Fourth Circuit Continues Trend toward Narrowing Scope of CERCLA Arranger Liability

Action Item: With federal courts moving toward limiting arranger liability under CERCLA, companies that sell new or used products containing hazardous substances should heed the guidance of those courts and take certain precautions to minimize their exposure to liability. For further information, please contact John DiChello or a member of Blank Rome’s Environmental, Energy and Natural Resources Practice Group.

The United States Court of Appeals for the Fourth Circuit is the latest federal appellate court to address the element of intent necessary to establish a claim for arranger liability under § 107(a)(3) of the Comprehensive Environmental Response, Compensation & Liability Act (“CERCLA”), 42 U.S.C. § 9607(a) (3). On March 20, 2015, the Fourth Circuit in Consolidation Coal Co. v. Georgia Power Co., No. 13-1603 (4th Cir.), held that an electric utility lacked the requisite intent to dispose of hazardous substances to qualify as an arranger when it sold used, but functional electrical transformers lined with oil containing polychlorinated biphenyls (“PCBs”) at competitive auctions to a purchaser who subsequently repaired, rebuilt, and resold the transformers to third parties for a profit. This ruling is consistent with a seeming trend toward limiting arranger liability since the United States Supreme Court issued its landmark decision in 2009 in Burlington Northern & Santa Fe Railway Co. v. United States, 556 U.S. 599 (2009). The ruling in Georgia Power also evidences the highly factual, case-specific analysis required to evaluate a putative arranger’s liability.

Background on CERCLA Arranger Liability

Section 107(a) of CERCLA imposes liability for the response and cost of cleaning up environmental contamination by hazardous substances on four classes of potentially responsible parties, one of which is “arrangers.” 42 U.S.C. § 9607(a). CERCLA defines an “arranger” as follows:

any person who by contract, agreement or otherwise arranged for disposal or treatment, or arranged with a transport for transport for disposal or treatment, of hazardous substances owned or possessed by such person, by any other party or entity, at any facility or incineration vessel owned or operated by another party or entity and containing such hazardous substances.42 U.S.C. § 9607(a)(3).

CERCLA, however, does not define the term “arrange.”

The Supreme Court in Burlington Northern clarified what it means to “arrange for disposal.” In short, a party must “take[] intentional steps to dispose of a hazardous substance” to be
liable as an arranger. The Court provided some guidance on the type of evidence that could satisfy the intent element for purposes of arranger liability. For example, a party’s knowledge that its product will be spilled by others may constitute evidence of that party’s intent to dispose, but knowledge, without more, is insufficient to prove the necessary mens rea. Moreover, “CERCLA liability would attach ... if an entity were to enter into a transaction for the sole purpose of discarding a used and no longer useful hazardous substance,” but “an entity could not be held liable as an arranger merely for selling a new and useful product if the purchaser of that product later, and unbeknownst to the seller, disposed of the product in a way that led to contamination.” Most cases, including Georgia Power, fall between the latter two extremes and demand a fact-intensive inquiry.

The Fourth Circuit’s Decision in Georgia Power

The Facts

Georgia Power Company (“Georgia Power”), an electric utility, used electrical transformers to generate electricity. When it stopped using transformers, Georgia Power inspected them, tested them for PCBs, and discarded transformers that were unusable or contained PCBs at levels exceeding 50 parts per million (the Toxic Substances Control Act (“TSCA”) prohibited the sale of transformers containing PCBs at such concentrations). Georgia Power retained certain transformers for its own reuse, but it also sold at auction transformers that could be repaired and reused after it drained and removed the oil from the transformers. The oil removal process drained all oil except for a thin sheen within the transformers and on certain inner parts. Georgia Power left some of the drained transformers uncapped and exposed to moisture prior to sale, making the internal components susceptible to damage.

During the 1980s, Ward Transformer Company (“Ward”) was in the business of purchasing used transformers, repairing and reconditioning them, and then reselling the transformers. Ward purchased 101 used transformers from Georgia Power at four different auctions. Ward also bid on additional lots of transformers sold by Georgia Power, but lost to other bidders. Some of the transformers that Ward acquired included oil that had not been drained or residual oil containing PCBs. After reconditioning and rebuilding some of the transformers in accordance with its customers’ specifications, Ward resold all 101 transformers in working condition to third parties for a profit. None of the transformers were sold for scrap. PCB-laden oil was discharged at the Ward site during the time that Ward stored and worked on the transformers.

Around the same time, Savannah Electric and Power Company (“Savannah Electric”), which later merged with Georgia Power, replaced all its transformers that contained PCBs. In doing so, Savannah Electric sold 20 transformers at auction to Electric Equipment Company of New York (“EECNY”). None of the transformers had been drained of oil containing PCBs. The transformers were functioning, in good shape, lacked problems or defects, and required no remanufacturing other than in some instances alteration of outdated voltage configurations. EECNY shipped the transformers to the Ward site and, after Ward updated the voltage configurations of certain transformers, Ward sold all 20 transformers for a profit. PCBs were released at the Ward site at that time.

Procedural History

Consolidation Coal Company (“Consol”) and Duke Energy Progress, Inc. (“Progress”) initiated cleanup at the Ward site pursuant to an administrative settlement with the United States Environmental Protection Agency, and PCS Phosphate Company, Inc. (“PCS”) subsequently joined the remediation efforts pursuant to a trust agreement with Consol and Progress. Consol and Progress then sued Georgia Power, PCS, and others seeking contribution for cleanup costs under § 107(a)(3) of CERCLA. PCS counterclaimed and asserted a cross-claim against Georgia Power and others for contribution. Consol, Progress, and PCS contended that Georgia Power “arranged for disposal” of PCBs under CERCLA when it sold the used transformers with oil containing PCBs to Ward. They argued that Georgia Power had a dual intent—to gain revenue by selling the transformers, on the one hand, and to get rid of PCBs, on the other hand—and that this “secondary motive” was sufficient to create arranger liability.

The Court’s Analysis

In affirming the district’s court grant of summary judgment in favor of Georgia Power, the Fourth Circuit in Georgia Power held that Georgia Power lacked the requisite intent for disposal articulated by the Court in Burlington Northern and Fourth Circuit case law to qualify as an arranger. The Fourth Circuit concluded that no direct evidence existed that Georgia Power
intended to arrange for the disposal of PCBs when it sold used transformers. Rather, the evidence showed that Georgia Power sold transformers at auction to generate revenue and achieve the greatest commercial advantage. The mere fact that Georgia Power called the sales of used transformers “scrapping” and “disposals” in its internal documents, the Fourth Circuit stated, did not demonstrate that Georgia Power possessed the necessary intent to dispose for purposes of arranger liability because it was clear Georgia Power used those terms to reflect transformers that were “actually sold” to others. The Fourth Circuit added that Georgia Power’s testing of PCB concentrations in used transformers before sale reflected its efforts to comply with TSCA requirements, not any intention to dispose of PCBs.

The Fourth Circuit in Georgia Power also did not find any circumstantial evidence of Georgia Power’s intent to dispose of PCBs. To reach this conclusion, and consistent with the dictates of Burlington Northern, the Fourth Circuit applied the following four factors enumerated in Pneumo Abex Corp. v. High Point, Thomasville and Denton Railroad Co., 142 F.3d 769 (4th Cir. 1998), for determining whether a party arranged for the disposal of a hazardous substance or merely sold a valuable product:

1. “the intent of the parties to the contract as to whether the materials were to be reused entirely or reclaimed and then reused”;
2. “the value of the materials sold”;
3. “the usefulness of the materials in the condition in which they were sold”; and
4. “the state of the product at the time of transferral (was the hazardous material contained or leaking/loose).”

The Fourth Circuit concluded that these factors, taken individually or together, counseled against a finding that Georgia Power intended to dispose of PCBs.³

As to intent for reuse of the product, the Fourth Circuit concluded that the evidence showed Georgia Power sold the used transformers entirely for reuse and Ward intended to reuse the transformers to the fullest extent. There was no evidence that Georgia Power or Ward intended for the transformers to be scrapped or sold for parts as reclaimed materials. Moreover, at the time of sale Georgia Power and Ward did not have any agreement or understanding on how Ward would handle the PCB-containing oil or parts. Indeed, Georgia Power had no knowledge of or control over Ward’s use of the transformers that it purchased and did not know anything about Ward’s reuse of the oil and oil-coated parts containing PCBs. The Fourth Circuit reasoned that Ward’s decision not to reuse oil or parts coated with oil did not imply that Georgia Power intended to dispose of oil when selling the transformers because the specifications of Ward’s customers and Ward’s own business judgment dictated the way in which Ward processed and rebuilt the transformers.

As to the value of the materials sold, the Fourth Circuit found that the used transformers sold by Georgia Power had marketable commercial value. Georgia Power sold the used transformers at competitive auctions for amounts “in excess of scrap value” so that they could be resold to third parties. Ward, for its part, profited from the resale of the transformers, reselling most, if not all, of the transformers to third parties for “thousands of dollars more than what Ward paid Georgia Power” after rebuilding and reconditioning them. In addition, the Fourth Circuit noted there was no evidence that Ward paid less for transformers based on the presence or absence of PCBs—a fact that would have suggested Georgia Power intended to get rid of waste when it sold the used transformers. In fact, the undrained transformers carried more value with oil and oil-coated parts because they could not function without them. And the presence of residual PCB-oil sheen in drained transformers did not increase Ward’s repair and rebuilding costs or affect the auction price of the transformers. Simply put, there was no evidence that the sale of used transformers to Ward amounted to “an intended PCB disposal arrangement.”

Furthermore, the Fourth Circuit concluded that the concentration of PCBs did not factor into the usefulness of the transformers sold by Georgia Power. Although Georgia Power decided to keep some of the used transformers rather than sell them, its decision was not motivated by the content of PCB in the transformers. Rather, Georgia Power retained certain used transformers based on their age, obsolescence, the need for a particular transformer type, and the nature and extent of necessary repairs. The Fourth Circuit further reasoned that Ward was not required to remove oil containing PCBs from the transformers that it purchased from Georgia Power; its customers’ specifications dictated removal of that oil.
With respect to the **state of the product** at the time of sale, the Fourth Circuit stated that the evidence showed the transformers including PCB-oil were not leaking and were capped when Georgia Power sold them to Ward. No evidence existed that any transformers leaked or spilled during the sale transfer. In other words, the transformers containing PCBs were contained when sold, but became hazardous when used by Ward.

Lastly, in addition to the *Pneumo Abex* factors, the Fourth Circuit in *Georgia Power* analyzed whether Georgia Power had **knowledge** of any spills of oil containing PCBs by Ward. The court concluded that Georgia Power did not have even knowledge of the disposition and processing of the transformers after Ward purchased them, much less knowledge of spills. The only evidence regarding knowledge of any kind concerned Georgia Power’s general expertise concerning transformers and PCB-laden oil. The Fourth Circuit stated that, based on Georgia Power’s “clear intent to sell a valuable product on a competitive market, and its lack of specific knowledge regarding how Ward would process the transformers, the ‘knowledge’ factor [was] of no aid to Consol and PCS.”

For these reasons, the Fourth Circuit affirmed the district court’s ruling that Georgia Power lacked the requisite intent for arranger liability under § 107(a)(3) of CERCLA.²

**Lessons Learned**

The Fourth Circuit’s decision in *Georgia Power* reaffirms that the element of intent for purposes of arranger liability under CERCLA is difficult to prove and requires a fact-intensive determination. That determination involves several factors, including: (1) whether the parties intended for the product to be reused entirely or sold for parts or scrapped; (2) the value of the product (is it more than “scrap value”); (3) the usefulness of the product (can the product be reconditioned, resold, and used again, or perhaps even used “as is”); (4) the state or condition of the product when sold (was it leaking or spilling, and did the seller take steps to remove or contain the hazardous substance); (5) the seller’s knowledge of the disposal (which may provide evidence of intent, but does not equate to intent); and (6) the ownership, possession, and control of the product at the time of disposal.

*Georgia Power* also underscores the importance of taking certain precautions to minimize the risk of arranger liability under CERCLA. For example, if a company sells a used product, it should prepare the item for sale by removing hazardous substances to the greatest extent possible and ensuring such substances cannot be released from the product during sale or transport. Moreover, like Georgia Power, a company may create different internal procedures and processes for sales of products, on the one hand, and disposals of waste/scrap, on the other hand. A company also could list used, but useful products containing hazardous substances as assets on its balance sheet to show that it has assigned real monetary value to the products and does not consider them to be mere waste or scrap. And while the use of terms like “scrap” and “disposal” did not hurt Georgia Power’s defense, a company should choose other ways to describe its legitimate sale of used products to avoid any confusion or basis for arguing arranger liability.

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1. In arguing their respective positions on the *Pneumo Abex* factors, Georgia Power focused on the overall product—i.e., used transformers—while Consol and PCS concentrated on the hazardous waste within the product—i.e., PCB-contaminated oil. The Fourth Circuit in *Georgia Power* explained that “if the hazardous materials are an ‘incidental’ component of a legitimate sale, then their inclusion in the transaction may well demonstrate nothing more than the seller’s intent to complete the sale of the overall product.” On the other hand, “if the hazardous material could practicably have been excluded from the sale, that may suggest the seller entered the transaction with a further intent to arrange for a disposal.” The Fourth Circuit seemed to focus its analysis more on the overall product (the used transformer) than the hazardous waste within the product (oil containing PCBs).

2. The Fourth Circuit also concluded that the *Pneumo Apex* factors did not support an inference that Savannah Electric (which merged into Georgia Power) intended to dispose of PCBs when it sold 20 used, but useable and working, transformers at auction because Savannah Electric intended for the transformers to be reused entirely; the transformers retained significant value; the transformers were in useful condition; and the transformers did not leak at the time of sale. The circumstances “[fell] squarely on the side of a legitimate sale and against arranger liability.”

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