

Viewpoint

One of a series of opinion columns by bankruptcy professionals

2009 Environmental Decisions A Double-Edged Sword

By Eric R. Wilson and Dana P. Kane

Courts have long struggled to reconcile the goals of environmental statutes such as the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) and the Resource Conservation and Recovery Act (RCRA), which require potentially responsible parties (PRPs) to bear the costs of remediation, with the Bankruptcy Code's objective of providing a fresh start for the debtor.

The year 2009 was no exception. Two important cases were decided by high courts that will impact companies with environmental liabilities facing the possibility of bankruptcy and their co-PRPs: the Supreme Court's 2009 decision in *Burlington Northern & Santa Fe Railway Co. v. U.S.* and the 7th U.S. Circuit Court of Appeal's decision in *United States v. Apex Oil Co., Inc.* Apex Oil involved the environmental liability of a corporate successor to an entity that received a discharge in bankruptcy 15 years earlier. Burlington Northern involved consolidated recovery actions for environmental liability against the remaining PRPs after the primary "wrongdoer" had ceased operations. Although neither decision originated from an active bankruptcy case, they are notable for bankruptcy practitioners because of their divergent anticipated effects on debtors.

In Apex Oil, the 7th Circuit held that an injunctive order obtained by the government under RCRA is not a "claim" under section 101(5) of the Bankruptcy Code that is dischargeable in bankruptcy. The decision resulted in an estimated \$150 million in clean-up costs for reorganized Apex - a high price under any scenario, but particularly where the contaminated property was sold by the debtor during the course of its Chapter 11 bankruptcy case.

The issue in Apex Oil was whether the debtor's breach of an injunctive clean-up order issued under section 7003 of RCRA "gives rise to a right to payment" in favor of the government under section 101(5)(B) such that the liability is a "claim" dischargeable in bankruptcy. The 7th Circuit identified two narrow circumstances in which the breach of an injunctive order "gives rise to a right to payment": (1) where the order can be replaced by a money judgment, or (2) where the injunction itself is tantamount to an order to pay money (e.g., an injunctive order to pay back wages in an employment case). Relying on the Supreme Court's decision in *Meghrig v. KFC Western Inc.* and its own precedent analyzing the private citizen suit provisions of RCRA, the court

concluded that money damages are not available under the analogous provisions of RCRA applicable to suits brought by the government. Because the government had no right to money damages under RCRA, it had no right to payment from the debtor for breach of the injunctive order. The court also rejected the reorganized debtor's argument that the cost to comply with the order converted the injunction into a dischargeable claim for money damages, because virtually every injunctive order involves costs of compliance.

To the extent that Apex Oil is followed, PRPs confronted with a RCRA clean-up order will find it more difficult to reorganize in Chapter 11. Indeed, in Apex Oil, reorganized Apex unsuccessfully argued that had it known at the inception of the bankruptcy that the debtor would be liable for such staggering clean-up costs post-emergence, it would have liquidated instead.

In Burlington Northern, the Supreme Court relaxed the general rule of joint and several liability among PRPs under CERCLA and RCRA and introduced standards for apportionment of liability. Under CERCLA and RCRA, joint and several liability of PRPs has been the norm, with apportionment of liability the exception. Imposing joint and several liability on a PRP that is a debtor in bankruptcy can render the debtor's estate responsible for the entire cost to remediate sites that the debtor no longer owns or operates. This result can burden bankruptcy estates with enormous liability, which dilutes the recoveries of non-environmental creditors and can impair or eliminate a debtor's ability to reorganize. Burlington Northern's holding softens the general rule by providing a means to hold a debtor-PRP responsible only for a portion of clean-up costs, provided there is a reasonable basis for divisibility. Disagreeing with the 9th Circuit, the Supreme Court approved the district court's consideration of percentage of land area, length of ownership and type and volume of the contaminants, as appropriate factors to determine a PRP's share of liability.

Although the impact of Burlington Northern in bankruptcy remains to be seen, its significance is clear. Burlington Northern gives bankruptcy judges flexibility to limit the estate's joint and several liability for clean-up of land that the debtor no longer owns or operates. A debtor that can marshal facts supporting divisibility may be able to limit

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liability to its allocable share, improve the chances of a successful reorganization and provide a greater return to the estate's non-environmental creditors.

The impact of these decisions may be revealed in the Chemtura Corporation bankruptcy pending in the Southern District of New York, where both Apex Oil and Burlington Northern have been raised. Late in 2009, Chemtura filed a complaint seeking a declaratory judgment that certain environmental obligations are dischargeable relating to sites that (i) the debtors no longer owned or operated as of the bankruptcy filing or (ii) were never owned by the debtors. In support of its bid to withdraw the matter from the bankruptcy court, the U.S. cited Apex Oil as raising issues of first impression in the 2nd Circuit under federal non-bankruptcy law that will have to be considered by the district court for Chemtura's complaint to be resolved. Additionally, earlier this year, Chemtura filed a wave of objections to government environmental claims, which cite to Burlington Northern and argue that such claims fail to account for the debtors' limited contribution to the contamination or the actions of other PRPs.

These decisions show that courts continue to experience difficulty balancing environmental statutes with the Bankruptcy Code. The intersection of these two bodies of law has always been a difficult area to navigate, and it does not appear as if that will change any time soon.

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