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CERCLA Alert – Trustees, Trust Not! Personal Liability Ahead: An Analysis of City of Phoenix v. Garbage Services Company

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**CERCLA ALERT — TRUSTEES, TRUST NOT! PERSONAL
LIABILITY AHEAD: AN ANALYSIS OF *CITY OF PHOENIX*
v. *GARBAGE SERVICES COMPANY***

INTRODUCTION

Trustees, beware! You may have to finance *personally* the clean-up of hazardous waste even though you are not responsible for the contamination. In *City of Phoenix v. Garbage Services Co.*,¹ the most important decision regarding trustee liability under CERCLA² to date, the district court of Arizona (Arizona court), held a testamentary trustee personally liable for response costs³ beyond the assets held in trust. As it now stands, every past and present trustee who has possessed or possesses power over the utilization of trust property is potentially liable for the cost of hazardous waste clean-up. The Arizona court's decision has sent shock waves throughout the trustee community. With no appeal pending,⁴ the Arizona court's decision is the only decision addressing trustee liability under CERCLA.

While the Arizona court allowed the trustee to seek indemnification from trust assets, if those assets are insufficient the trustee is ultimately responsible for the balance. This is an alarming prospect especially in light of the fact that CERCLA provides few defenses,⁵ is

1. 827 F Supp. 600 (D. Ariz. 1993) [hereinafter *Phoenix II*].

2. The Comprehensive Environmental Response, Compensation and Liability Act of 1980, Pub. L. No. 96-510, 94 Stat. 2767 (codified as amended in scattered sections of 26 U.S.C., 33 U.S.C., 42 U.S.C. and 49 U.S.C.).

3. Response costs include the costs of all actions undertaken to clean-up, remove, mitigate, prevent the release of hazardous substances into the environment. See 42 U.S.C. 9601, §§ 23, 24. In an earlier decision, *City of Phoenix v. Garbage Servs. Co.*, 816 F Supp. 564, 567 (1993) [hereinafter *Phoenix I*], the court held that a trustee is an "owner" as defined by CERCLA.

4. In a Telephone Interview with Barry Sandler, Esq. of Morrison & Foerster, attorneys for the defendant, in San Francisco, CA, this author was told that the case has been settled and is not being appealed (Feb. 14, 1994).

5. 42 U.S.C. § 9607(b) (1986) lists the following defenses:

There shall be no liability under subsection (a) of this section for a person otherwise liable who can establish by a preponderance of the evidence that the release or threat of release of a hazardous substance and the damages resulting therefrom were caused solely by—

- (1) an act of God;
- (2) an act of war;
- (3) an act or omission of a third party other than an employee or agent of the defendant, or than one whose act or omission occurs in connection with a contractual relationship, existing directly or indirectly, with the defendant (except where the sole contractual arrangement arises from a public tariff and acceptance for a carriage by a common carrier by rail), if the defendant establishes by a preponderance of the evidence that (a) he exercised due care with respect to the hazardous substance concerned, taking into consideration the characteristics of such hazardous substances, in light of all relevant facts and circumstances, and (b) he took precautions against foreseeable acts or omissions of any such third party and the consequences that could foreseeably result from such acts or omissions; or

applied retroactively⁶ and demands staggering amounts of money for response costs while insurance is virtually impossible to obtain.⁷

Prior to the *Phoenix I* and *Phoenix II* decisions, many commentators⁸ speculated as to whether courts would hold trustees liable under CERCLA. While blind speculation is no longer necessary, one may now ruminate as to whether the Arizona court decisions are an aberration or precedent other courts will follow. If treated as precedent, the Arizona court decisions will evoke much fear from trustees throughout the country. Several commentators offer advice to prospective trustees on how to insulate themselves from CERCLA liability, but that advice provides no solace to current or past trustees.⁹

This Note analyzes the Arizona court's decision to hold trustees personally liable as "owners" within the meaning of CERCLA. Part I gives a brief overview of CERCLA. Part II discusses the traditional common law of trusts and the modern trend in trustee liability. Part III analyzes the recent cases, *Phoenix I* and *Phoenix II*, focusing on the court's adoption of the common law of trusts. Part IV presents the legislative response and Part V concludes by asserting that *Phoenix I* and *Phoenix II* were erroneously decided. Future courts should follow the trust law trend which relieves trustees from personal liability when they are without fault. In the alternative, CERCLA should be amended to exempt trustees from the definition of "owner" when the trustee is without fault for the contamination.

(4) any combination of the foregoing paragraphs.

6. *United States v. Shell Oil Co.*, 605 F. Supp. 1064, 1075 (D. Colo. 1985); *United States v. Monsanto, Co.*, 858 F.2d 160, 173-74 (4th Cir. 1988) (holding CERCLA's retroactivity consistent with due process), *cert. denied*, 1095 S. Ct. 3156 (1989).

7. See William L. Hoey, Note, *Personal Liability of Trustees Under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA)*, 68 U. DET. L. REV. 73 n.12 (1993).

8. See Douglas M. Garrou, Note, *The Potentially Responsible Trustee: Probable Target for CERCLA Liability*, 77 VA. L. REV. 113 (1991); Hoey, *supra* note 7; Deborah A. Lawrence, *Liability of Trustees under CERCLA*, 34 RES. GESTAE 561 (1991); Joel S. Moskowitz, *Trustee Liability under CERCLA*, 21 ENVTL. L. REP. (Envtl. L. Inst.) 10,003 (1991); Kurt R. Strasser & Denise Rodosevich, *Seeing the Forest Through the Trees in CERCLA Liability*, 10 YALE J. ON REG. 493 (1993); Larry Schnapf, *Lender Liability Rule Doesn't Help Trustees*, NAT'L L.J., May 10, 1993, at 12.

9. See Kevin C. Murphy & Elizabeth C. Yen, *Trustee Liability for the Cost of Site Environmental Cleanup*, 110 BANKING L.J. 467 (1993), who recommend the following precautions:

Evaluate the environmental condition of real property before agreeing to serve as trustee; ensure that the trust agreement or will permits the trustee or executor to decline to serve; require the settlor to obtain environmental impairment insurance that is explicitly transferable to the trustee or executor; ensure that the trust agreement expressly provides for commitment of trust estate assets towards environmental cleanup; arrange for indemnification by the beneficiary or other party.

I. CERCLA OVERVIEW

CERCLA¹⁰ was a hastily drafted piece of legislation in response to congressional concern for the problem of active and inactive hazardous waste sites and hazardous waste spills. In enacting CERCLA, Congress sought two basic objectives. First, to give the federal government the tools necessary for a prompt and effective response to the environmental problems of national magnitude caused by hazardous waste disposal.¹¹ Second, Congress sought to impose fiscal responsibility on appropriate persons for problems caused by the disposal of hazardous substances.¹²

CERCLA provides the federal and state governments with a comprehensive device to remedy the problems of hazardous waste liability, compensation and clean-up. Specifically, CERCLA authorizes Environmental Protection Agency (EPA)¹³ to identify abandoned hazardous waste sites, use "Superfund"¹⁴ resources to clean-up those sites and sue any potentially responsible parties (PRP) it can locate for reimbursement of clean-up costs.¹⁵

Despite Congress' effort to list PRPs, courts continue to grapple with congressional intent as to who comprises the nefarious club of "owners" and "operators" under CERCLA, which is clouded with ambiguity.¹⁶ Moreover, the dearth of legislative history provides the courts with little guidance, which has led one court to comment that "CERCLA has acquired a well-deserved notoriety for vaguely drafted provisions and an indefinite, if not contradictory, legislative history."¹⁷

10. This paper includes a brief overview of CERCLA since there is a plethora of sources already available detailing the legislative history of CERCLA. For a thorough explanation of CERCLA's history, see generally Frank P. Grad, *A Legislative History of the Comprehensive Environmental Response, Compensation and Liability ("Superfund") Act of 1980*, 8 COLUM. J. ENVTL. L. 1 (1982).

11. *Dedham Water Co. v. Cumberland Farms Dairy, Inc.*, 805 F.2d 1074, 1080 (1st Cir. 1986).

12. *Id.* at 1080.

13. EPA is the federal agency charged with much of the enforcement of CERCLA. See *Phoenix II*, 827 F. Supp. at 606 n.6.

14. "Superfund" is a fund established to cover cleanup costs for a contaminated site. Superfund covers cleanup costs if the site has been abandoned, if the responsible parties elude detection, or if private resources are inadequate. The funds for Superfund come from taxes collected over a five-year period on petroleum and certain inorganic chemicals, as well as from general federal revenues. See 42 U.S.C. § 9631 (1986); *New York v. Shore Realty Corp.*, 759 F.2d 1032, 1041 (2d Cir. 1985).

15. See *id.* § 9607(1)-(4) for a list of "responsible parties."

16. *United States v. Fleet Factors Corp.*, 901 F.2d 1550, 1554 n.3 (11th Cir. 1990) citing *Coastal Casting Serv. v. Aron*, 1988 WL 35012 (S.D. Tex. 1988) ("It is well known that CERCLA was hastily drafted and adopted, with resulting ambiguities."); *United States v. Maryland Bank & Trust Co.*, 632 F. Supp. 573, 578 (D. Md. 1986) ("The structure of section 107(a), like so much of this hastily patched together compromise Act, is not a model of statutory clarity."); see also *United States v. Northeast Pharmaceutical & Chem. Co.*, 579 F. Supp. 823, 838 (W.D. Miss. 1984).

17. *Dedham Water*, 805 F.2d at 1080 (quoting *United States v. Mottolo*, 605 F. Supp. 898, 902 (D.N.H. 1985)).

It is therefore not surprising that courts throughout the country struggle and sometimes stumble in an attempt to decipher the meaning of CERCLA and who it includes.

Nonetheless, CERCLA purports to hold four groups of "persons"¹⁸ strictly liable¹⁹ for government²⁰ and private-party clean-up costs:²¹ any person who is a current "owner" or "operator" of facilities contaminated by hazardous substances regardless of whether the pollution occurred before the current owner owned the property; any person who owned or operated a facility when hazardous substances were deposited there whether or not they owned the property at the time of clean-up; anyone who arranges for disposal or treatment of hazardous substances; and transporters who carry the hazardous waste to disposal and treatment facilities are liable under CERCLA. The problem lies in trying to determine who comes within one of the four groups. The normal rule of statutory construction is a reading of the statute itself and the legislative history behind it, if necessary, to clarify any ambiguities.²² When neither source provides the court with the necessary insight, however, a judicial method must be developed to fill the statute's interstices.²³

Significantly, courts have been inclined to interpret CERCLA²⁴ broadly and to include corporate officers²⁵ and active stockholders among those on the CERCLA "wanted list."²⁶ On the other hand,

18. The term "person" means an individual, firm, corporation, association, partnership, consortium, joint venture, commercial entity, United States Government, State, municipality, commission, political subdivision of a State, or any interstate body. CERCLA § 101(21), 42 U.S.C. § 9601(21).

19. *United States v. Northeastern Pharmaceutical & Chem. Co.*, 810 F.2d 726, 732 n.3 (8th Cir. 1986) (stating that most cases have imposed strict liability under CERCLA), *cert. denied*, 484 U.S. 848 (1986) [hereinafter NEPACCO].

20. Government clean-up costs are incurred when the EPA responds to a release or threat of a release of a hazardous substance, pollutant, or contaminant. CERCLA § 104(a), 42 U.S.C. § 9604(a) (1988).

21. For the procedures private parties must follow for private actions under CERCLA, see generally Jeffrey M. Gaba, *Recovering Hazardous Waste Cleanup Costs: The Private Cause of Action Under CERCLA*, 13 *ECOLOGY L.Q.* 181, 196-232 (1986); Patricia L. Quentel, Comment, *The Liability of Financial Institutions for Hazardous Waste Cleanup Costs Under CERCLA*, 1988 *Wis. L. Rev.* 139.

22. See generally *Joslyn Mfg. Co. v. T.L. James & Co.*, 893 F.2d 80, 82 (5th Cir. 1990).

23. *United States v. Alcan Aluminum Corp.*, 964 F.2d 252, 268 n.26 (3d Cir. 1992).

24. *Dedham Water*, 805 F.2d at 1081 ("We are obligated to construe [CERCLA's] provisions liberally to avoid frustration of the beneficial legislative purposes."); *United States v. Burns*, No. C-88-94-L, 1988 WL 242553, at *1 (D.N.H. Sept. 12, 1988) ("The term 'owner' like the Act generally, should be construed broadly.") [hereinafter *Burns I*]; *United States v. South Carolina Recycling & Disposal, Inc.*, 653 F. Supp. 984, 1003 (D.S.C. 1984) (held lessee/sublessee liable as owners under CERCLA, stating, "[t]o conclude otherwise would frustrate Congress' intent that persons with responsibility for hazardous conditions bear the cost of remedying those conditions").

25. NEPACCO, 810 F.2d at 742-44.

26. See *Vermont v. Staco, Inc.*, 684 F. Supp. 822 (D. Vt. 1988).

some courts have construed CERCLA narrowly and have refused to further expand its scope.²⁷ The holdings rendered in *Phoenix I* and *Phoenix II*, however, further broadened the list of PRPs by including trustees. Since hazardous substance contamination is considered an environmental tort,²⁸ resolution of these trust law issues is imperative before one can analyze the liability of a trustee under CERCLA.

II. THE COMMON LAW OF TRUSTEES: PERSONAL LIABILITY

Trusts are a unique way of passing and holding title to property. A trust is a fiduciary relationship with respect to property. The person who holds the property is subjected to equitable duties to manage it for the benefit of another person, which arise as a result of a manifestation of intention to create it.²⁹

Trusts can be created in a variety of contexts. For example, trusts may be created for estate planning, business arrangements, sales transactions, debtor-creditor relationships and management of an individual's assets during his or her life. Trusts can also serve various purposes such as the conservation of property for beneficiaries.³⁰ The three principal players involved in a trust are the settlor,³¹ trustee³² and beneficiary.³³ The trustee and beneficiary each have an interest in

27. *Edward Hines Lumber Co. v. Vulcan Materials Co.*, 861 F.2d 155, 157 (7th Cir. 1988) ("It is not our function to design rules of liability from the ground up. A court's job is to find and enforce stopping points no less than to implement other legislative choices."); see also *Joslyn Mfg Co.*, 893 F.2d at 83 (holding that without an express congressional directive to the contrary, common-law principles govern the court's analysis).

28. *Phoenix II*, 827 F. Supp. at 603.

29. RESTATEMENT (SECOND) OF TRUSTS § 2 (1959) [hereinafter RESTATEMENT].

30. Some purposes include conservation of property for beneficiaries as a protection against their own inability to manage (whether due to disability, narvete regarding investments, susceptibility to excessive solicitations or spendthrift propensities), to avoid guardianship requirements for the receipt of assets by minors or other incapacitated persons, to minimize probate and accompanying transfer costs and, in certain instances, to minimize taxes. Karen J. Walsh & Fredda L. Cohen, "Overview of Trusts" Planning for the Elderly Client: Revocable Trusts, Irrevocable Trusts and Medicaid Trusts, N.Y.S.T.B.A., at 19 (Oct. 20, 1992) [hereinafter Overview].

31. The settlor is the grantor or donor in a deed of settlement who creates the trust. RESTATEMENT, *supra* note 29, § 3(1). The person who brings a trust into existence is known as either the "settlor," "grantor," "donor" or "trustor." Overview, *supra* note 30, at 19.

32. A trustee is a person holding property in trust. RESTATEMENT, *supra* note 29, § 3(3). The person or entity who is acting as the manager of the trust is known as the "trustee." The trustee has legal title to the trust assets and manages those assets in a fiduciary capacity. There may be more than one trustee for a trust, if the trust instrument so provides. Overview, *supra* note 30, at 20.

33. The beneficiary is the person for whose benefit property is held in trust. RESTATEMENT, *supra* note 29, § 3(4). The beneficiary can be an individual or a group of individuals or entities. The beneficiary has the right to receive some benefit from the trust property. The rights of the individuals or entities may vary as to income rights or principle distributions, or combinations of both. Such rights may be absolute or contingent on some circumstance (e.g., survival of income beneficiary) and they may be

the trust property, but the trustee holds only the legal interest while the beneficiary holds the equitable interest.³⁴

The only way to perfect a trust is by the settlor passing title of the property to the trustee by delivery of the trust subject matter of an instrument of transfer.³⁵ However, while the trustee holds *legal* title she has no economic interest in the trust enterprise and carries out her duties solely for the benefit of the beneficiary who is entitled to the entire economic interest in the trust enterprise.³⁶ The manner in which the trust is to be managed is set forth in the trust instrument.³⁷ The trust instrument generally grants the trustee broad powers to manage the trust property.

Many types of trusts can be created. Testamentary trusts (which are relevant to this discussion) are created under a testator's will and take effect when the testator dies, after the letters of trusteeship are granted and the will has been admitted to probate.³⁸ The trust may be changed until the testator's death, when it becomes irrevocable.³⁹

A. *Liability of Trustees*⁴⁰

The Restatement explains that a trustee is a person in a fiduciary relationship to the beneficiary and is under a duty to act for the benefit of the beneficiary as to matters within the scope of the relationship.⁴¹ Trustees may incur liability to third persons for torts committed in the course of administration of the trust⁴² or simply by

mandatory or discretionary with the trustee, according to the terms of the trust instrument. *Overview, supra* note 30, at 20.

34. RESTATEMENT, *supra* note 29, § 2f.

35. 3A AUSTIN W. SCOTT & WILLIAM F. FRATCHER, THE LAW OF TRUSTS § 265 (4th ed. 1988) [hereinafter 3A SCOTT]; 1 AUSTIN W. SCOTT AND WILLIAM F. FRATCHER, THE LAW OF TRUSTS § 2.6 (4th ed. 1987) (a trust exists only where title to property is held by one person for the benefit of another) [hereinafter 1 SCOTT].

36. Harlan F. Stone, *A Theory of Liability of Trust Estates for the Contracts and Torts of the Trustee*, 22 COLUM. L. REV. 527, 527 (1922).

37. Generally, a trust is created by a written instrument (but not always) which contains the terms and conditions of the trust. Such trust documents are often referred to as the "trust agreement" or "trust indenture." *Overview, supra* note 30, at 20. The typical powers a state bestows upon a trustee are found in the Uniform Trustees' Powers Act (which can be found within the UNIF. PROB. CODE, U.L.A. § 2-101 (1983)).

38. *Overview, supra* note 30, at 20. There are many other types of trusts, but for purposes of this Note, only testamentary trusts are explained since this was the type of trust at issue in *Phoenix I* and *Phoenix II*.

39. *Overview, supra* note 30, at 20-21.

40. The question of trustee liability by virtue of "ownership" and "power" is the precise issue dealt with in *Phoenix I* and *Phoenix II*.

41. RESTATEMENT, *supra* note 29, § 2.

42. RESTATEMENT, *supra* note 29, § 264, provides:

The trustee is subject to personal liability to third persons for torts committed in the course of the administration of the trust to the same extent that he would be liable if he held the property free of trust.

virtue of holding title to the trust property.⁴³ As the esteemed Harlan Fiske Stone explained, the rationale behind this general rule is that "the economic enterprise should carry the burdens of loss occasioned by the tortious acts of those engaged in it."⁴⁴ The beneficiary who is dispossessed of legal title, however, is not subject to the liabilities of third persons that are imposed upon the holder of legal title.⁴⁵

It is important to distinguish between a trustee who is held liable as a fiduciary of the trust and a trustee who is held liable personally.⁴⁶ When a trustee acts in her fiduciary capacity, she acts in a representative capacity with respect to property in which others own the beneficial interest. In contrast, a fiduciary, in her personal capacity, acts with respect to her own property. Accordingly, a claim brought against a trustee in her personal capacity is one against the trustee's own money, while a claim against the trustee in her fiduciary capacity is a claim against the trust's money.⁴⁷

Because a trust is not a person, it is incapable of committing a tort or being liable for any tort.⁴⁸ Thus, the victim of a tortious act must sue the trustee. If found liable in tort, the trustee must pay the damages out of her personal assets.⁴⁹ If personally without fault for the tortious act, however, the trustee may seek indemnification from the trust.⁵⁰

Indemnification, however, will fail to compensate the trustee when trust assets are insufficient. This is a questionable result, inasmuch as

43. RESTATEMENT, *supra* note 29, § 265, provides:

Where a liability to third person is imposed upon a person, not as a result of a contract made by him or a tort committed by him but because he is the holder of the title to property, a trustee as holder of the title to the trust property is subject to personal liability, but only to the extent to which the trust estate is sufficient to indemnify him.

RESTATEMENT, *supra* note 29, § 265 cmt. a, reads in part:

a. *Scope of the rule* Where, however, the trustee is liable only as holder of the title to the trust property, and where, without fault on the part of the trustee, the trust estate is insufficient to indemnify him, he is liable only to the extent to which the trust estate is sufficient to indemnify him. The modern trend has been to hold the trustee as holder of the title to the trust property liable to third persons only as trustee, that is only to the extent to which the trust estate is sufficient to indemnify him.

44. Stone, *supra* note 36, at 529.

45. RESTATEMENT, *supra* note 29, § 277 cmt. a.

46. The following discussion of trustee liability in a fiduciary capacity and a personal capacity is adapted from Michael L. Graham & Philip Lindquist, *City of Phoenix Case Lays Sound Foundation for the Environmental Liability of Fiduciaries*, 8 NAT. RESOURCES & ENV'T 2, 46 (1993) [hereinafter *Sound Foundation*].

47. *Id.*

48. GEORGE G. BOGERT & GEORGE T. BOGERT, THE LAW OF TRUSTS AND TRUSTEES § 732 (rev. 2d ed. 1982).

49. See Stone, *supra* note 36, at 527 ("[The trustee is] personally liable for the torts committed by him or his employees in carrying out the trust. ").

50. See *id.* ("[The trustee] may appropriate from the assets of the trust such amount as is required to indemnify him, unless his act in incurring the liability . . . [is a] violation of his duties as trustee. ").

the trustee derives no economic benefit from the trust except for a nominal trustee fee. The inequity of holding a trustee personally liable for a tort for which she is not personally at fault has led to the modern trend away from holding trustees personally liable.⁵¹

If a trustee acts for the benefit of the trust, one can proffer a strong argument that the trustee should be relieved of personal liability because any liabilities incurred by the trustee are in furtherance of an enterprise in which the trustee has no economic interest. If without personal fault, a trustee should have the right of exoneration from liability, not just indemnification for payments she actually makes.⁵² Such exoneration, however, is limited to situations where the trustee acted in good faith and actually benefitted the trust.⁵³

While traditionally courts held trustees personally liable for torts committed during the administration of the estate, modern statutes do not. The Uniform Probate Code (UPC) explicitly relieves trustees of personal liability when the trustee is not personally at fault for the tortious act.⁵⁴ Most states have adopted the relief afforded trustees by the UPC.⁵⁵ "The purpose of this [relief] is to make the liability of the trust and trustee the same as that of the decedent's estate and personal representative."⁵⁶ Since the Arizona court embraced traditional trust law instead of following the modern trend, the principles of the traditional law must be examined.

51. See UNIF. PROB. CODE § 7-306 (1989).

52. See generally Austin W. Scott, *Liabilities Incurred in the Administration of Trusts*, 28 HARV. L. REV. 725 (1915) [hereinafter *Liabilities*].

53. *Id.* at 735.

54. UNIF. PROB. CODE § 7-306 addresses personal liability of the trustee to third parties. The section reads in its entirety:

(a) Unless otherwise provided in the contract, a trustee is not personally liable on contracts properly entered into in his fiduciary capacity in the course of administration of the trust estate unless he fails to reveal his representative capacity and identify the trust estate in the contract.

(b) A trustee is personally liable for obligations arising from ownership or control of property of the trust estate or for torts committed in the course of administration of the trust estate only if he is personally at fault.

(c) Claims based on contracts entered into by a trustee in his fiduciary capacity, on obligations arising from ownership or control of the trust estate, or on torts committed in the course of trust administration may be asserted against the trust estate by proceeding against the trustee in his fiduciary capacity, whether or not the trustee is personally liable therefor.

(d) The question of liability as between the trust estate and the trustee individually may be determined in a proceeding for accounting, surcharge or indemnification or other appropriate proceeding.

UNIF. PROB. CODE § 7-306 (1989).

55. See *Sound Foundation*, *supra* note 46, at 66 ("[S]ection 7-306, or comparable language, has been adopted in thirty-two states, including California and New York, which are generally regarded as the bellwether states for purposes of fiduciary law.").

56. UNIF. PROB. CODE § 7-306 cmt. (1989).

B. *Liability in the Course of Administration of the Trust*

Traditional trust law holds trustees *personally* liable for torts committed in the course of the administration⁵⁷ of the trust and “for injuries resulting from the condition of the trust premises.”⁵⁸ According to section 264 of the Restatement, the trustee’s personal liability for a tort committed during the administration of the trust is the same liability she would bear if she held the property free of trust. In other words, liability attaches as if the property were her own. For example, under this section, a trustee would be liable for a personal injury arising from some defect in or on the trust property.⁵⁹ However, if the trustee discharged a liability incurred during the proper administration of the trust, she ordinarily has a right to be reimbursed by the trust.⁶⁰ But if the trustee was not authorized to incur the liability, she has no right to reimbursement.⁶¹

C. *Liability of Trustee as Title Holder*

Section 265 of the Restatement sets forth another way in which a trustee may incur liability under traditional common law: simply by holding title to the property. Examples of trustee liability arising by virtue of holding title to the property include property taxes, shareholder assessments⁶² and liabilities arising from covenants that run with the land. If liability attaches to the trustee because she is the holder of title to property, she is subject to personal liability, but only to the extent the trust estate is sufficient to indemnify her.⁶³

III. CITY OF PHOENIX V. GARBAGE SERVICES COMPANY

In two separate decisions, the Arizona court decided the issue of trustee liability under CERCLA. In the first decision, *Phoenix I*, the court held that a trustee is an owner within the CERCLA definition. In the second, *Phoenix II*, the court decided that as an owner, a trustee may be personally liable for response costs regardless of the trust’s ability to indemnify him.⁶⁴

The court synthesized CERCLA liability principles with those of the common law of trusts to develop a “new” standard by which to

57. RESTATEMENT, *supra* note 29, § 264.

58. *Liabilities*, *supra* note 52, at 726.

59. See *Cook v. Holland*, 575 S.W.2d 468, 472 (Ky. Ct. App. 1978); *Marion v. Chandler*, 81 S.E.2d 89, 93-95 (W. Va. 1954).

60. *Liabilities*, *supra* note 52, at 727.

61. *Id.*

62. RESTATEMENT, *supra* note 29, § 265 cmts. b, c.

63. *Id.* § 265.

64. The trustee in the *Phoenix I* and *Phoenix II* decisions will be referred to by masculine pronouns to avoid confusion since the court referred to Valley National Bank [hereinafter VNB] using the masculine pronouns. Feminine pronouns are used in this Note when discussing trustees in general.

judge the liability of a trustee under CERCLA. This new standard focuses on whether there is sufficient evidence from which to infer the trustee's "power to control" the use of trust property and whether she "knowingly" allowed the property to be used for the disposal of hazardous substances.⁶⁵ According to the court, those elements, when fused with CERCLA's definition of "owner," render a trustee personally liable for response costs.

Phoenix I is the most recently published decision addressing the issue of trustee liability under CERCLA. The City of Phoenix (City)⁶⁶ brought an action under CERCLA against defendant, VNB,⁶⁷ seeking to recover response costs that the City incurred in cleaning up a contaminated site.⁶⁸ The City alleged that the hazardous substances were deposited when the landfill was an asset of the settlor estate. VNB, however, argued that it was not an "owner" under CERCLA and therefore not a PRP.⁶⁹

The settlor, Wilbur Calvin Estes (Estes) owned a landfill site. In 1965, Estes sold the landfill but retained an option to repurchase it. Estes died later that year. His will nominated VNB as executor, and VNB agreed to assume that role. The will also provided for a testamentary trust and conveyed the balance of Estes' property, including the option to purchase the landfill, to VNB as trustee.

VNB exercised the purchase option on the landfill in 1966. At the time of purchase, Garbage Services Company (GSC) was managing the property.⁷⁰ Estes had been the president of GSC and owned 100 percent of its stock. VNB now held this stock as an asset of the trust formed by Estes' will.⁷¹

65. *Phoenix II*, 827 F Supp. at 607.

66. In an initial decision, *City of Phoenix v. Garbage Servs. Co.*, 33 Env't Rep. Cas. (BNA) 1655 (D. Ariz. 1991), "the court held that, under the then existing posture of the case, no liability attached to [VNB]. solely by virtue of the warranty deed conveying the landfill to the bank, as trustee, but that a question of material fact existed as to whether the bank bore the necessary indicia of CERCLA ownership in either its capacity as executor or trustee." See Kevin C. Murphy & Elizabeth C. Yen, *Court Limits the Potential of Trustee Liability for the Cost of Site Environmental Cleanup*, 111 BANKING L.J. 89, 90 (1994).

67. Several Amicus Curiae briefs were submitted on behalf of VNB: John Gill, Michael F. Crotty and Thomas J. Greco, American Bankers Ass'n, Washington D.C., on brief for amicus curiae American Bankers Ass'n; Michael L. Graham & Philip M. Lindquist, Baker & Botts, Dallas, TX, on brief for amicus curiae National Trust Real Estate Ass'n; G. Van Velsor Wolf, Jr. and Martha E. Gibbs, Snell & Wilmer, Phoenix, AZ, on brief for amicus curiae Arizona Bankers Ass'n; Theodore V.H. Mayer, Hughes Hubbard & Reed, New York City, on brief for amicus curiae IJB Schroeder Bank and Trust Co., The Northern States Trust Co., and U.S. Trust Co. of New York. *Phoenix II*, 827 F Supp. at 601.

68. *Phoenix I*, 816 F Supp. at 565-66.

69. *Id.* at 566.

70. *Id.*

71. *Phoenix II*, 827 F Supp. at 602.

VNB continued to lease the site to GSC, which managed and administered the landfill until 1972 when the landfill was closed.⁷² During the six years GSC managed the site for VNB, VNB paid the property taxes on the site and obtained liability insurance for the landfill. In 1980, the City initiated condemnation proceedings by which it acquired the entire landfill (the City had acquired parts of the landfill earlier). After the City incurred clean-up costs at the site, it filed an action against the trustee for reimbursement.⁷³

VNB moved for partial summary judgment on the ground that VNB was not an "owner" or "operator" of the landfill and was therefore not a responsible party under CERCLA.⁷⁴ The City responded by filing a cross-motion for summary judgment on the same issue.⁷⁵ In denying VNB's motion and granting the City's cross-motion, the court reasoned that while VNB did not qualify as an "operator," VNB was liable as an "owner."⁷⁶

In *Phoenix II*, VNB moved for partial summary judgment, to limit its liability to the amount of assets held in trust.⁷⁷ This motion was also denied⁷⁸ and VNB was held personally liable, beyond the trust's ability to indemnify.⁷⁹ The court held that any trustee who possesses "power to control" the use of the property and "knowingly" allows property to be used for hazardous substance disposal, is subject to personal liability.⁸⁰

IV. ANALYSIS OF THE PHOENIX DECISIONS

A. Trustee as Operator

In *Phoenix I*, the court first analyzed a trustee's status as a potential "operator." The City argued that since VNB's status as a trustee gave VNB "authority to control" the landfill, VNB should be held liable for response costs as an "operator."⁸¹ The court rejected the City's "operator" argument and explained that VNB was not involved in the day-to-day administration of the landfill and therefore did not qualify as an "operator."⁸²

Prior to *Phoenix I*, courts had defined "operator" not as one who had actual control over operations, but rather as one who possesses mere "authority to control" the operations and decisions relating to

72. *Phoenix I*, 816 F Supp. at 566.

73. *Id.*

74. *Id.*

75. *Id.*

76. *Id.* at 568 ("This court holds that a trustee is an 'owner' for the purposes of Section 107 of CERCLA, even though the trustee may hold only bare legal title.").

77. *Phoenix II*, 827 F Supp. at 601.

78. *Id.* at 607.

79. *Id.* at 606-607.

80. *Id.* at 606.

81. *Phoenix I*, 816 F Supp. at 567.

82. *Id.*

the disposal of hazardous substances at the site.⁸³ The Arizona court purported to adopt the definition of "operator" previously set forth by other courts.⁸⁴ Apparently, however, it was precisely VNB's lack of authority to control the day-to-day management and administration of the facility which discouraged the court from holding VNB responsible as an "operator."⁸⁵ Since operational matters were handled entirely by GSC, VNB could not, said the court, be held liable as an "operator."⁸⁶

The Arizona court's "operator" analysis, however, is flawed. Instead of analyzing whether VNB *could have* exercised control if it *chose to do so*, the court focused on what VNB *actually did* and did not do. If that is the analysis the court intended to adopt, a better way to describe the "Arizona operator standard" would be to state that a trustee must "actually have exercised control" over the day-to-day management and administration, in order to be held liable as an "operator" under CERCLA.

On the contrary, if the court intended to follow the precedents it cited,⁸⁷ then inquiry should have been made into whether or not VNB, as owner, had the authority to control the day-to-day details of operation.⁸⁸ Since the court neglected to make such an inquiry, the court did not adhere to earlier definitions of "operator." Nonetheless, the court did not hold VNB liable as an "operator" but rather as an "owner," so examination of the analysis shifts to trustee liability as an "owner."

83. This is the definition of "operator" that most courts have adopted. See *Nurad, Inc. v. Hooper & Sons Co.*, 966 F.2d 837, 842 (4th Cir. 1992); *Kaiser Aluminum & Chemical Corp. v. Catellus Development Corp.*, 976 F.2d 1338, 1341 (9th Cir. 1992) (relying on *Hines Lumber*, 861 F.2d 155 (7th Cir. 1988)); *Hines Lumber*, 861 F.2d at 157-158; *CPC Int'l Inc. v. Aerojet-General Corp.*, 731 F. Supp. 783, 788 (W.D. Mich. 1989); *Idaho v. Bunker Hill Co.*, 635 F. Supp. 665, 671-72 (D. Idaho 1986).

84. Apparently, the Arizona court read *Kaiser Aluminum*, 976 F.2d at 1341, as meaning "actual control." The Kaiser court held that "operator" liability under CERCLA attaches *only* if the defendant had the "authority to control" the cause of the contamination *at the time* the hazardous substances are released into the environment.

85. *Phoenix I*, 816 F. Supp. at 567 (The Arizona court based its conclusion on the following facts: "VNB did not enter into or negotiate contracts for the disposal of wastes at the landfill. VNB did not know the identity or the nature of GSC's customers. VNB's communication with GSC's personnel was limited to matters involving Estes' estate, such as tax questions, and not the operation of the landfill.").

86. *Id.*

87. The Arizona court cites cases in support of its conclusion which are in stark contrast to the position taken by the Arizona court. See generally *Nurad*, 966 F.2d 837 (4th Cir. 1992) and *Hines Lumber*, 861 F.2d 155 (7th Cir. 1988).

88. For support of this argument, see Kim Maree Johannessen, *Special Liability Issues and Caselaw Update Under Superfund*, C851 ALI-ABA 303, 313 (Aug. 18, 1993) ("While the Phoenix court did not reject the *Kaiser Aluminum* decision outright, it read it as requiring actual control over the operation of the facility.").

B. Trustee as Owner

Phoenix I stands for the proposition that trustees as holders of legal title are liable as "owners" under CERCLA.⁸⁹ That concept was first considered by the district court of New Hampshire in *Burns I*,⁹⁰ where the court discussed the potential liability of trustees as "owners" of the property.⁹¹

Burns I was a civil action under CERCLA against William Burns and others for response costs incurred in a clean-up of hazardous substances. The Gonic Realty Trust (Gonic) had acquired ownership of a certain industrial mill complex. Gonic had been established by Harry Freidberg and Raymond Crowley for the benefit of Gonic Realty Associates, a partnership formed by Freidberg and Crowley, the co-trustees.⁹²

During Gonic's ownership of the mill, Gonic hired a managing agent who leased portions of the mill to various tenants for business and manufacturing activities. One or more of these tenants left hazardous substances behind which contaminated the property. Crowley, as the sole trustee, directed the managing agent to contact EPA who determined that the hazardous substances had to be removed. EPA proceeded to "clean-up" and subsequently commenced an action for response costs.

Crowley moved to dismiss, asserting that he never owned the land and that he never personally participated in conduct that violated CERCLA.⁹³ The court rejected the argument and denied the motion. The court held that Crowley, as trustee, held legal title to the trust property and under trust law could be liable for obligations as the owner of the property.⁹⁴

Subsequently, the New Hampshire district court ruled on the merits and applied New Hampshire partnership law in *Burns II*.⁹⁵ Under New Hampshire partnership law, a partner may incur unlimited personal liability. Gonic was a partnership governed by a trust agree-

89. *Phoenix I*, 816 F. Supp. at 568.

90. See *Burns I*, 1988 WL 242553.

91. *Id.* at *2 ("as trustee, Crowley held legal title to the trust property and under trust law could be liable for obligations as the owner of the property.")

92. United States v. Burns, No. 88-094-S, slip op. at 2 (D.N.H. Aug. 9, 1990) ("Gonic Realty Trust was [eventually] dissolved and its assets were distributed to its partners. Freidberg transferred his beneficial interest in Gonic to Gracia Crowley for valuable consideration.") [hereinafter *Burns II*].

93. *Burns I*, 1988 WL 242553 at *1.

94. The court cited RESTATEMENT, *supra* note 29, §§ 265 and 265.1 and 3A SCOTT, *supra* note 35.

Graham and Lindquist argue that §§ 265 and 265.1 did not support the court's ruling. "It is ironic that the *Burns I* court relied on §§ 265 and 265.1 which do not support the court's ruling, when the court could have relied on § 277.1 which readily supports the court's refusal to dismiss Crowley as a party." *Sound Foundation*, *supra* note 46, at 9-10.

95. See *Burns II*, No. 88-094-S.

ment which subjected Crowley *as a partner* to unlimited liability. Crowley's status as a trustee was irrelevant in the court's determination of liability. The Arizona court, however, relied on *Burns I* as authority for imposing liability on a trustee as an owner. As explained, the *Burns II* court based its holding on partnership law—not trust law, thus the Arizona court's reliance was misguided.⁹⁶

In another attempt to buttress its decision, the Arizona court invoked *Lone Star Industries v. Horman Family Trusts*.⁹⁷ Based on *Lone Star*, the *Phoenix I* court stated that "[t]he EPA's practice seemingly is to argue that trustees are 'owners' within the meaning of CERCLA."⁹⁸ No text in *Lone Star* indicates that EPA issued a formal notice to the *Lone Star* trustee as an "owner."⁹⁹ While EPA did issue a formal notice to the trustee, among others, as notification that each was a PRP, there is no text in that decision that says EPA issued the notice to the trustee as "owner." *Lone Star*, however, alleged that "by accepting the waste CKD the Hormans and the Williamsens became the 'owners' thereof and 'accepted responsibility' therefore . . ."¹⁰⁰ It is not surprising that *Lone Star*, as plaintiff, would make such an assertion, but the fact remains that it was not EPA who made the assertion and the court's reliance on that misstatement of fact is again, misguided and unpersuasive.

The Arizona court found additional support in the legislative intent behind CERCLA. As an indication that Congress intended "owner" to have broad application, the court cited a House Report which

96. Graham & Lindquist in their *Amicus* brief point out that "the *Burns I* court's misunderstanding of Scott on Trusts did *not* result in that court's imposing CERCLA "owner" liability on the trustee in his personal capacity as a consequence of his ownership of contaminated property in his *fiduciary* capacity." Brief at 10 (emphasis in the original). See also *Burns II*, No. 88-094-S, at 8; *In re Gonic Realty Trust*, 50 B.R. 710, 711 (Bankr. D.N.H. 1985)).

Furthermore, the Arizona court misstated that the *Burns I* court could have disregarded the trust because Crowley was the sole trustee and beneficiary. Crowley was never the sole beneficiary of the Gonic Realty Trust. At all times, Crowley directly or indirectly owned only one-half of the trust's beneficial interests. Hence, the Arizona court's advancement of the precedential value of *Burns I* is unpersuasive.

97. 960 F.2d 917 (10th Cir. 1992). The only issue before the court in *Lone Star*, on appeal, was whether the amended complaint was sufficient to withstand a 12(b)(6) motion. Its relevance to the *Phoenix I* issue was the fact that the underlying complaint involved an action to recover response costs from the trustee.

98. *Phoenix I*, 816 F. Supp. at 568.

99. The court cites *Lone Star*, 960 F.2d at 921. The only reference to EPA's formal notice to the defendants is the following:

From paragraph 16 we learn that the Environmental Protection Agency on July 26, 1989, issued a formal notice to *Lone Star*, the Hormans and the Williamsens, advising all three that each was a "potentially responsible party" under CERCLA and, as such, each was potentially liable for response costs incurred in connection with remedial action at the site.

Id. In the above referenced excerpt from *Lone Star* EPA does not specifically refer to the Hormans (Sidney Horman was the trustee) as "owners," rather that was the Arizona court's interpretation.

100. *Id.*

states that “ ‘[o]wner’ is defined to include not only those persons who hold title to a . . . facility, but those who, in the absence of holding title, possess some equivalent indicia of ownership.”¹⁰¹ The court also pointed out that only one exception to titleholder liability is found in CERCLA which only “exempts lenders who hold ‘indicia of ownership primarily to protect [their] security interest.’ ”¹⁰² While not dispositive that Congress intended to include trustees as owners, the congressional intent analysis the court used is more persuasive than prior analysis in the decision. Mostly, the *Phoenix I* decision offered unpersuasive reasoning. A future court should have little trouble deviating from the *Phoenix I* holding by employing more cogent analysis.

For example, courts faced with issues regarding bankruptcy trustee liability under CERCLA have reached different conclusions. One court refused to hold a bankruptcy trustee liable as an “owner,” stating that “[i]t is the estate itself and not the [bankruptcy] trustee which is the owner. . . .”¹⁰³ In another case, a state court found that since a trustee did not act outside the scope of his authority in violating the state’s environmental laws, the trustee could not be subjected to personal liability.¹⁰⁴ Although those cases dealt with *bankruptcy* trustees, they offer an alternate method of reasoning for future courts faced with trustee liability. Should a future court find a trustee personally liable, however, analysis will shift to an exploration of the extent of trustee liability.

C. Personal Liability Imposed on Trustees Under CERCLA

In *Phoenix II*, a court squarely addressed for the first time the *extent* of a trustee’s liability under CERCLA. To reach its conclusion, the court attempted to synthesize CERCLA liability principles with trust common law. That synthesis was incorporated into a *uniform federal common law* which holds the trustee *personally* liable in certain cases.

In fashioning its uniform federal common law, the Arizona court first explained that nothing in the statute or its legislative history deals with the issue of trustee liability.¹⁰⁵ The Arizona court agreed with the Third Circuit that CERCLA’s meager legislative history and lack of case law dealing with trustee liability indicated that “Congress ex-

101. *Phoenix I*, 816 F. Supp. at 567 (quoting H.R. REP. NO. 172, 96th Cong., 2d Sess. 36, reprinted in 1980 U.S.C.C.A.N. 6119, 6160, 6181).

102. *Id.* at 568 (alteration in the original) (quoting 42 U.S.C. § 9601 (20)(A)).

103. *In re T.P. Long Chem., Inc.*, 45 B.R. 278, 283 (Bankr. N.D. Ohio 1985).

104. *Wisconsin v. Better Brite Plating, Inc.*, 483 N.W.2d 574 (Wis. Sup. Ct. 1992); see also *In re Sundance Corp., Inc.* 149 B.R. 641 (Bankr. E.D. Wash. 1993) (non-liability of a court appointed receiver).

105. *Phoenix II*, 827 F. Supp. at 602.

pected the courts to develop a federal common law to supplement the statute."¹⁰⁶

The court balanced the federal objectives of CERCLA with commercial relationships predicated on state law.¹⁰⁷ Following the Ninth Circuit lead,¹⁰⁸ the court purported to structure the uniform federal common law based on the common law of trusts. The court adopted the Restatement as a fair representation of common law because "[t]he law governing trustee liability is well settled, and is nearly uniform throughout all jurisdictions."¹⁰⁹ The court, however, ignored the modern trend in trust law adopted by most states.¹¹⁰

VNB argued that the court should adopt Restatement section 265 as the uniform federal law for trustee liability which would only hold trustees liable to the extent of the assets held in trust.¹¹¹ Since VNB did not contaminate the property, and therefore was not at fault, VNB argued that as title holder it should be held liable only to the extent of the amount of assets held in trust.¹¹² The court disagreed, and responded that CERCLA addresses a type of environmental tort which is not committed simply by virtue of holding title, but rather addresses a tort that is committed during the administration of the trust. Thus, Restatement section 264 is triggered, not section 265.¹¹³

Next, the court differentiated between CERCLA sections 107(a)(1) and 107(a)(2).¹¹⁴ The court agreed with VNB that under Section 107(a)(1), liability is imposed on current owners because of the mere

106. *Id.* citing *Louisiana-Pacific Corp. v. Asarco, Inc.*, 909 F.2d 1260, 1263 (9th Cir. 1990) (quoting *Smith Land & Improvement Corp. v. Celotex Corp.*, 851 F.2d 86, 91 (3d Cir. 1988)) (9th Cir. 1990).

107. *Phoenix II*, 827 F. Supp. at 602-03 (adopting the balancing test set forth in *United States v. Kimbell Foods*, 440 U.S. 715, 727-28 (1979)).

108. *Louisiana-Pacific Corp.*, 909 F.2d 1260 (9th Cir. 1990).

109. *Phoenix II*, 827 F. Supp. at 603. The City, VNB and *amici* all agreed, according to the court, that the RESTATEMENT, *supra* note 29, best represented the common law on issues of trustee liability in most jurisdictions.

110. Since most states have adopted the UPC provision relieving trustees of personal liability absent personal fault, the court should have incorporated this modern trend into the uniform federal common law. The Restatement sections adopted by the court were last updated in 1957, whereas the statutory law relieving trustees of personal liability is what the states have chosen to adopt more recently.

The statutory law exculpates trustees from personal liability when they are without fault. This approach is sensible, especially in light of the fact that a trustee receives little benefit from her position, but for a "nominal" fee received.

111. *Phoenix II*, 827 F. Supp. at 603.

112. *Id.*

113. *Id.* at 603-04 ("Liability does not arise from the mere fact of property ownership, but from the fact that property one owns (or previously owned) presents a potential environmental hazard. Environmental hazards do not just happen, as VNB and *amici* suggest; rather, somebody at some time used the property for the disposal of hazardous substances.").

114. *Id.* at 604 (construing 42 U.S.C. § 9607 (a)(1)-(2)). The statute, 42 U.S.C. § 9607(a)(1)-(2) reads as follows:

(a) Covered persons; scope; recoverable costs and damages; interest rate; "comparable maturity" date.

fact of property ownership, regardless of when or how the property became contaminated, and that under traditional common law principles, the trustee's liability would be limited to the amount of the assets held in trust.¹¹⁵ The court stated that liability under this subsection "is based on Congress' judgment that among innocent parties, the current owner of contaminated property should bear at least part of the burden of environmental clean up."¹¹⁶

In contrast, the Arizona court found that section 107(a)(2) imposed liability on current and past owners, provided that they owned the site at the time of disposal of the hazardous substances.¹¹⁷ The Arizona court interpreted the difference between sections 107(a)(1) and 107(a)(2) as that between the current property owner, who was not the owner at the time of disposal, and the current or past owner who was the owner at the time of disposal.¹¹⁸

Following its interpretation of sections 107(a)(1) and (a)(2), the court stated that by enacting CERCLA, Congress codified the common law rule of strict liability for ultrahazardous activities, and classified the disposal of hazardous substances as an ultrahazardous activity. According to the court (which did not cite any authority), under section 107(a)(2), an owner is strictly liable in his personal capacity for the disposal of hazardous substances, but an owner under section 107(a)(1) is strictly liable only in his representative capacity.¹¹⁹ Since the trustee had both the *power* and the *responsibility* to control the use of the property, the court reasoned, the owner should be personally responsible under section 107(a)(2).¹²⁰

In applying the above analysis to trustees, the court explained that if the trustee had the power to determine how the trust property would be used, section 107(a)(2) would impose strict personal liability on the trustee.¹²¹ Accordingly, the court held that under section 107(a)(2) an "owner" is *strictly liable* for response costs when the owner possesses *power* over the use of the property *and* has the *responsibility to control* the use of the property.¹²²

Notwithstanding any other provision or rule of law, and subject only to the defenses set forth in subsection (b) of this section:

- (1) the owner and operator of a vessel or a facility,
- (2) any person who at the time of disposal of any hazardous substance owned or operated any facility at which such hazardous substances were disposed of.

115. *Phoenix II*, 827 F Supp. at 604 (citing RESTATEMENT, *supra* note 29, § 265).

116. *Id.*

117. *Id.*

118. *Id.*

119. *Id.*

120. *Id.* ("Liability under this subsection is not based on mere ownership of property, but on the property owner's decision to allow his property to be used for an ultrahazardous activity.").

121. *Id.*

122. *Id.*

The court noted, however, that section 107(a)(2) does not apply to trustees in instances where the trust instrument strips the trustee of the power to control the use of the property.¹²³ Furthermore, section 107(a)(2) does not apply to trustees when the terms of the trust give a third person the exclusive power to control the actions of the trustee with respect to the use of the property.¹²⁴

To help clarify its holding, the court offered an illustration. If, for example, a trustee has control over the trust property, and *knowingly* allows it to be used for the disposal of hazardous substances, then it is the trustee who is responsible for the decision to use the property for an ultrahazardous activity.¹²⁵ According to the court, a trustee is not liable merely because he held title to the property, but because it was in his *power to control* the use of the property, *and* in exercising that power he chose to allow it be used it for the disposal of hazardous substances.¹²⁶

The Arizona court explained that in VNB's case the trustee chose to use the property as a landfill. Since that choice resulted in the contamination of the property, under section 107(a)(2), the trustee must be held liable for response costs.¹²⁷ Moreover, since the trustee's decision was made in the course of administration of the trust the court held the trustee personally liable regardless of the trust's inability to indemnify him.¹²⁸ The court relied entirely on the text of the Restatement section 264, without citing any case law in support of its conclusion.¹²⁹ VNB and *amici* argued that the Arizona court should have adopted the holdings of three Illinois federal courts which held that

123. *Id.*

124. *Id.* ("In such cases, the trustee's sole duty is to abide by the third person's wishes, provided they do not violate the terms of the trust."); see RESTATEMENT, *supra* note 29, § 185.

125. *Phoenix II*, 827 F Supp. at 605.

126. *Id.*

127. *Id.* ("The trustee is not liable merely because he held title to the property, but because it was in his power to control the use of the property, and he opted to use it for the disposal of hazardous substances. Although the trustee's status as the holder of legal title is the vehicle by which subsection 107(a)(2) imposes liability, there would not be any liability but for the trustee's decision.").

128. *Id.* (citing RESTATEMENT, *supra* note 29, § 264.)

129. Courts have been reluctant to hold trustees personally liable absent fault even before the statutory changes. See *Shriners Hosps. for Crippled Children v. Gardiner*, 152 ARIZ. 527 (Sup. Ct. 1987) (en banc) (court refused to hold trustee personally liable absent a breach of trust); *Matter of Heizer Corp. v. Hackbarth*, 1988 WL 58272 (Del. Ch. June 6, 1988) (absent gross negligence, the trustee is not personally liable for any error of judgment made in good faith); *Sisters of Mercy Health Corp. v. First Bank of Whiting*, 624 N.E.2d 520 (Ind. Ct. App. 1988) (according to Indiana statute a trustee is personally liable when injury results because of the trustee's personal act or omission); *Cook v. Holland*, 575 S.W.2d 468 (Ky. App. 1978) (trustee was found liable but the court notes that section 7-306 of the Uniform Probate Code was enacted *after* the date of the accident and that neither party cited that section).

trustees are not "owners" under CERCLA.¹³⁰ In all three cases, the Illinois courts refused to hold that "bare legal title" constitutes "ownership" for purposes of CERCLA.¹³¹

Under the terms of an Illinois land trust, a trustee is powerless and the beneficiary retains the power to direct or control the trustee in dealing with the title, and also has exclusive control of the management, operation, renting and selling of the trust property.¹³² The Illinois courts reasoned that since the trustee was powerless over decisions concerning the property held in trust, the trustee could not be considered an "owner." Since VNB possessed power to control the property (unlike Illinois land trustees), the Arizona court reasoned that VNB is liable under CERCLA. The Arizona court explained that it accepted the Illinois courts' holdings because the trustees in those cases were powerless trustees, but it rejected the Illinois courts' refusal to recognize trustees as "owners."

While trustees are powerless in Illinois and not in Arizona, the courts, nonetheless, differ on the fundamental point of whether a trustee is an "owner" or not. Regardless, the Arizona court found trustees are "owners" for purposes of CERCLA and chose to concentrate on a trustee's power to control the property. Apparently, that power to control the property was the pivotal factor in the Arizona court's decision. Still, the court had to incorporate trust law principles into its holding and synthesize the two fields of law.

D. *Synthesis of Trust Law and CERCLA*

The court set forth three general rules for trustee liability under CERCLA.¹³³ First, where a trustee is held liable under section 107(a)(1) as the current owner of contaminated property, the trustee's liability is limited to the extent that the trust assets are sufficient to indemnify him. This means that if a trust acquires property that is already contaminated, the trustee is liable as an "owner," but only to the extent of the assets held in trust.¹³⁴

Second, where a trustee is held liable under section 107(a)(2), but did not have the power to control the use of trust property, the

130. *United States v. N.L. Indus.*, 1992 WL 359986, at *4 (S.D. Ill. Apr. 23, 1992) ("It is inconsistent to exempt [secured parties] while holding liable a bank which merely administers the title for a nominal yearly fee."); *Premium Plastics, Inc. v. La Salle Nat'l Bank*, 1992 WL 309561, at *4 (N.D. Ill. Oct. 22, 1992) ("[T]his court will not subject an innocent party such as [the trustee] to liability in order to assure that plaintiffs have a source of recovery. . ."). *In re Petersen Sand and Gravel Inc.*, 806 F Supp. 1346, 1359 (N.D. Ill. 1992) ("Recognizing that trustee liability does not serve the legislative ends of CERCLA, the EPA does not consider trustees liable.").

131. *Id.*

132. *Phoenix II*, 827 F Supp. at 605 (citing *N.L. Indus.*, 1992 WL 359986 at *1). *N.L. Industries* and *Petersen* courts specifically refer to the trustee's lack of "control" over the trust in explaining the rationale behind the holdings.

133. *Id.* at 605.

134. *Id.*

trustee's liability is limited to the extent that the trust assets are sufficient to indemnify him. Thus, when the trustee had no power over the decisions which resulted in the contamination of the property, her liability is limited to the assets held in trust.¹³⁵

Finally, where a trustee has the power to control the use of trust property, and knowingly allowed the property to be used for the disposal of hazardous substances, then the trustee is liable under section 107(a)(2) to the same extent that she would be liable if she held the property free of trust. This rule holds the trustee personally liable, beyond the assets held in trust, because the trustee *chose* to permit the contamination of the property.¹³⁶

The first rule relates to the liability of the trustee as a current owner who was not the owner at the time of disposal of hazardous substances. The second and third rules relate to the liability of current and past owners who were the owners at the time of disposal.¹³⁷ Trustees who come within the definitions set forth in the second and third rules will be held personally liable.

The court's decision raises several concerns. For example, the court presupposes that in 1966, VNB "knew" that the substances deposited in the landfill were "hazardous." What did the court mean by "knowingly?" It cites no evidence that VNB knew that the substances in the landfill were hazardous or that VNB was cognizant of the possible ramifications. Perhaps the court meant that regardless of whether a trustee knew the substances were hazardous, the mere fact that the trustee's decision consequently gave rise to contaminated property and clean-up costs is enough to hold the trustee personally liable. Such ambiguity leaves room for various interpretations. For example, some future court may interpret knowingly as requiring a showing that the trustee possessed actual knowledge, while another may only require a showing that the trustee possessed mere constructive knowledge.

Seemingly as a justification for its holding, the court asserted that its general rules are "consistent with the stated position of the environmental rule on lender liability."¹³⁸ In 1992, EPA issued its "Final Rule"¹³⁹ on lender liability which significantly reduced the circum-

135. *Id.*

136. *Id.*

137. *Id.*; see also *Sound Foundation*, *supra* note 46, at 66. *Amicus curiae* Graham and Lindquist suggest that the court formulated the first two general rules in reliance on RESTATEMENT, *supra* note 29, § 265, and are sound statements of the applicable law. General rule 3, on the other hand, is premised on RESTATEMENT, *supra* note 29, § 264. Graham and Lindquist reject this rule because the "court mistakenly looked to § 264 as the currently operative rule of decision in most states, and thus adopted the wrong approach in its third rule." *Sound Foundation*, *supra* note 46, at 66.

138. *Phoenix II*, 827 F Supp. at 606.

139. 57 Fed. Reg. 18,344, 18,349 (to be codified in 40 CFR 300). EPA expressed this view in the Summary as follows:

stances under which a lender can be held liable under CERCLA. The Final Rule does not exempt trustees from liability under CERCLA. The preamble to the Final Rule, however, discusses why trustees are not specifically excluded, but does not advocate holding trustees personally liable.

Furthermore, the Arizona court emphasized EPA's reference to "innocent" trustees in its Final Rule. The Arizona court construed "innocent" as meaning those trustees "that would have no way of knowing whether the trust's property was contaminated, nor would they have been able to have prevented the contamination."¹⁴⁰ It is important to note that EPA did not define the term "innocent"; rather the court gave it a meaning. The court seems to have disregarded EPA's emphasis that courts should rely on "the applicable laws governing trustee and fiduciary liability."¹⁴¹ The applicable laws, when interpreted in light of the developing trend in trust law, would relieve a trustee from personal liability.

IV. LEGISLATIVE ACTION

Both the House of Representatives and the Senate have proposed legislation which would provide fiduciaries some protection from CERCLA. Currently, four bills are in various committees, three of which specifically address fiduciary liability under CERCLA.¹⁴²

On June 17, 1993, Senator D'Amato introduced the Depository Institutions Regulatory Improvements Act of 1993¹⁴³ ("D'Amato Bill") which seeks "to enhance credit availability by streamlining Federal regulations applicable to financial institutions."¹⁴⁴ The bill is designed to remove and lighten regulatory burdens on lending institutions by including environmental provisions which limit CERCLA lender liability for those who hold property in a fiduciary capacity.¹⁴⁵

The proposed rule did not address trustees because neither the section 101(20)(A) security interest exemption nor any other section of CERCLA makes any special provision for trustees. However, with one important exception, EPA agrees with most of the commentators' general statements regarding the circumstances under which trusts and trustees are responsible for costs incurred under CERCLA to address hazardous substance contamination, because they are generally accurate statements of the applicable laws governing trustee and fiduciary liability: "innocent" trustees or fiduciaries are not liable under CERCLA.

140. *Phoenix II*, 827 F Supp. at 606.

141. 57 Fed. Reg. 18,344, 18,349.

142. A fourth bill is H.R. 3800, 103d Cong., 2d Sess., introduced by Rep. Swift offers scant relief to "owners" and "operators" under CERCLA.

143. S. 1124, 103d Cong., 1st Sess. (1993).

144. See S. 1124, synopsis (1993).

145. S. 1124, 103d Cong., 1st Sess., § 201 (e)(3); See Theodore C. Taub, *Pre-Transaction and Transactional Issues Involving Hazardous Materials/Waste*, C851 ALI-ABA 251, 329 (1993).

The D'Amato bill also provides a "safe harbor" provision which relieves a trustee, *inter alia*, of CERCLA liability when such liability is based solely on the fact that the trustee "ha[d] the unexercised capacity to influence operations at or on property in which it has a security interest."¹⁴⁶ This provision would protect those trustees who possess the typical trustee powers but who do not actually manage the property operations.¹⁴⁷

Two other bills introduced are still in the House of Representatives. Representative La Falce introduced H.R. 2462 (La Falce bill) on June 18, 1993¹⁴⁸ and Representative Cox introduced H.R. 2718 (Cox bill) on July 26, 1993.¹⁴⁹ Like the D'Amato bill, the La Falce and Cox bills both seek to limit potential CERCLA liability of trustees and other fiduciaries. The La Falce bill seeks to relieve a trustee from liability when she is not at fault for the property contamination. Further, it attempts to narrow liability to of those who participate in the "actual" management instead of holding a fiduciary liable for merely having the "capacity to influence" the property operations.¹⁵⁰

The Cox bill proposes to remove a trustee from the "owner" and "operator" definition under CERCLA but does not protect one who places property in trust in order to shield herself from CERCLA liability.¹⁵¹ Moreover, the Cox bill offers additional comfort to the trustee community by providing that a trustee liable under CERCLA is liable only in her representative capacity. Accordingly, a trustee would not be liable beyond the trust's ability to indemnify the trustee.¹⁵²

V. CONCLUSION

The *Phoenix I* and *Phoenix II* decisions present a *double entendre*. Although the courts' approach to the issue of trustee liability under CERCLA is strained and, in some respects, erroneous, it did establish a good framework for analysis by basing its decision in part on trust law. The court did lament the fact that CERCLA "casts too wide a net," perhaps indicating that it felt compelled to hold the trustee liable.¹⁵³

146. S. 1124, § 201(b); Taub, *supra* note 145, at 329. "Security interest" includes a "deed of trust." See S. 1124, 103d Cong., 1st Sess., § 201 (e)(8).

147. It is important to note that the D'Amato bill is careful not to define trustee liability too broadly. For example, if a trustees "cause" or "significantly and materially" contribute to the release of hazardous substances they are responsible for clean-up. See S. 1124 § 201(c).

148. H.R. 2462, 103d Cong., 1st Sess. (1993).

149. H.R. 2718, 103d Cong., 1st Sess. (1993).

150. H.R. 2462 § 2(5).

151. H.R. 2718 § 1(a)(2)(F)(3).

152. H.R. 2718 § 1(a)(2)(F)(II).

153. *Phoenix II*, 827 F Supp. at 605.

On the one hand, by formulating a uniform federal rule of decision based on trust law, the decisions provide future courts with a solid framework for analysis.¹⁵⁴ On the other hand, the court mistakenly looked to Restatement section 264 as the currently operative rule of decision in most states and completely disregarded UPC section 7-306 which explicitly resolves trustees of liability absent fault.¹⁵⁵ This is a significant oversight because the court, without any explanation, completely disregarded the rule in most states, enabling environmental plaintiffs to reach trustees' personal assets.

It is impossible to predict how future courts will decide the trustee liability issue. It is certain, however, that they will experience great difficulty, mainly because it is unclear what Congress *intended* by including "owner" as a PRP under CERCLA. If future courts decide to interpret "owner" by its plain meaning, trustees will have to be found liable as an owner. This is so because CERCLA does not differentiate between legal and equitable owners. Nor is there legislative history to guide the courts.

It is unlikely, however, that future courts will hold "owners" liable based solely on ownership, *regardless of other factors*, since they have been reluctant to do so in the past. For example, in cases involving shareholder liability under CERCLA, courts have refrained from holding a shareholder liable based solely on its ownership of the corporation.¹⁵⁶ Rather, shareholders have been held liable as "operators" in situations where they controlled and directed the hazardous activity.¹⁵⁷ Moreover, in *Phoenix I* and *Phoenix II*, the Arizona court made a painstaking effort to hold the trustee liable for reasons other than mere legal ownership.¹⁵⁸

As explained, a trust is a unique form of ownership since legal title to property is divorced from equitable title. The trustee derives none of the benefits of a "typical" property owner.¹⁵⁹ Simply put, a trustee's ownership is different and should be treated differently. The question which must inexorably follow is, how?

Since the beneficiary is the beneficial owner of the property, it is the beneficiary who benefits from the ownership. It follows, therefore, that the beneficiary should be deemed the "true" owner of the property. If, however, Congress intended that ownership must be accompanied by other factors, then a court may consider a beneficiary's lack of control over the disposition or use of the property before taking

154. See *Sound Foundation*, *supra* note 46, at 66.

155. The UPC supersedes RESTATEMENT, *supra* note 29, § 264, which was last updated in 1957.

156. NEPACCO, *supra* note 19, at 743-44; *United States v. Kayser-Roth Corp., Inc.*, 910 F.2d 24, 27 (1st Cir. 1990).

157. *Id.*

158. *Phoenix II*, 827 F Supp. at 604.

159. The trustee derives no benefit from the trust property as long as the trustee is not also the beneficiary.

title and refuse to hold a beneficiary liable under CERCLA.¹⁶⁰ Because of the unique ownership of trusts, however, neither a trustee or a beneficiary fit comfortably into the "owner pigeonhole."¹⁶¹ Consequently, a court may choose to resolve this conflict by holding both the trustee and beneficiary liable.¹⁶²

Moreover, a future court may choose not to follow the Arizona court's decision. Instead, trustees' liability may be limited to the assets held in trust. Since contaminated property may be valueless, no funds may be available.¹⁶³ Troubling, however, is that "such a limitation on liability would create a powerful incentive for covered persons to place contaminated property in trust, in order to shield themselves from liability."¹⁶⁴ Therefore, it would be imperative that a court investigate the purposes behind a party's creation of a trust.

Should a future court follow the lead of the Arizona court, a different standard could be employed that would protect past trustees who could not have "known," at the time decisions were made, the future ramifications of those decisions. If a future court chooses to follow the Arizona court's lead by adopting traditional trust law instead of the growing statutory law, a more difficult burden of "knowing" should be employed, at least with respect to trustees who made decisions predating CERCLA.

For example, before a trustee is held personally liable beyond the extent of the trust assets, there should be a showing that the trustee acted "with wanton and reckless disregard" for the consequences. As for prospective trustees, the Arizona court's "knowingly" standard must be clarified and an actual knowledge requirement should be implemented instead of merely requiring constructive knowledge. It is desirable to employ skilled trustees to deal with the complex issues present in the environmental realm. Accordingly, there should be concern among the legal community that such skilled people not be alienated by a draconian regulation scheme.¹⁶⁵

Alternatively, Congress could amend CERCLA to exclude innocent trustees from personal liability. In fashioning a definition for "innocent," Congress could incorporate a "knowing" standard such as the one suggested above. While the bills currently in the House and Senate offer some relief and protection to trustees, they do not offer enough protection. Although it is inadvisable to offer blanket fiduciary protection, trustees without fault should not be held personally liable.

160. George Pendygraft et al., *Who Pays for Environmental Damage: Recent Developments in CERCLA Liability and Insurance Coverage Litigation*, 21 Ind. L. Rev. 117, 137 (1988).

161. *Id.*

162. *Id.*

163. *Id.* at 138.

164. *Id.*

165. See generally *Better Brite*, 483 N.W.2d at 583.

It remains to be seen exactly how successful the trustee community will be in exerting pressure on EPA and Congress to make amendments to protect trustee personal assets. Until then, trustees can consider themselves on the membership list of the non-exclusive CERCLA club!

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