involvement in the activities from which liability arises, or where the corporate veil can be pierced. Similar principles are likely to apply in the LLC context. As a result of this potential risk, parent corporations must be careful about engaging in subsidiary support activities that could be viewed as taking a direct role in pollution-related activities. Similarly, if the parent corporation implements an environmental management system, the company should take steps to ensure that such activities are not characterized as active participation in a subsidiary's pollution-related activities.

There is also the potential risk to parent corporations of indirect CERCLA liabilty as a result of forming or maintaining a subsidiary that could be perceived as an alter ego. Parent corporations and other parent entities should therefore ensure that their subsidiaries are properly formed, sufficiently capitalized, and that corporate formalities are observed. Acquisitions of companies and their assets also pose a risk of successor liability. Parent corporations and other parent entities should be aware of the liability risk associated with mergers or consolidations and consider structuring deals as asset purchases to protect against this risk.

Executives may also incur civil or criminal liability based upon inaccurate financial reporting relating to environmental liabilities of the company. It is therefore important to ensure that systems are in place to accurately quantify environmental liabilities and to ensure that they are appropriately reported in financial disclosures.

---

48. ConAgra Foods, Inc., Litigation Release No. 20262, 2007 WL 2126401 (July 25, 2007).
49. Ashland, Inc., Exchange Act Release No. 54830, 2006 WL 3435637 (Nov. 29, 2006).