



AN 'APEX' THAT MAY BE A TURNING POINT

Ruling in oil company case holds debtor responsible for clean-up obligations

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Connecticut has its fair share of environmentally contaminated sites and companies with exposure for cleanup. Especially in today's economic climate, many of these companies will consider filing for Chapter 11 as a way of addressing their obligations to clean up those sites.

Other Connecticut companies will have to respond to Chapter 11 filings of potentially responsible parties (PRPs) that would otherwise be jointly and severally liable with them for cleanup. Both the Connecticut Department of Environmental Protection and the U.S. Environmental Protection Agency will similarly have to reassess their strategy for obtaining cleanup of a site. The decisions these agencies make will affect co-PRPs of the Chapter 11 debtor and likely will often require the co-PRPs to assume responsibility for the debtor's share of cleanup.

One of the most important questions in the bankruptcy of a company with environmental exposure is whether the company can use bankruptcy to discharge its cleanup obligations. This brings the competing policies of environmental and bankruptcy laws into direct conflict. The environmental laws seek to ensure responsible parties clean up contamination, while the bankruptcy laws seek to provide the bankruptcy debtor a broad discharge of its past obligations to facilitate its financial rehabilitation.

In *United States v. Apex Oil Co.*, 2009 WL

2591545 (7th Cir. Aug. 25, 2009), the Seventh Circuit Court of Appeals tipped the balance between the two conflicting policies decidedly in favor of the environmental laws. In *Apex*, the court held that confirmation of a Chapter 11 plan had not discharged a reorganized debtor's obligations to clean up property that had been sold before confirmation. In so doing, the Seventh Circuit joined the Third Circuit in squarely holding a debtor responsible for clean-up obligations owed the government at land the debtor no longer owned or operated.

Discharge Of Obligations

As a general rule, bankruptcy discharges a debtor from any liability on a claim that arose before the date of confirmation of a Chapter 11 plan of reorganization. The Bankruptcy Code defines "claim" as not only a simple "right to payment," but also a "right to an equitable remedy for breach of performance if such breach gives rise to a right to payment."

In the environmental context, the question is whether the right to a cleanup order or injunction, which are equitable remedies, are dischargeable "claims." The leading case on this question is *Ohio v. Kovacs*, 469 U.S. 274 (1985). There, the Supreme Court held that the state had converted its cleanup order into a dischargeable claim for money damages by 1) divesting the debtor of his assets and control of the contaminated site through appointment of a receiver, and 2)

thereafter seeking only money from the debtor to defray the receiver's clean-up costs.

Courts have struggled to apply *Kovacs* outside its facts. The Seventh Circuit has confirmed that a reorganized debtor remains liable as the current owner or operator for cleanup of contaminated land it continues to own or operate after confirmation. According to that court, the liability "runs with the land." *In re CMC Heartland Partners*, 966 F.2d 1143 (7th Cir. 1992).

The Third Circuit took *CMC* one step further in *In re Torwico Electronics Inc.*, 8 F.3d 146 (3d Cir. 1993), a decision that still gener-



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ates debate. There, the court held that a debtor had ongoing obligations to the state to remediate land it had not owned or possessed since four years before bankruptcy. The court reasoned that the debtor had an ongoing obligation under state law to clean up its waste at the site that posed a continuing hazard. The court explained that while the debtor's obligations no longer ran with the land, they did "run with the waste."

The Seventh Circuit cited *Torwico* in *AM International Inc. v. Datacard Corp.*, 106 F.3d 1342 (7th Circuit 1997), in concluding, with little analysis, that a clean-up injunction issued under the citizen suit provision of section 7002 of the Resource Conservation and Recovery Act (RCRA) is not a dischargeable "claim." In reaching its decision, the court relied on the Supreme Court's holding in *Meghrig v. KFC Western Inc.*, 516 U.S. 479 (1996), that RCRA's citizen suit provision does not provide a private citizen a right to any monetary relief.

The weight to afford *Datacard* is unclear. There, the reorganized debtor had operated the contaminated land for a short period after bankruptcy, potentially an independent basis for liability (although not relied on by the court). Also, the court found that the plaintiff lacked knowledge of its environmental rights at the time of confirmation. As a result, the plaintiff's environmental claims had not arisen at the time of confirmation and consequently could not have been discharged.

The Sixth Circuit reached a different conclusion in *United States v. Whizco Inc.*, 841 F.2d 147 (6th Cir. 1988), on unique facts involving the mine reclamation obligations of a 63-year-old Chapter 7 debtor. There, the Sixth Circuit held that because the debtor

could comply with his obligations only by spending money, such obligations constituted a dischargeable claim.

Apex Decision

In *Apex*, the United States brought suit under RCRA section 7003 for an injunction requiring Apex Oil Co. to abate alleged petroleum-based contamination at and adjacent to an oil refinery Apex's predecessor had sold in 1989 during a previous bankruptcy. The United States also sought a declaration that its right to injunctive relief had not been discharged by the 1990 confirmation of the predecessor's Chapter 11 plan. The district court ruled in favor of the United States and held that the government's injunctive rights had not been discharged and issued the requested injunction. Apex appealed.

The Seventh Circuit affirmed. The court explained that "the natural reading" of the definition of "claim" is "that if the holder of an equitable claim can, in the event that the equitable remedy turns out to be unobtainable, obtain a money judgment instead, the claim is dischargeable." The Seventh Circuit then became the first appellate court since the Supreme Court decided *Meghrig* to hold that RCRA section 7003 provides the government a right to injunctive relief only and not a monetary remedy.

The court rejected Apex's argument that the cost of complying with the RCRA injunction was subject to discharge as a bankruptcy claim. The court observed that almost every equitable decree imposes a cost on the defendant. A rule that all such decrees can be discharged as monetary claims absent specific exception in the Bankruptcy Code is inconsistent with the code's limited definition of the type of equitable remedy

that is a dischargeable claim.

For that reason, the court disagreed with the Sixth Circuit's holding in *Whizco* and limited the application of *Kovacs* to cases where the government actively seeks payment of money from the debtor rather than an order to clean up. The court concluded by rejecting Apex's unrelated alternative basis for reversal, that the terms of the injunction were impermissibly vague.

Import Of Apex

The significance of *Apex* is twofold. First, it follows the controversial lead of the Third Circuit in *Torwico* and squarely holds that a debtor remains liable for remediation of property under RCRA even if (a) the debtor no longer owns or operates the property at the time of discharge and (b) the debtor's involvement at the site is completely pre-confirmation.

The focus of the inquiry is strictly on whether the holder of the equitable clean-up remedy could have instead obtained a money judgment against the debtor. Discharge of clean-up obligations does not depend on whether the debtor owns or operates the contaminated property after confirmation.

Second, *Apex* establishes RCRA as providing remediation remedies for the government that cannot be discharged in bankruptcy, since RCRA provides no monetary remedy. As a result, RCRA injunctive suits are emerging as the government's enforcement mechanism of choice when a PRP is in bankruptcy or has previously received a discharge in bankruptcy. *Apex* also reinforces the Seventh Circuit's earlier *Datacard* decision, strengthening the hand of private citizens seeking to use RCRA to require debtors or reorganized debtors to remediate. ■