

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF:)
)
MICHAEL & MAUREENA STRONG,)
)
Debtor(s).) CASE NO. BK00-81356
STATE OF NEBRASKA ex rel.) A00-8058
MICHAEL LINDER, DIRECTOR of the)
NEBRASKA DEPARTMENT OF)
ENVIRONMENTAL QUALITY,)
)
Plaintiff,) CH. 7
)
vs.)
)
MICHAEL K. STRONG,)
)
Defendant.)

MEMORANDUM

Hearing was held in Omaha, Nebraska, on August 15, 2002, on the Plaintiff's Motion for Order of Non-Dischargeability (Fil. #38) and Resistance by the debtors (Fil. #41). John Turco appeared for the debtor, William Howland appeared for the State of Nebraska, and Lisa Buechler appeared for Nebraska Department of Environmental Quality. This memorandum contains findings of fact and conclusions of law required by Fed. R. Bankr. P. 7052 and Fed. R. Civ. P. 52. This is a core proceeding as defined by 28 U.S.C. § 157(b)(2)(I).

This motion is essentially one for summary judgment. The debtor¹ owns and formerly operated a tire recycling facility near

¹There is some dispute between the parties concerning the entity operating the business. The debtor contends that he operated the business as a sole proprietorship until October 1996, and the corporate entity of Strong Tire Company operated the business thereafter. The State contends that it dealt only with Michael Strong individually and not as a representative of a corporation.

For purposes of this motion, which is directed only at legal issues, I need not determine the factual issue of the business form in which the company was operated, and any reference herein

(continued...)

Wakefield, Nebraska. The company appears to have become ensnared in the complex web of environmental regulations; the regulatory requirements, combined with the lack of a buyer or end-user for the recycled material, sent the business into an economic vortex from which it has been unable to escape. The State, by way of the Department of Environmental Quality ("NDEQ"), seeks to force the debtor to clean up the site, and has moved for an order declaring any fines, penalties, forfeitures, and/or injunctive relief imposed against the debtor to be non-dischargeable in bankruptcy. The State also wants to proceed in state court with efforts to enforce previous court orders requiring the debtor to remove and properly dispose of all tires and tire products and cease all scrap-tire operations at the facility. The debtor believes that the State is responsible in large part for the failure of the business by refusing to approve his proposals for selling the tires or the recycled product, and contends that the State should be permanently restrained, by way of his discharge, from taking any further action against him to force the clean-up of the site or to recover any costs of cleaning up the site.

Background

The debtor began the business in 1993, apparently without State approval. He collected used tires from retailers in three states. He shredded some of the tires, but has been unable to find a viable market for the processed or recycled material. As a result, whole and shredded tires remain on the site. The State found after an administrative hearing that as of October 1999 the equivalent of some 948,000 tires were stored on the site.²

In 1994, the State sued the debtor in the District Court of Dixon County for operating a solid waste management facility without a permit, and obtained a consent decree in July 1995. The consent decree included the provision that debtor was to

¹(...continued)
to "the debtor" will encompass whatever entity ran the company.

²The NDEQ director acknowledges that in the absence of evidence as to the actual number of tires at the site, the department liberally estimated the number in order to determine the level of financial assurance that should have been provided by the debtor in connection with his permit. Final Order of Jan. 14, 2000, at ¶ 6.

comply with all state environmental regulations, and imposed a \$5,000 fine, with an additional fine of \$10,000 if the debtor failed to abide by the consent decree.

In January 1997, the debtor obtained an environmental permit from the State allowing him to collect, process, and haul scrap tires and operate a scrap-tire collection site. The permit also required that all scrap tires collected were to be processed and removed to an end market within 18 months.

In March 1998, the District Court of Dixon County held the debtor in contempt for failing to comply with state environmental laws in accordance with the 1995 consent decree. The court enjoined the debtor from causing further environmental harm and imposed a penalty of \$10,000, but offered the option of paying a reduced penalty if the debtor removed the tires and rubber products from the site within a certain time period. The debtor paid \$2,500, but did not completely comply with the court's clean-up schedule. He has not paid the remainder of the penalty.

In October 1998, the NDEQ issued an administrative complaint and order to the debtor, directing him to comply with the terms of his permit or properly close the facility. The debtor requested a hearing before the NDEQ on the matter, which was held in July 1999.

The State entered a final order in January 2000, revoking the debtor's scrap-tire permit and requiring him to remove and properly dispose of all scrap tires, tire-derived products, and residuals from the site by May 15, 2000. The debtor did not appeal this order.

The scrap tires and related materials remain on the property. The debtor faces the potential imposition of penalties of up to \$1,000 per day for each day the violation continues.

The debtor filed for Chapter 7 bankruptcy relief on June 13, 2000, and in amended schedules listed the State as an unsecured creditor with a contingent unliquidated claim. The State does not have a judgment for a dollar amount, although the parties agreed in the administrative proceeding that clean-up costs would exceed \$800,000. The State has collected an \$85,000 surety bond put up by the debtor to indemnify the State for clean-up and closure costs. The State has abandoned any claim to recover the costs of abating the nuisance. It is focusing on future

finances and contempt orders and obtaining a finding that the debtor is not discharged from those obligations or the future enforcement of those obligations.

Discussion

The debtor has identified two factual issues which he argues would prevent the entry of summary judgment on dischargeability. One is the form of his business ownership, and the other is his assertion that the State's actions in refusing to approve his proposed uses of the recycled tires caused his inability to comply with the environmental regulations.

That second argument was raised at the administrative hearing and disposed of by the final order of the NDEQ: "I find no merit to the argument that Strong cannot find an acceptable use for tire product. This is clearly the type of risk that any business venture must weigh before undertaking the enterprise[,] and poor judgment should not become the problem of the citizens of Nebraska." Final Order of Jan. 14, 2000, at ¶ 7. The Final Order was not appealed, so its findings stand.

The parties request a decision on two issues of law: first, is the State engaged in the type of effort to enforce police or regulatory powers that is outside the scope of the automatic stay pursuant to 11 U.S.C. § 362(b)(4), and second, is any fine, penalty, or forfeiture owed by the debtor to the State or an agency thereof the type of debt that is excepted from discharge under 11 U.S.C. § 523(a)(7)?

The State also suggests that the debtor should be denied a discharge of all his debts under 11 U.S.C. §§ 727(a)(2), (3), and (4) by allegedly transferring or concealing property and failing to provide accurate information concerning his finances.

The debtor agrees that steps should be taken to assess the problem and begin abatement at the site. However, he is no position to pay for or contribute to the financial costs of the clean-up operation. He fears that by seeking a denial of discharge of this obligation, the State intends to hold him liable in perpetuity for the balance of the costs.

A. 11 U.S.C. § 362(b)(4)

The filing of a bankruptcy petition does not automatically stay "the commencement or continuation of an action or

proceeding by a governmental unit . . . to enforce such governmental unit's . . . police and regulatory power, including the enforcement of a judgment other than a money judgment, obtained in an action or proceeding by the governmental unit to enforce [its] police or regulatory power." 11 U.S.C. § 362(b)(4).

The legislative history of this section indicates that when a debtor is sued by a governmental unit "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." S. Rep. No. 95-989, at 52 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5838; H.R. Rep. No. 95-595, at 343 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6299; United States v. Commonwealth Cos., Inc. (In re Commonwealth Cos., Inc.), 913 F.2d 518, 522 (8th Cir. 1990).

If the purpose of the law that the government is attempting to enforce is to promote public safety and welfare or to effectuate public policy, § 362(b)(4) applies. However, if the purpose of the law is to protect the government's pecuniary interest in the debtor's property or to protect private rights, then § 362(b)(4) does not apply. See Safety-Kleen, Inc. (Pinewood) v. Wyche, 274 F.3d 846, 865 (4th Cir. 2001); Commonwealth, 913 F.2d at 523 & n.6.

State and federal enforcement of environmental protection laws and regulations against debtors has been allowed to proceed under § 362(b)(4) because the primary purpose of such laws is to promote public safety and welfare. See Ohio v. Kovacs, 469 U.S. 274, 283 n. 11 (automatic stay does not apply to suits to enforce the regulatory statutes of the state); Safety-Kleen, 274 F.3d at 865-66 (enforcement of state financial assurance regulations allowed against hazardous waste facility because the purpose is to deter environmental misconduct and promote safety in the facility's design and operation); City of New York v. Exxon Corp., 932 F.2d 1020, 1024 (2d Cir. 1991) (governmental actions under CERCLA to recover costs expended in response to completed environmental violations are not stayed by bankruptcy); Commonwealth Oil Refining Co., Inc. v U.S. Env'tl. Prot. Agency (In re Commonwealth Oil Refining Co., Inc.), 805 F.2d 1175, 1186 (5th Cir. 1986) (EPA's attempt to enforce closure and compliance order against operator of hazardous waste site was permitted because enforcement "falls squarely within

the [government's] police and regulatory powers"); United States v. Nicolet, Inc., 857 F.2d 202, 208-10 (3d Cir. 1988) (EPA's lawsuit to fix and recover costs already expended for clean-up of hazardous-waste site permitted up to and including entry of monetary judgment).

Enforcement actions are permitted to proceed even though compliance will cause the debtor to spend money. Commonwealth Oil Refining, 805 F.2d at 1186. As the Third Circuit has observed:

Were we to find that any order which requires the expenditure of money is a "money judgment," then the exception to section 362 for government police action, which should be construed broadly, would instead be narrowed into virtual nonexistence. Yet we cannot ignore the fundamental fact that, in contemporary times, almost everything costs something. An injunction which does not compel some expenditure or loss of monies may often be an effective nullity.

Penn Terra Ltd. v. Dep't of Env'tl. Res., 733 F.2d 267, 277-78 (3d Cir. 1984).

These decisions indicate that § 362(b)(4) allows the State to proceed with its efforts to enforce the orders requiring debtor to clean up the site.

B. Dischargeability

1. 11 U.S.C. § 523(a)(7)

To the extent fines and/or penalties have been imposed on a debtor for violations of state law, such obligations are not discharged in bankruptcy. 11 U.S.C. § 523(a)(7); Ohio v. Kovacs, 469 U.S. 274, 284 (1985).

Where a tax penalty is not at issue, three requirements must be met before a debt is excepted from discharge under § 523(a)(7): (1) there must be a debt for a fine, penalty, or forfeiture; (2) the debt must be payable to and for the benefit of a governmental unit; and (3) the debt cannot constitute compensation for actual pecuniary loss. Kentucky Natural Res. & Env'tl. Protection Cabinet v. Seals, 161 B.R. 615, 618 (W.D. Va. 1993).

Nebraska courts have held that "a fine is an appropriate sanction in a civil contempt proceeding so long as the contemnor may avoid the fine by complying with the court's order." Jessen v. Jessen, 567 N.W.2d 612, 617 (Neb. Ct. App. 1997) (citing United Mine Workers v. Bagwell, 512 U.S. 821 (1994)). There is no suggestion in the present case that the penalty imposed by the District Court of Dixon County was intended to be compensatory; it appears to have been levied solely to encourage the debtor to comply with the clean-up order, and was subject to reduction if the debtor did in fact comply.

In this case it is undisputed that the fine or penalty assessed by the District Court of Dixon County is a debt payable to and for the benefit of a governmental unit. There has been no assertion that it constitutes compensation for actual pecuniary loss. Accordingly, I find that § 523(a)(7) excepts that debt from discharge.

Moreover, any action taken by the State from this point forward to enforce the environmental laws or regulations is not pre-petition action, is not stayed by the automatic stay or the discharge injunction of § 524(a), and relates only to the debtor's post-petition obligation to clean up the site. Such obligation and the financial burden of the cost of clean-up or fines for failing to take appropriate action are not discharged in this case.

2. 11 U.S.C. §§ 727(a)(2), (3), and (4)

In its second amended complaint, the State alleges that the debtor failed to timely provide information to the Chapter 7 trustee regarding the sale of a piece of tire shredding equipment for which the debtor is still owed money. The State suggests that the debtor may have concealed or transferred property of the estate or of the debtor with the intent to delay, hinder, or defraud creditors; may have concealed, falsified, or failed to keep information from which his financial condition and business transactions might have been ascertained; and may have knowingly and fraudulently made a false oath or account or withheld information from an officer of the estate. For these reasons, the State asserts that the debtor should be denied a discharge.

These allegations require factual development. A ruling on them at this time would be premature.

CONCLUSION

The § 362(b)(4) exception to the automatic stay allows the State to proceed with its efforts to enforce the orders requiring debtor to clean up the site.

The fines and penalties that were imposed on the debtor pre-petition are excepted from discharge in bankruptcy pursuant to § 523(a)(7).

The balance of the assertions by the State that the debtor should be denied a discharge of all debts is denied on this record. If the State desires to proceed on such claim or claims, the parties shall file a preliminary pretrial statement on those issues in 30 days. Otherwise, the determinations made herein are final and the balance of the case may be dismissed upon motion of either party.

Separate order to be entered.

DATED: September 27, 2002

BY THE COURT:

/s/Timothy J. Mahoney
Chief Judge

Notice given by the Court to:

*William Howland
*Lisa Buechler
John Turco
U.S. Trustee

Movant (*) is responsible for giving notice of this order to all other parties not listed above if required by rule or statute.

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ORDER

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IT IS ORDERED:

The § 362(b)(4) exception to the automatic stay allows the State to proceed with its efforts to enforce the orders requiring debtor to clean up the site.

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See Memorandum filed this date.

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