

# ENVIRONMENTAL AFFAIRS IN BANKRUPTCY: 2004

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## INTRODUCTION

During the 1930s, it was said that Germany's situation was serious but not hopeless whereas Austria's situation was hopeless but not serious. The present treatment of environmental obligations in bankruptcy is serious *and* hopeless. It is not possible to treat all claims equitably *and* to give environmental claims special preference. It is not possible to give debtors a fresh start *and* make them pay for cleanups. The goals of bankruptcy conflict with the goals of environmental law, in particular, CERCLA.<sup>1</sup> For years now, courts have noted the tension<sup>2</sup> and its inevitable by-product, confusion.<sup>3</sup> Courts and commentators have called on Congress or the Supreme Court to establish which should prevail.<sup>4</sup> The silence has been deafening. Courts have had to do the best they could under difficult circumstances.

The case law mishmash is hardly surprising. Some opinions reflect the gravitational pull of bankruptcy. Others orbit around environmental concerns and enforcement of environmental laws. *All* opinions find support for their conclusions

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<sup>1</sup> CERCLA is the acronym for the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, Pub. L. No. 96-510, 94 Stat. 2767 (1980) (codified as amended at 42 U.S.C. §§ 9601–9675 (2000)) (providing regulation aimed toward protection of public health and environment).

<sup>2</sup> As one court stated:

[t]his case demonstrates the difficulty encountered when two governmental policies—one federal and one state—come into arguable conflict. On the one hand, the federally created bankruptcy policy requires that the assets of a debtor be preserved and protected, so that in time they may be equitably distributed to all creditors without unfair prejudice. On the other hand, the environmental policies of the Commonwealth of Pennsylvania requires [sic] those within its jurisdiction to preserve and protect natural resources and to rectify damage to the environment which they have caused. The potential conflict between these two policies is presented in this case, in which the Commonwealth has attempted to force a company which has petitioned in bankruptcy to correct violations of state antipollution laws, even though this action would have the effect of depleting assets which would otherwise be available to repay debts owed to general creditors.

*Penn Terra Ltd. v. Dep't of Env'tl. Res.*, 733 F.2d 267, 269 (3d Cir. 1984); *see In re Chi., Milwaukee, St. Paul & Pac. R.R. Co.*, 974 F.2d 775, 777 (7th Cir. 1992) ("The interface of bankruptcy laws and environmental laws has perplexed courts since the passage of the Comprehensive Environmental Response, Compensation and Liability Act . . ."); *In re Elsinore*, 66 B.R. 723, 735 (Bankr. D.N.J. 1986) (recognizing conflict exists between United States Bankruptcy Code and state environmental laws).

<sup>3</sup> *See Cal. Dep't of Health Servs. v. Jensen (In re Jensen)*, 995 F.2d 925, 928 (9th Cir. 1993) (stating "[c]onflict and confusion are almost inevitable."); *Chi., Milwaukee, St. Paul & Pac. R.R. Co.*, 974 F.2d at 777 (discussing conflict arising from interface of bankruptcy and environmental law); *Signature Combs, Inc. v. United States*, 253 F. Supp. 2d 1028, 1038 (W.D. Tenn. 2003) (recognizing inability to avoid conflict and confusion which arise from interplay of bankruptcy and environmental law).

<sup>4</sup> *See Debra L. Baker, Bankruptcy: The Last Environmental Loophole?*, 34 S. TEX. L. REV. 379, 404 (1993) (arguing Congress must set forth correct application and enforcement of environmental laws); Kathryn R. Heidt, *Environmental Obligations in Bankruptcy: A Fundamental Framework*, 44 FLA. L. REV. 153, 155 (1992) (saying "[e]ither the United States Supreme Court or the United States Congress must resolve definitively the issue of the proper status of environmental claims in bankruptcy proceedings."); David W. Marston, Jr., *In re Reading Co.: Cutting off Environmental Claims that Never Existed During Bankruptcy*, 43 VILL. L. REV. 637, 639 n.9 (1998) (stating "[t]he United States Supreme Court has not ruled on the precise issue of when a CERCLA claim arises for bankruptcy purposes.").

in *Ohio v. Kovacs*<sup>5</sup> and *Midlantic National Bank v. New Jersey Department of Environmental Protection*,<sup>6</sup> two Supreme Court pronouncements in the area. Lower courts have revisited and reexamined these opinions much like ancient priests studied the entrails of goats. *Kovacs* and *Midlantic* have meant different things to different courts.

This article attempts to canvass the present state of environmental affairs in bankruptcy. The picture it paints is not pretty. As one court observed:

[t]he interface of environmental cleanup laws and federal bankruptcy statutes is never tidy; jurisprudentially, it is somewhat grubby . . . [CERCLA] . . . seek[s] to protect public health and the environment by facilitating the cleanup of environmental contamination and imposing costs on the parties responsible for the pollution . . . . [Bankruptcy law was] designed to give a debtor a fresh start by discharging as many of its debts as possible. The tension between these fundamental aspects of our national policy is profound.<sup>7</sup>

We begin with a brief overview of environmental laws.

## I. ENVIRONMENTAL LAWS

### A. CERCLA

#### 1. Purpose

Most environmental-bankruptcy case law involves CERCLA.<sup>8</sup> Congress enacted CERCLA in 1980 principally to: (1) ensure immediate cleanup of contaminated sites; and (2) allocate the cleanup costs to those responsible for the problem.<sup>9</sup> The legislative history and case law suggest CERCLA was also intended

<sup>5</sup> 469 U.S. 274, 279–81 (1985) (holding obligation to clean up hazardous waste site is debt and is subject to discharge).

<sup>6</sup> 474 U.S. 494, 506–07 (1986) (holding bankruptcy court did not have power to authorize abandonment of facility where waste oil was processed without conditions to protect public health and safety).

<sup>7</sup> *CMC Heartland Partners v. Union Pac. R.R.* (*In re Chicago, Milwaukee, St. Paul & Pac. R.R. Co.*), 3 F.3d 200, 201 (7th Cir. 1993); see, e.g., *Carter Day Indus. v. EPA* (*In re Combustion Equip. Assocs.*), 838 F.2d 35, 37 (2d Cir. 1988) (recognizing conflict between CERCLA and Bankruptcy Code because goals of CERCLA are at odds with underlying premise of bankruptcy); *Jensen v. Bank of Am. N.T. & S.A.* (*In re Jensen*), 114 B.R. 700, 705 (Bankr. E.D. Cal. 1990) (discussing inherent conflict between CERCLA and Bankruptcy Code).

<sup>8</sup> This article will refer to CERCLA's internal section numbering, where section 101 corresponds to 42 U.S.C. § 9601, section 102 to 42 U.S.C. § 9602, and so forth.

<sup>9</sup> See Lewis M. Barr, *CERCLA Made Simple: An Analysis of the Cases Under the Comprehensive Environmental Response, Compensation & Liability Act of 1980*, 45 BUS. LAW. 923, 924 (1990) (indicating CERCLA allows federal government to conduct its own cleanup of toxic substances and authorizes those who incur cleanup costs to recover them within limitations of Act); see also *Aviall Servs., Inc. v. Cooper Indus.*, 312 F.3d 677, 681 (5th Cir. 2002) ("CERCLA's twin purposes are to promote prompt and effective

to: ensure proper handling of hazardous wastes; promote voluntary cleanups; encourage early reporting of hazardous spills; and deter future contamination.<sup>10</sup> Because Congress assumed it would not take long to clean up our country's environmental disasters, CERCLA had a five-year sunset date. The Superfund Amendments and Reauthorization Act of 1986 (SARA) not only reauthorized CERCLA, but fortified its provisions.<sup>11</sup>

## 2. Scope

CERCLA covers responses to releases *and* threatened releases of "hazardous substances." Hazardous wastes are a subcategory of hazardous substances.<sup>12</sup> Chemicals listed as hazardous in the Federal Water Pollution Control Act and the Solid Waste Disposal Act are included, as are 700 additional hazardous substances

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cleanup of hazardous waste sites and the sharing of financial responsibility among the parties whose actions created the hazards."); *Wickland Oil Terminals v. Asarco, Inc.*, 792 F.2d 887, 890 (9th Cir. 1986) ("Congress enacted CERCLA in 1980 to provide a comprehensive response to the problem of hazardous substance release.").

<sup>10</sup> See H.R. REP. NO. 96-1016, at 17 (1980), *reprinted in* 1980 U.S.C.C.A.N. 6119, 6128 (noting bill would establish program for appropriate environmental response to protect public health and induce persons to voluntarily take remedial measures); Heidt, *supra* note 4, at 156 ("Congress enacted CERCLA with the primary goals of (1) identifying and cleaning up toxic waste sites and (2) placing the cleanup cost on persons responsible for the contamination."); see also Barr, *supra* note 9, at 924 (citing *Chemical Waste Mgmt. v. Armstrong World Indus.*, 669 F. Supp. 1285, 1290 n.6 (E.D. Pa. 1987)).

<sup>11</sup> See Pub. L. No. 99-499, 100 Stat. 1613 (1986) (indicating act's purpose is "[t]o extend and amend the Comprehensive Environmental Response, Compensation, and Liability Act of 1980"). SARA strengthened the original enactment of CERCLA by creating more stringent cleanup standards, creating the Emergency Planning and Community Right-to-Know Act, increasing Superfund monies, and codifying judicial interpretation of the original Act. See John C. Cruden, *CERCLA Overview*, SG101 A.L.I.-A.B.A. 351, 353-54 (2002) (discussing SARA's and Superfund's more stringent standards). Congress has repeatedly reauthorized CERCLA, each time setting aside more money for cleanups. See also *EPA v. Sequa Corp. (In re Bell Petroleum Servs.)*, 3 F.3d 889, 915 (5th Cir. 1993) (noting SARA has "undoubtedly clarified and strengthened executive's CERCLA responsibilities and authority.").

<sup>12</sup> As defined in CERCLA, hazardous substances include the following:

(A) any substance designated pursuant to section 1321(b)(2)(A) of title 33, (B) any element, compound, mixture, solution, or substance designated pursuant to section 9602 of this title, (C) any hazardous waste having the characteristics identified under or listed pursuant to section 3001 of the Solid Waste Disposal Act [42 U.S.C. 6921] (but not including any waste the regulation of which under the Solid Waste Disposal Act [42 U.S.C. 6901 *et seq.*] has been suspended by Act of Congress), (D) any toxic pollutant listed under section 1317(a) of Title 33, (E) any hazardous air pollutant listed under section 112 of the Clean Air Act [42 U.S.C. 7412], and (F) any imminently hazardous chemical substance or mixture with respect to which the Administrator has taken action pursuant to section 2606 of Title 15. The term does not include petroleum, including crude oil or any fraction thereof which is not otherwise specifically listed or designated as a hazardous substance under subparagraphs (A) through (F) of this paragraph, and the term does not include natural gas, natural gas liquids, liquefied natural gas, or synthetic gas usable for fuel (or mixtures of natural gas and such synthetic gas).

42 U.S.C. § 9601(14) (2000). The petroleum exclusion is significant. Petroleum is listed as hazardous in other environmental laws, but petroleum companies are oftentimes not liable under CERCLA. See Robert T. Lee, *Comprehensive Environmental Response, Compensation, & Liability Act*, in *ENVIRONMENTAL LAW HANDBOOK* 267, 270 (Government Institutes, Inc., 12th ed. 1993).

listed by the EPA.<sup>13</sup> CERCLA also covers releases of "pollutants or contaminants,"<sup>14</sup> a broad category of substances that "will or may reasonably be anticipated to cause" harmful health effects.<sup>15</sup> The broad scope of "pollutants or contaminants" seldom impacts private parties because CERCLA only gives the EPA a cause of action for cleanup of hazardous substances.

"Release," like most terms in CERCLA, is defined broadly. It seems to include every conceivable manner in which a substance might leave its container,<sup>16</sup> with the exception of motor vehicle exhaust emissions, which are specifically excluded.

### 3. Causes of Action

#### *a. Cleanup by Third Parties & Recovery of Costs*

CERCLA provides three main remedies. First, section 104<sup>17</sup> authorizes the President, and thus the EPA, to remove or arrange for removal of hazardous substances. Under this section, the EPA may institute a removal action or a remedial action in response to a release or threatened release of hazardous substances. A removal action is a short-term action designed to protect the public health and welfare.<sup>18</sup> A remedial action is a long-term, permanent action designed to address the contamination.<sup>19</sup> The EPA may convert a removal action to a remedial

<sup>13</sup> See Designation of Hazardous Substances, 40 C.F.R. § 302.4 (2003) (listing hazardous substances); see also *Massachusetts v. Blackstone Valley Elec. Co.*, 67 F.3d 981, 984 (1st Cir. 1995) (noting hazardous substance is defined in CERCLA by incorporating lists of substances in other statutes such as Clean Water Act); *United States v. New Castle County*, 642 F. Supp. 1270, 1274 (D. Del. 1986) (indicating statute relies on cross-referencing to other environmental statutes to define its terms).

<sup>14</sup> 42 U.S.C. § 9604 (2000); see *Apache Powder Co. v. United States*, 968 F.2d 66, 68 (D.C. Cir. 1992) (noting CERCLA "directs EPA to establish criteria for determining the highest-priority sites for removal of releases or threatened releases of . . . pollutants or contaminants."); *Eagle-Picher Indus. v. EPA*, 759 F.2d 922, 925 (D.C. Cir. 1985) (stating CERCLA authorizes EPA to "respond to the release of . . . pollutants or contaminants" . . . which may present "an imminent and substantial danger to the public health or welfare.").

<sup>15</sup> 42 U.S.C. § 9601(33) (2000); see *Eagle-Picher Indus.*, 759 F.2d at 925 (indicating EPA is authorized to take remedial measures in response to release of hazardous substances); *United States v. Wallace*, 893 F. Supp. 627, 630 (N.D. Tex. 1995) (noting release of hazardous substances which posed substantial threat to public health, welfare and environment warranted remedial action under CERCLA).

<sup>16</sup> A "release" is "any spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, dumping, or disposing into the environment." 42 U.S.C. § 9601(22) (2000).

<sup>17</sup> See 42 U.S.C. § 9604(a)(1) (2000) (authorizing president to take remedial measures when hazardous substances have been released into environment); *Indus. Park Dev. Co. v. EPA*, 604 F. Supp. 1136, 1139 (E.D. Pa. 1985) (noting authority of EPA to take remedial measures is presumed under CERCLA section 104); *Pinole Point Props., Inc. v. Bethlehem Steel Corp.*, 596 F. Supp. 283, 286 (N.D. Cal. 1984) (stating "section 104 gives the President the authority to act in response to the release of hazardous substances.").

<sup>18</sup> See 42 U.S.C. § 9601(23) (2000) (defining removal actions). These cleanups are limited to a twelve month time period and a project cost of \$2 million. See *Cruden*, *supra* note 11, at 359 (discussing cleanup process). However, the time and cost constraints may be avoided if the situation fits within statutory exceptions outlined in section 104(c). 42 U.S.C. § 9604(c) (2000). "The breadth of these exceptions generally means that in situations where EPA wants to continue a removal action beyond one year or above \$2 million, it can find a basis for doing so." Lee, *supra* note 12, at 276.

<sup>19</sup> 42 U.S.C. § 9601(24) (2000). See *Juniper Dev. Group v. Kahn* (*In re Hemingway Transp., Inc.*), 993 F.2d 915, 931 n.19 (1st Cir. 1993) (discussing remedial action); *Cruden*, *supra* note 11, at 359 (analyzing three-step remedy process under CERCLA).

action when necessary.

Remedial actions require the property to be listed on the National Priorities List (NPL).<sup>20</sup> Remedial actions are funded from the Hazardous Substance Superfund, widely known as Superfund.<sup>21</sup> The Superfund allows remediation of contaminated sites even when responsible parties do not exist or when they exist but lack the requisite resources to fund the cleanup.

Before the EPA begins a cleanup, it must evaluate the site extensively and prepare a record of its proposals. It must address any public comments in that record. The record forms the basis for judicial review.

If the EPA funds the cleanup, section 107 permits it to recover the associated costs from potentially responsible parties (PRPs).<sup>22</sup> This is known as a "reimbursement" or "cost recovery" action. This right to reimbursement remedy is available to states, private parties, and the federal government.<sup>23</sup> So, if a private party or a state performs a cleanup, it has the right, under CERCLA, to seek reimbursement from responsible parties.<sup>24</sup>

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<sup>20</sup> Section 105 of CERCLA created the NPL. Based on a variety of factors, the EPA assigns a "score" to a contaminated site. See 42 U.S.C. § 9605(a)(8)(A) (2000) (determining criteria for priorities among releases or threatened releases). This allows the EPA to rank sites objectively, and, as the name implies, to establish priorities. The NPL is part of the National Contingency Plan (NCP). The EPA must update it each year. Because a listing on the NPL often means the EPA is willing to institute a remedial action, parties sometimes challenge the proceedings—usually unsuccessfully. See Lee, *supra* note 12, at 273 (explaining NPL and noting its importance as CERCLA response procedure).

<sup>21</sup> The Superfund is funded by a general corporate tax, taxes on certain chemicals and oil, and appropriations from general revenue. 42 U.S.C. § 9607 (2000). Before the federal government may commence a remedial action, it must secure an agreement from the state to pay 10% of the costs. 42 U.S.C. § 9604(c)(3) (2000) (providing choice between 10% of costs or 50% of sum expended in response to release).

<sup>22</sup> Thomas J. Salerno & Robert J. Miller, *Environmental Issues*, in CHAPTER 11 THEORY & PRACTICE: A GUIDE TO REORGANIZATION (James F. Queenan, Jr. et al. eds., LRP 1994 & Supp.) (citing 42 U.S.C. §§ 9606(a)–(b), 9607(a) (1988)); see *In re Kaiser Group Int'l, Inc.*, 289 B.R. 597, 604–05 (Bankr. D. Del. 2003) (discussing purpose of section 107 and how it applies in cases when government is potentially responsible party); *In re Eagle-Picher Indus.*, 144 B.R. 765, 769 (Bankr. S.D. Ohio 1992) (holding defendant and plaintiffs co-liaible for future cleanup costs under section 107(a)(3)).

<sup>23</sup> Section 107 states, in relevant part:

Any person who accepts or accepted any hazardous substances for transport to disposal or treatment facilities, incineration vessels or sites selected by such person, from which there is a release, or a threatened release which causes the occurrence of response costs, of a hazardous substance, shall be liable for - (A) all costs of removal or remedial action incurred by the United States Government or a State or Indian tribe not inconsistent with the national contingency plan; (B) any other necessary costs of response incurred by any other person consistent with the national contingency plan.

42 U.S.C. § 9607(a)(4)(A)–(B) (2000); see *Dico, Inc. v. Amoco Oil Co.*, 340 F.3d 525, 529 (8th Cir. 2003) (finding landowner could not bring action unless it fell within enumerated defense of section 107(b)); *Goodrich Corp. v. Middlebury*, 311 F.3d 154, 173 (2d Cir. 2002) (citing statute and resolving contribution claims).

<sup>24</sup> The only difference between the two actions is the burden of proof. Under section 107(a)(4)(A), the EPA is entitled to any costs "not inconsistent" with the NPL, whereas private parties are entitled to costs "consistent" with the NCP. In a private action, the burden is on the party seeking reimbursement to show compliance with the NCP. See 42 U.S.C. § 9607(a)(4)(A) (2000).

*b. Potentially Responsible Parties (PRPs)*

Environmental contamination is bad. Cleanups are not cheap.<sup>25</sup> The class of parties potentially liable under CERCLA is broad. Congress believed a broad net was necessary to fund cleanups and deter future contamination. PRPs include the following:<sup>26</sup>

1. any owner or operator of a vessel or a facility,<sup>27</sup>
2. any person who at the time of disposal of any hazardous substance owned or operated any facility at which such hazardous substances were disposed of,
3. any person who by contract, agreement, or otherwise arranged for disposal or treatment, or arranged with a transporter for transport for disposal or treatment, of hazardous substances owned or possessed by such person, by any other party or entity, at any facility or incineration vessel owned or operated by another party or entity and containing such hazardous substances,<sup>28</sup> and
4. any person who accepts or accepted any hazardous substances for transport to disposal or treatment facilities, incineration vessels or sites selected by such person, from which there is a release, or a threatened release which causes the occurrence of response costs, of a hazardous substance . . . .<sup>29</sup>

CERCLA defines "person" broadly. A "person" is any individual, firm, corporation, association, partnership, consortium, joint venture, commercial entity, United States government, state, municipality, commission, political subdivision of a State, or any interstate body.<sup>30</sup> According to the case law, a bankruptcy estate qualifies as a "person."<sup>31</sup>

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<sup>25</sup> Cleanups seldom cost less than \$1 million and "not infrequently" exceed \$50 million. *See Lee, supra* note 12, at 284 (noting association between increased costs and extensive groundwater contamination).

<sup>26</sup> 42 U.S.C. § 9607(a)(1)–(4) (2000); *see Dico, Inc.*, 340 F.3d 525 at 529 (quoting statute); *Buffalo Color Corp. v. AlliedSignal, Inc.*, 139 F. Supp. 2d 409, 415 (W.D.N.Y. 2001) (citing and applying statute).

<sup>27</sup> The definition of "owner or operator" excludes two categories of owners: those who "without participating in the management of a vessel or facility, hold indicia of ownership to protect [a] security interest," and any unit of local government that received control of property due to tax delinquency or bankruptcy. *See* 42 U.S.C. § 9601(20)(A) (2000).

<sup>28</sup> This category of PRPs often contains the defendants with the deepest pockets. *See Lee, supra* note 12, at 293 (noting of most major CERCLA sites many of these parties are Fortune 500 companies).

<sup>29</sup> This fourth category encompasses transporters and resellers of hazardous substances.

<sup>30</sup> *See* 42 U.S.C. § 9601(21) (2000); *see United States v. Bestfoods*, 524 U.S. 51, 56 (1998) (quoting definition in statute); *United States v. Brighton*, 153 F.3d 307, 323 (6th Cir. 1998) (stating statute broadens term "person" to include United States government, states, municipalities, and others).

<sup>31</sup> *See In re T.P. Long Chem., Inc.*, 45 B.R. 278, 284 (Bankr. N.D. Ohio 1985) (treating debtor's estate as "person" under CERCLA); *Juniper Dev. Group v. Kahn (In re Hemingway Transp., Inc.)*, 73 B.R. 494, 499 (Bankr. D. Mass. 1987), *aff'd in relevant part*, 126 B.R. 656 (Bankr. D. Mass. 1991), *aff'd*, 954 F.2d 1 (1st Cir. 1992) (deeming debtor and debtor's estate as "person" within meaning of CERCLA); *In re Stevens*, 68 B.R. 774, 779 (Bankr. D. Me. 1987) (discussing principal debtor's estate as person under CERCLA).



CERCLA distinguishes between current owners and former owners.<sup>32</sup> Current owners and operators of a vessel or facility are liable for any release of a hazardous substance. Former owners are liable only if they owned or operated a vessel or facility "at the time of disposal." The term "release" is broader than "disposal."<sup>33</sup> Courts construe "disposal" differently.<sup>34</sup> The distinction only matters when a former owner is sued for "passive migration." Assume Owner 1 introduces contaminants into the environment. They spread throughout the soil and groundwater during Owner 2's ownership *without any human intervention*. This type of spreading is commonly described as "leaching." The definition of "release" includes "leaching." The definition of "disposal" does not. Consequently, current owners are liable for leaching. Former owners are not.

Nevertheless, the lot of former owners is hardly ideal. They may be liable for other types of "passive" harm. Several of the words used to define "disposal" have both an "active" and a "passive" sense.<sup>35</sup> For example, it is often impossible to determine when a tank stopped leaking—after which time, passive environmental harm alone can occur. Courts have struggled to determine whom Congress meant to hold liable in this type of situation.

At one extreme is the Fourth Circuit, which held a landowner liable when it purchased and promptly resold property that had been contaminated by leaking underground storage tanks.<sup>36</sup> According to the court, RCRA case law established that the definition of "disposal" included passive leaking, leaking that did not involve affirmative human intervention. The court noted it could not ignore RCRA case law. Moreover, a contrary holding would frustrate CERCLA's purpose of encouraging prompt cleanup of hazardous substances. If former owners were not liable, an owner could avoid liability by selling the property. Current owners, no less "passive" than their predecessors, could not pursue them for a share of the cleanup costs.<sup>37</sup>

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<sup>32</sup> Current owners are put into a separate category from former owners. See 42 U.S.C. § 9607(a)(1) (2000) (current owners); *id.* § 9607(a)(2) (former owners) (2002).

<sup>33</sup> The definition of "release" includes the term "disposal," every word that the definition of "disposal" includes, and some additional words. Compare 42 U.S.C. § 6903(3) (2000) (defining "disposal") with 42 U.S.C. § 9601(22) (2000) (defining "release").

<sup>34</sup> Congress defined the term in RCRA: "the discharge, deposit, injection, dumping, spilling, leaking, or placing of any . . . hazardous waste . . . [such that it] may enter the environment or be emitted into the air or discharged into any waters." 42 U.S.C. § 6903(3).

<sup>35</sup> Technically, the distinction is between a transitive and intransitive sense. Consider the word "leak": "he leaked sensitive information to the press" vs. "the pipe leaked." The latter could be described as "passive" because no human conduct effected the leaking.

<sup>36</sup> See *Nurad, Inc. v. William E. Hooper & Sons, Co.*, 966 F.2d 837, 847 (4th Cir. 1992); see also *United States v. Aceto Agric. Chem. Corp.*, 872 F.2d 1373, 1381 (8th Cir. 1989) (holding responsibility under CERCLA cannot be contracted to another party); *New York v. Shore Realty Corp.*, 759 F.2d 1032, 1052 (2d Cir. 1985) (finding liability even without ownership of site at time of disposal).

<sup>37</sup> See *S.C. Dep't of Health & Envtl. Control v. Commerce & Indus. Ins.*, 372 F.3d 245, 261 (4th Cir. 2004) (discussing CERCLA declaratory judgment claim for present or retrospective harm); *Nurad*, 966 F.2d at 845–46 (recognizing owner could avoid liability by standing idle while hazard festered); *In re FCX, Inc.*, 96 B.R. 49, 55 (Bankr. E.D.N.C. 1989) (holding polluted property may be abandoned if violations do not pose immediate threat to public).

In the middle, a majority, are the Second, Third, Fifth, and Sixth Circuits. They have imposed liability only when "active" human intervention occurred.<sup>38</sup> According to those courts, Congress would have no reason to divide current owners and former owners into separate categories if *all* owners—both at the time of release and thereafter—were responsible.

The Ninth Circuit has rejected the active-passive distinction altogether.<sup>39</sup> It says the proper inquiry is to "determine whether the movement of contaminants is, under the plain meaning of the terms, a 'disposal.' Put otherwise, do any of the terms fit the hazardous contamination at issue?"<sup>40</sup> Applying its plain meaning standard, the Ninth Circuit concluded that no "disposal" had occurred when hazardous substances emerged from tar-like and slag materials that had entered the soil. "[S]preading, 'migration,' 'seeping,' 'oozing,' and possibly 'leaching'" could describe what occurred, but not "discharge, . . . injection, dumping, . . . or placing."<sup>41</sup>

Regardless of the standard, the passive migration analysis is distinct from the innocent landowner defense.<sup>42</sup> The former focuses exclusively on whether a "disposal" occurred while a former owner held title to the property. Courts that immunize former owners from passive migration do so because their construction of "disposal" requires affirmative human conduct. Courts that allow former owners to assert the innocent landowner defense (not all do) do not look at the character of the "disposal," or indeed, at the landowner's conduct at the time of disposal at all. Instead, they inquire into the landowner's conduct *prior to purchase*, i.e., whether the landowner "undertook all appropriate inquiry into the previous ownership and uses of the property."<sup>43</sup>

CERCLA imposes liability for all costs of removal or remedial action, all other response costs,<sup>44</sup> damages for the injury or destruction of natural resources, and the

<sup>38</sup> See *United States v. 150 Acres of Land*, 204 F.3d 698, 707 (6th Cir. 2000) (noting certain actions must be taken to prevent or mitigate damage to public health); *ABB Indus. Sys. v. Prime Tech.*, 120 F.3d 351, 358 (2d Cir. 1997) (discussing CERCLA's innocent owner defense); *United States v. CDMG Realty Co.*, 96 F.3d 706 (3d Cir. 1996) (defining class of people liable for response costs and contribution); *Joslyn Mfg. Co. v. Koppers Co.*, 40 F.3d 750, 761 (5th Cir. 1994) (declining to adopt Fourth Circuit rationale).

<sup>39</sup> See *W. Props. Serv. Corp. v. Shell Oil Co.*, 358 F.3d 678, 689 (9th Cir. 2004) (analyzing CERCLA claim between several potentially responsible parties); *Carson Harbor Vill., Ltd. v. Unocal Corp.*, 270 F.3d 863, 879 (9th Cir. 2001) (en banc) (promulgating new inquiry to determine liability); *Servco Pac. Inc. v. Dods*, 193 F. Supp. 2d 1183, 1197 (D. Haw. 2002) (discussing Ninth Circuit's holding in *Carson*).

<sup>40</sup> *Carson Harbor Vill., Ltd.*, 270 F.3d at 879; see *Cal. Ex Rel. Dept. of Toxic Substances Control v. Neville Chem.*, 358 F.3d 661, 663 (9th Cir. 2004) (determining which terms fit contamination at issue); Andrea Ruiz Esquide, Note, *Carson Harbor Village v. Unocal Corporation: Using Background Principles to Solve CERCLA's Ambiguities?*, *ECOLOGY L.Q.* 473, 481–85 (2003) (discussing and analyzing Ninth Circuit's *en banc* decision in *Carson* regarding disposal).

<sup>41</sup> *Carson Harbor Vill., Ltd.*, 270 F.3d at 879; see 42 U.S.C. § 6903(3) (2000) (defining disposal); *Gilroy Canning Co. v. Cal. Cannery & Growers*, 15 F. Supp. 2d 943, 946 (N.D. Cal. 1998) (stating diligent pursuit would preclude action for cleanup costs).

<sup>42</sup> See discussion *infra* Part 3(h).

<sup>43</sup> 42 U.S.C. § 9601(35) (2000). See generally *In re Diamond Reo Trucks, Inc.*, 115 B.R. 559, 565 (Bankr. W.D. Mich. 1990) (discussing liability of subsequent owners).

<sup>44</sup> Although generally the government may recover attorneys' fees because "enforcement" costs, including attorneys' fees, are a subset of "response" costs, the courts are split as to whether private parties may recover them. See Lee, *supra* note 12, at 296 (explaining some courts find private attorney fees to be unrecoverable).

costs of any necessary health effects or assessment studies.<sup>45</sup> Section 107 gives private parties who are not responsible for the contamination a right to clean up and seek reimbursement from PRPs.<sup>46</sup> This encourages private parties to perform cleanups. Responsible parties who clean up have a right of contribution against other responsible parties.<sup>47</sup> Courts allocate the cost among PRPs using a variety of equitable factors. PRPs who have settled their liability with the government can sue other PRPs who have not.

To sum up, there are five elements of a claim under section 107 for cost recovery:

- (i) the defendant is a PRP; and
- (ii) there has been a release or a threat of release,
- (iii) of a hazardous substance,
- (iv) from a vessel or facility,
- (v) which has led to the incurrence of response costs.<sup>48</sup>

### c. Cleanup by Responsible Parties

Sections 104 and 106 also authorize an EPA administrative action to compel a PRP to clean up a site.<sup>49</sup> The EPA may require the property owner or other PRP to perform the cleanup if the EPA determines the PRP will do so "properly and promptly."<sup>50</sup> Cleanup orders to PRPs are often referred to as "unilateral administrative orders."<sup>51</sup> This remedy is available only if the harm poses an

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response costs while other courts reason enforcement costs extend to private attorney fees because parties are seeking to *enforce* their right to recover in CERCLA actions).

<sup>45</sup> See 42 U.S.C. § 9607(a) (2000) (describing scope of liability and damages); see also *In re Kaiser Group Int'l, Inc.*, 289 B.R. 597, 608 (Bankr. D. Del. 2003) (holding party liable for total response costs); *In re Eagle-Picher Indus.*, 144 B.R. 765, 770 (Bankr. S.D. Ohio 1992) (discussing responsibility for remediating waste sites).

<sup>46</sup> See 42 U.S.C. § 9607; see also Barr, *supra* note 9, at 997 (discussing right of private parties to seek reimbursement); see also discussion *infra* Part 3(g).

<sup>47</sup> See 42 U.S.C. § 9613(f) (2000) (stating "[a]ny person may seek contribution from any other person who is liable or potentially liable"). Until SARA, there was no explicit right of contribution, although courts interpreted section 107 to permit contribution. Congress added section 113(f) to "clarify and confirm" the right. See discussion *infra* Part 3(g).

<sup>48</sup> See Lee, *supra* note 12, at 295; see also *United States v. Consol. Coal Co.*, 345 F.3d 409, 413 (6th Cir. 2003) (discussing elements necessary for section 107 liability); *Blasland, Bouck & Lee, Inc. v. City of N. Miami*, 283 F.3d 1286, 1302 (11th Cir. 2002) (announcing elements of CERCLA *prima facie* case for either direct recovery or contribution).

<sup>49</sup> See 42 U.S.C. §§ 9604, 9606 (2000); see also *United States v. E.I. du Pont de Nemours & Co.*, No. 1:01CV00658, 2004 WL 1943740, at \*15 (W.D.N.Y. Aug. 31, 2004) (discussing interplay between sections 104 and 106).

<sup>50</sup> See 42 U.S.C. § 9604(a)(1) (2000) (granting authority for removal and other remedial actions); see also *Hi-Mill Mfg. Co. v. Aetna Cas. & Sur. Co.*, 884 F. Supp. 1109, 1116 (E.D. Mich. 1995) (discussing EPA actions and defense costs); *United States v. Akzo Coatings of Am., Inc.*, 719 F. Supp. 571, 577 (E.D. Mich. 1989) (recognizing EPA's authority to ensure prompt cleanup of hazardous waste sites).

<sup>51</sup> See *Gen. Elec. Co. v. EPA*, 360 F.3d 188, 190 (D.C. Cir. 2004) ("EPA may issue unilateral administrative orders ("UAOs") after notice to the affected state, directing the responsible parties to clean up the hazardous sites . . ."); *United States v. BP Amoco Oil PLC*, 277 F.3d 1012, 1014–15 (8th Cir. 2002)

imminent and substantial endangerment to the public health or welfare or the environment.<sup>52</sup> The existence of a *risk* of harm satisfies the "imminent harm" requirement.<sup>53</sup> If the individual or corporation ordered to do the cleanup is skilled in the field, the order may require the responsible party itself to do the cleanup. Alternatively, the order may require the responsible party to hire a third party to do it.

CERCLA imposes hefty penalties on those who fail to comply with a cleanup order.<sup>54</sup> This remedy is only available to the federal government.

#### *d. Injunctions to Stop Future Releases*

Finally, section 106 authorizes the EPA to request an injunction to prevent a party from engaging in further releases of hazardous waste.<sup>55</sup> This form of relief, sometimes called an "abatement" action, is available when: (1) the EPA determines that a threat is presented by an "actual or threatened release of a hazardous substance from a facility;" and (2) the danger or threat poses "imminent and substantial endangerment to the public health or welfare or the environment."<sup>56</sup> Once again, only the federal government can seek injunctive relief. The United States district court with jurisdiction over the contaminated site is authorized to

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(noting issuance of two administrative orders); *Centerior Serv. Co. v. Acme Scrap Iron & Metal Corp.*, 153 F.3d 344, 347 (6th Cir.1998) (recognizing use of unilateral administrative orders).

<sup>52</sup> See 42 U.S.C. § 9606(a); see also *Supporters to Oppose Pollution, Inc. v. Heritage Group.*, 973 F.2d 1320, 1325 (7th Cir. 1992) (emphasizing substantial danger to public and environment). Cf. *Midlantic Nat'l Bank v. N.J. Dept. of Envtl. Prot.*, 474 U.S. 494, 516 (1986) (noting respondent's interest in protecting public health).

<sup>53</sup> See Barr, *supra* note 9, at 933 (noting government need only prove endangerment may exist); see also *In re Rancourt*, 207 B.R. 338, 344 (Bankr. D.N.H. 1997) (recognizing actual or threatened release of hazardous substances posed imminent and substantial endangerment to public health or welfare or environment); *In re MCI, Inc.*, 151 B.R. 103, 108 (Bankr. E.D. Mich. 1992) (discussing burden of proving there is no imminent danger to public).

<sup>54</sup> See 42 U.S.C. § 9606 (announcing amount of fines permissible for failing to comply with order); see also *Kelley v. EPA*, 15 F.3d 1100, 1103 (D.C. Cir. 1994) (noting EPA's ability to assess civil penalties for noncompliance with certain CERCLA provisions); Barr, *supra* note 9, at 934 (discussing penalty scheme and available penalty enhancements).

<sup>55</sup> See 42 U.S.C. § 9606(a) (giving President power to take action if environmental threat arises); see also *Colorado v. Idarado Mining Co.*, 916 F.2d 1486, 1493 (10th Cir. 1990) (explaining section 106 limits availability of injunctive relief to federal plaintiffs, including EPA); *Velsicol Chem. Corp. v. Reilly Tar & Chem. Corp.*, No. CIV-1-81-38921, 1984 U.S. Dist. LEXIS 24317, at \*6-\*7 (E.D. Tenn. August 16, 1984) (claiming injunctive relief may only be brought by Attorney General at request of President, who is advised by EPA).

<sup>56</sup> 42 U.S.C. § 9606(a); see *United States v. Conservation Chem. Corp.*, 619 F. Supp. 162, 191-94 (W.D. Mo. 1985) (stating section 106(a) authorizes United States to seek mandatory injunction against responsible parties when President determines there may be imminent and substantial endangerment to public health, welfare, or environment because of actual or threatened release of hazardous substance); Barr, *supra* note 9, at 932-33 (explaining government must establish elements set forth in section 9606(a) and show hazardous substance may pose imminent threat and substantial endangerment to public health, welfare, or environment).

grant such relief.<sup>57</sup>

*e. Types of Liability*

PRPs are strictly liable under CERCLA.<sup>58</sup> For example, even if the contamination occurred before an owner acquired the property, the owner is still strictly liable.<sup>59</sup> PRPs do not necessarily have to have known a site is contaminated.<sup>60</sup> Congress determined that strict liability was appropriate under CERCLA because activities related to the manufacture, transportation, usage, and disposal of hazardous substances are abnormally dangerous or ultrahazardous.<sup>61</sup> Although the Act is silent, courts have made liability under CERCLA joint and several.<sup>62</sup> Joint and several liability relieves courts of the arduous, if not impossible, task of apportioning fault. Strict liability, acting in tandem with joint and several liability, obviates the need to identify each and every PRP and its contribution before requiring one PRP to clean up.<sup>63</sup>

<sup>57</sup> See 42 U.S.C. § 9606(a); Barr, *supra* note 9, at 933 ("[T]he district court of the United States in the district in which the threat occurs shall have jurisdiction to grant such relief . . ."); see also *Conservation Chem. Corp.*, 661 F. Supp. at 1427 (stating CERCLA requires full trial when mandatory injunctive relief is sought).

<sup>58</sup> See *New York v. Shore Realty Corp.*, 759 F.2d 1032, 1042 (2d Cir. 1985):

Congress intended that responsible parties be held strictly liable, even though an explicit provision for strict liability was not included in the compromise. Section 9601(32) provides that "liability" under CERCLA "shall be construed to be the standard of liability" under section 311 of the Clean Water Act, 33 U.S.C. § 1321, which courts have held to be strict liability . . . .

*Id.*; see also *Juniper Dev. Group v. Kahn (In re Hemingway Transp., Inc.)*, 993 F.2d 915, 921 (1st Cir. 1993) (stating all PRPs are strictly liable); *United States v. Kayser-Roth Corp.*, 910 F.2d 24, 26 (1st Cir. 1990) ("liability for cost incurred is strict . . .").

<sup>59</sup> See *Shore Realty Corp.*, 759 F.2d at 1044–45 (stating reason for strict liability is to impose liability in situations where person who contaminated land cannot be located); see also *New York v. Westwood-Squibb Pharm. Co.*, 138 F. Supp. 2d 372, 380 (W.D.N.Y. 2000) (stating owner's liability extends to disposals occurring during and before ownership of property); *In re Chi., Milwaukee, St. Paul, & Pac. R.R. Co.*, 130 B.R. 521, 523 (N.D. Ill. 1991) ("The Supreme Court has recognized that anyone in possession of a hazardous waste site is liable for remedying the situation.").

<sup>60</sup> See *SALERNO & MILLER*, *supra* note 22, at 26:7 (explaining defendant does not have to have knowledge or intent to be held liable); see also *O'Neil v. Picillo*, 682 F. Supp. 706, 719 (D.R.I. 1988) (stating if plaintiff can prove the statutory elements of section 107(a)(3), then defendant may be held liable whether she had knowledge or not); *In re Chi., Milwaukee, St. Paul, & Pac. R.R. Co.*, 130 B.R. at 523 (finding current owner of facility subject to strict liability standard).

<sup>61</sup> See 126 CONG. REC. H31, 964–65 (1980) (statement of Rep. Florio); 126 CONG. REC. H31, 978 (1980) (statement of Rep. Jeffords); 126 CONG. REC. S30, 932 (1980) (statement of Sen. Randolph); see also Barr, *supra* note 9, at 976 (affirming legislative history shows strict liability is imposed because manufacture, transportation, usage, or disposal of hazardous substances is an "abnormally dangerous" or "ultrahazardous" activity).

<sup>62</sup> Congress purposely did not impose joint and several liability on CERCLA defendants in the 1980 version of the Act. Congress left the nature of the liability to the courts to decide. See Barr, *supra* note 9, at 977–78 (stating courts have noted Congress struck proposal to impose joint and several liability in all CERCLA cases).

<sup>63</sup> See, e.g., *United States v. Dickerson*, 640 F. Supp. 448, 450 (D. Md. 1986) ("The courts have consistently rejected attempts by CERCLA defendants to compel the government to round up every other available defendant, noting that defendants can protect themselves through the impleader provision of Rule 14."); see also *Kelley v. Thomas Solvent Co.*, 714 F. Supp. 1439, 1450 (W.D. Mich. 1989) (citing

*f. Corporate Liability*

Under section 107(a)(3), "any person" who "owned or possessed" a hazardous substance and arranged for its disposal or transportation for disposal may be held directly liable. According to the case law, "person" includes corporate officers and parent corporations.<sup>64</sup> After all, Congress could have limited the definition of "person" just like it limited the definition of "owner or operator" in section 101(20)(A).<sup>65</sup> It chose not to. Therefore, corporate officers and parent corporations may be held liable as "arrangers."

Moreover, under section 107(a)(1) and (2), parent corporations may be held directly liable as "operators."<sup>66</sup> Some courts have focused on whether the parent corporation exercised "substantial control" over the PRP corporation's overall business activities—not merely on its control over the liability-creating hazardous substance activities.<sup>67</sup> The parent's conduct did not always approach the level required under a veil-piercing analysis (usually formulated as "domination" or "mere instrumentality"). Parent corporations actively involved in running the subsidiary, perhaps without actually making its environmental decisions, have been held liable.<sup>68</sup>

*Dickerson*); Barr, *supra* note 9, at 978–79 (noting CERCLA plaintiffs can chose among jointly liable parties and are not required to bring in all available defendants).

<sup>64</sup> 42 U.S.C. § 9601(21) (2000); *United States v. Northeastern Pharm. & Chem. Co.*, 810 F.2d 726, 743 (8th Cir. 1986) (explaining "person" under section 107(a)(3) includes both individuals and corporations, including corporation's officers and employees); *United States v. Ward*, 618 F. Supp. 884, 894 (E.D.N.C. 1985) (stating both corporations and individuals fall under statute's definition of "person.").

<sup>65</sup> See *Northeastern Pharm. & Chem. Co.*, 810 F.2d at 743 (applying "owner or operator" definition); see also *Ward*, 618 F. Supp. at 884 (holding corporate officer liable as arranger); *accord* *Gen. Elec. Co. v. Aamco Transmissions, Inc.*, 962 F.2d 281, 286 (2d Cir. 1992) (stating corporate defendants may be held liable as arrangers).

<sup>66</sup> 42 U.S.C. § 9607(a)(1)–(2) (2000); see, e.g., *FMC Corp. v. U.S. Dep't of Commerce*, 29 F.3d 833, 843 (3d Cir. 1994) (noting some courts have found corporations liable as operators); *Lansford-Coaldale Joint Water Auth. v. Tonolli Corp.*, 4 F.3d 1209, 1220 (3d Cir. 1993) (finding some parent corporations liable as operators). But see *United States v. Bestfoods*, 524 U.S. 51, 58–59 (1998) (stating parent corporations are only liable under section 107(a)(2) as operators if they exert power or influence over their subsidiary by actively participating in and exercising control over the subsidiary's business); *Joslyn Corp. v. T.L. James & Co.*, 696 F. Supp. 222, 233 (W.D. La. 1988) (finding corporation not liable as operator when it did not engage in daily operations of disposal of hazardous waste).

<sup>67</sup> See *FMC Corp.*, 29 F.3d at 843 (stating factors to determine operator status include whether person or entity controlled finances of facility, managed employees of facility, and managed daily business operations of facility); see also *Lansford-Coaldale Joint Water Auth.*, 4 F.3d at 1220 (holding corporation must have substantial control over facility in question to be liable as operator); *Joslyn Corp.*, 696 F. Supp. at 233 (holding corporation liable under owner and operator status).

<sup>68</sup> See *Lansford-Coaldale Joint Water Auth.*, 4 F.3d at 1220 (declaring some corporations liable under operator status strictly on basis of control over facility); *Ward*, 618 F. Supp. at 894 (implying mere capacity to control the facility is enough to find liability under operator status); *United States v. Mottolo*, 605 F. Supp. 898, 913 (D.N.H. 1985) (denying defendant corporation's motion for summary judgment because corporation may have been operator under statute). Circuits were split over whether the *authority* to control, as opposed to *actual* control, was sufficient. Compare *Kaiser Aluminum & Chem. Corp. v. Catellus Dev. Corp.*, 976 F.2d 1338 (9th Cir. 1992) and *Nurad, Inc. v. Hooper & Sons Co.*, 966 F.2d 837 (4th Cir. 1992), *cert. denied*, 506 U.S. 940 (1992) (both adopting authority to control standard), with *Jacksonville Elec. Auth.*

A recent Supreme Court opinion, *United States v. Bestfoods*,<sup>69</sup> casts doubt on these decisions. The Court clarified the differences between direct and derivative liability. It reasoned that CERCLA did not abrogate the common law rule proscribing the use of the corporate form to perpetrate a fraud or injustice.<sup>70</sup> It then held that a parent corporation can be held *derivatively* liable under subsections 107(a)(1) and (2) *only if* the corporate veil could be pierced.<sup>71</sup> Finally, it emphasized that a parent could be held directly liable as an "operator."

The Court purported to abrogate cases holding parent corporations "directly" liable—via a broad construction of "operator"—on facts that would be insufficient to pierce the veil.<sup>72</sup> The Court did not mention the "control" test at all, even though it was the way courts would apparently get around the veil-piercing rules. In reaffirming direct "operator" liability for parent corporations, it provided no new standard, thus inviting courts to use a modified "control" test (perhaps confining their inquiry to control over hazardous substance activities). In the bankruptcy context, the *Bestfoods* decision has important implications for successor liability. Every circuit court to decide the issue has concluded that Congress intended to impose liability on successor corporations, even though it gave no explicit statutory authorization.<sup>73</sup> CERCLA is designed to promote speedy cleanups. Imposing the

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v. Bernuth Corp., 996 F.2d 1107 (11th Cir. 1993) and *United States v. Kayser-Roth Corp.*, 910 F.2d 24 (1st Cir. 1990), *cert. denied*, 498 U.S. 1084 (1991) (adopting actual control standard).

<sup>69</sup> 542 U.S. 51 (1998).

<sup>70</sup> *Id.* at 61 (declaring CERCLA did not abrogate corporate liability law); *cf.* *Burnet v. Clark*, 287 U.S. 410, 415 (1932) (explaining generally a corporation and its stockholders are two separate entities); *Coxe v. Handy*, 24 F. Supp. 178, 180 (D. Del. 1938) (stating as general rule corporations are separate entities from their stockholders).

<sup>71</sup> *See Bestfoods*, 524 U.S. at 63–64 ("The Court of Appeals was accordingly correct in holding that when (but and only when) the corporate veil may be pierced, may a parent corporation be charged with derivative CERCLA liability for its subsidiary's actions."); *see also* *Am. Cyanamid Co. v. Capuano*, 381 F.3d 6, 22–23 (1st Cir. 2004) (citing *Bestfoods*); *United States v. Kayser-Roth Corp.*, 103 F. Supp. 2d 74, 77 (1st Cir. 2000) (recognizing change in corporations' liability as owners and operators recognized by Supreme Court).

<sup>72</sup> *See, e.g., Lansford-Coaldale Joint Water Auth.*, 4 F.3d at 1220 (3d Cir. 1993) (holding parent corporation liable based on some control over subsidiaries); *Ward*, 618 F. Supp. at 894 (implying some corporations may be liable based simply on their capacity to control subsidiaries); *Mottolo*, 605 F. Supp. at 913 (stating defendant was possibly liable as operator even if corporate veil could not be pierced).

<sup>73</sup> *See N. Shore Gas Co. v. Salomon Inc.*, 152 F.3d 642, 649 (7th Cir. 1998) (reasoning, based on judicial rule of construction, Congress "intended to include all known forms of business and commercial enterprises" by using "person" in CERCLA); *B.F. Goodrich v. Betkoski*, 99 F.3d 505, 518–19 (2d Cir. 1996) (declining to read section 9607(a) in manner "subverting the Act's purpose of holding responsible parties liable for cleanup costs" and instead, reading CERCLA "to advance its primary goals."); *John S. Boyd Co. v. Boston Gas Co.*, 992 F.2d 401, 405 (1st Cir. 1993) (concluding "liabilities traveled to the successor"); *United States v. Carolina Transformer Co.*, 978 F.2d 832, 837 (4th Cir. 1992) (holding successor liability is permitted under CERCLA); *United States v. Mex. Feed & Seed Co.*, 980 F.2d 478, 486–87 (4th Cir. 1992) ("It would serve little purpose to include corporations responsible for hazardous waste sites, but not their corporate successors, within the class of 'covered persons.'"); *Anspec Co. v. Johnson Controls, Inc.*, 922 F.2d 1240, 1245 (6th Cir. 1991) ("Congress intended successor corporations within the description of entities that are potentially liable under CERCLA for cleanup costs."); *La.-Pac. Corp. v. Asarco, Inc.*, 909 F.2d 1260, 1262 (9th Cir. 1990) (holding Congress did intend successor liability in CERCLA and extending *Smith Land* to asset purchase); *Smith Land & Improvement Corp. v. Celotex Corp.*, 851 F.2d 86, 92 (3d Cir. 1988) ("Congressional intent supports the conclusion that, when choosing between the taxpayers or a successor corporation, the successor should bear the cost.").

cost of the cleanup on the purchasing entity—which benefited from the selling entity's environmental abuses through a lower price in an asset sale, merger or other business combination—is not unfair.<sup>74</sup> Bankruptcy courts have long struggled to apply CERCLA's successor liability principles in the context of asset sales and reorganizations.<sup>75</sup>

In *New York v. National Services Industries, Inc.*,<sup>76</sup> the Second Circuit reexamined the proper standard for successor liability after *Bestfoods*. Prior courts had adopted a "substantial continuity" test because it was more consistent with CERCLA's purposes than the common law approach.<sup>77</sup> However, the court understood *Bestfoods* to mean that the courts "must apply common law rules and not create CERCLA-specific ones."<sup>78</sup> Accordingly, the court remanded to determine whether a corporation's purchase of customer lists, contracts, inventory, and

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<sup>74</sup> See *N. Shore Gas Co.*, 152 F.3d at 650 ("Holding the successor corporation liable for the cost of cleanup is not necessarily unfair, since the successor and its shareholders likely will have derived some benefit from the predecessor's use of the pollutant and savings that resulted from the hazardous methods."); *Smith Land & Improvement Co.*, 851 F.2d at 92 ("Benefits from the use of the pollutant as well as savings resulting from the failure to use non-hazardous disposal methods inured to the original corporations, its successors, and their respective stockholders . . ."). See generally Ronald H. Rosenberg, *The Ultimate Independence of the Federal Courts: Defying the Supreme Court in the Exercise of Federal Common Law Powers*, 36 CONN. L. REV. 425, 463–64 (2004) (discussing potential for corporations to manipulate general rule of asset purchaser non-liability and common law exceptions necessary to avoid abuse).

<sup>75</sup> See, e.g., *Andritz Sprout-Bauer, Inc. v. Beaser E., Inc.*, 12 F. Supp. 2d 391, 405–06 (M.D. Pa. 1998) (applying successor liability based on "continuity enterprise" theory in CERCLA action against manufacturer that previously contaminated site); *New York v. Panex Indus., Inc.*, No. 94-CV-0400E, 1996 WL 378172, at \*7 (W.D.N.Y. June 24, 1996) (analyzing whether "asset purchase" resulted in *de facto* merger or "substantial continuation" when successor acquired company after seller reorganized); *Ninth Ave. Remedial Group v. Allis-Chalmers Corp.*, 195 B.R. 716, 729 (N.D. Ind. 1996) (concluding bankruptcy court order approving sale of debtor's assets to defendant "free and clear" of all claims did not preclude successor liability); *New York v. N. Storonske Cooperage Co.*, 174 B.R. 366, 382, 386, 389 (N.D.N.Y. 1994) (determining asset purchase resulted in *de facto* merger as well as a "continuing enterprise" or "substantial continuity" between buyer and seller, and chapter 7 debtor was deemed liable as successor).

<sup>76</sup> 352 F.3d 682, 684–85, 687 (2d Cir. 2003) (refusing to find substantial continuity doctrine is part of general federal common law and finding after *Bestfoods*, it should have no bearing in determination whether corporation assumes CERCLA liability based on asset purchase); see *New York v. Westwood-Squibb Pharm. Co., Inc.*, 90-CV-1324C, 2004 U.S. Dist. LEXIS 13841, at \*59 (W.D.N.Y. May 25, 2004) (citing *National Services Industries*, 352 F.3d at 687, and concluding substantial continuity test is "no longer good law"); *CERCLA: 'Substantial Continuity' Test Can't Be Used For Successor Liability Under CERCLA*, ANDREWS ENVTL. LITIG. REP. (Jan. 16, 2004) (discussing holding in *National Services Industries*).

<sup>77</sup> *Nat'l Servs. Indus.*, 352 F.3d at 685 (discussing court's application of substantial continuity test articulated in *Betkoski*, rather than federal common law rule, was more consistent with CERCLA's goals); see *Betkoski*, 99 F.3d at 519 ("CERCLA is entitled to a construction that advances its primary goals. Because the substantial continuity test is more consistent with the Act's goals, it is superior to the older and more inflexible 'identity rule.'"); *Mex. Feed & Seed Co.*, 980 F.2d at 487–89 (justifying imposition of CERCLA liability under substantial continuation test).

<sup>78</sup> *Nat'l Servs. Indus.*, 352 F.3d at 685; see *Schiavone v. Pearce*, 79 F.3d 248, 255 (2d Cir. 1996) (stating this school refuses to "depart[] from the longstanding principles of corporate law," though rejecting view); *Westwood-Squibb Pharm. Co.*, 2004 U.S. Dist. LEXIS 13841, at \*59 (quoting *Bestfoods*: "[i]n order to abrogate a common-law principle, the statute must speak directly to the question addressed by the common law.").



trademarks fit into one of the traditional successor liability exceptions.<sup>79</sup>

If other courts follow the same restrictive approach, purchasing entities (and arguably reorganized debtors) may be able to avoid more easily the environmental liabilities of their predecessors. Moreover, after *Bestfoods*, the question remains open whether general federal common law (as applied in labor and securities cases) or state common law governs.<sup>80</sup>

### *g. Contribution Actions*

So far, we have addressed three different scenarios for cleanup and cost recovery. In one scenario, a non-responsible party, such as a neighbor, a local government, or the EPA, cleans up a site. In that case, the non-responsible party would bring a reimbursement action under section 107 against one, several or all PRPs. Any PRP is liable to a non-responsible party for 100% of the cleanup cost. The non-responsible party need not, and probably would not, join all PRPs in its reimbursement action. Congress wanted to ensure prompt reimbursement of non-responsible parties. The plaintiff-non-responsible party only needs to sue the most obvious or most convenient PRP, probably the current owner in many cases.

Suppose the non-responsible party sues the current owner (and only the current owner). It obtains a \$2 million judgment. It would be unfair for the current owner to foot the entire bill, especially if it did not create the mess or was one of several parties responsible for it. The current owner, now judged liable, can bring a contribution action under section 113(f) against any other PRPs to recover some or all of the \$2 million. Section 113 gives courts broad discretion to allocate the costs fairly and equitably among PRPs joined in a contribution action.<sup>81</sup>

In a second scenario, the EPA goes to federal court to obtain an injunction under section 106 ordering the current owner-PRP to stop harming a site. In a third scenario, the EPA issues an administrative order under sections 104 and 106,

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<sup>79</sup> *Natl Servs. Indus.*, 352 F.3d at 687. These exceptions were typical of successor liability rules, which hold the purchasing entity liable if: (1) the transaction was a de facto merger, (2) the purchaser impliedly accepted the liabilities, or (3) the purchasing entity was a "mere continuation" of the selling entity. The "mere continuation" exception generally requires an identity of stock, stockholders, and directors. New York unsuccessfully argued that the "substantial continuation" exception was a specialized application of the "mere continuation" exception. *Id.* at 685-86.

<sup>80</sup> See *United States v. Bestfoods*, 524 U.S. 51, 63 n.9 (1998) ("There is significant disagreement among courts and commentators over whether, in enforcing CERCLA's indirect liability, courts should borrow state law, or instead apply a federal common law of veil piercing."); *N. Shore Gas Co. v. Salomon, Inc.*, 152 F.3d 642, 650 (noting most circuits holding successor liability is available under CERCLA have "concluded that the parameters of the doctrine should be fashioned by federal common law."); *Mex. Feed & Seed Co.*, 980 F.2d at 487 n.9 (stating "considering the national application of CERCLA and fairness to similarly situated parties, the district court was probably correct in applying federal law.").

<sup>81</sup> 42 U.S.C. § 9613(f)(1) (2000) ("In resolving contribution claims, the court may allocate response costs among liable parties using such equitable factors as the court determines are appropriate."); see also *Bancamerica Commercial Corp. v. Mosher Steel of Kan., Inc.*, 100 F.3d 792, 802-03 (10th Cir. 1996) (upholding district court's holding relying on grant of broad discretion in section 9613(f)(1)); *Westwood-Squibb Pharm. Co.*, 2004 U.S. Dist. LEXIS 13841 at \*64 (interpreting section 9613(f)(1) to afford court "broad discretion to balance the equities in the interests of justice.").

ordering the current owner to clean up a site. Here, too, the PRP would cast around for other PRPs against whom it could bring a contribution action under section 113(f).<sup>82</sup>

In all three situations, the law is settled. Any PRP who involuntarily incurs more than its "fair share" of cleanup costs—whether by paying a money judgment or by complying with an injunction or EPA administrative action—can recover the difference under section 113(f).

What about the PRP who *voluntarily* remediates a site? Here, the result is not so clear.

Suppose the current owner of a warehousing site knows that the prior owners dumped hazardous chemicals into the soil. The current owner has not contributed to any deterioration. The chemicals now pose a problem because the owner wishes to convert the warehouses into something else. Moreover, it plans to sell a parcel of the property. A sale will be difficult because any future owner will become a PRP and hence, liable for part of the cleanup, if it ever occurs. Few buyers want to assume that liability.

Because a "release" has occurred, the EPA could order the current owner to clean up the site, but the EPA has not yet exercised that power. The local authorities are likewise unwilling or unable to expend funds to clean up, even though they could recover the cost from the current owner. Can the current owner clean up the site and sue the former owners who actually created the mess? Or must the current owner sit around and wait for an EPA administrative action or a clean up by a non-PRP who then sues the current owner? Given the cost of some cleanups, knowing in advance when and from whom the money will come makes a difference. Moreover, if the current owner cannot voluntarily undertake a clean up with recourse against other PRPs, the property is not put to its most efficient use, and neighbors and the public must tolerate the mess.

In 1980, the PRP who voluntarily cleaned up had to rely on section 107(a)'s right of reimbursement (cost recovery) remedy. Courts interpreted this provision to permit a PRP who incurred cleanup costs in excess of its equitable share to sue other PRPs to recoup some or all of the costs. This interpretation effectively transformed a right of reimbursement into a right of contribution. It made one joint and several tortfeasor liable to another.

In the seminal case, *City of Philadelphia v. Stepan Chemical Co.*,<sup>83</sup> a number of chemical companies had dumped hazardous materials into a city-owned landfill in contravention of state law. The illicit dumping had contaminated the groundwater, adjacent soil, and the Delaware River. The EPA had placed the site on the NPL, but had not yet ordered the city to clean up the site. Rather than wait for the EPA or the state agency to clean up the mess, the city implemented a comprehensive cleanup program at a cost of \$30 million, which it sought to recover from the defendant chemical companies. It relied on section 107(a)(4)(B) to establish that it could

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<sup>82</sup> Unless, of course, the PRP compelled to clean up the site believes it is solely responsible for the mess.

<sup>83</sup> 544 F. Supp. 1135, 1139 (E.D. Pa. 1982).

recover response costs notwithstanding its own liability as a current owner of the landfill.<sup>84</sup>

According to section 107, PRPs shall be liable for: "(A) all costs of removal or remedial action incurred by the United States Government or a State or an Indian tribe . . . ; (B) any other necessary costs of response incurred by any other person."<sup>85</sup> The city argued that "any other person" meant anyone other than the government entities listed in subsection (A). In other words, subsection (B)'s reference to "other person" did not exclude the PRPs listed in subsections (1) through (4).

The court agreed. It reasoned that giving PRPs the same right as non-culpable parties to sue other PRPs was not inconsistent with CERCLA's language, legislative history, or purpose, particularly because the city had not voluntarily permitted the illegal dumping for which it was potentially responsible.<sup>86</sup> Although the *Stepan Chemical* court seemed swayed in part by the equities of the case, courts in the four years preceding the enactment of section 113(f) followed its lead.<sup>87</sup>

Congress enacted section 113(f) as part of SARA. SARA's legislative history states that Congress intended section 113(f) to "clarify and confirm" the right of contribution, to "encourage quicker, more equitable settlements, decrease litigation and thus facilitate cleanups."<sup>88</sup> Unfortunately, the text of section 113(f) does not live up to its legislative history. As one court put it, section 113(f)'s "syntax is confused, its grammar inexact, and its relationship to other CERCLA provisions

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<sup>84</sup> *Id.* at 1141; see *Wichita v. Aero Holdings, Inc.*, 177 F. Supp. 2d 1153 (D. Kan. 2000) (deciding action pursuant to section 107(a)(4)(B) to recover response costs incurred cleaning up groundwater contamination); *Raytheon Co. v. McGraw-Edison Co.*, 979 F. Supp. 858, 864 n.7 (E.D. Wis. 1997) (rejecting defendant's argument that plaintiff's actions, particularly cleaning up site, should bar it from section 107(a) action).

<sup>85</sup> 42 U.S.C. § 9607(a)(4)(A)–(B) (2000) (emphasis added); see *United States v. Davis*, 261 F.3d 1, 15–16 (1st Cir. 2001) (discussing action for past and future response costs under section 107(a)); *Kalamazoo River Study Group v. Menasha Corp.*, 228 F.3d 648, 652–53 (6th Cir. 2000) (involving action seeking response costs from PRPs under section 107(a)).

<sup>86</sup> *Stepan Chem. Co.*, 544 F. Supp. at 1142–43; see *Artesian Water Co. v. Gov't of New Castle County*, 605 F. Supp. 1348, 1356 (D. Del. 1985) (citing *Stepan Chemical* and holding private parties may sue under section 107(a) of CERCLA); *Bulk Distrib. Ctrs., Inc. v. Monsanto Co.*, 589 F. Supp. 1437, 1443 (S.D. Fla. 1984) (relying on *Stepan Chemical* in its analysis of whether section 107(a)(4)(B) "empower[s] a private party to seek compensation from other responsible parties for costs incurred cleaning up a spill site").

<sup>87</sup> See, e.g., *Wickland Oil Terminals v. Asarco, Inc.*, 792 F.2d 887, 891 (9th Cir. 1986) (stating former owner may be liable under section 107 to current owner who cleaned up site, reversing district court's holding that other necessary costs of response must be incurred pursuant to governmental order); *Artesian Water Co.*, 605 F. Supp. at 1356 (relying on *Stepan Chemical*, and permitting water utility to sue county whose landfill contaminants polluted groundwater, even though the EPA and state government had not compelled cleanup); *Pinole Point Props., Inc. v. Bethlehem Steel Corp.*, 596 F. Supp. 283, 291 (N.D. Cal. 1984) (relying on *Stepan Chemical*, and holding plaintiff, current owner of pond purchased from defendant, could sue for response costs because section 107 creates "separate and independent cause of action" not requiring governmental action).

<sup>88</sup> H.R. REP. NO. 99-253, at 79, 59, reprinted in 1986 U.S.C.C.A.N. 2835, 2861, 2841 (citing *United States v. Ward*, 8 Chem. & Rad. Waste Litig. Rep. 484 (D.N.C. May 14, 1984), and *United States v. S.C. Recycling & Disposal, Inc.*, 7 Chem. & Rad. Waste Litig. Rep. 674 (D.S.C. Feb. 23, 1984)). Congress emphasized that parties "may be more willing to assume the financial responsibility" for a cleanup "if they are assured they can seek contribution from others." *Id.* at 80, reprinted in 1986 U.S.C.C.A.N. 2835, 2862.

ambiguous."<sup>89</sup>

Section 113(f) provides:

Any person may seek contribution from any other person who is liable or potentially liable under section 107(a), during or following any civil action under section 106 or under section 107(a) . . . . Nothing in this subsection shall diminish the right of any person to bring an action for contribution in the absence of a civil action under section 106 or section 107.

Section 113(f)'s first sentence recognizes a right of contribution among PRPs during or following any civil action for an abatement injunction (section 106) or reimbursement of cleanup costs (section 107). It says nothing about a PRP cleanup that takes place before any civil action, i.e., it says nothing about a PRP's voluntary cleanup. Section 113(f)'s last sentence (the "savings clause") suggests a PRP's right to contribution is not limited to lawsuits the PRP brings during or following civil actions brought against it under section 106 or 107.

A recent case highlights section 113(f)'s interpretive difficulty. In *Aviall Services, Inc. v. Cooper Industries, Inc.*,<sup>90</sup> the plaintiff-current owner voluntarily, i.e., not under section 106 compulsion, cleaned up property it had purchased from the defendant. A panel of the Fifth Circuit denied the current owner contribution from the former owner who had caused the mess. The court reasoned that the first sentence of section 113(f) was an enabling clause. It created a cause of action where "[a]ny person may seek contribution from any other person . . . ." In an enabling clause, "may" denotes "shall" or "must." In its view, Congress granted the exclusive federal remedy in the first sentence, and included the last sentence only to preserve state law contribution rights.<sup>91</sup> To conclude otherwise would violate the canon of construction which holds that the specific governs the general. The court acknowledged the result was inconsistent with CERCLA's general policy goals, but noted that policy arguments cannot supersede a statute's plain language.<sup>92</sup>

The Fifth Circuit, *en banc*, reversed. It permitted the plaintiff's contribution action, reasoning that it would have been "arbitrary" for Congress to change the

<sup>89</sup> *Aviall Servs., Inc. v. Cooper Indus., Inc.*, 312 F.3d 677, 680 (5th Cir. 2002) (*en banc*), *cert. granted*, 124 S. Ct. 981 (2004). See generally William D. Araza, *Text, Purpose and Facts: The Relationship Between CERCLA Sections 107 and 113*, 72 NOTRE DAME L. REV. 193, 224-26 (1996) (discussing limited usefulness of SARA's legislative history and interpretive difficulties).

<sup>90</sup> 263 F.3d 134 (5th Cir. 2001), *rev'd en banc*, 312 F.3d 677 (5th Cir. 2002), *cert. granted*, 124 S. Ct. 981 (2004); see Derek J. Lisk, *Passing the Hat For CERCLA Cleanup Costs, If You Clean Up, Will Others Chip In?*, 12 METROPOLITAN CORPORATE COUNSEL 1, 1-4 (Metropolitan Corporate Counsel, Inc. 2004) (comparing Fifth Circuit's holding in *Aviall Services* with District Court of New Jersey and Ninth Circuit decisions).

<sup>91</sup> This argument is not without merit because some courts have interpreted CERCLA to preempt state law remedies. See *Bedford Affiliates v. Sills*, 156 F.3d 416, 427 (2d Cir. 1998) ("CERCLA preempts the state law remedies of restitution and indemnification.").

<sup>92</sup> *Aviall Servs.*, 263 F.3d at 139-40 (holding CERCLA requires party seeking contribution to be, or have been, defendant in section 106 or section 107 proceeding); see *Rockwell Int'l Corp. v. IU Int'l Corp.*, 702 F. Supp. 1384, 1389 (N.D. Ill. 1988) (stating purpose of section 113(f) was to provide liable parties an avenue for obtaining compensation from other responsible parties); S. REP. NO. 96-848, at 12-13 (1980) (stating primary goal of CERCLA is to create a superfund for immediate cleanup and hold polluters responsible).

standard of contribution existing in 1986 if it meant to "clarify" or "confirm" anything. It also concluded that the plain language of section 113(f)'s first sentence does *not* include any word clearly expressing an intent to create an exclusive federal remedy. The panel decision had effectively read the statute as "[a]ny person may *only* seek contribution . . . during or following any civil action under section 106 or section 107." This reading of the first sentence eviscerated the last sentence and conflicted with CERCLA's clear policy goals. Finally, it would be odd for Congress to rely on state law contribution remedies to mitigate the effect of the first sentence—which, if the exclusive remedy, would give PRPs the perverse incentive *not* to clean up.<sup>93</sup>

Under the *en banc* court's reasoning, *Stepan Chemical* would come out the same way today. The last sentence of section 113(f) incorporated its holding that section 107(a)(4)(B) creates an implied right of contribution among PRPs.

Most courts would permit a PRP's contribution action in the absence of a pending or adjudged section 106 or 107 action against it.<sup>94</sup> But courts in the Third and Seventh Circuits have taken a narrower view of section 113(f)'s last sentence.<sup>95</sup>

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<sup>93</sup> *Aviall Servs., Inc. v. Cooper Indus., Inc.*, 312 F.3d 677, 685–90 (5th Cir. 2002) (*en banc*) (explaining why expansive reading of section 113(f), enabling PRP to seek contribution at any time during cleanup process, better suits CERCLA's text than dissent's more restrictive reading); *see also* William D. Araiza, *supra* note 89, at 214 (suggesting section 107 should be interpreted not according to its plain meaning but as part of integrated whole); Brent J. Horton, Note, *CERCLA's Contribution Provision: Must a PRP First Face An Administrative Order or Cost Recovery Action? A Proposal for Amendment*, 53 SYRACUSE L. REV. 209, 234 (2003) (noting interaction between section 113 and section 106 or section 107 potentially leads to inequitable results).

<sup>94</sup> *See Aviall Servs., Inc.*, 312 F.3d at 679 (reversing earlier decision by divided panel holding *Aviall* could not assert contribution claim because it had not been subjected to action under section 106 or section 107); *Waukesha v. Viacom, Inc.*, 221 F. Supp. 2d 975, 977–78 (E.D. Wis. 2002) (denying polluter's motion to dismiss city's claim for cleanup of landfill toxins, expressly holding that absence of "only" is significant, and criticizing reasoning and strength of precedent to contrary); *Coastline Terminals of Conn., Inc. v. USX Corp.*, 156 F. Supp. 2d 203, 208 (D. Conn. 2001) (interpreting Second Circuit decision in *Bedford Affiliates* to mean "parties precluded from bringing cost recovery claims pursuant to § 107 may bring contribution actions"); *Ninth Ave. Remedial Group v. Allis Chalmers Corp.*, 974 F. Supp. 684, 690–91 (N.D. Ind. 1997) (stating because Seventh Circuit had not held to the contrary, contribution action does not depend on current or prior liability under sections 106 or 107); *Johnson County Airport Comm'n v. Parsonitt Co.*, 916 F. Supp. 1090, 1095 (D. Kan. 1996) (granting leave to amend complaint for PRP to assert contribution claim); *cf.* *Crofton Ventures Ltd. P'ship v. G&H P'ship*, 258 F.3d 292, 297–98 (4th Cir. 2001) (permitting contribution action to proceed without directly ruling on question); *Bedford Affiliates*, 156 F.3d at 424 (stating PRP who entered into negotiated agreement with state DEP to rehabilitate contaminated site could only sue under section 113(f), but court did not directly address question); *Pinal Creek Group v. Newmont Mining Corp.*, 118 F.3d 1298, 1305–06 (9th Cir. 1997) (explaining once a PRP incurs response costs, it and all other PRPs under section 107 become liable for the costs under section 113(f), independent of any liability to government); *Amoco Oil Co. v. Borden*, 889 F.2d 664, 667–68 (5th Cir. 1989) (permitting contribution action, but not directly ruling on question). *But see* *E.I. Du Pont de Nemours & Co. v. United States*, 297 F. Supp. 2d 740, 746 (D.N.J. 2003) (permitting "contribution" actions, i.e., those in which one party has been adjudged liable, only under section 113); *Rumpke, Inc. v. Cummins Engine Co.*, 107 F.3d 1235, 1241 (7th Cir. 1997) (stating in dictum "a § 106 or § 107 action apparently must either be ongoing or already completed" for contribution action to be permitted).

<sup>95</sup> *E.I. Du Pont de Nemours & Co.*, 297 F. Supp. 2d at 745 (stating Third Circuit law requires prior suit to seek section 113 contribution); *Deby, Inc. v. Cooper Indus.*, No. 99-C-2464, 2000 WL 263985, at \*1, 5 (N.D. Ill. Feb. 29, 2000) (dismissing contribution action because party must be found liable in earlier or

They have essentially adopted the Fifth Circuit panel's position. The first sentence is the exclusive federal contribution remedy.<sup>96</sup> The last sentence recognizes actions pursuant to other state and federal laws, but does not permit actions pursuant to pre-SARA case law.<sup>97</sup>

The Supreme Court has granted certiorari in *Aviall* and presumably will decide the issue. The United States wants the Court to reverse the *en banc* decision.<sup>98</sup> In addition to the points made in the Fifth Circuit panel opinion, the United States has emphasized another CERCLA goal: facilitating settlements through the EPA.<sup>99</sup>

A compromise position, which shows due regard for the statutory text and CERCLA's clear policy goals, is possible. A "contribution" action is a suit by one joint and severally liable tortfeasor against another to recover the defendant's proportionate share of *liability*. But a "potentially responsible party" is just that—*potentially liable*—until a court has adjudged it liable. The cleanup does not trigger liability. A judgment does. Therefore, both the first and last sentences of section 113(f) do not apply to a PRP's voluntary cleanup. Section 107, which permits cost recovery by "any . . . person," authorizes such an action for PRPs and non-PRPs alike. A court's equitable apportionment of some of the cost to a PRP-defendant does not transform the cost recovery action into a "contribution" action.

Even if this is a hyper-technical interpretation of "contribution," recognizing the lack of clarity would at least permit a court to resolve doubts in favor of CERCLA's primary policy of encouraging prompt cleanups. Moreover, if Congress wanted sole control over settlements, it would not have permitted *any party* to clean up and

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pending action to receive "actual compensation"); *Estes v. Scotsman Group, Inc.*, 16 F. Supp. 2d 983, 989 (C.D. Ill. 1998) (noting dichotomy between section 113(f)'s first and last sentences and relying on *Rumpke* dictum); *cf. Rockwell Int'l Corp. v. IU Int'l Corp.*, 702 F. Supp. 1384, 1389 (N.D. Ill. 1988) (reasoning contribution is unavailable under federal law unless federal statute "expressly establishes" remedy, but noting that "during or following" language does not limit but rather "recogniz[es] that actual payment of damages cannot occur until such time").

<sup>96</sup> The *Du Pont* court relied on *In re Reading*, 115 F.3d 1111 (3d Cir. 1997), for the proposition that section 113(f) replaced (and to the extent it conflicted, superseded) pre-SARA case law. It then examined the features of "contribution" actions at common law. It concluded that the savings clause permitted "contribution" actions by allowing a party to sue another tortfeasor under other, non-CERCLA law. Congress only modified the common law sense of "contribution" by permitting a contribution action *during* a civil action under section 106 or 107. *See E.I. Du Pont de Nemours & Co.*, 297 F. Supp. 2d at 742–50.

<sup>97</sup> *See E.I. Du Pont de Nemours & Co.*, 297 F. Supp. 2d at 746–47 (stating enactment of SARA amendments means pre-SARA case law is no longer controlling legal authority); *Reichhold Chems. Inc. v. Textron Inc.*, 888 F. Supp. 1116, 1123–24 (N.D. Fla. 1995) (asserting once Congress addresses subject by passing statute, role of courts is no longer to apply common law but to interpret the statute). Those courts must still resolve whether an EPA administrative enforcement proceeding under section 104, not contested in federal court, constitutes a "civil action" within the meaning of section 113(f), and if so, whether a PRP who cleans up following such an order has a contribution remedy. *Aviall Servs. Inc.*, 312 F.3d at 686–87.

<sup>98</sup> *See* Brief for the United States as Amicus Curiae Supporting Petitioner, No. 02-1192, 2004 WL 354181, at \*1 (Feb. 23, 2004).

<sup>99</sup> *See id.* at 27–29. Section 113(f)(2) absolves a settling party of any contribution liability to any other PRP, and reduces the potential liability of the other PRPs by the amount of the settlement. The EPA manages the potentially complicated liability scheme by providing a strong settlement incentive; *cf. United States v. Charles George Trucking Inc.*, 34 F.3d 1081, 1086 (1st Cir. 1994) (stating settlement is faithful to CERCLA's goals because the "ultimate measure of accountability in environmental case is overall recovery, not the amount of money paid by any individual defendant").

seek reimbursement, spawning a minefield of litigation. Giving PRPs a hybrid reimbursement-contribution right makes at least as much sense as allowing a reimbursement right to local governments and neighbors.

#### *h. Defenses to Liability*

CERCLA provides three (extremely) narrow defenses to liability. These include acts of God, acts of war, and acts or omissions of unrelated third parties.<sup>100</sup> In terms of the last defense, the defendant must shoulder the burden of proof. The defendant must prove: (1) a third party was solely responsible for the contamination; (2) the third party was not an employee or agent of the defendant; (3) the contamination did not occur as the result of a contractual relationship with the defendant; and (4) the defendant exercised due care with regard to foreseeable acts and omissions of the third party.<sup>101</sup>

Two groups may be exempt from CERCLA liability. Congress extended the third-party defense in the 1986 SARA amendments to encompass innocent landowners.<sup>102</sup> The "innocent landowner" defense applies when: (1) the owner acquired the property with no knowledge and no reason to know of the contamination; (2) the government acquired the property by involuntary transfer; or (3) the owner acquired the property by inheritance or bequest.<sup>103</sup> In 2001, the Small Business Liability Relief and Brownfields Revitalization Act expanded the "innocent landowner" defense. It added protections for adjacent landowners, prospective purchasers, and small businesses.<sup>104</sup> Secured parties may also be

<sup>100</sup> See 42 U.S.C. § 9607(b) (2000) (establishing affirmative defenses to CERCLA liability); *United States v. Inwood Assocs. LLP*, No. 96-CV-147DRHETB, 2004 WL 1801795, at \*14 (E.D.N.Y. Aug. 6, 2004) (stating defendants are barred from asserting defenses not listed within section 107(b)); *United States v. Kramer*, 757 F. Supp. 397, 410 (D.N.J. 1991) (noting in keeping with broad liability scheme of CERCLA, defendants are limited to defenses enumerated in section 107(b)).

<sup>101</sup> *Barr*, *supra* note 9, at 985 (citing *United States v. B.R. MacKay & Sons, Inc.*, No. 85-C-6925, 1986 WL 1583 (N.D. Ill. Jan. 21, 1986)); see *United States v. Iron Mountain Mines, Inc.*, 987 F. Supp. 1263, 1273 (E.D. Cal. 1997) (declaring third party defense in CERCLA is affirmative defense and therefore defendant bears burden of proof); *Foster v. United States*, 922 F. Supp. 642, 658 (D.D.C. 1996) (stating CERCLA's affirmative defenses shift burden of proof from plaintiff to defendant).

<sup>102</sup> Pub. L. No. 99-499, 100 Stat. 1613, 1616 (1986) (codified as amended at 42 U.S.C. § 9601(35A)); see *United States v. Domenic Lombardi Realty, Inc.*, 290 F. Supp. 2d 198, 208-09 (D.R.I. 2003) (explaining innocent landowner defense); Craig N. Johnston, *Current Landowner Liability Under CERCLA: Restoring the Need for Due Diligence*, 9 *FORDHAM ENVTL. L.J.* 401, 401-02 (1998) (describing typical scenarios involving innocent landowner provision).

<sup>103</sup> See *Barr*, *supra* note 9, at 986; see also *United States v. CDMG Realty Co.*, 96 F.3d 706, 716 (3d Cir. 1996) (explaining structure of innocent landowner defense); *United States v. Manzo*, 182 F. Supp. 2d 385, 409 (D.N.J. 2000) (listing elements defendant must prove to satisfy innocent landowner defense); *Grand St. Artists v. Gen. Elec. Co.*, 28 F. Supp. 2d 291, 295 (D.N.J. 1998) (listing elements defendant asserting affirmative defense must prove to escape liability).

<sup>104</sup> Pub. L. No. 107-118, 115 Stat. 2356, 2372-73 (2002) (codified in scattered sections of 42 U.S.C. §§ 9601-9607). The Amendments give further guidance for the adjacent landowner defense, prospective purchaser defense, other liability exemptions, and de minimis settlements. See Lisa Spickler Goodwin, *Environmental Law*, 37 *U. RICH. L. REV.* 117, 118-21 (2002) (citing 42 U.S.C. § 9601(35)). In addition, the Amendments now require that a landowner: (1) "provide full cooperation, assistance, and facility access to the persons that are authorized to conduct response actions;" (2) "not impede the effectiveness or integrity of

exempt from liability under CERCLA because of the Asset Conservation, Lender Liability, and Deposit Insurance Act of 1996.<sup>105</sup> Generally, a lender will not be a PRP if it did not participate in management of the property.<sup>106</sup>

### *i. Challenges to EPA Actions*

CERCLA limits a federal court's jurisdiction to review the EPA's broad powers to remediate environmental harm. Thus, if the EPA cleans up a site, a potentially responsible party may not challenge the EPA's actions in federal court until the EPA sues that party to recover its costs.<sup>107</sup> The same is true if the EPA orders a PRP to clean up under a unilateral administrative order. Congress barred such pre-enforcement review to keep the EPA from having "to litigate each detail of its removal and remedial plans before implementing them."<sup>108</sup> To our knowledge, no federal court has failed to uphold the bar on pre-enforcement review when a PRP sought to challenge the EPA's *statutory* authority to enforce CERCLA. On the other hand, several courts have held that a PRP may, pre-enforcement, challenge an EPA lien or unilateral administrative order on due process grounds.<sup>109</sup> In *Reardon v. United States*, the First Circuit concluded a CERCLA lien unconstitutionally deprived the owner of property without due process.<sup>110</sup> In *Reardon*, the EPA

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any institutional control employed at the facility in connection with a response action;" and (3) take "reasonable steps to . . . stop any continuing release; . . . prevent any threatened future release; and prevent or limit any . . . exposure to any previously released hazardous substance." *Id.* at 118.

<sup>105</sup> Pub. L. No. 104-208, 110 Stat. 3009, 3009-462-69 (1996); see Cruden, *supra* note 11, at 376 (discussing Act); see also *In re DuFrayne*, 194 B.R. 354, 362-63 (Bankr. E.D. Pa. 1996) (stating secured lenders are statutorily excluded from "owner or operator" language of CERCLA).

<sup>106</sup> Cruden, *supra* note 11, at 376; see *United States v. Fleet Factors Corp.*, 901 F.2d 1550, 1557-58 (11th Cir. 1990) (holding secured creditor may incur CERCLA liability "without being an operator, by participating in the financial management of a facility to a degree indicating a capacity to influence the corporation's treatment of hazardous wastes"); Paul Stanton Kibel, *The Urban Nexus: Open Space, Brownfields, and Justice*, 25 B.C. ENVTL. AFF. L. REV. 589, 600 (1998) (stating lenders are liable as PRPs if they influenced management decisions of property owners).

<sup>107</sup> 42 U.S.C. § 9613(h) (2000).

No federal court shall have jurisdiction under Federal law other than under section 1332 of title 28 (relating to diversity of citizenship jurisdiction) or under State law which is applicable or relevant and appropriate under section 9621 of this title (relating to cleanup standards) to review *any challenges to removal or remedial action selected under section 9604 of this title, or to review any order issued under section 9606(a) of this title*, in any action except one of the following [exceptions] . . .

*Id.* (emphasis added). Section 113(h) enumerates five exceptions, all actions filed by the government or by a private citizen seeking to enforce CERCLA or to recover costs for its enforcement. *Id.*

<sup>108</sup> *Reardon v. United States*, 947 F.2d 1509, 1513 (1st Cir. 1991) (en banc); see Voluntary Purchasing Groups, Inc. v. Reilly, 889 F.2d 1380, 1390 (5th Cir. 1989) (stating ban serves other goals like avoiding piecemeal litigation and avoiding inconsistent results).

<sup>109</sup> See U.S. CONST. amend. V (stating that "[n]o person shall . . . be deprived of . . . property without due process of law").

<sup>110</sup> 947 F.2d 1509, 1523 (1st Cir. 1991) (en banc); see *Gen. Elec. Co. v. EPA*, 360 F.3d 188, 191 (D.C. Cir. 2004) (agreeing with "plain text interpretation that . . . § 113(h) does not bar pre-enforcement review of facial constitutional challenges to CERCLA"); *Farmers Against Irresponsible Remediation v. EPA*, 165 F. Supp. 2d 253, 262 (N.D.N.Y. 2001) ("In *Reardon*, the First Circuit held that a due process challenge to several CERCLA statutory provisions did not fall within the section 9613(h) jurisdictional prohibition.").



removed hazardous substances from the plaintiffs' property. It then filed a notice of lien on the property for the amount it had spent cleaning up the land. The owners sued to have the notice of lien removed, arguing that the EPA's filing of the notice without a hearing was a deprivation of property without due process. They also made two statutory claims.<sup>111</sup> The district court denied the plaintiffs' motion for a preliminary injunction and dismissed their suit.<sup>112</sup> It concluded that it had no jurisdiction to hear the statutory claims, and that, even though it had jurisdiction to hear the constitutional claim, filing the notice of lien was not a taking of a significant enough property interest to trigger the protection of the due process clause. On appeal, a panel of the First Circuit affirmed.<sup>113</sup> The case was re-argued *en banc*, and the full First Circuit reversed, concluding that CERCLA's lien provisions violated the Fifth Amendment's Due Process Clause.<sup>114</sup>

In reaching this conclusion, the court applied a standard two-part analysis for deciding a property-based due process challenge: (1) does the statute authorize the taking of a "significant" property interest protected by the Fifth Amendment, and (2) if a significant property interest is involved, what process is due?<sup>115</sup> In examining the first prong, the court concluded that, under *Connecticut v. Doebr*,<sup>116</sup> a Supreme Court case decided after oral argument in the *en banc* rehearing, a CERCLA lien "amounts to deprivation of a 'significant property interest' within the meaning of the due process clause."<sup>117</sup> The court then focused on whether the process the CERCLA lien provided was adequate. It concluded that:

[T]he lien statute completely lacks procedural safeguards; that the government has no recognized pre-existing interest in the property; that the statute has no "exigent circumstances" requirement (nor have any such circumstances been shown in this case) . . . As applied in this case, the statute thus deprives persons of property with far less process than the State of Connecticut provided in the attachment law found unconstitutional in *Doebr*. Thus, we are constrained to find that the CERCLA lien provisions, by not providing, at the very least, notice and a pre-deprivation hearing to

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<sup>111</sup> *Reardon v. United States*, 731 F. Supp. 558, 559–61 (D. Mass. 1990) (arguing they were not liable because they were "innocent landowners," and even if they were liable, lien was over-extensive because it affected parcels not involved in cleanup), *aff'd*, 922 F.2d 28 (1st Cir. 1990) (withdrawn), *rev'd en banc*, 947 F.2d 1509 (1st Cir. 1991).

<sup>112</sup> *Id.* at 559.

<sup>113</sup> *Reardon v. United States*, 922 F.2d 28, 28–32 (1st Cir. 1990) (withdrawn), *rev'd en banc*, 947 F.2d 1509 (1st Cir. 1991).

<sup>114</sup> *Reardon*, 947 F.2d at 1510 (*en banc*) ("[T]he district court correctly decided that it did not have jurisdiction to consider the Reardons's statutory claims, but we find that the CERCLA lien provisions do violate the fifth amendment due process clause.").

<sup>115</sup> *Id.* at 1517 (citing *Fuentes v. Shevin*, 407 U.S. 67, 86 (1972) and *Mathews v. Eldridge*, 424 U.S. 319, 335 (1976)).

<sup>116</sup> 501 U.S. 1 (1991) (discussing due process attack on state statute authorizing prejudgment attachment of real estate which did not require preattachment hearing or notice or some showing of exigent circumstances).

<sup>117</sup> *Reardon*, 947 F.2d at 1518.

a property owner who claims that the property to be encumbered is not "subject to or affected by a removal or remedial action," violate the fifth amendment due process clause.<sup>118</sup>

The court also concluded that any "additional procedural requirements [were] likely to place significant, but not overwhelming, administrative burdens on the government."<sup>119</sup> In other words, the government had no significant interest to balance against the *Reardon's* property interest and the procedural defects of CERCLA.

Little fallout has resulted from *Reardon*. No other reported case has used it to allow a constitutional challenge to the EPA's ability to file a pre-enforcement lien under CERCLA. On the other hand, a court recently extended *Reardon's* logic to a constitutional challenge to an EPA unilateral administrative order.<sup>120</sup> In *General Electric Co. v. EPA*, General Electric (GE) sought a declaratory judgment that the EPA's power under CERCLA to order cleanup of contaminated properties violated an owner's due process rights.<sup>121</sup> The EPA moved to dismiss. It argued that CERCLA, section 113(h), bars judicial review of EPA actions until the EPA seeks to enforce its remedies in court. The district court, concluding that it lacked subject matter jurisdiction over General Electric's suit, granted the EPA's motion.

The D.C. Circuit reversed.<sup>122</sup> The court, relying on *Reardon*, narrowly construed section 113(h). Its "any challenges" language only barred challenges to EPA removal or remedial actions under section 104 or EPA orders under section 106(a).<sup>123</sup> Aside from *Reardon*, the court relied primarily on cases dealing with veterans' affairs and immigration. In fact, the court dismissed a series of post-*Reardon* environmental cases that had dismissed constitutional challenges to section

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<sup>118</sup> *Id.* at 1523–24.

<sup>119</sup> *Id.* at 1523.

<sup>120</sup> *Gen. Elec. Co. v. EPA*, 360 F.3d 188 (D.C. Cir. 2004) (discussing claim by potentially responsible party challenging CERCLA's unilateral administrative order regime as facially violative of due process).

<sup>121</sup> *Gen. Elec. Co. v. Whitman*, 257 F. Supp. 2d 8 (D.D.C. 2003), *rev'd*, *Gen. Elec. Co. v. EPA*, 360 F.3d 188 (D.C. Cir. 2004). GE argued:

[T]he [section 106] regime thus imposes a classic and unconstitutional Hobson's choice: Either do nothing and risk severe punishment without meaningful recourse or comply and wait indefinitely before having any opportunity to be heard on the legality and rationality of the underlying order.

*Id.* at 15.

<sup>122</sup> *Gen. Elec. Co.*, 360 F.3d at 189 ("[T]he plain text of § 113(h) does not bar GE's facial constitutional challenge to CERCLA and accordingly, we reverse and remand the case to the district court."); see *Berriochoa Lopez v. United States*, 309 F. Supp. 2d 22, 28 (D.D.C. 2004) ("The D.C. Circuit emphasized . . . that the apparently broad 'any challenges' language was not 'without qualification.'"); Michael B. Gerrard, *Courts Enforce Consent Orders, Question Unilateral Orders*, N.Y. L.J., May 28, 2004, at 3, col. 1 (noting importance of D.C. Circuit's decision on unilateral orders).

<sup>123</sup> *Gen. Elec. Co.*, 360 F.3d at 191 ("Congress . . . enumerated only two types of challenges over which federal courts lack jurisdiction—challenges to § 104 actions and § 106(a) orders. Although § 113 (h) refers broadly to 'any challenges,' the plain language does not bar 'any challenge,' without qualification."); see *Hoosier Envtl. Council, Inc. v. N. Ind. Pub. Serv. Co.*, 2004 U.S. Dist. WL 2011470, at \*2 (N.D. Ind. May 21, 2004) (discussing construction of section 113(h) by D.C. Circuit).

113(h):

To the extent that other courts have concluded a constitutional claim is barred by § 113(h), they have done so in cases involving challenges to specific EPA orders and actions, *see Oil Chem. & Atomic Workers Int'l Union v. Richardson*, 214 F.3d 1379 (D.C. Cir. 2000); *McClellan Ecological Seepage Situation v. Perry*, 47 F.3d 325, 327 (9th Cir. 1995); *Schalk v. Reilly*, 900 F.2d 1091, 1094 (7th Cir. 1990); *Voluntary Purchasing Groups, Inc. v. Reilly*, 889 F.2d 1380, 1390 (5th Cir. 1989), or they have not focused on the plain text of § 113(h), *see Barmet Aluminum Corp. v. Reilly*, 927 F.2d 289, 293 (6th Cir. 1991); *Schalk*, 900 F.2d at 1094; *South Macomb Disposal Auth. v. EPA*, 681 F. Supp. 1244, 1251 (E.D. Mich. 1988).<sup>124</sup>

Yet, the EPA had, in fact, ordered GE to clean up specific, environmentally challenged sites. Thus, GE's suit, in effect, challenged specific EPA orders. The court seemed to ignore that fact.

Assuming neither the full D.C. Circuit nor the Supreme Court reverses the panel opinion, it is hard to imagine how any PRP faced with a cleanup order would fail to ask a federal court in the District of Columbia to enjoin further enforcement of the cleanup order pending resolution of *General Electric*.

Taken together, *Reardon* and *General Electric* provide a debtor-in-possession with the possibility of avoiding a pre-petition EPA lien or enjoining enforcement actions against property of the estate.

#### 4. Settlement

One of CERCLA's professed purposes is to encourage prompt settlements because that, in turn, encourages prompt cleanups. Congress enacted section 122 ("Settlements") as part of SARA. Section 122 codified many of the settlement procedures the EPA had followed for the prior six years.<sup>125</sup> The EPA has always preferred to settle disputes.<sup>126</sup> However, the most important terms of the

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<sup>124</sup> *Gen. Elec. Co.*, 360 F.3d at 193.

<sup>125</sup> Lee, *supra* note 12, at 312 (acknowledging section 122 was codification of prior EPA settlement practices and noting importance of consulting section 122 before settling CERCLA case); *see Georgoulis v. Allied Prod. Corp.*, 796 F. Supp. 986, 989 (N.D. Tex. 1991) ("The language of CERCLA clearly indicates that EPA's allocation of the responsibilities for cleanup to PRP's, under §§ 104 and 122, is meant to 'expedite effective remedial actions and minimize litigation.'"); Alfred R. Light, *Superfund's Second Master: The Uneasy Fit of Private Cost Recovery Within CERCLA*, 6 ST. THOMAS L. REV. 97, 121 (1993) (stating CERCLA section 122(e)(6) "requires a private party to obtain EPA's permission before proceeding with a remedial action at a site where EPA has an RI/FS under way.").

<sup>126</sup> *See* Hazardous Waste Enforcement Policy, 50 Fed. Reg. 5034 (1985) (discussing EPA's original policy); *see also* *United States v. Atlas Minerals & Chems., Inc.*, 851 F. Supp. 639, 653 (E.D. Pa. 1994) (noting EPA's stated policy favoring early settlement with municipalities); *Prof'l Rental, Inc. v. Shelby Ins.*

settlement—the type of remedial action the EPA will pursue, the proportion of the harm allocated to the settling party—are often non-negotiable.<sup>127</sup> Moreover, section 122(f) prescribes strict guidelines for issuing a covenant not to sue. For example, it must be in the public interest. If later information about risks makes a settlement no longer in the public interest, the covenant is no longer valid. The covenant must also provide an exception for unknown conditions that are later discovered. Liability remains even after a "settlement," rendering negotiation a waste of time and money. A party might prefer to wait for the EPA to issue an administrative order before discharging its obligation.

Often, several PRPs contribute small amounts of contamination to a site. Each PRP's individual contribution is barely significant. The costs of settling with each might outweigh the benefits. Section 122(g) provides special procedures in these cases ("de minimis settlements").<sup>128</sup>

Like administrative orders, EPA settlements often include stipulated penalties for failure to comply. The EPA often insists that penalties continue to accrue while any dispute is pending.<sup>129</sup> If the EPA wins, the settling party loses the accrued amount.

CERCLA's settlement provisions do not deviate from its singular focus: to encourage prompt cleanups paid for by those responsible for the mess. PRPs may be no better off settling with the EPA than they would be litigating—but they are likely to be no worse off. Given the judicial propensity to construe broadly almost every element of CERCLA, a PRP is not likely to find a loophole. A settlement may be the most cost-effective option. Moreover, settlement gives the EPA a pre-petition claim should the settling PRP subsequently petition for bankruptcy relief.

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Co., 599 N.E.2d 423, 429 (Ohio Ct. App. 1991) ("Generally, the EPA's first move is to issue administrative notices to one or more PRPs to initiate the settlement process.").

<sup>127</sup> Lee, *supra* note 12, at 312 ("While it is EPA's policy to settle, increasingly it has demonstrated inflexibility both with regard to the remedial action selected and with the terms of the settlement agreement."); see *United States v. Charles George Trucking, Inc.*, 34 F.3d 1081, 1086 (1st Cir. 1994) (stating "the ultimate measure of accountability in an environmental case is the extent of the overall recovery, not the amount of money paid by any individual defendant"); *United States v. Acton Corp.*, 733 F. Supp. 869, 872 (D.N.J. 1990) ("It is not our function to determine whether a better settlement could be calculated, but only whether the existing settlement is reasonable.").

<sup>128</sup> A de minimis settlement is appropriate either when (A) the amount and toxicity of the substance a party contributed is minimal compared to other substances at the site, or (B) a current owner did not conduct or permit generation, transportation, storage, treatment, or disposal of the hazardous substance, and did not contribute to the release of a hazardous substance through any act or omission. 42 U.S.C. § 9622(g) (2000).

<sup>129</sup> Lee, *supra* note 12, at 317 ("One of the policy's more disturbing features to settlers is EPA's insistence that stipulated penalties continue to accrue during any delay cause by a dispute under the consent decree."); see 42 U.S.C. § 9622(l) (outlining civil penalties for potentially responsible parties). See generally *United States v. Occidental Chem. Corp.*, 200 F.3d 143, 147 (3d Cir. 1999) (explaining different settlement agreements and contingency plan of government when United States enters into settlement agreement).

## B. RCRA

The Resource Conservation and Recovery Act of 1976 (RCRA)<sup>130</sup> establishes a statutory scheme for monitoring solid wastes and their disposal, with a focus on the disposal of hazardous wastes. This "cradle to grave" regulatory scheme is intended to *prevent* the types of untreated releases that CERCLA is designed to clean up. RCRA stringently regulates the disposal of solid waste. It creates a complex monitoring and reporting program that seeks to create accountability for solid waste through every step of its life cycle. RCRA also imposes strict standards for the handling and treatment of solid waste. These standards are even stricter if a solid waste qualifies as "hazardous" under the Act.<sup>131</sup>

RCRA prohibits treatment, storage, or disposal of hazardous wastes without a permit. The first step of RCRA monitoring, therefore, requires a permit to operate a treatment, storage and disposal facility (TSD).<sup>132</sup> A facility can only obtain a permit if it can show it has adequate financing and insurance to comply with RCRA's requirements.<sup>133</sup> The government may require permit applicants to take corrective action to remediate past releases of hazardous waste on the facility site.<sup>134</sup> Once a permit is in place, RCRA imposes standards the TSD must meet to ensure compliance, e.g., specific record keeping, use of a manifest system to list wastes, operating criteria, site requirements, contingency planning, financial responsibility, and other permit requirements.<sup>135</sup> The EPA can assess civil, criminal and

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<sup>130</sup> 42 U.S.C. §§ 6901–6991 (2000); *see, e.g.*, *Chicago v. Envtl. Def. Fund*, 511 U.S. 328, 331 (1994) (noting "cradle to grave" regulatory scheme of RCRA); *Gen. Motors Corp. v. EPA*, 363 F.3d 442, 444 (D.C. Cir. 2004) (discussing comprehensive safeguards and waste management procedures of RCRA).

<sup>131</sup> The term hazardous waste means:

a solid waste, or combination of solid wastes, which because of its quantity, concentration, or physical, chemical, or infectious characteristics may: (A) cause, or significantly contribute to an increase in mortality or an increase in serious, irreversible, or incapacitating reversible, illness; or (B) pose a substantial present or potential hazard to human health or the environment when improperly treated, stored, transported, or disposed of, or otherwise managed.

42 U.S.C. § 6903(5) (2000).

<sup>132</sup> 42 U.S.C. § 6924(a)(7) (2000); *see S.C. Dept. of Health & Envtl. Control v. Commerce & Indus. Ins. Co.*, 372 F.3d 245, 250 (4th Cir. 2004) (addressing RCRA requirement of permit to treat, store, or dispose of certain enumerated "hazardous wastes"); *Fla. Power & Light Co. v. EPA*, 145 F.3d 1414, 1416 (D.C. Cir. 1998) (acknowledging statutory requirements of RCRA which require permit be obtained before certain wastes are treated, stored, or disposed).

<sup>133</sup> John A. Barrett, Jr., *The U.S. Approach to Resolving the Tension between Environmental Liability and Bankruptcy Debt Forgiveness*, in ENVIRONMENTAL ISSUES IN INSOLVENCY PROCEEDINGS 141 (John A. Barret, ed., 1998); *see* 42 U.S.C. § 6924(t) (indicating requirement of financial responsibility); *see also S.C. Dept. of Health and Envtl. Control*, 372 F.3d at 251 n.4 (explaining meaning of "guarantor" under financial responsibility provision of RCRA).

<sup>134</sup> 42 U.S.C. § 6924(a)(1); *see Miriam Feder, The Permit Application Process Under RCRA—A Lament*, 18 ENVTL. L. 671, 677–78 (1988) (explaining necessity of correcting deficiencies during lengthy application process). *But cf. Furrer v. Brown*, 62 F.3d 1092, 1098 (8th Cir. 1995) (stating primary goal of RCRA is to prevent creation of hazardous waste, not promote its cleanup).

<sup>135</sup> 42 U.S.C. § 6924(a); *see Randolph L. Hill, An Overview of RCRA: The "Mind-Numbing" Provisions of the Most Complicated Environmental Statute*, 21 ENVTL. L. REP. 10254 n.160 (1991) (providing overview

administrative penalties for failure to comply with RCRA's requirements.<sup>136</sup>

Congress intended regulations under RCRA to occur through a partnership between the federal and state government with the state assuming primary responsibility for enforcement.<sup>137</sup> The EPA may authorize a state program to substitute for the federal program, but the state requirements must be at least as stringent as the federal requirements.<sup>138</sup> Once a state program is in place, it is federally enforceable.<sup>139</sup>

RCRA, like CERCLA, authorizes citizen suits to enforce its provisions. Citizens who are substantially endangered by a hazardous release may bring suit for an injunction to stop certain activities, or to require a party to take certain steps. A citizen suit is not available to recover the costs of a cleanup.<sup>140</sup> Moreover, a citizen suit is not available if CERCLA proceedings have been undertaken, or if the EPA is engaged in a RCRA enforcement action.<sup>141</sup>

Citizens may file three types of suits under RCRA: (1) actions against any person in violation of a RCRA permit or regulation; (2) actions against any person to compel abatement of imminent or substantial endangerment; and (3) actions against the EPA to compel duties under RCRA.<sup>142</sup>

### C. Other Federal & State Laws

Parties can incur environmental liability under other statutory schemes in addition to CERCLA and RCRA. These include the Federal Water Pollution

of operating requirements within section 3004 of RCRA); *see also* Empire Energy Mgmt. Sys., Inc. v. Roche, 362 F.3d 1343, 1350 (Fed. Cir. 2004) (identifying operating criteria within RCRA).

<sup>136</sup> 42 U.S.C. § 6928 (2000). These fines run between \$25,000 a day for civil fines, and \$50,000 per day for criminal penalties. If anyone is subjected to bodily injury or death, a fine of \$250,000 for individuals or \$1,000,000 for entities may be assessed. *Id.*

<sup>137</sup> Hill, *supra* note 135, at n.348-53; *see* Harmon Indus. v. Browner, 19 F. Supp. 2d 988, 996 (W.D. Mo. 1998) (defining responsibilities of state and federal governments with respect to hazardous waste regulation); Orange Env't., Inc. v. County of Orange, 860 F. Supp. 1003, 1020 (S.D.N.Y. 1994) (explaining integration of federal and state hazardous waste programs).

<sup>138</sup> 42 U.S.C. § 6929 (2000); *see also* Hill, *supra* note 135, at n.353 (citing section 6929).

<sup>139</sup> 42 U.S.C. § 6928(a)(3); *see also* Hill, *supra* note 135, at n.351 (citing section 6928(a)(3)).

<sup>140</sup> 42 U.S.C. § 6972(a) (2000); *see* Meghri v. KFC W., Inc. 516 U.S. 479, 486 (1996) ("[Section] 6972(a) was designed to provide a remedy that ameliorates present or obviates the risk of future 'imminent' harms, not a remedy that compensates for past cleanup efforts."); Avondale Fed. Sav. Bank v. Amoco Oil Co., 170 F.3d 692, 694 (7th Cir. 1999) (concluding RCRA is not directed at providing compensation for past cleanup costs).

<sup>141</sup> 42 U.S.C. § 6972(b)(2)(C); *see* Meghri, 516 U.S. at 486 (stating citizen suit may not be brought against defendant if EPA or state has commenced and is pursuing some other enforcement action); Waste, Inc. Cost Recovery Group v. Allis Chalmers Corp., 51 F. Supp. 2d 936, 940 (N.D. Ind. 1999) (disallowing plaintiff's citizen suit on grounds that no citizen suit can proceed if either the state or EPA is involved in separate enforcement action).

<sup>142</sup> 42 U.S.C. § 6972(a); *see* Orange Env't., Inc. v. County of Orange, 860 F. Supp. 1003, 1020 (S.D.N.Y. 1994) (noting RCRA provides for three different types of citizen suits); *cf.* Susan Verdicchio, *Environmental Restoration Orders*, 12 B.C. ENVTL. AFF. L. REV. 171, 197 (1985) (categorizing most federal environmental laws providing civil enforcement provisions into three types—civil actions by EPA, civil actions by citizens, and civil emergency provisions).

Control Act (widely known as the Clean Water Act),<sup>143</sup> the Clean Air Act,<sup>144</sup> and a host of state regulatory schemes. Common law theories of contract and tort can also create liability.<sup>145</sup>

CERCLA and state environmental laws have played the biggest role in bankruptcy proceedings. Often the line between federal and state will blur because a state will seek reimbursement for cleanup costs under CERCLA.

## II. ABANDONMENT

### A. Abandonment Power

Section 554(a) authorizes the trustee to "abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate."<sup>146</sup> The abandonment power was obvious, innocuous, and non-controversial until a chapter 7 trustee tried to abandon a toxic waste site.

In *Midlantic National Bank v. New Jersey Department of Environmental Protection*,<sup>147</sup> the Supreme Court had to decide whether a trustee could abandon contaminated property. That was in 1986. To this day, there is no consensus on what *Midlantic* actually held and when a trustee can abandon contaminated property.

### B. Midlantic

Quanta Resources Corporation (Quanta) operated two waste oil facilities, one in New Jersey, the other in New York. The New Jersey Department of Environmental Protection (NJDEP) discovered that Quanta's New Jersey site had accepted 400,000 gallons of waste oil containing PCB, a toxic carcinogen. During cleanup negotiations, Quanta petitioned for chapter 11. The case was later converted into chapter 7. Subsequently, NJDEP discovered 70,000 gallons of PCB-contaminated waste oil at Quanta's New York site. The bankruptcy court granted the trustee's motion to abandon because the property was burdensome and of inconsequential value to the estate. The court did so "over NJDEP's objection that the estate had sufficient funds to protect the public from the dangers posed by the hazardous waste."<sup>148</sup> Upon abandonment, the trustee removed the guard service and fire-suppression system that protected the New York property. The State of New York

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<sup>143</sup> 33 U.S.C. §§ 1251-1387 (2000).

<sup>144</sup> 42 U.S.C. §§ 7401-7671 (2000).

<sup>145</sup> Breach of contract liability can arise pursuant to violation of an environmentally related contract. Tort law encompasses environmental liability under both nuisance and trespass actions. For a further discussion of these causes of action, see Barrett, *supra* note 133, at 136-38.

<sup>146</sup> 11 U.S.C. § 554(a) (2000); see *Borden, Inc. v. Wells-Fargo Bus. Credit (In re Smith-Douglass, Inc.)*, 856 F.2d 12, 15 (4th Cir. 1988) (recognizing right of abandonment); see also *Midlantic Nat'l Bank v. N.J. Dep't of Env'tl. Prot.*, 474 U.S. 494, 501 (1986) (holding trustee could not exercise abandonment power in violation of state and federal laws).

<sup>147</sup> 474 U.S. 494 (1986).

<sup>148</sup> *Midlantic Nat'l Bank*, 474 U.S. at 498-99.

spent approximately \$2.5 million to decontaminate the facility.

On appeal, the district court affirmed. The Third Circuit reversed, holding that Congress, in enacting section 554, did not intend to pre-empt pre-Code, judge-made restrictions on a trustee's ability to abandon property. The Supreme Court affirmed the Third Circuit.

According to the Court, pre-Code, courts had limited the abandonment power "to protect legitimate state or federal interests." At the time Congress enacted section 554, "there were well-recognized restrictions on a trustee's abandonment power."<sup>149</sup> When Congress enacted section 554, it "presumably included the established corollary that a trustee could not exercise his abandonment power in violation of certain state and federal laws."<sup>150</sup> The Court pointed to 28 U.S.C. § 959(b) to bolster its conclusion that Congress did not intend the Bankruptcy Code to pre-empt all state laws: "Section 959(b) commands the trustee to 'manage and operate property in his possession . . . according to the requirements of the valid laws of the State.'"<sup>151</sup>

The Court continued:

The Bankruptcy Court does not have the power to authorize an abandonment without formulating conditions that will adequately protect the public's health and safety. Accordingly, without reaching the question whether certain state laws imposing conditions on abandonment may be so onerous as to interfere with the bankruptcy adjudication itself, we hold that a trustee may not abandon property in contravention of a state statute or regulation that is reasonably designed to protect the public health or safety from identified hazards.<sup>152</sup>

The Court qualified its holding in footnote nine:

This exception . . . is a narrow one. It does not encompass a speculative or indeterminate future violation of such laws that may stem from abandonment. The abandonment power is not to be fettered by laws or regulations not reasonably calculated to protect the public health or safety from imminent and identifiable harm.<sup>153</sup>

Justice Rehnquist, in a dissent joined by Chief Justice Burger and Justices Stevens and O'Connor, criticized the majority's assertion that Congress, in enacting section 554, had codified well-recognized restrictions on the trustee's abandonment power. The majority's reasoning "rests on a misreading of three pre-Code cases, the

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<sup>149</sup> *Id.* at 501.

<sup>150</sup> *Id.*

<sup>151</sup> *Id.* at 505.

<sup>152</sup> *Id.* at 506-07.

<sup>153</sup> *Id.* at 507 n.9.



elevation of that misreading into a 'well-recognized' exception to the abandonment power, and the unsupported assertion that Congress must have meant to codify the exception (or something like it)."<sup>154</sup>

The dissent also pointed out that section 959(b) did not directly apply to chapter 7 cases.<sup>155</sup> The majority did not explain how it applied indirectly. Even if it had, the dissent disagreed that section 959(b) precluded abandonment: "[A] trustee's filing of a petition to abandon, as opposed to continued operation of a site pending a decision to abandon, does not constitute 'manage[ment]' or 'opera[tion]' under that provision."<sup>156</sup>

By any standard, the Court's "holding" is elastic. It has spawned several different interpretations of when a trustee can abandon contaminated property.

### C. No Abandonment in Contravention of State Statutes Reasonably Designed To Protect Public Health or Safety from Identified Hazards

Some courts have interpreted *Midlantic* to prohibit abandonment if abandonment would violate a state statute or regulation designed to protect public health or safety.<sup>157</sup> This interpretation means a trustee cannot abandon contaminated property unless and until it complies with state or federal environmental regulations. If the trustee cannot abandon, and 28 U.S.C. § 959(b) requires the trustee to comply with all valid state laws, the trustee must remediate the property (with estate assets) or let someone else do it as an administrative expense.<sup>158</sup>

For example, in *Pennsylvania Department of Environmental Resources v.*

<sup>154</sup> *Id.* at 507–08 (Rehnquist, J., dissenting).

<sup>155</sup> *Id.* at 513–14 (Rehnquist, J., dissenting); see cases cited *infra* note 156.

<sup>156</sup> *Midlantic Nat'l Bank*, 474 U.S. at 514 (Rehnquist, J., dissenting); see *Ala. Surface Mining Comm'n v. N.P. Mining Co.* (*In re N.P. Mining Co.*), 963 F.2d 1449, 1460 (11th Cir. 1992) (canvassing cases establishing section 959(b) does not apply when business operations have ceased and trustee is merely liquidating); *In re Valley Steel Prods. Co.*, 157 B.R. 442, 448 (Bankr. E.D. Mo. 1993) (citing decisions which declined to apply section 959(b) to chapter 7 cases); *In re Corona Plastics, Inc.*, 99 B.R. 231, 236 (Bankr. D.N.J. 1989) (stating section 959(b) only applies when trustee is "conducting business").

<sup>157</sup> See, e.g., *Lancaster v. Tennessee* (*In re Wall Tube & Metal Prods. Co.*), 831 F.2d 118, 122 (6th Cir. 1987) (discussing how trustee cannot abandon property when it would result in economic health hazard); *In re Stevens*, 68 B.R. 774, 780–81 (Bankr. D. Me. 1987) (denying abandonment because contaminated waste oil threatened public safety and abandonment would contravene state law); *In re Peerless Plating*, 70 B.R. 943, 946 (Bankr. W.D. Mich. 1987) ("[A] trustee may not abandon property in contravention of a state statute or regulation that is reasonably designed to protect the public health or safety from identified hazards." (quoting *Midlantic Nat'l Bank*, 474 U.S. at 507)); cf. *In re Unidigital, Inc.*, 262 B.R. 283, 286–90 (Bankr. D. Del. 2001) (deciding debtor's landlord not entitled to administrative expense for cleanup costs to remove printer because printer did not pose imminent identifiable harm and landlord did not specify any particular law which abandonment would violate); *In re Mahoney-Troast Constr. Co.*, 189 B.R. 57, 59 (Bankr. D.N.J. 1995) (holding landlord's cleanup costs were not entitled to administrative expense priority because landlord could not specify any state law requiring remediation of the contaminated property).

<sup>158</sup> For instance, in *In re Microfab*, 105 B.R. 161, 166 (Bankr. D. Mass. 1989), the court stated: "[i]n effect, *Midlantic* requires a Chapter 7 trustee to bring contaminated estate property into compliance with state environmental laws on an administrative basis." Nevertheless, the court denied the state's request to order the trustee to remediate the site because expenditure of all estate assets would not make any appreciable difference. *Id.*

*Conroy*,<sup>159</sup> the Pennsylvania Department of Environmental Resources (DER) discovered drums of hazardous waste left on a site that was operated by printing company Frank Conroy.<sup>160</sup> The DER considered the site a danger to public health and safety.<sup>161</sup> The Pennsylvania Hazardous Sites Cleanup Act prohibited the "release" of a hazardous substance.<sup>162</sup> "Abandonment of a hazardous substance constitutes a 'release' . . . . Therefore, Pennsylvania law effectively prohibited the Conroys from abandoning the hazardous wastes located on the printing facility premises."<sup>163</sup> As in many abandonment cases, the issue in *Conroy* was not really about the trustee's right to abandon, but who would pay for the cleanup costs. For many courts, the starting premise is the trustee's inability to abandon. As noted, if the trustee cannot abandon, then he or she must clean up or otherwise remediate the property. If a third party cleans up and thereby performs the trustee's duties, that third party is entitled to recover its costs as an administrative expense. And so *Conroy* held.<sup>164</sup>

#### D. Narrower Readings of *Midlantic*

Most courts do not give *Midlantic* such a broad reading.

##### 1. No Imminent & Identifiable Harm

Several courts have interpreted *Midlantic* to prohibit abandonment only when the property poses an imminent and identifiable harm to the public health or safety.<sup>165</sup> Absent an imminent and identifiable harm, abandonment is permitted even though it contravenes (violates) a state law or regulation reasonably designed to protect the public health or safety from identified hazards. Some courts permit abandonment if there is no imminent, identifiable harm *and* there are no unencumbered estate assets to remediate the problem.<sup>166</sup> Others do not decide what

<sup>159</sup> 24 F.3d 568 (3d Cir. 1994).

<sup>160</sup> *Id.* at 569.

<sup>161</sup> *Id.*

<sup>162</sup> *Id.*

<sup>163</sup> *Id.*

<sup>164</sup> *Id.* at 570; see *Lancaster v. Tennessee (In re Wall Tube & Metal Prods. Co.)*, 831 F.2d 118, 124 (6th Cir. 1987) (awarding state of Tennessee compensation for cleanup as administrative expense); *In re Stevens*, 68 B.R. 774, 783-84 (Bankr. D. Me. 1987) (awarding DEP compensation as administrative expense).

<sup>165</sup> See *infra* note 180; see also *In re Doyle Lumber, Inc.*, 137 B.R. 197, 203 (Bankr. W.D. Va. 1992) (finding lumber treatment plant contaminated by chromium and arsenic not imminent threat when plant complied with state waste management regulations and only ground for objection was plant had not been closed down); cf. *In re S. Int'l Co.*, 165 B.R. 815, 823 (Bankr. E.D. Va. 1994) (stating "very fact" it took six weeks for spill to occur proves threat was not imminent); *In re Sheffield Oil Co.*, 162 B.R. 339, 341 (Bankr. M.D. Ala. 1993) (holding trustee not required to spend estate funds to assess underground petroleum tanks when no evidence of contamination existed); *In re H.F. Radandt, Inc.*, 160 B.R. 323, 328 (Bankr. W.D. Wis. 1993) (stating DNR inaction was proof problem was not imminent).

<sup>166</sup> See, e.g., *Borden v. Wells-Fargo Bus. Credit (In re Smith-Douglass, Inc.)*, 856 F.2d 12, 16 (4th Cir. 1988) (permitting abandonment when estate had no unencumbered assets and site did not pose serious public health or safety risk); *In re Better-Brite Plating, Inc.*, 105 B.R. 912, 917 (Bankr. E.D. Wis. 1989) (permitting

*Midlantic* means or requires because the situation involves an imminent, identifiable harm *and* abandonment would violate a state statute reasonably designed to protect the public health and safety.<sup>167</sup>

## 2. No Unencumbered Estate Assets

Some courts allow abandonment even in the face of an identified, imminent threat to public health and safety if the estate has no unencumbered assets. *In re Oklahoma Refining Co.*,<sup>168</sup> is a case in point. The environmental problems were "the culmination of 65 years of crude oil refining at this site."<sup>169</sup> The estate owed secured claims in excess of \$40 million. The estate's assets had a value of about \$4 million. There were no unencumbered assets. The trustee sought to abandon the property. Once cleaned up, the land would have been worth about \$100,000. The cleanup cost was estimated to be \$2.5 million. The court noted:

The trustee thus finds himself confronted with a formidable dilemma. On one hand he has no funds which are not cash collateral but, under a strict reading of *Midlantic*, he could be required to comply with State laws and regulations which is impossible because of section 363(c)(2) . . . . We do not believe the Supreme Court intended to place bankruptcy trustees in such a predicament but rather *Midlantic* requires the bankruptcy court, in determining whether to permit abandonment, [to] take state environmental laws and regulations into consideration . . . .

. . . .

. . . For all purposes the difference between denying abandonment and allowing abandonment produces the same result. Under either scenario there are no funds available to finance the closure plan or post-closure monitoring . . . .

To require strict compliance with State environmental laws under the facts of this case could create a bankruptcy case in perpetuity and fetter the estate to a situation without resolve. This trustee, with the consent of the secured creditors, has done what is reasonable under the circumstances. To pre-empt the administration of this

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abandonment because estate did not possess enough unencumbered assets to fund cleanup; there was no evidence of imminent harm or danger to public); *see also In re FXC, Inc.*, 96 B.R. 49, 54 (Bankr. E.D.N.C. 1989) (following *Smith-Douglass*).

<sup>167</sup> *See, e.g., Guterl Special Steel Corp. v. Econ. Dev. Admin. (In re Guterl Special Steel Corp.)*, 198 B.R. 128, 133 (Bankr. W.D. Pa. 1996) (noting neither view would permit abandonment on facts of case).

<sup>168</sup> 63 B.R. 562 (Bankr. W.D. Okla. 1986).

<sup>169</sup> *Id.* at 563.

estate would derogate the spirit and purpose of the bankruptcy laws requiring prompt and effectual administration within a limited time period . . . . The Oklahoma laws regarding environmental protection are not unreasonable but juxtaposed to the Bankruptcy Code cannot be reconciled to satisfy the strict compliance sought by the State agencies.<sup>170</sup>

The court granted the trustee's motion to abandon.

### 3. Abandonment Subject to Conditions

Some courts understand *Midlantic* to focus on the trustee's act of abandonment. Will the act of abandonment itself pose an imminent, identifiable harm? Under that strand of thinking, if abandonment will not aggravate the threat to public health and safety, the court will allow it.<sup>171</sup> Other courts permit abandonment if the trustee takes steps to protect the public's health and safety.<sup>172</sup> Yet others condition abandonment on setting aside estate funds for the cleanup,<sup>173</sup> or ordering that the proceeds from a sale of the decontaminated property go first to satisfy the EPA's cleanup costs.<sup>174</sup>

### 4. Multi-Part Tests for Abandonment

Other courts have developed multi-part tests based on *Midlantic*'s language and the cases construing it. In *New Jersey Department of Environmental Protection v. Atkinson (In re St. Lawrence Corp.)*,<sup>175</sup> a district court considered a DEP appeal from a bankruptcy court judgment allowing abandonment. The debtor leased real property. In the course of preparing estate property for sale, the bankruptcy trustee had ordered a site assessment. It indicated no serious environmental issues and no imminent danger to the public. A prospective purchaser sought to modify its

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<sup>170</sup> *Id.* at 565–66.

<sup>171</sup> See, e.g., *N.J. Dep't of Env'tl. Prot. v. N. Am. Prods. Acquisition Corp.*, 137 B.R. 8, 12 (D.N.J. 1992) (stating abandonment permitted if it "will not aggravate the threat of harm to the health and safety of the public or create some additional harm"); *In re Smith-Douglass, Inc.*, 75 B.R. at 998 (noting exception in *Midlantic* requires trustee to take adequate precaution to ensure public is not threatened by imminent danger resulting from abandonment); *In re Okla. Ref. Co.*, 63 B.R. 562, 565 (Bankr. W.D. Okla. 1986) (emphasizing "abandonment will not aggravate the existing situation.").

<sup>172</sup> *In re Smith-Douglass, Inc.*, 856 F.2d at 16 ("According to the teachings of *Midlantic*, where the public health or safety is threatened with imminent and identifiable harm, abandonment of the contaminated property must be conditioned on the performance of procedures that will adequately protect public health and safety."). See generally *Leavell v. Karnes*, 143 B.R. 212, 218 (S.D. Ill. 1990) (comparing broad and narrow approaches to placing conditions on abandonment).

<sup>173</sup> *In re FCX, Inc.*, 96 B.R. 49, 55 (Bankr. E.D.N.C. 1989) (holding trustee can abandon pesticide production site despite immediate threat to public from buried pesticides if he sets aside \$250,000 for cleanup).

<sup>174</sup> *In re Mowbray Eng'g Co.*, 67 B.R. 34, 36 (Bankr. M.D. Ala. 1986) (giving EPA's cleanup costs administrative expense priority).

<sup>175</sup> 248 B.R. 734, 736 (D.N.J. 2000).

purchase offer, claiming possible contamination. The sale of the property fell through. The trustee ultimately moved to abandon it. The DEP objected to the abandonment arguing the site assessment was not satisfactory under the New Jersey Industrial Site Recovery Act (ISRA) and the DEP did not have enough information about the rest of the site.

In agreeing that the trustee could abandon the property, the court articulated a four-part test.<sup>176</sup> First, the court had to determine if the property posed a risk of imminent and identifiable harm to the public health and safety.<sup>177</sup> According to the court, the only evidence of contamination was a letter from an environmental consultant stating there was possible contamination on site.<sup>178</sup> The DEP did not prove there was an imminent risk of any kind.<sup>179</sup> Moreover, even direct proof of contamination would not, in itself, mean the site posed an imminent and identifiable hazard.<sup>180</sup>

The court could have stopped here. Instead, it went on to consider whether abandonment of the property would violate a state statute or regulation, and if so, whether that statute was reasonably designed to protect the public health and safety from imminent and identifiable harm.<sup>181</sup> The court assumed, *arguendo*, that the site violated ISRA. Was ISRA reasonably designed to protect the public health and safety from imminent and identifiable harm?<sup>182</sup> The court concluded ISRA's purposes were much broader. Moreover, the DEP did not allege violations of particular sections of ISRA specifically intended to protect the public health and safety. Therefore, that prong was not satisfied. Because no exception to abandonment was present, the trustee could abandon the property. The court did

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<sup>176</sup> *Id.* at 739–40.

<sup>177</sup> *Id.* at 739. Most courts who narrowly construe the exception to abandonment power permit abandonment because no imminent and identifiable harm to public health or safety exists. See *In re Smith-Douglass, Inc.*, 856 F.2d at 16 (permitting abandonment when estate had no unencumbered assets and property did not pose serious public health or safety risk); *In re Sheffield Oil Co.*, 162 B.R. 339, 341 (Bankr. M.D. Ala. 1993) (finding trustee was not required to spend estate funds to assess underground petroleum tanks absent evidence of contamination); *In re Better-Brite Plating, Inc.*, 105 B.R. 912, 917 (Bankr. E.D. Wis. 1989) (allowing abandonment because estate did not possess enough unencumbered assets to fund cleanup and no evidence existed of imminent harm or danger to public).

<sup>178</sup> *In re St. Lawrence Corp.*, 248 B.R. at 742.

<sup>179</sup> *Id.* at 743.

<sup>180</sup> See *N.M. Env'tl. Dep't v. Foulston (In re L.F. Jennings Oil Co.)*, 4 F.3d 887, 890 (10th Cir. 1993) (stating despite oil contamination, there was no immediate threat to public health or safety because site was not listed on state contaminated site list and state's expert could not state positively if threat existed); *In re Anthony Ferrante & Sons, Inc.*, 119 B.R. 45, 50 (D.N.J. 1990) (noting despite bacterial contamination of public water supply system, no imminent danger existed because public knew of danger and had means to protect itself); *In re Brio Ref., Inc.*, 86 B.R. 487, 489 (N.D. Tex. 1988) (holding trustee could abandon site listed on NPL because no evidence showed imminent identifiable risk to public); *In re Purco, Inc.*, 76 B.R. 523, 533 (W.D. Pa. 1987) (finding no evidence drums of cut-back asphalt and thinners were hazardous, and even if they were, no evidence they presented risk of harm or threat to public safety).

<sup>181</sup> *In re St. Lawrence Corp.*, 248 B.R. at 743–44.

<sup>182</sup> *Id.* at 743. Other cases hold state law only needs to be considered. See *In re Okla. Ref. Co.*, 63 B.R. 562, 565 (Bankr. W.D. Okla. 1986) (taking position Supreme Court did not intend to put bankruptcy trustees in position where they could not comply with state law: rather Court simply wanted bankruptcy courts to consider state environmental laws when ruling on abandonment).

not reach the question of whether the statute was so onerous as to interfere with administration of the bankruptcy case.<sup>183</sup>

Another court posited a five-part inquiry for abandonment: "(1) the imminence of danger to the public health and safety; (2) the extent of probable harm; (3) the amount and type of hazardous waste; (4) the cost to bring the property into compliance with environmental laws; and (5) the amount and type of funds available for cleanup."<sup>184</sup> Yet another court stated a presumption against abandonment subject to three exceptions:

1. the environmental law in question is so onerous as to interfere with the bankruptcy adjudication itself; or
2. the environmental law in question is not reasonably designed to protect the public health or safety from identified hazards; or
3. the violation caused by abandonment would be merely speculative or indeterminate.<sup>185</sup>

Finding that none of the exceptions applied, the court denied the trustee's motion to abandon. The trustee's compliance with CERCLA might deplete the estate, preclude any distribution to the unsecureds, and vastly reduce the payout to other administrative claimants, but exhaustion of estate assets would not make compliance with the law so onerous as to interfere with the bankruptcy adjudication. After all, "the normal course of affairs in any chapter 7 is to deplete the estate by liquidating it and distributing it to creditors as required by law."<sup>186</sup> The harm was immediate and of the kind Congress intended to prevent by enacting CERCLA. Finally, the presence of the hazardous materials was not a speculative or indeterminate violation but an ongoing violation of CERCLA. Because the estate was the owner of the site and could not abandon it, it was liable under CERCLA as an owner. "[T]he trustee had a duty to expend all the unencumbered assets of the

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<sup>183</sup> *In re St. Lawrence Corp.*, 248 B.R. at 744. Some courts have concluded that an environmental statute is so onerous as to interfere with bankruptcy administration when the estate has no assets to effect a cleanup. See, e.g., *Borden v. Wells-Fargo Bus. Credit (In re Smith-Douglass, Inc.)*, 856 F.2d 12, 16 (4th Cir. 1988) (noting abandonment permitted in part because there were no unencumbered assets to fund cleanup); *In re Better-Brite Plating, Inc.*, 105 B.R. 912, 917 (Bankr. E.D. Wis. 1989) (finding abandonment permitted in part because estate did not possess enough unencumbered assets to fund cleanup).

<sup>184</sup> *In re Franklin Signal Corp.*, 65 B.R. 268, 272 (Bankr. D. Minn. 1986).

<sup>185</sup> *In re Peerless Plating Co.*, 70 B.R. 943, 947 (Bankr. W.D. Mich. 1987); see, e.g., *Anthony Ferrante & Sons, Inc.*, 119 B.R. at 49 (asserting trustee may not abandon property in contravention of state law unless one of three exceptions applies); *In re Microfab, Inc.*, 105 B.R. 161, 169 (Bankr. D. Mass. 1989) (discussing full compliance with state environmental laws is subject to these three limits).

<sup>186</sup> *In re Peerless Plating Co.*, 70 B.R. at 947; see *New York v. Quanta Res. Corp. (In re Quanta Res. Corp.)*, 739 F.2d 912, 915 (3d Cir. 1984) (describing purpose of chapter 7 proceeding); Richard B. Paige, *In re Quanta Resources Corp.: Bankruptcy Policy v. Environmental Interests; A Polluted Judicial Theory*, 59 AM. BANKR. L. J. 357, 357 (1985) (asserting chapter 7 liquidation's paramount purpose is expeditious reduction of estate assets into cash to distribute to creditors).

estate in remedying the situation, as required by *Midlantic*.<sup>187</sup>

### E. Significance of Abandonment Issue: Much Ado About Nothing?

As noted, when all is said and done, the debate about the trustee's abandonment power is really a debate about who will pay for the cleanup. If the trustee cannot abandon a site, it remains part of the estate. 28 U.S.C. § 959(b) requires those who operate and manage property to comply with all valid state laws.<sup>188</sup> Courts have understood this to require the trustee to remediate the property or accord administrative expense priority to the party who fulfills the trustee's obligations.<sup>189</sup>

But, as one court remarked, abandonment of the property does not mean the estate is "abandoning" or shedding its environmental liability.<sup>190</sup> The estate is a person under CERCLA.<sup>191</sup> The estate owns the debtor's pre-petition assets. All persons who currently own or operate property containing hazardous substances are PRPs.<sup>192</sup> All persons who are former owners of property during the time of a disposal are also PRPs.<sup>193</sup> Therefore, the estate is a PRP and it remains liable as

<sup>187</sup> *In re Peerless Plating Co.*, 70 B.R. at 948-49.

<sup>188</sup> Section 959(b) of the United States Code provides:

[e]xcept as provided in section 1166 of title 11, a trustee, receiver or manager appointed in any case pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

28 U.S.C. § 959(b) (2000); see *In re Quanta Res. Corp.*, 739 F.2d at 919 (asserting section 959(b) embodies Congress's implicit goal of preserving state regulatory laws); *Wilner Wood Prods. Co. v. Me. Dept. of Envtl. Prot.*, 128 B.R. 1, 2 (Bankr. D. Me. 1991) (deciding section 959(b) evidences Congress' intent that debtors in possession comply with state environmental laws).

<sup>189</sup> See *In re Guterl Special Steel Corp.*, 198 B.R. 128, 135 (Bankr. W.D. Pa. 1996) (holding cleanup costs were administrative expense because trustee must comply with section 959(b) and cleanup preserved estate); *In re Stevens*, 68 B.R. 774, 781-82 (Bankr. D. Me. 1987) (deciding cleanup costs are administrative expense because trustee may not abandon hazardous waste and section 959(b) requires trustee to comply with environmental laws); *In re T.P. Long Chem., Inc.*, 45 B.R. 278, 286 (Bankr. N.D. Ohio 1985) (asserting estate cannot escape liability by abandoning, hence EPA is entitled to administrative expense priority for its cleanup).

<sup>190</sup> See *In re T.P. Long Chem., Inc.*, 45 B.R. at 284-85 (stating "[s]ubsequent abandonment or transfer of drums does not transfer estate's liability"); see also *In re Stevens*, 68 B.R. at 781 (holding cleanup of hazardous waste remains responsibility of estate even if property is abandoned).

<sup>191</sup> See *In re Stevens*, 68 B.R. at 779 (stating "the debtor, and hence the debtor's estate, is a person as defined under CERCLA") (quoting *In re T.P. Long Chem., Inc.*, 45 B.R. at 284); see also 42 U.S.C. § 9601(21) (2000) (defining "person" as "an individual, firm, corporation, association, partnership, consortium, joint venture, commercial entity, United States Government, State, municipality, commission, political subdivision of a State, or any interstate body.").

<sup>192</sup> See 42 U.S.C. § 9607(a)(1) (2000); see also Kathryn R. Heidt, *Product Liability, Mass Torts and Environmental Obligations in Bankruptcy: Suggestions for Reform*, 3 AM. BANKR. INST. L. REV. 117, 139 (1995) ("Environmental law presently requires the current owner or operator, or the debtor to clean up the property."); Kathryn R. Heidt, *The Automatic Stay In Environmental Bankruptcies*, 67 AM. BANKR. L.J. 69, 110 (1993) ("The obligation to cleanup is a new obligation that arises every day because the current owner or operator of the property is liable for cleanup.").

<sup>193</sup> See 42 U.S.C. § 9607(a)(2); see also *In re CMC Heartland Partners*, 966 F.2d 1143, 1145 (7th Cir. 1992) (describing language of section 107(a)(2)); John P. Berkery, Comment, *The Dischargeability of*

such even if the trustee abandons property. As one court explained:

Mere abandonment by the trustee is not the ultimate goal sought by the trustee. The ultimate goal is to escape the estate's obligation to the E.P.A. under CERCLA. Abandonment is viewed as a means to this end . . . .

If the drums were abandoned, they would cease to be the property of the estate and the estate's interest therein would revert to the debtor. It does not necessarily follow, however, that the estate's liability for the environmental damage caused by the drums would also be transferred to the debtor. Although the drums are the source of the estate's liability under CERCLA, that liability cannot simply be transferred with the drums . . . .

[O]nce the drums became property of the estate, the estate became potentially liable under CERCLA. This liability is based on the estate's relationship to the drums, but is independent of the drums themselves. Subsequent abandonment or transfer of the drums does not transfer the estate's liability.<sup>194</sup>

A bankruptcy estate *is* a separate judicial entity. Therefore, it *is* a person under CERCLA. A bankruptcy estate *owns* all property the debtor owned as of the commencement of its case.<sup>195</sup> As an owner of a contaminated site, the estate is a PRP under CERCLA in its own right. Therefore, isn't the abandonment debate much ado about nothing? Even if an estate can abandon toxic property, doesn't it remain liable under CERCLA as a PRP?

The answer depends on the legal significance of the abandonment of property. If title to abandoned property "revests . . . retroactively to the date of the commencement of the case,"<sup>196</sup> the estate is deemed never to have owned the property. If the estate never owned the property, the estate cannot be a PRP in its own right. According to the Supreme Court in *Sessions v. Romadka*,<sup>197</sup> "the abandonment relates back to the commencement of the proceedings in bankruptcy,

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*CERCLA Cleanup Costs Incurred After Bankruptcy*, 9 BANKR. DEV. J. 417, 420–21 (1992) (discussing potential liability of PRPs).

<sup>194</sup> *In re T.P. Long Chem., Inc.*, 45 B.R. at 284–85.

<sup>195</sup> See 11 U.S.C. § 541(a)(1) (2000) (stating "estate is comprised of . . . all legal or equitable interests of the debtor in property as of the commencement of the case"); see also *Tidewater Fin. Co. v. Moffett* (*In re Moffett*), 356 F.3d 518, 521 (4th Cir. 2004) (noting section 541(a)(1)'s broad scope reflects Congress's desire to facilitate a debtor's financial rehabilitation); *In re Commodore Bus. Machines, Inc.*, 180 B.R. 72, 82 (Bankr. S.D.N.Y. 1995) (discussing difference between legal and equitable interests in property for purposes of section 541).

<sup>196</sup> *In re Peerless Plating Co.*, 70 B.R. 943, 948 (Bankr. W.D. Mich. 1987).

<sup>197</sup> 145 U.S. 29 (1892).



and the title stands as if no assignment had been made."<sup>198</sup> Sessions held that title reverts retroactively into the debtor upon abandonment. It establishes that if property is abandoned, the estate would *not* be an owner for purposes of CERCLA. The estate would not be a current owner, and would not be a former owner, because legally, it is treated as if it never owned the property at all. Therefore, the estate would *not* incur independent liability under CERCLA if abandonment were permitted.

Few courts consider the legal significance of abandonment in their analysis. Is that because it is so obvious that it does not bear repeating? One thinks not. If it were a given, we would not have cases like *T.P. Long Chemical* in which the court concluded that abandonment of the property would not eliminate the estate's liability under CERCLA.<sup>199</sup>

Assuming the Supreme Court's pronouncement in 1892 remains valid today, the issue of abandonment is, in fact, much ado about a lot. If a debtor, as of the commencement of its case, has an ownership interest in the toxic site, the estate becomes an owner. As an owner, the estate incurs its own separate CERCLA liability. This means the EPA or other environmental claim holder has two claims: one against the (pre-petition) debtor and another against the estate. The claim against the estate may qualify as an administrative expense because it only arises post-petition and it is an actual, necessary expense of preserving the estate. If the estate is permitted to abandon the property, and abandonment retroactively reverts the property in the debtor, the EPA or other environmental claim holder has one claim—against the debtor—and it is a pre-petition, nonpriority, typically unsecured claim entitled to pennies on the dollar on a lucky day.

With the exception of the two opinions noted above,<sup>200</sup> courts have not discussed an estate's CERCLA liability. No one has considered whether an estate can assert the innocent owner defense.

### III. TREATMENT OF ENVIRONMENTAL OBLIGATIONS IN BANKRUPTCY

#### A. Introduction

Ironically, many trees have died in the name of determining whether a governmental unit [hereinafter "government" or "State"] holds a claim in a debtor's bankruptcy and if so, the nature of that right to payment—is it a pre-petition claim, and hence dischargeable, or a post-petition right to payment entitled to administrative expense priority, or both? It is very easy to get confused in and by this case law. We do our best to shed a little light onto this dark corner of the law.

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<sup>198</sup> *Id.* at 51–52 (emphasis added). The *Peerless* court cited to *In re Tarpley*, 4 B.R. 145, 146 (Bankr. M.D. Tenn. 1980), for the proposition that abandonment retroactively reverts title in the debtor as of the commencement of the case. *In re Peerless Plating Co.*, 70 B.R. at 948. The *Tarpley* court, in turn, cited to *Sessions*. *In re Tarpley*, 4 B.R. at 146.

<sup>199</sup> *In re T.P. Long Chem., Inc.*, 45 B.R. at 284–85.

<sup>200</sup> See *In re Peerless Plating Co.*, 70 B.R. at 948; *In re T.P. Long Chem., Inc.*, 45 B.R. at 284.

We begin with the Supreme Court's pronouncements (or lack thereof) on the issue.

## B. *Ohio v. Kovacs*

The question presented in *Ohio v. Kovacs*<sup>201</sup> was easy. The Court left all the hard questions unanswered.

### 1. What *Kovacs* Decided

Mr. Kovacs was the CEO and stockholder of Chem-Dyne Corporation which, along with other companies, operated an industrial and hazardous waste disposal site in Ohio.<sup>202</sup> The State of Ohio sued him and the companies "for polluting public waters, maintaining a nuisance, and causing fish kills."<sup>203</sup> The parties settled the lawsuit. Mr. Kovacs signed a stipulation that enjoined all the parties from further pollution, prohibited them from bringing additional wastes to the site, and required them to remove the wastes. The stipulation further ordered a \$75,000 compensatory payment for injury to wildlife.<sup>204</sup> The defendants did not comply with their obligations. The State of Ohio had a receiver appointed. The receiver was to take possession of all property and assets of all the defendants and clean up the site. Mr. Kovacs petitioned for bankruptcy relief after the receiver took possession but before the receiver had completed the tasks assigned.

The State wanted to attach Mr. Kovacs' post-petition income to help pay for the cleanup. It filed a motion in state court to discover his income and assets. The bankruptcy court, pursuant to Mr. Kovacs' request, stayed those proceedings.<sup>205</sup> The State then asked the bankruptcy court to declare that "Kovacs' obligation under the stipulation and judgment order to clean up the Chem-Dyne site was not dischargeable in bankruptcy because it was not a 'debt.'"<sup>206</sup>

The State argued that "debt" is defined as liability on a claim. "Claim" is limited to rights to payment or rights to an equitable remedy for breach of performance if such breach gives rise to a right to payment.<sup>207</sup> According to the State, Kovacs' cleanup obligation was not a claim because: (1) Kovacs' default

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<sup>201</sup> 469 U.S. 274 (1985).

<sup>202</sup> *Id.* at 276.

<sup>203</sup> *Id.*

<sup>204</sup> *Id.*

<sup>205</sup> *Id.*

<sup>206</sup> *Id.* at 277.

<sup>207</sup> 11 U.S.C. § 101(5) (2000). At the time, 11 U.S.C. § 101(4) defined "claim." Today, section 101(5) controls. The statute states: "claim" means—(A) right to payment . . . ; or (B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment." See *Kovacs*, 469 U.S. at 278–79 ("Congress desired a broad definition of a 'claim' that could include statutory remedies that required clean up of waste sites); *United States v. Union Scrap Iron & Metal*, 123 B.R. 831, 835 (Bankr. D. Minn. 1990) ("A claim exists only when the pre-bankruptcy relationship between the debtor and third party contained all the elements necessary to give rise to a legal obligation under the relevant substantive non-bankruptcy law.").

breached a statute, not a contract; and (2) breach of his statutory obligation did not give rise to a right to payment.

The Court gave short shrift to the first argument. The definition of "claim" does not limit a debtor's breach of performance to contractual arrangements. A debtor can fail to perform, i.e., "breach," a statutory obligation just as it can breach a contract obligation. Among other things, the State had ordered Mr. Kovacs to pay \$75,000 for injury to wildlife. The order to pay \$75,000 was to remedy Mr. Kovacs' failure to perform his statutory duties. The State freely admitted that Kovacs' failure to pay the \$75,000 gave rise to a dischargeable debt; thus, there was no reason to treat the clean up order to remedy the statutory violation any differently.<sup>208</sup>

Moreover, Kovacs' breach gave rise to a right to payment even though it was not stated as a monetary obligation. The only performance sought from Kovacs was "the payment of money."<sup>209</sup>

The injunction surely obliged Kovacs to clean up the site. But when he failed to do so, rather than prosecute Kovacs under the environmental laws or bring civil or criminal contempt proceedings, the State secured the appointment of a receiver, who was ordered to take possession of all of Kovacs' nonexempt assets as well as the assets of the corporate defendants and to comply with the injunction entered against Kovacs. As wise as this course may have been, it dispossessed Kovacs, removed authority over the site, and divested him of assets that might have been used by him to clean up the property. Furthermore, when the bankruptcy trustee sought to recover Kovacs' assets from the receiver, the latter sought an injunction against such action. Although Kovacs had been ordered to "cooperate" with the receiver, he was disabled by the receivership from personally taking charge of and carrying out the removal of wastes from the property. What the receiver wanted from Kovacs after bankruptcy was the money to defray the cleanup costs. At oral argument in this Court, the State's counsel conceded that after the receiver was appointed, the only performance sought from Kovacs was the payment of money. Had Kovacs furnished the necessary funds, either before or after bankruptcy, there seems little doubt that the receiver and the State would have been satisfied. On the facts before it, and with the receiver in control of the site, we cannot fault the Court of Appeals for concluding that the cleanup order had been converted into an obligation to pay money, an obligation that was dischargeable in bankruptcy.<sup>210</sup>

What does *Kovacs* teach us then? The State was seeking the payment of money

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<sup>208</sup> *Kovacs*, 469 U.S. at 279; see *In re Norwesco Dev. Corp.*, 68 B.R. 123, 129 (Bankr. W.D. Pa. 1986) (quoting *Kovacs*, 469 U.S. at 279); *In re S. Indus. Banking Corp.*, 46 B.R. 306, 312 (Bankr. E.D. Tenn. 1985) (quoting same).

<sup>209</sup> *Kovacs*, 469 U.S. at 283; *In re Indus. Salvage*, 196 B.R. 784, 787 (Bankr. S.D. Ill. 1996) (citing *Kovacs*, 469 U.S. at 283); *In re Norwesco Dev. Corp.*, 68 B.R. at 128 (pointing to *Kovacs*, 469 U.S. at 283).

<sup>210</sup> *Kovacs*, 469 U.S. at 282-83; see Baker, *supra* note 4, at 389 (discussing once "Kovacs' cleanup duty had been reduced to a monetary obligation, the monetary payment obligation sought from Kovacs was a liability on a claim that was dischargeable under the bankruptcy statute."); Kristy Kutz, *Who Is Going To Pay: CERCLA v. Bankruptcy*, 31 WASHBURN L.J. 573, 586 (1992) (explaining Kovacs could only comply with cleanup order by paying state because appointment of receiver dispossessed Kovacs of property).

from Mr. Kovacs even though it was not expressed as such. The right to payment was a "claim" for bankruptcy purposes even though it sprang from violating a statutory duty. Because the right to payment arose pre-petition, it was dischargeable in Mr. Kovacs' bankruptcy case.<sup>211</sup>

## 2. What *Kovacs* Did NOT Decide

The Court was careful to spell out what it had not decided. It had *not* held that Kovacs' discharge would shield him from prosecution for violation of Ohio's environmental laws. The discharge did *not* shield him from criminal contempt for not performing his obligations under the pre-bankruptcy injunction. The discharge did *not* discharge fines for violations of environmental laws because section 523(a)(7) excepted such fines from discharge. The Court went on:

Third, we do not address what the legal consequences would have been had Kovacs taken bankruptcy before a receiver had been appointed and a trustee had been designated with the usual duties of a bankruptcy trustee. Fourth, we do not hold that the injunction against further toxic wastes on the premises or against any conduct that will contribute to the pollution of the site or the State's waters is dischargeable in bankruptcy; we here address . . . only the affirmative duty to clean up the site and the duty to pay money to that end. Finally, we do not question that anyone in possession of the site—whether it is Kovacs or another in the event the receivership is liquidated and the trustee abandons the property, or a vendee from the receiver or the bankruptcy trustee - must comply with the environmental laws of the State of Ohio. Plainly, that person or firm may not maintain a nuisance, pollute the waters of the State, or refuse to remove the source of such conditions.<sup>212</sup>

The Supreme Court left it to the lower courts to decide what would happen if a state ordered a debtor to clean up, no receiver was appointed, and the debtor

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<sup>211</sup> As Thomas Salerno has noted, the Court could have reached the same result through a straightforward application of the definition of "claim." Salerno & Miller, *supra* note 22, at § 26.64. The State of Ohio had a right to a mandatory injunction and a right to payment of its cleanup costs. Therefore, it had a right to payment in the alternative for breach of its equitable remedy. See *River Place E. Hous. Corp. v. Rosenfeld* (*In re Rosenfeld*), 23 F.3d 833, 836 (4th Cir. 1994) (defining rights to payment which arise before debtor's bankruptcy as pre-petition debts and thus dischargeable); *In re Jimmo*, 204 B.R. 655, 660 (Bankr. D. Conn. 1997) (discussing how *Kovacs* determined "where the state essentially seeks from a debtor monetary payments to clean up a hazardous waste disposal site for the debtor's prepetition violation of state environmental laws, such payments are a liability on a claim under 11 U.S.C. § 101(5) and (12) and dischargeable under the bankruptcy statute.").

<sup>212</sup> *Kovacs*, 469 U.S. at 284–85; see *In re Alongi*, 272 B.R. 148, 156 (Bankr. D. Md. 2001) (citing *Kovacs*, 469 U.S. at 284); see also Francis E. Goodwyn, *Claims Estimation and the Use of the "Cleanup Trust" in Environmental Bankruptcy Cases*, 9 AM. BANKR. INST. L. REV. 769, 776–77 (2001) (discussing *Kovacs* and how Court limited its holding to facts of particular case, rather than disposing of potential issues).

petitioned for bankruptcy relief. It suggested that injunctions to abate further pollution would not be claims and whoever possessed a toxic site would have to comply with state environmental laws.

### C. Injunctive Relief

#### 1. Injunctive Relief: Does It Give Rise to a Claim?

The Court in *Kovacs* did not "hold that the injunction against further toxic wastes on the premises or against any conduct that will contribute to the pollution of the site or the State's waters is dischargeable in bankruptcy."<sup>213</sup> So, does injunctive relief regarding environmental matters give rise to a dischargeable claim? The courts disagree, just as they do on most issues involving environmental and bankruptcy law. The Sixth Circuit has held that injunctive relief gives rise to a dischargeable claim unless the debtor can comply without expending any funds.<sup>214</sup> The Third Circuit would likely hold that an injunction to prevent future harm does not give rise to a dischargeable claim, even if compliance with the injunction required the debtor to expend funds.<sup>215</sup>

The Second Circuit's answer depends on the nature of the injunctive relief sought. If the entity obtaining injunctive relief has an alternative right to payment, a claim exists.<sup>216</sup> This reasoning tracks the Bankruptcy Code's definition of claim.

<sup>213</sup> *Kovacs*, 469 U.S. at 285; see Goodwyn, *supra* note 212, at 776–77 (discussing how in *Kovacs*, Court limited its holding and did not fully address issue of whether injunction against further pollution is dischargeable); Kevin J. Saville, *Discharging CERCLA Liability in Bankruptcy: When Does a Claim Arise*, 76 MINN. L. REV. 327, 337 n.56 (1991) (writing Court in *Kovacs* "hinted that a debtor may not always be discharged from the responsibility to clean up environmental contamination").

<sup>214</sup> *In re Daniels*, 130 B.R. 239, 240–41 (Bankr. E.D. Ky. 1991) (discussing "an injunction requiring a person to reclaim a mining site was a debt dischargeable in bankruptcy to the extent that the party would have to expend money"); see *United States v. Whizco, Inc.*, 841 F.2d 147, 150–51 (6th Cir. 1988) (holding "to the extent that fulfilling his obligation to reclaim the site would force the defendant to spend money, the obligation was a liability on a claim as defined by the Bankruptcy Code"); see also *Kennedy v. Medicap Pharmacies, Inc.*, 267 F.3d 493, 496 (6th Cir. 2001) (citing *U.S. v. Whizco, Inc.*, 841 F.2d 147, 150–51 (6th Cir. 1988)).

<sup>215</sup> *Penn Terra Ltd. v. Pa. Dep't of Envtl. Res.*, 733 F.2d 267, 278 (3d Cir. 1984).

We believe that the inquiry is more properly focused in the nature of the injuries which the challenged remedy is intended to redress—including whether plaintiff seeks compensation for the past damages or prevention of future harm—in order to reach the ultimate conclusion as to whether these injuries are traditionally rectified by a money judgment and its enforcement.

*Id.*; see *Torwico Elec., Inc. v. N.J. Dep't of Envtl. Prot. (In re Torwico Elec., Inc.)*, 8 F.3d 146, 150 (3d Cir. 1993) (holding state's concern regarding present and future leaking of hazardous wastes was correct in forcing debtor to comply with applicable environmental laws by remedying existing hazards, rather than right to payment); *In re Norwesco Dev. Corp.*, 68 B.R. 123, 128 (Bankr. W.D. Pa. 1986) (questioning whether certain obligations imposed upon companies by state, such as providing water supply systems, are actually equivalent to money judgments).

<sup>216</sup> See *United States v. LTV Corp. (In re Chateaugay Corp.)*, 944 F.2d 997, 1008 (2d Cir. 1991) (explaining EPA injunction under CERCLA gives rise to claim because CERCLA gives EPA alternative right to payment); see also *Downtown Athletic Club of N.Y.C. v. Kremer*, No. M-47, 2000 WL 744126, at \*3 n.4 (Bankr. S.D.N.Y. 2000) (stating "order giving rise to injunctive relief is not a 'claim' if creditor has no

Thus, injunctive relief the EPA obtains under CERCLA gives rise to a dischargeable claim because CERCLA gives the EPA an alternative right to seek reimbursement of cleanup costs expended.<sup>217</sup> In contrast, injunctive relief the EPA obtains under RCRA will never give rise to a claim because RCRA only authorizes injunctive relief. It does not recognize an alternative right to payment.

The Second Circuit further distinguishes between injunctions that impose an obligation as an alternative to a right to payment and cleanup orders that seek to prevent future harm as well as to remedy past harms. The latter "dual objective" injunction does not constitute a claim:

It is true that, if in lieu of such an order, EPA had undertaken the removal itself and sued for the response costs, its action would have both removed the accumulated waste and prevented continued pollution. But it is only the first attribute of the order that can be said to remedy a breach that gives rise to a right to payment. Since there is no option to accept payment in lieu of continued pollution, any order that to any extent ends or ameliorates continued pollution is not an order for breach of an obligation that gives rise to a right of payment . . . .<sup>218</sup>

In the Second and Third Circuits, then, injunctive relief ordering the debtor to stop further pollution or contamination will not give rise to a dischargeable claim. Moreover, in the Second Circuit, no claim arises even when the injunctive relief seeks redress of past harms so long as it also orders future contamination to cease.

At first blush, these case law niceties appear to give environmental agencies an easy way to skirt the impact of bankruptcy. The question then becomes why the case reporters are not filled with courts minutely examining the entrails of specific orders for injunctive relief. One possible answer is that the strategy does not get the environmental agency very far. The specter of open-ended liability post-

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option to accept payment in lieu of enforcement of order" (citing *In re Chateaugay Corp.*, 944 F.2d at 1008); *In re Mitchell*, 249 B.R. 55, 59 (Bankr. S.D.N.Y. 2000) ("An equitable remedy, such as an injunction will 'give rise to a right to payment,' and therefore be discharged, if payment of a monetary obligation is an alternative to the equitable remedy" (quoting *Kovacs*, 469 U.S. at 282-83)).

<sup>217</sup> See *In re Chateaugay Corp.*, 944 F.2d at 1008 ("[I]f EPA directs LTV to remove some wastes that are not currently causing pollution, and if EPA could have itself incurred the costs of removing such wastes and then sued LTV to recover the response costs, such an order is a 'claim' under the Code."); Stephen P. Ferrey, *Allocation and Uncertainty in the Age of Superfund: A Critique of the Redistribution of CERCLA Liability*, 3 N.Y.U. ENVTL. L.J. 36, 43 (1994) (discussing how government acquires right to seek imbursement from PRPs for costs incurred and paid for cleanup); Saville, *supra* note 212, at 337 ("If the EPA eliminates environmental contamination and then seeks reimbursement for its efforts, the EPA's rights clearly represent a 'right to payment' that can be discharged in bankruptcy under Bankruptcy Code Section 101(5)(A).").

<sup>218</sup> *In re Chateaugay Corp.*, 944 F.2d at 1008; see Baker, *supra* note 4, at 396-97 (describing Second Circuit's decision as one which would render most environmental injunctions as non-claims, because they are not breaches of obligations, but orders to end pollution); Cahalane, *supra* note 92, at 273-74 (discussing injunctions which order cleanup and abatement of ongoing waste as not embodying alternative right to payment and therefore not constituting claim).

confirmation will prevent many debtors from "getting to confirmation." Moreover, the environmental agency wants the debtor to clean up or pay up. The latter creates a claim—a right to payment. Furthermore, a claim is also created if the debtor's choice is to "clean-up-or-in-the-alternative, pay-up."

## 2. Injunctive Relief: Does It Violate the Stay?

Surprisingly, the courts mostly agree in this area. An injunction is exempt from the stay even if it orders a debtor to remediate a site and compliance with the order will require the debtor to expend funds.<sup>219</sup> The primary issue is whether the governmental unit is enforcing its police or regulatory powers to collect a money judgment. Section 362(b)(4) excepts from the automatic stay the commencement or continuation of actions or proceedings by governmental units to enforce police or regulatory powers. Section 362(b)(5) reins in this exception by establishing that the stay *does* apply (or the exception does not) if the governmental unit is seeking to enforce a money judgment.

What does "enforcement of a money judgment" entail? The Code does not define the phrase. In *Penn Terra Ltd. v. Pennsylvania Department of Environmental Resources*, the Third Circuit inferred that Congress meant to incorporate the commonly understood meaning of the term "money judgment."<sup>220</sup> A "money judgment" involves "(1) an identification of the parties for and against whom judgment is being entered, and (2) a definite and certain designation of the amount which plaintiff is owed by defendant."<sup>221</sup> Enforcement of a money judgment

<sup>219</sup> See, e.g., *Penn Terra Ltd. v. Pa. Dep't of Env'tl. Res.*, 733 F.2d 267, 278 (3d Cir. 1984); accord *New York v. Mirant N.Y., Inc.*, 300 B.R. 174, 179 (Bankr. S.D.N.Y. 2003) (determining consent decree between state and power plant was not subject to stay despite possible future expenditures); *N.J. Dep't of Env'tl. Prot. & Energy v. Madison Indus., Inc. (In re Madison Indus., Inc.)*, 161 B.R. 363, 366 (Bankr. D.N.J. 1993) (finding N.J. DEPE injunction excepted from stay against chemical manufacturer); *In re Laurinburg Oil Co.*, 49 B.R. 652, 654 (Bankr. M.D.N.C. 1984) (holding stay did not protect debtor from state injunction to abate violations of state water laws). But see Kathryn R. Heidt, *The Automatic Stay in Environmental Bankruptcies*, 67 AM. BANKR. L.J. 69, 90–91 (1993) (criticizing principle as perversion of Code). See generally Janette Brimmer, *Environmental Issues in Bankruptcy: An Overview*, 3 WIS. ENVTL. L.J. 159, 163–66 (1996) (providing overview of section 362 automatic stay provision and effect of *Penn Terra* precedent on it).

<sup>220</sup> *Penn Terra Ltd.*, 733 F.2d at 274–75; see *NLRB v. Amax Coal Co.*, 453 U.S. 322, 328–30 (1981) (presenting principle of inferring commonly understood meaning as definition of Code term); *Mirant*, 300 B.R. at 179–82 (adhering to *Penn Terra* interpretation of "money judgment."); *Eaves v. Cape May*, 239 F.3d 527, 532–33 (3d Cir. 2001) (stating "money judgment" is term of art with clear inference). But see *Kovacs*, 469 U.S. at 283 n.11 (purporting to distinguish *Penn Terra* despite holding clean up order was dischargeable in bankruptcy); Douglas P. Demoss, Note, *The Bankruptcy Code and Hazardous Waste Cleanup: An Examination of the Policy Conflict*, 27 WM. & MARY L. REV. 165, 181–82 (1985) (arguing *Penn Terra* holding broad and inappropriate).

<sup>221</sup> *Penn Terra Ltd.*, 733 F.2d at 275; see *Friends of Sakonnet v. Dutra*, 125 B.R. 69, 71–72 (Bankr. D.R.I. 1991) (quoting *Penn Terra* and applying definition); Michael Bentley Guss, *Ohio v. Kovacs: The Conflict Between Federal Bankruptcy Laws and State Environmental Regulations*, 34 AM. U. L. REV. 1263, 1292–94 (1985) (analyzing judicial development of injunction and equitable remedy). But see *Associated Gen. Contractors of Ohio, Inc. v. Drabik*, 250 F.3d 482, 489 (6th Cir. 2001) (characterizing continued reliance on *Penn Terra* holding as puzzling).

involves a proceeding in which the plaintiff tries to seize the defendant's assets to satisfy the judgment.<sup>222</sup>

The Department of Environmental Resources (DER) order required the debtor, the operator of coal surface mines, to rectify its violations of state environmental laws. The debtor was required to backfill, remove water from pits, restore and revegetate land.<sup>223</sup> According to the Third Circuit, the DER brought its action in equity. It did not seek payment or compensation, and, therefore, the proceeding could not have resulted in "adjudication of liability for a sum certain, an essential element of a money judgment."<sup>224</sup> Moreover, the government did not intend to obtain a money judgment in fact. According to the court, an important factor in identifying whether a proceeding is one to enforce a money judgment is "whether the remedy would compensate for *past* wrongful acts resulting in injuries already suffered, or protect against potential *future* harm."<sup>225</sup> It is not possible to liquidate damages yet to be suffered or calculate such sums with the requisite certainty.<sup>226</sup> If the court were to hold that any order requiring the expenditure of money were a money judgment, then the government police action exception would be narrowed "into virtual nonexistence."<sup>227</sup> The court observed that "almost everything costs something."<sup>228</sup> Moreover, the court held that

Congress recognized that in some circumstances, bankruptcy policy must yield to higher priorities. Indeed, if the policy of preservation of the estate is to be invariably paramount, then one could not have exceptions to the rule. Since Congress did provide for exceptions, however, we may assume that the goal of

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<sup>222</sup> *Penn Terra Ltd.*, 733 F.2d at 275. *But see Kovacs*, 469 U.S. at 283 n.11 (finding requested relief indistinguishable from enforcement of money judgment). *See generally* Roger D. Colton et al., *Seven-Cum-Eleven: Rolling the Toxic Dice in the U.S. Supreme Court*, 14 B.C. ENVTL. AFF. L. REV. 345, 352-66 (1987) (analyzing treatment of enforcement of money judgment under *Penn Terra* and *Kovacs*).

<sup>223</sup> *Penn Terra Ltd.*, 733 F.2d at 270; *see Mirant*, 300 B.R. at 174, 179-80 (finding automatic stay did not apply to post-petition consent decree); *In re Madison Indus. Inc.*, 161 B.R. at 364-67 (holding open fertilizer pile was danger to health, safety and welfare of public and not subject of stay); *Friends of the Sakonnet*, 125 B.R. at 70 (holding analysis also applied to injunction coupled with modified attached order to garnish debtor's income).

<sup>224</sup> *Penn Terra Ltd.*, 733 F.2d at 275. *But see Kovacs*, 469 U.S. at 281 n.9 (affirming bankruptcy court's finding that debt is dischargeable if debtor cannot perform without paying money). *See generally* Guss, *supra* note 221, at 1292-97 (providing overall view of struggle to define term).

<sup>225</sup> *Penn Terra Ltd.*, 733 F.2d at 277; *see Commonwealth Oil Ref. Co. v. U.S. Env'tl. Prot. Agency (In re Commonwealth Oil Ref. Co. Inc.)*, 805 F.2d 1175, 1187-88 (5th Cir. 1986) (compelling debtor to comply with EPA laws despite injunction's action); *Patterson v. Newspapers & Mail Deliverers' Union*, 138 B.R. 149, 153-54 (Bankr. S.D.N.Y. 1992) (finding contributions toward Administrator's Fund were not remedies for past injury). *See generally* Jill Thompson Losch, *Bankruptcy vs. Environmental Obligations: Clash of the Titans*, 52 LA. L. REV. 137, 153-56 (1991) (analyzing distinction between future and past injury).

<sup>226</sup> *Penn Terra Ltd.*, 733 F.2d at 277. *But see* Jeffrey S. Theuer, *Aligning Environmental Policy and Bankruptcy Protection: Who Pays for Environmental Claims Under the Bankruptcy Code?*, 13 T.M. COOLEY L. REV. 465, 494-96 (arguing in many situations, no functional distinction exists between past and future harm). *See generally* Guss, *supra* note 221, at 1271-75 (articulating basics of chapter 7 liquidation).

<sup>227</sup> *Penn Terra Ltd.*, 733 F.2d at 277-78; *see In re Commonwealth Oil Ref. Co.*, 805 F.2d at 1186 (citing *Penn Terra*); *Mirant*, 300 B.R. at 180 (quoting *Penn Terra*).

<sup>228</sup> *Penn Terra Ltd.*, 733 F.2d at 278; *see In re Commonwealth Oil Ref. Co.*, 805 F.2d at 1186 (citing *Penn Terra*); *In re Madison Indus., Inc.*, 161 B.R. at 367 (quoting *Penn Terra*).



preserving the debtor's estate is not always the dominant goal.<sup>229</sup>

The court emphasized that a remedy attempts to enforce a money judgment if it seeks compensation for past damages. It is not, however, an attempt to enforce a money judgment if it seeks to prevent future harm:<sup>230</sup>

Here, the Commonwealth Court injunction was, neither in form nor substance, the type of remedy traditionally associated with the conventional money judgment. It was not intended to provide compensation for past injuries. It was not reducible to a sum certain. No monies were sought by the Commonwealth as a creditor or obligee. The Commonwealth was not seeking a traditional form of damages in tort or contract, and the mere payment of money, without more, even if it could be estimated, could not satisfy the Commonwealth Court's direction to complete the backfilling, to update erosion plans, to seal mine openings, to spread topsoil, and to implement plans for erosion and sedimentation control. Rather, the Commonwealth Court's injunction was meant to prevent future harm to, and to restore, the environment.<sup>231</sup>

The distinction between an equitable action to prevent future harm and one to compensate for past damages is a slippery one. Moreover, one injunction may possess both components. For example, an order to stop further contamination and to remediate a site involves both. Will the stay apply to enjoin its enforcement? Arguably, the case law analyzing whether an injunction gives rise to a claim would also determine if the stay enjoins enforcement of the injunction.

#### D. When Does Environmental Liability Arise?

Assuming a claim—a right to payment—exists, the next critical question is *when* does the claim arise? If it arises pre-petition, the claim holder is a creditor and the debt is discharged.<sup>232</sup> Debts that arise pre-confirmation against a chapter 11

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<sup>229</sup> *Penn Terra Ltd.*, 733 F.2d at 278. See *City of New York v. Quanta Res. Corp.* (In re Quanta Res. Corp.), 739 F.2d 912, 921 (3d Cir. 1984) (articulating need to balance state and federal concerns when considering abandonment); Guss, *supra* note 221, at 1296–99 (explaining why courts must balance state and federal interests when deciding whether bankruptcy policy should yield); Joseph F. Lafleur, *Hazardous Waste Removal, State Court Injunctions, and the Bankruptcy Code: Ohio v. Kovacs*, 105 S.Ct. 705 (1985), 54 U. CIN. L. REV. 1101, 1108–10 (arguing *Kovacs* is flawed because Court failed to balance state and federal concerns).

<sup>230</sup> *Penn Terra Ltd.*, 733 F.2d at 275; see *In re Commonwealth Oil Ref. Co.*, 805 F.2d at 1187–88 (finding action to compel compliance with environmental laws is not attempt to enforce money judgment). But see Losch, *supra* note 225, at 153–56 (arguing remedy in *Penn Terra* actually redressed past harm).

<sup>231</sup> *Penn Terra Ltd.*, 733 F.2d at 278.

<sup>232</sup> 11 U.S.C. § 727(b) (2000); see Buckmaster de Wolf, Note, *Strange Things are Afoot at the Circle K: Agency Action Against Leased Sites in Environmental Bankruptcy*, 21 B.C. ENVTL. AFF. L. REV. 145, 151–52, 161–64 (1993) (analyzing claims arising pre-petition); Losch, *supra* note 225, at 171–72 (discussing resulting discharge).

debtor are discharged upon confirmation of the plan.<sup>233</sup>

The ability to discharge debt is the principal reason debtors seek bankruptcy relief. CERCLA's primary goals are to preserve the right to collect and to actually collect environmental debts. In this area, the irresistible force of environmental aims meets the immovable object of bankruptcy goals.

In addition to the pull and tug of competing policies, two other factors are at work here. First, courts are concerned with fairness. Those with rights to payment are entitled to fair notice—due process—before their rights are taken away, i.e., discharged. Second, many courts are trying to heed the Supreme Court's directive to harmonize, when possible, bankruptcy and environmental laws. Today, many courts seem to agree. A claim exists when the debtor's conduct gives rise to the claim and a relationship exists between the parties which indicates that the right to payment, even for future response costs, was in the parties' contemplation.<sup>234</sup> If the conduct and the requisite relationship both exist pre-petition, the environmental obligor holds a pre-petition, dischargeable claim.

The following briefly recounts the evolution of "claims jurisprudence" regarding environmental obligations in bankruptcy.

## 1. Claim Exists When Right to Payment Exists

*United States v. Union Scrap Iron & Metal*<sup>235</sup> illustrates one extreme. The court held "a claim exists only when the pre-bankruptcy relationship between the debtor and third party contained all the elements necessary to give rise to a legal obligation under the relevant substantive non-bankruptcy law."<sup>236</sup> Under this view, a claim does not exist until the claimant has an enforceable right to payment under applicable non-bankruptcy law.<sup>237</sup> In *Union Scrap*, the government brought an

<sup>233</sup> 11 U.S.C. § 1141(d)(1)(A) (2000); see Hon. Leif M. Clark, *Chapter 11—Does One Size Fit All?*, 4 AM. BANKR. INST. L. REV. 167, 192 n.152 (1996) (reciting three conditions necessary for confirmation to operate as discharge). But see *Shapiro v. Gherman* (*In re Gherman*) 103 B.R. 326, 330 (Bankr. S.D. Fla. 1989) (denying discharge to debtor who attempted to defraud system).

<sup>234</sup> *In re Nat'l Gypsum Co.*, 139 B.R. 397, 407 (N.D. Tex. 1992).

True, EPA does not yet know the full extent of the hazardous waste removal costs that it may one day incur and seek to impose upon LTV, and it does not yet even know the location of all the sites at which such wastes may yet be found. But the location of these sites, the determination of their coverage by CERCLA, and the incurring of response costs by EPA are all steps that may fairly be viewed, in the regulatory context, as rendering EPA's claim "contingent," rather than as placing it outside the Code's definition of "claim."

*Id.*; see *Ohio v. Kovacs*, 469 U.S. 274, 280 (1991) (finding debtor's obligation to clean hazardous waste disposal site gave rise to claim); Goodwyn, *supra* note 212, at 775–80 (2001) (analyzing what constitutes claim under Bankruptcy Code).

<sup>235</sup> 123 B.R. 831 (Bankr. D. Minn. 1990).

<sup>236</sup> *Id.* at 835.

<sup>237</sup> *Id.*; see *Avellino & Bienes v. M. Frenville Co. (In re M. Frenville Co.)* 744 F.2d 332, 337–38 (3d Cir. 1984) (illustrating Third Circuit's position third party defendant's claim, as well as its cause of action, arose post-petition because creditors' suit began fourteen months after debtor's involuntary chapter 7 was commenced). But see *Grady v. A.H. Robins Co.* 839 F.2d 198, 201 (4th Cir. 1988) (stating all courts outside Third Circuit have declined to follow *Frenville's* limited definition of claim).

action to recover response costs it had incurred to clean up a site the debtor had used but did not own. The debtor sought to dismiss the action arguing its chapter 11 proceeding had discharged the government's CERCLA claim. The debtor's plan preserved from discharge "allowed claims of all governmental units . . . arising out of alleged violations by the Debtor of federal or state environmental statutes and regulations in connection with the Debtor's operations at any of its facilities."<sup>238</sup> All other claims not filed and not allowed or scheduled were discharged.<sup>239</sup>

The EPA had not filed a claim in the debtor's bankruptcy, and the debtor's plan did not acknowledge its potential liabilities at the site concerned (Washington Avenue site). Notably, the EPA did not know the debtor had any relationship to that site.

The court analyzed the timing as to when a legal relationship existed between the debtor and the EPA under CERCLA, the relevant substantive non-bankruptcy law. A legal obligation under CERCLA involves four elements: "(1) there must be a facility; (2) there must be a release or threatened release of a hazardous substance at the facility; (3) there must be a responsible person; . . . and (4) the United States must have incurred necessary costs in responding to the release at the facility."<sup>240</sup> Because the EPA had not incurred any response costs at the time the debtor's plan was confirmed, the EPA did not have a claim in the debtor's bankruptcy proceedings, i.e., the debtor did not have a legal obligation to the EPA under CERCLA.<sup>241</sup>

The debtor maintained the pre-petition release gave rise to a *contingent* claim. The court disagreed. According to the court, a contingent claim requires a right to payment that is triggered by the occurrence of a future event "within the actual or presumed contemplation of the parties at the time the original relationship of the

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<sup>238</sup> *Union Scrap*, 123 B.R. at 835. See generally Dale Ellen Azaria, *When Is A Claim A Claim? Bankruptcy Code Riddle*, 62 TENN. L. REV. 205, 215 (1995) (noting issue before court was whether debtor's discharge in bankruptcy barred EPA from asserting post-petition response cost claim for pre-petition pollution); Jason V. Stitt, Note, *The Dischargeability of Environmental Claims in Bankruptcy: Resolution to Diametrically Opposed Goals*, 17 J. NAT. RESOURCES & ENVTL. L. 27, 36 (2003) (summarizing debtor's argument alleging its CERCLA liabilities were discharged when reorganization plan was confirmed because release of hazardous pollution occurred prior to plan confirmation).

<sup>239</sup> *Union Scrap*, 123 B.R. at 833-34. See generally John C. Ryland, Note, *When Policies Collide: The Conflict Between the Bankruptcy Code and CERCLA*, 24 MEM. ST. U. L. REV. 739, 763 (1994) (stating debtor argued its CERCLA liabilities were discharged under its chapter 11 reorganization); Stitt, *supra* note 238, at 36 (stating although debtor's bankruptcy reorganization plan was confirmed in 1985, debtor unsuccessfully argued its CERCLA liabilities were discharged when reorganization plan was confirmed).

<sup>240</sup> *Union Scrap*, 123 B.R. at 835; see, e.g., *United States v. Aceto Agric. Chems. Corp.*, 872 F.2d 1373, 1378-79 (8th Cir. 1989) (stating same); *United States v. Bliss*, 667 F. Supp 1298, 1304 (E.D. Mo. 1987) (stating same).

<sup>241</sup> *Union Scrap*, 123 B.R. at 836. See generally Ryland, *supra* note 239, at 763-64 (summarizing EPA's argument and court's eventual holding, and stating CERCLA liability did not arise until cleanup costs were incurred, and these costs were not dischargeable because they were not incurred until after debtor's bankruptcy); Stitt, *supra* note 238, at 37 (stating court attempted to balance goals of bankruptcy and environmental law by providing claims only arise when EPA expends funds).

parties was created."<sup>242</sup> The debtor maintained that the EPA had actual or presumed knowledge of the environmental hazards at the Washington Avenue site because the EPA had negotiated with the debtor regarding hazards at other sites. According to the court:

That the EPA can imagine hazards at [Debtor's] many facilities does not give rise to a presumption of knowledge of the hazards at the Washington Avenue site, especially when the debtor did not operate that site and the EPA did not know the debtor was in any way involved with that site . . . .<sup>243</sup>

The court noted that adopting the debtor's position that release or threatened release alone would establish a dischargeable claim would undermine CERCLA's goals. Furthermore, the court held that the policies underlying CERCLA supported preserving the debtor as a PRP:

First, Congress intended that the federal government be immediately given the tools necessary for a prompt and effective response to the problems of national magnitude resulting from hazardous waste disposal. Second, Congress intended that those responsible for problems caused by the disposal of chemical poisons bear the costs and responsibilities for remedying the harmful conditions they created.<sup>244</sup>

The court explained that adopting the debtor's position would require the government to reverse the CERCLA scheme:

If the EPA is forced to expend its resources on preserving its rights to eventual recovery against any [potentially responsible party] the EPA will have less ability to pursue its primary mission of cleaning the sites . . . Congress has directed the courts to be especially wary

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<sup>242</sup> *Union Scrap*, 123 B.R. at 836 (quoting *In re All Media Props., Inc.*, 5 B.R. 126, 133 (Bankr. S.D. Tex. 1980)); see, e.g., *United States v. LTV Corp. (In re Chateaugay Corp.)*, 944 F.2d 997, 1004 (2d Cir. 1991) (stating contingent claim must be within parties' contemplation at time of their original relationship); see also *Big Yank Corp. v. Liberty Mut. Fire Ins. Co. (In re Water Valley Finishing, Inc.)*, 139 F.3d 325 (2d Cir. 1998) (citing standard set forth in *In re Chateaugay*).

<sup>243</sup> *Union Scrap*, 123 B.R. at 836; see Patrick D. Shaw, *See No Evil, Speak No Evil: Discharging CERCLA Claims in Bankruptcy Without Notice*, 6 TUL. ENVTL. L.J. 127, 137 (1992) (quoting *Union Scrap* "imagine" language); see also Marion M. Walsh, *The Dischargeability of Post-Confirmation CERCLA Liability in Bankruptcy: In re Chateaugay and Beyond*, 1 N.Y.U. ENVTL. L.J. 95, 116 (1992) (paraphrasing *Union Scrap* court's "imagine" language).

<sup>244</sup> *Union Scrap*, 123 B.R. at 837 (quoting *U.S. v. Reilly Tar & Chem. Corp.*, 546 F. Supp. 1100, 1112 (Bankr. D.C. Minn. 1982)); see *Reilly Tar & Chem. Corp.*, 546 F. Supp. at 1112 (summarizing CERCLA's congressional legislative history); Michael P. Healy, *The Effectiveness and Fairness of Superfund's Judicial Review Preclusion Provision*, 15 VA. ENVTL. L.J. 271, 273 (1995) (quoting Reilly's enumeration of Congress's CERCLA goals).

of interfering with CERCLA work . . . in part because toxic waste sites threaten the public health and must be eradicated quickly.<sup>245</sup>

The *Union Scrap* definition of when a claim arises was too extreme. In a subsequent opinion, the Minnesota District Court itself discarded the "response costs" rule, focusing instead on when the party asserting the CERCLA claim had notice of the claim.<sup>246</sup>

Making "claim" and "cause of action" coterminous would also give CERCLA plaintiffs enormous power to manipulate the situation. Because a right of reimbursement does not exist under CERCLA until cleanup costs are incurred, a party could postpone any cleanup until after the debtor petitioned for bankruptcy relief. That would set the stage for administrative expense priority for the cleanup costs.

## 2. Claim Exists When Conduct Giving Rise to Liability Occurs

At the other extreme, a claim arises when the conduct giving rise to the liability occurs. If the debtor's conduct occurs pre-petition, the claim holder is a creditor and its right to payment is discharged even if the claim holder does not know it has a right to payment.<sup>247</sup> The Ninth Circuit Bankruptcy Appellate Panel's opinion in *In re*

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<sup>245</sup> *Union Scrap*, 123 B.R. at 838 (quoting *In re Combustion Equip. Assocs.*, 838 F.2d 35, 40 (2d Cir. 1988)); see *In re Combustion Equip. Assocs.*, 838 F.2d at 40 (discussing negative ramifications of EPA expending its resources preserving its right to eventual recovery based on bankruptcies as opposed to pursuing its primary mission). See generally *Wagner Seed Co. v. Daggett*, 800 F.2d 310, 315 (2d Cir. 1986) (stating Congress did not want to burden EPA with court proceedings that delayed its response to potential environmental disasters).

<sup>246</sup> See *Sylvester Bros. Dev. Co. v. Burlington N. R.R.*, 133 B.R. 648, 653 (Bankr. D. Minn. 1991) ("When the debtor has not disclosed its potential [environmental] liabilities in long-since closed bankruptcy proceedings, and the governmental agency has not had actual knowledge of the potential claim in sufficient time to file a claim in those proceedings, the potential claim is not discharged."). See generally Kerry H. Mithalal, Note, *Balancing CERCLA and the Bankruptcy Code: The Legitimacy of Discharging Contingent Claims for Unincurred Response Costs in Chapter 11*, 4 FORDHAM ENVTL. L. REP. 241, 247 n.48 (1993) (stating *Union Scrap* court shifted its attention from whether response costs had been incurred to whether creditor knew of claim's existence prior to close of debtor's bankruptcy); Stanley M. Spracker & James D. Barnette, *The Treatment of Environmental Matters in Bankruptcy Cases*, 11 BANKR. DEV. J. 85, 98 n.97 (1995) (stating Seventh Circuit did not follow *Union Scrap* test because rule hinged on whether response costs had been incurred would frustrate both bankruptcy court's interest in having all claims before it and CERCLA's goal of encouraging speedy cleanups).

<sup>247</sup> See generally *Gull Indus., Inc. v. John Mitchell Inc. (In re Hanna)*, 168 B.R. 386, 389 (B.A.P. 9th Cir. 1994) (holding although oil continued post-petition to passively leach into the soil, all environmental damage was deemed to occur pre-petition because acts giving rise to alleged liability, namely petroleum leaks, had occurred pre-petition); *In re Chateaugay Corp.*, 944 F.2d at 1005 (holding EPA's response costs under CERCLA were pre-petition claims dischargeable in bankruptcy, regardless of when they were incurred); *In re Biocoastal Corp.*, 147 B.R. 258, 260 (Bankr. M.D. Fla. 1992) (holding if debtor, as of petition date, had no interest in property allegedly contaminated, claim must be pre-petition, and thus, pre-petition purchaser of property held pre-petition, dischargeable claim); *In re Pierce Coal & Constr., Inc.*, 65 B.R. 521, 531 (Bankr. N.D.W. Va. 1986) (holding state's reclamation claim for pre-petition damages was pre-petition claim).

*Jensen*<sup>248</sup> best explains the rationale for this approach.<sup>249</sup> In *Jensen*, the Jensens owned a lumber company where they engaged in the process of dipping logs in fungicide tanks. The state water quality board inspected the site and declared it a hazardous waste problem. Shortly thereafter, the Jensens petitioned for chapter 7 relief. They did not list any claim for cleanup costs, and the state did not incur any cleanup costs during the proceeding. The Jensens received their discharge in 1984. The state came after them in 1989. They filed an adversary proceeding to determine if the state's claim for cleanup costs had been discharged.<sup>250</sup>

The court framed the issue as when the state's claim arose for purposes of bankruptcy.<sup>251</sup> It quoted the definition of claim and noted the legislative history establishing Congress's intent to give "claim" an expansive reading.<sup>252</sup> It further noted that neither *Kovacs* nor *Midlantic* discussed the issue.<sup>253</sup>

It criticized the *Frenville-Union Scrap* approach for not recognizing the possibility of a contingent right to payment even though the definition of "claim" expressly includes contingent rights to payment.<sup>254</sup> Applying the *Union Scrap*

<sup>248</sup> 127 B.R. 27 (B.A.P. 9th Cir. 1991).

<sup>249</sup> *In re Jensen*, 127 B.R. at 33 (holding threatened release of hazardous waste occurred pre-petition, making state government's claim dischargeable in debtor's bankruptcy). Given the facts, it is entirely possible to reach the same result using the more modern tests of conduct plus relationship and reasonable contemplation. See generally *In re Ritter Ranch Dev., L.L.C.*, 255 B.R. 760, 765 (B.A.P. 9th Cir. 2000) (stating fair contemplation test is equivalent of "conduct plus pre-petition relationship" test); *Lemelle v. Universal Mfg. Corp.*, 18 F.3d 1268, 1277 (5th Cir. 1994) (discussing *Jensen*'s assertion that not only must claimant and debtor have pre-petition relationship but claim must have been within parties' fair contemplation at time of debtor's bankruptcy).

<sup>250</sup> *In re Jensen*, 127 B.R. at 28; see Baker, *supra* note 4, at 400 n.151 (summarizing facts of *Jensen*); Myron A. Eng, Summary, *In re Jensen: Determining When A Bankruptcy Claim Arises in the Context of Environmental Liability*, 23 GOLDEN GATE U. L. REV. 259, 260-61 (1993) (summarizing facts of *Jensen*).

<sup>251</sup> *In re Jensen*, 127 B.R. at 29 (indicating further claim is one arising under CERCLA); *Cal. Dep't of Health Servs. v. Jensen (In re Jensen)*, 995 F.2d 925, 928 (9th Cir. 1993) (naming lower court in *Jensen* as one of many courts to consider when claim arises for bankruptcy environmental purposes); *In re Chi., Milwaukee, St. Paul & Pac. R.R.* 974 F.2d 775, 784 (7th Cir. 1992) (discussing possibility CERCLA claim arises at time of release or threatened release of hazardous substance in response to question of whether parties had pre-petition claim).

<sup>252</sup> *In re Jensen*, 127 B.R. at 29 (determining breadth of "claim" by examining intent of both House of Representatives and Senate); *In re Nat'l Gypsum Co.*, 139 B.R. 397, 405 (N.D. Tex. 1992) (explaining Congress's intent to interpret "claim" broadly so "all legal obligations of the debtor, no matter how remote or contingent will be able to be dealt with in the bankruptcy case"). For a general discussion on how various courts use the broad definition of "claim" in their holdings, see J. Ricky Arriola, *The Life & Times of a CERCLA Claim in Bankruptcy: An Examination of Hazardous Waste Liability in Bankruptcy Proceedings*, 67 ST. JOHN'S L. REV. 55 (1993).

<sup>253</sup> For discussion of *Kovacs* and *Midlantic* and why courts have not followed them, see *In re Jensen*, 127 B.R. at 29-30, and see also Eng, *supra* note 250, at 262-63, which explained that *Jensen* departed from *Kovacs* or *Midlantic* because neither addressed when bankruptcy claims arise. See generally *Midlantic Nat'l Bank v. N.J. Dep't of Envtl. Prot.*, 474 U.S. 494 (1986); *Ohio v. Kovacs*, 469 U.S. 274 (1985).

<sup>254</sup> *In re Jensen*, 127 B.R. at 31 (stating section 101(4) applies not only to rights vested in judgments, but also to contingent and unmatured rights to payment); see *In re Symes*, 174 B.R. 114, 118 (Bankr. D. Ariz. 1994) (referring to *Jensen*'s disagreement with *Frenville*'s interpretation of "claim" because it neglects to include contingent and unmatured rights); see also Philippe J. Kahn, *Bankruptcy Versus Environmental Protection: Discharging Future CERCLA Liability in Chapter 11*, 14 CARDOZO L. REV. 1999, 2020 n.106 (1993) (indicating CERCLA claim becomes analogous in its elemental structure to tort claim in *Union Scrap*

definition of claim to CERCLA obligations would always mean a claim would only exist *after* a party had incurred response costs because a party seeking reimbursement under CERCLA has no right to payment until that point. Moreover, adoption of such a narrow definition would undermine the goal of the fresh start and encourage creditor manipulation to the detriment of the debtor's other creditors. On the *Jensen* facts, if the state only had a claim after it incurred cleanup costs, it could pursue the Jensens while the Jensens' other pre-petition claimants could not.

The court also refused to hold that a claim arises only when a relationship exists between the debtor and creditor. It reasoned that such a conclusion would favor the state because it did not become involved until after the Jensens had filed bankruptcy.<sup>255</sup>

The court concluded a claim arises when the conduct giving rise to the liability occurs. Such an approach implements bankruptcy's goal of providing debtors with a fresh start while also discouraging manipulation of the bankruptcy process.<sup>256</sup>

The court found itself powerless to treat environmental obligations specially despite the important policy objectives and social concerns underlying environmental laws. Congress, not the courts, fixes priorities.<sup>257</sup>

### 3. Claim Exists When Conduct Plus Relationship Exists

Another approach holds a claim only arises when the conduct has occurred and the debtor has a relationship with the claim holder. The bankruptcy court in *Piper Aircraft* adopted this approach outside of an environmental context.<sup>258</sup> Courts in the

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because release or threatened release [of hazardous substances] establishes contingent right to payment in much the same way as debtor's conduct does in *Union Scrap*).

<sup>255</sup> *In re Jensen*, 127 B.R. at 31 (explaining state's claims would not be discharged because state only became involved post-petition in Jensens' individual bankruptcy); see *Roach v. Edge (In re Edge)*, 60 B.R. 690, 699–700 (Bankr. M.D. Tenn. 1986) (illustrating relationship test can disadvantage creditor by discharging creditor's claim if relationship existed pre-petition). For a further discussion of the consequences of concluding a claim arises when a debtor-creditor relationship exists, see generally Saville, *supra* note 213, at 353.

<sup>256</sup> *In re Jensen*, 127 B.R. at 31 ("The creditor, aware of a debtor's precarious financial situation, will delay expenditures in anticipation of the debtor's bankruptcy, thereby preventing discharge of the creditor's claims."); see Eng, *supra* note 250, at 264 (suggesting if bankruptcy claim arose based on statutory right to payment, bankruptcy process would be manipulated, contravening Bankruptcy Code's goal of providing fresh start to debtors); see also 1 William E. Knepper & Dan A. Bailey, *LIABILITY OF CORPORATE OFFICERS AND DIRECTORS* § 10.09 MB (7th ed. 2003) (explaining manipulation of bankruptcy proceeding is discouraged if claim is deemed to arise when actual or threatened release of hazardous waste occurs rather than when plaintiff regulatory agency incurs cleanup costs).

<sup>257</sup> *In re Jensen*, 127 B.R. at 33 (discussing generally power of Congress and limitations of courts); see *Gull Indus., Inc. v. John Mitchell, Inc. (In re Hanna)*, 168 B.R. 386, 390 (B.A.P. 9th Cir. 1994) (acknowledging Congress alone fixes priorities). See generally *Burlington N. R.R. v. Dant & Russell, Inc. (In re Dant & Russell, Inc.)*, 853 F.2d 700, 709 (9th Cir. 1988) (explaining how states can protect their interests in enforcement of environmental laws without impinging on Congress's authority).

<sup>258</sup> *In re Piper Aircraft Corp.*, 162 B.R. 619, 625–28 (Bankr. S.D. Fla. 1994), *aff'd sub nom.* Epstein v. Official Comm. of Unsecured Creditors of Estate of Piper Aircraft Corp. (*In re Piper Aircraft Corp.*), 168 B.R. 434 (Bankr. S.D. Fla. 1994), *aff'd*, 58 F.3d 1573 (11th Cir. 1995) (holding pre-petition relationship test finds claim when there is "contact, exposure, impact, or privity between the debtor's pre-petition conduct and claimant."); *In re Agway, Inc.*, 313 B.R. 31, 42 (Bankr. N.D.N.Y. 2004) (indicating *Piper* court used pre-

environmental arena have modified the *Piper Aircraft* approach to meet due process concerns.

#### 4. Claim Exists When Conduct, Relationship & Fair Contemplation of Liability Exist

Several courts, including the Ninth Circuit in *In re Jensen*,<sup>259</sup> have adopted an approach first posited by a Texas district court in *In re National Gypsum*.<sup>260</sup> According to the Seventh Circuit formulation:

when a potential CERCLA claimant can tie the bankruptcy debtor to a known release of a hazardous substance which the potential claimant knows will lead to CERCLA response costs, and when this potential claimant has, in fact, conducted tests with regard to this contamination problem, then this potential claimant has, at least, a contingent CERCLA claim for purposes of Section 77.<sup>261</sup>

All courts adopting this approach stress that "it is not a question of which statute should be accorded primacy over the other, but rather what interaction between the two statutes serves most faithfully the policy objectives embodied in the two separate enactments of Congress."<sup>262</sup> The Ninth Circuit in *Jensen* noted that the *Union Scrap-Frenville* approach did not properly account for the Bankruptcy Code's broad definition of claim and its critical role in implementing the

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petition relationship test and fashioned it to apply to product liability claims for which debtor would be directly liable); see Donald J. Quigley, *Treating Latent Medical Tort Claims in Bankruptcy*, 11 AM. BANKR. INST. J. 1, 18 (July/Aug. 2002) (explaining application of pre-petition relationship test to products liability case requires two things: debtor, pre-petition, must introduce defective product into stream of commerce and creditor, pre-confirmation, must have involvement with product which results in harm).

<sup>259</sup> 995 F.2d 925 (9th Cir. 1993).

<sup>260</sup> 139 B.R. 397 (N.D. Tex. 1992) (examining pre-petition conduct fairly within parties' contemplation at time of debtor's bankruptcy to determine when claim arose); *In re CD Realty Partners*, 205 B.R. 651, 656 (Bankr. D. Mass. 1997) (referring to what it believed was *Gypsum's* proper use of fair contemplation test). *Mesiti v. Microdot, Inc.*, 156 B.R. 113, 118 (Bankr. D.N.H. 1993) (referring to *Gypsum's* use of fair contemplation test).

<sup>261</sup> *In re Chi.*, Milwaukee, St. Paul & Pac. R.R., 974 F.2d 775, 786 (7th Cir. 1992); see 11 U.S.C. § 103(a)(8) (1976) (repealed 1978) (indicating "contingent debt" or "contingent contractual liability" exists for bankruptcy purposes even if no CERCLA response costs have been incurred); *Cal. Dep't of Health Servs. v. Jensen (In re Jensen)*, 995 F.2d 925, 929 (9th Cir. 1993) (stating Seventh Circuit has held potential claimant has contingent CERCLA claim for purposes of section 77 when it can tie debtor to act and has conducted tests with regard to damage caused by debtor's act).

<sup>262</sup> *In re Nat'l Gypsum Co.*, 139 B.R. at 404 (explaining to best serve goals of CERCLA, court must "recognize the circumstances particular to bankruptcy proceedings and provisions of the Code . . ."); see also *In re Chic.*, Milwaukee, St. Paul & Pac. R.R., 3 F.3d 200, 201 (7th Cir. 1993) (discussing how purposes of environmental and bankruptcy laws create conflicting objectives that require reconciliation). For further discussion on CERCLA and the Bankruptcy Code and their interaction with each other, see generally *Revere Copper & Brass Inc. v. Acushnet Co. (In re Revere Copper & Brass Inc.)*, 172 B.R. 192, 197 (Bankr. S.D.N.Y. 1994).



Bankruptcy Code's policy of giving debtors a fresh start.<sup>263</sup> The conduct test was also flawed because nothing in the Bankruptcy Code suggested "that Congress intended to discharge a creditor's rights before the creditor knew or should have known that its rights existed."<sup>264</sup> In addition, according to the court, "discharging liability solely because a release of hazardous substances occurred pre-petition may conflict with CERCLA's goal of cleaning up the environment quickly."<sup>265</sup>

Moreover, a broad definition of relationship that fails to require some interaction between the debtor and potential claimant suffers from the same infirmities as the conduct test. The Ninth Circuit, following *National Gypsum's* lead, adopted the "fair contemplation test." Future response costs and damages based on pre-petition conduct are pre-petition claims and hence dischargeable only if they are fairly in the contemplation of the parties.<sup>266</sup>

The court in *In re National Gypsum* gave examples of when a right to future response costs would be fairly contemplated: knowledge by the parties of a site for which the debtor might be liable, listing on the National Priorities List, EPA notification of liability, or an EPA investigation or clean up.<sup>267</sup>

The "fair contemplation" test balances a debtor's interests in bankruptcy relief with the environmental agency's interest in knowing of the potential problem and the ability to assert its rights.

Although the "fair contemplation" test seems to indicate when an environmental obligation arises, it does not resolve all questions related to the treatment of environmental obligations in bankruptcy. Currently, courts are struggling to determine if an environmental claimant is entitled to administrative expense priority.

Is it possible for one environmental claimant to have two different rights to

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<sup>263</sup> *In re Jensen*, 995 F.2d at 928; see *Reynolds Bros., Inc. v. Texaco, Inc.*, 647 N.E.2d 1205, 1209 (Mass. 1995) (noting courts have widely criticized *Union Scrap's* "right to payment" approach as inconsistent with broad statutory definition of "claim" and Bankruptcy Code goal of providing debtors with a "fresh start."); see also *Signature Combs, Inc. v. United States*, 253 F. Supp. 2d 1028, 1038 (W.D. Tenn. 2003) (holding fair contemplation standard is only test that tries to accommodate bankruptcy's fresh start goal).

<sup>264</sup> *In re Jensen*, 995 F.2d at 930 (quoting Saville, *supra* note 213, at 349); see *Sylvester Bros. Dev. Co. v. Burlington N. R.R.*, 133 B.R. 648, 653 (Bankr. D. Minn. 1991) (indicating CERCLA liability is not discharged when debtor has not disclosed CERCLA liabilities and creditor has no actual knowledge of claim with sufficient time to file claim in those proceedings); Deborah E. Parker, *Environmental Claims in Bankruptcy: It's a Question of Priorities*, Comment, 32 SAN DIEGO L. REV. 221, 236 (1995) (explaining creditor's knowledge of potential claim is important factor to consider in applying the debtor's conduct test).

<sup>265</sup> *In re Jensen*, 995 F.2d at 930 (quoting Saville, *supra* note 213, at 350); see *In re Nat'l Gypsum Co.*, 139 B.R. at 407-08 (criticizing *Chateaugay* for failing to give enough importance to CERCLA's objective of environmental cleanup); *United States v. Union Scrap Iron & Metal*, 123 B.R. 831, 836-37 (Bankr. D. Minn. 1990) (rejecting *Chateaugay* because it undermines CERCLA's goals).

<sup>266</sup> *In re Jensen*, 995 F.2d at 930; see Graham Stieglitz, *Stuck in the Middle Again! How to Treat Straddle-Year Income Taxes in a Corporate Chapter 11 Reorganization*, 9 AM. BANKR. INST. L. REV. 467, 488 (2001) (explaining why court developed narrower view of pre-petition relationship test). See generally Spracker & Barnette, *supra* note 246, at 97 (discussing "fair contemplation test" generally and its consequences on parties in bankruptcy proceedings).

<sup>267</sup> See *In re Jensen*, 995 F.2d at 930 (discussing *In re Nat'l Gypsum Co.*, 139 B.R. at 408). See Goodwyn, *supra* note 212, at 782 n.79 (discussing fair contemplation indicators further); see also Spracker & Barnette, *supra* note 246, at 96.

payment based on the same environmental problem? According to the case law, yes. One environmental claimant can have both a pre-petition, dischargeable claim and an administrative expense. For example, assume a contaminated site that becomes property of a debtor's estate. The trustee cannot abandon the property. The trustee must comply with all valid state laws including state environmental laws. The estate would be liable for the clean up. The clean up costs, as an estate liability, would be an administrative expense even though the environmental agency would also have a pre-petition, dischargeable claim against the debtor.

## 5. Post-confirmation Liability

Assume a company successfully reorganizes. Its chapter 11 plan describes its pre-petition environmental liability and that liability is discharged. The company is still not necessarily home free. If the company, post-confirmation, still owns contaminated property, it is an owner, and therefore, a PRP under CERCLA.<sup>268</sup> It is liable. As one court explained, bankruptcy affects claims based on damages for *past* releases of hazardous substances. It does not affect claims for remediation of present and future threats.<sup>269</sup>

If a company cannot abandon contaminated property during its reorganization, its best hope is to negotiate a reasonable and feasible settlement with environmental claimants. Otherwise, its reorganization would seem doomed. Needless to say, dooming a company's reorganization does not clean up the property. It just kills the company and thereby removes one potentially responsible party from the scene.

## 6. Post-petition Creation & Perfection of Superlien: Violation of the Automatic Stay?

Some states permit the state to obtain a superlien to secure reimbursement of cleanup costs.<sup>270</sup> Does post-petition creation and perfection of a superlien violate the stay? The First Circuit concluded "no" within an uncooperative statutory

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<sup>268</sup> 42 U.S.C. § 9607(a) (2000); see *CMC Heartland Partners v. Gen. Motors Corp.*, No. 92-C4449, 1994 U.S. Dist. LEXIS 12228, at \*7 (N.D. Ill. Aug. 30, 1994) (referring to potentially responsible parties, or, PRP's); William B. Johnson, Annotation, *Equitable Considerations in Allocating Response Costs to Owner or Occupant of Previously Contaminated Facility in Action Pursuant To § 113 (f) of Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA)* (42 U.S.C.A. § 9613(F)), 148 A.L.R. FED. 203 at 6(a) (2002) (discussing current owner's situation when it succeeded to ownership of property as result of predecessor's bankruptcy reorganization).

<sup>269</sup> *CMC Heartland Partners*, 1994 U.S. Dist. LEXIS at \*13-\*14; see *In re CMC Heartland Partners*, 966 F.2d 1143, 1146 (7th Cir. 1992) (paying for damage done does not immunize reorganized company from responsibility for preventing future harm); *Boston & Me. Corp. v. Chi. Pac. Corp.*, 785 F.2d 562, 565 (7th Cir. 1986) ("Bankruptcy draws a line between the existing claims to a firm's assets and newly-arising claims.").

<sup>270</sup> See, e.g., MASS. GEN. LAWS ch. 21E, § 13 (2002); (stating debt constitutes lien on property); N.H. REV. STAT. ANN. § 147-B:10-b (2003) (stating same). See generally Cahalane, *supra* note 92, at 285 (discussing constitutionality of superlien statutes).

framework.<sup>271</sup>

Section 362(b)(3) excepts from the stay "acts to perfect . . . an interest in property to the extent that the trustee's rights and powers are subject to such perfection under section 546(b)." This exception seems limited to the post-petition perfection of pre-petition liens. For example, it excepts post-petition perfection of liens that were in existence pre-petition. Statutory liens are often created and perfected simultaneously. The First Circuit, like Procrustes, did a little sawing and stretching to fit a post-petition superlien into the section 362(b)(3) exception.

The court's initial premise was the state had a pre-petition *interest* in the property. According to the court, the term "interest" is broader than "lien."<sup>272</sup> The debtor was liable to the state for past and future cleanup costs. The state had a present right to record a lien on the property. That present right to record a lien on the property gave it an interest in the property.<sup>273</sup> Section 362(b)(3)'s language "any act to perfect . . . an interest in property" meant the stay did not enjoin perfection of a lien. That language had to encompass statutory liens that were created and perfected simultaneously. Otherwise, the statute would lead to an absurd result. A single act creates and perfects an environmental lien. Read literally, section 362(b)(3) would both stay the act (creation of the lien) *and* not stay it (perfection of the lien). The court "decline[d] to indulge in so schizophrenic a reading of the Bankruptcy Code."<sup>274</sup>

Despite the First Circuit's strained reading, one suspects other courts will follow its lead. As Justice O'Connor observed in *Kovacs*, "a State may protect its interest in the enforcement of its environmental laws by giving cleanup judgments the status of statutory liens or secured claims."<sup>275</sup> When a state chooses to do so, presumably

<sup>271</sup> 229 Main St. Ltd. P'ship v. Mass. Env'tl. Prot. Agency (*In re* 229 Main St. Ltd. P'ship), 262 F.3d 1, 9 (1st Cir. 2001); see *In re* Microfab, Inc., 105 B.R. 152, 160 (Bankr. D. Mass. 1989) (concluding state can record lien against property without violating automatic stay); Jonathan Remy Nash, *Environmental Superliens and the Problem of Mortgage-Backed Securitization*, 59 WASH. & LEE L. REV. 127, 151 n.96 (2002) ("[C]ourts have held that the state's action in filing a superlien falls within an exception to the automatic stay.").

<sup>272</sup> *In re* 229 Main St. Ltd. P'ship, 262 F.3d at 7. For cases supporting the court's use of plain meaning statutory construction, see *Duncan v. Walker*, 533 U.S. 167, 173 (2000) (quoting *Bates v. United States*, 522 U.S. 23, 29–30 (1997) ("It is well settled that where Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion.")); *Pritzker v. Yari*, 42 F.3d 53, 67–68 (1st Cir. 1994) (refusing to undertake extra-textual measures when law is clear and unambiguous).

<sup>273</sup> *In re* 229 Main St. Ltd. P'ship, 262 F.3d at 7; see *In re* Perona Bros., 186 B.R. 833, 839 (Bankr. D.N.J. 1995) (analyzing state's pre-petition interest in property in context of environmental superlien). For general discussion of Massachusetts' superlien statute, see *Acme Laundry Co. v. Sec'y of Env'tl. Affairs*, 575 N.E.2d 1086 (1990).

<sup>274</sup> *In re* 229 Main St. Ltd. P'ship, 262 F.3d at 9. See generally Leonard P. Goldberger, *Who's On First? Retroactive Lien Priority Meets the Automatic Stay*, 20 AM. BANKR. INST. J., at 24–27 (Dec./Jan. 2002) (analyzing court's treatment of simultaneous creation and perfection under section 362(b)(3)). For general analysis of section 362(b)(3) post-petition perfection of interest in property, see 3 COLLIER ON BANKRUPTCY, ¶ 362.05, at 4 (Lawrence P. King et al. eds., 15th ed. rev. 1997).

<sup>275</sup> *Ohio v. Kovacs*, 469 U.S. 274, 286 (1985) (O'Connor, J., concurring); see Richard B. Paige, *In Re Quanta Resources Corp.: Bankruptcy Policy v. Environmental Interests; A Polluted Judicial Theory*, 59 AM. BANKR. L.J. 357, 380 (1985) ("States can [protect themselves] by enacting statutes classifying their claims,

courts will bend over backwards to give them effect.

### *E. Environmental Obligations as Administrative Expense?*

#### 1. Significance of Administrative Expense Issue

The tension between environmental and bankruptcy policies is most palpable when an environmental claimant seeks administrative expense priority for its claim.

Generally, every unsecured claimant would like its right to payment to enjoy administrative expense status. Holders of environmental claims are no different in that regard, but environmental obligations are distinguishable because they are often *huge*, sometimes in the millions of dollars. Granting administrative expense priority to an environmental obligation in a chapter 11 effectively gives the holder control of the case. Confirmation requires a plan to pay each administrative expense in cash in full on the effective date of the plan unless the holder agrees to less favorable treatment.<sup>276</sup> If the administrative expense holder insists on cash on the effective date of the plan, and the debtor does not have the requisite cash, the court cannot confirm the plan. The chapter 11 is over. In most chapter 7 cases, a large administrative expense will preclude any distribution to unsecured creditors. It will also dwarf the distribution to other administrative expense holders. Essentially, granting administrative expense priority to environmental obligations can upset the bankruptcy game plan. It can undermine a debtor's opportunity to reorganize, and it can redistribute most of the "wealth" to a single party contrary to bankruptcy's "equality is equity" creed.

On the other hand, treating an environmental obligation as a lowly general, prepetition, unsecured claim means bankruptcy will discharge the claim for pennies on the dollar, if that. Discharging the unpaid environmental liability subverts CERCLA's goal of requiring those responsible for the contamination to clean it up. And that can undermine CERCLA's other goal—prompt cleanup. As a policy matter, creditors of the debtor benefited from the debtor's failure to comply with environmental laws. The question therefore becomes shouldn't those creditors have to stand in line behind the environmental claim?

The two policies conflict. Congress has sat silently on the sidelines, with a blanket over its head. Once again, courts have had to make their own way. The case law *generally*<sup>277</sup> seems to accord the environmental obligation administrative

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for amounts spent cleaning up hazardous waste sites belonging to a bankrupt's estate, as perfected security interests or liens on the property itself."); Morris G. Shanker, *A Bankruptcy Superfund for Some Super Creditors From Ohio to Midlantic and Beyond*, 61 AM. BANKR. L.J. 185, 190 (discussing potential implications of Justice O'Connor's concurrence in *Ohio v. Kovacs*).

<sup>276</sup> 11 U.S.C. § 1129(a)(9)(A) (2000); see *In re Cheatham*, 78 B.R. 104, 106–07 (Bankr. E.D.N.C. 1987) (discussing same); *First State Bank v. Advisory Info. & Mgmt. Sys., Inc.* (In re Advisory Info. & Mgmt. Sys., Inc.), 50 B.R. 627, 630 (Bankr. M.D. Tenn. 1985) (quoting *In re Briggs Transp. Co.*, 47 B.R. 6, 8 (Bankr. D. Minn. 1984) ("Since § 1129(a)(9)(A) requires that all of the priority administrative expenses be paid in full on the effective date of confirmation, such creditors could effectively veto any plan.")).

<sup>277</sup> The word "generally" is italicized because generalizations are dangerous in this area of the law.

expense priority if the debtor owned the contaminated property as of the commencement of the case. Courts do so on a variety of theories, ranging from the timing of the cleanup, to 28 U.S.C. § 959(b), which requires a trustee to comply with all state laws, to a *Reading v. Brown* fairness exception, or some combination. If the debtor did *not* own the property at the commencement of the case (for example, if the debtor was a gas station-lessee), courts tend to characterize the environmental obligation as a pre-petition claim.

## 2. *Reading v. Brown*: The Fairness Exception

The tension between bankruptcy law and other public policies is hardly new. In *Reading Co. v. Brown*,<sup>278</sup> an Act case, the I.J. Knight Realty Corporation petitioned for an arrangement. A receiver was appointed and authorized to conduct the debtor's business "which consisted principally of leasing the debtor's only significant asset, an eight-story industrial structure."<sup>279</sup> A fire broke out, destroying the building and adjacent property. The fire victims filed claims for administrative expenses, based on the receiver's negligence. The claims exceeded \$3.5 million and the total assets of the debtor's estate.

The parties agreed that "the words 'preserving the estate' included the larger objective, common to arrangements, of operating the debtor's business with a view to rehabilitating it."<sup>280</sup> According to the trustee, the negligence claims were not entitled to first priority—they were not actual and necessary costs of operating the debtor's business. Furthermore, giving them first priority was "not necessary to encourage third parties to deal with an insolvent business," because it would "reduce the amount available for the general creditors," and it would "discourage general creditors from accepting arrangements."<sup>281</sup>

According to a majority of the Court, the negligence claims were entitled to administrative expense status as a matter of fairness:

[F]airness to all persons having claims against an insolvent . . .

. . . At the moment when an arrangement is sought, the debtor is insolvent. Its existing creditors hope that by partial or complete

<sup>278</sup> 391 U.S. 471 (1968).

<sup>279</sup> *Id.* at 473.

<sup>280</sup> *Id.* at 475; see *In re Jartran, Inc.*, 732 F.2d 584, 586 (7th Cir. 1984) ("It is well settled that expenses incurred by the debtor-in-possession in attempting to rehabilitate the business during reorganization are within the ambit of § 503."); *In re N.Y. Trap Rock Corp.*, 137 B.R. 568, 572 (Bankr. S.D.N.Y. 1992) (rehabilitation expenses incurred by possessing debtor during reorganization fall within expense of "preserving the estate" of 11 U.S.C. § 503(b)(1)(A)).

<sup>281</sup> *Reading*, 391 U.S. at 477. The Court's rejection of the trustee's arguments is further discussed in *In re Con'l Airlines*, 148 B.R. 207, 214 (Bankr. D. Del. 1992) and *In re Chi. Pac. Corp.*, 773 F.2d 909, 913–14 (7th Cir. 1985).

postponement of their claims they will, through successful rehabilitation, eventually recover from the debtor either in full or in larger proportion than they would in immediate bankruptcy. Hence the present petitioner did not merely suffer injury at the hands of an insolvent business: it had an insolvent business thrust upon it by operation of law. That business will, in any event, be unable to pay its fire debts in full. But the question is whether the fire claimants should be subordinated to, should share equally with, or should collect ahead of those creditors for whose benefit the continued operation of the business . . . was allowed.

. . . [T]he business [was] operating under a Chapter XI arrangement for the benefit of creditors and with the hope of rehabilitation. That benefit and that rehabilitation are worthy objectives. But it would be inconsistent both with the principle of respondeat superior and with the rule of fairness in bankruptcy to seek these objectives at the cost of excluding tort creditors or the arrangement from its assets, or totally subordinating the claims of those on whom the arrangement is imposed to the claims of those for whose benefit it is instituted.<sup>282</sup>

The Court held that the phrase "actual and necessary costs" includes the costs ordinarily incident to operation of a business. Such costs are not limited to those expenses "without which rehabilitation would be impossible."<sup>283</sup>

Chief Justice Warren, joined by Justice Douglas, dissented. He believed the Court's holding frustrated the underlying purposes of chapter 11, and gave an unwarranted preference to claimants who were lucky enough to incur their injury post-petition. The Chief Justice argued that tort claimants would "exhaust the estate to the exclusion of the general creditors as well as of the wage claims and government tax claims for which Congress has shown an unmistakable preference."<sup>284</sup> Further, the dissent argued that it was not equitable to impose the

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<sup>282</sup> *Reading*, 391 U.S. at 478-79. For a general discussion of the exception created in *Reading*, and the courts' treatment thereof, see Karen Cordry, *Administrative Expenses, Criminal Law and the Code*, 18 AM. BANKR. INST. J. 1, 8, 46 (Dec./Jan. 2000); William L. Medford, *Post-petition Claims and Administrative Expense Authority: Timing Alone Does Not Entitle You to Payment*, 21 AM. BANKR. INST. J. 1, 24-25 (June 2002).

<sup>283</sup> *Reading*, 391 U.S. at 483 (identifying what constitutes "actual and necessary costs."); see Joanne Gelfand, *The Treatment of Employment Discrimination Claims in Bankruptcy: Priority Status, Stay, Relief, Dischargeability, and Exemptions*, 56 U. MIAMI. L. REV. 601, 607-08 (2002) (discussing interpretation of "actual and necessary costs" in *Reading*); Stephen D. Hurd, *Re-reading Reading: "Fairness to All Persons" in the context of Administrative Expense Priority for Postpetition Punitive Fines in Bankruptcy*, 51 VAND. L. REV. 1459, 1468-71 (1998) (analyzing facts of *Reading*).

<sup>284</sup> *Reading*, 391 U.S. at 486-87 (Warren, C.J., dissenting). For a further discussion of Warren's dissent, see Hurd, *supra* note 283, at 1483-84; see also Susan R. DeSimone, Note, *The Price of Doing Business: Environmental Criminal Fines and the Administrative Expense Solution*, 17 BANKR. DEV. J. 489, 513-14 n.123 (2001) (illustrating Justice Warren's interpretation of Bankruptcy Code).

loss on the unsecured creditors because they had thrust the insolvent business upon the tort claimants:

An economically distressed businessman seeks an arrangement for his own and not for his creditors' benefit. Of course, the creditors will benefit if the arrangement is successful, just as they would have benefited if the businessman had been successful without resorting to an arrangement. But a business in arrangement is no more thrust upon the public than is any other business enterprise which is conducted for the mutual prosperity of the owners, the wage earners and the creditors. Realistically, the only difference is that a business administered under Chapter XI has not been prosperous. If the arrangement is successful, the owners, wage earners and creditors will all benefit; if it is not, they will all be injured. Thus, I would not distinguish in this case between petitioner and the other general creditors, none of whom was responsible for the catastrophe for which all of them must sustain some loss. Instead, . . . I would adhere to the Act's basic theme of equality of distribution.<sup>285</sup>

Chief Justice Warren concluded his dissent by stating that he saw no basis in law or policy to make the unsecured creditors involuntary insurers.<sup>286</sup>

The Eleventh Circuit relied on *Reading* and 28 U.S.C. § 959(b) to accord administrative expense status to punitive civil penalties the estate had incurred in operating.<sup>287</sup> According to the court, "a policy of ensuring compliance by trustees with state law is sufficient justification to place civil penalties assessed for post-petition mining operations in the category of the "some cases" in which "costs ordinarily incident to operation of a business . . . are accorded administrative

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<sup>285</sup> *Reading*, 391 U.S. at 487–88 (Warren, C.J., dissenting); see Thomas H. Jackson, *Of Liquidation, Continuation, and Delay: An Analysis of Bankruptcy Policy and Nonbankruptcy Rules*, 60 AM. BANKR. L.J. 399, 424–25 (1986) (reiterating Justice Warren's opinion that this result upsets bankruptcy's pro rata distribution policy); Donald R. Korobkin, *Rehabilitating Values: A Jurisprudence of Bankruptcy*, 91 COLUM. L. REV. 717, 783–86 (quoting Justice Warren in his dissent in *Reading*).

<sup>286</sup> *Reading*, 391 U.S. at 489 (Warren, C.J., dissenting). See generally David W. Allard, *Personal Liability of Trustees and Debtors in Possession: Review of Varying Standards of Care in the United States*, 106 COM. L.J. 415, 435 (2000) ("In the *Reading* case . . . the court reasoned that . . . tort claims would lie in favor of pre-petition creditors against the trustee . . . if the trustee negligently failed to procure insurance."); James K. McBain, *Environmental Impediments to Bankruptcy Reorganizations*, 68 IND. L.J. 233, 241–44 (1992) (discussing Justice Warren's dissent in *Reading*).

<sup>287</sup> See *Ala. Surface Mining Comm'n v. N.P. Mining Co. (In re N.P. Mining Co.)*, 963 F.2d 1449–59 (11th Cir. 1992) (holding civil penalties assessed post-petition against debtor as punishment for environmental violations qualified as administrative expenses to extent incurred as consequences of ongoing business pursuant to 28 U.S.C. § 959(b)); see also *In re Lickman*, 273 B.R. 691, 704 n.13 (Bankr. M.D. Fla. 2002) (examining court's holding in *In re N.P. Mining Co.*); Parker, *supra* note 264, at 275–79 (identifying 28 U.S.C. § 959's role in determining administrative priority).

expense priority."<sup>288</sup> The Court reasoned that a contrary holding would give debtors in possession an unfair advantage over non-bankrupt competitors.<sup>289</sup> The court excluded any post-petition penalties assessed for the trustee's failure to abate pre-petition violations of state mining laws because that would "deprive the estate of its 'new day' beginning and frustrate the purpose of the bankruptcy statute."<sup>290</sup>

### 3. *Midlantic* Corollary

Most courts rely on *Midlantic* to give the environmental obligation administrative expense priority. Sometimes, the court's "reasoning" is mystifying. In *Midlantic*, the Court held that "a trustee may not abandon property in contravention of a state statute or regulation that is reasonably designed to protect the public health or safety from identified hazards."<sup>291</sup> To bolster its conclusion "that Congress did not intend for the Bankruptcy Code to pre-empt all state laws,"<sup>292</sup> the Court noted 28 U.S.C. § 959(b) requires trustees to comply with state laws in managing and operating estates.<sup>293</sup> Moreover, in *Kovacs*, the Court had stated:

[W]e do not question that anyone in possession of the site—

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<sup>288</sup> *In re N.P. Mining Co.*, 963 F.2d at 1459; see also Hurd, *supra* note 283, at 1478–79 (discussing court's assessment of punitive fines as administrative expense priority in *In re N.P. Mining*); Seth M. Mandelbaum, Pennsylvania v. Conroy: *Expanded Administrative Expense Priority for State-Funded CERCLA Cleanups*, 12 PACE ENVTL. L. REV. 319, 332 (1995) ("In *In re N.P. Mining Co.*, punitive penalties were not given priority because there was no threat to public health or safety; thus, the fines were not part of the actual, necessary expenses of preserving the estate.").

<sup>289</sup> See *In re N.P. Mining Co.*, 963 F.2d at 1458 (holding debtors must not receive preferential treatment). For further discussion of administrative expense status in *In re N.P. Mining*, see Parker, *supra* note 264, at 278–79. Spracker & Barnette, *supra* note 246, at 102 (analyzing administrative expense status of environmental claims arising after filing of bankruptcy petition).

<sup>290</sup> *In re N.P. Mining Co.*, 963 F.2d at 1459; see *In re Bill's Coal Co.*, 124 B.R. 827, 830 (Bankr. D. Kan. 1991) (suggesting fine for violating environmental laws is cost incidental to operation of business and penalty for post-petition conduct is entitled to administrative priority); Hurd, *supra* note 283, at 1475 (identifying court's reasoning in *In re Bill's Coal Co.* as "punitive fines are ordinarily incident to regulated mining operations and should therefore receive administrative expense priority").

<sup>291</sup> *Midlantic Nat'l Bank v. N.J. Dep't of Env'tl. Prot.*, 474 U.S. 494, 507 (1986); see Joseph P. Cistulli, *Striking a Balance Between Competing Policies: The Administrative Claim as an Alternative to Enforce State Clean-Up Orders in Bankruptcy Proceedings*, 16 B.C. ENVTL. AFF. L. REV. 581, 590–96 (1989) (discussing *Midlantic's* recognition of "importance of a safe environment as reason enough to allow administrative expense status for clean-up orders"); Walter W. Miller, Jr. & Maureen A. O'Rourke, *Bankruptcy Law v. Privacy Rights: Which Holds the Trump Card?*, 38 HOUS. L. REV. 777, 824 (2001) (acknowledging abandonment power is not meant to be impeded by laws that do not protect public health or safety).

<sup>292</sup> *Midlantic*, 474 U.S. at 505; see Adam Feibelman, *Federal Bankruptcy Law and State Sovereign Immunity*, 81 TEX. L. REV. 1381, 1423 (2003) (noting role of section 959(b) in deciding this case); Thomas E. Plank, *The Erie Doctrine and Bankruptcy*, 79 NOTRE DAME L. REV. 633, 636 (2004) (noting federal courts in bankruptcy must apply state law).

<sup>293</sup> See 28 U.S.C. § 959(b) (2000) (stating debtors in possession should operate property according to state law requirements); *Midlantic*, 474 U.S. at 505 ("Section 959(b) commands the trustee to 'manage and operate the property in his possession . . . according to the requirements of the valid laws of the state.'"); see also Frederick Tung, *Is International Bankruptcy Possible?*, 23 MICH. J. INT'L L. 31, 73 (2001) (stating trustees must adhere to local health and safety laws).



whether it is Kovacs or another in the event the receivership is liquidated and the trustee abandons the property, or a vendee from the receiver or the bankruptcy trustee—must comply with the environmental laws of the State of Ohio. Plainly, that person or firm may not maintain a nuisance, pollute the waters of the State, or refuse to remove the source of such conditions.<sup>294</sup>

If a trustee cannot abandon property because abandonment would violate a state law reasonably designed to protect the public health or safety from identified hazards *and* the trustee must comply with all valid state laws when managing and operating property of the estate, the trustee *must* expend estate funds to comply with state environmental laws. That rationale effectively accords administrative expense status to environmental obligations.

*In re Laurinburg Oil Co.*<sup>295</sup> is illustrative. The debtor operated a waste disposal facility which was filled beyond capacity and leaking. The state informed the bankruptcy court that the debtor's wastewater lagoon constituted a threat to public health and safety. The state did not seek a money judgment.<sup>296</sup> Instead, it sought to compel the debtor to clean it up—to restore it to a condition that would no longer violate environmental pollution laws. The court stated: "The provisions of 28 U.S.C. § 959(b) require a debtor in possession to manage and operate the property according to the valid laws of the state in which the property is situated. This provision is applicable to the matter before the court."<sup>297</sup> Moreover, "the reasonable and necessary expenses . . . [the debtor incurs] should be considered administrative expenses necessary to preserve the debtor's estate . . . ."<sup>298</sup>

Other courts have followed a similar path.<sup>299</sup> *In Lancaster v. Tennessee (In re*

<sup>294</sup> *Ohio v. Kovacs*, 469 U.S. 274, 285 (1985). See generally Arriola, *supra* note 252, at 68 (analyzing implication of *Kovacs* on environmental claims in bankruptcy); Cistulli, *supra* note 291, at 590–96 (discussing facts of case).

<sup>295</sup> 49 B.R. 652 (Bankr. M.D.N.C. 1984).

<sup>296</sup> *Id.* at 654 ("The state's proposed action seeks traditional injunctive relief, not the payment of a money judgment."). For a discussion of the facts in *In re Laurinburg Oil Co.*, see *In re Harmar Coal Co.*, 548 A.2d 1224, 1227 (Pa. Super. 1988). See also Parker, *supra* note 264, at 277 (suggesting based on case law, "penalties for violations of state and federal law are entitled to administrative expense priority as necessary costs of the continued operation of Chapter 11 debtor's business.").

<sup>297</sup> *In re Laurinburg Oil Co.*, 49 B.R. at 654; see 28 U.S.C. § 959(b) (2000) (giving debtor in possession responsibility to manage its property); see, e.g., Margaret E. Juliano, *Stalemate: The Need for Limitations on Regulatory Deference in Electric Bankruptcies*, 20 BANKR. DEV. J. 245, 265 (assessing section 959(b)'s role in trustee or debtor's operation of property).

<sup>298</sup> *In re Laurinburg Oil Co.*, 49 B.R. at 654; see DeSimone, *supra* note 284, at 518–19 (citing 28 U.S.C. § 959(b) explaining "[f]ollowing this logic, courts have held that because bankrupt corporations cannot cut business expenses by ignoring health, safety, environmental, or other relevant state laws, any fines incurred by a bankrupt business for violation of these laws, or § 959, deserve administrative expense priority status"); David Van Epps, *A Fiduciary's Liability Under CERCLA: The Collision of Fundamental Policies—Beyond Ohio v. Kovacs and Midlantic National Bank v. New Jersey Department of Environmental Protection*, 21 N. KY. L. REV. 585, 597–98 (1993) (arguing clean-up expenses could be allowable administrative expenses).

<sup>299</sup> See, e.g., *Guterl Special Steel Corp. v. Econ. Dev. Admin. (In re Guterl Special Steel Corp.)*, 198 B.R. 128 (Bankr. W.D. Pa. 1996); *White Front Feed & Seed v. State Nat'l Bank of Platteville (In re Ramaker)*,

*Wall Tube & Metal Products Co.*),<sup>300</sup> the debtor manufactured automobile bumpers, outdoor furniture, steel tubes and other metal products. Its manufacturing process generated hazardous substances. It leased its premises. It ceased operating. State environmental authorities inspected the premises, issued a notice of violations and recommended that the debtor immediately and properly dispose of the wastes at the site. The debtor did not comply and eventually petitioned for chapter 7 relief. The state notified the chapter 7 trustee of the violations. Ultimately, the state filed a request for administrative expense treatment for its response costs. The bankruptcy court denied the request because the costs were not actual, necessary costs and expenses of preserving the estate within the meaning of section 503(b).<sup>301</sup> Moreover, the court held that 28 U.S.C. § 959(b) did not apply to a chapter 7 trustee liquidating an estate. It was limited to those who manage and operate.<sup>302</sup> Because "the State's activity neither benefited the estate nor fulfilled a legal obligation under State law, the State's recovery costs could not be accorded administrative expense status."<sup>303</sup>

On appeal, the Sixth Circuit relied on *Midlantic* to conclude that the efforts of the trustee "to marshal and distribute the assets of the estate must yield to the governmental interest in public health and safety."<sup>304</sup> The trustee could not abandon the property because abandonment would pose a threat comparable to that in *Midlantic*, "a continuing, potentially disastrous environmental health hazard with no one clearly responsible for remedial action."<sup>305</sup> If the trustee could not abandon the

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117 B.R. 959 (N.D. Iowa 1990); *United States v. Ilco, Inc. (In re Ilco, Inc.)*, 48 B.R. 1016 (Bankr. N.D. Ala 1985).

<sup>300</sup> 831 F.2d 118 (6th Cir. 1987). See generally McBain, *supra* note 286, at 242 n.61 (discussing implications of case, "the leading example of administrative expense priority for CERCLA § 107 claims."); Losch, *supra* note 225, at 162-64 (explaining case espouses majority view among circuits by granting administrative priority to environmental claims).

<sup>301</sup> *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 121 (explaining lower court denied request for administrative expense); see *In re Wall Tube & Metal Prods. Co.*, 56 B.R. 918, 924 (Bankr. E.D. Tenn. 1986) *rev'd*, 831 F.2d 118 (6th Cir. 1987); see also *Ala. Surface Mining Comm'n. v. N.P. Mining Co., Inc. (In re N.P. Mining Co.)*, 963 F.2d 1449, 1452 (11th Cir. 1992) (stating section 503(b)(1)(a) administrative expenses include "the actual, necessary costs and expenses of preserving the estate . . .").

<sup>302</sup> *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 121 (noting lower court did not apply section 959(b) to trustee liquidating estate); *In re Wall Tube & Metal Prods. Co.*, 56 B.R. at 925-26 (concluding that omission of term in section 959(b) that appears in section 959(a) indicates Congressional intent to limit scope of liability for trustee who merely liquidates estate under section 959(b)); see *Walker v. Maury County (In re Scott Hous. Sys., Inc.)*, 91 B.R. 190, 195-96 (Bankr. S.D. Ga. 1988) (deciding section 959(b) excepts trustees who liquidate but do not manage or operate estate).

<sup>303</sup> *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 121; *In re Wall Tube & Metal Prods. Co.*, 56 B.R. at 925 (finding no liability under section 959(b)); see Lynn Tadlock Manolopoulos, *A Congressional Choice: The Question of Environmental Priority in Bankrupt Estates*, 9 UCLA J. ENVTL. L. & POLY 73, 90-91 (1990) (stating lower court decision to exempt liquidating trustee from section 959(b) implied environmental claims did not warrant priority status in bankruptcy).

<sup>304</sup> *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 122 (quoting *Midlantic Nat'l Bank v. O'Neill*, 474 U.S. 494, 507 (1986)); see *In re N.P. Mining Co.*, 963 F.2d at 1457 (relying on same quote to support administrative expense claim); *In re FCX, Inc.*, 96 B.R. 49, 56 n.11 (Bankr. E.D.N.C. 1989) (stating Sixth Circuit interpreted *Midlantic* exception more broadly than other circuits).

<sup>305</sup> *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 122; see *In re Unidigital Inc.*, 262 B.R. 283, 286-87 (Bankr. D. Del. 2001) (stating "imminent and identifiable threat" finding was important to *In re Wall Tube*

property, then he could not maintain or possess it in continuous violation of that same state law. Moreover, the Sixth Circuit held that 28 U.S.C. § 959(b) applied whether the trustee was liquidating or reorganizing.<sup>306</sup> The court relied on *Reading v. Brown*'s expansive reading of what constitutes an actual, necessary expense to conclude that the cleanup costs were administrative expenses.<sup>307</sup> It emphasized the importance of complying with laws designed to protect the public's health and safety.<sup>308</sup> It concluded that if an estate cannot avoid CERCLA liability, "the cost incurred . . . in discharging this liability is an actual, necessary cost of preserving the estate entitled to administrative expense priority."<sup>309</sup>

In *In re Stevens*,<sup>310</sup> the court stated that *Midlantic* altered the criteria for determining allowance of administrative expenses.<sup>311</sup> For example, a trustee cannot abandon hazardous waste. Furthermore, 28 U.S.C. § 959(b) requires the trustee to comply with valid state laws. Thus, cleanup responsibility remains the responsibility of the estate:

The trustee was obligated to comply with valid Maine law regulating the disposal of hazardous waste. Since the trustee did not

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holding). *But see In re Shore Co.* 134 B.R. 572, 578 (Bankr. E.D. Tex. 1991) (rejecting broad reading of *Midlantic* to allow abandonment when estate violated environmental laws but no imminent harm existed).

<sup>306</sup> *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 122 (stating liquidating trustee had duty under state law); see *Windolph Trust v. Leitch (In re Kent Holland Die Casting & Plating, Inc.)*, 125 B.R. 493, 500 (Bankr. W.D. Mich. 1991) ("[T]hat the trustee in this case is liquidating the estate, rather than reorganizing it is inconsequential, especially in the critical context of the public's welfare."). *But see Mo. Dep't of Natural Res. v. Valley Steel Prods. Co.*, (*In re Valley Steel Prods. Co.*), 157 B.R. 442, 449 (Bankr. E.D. Mo. 1993) (rejecting contention that section 959(b) applies to trustee who merely liquidates estate).

<sup>307</sup> *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 123 (noting *Reading* justifies expansive reading of administrative expense); see *In re N.P. Mining Co.*, 963 F.2d at 1453 (citing *Reading* to support argument for administrative expense for civil mining penalties). *But see In re Mahoney-Troast Constr. Co.*, 189 B.R. 57, 62 (Bankr. D.N.J. 1995) (declining to extend *Reading* to case where creditor removed contaminated soil that did not pose ongoing threat to public health).

<sup>308</sup> *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 123; see 1 COLLIER ON BANKRUPTCY ¶ 10.04 [5] (Lawrence P. King et al. eds., 15th ed. rev. 1997) ("[A]n overriding concern with public health and safety led the Sixth Circuit to override the express language of section 959 . . ."). *But see Parker, supra* note 264, at 264-65 (1995) (contending facts of *In re Wall Tube* do not support court's conclusion of "imminent and identifiable threat" of harm to public safety).

<sup>309</sup> *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 123-24 (quoting *In re T.P. Long Chem., Inc.* 45 B.R. 278, 286 (Bankr. N.D. Ohio 1985)); see *Pa. Dep't of Env'tl. Res. v. Conroy*, 24 F.3d 568, 569-70 (3d Cir. 1994) (following *In re Wall Tube* to hold Bankruptcy Code did not preempt state law prohibiting abandonment of hazardous waste, and state's cleanup costs including administrative and legal costs were administrative expenses); *In re Kent Holland Die Casting & Plating, Inc.*, 125 B.R. at 500 (Bankr. W.D. Mich. 1991) (explaining *In re Wall Tube* holding that CERCLA liability led court to allow administrative expense).

<sup>310</sup> 68 B.R. 774 (Bankr. D. Me. 1987). Compare *In re Unidigital Inc.*, 262 B.R. at 286-87 (stating *In re Stevens* was part of majority of courts who denied abandonment only when imminent and identifiable threat existed), with *Guterl Special Steel Corp. v. Econ. Dev. Admin.* (*In re Guterl Special Steel Corp.*), 198 B.R. 128, 134 (Bankr. W.D. Pa. 1996) (contending *In re Stevens* was part of minority of courts denying abandonment if state law violation occurred, regardless of whether imminent and identifiable threat existed).

<sup>311</sup> *In re Stevens*, 68 B.R. at 780; see *Cistulli, supra* note 291, at 597 (stating *In re Stevens* court used *Midlantic* to allow administrative expense, but different result would follow from pre-*Midlantic* "benefit/burden" test); *Ryland, supra* note 239, at 755 (finding *In re Stevens* interpreted *Midlantic* broadly).

arrange for its removal and disposal, the estate is liable for all costs incurred by the state in removing the waste oil . . . .

. . . [T]he improper and illegal storage of waste oil containing PCB's constitutes an imminent and identifiable danger, and . . . the costs of protecting the public from that danger are entitled to treatment as costs of administration."<sup>312</sup>

Other courts have adopted similar logic to reach a similar conclusion.<sup>313</sup>

#### 4. Ongoing Duty; Ongoing Expense

Even when an estate is not operating and no hazardous substance is involved, courts have held that post-petition reclamation costs are an administrative expense. For example, in *Coal Stripping, Inc. v. Claredon National Insurance Co. (In re Coal Stripping, Inc.)*,<sup>314</sup> the debtor had ceased its surface coal-mining activities before petitioning for bankruptcy relief. It had not reclaimed the land as it was required to do, but no hazard to public health or safety existed. It was not operating in the chapter 11. According to the court, a cleanup claim for nonhazardous waste had to meet the definition of section 503(b) to qualify for administrative expense status. It had to be an actual, necessary cost of preserving the estate. The court held the state was entitled to an administrative claim to the extent it performed a post-petition cleanup: "debtor-in-possession [status] carries with it certain obligations, including an on-going duty to restore the land."<sup>315</sup>

<sup>312</sup> *In re Stevens*, 68 B.R. at 782-83.

<sup>313</sup> See, e.g., *Texas v. Lowe (In re H.L.S. Energy Co.)*, 151 F.3d 434, 438 (5th Cir. 1998) (finding state's claim to plug oil well is administrative expense even though estate produced no oil and received no revenue from well, because trustee must comply with state law and unplugged, unproductive wells operated as legal liability on estate); *In re Guterl Special Steel Corp.*, 198 B.R. at 135-36 (deciding threat to public health precluded abandonment, and EPA was entitled to recover cleanup costs from estate funds including funds paid to secured creditor from sale of non-toxic collateral, because trustee who cleans up hazardous waste on property of estate is discharging legal obligation of estate); *First Va. Bank of Tidewater v. Va. Builders, Inc. (In re Va. Builders, Inc.)*, 153 B.R. 729, 733 (Bankr. E.D. Va. 1993) (noting courts construe section 503(b)'s language broadly following *Reading v. Brown*, and grant environmental claims administrative status based on three grounds: (1) the timing of the damage; (2) the provisions of 28 U.S.C. § 959(b); and (3) the judicially created exception in *Midlantic*; bank's actual costs to clean up dumping ground qualified for administrative expense priority on all three grounds).

<sup>314</sup> 222 B.R. 78 (Bankr. W.D. Pa. 1998); see *Ala. Surface Mining Comm'n v. N.P. Mining Co. (In re N.P. Mining Co.)*, 963 F.2d 1449, 1453 (11th Cir. 1992) (extending administrative expense costs to post-petition civil mining penalties under section 503(b)); *In re Pierce Coal & Constr., Inc.*, 65 B.R. 521, 530 (Bankr. N.D.W. Va. 1986) (stating debtor in possession's post-petition reclamation costs were clearly administrative expense under section 503(b)).

<sup>315</sup> *In re Coal Stripping, Inc.*, 222 B.R. at 82; see *In re Pierce Coal & Constr., Inc.*, 65 B.R. at 528 (stating Supreme Court has ruled debtor in possession must remove condition that violates environmental law). But see *In re G-I Holdings, Inc.*, 308 B.R. 196, 207 (Bankr. D.N.J. 2004) (distinguishing *In re Coal Stripping* to deny administrative expense when private party, not state agency, performed cleanup and private party was surety seeking subrogation).

In *United States v. LTV Corporation (In re Chateaugay Corporation)*,<sup>316</sup> the Second Circuit characterized a debtor's unincurred CERCLA response costs for pre-petition releases as a dischargeable claim.<sup>317</sup> According to the court, the EPA, pre-petition, held a contingent right to payment.<sup>318</sup> That right to payment was "within the actual or presumed contemplation of the parties at the time the original relationship between the parties was created."<sup>319</sup> But the EPA *also* had an administrative expense for costs assessed post-petition on LTV properties involving a pre-petition release or threatened release.<sup>320</sup> The issue became how the pre-petition conduct creating a pre-petition claim also created post-petition administrative expense liability. The court held that the "EPA . . . is acting, during the administration of the estate, to remedy the ongoing effects of a release of hazardous substances."<sup>321</sup> A trustee cannot abandon property in contravention of a

<sup>316</sup> 944 F. 2d 997 (2d. Cir. 1991).

<sup>317</sup> *Id.* at 1005; see 11 U.S.C. § 101(4)(A) (2000) (defining "claim" as "a right to payment, whether or not such right is . . . contingent . . ."); see also *Jensen v. Cal. Dep't of Health Servs. (In re Jensen)*, 127 B.R. 27, 33 (B.A.P. 9th Cir. 1991) (concluding broad definition of "claim" supports "fresh start" bankruptcy goal). But see *In re Nat'l Gypsum Co.*, 139 B.R. 397, 407-08 (N.D. Tex. 1992) (favoring CERCLA's environmental cleanup objective over Bankruptcy Code's "fresh start" objective by narrowing definition of "claim" and emphasizing "fair" contemplation of parties).

<sup>318</sup> *In re Chateaugay Corp.*, 944 F. 2d at 1004-05; see *In re Michaelson*, 74 B.R. 245, 249 (Bankr. D. Nev. 1987) (accepting definition of contingent claim as defined in *In re All Media Prop., Inc.*, 5 B.R. 126, 133 (Bankr. S.D. Tex. 1980), *aff'd mem.*, 646 F. 2d 193 (5th Cir. 1981)); *In re All Media Props.*, 5 B.R. at 133 (concluding claim is contingent if debtor will be called upon to pay it only upon occurrence or happening of triggering extrinsic event and parties reasonably contemplated such triggering event or occurrence at time event giving rise to claim occurred).

<sup>319</sup> *In re Chateaugay*, 944 F. 2d at 1004 (concluding claim is contingent if debtor will be called upon to pay it only upon occurrence or happening of triggering extrinsic event and the parties reasonably contemplated such triggering event or occurrence at time event giving rise to claim occurred (quoting *In re All Media Props., Inc.*, 5 B.R. at 133)); see also *In re Mavellia*, 149 B.R. 301, 304 (Bankr. E.D.N.Y. 1991).

[t]he statement of what constitutes a contingent debt which has received universal acceptance by the bankruptcy courts . . . is "[c]laims are contingent as to liability if the debt is one which the debtor will be called upon to pay only upon the occurrence or happening of an extrinsic event which will trigger the liability of the debtor to the alleged creditor and if such triggering event or occurrence was one reasonably contemplated by the debtor and creditor at the time the event giving rise to the claim occurred."

*Id.* (citing *In re All Media Props., Inc.*, 5 B.R. at 133).

<sup>320</sup> *In re Chateaugay Corp.*, 944 F. 2d at 1010; see 11 U.S.C. § 503 (b)(1)(A) (2000) (providing actual necessary costs and expenses of preserving estate are entitled to administrative expense priority); see also *Midlantic Nat'l Bank v. N.J. Dep't of Envtl. Prot.*, 474 U.S. 494, 507 (1986) (ruling bankruptcy trustee cannot abandon property in contravention of state or local laws designed to protect public health or safety); *In re Stevens*, 68 B.R. 774, 783 (Bankr. D. Me. 1987) (holding trustee could not abandon hazardous waste and had to comply with state environmental law).

<sup>321</sup> *In re Chateaugay Corp.*, 944 F. 2d at 1010; see *Midlantic*, 474 U.S. at 507 (ruling bankruptcy trustee cannot abandon property in contravention of state or local laws designed to protect public health or safety and expenses to remove threat are necessary to preserve estate); *Lancaster v. Tennessee (In re Wall Tube & Metal Prods., Co.)*, 831 F. 2d 118, 123-24 (6th Cir. 1987) (holding trustee could not abandon property in contravention of state statute designed to protect public health and response costs were actual and necessary to preserve estate in compliance with state law); *In re Stevens*, 68 B.R. at 783 (holding trustee could not abandon hazardous waste and had to comply with state environmental law and costs were entitled to administrative expense priority).

state law reasonably designed to protect the public's health and safety.<sup>322</sup> If the trustee cannot abandon the property, the expenses to remove the threat are necessary to preserve the estate.<sup>323</sup> Both the debtor *and* the estate incurred environmental liability leading to both a pre-petition claim and an administrative expense.

## 5. Cleanup Costs Are Not Administrative Expense

Although several cases deny the environmental claimant administrative expense status for post-petition cleanup, most of these cases involve a nondebtor-lessor.<sup>324</sup> All of the cases involve property that was not property of the estate,<sup>325</sup> i.e., the debtor did not own the property as of the commencement of the case.

For example, in *Burlington Northern Railroad v. Dant & Russell, Inc. (In re Dant & Russell)*,<sup>326</sup> the debtor-lessee rejected a lease containing contaminated property. The landlord contended it was entitled to administrative expense priority because it was jointly liable with the debtor under CERCLA for the cleanup costs caused by the debtor's use of the premises.<sup>327</sup> Denying the landlord's request, the Ninth Circuit distinguished the landlord's expenses from costs that preserved or

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<sup>322</sup> *In re Chateaugay*, 944 F. 2d at 1010; see *Midlantic*, 474 U.S. at 507 (ruling bankruptcy trustee cannot abandon property in contravention of state or local laws designed to protect public health or safety and expenses to remove threat are necessary to preserve estate); *In re Stevens*, 68 B.R. at 783 (holding trustee could not abandon hazardous waste and had to comply with state environmental law with costs to do so entitled to administrative expense priority); *In re Wall Tube & Metal Prods., Co.*, 831 F. 2d at 123-24 (holding trustee could not abandon property in contravention of state statute designed to protect public health and response costs were actual and necessary to preserve estate in compliance with state law).

<sup>323</sup> See *supra* note 322.

<sup>324</sup> See, e.g., *Burlington N. R.R. v. Dant & Russell, Inc. (In re Dant & Russell, Inc.)*, 853 F.2d 700, 709 (9th Cir. 1988) (denying non-debtor lessor administrative expense status for its post-petition contamination cleanup costs caused by debtor-lessee's operation of wood treatment facility); *Gull Indus., Inc. v. John Mitchell, Inc. (In re Hanna)*, 168 B.R. 386, 390-91 (B.A.P. 9th Cir. 1993) (denying adjacent landowner administrative expense priority for its costs to clean up debtor's pre-petition contamination of groundwater); *In re Unidigital, Inc.*, 262 B.R. 283, 288-89 (Bankr. D. Del. 2001) (denying landlord administrative expense priority for its costs to remove lessee's 30,000 pound printer and fluids); *In re McCrory Corp.*, 188 B.R. 763, 770 (Bankr. S.D.N.Y. 1995) (denying nondebtor-lessor administrative expense priority for its clean-up costs of debtor-lessee's truck terminal); *In re Biocoastal Corp.*, 147 B.R. 258, 260-61 (Bankr. M.D. Fla. 1992) (denying plaintiff administrative expense priority because debtor no longer owned property).

<sup>325</sup> See generally *In re Dant & Russell, Inc.*, 853 F.2d at 700 (involving debtor-lessee who had rejected leased premises); *In re Hanna*, 168 B.R. at 386 (pertaining to clean-up costs of adjacent landowner's property and not debtor's property); *In re McCrory*, 188 B.R. at 763 (denying administrative expense priority because lease was not currently property of estate); *In re Biocoastal*, 147 B.R. at 258 (denying plaintiff administrative expense priority).

<sup>326</sup> 853 F.2d 700 (9th Cir. 1988).

<sup>327</sup> *Id.* at 708; see 42 U.S.C. § 9601(21) (2000) (defining "person" to include "firm, corporation, association, partnership, consortium, joint venture [and] commercial entity . . ."). But see *Midlantic*, 474 U.S. at 507 (reserving question of priority status of environmental clean-up costs while holding trustee could not abandon property in contravention of state statute or regulation reasonably designed to protect public health or safety from identifiable hazards); *In re Chateaugay Corp.*, 944 F.2d at 1010 (holding debtor's unincurred response costs for pre-petition releases were general unsecured claim dischargeable in its bankruptcy).

benefited the estate.<sup>328</sup> According to the court, the landlord's prospective claim for cleanup costs and its claim for reimbursement of costs already expended arose from pre-petition activities.<sup>329</sup> Therefore, its right to payment was a general, pre-petition, unsecured claim. The court rejected the landlord's appeal to public policy and concern for the environment: "Congress alone fixes priorities . . . Courts are not free to formulate their own rules of super or sub-priorities within a specifically enumerated class."<sup>330</sup>

Similarly, in *In re Unidigital*, the court denied administrative expense priority to a landlord who had to remove a 30,000 pound printer and then dispose of its chemicals.<sup>331</sup> Because the printer posed no imminent threat of harm,<sup>332</sup> the court authorized the debtor to abandon the printer. The landlord argued the estate was still liable for its removal even if the debtor could abandon it.<sup>333</sup> The court adopted a narrow view of what qualifies as an administrative expense. The expense had to arise from a post-petition transaction between the estate and the creditor and it had to be necessary to preserve the estate.<sup>334</sup> According to the court, a narrow view of

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<sup>328</sup> *In re Dant & Russell, Inc.*, 853 F.2d at 709; see 11 U.S.C. § 503(b)(1)(A) (2000) ("[T]here should be allowed, administrative expenses . . . including . . . the actual, necessary costs and expenses of preserving the estate . . ."). Compare *Ohio v. Kovacs*, 469 U.S. 274, 282–83 (1985) (holding state of Ohio's injunction directing hazardous waste clean-up was general unsecured claim) and *S. Ry. Co. v. Johnson Bronze Co.*, 758 F.2d 137, 141 (denying lessor administrative expense priority against debtor in possession and sublessee for hazardous clean-up costs because lessor had general unsecured contract indemnity claim) with *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 124 (granting administrative expense priority to state for CERCLA response costs) and *In re Stevens*, 68 B.R. at 783 (granting administrative expense priority to state for costs incurred removing waste from property of estate).

<sup>329</sup> *In re Dant & Russell, Inc.*, 853 F.2d at 709; see *Juniper Dev. Group v. Kahn (In re Hemingway Transp., Inc.)*, 73 B.R. 494, 503 (Bankr. D. Mass. 1987) (granting administrative expense priority when liability for CERCLA costs arose post-petition). But see *In re Chateaugay*, 944 F.2d at 1010 (granting administrative expense claim for post-petition costs from pre-petition activity when costs incurred to preserve estate).

<sup>330</sup> *In re Dant & Russell, Inc.*, 853 F.2d at 709 (citing 3 COLLIER ON BANKRUPTCY ¶ 507.02[3], at 507–15 (Lawrence P. King et al. eds., 15th ed. rev. 1997) (discussing 11 U.S.C. § 507 (a) (1–7) priorities); see *Kovacs*, 469 U.S. at 286 (O'Connor, J., concurring) ("[A] state may protect its interests in the enforcement of its environmental laws by giving cleanup judgments the status of statutory liens or secured claims.")).

<sup>331</sup> *In re Unidigital, Inc.*, 262 B.R. 283, 285 (Bankr. D. Del. 2001).

<sup>332</sup> *Id.* at 287; see *Midlantic*, 474 U.S. at 507 (holding trustee may not abandon property in contravention of state statute or regulation reasonably designed to protect public health or safety from identified hazards); see, e.g., *Borden, Inc. v. Wells-Fargo Bus. Credit (In re Smith-Douglass, Inc.)*, 856 F.2d 12, 15 (4th Cir. 1988) (allowing abandonment because violations of state environmental laws did not pose serious imminent public health risks); *In re Franklin Signal Corp.*, 65 B.R. 268, 271–72 (Bankr. D. Minn. 1986) (holding trustee could abandon fourteen drums of various chemicals only if trustee took adequate precautionary measures to ensure no imminent danger to public).

<sup>333</sup> *In re Unidigital, Inc.*, 262 B.R. at 288; see *Pa. Dep't of Env'tl. Res. v. Conroy*, 24 F.3d 568, 569–70 (3d Cir. 1994) (holding costs necessary to remedy contamination were necessary to preserve estate given trustee could not abandon property under *Midlantic*). But see *In re Mahoney-Troast Constr. Co.*, 189 B.R. 57, 61 (Bankr. D.N.J. 1995) (denying non-debtor landlord administrative expense priority for cleanup costs when no imminent public harm existed and landlord acted voluntarily).

<sup>334</sup> *In re Unidigital, Inc.*, 262 B.R. at 288; see *Microsoft Corp. v. DAK Indus., Inc. (In re DAK Indus., Inc.)*, 66 F.3d 1091, 1095–96 (9th Cir. 1995) (denying administrative expense priority when debt arose pre-petition and no post-petition consideration was provided); *Gen. Am. Transp. Corp. v. Martin (In re Mid Region Petroleum, Inc.)*, 1 F.3d 1130, 1133 (10th Cir. 1993) (affirming disallowance of administrative expense priority for post-petition rent when debtor did not receive benefit from leased railcars).

administrative expense minimized administrative costs, preserved the estate's scarce resources and maximized the distribution to creditors.<sup>335</sup> Because the debtor had rejected the lease, all claims associated with the rejection were pre-petition, unsecured claims.<sup>336</sup> Moreover, the landlord had failed to prove how its removal had conferred a substantial benefit to the estate.<sup>337</sup> According to the court, it was "not enough to simply assert that the expense was incurred post-petition with regard to estate property to protect public health and welfare."<sup>338</sup>

The court also rejected the landlord's tort claims of trespass and nuisance. *Reading v. Brown* did not apply: "[T]he tort, if, in fact, there was one, did not arise from the operation of the Debtors' business."<sup>339</sup>

## 6. The Compromise Position: Some Administrative Expense, Some Not

Some courts have taken a middle ground. For example, the cleanup cost is an administrative expense to the extent the debtor in possession or the estate caused the environmental harm.<sup>340</sup> So, too, to the extent the estate must remedy the harm, the

<sup>335</sup> *In re Unidigital, Inc.*, 262 B.R. at 288; see *Stellwagen v. Clum*, 245 U.S. 645, 617 (1918) (describing bankruptcy system's general goal as giving debtors fresh start after fair property distribution for benefit of creditors); *In re Mid Region Petroleum, Inc.*, 1 F.3d at 1134 (identifying chapter 11 goal as keeping administrative costs at minimum to preserve debtor's scarce resources and encourage rehabilitation).

<sup>336</sup> *In re Unidigital, Inc.*, 262 B.R. at 288; see 11 U.S.C. § 502(g) (2000) (providing "rejection . . . of . . . unexpired lease of debtor . . . shall be determined the same as if such claim had arisen before the date of the filing of the petition"); see also *Burlington N. R.R. v. Dant & Russell, Inc.* (*In re Dant & Russell, Inc.*), 853 F.2d 700, 709 (9th Cir. 1988) (finding rejection of lease containing contaminated property was pre-petition conduct).

<sup>337</sup> *In re Unidigital, Inc.*, 262 B.R. at 288; see *In re Mid Region Petroleum, Inc.*, 1 F.3d at 1134 (affirming disallowance of administrative expense priority for post-petition rent when debtor did not receive benefit from leased railcars); *United States v. LTV Corp.* (*In re Chateaugay Corp.*), 944 F.2d 997, 1010 (2d Cir. 1991) (finding administrative expense priority when obligation in question arose from transaction with debtor in possession and resulted in direct benefit to estate).

<sup>338</sup> *In re Unidigital, Inc.*, 262 B.R. at 289 (quoting *In re Allen Care Ctrs., Inc.*, 163 B.R. 180, 186 (Bankr. D. Or. 1994) (holding costs of closing operation are not administrative expenses)); see also *Gull Indus., Inc. v. John Mitchell, Inc.* (*In re Hanna*), 168 B.R. 386, 390-91 (B.A.P. 9th Cir. 1994) (denying adjacent landowner administrative expense for cleanup costs caused by debtor's pre-petition oil leakage, when post-petition contamination was passive and cleanup did not benefit estate); *In re McCrory Corp.*, 188 B.R. 763, 770 (Bankr. S.D.N.Y. 1995) (denying non-debtor lessor administrative expense and holding debtor could abandon lease because there was no imminent public harm, the estate no longer owned the property and the cleanup did not benefit estate).

<sup>339</sup> *In re Unidigital, Inc.*, 262 B.R. at 290; see *Reading Co. v. Brown*, 391 US 471, 482 (1968) (favoring those injured by operation of business in bankruptcy by permitting them to recover ahead of creditors who would have benefited but for the tort); see also *In re Motel Invs. of Christiansburg L.L.C.*, 307 B.R. 536, 538-39 (Bankr. W.D. Va. 2004) (following *Unidigital* in denying administrative expense priority when no injuries arose from post-petition operation of debtor's business); Heidt, *supra* note 219, at 134-35 (noting bankruptcy policy requires claim to arise when wrongful act is committed).

<sup>340</sup> See 11 U.S.C. § 503(b)(1)(A) (2000) ("After notice and a hearing, there shall be allowed, administrative expenses, other than claims allowed under section 502(f) of this title, including -the actual, necessary costs and expenses of preserving the estate, including wages, salaries, or commissions for services rendered after the commencement of the case."); see, e.g., *Reading*, 391 U.S. at 485 (holding damages resulting from post-petition negligence by manager of estate property should constitute administrative expense); *In re Pierce Coal & Constr., Inc.*, 65 B.R. 521, 530 (Bankr. N.D.W. Va. 1986) (expenses incurred to operate estate are actual, necessary costs and expenses of preserving estate and therefore, damages chapter 7 trustee caused in



expenditure is an administrative expense.<sup>341</sup>

## 7. Post-petition Fines & Penalties as Administrative Expense

Most courts rely on *Reading v. Brown* to hold post-petition *compensatory* civil fines are "actual and necessary" costs to preserve the estate, and therefore, they are entitled to administrative expense treatment. In the words of *Spunt v. Charlesbank Laundry, Inc. (In re Charlesbank Laundry Inc.)*:<sup>342</sup>

The debtor in this case *deliberately* continued a violation of law month after month presumably because it was more lucrative for the business to operate outside the zoning ordinance than within it. If fairness dictates that a tort claim based on negligence should be paid ahead of pre-reorganization claims, then, *a fortiori*, an intentional act which violates the law and damages others should be so treated.<sup>343</sup>

*Reading's* and *Charlesbank's* reasoning seems to support similar treatment for *noncompensatory* fines. The Eleventh Circuit was the first to rule on this issue. In *Alabama Surface Mining Commission v. N.P. Mining Co. (In re N.P. Mining Co.)*,<sup>344</sup> the court held that noncompensatory, punitive civil fines for post-petition

operating estate are entitled to administrative expense status: pre-petition expenses occasioned by pre-petition debtor are not); Heidt, *supra* note 219, at 149 (stating costs entitled to administrative expense status only if debtor continues to own or operate contaminated property or estate is liable for some post-petition environmental wrongdoing).

<sup>341</sup> See *Torwico Elecs., Inc. v. N.J. Dep't of Envtl. Prot. (In re Torwico Elecs.)*, 8 F.3d 146, 150 (3d Cir. 1993) (finding cleanup obligation unavoidable, wastes at issue must present an ongoing hazard (citing *In re Chateaugay*, 944 F.2d at 1008)); *In re Mahoney-Troast Constr. Co.*, 189 B.R. 57, 63 (Bankr. D.N.J. 1995) (explaining claim for reimbursement would enjoy administrative expense priority if contamination posed imminent threat to public, but no imminent threat found); Heidt, *supra* note 219, at 149 (stating administrative expense priority applies because estate must comply with applicable environmental law to retain property or continue in business). But see Daniel Klerman, *Earth First? CERCLA Reimbursement Claims And Bankruptcy*, 58 U. CHI. L. REV. 795, 798 (1991) (stating courts have liberally interpreted "imminent and substantial endangerment" requirement when approving administrative orders).

<sup>342</sup> 755 F.2d 200 (1st Cir. 1985); see *Ala. Surface Mining Comm'n v. N.P. Mining Co. (In re N.P. Mining Co.)*, 963 F.2d 1449, 1453 (11th Cir. 1992) ("[W]e find that punitive, civil penalties assessed for post-petition mining activities qualify as an administrative expense . . ."); *In re Bill's Coal Co.*, 124 B.R. 827, 829 (D. Kan. 1991) ("The court agrees that penalties assessed for *pre-petition* misconduct or the continuing effect of *pre-petition* misconduct should not be considered an administrative expense.") (emphasis added). But see *In re Motel Invs. of Christiansburg L.L.C.*, 307 B.R. at 538 (declining to follow holding in *Spunt*).

<sup>343</sup> *In re Charlesbank Laundry, Inc.*, 755 F.2d at 203; see *Reading*, 391 U.S. at 482 (stating tort claims arising during an arrangement are actual and necessary expenses because it is more natural and just to allow those injured by operation of business during arrangement to recover ahead of those for whose benefit the business is carried on); see also *In re FBI Distrib. Corp.*, 330 F.3d 36, 41 (1st Cir. 2003) (noting administrative expenses are given first priority so businesses otherwise wary of dealing with chapter 11 businesses will provide goods and services); *Yorke v. NLRB*, 709 F.2d 1138, 1143 (7th Cir. 1983) (citing *Reading*, 391 U.S. at 482-84, and holding "those injured during administration of estate by Trustee entitled to priority claim as administrative expense").

<sup>344</sup> 963 F.2d 1449 (11th Cir. 1992).

violations of environmental regulations were entitled to administrative priority. In reaching this conclusion, the court relied on 28 U.S.C. § 959(b)'s requirement that the trustee manage and operate the property in compliance with state law.<sup>345</sup>

We find that a policy of ensuring compliance by trustees with state law is sufficient justification to place civil penalties assessed for postpetition mining operations in the category of [costs that] are accorded administrative-expense priority . . . Even though these civil penalties are not compensatory, it makes sense that when a trustee or debtor in possession operates a bankruptcy estate, compliance with state law should be considered an administrative expense. Otherwise, the bankruptcy estate would have an unfair advantage over non-bankrupt competitors. A mining operation could, under the protection of chapter 11, cut costs by ignoring safety and environmental violations.<sup>346</sup>

As another court noted, debtors in possession "do not have carte blanche to ignore" state and local environmental laws.<sup>347</sup> The Third Circuit, however, apparently disagrees.<sup>348</sup>

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<sup>345</sup> 28 U.S.C. § 959(b) (2000); see *Lancaster v. Tennessee (In re Wall Tube & Metal Prods. Co.)*, 831 F.2d 118, 122 (6th Cir. 1987) (stating 28 U.S.C. § 959(b) applied whether trustee was liquidating or reorganizing and emphasizing importance of complying with laws designed to protect public health and safety); *In re Laurinburg Oil Co.*, 49 B.R. 652, 654 (Bankr. M.D.N.C. 1984) ("The provisions of 28 U.S.C. § 959(b) require a debtor in possession to manage and operate the property according to the valid laws of the state in which the property is situated."); Heidt, *supra* note 219, at 141 (stating section 959(b) of title 28 reinforces need to comply with all applicable state rules so debtors do not gain competitive advantage).

<sup>346</sup> *In re N.P. Mining Co.*, 963 F.2d at 1458; see *Cumberland Farms, Inc. v. Fla. Dep't of Envtl. Prot.*, 116 F.3d 16, 21 (1st Cir. 1997) (concluding "it would be fundamentally unfair to allow Cumberland Farms to flout Florida's environmental protection laws and escape paying a penalty for such behavior"); *In re Chateaugay Corp.*, 112 B.R. at 525.

To the extent that [the debtor] continues to own and operate sites post-petition where there has been a release or threatened release of hazardous waste, [the debtor] is, under the law, under a continuing obligation to comply with the environmental laws . . . In addition, for the same reasons, civil penalties for post-petition violations would also be entitled to be treated as administrative expenses.

*Id.*; see also *Utah Div. of Oil, Gas & Mining v. Kaiser Steel Corp. (In re Kaiser Steel Corp.)*, 87 B.R. 662, 665 (Bankr. D. Colo. 1988) (concluding chapter 11 debtor must comply with Utah environmental laws in conduct of post-petition mining operations).

<sup>347</sup> *Cumberland Farms, Inc.*, 116 F.3d at 20; see *Midlantic Nat'l Bank v. N.J. Dep't of Envtl. Prot.*, 474 U.S. 494, 507 (1986) (holding debtor cannot abandon contaminated property in violation of state law designed to protect public safety); see also *In re Wall Tube & Metal Prods. Co.*, 831 F.2d at 121-22 (referring to *Midlantic*); *Pa. Dep't of Envtl. Res. v. Conroy (In re Conroy)*, 24 F.3d 568, 569 (3d Cir. 1994) (following holding in *Midlantic*); *In re Chateaugay Corp.*, 944 F.2d at 1010 (following holding in *Midlantic*); Denise M. Schuh, *The Cents of it: Dischargeability and Environmental Claims Under the Bankruptcy Code*, 14 N. ILL. U. L. REV. 191, 218 (1993) (noting Congress expressed legislative determination that trustee does not have carte blanche to ignore non-bankruptcy law but must yield to governmental interest in public health and safety).

<sup>348</sup> *Pa. Dep't of Envtl. Res. v. Tri-State Clinical Labs., Inc.*, 178 F.3d 685 (3d Cir. 1999), *cert. denied*, 528 U.S. 1075 (2000); see John W. Ames & Lisa H. Thomas, *Criminal Fines as Administrative Expenses? Don't Count on It . . .*, 18 AM. BANK. INST. J. 8, at 8 (Oct. 1999) (stating Third Circuit in *Tri-State Clinical Labs*

Tri-State Clinical Laboratories filed chapter 11 on August 14, 1990.<sup>349</sup> Shortly thereafter, two city workers were sprayed with human blood while emptying trash dumpsters behind Tri-State's lab. The blood came from test tubes that Tri-State had illegally placed in the dumpsters. In 1994, Tri-State was prosecuted and convicted for violating Pennsylvania's Solid Waste Management Act. It was fined \$10,000 for pre-petition and \$20,000 for post-petition violations.

The bankruptcy court and the district court refused to give the post-petition fine administrative priority. The Third Circuit affirmed. It concluded that neither Congress in drafting section 503(b)(1)(A), nor *Reading* in interpreting its predecessor statute, intended a broad reading of "actual and necessary" expenses: "[W]e believe Congress intended only for those 'actual necessary costs and expenses' that arise in the context of, or compensate for, legitimate business activity, or the losses resulting therefrom, to be treated as expenses of preserving the estate, and accorded priority as an administrative expense."<sup>350</sup>

In its view, "it does not follow that criminal fines and the conduct they attempt to punish are ordinarily incident to operating a business."<sup>351</sup> The court scoffed at the notion that a "legitimate" business might choose to violate laws because it was cheaper to do so.<sup>352</sup> Yet why else would the debtor in *Tri-State* have done what it did? Unless we assume that the debtor dumped the blood to harm others, it could only have done so because it was the cheapest way to dispose of it. Therefore, unless such a fine is treated as an administrative expense, debtors will have an economic incentive not to comply with environmental regulations, and will thereby gain an economic advantage over their law-abiding competitors. Indeed under *Tri-State's* reasoning, the worse the behavior, the less appropriate administrative

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held punitive criminal fines arising from post petition conduct are not administrative expenses); see also DeSimone, *supra* note 284 at 526 (stating *Tri-State Clinical Labs* "continued the bleak trend away from allowing post-petition environmental fines as administrative expenses.").

<sup>349</sup> *Tri-State Clinical Labs., Inc.*, 178 F.3d at 687; see also Ames & Thomas, *supra* note 348, at 526 (discussing Third Circuit in *Tri-State Clinical Labs*); DeSimone, *supra* note 284, at 526 (referring to facts of *Tri-State Clinical Labs*).

<sup>350</sup> *Tri-State Clinical Labs., Inc.*, 178 F.3d at 693; see *Burlington N. R.R. v. Dant & Russell, Inc.* (*In re Dant & Russell, Inc.*), 853 F.2d 700, 707 (9th Cir. 1988) (stating section 503(b)(1)(A)'s clear intent that administrative expenses be actual, necessary costs of preserving estate); *In re Nat'l Refractories & Minerals Corp.*, 297 B.R. 614, 617 (Bankr. N.D. Cal. 2003) (noting under section 503(b)(1) terms "actual" and "necessary" are construed narrowly); *In re Unidigital, Inc.*, 262 B.R. 283, 288 (Bankr. D. Del. 2001) (noting statutory provisions granting administrative expense priorities must be narrowly construed).

<sup>351</sup> *Tri-State Clinical Labs., Inc.*, 178 F.3d at 692. But see *In re N.P. Mining Co.*, 963 F.2d at 1458 (concluding fine for violating environmental regulations is cost ordinarily incident to operation of business); *Cumberland Farms, Inc.*, 209 B.R. at 793 (holding debtor in possession violated state environmental laws and compliance with state law should be considered administrative expense); *In re Bill's Coal Co.*, 124 B.R. 827, 830 (Bankr. D. Kan. 1991) ("[A] fine for the violation of environmental regulations should be considered a cost ordinarily incident to operation of a business.").

<sup>352</sup> *Tri-State Clinical Labs., Inc.*, 178 F.3d at 693; see DeSimone, *supra* note 284, at 534 ("Given *Tri-State*, why not simply lower overhead by ignoring burdensome and expensive environmental regulations? And if convicted of such misconduct, the violator need not fear any substantial criminal sanction."); Heidt, *supra* note 219, at 140 (permitting debtor to disregard environmental obligation would give debtor in bankruptcy competitive advantage over others because debtors could manufacture their products at cheaper cost because they would not be required to comply with applicable regulations).

priority treatment for the noncompensatory fine.<sup>353</sup>

Given the clear split in the circuits, it is somewhat surprising that the Supreme Court denied certiorari,<sup>354</sup> but the First and Eleventh Circuits have the better arguments based on both bankruptcy *and* environmental policy.

*F. Contingent Claims for Reimbursement or Contribution against Debtor: Section 502(e)(1)(B)*

11 U.S.C. § 502(e)(1)(B) provides:

Notwithstanding subsections (a), (b), and (c) of this section and paragraph (2) of this subsection, the court shall disallow any claim for reimbursement or contribution of an entity that is liable with the debtor on or has secured the claim of a creditor, to the extent that -

... (B) such claim for reimbursement or contribution is contingent as of the time of allowance or disallowance of such claim for reimbursement or contribution.

This language suggests disallowance of a PRP's contribution claim against a debtor-PRP for future, i.e., unincurred, response costs. Bankruptcy discharges a disallowed claim every bit as much as an allowed claim.<sup>355</sup> How does disallowance of contingent claims for contribution square with Congress's goal of equitable allocation of the cleanup costs among responsible parties? In a word, not very well.

Judge Cyr wrote an especially thoughtful opinion on the subject. In *Juniper Development Group v. Kahn (In re Hemingway Transport, Inc.)*,<sup>356</sup> the debtors owned and operated a trucking business. They petitioned for bankruptcy relief in July, 1982. A local developer, Juniper, purchased the facility from the debtor in

<sup>353</sup> In distinguishing *In re N.P. Mining Co., Inc.*, the court stated: "[w]e are not convinced the court's holding [in *N.P. Mining*] would be the same if it were faced with the kind of reckless conduct in which Tri-State engaged." *Tri-State Clinical Labs., Inc.*, 178 F.3d at 698; see also DeSimone, *supra* note 284, at 534 (concluding Third Circuit has condoned excusing corporation for its hazardous criminal violations in interest of creditor compensation).

<sup>354</sup> *Pa. Dep't of Env'tl. Res. v. Tri-State Clinical Labs., Inc.*, 178 F.3d 685 (3d Cir. 1999), *cert. denied*, 528 U.S. 1075 (2000).

<sup>355</sup> 11 U.S.C. § 1141(d)(1) (2000) provides:

Except as otherwise provided in this subsection, in the plan, or in the order confirming the plan, the *confirmation of a plan* -

(A) *discharges the debtor from any debt that arose before the date of such confirmation*, and any debt of a kind specific in section 502(g), 502(h), or 502(i) of this title, *whether or not* -

(i) a proof of the claim based on such debt is filed or deemed filed under section 501 of this title;

(ii) *such claim is allowed under section 502 of this title* . . . .

*Id.* (emphasis added). See generally Schuh, *supra* note 347, at 218 (stating congressional concern over public health and safety should extend to consider whether to enact dischargeability exception).

<sup>356</sup> 993 F.2d 915 (1st Cir. 1993).

possession in April, 1983 for \$1.6 million.<sup>357</sup> In April 1985, drums containing hazardous substances were found at the facility. The EPA notified Juniper, the purchaser, that it was a potentially responsible party under CERCLA. It ordered Juniper to remove the substances from the facility. Juniper incurred \$92,088 to comply with the EPA administrative order. It instituted an adversary proceeding against Hemingway Transport's estate for CERCLA response costs already incurred and future response costs to complete the remediation.<sup>358</sup> Judge Cyr wrote:

Juniper finds itself stranded at the increasingly crowded "intersection" between the discordant legislative approaches embodied in CERCLA and the Bankruptcy Code . . . CERCLA's settled policy objectives, reemphasized in the Superfund Amendments and Reauthorization Act of 1986 ("SARA"), prominently include the expeditious cleanup of sites contaminated or threatened by hazardous substance releases which jeopardize public health and safety, and the equitable allocation of cleanup costs, among all potentially responsible persons ("PRPs") . . . To foster CERCLA's primary objective—promotion of spontaneous private cleanup initiatives—all PRPs are deemed strictly liable for the total response costs required to remediate the contaminated facility.<sup>359</sup>

Moreover, CERCLA permits equitable allocation of liability by permitting PRPs to sue other PRPs for contribution. This encourages quick responses because one PRP, who takes the initiative and pays for the remediation, knows and can hold other PRPs liable.<sup>360</sup> But section 502(e)(1)(B) seems to preclude CERCLA's intended equitable allocation of responsibility: "There can be little doubt that but for section 502(e)(1)(B), the [debtor's estate] would share some measure of financial responsibility for the anticipated \$6.2 million in future response costs on which the Juniper claim is based."<sup>361</sup>

Judge Cyr carefully dissected section 502(e)(1)(B). It disallows a "claim of a codebtor who is liable with the debtor on the claim of a creditor."<sup>362</sup> He assumed

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<sup>357</sup> *Id.* at 919.

<sup>358</sup> *Id.* at 920.

<sup>359</sup> *Id.* at 921.

<sup>360</sup> *Id.* at 922; *accord* Dant & Russell, Inc. v. Burlington N. R.R. Co. (*In re* Dant & Russell, Inc.), 951 F.2d 246, 248 (9th Cir. 1991) (noting CERCLA private right of action encourages quick voluntary action because it allows private parties to recover their cleanup costs from PRPs). *See generally* H.R. REP. NO. 99-253, pt. 1, at 80 (1985) (noting CERCLA should make private parties more willing to bear costs of cleanup because they can attempt to recover part of their expenses from other PRPs through contribution litigation).

<sup>361</sup> *In re Hemingway Transp., Inc.*, 993 F.2d at 922.

<sup>362</sup> *Id.* at 925; *see* Syntex Corp. v. Charter Co. (*In re* Charter Co.), 862 F.2d 1500, 1503 (11th Cir. 1989) (concluding contingent CERCLA contribution claims are the type excusable under section 502(e)(1)(B)). *But see In re* G-I Holdings, Inc., 308 B.R. 196, 212 (Bankr. D.N.J. 2004) (finding debtor's contribution liability to another PRP under CERCLA was direct and therefore not subject to disallowance under section 502).

the EPA was a creditor because its contingent right to payment accrued while the debtor owned and operated the facility where the hazardous waste disposal had occurred.<sup>363</sup> Further, Juniper was co-liable with the debtor to the EPA, a creditor.

Concluding that Congress did not exempt CERCLA claims from disallowance, he disallowed Juniper's claim for future response costs:

[S]ection 502(e)(1)(B) may impede CERCLA's *subsidiary* policy of promoting equitable allocations of environmental cleanup costs among responsible parties, [but] pre-"fixing" disallowance does not conflict with CERCLA's *primary* goal—encouraging targeted PRPs to initiate cleanup efforts as expeditiously as practicable in the expectation that their contingent claims may become "fixed" in time for allowance against the debtor estate.<sup>364</sup>

But, relying on the policy underlying section 502(e)(1)(B), which is to prevent double-dipping against the estate, Cyr further held that if the EPA did not file a claim and no one filed a claim on behalf of the EPA, Juniper could file its own claim for future response costs.<sup>365</sup>

In another section 502(e)(1)(B) case,<sup>366</sup> the Sixth Circuit held that section 502(e)(1)(B) might disallow the contingent claim of a party co-liable with the debtor even though the bar date had passed and the EPA had not filed a claim. According to the court, the debtor and the EPA were in negotiations and the EPA still might file a claim. The bar date was not absolute. Therefore, the EPA's failure to file a claim by the bar date did not mean the debtor and non-debtor PRP were not co-liable.<sup>367</sup>

Chief Judge Martin concurred that it was premature to disallow the claim for contribution. Nevertheless, he was concerned that the court's opinion and *Pioneer Investment Services Co. v. Brunswick Associates Limited Partnership*'s<sup>368</sup> excusable

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<sup>363</sup> *In re Hemingway Transp., Inc.*, 993 F.2d at 926; see *In re Harvard Indus., Inc.*, 153 B.R. 668, 671 (Bankr. D. Del. 1993) (recognizing EPA as creditor when it had right to payment from debtor under CERCLA).

<sup>364</sup> *In re Hemingway Transp., Inc.*, 993 F.2d at 924–25; see Goodwyn, *supra* note 212, at 811–12 (asserting section 502(e)(1)(B) should be read in harmony with CERCLA's goal of quick cleanup).

<sup>365</sup> *In re Hemingway Transp., Inc.*, 993 F.2d at 928. Judge Cyr also noted that Juniper's claim arose post-petition as a result of its post-petition purchase. If it qualified for the innocent landowner defense under CERCLA, it would be entitled to administrative expense priority for incurred cleanup costs. There was no evidence that the estate contracted away its obligation to contribute or bargained for a right of indemnification. *Id.* at 930. The \$1.6 million purchase price benefited the estate and presumably supported the requisite baseline "consideration" for Juniper's right to contribution. *Id.* The court pointed out that section 502(e)(1)(B) is not limited to creditors. It disallows any contingent claim for contribution. That includes post-petition claimants as well as creditors.

<sup>366</sup> *Norpak Corp. v. Eagle-Picher Indus., Inc. (In re Eagle-Picher Indus. Inc.)*, 131 F.3d 1185 (6th Cir. 1997).

<sup>367</sup> *Id.* at 1188–89.

<sup>368</sup> 507 U.S. 380 (1993), *aff'g In re Pioneer Inv. Servs. Co.*, 943 F.2d 673 (6th Cir. 1991) (holding courts may accept late filings caused by inadvertence, mistake, carelessness or intervening circumstances beyond party's control).

neglect rule could permit parties:

[T]o hide behind the shield of a bankruptcy claim to escape responsibility for their lack of sound environmental stewardship . . . .

The majority opinion requires the disallowance of contingent claims against debtors when the debtor and claimant are potentially co-liable to a third party. Debtors could, however, argue that if that third party *does* actually bring a claim against the debtor, the majority opinion still allows the debtor to raise its bankruptcy as a defense. This is, in fact, what [the debtor] concedes it plans to do if the [EPA] or the New Jersey Department of Environmental Protection and Energy bring a claim against it. In doing so, [the debtor] is clearly relying on the hope that [the purchaser's] claims will be disallowed, its bankruptcy defense will be accepted, and it will be able to walk away from the mess it made without bearing any responsibility for it. This cannot be allowed.<sup>369</sup>

To read this case as allowing such a scenario contravenes Congress's clear intention in passing CERCLA. By passing CERCLA, Congress intended to respond efficiently and expeditiously to toxic spills, and to *hold those parties responsible for the release of environmental toxins liable for the costs of the clean-up* . . . Interpreting *Pioneer Investment Services* or the majority's opinion as allowing polluters to circumvent CERCLA's goals would be tantamount to turning a blind eye to clear Congressional mandate. Such flagrant disregard for legislative intent should not be tolerated.<sup>370</sup>

#### IV. THE STATE'S INTEREST IN ENVIRONMENTAL ISSUES & ISSUES OF SOVEREIGN IMMUNITY

State governments are often intensely interested in bankruptcy proceedings involving "environmentally challenged" property. Adjudicating a state's claim or other interest in a debtor's bankruptcy implicates a state's Eleventh Amendment sovereign immunity to suits in federal court.<sup>371</sup> In 1994, Congress substantially amended section 106(a) and (b) and added a new subsection (c)<sup>372</sup> in an attempt to

<sup>369</sup> *In re Eagle-Picher Indus.*, 131 F.3d at 1191 (Martin, J., concurring).

<sup>370</sup> *Id.* For a detailed discussion, see Kenneth W. Maxwell, *Bankrupting CERCLA: Amending the Bankruptcy Code to Allow CERCLA Contingent Claims for Contribution*, 13 J. ENERGY NAT. RESOURCES & ENVTL. L. 431 (1993).

<sup>371</sup> A detailed description of the origins and development of Eleventh Amendment jurisprudence is well beyond the scope of these materials. For a recent study of those issues, see Caleb Nelson, *Sovereign Immunity as a Doctrine of Personal Jurisdiction*, 115 HARV. L. REV. 1559 (2002).

<sup>372</sup> 11 U.S.C. § 106(a)-(c) (2000), as amended by Bankruptcy Reform Act of 1994, § 113, Pub. L. 103-394, 108 Stat. 4117 (1994).

eliminate sovereign immunity for both federal and state government units.<sup>373</sup> In *Seminole Tribe of Florida v. Florida*,<sup>374</sup> the Supreme Court interpreted the reach of the Eleventh Amendment's<sup>375</sup> grant of sovereign immunity to the states. *Seminole*

Waiver of sovereign immunity:

(a) Notwithstanding an assertion of sovereign immunity, sovereign immunity is abrogated as to a governmental unit to the extent set forth in this section with respect to the following:

(1) Sections 105, 106, 107, 108, 303, 346, 362, 363, 364, 365, 366, 502, 503, 505, 506, 510, 522, 523, 524, 525, 542, 543, 544, 545, 546, 547, 548, 549, 550, 551, 552, 553, 722, 724, 726, 728, 744, 749, 764, 901, 922, 926, 928, 929, 944, 1107, 1141, 1142, 1143, 1146, 1201, 1203, 1205, 1206, 1227, 1231, 1301, 1303, 1305, and 1327 of this title.

(2) The court may hear and determine any issue arising with respect to the application of such sections to governmental units.

(3) The court may issue against a governmental unit an order, process, or judgment under such sections or the Federal Rules of Bankruptcy Procedure, including an order or judgment awarding a money recovery, but not including an award of punitive damages. Such order or judgment for costs or fees under this title or the Federal Rules of Bankruptcy Procedure against any governmental unit shall be consistent with the provisions and limitations of section 2412(d)(2)(A) of title 28.

(4) The enforcement of any such order, process, or judgment against any governmental unit shall be consistent with appropriate nonbankruptcy law applicable to such governmental unit and, in the case of a money judgment against the United States, shall be paid as if it is a judgment rendered by a district court of the United States.

(5) Nothing in this section shall create any substantive claim for relief or cause of action not otherwise existing under this title, the Federal Rules of Bankruptcy Procedure, or nonbankruptcy law.

(b) A governmental unit that has filed a proof of claim in the case is deemed to have waived sovereign immunity with respect to a claim against such governmental unit that is property of the estate and that arose out of the same transaction or occurrence out of which the claim of such governmental unit arose.

(c) Notwithstanding any assertion of sovereign immunity by a governmental unit, there shall be offset against a claim or interest of a governmental unit any claim against such governmental unit that is property of the estate.

*Id.*

<sup>373</sup> Congress seemed to have intended these amendments to reject the Supreme Court's interpretation of section 106 in *United States v. Nordic Village*, 503 U.S. 30 (1992), and *Hoffman v. Conn. Dept. of Income Maint.*, 494 U.S. 96 (1989); see 140 Cong. Rec. H10752, H10766 (daily ed. October 4, 1994) (statement of Rep. Brooks) ("This section would effectively overrule two Supreme Court cases that have held the States and Federal Government are not deemed to have waived their sovereign immunity by virtue of enacting § 106(c) of the Bankruptcy Code."). Both *Nordic Village* and *Hoffman* concerned the applicability of former section 106(c) to bankruptcy avoidance actions against governmental entities. In *Nordic Village*, the bankruptcy trustee sought to recover a preference from the Internal Revenue Service under sections 549(a) and 550(a). *Hoffman* involved two unrelated actions against agencies of the state of Connecticut under sections 543(b) and 547(b).

<sup>374</sup> 517 U.S. 44, 47 (1996) (analyzing whether Indian Commerce Clause grants Congress power to abrogate States' sovereign immunity); see Brett E. Cooper, Note, *Ageism, The ADEA, and the Ageless Debate Over Statutory Interpretation*, 74 ST. JOHN'S L. REV. 175 n.2 (2000) (explaining "*Seminole Tribe v. Florida*, 517 U.S. 44, 55 (1996) . . . overrul[ed] *Pennsylvania v. Union Gas Co.*, 491 U.S. 1 (1989) and announc[ed] a stringent two-part test to be utilized when analyzing legislation that abrogates Eleventh Amendment sovereign immunity."); Kenneth N. Klee et al., *State Defiance of Bankruptcy Law*, 52 VAND. L. REV. 1527, 1549 n.108 (1999) (noting Justice Stevens dissented in *Seminole Tribe*).

<sup>375</sup> U.S. CONST. amend. XI (stating "[t]he Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of



has cast doubt on section 106's constitutionality.

*Seminole Tribe* held that state sovereign immunity under the Eleventh Amendment extends to all suits against a state by any person, including its own citizens. This immunity is not absolute. States can waive sovereign immunity and Congress can abrogate it. Congressional abrogation requires Congress' unequivocally expressed intent to abrogate the immunity pursuant to valid exercise of a power rooted in the Fourteenth Amendment.<sup>376</sup>

In a paragraph with obvious relevance to section 106's continued viability, the Court stated:

[T]oday, we reconfirm that the background principle of state sovereign immunity embodied in the Eleventh Amendment is not so ephemeral as to dissipate when the subject of the suit is an area, like the regulation of Indian commerce, that is under the exclusive control of the Federal Government. Even when the Constitution vests in Congress complete law-making authority over a particular area, the Eleventh Amendment prevents congressional authorization of suits by private parties against unconsenting States. The Eleventh Amendment restricts the judicial power under Article III, and Article I cannot be used to circumvent the constitutional limitations placed upon federal jurisdiction.<sup>377</sup>

In response to Justice Stevens' plaint that *Seminole Tribe* prohibited federal jurisdiction over states in areas of exclusive federal jurisdiction, such as bankruptcy,

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another State, or by Citizens or Subjects of any Foreign State"); see Tanika Michelle Capers, *The Curtailment of Federal Court Jurisdiction: Seminole Tribe of Florida v. Florida*, 24 T. MARSHALL L. REV. 109, 111 (1998) ("[T]he Supreme Court construed the [Eleventh] Amendment to embody a constitutional right to sovereign immunity that arose from the structure of the Constitution itself and the spirit of the Eleventh Amendment."); Michelle Lawner, *Why Federal Courts Should Be Required to Consider State Sovereign Immunity Sua Sponte*, 66 U. CHI. L. REV. 1261, 1265 (1999) ("[T]he Supreme Court's Eleventh Amendment jurisprudence demonstrates a strong commitment to the principle of state sovereignty, and . . . [t]he Supreme Court has applied . . . the Eleventh Amendment expansively to guard state sovereignty and to limit the reach of federal jurisdiction.").

<sup>376</sup> See *Seminole Tribe*, 517 U.S. at 44, 47, 55 (determining whether Congress has abrogated the States' sovereign immunity depends on "whether Congress has 'unequivocally expresse[d] its intent to abrogate the immunity," and "whether Congress has acted 'pursuant to a valid exercise of power'" (citing *Green v. Mansour*, 474 U.S. 64, 68 (1985)); see also Cooper, *supra* note 274, at 181 (recognizing Supreme Court in *Seminole Tribe* established two-part test to determine whether legislation successfully abrogated Eleventh Amendment immunity. "A court must determine: (1) whether Congress has unequivocally expressed its intent to abrogate the states' immunity; and (2) whether Congress has acted pursuant to a valid exercise of power under Section 5 of the Fourteenth Amendment.").

<sup>377</sup> *Seminole Tribe*, 517 U.S. at 72, 73 (overruling *Pennsylvania v. Union Gas Co.*, 491 U.S. 1 (1989)); see *Bd. of Trs. of Univ. of Ala. v. Garrett*, 531 U.S. 356, 364 (2001) ("The Eleventh Amendment restricts the judicial power under Article III, and Article I cannot be used to circumvent the constitutional limitations placed upon federal jurisdiction." (quoting *Seminole Tribe*, 517 U.S. at 72)); *Kimel v. Fla. Bd. of Regents*, 528 U.S. 62, 78 (2000) ("Even when the Constitution vests in Congress complete lawmaking authority over a particular area, the Eleventh Amendment prevents congressional authorization of suits by private parties against unconsenting States." (quoting *Seminole Tribe*, 517 U.S. at 72)).

copyright, and antitrust,<sup>378</sup> the majority responded with words that chilled the blood of many participants in the bankruptcy system: "it has not been widely thought that the federal antitrust, bankruptcy, or copyright statutes abrogated the States' sovereign immunity. This Court never has awarded relief against a State under any of those statutory schemes."<sup>379</sup>

*Seminole Tribe* precipitated a wave of bankruptcy litigation. In some cases, states have directly challenged section 106's constitutionality, maintaining section 106 was based on an *invalid* exercise of congressional power.<sup>380</sup> In others, states have argued that states do not waive their sovereign immunity simply by filing a proof of claim or by participating in a bankruptcy case or proceeding.<sup>381</sup> In still

<sup>378</sup> See *Seminole Tribe*, 517 U.S. at 77 (Stevens, J., dissenting) (asserting majority opinion "prevents Congress from providing a federal forum for a broad range of actions against States, from those sounding in copyright and patent law, to those concerning bankruptcy, environmental law, and the regulation of our vast national economy"); see also *Id.* at 77 n.1 (Stevens, J., dissenting) (arguing "the majority's conclusion that the Eleventh Amendment shields States from being sued under them in federal court suggests that persons harmed by state violations of federal copyright, bankruptcy, and antitrust laws have no remedy"). See generally H. Stephen Harris, Jr. & Michael P. Kenny, *Eleventh Amendment Jurisprudence After Atascadero: The Coming Clash With Antitrust, Copyright, and Other Causes of Action Over Which the Federal Courts Have Exclusive Jurisdiction*, 37 EMORY L.J. 645, 652 (1988) (contending Supreme Court's interpretation of Eleventh Amendment has "threaten[ed] to undermine the federal antitrust and copyright laws," and has threatened "to deprive citizens injured by unlawful state action of a forum in which they can vindicate their federal rights").

<sup>379</sup> *Seminole Tribe*, 517 U.S. at 72, 73 n.16 (describing Justice Stevens' conclusion there is "no remedy" for state violations of federal bankruptcy, copyright, and antitrust statutes as "exaggerated both in its substance and in its significance"); see Craig Peyton Gaumer, *States' Rights and the Bankruptcy Code*, 22 AM. BANKR. INST. J. at 8 (stating Chief Justice Rehnquist essentially agreed *Seminole* would adversely affect debtors' ability to bring states into bankruptcy court); Kurt E. Springmann, *The Impact of Seminole on Intellectual Property Infringement by State Actors: The Interaction of Article I, Article III, the Eleventh Amendment, and the Fourteenth Amendment*, 29 ARIZ. ST. L.J. 889, 898 (1997) (hypothesizing "[t]he significance of [Chief Justice Rehnquist's] comment regarding a lack of tradition in enforcing copyright actions against states remains an open question").

<sup>380</sup> See, e.g., *Mitchell v. Cal. Franchise Tax Bd.* (*In re Mitchell*), 209 F.3d 1111, 1119–20 (9th Cir. 2000) (implicating section 106(a) was not remedial, "and thus was not an appropriate exercise of Congress' enforcement powers (even if Congress intended it to be)" and stipulating "[u]ntil Congress makes findings of a pattern of state violations and passes legislation that is proportional to its remedial claims, § 106(a) must be viewed as an unconstitutional assertion of Congress' power" concluding "Congress did not act within the scope of its abrogation power in enacting § 106(a)"); see also *Murphy v. Mich. Guar. Agency* (*In re Murphy*), 271 F.3d 629, 633 (6th Cir. 2001) (agreeing with court's reasoning in *Mitchell* and *Greenwood*, and holding "that an adversary proceeding to determine the dischargeability of a debt constitutes a suit within the ambit of the Eleventh Amendment"); *Dept. of Transp. & Dev. v. PNL Asset Mgmt. Co.* (*In re Estate of Fernandez*), 123 F.3d 241, 242 (5th Cir. 1997) (holding "Congress cannot constitutionally displace State's immunity by § 106(a) of the Bankruptcy Code."); *Tex. Higher Educ. Coordinating Bd. v. Greenwood* (*In re Greenwood*), 237 B.R. 128, 131 (Bankr. Tex. 1999) (noticing several lower courts, including United States Court of Appeals for Fifth Circuit, relied on *Seminole Tribe* and held "that § 106(a), which purports to abrogate sovereign immunity, violates the Eleventh Amendment and is therefore unconstitutional" declaring "[i]t is clear that Congress may not constitutionally abrogate state sovereign immunity in bankruptcy proceedings").

<sup>381</sup> See, e.g., *Schlossberg v. Maryland* (*In re Creative Goldsmiths, Inc.*), 119 F.3d 1140, 1143, 1149 (4th Cir. 1997), cert. denied, 523 U.S. 1075 (1998) (concluding state did not waive its immunity when state "filed an affirmative proof of claim in the debtor's bankruptcy to recover from the bankruptcy estate sales and withholding taxes which the debtor collected for the state from third parties"). But see *Gardner v. New Jersey*, 329 U.S. 565, 574 (1947) ("When the State becomes the actor and files a claim against the fund it

others, states have argued that *Ex Parte Young*<sup>382</sup> cannot be used for prospective declaratory or injunctive relief against a state official in her individual capacity. In effect, many states have argued, and many courts have agreed, that states are simply not subject to the jurisdiction of the bankruptcy courts.

Five circuit courts concluded that *Seminole Tribe* barred Congress from abrogating state sovereign immunity under the Bankruptcy Clause.<sup>383</sup> The Sixth Circuit broke with this near unanimous reading of *Seminole*, concluding that Congress could constitutionally abrogate state sovereign immunity.<sup>384</sup> Faced with a

waives any immunity which it otherwise might have had respecting the adjudication of the claim."); *Ga. Dep't of Revenue v. Burke* (*In re Burke*), 146 F.3d 1313, 1319–20 (11th Cir. 1998) (interpreting Supreme Court's decision in *Gardner* to establish "that, by filing a proof of claim in the debtor's respective bankruptcy proceedings, the State [of Georgia] waived its sovereign immunity for purposes of the adjudication of those claims," holding that such waiver included "the bankruptcy court's enforcement of the discharge injunction and the automatic stay."); *Stanley v. Student Loan Servs., Inc.* (*In re Stanley*), 273 B.R. 907, 911 (Bankr. N.D. Fla. 2002) ("The sovereign immunity afforded to States by the Eleventh Amendment to the United States Constitution was waived when the lender, acting pursuant to the instructions of the State, filed proofs of claim in [the] bankruptcy case.").

<sup>382</sup> 209 U.S. 123 (1908); *see, e.g.*, *Goldberg v. Ellett* (*In re Ellett*), 254 F.3d 1135, 1138 (9th Cir. 2001), *cert. denied*, 534 U.S. 1127 (2002) (referring to *Ex Parte Young* doctrine as "fiction" in which "a state officer who violates federal law in his official capacity, pursuant to his authority under state law, is nonetheless not a state agent for sovereign immunity purposes"). *But see* *Will v. Mich. Dep't of State Police*, 491 U.S. 58, 70 n.10 (1989) (recognizing "a state official in his or her official capacity, when sued for injunctive relief, would be a person under § 1983 because 'official-capacity actions for prospective relief are not treated as actions against the State'"); *Ex Parte Young*, 209 U.S. at 155–56, 159, 160 (asserting "individuals, who, as officers of the State, are clothed with some duty in regard to the enforcement of the laws of the State . . . may be enjoined by a Federal court of equity" from an action attempting "to enforce against parties affected an unconstitutional act, violating the Federal Constitution" adding when an official claims to be acting under the authority of the state and the act to be enforced is alleged to be unconstitutional, such official is "stripped of his official or representative character and is subjected in his person to the consequences of his individual conduct").

<sup>383</sup> U.S. CONST. art. I, § 8, cl. 4 (stating Congress has power "[t]o establish an uniform Rule of Naturalization, and uniform Laws on the subject of Bankruptcies throughout the United States"); *see also* *Nelson v. La Crosse County Dist. Attorney* (*In re Nelson*), 301 F.3d 820, 832 (7th Cir. 2002) (concluding Congress did not validly abrogate state sovereign immunity when enacting section 106(a)); *In re Mitchell*, 209 F.3d at 1121 ("Under *Seminole Tribe* . . . we conclude that Congress did not act within the scope of its abrogation power in enacting section 106(a)."); *Sacred Heart Hosp. v. Pennsylvania* (*In re Sacred Heart Hosp.*), 133 F.3d 237, 243–45 (3d Cir. 1998) (holding "the Bankruptcy Clause is not a valid source of abrogation power" and finding "§ 106(a) is unconstitutional to the extent that it purports to abrogate state sovereign immunity in federal court"); *In re Creative Goldsmiths, Inc.*, 119 F.3d at 1143, 1145, 1147 (repeating "[b]ecause the holding in *Seminole* extended to restrict all federal jurisdiction over the states based on Article I powers, we hold . . . that Congress has no authority under the Bankruptcy Clause . . . to abrogate state sovereign immunity in federal courts." Mentioning specifically "Congress' effort to abrogate the states' Eleventh Amendment immunity through its 1994 enactment of 11 U.S.C. § 106(a) is unconstitutional and ineffective"); *In re Estate of Fernandez*, 123 F.3d at 246, *as amended on denial of reh'g*, 130 F.3d 1138, 1139 (5th Cir. 1997) (rationalizing "[s]ection 106(a) of the Bankruptcy Code is unconstitutional," and instructing "Congress cannot locate the authority . . . to abrogate sovereign immunity in either the Bankruptcy Clause or in Section 5 of the Fourteenth Amendment.").

<sup>384</sup> *See Hood v. Tenn. Student Assistance Corp.* (*In re Hood*), 319 F.3d 755, 758, 762 (6th Cir. 2003), *aff'd on other grounds*, 124 S.Ct. 1905 (2004) (concluding "the text of the Constitution and other evidence of the Framers' intent demonstrate that under the Bankruptcy Clause of Article I, section 8, Congress has the power to abrogate state sovereign immunity"); *Mayes v. Cherokee Nation* (*In re Mayes*), 294 B.R. 145, 161 (B.A.P. 10th Cir. 2003) (McFeely, J., dissenting) (acknowledging *Hood's* Sixth Circuit decision found section 106(a) of Bankruptcy Code "was a valid abrogation of state sovereign immunity based on a constitutional compact

clear split in the circuits, the Supreme Court granted certiorari in *Hood v. Tennessee Student Assistance Corp.* on a single issue: the constitutionality of section 106 abrogation of sovereign immunity.<sup>385</sup> But rather than deciding the issue, the Court further muddled the waters. It held that discharge of a student loan debt did "not implicate a State's Eleventh Amendment immunity" because it is an appropriate exercise of the bankruptcy court's in rem jurisdiction.<sup>386</sup> As Justice Thomas noted, none of the lower courts had ruled on this issue, and none of the litigants had raised it before the Supreme Court.<sup>387</sup>

By ducking the issue for which it had granted certiorari, the Supreme Court has invited continued litigation on section 106's constitutionality. It has also opened a new can of especially plump and juicy worms: the relationship between a bankruptcy court's in rem jurisdiction and sovereign immunity.

In deciding *Hood*, the Supreme Court relied on its decision in *California v. Deep Sea Research, Inc.*<sup>388</sup> In *Deep Sea Research*, a treasure salvor filed an in rem admiralty action seeking title to a wreck that sank off the California coast in 1865. The State of California intervened to assert an ownership claim in the wreck, contending that the salvor's in rem action against the wreck was in effect a suit against the State barred by the Eleventh Amendment. In writing for the Court,

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between the states as expressed through the Constitution's uniformity requirement"). But see *id.* at 158 (McFeely, J., dissenting) (noticing "[t]here is little case law delineating what constitutes a clear and unequivocal abrogation of sovereign immunity").

<sup>385</sup> See *Tenn. Student Assistance Corp. v. Hood*, 539 U.S. 986, (2003) (granting petition for writ of certiorari to the United States Court of Appeals for Sixth Circuit); *Hood*, 124 S. Ct. at 1908–09 (recognizing grant of certiorari to determine whether Bankruptcy Clause grants Congress authority to abrogate state sovereign immunity from private suits, and affirming Court of Appeals judgment 11 U.S.C. § 106(a) was a valid abrogation of Tennessee Student Assistance Corporation's sovereign immunity); see also *id.* at 1915 (Thomas, J., dissenting) (acknowledging Supreme Court granted certiorari in *Hood* "to decide whether Congress has the authority to abrogate state sovereign immunity under the Bankruptcy Clause" arguing majority avoided addressing principal argument that was basis for Court of Appeals' decision and "which this Court granted certiorari in order to address—namely, that Congress possesses the power under the Bankruptcy Clause to abrogate a State's sovereign immunity from suit"); see also Michael J. Lichtenstein, *Supreme Court Ducks Sovereign Immunity Question: A Recap of the Remaining Circuit Conflicts*, 23 AM. BANKR. INST. J., at 28 (July/Aug. 2004) (describing holding in *Hood* and noting Justice Thomas' statement in dissent).

<sup>386</sup> See *Hood*, 124 S. Ct. at 1908–10; *Gardner*, 329 U.S. at 574 (defining bankruptcy proceedings as State's desire to obtain assets from debtor, maintaining "whole process of proof, allowance, and distribution [in bankruptcy proceedings] is . . . an adjudication of interests claimed in a res."); *New York v. Irving Trust Co.*, 288 U.S. 329, 333 (1933) (prophesizing "[i]f a state desires to participate in the assets of a bankrupt, she must submit to appropriate requirements by the controlling power").

<sup>387</sup> See *Hood*, 124 S. Ct. at 1915–16 (Thomas, J., dissenting) (disagreeing with majority because "[e]ven if the Bankruptcy Court could have exercised its in rem jurisdiction to make an undue hardship determination by motion, [Justice Thomas] cannot ignore the fact that the determination in this case was sought pursuant to an adversary proceeding"); Hon. James D. Walker, Jr. & Amber Nickell, *Bankruptcy*, 55 MERCER L. REV. 1101, 1102 (2004) (interpreting Justice Thomas' dissent in *Hood* as arguing "that while the in rem exception to sovereign immunity may be appropriate for matters initiated by motion, it should not apply to adversary proceedings, which are similar to civil litigation"). But see *Hood* 124 S. Ct. at 1914 (disapproving of Justice Thomas' views because such views would mandate overruling several cases which resembled traditional civil adjudications and Court was "not willing to take such a step").

<sup>388</sup> 523 U.S. 491 (1998) (involving issue of whether Eleventh Amendment bars jurisdiction of federal court over in rem admiralty action when res is not within State's possession).

Justice O'Connor held that the Eleventh Amendment did not bar a federal court's jurisdiction over an *in rem* admiralty action when the State does not possess the res.<sup>389</sup>

Although much of the opinion focuses on the development of admiralty jurisdiction, it also points to potentially successful arguments that the Eleventh Amendment might not apply in a particular situation. Thus, in a case decided before *Deep Sea Research*, the Fourth Circuit held that a state taxing authority could not recover taxes on transfers made by a debtor under a confirmed reorganization plan.<sup>390</sup> The state had neither filed a proof of claim nor in any other way participated in the bankruptcy case. It argued that the Eleventh Amendment barred adjudication of its claim in bankruptcy. In rejecting the state's argument, the Court concluded that the power to enter a confirmation order was not a "suit" against a state, but derived from the bankruptcy court's jurisdiction over the debtor and property of the estate.<sup>391</sup> If Maryland did not like that result, it should have intervened in the bankruptcy, i.e., waived its sovereign immunity. This results comports with *Deep Sea Research*. So long as the state does not have possession of property of the estate, it, like any other creditor, must file a proof of claim to protect its rights.

Another Supreme Court case sheds light on the limits of a state's sovereign

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<sup>389</sup> *Deep Sea Research Inc.*, 523 U.S. at 494-95 ("We conclude that the Eleventh Amendment does not bar the jurisdiction of a federal court over an *in rem* admiralty action where the res is not within the State's possession."); see *Bliemeister v. Indus. Comm'n of Ariz.* (*In re Bliemeister*), 251 B.R. 383, 392 (Bankr. D. Ariz. 2000) (noting significance of holding that states' sovereign immunity does not extend to *in rem* proceedings because of fundamental *in rem* nature of bankruptcy suits); Ralph Brubaker, *Of State Sovereign Immunity and Prospective Remedies: The Bankruptcy Discharge as Statutory Ex Parte Young Relief*, 76 AM. BANKR. L.J. 461, 543 (2002) (suggesting by analogizing to admiralty jurisprudence there may be an *in rem* bankruptcy exception to state sovereign immunity).

<sup>390</sup> *Maryland v. Antonelli Creditors' Liquidating Trust*, 123 F.3d 777, 779 (4th Cir. 1997) ("[T]he State of Maryland and Montgomery County are bound by the bankruptcy court's confirmation order and may not challenge it collaterally in a subsequent court proceeding."); see *In re Linc Capital, Inc.*, 280 B.R. 640, 645 (Bankr. N.D. Ill. 2002) ("[T]he 11th Amendment does not bar bankruptcy courts from exercising jurisdiction over the debtor's estate, even if a consequence of such exercise indirectly affects the interest of a state." (citing *Antonelli*, 123 F.3d at 787)); *Univ. of Va. v. Robertson*, 243 B.R. 657, 663 (Bankr. W.D. Va. 2000) (interpreting *Antonelli* to hold "the Eleventh Amendment is not implicated when a bankruptcy court, by a confirmation order, prevents the assessment of certain state taxes when bankruptcy estate assets are sold according to that order").

<sup>391</sup> *Antonelli*, 123 F.3d at 786 ("While resolution of an adversary proceeding against a state depends on court jurisdiction over that state, the power of the bankruptcy court to enter an order confirming a plan . . . derives . . . from jurisdiction over debtors and their estates."); see Patricia L. Barsalou & Scott A. Stengel, *Ex parte Young: Relativity in Practice*, 72 AM. BANKR. L.J. 455, 455 (1998) ("More recently, the idea that *in rem* jurisdiction may circumvent the Eleventh Amendment bar has received some attention, if not encouragement.") (citations omitted); Leonard H. Gerson, *A Bankruptcy Exception to Eleventh Amendment Immunity: Limiting the Seminole Tribe Doctrine*, 74 AM. BANKR. L.J. 1, 18 (2000) ("[T]he *Antonelli* Court avoided the Eleventh Amendment challenge to the bankruptcy court's jurisdiction by finding that the power . . . was derived from the bankruptcy court's jurisdiction over the debtor and its estate . . ."); Richard Lieb, *Eleventh Amendment Immunity of A State in Bankruptcy Cases: A New Jurisprudential Approach*, 7 AM. BANKR. INST. L. REV. 269, 306 (1999) ("Such an '*in rem*' exception to the Eleventh Amendment has been recognized in several post-*Seminole Tribe* decisions of appellate and bankruptcy courts . . .").

immunity in bankruptcy. In *Lapides v. Board of Regents of the University System of Georgia*,<sup>392</sup> a unanimous<sup>393</sup> Supreme Court held that a state waives its Eleventh Amendment immunity by removing a case from state to federal court. The Supreme Court concluded that:

It would seem anomalous or inconsistent for a State both (1) to invoke federal jurisdiction, thereby contending that the "Judicial power of the United States" extends to the case at hand, and (2) to claim Eleventh Amendment immunity, thereby denying that the "Judicial power of the United States" extends to the case at hand.<sup>394</sup>

The impact of this decision on bankruptcy are apparent. In reaching its unremarkable conclusion, the Supreme Court cited to three old and half-forgotten cases, including *Gardner v. New Jersey*.<sup>395</sup>

In *Gardner*, a railroad reorganization case, the State of New Jersey had filed a claim for unpaid taxes of nearly \$20,000. The debtor and the trustee objected to the claim, and petitioned the court to determine the validity and extent of the state's claim. The state then entered a special appearance arguing that adjudicating the

<sup>392</sup> 535 U.S. 613 (2002); see *Omosogbon v. Wells*, 335 F.3d 668, 673 (7th Cir. 2003) ("What the Court said [in *Lapides*], more precisely, was that a state's voluntary invocation of a federal court's jurisdiction through removal waives a state's 'otherwise valid objection' to litigation of a state-law claim in a federal forum."); *Ku v. Tennessee*, 322 F.3d 431, 435 (6th Cir. 2003) (appearing without objection and defending on merits when district court has original jurisdiction is sufficient to waive Eleventh Amendment immunity defense). Cf. Jonathan R. Siegel, *Waivers of State Sovereign Immunity and the Ideology of the Eleventh Amendment*, 52 DUKE L.J. 1167, 1217-18 (2003) ("The impact of *Lapides* has, however, been disputed . . . [s]ome [lower courts] have treated it as a narrow decision applicable only to cases following its precise pattern . . . while others have applied a broad rule of waiver in light of the 'spirit' of *Lapides*."). (citations omitted).

<sup>393</sup> *Lapides*, 535 U.S. at 624 ("We conclude that the State's action joining the removing of this case to federal court waived its Eleventh Amendment immunity—though, as we have said, the District Court may well find that this case, now raising only state-law issues, should nonetheless be remanded to the state courts for determination."). It is interesting to note here that Justice Breyer, the author of *Lapides* and a dissenter in *Seminole*, made no mention of *Seminole* in his opinion. See generally *Seminole Tribe of Fla. v. Florida*, 517 U.S. 44, 72-73 (1996) (holding Congress may abrogate Eleventh Amendment immunity only under section 5 of Fourteenth Amendment). For two other Eleventh Amendment opinions authored by Justice Breyer, see generally *Fed. Mar. Comm'n v. S.C. State Ports Auth.*, 535 U.S. 743, 785-87 (2002) (Breyer, J., dissenting) (rejecting majority's holding state sovereignty bars federal administrative agency from adjudicating private individuals' claim against nonconsenting state on practical and federalism grounds); *Wis. Dep't of Corr. v. Schacht*, 524 U.S. 381, 392-93 (1998) (writing for Court, Justice Breyer concluded that "[a] State's proper assertion of an Eleventh Amendment bar after removal means that the federal court cannot hear the barred claim. But that circumstance does not destroy removal jurisdiction over the remaining claims in the case before us").

<sup>394</sup> *Lapides*, 535 U.S. at 619.

<sup>395</sup> 329 U.S. 565 (1947). For the other two old and half-forgotten cases, see *Gunter v. Atl. Coast Line R.R. Co.*, 200 U.S. 273, 284 (1906) ("Although a State may not be sued without its consent, such immunity is a privilege which may be waived . . . where a State voluntarily becomes a party to a cause and submits its rights for judicial determination, it will be bound thereby . . ."); *Clark v. Barnard*, 108 U.S. 436, 447 (1883) ("The immunity from suit belonging to a State . . . is a personal privilege which it may waive at pleasure; so that in a suit . . . in which a State had sufficient interest . . . its appearance in a court of the United States would be a voluntary submission to its jurisdiction . . .").

petition would violate its Eleventh Amendment immunity. The Supreme Court rejected the argument, holding that "the whole process of proof, allowance, and distribution [of claims] is . . . an adjudication of interest claimed in a res . . . . When the State becomes an actor and files a claim against the fund it waives any immunity . . . respecting the adjudication of the claim."<sup>396</sup>

Several circuits had anticipated the Supreme Court's resurrection of *Gardner* in *Lapides* and held that a state waives its Eleventh Amendment immunity by filing a proof of claim.<sup>397</sup> Thus, as one court noted: "[t]he question . . . then, is not whether a state waives its Eleventh Amendment immunity by filing a proof of claim in bankruptcy. *Gardner* establishes that it does . . . . Rather, the relevant question [is] the extent of this waiver . . . ."<sup>398</sup>

Courts agree that, by filing proofs of claim, states waive their Eleventh Amendment immunity "in regard to the debtor's claims which arise out of the same transaction or occurrence as the state's proof of claim."<sup>399</sup> As might be expected, they disagree on how broadly or narrowly to define "same transaction or

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<sup>396</sup> *Gardner*, 329 U.S. at 574; see *Missouri v. Fiske*, 290 U.S. 18, 25 (1933) (recognizing waiver of immunity via litigation but holding State's application to intervene did not constitute waiver); *New York v. Irving Trust Co.*, 288 U.S. 329, 333 (1933) ("If a state desires to participate in the assets of a bankrupt, she must submit to appropriate requirements by the controlling power; otherwise, orderly and expeditious proceedings would be impossible and a fundamental purpose of the Bankruptcy Act would be frustrated."). For a more current application of this doctrine, see *Confederated Tribes of the Colville Reservation Tribal Credit v. White (In re White)*, 139 F.3d 1268, 1271 (9th Cir. 1998) ("The Supreme Court made clear in [*Gardner*] that when a sovereign files a claim against a debtor in bankruptcy, the sovereign waives immunity with respect to adjudication of the claim.").

<sup>397</sup> See, e.g., *Ossen v. Dep't of Social Servs. (In re Charter Oak Assocs.)*, 361 F.3d 760, 767 (2d Cir. 2004), petition for cert. filed, (U.S. June 17, 2004) (No. 03-1672) ("One practical application of the waiver-by-litigation doctrine is the long-standing rule that a state waives its sovereign immunity by filing a proof of claim in a bankruptcy case."); *Cal. Franchise Tax Bd. v. Jackson (In re Jackson)*, 184 F.3d 1046, 1050 (9th Cir. 1999) (concluding sovereignty immunity was waived when proof of claim filed); *Ga. Dep't of Revenue v. Burke (In re Burke)*, 146 F.3d 1313, 1318 (11th Cir. 1998) (extending waiver to bankruptcy court's enforcement of discharge injunction and automatic stay); *DeKalb County Div. of Family & Children Servs. v. Platter (In re Platter)*, 140 F.3d 676, 679 (7th Cir. 1998) ("Because a state voluntarily chooses to enter a bankruptcy case when it initiates an adversary proceeding, we hold that a state removes itself from the Eleventh Amendment's protection by starting one . . . .") (citations omitted).

<sup>398</sup> *Schulman v. California (In re Lazar)*, 237 F.3d 967, 976-78 (9th Cir. 2001) (holding filing proof of claim in bankruptcy proceeding waives state's Eleventh Amendment immunity regarding bankruptcy estate's claims arising from same transaction or occurrence as its own); see, e.g., *Jones v. Yorke (In re Friendship Med. Ctr., Ltd.)*, 710 F.2d 1297, 1301 (7th Cir. 1983) ("[T]he limited waiver of sovereign immunity created by the filing of the claim extends only so far as necessary to adjudicate that claim . . . ."); *Fed. Sav. & Loan Ins. Corp. v. Quinn*, 419 F.2d 1014, 1017 (7th Cir. 1969) ("Waiver does not extend to what federal procedure terms 'permissive counterclaims' . . . claims for affirmative relief in excess of or different in kind from that sought by the plaintiff.") (citations omitted).

<sup>399</sup> *In re Lazar*, 237 F.3d at 977 (quoting *In re Jackson*, 184 F.3d at 1049); see *Rose v. U.S. Dep't of Educ. (In re Rose)*, 187 F.3d 926, 930 (8th Cir. 1999) (holding submission of proof of claims in bankruptcy case waives immunity in related proceedings required for adjudication); *Schlossberg v. Maryland (In re Creative Goldsmiths, Inc.)*, 119 F.3d 1140, 1148 (4th Cir. 1997) ("[W]e hold that to the extent a defendant's assertions in a state-instituted federal action, including those made with regard to a state-filed proof of claim in a bankruptcy action, amount to a compulsory counterclaim, a state has waived any Eleventh Amendment immunity against that counterclaim . . . .").

occurrence."<sup>400</sup> Still, *Lapides* makes it clear that Congress has the *constitutional* power to determine that a state waives its Eleventh Amendment immunity by filing a proof of claim, or otherwise intervening in a bankruptcy. In the environmental context, any state's effort to enforce its environmental laws against a debtor in possession or trustee will likely amount to a waiver of the state's Eleventh Amendment immunity.

The Second Circuit recently expanded the effect of a state filing a proof of claim. In *Ossen v. Connecticut Department of Social Services (In re Charter Oak Associates)*,<sup>401</sup> the court held that if *one* state agency filed a proof of claim, that filing waived sovereign immunity for *all* state agencies against which the estate might have a claim.<sup>402</sup> In *Ossen*, the Connecticut Department of Revenue Services (DRS) filed a proof of claim for unpaid taxes of \$148,643.34. At the same time, the Connecticut Department of Social Services (DSS) owed the debtor \$225,309.29 in rental reimbursements. The trustee filed an adversary proceeding against DSS seeking the withheld reimbursements. DSS moved to dismiss the complaint on Eleventh Amendment grounds. It argued that the estate's claim against DSS did not arise out of the same transaction or occurrence as DRS's claim against the estate. Section 106(c)'s creation of a right of set off under such circumstances violated the Eleventh Amendment.<sup>403</sup>

Relying on *Lapides*, the Second Circuit disagreed. It saw "no reason why a state that has filed a proof of claim in a bankruptcy case should be permitted to raise

<sup>400</sup> See *In re Charter Oak Assocs.*, 361 F.3d at 768 ("Most circuits agree, however, that when a state files a proof of claim, it waives its immunity as to at least some counterclaims, specifically compulsory counterclaims."); *In re Lazar*, 237 F.3d at 978 ("Our sister circuits, in addressing [the question of how far a waiver extends], have not yet reached consensus on the proper rule."); see, e.g., *Arecibo Cmty. Health Care, Inc. v. Puerto Rico*, 270 F.3d 17, 26 (1st Cir. 2001) (concluding state's immunity is waived with respect to compulsory counterclaims); *Wyo. Dep't of Trans. v. Straight (In re Straight)*, 143 F.3d 1387, 1391 (10th Cir. 1998) (employing "same transaction or occurrence" standard).

<sup>401</sup> 361 F.3d 760 (2d Cir. 2004); see *In re Straight*, 143 F.3d at 1391 (concluding in bankruptcy, state agencies should be regarded as one entity); 5 COLLIER ON BANKRUPTCY ¶ 553.03, at 33 (Lawrence P. King et al. eds., 15th ed. rev. 1997) ("[D]ifferent agencies of a state will be treated as a single unitary creditor for setoff purposes in bankruptcy.").

<sup>402</sup> *In re Charter Oak Assocs.*, 361 F.3d at 772 (holding when two state agencies act as unitary creditor, fairness requires waiver by one agency constitutes waiver by other).

<sup>403</sup> *In re Charter Oak Assocs.*, 361 F.3d at 766 ("DSS argues that § 106(c) extends the scope of a state's waiver too far because, under the Eleventh Amendment, a state's filing of a proof of claim can be construed at most as a waiver of immunity with respect to claims that arose out of the same transaction or occurrence . . ."); see 11 U.S.C. § 106(b)-(c) (2000).

A government unit that has filed a proof of claim . . . is deemed to have waived sovereign immunity with respect to a claim . . . that arose out of the same transaction or occurrence . . . and there shall be offset against a claim or interest of a government unit any claim against such government unit that is property of the estate.

*Id.*; 17A JAMES WM. MOORE, MOORE'S CURRENT DEVELOPMENTS: CASES, LEGISLATION, AND RULES § 123.41 at 11 (Daniel R. Coquillette et al. eds., 2004) ("The Second Circuit held that Bankruptcy Code Section 106(c) that permits the offset of a bankruptcy estate's claims against claims of governmental units regardless of any assertion of sovereign immunity, constitutes a proper codification of the rule that voluntary invocation of a federal court's jurisdiction waives Eleventh Amendment immunity."). See generally 2 COLLIER ON BANKRUPTCY ¶ 106.02, at 17 (Lawrence P. King et al. eds., 15th ed. rev. 1997) (discussing constitutional concerns over 11 U.S.C. § 106 (c)).



the immunity shield in response to permissive counterclaims brought by the debtor, at least where those counterclaims are capped by a setoff limitation, as they are under § 106(c).<sup>404</sup>

Even more than *Hood*, *Ossen* has relevance for environmental claims in bankruptcy. States often have significant claims against estates. Once a state files a proof of claim, *Ossen* allows the estate to set its own claims off against the state's claims without worrying about Eleventh Amendment issues. Because *Ossen* reached the opposite conclusion from the Fourth Circuit, the only other court to have considered section 106(c)'s constitutionality,<sup>405</sup> the Supreme Court may grant certiorari and decide the issue. But then again, given *Hood*, it may not, in which case, the confusion will continue and opportunities for attorneys will abound.

One final source of bankruptcy court jurisdiction over states in the post-*Seminole Tribe* world is the so-called *Ex parte Young*<sup>406</sup> doctrine. *Young* creates an exception to the general Eleventh Amendment immunity rule forbidding suits against states for money damages. It allows prospective declaratory and injunctive relief against a state official as an individual to prevent that individual from continuing to violate a federal statute. Such relief is valid even if it has a "substantial ancillary effect on a state's treasury."<sup>407</sup> Under *Young*, then, states cannot circumvent the automatic stay or the discharge injunction by wrapping themselves in the Eleventh Amendment.

Thus, even if the Supreme Court holds section 106 unconstitutional, a

<sup>404</sup> *In re Charter Oak Assocs.*, 361 F.3d at 769; see *Fed. Mar. Comm'n v. S.C. State Ports Auth.*, 535 U.S. 743, 760 (2002) ("The preeminent purpose of state sovereign immunity is to accord States the dignity that is consistent with their status as sovereign entities."); *Lapides v. Bd. of Regents*, 535 U.S. 613, 620 (2002) ("[A]n interpretation of the Eleventh Amendment that finds waiver in the litigation context rests upon the Amendment's presumed recognition of the judicial need to avoid inconsistency, anomaly, and unfairness . . .").

<sup>405</sup> *In re Creative Goldsmiths Inc.*, 119 F.3d at 1147 (finding 11 U.S.C. § 106 invalid exercise of Congress' power and therefore unconstitutional). But see *In re Charter Oak Assocs.*, 361 F.3d at 770 ("We are not convinced by the Fourth Circuit's reasoning . . . the balance of these equities favors a construction of the Eleventh Amendment that would permit a debtor to assert a permissive counterclaim capped by a setoff limitation against a state that has filed a proof of claim."). See generally 2 COLLIER ON BANKRUPTCY ¶ 106.02 at 17 (Lawrence P. King et al. eds., 15th ed. rev. 1997) ("By permitting a setoff against a state's claim . . . section 106(c) potentially runs afoul of the Eleventh Amendment by subjecting a state to a bankruptcy court's determination of a claim against it . . .").

<sup>406</sup> 209 U.S. 123, 155–56 (1908) ("[I]ndividuals, who, as officers of the State, are clothed with some duty in regard to the enforcement of the laws of the State . . . may be enjoined by a Federal court of equity from such action."); see *Seminole Tribe of Fla. v. Florida*, 517 U.S. 44, 72 n.16 ("[A]n individual may obtain injunctive relief under *Ex Parte Young* in order to remedy a state officer's ongoing violation of federal law."); see, e.g., *DeAngelis v. Laskey* (*In re DeAngelis*), 239 B.R. 426, 432 (Bankr. D. Mass. 1999) (holding debtor could invoke *Ex Parte Young* doctrine in chapter 7 case).

<sup>407</sup> *Goldberg v. Ellett* (*In re Ellett*), 254 F.3d 1135, 1144 (9th Cir. 2001), cert. denied, 534 U.S. 1127 (2002) ("The Court has . . . observed that prospective relief awarded pursuant to *Ex Parte Young* may have a substantial ancillary effect on a State's treasury . . . but has nevertheless consistently held that this fact alone is insufficient to convert such actions into actions against the State for state sovereign immunity purposes.") (citations omitted); see, e.g., *In re Chambers*, 348 F.3d 650, 652 n.2 (7th Cir. 2003) (allowing, under *Ex Parte Young*, student to sue state school chancellor to declare student loan discharged); *Palm v. Stack* (*In re Palm*), 286 B.R. 710, 717 (Bankr. N.D. Iowa 2002) (holding determination of debtor's dischargability of income tax obligations may be brought pursuant to *Ex Parte Young*).

bankruptcy estate retains several arrows in its quiver. A state's interest in environmental issues makes the state a sitting duck.

#### CONCLUSION

Environmental law and bankruptcy law have at least one thing in common: neither anticipates confronting another set of policy objectives as imperative as its own. Environmental law imposes liability on practically all parties involved with a site. Liability remains unless and until the site is cleaned up at the expense of those responsible. Bankruptcy acts to discharge liability. Each law expresses a singular purpose. Those purposes are in direct conflict with each other. The present case law morass is an inevitable by-product of that conflict.

Until Congress or the Supreme Court speaks, courts will continue to be free to decide an issue based on the court's own resolution of the conflict. Support exists for almost any position a court might want to take. The present situation creates unpredictability and its constant companion, litigation. Only lawyers, not the environment and not a debtor's creditors, benefit. It is time for Congress or the Supreme Court to step up to the plate.