ENVIRONMENTAL LIABILITIES AND BANKRUPTCY
Reference: Stroock & Stroock 6/23/10

Debtors Can File Without Insolvency
The Bankruptcy Code provides that a "person who has a domicile, a place of business, or property in the United States may be a chapter 11 debtor." There is no requirement that a debtor be insolvent at the time of filing to take advantage of the US bankruptcy laws.

> Section 109 (a) Notwithstanding any other provision of this section, only a person that resides or has a domicile, a place of business, or property in the United States, or a municipality, may be a debtor under this title.

There is no requirement that a debtor be insolvent at the time of filing to take advantage of the US bankruptcy laws.

USG Corporation and W.R. Grace & Co availed themselves of Chapter 11 protections in order to effectively resolve their substantial asbestos mass-tort liabiliities, notwithstanding that both companies claimed they were otherwise solvent.

> See *In re USG Corp.*, No. 01-2094 (Bankr. D. Del. 2001) and *In re W.R. Grace & Co.*, No. 01-01139 (Bankr. D. Del. 2001)

A non-US incorporated member of a group with a US nexus that files for Chapter 11 could file an insolvency proceeding in its applicable foreign country and then seek to have its foreign bankruptcy proceeding recognized in the US under Chapter 15 of the Bankruptcy Code

All claims might not be fully satisfied if only select entities within the group filed bankruptcy.

In a bankruptcy case, only legally valid claims against the debtor responsible for such liabilities would be allowed, and only against that entity, which as a result of such claims might not be solvent and able to satisfy its liabilities in full

In the absence of substantive consolidation or piercing the corporate veil among various debtors, allowed general unsecured claims, including commercial claims, might receive less than full recoveries.

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Protections from filing Chapter 11:

> **Establishment Of A Bar Date:** This would identify in a timely and expeditious manner the universe of claims neediing to be addressed and bar any claims not timely filed.
>
> **Centralization Of Litigation In One Judicial District:** The entity can attempt to litigate to judgment, in a single judicial district, the myriad claims asserted against it. Personal injury claim trials (brought, for example, by persons claiming they sustained injury or disease during the cleanup efforts), however, could not be heard in the bankruptcy court, which lacks subject matter jurisdiction over such claims, but rather would be heard in the related district court. The bankruptcy court could determine other types of claims and could render final judgments on them, unless they were not considered "core" bankruptcy claims, or the parties did not consent.
>
> **Litigation Procedures:** The estimation process for claims in bankruptcy requires the bankruptcy court to estimate "for purposes of allowance … any contingent or unliquidate claim, the fixing of which, as the case may be, would unduly delay the administration of the case …" S. 502 (c) The estimation of multiple related claims has been employed on an aggregated basis in numerous asbestos-related bankruptcy cases (Armstrong; Federal-Mogul). This process, however, does not preclude any individual claimant from seeking to litigate the claim, nor does it trump the right to a jury trial were one to exist with respect to the claim. Estimation alone may not be adequate to finally resolve the claims against the entity.

Much of the reported case law with respect to environmental claims has developed under the Comprehensive Environmental Response, Compensation and Liabilitiy Act of 1980 ("CERCLA"). This law imposes liability on those responsible persons who or operate contaminated property or who dispose of contaminated property.

The Oil Pollution Act of 1990 ("OPA") "imposes strict liability [for removal costs and damages] upon parties that discharge oil into 'navigable waters,'" and "into bodies of water adjacent to an open body of navigable water." The few reported decisions under OPA in the context of a bankruptcy case do not address the treatment of response cost claims of third parties against the debtor.

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The existing body of case law generally provides that cleanup costs incurred by third parties arising from the debtor's pre-bankruptcy conduct are general unsecured claims. Claims for costs incurred post-bankruptcy to bring the debtor into compliance with state and federal environmental and health laws, or to remedy contamination arising pre-bankruptcy and posing a continuing identifable and imminent harm to public health will be given administrative priority treatment in bankrupty under section 503(b)(1) of the Bankruptcy Code, where there is a determination that they were "actual, necessary costs and expenses [incurred to] preserve the estate." A debtor's ownership, operation or use of the contaminated property is a factor in determining whether the cleanup costs will receive administrative claim status.

Similarly, under existing law, courts agree that penalties and fines assessed for pre-petition misconduct or the continuing effects of pre-petition msconduct should not be considered on administrative expense. However, penalties assessed for pre-petition misconduct that continued into the post-petition period or for misconduct done post-petition may be treated as an administrative expense.

> Several courts have held that the pyament of fines and civil penalties is a cost of compliance, or in other words, a cost of doing business in a regulated industry, and therefore, are entitled to administrative priority.
>
> Other courts disagree and refuse to award administrative priority to fines and penalties that are noncompensatory in nature or criminal. These cases advocate for a narrower reading of what constitutes the "actual and necessary" expenses of preserving the estate and argue that violation of environmental laws is not a legitimate business activity, and therefore, cannot be viewed as part of the cost-benefit analysis of running a business.

Even if civil penalties do not receive administrative expense status, they may be entitled to priortity status above other general unsecured claims under section 507(a)(8)(G) which provides that allowed unsecured claims of governmental units are given a higher priority to the extent such claims are for a penalty related to a claim in compensation for actual pecuniary loss. However, at least one court has held that civil penalties asserted by the federal government under the Clean Water Act for discharge of oil into navigable water in violation of OPA was not "in compensation for actual loss." *See In re Jones*, 311 B.R. 647, 656 (Bankr. M.D. Ga. 2004).

ENVIRONMENTAL LIABILITIES AND BANKRUPTCY

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A filing may not halt the government's efforts to compel the entity to cooperate in the remediation of the spill, including the costs of cleanup. Section 362(b)(4) of the Code provides an exception for governmental entities acting within their "policy or regulatory power" to several of the prohibitions in the automatic stay provisions.

A debtor's ownership, operation or use of the contaminated property may also be a factoor in determining the appropriateness of the debtor having to comply with injunctions compelling remediation.

In addition, the police and regulatory exception has been found applicable to a governmental unit's (i) entry, but not the enforcement, of a money judgment, *see United States v. Oil Transport Co.*, 172 B.R. 834, 836 (E.D. La. 1994) (action by the federal government to enforce its regulatory authority under the Oil Pollution Act of 1990 for response costs incurred in responding to a spill or threatened oil spill by obtaining the entry of money judgment fell within the police and regulatory exception to the automatic stay) and (ii) efforts to fix civil penalties for violations of law, up to the point of collection.