In this update:

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Article One

The Court Cannot Save the Government From Overpayment Of CERCLA Remediation Costs That Were Its Own Choice

Lockheed Martin Corporation v. United States of America
(Case No. 14-5302, D.C. Cir. Aug. 19, 2016)

The United States (the "Government") pursued an appeal of its CERCLA liability for a portion of the cost of cleaning up hazardous substances at three California facilities owned by Lockheed. Lockheed produced rockets at these facilities, the process of which contaminated these sites. Acknowledging its share of CERCLA liability, the Government agreed to reimburse Lockheed's share of CERCLA liability via overhead charges on unrelated contracts. At issue is whether the Government has a valid claim that the particular mechanism by which it paid its share of the costs of environmental remediation under CERCLA - would result in impermissibly requiring the Government to make double payment. The Court concluded that the district court's CERCLA judgment did not create any double recovery. The Court rejected the Government's allegations that the crediting mechanism did not help, but instead harmed it further, and further noted that the Billing Agreement was of the parties' own choosing. The Court affirmed the lower court's judgment.

Background

Lockheed Propulsion Company, a corporate successor to Lockheed, operated the three sites at issue in this case - Redlands, Potrero Canyon, and LaBorde Canyon - between 1954 and 1975. The generation of hazardous waste was one of the consequences of Lockheed's rocket production work at these California sites.

In 1997, Lockheed Martin began to clean up the sites. That same year, Lockheed entered into an agreement with the Department of Justice ("DOJ") to toll the applicable statute of limitations for CERCLA claims. (42 U.S.C. § 9613(g)(2).) The tolling agreement was repeatedly renewed over the course of the next several years.

As of the start of the trial in this case, in February 2014, Lockheed incurred environmental response costs for the three California sites totaling approximately $287 million, and estimated that it would incur another $124 million in the future. As the parties agreed in the DOSA, Lockheed charged some of these costs to its government customers as those costs were incurred.

The federal government pays its contractors for technology, products, and services in accordance with various statutes and regulations, including the Federal Acquisition Regulations ("FAR"), 48 C.F.R. § 1.000 et seq. There are two basic types of government contracts: fixed-price and cost-reimbursement. (*Id.*) Under a firm fixed price contract, the government pays an agreed-upon price without regard to the costs incurred by the contractor, which assumes the risk and responsibility for its costs. (*Id.*) Under a cost reimbursement contract, the government pays a contractor its "direct costs" and "indirect costs," plus a profit. (*Id.*)

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Article One (cont.)

The Court Cannot Save the Government From Overpayment of CERCLA Remediation Costs That Were Its Own Choice

Direct costs are those that relate to a specific contract, such as the costs of material and labor. (48 C.F.R. § 52.216-7(b).) Indirect costs are those not associated with a specific contract, such as overhead and general administrative expenses. (*Id.*) To be included in the price of goods or services, indirect costs must be "allowable." (*Id.*) That means that the costs, among other things, must be "allocable," "reasonable," and not otherwise disallowed. (*Id.*)

The FAR includes a "Credits Clause." 48 C.F.R. § 31.201-5, designed to prevent double recovery. This provision states, "[t]he applicable portion of any income, rebate, allowance, or other credit relating to any allowable cost and received by or accruing to the contractor shall be credited to the Government either as a cost reduction or by cash refund." (*Id.*)

In September 2000, Lockheed and the Government States resolved their dispute over environmental costs by entering into the DOSA. The Settlement Agreement provided that Lockheed could treat as "allowable," and thus include as indirect costs in contracts, the majority of its environmental-remediation costs at these three former sites.

In the DOSA, the Government agreed to permit Lockheed to place all of its "allowable" discontinued-operations costs, including those incurred in environmental cleanup, into the Discontinued Operations Pool ("DiscOps Pool"). Lockheed then allocated those sums across all of its business areas, which in turn can include whatever portion they were allocated, on an amortized basis over a five-year period, as part of the indirect costs in their contracts for goods and services. (*Id.*)

Court's Rationale

The lower court held that, under the FAR and the DOSA, when Lockheed recovered from the Government under CERCLA, there is "a commensurate reduction in the Settled Discontinued Operations Costs pool that Lockheed [can] charge as indirect costs in its government contracts." (*Id.*) In this manner, "Lockheed will not realize a double recovery," because, "[f]rom a monetary standpoint, Lockheed w[ill] be back where it started." (*Id.*) The lower court also concluded that it would be unfair to force Lockheed "to recover all of its response costs as indirect costs on its government contracts….proceeding in that way makes Lockheed less competitive in future contests for government contracts, because its need to recover response costs through indirect cost payments would require inflated and possibly non-competitive bids." (*Id.*)

On appeal, the Government's theories boiled down to an objection against double recovery. "If the government were to pay what is at most a 29 percent CERCLA share of the approximately $124 million in estimated future costs, its total CERCLA exposure for the future cost portion at the end of the cleanup would be approximately $36 million." (*Id.*) Stated another way, the Government alleged that it "has already paid 55 percent of the total past and future response costs that Lockheed is expected to incur…absent a CERCLA judgment, it will eventually pay 83 percent of total response costs at the site - well above its court-allocated equitable share of only 19 to 29 percent of future costs incurred in cleanup the sites." (*Id.*)

Lockheed countered that double recovery would not be the result as the Billing Agreement's crediting mechanism would require any CERCLA recovered from the government to be credited back to Lockheed's customers, more than offsetting the Government's payments. (*Id.*)

At first glance it would appear as if the Government had paid the vast majority of past cleanup costs, and that Lockheed would continue billing of its own remediation costs to its current and future contracts, mostly federal contracts, until it was reimbursed. "But here, the [lower court's] CERCLA judgment did not create a double recovery. The reason the government will end up paying far more that its own 19 to 29 percent share of future costs is that it voluntarily agreed to let Lockheed pass through its share, too. It was the government's choice to accept the Billing Agreement, authorizing Lockheed to assign to the DiscOps Pool charges as indirect contract costs certain cleanup costs related to facilities at which Lockheed had discontinued operations." (*Id.*)

Conclusion

The extent of the Government's payment was the result of their own choice and the Court was powerless to have changed the Billing Agreement. The Court was in no position to "save the government from the natural and probable consequences of its own conduct."

Article Two

A Unilateral Administrative Order ("UAO") Pursuant to CERCLA Section 106
is not a "Civil Action" for the Purposes of a CERCLA Section 113(f) for Contribution

Diamond X Ranch LLC., v. Atlantic Richfield Company

(Case No. 3:13-cv-00570-MMD-WGC, D Nev. Aug. 26, 2016)

Diamond X ("Plaintiff") owns more than 1700 acres of property in Douglas County, Nevada, and Alpine County, California. Plaintiff alleged that its property has been contaminated by acid mine drainage flowing from the Leviathan Mine, ("Mine"), in Alpine County. EPA listed the Mine on the National Priorities List in May 2000, and identified Atlantic Richfield ("ARCO") as a potentially responsible party ("PRP"). EPA issued a UAO against ARCO in November 2000, and a second in June of 2008. The UAOs identified ARCO as a PRP and required ARCO to initiate a Remedial Investigation and Feasibility Study ("RI/FS"). Plaintiff and ARCO filed CERCLA section 107(a) and 113(f)(1) claims against each other - as against ARCO for its release of hazardous substances from the Mine; and for Diamond X's operation of an irrigation system on the Property, thereby determining "if, when, where and how much water containing hazardous substances was placed and deposited on the Diamond X Property." (*Id.*) Both parties filed motions to dismiss - Plaintiff moving to dismiss ARCO's section 107(a) and section 113(f)(1) claims alleging that ARCO was barred from asserting a section 107(a) claim because of Plaintiff's own section 107(a) claim, and because ARCO's response costs were incurred pursuant to EPA's UAOs - which amounted to "civil actions." The court denied Plaintiff's motion as: i) ARCO had incurred expenses that were outside the scope of contribution and the scope of Plaintiff's section 107(a) claim; ii) the UAOs were not "civil actions" under section 106(a).

Background

Plaintiff filed a 10-count complaint against ARCO in 2013, complaining that its subsidiary's use of the Leviathan Mine from 1953 until 1962 resulted in discharges of acidic mine drainage that migrated onto Plaintiff's property. Diamond X alleged causes of action under the Clean Water Act and under CERCLA for money spent remediating the property.

Plaintiff alleged a section 107(a) claim to recover cleanup costs on the property in response to hazardous waste releases from the Mine. Plaintiff alleged that ARCO's remedy was limited to contribution under Section 113(f)(1) in primary reliance on *Whittaker Corp. v. United States*, 825 F.3d 1002 ((9th Cir. 2016). In *Whittaker*, the Supreme Court held that section 107(a) cost recovery and section 113(f)(1) are distinct remedies available to parties under distinct procedural circumstances. The Supreme Court explained:

"[T]he remedies available in §§107(a) and 113(f) complement each other by providing causes of action to 'persons in different procedural circumstances.' Section 113(f)(1) authorizes a contribution action to PRPs with common liability stemming from an action instituted under...§107(a). And §107(a) permits cost recovery (as distinct from contribution) by a private party that has itself incurred cleanup costs. Hence, a PRP that pays money to satisfy a settlement agreement or a court judgment may pursue §113(f) contribution. But by reimbursing response costs paid by other parties, the PRP has not incurred its own costs of response and therefore cannot recover under section 107(a). As a result, though eligible to seek contribution under §113(f)(1), the PRP cannot simultaneously seek to recover the same expenses under §107 (a)." (*U.S. v. Atlantic Research Corp.* (2007) 551 U.S. 128, 139, as quoted in *Whittaker*.)

Court's Ruling

Whittaker brought two § 107(a) cost recovery claims alleging owner and arranger liability against the defendant United States of America (the "Federal Government") for response costs incurred to clean up contamination in the soil and groundwater at a former military munitions manufacturing site (the "Site"). According to Whittaker's first amended complaint ("FAC"), Whittaker voluntarily performed and incurred costs for interim remedial efforts at the Site under the oversight of the California Department of Toxic Substances Control ("DTSC"). Whittaker alleged that it entered into a voluntary consent order (the "Consent Order") with DTSC in 1994 related to such efforts. In 2002, DTSC issued an Imminent and Substantial Endangerment Determination and Order and Remedial Action Order ("Endangerment Order") for Whittaker to remediate the site, which provided, in part, that Whittaker remain subject to the Consent Order. Whittaker alleged that neither Order was entered into subject to CERCLA or a court order.

In 2000, Whittaker itself was subject to § 107(a) cost recovery claims brought by a group of water agencies and companies in the area of the Site (collectively, the "Water Purveyors") for reimbursement of costs expended by the Water Purveyors to respond to groundwater contamination in certain off-Site production wells (the "Water Purveyor Action"). This action was eventually settled in 2007 (the "Water Purveyor Settlement"). Whittaker alleged that its subsequent FAC against the Federal Government sought response costs outside the scope of the Water Purveyor Action.

The Federal Government brought a motion to dismiss Whittaker's FAC, arguing that Whittaker was limited to contribution actions as a PRP with common liability stemming from the § 107(a) claims in the Water Purveyor Action. Whittaker countered that it still possessed § 107(a) claims because no § 113(f) claim was available for response costs outside the scope of the Water Purveyor Action. The District Court disagreed with Whittaker, and held that nothing in the text of § 113(f)(1) limits recovery under a contribution action to the scope of the previous cost recovery action against the plaintiff. "Here, [Whittaker] meets the procedural circumstances of § 113(f)(1), and its remedy for the costs it seeks 'during or following' the [Water Purveyor Action] is a contribution claim under § 113(f)(1)." (*Id.*) Accordingly, the District Court held that Whittaker's § 107(a) cost recovery claims could not survive a Motion to Dismiss and dismissed its FAC, which did not seek relief under § 113(f)(1), with prejudice.

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Article Two (cont.)

A Unilateral Administrative Order ("UAO") Pursuant to CERCLA Section 106 is not a "Civil Action" for the Purposes of a CERCLA Section 113(f) for Contribution

On appeal, the Ninth Circuit held that Whittaker was not limited to a contribution action and reversed. The Ninth Circuit held that Whittaker was now seeking to recover "a different set of expense [] for which Whittaker was no found liable" under its settlement agreement in the Water Purveyor Action. (*Id.*) The Ninth Circuit rejected the Federal Government's argument that a party who has been sued in a section 107 cost recovery action for expenses related to pollution at a site should be limited to a contribution action for all of their expenses at the site. (*Id.*) "Thus, the court held that Whittaker was not required to being a claim for contribution under section 113(f)(1) against the government because it is seeking section 107(a) claim 'to recover expenses that are separate from those for which Whittaker's liability is established or pending.'" (*Id.*)

Similarly, ARCO alleged that its counterclaim sought to recover for costs that were separate from those Plaintiff sought to recover under its section 107(a) claim. Accepting ARCO's claim as true, as it must under a motion for dismiss, the court held that ARCO incurred expenses that are outside the scope of contribution and the scope of Plaintiff's section 107(a) claim for which liability had not been set.

Regarding the UAOs, the court disagreed with Plaintiff's interpretation of *U.S. v. Atlantic Research Corporation* (*Atlantic II*), 551 U.S. 128 (2007) to argue that UAOs are "enforcement actions." Plaintiff cited to the Supreme Court's holding that PRPs who "have been subject to section 106 or 107 enforcement actions are still required to use section 113, thereby ensuring its continued vitality." (*Atlantic II* at 134.) Although this quote would appear to include UAOs under "civil actions," this interpretation ignores the procedural posture of this case. Atlantic Research "commenced suit [against the United States] before, rather than during or following, a CERCLA enforcement action," thus it could not bring a section 113(f) action as it had to rely on a section 107 claim to recover its costs. (*Id.*)

Plaintiff relied on *PCS Nitrogen, Inc. v. Ross Development Corporation*, 104 F.Supp. 3d 729 (D.S.C. 2015), which presses the minority opinion that a UAO is equivalent to a "civil action." The majority of courts hold that UAOs under section 106(a) are not a "civil action" for the purposes of section 113(f)(1). (See, *Emhart Industries, Inc. v. New Eng. Container Co., Inc.*, 478 F.Supp. 2d 199, 203 (2007).)

Conclusion

For civil actions in the Ninth Circuit, a final judgment ends the litigation on the merits leaving nothing more for the court to do but to enter judgment. (See *Williamson v. UNUM Life Ins. Co. of Am.*, 160 F.3d 1247, 1250 (9th Cir. 1998).) Here, the UAOs did not express such finality as, at a minimum, the phased RI/FS study, requiring ongoing evaluations by EPA and ARCO to determine the final remediation plan - lacked the same definitive scope or finality as a judgment in a "civil action." (*Id.*)

About Thierry R. Montoya

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Thierry also represents clients in natural resources issues involving water, oil and gas interests, air and water permitting and violations including NPDES and Title V.

On the land use side, Thierry provides permitting, zoning, CEQA/NEPA, and eminent domain expertise. Thierry also represents public and private sector clients in construction biddings, contracting, and litigation.

Article Three

EPA's Implementation Rule Was A Reasonable Exercise of EPA's Gap-Filling Authority

WildEarth Guardians, et al. v. Environmental Protection Agency

(Case No. 14-1145, D.C. Cir. July 29, 2016)

The D.C. Circuit ("Court") upheld EPA's compliance deadlines for states to meet the NAAQS for fine particulate matter ("PM2.5"). The lower court previously ruled that the framework EPA had been applying to PM2.5 was incorrect, and ordered EPA to apply a stricter statutory framework. EPA then promulgated the present implementation rule. However, at the time EPA had been applying the incorrect statutory framework, some of the stricter compliance deadlines that would have applied under the correct statutory framework had already elapsed. EPA therefore adjusted those deadlines in the new rule to avoid treating states as having already missed deadlines of which they were never aware. WildEarth argued that EPA lacked authority to adjust the deadlines. The Court held that given the novel circumstances presented here, EPA reasonably acted within its statutory authority in adopting new deadlines.

Background

EPA's rule arose in response to the *Natural Resources Defense Council* ("*NRDC*") v. EPA, 706 F.3d 428 (D.C. Cir. 2013) decision – remanding EPA's earlier rules implementing the 1997 national ambient air quality standards ("NAAQS") for PM2.5. In *NRDC* the Court held that EPA erred as a matter of law by applying only the provisions of subpart 1 in its implementation rules, rather than also applying subpart 4. (*NRDC*, 706 F.3d at 429.) The Court accordingly "remand[ed] to EPA to re-promulgate these rules pursuant to Subpart 4 consistent with this opinion." (*Id.* at 437.) Thereafter, EPA promulgated the Classification and Deadline Rule in an ongoing effort to implement the PM2.5 NAAQS under subpart 4, as ordered on remand.

WildEarth challenged the deadline EPA established in this rule for states to submit plans for EPA's approval implementing subpart 4, and EPA's classifications of certain nonattainment areas. WildEarth alleged that the Classification and Deadline Rule avered from subpart 4 – exceeding EPA's rulemaking authority. EPA developed this rule, however, in response to unique circumstances - specifically, as a result of the *NRDC* decision of this Court in 2013 holding for, the first time, that subpart 4 governed implementation of PM2.5 NAAQS pursuant to subpart 4. The Court's remand in *NRDC* did not vacate EPA's earlier implementation rules or hold that any such rule should be applied retroactively to states' earlier actions taken in compliance with those earlier rules. Rather, the Court held that EPA should act prospectively by promulgating new or revised rules that would provide for implementation of the PM2.5 NAAQS pursuant to subpart 4

Under the Clean Air Act ("CAA"), EPA identifies air pollutants anticipated to endanger the public health and welfare, and formulates NAAQS, which establish maximum permissible concentrations of those pollutants in the ambient air. (42 U.S.C. §§ 7408-09; 40 C.F.R. pt. 50.) NAAQS is reviewed at least once every five years and revised as "appropriate in accordance with [42 U.S.C. § 7408 and 7409(b)]." (42 U.S.C. § 7409(d)(1).) After promulgating a new or revised NAAQS, EPA must "designate" areas of the country as "attainment" (i.e., meeting that NAAQS), "nonattainment" (i.e., not meeting that NAAQS), or "unclassifiable," 42 U.S.C. § 7407(d)(1). The Act then requires each state to prepare a state implementation plan ("SIP" or "plan") that explains how the state will implement, maintain, and enforce the NAAQS and ensure that any nonattainment areas within its borders will attain the NAAQS. (*Id.* §§ 7410(a)(1)- (2); see Lead Indus. Ass'n v. EPA, 647 F.2d 1130, 1137 (D.C. Cir. 1980).)

EPA reviews each submitted SIP for compliance with the applicable provisions of the CAA. (Louisiana Envtl. Action Network v. EPA, 382 F.3d 575, 578-79 (5th Cir. 2004); 42 U.S.C. § 7410(k).)

Until *NRDC* in January 2013, states relied on EPA's implementation of its 1997 and 2006 PM2.5 standards under The CAA's Subpart 1, 42 U.S.C. §§ 7501, et seq. Therefore, until the *NRDC* ruling, states had been on notice that their PM2.5 SIP development and rulemaking efforts would be evaluated under Subpart 1, not Subpart 4.

Court's Rationale

After meeting its standing obligation, the Court turned to merits of WildEarth's argument that the plan submission deadline set by the Implementation Rule was incompatible with Subpart 4. Given the unique circumstances at issue – the Court held that the Rule "constitutes a reasonable exercise of EPA's rulemaking authority." (*Id.*)

WildEarth argued that once EPA established a particulate matter standard and identified nonattainment areas, "Subpart 4 constrains the agency's discretion over implementation of the standard in certain ways." (*Id.*, citations omitted.) The point being, WildEarth argued, EPA was required to issue immediate "failure-to-submit" findings to any state that had not yet submitted a plan that was compliance with Subpart 4. (*Id.*)

The Court held that "…EPA acted within its authority under the statute. It is true that Subpart 4 sets the schedule for plan submission and failure-to-submit findings once the agency issues nonattainment designations, and that the agency generally lacks discretion to modify that schedule. But the statute does not address what should happen if, as in the novel circumstances of this case, all affected parties have been long acting on the mistaken assumption that a different framework – and hence a different schedule – controls." (*Id.*)

EPA acted reasonably in not finding states to have been in violation, but in setting a modified deadline for the submission of moderate-area plans to, thereby, eliminate a state's ability to request voluntary reclassification of a moderate area as serious. As a result, EPA's Rule avoids a situation in which EPA's action would impose retroactive consequences on states, "a result we have sought to avoid in our decisions." (*Id.*)

(Cont.)

Article Three (cont.)

EPA's Implementation Rule Was A Reasonable Exercise of EPA's Gap-Filling Authority

Conclusion

The Classification and Deadline Rule accomplishes that end without unfairly penalizing states for their past reliance on EPA's earlier implementation rules and guidance. Avoiding the imposition of retroactive consequences is a matter of judicial concern. In *Sierra Club v. Whitman*, 285 F.3d 63 (D.C. Cir. 2002), the Court ordered EPA to make a mandatory ozone NAAQS determination for the St. Louis area, which should have been done years before. The Court rejected the argument that EPA backdate its determination "to the date the statute envisioned, rather than the actual date of EPA's action." (*Id.* at 68.) The Court saw no reason to conclude that "Congress intended to give EPA the unusual ability to implement rules retroactively." (*Id.*)

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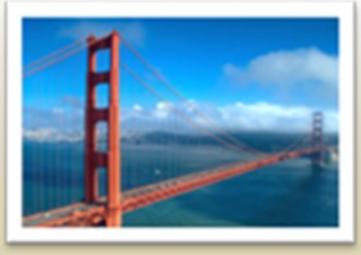

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