Journal of Natural Resources & Environmental Law

Volume 6
Issue 2 *Journal of Mineral Law & Policy, volume 6, issue 2*

Article 7

January 1991

Abandonment of Contaminated Property Under the Bankruptcy Code--From *Midlantic* to *In Re Smith Douglas*, What Next?

Brian Cumbo
University of Kentucky

Abandonment of Contaminated Property Under the Bankruptcy Code—From *Midlantic* to *In Re Smith Douglas*, What Next?

INTRODUCTION

The abandonment of property[1] upon which state environmental violations exist has become a controversial issue. "It is only recently that the public has learned of the magnitude of the dangers associated with toxic waste disposal; at the same time, the last few years have witnessed a rising tide of bankruptcies."[2] Prior to *Midlantic National Bank v. New Jersey Department of Environmental Protection*,[3] abandonment of contaminated property was the general rule.[4] *In re Smith-Douglas, Inc.*[5] is the highest decision to date to interpret the issue addressed in *Midlantic* on point. This Comment considers post-*Midlantic* attempts to resolve the problems presented by abandonment of contaminated property under the Bankruptcy Code.

I. SECTION 554(a)

The overriding purpose of bankruptcy liquidation is the expeditious reduction of the debtor's property to money, for equitable distribution to creditors.[6] Abandonment is "the release from the debtor's estate of property previously included in that

---

[1] As authorized under 11 U.S.C.A. § 554(a) (West Supp. 1990).

[2] Matter of Quanta Resources Corp., 739 F.2d 912, 921 (3d Cir. 1984). *See also*, Cosetti and Friedman, *Midlantic National Bank, Kovacs, and Penn Terra: The Bankruptcy Code and State Environmental Law-Perceived Conflicts and Options for the Trustee and State Environmental Agencies*, 7 J. L. & COM. 65 (1987) ("As of August 1985, it was estimated that 74 hazardous waste facilities had filed for bankruptcy. An EPA study concluded that over the next fifty years, 25-30% of the firms owning land disposal facilities will petition for bankruptcy.")

[3] 474 U.S. 494 (1986).

[4] In re 82 Milbar Blvd. Inc., 91 B.R. 213, 218 n.16 (Bkrtcy. E.D.N.Y. 1988).

[5] 856 F.2d 12 (4th Cir. 1988).

[6] Kothe v. R. C. Taylor Trust, 280 U.S. 224, 227 (1930).

estate."[7] Abandonment permits the trustee to efficiently reduce the debtor's property to money for distribution to creditors, by freeing the estate of property that was worthless or not expected to sell for a price sufficiently in excess of encumbrances to offset the costs of administration.[8] Section 554(a) provides; "After notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value to the estate." In *Midlantic National Bank v. New Jersey Department of Environmental Protection*,[9] the Supreme Court addressed the issue of abandonment of property upon which state environmental violations exist, and carved out a narrow exception to that abandonment power.[10]

II. *MIDLANTIC NATIONAL BANK V. NJDEP*

Any discussion of a bankruptcy trustee's power to abandon property upon which state environmental violations exist must begin with a discussion of *Midlantic*. In a 5-4 decision, the Court created an exception to the abandonment power, holding "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."[11] However, the plain language of § 554(a) does not place any restraints on abandonment.[12]

The identified hazard in *Midlantic* was waste oil contaminated by PCB's, a highly toxic carcinogenic.[13] Quanta Resources Corporation ("Quanta") was in the business of processing waste

---

[7] 2 W. NORTON, BANKRUPTCY LAW AND PRACTICE § 30.01 (1984).

[8] 4 L. KING, COLLIER ON BANKRUPTCY § 554.01 (5th ed. 1985).

[9] 474 U.S. 494 (1986).

[10] "This exception to the abandonment power vested in the trustee by §554 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 be fettered by laws or regulations not reasonably calculated to protect the public health or safety from imminent and identifiable harm." *Midlantic*, 474 U.S. at 507 n.9.

[11] *Id.* at 507.

[12] *See* Cosetti and Friedman, *supra* note 2, at 67.

[13] In *Matter of Quanta Resources Corp.*, 739 F.2d 912, 913 n.1 (3d Cir. 1984) it was found that, "PCB's are themselves toxic. (Citation omitted). Their oxidation products (produced upon burning PCB's) are also toxic. Among the oxidation products of PCB's are polychlorinated dibenzo-p-dioxins (the so-called "dioxins") and polychlorinated dibenzo forans, which are powerful carcinogens, teratogens, and liver toxins." Citing Affidavit of Dan Levy, New York State Department of Law Environmental Scientist, App. 19-22.

oil at 2 facilities, one in Long Island City, New York and the other in Edgewater, New Jersey.[14] The Edgewater facility was operating under a temporary operating permit issued by the New Jersey Department of Environmental Protection ("NJDEP"), respondent in the case.[15] The petitioner, Midlantic National Bank, had provided Quanta with a $600,000 loan, secured by inventory, equipment, and accounts receivable.[16] That same month, NJDEP discovered Quanta had accepted 400,000 gallons of the PCB contaminated oil at the Edgewater site in violation of its operating permit, and ordered Quanta to cease operations. Quanta and the agency began negotiating the cleanup of the site, but Quanta filed a reorganization petition under Chapter 11[17] of the Bankruptcy Code before negotiations were complete, and the next day NJDEP issued an administrative order for Quanta to clean up the site.[18] The next month Quanta converted to Chapter 7 liquidation, and a trustee was appointed.[19] A subsequent investigation of the Long Island site disclosed that Quanta had stored over 70,000 gallons of the contaminated oil at the site in deteriorating and leaking containers.[20] After trying without success to sell the Long Island property, the trustee moved to abandon the real property pursuant to § 554(a). "No party to the bankruptcy proceeding disputed the trustee's allegation that the site was 'burdensome' and of 'inconsequential value to the estate' within the meaning of § 554."[21]

The city and state of New York objected, contending that abandonment would threaten the public's health and safety, and would violate state and federal environmental law. New York asked the Bankruptcy court to order that the assets of Quanta be used to clean up the site.[22] However, the Bankruptcy court approved the abandonment, finding the city and state were in a better position to do what needed to be done.[23] Shortly afterwards, the trustee moved to abandon the personal property at

---

[14] *Midlantic*, 474 U.S. at 497.
[15] *Id.*
[16] *Id.*
[17] *Id.*
[18] *Id.*
[19] *Id.*
[20] *Midlantic*, 474 U.S. at 497.
[21] *Id.*
[22] *Id.* at 498.
[23] *Id.*

the Edgewater site, which was approved over NJDEP's objections that the estate had sufficient funds to protect the public from the hazardous waste.[24]

The parties in the New York litigation consented to NJDEP's taking a direct appeal from Bankruptcy Court to the Court of Appeals pursuant to § 405(c)(1)(B) of the Code.[25] The appellate court reversed and remanded, and the Supreme Court granted certiorari.

A. Pre-Code Protections

The Supreme Court found that prior to the 1978 revisions of the Bankruptcy Code, a judicially-developed doctrine existed to protect state or federal interests, and determined that Congress did not intend to pre-empt that doctrine.[26] The court relied on three cases decided prior to the 1978 revisions to the Bankruptcy Code. In *Ottenheimer v. Whitaker*,[27] the Court of Appeals found that the trustee of a barge company could not abandon several barges which would have obstructed a navigable passage in contravention of federal law. The court held that the abandonment rule must give way when it conflicts with a safety of navigation statute, which is a duty and burden imposed by an Act of Congress in the public interest.[28]

In *In re Chicago Rapid Transit Co.*,[29] the Court of Appeals held that a trustee could not cease operations of a branch railway line in contravention of a local law requiring continued operation. The court did not forbid abandonment, but required the trustee's actions to conform with state law.[30] Likewise, *In re Lewis Jones, Inc.*,[31] required the debtor to seal off underground steam lines before abandonment. Relying upon these cases, the *Midlantic* Court declared that when Congress codified the rule of abandonment there were "well recognized restrictions on a trustee's abandonment power," and so must have meant to include the "established corollary that a trustee could not exer-

---

[24] *Id.*
[25] *Id.*
[26] *Id.* at 500-501. *See also* Cosetti and Friedman, *supra* note 2, at 76.
[27] 198 F.2d 289 (4th Cir. 1952).
[28] *Id.* at 290.
[29] 129 F.2d 1 (7th Cir. 1942).
[30] *Id.*
[31] 1 Bankr. Ct. Dec. 277 (Bankr. E.D. Pa. 1974).

cise his abandonment power in violation of certain state and federal laws."[32] Since the abandonment power was clearly restricted through judicial interpretation when Congress enacted § 554(a), if Congress intended for this legislation to alter that interpretation, it would specifically note any intended changes.[33]

B. Bankruptcy Code Protections

The Court found further support for the proposition that the abandonment power is restricted by looking to other sections of the Code. Section 362(a) of the Bankruptcy Code[34] is the automatic stay provision, which is

> one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy.[35]

---

[32] *Midlantic*, 474 U.S. at 501.

[33] *Id.*; *see also*, Edmonds v. Compagnie Generale Transatlantique, 443 U.S. 256, 266-277 (1979).

[34] Section 362(a) provides:

(a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970 (15 U.S.C. 78eee(a)(3), operates as a stay, applicable to all entities, of-

(1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other proceeding against the debtor that was or could have been commenced before the commencement of the old case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;

(2) the enforcement, against the debtor or against property of the estate, or of a judgment obtained before the commencement of the case under this title;

(3) any act to obtain possession of property of the estate or of property from the estate; (4) any act to create, perfect, or enforce any lien against property of the estate; (5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title; (6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title; (7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and (8) the commencement or continuation of a proceeding before the United States Tax Court concerning the debtor.

[35] S. Rep. No. 95-989, p. 54 (1978); H.R. Rep. No. 95-595, p. 340 (1977).

Despite this fundamental protection, Congress created several exceptions to the stay, and the Court cites § 362(b)(5), which permits the Government to enforce nonmonetary judgments against a debtor's estate.[36] The Court sidesteps the inference that express exceptions to the automatic stay provision would imply that an exception was not intended for the abandonment power provision,[37] finding instead that Congress had significantly broadened the scope of § 362, and that it "was necessary for Congress to limit this new power expressly."[38]

The Court also looks for support to Title 28 U.S.C. 959(b), which requires the trustee to manage and operate the property in his possession according to the requirements of the State.[39] Even though not applying to abandonment, the Court found the section "supports our conclusion the Congress did not intend for the . . . Code to pre-empt all state laws. . . ."[40]

C. *Other Statutory Protections*

The Court finds additional support in "repeated congressional emphasis on its 'goal of protecting the environment against toxic pollution,'"[41] referring to the Resource Conservation and Recovery Act, ("RCRA")[42] "which monitors hazardous wastes from their creation until after their permanent disposal,"[43] and the Comprehensive Environmental Response, Compensation, and Liability Act ("CERCLA")[44], which establishes a fund for the

---

[36] *Midlantic*, 474 U.S. at 503.

[37] *See, e.g., United States v. Wong Kim Bo*, 472 F.2d 720, 722 (5th Cir. 1972).

[38] *Midlantic*, 474 U.S. at 504.

[39] Section 959(b) provides:

> Except as provided in section 1166 of title 11, a trustee, receiver or manager appointed in any cause 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).

[40] *Midlantic*, 474 U.S. at 505.

[41] *Id.* (citing Chemical Manufacturers Assn., Inc. v. Natural Resources Defense Council, Inc., 470 U.S. 116, 143 (1985)).

[42] Pub. L. No. 94-580, 90 Stat. 2795 (codified as amended at 42 U.S.C. §§ 6901-6991 (1982 & Supp. 1987)).

[43] *Midlantic*, 474 U.S. at 505.

[44] Pub. L. No. 96-510, 94 Stat. 2767 (codified at 26 U.S.C. §§ 4611-4682 (1982) and at 42 U.S.C.A. § 6911(a), §§ 9601-9657 (West 1986 & Supp. 1990)).

cleanup of hazardous waste sites. The majority concludes that "[i]n the face of Congress' undisputed concern over the risks of the improper storage and disposal of hazardous and toxic substances, we are unwilling to presume that by enactment of § 554(a), Congress implicitly overturned longstanding restrictions on the common law abandonment power."[45] Therefore, 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."[46]

D. Minority Opinion Criticisms

In a scathing dissent by Justice Rehnquist, joined by the Chief Justice, and Justices White and O'Connor, the minority attacked the majority's reliance on "well recognized restrictions of a trustee's abandonment power"[47] prior to codification. Justice Rehnquist convincingly argues that the three cases cited by the majority do not stand for the proposition asserted by the majority. The minority opinion distinguishes *Ottenheimer*[48] because that case required reconciliation of a conflict with a federal statute and a judicial gloss on the Bankruptcy Act,[49] while in *Midlantic* the "conflict is with the uncertain commands of state laws the Court declines to identify."[50] Also, the pre-code law of abandonment was judge-made, and "raises . . . the inquiry as to whether that court would have decided the case the same way under the present Code."[51]

The minority concedes that *In re Lewis Jones, Inc.*[52] comes closer to supporting the majority's position, but "it too turns on the judge-made nature of the abandonment power," and that "the isolated decision of a single Bankruptcy Court [does not] rises to the level of 'established law' that we can fairly assume Congress intended to incorporate."[53]

---

[45] *Midlantic*, 474 U.S. at 506.

[46] *Id.* at 507 (Rehnquist, J., dissenting).

[47] *Id.*

[48] Ottenheimer v. Whitaker, 198 F.2d 289 (4th Cir. 1952). *See supra* text accompanying notes 27-28.

[49] *Midlantic*, 474 U.S. at 510 (Rehnquist, J., dissenting).*Id.*

[50] *Id.* at 510-11.

[51] *Id.* at 511.

[52] 1 Bankr. Ct. Dec. 277 (Bankr. E.D. Pa. 1974). *See supra* text accompanying note 31.

[53] *Midlantic*, 474 U.S. at 511 (citation omitted) (Rehnquist, J., dissenting).

The minority points out that in *In re Chicago Rapid Transit*,[54] the lower court authorized abandonment, with the imposition of conditions. The Court of Appeals affirmed the authorization of the abandonment, and the bankrupt did not appeal the propriety of the conditions. "So while . . . dicta [may] . . . support some limitation on the power of abandonment, the holding of the case certainly does not."[55]

The minority also cites Code §§ 362(b)(4) and (5) for the proposition that "Congress knew how to draft an exception covering the exercise of 'certain' police powers when it wanted to."[56] The dissent also cites § 1170(a)(2), pointing out that Congress "also knew how to draft a qualified abandonment provision."[57]

Rehnquist found the majority's discussion of § 959(b) "somewhat difficult to fathom."[58] The majority conceded that § 959(b) does not directly apply to abandonment, but does not delineate its indirect application. Rehnquist argues that abandonment does not fall within the parameters of "management or operation" of the estate under the § 959(b) provision.[59] He cites *In Re Adelphi Hospital Corp.*[60] for the language "in pre-Code liquidation proceedings the trustee is in no sense a manager of an institutions's operations."[61]

In Rehnquist's view, the Bankruptcy Court is a court of equity, but cannot enforce its views regarding sound public policy contrary to the Code's purpose, and forcing clean up of the sites using the assets of the estate is "plainly . . . contrary to the purposes of the Code."[62] While abandonment may aggravate existing dangers, notification of authorities before abandonment will adequately protect the public, and

> notice before abandonment in appropriate cases is perfectly consistent with the Code. It advances the State's interest in protecting the public health and safety, and, unlike the rather uncertain exception to the abandonment power propounded by

---

[54] 129 F.2d 1 (7th Cir. 1942). *See supra* text accompanying notes 29-30.
[55] *Midlantic*, 474 U.S. at 512 (Rehnquist, J., dissenting).
[56] *Id.* at 513.
[57] *Id.* at 513.
[58] *Id.*
[59] *Id.* at 514.
[60] 579 F.2d 726, 729, n.6 (2nd Cir. 1978).
[61] *Midlantic*, 474 U.S. at 514 (Rehnquist, J., dissenting).
[62] *Id.* at 514-15.

> the court, at the same time allows for the orderly liquidation and distribution of the estate's assets."[63]

Rehnquist concedes that there may be a far narrower condition, where abandonment "might create a genuine emergency that the trustee would be uniquely able to guard against."[64] In those circumstances, "the narrow exception that I would reserve surely would embrace that situation."[65]

III. A CRITICAL LOOK AT *MIDLANTIC*

This portion of the comment will address some of the concerns raised by the majority opinion's handling of *Midlantic*.

In *Ignoring Congressional Intent: Eight Years of Judicial Legislation*,[66] the authors share Justice Rehnquist's indignation regarding the majority's reasoning, and state that "[s]uch a limitation is clearly contrary to the legislative intent on the right to abandon."[67] The article in general attacks cases such as *Midlantic* as judicial legislation.[68] *Midlantic* infers from Congressional silence that the "well recognized restriction" on abandonment must clearly be included in the codification of § 554(a), since Congress did not make an explicit statement of its intent to change this judicial interpretation.[69] The legislative history of § 554(a) is sparse, consisting of this statement: "This section authorizes the court to authorize the trustee to abandon any property that is burdensome to the estate or that is of inconsequential value to the estate. Abandonment may be to any party with a possessory interest in the property abandoned."[70]

---

[63] *Id.* at 515.

[64] *Id.*

[65] *Id.*

[66] Klee and Merola, *Ignoring Congressional Intent: Eight Years of Judicial Legislation*, 62 AM. BANKR. L.J. 1 (1988).

[67] *Id.* at 8.

[68] *Id.* at 2, n.42:

> The 'mixed' signal the Supreme Court sends lower courts is clear though unarticulated—use rules of construction to support, rather than to determine a result. Adopt a 'plain meaning' posture where the language of the statute meets with judicial approval, and use legislative intent to contradict the language of the statute where a literal reading is not kind to the desired result. Leaving the courts with such flexibility allows the judiciary to construct a congressional intent that comports with any judge's view on an issue.

[69] *Midlantic*, 474 U.S. at 501.

[70] H.R. Rep. No. 595, 95th Cong., 1st Sess. 377 (1977); S. Rep. No. 989, 95th Cong., 2d Sess. 92 (1978).

While Justice Rehnquist did not stress the issue, other sections of the Code include restrictions, and the absence of any such restriction in § 554 should give rise to the inference that restrictions were intentionally excluded. "[W]here 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."[71]

The authors rely on Justice Rehnquist's dissent, the clear language of § 554(a) and its negative inferences, and the absence of legislative history, in concluding, "Congress never envisioned any restriction to the § 554 powers. The Supreme Court's decision does little more than legislate a priority imposing the cost of clean-up on the creditors of a bankrupt company rather than on the entire populace of a particular state."[72]

Another article agreed with the conclusion reached by the *Midlantic* Court, but was dissatisfied with its analysis.[73] Pointing to the three pre-Code cases cited for the judicially created exception to the abandonment power, the author reasoned that the Court should have furthered its analysis by pointing out that the purpose of these holdings were to prevent future harm. If the court had recognized these considerations, the author reasons, they could have established a specific common law limitation: prevention of future harm to people or the environment.[74]

However, the holding of the *Midlantic* decision may be more valid and reasonable than at first thought. The risk to public health and safety immediately comes to mind. When considered in light of the facts of *Midlantic*, the Court's holding is quite reasonable. The *Midlantic* trustee was not required to take any steps to reduce danger to the public, and actually aggravated the danger by allowing the removal of a 24 hour security patrol and the shutting down of a fire suppression system.[75]

---

[71] United States v. Wong Kim Bo, 472 F.2d 720, 722 (5th Cir. 1972), quoted with approval in Russello v. United States, 464 U.S. 16, 23 (1983).

[72] Klee and Merola, *supra*, note 66, at 10 n.35.

[73] Note, *Creditor's Right when Federal Bankruptcy Laws Conflict with State Environmental Agency Enforcement Powers after Midlantic National Bank*, 48 U. PITT. L. REV. 879 (1987).

[74] *Id.* at 888.

[75] *Midlantic*, 474 U.S. at 499, n.3: "The trustee was not required to take even relatively minor steps to reduce imminent danger, such as security fencing, drainage and diking repairs, sealing deteriorating tanks, and removing explosive agents. *Moreover,*

While the statutory construction given § 554(a) in *Midlantic* is strained, it can be viewed as logical and conforming with the rule that statutes on the same subject are construed together.[76] "Provisions in one act which are omitted in another on the same subject matter will be applied when the purpose of the two acts is consistent."[77]

IV. SUBSEQUENT CASES

The decisions following *Midlantic* have covered a wide spectrum, from allowing abandonment only if the estate has fully complied with all environmental laws and regulations, to allowing abandonment in all cases unless there is an immediate, imminent, and identifiable risk of harm to the public health and safety.

In re Peerless Plating[78] interpreted the *Midlantic* decision as requiring full compliance with applicable law. While the bankrupt in *Peerless* was found to be in violation of CERCLA instead of state law, the bankruptcy court found that this was not a significant distinction.[79] The court further found that the language in *Midlantic* called for a three part test:

> The clear impact of the Midlantic language . . . would appear to be that a trustee may not abandon a hazardous waste site unless:
> 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 merely be speculative or indeterminate.[80]

---

the trustee's abandonment at both sites aggravated already existing dangers by halting security measures that prevented public entry, vandalism, and fire." Joint Appendix in No. 83-5142 (CA3). pp. 11-12 (affidavit of Richard Docyk, Deputy Chief Inspector for N.Y. City Fire Department); *id.* at 26 (transcript of proceedings before DeVito, J.) (emphasis added). The 470,000 gallons of highly toxic and carcinogenic waste oil in unguarded, deteriorating containers, "present[ed] risks of explosion, fire, contamination of water supplies, destruction of natural resources, and injury, genetic damage, or death through personal contact." Brief for United States as *Amicus Curiae* 4, 23.

[76] Sutherland Stat. Const. § 51.02 (4th ed. 1984).

[77] *Id.*; *see generally, State "Superlien" Statutes: An Attempt to Resolve the Conflict Between the Bankruptcy Code and Environmental Law*, 59 TEMPLE L. Q. 981, 1003-1005 (1986).

[78] 70 B.R. 943 (Bkrtcy. W.D. Mich. 1987).

[79] *Id.* at 948 n.4.

[80] *Id.* at 947.

As to the first part of the test, the court noted that *Midlantic* did not provide an example of such an "onerous" law, but found that depletion of the estate's assets is not a valid argument for allowing abandonment.[81] The court speculated that such an onerous law could be one that prohibited abandonment even after the estate was exhausted.[82]

Although the evidence presented at trial in an attempt to prove the threat of immediate harm was "slapdash", the court nevertheless found that there was an immediate harm of the sort Congress meant to prevent by enacting CERCLA.[83] The court further found that since the presence of hazardous conditions was ongoing, it was not merely "a speculative or indeterminate violation."[84] Perhaps the notable distinction in *Peerless* is the court's declaration that the trustee must expend the *unencumbered* assets of the estate in cleaning up the property.[85]

The other end of the spectrum is represented by *In re Franklin Signal Corporation*.[86] The bankruptcy court essentially held that a trustee is required to take minimal steps to protect the public from imminent danger as a result of abandonment.[87] The court would apply a case-by-case approach to analyzing whether abandonment of hazardous wastes should be authorized.[88] It would require two affirmative steps by the trustee prior to abandonment: first, to conduct an investigation to determine what hazardous substances burden the property,[89] and second, to inform the appropriate agencies of the situation, including the intent to abandon.[90]

---

[81] *Id.*

[82] *Id.* at 947 n.3.

[83] *Id.* at 947.

[84] *Peerless*, 70 B.R. at 947.

[85] *Id.* at 948 (emphasis added).

[86] 65 B.R. 268 (Bkrtcy. D. Minn. 1986).

[87] *Id.* at 272.

[88] *Id.* at 272: "At least five factors must be considered: (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."

[89] *Id.* at 273 n.8:

> This condition does not require a trustee to investigate all property subject to abandonment. It is only when the trustee reasonably believes that an abandonment would violate state environmental laws that a preliminary investigation is required. Furthermore, the trustee does not necessarily have to employ an independent investigator to determine if the property is contaminated. Any reasonable means of investigation is permissible.

[90] *Id.* at 273.

In *In re Purco*[91], the trustee moved to abandon inventory located on the real property of the debtor. While there was no qualified testimony that the inventory was hazardous waste, the bankruptcy court assumed for the purposes of its opinion that it was, yet found "there is no showing that the public health and safety are not adequately protected . . ." and so allowed abandonment.[92]

In *In re Oklahoma Refining Co.*,[93] the violations were the result of 65 years of crude oil refining at the site. Large quantities of spent acid and caustic materials, as well as other waste substances, were dumped into open pits near a stream. The primary public health and safety concern is the leaching of "noxious" substances into the underground aquifer, and into the stream, which is a tributary of other streams that provide water for public consumption.[94] No contamination of the water supplies have yet been detected.[95] All of the expert witnesses testified that harm to the public is not now imminent; however, a toxicologist testified that something "bad" will eventually happen.[96] The court distinguished *Midlantic* factually, by reasoning that, there, abandonment would have aggravated existing dangers, while in the instant case, "denying and allowing abandonment produces the same result."[97] The court allowed abandonment, saying "[t]o require strict compliance with State environmental law under the facts of this case could create a bankruptcy case in perpetuity and fetter the estate to a situation without resolve."[98]

V. IN RE SMITH-DOUGLAS

The property involved in *In re Smith-Douglas*[99] was a fertilizer plant located at Streator, Illinois, part of the estate of Smith-Douglas, Inc. Upon it were conditions that violated Illinois'

---

[91] 76 B.R. 523 (Bkrtcy. W.D. Pa. 1987).

[92] *Id.* at 533.

[93] 63 B.R. 562 (Bkrtcy. W.D. Okl. 1986).

[94] *Id.* at 563.

[95] *Id.*

[96] *Id.* at 563-64.

[97] *Id.* at 565. "Under either scenario there were no funds available to finance the closure plan or post closure monitoring."

[98] *Id.* at 565.

[99] 856 F.2d 12 (4th Cir. 1988).

environmental laws.[100] The Illinois Environmental Protection Agency ("IEPA") monitored the facility, but had never taken any enforcement action. *Smith-Douglas* at first attempted a reorganization, but subsequently determined that it would be unsuccessful, and converted to a Chapter 7 liquidation proceeding. A trustee was appointed, and began liquidating the estate. There were no unencumbered assets. Eventually all of the property was sold, except the plant. The trustee moved to abandon, with Borden, Garrett[101] and the State of Illinois opposing abandonment. The Bankruptcy Court concluded that the environmental violations did not present any imminent danger to the public. The District Court affirmed the findings of the Bankruptcy

---

[100] *Id.* at 14. The violations were as follows:

A. Ponds 1, 2, 3, 4 and 5 were considered as treatment works, but they were operated without operating permits.

B. Pond 2 was subject to flooding during wet weather periods. It was not constructed, nor was it being operated, to minimize violations during wet weather periods.

C. Contaminants were deposited upon the land so as to create a water pollution hazard. Contaminants also had entered waters of the state at a number of locations at the facility and had caused violations of the Stream Water Quality Standards.

D. The discharge from sewer 4 and the discharge ditch out of pond 4 were considered point source discharges which require National Pollutant Discharge Elimination System Permits. The facility had no such permits.

E. Waters in the abandoned creek bed violated the water quality standards as follows: (1) The waters contained unnatural sludge, bottom deposits, color and turbidity. (2) Two water samples demonstrated a low pH (less than 6.5) and contamination by excessive amounts of fluoride, sulfate, cadmium, iron, and manganese.

F. Contaminants were entering Phillips Creek, causing the creek to contain unnatural sludge, bottom deposits, color and turbidity.

G. Waters contained in the roadside ditch adjacent to Smith-Douglas Road violated water quality standards as follows: (1) The waters contained unnatural sludge, bottom deposits, color, turbidity and odor. (2) A water sample showed a low pH (less than 6.5) and contamination by excessive amounts of fluoride, sulfate, iron, and manganese.

H. A sediment sample at pond 2 indicated an arsenic concentration that is higher than authorized but not at the danger level.

I. A liquid sample in a sump at the base of two tanks had a pH of less than one which is considered "hazardous" under regulations.

J. There were several 55 gallon drums of liquid waste with a flash point below 140.

K. One 55 gallon drum contained hazardous waste.

L. There were over ten drums of spent vanadium pentoxide waste which is a hazardous waste.

M. Three tanks contained spent sulfuric acid.

In re Smith-Douglas, 856 F.2d at 14.

[101] Borden Inc., and Bernard Garrett were former owners of the Streator facility.

Court, but found the financial condition of the debtor irrelevant.

The Fourth Circuit Court of Appeals affirmed the District Court, save for the financial condition of the debtor being irrelevant. The appellate court began its discussion with the problem of enforcing both a federal statute and a conflicting state statute, holding that state laws which require a bankruptcy trustee to maintain burdensome property may be pre-empted by the Supremacy Clause of Article VI of the United States Constitution.[102] The *Smith-Douglas* court held that *Midlantic* created "a narrow exception to the trustee's abandonment power in order to protect the public safety rather than a broad exception to shield the state treasury."[103] While recognizing this exception is contrary to the purposes of abandonment, "where conditions on property pose a danger of imminent death or illness, the person in control should not be permitted to abandon it with such conditions unattended."[104] The *Smith-Douglas* court qualified this holding by requiring that there be a serious health risk, where public health and safety is threatened with imminent and indentifiable harm, not where hazards are "speculative or may await appropriate action by an environmental agency."[105]

It seems apparent from this language that compliance with state environmental regulations will be unnecessary, and the abandonment prohibition applies only when the public is immediately threatened. However, the court opined that when an estate has unencumbered assets, stricter compliance with state environmental laws should be required. Cleanup costs are an "administrative expense within the meaning of § 507(a)(1), and would have priority over unsecured claims but be subordinate to secured claims."[106]

When presented with the question of whether to authorize abandonment of property upon which state environmental violations exist, the *Smith-Douglas* court held that the bankruptcy court must make the initial determination as to whether "the

---

[102] *Smith-Douglas*, 856 F.2d at 16. "[W]hen enforcement of a state law or regulation would undermine or stand as an obstacle to the accomplishment of the full purposes and objectives of Congress in enacting a federal statute, the conflict must be resolved in favor of the federal law." *Id.* at 15 (*citing* Hines v. Davidowitz, 312 U.S. 52, 66-67 (1941)).

[103] *Smith-Douglas*, 856 F.2d. at 16.

[104] *Id.*

[105] *Id.*

[106] *Id.* at 17.

risk of imminent harm exists in reference to the design of state law."[107] If such a risk exists, there must be "conditions that will adequately protect the public health and safety in accordance with governing state law."[108] Since the IEPA had not taken any enforcement action, [109] it was not clearly erroneous to determine that there was no threat of immediate harm.

CONCLUSION

The *Smith-Douglas* decision correctly tracks the language and spirit of *Midlantic*, and applies a well reasoned analysis of the facts of the case to the prohibition against abandonment. Within the bounds of existing law, the *Smith-Douglas* decision is a sound approach. However, *Smith-Douglas* takes a disturbing step towards the establishment of a presumption that the inactivity of a state agency implies there is no public health or safety threat. This may prove to be a significant contribution to a dangerous trend. Inactivity of a state agency regarding existing environmental law violations should merely be one of several factors when applying the imminent threat to public safety analysis.

It remains to be seen whether *Smith-Douglas* will resolve the conflict among the Bankruptcy Courts regarding abandonment of property upon which state environmental violations exist. The only certainty is that abandonment will not be permitted if there is an imminent, immediate danger to the public health and safety. One possible corollary is that a presumption that there is no immediate threat of harm will develop if the state agency has not taken action against the violator. Until Congress acts,[110]

---

[107] *Id.* at 16: "The Bankruptcy Court does not have the power to substitute its judgment for that of the state as to what constitutes a serious public health or safety risk."

[108] *Id.*

[109] *Id.*; *See also, In re Purco, Inc.* 76 B.R 523, 533 (Bkrtcy. W.D.Pa. 1987)(inactivity of agency indicates lack of threat to public health or safety); *But see, In re FCX, Inc.* 96 B.R. 49 (Bkrtcy. E.D.N.C. 1989) (While that may be some evidence that the governments did not consider this site to pose an immediate danger, it certainly does not decide the matter.).

[110] Sward, E., *Resolving Conflicts between Bankruptcy Law and The State Police Power*, 1987 WIS. L. R. 403, 449 (1987):

> [E]nvironmental pollution respects no borders, which suggests that the solution should be at the national level rather than at the state level. Since the national scope of environmental pollution prompted Congress to act on it in the first place, perhaps Congress should protect the legislation it

or until the Supreme Court again addresses the issue, there is little certainty as to how a motion to abandon contaminated property under § 554(a) will fare.

Brian Cumbo

---

has set up from being undermined by bankruptcy law . . . there are other areas of state regulation that have received much less attention but that also need some accommodation in bankruptcy. . . .