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LENDER LIABILITY FOR ENVIRONMENTAL DAMAGE

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I. INTRODUCTION

WHY make a commercial lender liable for environmental damage? As Jarvis and Fordham observe:[1] "Banks do not pollute rivers. Why should they be responsible for the activities of their borrowers? If someone buys a car and kills a pedestrian the bank which provided the loan is not held responsible." Answers vary.[2] Lenders provide the funds to enable the polluting activity to continue and may have made considerable profits from that activity. Lenders have "deep pockets" and are able to meet clean-up costs. Lenders are in a good position to investigate and require environmental compliance from their borrowers. Political and economic considerations are at work here just as much as legal ones.[3]

The risk of environmental liability must be taken seriously by commercial lenders and their advisers. It has direct and indirect consequences for the lender. The most important *direct* consequence is the possibility that the lender itself may be held liable to pay a fine, clean-up costs or compensation to affected persons (liability risks). The *indirect* consequences can be just as serious. Environmental compliance costs may affect the borrower's ability to service its debt (credit risks). Clean-up costs may reduce the value of the asset over which the lender has taken security (security risks).

This article has two aims. First, to examine how credit risks, security risks and, particularly, liability risks arise. Secondly, to consider how lenders may reduce their exposure to such risks. These issues have recently been brought sharply into focus by the introduction on 1 April 2000 of a new, and potentially far-reaching, contaminated land regime in England under Part IIA of the Environmental Protection Act 1990, as amended by the

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[1] J. Jarvis Q.C. and M. Fordham, *Lender Liability: Environmental Risk and Debt* (1993), p. 2.
[2] *Ibid.*, p. 2. M. Fordham, "A rude awakening" [1993] N.L.J. 750.
[3] See R.M. Auerback, "Environmental Law, Practice and Liability: Background", Ch. 1 in J.J. Norton, R.M. Auerback and J.M. Gaba (eds.), *Environmental Liability for Banks* (1995).

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Environment Act 1995.[4] The main objective of the regime is to provide an improved system for the identification and remediation (clean-up) of contaminated land, where the contamination is causing unacceptable risks to human health or the wider environment. This article is set against the backdrop of that new regime.

II. Indirect Consequences

(a) Credit Risks

The cost of environmental compliance may affect the borrower's profitability and hence its ability to service its debt. Strict licensing regimes control various areas of commercial activity where there is a recognised risk of pollution. The compliance costs of meeting the conditions attached to such licences can be high. Failure to obtain a licence or breach of licensing conditions can bring heavy fines.[5] There are also various statutes giving regulatory authorities powers to require clean-up by the polluter or the owner or occupier of land.[6] Again, the costs may be high and insurance cover may be difficult, if not impossible, to obtain. At common law, the borrower may be held liable to pay compensation to affected persons for nuisance, under the rule in *Rylands* v. *Fletcher*,[7] for negligence, or for breach of statutory duty. Moreover, a borrower can incur liability in other countries as a result of operations there, or because of products exported there, or because of operations in the

[4] The Act is supplemented by the Contaminated Land (England) Regulations 2000, SI 2000/227, and Guidance Notes issued in the form of a Department of the Environment, Transport and the Regions Circular 02/2000 on Contaminated Land (hereafter "Guidance Notes"). For Scotland, see the Contaminated Land (Scotland) Regulations 2000, SI 2000/178, in force as from 14 July 2000. The Welsh and Northern Ireland Assemblies have yet to introduce similar legislation.

[5] Legislation giving rise to *criminal liability* includes the following. The integrated pollution control (I.P.C.) regime (Environmental Protection Act 1990, Pt. 1) and its replacement, the pollution prevention and control (P.P.C.) regime (Pollution Prevention and Control Act 1999; Pollution Prevention and Control (England) Regulations 1999), make it an offence to carry out heavily polluting industrial processes (*e.g.*, chemical and metal manufacture) without or in breach of a licence to do so. Under s. 33 of the E.P.A. 1990, it is a criminal offence to dispose of controlled waste on a site without or in breach of a licence. In relation to contaminated land, failure to remediate when instructed to do so is a criminal offence under the E.P.A. 1990, Pt. IIA. Section 79 of the E.P.A. 1990 lists certain statutory nuisances, failure to abate which when required to do so is a criminal offence under s. 80. Sections 85 and 161A of the Water Resources Act 1991 provide for the offences of polluting controlled water without or in breach of a licence, and failing to clean up water when instructed to do so (discharge of trade effluent into sewers is covered by s. 118 of the Water Industry Act 1991).

[6] Clean-up liabilities include those for I.P.C. (E.P.A. 1990, s. 27) or P.P.C. (Pollution Prevention and Control Act 1999; Pollution Prevention and Control (England) Regulations 2000); controlled waste (E.P.A. 1990, s. 59); contaminated land (E.P.A., Pt. IIA); statutory nuisance (E.P.A. 1990, s. 81); and water pollution (Water Resources Act 1991, s. 161A).

[7] (1868) L.R. 3 H.L. 330.The availability of this cause of action has been severely restricted since the House of Lords held in *Cambridge Water Co.* v. *Eastern Counties Leather plc.* [1994] 2 A.C. 264 that foreseeability of harm by the defendant was a pre-requisite to recovery of damages.

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United Kingdom causing damage there (*e.g.*, the potential for claims against UK electricity generators for damage caused by acid rain in Germany and Scandinavia).[8] Most Member States of the European Union, for example, have implemented strict liability laws for environmental damage.[9]

(b) Security risks

The lender's security over land may prove worthless because of contamination. The threat of contamination can undermine property values as much as actual contamination. The new regime for the clean-up of seriously contaminated land enables local authorities in England, or the Environment Agency in the case of certain "special sites", referred to as the "enforcing authority" in Part IIA of the Environmental Protection Act 1990, to serve a remediation (clean-up) notice on an "appropriate person" specifying what the recipient must do to clean up the site.[10] Every enforcing authority must keep a public register recording designations of contaminated land, specified clean-up works, voluntary works undertaken and any appeals lodged.[11] There is no statutory mechanism for removing land from the register even after it has been cleaned up.[12] Moreover, lenders should be aware that, under the new regime, where the enforcing authority itself incurs costs in cleaning up contaminated land it may serve a charging notice on the owner which will constitute a charge on the premises which consist of or include the contaminated land in question, and the authority will have the powers and remedies available under the Law of Property Act 1925 to enforce the charge.[13] This will include the power to appoint a receiver and sell the property. The enforcing authority's charge is likely to have priority over all other interests in the land.[14]

[8] S. Cromie, "Contaminated Land. The Risks for Lenders" (1997) 8 (1) P.L.C. 33, 37.

[9] P. Thieffry and D. McKenney, "Lender's Liability in the European Union", Ch. 4 in J.J. Norton, R.M. Auerback and J.M. Gaba (eds.), *Environmental Liability for Banks* (1995), pp. 83–88; N.S.J. Koeman (ed.), *Environmental Law in Europe* (1999). See also the 1993 European Commission Green Paper on Remedying Environmental Damage, COM (93) 47 final, and the 2000 European Commission White Paper on Environmental Liability, COM (2000) 66 final. There is a voluminous literature on EC environmental law and its impact on the national laws of Member States. J. Scott, *EC Environmental Law* (1998) provides an entertaining and thought-provoking overview. See also K. Kramer, *EC Environmental Law* (4th ed., 2000).

[10] E.P.A. 1990, s. 78F provides that the "appropriate person" is, in the first instance, the person who caused or knowingly permitted the contamination (known as a Class A person) or, if such a person cannot be found after reasonable enquiry, the current owner or occupier of the land (known as a Class B person).

[11] E.P.A. 1990, s. 78R.

[12] Although the D.E.T.R. Guidance Notes indicate how the enforcing authority may "sign off" a site on an informal basis (Guidance Notes, Annex 2, para. 15.6).

[13] E.P.A. 1990, s. 78P.

[14] *Westminster City Council* v. *Haymarket Publishing Ltd.* [1981] 1 W.L.R. 677, C.A. (unpaid rating surcharge that constituted a charge on the land under the General Rate Act 1967 held to take priority over all other interests in the land).

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Without the availability of a statutory mechanism to recover clean-up costs by means of a charging order, there would be some doubt as to whether an enforcing authority, that has cleaned up a site itself, could take priority over an insolvent polluter's other creditors when seeking reimbursement of those clean-up costs. In Canada, for example, there seems to be a distinction between clean-up debts and clean-up duties. In *Panamericana De Bienes Y Servicos* v. *Northern Badger Oil & Gas*,[15] the Alberta Court of Appeal held that clean-up costs incurred by the polluter's receiver in complying with an order of the relevant authority had the effect of reducing the assets of the polluter available for distribution to its creditors. Assets collected by the receiver were to be used to finance the clean-up and not to be paid to secured creditors. Laycraft C.J.A., delivering the judgment of the court, held that the enforcing authority was not simply a creditor with a provable debt but a public authority with a duty to enforce public law.[16] By contrast, in *Re Shirley*,[17] Kennedy J. distinguished *Panamericana* and held that where the relevant authority does the clean-up itself and seeks reimbursement from the polluter then that claim for clean-up costs was a provable claim in the polluter's bankruptcy.

III. Direct Liability

There are a number of environmental provisions under which a lender could potentially incur environmental liability (there may even be some overlap between them, *e.g.*, the new contaminated land regime overlaps with other statutory provisions dealing with waste).[18] A lender may be liable under a number of environmental protection statutes if it has "caused or knowingly permitted" damage to the environment.[19] Other statutory provisions and common law rules impose liability on the "owner or occupier" of land, usually where the original polluter cannot be found.[20] These are the 'triggers' of liability.

[15] (1991) 81 D.L.R. (4th) 280, reversing (1989) 75 Alta. L.R. (2d) 185, MacPherson J.
[16] *Ibid.*, p. 291.
[17] (1996) 129 D.L.R. 105, Ontario Court, General Division.
[18] The E.P.A. 1990, Pt. IIA contains provisions dealing with overlap.
[19] Examples include the following. Water Resources Act 1991, s. 85: offence of causing or knowingly permitting any polluting matter to enter "controlled waters" (virtually any watercourse other than a sewer). E.P.A. 1990, s. 33: offence to knowingly cause or knowingly permit controlled waste to be deposited without a licence or in a manner likely to cause pollution of the environment or harm to human health. E.P.A. 1990, s. 78F(2): clean up of contaminated land by person who caused or knowingly permitted the contaminating substances to be present in, on or under the land (a Class A "appropriate person").
[20] Examples include the following. E.P.A. 1990, s. 59: owner or occupier of land upon which controlled waste has been deposited without a licence is liable for the cost of removing it unless he can show that he did not knowingly cause or knowingly permit the deposit of the offending waste. E.P.A. 1990, s. 78F (4): where, after reasonable enquiry, the original polluter (a Class A "appropriate person") cannot be "found" the owner or occupier for the time being

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(a) "Caused or knowingly permitted"

Pollution is "caused" on proof of some connection, however direct or indirect, between the activities of the polluter and the pollution in question. Simply carrying on the activity which caused the pollution is enough. There is no requirement of knowledge, negligence or fault.[21] The chain of causation may be broken by intervening factors such as the act of a third party or an Act of God,[22] but more than one person may be held to have caused the same pollution, even though they act quite independently of each other.[23]

A person may "permit" pollution to take place by allowing it to occur or continue, *i.e.*, not preventing it if it was possible to do so. This covers allowing pollution to remain on a site, even though it was already there when the site was acquired. However, a person can only permit pollution to take place where he has sufficient power to prevent it. Thus, in *Berton* v. *Alliance Economics Investment Co. Ltd.*, the phrase "to permit" was defined to include "abstain[ing] from taking reasonable steps to prevent [an] act where it is within a man's power to prevent it".[24] There must also be knowledge of the circumstances bringing about the pollution. In the context of the new contaminated land regime, this probably means that liability flows from mere knowledge that one is permitting substances to be present on the land, even though one does not know that the substances render the land contaminated within the meaning of Part IIA of the Environmental Protection Act 1990.[25] A person's knowledge may be actual or constructive, *i.e.*, a person is held to know that which he could in all the circumstances be expected to know.[26] Turning a blind eye, or deliberately

becomes the appropriate person (a Class B "appropriate person"). E.P.A. 1990, ss. 80 & 81: the owner or occupier of land can be ordered to abate a statutory nuisance if the person responsible for it cannot be found, or to pay the local authority's costs in abating it.

Common law: the owner or occupier can be held liable for nuisance or under *Rylands* v. *Fletcher* (1868) L.R. 3 H.L. 330, even if he did not create the nuisance or bring the damaging substance onto his land.

[21] *Alphacell Ltd.* v. *Woodward* [1972] A.C. 824, H.L.

[22] *Impress (Worcester) Ltd.* v. *Rees* [1971] 2 All E.R. 357; *National Rivers Association* v. *Wright Engineering Co. Ltd.* [1994] 4 All E.R. 281. Although note Lord Wilberforce's warning in *Alphacell Ltd.* v. *Woodward* [1972] A.C. 824, at 835, that it is not in every case that the act of a third party necessarily interrupts the chain of causation: "the answer to such questions is one of degree and depends on a proper attribution of responsibility".

[23] *Attorney-General's Reference (No. 1 of 1994)* [1995] 1 W.L.R. 599, C.A.

[24] [1922] 1 K.B. 742, 759, *per* Atkin L.J. See also *Test Valley Investments* v. *Tanner* [1964] Crim. L.R. 62, D.C. The D.E.T.R. Circular on Contaminated Land defines "permit" to include both the ability to take steps to prevent the substance being present or remove it and having a reasonable opportunity to do so (Annex 2, paras. 9.8–9.14).

[25] *Current Law Annotated Statutes 1995*, Vol. 3, p. 154.

[26] *Schulmans Incorporated Ltd.* v. *National Rivers Authority* [1993] Env. L.R. D.1, Q.B.D. Div. Ct.

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refraining from enquiry for fear of the truth, may attract liability.[27]

The theme linking "cause" and "knowingly permit" is that of "control". Either the defendant has control of the activity that causes pollution or such control that he could have prevented it. Does the mere lending of money to a borrower who operates a polluting facility give the lender such control over the borrower's affairs so as to make it vulnerable to direct environmental liability under these triggers? The greater danger probably lies under the "knowingly permitting" trigger. The mere act of lending does not seem sufficient to trigger liability as, in itself, the loan of money does not carry with it the necessary element of control over the borrower's business. However, most loans contain provisions requiring compliance with laws which will allow the lender to declare an event of default and demand repayment if it learns that the borrower is breaching environmental statutes. If that would close down the business and thus prevent further pollution, it is arguable that the lender had the power to prevent the contamination and failed to use it. As we have seen, turning a blind eye is not the answer.

The new contaminated land regime contains a special exemption for lenders.[28] It expressly excludes a lender who does nothing more than provide financial assistance from the category of Class A "appropriate persons" (*i.e.*, those who are responsible for remediation costs by reason of having "caused or knowingly permitted" contaminating substances to be in, on or under the land). The provision of financial assistance includes making loans or providing any other form of credit, as well as investing in the undertaking of a company by acquiring share capital or loan capital of that company (as long as a holding company/subsidiary relationship is not thereby created).[29] The fact that the lender is excluded from liability on this ground does not imply that the mere provision of financial assistance necessarily amounts to "causing or knowingly permitting".[30] However, there is an important limitation on the exclusion—it only applies if there are others who will be left in the Class A category after its operation.[31]

An English court considering whether to impose liability on a lender simply because the lender had the "capacity to control" the borrower's business, through the terms of the loan agreement, would do well to study the experiences of the United States' courts

[27] *Westminster City Council* v. *Croyalgrange Ltd.* [1986] 1 W.L.R. 674, H.L.
[28] Guidance Notes, Annex 3, Chapter D, para. 48(a).
[29] As defined in the Companies Act 1985, s. 736.
[30] Guidance Notes, Annex 3, Chapter D, para. 47.
[31] Guidance Notes, Annex 3, Chapter D, para. 41(c).

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in implementing the "Superfund" legislation. The Comprehensive Environmental Response Compensation and Liability Act 1980 ("C.E.R.C.L.A."), as amended, set up a large fund (the "Superfund") to be used by the Environmental Protection Agency to clean up contaminated sites. Those costs are then recoverable from "potentially responsible parties", which includes the current "owner or operator" of the site. Lenders will not be troubled by the risk of liability where they can rely on the "secured creditor" exception which defines "owner or occupier" to exclude "a person, who, without participating in the management of a vessel or facility, holds indicia of ownership primarily to protect his security interest in the vessel or facility".[32] The question is, when does a lender "participate in the management" of a facility so as to lose the benefit of the exemption?

United States v. *Fleet Factors Corporation*, is the seminal case.[33] There the Eleventh Circuit Court of Appeals, on an interlocutory application, proposed a test based on the lender's "capacity to influence" the borrower's treatment of waste. It was not necessary for a creditor to be involved in day-to-day operational decisions nor to participate in management decisions concerning hazardous waste. "A secured creditor will be liable if its involvement with the management of the facility is sufficiently broad to support the inference that it could affect hazardous waste disposal decisions if it so chose".[34] Interestingly, the court observed that nothing prevented a secured creditor from monitoring any aspect of the borrower's business, nor did it prevent the secured creditor from becoming involved in "occasional and discrete" financial decisions relating to the protection of its security interest.[35]

Fleet Factors prompted the federal Environmental Protection Agency to promulgate a regulation which provided, inter alia, that the lender's ability to influence the borrower's activities was not enough to impose liability.[36] In *Kelley* v. *Environmental Protection Agency*,[37] the D.C. Circuit declared the rule invalid on the ground that it was ultra vires the Environmental Protection Agency. This

[32] 42 U.S.C. s. 9601(20)(A).
[33] 901 F. 2d. 1550 (11th Cir. 1990); cert. denied, 111 S. Ct. 752 (1991).
[34] *Ibid.*, 1557–1558. In *Re Bergsoe Metal Corporation*, 910 F. 2d. 668 (9th Cir. 1990), the Ninth Circuit Court of Appeals, held that the lender does not lose exemption merely by having the power to become involved in the borrower's management; the lender must exercise actual management authority before liability attaches.
[35] *Ibid.*, 1558.
[36] *Fleet Factors* was remitted back to the District Court which held that, even under the standards laid down by the Environmental Protection Agency, the lender was liable as the sale of the borrower's assets by the lender's agent, following foreclosure by the lender on its security interest on some of the borrower's inventory and equipment, had led to the release of toxic chemicals and asbestos and had been conducted "with all the finesse of a Viking raiding party": 819 F. Supp. 1079 (S.D. 1993) and 821 F. Supp. 707 (S.D. Ga. 1993).
[37] 1994 WL 27881 (D.C. Cir. 1994).

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necessitated the passing, in September 1996, of the Asset Conservation, Lender Liability and Deposit Insurance Protection Act. This states that a lender is not liable for clean-up costs under C.E.R.C.L.A. as long as: (a) pre-foreclosure, it does not take over control of environmental compliance at the borrower's facility, or substantially all its operational function; and (b) post-foreclosure, it seeks to sell or otherwise dispose of the facility within a reasonable time and on commercial terms.

Under English law, the greatest danger for a lender would arise where it became too closely involved in its borrower's affairs. Normal financial monitoring should not pose a risk. But there would be a real danger of liability if the lender's actions made it a *shadow director*,[38] and knowing that the borrower was breaching environmental law, the lender failed to use its powers to stop them. Involvement in the management of the borrower's business should be avoided. Monitoring a rescue package so closely that the board effectively does what the lender tells it to is also dangerous.[39] Insisting on nominating a director to the board of the borrower may also be risky.[40] The risk of liability would be particularly acute where the borrower defaults and the lender foreclosed or went into possession. It is possible that, by taking over the borrower's business and continuing its activities after it has foreclosed or gone into possession, a lender may itself incur liabilities under the causing or knowingly permitting triggers.

(b) "Owner or occupier"

For the purposes of the new contaminated land regime, the term "owner" is defined in s. 78A(9) of the Environmental Protection Act 1990 as being the person, other than a mortgagee not in possession, who is or would be entitled to receive the rent for the property. One commentator suggests that the exclusion of a mortgagee who is not in possession from this category hardly seems necessary as "there seems no reason why the existence of a

[38] The standard definition of the term "shadow director" is prescribed by section 741(2) of the Companies Act 1985 and this is mirrored in other statutes, including section 22(5) of the Company Directors Disqualification Act 1986 and section 251 of the Insolvency Act 1986. Section 251 of the Insolvency Act 1986 provides that: "'shadow director', in relation to a company, means a person in accordance with whose directions or instructions the directors of the company are accustomed to act (but so that a person is not deemed a shadow director by reason only that the directors act on advice given by him in a professional capacity)."

[39] *Secretary of State for Trade and Industry* v. *Deverell* [2000] 2 W.L.R. 907, C.A. However, a lender is not likely to be held a "shadow director" when it makes its proposals for rehabilitation of the company a condition for continuation of support. See *Re PFTZM Ltd.* [1995] 2 B.C.L.C. 530. See also E. Ferran, *Company Law and Corporate Finance* (1999), p. 484.

[40] Although the lender would have to control a governing majority of the board before being classed as a shadow director (*Kuwait Asia Bank EC* v. *National Mutual Life Nominees Ltd* [1991] 1 A.C. 187, P.C.).

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mortgage should increase the chances of a lender being found liable under any of the provisions under consideration, until the lender attempts to enforce its rights under it".[41] The position of the mortgagee in possession seem to be much less secure. In *Maguire* v. *Leigh-on-Sea UDC*,[42] a mortgagee in possession was held liable for local authority work, and in *Westminster City Council* v. *Haymarket Publishing Ltd.*,[43] it was held that a mortgagee in possession was liable to pay a rating surcharge as it was he "who has control of the letting".[44] In each case, by going into possession, the mortgagor is deemed to have taken the necessary degree of control of the mortgagor's affairs to warrant liability. By contrast in *Midland Bank* v. *Conway*,[45] where the bank collected rents paid by tenants of its customer, it was held not to be an "owner", for the purpose of being served with a noise abatement notice under the Public Health Act 1936,[46] but a mere "conduit-pipe" or "office boy", *i.e.*, the element of control was missing.[47] Nevertheless, there can be little doubt that by receiving rents lenders run an increased risk of liability.[48]

There is no statutory definition of the term "occupier" in the Environmental Protection Act 1990. It is submitted that for the purposes of this and other legislation where the term is undefined, occupation indicates some form of possession and control over premises.[49] In *Meigh* v. *Wickenden*,[50] a receiver and manager was held liable under ss. 130 and 133 of the Factories Act 1937 for failure to ensure adequate guards on machinery in a factory which the receiver was continuing to run. The legislation made the occupier liable and this was held to include the receiver. The receiver was liable because of his potential power of management and control, rather than any need for the actual exercise of

[41] Cromie, fn. 8 above, p. 36.
[42] (1906) 95 L.T. 319.
[43] [1981] 1 W.L.R. 677.
[44] *Ibid.*, 680, *per* Lord Denning.
[45] [1965] 1 W.L.R. 1165.
[46] The Public Health Act 1936, s. 343 defined an owner of property as "the person for the time being receiving the rackrent of premises ... whether on his own account or as agent or trustee for any other person".
[47] All three members of the court emphasised that the case only concerned the normal relationship of banker and customer and that if there were "special circumstances" the bank might be liable (at 1170B, *per* Lord Parker C.J., at 1172E, *per* Sachs J., and at 1173D, *per* Browne J.).
[48] Jarvis & Fordham, fn. 1 above, pp. 131–134; G. Beringer & E. Thomas, "Lenders and Environmental Liability" (1991) 2 (11) P.L.C. 3, p. 8.
[49] *Wheat* v. *E Lacon & Co* [1966] A.C. 552. See R. Lee, "Lending and the Environment in the UK: Environmental Risks for Bankers", Ch. 3 in J.J. Norton, R. Auerback & J. Gaba (eds.), *Environmental Liability for Banks* (1995), pp. 60–61.
[50] [1942] 2 K.B. 160.

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control.[51] It has been said that this approach is not far from the "capacity to influence" test in *Fleet Factors*.[52] Perhaps the case is best read in the particular context of the statute in issue, which imposed strict liability for breaches of workplace safety.[53]

The cases outlined above offer some comfort to the lender who does not foreclose or go into possession of mortgaged property. However, some degree of caution must be exercised when seeking to define a term used in one statute for the purposes of defining the same term in another statute. "No useful progress can be made ... by inquiring what meaning the courts have given [the word "occupier"] in reported cases, for they draw their meaning entirely from the purpose for which and the context in which they are used".[54] What is clear, however, is that in the context of the new contaminated land regime both foreclosure and possession render the lender the "owner or occupier" of contaminated land (a Class B "appropriate person"), and liable for clean-up costs if no Class A person can be found.[55] Banks and other institutions, such as the Council of Mortgage Lenders, expressed concern as the Environment Act 1995, which introduced Part IIA into the Environmental Protection Act 1990, passed through Parliament that this would expose lenders to liability in situations they could not readily control. What if the lender is in possession by default where the borrower abandoned the property and sent the keys to the lender? What if the lender took possession to a limited extent to secure the property or deal with obvious hazards? However, the Government proved unsympathetic to these concerns and was not prepared to give lenders special treatment in these circumstances.[56]

Where the borrower defaults the secured lender will usually consider it a safer option to appoint a receiver under the terms of its debenture. The mere appointment of a receiver over the borrower's assets will not, in itself, bring home to the lender any environmental liability of the receiver. It is well established that, at least until the point of liquidation, the receiver acts as agent of the company and not the charge-holder.[57] However, a lender will be

[51] *Ibid.*, 164–165, *per* Lord Caldecote.
[52] J. Jarvis Q.C., M. Fordham and D. Wolfson, "Domestic Environmental Liability", Ch. 5 in R. Cranston (ed.), *Banks, Liability and Risk* (2nd ed., 1995), p. 162.
[53] Lee, fn. 49 above, p. 60.
[54] *Southern Water Authority* v. *Nature Conservancy Council* [1992] 1 W.L.R. 775, 781, *per* Lord Mustill, quoting *Madrassa Anjuman Islamia* v. *Municipal Council of Johannesburg* [1922] 1 A.C. 500, 504, *per* Viscount Cave.
[55] E.P.A. 1990, s. 78F(4), (5). The Guidance Notes state that a company which has been dissolved cannot be found.
[56] *Hansard*, H.L. Vol. 560, col. 1445, H.L. Vol. 562, cols. 165, 1040, 1042–1043.
[57] See the dissenting judgment of Rigby L.J. in *Gaskell* v. *Gosling* [1896] 1 Q.B. 669, which was approved by the House of Lords [1897] A.C. 575. The Insolvency Act 1986, s. 44(1)(a), provides that an administrative receiver is deemed to be the agent of the company unless and until the company goes into liquidation.

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held liable for the defaults of a receiver if it "gives him directions or interferes with his conduct of the realisation".[58] Following liquidation it will be a question of fact as to whether the receiver acts on his own behalf or as agent for the mortgagee.[59] However, the lender cannot ignore the risk of paying for environmental liability incurred by the receiver (as "owner or occupier" or for "causing or knowingly permitting" pollution). A receiver will usually require an indemnity from the lender which means that the lender assumes environmental liability indirectly. The lender would be well advised to try and limit the extent of the indemnity by excluding liability for contamination or other pollution caused or knowingly permitted by the receiver or, if that is unacceptable to the receiver, for contamination or other pollution resulting from his unreasonable acts or omissions.

The new contaminated land regime does provide some protection to receivers, which will benefit lenders who have given the receiver an indemnity. Neither a receiver nor administrator is personally liable for the cost of any remedial work, unless it is referable to his own acts or omissions, and they were unreasonable.[60] One commentator suggests that "ordinary receivers appointed under a debenture or other security who are not licensed insolvency practitioners would not be covered by this exemption".[61] It is submitted that this interpretation of the statute is wrong for it ignores the express wording of s. 78X(4)(f)(ii) extending the exemption to "a person acting as receiver or receiver and manager ... by virtue of his appointment as such by an order of a court *or by any other instrument*" (emphasis added).

In the United Kingdom a lender which forecloses or takes possession of land in order to sell it may be liable to clean it up. By contrast, in the United States the Asset Conservation, Lender Liability and Deposit Insurance Protection Act 1996, s. 2502 (amending C.E.R.C.L.A., s. 107) protects the lender post-foreclosure when seeking to sell or otherwise dispose of the borrower's facility as long as this is done within a reasonable time and on commercial terms. Lenders in the United Kingdom would appear to be in a worse position than their counterparts in the United States in this respect.

[58] *Standard Chartered Bank* v. *Walker* [1982] 1 W.L.R. 1410, 1416, *per* Lord Denning M.R.
[59] *American Express International Banking Corp.* v. *Hurley* [1985] 3 All E.R. 564.
[60] E.P.A. 1990, s. 78X(3), (4).
[61] T. Hellawell, *Contaminated Land* (2000), p. 24.

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IV. Conclusion

The banking industry has been quick to point out the dangers of too readily imposing liability on lenders for environmental damage.[62] Uncertainty as to the extent of the lender's potential liability, together with the risk of being held liable for huge uninsurable losses that could affect a bank's capital adequacy requirements, could inhibit lending to environmentally sensitive industries. There is evidence from the United States that, following the *Fleet Factors* decision, businesses in environmentally sensitive industries have found it more difficult to raise money from banks and that insurance companies have limited environmental cover.[63] With this in mind, it is hoped that the English courts will not go down the "capacity to influence" route that has been so recently rejected in the United States. Lenders not exercising operational control should not incur liability.[64]

Lenders cannot ignore the risks of direct or indirect environmental liability. However, they should not live in fear of those risks, which in many cases are remote. In any event, the risk of environmental liability can be considerably reduced by following safe lending practices. These safe lending practices attempt to tread the (sometimes fine) line between the lender being fully aware of all risks in respect of the lending and avoiding conduct which might be characterised as participation in or control of the borrower's business. The following points are offered as general guidance to banks and other lenders:[65] (i) ensure that relevant staff are properly trained; (ii) carry out environmental audits prior to lending and before enforcing security; (iii) ensure adequate warranties, covenants and events of default are contained in contractual documentation, including a requirement that the borrower complies with environmental laws and allowing the lender to declare an event of default if he does not; (iv) take an assignment of any environmental insurance policy that the borrower may have;[66] (v) consider

[62] British Bankers' Association, "Position Paper on Banks and the Environment" (July 1993); E. Welch and T. Parker, "A Bank's View of Lender Liability in Environmental Legislation" [1993] J.I.B.L. 217.

[63] P. Blackman, "Lender Liability and Deep Pockets; Managing Environmental Risks in Financing Businesses in Europe", Ch. 13 in H. Enmarch-Williams (ed.), *Environmental Risks and Rewards for Business* (1996).

[64] This reflects the stance taken by the European Commission in its recent White Paper on Environmental Liability, COM (2000) 66 final.

[65] Jarvis & Fordham, fn. 1 above, pp. 168–174; Jarvis, Fordham & Wolfson, fn. 52 above, pp. 168–170; Cromie, fn. 8 above, pp. 38–40; Beringer & Thomas, fn. 48 above, p. 8.

[66] Insurance cover for gradually occurring pollution damage, as opposed to that caused by a catastrophe, is increasingly difficult to find. See Blackman, fn. 63 above, p. 99; Cromie, fn. 8 above, p. 38.

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taking security over assets other than land and (vi) when enforcing security, seek methods of obtaining the benefit of that security which do not involve "ownership" or "occupation" of secured property.

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