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STRIKING A BALANCE BETWEEN COMPETING POLICIES: THE ADMINISTRATIVE CLAIM AS AN ALTERNATIVE TO ENFORCE STATE CLEAN-UP ORDERS IN BANKRUPTCY PROCEEDINGS

*Joseph P. Cistulli**

I. INTRODUCTION

In the spirit of a fresh start, filing for bankruptcy allows a debtor to avoid many claims.¹ Creditors, therefore, can expect little or no return on their investments.² If an estate has any unencumbered funds, the Bankruptcy Code ("the Code") will determine in which order they will be distributed.³ At the top of this hierarchy in section 507 of the Code is the administrative claim.⁴ Section 503(b)(1)(A) defines the administrative claim as any claim which is an actual and necessary cost or expense needed to preserve the estate.⁵

A review of the history of the administrative claim reveals its broadening use by courts as means of enforcing certain judgments. Section 503(b)(1)(A) provides a statutory basis for elevating general,

* Solicitations Editor, 1988-89, BOSTON COLLEGE ENVIRONMENTAL AFFAIRS LAW REVIEW.

¹ 11 U.S.C. § 727(a) (1982 & Supp. II 1984). An order for relief in bankruptcy proceedings discharges the debts of an individual debtor. Note, *State "Superlien Statutes: An Attempt to Resolve the Conflict between the Bankruptcy Code and Environmental Law*, 59 TEMPLE L.Q. 981, 981-82 n.11 (1986) [hereinafter Note, *Superlien Statute*]. The phrase "fresh start" derives from the language in *Williams v. United States Fidelity Ins. Guar. Co.*, 236 U.S. 549, 554-55 (1945) (The bankruptcy code allows a debtor to "start afresh free from the obligations and responsibilities consequent upon business misfortunes.").

² J. ROGERS, TEACHING MATERIALS ON COMMERCIAL LAW, BOOK I 129 (1986) (available in Boston College Law School Library).

³ 11 U.S.C. § 507 (1982 & Supp. IV 1986) (listing priorities of expenses and claims).

⁴ *Id.* § 503(b)(1)(A).

⁵ *Id.*

unsecured claims to the level of an administrative claim.⁶ Many times courts, citing the administrative claim provision, actually base their decisions to elevate claims on policy considerations.⁷ Prioritizing claims based on policy considerations is nowhere more evident than in the area of toxic waste clean-up orders. Courts frequently cite the "actual and necessary" language of section 503(b)(1)(A) but in reality they go beyond the plain meaning of the statute to allow administrative claim status for hazardous waste clean-up orders.⁸

Because a petition for administrative claim status involves a hearing, the bankruptcy court can fairly adjudicate individual claims.⁹ Recent Supreme Court decisions indicate a willingness to accept the administrative claim argument as long as the claim is not a money judgment under Chapter 11.¹⁰ The reasoning and dicta of these cases, *Ohio v. Kovacs*¹¹ and *Midlantic National Bank v. New Jersey Department of Environmental Protection*,¹² provide a broad reading of section 503(b)(1)(A). Heightened public awareness of the health hazards posed by toxic waste disposal helps tip the balance in favor of allowing a 503(b)(1)(a) claim notwithstanding the fresh start policy.

After reviewing the history of the administrative claim in bankruptcy proceedings, this Comment traces the development of the administrative claim as a tool to enforce environmental claims against bankrupt estates. This Comment next examines how courts balance the imperative of the Code to provide a fresh start for bankrupt estates against the imminent harm posed by untreated hazardous waste sites. This Comment then describes various states' reactions to the Supreme Court decisions in *Ohio v. Kovacs* and *Midlantic National Bank v. New Jersey Department of Environmental Protection*. The Comment ultimately proposes that the administrative claim is an effective means of striking a balance between the competing policies of the Code and the state's interest in cleaning up hazardous wastes.

⁶ See *id.*

⁷ See *Midlantic Nat'l Bank v. New Jersey Dep't of Env'tl. Protection* (NJDEP), 106 S. Ct. 755, *reh'g denied*, 106 S. Ct. 1482 (1986).

⁸ See *In re Stevens*, 68 Bankr. 774 (Bankr. D. Me. 1987).

⁹ See 11 U.S.C. § 503(b)(1)(A) ("after notice and a hearing, there shall be allowed administrative expenses" (*emphasis added*)).

¹⁰ See *Midlantic Nat'l Bank v. NJDEP*, 106 S. Ct. 755, *reh'g denied*, 106 S. Ct. 1482 (1986).

¹¹ 469 U.S. 274 (1985).

¹² 106 S. Ct. 755.

II. ADMINISTRATIVE CLAIM STATUS UNDER SECTION 503(b)(1)(A) OF THE BANKRUPTCY CODE

A. An Overview of How Bankruptcy Affects a State Clean-Up Order

When a corporation files for bankruptcy under Chapter 7¹³ or Chapter 11¹⁴ creditors can expect little or no return on their investments.¹⁵ Chapter 11 reorganization proceedings may leave the debtor's business intact but inherent in reorganization is a restructuring of debt that leaves creditors only partially satisfied.¹⁶ Section 507 of the Bankruptcy Code establishes a hierarchy.¹⁷ Under a Chapter 7 liquidation proceeding, the trustee satisfies secured creditors,¹⁸ pays administrative expenses,¹⁹ and distributes the remaining pennies to general creditors.²⁰ Creditors cannot change the priority scheme but if creditors can improve their position in the scheme they can generally expect a better return on their investments.²¹

The priority list of the Code provides for an orderly distribution of assets to satisfy most claims.²² Non-monetary claims, such as government orders, however, complicate the orderly disbursement of funds to creditors.²³ As concern for a clean environment grows, bankruptcy courts are seeing a greater number of state environmental clean-up orders designed to ensure the cleanup of a bankrupt's real property.²⁴ A state's authority to initiate a cleanup or receive compensation for a completed cleanup is unclear.

When a company is solvent, a state agency, under the provisions of the Comprehensive Environmental Response, Compensation and

¹³ 11 U.S.C. §§ 701, 702 (1982 & Supp. IV 1986).

¹⁴ 11 U.S.C. § 521 (1982 & Supp. IV 1986).

¹⁵ R. HENSEN, SECURED TRANSACTIONS § 2-3 (1979).

¹⁶ See J. MACLACHLAN, BANKRUPTCY § 311, at 375 (1956).

¹⁷ 11 U.S.C. § 507.

¹⁸ 11 U.S.C. §§ 725, 507.

¹⁹ 11 U.S.C. § 507.

²⁰ 11 U.S.C. §§ 725, 507.

²¹ See MACLACHLAN, *supra* note 16, § 150, at 145; see, e.g., 3 L. KING, K. KLEE & R. LEVIN, COLLIER ON BANKRUPTCY § 507.02 (15th ed. 1985) [hereinafter COLLIER ON BANKRUPTCY].

²² 11 U.S.C. § 507.

²³ See generally *Ohio v. Kovacs*, 469 U.S. 274 (1985).

²⁴ See, e.g., *In re Stevens*, 68 Bankr. 774 (Bankr. D. Me. 1987); *In re Pierce Coal & Constr.*, 65 Bankr. 521 (Bankr. N.D. W. Va. 1986); *In re Security Gas & Oil, Inc.*, 15 Bankr. Ct. Dec. (CRR) 762 (Bankr. N.D. Cal. 1987).

Liability Act ("CERCLA")²⁵ or similar statutes,²⁶ can initiate a cleanup.²⁷ A state may either order a cleanup or begin the process itself.²⁸ If a state begins a cleanup, the state will be indemnified by the violating company.²⁹ Bankruptcy upsets this scheme. Under 11 U.S.C. § 554 the estate can attempt to abandon the hazardous waste as a liability.³⁰ Moreover, in the spirit of a fresh start, the bankruptcy court delegates the state's claim to general, unsecured status.³¹ If the state wants the area cleaned up it must pay for it.³² The cost of cleanup, however, impedes the execution of the order.³³ In either case the public suffers both fiscally and physically: the cleanup depletes state funds, and the neglect of the hazard threatens to cause permanent damage to property and life.

Government clean-up orders illustrate the tension between the Code's policy of protecting the rights of creditors and a general national policy of protecting the environment.³⁴ In the 1980's, environmental forces in the states have sought to supersede the Code's priority list.³⁵ To prevent evasion of state clean-up orders through bankruptcy, the states have begun to implement "super-lien" statutes.³⁶

Apart from state legislative efforts, the government, as a party to a bankruptcy proceeding, has sought to enhance its position by elevating its order to administrative claim status.³⁷

²⁵ Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA) 42 U.S.C. §§ 9601-9657 (1982 & Supp. IV 1986).

²⁶ Federal Hazardous Substances Act, 15 U.S.C. §§ 1261-1276 (1982 & Supp. IV 1986).

²⁷ See *supra* note 1 and accompanying text.

²⁸ See *id.*

²⁹ Fox & Gallagher, *Hazardous Waste Management: Legal Implications of Cleaning Up Inactive Sites*, in HAZARDOUS WASTE MANAGEMENT FOR THE 80's 441, 444-45 (T. SWEENEY ET AL. eds. 1982).

³⁰ 11 U.S.C. § 554 (1982).

³¹ *In re Security Gas & Oil, Inc.*, 15 Bankr. Ct. Dec. (CRR) 762, 768 (Bankr. N.D. Cal. 1987).

³² See Note, *Superlien Statute*, *supra* note 1, at 982.

³³ See *id.* at 982 n.9. "The cost of compliance with environmental statutes and cleanup [sic] orders is enormous. To illustrate the expense of cleanup, commentators have pointed out that the EPA spends an average of approximately \$12 million per Superfund site." *Id.*; see e.g., Moorman, Drabkin & Kirsh, *Bankruptcy and the Cleanup of Hazardous Waste: Caveat Creditor*, 15 *Envtl. L. Rep.* (Envtl. L. Inst.) 10,168, 10,169 & n.8 (1985) (citing 49 Fed. Reg. 40,320, 40,325 (1984)).

³⁴ See *Midlantic Nat'l Bank v. NJDEP*, 106 S. Ct. 755, 760, *reh'g denied*, 106 S. Ct. 1482 (1986).

³⁵ See Note, *Superlien Statute*, *supra* note 1, at 1005-06.

³⁶ See Zarin, *State Recovery of Hazardous Waste Cleanup Costs and Bankruptcy: The Constitutionality of Retroactive State Super Priority Lien Statutes*, 90 *COM. L.J.* 346 (1985). For examples of "superlien" statutes see MASS. GEN. L. ch 21E, § 1 (1986); N.H. REV. STAT. ANN. § 147-B:10 (Supp. 1988); N.J. STAT. ANN. § 58:10-23.11 f(f) (West 1982 & Supp. 1988)

³⁷ 11 U.S.C. § 507.

B. Section 503(b)(1)(A)

Section 507 of the Bankruptcy Code dictates the system of priorities under which claims against a bankrupt estate must be discharged.³⁸ If it were possible to discharge every claim of general creditors, while satisfying the costs of administration, trustees would not need a system of priorities.³⁹ Because it is usually impossible to satisfy all claims, the priorities assure payment of certain claims before others are satisfied.

Despite these priorities, courts nonetheless make policy considerations about the priority of creditors by applying equitable principles such as good faith, fairness to creditors and danger to the public.⁴⁰ Moreover, courts have looked to policy considerations to include or exclude certain expenses within the top priority category of administrative expenses.⁴¹ Because administrative expenses have priority over unsecured claims, the determination of what constitutes an administrative claim will decide whether the creditor receives full payment, partial payment, or no payment.⁴²

As early as the Act of 1800, Congress has recognized the first priority status of administrative claims.⁴³ Historically, bankruptcy legislation has recognized the sovereign's priority claim to a bankrupt's estate.⁴⁴ Although the Act of 1841 did not specify a priority for administrative claims,⁴⁵ claimants could achieve priority status through a court order.⁴⁶ The Act of 1867 set up a more complete framework including five priority levels with administrative claims being first.⁴⁷ Following this theme of priority, the Act of 1898, which

³⁸ Note, *The Administrative Expense Priority in Bankruptcy—A Survey*, 36 DRAKE L. REV. 135 (1987).

³⁹ 3 COLLIER ON BANKRUPTCY *supra* note 21, § 507.02 (15th ed. 1985).

⁴⁰ *Id.*

⁴¹ See 11 U.S.C. § 507(a)(1) (1982 & Supp. IV 1986). "The following expenses and claims have priority in the following order: (1) First, administrative expenses allowed under § 503(b) of this title [11 U.S.C. § 503(b)] . . ." *Id.*

⁴² See Note, *supra* note 38 and accompanying text.

⁴³ Pearlstein, *Bankruptcy Administrative Claimants—Beware!*, 90 COM. L.J. 632 (1985). "The Act of 1800 provided that debts owed to the United States would receive priority in distribution and in effect granted priority for reimbursement of expenses incurred in the administration of the bankrupt estate." *Id.*

⁴⁴ See COLLIER ON BANKRUPTCY *supra* note 21, §§ 507.01, 507.02.

⁴⁵ *Id.* "Three classes of priority were created by the Act of 1841: (1) debts due the United States, (2) debts due sureties for moneys actually paid out in behalf of the bankrupt, and (3) debts up to a maximum of twenty-five dollars for labor performed within six months of the bankruptcy." *Id.*

⁴⁶ *Id.*

⁴⁷ See Note, *supra* note 38, at 136; see also COLLIER ON BANKRUPTCY, *supra* note 21, § 507.01. The five classes of priority were: "(1) expenses of administration, (2) debts and taxes due the United States, (3) debts and taxes due the states, (4) wages due an operative, clerk,

remained in effect until October 1, 1979, provided for the priority of administrative expenses.⁴⁸ After a rearranging of priorities in the Acts of 1926 and 1938, an amendment in the Act of 1952 established administrative expenses as preferred.⁴⁹

Section 503(b)(1)(A) of the current Bankruptcy Code lists the expenses allowable as administrative priorities.⁵⁰ Generally, the expenses are those that are actual and necessary to preserve the estate. They include wages, salaries, and commissions for services rendered after the commencement of the proceedings.⁵¹ In the environmental area, the government is attempting to secure administrative expense priority by demonstrating that the cleanup of hazardous waste is a necessary expense to preserve the estate.⁵² There is latitude for determining what constitutes an administrative claim. The Code allows courts to view pre-Code cases as relevant in interpreting the "administrative nature of a claim."⁵³

Throughout the Code's development the administrative claim has remained a top priority in bankruptcy proceedings. By filing for administrative expense status, the states or private parties seeking to enforce environmental clean-up orders draw on the power of statutory history to enforce administrative claimants' rights. Since the inception of modern bankruptcy law two centuries ago, Congress has recognized the importance of the administrative expense as an inducement for third parties such as dealers and suppliers to deal with the bankrupt estate.⁵⁴

or house servant up to fifty dollars for labor performed within six months of bankruptcy, and (5) debts due any person entitled to a priority or preference under the laws of the United States." *Id.*

⁴⁸ See Note, *supra* note 38, at 136.

⁴⁹ See Pearlstein, *supra* note 43, at 633. "Section 64a(1) was amended in 1952 to provide that 'where an order is entered in a proceeding under any chapter of this act [of 1952] directing that bankruptcy be proceeded with, the costs and expenses of administration incurred in the ensuing bankruptcy proceeding shall have priority in advance of payment of the unpaid costs and expenses of administration, including the allowances provided for in such chapter, incurred in the superceded bankruptcy proceeding, in any The new language was provided to protect the Chapter 7 and to avoid the danger of a breakdown of administration.'" *Id.*

⁵⁰ 11 U.S.C. § 503(b)(1)(A) (Supp. IV 1984): "(b) after notice and a hearing, there shall be allowed administrative claims, other than claims allowed under § 502(f) of this title including: (1)(A) the actual and necessary costs and expenses of preserving the estate, including, wages, salaries, or commissions for services rendered after commencement of the case." *Id.* The similarity of section 64(a)(1) of the Bankruptcy Act of 1978 and 503(b)(1)(A) of the current Bankruptcy Code allow the courts to view pre-code cases as relevant in interpreting the "administrative nature of a claim." See Note, *supra* note 38, at 137, citing NORTON, BANKRUPTCY LAW AND PRACTICE § 12.11 (1984).

⁵¹ See Note, *supra* note 38, at 137.

⁵² See generally *In re Stevens*, 68 Bankr. 774 (Bankr. D. Me. 1987).

⁵³ 11 U.S.C. § 503(b)(1)(A).

⁵⁴ See Note, *supra* note 38, at 137 (citing *In re Mammoth Mart*, 536 F.2d 950, 954 (1st Cir.

Administrative expense priority also assures that efficient administration does not go unrewarded.⁵⁵ By encouraging third party interaction, the Code achieves one of two purposes: 1) rehabilitation of a debtor's estate under Chapter 11; or 2) preservation of assets of the estate for liquidation under Chapter 7.⁵⁶ Both efforts of the trustee ultimately benefit the creditors in either Chapter 11 or Chapter 7. As one court has explained: "Without a provision for administrative expense priority, 'efforts to reorganize would be hampered by the necessity of prepayment for all goods and services supplied to the estate, since presumably no creditor would willingly assume the status of a non-priority creditor to a debtor undergoing reorganization.'"⁵⁷

Traditionally, the administrative expense has been utilized to assure continued business transactions.⁵⁸ In this sense the expenses are "necessary."⁵⁹ Without regular business relations with third parties, reorganization could be impossible and could lead to an economically wasteful liquidation.⁶⁰ If a company liquidates, the administrative expense priority allows compensation for those managing and liquidating the estate.⁶¹ Courts are now extending the meaning of "necessary" to include compliance with state laws.⁶² Payment of such claims neither rehabilitates the estate nor preserves its assets, yet based on a public policy of protecting the environment, courts are broadening the meaning of "necessary" to enforce environmental clean-up orders.⁶³

C. Courts' Treatment of Section 503(b)(1)(A): A Review of Four Relevant Criteria

The range of claims allowed as administrative expenses against a bankrupt estate indicate a court's broad discretion in determining whether to elevate a claim to administrative expense status.⁶⁴ Sec-

1976)). The value of the business decreases when customers and dealers will not continue to deal with the bankrupt estate. Generally such interaction will increase the assets for all creditors. Administrative expense priority assures payment to those who continue dealing with the company.

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ *Id.* (citing *In re Jartran, Inc.*, 732 F.2d 584, 586 (7th Cir. 1984)).

⁵⁸ See *Mammoth Mart*, 536 F.2d at 954.

⁵⁹ See COLLIER ON BANKRUPTCY, *supra* note 21, § 503.20.

⁶⁰ *Id.*

⁶¹ See *id.* §§ 503.19-503.20.

⁶² See *In re Stevens*, 68 Bankr. 774, 782 n.7 (Bankr. D. Me. 1987).

⁶³ *Id.*

⁶⁴ See Note, *supra* note 38, at 137.

tion 503(b)(1)(A) of the Code allows payment as administrative expenses of the *actual and necessary* costs of preserving the estate.⁶⁵ Courts consider several factors when determining whether a claim fits under section 503. Specifically the claims must: 1) arise post-petition; 2) benefit the estate; 3) be necessary to prevent imminent harm; and 4) in the environmental area, be of a non-monetary nature.⁶⁶

The first factor is whether goods or services were acquired by the estate after the filing of bankruptcy.⁶⁷ Courts follow the general rule that post-petition filing is required to distinguish the claims as "necessary" to the estate.⁶⁸ *In re Giltex*, in which goods delivered to the debtor several hours prior to filing were not treated as administrative expenses, illustrates the strict enforcement of the post-petition filing rule by the courts.⁶⁹

In the environmental area the post-petition rule takes on a new meaning. In many cases the hazardous waste was stored on the property before the filing of bankruptcy.⁷⁰ Usually such a pre-petition storage condition gives rise to a general, unsecured claim.⁷¹ As illustrated in *In re Stevens*, however, some courts may allow administrative expense priority for conditions created pre-petition.⁷² Generally, when the debtor creates the hazard post-petition, clean-up orders can be treated as administrative expenses.⁷³ These somewhat different positions indicate the tension between the policy of the Bankruptcy Code and the policy of protecting the environment.⁷⁴

The second factor required to classify a claim as an administrative expense is that the goods or services giving rise to the claim benefit

⁶⁵ 11 U.S.C. § 503(b)(1)(A) (emphasis added).

⁶⁶ See *infra* notes 68-94 and accompanying text.

⁶⁷ Note, *supra* note 38, at 138 (citing NORTON, BANKRUPTCY LAW AND PRACTICE 12.05 (1984)).

⁶⁸ See 11 U.S.C. § 362(a)(1) (1982).

⁶⁹ 4 Bankr. Ct. Dec. (CRR) 1066 (Bankr. S.D.N.Y. 1978).

⁷⁰ See generally *Southern Ry. v. Johnson Bronze Co.*, 758 F.2d 137 (3d Cir. 1985); *In re Dant & Russell, Inc.*, 61 Bankr. 668 (Bankr. D. Or. 1985), *aff'd* No. 86-4435, (9th Cir. August 2, 1988).

⁷¹ *In re Security Gas & Oil, Inc.*, 15 Bankr. Ct. Dec. (CRR) 762, 768 n.5 (Bankr. N.D. Cal. 1987).

⁷² See *In re Stevens*, 68 Bankr. 774 (Bankr. D. Me. 1987).

⁷³ See *In re Pierce Coal & Constr.*, 65 Bankr. 521, 531 (Bankr. N.D. W. Va. 1986).

⁷⁴ See *infra* notes 252-82 and accompanying text. If the policy of protecting the environment at any cost prevailed, the creation of a hazardous condition pre or post-petition would have no bearing on environmental cleanup. That courts recognize the general post-petition rule even in environmental cases indicates an appreciation of the Code's priorities and a lack of a comprehensive environmental clean-up plan in bankruptcy.

the estate.⁷⁵ For example, in *Matter of Chicago, Rock Island and Pacific Railroad Company v. Iowa Department of Transportation*,⁷⁶ the court refused to allow an administrative expense for the removal of old railroad lines.⁷⁷ The removal might have benefitted creditors by eliminating the possibility of a tort claim.⁷⁸ The court, however, concluded that the benefit was too slight, indirect, and conjectural to justify classifying the expense as administrative.⁷⁹

When the debtor stores toxic material, the requirement of a benefit to the estate is expressed in terms of the threat of imminent harm⁸⁰—the third element of administrative expense categorizing. When determining the parameters of the actual and necessary expenses of preserving the estate,⁸¹ courts have found that debtors cannot abandon toxic waste in contravention of state health laws designed to protect the public health and safety from identified hazards.⁸² In *Stevens*,⁸³ the court explained the imminent harm and benefit to the estate standards in light of the Code's provisions for abandonment.⁸⁴ The explanation describes a need to prioritize toxic waste cleanup:

The clean up did confer benefit on the debtor's estate by bringing the estate into compliance with the cleanup mandate of state and federal law and by protecting the estate from increased liability [by abandonment] which would result in the event of spill Accordingly, the cleanup costs should be allowed as an administrative expense.⁸⁵

The decision in *Ohio v. Kovacs* completes the picture of the treatment of clean-up orders as administrative expenses in bankruptcy proceedings.⁸⁶ The Court describes the fourth test to determine administrative claim status. The Supreme Court held that Ohio's claim against a debtor for toxic waste cleanup was a money judgment and therefore dischargeable in bankruptcy.⁸⁷ The language suggesting

⁷⁵ *In re Mammoth Mart*, 536 F.2d 950, 954 (1st Cir. 1976).

⁷⁶ 756 F.2d 517 (7th Cir. 1985).

⁷⁷ *Id.* at 520.

⁷⁸ *Id.*

⁷⁹ *Id.*

⁸⁰ *See id.*

⁸¹ *See* 11 U.S.C. § 503(b)(1)(A).

⁸² *Midlantic Nat'l Bank v. NJDEP*, 106 S. Ct. 755, 762, *reh'g denied*, 106 S. Ct. 1482 (1986).

⁸³ *See In re Stevens*, 68 Bankr. 774 (Bankr. D. Me. 1987).

⁸⁴ *Id.*

⁸⁵ *Id.*

⁸⁶ *Ohio v. Kovacs*, 469 U.S. 274 (1985).

⁸⁷ *See id.* at 285. That a receiver had taken control of the company's operations and it was therefore impossible to comply with the clean-up order, also influenced the court. *Id.* at 263.

that the clean-up order had been converted into an obligation to pay money forced courts to reevaluate the actual nature of a clean-up order.⁸⁸ The ensuing struggle, fueled by dicta in *Kovacs*, has left the courts divided, but the struggle seems to be yielding to a popular willingness to allow administrative claims for the cleanup of hazardous waste.⁸⁹ By distinguishing fact patterns from the facts of *Kovacs*⁹⁰ and using the imminent harm criteria of *Midlantic National Bank*,⁹¹ some courts have found the clean up of toxic waste an appropriate administrative expense.⁹² The extent to which the clean-up priority will disrupt the Code's provisions remains to be seen, especially when the estate does not have enough money to pay the secured creditors.⁹³

III. THE DECISIONS OF *KOVACS* AND *MIDLANTIC NATIONAL BANK*

With concern for a clean environment as a background, courts also look to what restricts their equitable power to enforce state environmental laws—namely, the *Kovacs* precedent, the no-benefit rule, the pre-petition rule, the imminent danger standard, and the practical concern of the financial restraints of the estate. A legitimate question is whether the administrative claim provision provides adequate statutory authority to overcome these obstacles. In some cases the answer is yes.⁹⁴ This section explores the decisions in *Ohio v. Kovacs* and *Midlantic National Bank*. While *Kovacs* appears to restrict the enforcement of clean-up orders, the language and dicta of the case suggest that policy concerns will play a role in overcoming statutory mandates. *Midlantic National Bank* explicitly recognizes the importance of a safe environment as reason enough to allow administrative expense status for clean-up orders.

A. *Ohio v. Kovacs*

Before evaluating these obstacles as applied to recent cases, a review of *Ohio v. Kovacs* illustrates the Supreme Court's effort to keep the Code intact as a shelter for orderly reorganization and

⁸⁸ *Penn Terra Ltd. v. Department of Env'tl Resources*, 733 F.2d 267, 277-78 (3d Cir. 1984).

⁸⁹ See *In re Stevens*, 68 Bankr. at 783; see, e.g., *In re Pierce Coal & Constr.*, 65 Bankr. 521, 540 (Bankr. N.D. W. Va. 1986).

⁹⁰ See *Southern Ry. v. Johnson Bronze*, 758 F.2d 137, 141 (3d Cir. 1985).

⁹¹ See *infra* notes 124-44 and accompanying text.

⁹² See *infra* notes 220-47 and accompanying text.

⁹³ See *In re T.P. Long Chemical, Inc.*, 45 Bankr. 278 (Bankr. N.D. Ohio 1985).

⁹⁴ See *infra* notes 143-247 and accompanying text.

liquidation.⁹⁵ In *Kovacs*, Chem-Dyne Corporation ("Chem-Dyne") operated a hazardous waste management facility in Hamilton, Ohio.⁹⁶ The state initiated an action under Ohio law against Chem-Dyne for the pollution of waters⁹⁷ and public nuisance.⁹⁸ After Chem-Dyne failed to comply with a court-imposed clean-up order, the court appointed a receiver to implement the order.⁹⁹

Before the receiver could complete the task, Kovacs, a shareholder of the company and its chief executive officer, filed for reorganization under Chapter 11 of the Code.¹⁰⁰ Subsequently, at Kovacs's request, the court converted the proceeding to one of liquidation under Chapter 7.¹⁰¹ The state then filed an action to declare Kovacs's obligation nondischargeable in bankruptcy.¹⁰² Ohio asserted two arguments, both of which the Supreme Court rejected.¹⁰³

First, the state argued that it did not have a claim against Kovacs under Code section 101(4) because "breach of performance" does not include a violation of state statute. If the state did not have a claim against Kovacs, then under the Code, the state's "nonclaim" is not dischargeable in bankruptcy.¹⁰⁴ Under section 101(4) of the Code breach of performance is a claim.¹⁰⁵ Therefore, if Kovacs's inaction is described as a "breach of performance" the state's demand for

⁹⁵ See generally Note, *Dumping Waste, Discharging Debts: Ohio v. Kovacs (Kovacs II)*, 13 *ECOLOGICAL L.Q.* 661 (1986).

⁹⁶ *Ohio v. Kovacs*, 469 U.S. 274, 276 (1985).

⁹⁷ See *id.*, referring to OHIO REV. CODE ANN. § 6111.04 (Baldwin 1977).

⁹⁸ *Kovacs*, 469 U.S. at 276.

⁹⁹ *Id.*

¹⁰⁰ *Id.*

¹⁰¹ *Id.* at 276 n.1.

¹⁰² *Id.* at 276-77.

¹⁰³ *Id.* at 284-85.

¹⁰⁴ See *id.* at 278-79; Note, *supra* note 96, at 663 n.17.

The distinction between a "claim" and what could be called a "non-claim" is essential to an understanding of *Kovacs II*. The advantage of having a "claim" against a debtor is that it provides a party with "creditor" status, see 11 U.S.C. § 101(9) (1982) (defining "creditor" in part as an "entity that has a claim against the debtor") and enables the creditor to share in the distribution of the bankruptcy estate, see *id.* § 726 (providing for distribution of the estate based on claims against the estate). The disadvantage of having a claim is that the claim, as a debt of the bankrupt individual, is dischargeable in bankruptcy Thus, if the bankruptcy estate is insufficient to satisfy the claim, the individual debtor is freed from any further obligation to the creditor. By the same token, a "nonclaim" does not entitle a party to share in the bankruptcy estate, but it has the advantage of not being dischargeable in bankruptcy. Therefore, if Ohio did not have a "claim" against Kovacs, it would be entitled to enforce the clean up obligation against him after bankruptcy.

Note, *supra* note 96, at 663 n.17; see, e.g., 11 U.S.C. § 101(4) (1982).

¹⁰⁵ 11 U.S.C. § 101(4).

action is dischargeable.¹⁰⁶ Ohio asserted that “breach of performance” applies only in commercial settings.¹⁰⁷ The Court rejected this position, finding that Ohio had conceded that the \$75,000 injury to wildlife claim was within section 101(4).¹⁰⁸ Because the wildlife claim and clean-up order both arose from the violation of statutes, the Court found no reason to distinguish the two.¹⁰⁹ Looking to legislative history, the Court also found congressional intent to give “claim” a broad reading.¹¹⁰

The Court also dismissed Ohio’s second contention, that its claim was not a money judgment.¹¹¹ Under the Code money judgments used to enforce police powers are dischargeable.¹¹² With a receiver in control of the site to shield Kovacs from “personally taking charge of . . . the removal of wastes . . .”¹¹³ the Court held that the state effectively converted Kovacs’s affirmative responsibility into a money judgment.¹¹⁴ The Court found that “[w]hat the receiver wanted from Kovacs after Bankruptcy was the money to defray clean up costs.”¹¹⁵

Having decided that the cost of cleanup was dischargeable in bankruptcy, the Court distinguished *Penn Terra Ltd. v. Department of Environmental Resources*.¹¹⁶ In *Penn Terra*, “there had been no

¹⁰⁶ See *Kovacs*, 469 U.S. at 279–80.

¹⁰⁷ *Id.* at 279.

¹⁰⁸ *Id.*

¹⁰⁹ *Id.*

¹¹⁰ *Id.*; see also Note, *supra* note 96, at 665 n.31:

‘claim’ was described as allowing ‘all obligations of the debtor, no matter how remote or contingent . . . to be dealt with in the bankruptcy case.’ A broad definition of ‘claim’ serves at least two purposes. First, it effectuates the ‘fresh start’ purpose of the Bankruptcy Code because the individual debtor’s liability on a claim is dischargeable under the Code [see 11 U.S.C. § 727 (1982 & Supp. IV 1986); 11 U.S.C. § 101(4) (1982)]. Second, it gives potential creditors the greatest access to the estate in order to satisfy the unmet obligations of the debtor because a ‘claim’ is a prerequisite to a share in the estate.

See Note, *supra* note 96, at 665 n.31.

¹¹¹ See *Kovacs*, 469 U.S. at 284; see also 11 U.S.C. § 362(b)(5) (1982). Under this section money judgments to enforce police or regulatory powers are subject to the automatic stay, and are therefore dischargeable. 11 U.S.C. § 362(b)(5).

¹¹² See 11 U.S.C. § 362(b)(5).

¹¹³ See *Kovacs* 469 U.S. at 283.

¹¹⁴ *Id.* at 282.

¹¹⁵ *Id.* at 283.

¹¹⁶ 733 F.2d 267 (3d Cir. 1984). In *Penn Terra*, a mining company operated several mines in violation of various state environmental protection statutes. *Id.* at 269 n.1. The state of Pennsylvania filed for an injunction for the clean-up of the mines. Before the company complied with the clean-up order, it filed for bankruptcy under Chapter 7. The court considered the following issues when ruling that the injunction was nondischargeable: that in its form and substance the equitable remedy of injunction is not traditionally associated with the charac-

appointment of a receiver who had the duty to comply with the state law and who was seeking money from the bankrupt."¹¹⁷

Another distinction the Court made when deciding *Kovacs* was the effect on the trustee's action if a receiver had not been appointed:¹¹⁸

Had no receiver been appointed prior to Kovacs's bankruptcy, the trustee would have been charged with the duty of collecting Kovacs's nonexempt property and administering it. If the site at issue were Kovacs's property, the trustee would shortly determine whether it was of value to the estate. If the property was worth more than the costs of bringing it into compliance with state law, the trustee would undoubtedly sell it for its net value, and the buyer would clean up the property, in which event whatever obligation Kovacs might have had to clean up the property would have been satisfied. If the property were worth less than the clean up, the trustee would likely abandon it to its prior owner, who would have to comply with the state environmental law to the extent of his or its ability.¹¹⁹

Although *Kovacs* is often cited as a landmark decision adversely affecting environmental claims, the Court's reasoning and dicta in fact open the door for allowance of administrative status for clean-up orders.¹²⁰ The main limitation the case creates—unenforceability of money judgments—is itself overshadowed by the receiver's taking over the estate.¹²¹ The applicability of *Kovacs* for avoiding administrative expense status is limited to clear monetary claims.¹²²

B. Midlantic National Bank

With the *Midlantic National Bank*¹²³ decision the Court has limited the ability of a trustee in bankruptcy to abandon hazardous waste properties. In *Midlantic*, Quanta Resources Corporation

teristics of a money judgment—which is a remedy intended for compensation of past injuries that is not reduceable to a certain sum. Additionally, monies were not sought by the Commonwealth as creditor or obligee, money could not satisfy the Commonwealth, and the remedy was designed to prevent *future* harm and restore the environment. *Id.* at 278.

¹¹⁷ *Kovacs*, 469 U.S. at 283 n.11.

¹¹⁸ See Note, *supra* note 95, at 667.

¹¹⁹ *Kovacs*, 469 U.S. at 284–85 n.12.

¹²⁰ See *In re Stevens*, 68 Bankr. 774, 783 (Bankr. D. Me. 1987).

¹²¹ *Kovacs*, 469 U.S. at 283.

¹²² Compare *Penn Terra Ltd. v. Department of Env'tl. Resources*, 733 F.2d 267, 278 (3d Cir. 1984) (injunction compelling expenditure is the type of remedy associated with a money judgment). The court, finding that most injunctive orders compel expenditure, stated that "almost everything costs something." *Id.*

¹²³ See *infra* notes 186–95 and accompanying text.

("Quanta"), a waste oil processing company, accepted 400,000 gallons of PCB contaminated oil in violation of its operating permit.¹²⁴ Before the New Jersey Department of Environmental Protection ("NJDEP") and Quanta could negotiate a clean-up plan, Quanta filed for reorganization under Chapter 11.¹²⁵ The next day, NJDEP filed an administrative order to clean up the site.¹²⁶ Due to its perilous financial state, Quanta converted to a Chapter 7 liquidation and sought to abandon the property under section 554(a).¹²⁷ 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."¹²⁸ The Court rejected Quanta's contention that the automatic stay¹²⁹ provision prevented the state from enforcing environmental laws.¹³⁰ Generally, the automatic stay provision prevents creditors from enforcing a judgment against the debtor.¹³¹

¹²⁴ Midlantic Nat'l Bank v. NJDEP, 106 S. Ct. 755, 757, *reh'g denied*, 106 S. Ct. 1482 (1986).

¹²⁵ *Id.*

¹²⁶ *Id.*

¹²⁷ *Id.* at 758.

¹²⁸ *Id.* at 762 (footnote omitted).

¹²⁹ 11 U.S.C. § 362(a) (1982) 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 of employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the 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 the property of the estate, 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 or to exercise control over property of 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.

Id.

¹³⁰ See Midlantic Nat'l Bank v. NJDEP, 106 S. Ct. 755, 761, *reh'g denied*, 106 S. Ct. 1482 (1986).

¹³¹ See *supra* note 129 and accompanying text.

In its analysis, the *Midlantic* Court pointed to dicta in *Kovacs*¹³² suggesting that the bankruptcy trustee must comply with state laws designed to protect public health and safety.¹³³ In addition, the Court emphasized statutory exceptions, such as section 362(b)(5), permitting the government to enforce "nonmonetary" judgments against the debtor's estate.¹³⁴ The *Midlantic* Court explained that the legislative history of section 362(a) indicates that the exception's purpose is to protect public health and safety.¹³⁵ Moreover, the Court found congressional intent against the Code's pre-emption of state laws in 28 U.S.C. § 959(b), which commands a trustee in bankruptcy to "manage and operate the property in his possession . . . according to the requirements of the valid laws of the state."¹³⁶

In the face of the expanded power of section 362, which seemed to foreclose the state's efforts to enforce anti-pollution laws,¹³⁷ Congress overruled such broad language in its 1978 version of the Bankruptcy Rules of 1973.¹³⁸ Before 1978 the Code in effect protected polluters.¹³⁹ The 1978 amendments clarified Congress's intention to enforce environmental laws.¹⁴⁰

These expressions of congressional intent to protect the environment from toxic pollution in the bankruptcy area reflect an expanded effort to control the treatment, disposal and storage of hazardous waste.¹⁴¹ In *Midlantic*, the Court viewed the wave of congressional

¹³² 469 U.S. 274 (1985).

¹³³ See *Midlantic Nat'l Bank*, 106 S. Ct. at 760.

¹³⁴ *Id.* at 761; see *infra* notes 96-120 and accompanying text.

¹³⁵ See *Midlantic Nat'l Bank*, 106 S. Ct. at 761. "Thus, where a governmental unit is suing a debtor to prevent or stop violation of fraud, *environmental protection*, consumer protection, *safety*, or *similar police or regulatory laws*, or attempting to fix damages for violation of such a law, the action or proceeding is not stayed under the automatic stay." *Id.* (emphasis supplied).

¹³⁶ See *id.* Section 959(b) is a section of Judiciary and Judicial Procedure. 28 U.S.C. §§ 1-2906 (1982 & Supp. IV 1986).

¹³⁷ *Midlantic Nat'l Bank*, 106 S. Ct. at 761 n.6 (citing *Hillside Foundry Co. v. Michigan ex rel. Kelly*, 1 Bankr. Ct. Dec. (CRR) 195 (Bankr. W.D. Mich. 1974), "action by Michigan Attorney General to enforce State's antipollution laws held subject to automatic stay. The House Report also referred to an unreported case from Texas where a stay prevented the state of Maine from closing down a debtor's plant that was polluting a river in violation of the State's environmental protection laws.") *Midlantic Nat'l Bank*, 106 S. Ct. at 761, discussing H.R. REP. NO. 595, 95th Cong., 1st Sess. 174, 175, *reprinted in* 1978 U.S. CODE CONG. & ADMIN. NEWS 6134-36.

¹³⁸ *Id.*

¹³⁹ *Midlantic Nat'l Bank*, 106 S. Ct. at 761.

¹⁴⁰ See 11 U.S.C. § 362(b) (1982).

¹⁴¹ See Solid Waste Disposal Act, 42 U.S.C. §§ 6901-6987 (1982 & Supp. IV 1986) (Act to monitor waste from creation to after disposal; authorizes U.S. to seek judicial or administrative restraint of activities involving hazardous wastes that "present imminent and substantial endangerment to health or the environment.") 42 U.S.C. § 6973; CERCLA, 42 U.S.C.

action favoring environmental protection as overshadowing the abandonment provisions of the Bankruptcy Code.¹⁴² Moreover, public concern about the storage of hazardous waste in some instances supersedes statutory dictates of the Bankruptcy Code.¹⁴³

IV. SUBSEQUENT CASE LAW: THE CONTINUING INFLUENCE OF *OHIO V. KOVACS* AND *MIDLANTIC NATIONAL BANK*

In light of *Kovacs*, any agency seeking to enforce an environmental order against a bankrupt estate should not phrase the order in terms of monetary relief.¹⁴⁴ In the wake of *Midlantic* and *Kovacs* the other factors, "no benefit, no burden," pre-petition filing, and imminent danger, have influenced courts in varying degrees. A review of the relevant case law interpreting these factors reveals a wide range of decisions not easily reconciled.

While the no benefit no burden prong has a statutory basis, the Supreme Court has limited its value in the environmental area. Under section 554(a) of the Code a trustee can abandon "any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate."¹⁴⁵ *Midlantic*, however, restricts abandonment power when it would threaten public health and safety.¹⁴⁶ If trustees cannot abandon the real estate, then they must comply with state environmental laws.¹⁴⁷ It follows that the cost then becomes an "actual and necessary" administrative cost under section 503(b)(1)(A).¹⁴⁸

§§ 9601-9657 (1982 & Supp. IV 1986) (establishes fund to finance toxic waste clean-up and seek reimbursement from responsible parties; also empowers Federal Government to pursue relief necessary to prevent imminent harm to public health from release of hazardous substances).

¹⁴² See *Midlantic Nat'l Bank v. NJDEP*, 106 S. Ct. 755, 762, *reh'g denied*, 106 S. Ct. 1482 (1986).

¹⁴³ *Id.* While the Court did not expressly hold that environmental policy supersedes the Code, its statutory interpretation revealed a bias in favor of non-abandonment and therefore cleanup. See generally Note, *The Future of the Environmental Enforcement Injunction after Ohio v. Kovacs*, 13 B.C. ENVTL. AFF. L. REV. 397, 397-401 (1986).

¹⁴⁴ See generally *Ohio v. Kovacs*, 469 U.S. 274 (1985); see also *Penn Terra*, 733 F.2d 267 (3d Cir. 1984) (court vigorously defends the position that the claim is not monetary).

¹⁴⁵ 11 U.S.C. § 554(a).

¹⁴⁶ See *Midlantic Nat'l Bank*, 106 S. Ct. at 760.

¹⁴⁷ See *supra* note 135 and accompanying text.

¹⁴⁸ See *In re Stevens*, 68 Bankr. 774, 782 n.7 (Bankr. D. Me. 1987). Before *Midlantic*, in *In re Wall Tube & Metal Products*, 56 Bankr. 918 (Bankr. E.D. Tenn. 1986), the court declined to allow priority status to sampling and analyses of hazardous wastes. Because neither the estate nor its creditors benefitted, the court reasoned that the costs of such testing were not "actual and necessary costs and expenses of preserving the estate within the meaning of § 503(b)." *Id.*

In the wake of *Midlantic*, the policy exception to the benefit/burden abandonment criterion appears to be settled in favor of environmental enforcement. In *In re Stevens*, debtors stored PCB-contaminated oil in violation of State Department of Environmental Protection orders to remove it.¹⁴⁹ The *In re Stevens* court held that the trustee could not abandon the property even though the property did not benefit the estate.¹⁵⁰

Allowing the trustee to abandon the waste, reasoned the court, would result in reverting title to individual debtors, who would be without the resources to dispose of the oil.¹⁵¹ The estate would then be violating certain state environmental laws. Under the state's environmental protection statute, the trustee would be permitting a threatened discharge.¹⁵² Ongoing storage violated state law,¹⁵³ and revesting title in debtors would constitute a discharge by the trustee.¹⁵⁴ Abandoning the waste, therefore, would violate the state's public policy expressed by statute and affirmed by the Supreme Court in *Midlantic*.¹⁵⁵ The clear language of *Midlantic* enables courts to invoke the public policy of protecting health and safety to temper the Code's abandonment provisions.

Whereas *Midlantic's* decree on abandonment is clear, the specifics of what constitutes "imminent danger"¹⁵⁶ have yet to be determined. If a court classifies hazardous waste storage as imminently dangerous, the court will not allow the trustee to abandon the property. In *Midlantic*, Justice Powell stated that "[t]he Bankruptcy Code does not have the power to authorize an abandonment without formulating conditions that will adequately protect the public's health and safety."¹⁵⁷ Powell did not expand on what conditions will adequately protect the public health from "imminent and identifiable harm."¹⁵⁸ Whether courts view identifiable harm as inherent in the storage of

¹⁴⁹ *Stevens*, 68 Bankr. at 776.

¹⁵⁰ *See id.* at 780.

¹⁵¹ *Id.* at 780-81 n.6.

¹⁵² *Id.*

¹⁵³ *Id.* (citing ME. REV. STAT. ANN. tit. 38, § 1306(1) (1987)).

¹⁵⁴ *Id.* (citing ME. REV. STAT. ANN. tit. 38, §§ 1303(3) (defining "disposal" as including the placing of hazardous waste so that the hazardous waste may enter the environment), 1317 (defining discharge as including "disposing"), 1317A (prohibiting discharge of hazardous material)).

¹⁵⁵ *Id.* (citing ME. REV. STAT. ANN. tit. 38, § 1302 ("waste oil if not properly handled, is a threat to the public health, safety, and welfare and to the environment and therefore must be controlled")).

¹⁵⁶ *Midlantic Nat'l Bank v. NJDEP*, 106 S. Ct. 755, 762 (1986).

¹⁵⁷ *Id.*

¹⁵⁸ *Id.* at 762-63 n.9.

toxic waste or whether the debtor can take appropriate measures to protect public safety determines whether the court will allow abandonment.¹⁵⁹

At one end of the spectrum are the cases that consider environmental laws but do not demand full compliance with those laws.¹⁶⁰ For example, in *In re Franklin Signal Corp.*, the court interpreted *Midlantic* to mean that the trustee “only needs to take adequate precautionary measures to ensure that there is no imminent danger to the public as a result of abandonment.”¹⁶¹ The court formulated five criteria to be considered before abandonment would be permissible: “1) the imminence of danger to 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 for cleanup.”¹⁶² Applying these considerations to the facts of the case—storage of fourteen drums of hazardous chemicals—the court concluded that although the drums were in a deteriorating condition they did not pose a threat to public health.¹⁶³

In a footnote, the court rejected the holding of *In re Oklahoma Refining Co.*, that the court need only “take environmental laws and regulations into consideration.”¹⁶⁴ The *Franklin* court determined that *Midlantic* required more than mere consideration but something less than full compliance.¹⁶⁵

To support this interpretation of *Midlantic*, the *Franklin* court reasoned that strict compliance would leave the trustee helpless.¹⁶⁶ On the one hand, without funds the trustee could not pay for the cleanup.¹⁶⁷ On the other hand, the court could not authorize abandonment if abandonment would contravene state environmental laws.¹⁶⁸ The court speculated that the result would be an abandon-

¹⁵⁹ See *id.* at 766 (Rehnquist, J., dissenting).

¹⁶⁰ See, e.g., *In re Franklin Signal Corp.*, 15 Bankr. Ct. Dec. (CRR) 55, 59 (Bankr. D. Minn. 1986); *In re Oklahoma Refining Co.*, 63 Bankr. 562, 566 (Bankr. W.D. Okla. 1986); see also *In re Catamount Dyers, Inc.*, 13 Bankr. Ct. Dec. (CRR) 321, 323 (Bankr. D. Vt. 1985) (decided before the Supreme Court decision in *Midlantic* and accepting the dissent in the Third Circuit decision of the same case).

¹⁶¹ *Franklin*, 15 Bankr. Ct. Dec. (CRR) at 57.

¹⁶² *Id.*

¹⁶³ *Id.* at 59.

¹⁶⁴ *Id.* at 57 n.4 (quoting *In re Oklahoma Refining Co.*, 63 Bankr. 562 (Bankr. W.D. Okla. 1986)).

¹⁶⁵ *Franklin*, 15 Bankr. Ct. Dec. (CRR) at 57 n.4.

¹⁶⁶ *Id.* at 57 n.5.

¹⁶⁷ *Id.*

¹⁶⁸ *Id.*

ment by default under 11 U.S.C. 554(c).¹⁶⁹ If a trustee abandons property by default the property reverts to the debtor who usually does not have the funds to pay for cleanup.¹⁷⁰

This reasoning led the court to assume that the majority in *Midlantic* did not intend such a result.¹⁷¹ After explaining five factors, the imminence of danger, the extent of possible harm, the amount or type of hazardous waste, the cost to bring the property in compliance with environmental laws, and the amount of funds available, the court concluded that a trustee take only precautionary measures to secure the waste before abandonment.¹⁷² The court also rested its conclusion on a distinction of the facts of *Midlantic*. *Midlantic* involved 470,000 gallons of highly toxic and carcinogenic waste which presented risks of fire, explosion and death.¹⁷³ The *Franklin* case "is not nearly as alarming with respect to the amount and type of waste. The issue is not one of public safety but one of money; who must bear the cost of clean-up."¹⁷⁴ The *Franklin* court appears to have relied on the degree of harm, perhaps ignoring Powell's imminent and identifiable harm standard.¹⁷⁵

Conversely, there are cases that do not allow abandonment and require administrative expense priority for the cleanup of toxic waste.¹⁷⁶ In *In re Stevens*, the trustee of a bankrupt estate sought to secure twenty-nine drums of PCB-contaminated waste by storing them in a tractor trailer, roping off the area and posting warning signs.¹⁷⁷ The Department of Environmental Protection ("DEP") informed the trustee that such storage was inadequate.¹⁷⁸ When the trustee failed to comply with the pertinent storage regulations, the DEP contracted for the removal at a cost of \$7572.20.¹⁷⁹ The DEP

¹⁶⁹ 11 U.S.C. § 554(c) provides: "any property scheduled under section 521(1) of this title is not otherwise administered at the time of the closing of a case is abandoned to the debtor and administered for purposes of section 350 of this title."

¹⁷⁰ *Franklin*, 15 Bankr. Ct. Dec. (CRR) at 57 n.5.

¹⁷¹ *Id.* at 57-58 n.5.

¹⁷² *See id.* at 57-59.

¹⁷³ *Id.* at 59 n.9.

¹⁷⁴ *Id.*

¹⁷⁵ *See Midlantic Nat'l Bank v. NJDEP*, 106 S. Ct. 755, 762, *reh'g denied*, 106 S. Ct. 1482 (1986).

¹⁷⁶ *See In re Stevens*, 68 Bankr. 774, 783 (Bankr. D. Me. 1987); *In re T.P. Long Chem., Inc.*, 45 Bankr. 278, 286, 289 (pre-*Midlantic Nat'l Bank* decision barring estate from escaping liability by abandoning drums of waste).

¹⁷⁷ *Stevens*, 68 Bankr. at 776.

¹⁷⁸ *Id.*

¹⁷⁹ *Id.* at 776. Absent indications from the court in *Midlantic Nat'l Bank*, state law determines what constitutes conditions which adequately protect the public's health and safety. *See*

sought reversal of the Bankruptcy court decision that did not allow recovery of this amount as an administrative expense.¹⁸⁰

In allowing recovery and rejecting the trustee's attempt to abandon the property, the *Stevens* court supported the public policy of protecting health and safety:

Midlantic leaves no room for the estate to avoid the administrative expense attendant upon its possession of hazardous waste, except upon the acquiescence of the public authorities whose ultimate legal obligation it is to protect the public health and safety from hazardous waste abandoned by those responsible for its existence.¹⁸¹

The Court continued that: “[u]nless *Midlantic* is to be disregarded the trustee may not be permitted simply to walk away from hazardous wastes in circumstances where the bankruptcy court itself would be powerless to authorize their abandonment.”¹⁸²

By not removing the waste the trustee became liable under Maine law for its cleanup.¹⁸³ The deference of the *In re Stevens* court to state law contrasts with the *Franklin* court's willingness to set judicial standards for the cleanup of toxic waste.¹⁸⁴ The conflict in applying judicial authority illustrates the different approaches to public policy. By deferring to state law, supposedly under the authority of *Midlantic*, the *In re Stevens* court avoided the public policy issue of determining public safety standards under the Code. By setting a judicial standard for public policy, the *Franklin* court reconciled federal and state law. This reconciliation, however, is at the expense of dictating state public policy, which is normally a state legislative function.

A flexible approach to the administrative claim issue was used in *In re Peerless*.¹⁸⁵ There, the Bankruptcy Court allowed administrative claim status for a clean-up order issued under CERCLA.¹⁸⁶

id. at 782 n.7. In this case the conditions were not met. *Id.* (which set of conditions is a “quintessential legislative determination”).

¹⁸⁰ *See id.* at 777.

¹⁸¹ *Id.* at 781. The *Stevens* court realized that curbing the power of the bankruptcy court involved balancing public health and safety with the “more parochial concerns of efficient bankruptcy administration.” *Id.* The Maine court subscribed to the premise that actual and necessary expenses include those expenses incurred to comply with state laws. *See id.* at 782 n.7.

¹⁸² *Id.* at 782.

¹⁸³ *Id.*

¹⁸⁴ *See id.*

¹⁸⁵ *In re Peerless Plating Co.*, 70 Bankr. 943 (Bankr. W.D. Mich. 1987).

¹⁸⁶ *Id.* at 948-49.

Although the trustee argued that the violation arose pre-petition, the court found that the bankrupt estate was an owner and therefore liable under CERCLA.¹⁸⁷ In a footnote the court recognized the tension between the Code and the *Midlantic* decision.¹⁸⁸

The most significant aspect of *In re Peerless* is the court's effort to enforce the CERCLA order. There was no indication that the waste posed any imminent harm.¹⁸⁹ Further, the trustee argued for equitable subordination of EPA's claim because of alleged bad faith.¹⁹⁰ In direct defiance of a court order, the EPA had entered the property to clean up the waste.¹⁹¹ The EPA petitioned the court for administrative expense priority long after the cleanup was complete.¹⁹² The court concluded that a lack of bankruptcy expertise rather than malice prompted the EPA's erroneous actions.¹⁹³ Based on the record as a whole, the court granted administrative expense status.¹⁹⁴

The ability of the court in *In re Peerless* to weigh the evidence and measure the credibility of witnesses validated the proceeding. Allowing an adjudication of the administrative claim expense issue permits a balanced approach to the individual bankruptcy. In this case a superlien statute would automatically allow recovery for the EPA without an appraisal of possible bad faith or malicious prosecution or whether in fact the waste posed imminent harm to the area.

What constitutes imminent harm thus remains open to judicial determination, as does the fourth prong of the administrative claim test—the necessity that the claim be post-petition.¹⁹⁵ Some courts have strictly adhered to the post-petition requirement. Various courts, however, circumvent the post-petition claim requirement, invoking public policy concerns to overcome statutory construction.

*Southern Railway Co. v. Johnson Bronze Co.*¹⁹⁶ supports the proposition that a bankruptcy court has no authority to elevate a pre-

¹⁸⁷ *Id.* at 948.

¹⁸⁸ *Id.* at 947 n.1.

¹⁸⁹ *See id.* at 947. In fact an inspector had dipped his hands into the drums of chemicals without harm. *Id.*

¹⁹⁰ *Id.* at 948.

¹⁹¹ *Id.*

¹⁹² *Id.*

¹⁹³ *Id.*

¹⁹⁴ *See id.* at 947.

¹⁹⁵ *See supra* notes 68–79 and accompanying text describing policy of allowing post-petition debts priority status as well as the theory that pre-petition claims should not be allowed because creditors usually bear the risk of dealing with the corporation of their choice.

¹⁹⁶ 758 F.2d 137 (3d Cir. 1985).

petition unsecured claim to an administrative priority.¹⁹⁷ There, Southern Railway brought an action seeking to hold the debtor in possession liable for the cleanup of hazardous waste that the debtor had deposited into a drainage ditch.¹⁹⁸ The debtor's successor in title cross-claimed for the cost of removing the sludge, and filed a claim for administrative priority to collect the money it expended in cleaning up the site.¹⁹⁹ Relying on *Kovacs*, the *Southern Railway* court found that both claims were general and unsecured.²⁰⁰ The administrative order issued by the South Carolina Department of Health and Environment to clean up the waste could not elevate the clean-up order to priority status²⁰¹ because the clean-up order itself was general and unsecured pursuant to *Kovacs*.²⁰²

The *Southern Railway* court reasoned that the claim was prepetition because the parties knew of the waste disposal and because the Johnson license to operate was founded on the notion that "Johnson maintain the ditch, restore it to its original condition, and indemnify Southern for any liability arising from its use."²⁰³ Because *Kovacs* did not decide the legal consequences of a debtor entering into bankruptcy prior to receivership, that case could not be viewed as determinative of priority status.²⁰⁴

Similarly, in *In re Dant & Russel, Inc.*,²⁰⁵ the court disallowed administrative priority to costs for hazardous waste cleanup incurred before a petition for bankruptcy.²⁰⁶ The district court, affirming the decision, also stated that environmental authorities identified the toxic waste problem post-petition, and the lessor in possession in-

¹⁹⁷ *Id.* at 142.

¹⁹⁸ *Id.* at 138. The court assumed that the private party liable for clean up costs enjoyed the same rights against the debtor as did the state. *See id.* at 141; *see also In re Stevens*, 68 Bankr. 774, 780 n.5 (Bankr. D. Me. 1987); *In re Pierce Coal and Constr. Inc.*, 65 Bankr. 521, 525 (Bankr. N.D. W. Va. 1986).

¹⁹⁹ 758 F.2d at 138.

²⁰⁰ *Id.* at 141.

²⁰¹ *See id.*

²⁰² *Id.*

²⁰³ *Id.* at 139.

²⁰⁴ *See also In re Wall Tube & Metal Prod. Co.*, 56 Bankr. 918, 927 (Bankr. E.D. Tenn. 1986) (allowing administrative expense for clean up of drums containing hazardous waste is "judicially legislating . . . by stretching § 503(b) beyond its scope"). There is the "potential for unwittingly creating an incentive for governmental authorities to postpone environmental clean up activities for financially strategic reasons in order to gain the advantage of priority treatment in a bankruptcy context. In addition, there is a danger of dissipating and depleting those funds which under the current statutory design are essential for an effective administration of the estate." *Id.*

²⁰⁵ 61 Bankr. 668 (Bankr. D. Or. 1985), *aff'd*, 67 Bankr. 360, 365 (D. Or. 1986).

²⁰⁶ 61 Bankr. at 670-71.

curred the costs to mitigate the hazards under the agreement with the EPA post-petition as well.²⁰⁷ Although the court found that the debtor's liability for damages arose before Chapter 11, the post-petition identification did not trigger an administrative priority for cleanup.²⁰⁸ The court also distinguished *Midlantic*, but seemed to rest its conclusion on the fact that the contamination occurred pre-petition.²⁰⁹

Following the line of cases disallowing pre-petition claims, the court in *In re Pierce Coal and Construction Inc.*,²¹⁰ considered the priority status of the costs of reclaiming land disturbed by strip mining.²¹¹ The debtor mining company operated for a year after its Chapter 11 petition was filed before converting to a liquidation proceeding under Chapter 7.²¹² After the debtor filed the Chapter 7 petition, the company continued to operate for an additional thirty days.²¹³ The bankruptcy court concluded that the priority of the reclamation costs would turn on the timing of the operations, whether before or after the debtor filed a petition for bankruptcy.²¹⁴ The court determined that the costs incurred after the filing were entitled to administrative priority under section 503(b)(1)(A)'s "actual and necessary costs and expenses of preserving the estate"²¹⁵ The court concluded that with one exception, pre-petition costs could not be accorded administrative expense priority. Agreeing with *Southern Railway*, the court expressed concern that it lacked authority to elevate pre-petition claims to administrative priority status.²¹⁶

The court did, however, recognize *Midlantic's* imminent and identifiable harm exception to the general rule:

The United States Supreme Court has indicated in its decision that when imminent and identifiable harm is present, the priorities of the Bankruptcy Code may be subservient to the environ-

²⁰⁷ *Dant*, 67 Bankr. at 362.

²⁰⁸ *See id.* at 364.

²⁰⁹ *Id.* This decision conflicts with *Stevens* and *Pierce Coal* in that those decisions allowed administrative priority when the damage was done pre-petition. *See supra* notes 177-85 and accompanying text; *see also infra* notes 211-19 and accompanying text.

²¹⁰ 65 Bankr. 521 (Bankr. N.D. W. Va. 1986).

²¹¹ *Id.* at 525.

²¹² *See id.* at 522, 523.

²¹³ *Id.* at 523.

²¹⁴ *See id.* at 531.

²¹⁵ *Id.* at 530 ("The Bankruptcy Code clearly provides that expenses occasioned by the debtor in possession while operating as a debtor in possession are 'actual and necessary'").

²¹⁶ *Id.* at 531.

mental laws designed to protect the public safety. It is reasonable to expect that under a given set of circumstances, the necessary costs of protecting the public health or safety from imminent and identifiable harm may be elevated to administrative priority and perhaps, even to a type of secured priority.²¹⁷

A literal reading of the Code's language supports the *Southern Railway, In re Dant*, and *In re Pierce Coal* courts' strict construction of the post-petition test.²¹⁸

In contrast to these cases, the District Court of Maine decided that the post-petition cleanup of a pre-petition environmental hazard constituted a first priority administrative expense.²¹⁹ The court agreed with the *Pierce Coal* court that *Midlantic* had altered the criteria for determining the allowance of administrative expenses under section 503(b)(1)(A).²²⁰ When imminent and identifiable harm is present the mandate of the Code "may be subservient to state laws designed to protect public safety."²²¹ The court found such a danger and therefore the clean-up costs incurred in removing the twenty-nine barrels of PCB-contaminated oil were deemed to be an administrative expense.²²²

In *In re Distrigas*,²²³ the Massachusetts bankruptcy court addressed the issue of whether the State of New Jersey was an impaired class and accordingly entitled to a confirmation vote of any reorganization plan.²²⁴ New Jersey wanted to be classified as an impaired class because at least one entity within such a class must approve any reorganization plan.²²⁵ The court held that the state was not an impaired class because New Jersey had taken no formal action to clean up Distrigas' toxic waste.²²⁶ New Jersey was, how-

²¹⁷ *Id.* (the court did not find such a situation in this case).

²¹⁸ See 11 U.S.C. § 503(b)(1)(A) ("the actual, necessary costs and expenses of preserving the estate, including wages, salaries, or commissions for services rendered after the commencement of the case").

²¹⁹ *In re Stevens*, 68 Bankr. 774, 780 (Bankr. D. Me. 1987).

²²⁰ *Id.*

²²¹ *Id.* (quoting *In re Pierce Coal & Constr., Inc.*, 65 Bankr. 521, 531 (Bankr. N.D. W. Va. 1986)).

²²² *Id.* at 775, 783-84.

²²³ *In re Distrigas*, 66 Bankr. 382 (Bankr. D. Mass. 1986).

²²⁴ See *id.*

²²⁵ See *id.*; 11 U.S.C. § 1129(a)(10) (1982 & Supp. III 1985) states: "(a) The court shall confirm a plan only if all of the following requirements [*inter alia*] are met:

(10) If a class of claims is impaired under the plan, at least one class of claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any insider."

²²⁶ *Distrigas*, 66 Bankr. at 385, 386. New Jersey did send a letter in an attempt to enforce its clean-up powers. *Id.* at 385.

ever, entitled to an administrative expense under *Midlantic*.²²⁷ As in *In re Dant*, the toxic waste problem occurred before filing under Chapter 11.²²⁸ Unlike the *Dant* court, however, the *Distrigas* court advised New Jersey that under *Midlantic* it could obtain a first priority expense.²²⁹ In *In re Dant*, the court disallowed administrative expense priority, but in *Distrigas* the court allowed the administrative expense despite the fact that the conditions arose pre-petition. Distinguishing the facts of the cases does not explain the divergent views of these courts. Both the *Distrigas* and the *In re Dant* courts purport to follow the post-petition rule. The divergent results, moreover, indicate the diverse interpretations of the rule.

*In re Hemingway Transport*²³⁰ adds another twist to determining the priority of pre-petition liability for hazardous waste cleanup. After reviewing the pertinent cases, the Massachusetts bankruptcy court chose not to follow any of the holdings.²³¹ In *Hemingway*, the debtor sold contaminated property of Juniper Development Group for which the Massachusetts Department of Environmental Quality Engineering ("DEQE") had issued a clean-up order.²³² Subsequently, the EPA discovered the waste and ordered its cleanup.²³³ Juniper filed an action seeking contribution from the trustee on the grounds that the trustee is liable under CERCLA.²³⁴

After the court discussed the relevant cases, it determined that neither *Kovacs* nor *Midlantic* controlled.²³⁵ Rather, relying on *Reading Co. v. Brown*,²³⁶ the *Hemingway* court concluded that Juniper's claim rose to the level of an administrative expense, on a theory of "fairness to all persons having claims against an insolvent."²³⁷ Complying with section 64(a), the forerunner of sections 503 and 507,²³⁸ the Supreme Court in *Brown* decided that when the receiver acted negligently within the scope of its authority such negligence gave

²²⁷ *Id.* at 386.

²²⁸ *See id.* at 385.

²²⁹ *Id.* at 386.

²³⁰ 73 Bankr. 494 (Bankr. D. Mass. 1987).

²³¹ *Id.* at 504.

²³² *Id.* at 496 (the property was contaminated with 12 barrels of hazardous waste).

²³³ *Id.*

²³⁴ *Id.*

²³⁵ *Id.* at 504.

²³⁶ 391 U.S. 471 (1968).

²³⁷ *Hemingway*, 73 Bankr. at 504 (quoting *Reading Co. v. Brown*, 391 U.S. 471, 477 (1968)). In *Brown* the Court allowed administrative expense status to a claimant whose property was damaged as a result of a fire negligently started on an adjoining parcel involved in a bankruptcy proceeding. 391 U.S. at 484.

²³⁸ *See* Pearlstein, *supra* note 43, at 633.

rise to actual and necessary costs of operating the debtor's business.²³⁹ The Court noted the policy arguments against allowing an administrative claim: "1) that first priority status for negligence claims would not encourage third parties to deal with the insolvent business; 2) such status would reduce the amount of funds for unsecured creditors; and 3) such status would discourage general creditors from accepting arrangements."²⁴⁰ Discussing the Supreme Court's observations, the *Hemingway* court concluded that since "the victims of receiver's negligence did not merely suffer injury but had an insolvent business thrust upon them by operation of law . . .,"²⁴¹ it would offend notions of fairness to exclude tort creditors from an estate's assets.²⁴²

The *Hemingway* court found the facts in *Brown* more analagous to its own facts, and concluded that "if damages leading to a negligence claim against a receiver qualify as administrative expenses then so do damages giving rise to a strict liability claim against a Chapter 11 debtor-in-possession under CERCLA."²⁴³ The court in *Hemingway*, therefore, skirted the issue of allowing an administrative expense merely for the cleanup of environmental hazards by raising CERCLA violations to the level of a tort claim. Courts have recognized tort claims as proper administrative expenses since *Brown*.²⁴⁴

As courts struggle to resolve the post-petition problem, two lines of cases emerge—those which adhere unfliningly to the rule and those which defer to policy considerations to circumvent the rule. *Southern Railway* and *In re Dant & Russell* support the proposition that pre-petition environmental claims are general and unsecured. Other courts, notably the *In re Stevens* and *Distrigas* courts, recognize that in many instances environmental hazards are created pre-petition, but in light of *Midlantic* they hold that policy considerations outweigh the mandates of the Code. Allowing courts to balance competing policies will not necessarily create neat precedent. In the tradition of equity courts, however, such a balancing promotes

²³⁹ 391 U.S. at 485.

²⁴⁰ See also *In re Hemingway Transport*, 73 Bankr. at 504 (citing *Reading Co. v. Brown*, 391 U.S. 471, 477 (1968)).

²⁴¹ *Id.* at 504.

²⁴² *Id.*

²⁴³ *Id.* at 505.

²⁴⁴ See Note, *supra* note 38, at 152; cf. *In re Chicago, Rock Island & Pacific R.R.*, 756 F.2d 517, 518-19 (7th Cir. 1985) (removal of old railroad tracks of bankrupt estate might be necessary to avert imminent danger; such a transaction would benefit the creditors by protecting the bankrupt estate against tort liability for crossing accidents).

what the Supreme Court in *Brown* terms "fairness to all persons having claims against an insolvent."²⁴⁵

No clear precedents emerge from a survey of the recent law concerning the administrative claim provision in section 503(b)(1)(A). Courts use various approaches depending on their readings of *Ohio v. Kovacs* and *Midlantic National Bank* as well as their interpretations of the post-petition and no benefit/no burden rules. What does emerge is a picture of a fact specific line of decisions. Circumstances dictate which policy considerations should prevail. As the cases reveal, the adjudication of administrative claim status exposes specific concerns that a rule of law or blind application of fact-specific precedent might otherwise conceal.²⁴⁶

V. THE MERITS OF APPLYING SECTION 503(b)(1)(A) ADMINISTRATIVE CLAIMS ANALYSIS TO STATE CLEAN-UP ORDERS IN BANKRUPTCY PROCEEDINGS

A. *Balancing the Competing Policies*

The resolution of an administrative claim petition involving environmental cleanup will depend on the court's interpretation of the Code. Implicit in this determination is a balancing of the Code's policy, the orderly disbursement of funds, with the policy of cleaning up hazardous waste sites.²⁴⁷

Enforcing environmental clean-up orders can thwart the Code's policy in several ways. First, by giving pre-filing clean-up orders preferred status, the enforcement interferes with the statutorily prescribed scheme of creditor priorities.²⁴⁸ Normally a state seeking to enforce environmental clean-up orders assumes the status of a general, unsecured creditor.²⁴⁹ A state may, however, elevate the claim to the status of a statutory lien.²⁵⁰ Without a state statutory lien provision, the government as an unsecured creditor will proba-

²⁴⁵ See *supra* notes 145-59 and accompanying text. Although the *Brown* Court referred to tort claimants, the basic concept is easily extrapolated to include the predicament of creditors subordinated by environmental claims.

²⁴⁶ *Id.*

²⁴⁷ See generally Note, *The Bankruptcy Code and Hazardous Waste Cleanup: An Examination of the Policy Conflict*, 27 WM. & MARY L. REV. 165, 209-10 (1985).

²⁴⁸ See *infra* notes 281-98 and accompanying text.

²⁴⁹ See *supra* note 247 and accompanying text.

²⁵⁰ See *In re Security Gas & Oil*, 15 Bankr. Ct. Dec. (CRR) 762, 768 (Bankr. N.D. Cal. 1987).

bly only receive a percentage of its interest.²⁵¹ Although this scheme satisfies the priority list of the Code, it restricts the power of states and agencies to enforce clean-up orders.²⁵² Elevating the claim to secured status, however, distorts "the Congressionally created priority scheme and harms other secured creditors."²⁵³ A question remains whether allowing administrative expense priority for clean-up orders resolves these two extreme positions of a state seeking to enforce a clean-up order in bankruptcy proceedings.²⁵⁴

A second way in which elevating a clean-up order to preferred status interferes with the precepts of the Code is by limiting the "breathing space" necessary for a debtor to reorganize.²⁵⁵ If a company must liquidate because of a destructive race caused by lack of "breathing space," the goals of the Code are frustrated. Liquidation under these circumstances would defeat the purpose of the Code in allowing a preservation of assets until the trustee can conduct an orderly liquidation.²⁵⁶ Allowing an apparently non-statutory claim preferred status may initiate a "destructive race" that destroys the going concern value of the business.²⁵⁷

Balanced against the policies and provisions of the Code is the state's interest in protecting the health and safety of its citizens from improper storage of hazardous waste.²⁵⁸ When the state discovers improper storage of hazardous waste in the context of a bankruptcy proceeding, the court must consider the immediacy, severity, and certainty of danger to the public.²⁵⁹ This is the teaching of *Midlantic National Bank*.²⁶⁰ When the hazardous waste poses an imminent

²⁵¹ See *id.* at 769; see generally Note, *supra* note 247.

²⁵² See Note, *supra* note 247, at 208-09.

²⁵³ *Security Gas & Oil*, 15 Bankr. Ct. Dec. (CRR) at 768.

²⁵⁴ *Id.*

²⁵⁵ *Id.*

²⁵⁶ *Id.*

²⁵⁷ *Id.*; see also Jackson, *Of Liquidation, Continuation, and Delay: An Analysis of Bankruptcy Policy and Nonbankruptcy Rules*, 60 AM. BANKR. L.J. 399, 401-02 (1986). The theory behind "going concern value" is that the business as a whole is worth more than its separate parts. If the creditors are not involved in a race to maximize individual returns they will act collectively to increase the total pool of assets. Absent outside forces, however, the participants may be involved in a Prisoner's Dilemma which makes cooperation the irrational option. For a description of a Prisoner's Dilemma in the environmental area, Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors Bargain*, 91 YALE L.J. 857, 861-65 (1982).

²⁵⁸ S. EPSTEIN, L. BROWN, & C. POPE, *HAZARDOUS WASTE IN AMERICA* (1984).

²⁵⁹ See *In re Security Gas & Oil, Inc.*, 15 Bankr. Ct. Dec. (CRR) 762, 769 (Bankr. N.D. Cal. 1987).

²⁶⁰ See *Midlantic Nat'l Bank v. NJDEP*, 106 S. Ct. 755, *reh'g denied*, 106 S. Ct. 1482 (1986).

threat to the environment, the trustee cannot abandon the estate.²⁶¹ If the storage of the waste violates state law then its cleanup becomes "actual and necessary" and thus allowable as an administrative claim under 503(b)(1)(A).²⁶²

In addition to prevention of imminent harm, the enforcement of a clean-up order is also consistent with the state's exercise of police power.²⁶³ When state and federal laws conflict, the federal law controls.²⁶⁴ States, however, enact laws pursuant to police powers granted to them by the Constitution while Congress enacts laws pursuant to powers not granted to the states.²⁶⁵ Facially there is no conflict and courts are not willing to imply one.²⁶⁶ Therefore, the enforcement of environmental laws in spite of the Code may not raise preemption problems.²⁶⁷ When conflicts do arise a judicial proceeding can best resolve them.²⁶⁸

Enforcing a clean-up order is also the best way to prevent fraud by the estate.²⁶⁹ Such enforcement will prevent filing for bankruptcy to avoid a clean-up order.²⁷⁰ An administrative claim can foreclose the possibility of fraud.²⁷¹

A review of the policy considerations indicates that a judicial hearing can best resolve any conflicts. The administrative claim can

²⁶¹ *Id.* at 762.

²⁶² 11 U.S.C. § 503(b)(1)(A) (1982 & Supp. IV 1986).

²⁶³ U.S. CONST. amend X.

²⁶⁴ See Note, *supra* note 247, at 204.

²⁶⁵ *Id.*

²⁶⁶ *Id.* (citing *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142 (1963)) ("when statutory schemes as a whole do not conflict, a conflict is not to be construed between particular provisions because preemption is disfavored unless that conclusion is unmistakable").

²⁶⁷ 11 U.S.C. § 725 (1982 & Supp. IV 1986). In fact Bankruptcy law incorporates some state lien provisions.

²⁶⁸ Far from resolving preemption issues state superlien statutes raise legitimate preemption problems. While the Code defers to state law on standards for environmental safety, the vast array of possible superlien statutes has the potential of upsetting federally mandated priorities. States are in effect engrafting onto the Code as many exceptions as there are states enacting such statutes. Such a potpourri of laws interferes with the orderly distribution of the estate. The problem is most acute when a national company is bankrupt. If the statute provides, the state in which the environmental violation occurs would be able to reach assets outside of the state. Knowing this creditors would be more inclined to a destructive race thereby further depleting the estate. The near collapse of Texaco invites speculation about the possible ramifications of state superlien statutes on creditor priority.

²⁶⁹ See Note, *supra* note 247, at 206.

²⁷⁰ *Id.* at 205-06.

²⁷¹ See *id.* Any law prioritizing environmental cleanup can prevent fraud by foreclosing the option of bankruptcy to avoid cleanup. In this case a "superlien" statute would have a similar effect.

be used either to enforce a clean-up order or to relegate the order to a lesser, yet potentially collectible, status. At least one court has articulated an appropriate balancing test.

The court in *In re Security Gas & Oil, Inc.*²⁷² suggested an appropriate test to resolve these difficulties. The court suggested balancing the state's interests against the policies of the Code "in determining whether to enjoin an environmental clean up order under section 105."²⁷³ After holding that the automatic stay provision did not protect Security Gas & Oil, the court reviewed the company's petition for an affirmative injunction against the environmental clean-up order.²⁷⁴ Under section 105 the Bankruptcy court may issue an injunction against any action which would interfere with the proper functioning of the Code.²⁷⁵ Such interference could result from enforcing a clean-up order.

The *Security Gas & Oil* court suggested certain factors to consider when balancing these competing policies. The factors include the ability of the debtor to effect a cleanup, the immediacy of the harm, and the effect of enforcement on reorganization.²⁷⁶ These factors can be applied when the court determines a petition for administrative claim status.

Whether other courts will look to the equitable factors considered by the *Security Gas & Oil* court remains to be seen. Some courts

²⁷² 15 Bankr. Ct. Dec. 762 (Bankr. N.D. Cal. 1986).

²⁷³ See *In re Security Gas & Oil*, 15 Bankr. Ct. Dec. (CRR) 762, 769 (Bankr. N.D. Cal. 1987). The court listed 9 factors to consider:

- 1) The immediacy, severity, and certainty of the danger created by the environmental hazard subject to the clean-up order;
- 2) The extent to which debtor is uniquely able to effect the cleanup;
- 3) The extent to which creditor priorities would be distorted by enforcement of the clean-up order;
- 4) The effect of the enforcement order on the likelihood of a successful reorganization, and whether a successful reorganization will substantially increase the payoff to creditors and/or preserve jobs;
- 5) How long the bankruptcy case has been open;
- 6) How long the State delayed in attempting to force debtor to clean up the environmental hazard;
- 7) The extent to which debtor continues to operate a similar business in the State;
- 8) the extent to which orders other than full prohibition of enforcement of clean-up orders can better accommodate the State health and welfare concerns with the policies of the Bankruptcy Code; and
- 9) Any other consideration relevant to whether injunctive relief should be granted, including the good or bad faith of the parties.

Id.

²⁷⁴ See *id.*

²⁷⁵ 11 U.S.C. § 105 (1982 & Supp. IV 1986).

²⁷⁶ See *Security Gas & Oil*, 15 Bankr. Ct. Dec. at 769.

make policy decisions when electing to enforce a clean-up order.²⁷⁷ Some of the factors of *Security Gas & Oil* will likely play a role in that decision. For example, any court reviewing an administrative claim petition must look at *Midlantic's* imminent harm standard. Nonetheless, courts make the decision and frequently they rely on statutory language not designed to cover the present situation.²⁷⁸ When combined with the restrictions of *Kovacs*, the post-petition rule, the benefit/burden rule, and the imminent danger standard, the administrative claim provision provides the statutory basis for preempting Code priority status.²⁷⁹

B. Section 503(b)(1)(A) Provides for Fair Adjudication on the Merits

Ohio v. Kovacs and *Midlantic National Bank* give courts the authority to either enforce an environmental clean-up order by prioritizing the claim under section 503(b)(1)(A) of the Code or to subrogate the order to the position of a general, unsecured creditor.²⁸⁰ Given the financial disposition of a bankrupt estate, the position a court takes will determine who bears the burden of the cleanup.²⁸¹ Through a myriad of fact situations the argument usually comes down to a conflict between competing policies: the Code's purpose in providing a fresh start and the public health and safety issues compelling the cleanup of hazardous waste.

One commentator has listed the factors that will give rise to an administrative priority:

- 1) Was the claim post-petition?
- 2) Was the claim actual and necessary to rehabilitate the debtor, preserve the estate, or liquidate the estate?
- 3) Did the expense benefit the estate?
- 4) Did the estate incur the expense or did a third party volunteer assert the claim?²⁸²

The issue of toxic waste cleanup subjects these considerations to many inconsistent interpretations. As the courts struggle to factor the importance of states' clean-up policies into their determination,

²⁷⁷ See *In re Stevens*, 68 Bankr. 774, 782 (Bankr. D. Me. 1987).

²⁷⁸ See *id.* at 780.

²⁷⁹ *Id.*

²⁸⁰ See *Ohio v. Kovacs*, 469 U.S. 274 (1985); *Midlantic Nat'l Bank v. NJDEP*, 106 S. Ct. 755, *reh'g denied*, 106 S. Ct. 1482 (1986).

²⁸¹ For example, in *In re Peerless*, if the court held for the debtor, the money expended by the EPA would not have been reimbursed. 70 Bankr. 943 (Bankr. W.D. Mich. 1987).

²⁸² See Note, *supra* note 38, at 153-54.

words like "criminal" and "fairness" appear in the opinions and commentary.²⁸³ Whether all polluters are criminal and should be treated accordingly appears to contradict the Bankruptcy Code's policy of fairness to all creditors.²⁸⁴ Justice Powell stated that whether the public will be adequately protected should be the proper measure of whether a court should allow an administrative priority.²⁸⁵ This view represents a rational deviation from the Code's strict priority list. Subjecting a community to 470,000 gallons of carcinogenic and toxic substances should not be permitted through lowering the state's claim to that of a general unsecured creditor.²⁸⁶ As a general creditor the state would be unable to recoup funds for its cleanup. If the state could not clean up the site immediately, the safety systems, including sprinkler systems and guard patrols, would be terminated.²⁸⁷ Without these precautions, the likelihood of a dangerous spill would increase dramatically.²⁸⁸

By use of the imminent and identifiable danger concept, Powell invited varied interpretations. One court has taken the language to its extreme. In Maine a court concluded that twenty-nine barrels of contaminated oil secured in a tractor trailer posed imminent danger to the community.²⁸⁹ Absent explicit evidence of such danger the contention seems strained, especially since the barrels were sealed, contained, and in a roped-off area designated by warning signs.

To resolve the competing priorities some states have adopted superlien statutes to allow secured liens for hazardous waste cleanup.²⁹⁰ These statutes raise issues of fairness and notice to other creditors.²⁹¹ Where superlien provisions exist the state has made a rational legislative decision, thus mooting the discussion of administrative claim priority.²⁹²

²⁸³ See Note, *supra* note 143, at 397; *Reading Co. v. Brown*, 391 U.S. 471 (1968).

²⁸⁴ See Note, *supra* note 143, at 437.

²⁸⁵ *Midlantic Nat'l Bank v. NJDEP*, 106 S. Ct. 755, 762, *reh'g denied*, 106 S. Ct. 1482 (1986).

²⁸⁶ *Id.* at 758 n.3.

²⁸⁷ *Id.* at 758.

²⁸⁸ *Id.*

²⁸⁹ *In re Stevens*, 68 Bankr. 774, 783 (Bankr. D. Me. 1987).

²⁹⁰ See, e.g., 58 N.J. STAT. ANN. § 10-23.11f(f) (West 1982 & Supp. 1988).

²⁹¹ Lockett, *Caveat Creditor, Environmental Liability Enforcement and the Bankruptcy Act of 1978: A study of H.R. 2767, the "Superlien" provision*, 19 REAL PROP. PROB. & TR. J. 859 (1984) (describing how a member of Congress unsuccessfully sought to impose a similar lien status on CERCLA claims).

²⁹² See Jackson, *supra* note 259, at 405-06. In the process the state may be discouraging third party participation with the estate. The spectre of an environmental claim discourages third party participation. Rational merchants, even trustees, might hesitate to deal with a bankrupt estate knowing that they will receive no payment.

As long as parties turn to section 503(b)(1)(A) of the Code, however, the courts are able to resolve the fairness issue. Some courts use a reasoned balance test similar to that which a legislature might employ when adopting legislation.²⁹³ Other courts use the applicable precedent blindly to resolve the policy considerations.²⁹⁴ The bottom line is that toxic waste cleanup is not prioritized in the Code under section 507. As a result, courts are creating an exception based on a policy consideration. With continuing judicial resolution, a body of law is developing that accepts environmental soundness as a priority, but that also supports notions of fairness to creditors. Unless drafted to incorporate a balancing of competing interests, superlien statutes fail to address a variety of issues which arise in bankruptcy proceedings.²⁹⁵ The proper use of a balancing test in toxic waste cleanup cases should resolve the competing interests equitably because such a test can balance the competing policies of the Code's "fresh start" approach and the states' interest in cleaning up hazardous waste.

By creating superlien statutes, states, to the detriment of the Code, are avoiding such a reasoned analysis. Use of the administrative expense priority instead of superlien statutes allows an *ad hoc* adjudication of the issues. Not only is a priority fair to the parties involved, but it also preserves, to the extent possible, the priorities of the Code.

Superlien statutes answer the clean-up problem broadly.²⁹⁶ A state's legislative effort engrafts a new priority on the federal Code.²⁹⁷ The superlien solution appears to eliminate needless litigation and expense. The price, of course, is fairness to all creditors. If the bankruptcy proceeding is already in court, letting the process work to its fruition is a small concession to afford all parties concerned an equitable resolution. Indeed, environmental claims are not barred from the process; a survey of the case law indicates their success.²⁹⁸

A revision of the Code itself would encounter difficulties that would render such an effort frustrating. Prioritizing environmental

²⁹³ See *supra* notes 273-80 and accompanying text.

²⁹⁴ See *supra* notes 185-94 and accompanying text.

²⁹⁵ As a piece of legislation designed to cover all situations, superlien statutes cannot adequately address unique factual circumstances.

²⁹⁶ See generally MASS. GEN. L. ch. 21E, §§ 1-13; N.H. REV. STAT. ANN. § 147-B:10 (Supp. 1988).

²⁹⁷ See *supra* notes 264-69 and accompanying text.

²⁹⁸ See *supra* notes 146-59 and accompanying text.

claims would involve a struggle at the political level. Even if a compromise could be reached the result might be either vague or overly specific, inviting litigation to resolve the issues. Once Congress establishes a laundry list, bankruptcy courts may tend to pigeonhole claims that have irregular fact patterns or that raise unusual points of law. The overall picture of Code revision on this point is one of a prolonged struggle to enact legislation and an even longer period of judicial interpretation. Absent such an effort to determine a new direction for the Code in the toxic waste area, the use of the administrative priority can be an effective method to liquidate an estate in a manner consistent with the legal rights of all the creditors.

VI. CONCLUSION

This Comment examines the history of the administrative claim in the Bankruptcy Code. What appears is a picture of broadening exceptions given priority under section 503(b)(1)(A). Throughout the broadening process courts have had difficulty articulating a statutory basis for allowing administrative claims, and have ultimately relied on policy considerations. Nowhere is this more evident than in the area of toxic waste clean-up orders. Although courts look to the "actual and necessary" language of the Code, they must go beyond its plain meaning to adapt the language to the hazardous waste area. The Supreme Court opinion in *Midlantic* recognizes that the Code neglects toxic waste cleanup, but finds a strong policy in favor of allowing the claim to protect the environment. Before state legislatures usurp the field by implementing superlien statutes that use the Code to prioritize what are deemed to be important claims, courts should take steps to broaden the use of the administrative priority in toxic waste cleanup. Use of the administrative claim allows a fair adjudication on the merits of individual cases. Adjudication legitimizes an otherwise haphazard approval of toxic waste cleanup undertaken by the states. The administrative claim is one tool to implement a broader policy consistent with both the Code and the states' interest in promoting public health and safety.