

Coping With The "BRAC" Military Base Closure And Reuse Process

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A discussion of the challenges facing redevelopers of retired military installations in dealings with the U.S. Department of Defense and local government reuse authorities (LRAs), with particular emphasis on vehicles for expedition of privatization through various disposition models and methods for mitigating the legal and economic risks of environmental contamination.

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I. INTRODUCTION

Since the enactment of the first federal base realignment and closure ("BRAC") legislation in 1988, nearly one hundred military installations of varying size and located in every part of the country have been selected for conversion from military to civilian uses. These sites offer new, and often unique, redevelopment opportunities of unprecedented scale for urban infill and suburban residential and commercial projects. The nation's largest development companies have been quick to respond to these opportunities.

Military base closures have saved the federal government many billions of dollars since initiation of the first base retirements in the late 1980's; but these closures have also brought considerable disruption and economic loss to affected local communities. The BRAC process was enacted to overcome the Congressional politics and log rolling that for many years thwarted efforts to identify and close individual military bases. The legislation provides for a periodic listing of proposed conversions recommended by a federal base closure commission and endorsed by the President, which recommendations must, in turn, be approved by Congress on an all or nothing basis. The selection procedure and the related political and economic aspects have been highly publicized and broadly debated. In all events, it is unlikely that the program will be discontinued; indeed, there have been estimates that more than a quarter of the remaining operating bases will be retired commencing with the next round of scheduled closures in 2005.

Federal law includes at least eight different authorizations for sale of BRAC properties, including public benefit conveyances for parks, recreation, and similar public uses; conveyances at no cost directly to representatives of the homeless; negotiated sales to state and local public agencies; and transfers to other federal agencies. The authorized conveyances most relevant to private developers are (i) Economic Development Conveyances ("EDCs") to a local redevelopment or reuse authority ("LRA") at or below fair market value, and often at no cost to the LRA, and (ii) advertised public sales to the highest bidder, usually a private developer or investor, at no less than fair market value. In the case of EDCs, the LRA (often an established local redevelopment agency vested by state statute with broad powers, but sometimes a

specially formed, single purpose authority) normally selects one or more private developers and contracts with the developer(s) for further conveyance and redevelopment of the site. When property is conveyed by public sale, the developer has much more immediate involvement with the government and the remediation process.

The vast majority of base conversions earmarked for private development are EDCs. As noted, these transactions normally involve conveyance from the military to an LRA under a Conveyance Agreement and subsequent transfer to a developer pursuant to a real estate Disposition and Development Agreement (DDA) or, where the local agency as a matter of public policy or legal obligation retains a fee interest in the site, by a Lease Disposition and Development Agreement (LDDA). The transition from federal government to developer ownership or control can be lengthy and expensive to the public and private parties to these transactions, even where, as in many cases, the property is conveyed to the LRA and/or private developer at "no cost".

The military base retirement, conveyance and redevelopment process is driven, perhaps like no other real estate transaction, by environmental remediation. It is the rare military base that is not seriously contaminated by hazardous materials, including, in the worst case, unexploded ordinance or nuclear radiation. The timing and extent of cleanup is central to both the land use planning and ultimate development of the project, and the methods chosen for implementation and verification of environmental remediation pervade every aspect of the process.

The following includes (i) a brief overview of BRAC EDCs, (ii) an analysis of the primary environmental concerns and potential impacts that must be considered by a private developer for such projects and its counsel, (iii) a discussion of methods for eliminating or mitigating such impacts and (iv) a comparison of two principal alternatives for site remediation and conveyance — that is, remediation prior to transfer by the military under a Finding of Suitability to Transfer (FOST) and conveyance prior to cleanup under a Finding of Suitability for Early Transfer (FOSET).

II. AN OVERVIEW OF THE BRAC AND EDC PROCESS

The military base closure process is governed by a series of federal enactments, commencing with the first BRAC legislation in 1988¹. It begins with the final determination by the federal government to close a given military installation. In

¹ Nearly 100 military bases have been closed under the Defense Authorization Amendments and Base Closure and Realignment Act of 1988 and the Defense Base Closure and Realignment Act of 1990 (both at 10 U.S.C. § 2687). It is anticipated that the National Defense Authorization Act for Fiscal Year 2002 (Pub.L.107-107) calling for the next round of closures in 2005 could involve from 75 to 100 additional bases. A convenient website for many of the publications referred to in this paper and other current information on the BRAC process can be found at <http://www.acq.osd.mil/installation/reinvest/manual/toc.html>.

the case of an EDC, upon final selection of a base for closure, an LRA is established or designated and begins the development of a preliminary reuse plan, normally through a public hearing process involving various local agencies and community "stakeholders." At the same time, in consultation with the LRA and in response to the LRA's conceptual reuse plan, the relevant military department develops its own program for disposition, remediation and management activities.

In its 1995 Base Reuse Implementation Manual and its 1996 Community Guide to Base Reuse, the Department of Defense ("DOD") offers an overview of the process, identifying several stages and typical time lines for the BRAC base conversions. The three general phases of the process are identified as (i) Reuse Planning, (ii) Disposal and Reuse Decision Making and (iii) Decision Implementation. In reality, the process is far less segmented, and envisions continuing parallel activities on the part of the military department and the LRA, which, if not iterative in nature, at least involve significant continuing communication between the two as each party exercises its planning and decision making functions. Many of the planning activities on the part of the local community are undertaken well before the formal application by, and selection of, the LRA as the designated transferee of the site and before the submittal and approval of its redevelopment plan.

The planning phase begins when the relevant military department determines and publishes a notice as to which portions of the base will not be needed by the DOD or another Federal agency and therefore are available for transfer to an LRA, or otherwise, as excess property. At about the same time, the military will establish and begin consultation with a BRAC Cleanup Team, composed of a BRAC environmental coordinator (an official of the military department) and representatives of the regional office of the U.S. Environmental Protection Agency ("EPA") and State environmental agencies. In addition, the department must establish a Restoration Advisory Board ("RAB"), composed of representatives of both the military and affected community groups. While the RAB has no official jurisdiction over the cleanup process, it is viewed as an important vehicle for stakeholder input into site characterization and remediation planning.

The first step in remediation planning is the undertaking by the military of an Environmental Baseline Survey ("EBS") which "characterizes" the site by identification of environmental conditions. The EBS is a study not unlike the so-called Phase 1 environmental assessment frequently used in environmental due diligence for private party real estate acquisitions. It includes the results of a physical inspection of the property, a chain of title search, interviews with current and former base occupants and employees and comparable investigations, exclusive of site drilling, sampling or testing.

All of these events normally occur within six months following final determination of base closure.

During the following six months, the LRA normally publishes or otherwise disseminates notices to interested public agencies, soliciting indications of interest for use of the site. Within six to twelve months thereafter, the LRA prepares a formal reuse or redevelopment plan (the "Reuse Plan"). By law the Reuse Plan is required to balance community and economic needs and to take into consideration remediation planning and other environmental concerns. The Reuse Plan is then submitted to the military department and circulated to other relevant agencies, including the federal Department of Housing and Urban Development ("HUD"), a process that may take an additional 6 to 12 months.

Finally, within twelve months following submittal of the LRA's Reuse Plan, the military department completes and publishes its environmental impact analysis of the conveyance and proposed reuse, either (i) by a Finding of No Significant Impact ("FONSI") based on an initial Environmental Assessment ("EA") or, (ii) far more likely, by an Environmental Impact Statement ("EIS"), under the National Environmental Policy Act ("NEPA"). The EIS is required by law to evaluate impacts of any proposed actions upon natural and cultural resources, including wetlands, endangered species, historic structures and Native American sites, among others.

The completion of the EIS, even with its twelve month deadline, is, as in other real estate development contexts, the procedure which is most likely to delay conveyance and commencement of development of a former military site. It includes an initial assessment of potential environmental impacts, public scoping of the impacts to be studied, the preparation and circulation of a Draft EIS and the approval of a Final EIS which responds to issues raised in public hearings and written public comment addressed to the Draft EIS. The EIS process and documentation are often combined with review and approval of the Reuse Plan by local authorities under applicable state environmental disclosure laws, such as California's Environmental Quality Act or New York's Environmental Conservation Law.

By this time, the military will have received, in the case of a transfer to an LRA, a formal EDC application. Based on the EBS and the LRA's Reuse Plan, the military department then formally selects the LRA as the proposed transferee of the site. The final determination as to the disposition of property is accomplished by a Record of Decision ("ROD") by the military department, not sooner than thirty days after publication of the Final EIS. The ROD, based on the Final EIS, includes the identification of the transferee, the disposition method chosen, possible alternatives considered and their environmental impacts, and proposed mitigation measures.

From the foregoing, it is evident that the entire planning and decision making process, from closure selection to a Final EIS and ROD, may in the best of circumstances take at least two to three years. As a practical matter, experience indicates that it takes much longer.

Interwoven in the activities leading to the final ROD is in many ways the most important (at least to the developer) part of the process — namely, the establishment of the BRAC Cleanup Team ("BCT") and the creation of the BRAC Cleanup Plan ("BCP"). The BCT is legally required to work closely with the LRA and the RAB to develop priorities and make mutually acceptable decisions. Ideally, the result is a BRAC Cleanup Plan more or less compatible with the LRA Reuse Plan. That said, because of differing views on the part of the military department and the LRA with regard to the scope of the "reasonable" site remediation required by BRAC law, and the fact that the military ultimately controls the outcome, the Cleanup Plan and the Reuse Plan are rarely congruent.

The traditional method for implementation of the foregoing planning and decision-making phases calls for the completion of hazardous materials remediation prior to conveyance. This phase begins with the identification by the military department, in consultation with EPA and State regulatory agencies, of portions of the base reuse site which are shown by the EBS to be "uncontaminated." The military must make this determination within 18 months after the date of closure designation and its decision is reflected in either a Finding of Suitability to Transfer (FOST) or a Finding of Suitability to Lease (FOSL). Portions of the site that are not initially determined to be uncontaminated are programmed for remediation in accordance with the BRAC Cleanup Plan and later disposition. In either case, no transfer can occur prior to the issuance of a FOST or FOSL for the property in question.

When the property to be conveyed is uncontaminated or cleaned up to unrestricted standards for any potential land use, the issuance of a FOST is a rather straightforward, albeit challenging, task. Often, however, a remediation program will be "risk based"; that is, based on a level of clean up compatible with some, but not necessarily all, land uses and resultant exposures to hazardous materials. The most frequent distinction in this regard is remediation of some portions of a site to unrestricted residential standards (such as to allow single-family houses with lawns and vegetable gardens) and other portions for commercial or industrial uses (where, for example, soils contact is limited or avoided.) In the latter case, BRAC Cleanup Plans will normally include permanent land use and development deed restrictions, commonly known as "Institutional Controls." The negotiation of such restrictions, which often include constraints not only on uses but also upon excavation and construction methods, can be the most daunting of the issues that are negotiated among the military department, the LRA, the environmental regulatory authorities, and, if present, the developer.²

² The potential conflict between federal clearances for transfer and state environmental regulation is an important and complex aspect of the process. As a consequence of the federal supremacy clause, DOD enjoys a preemption of state environmental laws, which is not available to subsequent owners and users. In

The interplay of divergent interests and various benchmark events in the processes leading to a disposition ROD is only the starting point for the potential developer, who may or may not be an identified player at the time. As noted, where conveyance is to an LRA, the other major component of the reuse process is the redistribution of property from the LRA to the private developer. This aspect frequently begins with a "beauty contest" solicitation of Requests for Qualifications (RFQs) or more detailed Requests for Proposals (RFPs) from various interested parties, leading to the selection of one or more developer entities. Too often this occurs only after a Reuse Plan and a BRAC Cleanup Plan based on it are well underway or fully complete. This linear approach results in separate planning processes and the negotiation of sequential transactions between the military department and the LRA and between the LRA and developer. The result can be disadvantageous for both the developer and the LRA in that a fixed Reuse Plan and the implementing BRAC Cleanup Plan may create limits on the introduction of innovative land use programs and the shift to market driven alternatives which are the very purpose of privatizing development. A "public/private partnership" approach for avoiding some of these problems is discussed below.

While the FOST approach has been the paradigm for base reuse, increasingly LRAs and developers have been prepared to negotiate what is commonly known as an "Early Transfer." Concerned about the time delays in a cleanup program undertaken by the government and desirous of obtaining control of the property for predevelopment or early development activities, LRAs and developers may negotiate a program for conveyance prior to cleanup, with a government funded, fixed price cleanup contract entered into with a private environmental remediation contractor. Where such contracts are adequately scoped and funded, and such funding may be utilized in a flexible fashion, this approach also avoids many of the constraints imposed by a predetermined Cleanup Plan and allows for replanning a site based on contamination discovered in the course of cleanup, changing real estate markets or other needs to revisit and revise the long term redevelopment plan.

The balance of this paper focuses on developer concerns and responses which are particularly relevant to military base reuse development, and a fuller analysis and a comparison of the merits of alternative conveyance methods.

order to avoid disparate views of environmental remedial responsibilities, LRAs and developers often pursue a FOST concurred in by state environmental regulators. Even when a "concurrent FOST" is established as a condition of transfer, difficult issues remain as to the scope and duration of Institutional Controls and the language of deed disclosures regarding unremediated conditions, each of which have obvious impacts on the development and marketing of the property.

III. STATUTORY PROTECTIONS AND METHODS FOR MINIMIZING ENVIRONMENTAL LIABILITY

In the typical situation of redevelopment of a contaminated reuse site, the sources of potential liability to the developer as a result of environmental conditions are numerous. They include (i) exacerbation of contamination during remediation activities or construction; (ii) increased costs of development associated with contamination left on the site by the government; (iii) liability as an owner (or "operator") of a contaminated property based on residual contamination at the site after the remediation is completed and (iv) exposure to third-party tort claims as a result of perceived injuries due to residual contamination following completion of development. These risks vary depending on the methods chosen for property transfer and whether remediation is undertaken before or after conveyance.

A. Statutory Covenants to be Given by the government

The Comprehensive Environmental Response, Compensation, and Liability Act ("CERCLA")³ places certain restrictions on the conveyance of federally owned properties to non-federal parties. Generally, Section 120(h) of CERCLA requires the United States (usually, a branch of the military) to take all remedial action necessary to protect human health and the environment with respect to any hazardous substances on federally owned property before it can be conveyed by deed to any other person or entity. The deed transferring the property must include a covenant that all necessary remedial action "has been taken" before the date of conveyance, and that any additional remedial action found to be necessary after the date of the transfer shall be conducted by the government. All necessary remedial action is deemed to have been taken when an approved remedial design has been constructed, and EPA determines that the remedy is operating properly and successfully. CERCLA also requires that the conveyance deed include a clause granting the government access to the property in any case in which remedial action or corrective action is found to be necessary after the date of the transfer.

The CERCLA covenant requirement applies to "any real property owned by the United States on which any hazardous substance was stored for one year or more, known to have been released, or disposed of."⁴ Additionally, similar covenant requirements apply to any closed or closing military installation subject to a BRAC "on which no hazardous substances and no petroleum products or their derivatives were known to have been released or disposed of."⁵ As a consequence, the government will be required

³ 42 U.S.C. § 9601 *et seq.*

⁴ 42 U.S.C. § 9620(h)(3)(A), generally cited as "Section 120(h)".

⁵ *Id.* at § 120(h)(4)(A), (E).

to give these covenants for clean as well as contaminated portions of the site, notwithstanding the fact that there may be no known history of hazardous material or petroleum releases or disposal.

The CERCLA covenant requirement will protect the developer from costs associated with remediating contamination not identified at the time of transfer, and those associated with known contamination which the EPA or other regulatory agency subsequently requires to be performed as a result of more stringent regulatory standards or additional data concerning the potential human health or environmental impacts of the contamination. Often, however, the government will take the position that any contamination that EPA or the State agencies do not require to be cleaned up prior to transfer — such as contaminated soils below the depth to which remediation was required to be conducted — is not the obligation of the government, but a cost of development. Whether government responsibility extends further, and what the remedies for breach of this covenant are, have yet to be defined by the Courts. Risk management strategies for dealing with these uncertainties are discussed below.

B. Statutory Indemnification by the Government

Section 330 of the National Defense Authorization Act for Fiscal Year 1993, Public Law 102-484, as amended ("Section 330"), requires the government to indemnify the transferees of a reuse site from claims for personal injury or property damage resulting from or related to the government's contamination of a reuse site. Specifically, Section 330 requires that the Secretary of Defense

shall hold harmless, defend and indemnify in full [any state, subdivision of a state or other person who acquires ownership or control of any facility that is closed pursuant to a base closure law] from and against any suit, claim, demand or action, liability, judgment, cost or other fee arising out of any claim for personal injury or property damage (including death, illness, or loss of or damage to property or economic loss) that results from, or is in any manner predicated upon, the release or threatened release of any hazardous substance, pollutant or contaminant, or petroleum or petroleum derivative as a result of Department of Defense activities at [a reuse site].⁶

As in the case of the Section 120(h) CERCLA covenant, the indemnity provision does not apply to persons and entities that contributed to any release or threatened release.

⁶ 10 U.S.C. § 2687

The statutory indemnity to be given by the government is intended to protect the transferees (the reuse authority, the developer and any subsequent transferees) from claims arising under CERCLA and other claims, whether brought by the EPA or third parties. The provision includes an obligation to defend the developer and others from such claims, as well as to indemnify for such claims, so long as the developer has not itself contributed to the release or threatened release of hazardous materials at the site. As with the CERCLA covenant, the scope of the Section 330 indemnity has yet to be judicially tested or defined.

C. Separate Entity Formation

A customary and traditional method for reducing exposure to legal liability involves the formation of a separate entity to engage in a particular activity or to acquire a particular parcel of property. Although the separate legal entity generally takes the form of a corporation or a limited liability company, other structures (i.e., limited partnerships, trusts, etc.) are used from time to time depending upon the circumstances.

1. CERCLA Liability

The principal area of exposure for the developer and its successors is for costs incurred by the government or private parties to remediate contamination which was caused or contributed to by the developer or its agents. This could happen if existing environmental conditions are exacerbated during remediation or development activities, either as a result of preconveyance involvement of a developer in remediation or other on-site activities or in the context of early conveyance and ownership prior to completion of third party remediation activities. In the event that the developer's conduct contributes to, but is not the sole cause, the government retains its obligation to provide a defense to any claims asserted against the developer. However, the government is entitled to seek contribution proportionate to the developer's relative share of responsibility for the contamination giving rise to the claim for indemnity. In all events, as a practical matter, acquisition of title to contaminated property is likely to subject the current owner to joinder in litigation brought against all other owners in the chain of title and create an affirmative burden of showing that the developer or its successors are not the responsible party.

As noted, the customary approach to insulating the developer from potential CERCLA and other liability is the formation of a separate corporation, limited liability company or similar entity structured to implement remedies as needed based on contaminants encountered in the field, and to assume all related liabilities, either as the owner of the site or as the party undertaking preconveyance activities.

2. Avoiding Liability for Subsidiary Entities' Actions

The United States Supreme Court recently enunciated in United States v. Bestfoods the standards for assessing the liability which a parent company may incur under CERCLA for the disposal of waste by its wholly owned subsidiary.⁷ Although the developer may form an entity which is farther removed from its own assets than a wholly owned subsidiary, Bestfoods is still the most instructive case regarding the potential liability a parent entity could incur as a shareholder or member of a limited liability entity which conducts the site cleanup or takes ownership of a contaminated site.

a. Derivative Liability Based on Ownership of Developer

According to Bestfoods, a parent company "that actively participated in, and exercised control over, the operations of a subsidiary may not, without more, be held derivatively liable as an operator of a polluting facility owned or operated by the subsidiary, unless the corporate veil may be pierced."⁸ This conclusion is based on the "general principle of corporate law . . . 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."⁹

The Supreme Court inferred from Congressional silence that CERCLA did not intend to abrogate this fundamental common law principle.¹⁰ Accordingly, the developer will incur derivative liability as a shareholder or member of the limited liability entity only if the entity veil can be pierced under applicable law of the corporate veil in the case of a corporation.

b. Piercing the Corporate Veil

In Bestfoods, the analysis of derivative liability was dismissed at the appellate level and therefore was not analyzed in detail. However, the Court did offer general principles to follow in determining when the limited liability veil might be disregarded. "[T]he corporate veil may be pierced and the shareholder held liable for the corporation's conduct when, *inter alia*, the corporate form would otherwise be misused to accomplish certain wrongful purposes, most notably fraud, on the shareholder's behalf."¹¹ In other words, the Court requires some indicia of fraud or bad faith on the part of the

⁷ 524 U.S. 51 (1998).

⁸ Id. at 61.

⁹ Id.

¹⁰ Id. at 62.

¹¹ Id.

shareholder in order to pierce the corporate veil or on the part of a member or partner in order to disregard an organizational structure.

There is some controversy over the choice of law applicable to a corporate or other limited liability entity veil analysis for CERCLA liability, which the Supreme Court specifically declined to address.¹² However, both the language in Bestfoods declining abrogation of state common law unless specifically authorized in the statute, and the cases that follow Bestfoods, suggest that state law will govern whether the corporate veil should be disregarded.¹³

Typically there are two requirements for piercing the corporate veil (and by analogy, the limited liability company or other entity veil) under what is commonly referred to as the "alter ego theory": "(1) that there be such unity of interest and ownership that the separate personalities of the corporation and the individual no longer exist, and (2) that, if the acts are treated as those of the corporation alone, an inequitable result will follow."¹⁴

The following is a list of factors (in order of importance) that state courts frequently consider in determining when the corporate entity (or by analogy, another limited liability entity) should be disregarded and the parent equity owners will be held derivatively liable:

(1) Failure to adequately capitalize a corporation; the total absence of corporate assets, and undercapitalization. If the developer fails to adequately capitalize its new entity, the limited liability veil may be pierced to reach the developer's assets. Although this factor alone does not require disregard of the new entity, it is one of the most important factors.¹⁵ A determination of whether an entity is adequately capitalized is a factual one, based upon the needs of the entity.

(2) Commingling of funds and other assets, failure to segregate funds of the separate entities, and the unauthorized diversion of corporate funds or assets to other than corporate uses. The parent entity must ensure that its assets are kept separate and distinct from those of the newly created entity in charge of cleanup. Similarly, the new entity should keep its own business records, and follow its own

¹² Id. at 64 n.9.

¹³ See Carter-Jones Lumber v. Dixie Distributing Co., 166 F.3d 840, 847 (6th Cir. 1999); IBC v. Velsicol Chemical Corp., 1999 US App. Lexis 15140 (6th Cir. 1999); Browning-Ferris v. Richard Ter Maat et al., 195 F.3d 953 (7th Cir. 1999).

¹⁴ Nilsson, Robbins, Dalgarn, Berliner, Carson & Wurst v. Louisiana Hydrolec, 854 F.2d 1538, 1543 (9th Cir. 1988) (quoting Mesler v. Bragg Management Co., 39 Cal. 3d 290 (Cal. 1985)) (emphasis added).

¹⁵ Associated Vendors, Inc. v. Oakland Meat Co., 210 Cal. App. 2d 825 (1962).

business formalities to support the fact that it is a separate and distinct entity from the parent entity.

(3) Holding out by an individual that the shareholder is personally liable for the debts of the corporation. This factor is rarely applicable to a shareholder or member unless it guarantees the debts of the entity or asserts that it is responsible for the cleanup.

(4) Use of a corporation as a mere shell, instrumentality or conduit for a single venture or the business of an individual or another corporation. This factor accords with the statement in Bestfoods requiring bad faith on the part of the shareholder. If the parent uses the new entity purely as a marketing conduit and attempts to "shield itself from liability based on its subsidiaries' activities, piercing the corporate veil is appropriate and the alter-ego test is satisfied."¹⁶ The organizational documents of the limited liability entity and the activities thereof should reflect appropriate good-faith purposes.

It should be observed that a determination of whether the veil of an entity should be pierced is a factual one, and must be analyzed in the context of a particular set of circumstances. While it is possible to identify the factors that courts will consider in determining whether it is appropriate to disregard a legal entity, it is difficult to predict with certainty whether a court will do so.

3. Direct Liability Based on the Parent Entity's Activities

The parent entity may be directly liable under CERCLA regardless of the creation of the limited liability entity if substantial evidence proves that the parent is the actual "operator" for purposes of CERCLA liability.¹⁷ The parent entity may be viewed as an operator of the facility if it undertakes beyond what constitutes normal investor activities, such as controlling day to day affairs of the cleanup, deciding the locations for placement of waste, or establishing specific environmental compliance policies for the site. The Bestfoods Court pointed out that nothing in the statute bars a parent entity from direct liability for its own actions in operating a facility owned by its subsidiary.¹⁸ Under the plain language of the statute, any person who operates a polluting facility is directly liable for the costs of cleaning up the pollution.¹⁹ "This is so regardless of whether that person is the facility's owner, the owner's parent corporation or business partner, or even

¹⁶ John Doe v. Unocal, 27 F. Supp.2d 1174, 1187 (C.D. Cal. 1998).

¹⁷ See Bestfoods, 524 U.S. at 65-66.

¹⁸ See id.

¹⁹ See 42 U.S.C. § 9607(a)(2).

a saboteur who sneaks into the facility at night to discharge its poisons out of malice."²⁰ Hence, the parent entity's own conduct may give rise to CERCLA liability even where there are no grounds for disregarding the corporate or company veil.²¹

The test for direct liability requires an analysis of the relationship between the parent entity and the project site to determine whether the parent can be considered an "operator" for CERCLA liability. According to Bestfoods, "to 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*."²² This language suggests that if the parent entity is performing operator activities such as managing compliance with environmental regulations, then that party may be held directly liable as an operator.

The parent will not be directly liable for "activities that involve the facility but which are consistent with [the parent's] investor status, such as monitoring of [the entity's] performance, supervision of [the entity's] finance and capital budget procedures. . . ." ²³ Thus, the developer may participate in such oversight activities without incurring direct operator liability.

The Seventh Circuit has interpreted Bestfoods narrowly to the effect that a parent corporation incurs direct liability *only* if it manages, directs or conducts the operations of the subsidiary's facility that are *specifically related to pollution*.²⁴ This interpretation, if adopted by other courts, would allow for a greater involvement by the parent in the cleanup or development of the site without incurring direct liability.

Further, under Bestfoods, the fact that officers and directors operated both the parent and the subsidiary was not enough to establish liability under common law or CERCLA for direct liability.²⁵ There is a presumption that the dual officers and directors are functioning as agents of the subsidiary when acting in their subsidiary capacity.²⁶ Accordingly, if an officer of the developer was also an officer of the newly created

²⁰ Bestfoods, 524 U.S. at 66.

²¹ See id. at 66; see also Riverside Market Dev. Corp. v. International Bldg. Prods., Inc., 931 F.2d 327, 330 (5th Cir. 1991).

²² Bestfoods, 524 U.S. at 66 (emphasis added).

²³ Bestfoods, 524 U.S. at 72.

²⁴ North Shore Gas Co. v. Salomon Inc., 152 F.3d 642, 648 (7th Cir. 1998) (emphasis added).

²⁵ Id. at 69.

²⁶ Bestfoods, 524 U.S. at 69.

company, no presumption of direct liability would flow from that relationship. However, if the officers of the parent entity intervened significantly in the environmental affairs of the newly formed entity, but was not an officer of the limited liability entity, the opposite conclusion would result.²⁷

D. Environmental Insurance Policy Coverage

Any of the transfer options chosen by an LRA or developer necessarily includes some risk of future costs or legal liability, despite the government's legal obligations to provide legal defense for and to indemnify the developer or other transferees for environmental conditions remaining at a reuse site. Recently, several insurance companies have entered the environmental coverage market, the terms of coverage for environmentally-based claims have been broadened significantly and premiums have been dramatically reduced. While the following outlines the general coverage types, the options available over and above standard coverages, policy limits and the like, it is important to note that virtually everything is negotiable in this expanding area of insurance coverage.

1. Insurable Risks

Environmental conditions at a reuse site following the government's departure, whether the government has completed remediation or has transferred responsibility for completing remediation to another party, pose potential risks to the developer in the form of increased costs of construction, third party environmental or toxic tort liability, and contract liability. Specifically, some or all of the following potential sources of financial loss to the developer can and should be addressed by some form of insurance coverage, regardless of the mechanism of transfer.

a. Cleanup Costs. In the event that an LRA, the developer or a remediation contractor agrees to perform the remediation at a reuse site, insurance coverage is available to limit the developer's exposure to such costs in the form of: (i) cost overruns for remediation; (ii) new requirements under regulatory orders due to changed conditions (requiring additional remediation after the cleanup was thought to be complete); (iii) discovery of new contaminants (although this should be covered by the government's Section 330 indemnity); and (iv) cleanup liability under CERCLA to the extent not covered by the government's indemnity (caused, for example, by exacerbating environmental conditions during developer-controlled remediation or as a result of development activities).

²⁷ Bestfoods, at 71.

b. Tort Liability. Common law establishes that the owner or operator of property may be held liable to third parties (such as future tenants, transferees or residents) for bodily injury or property damage under theories of nuisance, trespass, waste, negligence or strict liability. These potential liabilities, to the extent not adequately addressed in the government's indemnity under Section 330, should be minimized or eliminated by appropriate insurance coverage.

c. Contract Liability. The discovery of previously unknown contamination, or more extensive contamination than anticipated, may prevent the developer from meeting contractual obligations in the course of redevelopment and/or sale/transfer of portions of a reuse site. Contractual liability insurance is available for these circumstances.

d. Natural Resource Damages Claims. To the extent not addressed in the government's indemnity obligation, or to the extent that the developer's actions contribute to claimed natural resource damages, the developer could be exposed to such claims from state or federal agencies. Insurance is available to protect against these claims.

e. Diminution of Property Values. Although the state of information available on a reuse site following the developer's extensive due diligence effort and public disclosures of known problems reduces the risk of claims based on contamination or diminished value, the developer may nonetheless wish to obtain coverage for such claims asserted by subsequent purchasers and neighboring property owners.

f. Loss of Use/Lost Rents/Business Interruption. In addition to costs directly associated with remediation, the discovery of previously unknown contamination, or the release of contaminants (e.g., during remediation) can lead to delay or disruption in use of the property. Prolonged carrying costs and business interruption may be incurred by the developer, and claims of lost use or loss of rent may be asserted by subsequent transferees or tenants. These claims can also be addressed by appropriate insurance.

g. Defense of Legal Claims. Most of the risks described above can include expensive legal defense costs. While such expenses ought to be borne by the government under its Section 330 indemnity obligation in most circumstances, insurance should be obtained to address situations where a claim can be made that the developer's actions have caused the claimed damage, or where the government challenges its obligation to provide a defense.

2. Policy Types and Available Coverages

Until approximately 1996, the two principal policy types available to address environmental liability were the Pollution Legal Liability Policy ("PLL"), and coverage for the environmental services industry known generally as the Contractors' Pollution Liability Policy ("CPL"). Coverages offered under these two policies were fairly limited, and premiums were often cost prohibitive. Since that time, new companies have entered this market sector, introducing three general policy types (the expanded PLL, "Cost Cap" coverage to limit cleanup costs, and secured creditor policies), and the premiums have dropped substantially. The first two of these policies are those that are most relevant to landowners and developers.

Cost Cap coverage is intended principally to limit the exposure to remediation cost overruns for known contamination due to unexpected environmental site conditions, expanded cleanup required due to newly discovered contamination, increases in technology costs, increased cleanup requirements by regulatory agencies and comparable events.

The expanded PLL coverage has been packaged in a variety of formats intended to address unidentified site-specific conditions and resulting liabilities. Those policies are often referred to by such names as Environmental Response, Compensation and Liability Insurance Policy ("ERCLIP") or Brownfields Restoration and Development Policy ("BRAD"), though different providers may use somewhat different titles. The policies are negotiated with a particular site in mind, and coverages may include (i) bodily injury and property damage, (ii) contract damages, (iii) cleanup cost liabilities, (iv) legal defense costs, (v) business interruption/lost rent/loss of use and (vi) diminution in property value.

A variety of policy "enhancements" which are available beyond the basic terms of these policy types should also be considered to limit the developer's cost exposure in a base reuse transaction. In particular, these include (i) coverage for additional insureds (e.g., the government, the reuse authority), (ii) finite risk financing, (iii) development soft costs loss (pollution-related Builder's Risk), (iv) contingent transportation coverage for wastes hauled off-site, (v) full assignability of policy coverage to successors in property title/interest, (vi) asbestos and lead-based paint coverage and (vii) radioactive materials coverage.

3. Limits, Premiums and Policy Periods

The policy limits, premiums and policy periods available have all changed dramatically in the last few years, and are generally subject to negotiation with the carriers. Policies with limits in excess of \$100,000,000 are now available, and policy periods may be from ten to as many as thirty years. Policy payments may be made in

installments, or in a lump sum, as appropriate to the business objectives (such as tax consequences) of the insured.

E. EPA Enforcement Policy Towards Purchasers of Federal Facilities

As a result of the statutory deed covenants and indemnifications described above, EPA has concluded that transferees of federal facilities are not at the same risk for incurring liability vis-à-vis the United States under CERCLA as are prospective purchasers of privately owned property. As a result, EPA has determined that the Prospective Purchaser Agreement often negotiated in connection with acquisition of possibly contaminated property²⁸ is not necessary for landowners and transferees of federal facilities. Instead, EPA has adopted its "Policy Towards Landowners and Transferees of Federal Facilities" (June 13, 1997) ("EPA Policy"). This policy is intended "to promote the expeditious transfer and reuse of real property where the United States has ceased Federal government operations [and to implement] the President's initiatives to facilitate the redevelopment and reuse of closing military bases and Brownfields." Specifically, the EPA Policy provides that

[i]t is the Agency's position that where a person or entity acquires property from the United States that is subject to the covenants provided in Sections 120(h)(3) or 120(h)(4) of ... CERCLA ... or the indemnity provided ... [by Section 330], EPA will not take enforcement action against that person or entity, or its transferees or successors ..., to require the performance of response actions or the payment of response costs incurred to respond to contamination existing as of the date that person or entity acquires the property from the United States. However, EPA may take a CERCLA enforcement action against landowners and transferees who cause, contribute to, or exacerbate the release or threat of release of any hazardous substances, through act or omission, and EPA may seek information and access from any person pursuant to CERCLA.²⁹

The EPA Policy specifically indicates that EPA may take enforcement actions against owners or transferees of federal facilities to protect human health and the environment under certain circumstances, "such as when development or activity on the

²⁸ A Prospective Purchaser Agreement is a vehicle for potential purchasers who are not responsible for pre-existing property contamination to contract with EPA for a "covenant not to sue" or other limits on regulatory enforcement in consideration of monetary payments, property use restrictions, specified remedial actions and/or other commitments on the part of the prospective purchaser. (See 54 Fed. Reg. 34235, 34241 (1989))

²⁹ EPA Policy at 1.

property exacerbates the existing contamination, interferes with, or is inconsistent with, a federal response action, or poses a health risk to the community."³⁰ In other words, as is the case with the statutory indemnity and covenant obligations of the government, the EPA Policy does not protect the developer from liability associated with any of its own actions, or those of its contractors, that result in a worsening of existing environmental conditions at the site.

For developers who nonetheless seek the protection of a prospective purchase agreement, in recognition of the environmental benefits of encouraging the remediation and redevelopment of contaminated properties, in 1995 EPA issued its revised "Guidance on Agreements with Prospective Purchasers of Contaminated Property."³¹ That document describes the five criteria that must be met in order for EPA to enter into an Administrative Order on Consent with a prospective purchaser of contaminated property. Those administrative orders, in turn, include a covenant on the part of EPA not to sue for any contamination existing at the time of purchase.

F. Soil & Groundwater Management Plans

As discussed, the statutory covenant and indemnity obligations of the government and the EPA Policy exclude from their coverage any environmental harm caused by the actions of the transferee or developer. The principal mechanism for preventing liability associated with the conduct of the developer or its contractors (or sub-developers) following the property transfer will be the soil and groundwater management plans for the site. These documents are negotiated between the government, EPA, the LRA and the developer, and are referred to in recorded transfer instruments. Transferees of the property take ownership of the property subject to an obligation to comply with the provisions of these plans, and all contractors that subsequently conduct development activities on the site should also be contractually bound to adhere to them. These restrictions obviously affect not only development activities but also subsequent marketing and use of, for example, residential property.

The soil and groundwater management plans identify areas of known contamination, and articulate with specificity the appropriate means for handling contaminated soil or groundwater encountered during construction-related activities. The plans include procedures to protect worker safety in areas where native asbestos- and nickel-containing soils are prevalent, in areas below the levels that soils have been remediated, and in other areas of risk exposure. They describe under what circumstances excavation may proceed to or beyond the depth at which groundwater is encountered, and

³⁰ EPA Policy at 5.

³¹ 60 Fed. Reg. 34792 (1995).

procedures for disposal of contaminated soils or groundwater removed during construction. The plans also set forth protocols to be followed when previously undiscovered contaminants are encountered in the course of development, including the procedures for ensuring prompt government response to address such contaminants.

Strict adherence to the soil and groundwater management plans, in combination with the statutory protections described above, will further protect the developer and its transferees from liability associated with contamination by preventing the accidental exacerbation of environmental conditions present at the site during construction.

G. Increased Development Costs Related to Residual Contamination

Under each of the transfer models described in this paper, the developer will face the potential for increased construction and other costs associated with contamination to be left on site at depths beyond which the government has not been required to remediate, or otherwise not remediated, under an approved Cleanup Plan. Some of the cost impacts associated with encountering contaminated soils or groundwater can be reduced by employing newer technologies for pile driving, innovative design approaches (such as spread footings rather than traditional foundation techniques), or by redesigning the redevelopment plan and related construction methods altogether to avoid such contamination. Some risks and costs may also be reduced, although not necessarily eliminated, by one or more of the insurance coverages described above. Finally, in the case of an Early Transfer, as discussed below, the developer may be able to shift some of these costs to the government by negotiating sufficient cleanup funds to perform remedial work that exceeds the cleanup levels and/or soil excavation depths proposed by the government or by obliging the remediation contractor to undertake a scope of work in excess of the government's approved Cleanup Plan.

IV. MINIMIZING LIABILITY ASSOCIATED WITH VARIOUS ALTERNATIVES FOR TRANSFER OF REUSE SITES

The following examines three alternatives for completing the remediation of a reuse site and the conveyance of that site to a reuse authority or the ultimate developer. The first two, involving a FOST and FOSL, respectively, are really variations on the same approach; that is, remediation of toxics prior to conveyance in the case of a FOST, or, in the case of a FOSL, an interim lease pending ultimate transfer under a FOST. The third, involving early transfer with a FOSET, is decidedly different, insofar as it contemplates an early conveyance of fee title with a program for post-closing remediation.

A. Transfer by Finding of Suitability to Transfer (FOST) or Finding of Suitability to Lease (FOSL)

1. Transfer by Finding of Suitability to Transfer

Under the FOST approach, historically the standard method for the military base conversion, the government undertakes remediation of hazardous materials and toxic conditions, the formal confirmation of cleanup by appropriate regulatory agencies and the conveyance by a deed including both environmental covenants and indemnities as a prerequisite of transfer.

This process and these protections are described above. In brief, the transfer of contaminated federal facilities to non-federal ownership, including the responsibility for cleanup of such facilities, is governed by CERCLA. To comply with CERCLA, DOD has developed procedures for making the required Finding of Suitability to Transfer or FOST, which includes (i) notifying state and federal regulators, (ii) evaluating all information about the environmental condition of the parcel, (iii) determining the suitability of the parcel for transfer and preparing a draft FOST, (iv) circulating the draft FOST for public and regulatory comment and (v) finalizing and executing the FOST.

The objective of the FOST approach from the perspective of the LRA and/or developer is to require the military to take all responsibility for the remediation of a project site or a parcel within the site. Although under CERCLA the government is required to take all necessary remedial action and is ultimately responsible for the cost of the remediation, there is always the possibility that timely remedies for enforcing the government's obligations in a postclosing context will not be available or that unexpected additional costs will be incurred during cleanup. There is also a risk that the remediation process itself may exacerbate environmental conditions or cause environmental harm. If the military performs the cleanup, the government takes the risks of unexpected additional costs and any environmental harm caused by the remediation.

On the other hand, as noted, if the military department is in charge of all remediation, the LRA and developer will continue to have almost no control over the speed at which the remediation takes place, nor will the developer have the ability to direct those cleanup operations to ensure they are compatible with the applicable reuse plan. There is ample empirical evidence that delays in remediation and thus development are likely.

The primary risk in the FOST approach is the possibility that preclosing remediation by the government will be incomplete or inadequate and that the developer's subsequent ownership or post closing activities will subject it to liability under CERCLA which is not covered by the Section 330 indemnity. As discussed, there are essentially three ways to minimize such risks. The first is for the developer to undertake an appropriate due diligence to assure that remediation of known conditions is adequate

notwithstanding regulatory clearances and that no other unknown conditions exist. The second is the formation of a separate entity to acquire title to land. The third is the negotiation and purchase of a specially crafted insurance package.

2. Transfer by Finding of Suitability to Lease

FOSLs are used in two principal situations. The first is in the case of an "Interim Lease" to an LRA or other local public agency for a term not to exceed five years, and usually entered into prior to final disposal decision or ROD with a view toward reducing the government's operation and maintenance costs pending final determination of ultimate property disposition.

The second, and by far the more common use of a FOSL, is to facilitate a two-step conveyance of the site to the LRA and, through a sublease to the developer, to allow predevelopment and early development activities, and to shift the economic burdens of maintenance and security pending completion of cleanup. These longer term leases are known as Leases in Furtherance of Conveyance (LIFOCs). In such cases, the parties rely on the fact that CERCLA Section 120(h)(3)(B) exempts property transfers from the covenant requirements of Section 120(h)(A)(ii) (see above) in cases where the transfer of the former base property occurs by means of a lease.³² This exemption applies regardless of whether the lessee has agreed to ultimately purchase the property, or whether the duration of the lease is longer than 55 years.³³ For leases entered into after September 30, 1995, the department or agency leasing the closed or realigned military base property, in consultation with EPA, must determine that "the property is suitable for lease, that the uses contemplated for the lease are consistent with protection of human health and the environment, and that there are adequate assurances that the United States will take all remedial action referred to in [Section 120(h)] Subparagraph (A)(ii) that has not been taken on the date of the lease."³⁴

In December 1977, DOD issued its Policy on the Environmental Review Process to Reach a Finding of Suitability to Lease (FOSL) ("FOSL Guidance"). The objectives of the FOSL Guidance are (i) to develop a DOD-wide protocol to assess, determine and document the environmental suitability of properties for leasing to non-federal entities, (ii) to ensure that such leases do not interfere with the environmental cleanup of such parcels, (iii) to ensure compliance with all applicable environmental requirements and establish the basis for the DOD to notify lessees regarding the presence

³² 42 U.S.C. § 9620(h)(3)(B).

³³ See id.

³⁴ See id.

of hazardous materials and petroleum products on the property and (iv) to provide adequate public and regulatory participation in the outleasing of closed and realigned facilities.

As with the FOST procedure, the FOSL Guidance requires that the federal leasing agency conduct an environmental assessment of the property based on an Environmental Baseline Survey (EBS), and document its findings in the FOSL. In order to make a determination that the property is suitable for lease, the military must make one of the findings specified in the FOSL Guidance. On parcels where contamination has existed and remediation is not yet complete, the military must find that although a hazardous substance notice must be given, the property can be used pursuant to the proposed lease, under the specified use restrictions in the lease, with acceptable risk to human health or the environment and without interference with the environmental restoration process. The specific use restrictions must be listed in the FOSL.

The government must provide certain notices to regulatory agencies at the initiation of the EBS and the FOSL. It must notify the state in which the property is located prior to entering into any lease that will encumber the property beyond the date of termination of DOD's operations. Finally, the government must notify the public of the signing of the FOSL. The lease must include conditions to ensure that remedial activities will not be disrupted. Model lease provisions are provided by the FOSL Guidance.

Under the FOSL scenario, the government remains liable and responsible for completing all remedial activities on a particular parcel. However, as noted, the government can give the LRA and/or the developer access to particular parcels or lots to begin development where the appropriate findings are made.

The FOSL process is similar in many respects to the FOST procedure described above, except that less public notice and less formal regulatory agency participation is required and, in most cases, an EIS will not be necessary. The primary benefits of the interim leasehold approach is that the developer is able to obtain earlier access to the site in order to begin development before remediation of the entire parcel is completed. The FOSL transfer may prove particularly useful for parcels of the property on which remediation is complete, although the entire site is not cleaned up and phased conveyance of fee title is not possible or practicable.

A FOSL transfer involves the same principal risks as are associated with a FOST conveyance, and has additional risks as well. These include (i) the possibility that the developer's presence or work on a parcel before cleanup is completed could involve it, its contractors or the public in cleanup activities and accrue CERCLA or other liability; and (ii) the risk that the government will not complete cleanup as expeditiously if portions of a parcel are available for private use and the cost of operation and maintenance of those portions has been shifted to others.

The ways to minimize some of these risks are similar to those described above. They include formation of a separate entity to undertake the cleanup and hold leasehold title to land; the purchase of a specially crafted insurance product, probably with higher coverage amounts due to the increased numbers of persons potentially affected by cleanup activities; and contractual indemnities from the developer's own contractors or subtenants who are present on the site.

B. Conveyance under a Finding of Suitability for Early Transfer (FOSET)

1. Objectives and Process

Under the "Early Transfer" scenario, the military transfers all or portions of the reuse site to the LRA, or to the developer or a specially formed, limited liability entity prior to completion of environmental remediation. It does so by means of a Finding of Suitability for Early Transfer or FOSET for sites not included in the National Priorities List ("NPL") or by a Covenant Deferral Request ("CDR") for NPL sites. The remediation typically is funded by the government, but implemented by the LRA, the developer or its limited liability subsidiary, or, more commonly, an independent remediation contractor, under a fixed price arrangement, with environmental insurance Cost Cap coverage to ensure completion of the work.

As noted, the principal reasons that developers and LRAs consider Early Transfer of the entirety or portions of former federal facilities are (i) to take control of remedial activities, thereby ensuring that all cleanup is performed to a level supportive of planned reuses, (ii) to design and phase remedial activities to be integrated with development of the site thereby reducing costs, (iii) to accelerate completion of remediation and (iv) to expedite transfer of possession of the property to the developer.

2. Legal Bases for Early Transfer—CERCLA Section 334

CERCLA permits the transfer of contaminated federal facilities prior to completion of remedial activities under specified circumstances. Under the Early Transfer provisions which appear as Section 120(h)(3)(C) of CERCLA³⁵, the required finding that the government has completed all necessary remedial actions may be deferred until after transfer where the property is suitable for the proposed use, the intended use is consistent with protection of human health and the environment and arrangements have been made to ensure that all necessary response actions will be taken. This latter requirement includes committing to a schedule and a funding source for the necessary remediation.

³⁵ Section 334 of the Fiscal Year 1997 Defense Authorization Act (Pub.L. 104-201).

The principal steps involved in an Early Transfer are not dissimilar to the FOST approach, but with several decisive differences. The first action after the establishment of an LRA and its engagement with the military service that owns the reuse site is the assembly of a "review team," consisting of the BRAC cleanup team (BCT) (the constituency of which is the same as that selected for a FOST transfer, with the addition of the real estate office of the particular military branch and representatives of the LRA). The LRA, working with the government and utilizing an EBS, undertakes to identify property suitable for early transfer and the intended use of that property. The FOSET package is then developed and refined based on an approved Reuse Plan, which may include proposed Institutional Controls much the same as those described above with respect to the FOST conveyance.

Both the FOSET and the CDR must include an analysis of the early transfer proposal, a description of the contaminants identified by the EBS, the proposed remedial action plan and schedule for completion, and the intended interim use of the site by the transferee pending completion of cleanup. The CDR or FOSET package must also include a form of deed and conveyance agreement which address the schedule and funding of cleanup, any proposed interim or long term Institutional Controls, assurances of response to newly discovered toxic conditions and the right of governmental access to the property for responsive actions. The procedure includes the same circulation to and input by the RAB, the regional office of EPA, state environmental agencies, local governments and other community "stakeholders" as applies to the FOST procedure. Prior to conveyance, both the FOSET and the CDR must be concurred in by the Governor of the state in which the site is located and, in the case of an NPL property, the CDR must also be concurred in by the EPA. Once all necessary remedial action has been completed on a property subject to Early Transfer, the government must issue a warranty that satisfies the CERCLA covenant requirement described above.³⁶

3. Early Transfer Documentation

Concurrently with the foregoing Early Transfer process, the LRA, ideally in close consultation with the chosen developer, will normally undertake negotiation of several critically important agreements. The first is the Conveyance Agreement between the government and the LRA, which spells out the rights and obligations of the parties regarding conveyance, remediation, easement grants, closing procedures, and other matters typically included in a real estate purchase and sale agreement. Frequently the formal Conveyance Agreement is preceded by a Memorandum of Agreement ("MOA") outlining the terms of the transaction. With some exceptions, the Conveyance Agreement is essentially the same as that utilized in a FOST transfer.

³⁶ Id. at § 9620(h)(3)(C)(iii).

Another key document with respect to an Early Transfer transaction is the Environmental Services Cooperative Agreement ("ESCA") between the government and the LRA, which sets forth in detail the allocation of responsibility and respective obligations of the parties with regard to post-closing remediation activities and funding. The ESCA, among other things, documents the government's obligations and conditions for funding remediation and identification of known and unknown toxic conditions for which the military will have ongoing responsibility. The ESCA should provide for joinder by, or assignment of benefits to, the developer.

As noted above, a FOST concurred in by state environmental authorities is an important vehicle for achieving comprehensive regulatory clearance of a remediation program. The method for accomplishing this in a FOSET context is the execution of a Consent Agreement by and among the state regulatory agencies, the LRA and the developer, specifying the contaminated areas and conditions, a site remediation strategy, a clean up schedule or provision for developing such a schedule, and a Remedial Action Plan. The Consent Agreement thereby creates a degree of finality for an approved remediation program, which most developers will insist upon as a condition to property acquisition.

The other critical document in the typical Early Transfer scenario is the guaranteed maximum fixed price remediation contract entered into between the LRA and/or developer and the remediation contractor (the "Remediation Contract"). The Remediation Contract sets forth the obligations of the contractor to complete an agreed upon scope of work, and other obligations of the parties to complete and pay for the remediation work. This agreement raises important issues comparable of those involved in traditional construction contracts, including the definition of scope of work, the need for clarity of the remediation specifications, allowance for change orders and *force majeure* provisions, among others. Performance of the Remediation Contract is typically insured by Cost Cap insurance for cleanup of identified conditions. This insurance is complementary to PLL insurance coverage (discussed above), which ensures against unknown or subsequently discovered toxic conditions. The developer should be a party to, an assignee of, or otherwise a beneficiary of the rights and obligations under the Remediation Contract and a direct insured under the environmental insurance policies.

It is important to note both the distinction between, and interplay of, the functions of the Remediation Contract and the ESCA. The ESCA funding agreement, while based upon the LRA's original Reuse Plan, is for an agreed amount of money as fulfillment of the government's initial remediation obligation, and not necessarily for a given reuse program. The Remediation Contract scope of work may or may not be the same as the remediation program and Reuse Plan contemplated by the FOSET, either because the scope of the work may have changed or the Reuse Plan may be revised because of the input and modifications of a subsequently selected developer or for other reasons. It is crucial to the interests of the LRA and/or developer that maximum

flexibility be preserved for use of remediation funds, and that no particular remedial techniques or standards are prescribed; otherwise cost savings resulting from changes in the reuse plan that reduce environmental exposures and remediation expense in one area (e.g., a change from residential to commercial/industrial) may not be available for increased remediation costs, or shortfalls in available proceeds, elsewhere on the site. Thus, normally an amount of remediation funding is negotiated under the ESCA, while Institutional Controls, which dictate how those funds will likely be spent, are established later at the time of regulatory signoffs. Absent contrary specification in the ESCA, this approach allows for maximum flexibility in the use of government funding.

4. Protections for the Developer from Liability

There are some risks associated with Early Transfer that are not present, or present only to a lesser extent, in the other transfer scenarios described above. Most significant among these are:

- (1) the risk that the funds negotiated for cleanup of the site could be inadequate to complete remediation or that such funds will not be appropriated by the government in a timely fashion or at all;³⁷
- (2) the potential that remediation activities might subsequently be alleged to have exacerbated an existing environmental condition, thereby imposing some liability on the developer for resulting cleanup costs or third party damages under CERCLA;
- (3) the fact that early transfer of fee title to the developer entity would technically subject that entity to environmental liability to third parties as an "owner" or "operator" under CERCLA, as well as to toxic tort claims brought by third parties based on perceived risks resulting from contamination remaining on site after redevelopment; and
- (4) the risk that having once conveyed the property, the government will be less motivated to complete clean up or promptly respond to newly discovered problems.

³⁷ While a commitment from DOD would seem a reliable and creditworthy source of remediation funding, it must be remembered that every contractual obligation of a federal governmental agency is contingent directly or indirectly upon Congressional appropriations and subject to the federal Anti-Deficiency Act (31 U.S.C. §§ 1341.), which precludes a federal officer or employee from "[making or authorizing] an expenditure or obligation exceeding an amount available in an appropriation or fund for the expenditure or obligation." Legislatively earmarking, or otherwise assuring the availability of funds, is frequently a key element of DOD/LRA Conveyance Agreements.

These risks can be mitigated by a combination of the risk management tools described above. Specifically, as noted, the total cost of remediation can be limited by Cost Cap insurance coverage coupled with a fixed price cleanup contract. Third party liability under tort theories or CERCLA can similarly be limited by insurance. Increases in development costs associated with environmental conditions can also be limited by appropriate insurance coverage, and the assets of the developer and its parent/related corporate entities can be protected from potential claims by the formation of a corporate or other limited liability entity. As to other liability risks associated with the Early Transfer model, the government's defense and indemnity obligation, as well as strict adherence to soil and groundwater management plans for the property, will help protect the developer from liability to regulators and others.

C. Benefits of a Partnership Approach to Remediation and Redevelopment.

The legislation of authority for early transfer under CERCLA has become one of the more important tools for accelerating base closure and redevelopment and facilitating early involvement of the private developer in the formulation and negotiation of the remediation and reuse plan. Indeed, the participation of the private developer in these early aspects of the BRAC process is a critical element of a successful outcome, whether the conveyance utilizes a FOST model or is by way of an Early Transfer. In either case, the early engagement of the developer can help formulate a creative land use program based on market factors and other practical considerations, which are not likely to drive the decision making of the LRA, and to which the military department may be utterly indifferent. As discussed above, the ability to shift uses within the developer's market-sensitive alternatives should be crucial to the LRA's objectives in negotiating with the military department and often results in savings to all parties by reducing the overall cost of remediation. This is especially the case if the developer's presence allows for a plan of integrated remediation and development of the site under an Early Transfer conveyance. Having the developer "at the table", or at least utilizing its input, will likely facilitate the LRA's twin objectives of negotiating maximum funding and maximum, *relevant* flexibility, or indeed obviate the need for maximum flexibility by establishment of a realistic and practical reuse plan at the outset.

In addition, early involvement of the developer brings important resources to the LRA's negotiations with the federal government, including negotiating skills and credibility (and occasionally political clout), as well as due diligence expertise and capacity. The ability of the LRA independently to verify existing property conditions and the adequacy of a proposed cleanup plan under a FOST approach or to properly "scope" a fixed price remediation contract under early transfer is often beyond its financial or logistical capacity. In addition, the developer's real estate marketing expertise and experience will allow for identification and modification of problematic Institutional Controls and mandated deed disclosure language which the LRA may not fully appreciate.

In short, from the developer's perspective it is simply too late to become involved in a BRAC transaction only at the time of the DDA or LDDA. As the effective real party interest to the ultimate acquisition and development of the site, the developer cannot afford to inherit unresolved problems or mistakes made by the LRA in its bilateral transaction with the government. Early involvement of the developer benefits the other parties as well.

V. OTHER REAL ESTATE ISSUES PECULIAR TO BRAC TRANSACTIONS

The challenge of BRAC transactions to the developer and its counsel merely begins with the understanding and structuring of the base closure, planning and LRA acquisition process. The negotiation of the ensuing DDA or LDDA agreements and accommodation of development to the reuse process present familiar real estate issues, but also problems that are unusual, if not unique.

The DDA itself is essentially a purchase and sale agreement, but not without its special aspects. Perhaps the most distinguishing characteristics are the land use restrictions and development obligations which govern the post closing period. By the adoption of a local redevelopment plan permanently prescribing uses, the LRA acts both in a proprietary capacity as seller of the property and in a regulatory capacity establishing and enforcing long term land use restrictions. By stipulating a performance schedule for approval and the development of infrastructure and/or vertical improvements, the reuse authority ensures a number of public objectives, including the elimination of blight, enhancement of tax base and creation of tax increment, construction of affordable housing and other public benefits, which often constitute the primary or even sole consideration for the conveyance.

The economic structure of the transaction ranges from (i) a traditional DDA for a below market purchase price with all the costs, risks and benefits of ownership (including those related to infrastructure financing, financing and construction of vertical improvements, cost overruns, market values and project revenues) allocated to the developer to (ii) a full blown economic partnership in which the reuse authority conveys the property at no cost or greatly reduced purchase price, and provides post-closing financing of infrastructure (through tax increment, revenue bond or other public financing) and other investments in return for a significant profit participation in development lot sales to "vertical" developers or the net proceeds of vertical development itself.

The more familiar issues that arise in virtually all real estate development acquisitions, but are more challenging in BRAC transactions, include title matters, land use and subdivision issues, utilities and access easements and environmental matters.

As to the last mentioned, as already discussed, the treatment of the presence of hazardous materials on BRAC sites pervades the planning and acquisition process for

such properties. The allocation of risk between seller and buyer with respect to known and unknown toxic conditions in the typical private party transaction is the subject of considerable, and sometimes heated, debate. Those negotiations, at least in today's market, normally result in "as is, where is" sales, with a disclaimer of representations, warranties and indemnities of any kind on the part of the seller, and mutual releases by each party to the other, with respect to the existence or consequences of any known or unknown hazardous materials. Occasionally, a seller may elicit from the buyer an indemnity against the creation or exacerbation of toxic conditions resulting from buyer's postclosing activities, but, in general, the parties agree not to contractually reallocate hazardous material liability.

In the case of a BRAC transaction, such negotiations are preempted by federal statute; the Section 330 indemnity and the CERCLA § 223(h) cleanup covenant govern the acquisition of property by the LRA, the developer and its successor owners and occupants, whether or not included or referred to in the transactional documents. This, of course, does not obviate the need on the developer's part for an extensive due diligence to identify potential problems and the negotiation of an efficient, timely and adequately financed cleanup plan.

Title issues are again unique in BRAC acquisitions. In private transactions, the seller usually conveys property by a Grant Deed or Warranty Deed, with a title insurance policy subject only to limited, specified exceptions issued as a condition of closing. In the BRAC context, the government conveys title to the LRA or the developer by quitclaim deed, and normally refuses to include escrow closing and title insurance conditions in its Conveyance Agreement with the LRA or developer. Issuance of title insurance must somehow be correlated with the disposition transaction, as opposed to being an express condition to closing.

Land use approvals, subdivision and easement matters are also handled very differently. In the private context, real estate buyers will normally condition closing of acquisition of undeveloped or redevelopable property on some level of land use entitlement — at a minimum, a programmatic approval by the relevant land use regulatory authority. Regardless of preclosing entitlement, local subdivision laws require that no property can be conveyed unless it constitutes a "legal" parcel which has reliable access to public rights of way, is served by utilities and other public services, and is otherwise subject to minimum development standards under local law.

In contrast, in BRAC transactions, the standard government Conveyance Agreement does not include any land use entitlement closing conditions; nor, as a result of federal preemption, is federal property subject to local jurisdictional requirements regarding subdivision and conveyance of real estate parcels. As a result, BRAC property is conveyed in a truly undeveloped or "raw land" condition.

To the extent that the developer takes title to a BRAC site from an LRA, these problems can be addressed by appropriate provisions in the DDA. However, by the time that such conditions prove to be incapable of fulfillment because of problems not identified or resolved in the DOD/LRA transaction, the developer may have expended several million dollars in unrecoverable, preclosing investment.

In general, the military has refused to facilitate preclosing land use approvals, title remedies and related enhancements of its sites. All of these issues would clearly seem to have a significant adverse impact on both marketability and market value of BRAC sites. It will be interesting to see whether such impacts ultimately lead the government to reconsider its traditional approach.

VI. CONCLUSION

BRAC properties present significant opportunities for developers with the economic capacity and patience to deal with the extraordinary challenges. These transactions require considerable preclosing expenditures, without any contractual assurance of recovery if the property is not conveyed. They also require an understanding of, and ability to cope with, unusual federal procedures and practices regarding site remediation and conveyance, and more than the usual number of technical and legal issues. Nonetheless, BRAC transactions provide both local communities and developers the ability to take control of and redevelop important local assets, to mitigate the economic consequences of a local base closure and to realize the ultimate benefits of conversion to civilian uses.