

**ENVIRONMENTAL LIABILITY AND THE COMMERCIAL
LEASE - WHO PAYS THE COST TO REMEDIATE
CONTAMINATED LAND?**

UNA RADOJA
&
KORA PACIOREK

Environmental Liability and the Commercial Lease - Who Pays the Cost to Remediate Contaminated Land?

Exposure to environmental liability is a real and significant concern for both landlords that own and tenants that carry on operations on contaminated land in British Columbia. A fundamental aspect of British Columbia's environmental legislation is that relatively limited involvement with a contaminated site, which may not have given rise to the actual contamination, is often sufficient to trigger responsibility for the remediation of the site and result in liability for the costs of remediation. In a landlord / tenant context, an "innocent" landlord who leases his or her lands to a tenant whose operations cause contamination may have to pay for the costs of clean-up in order to redevelop the lands or prevent migration, for example, and, if the tenant no longer exists or is impecunious, may not be able to recover these costs from the polluting tenant. Such a landlord may also face liability for costs of cleaning up surrounding lands, if contamination migrated to other properties. Similarly, "innocent" tenants (i.e., tenants whose operations did not cause contamination), may in certain circumstances attract responsibility and liability for cleaning up contamination on the lands they lease, if, for example, the contamination expanded during tenant's operations on the leased premises and early clean-up was not possible due to tenant's operations. In cases where a tenant comes to land that is already polluted for the purposes of carrying out an operation that also carries environmental risk, at the end of the tenancy, issues may arise as to which portion of the clean-up costs are attributable to the tenant's operations and which are related to pre-existing contamination. In some cases, this is easy to establish – in others, almost impossible, and the tenant may bear some of the costs to remediate pre-existing contamination.

In Part I of this paper we provide an overview of the applicable regulatory regime and how it can give rise to environmental liability, in the context of a landlord/tenant relationship. In Part II, we discuss the available strategies to identify, minimize and/or allocate environmental liability risks.

I. Statutory Liability for Costs of Remediation

The *Environmental Management Act*, S.B.C. 2003, c. 53 (“EMA”) and the Contaminated Sites Regulation, B.C. Reg. 375/96 (“CSR”) provide the regulatory framework for identifying and allocating liability among persons responsible for remediation of contaminated sites in British Columbia. While the focus of this paper is on statutory liability (i.e., liability arising from the EMA and the CSR), it is important to note that liability can also arise in common law (i.e., tort of nuisance, strict liability doctrine in *Rylands v. Fletcher* and, in certain cases, negligence).

1. Civil and Regulatory Liability

There are two avenues by which a person may become liable for costs of remediating a contaminated site under the EMA: 1) in a civil, cost recovery action brought by another person who has incurred costs of remediation and is suing to recover them; and/or 2) by way of an order made by the director pursuant to the EMA (i.e., an order of the Ministry of Environment), requiring the person to investigate or remediate a contaminated site.¹ The civil cost recovery provision is, by far, the most common way persons attract liability under the EMA.

The civil cost recovery provision is set out in section 47(5) of the EMA. Pursuant to this provision, any person who has incurred reasonable costs of remediation in relation to a contaminated site can sue to recover such costs from any statutory “responsible person”. Such “responsible persons” (if there is more than one) are absolutely, retroactively, jointly and separately liable for all of the reasonably incurred costs of remediation.² “Costs of remediation” include not only the costs associated with the physical removal or risk-assessment of the contaminants in question, but also costs of carrying out environmental investigations at the site.³

Liability under section 47(5), EMA is “absolute”. No “fault”, “negligence” or any “wrongdoing” in the traditional sense is necessary to establish a claim. It is also “retroactive”, meaning that one can be liable for contamination that occurred prior to the

¹ Other orders may be made by the director including pollution abatement orders. The full extent of the director’s powers to make orders under the EMA is beyond the scope of this paper.

² s. 47(1), EMA

³ s. 47(3)

EMA and the CSR (and the predecessor legislation) coming into force. In fact, responsible persons can be liable for costs of remediation incurred by any person in relation to a contaminated site even if, at the time, the person had a permit allowing them to introduce contaminants into the environment.⁴

Given that liability among responsible persons in a cost recovery action is also “joint” and “separate”, each “responsible person” may be looked to for the full cost of clean-up, regardless of the extent of that person’s involvement with the property or its contamination. The court will, however, apportion reasonably incurred costs of remediation among responsible persons in a cost recovery claim, as the court considers fair.⁵ But, since liability is joint, if certain responsible persons are impecunious, those that are not may ultimately end up paying more than their allocated share.⁶

In deciding how to apportion the costs of remediation among the responsible persons, the court must consider various factors including the relative due diligence of the responsible persons, their contribution to contamination, and any remedial measures implemented by the responsible persons involved in the action. The court can also consider any other factors relevant to a fair and just allocation, such as any contracts between the responsible persons.⁷

2. “Responsible Person” Status - How Wide of a Net Is It?

Only those defined in the EMA as persons responsible for remediation of a contaminated site can face civil liability pursuant to section 47 of the EMA. While a director can technically make an investigation order against any person (not just a responsible person), other types of orders, such as remediation orders, for example, can only be made against a responsible person. In reality, even investigation orders are only made against responsible

⁴ s. 47(4), EMA

⁵ s. 47(9), EMA

⁶ In certain cases, a responsible person may escape joint and several liability by establishing that he or she is a “minor contributor” pursuant to section 50 of the EMA. Pursuant to this provision, a person will be liable in a cost recovery provision only up to the amount or portion specified by the director or the court is the portion of the total costs of remediation attributable to that person. To establish minor contributor status, the person must demonstrate that only a minor portion of the contamination present at the site can be attributed to the person, that either no remediation would be required solely as a result of the contribution of the person to the contamination at the site or the cost of remediation attributable to the person would be only a minor portion of the total cost of remediation required at the site, and in all the circumstances application of joint and separate liability would be unduly harsh.

⁷ s. 35(2), CSR

persons and orders (of any kind) are very rare and reserved only for heavily contaminated sites that pose a significant risk to human health and/or the environment.

Subject to specific exemptions set out in section 46 of the EMA and Part 7 of the CSR, all current and previous “owners” and “operators” of a “contaminated site” are persons responsible for remediation of the site.⁸ In circumstances where contaminants migrate from one site to another, subject to an exemption, all current and previous owners of the source site are also persons responsible for remediation of the site contaminated by the migrating contaminants from the source site.⁹ In addition to “owners” and “operators”, those who produced, transported or arranged for transport of a substance and who by, contract, agreement or otherwise, caused the substance to be disposed of, handled or treated in a manner that, in whole or in part, caused the site to become a contaminated site, are also “persons responsible” for remediation of the site and any sites impacted by contaminant migration from the source site. The focus of this paper will be on owners and operators as responsible persons.¹⁰

A person cannot attract responsible person status under the EMA on the basis of him or her assuming that status pursuant to a contract, unless the person meets the definition of “responsible person” in the EMA.¹¹ Nevertheless, those who are not responsible persons under the EMA can assume liability for costs of remediation by way of contract (vis-à-vis the other contracting party). Contractual clauses dealing with allocation of environmental risk are discussed further below.

Responsible person status pursuant to the EMA is triggered only once a site becomes a “contaminated site”.

A “contaminated site” is defined in the EMA as an area of land in which the soil or any groundwater lying beneath it, or the water or the underlying sediment, contains a hazardous waste or another prescribed substance in quantities or concentrations exceeding risk based or numerical criteria, standards or conditions set out in the CSR.¹²

⁸ s. 45(1)(a) and (b), EMA

⁹ s. 45(2)(a) and (b), EMA

¹⁰ s. 45(1)(c) and (d), EMA; s. 45(2)(c) and (d), EMA;

¹¹ *Shaol Point Management Ltd. v. ICI Canada Inc.*, 2006 BCSC 857

¹² s. 39, EMA

A large number of substances (i.e., hydrocarbons, metals, dry-cleaning solvent related compounds, etc.) are regulated by the CSR. Presence of such substances in soils, water (surface or groundwater), sediment, and/or soil vapour, in concentrations exceeding the standards applicable to the site in question (based on land use) means that the site is a “contaminated site”, and all current and previous “owners” and “operators” of such a site are persons responsible for remediation of the site, absent an exemption.

(a) Current and Previous Owners

“Owner” is defined very broadly in the EMA as a person who is in possession, has the right of control, or occupies or controls the use of real property, and includes a person who has an estate or interest, legal or equitable, in the real property.¹³ Therefore, the definition of “owner” goes beyond registered owner in fee simple. It can include the parent company of the registered owner (if the parent has the right of or actually controls the site in question), a beneficial owner, and anyone with an estate or interest in the property, including, for example, a tenant.

Landlords are “owners” as defined in the EMA, either as registered title holders or, if they are not registered owners in fee simple, as those with a beneficial interest or a right to control the leased property.

(b) Current and Previous Operators

“Operator” is also broadly defined as a person who is or was in control of or responsible for any operation located at a contaminated site.¹⁴

A person who makes decisions with respect to any operation at a contaminated site is “in control” of the operation and a person who has the authority to make decisions with respect to any operation is “responsible” for the operation. All such persons are “operators” under the EMA regardless of whether they are or were in control of or responsible for the specific activity that gave rise to the contamination.¹⁵ Tenants carrying on any operation at a contaminated site are, therefore, “responsible persons” as operators, subject to an exemption.

¹³ s. 39, EMA

¹⁴ s. 39, EMA

¹⁵ *Beazer East, Inc. v. British Columbia (Environmental Appeal Board)*, [2000] B.C.J. No. 2358 (S.C.)

Landlords are also responsible persons as “operators”, in addition to being responsible persons as “owners”. This was confirmed in *Gehring v. Chevron Canada Ltd.*, 2006 BCSC 1639 (“*Gehring*”), where the Court held that a landlord leasing the property to commercial tenants carried on a “leasing operation” at the property and could be considered an “operator” on this basis alone (in addition to also being an “owner”).¹⁶

(c) Directors, Officers, Employees and Agents of Corporate Responsible Persons

A “person” is defined in section 39(1) of the EMA as including “any director, officer, employee or agent of the person”.

As a result of the expanded definition of “person”, if a corporation is a “responsible person” (as an owner, operator, producer or transporter), the directors, officers, employees and agents of that company are automatically also “responsible persons”.¹⁷

Directors and officers of a dissolved company which was a responsible person prior to its dissolution cannot be considered responsible persons solely on the basis of their position with the dissolved company.¹⁸ In most situations, directors’ and officers’ exposure to liability arises simply from their relationship with the corporate entity that is considered a responsible person. Such directors and officers will be protected by the *Gehring* decision after the corporate entity dissolves.

However, directors and officers may also become responsible persons because of their personal and direct involvement with a contaminated site as current or past “owners” or “operators”. For example, if a director of a corporate tenant operating on a contaminated site has the right, in his or her personal capacity, to control the use of the contaminated site, the director is a responsible person in his or her own right, along with the company, in relation to that site. Such a director would remain a responsible person after the company dissolves.

¹⁶ *Gehring*, para. 29

¹⁷ *Gehring*, paras. 50 and 51

¹⁸ *Gehring*, paras. 59-62

In a cost recovery action under the EMA, the CSR affords some protection to directors, officers, employees and agents who are found to be “responsible persons”, whether merely by virtue of their relationship with the corporate responsible person or in their own right.

Pursuant to section 35(4), CSR, in order to succeed in a cost recovery action against a director, officer, employee or agent, the plaintiff must prove that the director, officer, employee or agent “authorized, permitted or acquiesced in the activity which gave rise to the cost of remediation”. Thus, while a corporate owner might be responsible and liable solely due to its status as legal title holder of a contaminated site, a director of such an owner would not shoulder liability unless the director authorized, permitted or acquiesced in the contaminating activity.

Because of the protection provided by section 35(4), CSR, a director who, for example, allowed the corporate entity to purchase an already contaminated site in circumstances in which an exemption does not apply, would likely still escape liability in a cost recovery claim (provided the director did not do anything to worsen the contamination). In this scenario, the director would not have an opportunity to authorize, permit or acquiesce in the historic activity that contaminated the property. However, if the contamination expands or migrates to other properties after the purchase of the contaminated land by the corporation, the director may lose the protection afforded by section 35(4), CSR.

On the other hand, a director who, for example, allows a corporate landlord to lease a site to a tenant whose operations cause contamination may be held to have “permitted” the contaminating activity and, as a result, may not be able to avail himself or herself of the protection set out in section 35(4), CSR. In such circumstances, both the landlord and its director may be liable for costs of remediation in a civil cost recovery claim brought, for example, by a subsequent owner or a neighbour impacted by contaminant migration.

3. Exemptions

As discussed above, absent an exemption, both a landlord who owns or has owned a site that is a contaminated site, and a tenant who operates or has operated on such a site, are responsible persons and may face liability in a cost recovery claim brought by any person who has incurred costs in remediating the site in question, such as, for example, a subsequent owner of the site or a neighbouring property owner whose lands were impacted

by contaminants that migrated from the site owned by the landlord and operated on by the tenant. Although in most cases, the current and former tenants will not be named in such a lawsuit unless it is clear that the tenant's operation caused the contamination (i.e., the tenant operated a gas station, dry-cleaning business, a foundry, or some other environmentally risky operation on the site), there may be circumstances warranting naming of an "innocent" tenant in a cost recovery claim, such as where the landlord (current or previous owner) and/or the actual polluter no longer exists or is impecunious. Such tenants, even if they ultimately escape liability, will still incur the financial and other costs inherent in defending a lawsuit.

Non-polluting landlords and tenants facing a cost recovery claim (or a director's order) will normally attempt to establish an exemption from responsible person status. Section 46 of the EMA and Part 7 of the CSR identify persons who are exempt from responsible person status. A person seeking to establish that he or she is not a responsible person on the basis of an exemption has the burden of proving all elements of the exemption on a balance of probabilities.¹⁹ Once an exemption is proven, the person is exempt from responsible person status and cannot face a remediation order or be found liable in a cost recovery action under the EMA.

A detailed discussion of all of the exemptions set out in the EMA and CSR is beyond the scope of this paper. Rather, in this paper, we will only deal with the most common exemptions and how they may apply in a landlord/tenant context.

(a) Innocent Acquisition Exemption

In cases of pre-existing contamination, not caused by the landlord (current owner) or the tenant, the landlord and tenant may be able to rely on the exemption contained in section 46(1)(d) of the EMA. This section provides an exemption from responsible person status to an owner or operator who establishes that at the time the person became an owner or operator of the site:

- the site was a contaminated site,
- the person had no knowledge or reason to know or suspect that the site was a contaminated site,

¹⁹ s. 46(3), EMA

- the person undertook all appropriate inquiries into the previous ownership and uses of the site and undertook other investigations, consistent with good commercial or customary practice at the time, in an effort to minimize potential liability, and
- the person did not by any act or omission, cause or contribute to the contamination of the site.

Section 28 of the CSR provides further clarification respecting the factors to consider in determining whether the person undertook “all appropriate inquiries” into the previous ownership and uses of the site.²⁰ These factors include:

- any personal knowledge or experience of the owner or operator respecting contamination at the time of the acquisition;
- the relationship of the actual purchase price to the value of the property if it was uncontaminated;
- commonly known or reasonably ascertainable information about the property at the time of acquisition;
- any obvious presence of contamination or indicators of contamination or the feasibility of detecting such contamination by appropriate inspection at the time of the acquisition.

Therefore, a person who buys or leases a contaminated site unknowingly may be able to establish an exemption under section 46(1)(d), EMA, if it can be clearly shown that all of the contamination occurred prior to the person becoming an owner or operator of the site, and the person did not cause or contribute to the contamination by any act or omission. For an owner/landlord, this is more difficult to establish than it sounds, particularly where it cannot be shown that the contamination was stable at the time the person became the owner, but rather could have been expanding throughout the property although the source of the contamination (i.e., old dry-cleaning business or gas station) was no longer present on the property at the time the person became an owner. If the contamination was expanding after the person became an owner, arguably the person did, by his or her omission (i.e., failure to remediate in a timely fashion), contribute to the contamination and the exemption should not apply. In the context of a tenant who comes to the contamination, even if the contamination did expand during the tenant’s lease of the site, the tenant could potentially establish the

²⁰ *Ibid.*; CSR, *supra* note 2 at s. 28

exemption in section 46(1)(d), EMA, if all other requirements of the exemption can be made out, including proper due diligence prior to entering into the lease agreement, on the basis that the tenant had no ability to stop the expansion (by remediating the site, for example), if no such right existed in the lease, and therefore did not, by its own omission, allow expansion.

Although innocent / non-polluting tenants will generally more easily establish this (and other) exemptions than non-polluting owners/landlords, tenants should consider carefully whether to lease sites that are or may be contaminated. Plaintiffs in cost recovery claims tend to name all potentially responsible persons and long-term tenants may well have to defend a cost recovery claim, even if their activity did not cause the contamination. This risk can be avoided by conducting due diligence respecting operations that were carried out historically on the property to be leased and choosing not to lease properties that are likely contaminated. In the alternative, if potentially contaminated property will be leased, the risk can be minimized through contractual protections (discussed further below), provided that the landlord has the financial means to provide meaningful protections.

(b) Third Party Exemption

Section 46(1)(c) of the EMA contains what is referred to as the third party exemption. It provides that a person who would become a responsible person only because of an act or omission of a third party, other than an employee, agent or a party with whom the person has a contractual relationship will be exempt from responsible person status, provided that the person exercised due diligence with respect to any substance that, in whole or in part, caused the site to become a contaminated site.

This exemption will generally apply to an owner/landlord or tenant who can establish when and how the contamination occurred and that it occurred solely as a result of an act or omission of a third party with whom the owner/landlord or tenant/operator did not have a contractual relationship (employment, agency or other). This exemption is often invoked in cases of an accidental spill caused by a third party on someone else's land. Once again, however, due diligence (this time in relation to the contaminating substance) is required to establish an exemption. In the example of an accidental spill caused by a third party, this means that if the owner/landlord and, arguably, even tenant/operator, witnesses or learns of the spill caused by a third party, but does nothing to abate it and prevent expansion of

contamination throughout the lands, they may not be able to avail themselves of this exemption.

Non-polluting tenants may be able to establish this exemption in other contexts (i.e., not involving accidental spills by third parties). For example, in cases of pre-existing contamination caused by a previous tenant, the non-polluting tenant will likely be able to establish this exemption, especially if no expansion of pre-existing contamination occurred during the innocent tenant's lease and/or if expansion did occur, the tenant had no ability, under its lease, to prevent such expansion.

(c) Innocent Owner or Operator Exemption

Section 46(1)(e), EMA, exempts from responsible person status an owner or operator who owned or occupied a site that at the time of acquisition was not a contaminated site during his/her ownership or operation, and the person did not dispose of, handle or treat a substance in a manner that, in whole or in part, caused the site to become a contaminated site. This exemption is often invoked by non-polluter owner and operators in situations where a clean site is acquired or leased, which subsequently becomes contaminated.

At a first glance, this exemption is helpful to landlords and/or tenants that did not directly cause a contamination; however, section 29 of the CSR significantly curtails the availability of this exemption in the case of a landlord. A landlord will not be able to rely on this exemption if he or she:

- (a) voluntarily leased, rented or otherwise allowed use of the real property by another person,
- (b) knew or had a reasonable basis for knowing that the other person described in paragraph (a) planned or intended to use the real property to dispose of, handle or treat a substance in a manner that, in whole or in part, would cause the site to become a contaminated site, and
- (c) the person used the real property to dispose of, handle or treat a substance in a manner that, in whole or in part, caused the site to become a contaminated site.

Therefore, a landlord who acquired a clean property and subsequently leased it to a tenant who contaminated the property will not be able to rely on the exemption in section 46(1)(d),

EMA, if the landlord knew or had a reasonable basis for knowing that the tenant's operation could cause contamination.

The rationale for holding landlords responsible for acts of their tenants was articulated in *British Columbia Railway Co. v. British Columbia (Ministry of Water, Land and Air Protection)*.²¹

[201]... A landlord, who leases property to an industrial tenant should not be allowed to "turn a blind eye" to activities of its tenant that cause the leased property and surrounding environment to become contaminated. The landlord should do more than rely on regulators or its tenant to deal with environmental problems. The benefits derived from leasing property should go hand in hand with some degree of responsibility for the property and activities occurring on it with the landlord's knowledge or consent.

Section 29 of the CSR was considered in the case of *O'Connor v Fleck*.²² Here, a previous landlord was held to be a "responsible person" for their tenant's contamination of the site. The tenant operated a brass and aluminum foundry in the plaintiff landlord's building for 26 years. After the tenant vacated the building, the landlord undertook an environmental investigation of the property which revealed contamination. The landlord remediated the site and sued the tenant for remediation costs incurred after the tenant had vacated. Since that tenant directly caused the pollution, there was no doubt that the tenant was a responsible person.

After finding that the former landlord was also *prima facie* a "responsible person", the court considered whether the landlord could avail itself of the innocent owner exemption. Although the court accepted that the site was not contaminated when the landlord purchased it and the landlord did not contribute to the contamination through his own activities, section 29 of the CSR disqualified the landlord from being able to rely on the exemption. The landlord knew of the defendant's operation and it could not be said that the landlord had no reasonable basis for knowing that the operations would cause the site to become contaminated. Although the landlord was a responsible person, ultimately, however, all of the costs of remediation were allocated to the polluting tenant. This will normally be the case whenever the polluter is around and can pay for the remediation. If

²¹ [2004] B.C.E.A. No. 6.

²² *O'Connor v Fleck*, [2000] BCJ No. 1546, 2000 BCSC 1147 [*O'Connor*].

the suit had instead been brought against the landlord by a neighbour impacted by contaminant migration, and the polluting tenant was no longer around or was impecunious, the “innocent” landlord would likely have shouldered all of the costs of remediating the neighbouring property since the landlord could not establish an exemption and the more culpable party (i.e., the polluting tenant) was not available to shoulder the costs.

(d) Migration Exemption

Section 46(1)(j), EMA exempts from responsible person status those who own or operate a contaminated site that was contaminated only by the migration of a substance from other real property not owned or operated by the person. Therefore, both landlords and tenants who respectively own and lease/operate on land contaminated by migration from other properties will be exempt from responsible person status. This means that if the property impacted by migration is sold and remediated by the new owner, the new owner will not have a claim against the former owner/landlord and its tenants. The new owner will only have a claim against the source property owner and operators.

(e) Certificate of Compliance Exemption

Pursuant to section 46(1)(m), EMA, a person who was a responsible person for a contaminated site for which a certificate of compliance²³ was issued and for which another person subsequently proposes or undertakes to change the use of the site and provide additional remediation, is exempt from the responsible person status.

Therefore, an owner whose land has been contaminated by his or her tenant, for example, can ensure that the saleability and value of his or her property are preserved by completing a remediation of the property and can, in effect, create an exemption by taking the extra step of obtaining a certificate of compliance for the site prior to selling it. All such costs, including the costs of obtaining a certificate, would, potentially, be recoverable from the former owners and operators, including, of course, the polluting tenant, if he or she is still around. A certificate of compliance will protect not only the person who obtained it (in this example the owner), but also others who would be responsible persons, but for the

²³ A certificate of compliance is a legal instrument issued by the Ministry of Environment on application by a person who has completed an investigation and remediation of a contaminated site in accordance with the EMA, CSR and director's protocols, guidances and procedures. The certificate confirms that the site has been properly remediated to meet the applicable risk-based or numeric standards, in respect of parameters listed in the certificate. Therefore, a certificate of compliance can provide significant comfort to purchasers, lenders, insurers and others considering dealing with previously contaminated land.

remediation and the issuance of the certificate. Thus, in this example, the polluting and non-polluting tenant would also be protected by the certificate from claims brought on by future owners who seek to change the use of the site and carry on further remediation. Importantly, such tenants would not, however, be protected in a claim brought by the owner who carried out the remediation and obtained the certificate, if that owner did not change the use of the site, but merely remediated it to obtain the certificate.

II Minimizing Risk

Since both landlords and tenants can attract statutory environmental liability arising from mere ownership or having carried out any (even non-polluting) operation on contaminated land, measures to minimize and, where appropriate, allocate, the liability risk should be considered by both prior to the commencement of the lease.

The nature of the protections and who will seek them (i.e., the landlord or the tenant) will depend on the type of property being leased, former operations that had been carried out on the property, the environmental condition of the property prior to the lease and the nature of the operations to be carried out by the prospective tenant.

a) Due Diligence

The first protective measure, for both the landlord and tenant, is to carry out sufficient due diligence prior to execution of the lease.

(i) Landlords

For the landlord, the due diligence process will be aimed at understanding the nature of the operations proposed to be carried out by the tenant on the property to be leased. If a sub-lease is being contemplated, the nature of the sub-tenants' operations, and the environmental risk, if any, they carry, will also have to be fully understood.

A number of potentially environmentally risky operations can be carried out on commercial and industrial lands. A comprehensive list is set out in Schedule 2 of the CSR, and includes operations such as:

- manufacture and/or wholesale bulk storage of adhesives, explosives, fire retardants, fertilizers, inks or dyes
- leather or hides tanning
- paint, lacquer or varnish manufacturing, formulation, recycling or wholesale bulk storage

- manufacture and storage of certain pharmaceutical products
- manufacture of resin and plastic products
- textile dyeing
- manufacture or bulk storage of pesticides
- manufacture or wholesale bulk storage of batteries (lead acid or other), electrical equipment or electronic equipment
- mining, milling or related industries and activities
- appliance, equipment or engine repair, reconditioning, cleaning or salvage
- asphalt tar manufacture, wholesale storage and distribution
- medical, chemical, radiological or biological laboratories
- road salt storage facilities
- dry cleaning facilities or operations and dry cleaning chemical storage
- petroleum and natural gas drilling, production, processing, retailing, distribution and storage
- automotive, truck, bus, subway or other motor vehicle repair, salvage or wrecking
- ship building or boat repair and maintenance
- truck, rail or marine bulk freight handling
- pulp and paper manufacturing
- veneer or plywood manufacturing
- sawmills
- antifreeze bulk storage or recycling
- biomedical waste disposal
- contaminated soil storage, treatment or disposal
- industrial waste storage, recycling or landfilling
- waste oil reprocessing, recycling or bulk storage

All of the above activities (the list is not exhaustive) carry the risk of environmental contamination. Landlords who lease their lands to tenants for the purposes of carrying out such operations face the risk that their lands may become contaminated by the tenant's operations. Furthermore, disclosure of these activities to municipal and provincial authorities will, in most cases, be required on redevelopment, followed by environmental investigations to confirm that the lands have not been polluted or that the contamination does not pose an unacceptable risk in the context of the proposed development.

In addition to ensuring that they fully understand the nature of the tenant's proposed operations and the environmental risk, if any, they carry, landlords should also make inquiries into the financial means of the prospective tenant to address environmental concerns, if contamination does occur. It may also be necessary to gather information about the history of the prospective tenant's compliance with environmental laws.

Having obtained this information, landlords should consider and carefully weigh the risks and benefits associated with leasing their property to tenants who will carry out on the property industrial or commercial activity that may result in environmental contamination.

The longer the term of the lease and the less control the landlord has over the property during the term, the more significant the risk.

(ii) *Tenants*

Tenants also need to perform their own environmental due diligence prior to entering into a lease. In contrast to the landlord (whose due diligence is aimed at understanding the tenant's proposed operation), the tenant's due diligence process will be aimed at obtaining information about the environmental condition of the land prior to commencement of the lease. The process may include a search of the Ministry of Environment Contaminated Sites Registry, a review of existing environmental reports respecting the lands to be leased (obtained from the Registry or provided by the landlord), inquiry into and verification of the financial means of the prospective landlord, and an inquiry into the prospective landlord's historical compliance with environmental laws.

Tenant due diligence is perhaps even more important for tenants who plan to carry on operations that may result in environmental contamination. Such tenants will want to know whether similar operations were carried out on the property by previous tenants, whether such tenants have introduced contamination at the property and, if so, whether it has been remediated. The primary concern for such tenants will be to ensure that at the end of their tenancy, they are not required to pay for the remediation of pre-existing contamination caused by a historic tenant who carried on a similar operation. Understanding the environmental condition of the property, and having, in essence, a baseline, prior to leasing the property will minimize such risk.

In many cases where the premises to be leased have already been contaminated and the contaminants of concern are of the kind the new tenant's operations may introduce, the prospective tenant will require that the existing contamination be remediated, at the landlord's expense, prior to commencement of the new tenancy. This will ensure that on completion of the new tenancy, it will be clear what contamination, if any, is attributable to the new tenant. The landlord, in such circumstances, will want to ensure that the new tenant agrees to carry out, at its expense, an environmental investigation at the end of the tenancy, as well as a remediation of contamination, if any, caused by the new tenant.

b) Environmental Insurance

Landlords and tenants exposed to potential environmental liability should consider obtaining an appropriate insurance policy. A commercial general liability policy typically will not cover environmental risk. Although environmental liability policies used to be prohibitively expensive, in recent years the insurance premiums for such policies have become more reasonable.

There are a variety of environmental liability policies available. "Pollution liability" policies deal with risks identified at a particular site and the liability arising from unanticipated pre-existing or new contamination. Such policies can cover third party claims, personal injury or property damage, business interruption costs, and other losses. "Clean-up costs cap" or "stop loss" policies typically provide coverage where there is known contamination at the site, or where contamination is likely to exist and where remediation of the property is required or is likely to be required.

Historic property insurance policies should also be considered whenever one is faced with a cost recovery or other type of claim. Some historic policies did not contain pollution exclusion clauses and may provide coverage.

c) Contractual Protections

Environmental risk can be allocated as between a landlord and a tenant in a lease agreement. Both parties need to consider carefully the environmental obligations they are assuming in a lease.

Contractual protections are, of course, only operative vis-à-vis the other contracting party, as one cannot contract out of responsible person status and, therefore, liability to non-parties to the contract. For example, a polluting tenant may provide to a landlord a covenant that the tenant will remediate the contamination on termination of the lease and, further, a release in favour of the landlord which will ensure that the tenant will have no claim against the landlord for any costs incurred in remediating the leased premises or any neighbouring lands impacted by migration from the leased premises. If the tenant does not remediate neighbouring lands impacted by migration from the leased premises, the release given by the tenant to the landlord will not prevent the impacted neighbouring property owner from commencing a statutory cost recovery claim against the landlord. While the

landlord would have a claim over against the polluting tenant, if the polluting tenant is no longer available to pay for the remediation costs of the impacted neighbour, the “innocent” landlord will likely have to shoulder that liability notwithstanding the contractual protections provided by the polluting tenant.

The following discussion highlights the common contractual protections that can be negotiated into a lease agreement, but does not (and cannot) provide an exhaustive list of all possible protective terms and situations where they may be appropriate. Landlords and tenants should consult with environmental lawyers early in the negotiations to ensure that they are properly advised of the environmental risk they are assuming and that sufficient and properly drafted protections are negotiated into the lease.

(i) Landlords

There are a number of provisions that a landlord may seek to negotiate into a lease to protect itself from environmental liability. The level of protection the landlord will seek to obtain will depend on the nature and extent of the environmental risk posed by the tenant as well as, to a lesser degree, the existing environmental condition of the land to be leased. For example, a landlord considering leasing a clean property to a tenant who intends to carry on it an environmentally risky operation will want to negotiate the highest level of protection possible.

The lease agreement can impose requirements on the tenant during the life of the tenancy, at the end of the term, and obligations that continue after the tenancy ends.

In circumstances involving a lease of a clean property, the landlord may want to obtain an acknowledgment from the tenant that the land to be leased was free and clear of contaminants prior to commencement of the lease.

In almost all environmentally risky tenancies, the landlord will require the tenant to prevent or, at the very least, take all reasonable steps to prevent, the introduction of contaminants at the leased premises, and to notify the landlord of any spills or discovery of contamination, as well as of any claim or demand being made by a neighbour or the regulator respecting environmental issues. The landlord will also normally require the tenant to seek the landlord’s prior consent before modifying the operations to be carried out on the leased premises in a manner that may increase the environmental risk.

The landlord may require the tenant to undertake environmental investigations during the term of the tenancy and address impacts as they arise, particularly if migration of contamination caused by the tenant is a concern. Terms allowing the landlord to access the leased premises for the purposes of carrying out its own inspections and, where the tenant fails to do so, an investigation and remediation of the leased premises, are also commonly negotiated, as are terms allowing the landlord to terminate the tenancy in circumstances where the tenant defaults on its environmental obligations.

The lease agreement can and, in most cases, should, also deal with the tenant's obligations at the end of the lease. For example, the landlord may require the tenant to investigate the site for the presence of contamination and, if necessary, remediate the leased premises at the end of the tenancy. Particular care should be taken when drafting investigation and remedial obligations. The period of time the tenant has to complete the obligation and the nature of the investigation and remediation to be performed must be clearly set out. If the landlord wants the tenant to obtain a certificate of compliance for the leased premises, following completion of the remediation at the end of the term, this requirement must be expressly stated in the lease.

Finally, the landlord may wish to seek protective clauses that will continue to be in effect after termination of the tenancy. These include a release from the tenant (to ensure that the tenant will not seek to recover any of its investigation / remedial costs, incurred in relation to the leased premises or impacted neighbouring properties, from the landlord) and an indemnity from the tenant in favour of the landlord to protect the landlord from any claims, losses, damages, expenses, etc., arising from the contamination including, for example, claims that may be brought by third parties who may be impacted by the tenant's operations and/or migration of contaminants from the leased premises.

It is, of course, in the landlord's interest to structure such releases and indemnities as broadly as possible, and it is in the tenant's interest to limit them. Whatever the language ultimately agreed upon, both parties need to be properly advised respecting the scope and the limits of these terms and the circumstances in which they will be triggered. The party receiving the benefit of the indemnity (in our example, the landlord) will need to understand that an indemnity does not act as a shield against a remediation order²⁴ or a cost recovery

²⁴ *Halme's Auto Service Ltd. v. British Columbia (Ministry of Environment)*, [2014] B.C.E.A. No. 4 (EAB)

claim, although the landlord could invoke the indemnity to recover its costs incurred in dealing with the order and/or a cost recovery claim, including to recover any judgment granted against the landlord. Depending on the scope of the indemnity, the landlord may also be able to seek recovery of its legal fees incurred in having to defend a cost recovery claim or in having to deal with an order of the director. While an indemnity can provide significant protection, the party standing to benefit from it must also understand that the strength of the indemnity is, of course, directly proportional to the financial resources of the person providing it.

(ii) *Tenants*

Prospective tenants will also want to negotiate protections into a lease agreement for their benefit, particularly where the tenant's due diligence reveals existing contamination or a substantial risk of contamination at the premises to be leased. If the tenant decides to proceed with the lease in such circumstances, the tenant may require the landlord to remediate the contamination prior to commencement of the term. If this cannot be negotiated, the tenant will want to take extra precautions and seek other protections, to the extent possible, to ensure that it is not burdened with the costs of cleaning up pre-existing contamination.

A number of clauses can be used for this purpose. Firstly, where it is clear that the land has pre-existing contamination at the commencement of the new tenancy, the landlord should be required to acknowledge that fact in the lease agreement. The tenant should also require the landlord to provide a release and indemnity in favour of the tenant in respect of all pre-existing environmental issues at the property. The tenant may also seek a covenant from the landlord that the landlord will remediate the contamination during the term if there is risk of expansion or migration – this will minimize the risk that the tenant will be named in a cost recovery claim brought by an impacted neighbouring property owner. The tenant may also wish to include terms that will provide it with compensation for business interruption and other losses incurred as a result of such remedial works during the term of the tenancy.

Lease agreements involving pre-existing contamination and a new tenant whose operations carry the risk of introducing additional contamination of the same type are generally the most difficult to deal with. Inevitably, the question of source of the contamination at the

leased premises at the end of the new tenancy will come up. The landlord may wish to take the position that most of the contamination is attributable to the new tenant (particularly if the party that introduced the pre-existing contamination is no longer in existence). The new tenant will, of course, argue that none of the contamination was introduced during its tenancy. In these situations, the tenant will want to ensure that it keeps excellent records respecting its operations, any spills that occurred, any investigations and remedial measures implemented, etc., during the term of the lease. In order to minimize the risk of having to deal with pre-existing contamination, in circumstances where such contamination will not be remediated prior to commencement of the new tenancy, the tenant should also consider performing a baseline investigation before taking on the lease, so that both the landlord and tenant have a clear idea of the extent of the existing contamination on the land prior to the new tenancy. The landlord, the tenant, or both can assume the responsibility for paying for such an investigation.

Tenants assuming remedial obligations in a lease should ensure that such obligations are reasonably limited. It should be made clear that the tenant has no obligation to deal with pre-existing contamination and the scope of the pre-existing contamination should be clearly defined. With respect to contamination, if any, introduced by the tenant, the standards to which such contamination will be remediated by the tenant should be clearly spelled out. If either a risk-based remediation or numerical remediation is acceptable to the landlord, the tenant should have the ability to choose the less expensive remedial methodology.

Tenants assuming indemnity obligations should ensure that such provisions are also reasonably limited to losses and claims arising as a result of the tenant's own acts or omissions that caused contamination. As noted above, tenants should also consider seeking an indemnity from the landlord in respect of claims made or liabilities alleged against the tenant where such claims and liabilities arise as a result of or in relation to acts or omissions on the part of the landlord or other parties and/or as a result of pre-existing contamination.

III Conclusion

Ownership and lease of commercial and industrial land in British Columbia carries environmental risk. As a result, parties to every lease agreement involving industrial or commercial land should have a good understanding of the environmental liability regime, the nature of the property to be leased and the operations the tenant proposes to carry out on it. Properly informed landlords and tenants may choose, for business or other reasons, to engage in environmentally risky tenancies. In such cases in particular, understanding the environmental risk and ways to mitigate it, and negotiating reasonable protections into the lease agreement, will be key to avoiding unpleasant surprises at the end of an otherwise successful tenancy.

As with all contractual clauses, it is paramount that environmental terms be carefully drafted. Precise drafting is particularly important when defining the contaminants to be addressed and the type of investigations and remedial activities to be undertaken. Definitions in the EMA and the CSR should be consulted and incorporated into lease agreements, where appropriate. Remedial standards (with respect to remediation covenants) should be clearly set out in the lease. The release and indemnity language should be clear and unambiguous and should cover all potential issues arising from the tenant's operations at the leased premises (where the terms are for landlord's protection) and, conversely, all issues arising from pre-existing contamination and/or acts or omissions of the landlord (where they are intended to benefit the tenant). Those assuming obligations to investigate and remediate should understand that environmental standards change over time, usually becoming more stringent. A remediation at the commencement of the term of a lease may, therefore, look very different and cost significantly more at the end of the lease term.

Una Radoja is an Associate in Harper Grey's Commercial Litigation, Environmental Regulation & Disputes and Securities Regulation & Litigation Practice Groups. Kora Paciorek is an Associate in Harper Grey's Insurance Law Practice Group.

If you have any questions regarding this paper or about environmental liability generally, please contact Una at 604.895.2822, uradoja@harpergrey.com or Kora at 604.895.2805, kpaciorek@harpergrey.com.