

**THE "MASS" EXODUS THROUGH CHAPTER 11:
MASS TORT REORGANIZATIONS**

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CHAPTER 15

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I. INTRODUCTION

A. The Rise and Significance of Mass Tort Cases

Johns-Manville, Dow Corning, Celotex, A.H. Robins, Federal-Mogul. Even accounting for the recent notoriety and complexity of recent mega-bankruptcies, and the whirlwind of corporate scandals surrounding them, mass tort bankruptcy cases unquestionably count among the most complex chapter 11 bankruptcy cases in history. They arise from a myriad of products liability and environmental pollution scenarios, but all share one distinguishing feature: the presence of unsecured tort claimants which dominates each case and largely dictates its progression through the bankruptcy process.¹

The prospects for a company faced with mass tort litigation are dire indeed. A single set of events and occurrences, often dormant long before injuries begin to manifest, can give rise to hundreds of thousands of tort claims asserted against an otherwise solvent and viable enterprise.² The proliferation of legal and business expenses arising therefrom can easily crush virtually any company, no matter the size or profitability.³ To date, the legal system has responded through two basic mechanisms designed to accomplish a more cost effective and orderly resolution of such claims: class action litigation, and now bankruptcy.

Mass tort litigation, and class actions in particular, were largely enabled by the 1966 amendments to the Federal Rules of Civil Procedure, specifically Rule 23, which substantially relaxed prior, rather formalistic

joinder requirements.⁴ Through class actions, a discreet number of "exemplary" plaintiffs can sue on behalf of the entire class of tort victims, subject to certain qualifications. To the plaintiffs, these cases promote an overall faster resolution of claims, by consolidating actions and freeing up judicial resources to address them. While a class action involving hundreds of plaintiffs and additional procedural issues may certainly progress more slowly than a suit brought by a single plaintiff, the plaintiff need not fear a "race to the courthouse" against potentially thousands of other similarly situated plaintiffs because their claims will be addressed together. Not only is the plaintiff assured a reasonably prompt progression in court, but also consistent treatment among its co-plaintiffs, thereby alleviating the concern that prior suits will exhaust the defendant's resources and assets and render the plaintiff's ordeal all for naught.

To the plaintiffs' attorney, mass tort suits offer significant notoriety and public exposure, and, by combining alleged victims' claims, the promise of a share in potentially mind-boggling damages.⁵ Add to the mix a

¹ Leonard P. Goldberger, *Insurance Issues in Mass Tort Bankruptcy Cases: Strategic Perspectives*, 1-2 (2002) (on file with White & Williams, L.L.P.).

² See *Report of the National Bankruptcy Review Commission*, 318 (October, 20, 1997)

³ S. Elizabeth Gibson, *Mass Tort Limited Fund Class Action Settlements & Bankruptcy Reorganizations*, Federal Judicial Center, at 7 (2000).

⁴ Richard L. Marcus, *Reassessing the Magnetic Pull of Megacases on Procedure*, 51 DePaul L.Rev. 457, 465 (2001). Class actions are of course, not limited to tort litigation. As Markus notes, an interesting fact regarding the revision to Rule 23 is that its drafters expressly disapproved that it be used in connection with mass tort litigation. *Id.* An in-depth review and evaluation of the class action vehicle outside of bankruptcy, including limited fund class action settlements, is largely beyond the scope of this paper, but for readers interested in these issues, Markus' article can be a good starting point. See also Markham R. Leventhal, *Class Actions: Fundamentals of Certification Analysis*, 72 Fla. B.J. 10 (1998).

⁵ Frederick Tung, *The Future Claims Representative in Mass Tort Bankruptcy: A Preliminary Inquiry*, 3 Chap. L. R. 43, 43 (2000); Stephen Carroll, et al., *Asbestos*

pool of typically highly sympathetic plaintiffs and the prospect of punitive damages⁶, and it is no surprise that even the largest mass tort companies typically find themselves facing bankruptcy.⁷

However, in today's legal climate, bankruptcy is no longer viewed as a last-ditch effort to address such claims. It provides an orderly forum for the resolution of aggregate claims, and in fact, utilizes a systemic framework which provides more detailed and specific guidance for legal professionals and courts. More importantly, it provides (in principle if not in practice) the key benefit, through the discharge of pre-petition claims, of "universal" finality. More and more, it is recognized as the most orderly and efficient vehicle for resolving the company's liabilities and moving forward.⁸

Despite its perceived superiority over class actions and limited fund class action settlements⁹, any guide for the practitioner for

dealing with mass tort cases must necessarily begin with a discussion of the major systemic problems endemic to them, for it is from these deficiencies that the major issues arise. Specifically, there is one general and glaring problem with the approach of using bankruptcy to address mass tort liabilities: the Bankruptcy Code ("Code") obviously was not originally drafted with mass tort cases in mind.¹⁰ Although amendments to the statute do incorporate provisions specifically addressing certain mass tort scenarios, these provisions are both ad hoc and extremely limited in scope.¹¹ In other words, the Code is deficient in providing guidance to legal professionals, courts, management, and other interested parties for many of the substantial issues that arise in such cases. That lack of guidance engenders both inconsistency, and unnecessary litigation.

Accordingly, as the scope of companies subject to becoming mass tort defendants grows with the ever wider net cast by plaintiffs' attorneys, it behooves the bankruptcy practitioner to familiarize itself with the particular vagaries that arise in such cases.¹²

1. A brief history lesson. Despite the recent explosion of asbestos litigation in the 1980's, the concept of mass tort litigation is not a new one. It has been around since the time of the nuclear radiation scares of the

Litigation Costs and Compensation, An Interim Report, at vii (Rand Institute for Civil Justice, 2002).

⁶ See R.H. Lockwood, *Allowance of Punitive Damages in Products Liability Cases*, 13 A.L.R.4th 52 (2002).

⁷ To date, asbestos liability has driven 67 companies into bankruptcy. *Asbestos Games*, The Wall Street Journal Online (April 9, 2003) (available at online.wsj.com).

⁸ Gibson, *supra* note 3, at 18; Mark J. Roe, *Bankruptcy and Mass Tort*, 84 Colum. L. Rev. 846, 848 (1984). But see Hon. Edith H. Jones, *Rough Justice in Mass Future Claims: Should Bankruptcy Courts Direct Tort Reform?*, 76 Tex. L. Rev. 1695, 1704 (1998) (explaining that this perceived superiority may be wistful).

⁹ The limited fund class action settlement method of dealing with mass tort claims suffered a serious blow in 1997, when the Supreme Court ruled that mass tort cases were not conducive for the certification of classes, due to the failure of the "predominance of common questions" requirement. *Amchem Products v. Windsor*, 521 U.S. 591 (1997); Marcus, *supra* note 4, at 465. The Court has since rejected another attempted class settlement of asbestos claims against

another major defendant, leaving this option in serious doubt. *Ortiz v. Fibreboard Corp.*, 527 U.S. 815 (1999). Note also the recent collapse of a national settlement program once touted by Owens-Corning Fiberglass Corporation, now in bankruptcy, under an unexpected crush of claims. Carroll, et al., *supra* note 5, at 31.

¹⁰ Alan N. Resnick, *Bankruptcy as a Vehicle for Resolving Enterprise-Threatening Mass Tort Liability*, 148 U. Pa. L. Rev. 2045, 2046 (June 2000).

¹¹ See 11 U.S.C. §524(g).

¹² The systemic roles and social functions played by plaintiffs' attorneys are beyond the scope of this article.

1960's.¹³ Shortly thereafter, mass tort litigation exploded onto the scene, led by suits over such products as Agent Orange, DES, Dalkon Shield, silicon gel implants, and of course, asbestos.¹⁴

As asbestos litigation began to flood courts in the 1980's, they progressively sought ways in which to reduce the strain upon the system, and approached the problem primarily through the consolidation and facilitation of suits.¹⁵ The reasoning was to slide these claims as quickly as possible through the process. Yet, the incidence of mass tort claims has not at all subsided, and commentators have suggested that judicial efforts to consolidate and facilitate claims has had a severely counter-productive effect: it makes asserting claims, particularly specious claims, that much easier.¹⁶

The problem of "unimpaired claims" is a serious one. These are recognized as legitimate claims under the current tort system, so if the Code continues to be used as a means to address mass tort liabilities, it (we) must do a better job addressing the issues that can surround these claims. Otherwise, they hopelessly clog judicial dockets, thereby impeding the efficient resolution of bona fide claims. Also, as

proceedings are compounded and protracted, litigation and administrative costs rise, thereby further threatening the defendant's economic viability as well as the prospects for recovery by the injured. As we will see, these claims can also complicate the claims estimation process, thereby significantly hindering plan formulation.

For these reasons, scholars have explained that systemic responsiveness to date has had a disastrous, spiraling counter effect. As more unimpaired claims are asserted, courts, left with no clear legislative directive addressing the problem, have had no choice but to respond by minimizing the judicial strain of such claims by remand, transfer and consolidation (such as through class actions and multidistrict litigation) intended to allow these claims to be treated more efficiently. In other words, as these claims are facilitated, it in turn prompts the assertion of still more unimpaired claims.¹⁷

2. A look inside the numbers. Despite having been around for just under three decades, the numbers related to asbestos litigation are staggering. Almost 60 companies have been driven into bankruptcy by alleged asbestos liabilities.¹⁸ The systemic cost to date has been estimated to be somewhere between \$21-54 billion, with projected costs of roughly \$43-50 billion for the next twenty years and a total price tag ultimately in the neighborhood of \$200-275 billion.¹⁹ Such figures indicate that the

¹³ See, e.g., Samuel D. Estep, *Radiation Injuries and Statistics: The Need for a New Approach to Injury Litigation*, 59 Mich. L. Rev. 259 (1960); Paul D. Rheingold, *The MER/29 Story - An Instance of Successful Mass Disaster Litigation*, 56 Cal. L. Rev. 116 (1968).

¹⁴ See Judge Spencer Williams' discussion in *IUD Products Liability Litigation*, 526 F. Supp. 887, 892 (N.D. Cal. 1981), *rev'd*, 693 F.2d 847 (9th Cir. 1982); Marcus, *supra* note 4, at 463.

¹⁵ Deborah R. Hensler, Mark A. Peterson, *Reinventing Civil Litigation: Evaluating Proposals For Change: Understanding Mass Personal Injury Litigation: A Socio-Legal Analysis*, 59 Brooklyn L. Rev. 961, 1028-30 (1993).

¹⁶ Marcus, *supra* note 4, at 465; Francis E. McGovern, *An Analysis of Mass Torts for Judges*, 73 Tex. L. Rev. 1821, 1822 (1995).

¹⁷ Carroll, et al., *supra* note 5, at 26. The authors stress that this paper is in no way intended to take any position among mass tort plaintiffs and defendants. Rather, we focus on practical and systemic issues.

¹⁸ Mark D. Plevin, Paul W. Kalish, *Where Are They Now? A History of the Companies That Have Sought Bankruptcy Protection Due to Asbestos Claims*, Vol. 16, No. 15 Mealey's Asbestos Bankr. Rep. 34 (Aug. 2001).

¹⁹ Cf. Mark A. Behrens, *Some Proposals For Courts Interested in Helping Sick Claimants and Solving Serious Problems in Asbestos Litigation*, 54 Baylor L. Rev. 331, 333 (2002); Todd R. Snyder, Deanne C. Siemer, *The Patronus*

percentage of possible claims which are in fact currently known could be in the range of 20% or less, although this figure is far from certain.

Because of the predominance of asbestos among mass tort cases, and the fact that its commercial use has been largely banned by the federal government (OSHA),²⁰ it was once thought that the mass tort phenomenon would be a short lived one, or at least, one with a discernible lifespan. The rationale was simple: because injuries from asbestos exposure typically would manifest within 15 to 40 years from the date of exposure, and because the use of asbestos has been *effectively* discontinued, it stands to reason that the universe of asbestos related claims would be known and addressed within roughly 40 years from the time of cessation.²¹

The insurance industry estimates that 600,000 to 700,000 asbestos claims are currently making their way through courts, corporate claims departments, or claims trusts.²² Moreover, commensurate with projections that we have seen only the tip of the asbestos iceberg, claims appear to be escalating rather than diminishing. From 1993 to 1999, the number of pending court cases doubled from 100 to 200,000. The number of cases has been projected up to

700,000 by year 2050, with future claimants numbering as much as 3,500,000.²³

Studies have revealed that unimpaired claims are fastest on the rise, the number of defendants and industrial sectors subjected to asbestos claims has expanded throughout the economy, and that from the early 1980's to mid 1990's, the number of average defendants named by any one plaintiff increased from approximately 20 to around 65 defendants.²⁴ Accordingly, it is clear that a company, no matter its business model, product or operations, cannot presume that it is safe from such suits simply because it is not involved in what it perceives to be the affected industry. Virtually all industrial sectors are now affected, and "non-traditional" defendants currently shoulder more than 60% of the administrative cost of processing these claims.²⁵

It is clear that as traditional defendants go the way of bankruptcy, more companies begin the long march towards (and through) it.²⁶ As shocking as the statistics are, they

Technique: A Practical Proposal for Asbestos-Driven Bankruptcies, 11 J.B.L.&P 357, 362 (2002); and Carroll, et al., *supra* note 5, at vii. Virtually all recent studies concede that the estimates are, if anything, overly conservative.

²⁰ Behrens, *supra* note 19 at 336 n. 25.

²¹ Behrens, *supra* note 19 at 336-337. Even this model does not put us any where near the end of the tunnel. OSHA was passed in 1970, but a proposed outright ban on the use of asbestos by the EPA in 1989, has been set aside. *See Corrosion Proof Fittings v. E.P.A.*, 947 F.2d 1201 (5th Cir. 1991) [No. 89-4596], *opinion clarified* (Nov. 15, 1991), *reh'g denied* (Nov. 27, 1991). Still, the use of asbestos in most products, including new products, remains banned. Carroll, et al., *supra* note 5, at 13.

²² Snyder and Siemer, *supra* note 19, at 362.

²³ Behrens, *supra* note 19 at 337; The Fairness in Asbestos Compensation Act of 1999: Legislative Hearing on H.R. 1283, Before the House Comm. on the Judiciary, 106th Cong. 4 (July 1, 1999) (statement of Christopher Edley, Jr., Professor, Harvard Law School); *Mass Tort Litigation Report Discusses Resolving Asbestos Cases Over Next 20 Years*, vol. 14, no. 10 Mealey's Litig. Rep.: Asbestos 22 (June 18, 1999); Judicial Conference Ad Hoc Committee on Asbestos Litigation, Report to the Chief Justice of the United States and Members of the Judicial Conference of the United States 5 (Mar. 1991) in vol. 6, no. 4 Mealey's Litig. Rep.: Asbestos (Mar. 15, 1991).

²⁴ Carroll, et al., *supra* note 5, at 41, 46-48.

²⁵ *Id.* at 49-50. This study revealed that asbestos defendants appeared in 75 of the 83 economic sectors tracked by the U.S. Dept. of Commerce. *See also In re Joint E. & S. Dist. Asbestos Litig.*, 129 B.R. 710, 747-48 (E. & S.D. N.Y. 1991).

²⁶ Behrens, *supra* note 19 at 331; Carroll, et al., *supra* note 5, at 31. Mass tort bankruptcies take a significant time to resolve. A sampling of major cases and

only tell the *asbestos* story. When factoring in other past and likely future products liability targets, the magnitude of the still-evolving mass tort problem begins to manifest. Yet, it is still one of the earliest mass tort bankruptcy cases which provides the blueprint for addressing these claims in bankruptcy.

B. General Features of Mass Tort Reorganizations

1. Third party injunctions, trusts, and §524(g). The Johns-Manville case commenced in 1982 was the first clear example of a large, seemingly healthy company felled solely by asbestos liabilities asserted against it.²⁷ After confirmation in that case four years later, its plan structure still serves today as the mass tort bankruptcy archetype.²⁸ So closely has it been followed that it constituted the impetus for Congress to amend the Code in 1994 with the addition of section 524(g). The general features include: (i) the creation of a trust implemented to process and satisfy the mass tort claims, funded primarily with at least a majority of the reorganized debtor's stock (and typically insurance assets); and (ii) the issuance of a channeling injunction to steer claims away from the reorganized debtor (and typically

certain non-debtor parties making contributions to the plan).²⁹

Section 524(g), which essentially codifies the plan structure of Johns-Manville, has several, important major features.³⁰ It expressly allows for the bankruptcy court to issue supplemental (third party) injunctions to channel all asbestos related claims to a trust implemented in the plan to address them. The trust must also be funded by the stock of at least one debtor, together with future payment obligations or dividends. Moreover, the court is required to determine: (i) that the debtor is likely to be subject to substantial future claims, the amounts, timing and numbers of which cannot be determined; (ii) that treatment of such claims outside of the plan threatens the plan's purpose; (iii) that the trust is structured through mechanisms designed to reasonably ensure its ability to equitably satisfy present and future claims (sufficiency and percentage distribution of assets); and (iv) that the terms of this plan structure have been adequately disclosed. Finally, and most importantly, section 524(g) plans may not be "cramdown" plans as to the trust (tort) claimants.³¹ These claimants must be placed in a separate class, and that class must accept the plan by a super-majority (75%), thereby giving those parties significant leverage in the plan formulation process.³²

the approximate duration to confirmation or closure: (i) UNR Industries, Inc. – 7 years; (ii) Forty-Eight Insulations, Inc. – 10 years; (iii) Raytech Corporation – 11 years; (iv) Celotex Corporation – 6 years; (v) Eagle-Picher Industries, Inc. – 5 years. Fred S. Hodara, Robert J. Stark, *Protecting Distributions for Commercial Creditors in Asbestos-Related Chapter 11 Cases*, 10 J.B.L. &P. 383, 399-405 (July/August 2001).

Confirmation doesn't necessarily end the ordeal. It often simply removes the litigation to a claims resolution forum, and can even give rise to hotly contested post-confirmation issues if these are overlooked prior to confirmation. The Amatex Trust did not become operational until six years after plan confirmation. Carroll, et al., *supra* note 5, at 68.

²⁷ Marcus, *supra* note 4, at 464.
²⁸ Hodara and Stark, *supra* note 26, at 389.

²⁹ *Id.* at 388-89. The authors are loathe to set forth the entire text of section 524(g) here, as it is cumbersome and would be disruptive. However, it is addressed herein, is critical to the analysis of mass tort bankruptcy cases, particularly asbestos related cases, and is provided as Exhibit "A" to this paper. Readers are encouraged to examine its terms closely.

³⁰ Snyder and Siemer, *supra* note 19, at 365.
³¹ More specifically, while a plan incorporating a section 524(g) plan might be a cramdown plan (confirmed over the objections and rejection of a class of creditors), a section 524(g) injunction may not be approved in a plan over the objection / rejection of the mass tort claimants.

³² See also Hodara and Stark, *supra* note 26, at 388-91.

Moreover, Section 524(g) must be read in conjunction with Code section 524(e), which provides that, except with respect to spouses, the discharge of a debtor's debts does not affect the liability of any other entities on such debts.³³ This section is particularly problematic in mass tort cases heavy on negotiations with critical non-debtor parties³⁴, such as insurers, who often must waive technical and potential defaults under their respective policies in order for the debtor to implement the plan, and the debtor's affiliates who are also often looked to for additional contributions to the plan.

These latter parties may waive their status as co-insureds under the debtor's insurance policies, intercompany claims against the debtor, and other rights to additional property they share interests in along with the debtor, in order to maximize the resources available to the estate.³⁵ Such parties' various contributions and concessions are often critical to obtaining confirmation of a plan.³⁶ These parties are interested in one thing above all others: obtaining finality from the assertion of mass tort claims arising from their involvement with the debtor.³⁷ Accordingly, absent the ability to provide them such relief through third party injunctions,

³³ 11 U.S.C. §524(e).

³⁴ See Lynn M. LoPucki and William C. Whitford, *Bargaining Over Equity's Share in the Bankruptcy Reorganization of Large Publicly Held Companies*, 139 U. Pa. L. Rev. 125, 138 (1990) (discussing consensual resolutions of bankruptcy cases); Marcus, *supra* note 4, at 473-74.

³⁵ See *In re Zale Corp.*, 62 F.3d 746 (5th Cir. 1995); *In re Forty-Eight Insulations, Inc.*, 133 B.R. 973 (Bankr. N.D. Ill. 1991);

³⁶ See, e.g., *In re Babcock & Wilcox Company, Inc.* (E.D. La. No. 00-10992). Amended Joint Disclosure Statement filed on March 28, 2003 [Docket No. 4073] (discussing the implementation of a non-debtor affiliate settlement agreement under which such affiliates contribute funds or release claims to assets, including insurance assets, shared with the debtor.)

³⁷ See, e.g., *Id.* at 114, 140-41 (third party affiliate release and injunction).

their incentive to cooperate in the plan formulation process evaporates.

2. Key reliance on insurance. Among the most troubling of issues in these cases are those surrounding insurance policies held by the debtor. One reason for this is simply the primacy and significance of insurance assets in mass tort bankruptcies.³⁸ In many cases, with most of the debtor's assets encumbered in favor of senior bank lenders, insurance policies and proceeds often constitute the greatest pool of assets available to satisfy mass tort claims.³⁹

It should be recognized that, regardless of whether a case involves mass tort claims, insurance policies and insurers are not viewed any differently under the Code. In reality, however, the legal professional often finds that mass tort cases do indeed give rise to unique insurance related considerations and scenarios. These in turn give rise to inconsistency and seeming vagaries across jurisdictions, and even within a given jurisdiction.⁴⁰

C. The Players, Goals and Objectives

1. The Court. In the absence of adequate guidance from the Code, bankruptcy courts will understandably be somewhat more result oriented. They are, after all, courts of equity, and many judges will naturally strive to, "do what is right" under the specific facts of a given case.⁴¹ Moreover, mass tort cases tend to be emotionally charged affairs, and the line of equity can be extremely difficult to draw. The court will almost invariably be caught between: (i) tort claimants, often grievously injured; (ii) an economically viable and productive debtors threatened with liquidation for having run afoul of doctrines of strict

³⁸ See *In re Johns-Manville Co.*, 40 B.R. 219, 229 (S.D. N.Y. 1984) (noting that insurance policies may be the single most important asset in a mass tort bankruptcy).

³⁹ Goldberger, *supra* note 1, at 2.

⁴⁰ Cf. *A.H. Robins Co.*, 880 F.2d 694, 702 (4th Cir. 1989) and *Zale*, 62 F.3d at 760.

⁴¹ Behrens, *supra* note 19 at 334.

products liability⁴²; and (iii) insurers who, despite generally having no part in the injury causing events, face being slapped with the multi million dollar price tag for resolving the claims.⁴³ All this, without even having mentioned the Herculean task of reigning in excessive administrative costs which threaten to swallow up the interests of all parties involved in the bankruptcy case, including the usual priority and general unsecured creditors of the estate.⁴⁴ Even secured lenders are far from immune. As the case languishes under often bitter negotiations, its duration inexorably undermines and depresses the debtor's economic viability and going concern value supporting their collateral.⁴⁵

It certainly need not be so dire, for the parties at the center of mass tort cases share a common goal: to address, settle and satisfy the debtor's mass tort liabilities.

2. Insurers. For the insurer, the first order of business is to determine whether a claim is even covered under the policy or policies in question. Because insurance policies are matters of private contract, the terms of coverage can vary widely – subject to state law limitations – and there is a series of routine insurance related questions which the insurer and the practitioner must navigate.

a. What type of claims(s) or loss is being asserted. (what are the general facts, timing, bases and theories of the asserted mass tort liability). This may be personal injury,

property damage, or even contractual rather than tort claims.⁴⁶

b. What type of policy is it? What years does it cover? Does it cover the insured's loss of property or its liability, property damage or personal injury?⁴⁷ Does it cover directors and officers only? All of the above? We are most concerned here with corporate general liability policies, those which are designed to compensate the victims of the insured's conduct.

c. Who is the beneficiary or beneficiaries, and/or co-insureds? These first three questions should *generally* answer the question of *potential* coverage and liability, but much more factors into the equation.

d. What are the key limits of the policy? Particular attention should be paid to: (i) whether it is a "claims made" or "occurrence based" policy⁴⁸, a primary or excess policy (the latter being triggered after the exhaustion of primary insurance); (ii) the limits of coverage. It must be known whether there is an aggregate limit, a per occurrence limit, and/or limits on defense costs and whether these are counted against the policy limit⁴⁹;

⁴² S. R. Shapiro, *Products Liability: Strict Liability in Tort*, 13 A.L.R.3d 1057 (2002).

⁴³ It is no surprise that this additional ripple effect has threatened the insolvency of numerous insurance companies. Asbestos liability to date has already exceeded the cost to these companies of all other natural disasters. As these costs mount, more and more insurers are being liquidated under state laws. Snyder and Siemer, *supra* note 19, at 365.

⁴⁴ Snyder and Siemer, *supra* note 19, at 369; Hodara and Stark, *supra* note 26, at 394.

⁴⁵ Snyder and Siemer, *supra* note 19, at 368.

⁴⁶ Recall that class actions were not originally intended to address mass tort claims.

⁴⁷ For example, casualty, collision, fire, and life insurance policies are intended to compensate the insured directly, and where the debtor is the beneficiary, it has such a right to payment of the proceeds of such policies (this distinction proves important, as discussed herein below).

⁴⁸ A claims made policy indemnifies the debtor for those claims made against it during the policy period. An occurrence based policy insures against claims arising from occurrences (such as exposure) during the policy period. See *EBSCO Industries, Inc. v. Royal Insurance Company of America*, 775 So.2d 128, 131-32 n. 3 (S.Ct.Ala. 2000).

⁴⁹ This is one area in which the latency of mass tort claims has been particularly problematic to the insurer. An insurer issuing a policy long before the rise of

(iii) whether and what exclusions, endorsements and amendments apply; and (iv) what other duties and covenants apply under the policy which might give rise to claims for breach by any party?

It is critical for the core parties to the case to determine the answers to these questions early, for they will determine the scope of insurance assets available to fund the plan and set the framework for negotiations. Clearly, a claims made policy has little significance where the policy years have since past. On the other hand, an occurrence based policy with "per occurrence" limits but no aggregate limit, and covering significant years of exposure or injury causing events may subject the insurer to claims made indefinitely (depending on the judicial interpretation of what constitutes an "occurrence"). The significance of policy limits is otherwise self explanatory, but the issue of defense costs is also significant. These can be quite large when dealing with tort claims, and what costs are chargeable as defense costs against the policy's limits, if any, can substantially affect available coverage and the insurer's potential losses.⁵⁰

Exclusions are also somewhat self-explanatory, and may cover exclusions for intentional acts, for claims covered by other insurance, and for claims made by one insured against another (insured v. insured exclusions).⁵¹ Endorsements and

amendments are often required by various states from time to time, and may implement additional exclusions.⁵² In particular, insurers now almost universally utilize asbestos insurance exclusions due to the excessive costs and exposure.⁵³ Moreover, it is important to be mindful of the insured's duties, such as duties of prompt notice and cooperation, for these are fertile ground for assertions of breaches terminating coverage. Unpaid deductibles and self-insured retentions can be among the most significant of these duties. The failure of the insured to make these payments can be ground for termination.

The duty to cooperate is in fact a good example of the differing concerns prevalent in mass tort bankruptcies. As discussed in Article II.A hereinbelow, courts tend to view the automatic stay more broadly as to litigation against a mass tort debtor's insurer, generally because the insurance policy is more critical to the estate and such litigation therefore has a perception of greater impact on the debtor's reorganization efforts. The

awareness of the tort causing elements and the solidification of the law around such issues (such as asbestos) might have a policy which is based (priced) on an erroneous calculation of risk. For example, a policy issued in 1960, before the problems of asbestos became widely known, might contain no aggregate limits, and eventually subject the insurer to unlimited liability for claims asserted forty years later.

⁵⁰ See *In re UNR Indus., Inc. v. Continental Ins. Co.*, 682 F.Supp. 1434 (N.D. Ill. 1988) (Insurer's duty to defend ends when limits of coverage have been reached).

⁵¹ Courts have explained the primary policy and purpose behind the insured v. insured

exclusion as being intended to "prevent collusive suits in which an insured company might seek to force its insurer to pay for poor business decisions of its officers or managers." *Cigna Insurance Company v. Gulf USA Corporation*, 1997 U.S. Dist. LEXIS 23816, at *18, citing, *Township of Center v. First Mercury Syndicate, Inc.*, 117 F.3d 115, 118 (3rd Cir. 1997); *In re Buckeye Countrymark, Inc.*, 251 B.R. 835, 841 (Bankr. S.D. Ohio 2000);

⁵² Rebecca M. Bratspies, *Splitting the Baby: Apportioning Environmental Liability Among Triggered Insurance Policies*, 1999 B.Y.U.L. Rev. 1215, 1222 (1999).

⁵³ See *Stonewall Ins. Co. v. Asbestos Claims Management Corp.*, 73 F.3d 1178, 1202 (2d Cir. 1995). *Stonewall* contains a thorough analysis of the typical exclusions utilized by the insurance industry prior to that time, and concluded that none excluded liabilities for asbestos related injuries. The form Commercial General Liability Policy was amended in 1986 to contain an asbestos pollution exclusion. Bratspies, *supra* note 52, at 1260.

case of *In re Fernstrom Storage & Van Co.*, 100 B.R. 1017, 1023 (Bankr. N.D. Ill. 1989), provides a good discussion of how, in the general sense, the automatic stay should not necessarily affect a debtor's duty to cooperate with an insurer as to suits launched against the latter party, but also noting the different circumstances of the mass tort scenario and their effect on this reasoning. Clearly, one can see the potential for disruption and distraction where a debtor has many insurers faced with hundreds of suits by thousands of plaintiffs, and is forced to pay substantive attention to such litigation.

The issue of "excess" insurers also substantially affects case administration and the conduct of litigation. The number and interests of the parties involved in mass tort bankruptcies are already tedious to address. The presence of excess insurers, often at multiple "layers" complicates this problem because there is not one, but two (or more) groups of insurers, with conflicting interests. While both share an interest in properly evaluating and valuing claims, excess insurers will strenuously argue for the maximum liability of layers below them, for the larger the lower layers are, the less likely that the higher layers will be triggered, and the longer it takes.⁵⁴

A recent opinion issued in a New York State court underscores these issues. On April 7, 2003, the Court issued an opinion in *Appalachian Ins. Co. v. General Electric Co.*, regarding a primary policy with a per occurrence limit of \$5 million. Ordinarily, one might expect the insured debtor to take the position that each exposure (each claimant) was a separate occurrence, in order to maximize coverage under that policy. However, the debtor argued that its decision

⁵⁴ This is one major reason why we see such an incidence of interventions by insurers into coverage actions in the bankruptcy case: each has a vested interest in the treatment of the others. Note also that these layers can be complex, in that an excess policy will pay after a primary policy for a given policy year, but not necessarily as to other policy years. Bratspies, *supra* note 52, at 1252.

to manufacture its asbestos-containing product (spanning nearly 100 years) was a single occurrence. The reason? It also possessed significant layers of excess insurance policies which were triggered to cover the amount of liability for each occurrence exceeding the \$5 million primary cap. Thus, these excess policies and proceeds could be more easily reached if the per occurrence limit of the policy would be more easily triggered. The Court found this interpretation strained, and ruled in favor of the excess insurers.⁵⁵

e. Standing. An insurer must also be prepared to confront issues of standing. One major concern is that mass tort jurisprudence is relatively recent and rapidly developing, and is thus somewhat incompatible with the concept in the bankruptcy context. The result is that the rule of standing does not seem to apply favorably to insurance companies.

One reason is that the Code grants general standing to "parties in interest" yet does not define the term and uses it in at least 40 sections, plus 30 additional procedural rules.⁵⁶ Many courts utilize a

⁵⁵ Case No. 122807/96. Tom Perrotta, *GE Can't Attach Excess Insurers in Asbestos Cases*, New York Law Journal (Apr. 9, 2003).

(available at www.law.com)

⁵⁶ §1109(b) states that, "a party in interest, including the debtor, the trustee, a creditor's committee, a creditor, an equity security holder, or any indenture trustee, may raise and appear and be heard on any issue in a case under this chapter." This is the closest that the Code comes to a definition of party in interest, but the definition is, by section 102(3), explicitly non-exclusive, and courts uniformly recognize this fact. See, e.g., *In re Peachtree Lane Assoc's, Ltd.*, 188 B.R. 815, 824-25 (N.D.Ill 1995); 5 *Collier on Bankruptcy* ¶ 1109.02 [22] (15th ed. 1994).

Consequently, the application of the doctrine is recognized to vary on a case by case basis. *In re Amatex Corp.*, 755 F.2d 1034, 1042 (3d Cir. 1985).

person aggrieved standard⁵⁷, while others note that this standard is both arcane applicable to appeals, not necessarily to lower court proceedings.⁵⁸

As to the insurer, under this standard, its position appears to be strongest in mass tort cases, for it is in these cases where insurance has the greatest significance, and are most likely to have significant consequences for the insurer's interests.⁵⁹ However, problems arise from a tendency to view insurance as a simple relationship. Courts which have denied standing have focused upon the basic rationale that an insurer is obligated to indemnify if the policy provides coverage, and since bankruptcy issues (in principle) do not vary that obligation, an insurer often lacks standing to object.⁶⁰

3. The debtor and its affiliates. The debtor is in the unenviable position of having to coordinate the interests of these many parties, steer the case through the usual requirements and issues, such as cash collateral and debtor-in-possession financing, and lead the negotiations towards a confirmable plan. During this course, it will be subjected to many incidences of conflicts. The debtor clearly has its own interests to consider, but may also still be largely controlled or influenced by its parent and affiliates, and their interests may not be directly aligned with its own. Complicating this position further are the debtors' fiduciary duties to the estate.⁶¹

As we have previously discussed, in order to maximize the estate's assets, affiliates may be called upon to forgive intercompany debts and waive their interests in shared assets, including their status as co-insureds under the debtor's policies.⁶² Their transactions with the debtor will of course be

⁵⁷ Defined as the impairment of a "direct pecuniary interest." *Krebs Chrysler-Plymouth, Inc., v. Valley Motors, Inc.*, 141 F.3d 490, 495 (3rd Cir. 1997).

⁵⁸ Cf. *In re Applied Safety, Inc.*, 200 B.R. 576, 587 (E.D.Pa. 1996) (utilizing the person aggrieved standard for objections to confirmation), with *In re Alpex Computer Corp.*, 71 F.3d 353, 357 n.6 (10th Cir. 1995) (§1109(b) expands right to be heard in Chapter 11 proceedings beyond "person aggrieved" standard, which applies to appeals.).

⁵⁹ *In re Keck, Mahin & Cate*, 241 B.R. 583, 596 (N.D.Ill., 1999) ("The insurance contract is property of the estate, §541(a)(1), and this Court must determine whether the Plan provides adequate means for its implementation."); *Commercial Union Insurance Co. v. Johns-Manville Corp.*, 31 B.R. 965, 972 (S.D.N.Y. 1983).

⁶⁰ See *In re Fuller-Austin Insulation*, 1998 U.S. Dist. LEXIS 18340, *9-12 (D.Del. 1998); *Travelers Insurance Company v. H.K. Porter Company, Inc.*, 45 F.3d 737, 740-42 (3rd Cir. 1995). Note that in *Travelers*, steps were taken which undercut the insurer's standing. Faced with objections to confirmation, the plan proponent simply inserted a clause providing that its provisions did not affect the insurance company's rights.

⁶¹ See C.R. Bowles, Jr. & Nancy B. Rapoport, *Has the DIP's Attorney Become the Ultimate Creditors' Lawyer in Bankruptcy Reorganization Cases?*, 5 Am. Bankr. Inst. L. Rev. 47, 53-54 (1997)

⁶² Note that, even absent a release of its interest, the co-insured must be reckoned with as to policy settlements reached with the insurer, for bankruptcy settlements cannot unduly prejudice the rights of third parties. "Even if a settlement is fair and equitable to the parties to the settlement, approval is not appropriate if the rights of others who are not parties to the settlement will be unduly prejudiced." *In re Devon Capital Management*, 261 B.R. 619, 623 (Bankr. W.D. Pa. 2001), citing *In re AWECO, Inc.*, 725 F.2d 293, 297-98 (5th Cir. 1984), cert. denied, 469 U.S. 880, 105 S. Ct. 244, 83 L. Ed. 2d 182 (1984). See also *Zale*, 62 F.3d at 754 (5th Cir. 1995), citing *Cullen v. Riley*, 957 F.2d 1020, 1026 (2d Cir. 1992) (holding that "where the rights of one who is not a party to a settlement are at stake, the fairness of the settlement to the settling parties is not enough to earn the judicial stamp of approval.")

subjected to the same scrutiny that applies in most cases, by parties looking to avoid transfers by the debtor to its affiliates in order to bring additional assets into the estate.

A prime example of the issues that can arise from this model can be found in the case of Babcock & Wilcox Company, Inc., *et al.*, an asbestos related case commenced in the Eastern District of Louisiana in 2000.⁶³ There, shortly before declaring bankruptcy, the debtors engaged in a number of intercompany transfers with its affiliates which asbestos claimants later sought to avoid. The debtor took the position that "it was not in the best interests of the estate" to pursue such actions, and had sought a declaratory judgment determining that it was solvent at the time of the transfers (a significant element in fraudulent transfer cases).⁶⁴ Interestingly, when the asbestos claimants' committees intervened and brought avoidance actions, the debtor was realigned as a defendant (along with its affiliates) in the suit.⁶⁵ While the debtor was able to defend its position based upon its litigation assessment, this scenario and how it squares with the debtor's fiduciary duties and the apparent influence asserted by its parent certainly raise a few eyebrows.

a. A (corporate) family's sacrifice. For its part, the parent's management may have long since determined that it is preferable to "sacrifice" the debtor through bankruptcy in order to shed the mass tort liabilities of the remaining corporate family.⁶⁶ The Babcock & Wilcox case certainly appears that the debtor's corporate family instituted a number of transfers within the family in preparation for the bankruptcy filings of certain subsidiaries. In fact, more and more, this advance planning and willingness to enter into bankruptcy early in the process, and when the debtor may still

⁶³ *Babcock & Wilcox*, *supra* note 36.

⁶⁴ *See, e.g.*, 11 U.S.C. § 548.

⁶⁵ *See Babcock & Wilcox*, *supra* note 36, Amended Disclosure Statement, at pp. 55-57. The defendants eventually prevailed on the solvency issue.

⁶⁶ This key interest again underscores the significance of third party releases and injunctions.

be solvent, appears to be growing. No doubt this is in part due to the staggering costs of mass tort litigation. RHI Refractories Holding Co., the world's leading supplier of refractory materials to the steel industry, recently utilized this general approach by sending two of its subsidiaries into bankruptcy, Harbison-Walker Refractories Co. and North American Refractories Co.⁶⁷

DII Industries, LLC, accessor to Dresser Industries and a subsidiary of Petroleum giant Halliburton Co., has not filed for bankruptcy protection, but appears to be headed that way. In a single day, on December 7, 2001, Halliburton lost almost half of its market value – a whopping \$3.8 billion – after investment analysts became concerned with its asbestos exposure in the wake of then-recent verdicts aggregating \$150 million against the company.⁶⁸ This, despite \$737 million in reserves devoted by Halliburton solely to combating such exposure.⁶⁹ Moreover, the bankruptcy case of related company Harbison provided it with significant reprieve. Harbison was formerly spun off by Halliburton's Dresser Industries, Inc. unit, and a temporary restraining order entered in its bankruptcy case against asbestos claims affected virtually all of the claims asserted against Halliburton entities.⁷⁰ This order has since been continued by the agreement of the parties.

4. Professionals. One salient feature of mass tort bankruptcy cases is the proliferation of professionals. Due to the significance of the mass tort claimants, the court usually

⁶⁷ Behrens, *supra* note 19 at 339. *See also* Snyder and Siemer, *supra* note 19, at 372-75 (arguing for asbestos defendants to unilaterally create special purpose subsidiaries to be placed into bankruptcy.)

⁶⁸ Behrens, *supra* note 19 at 340.

⁶⁹ Nelson Antosh, *Halliburton Hunkers Down to Fend Off Asbestos Litigation*, Houston Chronicle, Feb. 2, 2002 (available at www.chron.com).

⁷⁰ *Halliburton Stock Rises After Restraining Order Against Claims*, Naples Daily News, Feb. 16, 2002 (available at www.naplesnews.com).

approves an official committee (paid from assets of the estate) to represent their interests.⁷¹ A representative for future claims is also appointed. Each of these parties, like the usual creditors' committee, will employ its own battery of attorneys, consultants, and other professionals to assist it in the administration of the case and its duties, thereby increasing the cost of administration of such cases.⁷²

Another aspect of mass tort bankruptcies which further complicates matters for the legal professional, as well as complicating the *range* of professionals, particularly with respect to asbestos cases, is the prevalence and significance of complex technical issues. An extremely detailed (yet debatable) body of medical issues and criteria has sprung up around these cases.⁷³ The practitioner dealing with asbestos cases must familiarize itself with, for example, the different diseases and conditions it can cause, levels of impairment and exposure, medical causation, and standards of medical evidence.⁷⁴ The presence of such issues inexorably increases administrative costs as the practitioner strives to become knowledgeable, and can often result in the requirement of additional professionals.

5. The mass tort claimants. We have already seen how the mass tort claimant, through sheer numbers and claim amounts, combined with the requirements of section 524(g), can dominate a bankruptcy case, and specifically the plan voting process. However, the most unusual of mass tort claimants is the unknown future claimant.⁷⁵ One by product of

the long latency often involved in mass tort injuries is that the full range and identities of claimants injured by pre-petition conduct simply cannot be known.

It is the issue of these future claimants that in fact led the Supreme Court to largely forestall the use of class action settlements to address mass tort claims.⁷⁶ The Supreme Court's reasoning was that the class of mass tort claimants proposed for certification contained claimants whose interests were not sufficiently aligned. Specifically, present claimants have an interest in maximum present payment, whereas the interests of future claimants is in having an adequate, inflation insulated fund for their own claims.⁷⁷ Accordingly, the Court held that the settlements had been arrived at with insufficient representation for future claimants.⁷⁸

Of course, it is rather problematic in our system to resolve legal and judicial proceedings without giving the parties affected thereby their "day in court." This concern over the due process rights of future claimants has led to the use in mass tort cases of an official future claims representative, to guard and champion those interests.⁷⁹ Moreover, scholars have cried out for amendments to the Code, specifically providing for these protections.⁸⁰ The proposal, as well as current practice, has been to treat these representatives similarly to official committees, with the expenses and professionals paid out of the estate, but the precise practice is far from solidified, and the

⁷¹ See *Babcock & Wilcox*, *supra* note 36.

⁷² Snyder and Siemer, *supra* note 19, at 369-70 (also revealing that the cost to the estate of professionals can be as high as \$50 million in a single case.)

⁷³ Carroll, et al., *supra* note 5, at 16-18.

⁷⁴ *Id.* These types of issues can be present in virtually any type of toxic tort case, such as radiation exposure and silicon implants.

⁷⁵ The subject of future claimants in bankruptcy cases can easily occupy a treatise in itself. This section is intended only as an overview, but interested

readers can look to Tung, *supra* note 5, and Jones, *supra* note 8, for additional detail.

⁷⁶ See p. 2, note 9, *infra*.

⁷⁷ See Resnick, *supra* note 10, at 2062-63.

⁷⁸ *Windsor*, 521 U.S. at 627.

⁷⁹ See *Babcock & Wilcox*, *supra* note 36.

⁸⁰ See, e.g., Jones, *supra* note 8, at 1705-1706; *Final Report of the National Bankruptcy Review Commission (Bankruptcy: The Next Twenty Years)*, 1 National Bankr. Rev. Comm'n 316 (1997). Future claims are addressed somewhat in section 524(g)

problems with future claims can have severe consequences to the legitimacy of any judicial resolution.⁸¹

Unfortunately, because it is not particularly prescribed by the Code⁸², the terms of service of the future claims representatives are somewhat left to the vagaries of the specific case, and can severely affect its efficacy. The parties who must initiate the process of appointment have one real purpose behind their motivation: to provide for due process concerns in order to bind future claimants and obtain finality.⁸³ The problem is also directly related to the fact that the principals and constituents represented are unknown – they have no ability to evaluate its performance or to address perceived shortcomings in its conduct of the case.⁸⁴

Therefore, issues such as retention of professionals, allowed costs and fees, compensation, tenure and identity all may be at the substantial discretion of these parties, at least initially and subject to court overview, and will of course affect how well the representative champions its principals. Accordingly, courts are alert for possible compromises in the representative's ability to perform its functions, and can typically be relied upon to provide some guidance to the parties⁸⁵, although the parameters arrived at can still be rather ad hoc in the absence of governing Code provisions.

6. Forgetting the usual participants? Practitioners must be extremely wary during the course of addressing the myriad of mass tort problems in bankruptcy cases, not to forget the significance and importance of the

usual participants and issues of the typical bankruptcy case. Treating those issues is beyond the scope of this paper, but an example, again from the Babcock & Wilcox case, serves well to drive the point home. There, after the filing of several competing plans and intensive negotiations with insurers and asbestos claimants conducted over the course of several years, the debtors and asbestos constituents managed to agree upon, and file, a (substantially complete) joint plan on December 19, 2002.⁸⁶ Throughout that process, general unsecured claims were considered relatively negligible, as the debtor was operating and arguably solvent, and were proposed for 100% payment in the ordinary course.⁸⁷ Unfortunately, as parties gathered for the court's hearing on approval of the disclosure statement, it was discovered that unsecured claims might in fact have grown to be in excess of \$140 million. That sum is sufficient, to say the least, to potentially affect an entire plan structure, particularly at such an inconvenient juncture.

II. IMPACT OF BANKRUPTCY ON THE LITIGATION PROCESS

Having set the stage with the major parties and actors in our mass tort Chapter 11 play, we now move to the dance itself, and a discussion of the major issues litigated in the mass tort bankruptcy, as well as the effects of a bankruptcy case on mass tort litigation.

A. The Automatic Stay

The commencement of a case (i.e., the order for relief) results in an automatic stay over a broad range of actions against the debtor and its property interests.⁸⁸ However, the automatic stay generally does not apply to third-party entities, such as insurers.⁸⁹ In

⁸¹ See *In re Kentile Floors, Inc.* (S.D. N.Y. No. 92-B-46466).

⁸² Hon. Barbara J. Houser, *Chapter 11 as a Mass Tort Solution*, 31 Loy. L. Rev. 451, 467 (1998).

⁸³ Tung, *supra* note 5, at 54, 59-65.

⁸⁴ *Id.* at 60-61.

⁸⁵ Houser, *supra* note 82, at 467, citing *In re UNR Indus.*, 46 B.R. 671 (Bankr. N.D. Ill. 1985) (specific scope of duties detailed by the court); *In re Johns-Manville Corp.*, 52 B.R. 940 (Bankr. S.D. N.Y. 1985) (creditors' committee powers granted).

⁸⁶ See *Babcock & Wilcox*, *supra* note 36 [Docket No. 3835].

⁸⁷ See *Babcock & Wilcox*, *supra* note 36, Joint Plan of Reorganization, at p. 37.

⁸⁸ 11 U.S.C. § 362.

⁸⁹ *United States v. Wright*, 57 F.3d 561, 562 (7th Cir. 1995) ("The automatic stay does not apply to guarantors, sureties, insurers, partners, and other persons liable on the

order for the stay to apply to an insurer, it must be able to claim a unity of interests or identity with the debtor.⁹⁰ Those situations are traditionally limited to affiliates, officers and directors, and entities to whom the debtor owes an "unconditional" obligation to indemnify, because in such situations, a judgment against such an entity is in effect a judgment against the debtor, and are thus very likely to impact a debtor's reorganization efforts.⁹¹

However, even though the stay does not ostensibly apply to non-debtor third-parties such as insurers, it does operate to prevent acts to obtain possession of, or to exercise control over, property of the estate.⁹² Accordingly, sections 362(a)(3) and 541 of the Code may operate to preclude recovery by tort claimants against a debtor's insurance policy, to the extent that the policy and the proceeds therefrom are property of the estate.⁹³

1. Property of the Estate - The Policy v. Proceeds Distinction. Insurance policies are generally held to be property of the estate.⁹⁴ In the absence of controlling federal law (a

compelling federal interest), state law defines property interests.⁹⁵ States differ on the issue of insurance proceeds, as do federal jurisdictions on their interpretation and application of state law. The Second Circuit for example, holds that proceeds of an insurance policy are also proceeds of the underlying property insured. Thus, where a post-petition insurance policy insures property of the estate (such as a debtor's vehicle), and such property is destroyed, giving rise to payment under the policy, then the estate may lay claim to such payment as proceeds.⁹⁶ However, the Fourth Circuit, following Virginia law, found that such proceeds were *contractual* proceeds of the policy itself, and not proceeds of the property insured, such that payments under a post-petition policy covering estate property are not within the estate. *Id.* at 364-65.

The seminal case is the Dalkon Shield case, *A.H. Robins Co. v. Piccinin*, 788 F.2d 994 (4th Cir. 1986). There, the Court discussed prior cases providing a basis for staying actions against non-debtor third parties, stating that:

There must be "unusual circumstances" and certainly "something more than the mere fact that one of the parties to the lawsuit has filed a Chapter 11 bankruptcy must be shown in order that proceedings be stayed against non-bankrupt parties." This "unusual situation," it would seem, arises when there is such identity between the debtor and the third-party defendant that the debtor may be said to be the real party defendant and that a judgment against the third-party defendant will in effect be a judgment or finding against the debtor. An illustration of such a

debt." (emphasis added)); *Reliant Energy Services, Inc. v. Enron Canada Corp.*, 2002 U.S. Dist. LEXIS 23263 at *8-9 (Bankr. S.D. Tex. 2002) ("[I]n general, protection offered by the automatic stay extends only to debtors, not to non-debtor third parties such as insurers, co-defendants, or guarantors."); *Carway v. Progressive County Mut. Ins. Co.*, 183 B.R. 769, (N.D. Tex. 1995) (the automatic stay "generally does not extend to non-debtors such as insurers and co-defendants").

⁹⁰ *In re S.I. Acquisition, Inc.*, 817 F.2d 1142, 1148 (5th Cir. 1987).

⁹¹ *A.H. Robins Co.*, 788 F.2d 994 (4th Cir. 1986); *In re Babcock & Wilcox Co.*, 2001 U.S. Dist. LEXIS 6792, *10-11 (E.D. La. 2001).

⁹² 11 U.S.C. § 362(a)(3).

⁹³ Section 541 defines property of the estate, and does so extremely broadly. *In re Edgeworth*, 993 F.2d 51, 55 (5th Cir. 1993).

⁹⁴ See, e.g., *In re Minoco*, 799 F.2d 517, 518-19 (9th Cir. 1986).

⁹⁵ *American Bankers Ins. Co. v. Maness*, 101 F.3d 358, 363 (4th Cir. 1996).

⁹⁶ *Id.* at 363-64.

situation would be a suit against a third-party who is entitled to absolute indemnity by the debtor on account of any judgment that might result against them in the case. To refuse application of the statutory stay in that case would defeat the very purpose and intent of the statute.⁹⁷

In the indemnity context, liability found against the co-debtor might substantially be imputed to the debtor despite its non-involvement in the initial suit and additional considerations include the possibility of inconsistent judgments.⁹⁸ One key then is the jurisdiction of the bankruptcy court to issue a stay order (injunction) against such a suit, based upon its effect on the administration of the estate or upon estate property.⁹⁹ Still, those prior cases discussed by the *A.H. Robins* Court dealt primarily with indemnity obligations of the debtor itself, and are not expressly applicable to facts involving suits against non-debtor third parties who are covered under a debtor's insurance policy.

A.H. Robins did deal with suits involving a debtor's insurer, and specifically involved suits against a debtor's officers, directors and insurer. As is common, the former parties were entitled to indemnification by the debtor under its charter and state laws, and were

additional co-insureds under its policy.¹⁰⁰ It follows a prior line of cases in stating that, because insurance policies are unquestionably estate property, that "any action 'related to' bankruptcy proceedings against the insurer or against officers or employees of the debtor are unquestionably stayed under section 362(a)(3)."¹⁰¹ In those contexts, it makes sense for one court (the bankruptcy court) to administer the liquidation of all claims which may deplete the insurance policy coverage, and this is especially true in cases involving alleged mass tort and products liability – cases where insurance policies constitute critical estate assets. Moreover, as before, there are concerns with imputed liability notwithstanding that the debtor is not party to a suit, for a judgment against its employees may under certain circumstances result in preclusion in a subsequent proceeding.¹⁰²

However, because it is predicated on "related to" jurisdiction and an impact upon estate property and administration, the holding is limited to actions in which the judgment may diminish the asset of the estate.¹⁰³ In other words, if the insurance coverage is sufficient to cover all anticipated claims and there is no substantial question as to coverage, then a supplemental stay is not proper because a judgment against the insurer and third-party employee would have no impact upon the debtor's estate.

The *A.H. Robins* Court provides several bases for the issuance of a stay in favor of a non-debtor stay order: (i) section 362(a)(1) and (3); (ii) section 105; and (iii) the jurisdictional grant of 28 U.S.C. § 1334 and the inherent equitable powers of courts to efficiently manage judicial resources and grant relief.¹⁰⁴ Not all such provisions are

⁹⁷ *A.H. Robins Co.*, 788 F.2d at 999 (citations omitted). See also *E.I. Du Pont Nemours & Company v. Fine Arts Reproduction Company, Inc.*, 1995 U.S. Dist. LEXIS 7040, *5-6 (S.D. N.Y. 1995); *Holland v. High Power Energy*, 248 B.R. 53, 57-58 (S.D. W.Va. 2000). But see *Duval v. Gleason*, 1990 U.S. Dist. LEXIS 18398, *11 (N.D. Ca. 1990) ("The Ninth Circuit, however, has yet to recognize the....'unusual circumstances' exception...");

⁹⁸ *A.H. Robins Co.*, 788 F.2d at 999-1001.

⁹⁹ *Id.* at 1001. The *A.H. Robins* Court also contains helpful detail on procedures for obtaining a supplementary stay order or injunction. See *Id.* at 996-99.

¹⁰⁰ *Id.* at 1007.

¹⁰¹ *Id.* at 1001-03.

¹⁰² *Id.* at 1005; Marcus, *supra* note 4, at 473-74.

¹⁰³ *A.H. Robins Co.*, 788 F.2d at 1001-02. Section 362(a)(3) relates to any act to obtain possession, or exercise control, over property of or from the estate.

¹⁰⁴ *Id.* at 1004. Cf. *In re Lowenschuss*, 67 F.3d 1394 (9th Cir. 1995) (section 105 is

implicated in any given situation. Moreover, under the third (iii) basis, an additional standard applies: the court must conduct a balancing inquiry and justify the stay by clear and convincing circumstances outweighing the potential harm to the party enjoined. Moreover, because the context involves injunctive relief, the party requesting such relief should be prepared to address the requirements for preliminary injunctions. For example, the *A.H. Robins* Court discussed that: (i) irreparable harm to the estates would occur (collateral effects and reduction of available coverage); (ii) the debtor had nearly a certain likelihood of success (on the merits of the injunctive action); and (iii) the burden on the plaintiffs was outweighed by the hardships threatened to the estates and by the public policy in favor of reorganization.¹⁰⁵ In *In re Titan Energy, Inc.*, 837 F.2d 325 (8th Cir. 1988), a purchaser of several methanol plants sought recovery under an insurance policy of the debtor from whom the purchaser acquired the plants. The court noted that "co-defendants and insurers are not the intended beneficiaries of the automatic stay granted to the reorganizing debtor."¹⁰⁶ However, the court qualified this statement in a footnote stating:

Technically, our determination that the policies are property of Titan's estate triggers the automatic stay provision of 11 U.S.C. § 362, which prohibits any action against a debtor's property. However, subsection (d) allows the bankruptcy court to lift the stay "on request of a party in interest and after notice and a hearing." As our abstention discussion makes clear, following a proper motion and hearing, we would consider the bankruptcy court's

insufficient to override the specific limitations of section 524(e).
¹⁰⁵ *A.H. Robins Co.*, 788 F.2d at 1008.
¹⁰⁶ *Titan Energy*, 837 F.2d at 334.

grant of a motion to lift the stay entirely appropriate.¹⁰⁷

a. The Fifth Circuit. The Fifth Circuit has approvingly cited to *A.H. Robins* and likewise has confirmed that insurance policies are generally considered property of the estate.¹⁰⁸ However, this does not end the inquiry. As the *Titan Energy* Court explained above, this may be a technical point which the bankruptcy court can easily address by granting stay relief. The justification for such relief will depend upon the issue of whether the proceeds under the policy, those payments that the insurer would make pursuant thereto, are also considered property of the estate.

Under Fifth Circuit case law, this issue is somewhat muddled, but generally depends on the nature of the insurance policy.¹⁰⁹ Specifically:

The overriding question when determining whether insurance proceeds are property of the estate is whether the debtor would have a right to receive and keep those proceeds when the insurer paid on a claim. When a payment by the insurer cannot inure to the debtor's pecuniary benefit, then that payment should neither enhance nor decrease the bankruptcy estate. In other words, when the debtor has no legally cognizable claim to the insurance proceeds, those proceeds are not property of the estate.¹¹⁰

¹⁰⁷ *Id.*
¹⁰⁸ *Arnold v. Garlock, Inc.*, 278 F.3d 426, 436 (5th Cir. 2001); *In re Vitek, Inc.*, 51 F.3d 530, 533 (5th Cir. 1995). *Edgeworth*, 993 F.2d at 55; *Babcock & Wilcox*, 2001 U.S. Dist. LEXIS 6792, at *13.
¹⁰⁹ *In re Louisiana World Exposition, Inc.*, 832 F.2d 1391, 1399 (5th Cir. 1987).
¹¹⁰ *Edgeworth*, 993 F.2d at 55.

For example, under casualty, collision, fire, and life insurance policies, where the debtor is the beneficiary, it has such a right to payment. On the other side of the spectrum, under director and officer liability policies, the debtor company obtains the policy in its name but purely to indemnify its management, for the benefit of those aggrieved by their actions. The company itself has neither a right to the proceeds, nor a right to indemnification.

Between these extremes lie general commercial liability policies, to which parties look for the satisfaction of mass tort claims. There, the debtor's status as the insured does not entitle it to the receipt of payments. Rather, these policies are intended to benefit the victims of the debtor's actions.¹¹¹

Thus, it appears that, while Fifth Circuit courts accept the *A.H. Robins* holding, they substantially narrow its application. Under these authorities, it must be found that the Debtor has a direct right to the insurance proceeds at issue (is a covered insured), and specifically, would have a right to retain the payments made by the insurer.¹¹² In *In re Zale Corp.*, 62 F.3d 746, 761, n. 45 (5th Cir. 1998), the Court further noted that temporary injunctions in favor of third parties may be proper under the alternative ground that the third party action would have an adverse impact on the debtor's ability to reorganize.

In the context of commercial liability policies with multiple insureds, the benefits which the debtor derives are not impacted by suits against unrelated co-insureds seeking policy proceeds. The liabilities and resources involved are not those of the debtor. Accordingly, the proceeds of the policy are not property of the estate, even though the policy itself technically is. In other words, courts will weigh this distinction heavily, because where the proceeds are not property of the estate, a debtor has no right to them,

and should accordingly have no right to impair their payment.¹¹³

There are, however, situations involving liability policies where permitting suit against non-debtor co-insureds could conceivably prejudice a debtor, such as where it has some substantial need for significantly limited insurance coverage. In the context of mass torts, this is almost always the case. Absent such concerns, notwithstanding that a policy is property of the debtor, and thus protected by the automatic stay, the policy and/or the proceeds can be bifurcated as to the debtor's and other co-insured's respective interests.¹¹⁴ The possibility of such bifurcation substantially strengthens a plaintiff's case for relief from the automatic stay because the impact upon the debtor and its prospects for reorganization are negligible, if any.

However, where there is an issue as to whether the policy proceeds are sufficient to cover the claims which may be asserted against it, claims in excess of policy limits "spill-over" as claims against the estate itself.

2. Third Party Protections. These considerations of indemnity, contribution (substantial identity) and claims asserted against an insurance policy, which substantially exceed coverage, are among the group of "unusual circumstances" which *A.H. Robins* promulgated and which courts

¹¹¹ *Id.* at 56; *Babcock & Wilcox*, 2001 U.S. Dist. LEXIS 6792, at *14-15.

¹¹² *See Babcock & Wilcox*, 2001 U.S. Dist. LEXIS 6792, at *10-16.

¹¹³ *Louisiana World Expo.*, 832 F.2d at 1399. It should be noted that, in light of the conceptual uncertainties attendant to this policy/proceeds distinction, the Fifth Circuit has recently questioned its value. *Vitek*, 51 F.3d at 530. However, the *Vitek* Court was careful to very narrowly limit the precedential value of the opinion to future Chapter 11 cases. *Id.* at 533 n. 3. The author also cautions that, in light of the possibility of sanctions for violations of the stay, it is always good practice to seek the advance authorization of the court to proceed with litigation, notwithstanding an attorney's determination that an act against an insurance policy is not subject to the stay.

¹¹⁴ *See In re Spaulding Composites Co., Inc.*, 207 B.R. 899, 907 (9th Cir. B.A.P. 1997).

typically require in order to *extend* the automatic stay to enjoin actions against non-debtors.¹¹⁵ Such relief requires findings of at least: (i) essential identity (that liability against the defendant would essentially, "automatically" translate into the liability of the debtor); and (ii) prejudicial impact upon reorganization efforts. Moreover, these "unusual" situations are not unusual in mass tort cases. They *typically* occur in cases involving such liabilities, where a debtor is faced with scores of claims for which insurance coverage constitutes the critical pool of assets.

It is easy to see how piecemeal suits against non-debtor co-insureds in such situations can threaten a debtor's prospects for reorganization because they deplete a limited and critical resource of the estate needed for the satisfaction of liabilities which typically are the main precipitating factor for the bankruptcy case itself. As to any given policy, factors may include (in addition to the type of coverage) the relevant years and limits of coverage, and the estimated claimants and liabilities against it. Clearly, where a debtor must largely rely upon limited insurance coverage to satisfy the claims of a dominating class of creditors, depletion of those resources severely threatens its prospects for rehabilitation and unsurprisingly, justifies the protection of the stay.

So long as these issues are not present, courts can either bifurcate the respective interests in the policy and the proceeds, or simply hold that a non-debtor co-insured's interests in a policy (and proceeds paid on account thereof) are not property of the estate under section 541.¹¹⁶

As noted, in the mass tort bankruptcy these issues are almost always present, thereby maximizing the court's ability to bring the full limit of the policy, as well as co-insureds and insurers, under the protection of the automatic stay.

¹¹⁵ *In re Babcock & Wilcox Co.*, 2001 U.S. Dist. LEXIS 6792, at *18-19.

¹¹⁶ *Spaulding Composites*, 207 B.R. 899 at 907.

B. Select Additional Insurance Policy Issues

1. Insurance Policies as Executory Contracts. Executory contracts are governed by section 365 of the Code and are generally recognized as contract on which material performance (other than the mere payment of money) remains for both sides such that a breach by one would excuse performance by the other.¹¹⁷ Policies viewed as executory contracts may help insurers because section 365 contains beneficial requirements in order for a debtor-in-possession to assume the contract. These include the (assurance of) prompt cure of all defaults, performance of all obligations under the policy, a reaffirmation or reinstatement of the insurer's full range of rights under the policy, and a restriction against any modification of its terms by the debtor.¹¹⁸

Such requirements are extremely significant to the insurer, for they would cover the many significant aspects of the policy, including duties of cooperation, and rights to terminate, as well as the policy's procedure under which claims are to be addressed.¹¹⁹ However, even if the contract is not held to be executory, the policy's terms are generally not affected.¹²⁰

2. Coverage actions. One extremely common proceeding in mass tort bankruptcy cases is the coverage action, under which the insurer, or another party, seeks the court's declaratory judgment as to the parties' respective rights and duties. These disputes frequently provide the setting in which an estate's settlements with insurers, and the implementation of releases and third party injunctions thereunder, will be arrived at, which perhaps explains their frequency in

¹¹⁷ *In re Bradlees Stores, Inc.*, 2001 U.S. Dist. LEXIS 14755, *19-23 (S.D. N.Y. 2001).

¹¹⁸ This last requirement is also known as the cum onere principle.

¹¹⁹ Goldberger, *supra* note 1, at 5.

¹²⁰ *Id.*; Annette v. Jarvis and Kenneth L. Cannon, II, *Liability Insurance Settlements in Mass Tort Bankruptcy Cases*, 41 Fed. Bar News & J., Mar.-Apr. 1994, at 204-05.

mass tort cases.¹²¹ In fact, as one court has put it, a coverage dispute may be "the linchpin" of a mass tort debtor's plan.¹²²

a. Jurisdiction. Because of the significance and prevalence of coverage suits to a mass tort bankruptcy case, debtors will naturally seek to have the bankruptcy court, often perceived as pro-debtor, entertain them. Federal district courts (of which bankruptcy courts are adjuncts), have jurisdiction over all cases arising in, or related to, a bankruptcy case.¹²³ "Related to" jurisdiction is extremely broad, can include any proceeding that might "conceivably" have an effect on the bankruptcy estate¹²⁴, and includes coverage disputes between the debtor and insurer.¹²⁵ Insurers have in the past (unsuccessfully) sought to use possible interference with a coverage dispute as a basis for enjoining actions asserted by claimants directly against the insurer.¹²⁶

Still, the possibility of jurisdiction, especially over suits exclusively involving non-debtor parties, does not necessarily mean that the court will *retain* jurisdiction. The foregoing authorities must be read in conjunction with additional statutes relating to abstention, and defining "core v. non-core" matters in bankruptcy cases.¹²⁷ Abstention is strongest where a suit involves two non-debtor parties, and where the subject matter of the suit relates primarily to non-federal claims and law.¹²⁸ There is also a distinction between mandatory and permissive abstention. Mandatory abstention does not apply in personal injury tort cases, but does apply where the subject matter of a suit is purely a state law question and the acts complained of arose pre-petition.¹²⁹ Barring these, a bankruptcy court might abstain in the interests of comity, or in deference to a state's opportunity to decide an unsettled question of state law.¹³⁰

b. Coverage settlements. Despite the significant legal questions which have been answered in the context of coverage actions,¹³¹ scholars are quick to point out that they also serve the important function of providing a forum for negotiations between the debtor insured and the insurer in structuring a plan. Specifically, for the insurer it is an opportunity to demand "global peace" and third party releases in connection with the

¹²¹ Ralph Brubaker, *Nondebtor Releases and Injunctions in Chapter 11: Revisiting Jurisdictional Precepts and the Forgotten Callaway v. Benton Case*, 72 Am. Bankr. L.J. 1, 3 (1998).

¹²² *In re Celotex Corp.*, 140 B.R. 912, 915 (M.D. Fla. 1992).

¹²³ 28 U.S.C. § 1334.

¹²⁴ *Pacor v. Higgins*, 743 F.2d 984, 994 (3rd Cir. 1984). Cf. *In re Xonics, Inc.*, 813 F.2d 127, 131 (7th Cir. 1987)(the cognizable effect is limited to an effect upon distribution.).

¹²⁵ *In re U.S. Brass Corp.*, 110 F.3d 1261 (7th Cir. 1991). Note also that bankruptcy court jurisdiction may be found over suits between insurers and non-debtors as well, under the same rationale of the possible effect on assets available for distribution. *In re Dow Corning Corp.*, 86 F.3d 482 (6th Cir. 1996). Recall also our discussion of extensions of the automatic stay under a similar reasoning, at Art. II.A, *infra*.

¹²⁶ *Safeco Ins. Co. of Am. v. Norris & Hirshberg, Inc.*, 640 F. Supp. 712, 715-16 (N.D. Ga. 1986) (suit by injured party against insured could not be enjoined in aid of jurisdiction over insurance coverage suit between insurer and insured); *Pacific Indem. Co. v. Acel Delivery Serv., Inc.*,

432 F.2d 952, 954-56 (5th Cir. 1970) (same).

¹²⁷ See 28 U.S.C. § 1334(c)(abstention); 28 U.S.C. § 157(b) (core matters).

¹²⁸ Robert B. Miller and Mark D. Plevin, *Insurance Coverage in the New Millennium*, 4 ALI – ABA 79, 87-88 (Course of Study, Oct. 11-12, 2001, available at web2.westlaw.com)

¹²⁹ 28 U.S.C. § 157(b)(4) and (5); 28 U.S.C. § 1334(c)(2).

¹³⁰ *Id.*

¹³¹ See Harvey J. Kesner, *Future Asbestos Related Litigants as Holders of Statutory Claims Under Chapter 11 of the Bankruptcy Code and Their Place in the Johns-Manville Reorganization*, 62 Am. Bankr. L.J. 69, 70-71 (1988).

settlement.¹³² For the debtor and asbestos claimants, it of course resolves the primary issue of whether and what amount of insurance policy proceeds can be committed to the plan (trust) and provides significant comfort in the knowledge of presently available cash.

There are two basic types of insurance coverage settlements, "cash-out" settlements and the "coverage in place" settlements.¹³³ In the "cash-out" or "policy buy-back" scenario, the insurer pays a lump sum in exchange for a release of all further obligations in connection with the policy.¹³⁴ In the "in-place" settlement model, the insurer typically waives all defenses to coverage in exchange for a reduced policy limit, and the policy remains in force to be administered under its terms (the insurer will remain involved, typically with the trust, in claims evaluation and processing).¹³⁵ Factors influencing the amount paid in settlement, and the determination of whether to settle at all, naturally include the strength of the insurer's potential coverage defenses, the limits of liability, projected defense costs, the way in which the policy structures these (whether defense costs are included in limits), and even the cost of litigation to the estate. Additionally, if the settlement is coverage in place, the parties should know whether and what costs of administering the claims trust will be chargeable against the insurer's defense obligations.

Because of the impact of the settlement upon other potentially non-settling parties, such as the tort claimants, co-insureds and excess insurers, the settling parties must take great care to consider the structuring of the settlement and its impact on these other parties. We have already addressed the clout that co-insureds can wield in objecting to settlements. Another

concern is the duty of good faith that an insurer typically owes to its insured under state law, and excess insurers might also assert bad faith claims with respect to settlements of insurance at lower layers. Accordingly, the insurer must be extremely cautious and meticulous in its conduct of a coverage suit and a finding of good faith should be incorporated into the approval order issued by the court.¹³⁶

It is also critical to the insurer to incorporate its settlement into the plan if the settlement is arrived at prior to confirmation.¹³⁷ If not, it is important to attempt to "pave the way" for the settlement in the plan. This is because a settlement order will not have the breadth and import that the channeling third party injunction will have, and that relief (together with a ruling that the policy is not unlimited) that is paramount to the interests of the insurer.¹³⁸

III. THE PLAN PROCESS

Following the settlement of coverage issues, parties set their sights on the plan process and obtaining confirmation. We begin with a most troubling mass tort plan issue: claims estimation.

A. Determining the Span of Liabilities

Claims estimation can be a mammoth issue in mass tort bankruptcy cases. The issue of future claimants, or latency in the

¹³² See *In re Dow Corning*, 198 B.R. 214 (Bankr. E.D. Mich. 1996); Marcus, *supra* note 4, at 474.

¹³³ Miller and Plevin, *supra* note 128, at 90-91.

¹³⁴ Goldberger, *supra* note 1, at 9.

¹³⁵ *Id.*

¹³⁶ Miller and Plevin, *supra* note 128, at 91-92. Bankruptcy jurisprudence has its own requirements for settlements under Federal Rule of Bankruptcy Procedure 9019. These may generally be approved if they are found to be "fair and equitable." That standard includes factors such as: (i) the probability of success in the litigation, with due consideration for the uncertainty in fact and law; (2) the complexity, expense and likely inconvenience and delay of the litigation; and (3) all other factors bearing on the wisdom of the compromise (including good faith). *In re Cajun Elec. Power Co-op., Inc.*, 119 F.3d 349, 356 (5th Cir. 1997).

¹³⁷ Goldberger, *supra* note 1, at 10.

¹³⁸ *Id.*

manifestation of injuries legally caused in the past, makes the estimation of the eventual extent of damage extremely difficult. As uncertain as tort awards in litigation can be, the estimation process in bankruptcy can be exacerbated by the need to account for unimpaired claims.

As an example of the difficulties in mass tort claims estimation, the Johns-Manville trust, despite being funded with approximately \$3 billion at the outset, and employing significant cost controls and distribution ratios began paying claims in 1988 at a rate of about 40,000 per claimant (the then-stated liquidated value of the average claim).¹³⁹ By 1990, operations were suspended. Resuming in 1995, they were again suspended in 2001 and the projected rate of distributions is now at 1-8% of liquidated value.¹⁴⁰

The bankruptcy court is required in any bankruptcy case to estimate, for purposes of allowance, the amount of any contingent or unliquidated claim.¹⁴¹ These naturally include future mass tort claims.¹⁴² In addition to the dictates of the Code itself, estimation is critical to the plan formulation and confirmation processes (determination of feasibility)¹⁴³, as well as to the determination required by section 524(g)(4)(B)(ii) that the trust proposed in a plan is fair and equitable.

Despite these considerations, the Code gives no guidance as to how this estimation process should be conducted, and case law has generally relied upon a case by case resolution.¹⁴⁴ In practice, courts in mass

tort bankruptcy cases have tended towards a "summary trial" method.¹⁴⁵ The bankruptcy court will conduct an abbreviated evidentiary hearing using customary burdens of proof. The evidence however, is not conducive to a summary trial. The court will weigh the testimony and reports of health, industry, and medical experts, and will often have to factor in business and "spread" considerations, such as the number of products, extent of dissemination, market share, per unit degree of the injury causing element in the product, as well as historical figures (adjusted for inflation) and statistical data which can shed light on the debtor's past liabilities, as well as those of similarly situated companies.¹⁴⁶

There are other models which the court is free to utilize as well:

- The face value model – the court simply utilizes the proof of claim amount;
- The zero value model – the Court estimates the claim at a zero or nominal amount, simply allowing for participation;¹⁴⁷
- The market theory model – the Court attempts to assign a value that a hypothetical market would assign to the claim;

personal injury and wrongful death claims is not within the bankruptcy court's core jurisdiction, accordingly, estimation for purposes of distribution, unless settled, must typically be conducted in the district court. Houser, *supra* note 82, at 468.

Hodara and Stark, *supra* note 26, at 396. *Id.* at 396-98.

This particular model is resorted to under specific circumstances where the dollar amount of each individual claim is not necessary to the objective and where completing an estimation of individual claims is particularly burdensome or impractical. For example, where the universe of aggregate claims in a class has already been determined (estimated), a court may be less concerned with the exact dollar amount of each individual claim. In that context, allowing the claims to allow the individual claimants to participate in the process is of paramount concern. Houser, *supra* note 82, at 470.

¹³⁹ Michelle J. White, *Why the Asbestos Genie Won't Stay in the Bankruptcy Bottle*, at p. 5-6 (Presented at the Univ. of Cincinnati College of Law Conference, Mar. 2 2002) (available at www.econ.ucsd.edu/~miwhite/asb-bank.pdf).

¹⁴⁰ *Id.*

¹⁴¹ 11 U.S.C. § 502(c)(1).

¹⁴² See, e.g., *In re Eagle-Picher Indus., Inc.*, 189 B.R. 681, 683 ((Bankr. S.D. Ohio 1995).

¹⁴³ See *In re MacDonald*, 128 B.R. 161, 164 (Bankr. W.D. Tex. 1991).

¹⁴⁴ 5 *Collier on Bankruptcy* at ¶ 502.04[2]. Recall also that the adjudication of

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- The forced settlement model – the Court sets the claim within the range that the parties would be willing to accept in a hypothetical settlement; and
- The discounted value model – the Court takes the face value of the claim and multiplies it by the percentage likelihood that the claimant would prevail on its claims under state law.

Clearly, the method utilized by bankruptcy courts can vary widely.¹⁴⁸ Even under the trust distribution model, where the liquidation of specific claims will be through a trust, because the aggregate universe of mass tort claims of course affects feasibility and fairness determinations, the bankruptcy court must still engage in this activity. Moreover, courts have differed not only on the proper method of claims estimation, but also on its effect.¹⁴⁹

These effects of estimation can conflict with the rationale behind estimation. While estimation is not thought to require a full blown trial, estimation can clearly affect a tort claimant's substantive rights. There is something incongruous with the notion that a bankruptcy case can effectively liquidate the aggregate cap of all mass tort claims against a debtor without conducting any sort of trial, examining witnesses, or affording plaintiffs the range of due process protections generally recognized.¹⁵⁰ To make matters worse, there are particular difficulties in estimating mass tort claims which have not manifested and are highly speculative.¹⁵¹

¹⁴⁸ *Id.* at 469-470.
¹⁴⁹ *Id.* at 469 n. 98 (explaining that courts have differed on whether estimation results in a cap on distributions, or simply for voting purposes.) *citing In re Poole Funeral Chapel, Inc.*, 63 B.R. 527, 532 (Bankr. N.D. Ala. 1986); *In re MCorp Fin., Inc.*, 137 B.R. 219, 226 (Bankr. S.D. Tex. 1992).
¹⁵⁰ Jones, *supra* note 8, at 1714-15.
¹⁵¹ *Id.* at 1716. Noting that in the Dow Corning case, experts disagreed on the range of aggregate future claims by almost 1200%.

Fortunately, the problem is somewhat mitigated by the fact that estimation in mass tort bankruptcy cases is rarely litigated to conclusion.¹⁵² Instead, as we have indicated throughout, the process is heavily controlled by, and geared towards, negotiations and a hopefully consensual resolution. This resolution may be a slow process in mass tort bankruptcies, but that is not to say that the litigation conducted prior to arriving at a settlement is necessarily wasteful. Earlier stages of litigation may serve to narrow and determine significant issues and provide for a more definitive assessment of liability by the parties.

B. Class Votes

In light of the incidence and significance of settlements and other negotiations entered into by various players in the mass tort bankruptcy, the rather novel issue of class votes deserves some attention. In this context, "class" refers not simply to a class of claims under a plan, but to a class of claimants, such as in a certified class action under Fed. R. Civ. P. 23.

The party which arrives at an agreement involving a pledge of support for the plan with the representative(s) of the class (such as an insurer or debtor), will want some assurances that the representative can in fact cause all, or at least substantially all, of the critical class votes to be cast in accordance with that understanding. The consent of the class of mass tort claimants will be, after all, critical to confirmation. In the typical chapter 11 scenario, however, claims and plan votes are submitted on an individual basis, and this tension raises the issue of class voting, i.e., whether a class representative can be allowed to vote on behalf of all of its constituents.

a. **Class Proofs.** It should first be noted that a precursor to the issue of class voting is that of class proofs of claims. Not all Circuits allow such a class proof, but while this refusal was once prevalent¹⁵³, the majority trend is

¹⁵² Snyder and Siemer, *supra* note 19, at 370.
¹⁵³ *See Dade County Sch. Dist. v. Johns-Manville Corp.*, 53 B.R. 346, 351 (Bankr.

strongly in the direction of allowing such proofs and accommodating class actions in bankruptcy.¹⁵⁴ The early rationale was that the sanctity of bankruptcy claims bar dates is highly regarded, and allowing one representative to file a claim on behalf of thousands of principals, allows those underlying individuals to escape the purview of bar dates.¹⁵⁵

Courts have somewhat tempered the modern trend with a logical distinction drawn upon the issue of certification. Specifically, where a class has previously been certified, there has already been a judicial determination of the representative's status, and in such circumstances, it makes sense to allow the representative to guard those interests. The *Mortgage & Realty* case, in accordance with the majority, explained that certification under Rule 23 is a prerequisite to accepting the class representative(s) as the agent(s) of the individual creditors in the class.¹⁵⁶ As to timing, it is unclear whether certification is required prior to the filing of a

class proof, or if it is sufficient if the certification were granted upon an objection to the claim, such as to "ratify" the filing.

Unfortunately, a determination of certification does not end the class voting issue in bankruptcy. The possibility of class proofs, one claim filed for hundreds or thousands of claimants, raises another issue in connection with class votes. How is/are the vote(s) to be counted? If the certified class, a legally recognized entity, is viewed as the claimant, then perhaps it should be entitled to only one vote. Alternatively, the class may be certified, yet this could have occurred after the filing of individual votes by its constituents. Can the representative then vote for all such claims? There is very little case law on the exact issue of class voting tabulation.

Courts have generally answered the question by holding that the representative can vote on behalf of its constituents, but that in the event that an individual claimant casts its own dissenting vote, that vote must trump the class vote and be counted as cast.¹⁵⁷ Although addressing the issue in only cursory fashion, the *Mortgage & Realty* Court clearly accepted that votes would be counted in accordance with the number of individual class member creditors, by discussing the plan tabulation totals and the effects of dissenting votes filed by individual class members.¹⁵⁸ Importantly, the Court noted that although class representatives could vote for the entire class, that the policies

S.D.N.Y. 1985) ("Voting on a reorganization plan and distributions under the plan are made on the basis of individual claims and individual claimants.")

¹⁵⁴ Cf. *In re Standard Metals Corp.*, 817 F.2d 625, 630 (10th Cir. 1987) (class proofs not consistent with the Code), *vacated and rev'd in part on other grounds sub. nom., Sheftelman v. Standard Metals, Corp.*, 839 F.2d 1383 (10th Cir. 1987); with *In re Charter Co.*, 876 F.2d 866, 873 (11th Cir. 1989) (class proofs allowed); and *In re Mortgage & Realty Trust*, 125 B.R. 575, 579 (C.D. Ca. 1991).

¹⁵⁵ *In re Texaco, Inc.*, 81 B.R. 820 (Bankr. S.D. N.Y. 1988). Courts disallowing class proofs also rely upon section 501 of the Code, which sets forth certain representatives allowed to file claims for others, reasoning that the list is exclusive. See Jay D. Sanders, *The Permissibility of Class Proofs of Claims in Bankruptcy*, 1997 ABI JNL. LEXIS 262, *2 (Apr. 1997).

¹⁵⁶ *Mortgage & Realty*, 125 B.R. at 579. Note that Fed. R. Bankr. P. incorporates Rule 23.

¹⁵⁷ See, e.g., *In re American Family Enters.*, 256 B.R. 377, 404 n. 20 (D. N.J. 2000) ("The Class Representatives, acting through Lead Counsel, may vote on behalf of all Class Members who have not voted individually to accept or reject the Plan."). Cf. *In re Trebol Motors Distrib.*, 220 B.R. 500 (1st Cir. B.A.P. 1998). Although holding that a previously certified class could file a single claim because the class itself held the claim, this case did not address voting. However, in the course of its discussion, the court stated: "As we have held that a previously certified class is a single claimant..." *Id.* at 503.

¹⁵⁸ *Mortgage & Realty*, 125 B.R. at 583 n. 18.

underlying allowing such action must give way to those providing for individual participation in bankruptcy cases. Therefore, in the event that individual class members chose to vote on the plan, those votes would have to be counted as they were submitted, with the class representatives able to vote for the remainder.¹⁵⁹

IV. REFORM – LOOKING FORWARD

In light of the staggering systemic costs of mass tort cases, their continued prevalence, the growing use of bankruptcy proceedings to address these liabilities, and the many unresolved issues attendant to that approach, we take a moment now to provide a synopsis of reform.

A. Tort Reform

In doing so, it should be recognized that many of the problems dealing with mass tort litigation are endemic to tort, and not bankruptcy, law. These problems may require a more fundamental legislative reform outside of the provisions of the Code.

Just recently, on April 7, 2003, the Supreme Court issued a very significant opinion in the case of *State Farm Mutual Automobile Insurance Co. v. Campbell*, in which it overturned a punitive damage award of \$145 million (in comparison with a \$1 million compensatory damages award) imposed against an insurer.¹⁶⁰ In the majority opinion, Justice Stevens wrote that the ratio of punitive to compensatory damages should rarely exceed single digits, and often should not be in excess of 1 to 1. This is in sharp contrast to the high-end historic range, as great as 400 or 500 to 1. The Court

¹⁵⁹ *Id.* at 583. This issue makes clear the Court's recognition that class members receive individual recognition for voting tabulation purposes. The individually cast votes constituted the critical margin for whether the plan class had accepted or rejected the plan.

¹⁶⁰ Case No. 01-1289. Tony Mauro, *High Court Puts the Brakes on Large Punitives*, American Media Lawyer (Apr. 8, 2003) (available at bkinformation.com)

additionally explained that a defendants' wealth is an insufficient basis to overcome an unconstitutional punitive damage award.¹⁶¹

While this ruling is extremely significant, it is tempered by the continued progression of verdicts handed down in favor of asbestos related plaintiffs. Two verdicts totaling almost \$300 million were reached in the past month against defendants who did not manufacture asbestos but exposed workers to asbestos containing products, and the Supreme Court itself has recently ruled that railroad employees suffering from asbestosis can sue for "genuine and serious" fears of cancer.¹⁶² Each of these rulings appears to involve victims of bona fide, documented injuries. They underscore the possibility that a "race to the courthouse" will endanger future claimants' abilities to receive reasonably equivalent treatment as large awards push defendants closer to insolvency.

Other possible reforms currently being considered by Congress include the creation of an asbestos court, the standardization of medical standards, and the creation of official trust funds, but it remains to be seen whether any of these options can gain sufficient momentum in the face of opposition by the plaintiffs' bar.¹⁶³

B. Broadening and Relaxing Section 524(g)

We have seen that one glaring issue with section 524(g) is that it is expressly limited to asbestos liabilities, yet the third party injunctions and releases it utilizes have

¹⁶¹ *Id.* Several Justices dissented, including Justice Ginsburg, on the basis that the ruling must come from state authorities, as well as Justices Scalia and Thomas, arguing that the Constitution could not be read to limit punitive damages.

¹⁶² Peter Page, *Asbestos Exposure Cases Draw Big Awards*, The National Law Journal (April 10, 2003) (available at bkinformation.com); Tony Mauro, *Supreme Court Gives Boost to Those Claiming Asbestos Injury*, American Media Lawyer (Mar. 11, 2003) (available at www.law.com).

¹⁶³ *Asbestos Games*, *supra* note 7.

been accepted by bankruptcy courts under different scenarios, and are crucial incentives to insurers and contributing affiliates in any mass tort bankruptcy case. An easy solution would be to vary the requirements under section 524(g) to cover these instances and allow parties to avail themselves of its provisions. The National Bankruptcy Review Commission proposed as much in its 1997 report, arguing for: (i) the incorporation of a definition of mass future claims that is not limited to asbestos claims (which could then be used to trigger section 524(g)); (ii) the express recognition of channeling injunctions; and (iii) the express authorization for the bankruptcy court to approve sales of assets "free and clear" of (successor) liabilities.¹⁶⁴

C. Incorporate the Class Action

While some scholars, and the Supreme Court, have indicated that mass torts may not be conducive to class actions, and while still others urge an end to joinder and mass trials, it makes sense to incorporate class actions into the Code. The lack of guidance in this area can be addressed with a few short, minor amendments, such as the requirement of certification, allowing class representatives (once certified) to file claims, and specifying the Code's stance on voting and tabulation. Simply put, there is no need for inconsistency among jurisdictions in this regard.

D. Chapter 14?

It may even make sense to craft a wholesale change to the Code, incorporating a specific chapter for these cases. Those who disagree with Code reform to accommodate mass tort cases argue that the Code is not intended to address them. A separate chapter could address that concern. After all, scholars have argued that Chapter 11 specifically is needlessly disruptive to the

otherwise solvent company that needs only address mass tort liabilities.¹⁶⁵

V. CONCLUSION

Ultimately, the contours of this problem suggest that, perhaps more important than the specific solutions, some type of reform is needed yet has not occurred. Perhaps one reason is that the problem is still developing, and we are just now discovering the true weight of its systemic consequences. The perception that asbestos cases were a discreet phenomenon that will eventually diminish has not proven accurate. Whether the solutions are through legislation or the Courts, it is clear that mass torts will be a continuing issue for our legal and social system.

Regardless, it is now clear that there will be no diminishing trend absent reform, because asbestos cases have not diminished. Even if they someday do decline, the plaintiffs' bar has shown remarkable resilience and ingenuity in finding additional claimants and defendants to fuel the mass tort machine. They have ample material to work with, for even as widespread asbestos use continues to diminish, tobacco, firearms, and prescription drugs continue.

¹⁶⁴ Sheldon S. Toll, *Bankruptcy and Mass Torts, The Commissions Proposals*, 5 Am. Bankr. L. Rev. 363, 364 (Winter 1997).

¹⁶⁵ Snyder and Siemer, *supra* note 19, at 369-70.

EXHIBIT A

11 U.S.C. § 524(G)

Section 524(g) provides:

(g) (1) (A) After notice and hearing, a court that enters an order confirming a plan of reorganization under chapter 11 [11 USCS §§ 1101 et seq.] may issue, in connection with such order, an injunction in accordance with this subsection to supplement the injunctive effect of a discharge under this section.

(B) An injunction may be issued under subparagraph (A) to enjoin entities from taking legal action for the purpose of directly or indirectly collecting, recovering, or receiving payment or recovery with respect to any claim or demand that, under a plan of reorganization, is to be paid in whole or in part by a trust described in paragraph (2)(B)(i), except such legal actions as are expressly allowed by the injunction, the confirmation order, or the plan of reorganization.

(2) (A) Subject to subsection (h), if the requirements of subparagraph (B) are met at the time an injunction described in paragraph (1) is entered, then after entry of such injunction, any proceeding that involves the validity, application, construction, or modification of such injunction, or of this subsection with respect to such injunction, may be commenced only in the district court in which such injunction was entered, and such court shall have exclusive jurisdiction over any such proceeding without regard to the amount in controversy.

(B) The requirements of this subparagraph are that--

(i) the injunction is to be implemented in connection with a trust that, pursuant to the plan of reorganization--

(I) is to assume the liabilities of a debtor which at the time of entry of the order for relief has been named as a defendant in personal injury, wrongful death, or property-damage actions seeking recovery for damages allegedly caused by the presence of, or exposure to, asbestos or asbestos-containing products;

(II) is to be funded in whole or in part by the securities of 1 or more debtors involved in such plan and by the obligation of such debtor or debtors to make future payments, including dividends;

(III) is to own, or by the exercise of rights granted under such plan would be entitled to own if specified contingencies occur, a majority of the voting shares of--

(aa) each such debtor;

(bb) the parent corporation of each such debtor; or

(cc) a subsidiary of each such debtor that is also a debtor; and

(IV) is to use its assets or income to pay claims and demands; and

(ii) subject to subsection (h), the court determines that--

(I) the debtor is likely to be subject to substantial future demands for payment arising out of the same or similar conduct or events that gave rise to the claims that are addressed by the injunction;

(II) the actual amounts, numbers, and timing of such future demands cannot be determined;

(III) pursuit of such demands outside the procedures prescribed by such plan is likely to threaten the plan's purpose to deal equitably with claims and future demands;

(IV) as part of the process of seeking confirmation of such plan--

(aa) the terms of the injunction proposed to be issued under paragraph (1)(A), including any provisions barring actions against third parties pursuant to paragraph (4)(A), are set out in such plan and in any disclosure statement supporting the plan; and

(bb) a separate class or classes of the claimants whose claims are to be addressed by a trust described in clause (i) is established and votes, by at least 75 percent of those voting, in favor of the plan; and

(V) subject to subsection (h), pursuant to court orders or otherwise, the trust will operate through mechanisms such as structured, periodic, or supplemental payments, pro rata distributions, matrices, or periodic review of estimates of the numbers and values of present claims and future demands, or other comparable mechanisms, that provide reasonable assurance that the trust will value, and be in a financial position to pay, present claims and future demands that involve similar claims in substantially the same manner.

(3) (A) If the requirements of paragraph (2)(B) are met and the order confirming the plan of reorganization was issued or affirmed by the district court that has jurisdiction over the reorganization case, then after the time for appeal of the order that issues or affirms the plan--

(i) the injunction shall be valid and enforceable and may not be revoked or modified by any court except through appeal in accordance with paragraph (6);

(ii) no entity that pursuant to such plan or thereafter becomes a direct or indirect transferee of, or successor to any assets of, a debtor or trust that is the subject of the injunction shall be liable with respect to any claim or demand made against such entity by reason of its becoming such a transferee or successor; and

(iii) no entity that pursuant to such plan or thereafter makes a loan to such a debtor or trust or to such a successor or transferee shall, by reason of making the loan, be liable with respect to any claim or demand made against such entity, nor shall any pledge of assets made in connection with such a loan be upset or impaired for that reason;

(B) Subparagraph (A) shall not be construed to--

(i) imply that an entity described in subparagraph (A) (ii) or (iii) would, if this paragraph were not applicable, necessarily be liable to any entity by reason of any of the acts described in subparagraph (A);

(ii) relieve any such entity of the duty to comply with, or of liability under, any Federal or State law regarding the making of a fraudulent conveyance in a transaction described in subparagraph (A) (ii) or (iii); or

(iii) relieve a debtor of the debtor's obligation to comply with the terms of the plan of reorganization, or affect the power of the court to exercise its authority under sections 1141 and 1142 to compel the debtor to do so.

(4) (A) (i) Subject to subparagraph (B), an injunction described in paragraph (1) shall be valid and enforceable against all entities that it addresses.

(ii) Notwithstanding the provisions of section 524(e), such an injunction may bar any action directed against a third party who is identifiable from the terms of such injunction (by name or as part of an identifiable group) and is alleged to be directly or indirectly liable for the conduct of, claims against, or demands on the debtor to the extent such alleged liability of such third party arises by reason of--

(I) the third party's ownership of a financial interest in the debtor, a past or present affiliate of the debtor, or a predecessor in interest of the debtor;

(II) the third party's involvement in the management of the debtor or a predecessor in interest of the debtor, or service as an officer, director or employee of the debtor or a related party;

(III) the third party's provision of insurance to the debtor or a related party; or

(IV) the third party's involvement in a transaction changing the corporate structure, or in a loan or other financial transaction affecting the financial condition, of the debtor or a related party, including but not limited to--

(aa) involvement in providing financing (debt or equity), or advice to an entity involved in such a transaction; or

(bb) acquiring or selling a financial interest in an entity as part of such a transaction.

(iii) As used in this subparagraph, the term "related party" means--

(I) a past or present affiliate of the debtor;

(II) a predecessor in interest of the debtor; or

(III) any entity that owned a financial interest in-

(aa) the debtor;

(bb) a past or present affiliate of the debtor; or

(cc) a predecessor in interest of the debtor.

(B) Subject to subsection (h), if, under a plan of reorganization, a kind of demand described in such plan is to be paid in whole or in part by a trust described in paragraph (2)(B)(i) in connection with which an injunction described in paragraph (1) is to be implemented, then such injunction shall be valid and enforceable with respect to a

demand of such kind made, after such plan is confirmed, against the debtor or debtors involved, or against a third party described in subparagraph (A)(ii), if--

(i) as part of the proceedings leading to issuance of such injunction, the court appoints a legal representative for the purpose of protecting the rights of persons that might subsequently assert demands of such kind, and

(ii) the court determines, before entering the order confirming such plan, that identifying such debtor or debtors, or such third party (by name or as part of an identifiable group), in such injunction with respect to such demands for purposes of this subparagraph is fair and equitable with respect to the persons that might subsequently assert such demands, in light of the benefits provided, or to be provided, to such trust on behalf of such debtor or debtors or such third party.

(5) In this subsection, the term "demand" means a demand for payment, present or future, that--

(A) was not a claim during the proceedings leading to the confirmation of a plan of reorganization;

(B) arises out of the same or similar conduct or events that gave rise to the claims addressed by the injunction issued under paragraph (1); and

(C) pursuant to the plan, is to be paid by a trust described in paragraph (2)(B)(i).

(6) Paragraph (3)(A)(i) does not bar an action taken by or at the direction of an appellate court on appeal of an injunction issued under paragraph (1) or of the order of confirmation that relates to the injunction.

(7) This subsection does not affect the operation of section 1144 or the power of the district court to refer a proceeding under section 157 of title 28 or any reference of a proceeding made prior to the date of the enactment of this subsection.