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# Lessons Learned From the Intersection of CERCLA and Contract Law

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In *Blasland, Bouck & Lee, Inc. v. City of North Miami*,[1] the U.S. Court of Appeals for the Eleventh Circuit addressed two significant issues involving the interrelationship between Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA)[2] cost recovery actions and contract law. These issues, and the way the court addressed them, highlight problems for drafters of both commercial contracts and partial settlement releases, which if not carefully done can frustrate the intentions of the parties and cause significant economic loss to at least one of them.

First, in reversing the trial court, the Eleventh Circuit refused to give effect to an express limitation on liability in a contract between the parties. Instead, the court held that one party could use a CERCLA cost recovery action to avoid the contractual limitation on liability and recover precisely the amounts that the parties had agreed in the contract were not to be recoverable.

Second, based on the theory that the claimant may have been seeking to recover the same damages twice, the court held that a release given in settlement of a cost recovery action against generators in a prior CERCLA case barred recovery of damages in a subsequent action against a remedial action contractor for breach of contract. The Eleventh Circuit upheld the trial court's setoff of the total settlement amount in the first case against a jury verdict in the second case, thereby wiping out the recovery. The court did this even though the damages for breach of contract were, as a matter of law, unrecoverable in the CERCLA case that was settled.

Both these holdings carry significant warnings regarding the drafting of commercial agreements in which the parties seek to allocate liability for response costs. Additionally, the holdings may affect releases against one or more defendants when subsequent litigation is contemplated involving claims for losses that relate in any way to the initial settlement. This often occurs in multiple CERCLA settlements. This Dialogue will discuss the implications of the Eleventh Circuit's rulings for both transactional and litigation practitioners.

## Factual Background

### *The Contract Between the Parties*

The city of North Miami owned a 170-acre landfill known as the Munisport Site. In 1985, the U.S. Environmental Protection Agency (EPA) placed the landfill on the national priorities list (NPL)[3] because of ammonia in the groundwater that threatened aquatic organisms in Biscayne Bay and a nearby mangrove preserve. Ammonia is formed by the degradation of vegetative or other organic material and is a hazardous substance[4] under CERCLA.

In July 1990, EPA issued a record of decision (ROD) requiring remedial measures to address the release of ammonia from the site into the mangrove preserve. The ROD called for hydrogeologic studies of groundwater movement beneath the site, including water quality and volume and treatability studies. The studies were to provide the basis for the design of a groundwater barrier and extraction system that would intercept the contaminated groundwater before it reached the mangrove preserve and treat it to remove the ammonia. The ROD also required improvements to the mangrove preserve by breaching a causeway separating it from Biscayne Bay to allow free tidal flow into the preserve.[5] In 1992, the city entered into a consent decree with EPA to perform the remedial design and remedial action (R/D & R/A) required by the ROD.[6]

The city hired Blasland, Bouck & Lee (BB&L) to do the necessary groundwater studies and design the pump and treat system. To secure the funding, the city obtained a grant from the state of Florida. In the city-BB&L contract, the parties specifically agreed that BB&L would not be paid for any of its work unless and until the state approved BB&L's invoices and paid the amounts in question to the city under the grant. This clause, which became known as the "pay-when-paid" clause, provided in pertinent part as follows:

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1. 283 F.3d 1286, 32 ELR 20486 (11th Cir. 2002).
2. 42 U.S.C. §§9601-9675, ELR Stat. CERCLA §§101-405.
3. *See id.* §9605(a)(8), ELR Stat. CERCLA §105(a)(8); 40 C.F.R. pt. 300, app. B. The NPL is a list of sites maintained by EPA which, based on the volume and toxicity of the hazardous substances released to the environment and other factors, warrant investigation and appropriate response action on a high priority basis.
4. *See* 40 C.F.R. §302.4 and tbl. 302.4.
5. *See* 283 F.3d at 1290, 32 ELR at 20486.
6. *See* United States v. City of N. Miami, No. 91-2834 (S.D. Fla. 1992). Attached to the consent decree was a scope of work, which, as is typical with CERCLA consent decrees, embodied the general terms of the R/D & R/A that EPA required in its record of decision.

> CITY shall only be responsible for expeditiously processing . . . payment of such invoices of BB&L through the [Florida Department of Environmental Regulation], and BB&L recognizes that CITY's obligation of payment of compensation is specifically contingent upon CITY's receipt of funding from the [Florida Department of Environmental Regulation] for payment of such fees, costs and expenses of BB&L.[7]

The contract further provided that if invoices were not paid within 45 days, BB&L could suspend services. The contract also allowed the parties to agree to certain "out of scope" work, which was not subject to this "pay-when-paid" clause, and which would be invoiced by BB&L to the city at its normal hourly billing rates.

The contract between the city and BB&L obligated BB&L to carry out the R/D & R/A work "in accordance with the terms of the Consent Decree" between the city and EPA. As is standard practice under CERCLA, EPA assigned a remedial project manager to oversee BB&L's work and make sure that it complied with the consent decree and scope of work. While BB&L performed some of the work properly, it failed to adequately conduct the groundwater studies. As a result, both those studies and the design that BB&L proposed for the pump and treat system based upon the studies were found by EPA to be severely flawed. When BB&L refused to correct these flaws, the city fired BB&L in 1995 and hired another firm to complete the work.

*Trial Court Proceedings*

In 1997, BB&L sued the city for breach of contract and also to recover the unpaid contract amounts under CERCLA. The city counterclaimed for breach of contract and professional negligence. At the trial, the jury awarded BB&L $380,283 for amounts that it found the city should have paid BB&L under the contract. The jury also awarded the city $114,000 on its counterclaim based on professional negligence and breach of contract by BB&L.

BB&L's CERCLA cost recovery claim was tried separately to the court, which used the record of the jury trial plus one additional day of evidence taken on matters relating exclusively to the CERCLA claims, as the record for its decision. The court ruled that BB&L could recover $375,283, which was included in the prior jury award, thus providing a separate legal basis for recovery by BB&L of those same amounts. BB&L also sought to recover an additional $110,800 for three items of work for which the city had refused to pay because the state had declined to pay these amounts to the city.[8] The jury declined to award BB&L these amounts under its contract based on the "pay-when-paid" clause. The trial court in the CERCLA decision similarly held that BB&L could not recover these amounts since it had expressly agreed in its contract that such amounts would not be recoverable from the city unless the city received payment from the state, which it had not.

In 1995, almost two years prior to the BB&L litigation, the city brought a CERCLA contribution action against various towns and companies that had sent waste material (primarily garbage and trash) to the landfill, seeking to recover an equitable portion of its CERCLA response costs from these potentially responsible parties (PRPs). That case was captioned *City of North Miami v. A&E Construction, Inc.*[9] The city settled the *A&E* lawsuit in June 1997, and received in the aggregate just over $1 million from a substantial number of defendants. The city entered into a written settlement agreement with each settling defendant that included a release, specific to that defendant, from any and all claims of liability or contribution arising under the city's CERCLA complaint. These settlement agreements were not before the court, but the *facts* of the settlements and the total amounts were.

Following the jury verdict in the BB&L litigation, BB&L moved the court to set off the total amount of the *A&E* settlements against the city's counterclaim award. BB&L argued that the amounts recovered in the *A&E* settlements must have included amounts that the city sought to recover from BB&L for breach of contract and professional negligence. The Florida setoff statute provides, in pertinent part:

> At trial, if any person shows the court that the plaintiff . . . has delivered a written release or covenant not to sue to any person in partial satisfaction of the damages sued for, the court shall set off this amount from the amount of any judgment to which the plaintiff would be otherwise entitled at the time of rendering judgment.[10]

Though BB&L had made the motion, BB&L did not introduce the settlement agreements and releases from the prior litigation. Therefore, the city argued that because BB&L did not "show" a release or covenant not to sue to the court, BB&L had failed to satisfy a threshold requirement of the statute. The city further argued on the merits that there should be no setoff because the "damages" claimed in each case were entirely different. The city maintained that it was entitled to recover damages for breach of contract from BB&L as measured by the cost that the city ultimately had to pay to have the work correctly performed.[11] The city additionally argued that it had an entirely separate cause of action under CERCLA §113(f)(1)[12] to recover an equitable portion of its response costs against other PRPs, such as the generators in the *A&E* litigation, that the city had incurred over and above its own fair share, as long as those costs were consistent with the national contingency plan (NCP).[13]

7. Blasland, Bouck & Lee, Inc. v. City of N. Miami, 96 F. Supp. 2d 1375, 1377-78 (S.D. Fla. 2000).

8. This included claims for $75,000 for field data acquisition, $31,000 for landfill closure permit application work, and $4,800 for surface water sampling. See the decision of the trial court on the CERCLA claims reported in *id*. at 1378.

9. No. 95-0645-CIV-MARCUS (S.D. Fla. 1995). In addition, in 1992, the city had brought a CERCLA contribution action against the former operators of the landfill and obtained summary judgment as to liability. City of N. Miami v. Berger, 828 F. Supp. 401, 23 ELR 21494 (E.D. Va. 1993). The city then settled that case, based on the defendants' limited ability to pay, for $900,000 and title to a tract of land. That decision provides additional factual background on the Munisport Landfill.

10. FLA. STAT. §46.015(2).

11. *See* Grossman Holdings Ltd. v. Hourihan, 414 So. 2d 1037 (Fla. 1982) (a party is entitled to recover the cost of repairing the defect so that it is in compliance with the contract); Ray v. Dock & Marine Constr., Inc., 183 So. 2d 237, 238 (Fla. Dist. Ct. App. 1966) ("The measure of damages . . . is generally the reasonable cost of making the work performed conform to the contract.").

12. 42 U.S.C. §9613(f)(1), ELR STAT. CERCLA §113(f)(1).

13. *See* 40 C.F.R. pt. 300. The NCP provides the blueprint for site investigations and response actions under CERCLA. For response costs to be recoverable by one PRP against another, the costs must be consistent with the NCP. This includes the requirement that the R/A be "protective of human health and the environment . . . and . . . cost effective." 40 C.F.R. §300.700(c)(3)(ii); *See also* Blasland, Bouck & Lee, Inc. v. City of N. Miami, 283 F.3d 1286, 1295, 32 ELR 20486, 20488 (11th Cir. 2002).

To make clear that the "losses" sued for were different, the city argued that in the *A&E* case it had only sought to recover amounts paid to BB&L for work properly performed, consistent with the NCP, but that it did not and could not have claimed recovery of payments for work negligently performed. To prevail on a CERCLA cost recovery claim a plaintiff can only recover the cost of work that is "consistent with the [NCP]."[14] Work that is performed negligently and wastefully cannot, as a matter of law, be "consistent with the NCP" or "cost-effective." Thus, courts have held that negligence in performing CERCLA response action work generally renders those costs unrecoverable.[15]

The district court never addressed the city's procedural defense. Going straight to the "merits," the district court noted that "there is no precise way for the court to determine what amount, if any, the City recovered from others for damages attributed by the jury in this case to BB&L."[16] However, at the trial, BB&L introduced a list of expenditures prepared by the city's finance department, which BB&L had characterized as a list by the city of its damages sought in the *A&E* litigation, because the list had been produced in discovery in the *A&E* case. The city manager disputed that characterization and testified that this was a list of total expenses prepared by the finance department, not a list of its claimed damages in the *A&E* case.

The district court, however, accepted BB&L's characterization. The list of expenditures document showed payments to BB&L, and also to its successor, Secor, to redo the CERCLA remediation work properly, though it was never established in the *A&E* litigation or at the trial in this case whether the payments to BB&L were limited to work that BB&L had done properly or included work that was the subject of the city's counterclaim. In the absence of such a finding, the district court resolved the uncertainty against the city and granted the motion for setoff.[17]

The district court's specific holding, however, was not that the city sought to recover in the prior *A&E* litigation amounts that it had paid to BB&L for work that had been done negligently. Rather, the district court focused on the fact that in its case against BB&L, the city used as the measure of damages the cost it paid to BB&L's replacement, Secor, to redo BB&L's flawed work. The court noted that the city had sought to recover from the *A&E* defendants an equitable portion of what it had paid to Secor for the work to be done properly—a fact the city did not dispute. The court held: "Because in this case the City sought to recover from BB&L amounts it paid Secor to redo BB&L's work, the court finds the damages sought in *A&E Construction* included the damages sought here."[18]

*Proceedings in the Eleventh Circuit*

The Eleventh Circuit, in addressing the setoff issue, rejected the city's argument that BB&L should not be entitled to a setoff because it had failed to produce the settlement agreements containing the releases in question. The court stated that "both the fact and the amount of the *A&E* settlement was before the district court and were undisputed by the parties. This was enough to satisfy the statute's 'show the court' requirement."[19]

Turning to the "merits" of the issue, the Eleventh Circuit appeared initially to accept the gist of the city's argument that each of the two lawsuits involved different "losses" or "damages" claims. It stated that "the purpose of a setoff is to prevent a party from recovering twice for the same damages."[20] The court held that setoff is inappropriate "when the first and second lawsuits seek recovery for different injuries."[21] Additionally, the court summarized the city's argument as follows:

> In the first lawsuit against the *A&E* defendants, the City's injury for which the City was seeking compensation was paying for a "CERCLA-quality" cleanup of the Munisport site. [Footnote omitted.] In the second lawsuit, this one involving Blasland, the City's injury was money it lost because of Blasland's breach of its contractual promise to do a "CERCLA-quality" cleanup job. Thus, concludes the City, because its counterclaim award against Blasland was an award for a different injury than the one for which it was compensated in the *A&E* suit, there was no duplication of awards and should have been no setoff.[22]

The Eleventh Circuit rejected the city's argument based on the proposition that the scope of the setoff based on the *A&E* litigation was not limited to what the city might have been legally able to recover under CERCLA, but included the actual items claimed as damages. On this point, the Eleventh Circuit relied on the district court's finding that the list of expenditures prepared by the city's accounting department reflected its claims in the *A&E* case.

Thus, the Eleventh Circuit concluded that even though the city may not have been legally entitled to recover in the *A&E* litigation amounts for work negligently done by BB&L, it may have "sued for" those amounts, and they may well have been reflected in the settlement numbers. Therefore, the entire settlement amount was set off against the city's counterclaim.[23] The looseness of this proceeding is illustrated in the following statement by the Eleventh Circuit:

> In ruling on the setoff motion, the district court first noted that "there is no precise way for the court to deter-

14. 42 U.S.C. §9607(a)(1), (a)(2), (a)(3), (a)(4)(B), ELR STAT. CERCLA §107(a)(1), (a)(2), (a)(3), (a)(4)(B); *See also* Redwing Carriers, Inc. v. Saraland Apartments, Ltd., 94 F.3d 1489, 1496, 27 ELR 20028, 20029 (11th Cir. 1996). *See* 40 C.F.R. §300.700(c)(3)(ii).

15. *See* Stewman v. Mid-South Wood Prods. of Mena, Inc., 784 F. Supp. 611, 615 (W.D. Ark. 1992); United States v. Western Processing Co., 734 F. Supp. 930, 940, 20 ELR 20990, 20995 (W.D. Wash. 1990).

16. Blasland, Bouck & Lee, Inc. v. City of N. Miami, No. 97-1484-CIV-HURLEY, Order Granting Plaintiff's Motion for Setoff, Slip. Op. at 4 (Mar. 9, 2000) [hereinafter District Court Setoff Order]. The court acknowledged that the city had spent more money on cleanup than it had recovered in all of its litigation, so there was no finding of a possible windfall by the city. *See id.* at 3.

17. The court held that the city's settlement against the operator defendants in City of N. Miami v. Berger, 828 F. Supp. 401, 23 ELR 21494 (E.D. Va. 1993), could not be set off against its counterclaim award since that settlement occurred prior to BB&L's performance of the work that gave rise to its breach of contract and therefore could not have included the amounts in question. Blasland, Bouck & Lee, Inc. v. City of N. Miami, No. 97-1484CIV (Fla. Mar. 10, 2000).

18. *See* District Court Setoff Order, *supra* note 16, at 6.

19. Blasland, Bouck & Lee, Inc. v. City of N. Miami, 283 F.3d 1286, 1294, 32 ELR 20486, 20488.

20. *Id.* at 1295, 32 ELR at 20488.

21. *Id.*

22. *Id.* at 1296, 32 ELR at 20489. In the footnote the court clarified that in *A&E* the City sought only an equitable portion of its response costs.

> mine what amount, if any, the City recovered [in prior litigation] from others for damages attributed by the jury in this case to [Blasland]." Nonetheless, the district court granted the setoff motion, concluding that the sums sought by the City in the *A&E* suit "logically included money paid to [Blasland]."[24]

Here the Eleventh Circuit got the facts wrong. As noted above, the district court's finding of possible duplication was based on an assumed double recovery of amounts paid to Secor to redo the work, and not amounts paid to BB&L for work done negligently.[25] The holding on this issue, in effect, was that absent clear and limiting release language, once a moving party shows that a prior judgment or settlement may have included the loss or damages claimed in the later suit, any uncertainties are resolved in favor of setoff.

The Eleventh Circuit then reversed the trial court's holding on the "pay-when-paid" clause. The court held that BB&L could use a CERCLA cost recovery cause of action to recover from the city amounts that BB&L had expressly agreed in its contract could not be recovered unless the amounts had been reimbursed by the state (which they had not been). In reaching this result, the Eleventh Circuit characterized the contractual defense as "equitable" rather than "legal," and therefore not a cognizable defense in a CERCLA cost recovery action. As discussed further below, this holding by itself appears to place the Eleventh Circuit at odds with other circuits that have considered contractual waivers or allocations of liability or costs under CERCLA.

Further legal analysis of each of these two significant rulings is provided below, along with a discussion of the important lessons they contain for the practitioner.

## The CERCLA Cost Allocation Issues

As noted above, the Eleventh Circuit reversed the district court on the issue of the application of the "pay-when-paid" clause in the contract between the city and BB&L. The court held that BB&L could use a CERCLA §107(a) cost recovery action to recover from the city funds that it could not recover under the terms of the contract, which expressly provided that BB&L would not be paid unless and until the city had first been reimbursed by the state. The court refused to give effect to an express limitation on liability agreed to between the parties, holding instead that the city's contractual defense was "equitable" and therefore not cognizable in a CERCLA cost recovery action.

### *CERCLA §107(e)*

Section 107(e) of CERCLA expressly recognizes the rights of parties to allocate responsibility for CERCLA response costs among themselves by contract, including an agreement that one party may waive them or indemnify another for them. Specifically, §107(e) provides:

> No indemnification, hold harmless, or similar agreement or conveyance shall be effective to transfer from . . . any person who may be liable for a release or threat of release under this section, to any other person the liability imposed under this section. *Nothing in this subsection shall bar any agreement to insure, hold harmless, or indemnify a party to such agreement for any liability under this section*.[26]

It is clear from the plain language of the statute that the U.S. Congress did not want to allow any responsible parties to contract away their *liability* under CERCLA, but it fully recognized and endorsed the ability of private parties to *allocate the costs* arising by virtue of that liability via contract with other private parties.

Section 107(e) was the statutory basis asserted by the city before both the district court and the Eleventh Circuit for upholding the "pay-when-paid" clause. The Eleventh Circuit declined to even discuss §107(e), except in a single sentence stating that §107(e) only applies "in contribution suits" between responsible parties under §113.[27] Section 107(e), however, contains no such limitation. Furthermore, it is located within §107, the general cost recovery provision (the basis for BB&L's suit), and not in §113, which allows contribution suits. Additionally, the case law under §107(e) does not support any such limitation.[28] While many of the agreements authorized by §107(e) have functioned to shift cleanup costs among the various responsible parties at a site, other agreements, such as insurance contracts, result in a transfer of cleanup obligations from responsible parties to other parties with no connections to the site.

The "pay-when-paid" clause in the city-BB&L contract served to shift the risk of nonpayment of response costs by the state from the city to BB&L. In this regard, the clause served an identical function to other risk-shifting devices such as insurance contracts and other indemnification agreements. Yet, the Eleventh Circuit refused to give the clause effect under §107(e), because BB&L's claim was based on §107(a), rather than §113(f).[29] The court gave no explanation for this construction and application of the statute.

All nine federal circuit courts that have considered §107(e) (prior to the Eleventh Circuit's opinion) have held that a party to a contract allocating costs from CERCLA liability may not seek to recover CERCLA costs from another party to the contract in a manner that would be contrary to

23. *See id.* at 1296-97, 32 ELR at 20489. *See also* District Court Setoff Order, *supra* note 16, at 5-6.
24. 283 F.3d at 1293, 32 ELR at 20488 (bracketed text in original).
25. On this point it is worth noting that the amounts paid to Secor to redo the work properly are relevant to *both* items of "damages" claimed by the city. First, the cost of doing the work properly is the measure of breach of contract damages. *See supra* note 11. Second, in the CERCLA contribution action, the city had a statutory right to recover from other PRPs an equitable portion of the costs it had incurred in performing properly the remedial work required by EPA. The city thought this might have confused the trial court and discussed it in its appellate brief, Answer and Reply Brief of Appellant and Cross-Appellee City of North Miami at 1-2, Blasland, Bouck & Lee, Inc. v. City of N. Miami (Apr. 20, 2001) (No. 00-14975-A), but the issue was not discussed by the Eleventh Circuit.
26. 42 U.S.C. §9607(e), ELR STAT. CERCLA §107(e) (emphasis added).
27. *See* 283 F.3d at 1303, 32 ELR at 20491.
28. For example, in Fisher Dev. Co. v. Boise Cascade Corp., 37 F.3d 104, 25 ELR 20760 (3d Cir. 1994), Fisher sued Boise Cascade under §107(a), and Boise Cascade successfully invoked a contractual release, which did not specifically mention CERCLA, to avoid liability for response costs pursuant to §107(e). *See* 37 F.3d at 107-11, 25 ELR at 20762. Similarly, Olin Corp. v. Consolidated Aluminum Corp., 5 F.3d 10, 24 ELR 20021 (2d Cir. 1993), involved a §107(a) counterclaim and a §107(e) assignment of liability clause in an assignment and assumption agreement between a buyer and seller of contaminated property, which was held to be a proper defense.
29. The Eleventh Circuit said that if this had been a contribution action, "the pay when paid clause might well have been considered in deciding an equitable allocation of liability . . . . We need not decide that, however, because the district court found that [BB&L] was an innocent party." 283 F.3d at 1305 n.15, 32 ELR at 20492 n.15.

the contractual provisions.[30] The Eleventh Circuit declined to follow these holdings because the "pay-when-paid" clause did not expressly mention "CERCLA liability."[31] This too, however, goes against established precedent, which has construed contractual provisions under §107(e) as applying to CERCLA costs even if there is no specific mention of CERCLA in the contracts at issue.[32] When CERCLA is not specifically mentioned in a contract subject to a §107(e) analysis, courts have performed traditional contract interpretation to determine if CERCLA costs were within the scope of costs waived or transferred between the parties.[33] The Eleventh Circuit broke ranks with this well-established approach and allowed BB&L to recover costs under CERCLA §107(a) that it had contracted away with the execution of the "pay-when-paid" clause.

*The Eleventh Circuit's CERCLA Defense Analysis*

The Eleventh Circuit began its analysis of the city's contractual defense with a discussion of the §107(a) liability scheme and the available defenses. CERCLA §107(a) establishes the prima facie elements of CERCLA liability, under which current owners and operators, former owners and operators at the time of disposal, arrangers, and transporters are liable for response costs, "subject only to the defenses set forth in subsection (b) of this section."[34] But while the text of §107(a) appears to limit defenses to only the three listed in §107(b), a review of the statute as a whole reveals that Congress has identified nine other defenses to CERCLA liability or responsibility for response costs:

| Defense | Statutory Section |
|---|---|
| 1. Statute of Limitations | §113(g)(2), 42 U.S.C. §9613(g)(2) |
| 2. "Federally Permitted Release" (the release in question was authorized by a permit issued under any federal environmental law). | §§107(j) and 101(10), 42 U.S.C. §§9607(j) and 9601(10). |
| 3. The owner of the property where the hazardous substances are located acquired it without knowing, and without reason to know, that hazardous substances were there (the "innocent purchaser" defense). | §101(35)(A)(i), 42 U.S.C. §9601(35)(A)(i). |
| 4. The defendant is a government entity which acquired the facility by involuntary transfer or eminent domain. | §101(35)(A)(ii), 42 U.S.C. §9601(35)(A)(ii). |
| 5. The defendant acquired the facility by inheritance or bequest. | §101(35)(A)(iii), 42 U.S.C. §9601(35)(A)(iii). |
| 6. The defendant has entered into an agreement with the plaintiff in which the plaintiff has agreed to hold harmless or indemnify the defendant from CERCLA liability or similarly agreed not to seek such damages from defendant. | §107(e), 42 U.S.C. §9607(e). |
| 7. Covenant not to sue: the government or any other responsible party may issue a covenant not to sue, typically embodied in a consent decree or settlement agreement, which is an enforceable defense to any subsequent claim for response costs by the person issuing the covenant not to sue. | §122(c)(1) and (f); 42 U.S.C. §9622(c)(1) and (f). |
| 8. Defendant is a lender who "holds indicia of ownership primarily to protect [its] security interest." | §101(20)(E), 42 U.S.C. §9601(20)(E). |
| 9. The defendant is a nonnegligent response action contractor. | §119(a)(1)-(2), 42 U.S.C. §9619(a)(1)-(2). |

Indeed, the Eleventh Circuit properly recognized that "the exclusivity language of [§]107(a) is belied by a passel of defenses explicitly provided in other sections."[35]

In general, courts have limited the defenses available in a CERCLA cost recovery action to those enumerated in the statute. Most courts have held that equitable defenses are barred under CERCLA.[36] This bar against equitable defenses places significant pressure on parties to categorize

30. *See* White Consolidated Indus., Inc. v. Westinghouse Elec. Corp., 179 F.3d 403, 29 ELR 21202 (6th Cir. 1999); Lion Oil Co. v. Tosco Corp., 90 F.3d 268, 26 ELR 21584 (8th Cir. 1996); Joslyn Mfg. Co. v. Koppers Co., 40 F.3d 750, 25 ELR 20476 (5th Cir. 1994); *Fisher Dev.*, 37 F.3d at 104, 25 ELR at 20760; Harley-Davidson, Inc. v. Minstar, Inc., 41 F.3d 341, 25 ELR 20176 (7th Cir. 1994); Olin Corp. v. Consolidated Aluminum Corp., 5 F.3d 10, 24 ELR 20021 (2d Cir. 1993); John S. Boyd Co. v. Boston Gas Co., 992 F.2d 401, 23 ELR 21122 (1st Cir. 1993); United States v. Hardage, 985 F.2d 1427 (10th Cir. 1993); Mardan Corp. v. C.G.C. Music, Ltd., 804 F.2d 1454, 17 ELR 20209 (9th Cir. 1986).

31. *See* 283 F.3d at 1304, 32 ELR at 20492.

32. *See White Consolidated Indus*., 179 F.3d at 409-10, 29 ELR at 21504; *Fisher Dev*., 37 F.3d at 109-10, 25 ELR at 20762; *Olin Corp.*, 5 F.3d at 15-16, 24 ELR at 20023-24; *Hardage*, 985 F.2d at 1434-35; *Mardan Corp.*, 804 F.2d at 1460-61, 17 ELR at 20211; Folino v. Hampden Color & Chem. Co., 832 F. Supp. 757, 760-61, 24 ELR 20345, 20346 (D. Vt. 1993); Village of Fox River Grove v. Grayhill, Inc., 806 F. Supp. 785, 794-95 (N.D. Ill. 1992); Mobay Corp. v. Allied-Signal, Inc., 761 F. Supp. 345, 21 ELR 20791 (D.N.J. 1991).

33. For example, in *Fisher Development*, the court construed the plain language of the release and stated, "we can only take the phrase 'hereafter may have' to mean that the parties wished to release not only those claims of which they were currently aware, but also those they might subsequently discover . . . ." *Fisher Dev.*, 37 F.3d at 108, 25 ELR at 20762-63. In *Olin Corp.*, the court found that the language of the release "evidences the parties' clear and unmistakable intent" that all liabilities be transferred, even future unknown liabilities. 5 F.3d at 16, 24 ELR at 20024. And in *Hardage*, the U.S. Court of Appeals for the Tenth Circuit recognized that its inquiry must focus "on whether the parties unequivocally expressed an intent to indemnify. Intent must be determined by construing the contract as a whole, and the court must construe the contract so as to give effect to each provision." 985 F.2d at 1434.

34. 42 U.S.C. §9607(a), ELR STAT. CERCLA §107(a). The defenses in §107(b) include: (1) an act of God; (2) an act of war; and (3) an act of an unrelated third party. *See* 42 U.S.C. §9607(b), ELR STAT. CERCLA §107(b).

35. 283 F.3d at 1303, 32 ELR at 20491.

36. *See* Velsicol Chem. Corp. v. Enenco, 9 F.3d 524, 530, 24 ELR 20107, 20110-11 (6th Cir. 1993) (holding that the doctrine of laches may not bar a CERCLA cost recovery action); General Elec. Co. v. Litton Indus. Automation Sys., 920 F.2d 1415, 1418, 21 ELR 20453, 20454 (8th Cir. 1990) (holding that CERCLA does not provide for an unclean hands defense to liability); Smith Land & Improvement Corp. v. Celotox Corp., 851 F.2d 86, 90, 18 ELR 21026, 21028 (3d Cir. 1988) (holding that *caveat emptor* is not a defense to liability for contribution). *But see contra* United States v. Mottolo, 695 F. Supp. 615, 626, 19 ELR 20442, 20448 (D.N.H. 1988); United States v. Moore, 703 F. Supp. 455, 460, 18 ELR 21274, 21274 (E.D. Va. 1988); United States v. Conservation Chem. Co., 619 F. Supp. 162, 204, 16 ELR 20193, 20210 (W.D. Mo. 1985).

defenses as either "equitable" or "legal," i.e., statutory, in nature. Despite these efforts to draw a clear distinction, neither CERCLA nor the case law under §107(a) clearly defines an "equitable" defense. Rather, the courts focus on the specific statutory defenses enumerated in CERCLA and whether the defenses asserted in cases before them comport with the statutory language and congressional intent.[37] After dismissing §107(e) as a possibility, the Eleventh Circuit concluded that the pay-when-paid clause did not qualify under any of the other CERCLA defenses (nor did the city so argue) and instead concluded, based on its de novo reading of the contract, that the city's defense of the pay-when-paid clause was "equitable" and therefore barred.

*The Nature of Equitable Defenses*

When looking beyond the prism of CERCLA to general tenets of contract law, one discovers that the "pay-when-paid" clause is not analogous to an equitable defense. Traditionally, an equitable defense is characterized as a defense of fairness, and may be based on the *conduct* of the nonbreaching party, hardship on the party in breach, injury to third parties, or some combination of these circumstances.[38] The doctrines of equitable estoppel, unclean hands, and laches are described as general equitable defenses, and contract law provides specific equitable defenses such as duress, undue hardship, unconscionability, undue influence, mistake, and injury to third parties or the public.[39] A "legal" defense, on the other hand, is defined as "a defense which is complete and adequate in point of law," i.e., based on a statute or written enforceable instrument.[40] Legal defenses do not excuse a party from liability "simply because he lacked business acumen and made a bad bargain."[41]

Even the defense of "estoppel" has carried both "legal" and "equitable" meanings. "Legal" estoppel (estoppel by contract) arises out of a written instrument, most frequently a contract or deed to real property, and "means no more than that a party is bound by the terms of his own contract until set aside. It is based on the idea that a party to a contract will not be permitted to take a position inconsistent with its provisions, to the prejudice of another."[42] "Equitable" estoppel, on the other hand, arises through conduct and not a legally enforceable written instrument, and has been held to be distinct from "legal" estoppel.[43]

Despite these various distinctions, there is no bright analytical line in modern jurisprudence between "equitable" and "legal" defenses. The difficulty in distinguishing between equitable and legal defenses on a purely categorical basis is attributable to the merger of law and equity courts, which blurred the distinction.[44] Indeed, scholars have suggested that there is little practical distinction between equitable and legal defenses.[45]

In the context of determining permissible defenses in a CERCLA action, the lack of a clear definition for equitable defenses can cause confusion and inconsistency as a court must grapple with whether a defense is "legal" or "equitable." The Eleventh Circuit's opinion exemplifies this confusion, and by focusing on the issue of whether the "pay-when-paid" clause is an "equitable" defense, the court obscured the true issue in the case—whether the "pay-when-paid" clause constituted a complete waiver by BB&L of its right to sue for money not received by the city from the state, as contemplated by §107(e), or whether the clause is limited only to BB&L's state-law contractual claims against the city.

*The Eleventh Circuit's Contract Interpretation*

The Eleventh Circuit construed the "pay-when-paid" clause as not waiving BB&L's claim to recover under CERCLA the very same amounts it agreed not to seek under its contract: "Although [BB&L] did not release the City from CERCLA liability, it did release the City from contractual liability . . . . [T]he terms of the clause do not mention CERCLA liability. It is only in equity that the City's argument has a good ring to it."[46]

The district court, by contrast, performed traditional contract interpretation and held that the clause constituted a complete waiver of claims against the city for money it had not received from the state. The Eleventh Circuit gave no deference to this fact question resolved by the district court. The district court's analysis focused not on whether the city was raising an equitable or legal defense, but on the scope and validity of the "pay-when-paid" clause as a legal shield to BB&L's claim. The district court noted:

> The contract was the result of an [arm's]-length negotiation between two sophisticated parties. It does not contemplate an illegal act, nor was it the product of duress; and its enforcement would not be unconscionable. The pay-when-paid provision was clear on its face; BB&L understood the potential consequences and [did] not claim any surprise by the City's attempt to enforce it.[47]

While the district court inexplicably did not address the city's argument that the "pay-when-paid" clause was a statutory and therefore a "legal" defense under §107(e), it noted that the U.S. Court of Appeals for the Seventh Circuit in

37. *See supra* note 36.

38. *See* Emily L. Sherwin, *Law and Equity in Contract Enforcement*, 50 Md. L. Rev. 253, 272 (1991) (characterizing the values that "drive equitable defenses" as "values of fairness and justice between parties . . . . Equity represents 'ideal justice,' 'standards of decent and honorable conduct,' 'human brotherhood,' and 'the duty to share unanticipated misfortune'"); Edward Yorio, Contract Enforcement: Specific Performance and Injunctions §4.1 (1989).

39. *See* Kevin C. Kennedy, *Equitable Remedies and Principled Discretion: The Michigan Experience*, 74 U. Det. Mercy L. Rev. 609, 623, 631-34 (1997) (discussing duress, undue influence, and unconscionability as grounds for denying specific performance); *see also* Edward Yorio, *A Defense of Equitable Defenses*, 51 Ohio St. L.J. 1201, 1203 (1990) (listing "improper conduct by the plaintiff in formation of the contract; unreasonable delay by the plaintiff in instituting or pursuing an action for specific relief; inadequacy of consideration; impossibility; mistake; changed circumstances; hardship on the defendant; and injury to third parties or the public," as possible equitable defenses).

40. Black's Law Dictionary 420 (6th ed. 1990).

41. *See* Sherwin, *supra* note 38, at 265-67.

42. Woodward v. General Motors Corp., 298 F.2d 121, 129 (5th Cir. 1962).

43. *See* Daniell v. Sherrill, 48 So. 2d 736 (Fla. 1950); Booth v. Lenox, 34 So. 566 (Fla. 1903).

44. *See* Yorio, *supra* note 39, at 1207; Black's Law Dictionary, *supra* note 40, at 420.

45. Yorio, *supra* note 39, at 1207-08.

46. Blasland, Bouck & Lee, Inc. v. City of N. Miami, 283 F.3d 1286, 1303-04, 32 ELR 20486, 20491 (11th Cir. 2002).

47. Blasland, Bouck & Lee, Inc. v. City of N. Miami, 96 F. Supp. 2d 1375, 1382 (S.D. Fla. 2000).

*Town of Munster v. Sherman-Williams Co.*,[48] characterized as "legal or statutory defenses" res judicata, collateral estoppel, accord and satisfaction, and statutes of limitations.[49] The court then said:

> This is precisely the type of defense the City raises here, *i.e.*, BB&L, in a bargained-for exchange, contracted away its right to sue for money not received by the City from the State. By whatever label—estoppel by contract, waiver, covenant not to sue, etc.—the bottom line is that parties ought to be able to rely on the agreements they form with one another. That is *the* central premise of contract law. *See Chambers Dev. Co., Inc. v. Passaic County Util. Auth.*, 62 F.3d 582, 589 (3d Cir. 1995) ("The sanctity of a contract is a fundamental concept of our entire legal structure."). Therefore, the court concludes the pay-when-paid provision is valid and enforceable and prevents BB&L from recovering the damages [for which the City had not been reimbursed by the State].[50]

While the Eleventh Circuit reversed the lower court on the ground that the "pay-when-paid" clause constituted an equitable, rather than legal, defense, the actual disagreement between the two courts is in their construction of the contract. While the district court engaged in traditional contract interpretation to ascertain the intent of the parties, the Eleventh Circuit found, with no analysis or explanation, that "the pay-when-paid clause did not purport to release CERCLA liability, or any liability other than contractual liability."[51] The court then analogized the city's reliance on the clause to an argument for equitable estoppel (which is no defense under CERCLA §107(a)), but the court's assertion that the city's only argument is in equity depends wholly on the court's interpretation that the clause was restricted to contractual liability only. Given this narrow construction, the court concluded that the city's defense could only be equitable.

In reaching this result, the Eleventh Circuit ignored basic principles of contract interpretation: it did not give the words in the contract their plain meaning, and gave no effect to the apparent intent of the parties in entering into the contract and executing the "pay-when-paid" clause. Instead, it simply held that a pay-when-paid clause contractual defense is no defense to a CERCLA cost recovery action based on its narrow reading of the contract. As another short article on this case recently commented:

> The court . . . stated that once an innocent party has proven its prima facie case, as had been done here, the only defenses to liability available are those specifically set forth in the statute. Because no provision of CERCLA refers to a pay-when-paid clause, the Eleventh Circuit reasoned, such a clause cannot be a defense to CERCLA [§]107(a) liability. Therefore, the pay-when-paid clause was unenforceable.[52]

*Lessons Learned*

The Eleventh Circuit's ruling that §107(e) provides no defense to a CERCLA cost recovery case, coupled with its refusal to construe the parties' contract according to its terms and clear intent, are extremely troubling. If a waiver clause in a contract can be disregarded through the device of a CERCLA cost recovery action, will this impair parties' willingness to enter into contracts with potential CERCLA plaintiffs, including response action contractors? What can parties to commercial contracts do to avoid such results in future cases?

There is an important lesson for practitioners to take from the Eleventh Circuit's decision. In drafting commercial agreements in which the parties intend to waive or allocate environmental cleanup or other site response costs, counsel should expressly provide that the waiver, allocation, or other provision includes CERCLA response costs. This simple but vital drafting addition should satisfy the §107(e) requirements in most jurisdictions. Whether it would increase the likelihood of success in the Eleventh Circuit is a difficult question, as there can be no guarantee of success given the court's refusal to apply §107(e) in a §107(a) cost recovery case.

**Setoff of Prior CERCLA Recovery**

This case also provides important lessons on the drafting of settlement agreements in cases, such as CERCLA, that involve multiple defendants, as well as on trial procedures when confronting a setoff motion. In *BB&L*, the Eleventh Circuit upheld the district court's determination that a setoff of the city's award was warranted when there appeared to be a possibility that the same "damages" were being sought in two separate cases against separate defendants, even though the trial court acknowledged that it had no way to determine it definitively.

*Burden of Proof for Setoff*

The first issue raised by the Eleventh Circuit's opinion on setoff is procedural. Specifically, on whom should the burden be placed to produce the release or covenant not to sue: the party moving for setoff or the party who executes the release or covenant, and against whom setoff is sought? Normally, the party filing a motion and seeking affirmative relief bears the burden of producing whatever evidence is needed to support the granting of the motion.[53] In addition, it is widely held that requests for setoff are treated as either affirmative defenses or counterclaim demands, which must be "specifically pleaded and proved" by the party asserting setoff.[54] Here, both the trial and appellate courts effectively held that once the party seeking setoff shows that there was prior litigation in which the same damages *may* have been sought, the burden shifts to the party against whom setoff is sought to produce the releases and prove that there is not overlap in the damage claims. Neither court explained its reasoning or cited any authority for this dramatic departure from the normal rules regarding the burden of proof in support of a motion. In the future, any party against whom

48. 27 F.3d 1268, 1271-72, 24 ELR 21108, 21111 (7th Cir. 1994).
49. *See* 96 F. Supp. 2d at 1382.
50. *Id.*
51. 283 F.3d at 1303 n.13, 32 ELR 20491 n.13.
52. Douglas S. Arnold & Kristin H. Jones, *Regional Reports—Eleventh Circuit*, 13 A.B.A. Envtl. Litig. Committee Newsl., 22 (2002).
53. "In general, the law places the burden of proof on the party that asserts a contention and seeks to benefit from it." Martinelli v. Bridgeport Roman Catholic Diocesan Corp., 196 F.3d 409, 428 (2d Cir. 1999). *See also* Marcum v. United States, 452 F.2d 36, 39 (5th Cir. 1971) ("Burden of proving disputed facts rests on the one affirming their existence and claiming rights or benefits therefrom.").
54. *See* Zeeman v. United States, 275 F. Supp. 235, 255 (S.D.N.Y. 1967).

setoff is sought would be well advised to produce the release or covenant in question.

Furthermore, the courts took a very permissive view of the procedural requirements of the Florida setoff statute, allowing setoff "if any person shows the court that the *plaintiff . . . has delivered a written release or covenant not to sue to any person in partial satisfaction of the damages sued for.*"[55] As noted above, the Eleventh Circuit found that it was sufficient that "the fact and amount of the [prior] settlement were before the district court and were undisputed by the parties. This was enough to satisfy the statute's 'show the court' requirement."[56] Florida courts applying the setoff law, however, have traditionally wanted to analyze the actual terms and scope of releases before granting a motion for setoff.[57]

Other states also require the party asserting setoff to produce evidence of the releases that give rise to the claim of setoff. For example, in New York, "a defendant carries the burden of establishing the equitable shares attributable to a settling tortfeasor when seeking to reduce its own responsibility for damages."[58] In California, where setoffs are allocated under a set formula established by the California Court of Appeals, parties requesting setoff must present settlement documents to the court or offer other evidence of settlement terms if they wish to deviate from the state court's formula. "Where parties have agreed to allocate less than all of the settlement amount to a portion of the causes of action, an evidentiary showing is required to justify such allocation."[59] In Pennsylvania, courts have required a nonsettling defendant seeking to offset his liability to demonstrate that the release entitles him to a setoff,[60] and in Texas, where setoffs are termed "settlement credits," "a defendant seeking a settlement credit has the burden of proving its right to such a credit. This burden includes proving the settlement credit amount."[61]

Practitioners defending against a setoff motion would do well to determine early on who has the burden of proof in their jurisdiction. If there is doubt, and the release or covenant is favorable to the opponent, serious consideration should be given to producing it.

### *Determining Whether Setoff Is Appropriate*

Turning to the merits, there are important drafting lessons. The district court determined, and the Eleventh Circuit affirmed, that a setoff was appropriate based on the following established principles of setoff law. First, in order to avoid setoff, it is not enough simply to show that the plaintiff in the aggregate would not recover more in the multiple lawsuits combined than he has paid out. Instead, the focus is on whether the "loss" for which recovery is sought in the second lawsuit is one which appears to have been covered in the settlement or judgment in the first lawsuit.

Under Florida law according to the Eleventh Circuit, the relevant inquiry is not whether the monies in the subsequent litigation were legally recoverable in the prior action, but whether they were arguably included within the scope of damages sought and recovered in settlement or from a trial on the merits.[62] This is probably the law in many other jurisdictions as well. The Eleventh Circuit noted that when a settlement agreement does not detail the specific claims and damages to which the settlement pertains, a court will set off *the entire settlement amount* against a recovery in subsequent litigation where claims for damages appear to overlap.[63] While the trial court focused on the disputed expense list prepared by the city's finance department, the best evidence will in most cases be the settlement releases themselves.

The risk to practitioners from these setoff principles is evident. In order to survive a setoff motion and recover damages in subsequent litigation involving the same CERCLA site as prior lawsuits, releases in settlement agreements must be drafted very carefully so that they specify precisely what damage claims are being settled and do not preclude recovery of other related (or unrelated) claims in subsequent litigation against other parties. In the CERCLA cost recovery case, these releases may include specifying that the amount paid by the settling defendant is only that party's "fair share" of costs legally recoverable under CERCLA, that the plaintiff reserves all rights to proceed against other PRPs, and that this reservation is a material condition of the settlement. Sample language is as follows:

> (1) The parties hereto agree that the amount being paid under this settlement agreement, and for which the release herein from further liability is being given, constitutes the (settling defendant's) fair and equitable share of response costs which have been incurred by (settling plaintiffs) and which are legally recoverable under CERCLA.
>
> (2) Nothing in the Agreement shall be construed to create any rights in, or grant any cause of action to, any person not a party to this Agreement. Except as provided in this paragraph, each party expressly reserves any and all rights, including, but not limited to, any rights of contribution, defenses, claims, demands, and causes of action which each party may have with respect to any matter, transaction, or occurrences relating in any way to the (site or matter) against any person who is not a party to this Agreement. This reservation of rights is a material condition of this Agreement.

The specific language will need to be tailored to the facts and circumstances of each case, and possibly to the law of a particular jurisdiction. However, such careful drafting should minimize the risk of having an entire settlement amount set off against a recovery in a later lawsuit.

## Concluding Thoughts

The Eleventh Circuit's holdings on the setoff issues, as well as on the "pay-when-paid" limitation on liability issues, would not have been easily predicted by most practitioners.

55. FLA. STAT. §46.015(2) (emphasis added).
56. 283 F.3d at 1294, 32 ELR at 20488.
57. *See, e.g.*, Baudo v. Bon Secours Hosp., 684 So. 2d 211, 212-13 (Fla. Dist. Ct. App. 1996).
58. Hyosung America v. Sumagh Textile Co., 25 F. Supp. 2d 376, 387 (S.D.N.Y. 1998).
59. Erreca's v. Superior Court, 24 Cal. Rptr. 2d 156, 167 (App. 4th Dist. 1993).
60. Cole v. Altieri, 534 F. Supp. 165 (E.D. Pa. 1981).
61. Mobil Oil Corp. v. Ellender, 968 S.W.2d 917, 927 (Tex. 1998).
62. Blasland, Bouck & Lee, Inc. v. City of N. Miami, 283 F.3d 1286, 1296, 32 ELR 20486, 20488 (11th Cir. 2002).
63. *Id.* at 1297 n.9, 32 ELR at 20489 n.9.

They may strike some as disturbing. Most importantly, they provide a strong reminder that there are critical interrelationships between bodies of law, as well as potential pitfalls, in the drafting of contracts in which costs or liabilities are waived, conditioned, or allocated, as well as in the drafting of releases and covenants not to sue. The case also reminds us that in determining whether or not to present evidence—in this case the releases—doubts often should be resolved in favor of presenting it regardless of who technically has the burden of proof.