

12-15-2003

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Recommended Citation

Francis E. McGovern *Asbestos Legislation II: Section 524(g) Without Bankruptcy*, 31 Pepp. L. Rev. Iss. 1 (2003)

Available at: <https://digitalcommons.pepperdine.edu/plr/vol31/iss1/9>

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Asbestos Legislation II: Section 524(g) Without Bankruptcy

Francis E. McGovern*

Legislation is in season for asbestos litigation. Judges,¹ lawyers,² and legislators³ all share a belief that asbestos litigation is a national tragedy—a tragedy for victims and defendants alike—which deserves a national statutory solution. The dilemma is: which solution? There are at least five models for legislative reform being considered: (1) a criteria bill,⁴ (2) a defined contribution system,⁵ (3) a defined distribution system,⁶ (4) a hybrid involving all three of the above,⁷ and (5) the subject of this discussion, a statute proposing a bankruptcy-type end game without the necessity of filing for bankruptcy.⁸

* Professor of Law, Duke University School of Law. The background for this article is found in the author's experience as a court-appointed neutral in the Manville, UNR, Amatek, National Gypsum, Celotex, Federal-Mogol, Owens Corning, and Kaiser bankruptcies and as a mediator in several other asbestos cases. Great appreciation is due to the judges, attorneys, and experts who have contributed so much to an understanding of the complexities of this subject. Invaluable assistance has been provided specifically for this article by Joyce Cox, Maribeth Minella, Mark Hurford, Melanie Dunshee, Cathy Quezada, and Andrea Kloehn Naef. Many thanks for turning a speech into an article.

1. JUDICIAL CONFERENCE OF THE UNITED STATES, REPORT OF THE JUDICIAL CONFERENCE AD HOC COMMITTEE ON ASBESTOS LITIGATION (1991).

2. See, e.g., ABA COMMISSION ON ASBESTOS LITIGATION, RECOMMENDATION TO THE HOUSE OF DELEGATES (2003), available at http://www.abanet.org/leadership/full_report.pdf.

3. See Fairness in Asbestos Injury Resolution Act of 2003, S. 1125, 108th Cong. (2003).

4. See A Bill To Provide For the Fair And Efficient Judicial Consideration of Personal Injury And Wrongful Death Claims Arising Out of Asbestos Exposure, To Ensure That Individuals Who Suffer Harm, Now Or In The Future, From Illnesses Caused By Exposure To Asbestos Receive Compensation For Their Injuries, And For Other Purposes, S. 413, 108th Cong. (2003).

5. Francis E. McGovern, *Asbestos Legislation I: A Defined Contribution Plan*, TENN. L. REV. (forthcoming).

6. See, e.g., The September 11th Fund, *How We Work*, at <http://www.september11fund.org> (last visited Nov. 20, 2003) (explaining how funds are distributed).

7. Fairness In Asbestos Injury Resolution Act of 2003, S. 1125, 108th Cong. (2003).

8. See Francis E. McGovern, *The Tragedy of the Asbestos Commons*, 88 VA. L. REV. 1721,

The purpose of this article is not to support any single alternative, but to provide sufficient background and detail concerning the fifth option so that it can become part of the national conversation on asbestos litigation. This article first reviews the basic issues and historic outcomes in traditional asbestos bankruptcies. Next, it analyzes the intricacies of prepackaged bankruptcies involving asbestos companies. Finally, it outlines a statute that would allow asbestos companies the same protections from asbestos litigation found in bankruptcy without the necessity of these companies actually filing for bankruptcy.

I. TRADITIONAL ASBESTOS BANKRUPTCIES

There are approximately sixty companies that have filed for bankruptcy because of exposure to asbestos litigation. The total amount of money put in trust for asbestos claimants has grown to over \$10 billion,⁹ and the amount currently in controversy exceeds \$20 billion.¹⁰ The best estimates suggest that there have been around 600,000 claims to date against over 6,000 defendants.¹¹ Estimates of the number of future claimants vary from one to three million with projected costs ranging from \$200 billion to \$265 billion.¹²

This is the context of the traditional bankruptcy approach to resolving asbestos litigation. Once a company files for bankruptcy, there is a standard model that the bankruptcy follows: there are readily recognizable parties, procedures, issues, and information. Bargaining in accordance with this standard process has generally resulted in a predictable range of outcomes.

A. Parties

When a company facing asbestos liabilities files for bankruptcy, the critical players typically include the following:

1. Debtor
 - a. Management
 - b. Directors
 - c. Employer
2. General Creditors
 - a. Secured
 - b. Unsecured
3. Equity Holders
4. Insurers
5. Tort Claimants
6. Co-Defendants

1751-56 (2002).

9. STEPHEN J. CARROLL, ET AL., RAND INST. FOR CIVIL JUSTICE, ASBESTOS LITIGATION COSTS AND COMPENSATION: AN INTERIM REPORT 17 (2002), available at <http://www.rand.org>.

10. *Id.*

11. *Id.*

12. *Id.*

7. Public Interest Groups

The United States Trustee defines classes of parties and appoints separate committees for the classes so that each interest group is appropriately represented in the bankruptcy proceedings.¹³ In normal bankruptcies, the designation of committees and their memberships is routine. When there are large unliquidated claims, however, the task of identifying true representatives of those claims can be difficult. Because the funding for the appointed committees comes from the debtor,¹⁴ and the development of a plan of reorganization is dependant upon committee approval, there are enormous advantages to having a committee for a given set of interests and to being on that committee. As a result, there can be significant competition among the various interested individuals and interests who are seeking to maximum leverage during subsequent negotiations by having a committee and by being in control of that committee.

The debtor is not a monolithic entity. It is composed of interest groups that may compete with each other in the normal decision making process. This is particularly true when pension funds are heavily invested in the company's equity, thus allying employees and equity holders. At the same time, the board of directors may not share the same interests as management, particularly on a forward-going basis.

Likewise, there are financial creditors who have competing claims on limited assets. The bankruptcy code establishes an absolute priority for claims to assets under which higher-level claimants must be paid in full before claimants with lower priority are paid.¹⁵ Financing for the debtor in possession comes first. Then there are administrative claims, secured claims, guaranteed claims, and unsecured claims. Even within this hierarchy there may be competitive advantages between groups.

Insurers are potentially among the most complicated groups. There may be both settled and unsettled policies, provisions with and without indemnity, and some policies that are liquidated while others have coverage currently in place. Insurers who have made payments that have benefited the debtor may have potential subrogation claims against the debtor. Co-defendants may also seek contribution or indemnity for payments they have made.

If the debtor company has a sufficiently high profile, there may be a variety of other interest groups who wish to play a role in the bankruptcy. Associations of injured parties, unions, consumer groups, and others may attempt to represent their constituencies. This participation typically attracts significant media attention.

The tort claimants are usually further divided into the following groups:

13. See 11 U.S.C. § 1102(a)(1) (2000).

14. See 11 U.S.C. § 330(a) (2000); see also 11 U.S.C. § 1103 (2000).

15. See 11 U.S.C. § 507 (2000).

1. Property Damage
2. Personal Injury
 - a. Malignancies
 - b. Non-Malignancies
3. Contract Claims
4. Foreign Claims
5. Future Claims
 - a. Near
 - b. Far

Property damage tort claimants are typically owners of buildings that currently contain or have contained an asbestos product.¹⁶ The extent of these claims relates to the identity and quantity of the specific products sold by the debtor. In some cases, the United States Trustee appoints a separate committee for property damage claims.¹⁷ In others, they are included with other tort claims or with general unsecured creditors.¹⁸

Personal injury tort claims involve individuals who have suffered physical harm from exposure to asbestos. These asbestos-related diseases include malignancies such as mesothelioma, lung cancer or other cancers, and non-malignancies such as asbestosis and pleural disease.¹⁹

There are also tort claims from individuals who contracted to settle their claims prior to the bankruptcy filing but who were not paid.²⁰ Arguably, their rights against the debtor are based upon contract rather than tort.²¹ Whether these claimants have tort or contract claims is a decision for the bankruptcy court.

Many asbestos debtors have sold their products overseas, and persons in foreign countries have claims that are viable either in their own jurisdiction or in the United States.²² Although the debtor is generally eager to satisfy those claims as well, so that the entire asbestos liability of the company can be resolved, there are often jurisdictional complications. This is particularly true if the debtor has foreign assets that can be jeopardized by new claimants.

Future claims are treated somewhat differently. A “futures representative” is appointed by the bankruptcy court upon motion by the debtor and agreement by the various committees.²³ The futures

16. See, e.g., *Bd. of Educ. of Chicago v. A, C and S, Inc.*, 546 N.E.2d 580, 583 (Ill. 1989) (explaining that claimant school districts were suing for removal of asbestos).

17. See *In re Federal-Mogul Global, Inc.*, No. 01-10578 (D. Del. Oct. 28, 2003) (notice of appointment of Official Committee of Asbestos Property Claimants).

18. See, e.g., *In re Owens Corning*, No. 00-3837 (order establishing case management procedures for asbestos-related property damage claims).

19. CARROLL, *supra* note 9, at 17.

20. See, e.g., *Rovida v. Babcock & Wilcox Co.*, No. 00-10992, 2002 WL 1874863, at *1 (E.D. La. Aug. 13, 2002).

21. See *id.* at *3.

22. See generally *In re Federal-Mogul Global, Inc.*, 282 B.R. 301 (Bankr. D. Del. 2002).

23. 11 U.S.C. § 524(g)(4)(B)(i) (2000) (stating that a “legal representative for the purpose of protecting the rights of persons that might subsequently assert demands” must be appointed); see also *In re USG Corp.*, 290 B.R. 223, 224 (Bankr. D. Del. 2003) (giving order appointing a “futures

representative has responsibility for insuring that the rights of all future claimants are satisfied in the asbestos bankruptcy.²⁴ Those claims can include near futures—those who know that they have been exposed to an asbestos product, but who have no current injury—and far futures—those who are currently unaware of their asbestos exposure.²⁵

B. Procedure

The critical procedural steps in the life of an asbestos bankruptcy include the following:

1. Stay of Litigation
2. Plan of Reorganization
3. Exclusivity
4. Disclosure Statement
5. Valuation
6. Vote
7. Confirmation
8. Article III/Article I Responsibilities

Asbestos bankruptcies follow a procedural “life cycle.” Upon filing for bankruptcy, a debtor first seeks a stay of all litigation pending against it in its first day orders. The goal of this stay is to allow the debtor’s limited funds to be divided fairly among all claimants according to bankruptcy code priorities rather than on a first-come, first-serve basis.

The procedure established in the bankruptcy code provides that the debtor has the exclusive right to propose a plan of reorganization.²⁶ It is this plan that defines the rights and duties of both the debtor and the claimants and sets forth what must occur before the “reorganized” company can emerge from bankruptcy. The plan allocates all assets based upon a determination of all liabilities. Therefore, it must comply with the priority rules in the bankruptcy code, which mandate that parties with a higher priority be paid in full before parties with a lower priority can be paid at all. A synopsis of the plan, known as the disclosure statement, must be sent to the members of each class of interested parties for a vote.²⁷

In order for a plan of reorganization to be confirmed, there must be a positive vote of fifty percent in number and two-thirds in value from each voting class.²⁸ The exception to this rule is that classes lower in payment

representative”).

24. See 11 U.S.C. § 524(g)(4)(B)(i).

25. See generally *In re Asbestos Litig.*, 90 F.3d 963 (5th Cir. 1996).

26. See 11 U.S.C. § 1121(b) (2000).

27. 11 U.S.C. § 1125(b) (2000).

28. 11 U.S.C. § 1126(c) (2000). *But see* 11 U.S.C. § 524(g)(2)(B)(ii)(IV)(bb) (2000) (requiring that “a separate class or classes of the claimants whose claims are to be addressed by a trust” be established, that the claimants have the ability to vote on the proposed plan of reorganization, and

priority than any higher class not paid in full can be forced to accept the plan of reorganization by a process known as a “cram down.”²⁹ Secured claims are paid first, then unsecured claims, and finally equity holders.³⁰ For example, if the classes of claimants for secured and unsecured creditors vote in favor of the plan of reorganization, and the unsecured creditors are not paid in full, the plan can be confirmed even though the equity class rejects the plan.

In the event, however, that there is no agreement among the priority creditors, the procedure for confirming a plan of reorganization becomes more complicated. The contesting committees can challenge the values of the debtor’s assets and each other’s claims.³¹ So, for example, a lower priority committee might argue that the debtor has a larger value so that there is more of a remainder for its claims after the higher priority claims are paid in full. A committee might inflate the value of its own claims and deflate the value of other committees’ claims in order to gain a larger share of the available assets. In addition, the committees can contest each issue in the proceedings in an attempt to create bargaining power and negotiate a plan of reorganization that is more favorable to them.

Each committee’s goal is to establish sufficient bargaining power to assure that its claims receive as great a share as possible of the available assets as possible. Those with less bargaining power still have “legal aid.” The debtor funds all litigation efforts, even if those efforts are doomed to failure. Given the time value of money, transaction costs, and the opportunity costs of a debtor in bankruptcy, the ability to delay the confirmation of a plan of reorganization creates bargaining power in itself.

An Article I bankruptcy judge oversees this process.³² Appeals from the bankruptcy judge’s decisions go to an Article III federal district court judge.³³ In addition, the final release of the asbestos claims must be decided by the Article III judge.³⁴

C. Issues and Information

The prominent legal and factual issues in asbestos bankruptcies typically are the following:

1. Scope of Stay of Litigation
2. Bar Date
3. Claim Form
4. Claim Allowance

that the plan be approved “by at least 75% of those voting, in favor of the plan”). This provision of 11 U.S.C. § 524 applies to asbestos claimants.

29. See 11 U.S.C. § 1129(b) (2000) (making statements indicating use of a “cram down”).

30. See *id.*

31. See 11 U.S.C. § 502 (2000).

32. See 28 U.S.C. §§ 151 (designation of bankruptcy courts), 152 (appointment of bankruptcy judges), 157, 1334 (jurisdiction over bankruptcy cases and proceedings) (2000).

33. 28 U.S.C. § 158 (2000).

34. See 11 U.S.C. § 524(g)(2) (2000).

5. Estimation
6. Challenged Transfers or Preferences
7. Exclusivity
8. Voting Procedures
8. Section 524(g)
9. Claims Resolution Facility

The bankruptcy code provides for the bankruptcy court to stay all pending litigation against the debtor.³⁵ If there are entities related to the debtor that also have litigation pending against them, they may attempt to have that litigation stayed as well because their litigation is “related to” the debtor’s welfare and might adversely affect the debtor’s assets.³⁶ The scope of the stay can, therefore, become hotly contested depending upon the debtor’s corporate structure and the amount of pending litigation.

Issues regarding the claim form and the deadline for claimants to file a proof of claim (commonly referred to as the “bar date”) hinge on the availability of information concerning the values of the creditors’ claims.³⁷ For trade and financial creditors, the amount of the claim is typically readily available. However, interest on debts and the nature of securities can often be problematic. In other instances, there can be disputes concerning the validity of claims.

The type of information needed to assess the value of personal injury and property damage claims arising from asbestos exposure is much more difficult to obtain.³⁸ These claim values are generally based upon the results of past trials or settlements in the tort system but can vary considerably depending upon the nature of the alleged harm, the jurisdiction, and other factors.³⁹ Just as important as the value of claims is the number of asbestos claimants who will actually file a claim and the validity of the filed claims.⁴⁰ As is the case with many mass torts, there is substantial elasticity in the filing of claims.⁴¹

There are several methods for estimating the number and value of the asbestos claims that will eventually be filed.⁴² There can be extrapolation from historic values and a projection of future filings.⁴³ Alternatively, there can be a number of generic challenges to establish new threshold standards

35. 11 U.S.C. § 362(a) (2000).

36. *See id.*

37. *See* 11 U.S.C. § 502(b)(9) (2000); *see also* BANKR. R. 3002.

38. *See* RICHARD B. SABOL, *BENDING THE LAW: THE STORY OF THE DALKON SHIELD BANKRUPTCY* (1991).

39. *See* CARROLL, *supra* note 9, at 2.

40. *See* McGovern, *supra* note 8, at 1722, 1728, 1750.

41. *In re* Babcock & Wilcox Co., No. 00-558, 2001 WL 1204074, at *2 (E.D. La. Oct 11, 2001); *see also In re* USG Corp., 290 B.R. 223, 224 (Bankr. D. Del. 2003).

42. *See In re* USG Corp., 290 B.R. at 224-27 (large volumes of known and unknown claimants).

43. *See id.* at 226 (discussing various alternatives to evaluating the claims).

for maintaining viable claims. These types of challenges—*Daubert* hearings⁴⁴ and motions for summary judgment⁴⁵—follow both the Federal Rules of Civil Procedure and the Federal Rules of Evidence and have been proposed in a number of asbestos bankruptcies.⁴⁶ There is also the possibility of a claims allowance process by which claims can be challenged individually to determine their validity.⁴⁷

The bottom line for the bar date, claim form, claim allowance, and estimation issues is that the court must establish the total liability for all the debtor's asbestos claims in order to insure that all similarly situated creditors are treated equally. Thus, an appropriate allocation of the debtor's resources cannot be made, nor can the feasibility of a plan of reorganization be assured, without an estimate of all the debtor's liabilities. The higher the asbestos liabilities, the greater the percentage of the debtor's assets that asbestos claimants will receive, and vice versa.

Another typical area of controversy involves contesting the debtor's transfers of assets prior to the bankruptcy filing. Some of these contested transfers may involve asset sales that occurred long before the advent of bankruptcy.⁴⁸ Payments made to asbestos personal injury claimants immediately prior to the bankruptcy filing may also be contested.⁴⁹

As indicated above, the debtor has the exclusive right to propose a plan of reorganization unless that exclusivity is lifted by the court.⁵⁰ This right gives the debtor great bargaining power to veto any provisions of a proposed reorganization plan that it does not like. In the event that the debtor cannot propose a viable plan because of a deadlock among the committees, the court can lift the debtor's exclusivity privilege, allow all parties to file plans of reorganization, and have them sent out for a vote.⁵¹ Since the debtor does not have a "vote," this lifting of exclusivity shifts the bargaining power rather drastically.

The procedures for voting on a plan of reorganization are traditionally rather simple: one dollar, one vote; one claimant, one vote.⁵² In the case of asbestos personal injury claimants, however, the dollar value of actual claims can vary considerably.⁵³ Since there is no individual evaluation of claims prior to a vote on the plan of reorganization, courts recently have

44. See *Daubert v. Merrell Dow Pharm.*, 509 U.S. 579 (1993).

45. See *BANKR. R. 7056* (stating that FED. R. CIV. P. 56 applies to adversary proceedings in bankruptcy).

46. W.R. Grace's Supplemental Brief Regarding Procedures for the Litigation of the Common Personal Injury Liability Issues, *In re W.R. Grace & Co.*, No. 01-01139 (June 21, 2002).

47. See 11 U.S.C. § 502 (2000); see also *BANKR. R. 3002, 3003*.

48. See 11 U.S.C. § 548 (2000) (discussing fraudulent conveyances).

49. See 11 U.S.C. § 547 (discussing preferences).

50. See 11 U.S.C. § 1121 (2000) (stating that only the debtor may file a plan of reorganization until after 120 days from the date of the order for relief is entered).

51. *Id.*

52. See 11 U.S.C. § 1128(c) (2000); see also *In re Fighter Ltd.*, 118 F.3d 635 (9th Cir. 1997); *Concord Square Apartments v. Otham Prop., Inc.*, 174 B.R. 71, 74 (Bankr. S.D. Ohio 1994); *In re Gilbert*, 104 B.R. 206, 211 (Bankr. W.D. Mo. 1989).

53. *CARROLL*, *supra* note 9, at 9.

allowed each claimant to indicate the type of disease claim the individual is asserting and have assigned that individual a voting value equal to the value of the claim in the eventual plan of asset distribution.⁵⁴

Section 524(g) of the bankruptcy code is another unique aspect of asbestos bankruptcies. After the first few asbestos bankruptcies were resolved, a shadow of potential future asbestos liability remained over the reorganized debtors.⁵⁵ The risk of future liability reduced their marketplace values to a sufficient degree such that Congress passed a statute specifically to insure that no overhang of asbestos liability remained for the company emerging from bankruptcy.

Section 524(g) provides that if the following:

- (a) a trust is created which assumes the present and future asbestos personal injury and/or property damage liabilities of the debtor;⁵⁶ and
- (b) the trust is funded in whole or in part by securities of the debtor and obligations of the debtor to make future payments, including dividends;⁵⁷ and
- (c) the trust will own, or by exercise of rights granted under the plan will be entitled to own a majority of the voting stock of the debtor, parent, or subsidiary, if specified contingencies occur;⁵⁸ and
- (d) the trust will pay the present and future asbestos claims against the debtor;⁵⁹ and
- (e) the present and future claims will all be valued and paid in substantially the same manner;⁶⁰ and
- (f) the plan is approved by at least 75% of all asbestos claimants who vote;⁶¹ and
- (g) a futures representative is appointed;⁶²

then the planned discharge provisions can include an injunction issued by the district court barring the following claims:

- (a) for the debtor's asbestos torts against the reorganized debtor;⁶³ and

54. *In re Johns-Manville Corp.*, 40 B.R. 219 (Bankr. S.D.N.Y. 1984).

55. See Jeff Claubaugh, *W.R. Grace Falls on Senate Snag*, WASHINGTON BUS. J., July 10, 2003, available at <http://washington.bizjournals.com/washington/stories/2003/07/07/daily30.html>; Nelson Antosh, *Halliburton Hunkers Down to Fend Off Asbestos Litigation*, HOUS. CHRON., Feb. 22, 2002, available at <http://www.chron.com/cs/CDA/story.hts/business/1268264.html>; David Brinkerhoff, *Asbestos-Plagued Shares Up on Liability Limit Talk*, at http://biz.yahoo.com/rc/030916/manufacturing_stocks_1.html (September 16, 2003); Nat Worden, *Stocks With Potential Asbestos Liability Slide*, at http://www.thestreet.com/_yahoo/markets/stockwatch/10099232.html (July 10, 2003).

56. 11 U.S.C. § 524(g)(2)(B)(i)(I) (2000).

57. 11 U.S.C. § 524(g)(2)(B)(i)(II).

58. 11 U.S.C. § 524(g)(2)(B)(i)(III).

59. 11 U.S.C. § 524(g)(2)(B)(i)(IV).

60. 11 U.S.C. § 524(g)(2)(B)(ii)(V).

61. 11 U.S.C. § 524(g)(2)(B)(ii)(IV)(bb).

62. 11 U.S.C. § 524(g)(4)(B)(i).

63. 11 U.S.C. § 524(g)(1)(A)-(B).

(b) against third-parties who were past and present affiliates of the debtor, officers or directors of the debtor or a related party, insurers of the debtor, lenders to a purchaser of the debtor who have provided or agreed to provide benefits to the trust in amounts that make such protection fair and equitable.⁶⁴

In addition, any enforcement or construction of the injunction must be done by the same district court.⁶⁵

The protections of § 524(g) are greatly valued by the capital markets and have become a prerequisite for a successful asbestos bankruptcy. One effect of this development has been to give asbestos personal injury claimants, as a group, and a large number of claimants with less serious injuries in particular, a de facto veto over any plan of reorganization. This veto power is reinforced by the applicability of state substantive law to the personal injury claims.⁶⁶ This phenomenal increase in tort claimants' bargaining power has altered the traditional negotiation process, and adjusting to the new reality has been extremely difficult for some of the other involved creditors.

The assets devoted to asbestos claimants are typically placed in a trust⁶⁷ with an accompanying claims resolution facility designed to evaluate each asbestos personal injury or property damage claim and pay them accordingly.⁶⁸ The precise trust distribution plan, which assigns values to categories of claims, can also be controversial, particularly regarding the relative allocations of assets between malignancies and non-malignancies,⁶⁹ foreign and domestic claims,⁷⁰ and personal injury and property damage claims.⁷¹

D. The Bargaining Process

The bargaining process in asbestos bankruptcies is typically quite extended, lasting from four to six years.⁷² The mere passage of so much time lends itself to much mischief because of inevitable temporal changes in bargaining power and party alliances. The negotiation process often becomes a game in which the parties strategically vie for power and position. The sources of bargaining power include committee appointments, some of which do not occur until late in the case; decisions by the bankruptcy or federal district judge on the multiple issues discussed above;

64. 11 U.S.C. § 524(g)(4)(a)(i)(I)-(IV); *see also* 11 U.S.C. § 524(g)(4)(b)(i).

65. 11 U.S.C. § 524(g)(2)(A).

66. *Raleigh v. Ill. Dep't. of Revenue*, 530 U.S. 15, 20 (2000); *Butner v. United States*, 440 U.S. 48, 55 (1979).

67. *See* 11 U.S.C. § 524(g) (2000).

68. *See* 11 U.S.C. § 524(g).

69. *See In re Armstrong World Indus., Inc.*, 285 B.R. 864 (Bankr. D. Del. 2002); *In re Babcock & Wilcox Co.*, No. 00-10992, 2002 WL 1874836, at *1 (E.D. La. Aug 3, 2002).

70. *In re Johns-Manville Corp.*, 237 F. Supp. 2d 297 (E.D.N.Y. 2002).

71. *In re Celotex Corp.*, 227 F.3d 1336 (11th Cir. 2000); *In re Nat'l Gypsum Co.*, 2002 WL 1359715, at *1 (N.D. Tex. June 18, 2002).

72. *See Kane v. Johns-Manville Corp.*, 843 F.2d 636, 639-41(2d Cir. 1988).

scientific developments on evidence that may or may not be made available during the course of the proceedings; and legislative changes.

At the same time, parties may change their bargaining positions because of internal disputes or because of changing attitudes toward the relative value of the debtor's assets. Typically those assets include cash, stocks, warrants, debts, insurance, and investment opportunities. Variations in interest rates, changes in investment opportunities, and other changes in value or risk may result in commensurate changes in the bargaining postures of the parties.

The constantly changing alliances among the parties are key factors in the negotiation process. It is important for each party to form advantageous alliances with competing parties in the process. Yet, those alliances are rarely stable for long periods of time. Plaintiffs' counsel representing malignancies, for example, may potentially have common ground with the debtor, property damage claimants, financial creditors, the futures representative, or other personal injury claimants. Given the multiple parties and multiple interests, the bargaining process in asbestos bankruptcies has many facets. Because of the extended amount of time for negotiation, each party tends to continuously seek a more advantageous outcome, and interests and alliances shift.

At the end of the day, the bargaining power created by the bankruptcy code through the absolute priority rules and § 524(g) drives the broad outline of most asbestos bankruptcy resolutions. At the margin, however, there can be quite different outcomes based upon the negotiation skills of the respective parties.

E. Outcomes

The outcome of any bankruptcy involves complete or partial resolution of the following issues:

1. Equity Percentage
2. Secured Debt Percentage
3. Trade Debt Percentage
4. Unsecured Financial Debt Percentage
5. Tort Debt Percentage
6. Insurance
7. Trust and Claims Resolution Facility

The resolutions of asbestos bankruptcies have been relatively uniform, in large part because of the requirements of § 524(g).⁷³ Generally, companies do not file for bankruptcy until their asbestos liabilities exceed their assets. Given the priority of payment rules, which dictate that equity holders are paid only after secured and unsecured creditors are paid in full,

73. See 11 U.S.C. § 524(g) (2000).

there are generally few, if any, assets remaining for the shareholders. In some instances, equity holders have been able to receive funds out of the debtor's money warrants. The shareholders' bargaining power is typically derivative of the debtor's exclusivity rights, the ability to suppress the value of the tort claims, or the means to inflict sufficient costs to encourage a beneficial settlement.

Because secured creditors come first, they usually are paid in full unless the debtor is also financially bankrupt. In that event, there is a conflict between the bargaining power provided by the secured creditor's priority status and the bargaining power provided by the unsecured claimants' § 524(g) veto power.⁷⁴ Because the unsecured financial creditors must be treated equally with similarly situated unsecured asbestos claimants, they have additional bargaining power.

Most frequently, negotiations focus on the relative values of the unsecured financial creditors and the unsecured tort claimants. As indicated above, the contested issues involve preferences, claims valuation and estimation, and the valuation of corporate assets that are subject to financial and asbestos claims. In addition, there can be significant corporate governance issues. If the *in pari passu* requirements are to be met by giving a "strip"—a percentage of the cash, debt, and equity remaining in the debtor—to the financial and asbestos creditors, there may be debate concerning the rights of minority shareholders. These corporate governance issues can be addressed by the composition of the board or by giving minority shareholders specific rights.

In many asbestos bankruptcies, there are insurance policies that are arguably available to fund some of the asbestos tort claims. These insurance policies may raise issues of assignability and questions as to when payment is triggered. In addition, the policy provisions may create a duty on the insurance company to cooperate. Tort claimants typically wish to assign such insurance policies to a trust, deem the entire amount of the policies due upon the insured's filing of bankruptcy, and to process the claims without regard to the insurers. Conversely, the insurance companies typically contest such assignment, demand participation in the claims resolution process, and insist that claims be paid only as the insurers determine they are valid.

The assets made available to tort claimants are normally placed into a trust with trustees nominated by the claimants. Individual claims are then evaluated by a claims resolution facility. The facility's procedures are governed by a trust distribution plan (TDP), which is part of the overall reorganization plan. Usually, there are defined medical and exposure criteria that place the claimants into a series of categories. Each disease category is assigned a range of values, and a grid is then used to guide the facility in its analysis of each claim. Based on the grid value of each claim, the claims resolution facility makes an offer of payment to each individual claimant. The claimant may contest the offer using alternative dispute

74. *See id.*

resolution or may even go to trial. If there is insufficient funding to pay all claims in full, each claim is paid a percentage of its grid value in order for all present and future claimants to be treated equally.

The outcome of most asbestos bankruptcies is as follows:

1. Equity - relatively small participation
2. Secured Debt - paid in full or in kind
3. Trade Debt - paid in full or equivalently with other financial debt
4. Unsecured Financial Debt - paid *in pari passu* with the unsecured tort debt
5. Unsecured Tort Personal Injury Claims - paid at least 50.1% of the equity in the trust and claims resolution facility
6. Unsecured Tort Property Damage Claims - paid *in pari passu* with the personal injury claims
7. Futures - paid equivalently to the current tort personal injury claims.

II. PREPACKAGED ASBESTOS BANKRUPTCIES

The *Ortiz v. Fibreboard Corp.*⁷⁵ mandatory limited fund class action was the precursor to prepackaged asbestos bankruptcies.⁷⁶ In *Ortiz*, the asbestos company, Fibreboard, had limited assets plus an insurance policy arguably covering some of its asbestos personal injury liability.⁷⁷ Counsel representing personal injury plaintiffs negotiated with Fibreboard and its insurance carrier: (1) a settlement of pending cases; (2) a class action settlement for future cases; and (3) a default payment to Fibreboard from the insurance carrier in the event that the class action was not upheld.⁷⁸ The current cases were resolved.⁷⁹ The class action provided for both a lump sum payment into a trust fund and a trust distribution plan with a schedule of payments for claimants suffering from various asbestos-related diseases.⁸⁰

At the fairness hearing on this settlement, the trial court approved the mandatory limited fund class action over the objection of counsel for a minority of the plaintiffs.⁸¹ The Fifth Circuit Court of Appeals affirmed, but the United States Supreme Court reversed.⁸² This reversal triggered the default provisions, and Fibreboard received a lump sum payment from the

75. 527 U.S. 815 (1999).

76. *See id.*

77. *Id.* at 822-23.

78. *Id.* at 823-25.

79. *Id.*

80. *Id.* at 824-25, 27.

81. *Id.* at 827.

82. *Id.* at 815.

insurance carrier.⁸³ Fiberboard was subsequently purchased by Owens Corning—another asbestos manufacturer.⁸⁴

Ortiz had been preceded by *Amchem Products, Inc. v. Windsor*,⁸⁵ another attempt to bring closure to asbestos litigation by the use of a class action. *Amchem* involved a consortium of defendants who used a class action to settle their inventory of current claims and to offer payments based upon a predefined grid for all future claimants.⁸⁶ Any plaintiff desiring not to participate in the settlement grid program was given the opportunity to opt out of the settlement class and proceed normally in the tort system.⁸⁷ The Third Circuit Court of Appeals and the United States Supreme Court both reversed.⁸⁸

Ortiz and *Amchem* eliminated, as a practical matter, asbestos companies' attempts to use the class action device to provide finality for corporations involved in protracted personal injury asbestos litigation.⁸⁹ After *Ortiz* and *Anchem*, the remaining legal vehicle that can bring these defendants finality is bankruptcy and its § 524(g) protections.⁹⁰

Most companies are reluctant to file for bankruptcy except as a last resort. They wait until their assets have been diminished so greatly that bankruptcy is the only alternative. When, however, it is possible to pre-negotiate a plan of reorganization so that a company can file for bankruptcy knowing in advance what the outcome will be and go through the bankruptcy process quickly, then bankruptcy becomes a more viable option. A prepackaged bankruptcy occurs, then, when a company negotiates a plan of reorganization, sends out a disclosure statement, and conducts a vote all prior to actually filing for bankruptcy.

A. *The Process of a Prepackaged Bankruptcy*

The parties, issues, and information are roughly the same in any bankruptcy. The statutory procedures are also identical. There are a number of case-specific issues, however, that must be resolved prior to the filing of a successful prepackaged bankruptcy:

1. Confidentiality
2. Plaintiffs' "Committee"
3. Futures Representative
4. Stay of Litigation
5. Current Cases
6. Trigger Date

83. *See id.*

84. OWENS CORNING, INC., 1997 ANNUAL REPORT 30 (1997), available at http://www.corporate-ir.net/media_files/otcbb/owenq.ob/reports/97ar.pdf.

85. 521 U.S. 591 (1997).

86. *Id.*

87. *Id.*

88. *Id.*

89. *See Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 815 (1999); *Amchem*, 521 U.S. at 591.

90. *See* 11 U.S.C. § 524(g) (2000); *Ortiz*, 527 U.S. at 815; *Amchem*, 521 U.S. at 591.

7. Security
8. Gap Cases
9. Future Cases
10. Equivalency
11. Asbestos Values
 - a. Dollars
 - b. Category
12. Definition of Cases
13. Product Identification
14. Medical Criteria
15. Trust Composition
16. Claims Processing
17. Funding and Flow Rate
18. Insurance

Because there is no formal mechanism to oversee the negotiation of a prepackaged bankruptcy, organization of the early discussions is difficult. One of the most troublesome aspects of the lack of a formalized structure for the negotiations is the necessity of confidentiality. Premature release of information regarding the possibility of a bankruptcy filing could adversely affect both the stock price of any interested corporation and its approach to resolving its asbestos liabilities. At the same time, corporations have an obligation to disclose material changes to the investing public.

One of the key issues that must be resolved in negotiation of a prepackaged bankruptcy is an agreement concerning the total value of the present and future asbestos liabilities. One approach is to analyze the history of a company's settlements and trials and use those statistics to predict remaining liabilities. Naturally, defendants are reluctant to share such information with counsel for plaintiffs who are currently suing them. The dilemma is how to share this information without jeopardizing the future defense and negotiation of claims in the event that there is no agreement on the prepackaged bankruptcy. There are any number of potential solutions, one of which is to hire a neutral expert who can insulate the data while providing independent verification of aggregate information crucial to estimating the overall value of claims.

The actual negotiators will typically be (1) representatives of the company, (2) representatives of the insurers, (3) the plaintiffs' bar, and (4) the futures representative. The representatives of the putative debtor are readily identifiable and are paid by the debtor. If there are insurers involved, they are similarly situated.⁹¹ The plaintiffs' bar is represented by approximately twenty-five lawyers who serve on the various asbestos bankruptcy committees. Roughly seven to fifteen of those lawyers can effectively speak for all their peers. If those seven to fifteen lawyers can

91. See 11 U.S.C. § 524(g)(4)(B).

agree among themselves on the details of a prepackaged bankruptcy, there is a substantial likelihood that there will be no critical opposition from the plaintiffs to an eventual plan of reorganization. Those seven to fifteen lawyers are currently members of a committee that represents itself as available to negotiate prepackaged bankruptcies. There is a potential problem, however, in the fact that the United States Trustee is not bound to choose precisely the same lawyers for each bankruptcy negotiation committee; this lack of certainty can create substantial dislocation in the plan approval process.

There is no generally accepted way of paying these lawyers for their efforts in negotiating a plan of reorganization other than through their respective clients.⁹² Because the attorneys' volumes of clients vary considerably, one option for compensating counsel and experts for services that benefit all of the claimants is using the multi-district litigation model of a common benefit fund.⁹³ Under this approach, the debtor establishes a fund to be used to pay front-end expenses and counsel fees as approved by the district court. Both financial and statistical experts are similarly paid. The common benefit fund can also be used to pay mediators, facilitators, and arbitrators as necessary.

Likewise, the futures representative can be paid from the same fund.⁹⁴ The selection of the futures representative is problematic because having a weak futures representative is in the interests of both the debtor and the current claimants. Yet, under the bankruptcy code, they are precisely the parties who select the futures representative (subject to court approval). Any selection of a futures representative in a prepackaged bankruptcy must, by necessity, be approved by a court.⁹⁵

All debtors desire a stay of litigation pending resolution of the prepackaged bankruptcy negotiations, but these negotiations occur prior to any filing with a court. As a result, there is usually only an informal stay, which is subject to the usual hazards associated with informality. Notwithstanding an agreement by the parties to a stay of limited duration, there needs to be some jurisdictional hook in order to allow a court to issue an injunction staying litigation.

The first issue to be resolved is the trigger dates to be used in identifying three different types of cases: those liquidated prior to the bankruptcy filing, the "gap cases" filed after that trigger date but before the effective date, and the "future" cases. These three categories of cases have been handled using three fundamentally different approaches because there are several

92. See, e.g., McGovern, *supra* note 8, at 1745 (stating that "since *Amchem* and . . . *Ortiz* . . . , there has been no further judicial effort to coerce future asbestos plaintiffs into a predefined mode").

93. See, e.g., *In re Salzer Hip Prosthesis and Knee Prosthesis Liability Litig.*, 268 F. Supp. 2d 907 (N.D. Ohio 2003); HEMLER, ET AL., RAND INST. FOR CIVIL JUSTICE, CLASS ACTION DILEMMAS 15-37 (2000); MANUAL FOR COMPLEX LITIGATION (THIRD) § 33.24 et seq., (1995).

94. See 11 U.S.C. § 524(g)(2)(b)(ii)(v).

95. See 11 U.S.C. § 524(g)(4)(B)(i) (stating that if, under a plan of reorganization, a trust is to be used in connection with an injunction, such injunction is valid and enforceable if the court appoints a legal representative for future claimants).

competing interests that must be served in accommodating them. The unpaid current and gap cases have the right to vote in the bankruptcy, and 75% of them must be satisfied that their payments are guaranteed in order for them to vote in favor of the plan of reorganization.⁹⁶ The future cases must be treated equivalently to the current cases in order to comply with § 524(g).⁹⁷ This creates a conflict of interest between the voters and the non-voters.

The company, on the other hand, typically will not guarantee the payment of current claims unless it is certain that the prepackaged bankruptcy will be approved. The company knows that it has to pay even arguably valid current claims in order to get a favorable vote because even the most marginal claims are assigned one vote. However, the company does not want to have to pay those types of claims in the future. This creates a conflict between the company and the current and gap claims, as well as conflict over the requirement that all claims, even future claims, be treated equivalently.

Among plaintiffs, the lawyers who represent principally clients suffering from malignancies understand that current non-malignancy plaintiffs must be paid in order to achieve the requisite vote, but they do not want to see less serious cases dilute payments to the malignancies in the future. This creates a conflict between malignancies and non-malignancies and also between current and gap non-malignancies and future non-malignancies.

Finally, there is the problem of setting a trigger date that draws the line between current and gap claims. As soon as the trigger date is announced, many new entrants attempt to file before the deadline in order to be current claimants, an arguably more advantageous position than being a gap claimant. However, unlimited new claimants may dilute the funds available for immediate payment to the current claimants.

The approaches to reconciling these competing interests are both varied and ingenious. One technique is to create a pre-petition settlement trust, which is funded before the bankruptcy filing and pays a percentage of a predetermined, liquidated value of current claims. The unpaid portion of the liquidated value of these cases, known as the "stubb" payment, is paid from a second trust created after bankruptcy. This second, post bankruptcy trust pays all of the stubb payments on current claims, the entire amount of the gap claims, and future claims. The stubb payment is equivalent in value to the entire payment amount for gap and future cases. The net effect of this approach is to guarantee a substantial payment to the current plaintiffs, to allow current plaintiffs to vote because their claims have not been fully paid, to set a trigger that limits dilution by gap claims, and to treat all the remaining cases equivalently. However, one problem with this approach is

96. 11 U.S.C. § 524(g)(2)(B)(ii)(bb).

97. See 11 U.S.C. § 524(g)(2)(B)(ii)(v).

that the pre-petition settlement trust is typically larger on a per claim basis than the post bankruptcy trust. Equivalency is determined only within the confines of the post bankruptcy trust, not as between the two trusts together. The justification for this approach is that the company could have made settlement payments prior to filing for bankruptcy, so equivalency is required only for the claims which are paid post petition.

A second approach is to liquidate the current claims before the bankruptcy filing, but pay them, along with the gap and future claims, from a post bankruptcy trust. That trust is bound to pay the pre-bankruptcy liquidated amounts for the current claims, but would use a separate, negotiated grid for the gap and future claims. Again, there is arguably an equivalency problem, but it can be asserted that all post petition claims are handled in substantially the same fashion.

A third solution is to have three trusts: a pre-petition settlement trust for the malignancies, a pre-petition litigation trust for the lower value cases, and a post bankruptcy trust for only malignancy and serious asbestotics gap and future cases. The argument here is that the current, gap, future malignancy, and serious asbestotic cases are paid identically. The less serious, pre-petition cases receive nuisance payments and because there are no provisions to pay any gap or future less serious claims, they will never be filed at all. Therefore, there will never be an equivalency problem.

There are also a variety of other techniques that could be used to solve the equivalency problem. There could be a "collar" on future claims, which would assure that the bulk of the money went to malignancy and serious asbestotic claimants. Under this scenario, all the higher value claims would actually be paid equivalently and the lower value claims would only be paid if money was available. One relief valve would be to allow claims not fully paid to enter the tort system, although there would be restraints on damage awards and payment velocity.

Another approach would be for experts to project that all payments to current and future claimants would be at 100% of full value. If all claimants were paid 100%, there would be equivalency by definition. If a large part of the assets in a bankruptcy trust is equity in the new asbestos-liability-free entity emerging from bankruptcy, financial experts could take into account the increased value of the post bankruptcy equity and predict that there would be sufficient funds to pay all claims in full.

If there is a parent entity that wishes to benefit from § 524(g) protection, there could be a range of funding mechanisms available to a post bankruptcy trust. An evergreen trust that is continuously replenished with annual caps is one possibility. This type of trust would arguably promote equivalency in the payments made over time while providing substantial front-end payments to current claimants. If insurance is involved, the trust could be valued accordingly.

The fundamental dilemma of the prepackaged bankruptcy is illustrated by these mechanisms. The law requires that all claimants be paid the same regardless of their categorization; all claimants must get the same percentage of their claim's value. The current claimants may not agree to vote in favor

of a plan of reorganization unless they are comfortable that they are getting close to normal litigation values or slightly reduced values with greater velocity. The company, on the other hand, does not want to pay full litigation values for both current and future claimants. It will not agree to this process unless it is getting, at the least, some type of discount on normal litigation claim values or preferred treatment for one of its related entities. The pressure, then, is on the gap and future claims to bear the bulk of any discount, a scenario which creates the potential for unfairness.

Great scrutiny must be given, therefore, to the bankruptcy trust and the trust distribution plan. The trust distribution plan must establish the eligibility including the following: the medical and exposure criteria that make claimants eligible for payment, the value to be paid, and the methodology for making those payments. There is typically a payment grid setting forth the relative values of malignancies and non-malignancies.⁹⁸ There is usually also an option for claimants to be paid lower amounts quickly or higher amounts that are subject to individual review. In some plans, there is a predefined minimum percentage, or “collar,” on the amount of the trust to be used for malignancy claims. This prevents an increased number of non-malignancy filings from diluting the money available for the more serious cases.

The trust distribution plan has threshold medical criteria that claimants must satisfy to receive any payment at all.⁹⁹ There must also be categories of proof for product identification, which entitle a claimant to be paid either a standard amount for credible evidence of product exposure or a greater amount for compelling evidence of product exposure.

The organization and governance of the trust, the appointment of trustees, the selection of a trust advisory committee, and the nomination of members of boards of directors, if appropriate, must also be decided. In addition, the administration of the claims resolution facility must be described in great detail.

The funding mechanism for the trust is one of the more difficult issues to be resolved. Section 524(g) requires 50.1% ownership of the debtor if the funding is provided by equity.¹⁰⁰ There can also be various other financial instruments involved, such as an evergreen trust with defined flow rates.¹⁰¹ Insurance assets can also be put into the trust, assuming they can be assigned

98. See generally McGovern, *supra* note 8, at 1747 (discussing malignant versus non-malignant cases).

99. See, e.g., Fairness in Asbestos Compensation Act, H.R. 1283, 106th Cong. § 201 (1999) (establishing medical criteria for plaintiffs); McGovern, *supra* note 8, at 1751 nn.103, 104 and accompanying text (discussing probable medical threshold criteria).

100. See 11 U.S.C. § 524(g)(2)(B)(i)(III).

101. See *In re Johns-Manville Corp.*, 68 B.R. 618, 621 (Bankr. S.D.N.Y. 1986) (establishing, as the central provision of a reorganization plan, an evergreen trust to assume all asbestos liabilities of the corporation).

and that the trust distribution plan does not violate the terms of the insurance contract. Often insurance carriers would prefer to commute their policies and receive the benefits of § 524(g) protection prior to the effective date of the bankruptcy. On other occasions, the insurers prefer to contest issues related to the policies.

B. Varieties of Circumstances

Notwithstanding the similarities in the process for virtually all prepackaged asbestos bankruptcies, there are a number of different financial and corporate packages found among debtors that can alter the negotiation process:

1. Insurance Assets Only
 - a. Negotiation With Carriers
 - b. Negotiation Without Carriers
2. Debtor With Assets Plus Insurance
 - a. Current Claimant Trust
 - b. All Post Bankruptcy Payments
3. Parent or Other Non-Debtor and Debtor With Assets

Where the debtor has few assets other than insurance, there is typically an effort to use the prepackaged bankruptcy negotiations to create an advantageous bargaining posture for the resulting trust in any litigation against the insurance carriers. Knowing this tactic, some carriers attempt to derail the bankruptcy negotiations or attempt to prevent confirmation, either parallel to negotiations or as an independent strategy.

In a situation where the debtor has substantial assets, the negotiations tend to focus on discussions between current and future claimants and the reorganized debtor. Those negotiations can fall apart if there are significant outliers or if a normal “free-fall” bankruptcy is an attractive alternative. When insurance is also a factor, the overall plan may be so complex that there are simply too many complications to consummate a plan.

In the event that the subject corporation has a solvent parent or other entity that desires § 524(g) protection, the amount of potential funding can increase; however, the attractiveness of leaving the entire corporate entity in the tort system altogether also increases.¹⁰² In addition to the larger number of players who must agree and the larger number of issues that must be resolved, there are also larger expectations that must be met.

III. SECTION 524(g) WITHOUT BANKRUPTCY

The purpose of this proposed legislative model is to provide § 524(g) type protections to asbestos defendants without the necessity of their filing for bankruptcy. These protections would be available to entities capable of negotiating with asbestos personal injury plaintiffs to create a court-approved trust that is immediately funded or is funded with a renewing

102. See McGovern, *supra* note 8, at 1755.

mechanism that will provide sufficient assets to pay future asbestos claimants in full. The statute would provide, in effect, a structure for settlement, not litigation, of asbestos liability. The critical elements in the legislation are the following:

1. Qualifications for Use
2. Jurisdiction
3. Stay
 - a. Length
 - b. Scope
4. Plaintiffs' Counsel
 - a. Appointment
 - b. Compensation
 - c. Experts
5. Insurance Counsel
6. Futures Representative
 - a. Selection
 - b. Veto
7. Fund
 - a. Definition
 - b. Security
 - c. Tax
8. Trust Distribution Plan
 - a. Equivalency
 - i. Current Claims
 - ii. Future Claims
 - b. Administrator
 - c. Grid
 - d. Collar
 - e. Medical Criteria
 - f. Exposure Criteria
 - g. Alternative Dispute Resolution (ADR)
 - h. Access to Tort System
 - g. Punitive Damages
 - h. Medical Monitoring
 - i. Green Card
 - j. Audit/Fraud
 - k. Contribution
9. Insurance
 - a. Claims Facility
 - i. Medical
 - ii. Exposure
 - b. Speed
 - c. Assignability
10. Vote

- a. Percentage Necessary
 - i. Value
 - ii. Number
 - b. Filters
 - i. Medical
 - ii. Exposure
11. Injunction
- a. Permanency
 - b. Scope
 - i. Required Relationship
 - ii. Required Contribution

Any corporate defendant involved in asbestos personal injury litigation would be able to benefit from this proposed legislation. Current or projected insolvency would not be necessary in order to trigger the procedures envisioned in the statute.

In order to enhance the rigor of the negotiation process between a solvent defendant and asbestos personal injury plaintiffs, all proceedings would need to be conducted under court supervision. This court could be a single court of appeals for all such cases, a court of appeals in the defendant's jurisdiction, or a district court assigned by a court of appeals or the Judicial Panel for Multi-district Litigation (JPML). The applicable court would obtain jurisdiction upon notice by the defendant; that jurisdiction would continue, however, only for a defined period of time and would be contingent upon certain conditions being met. For instance, there would be a requirement of good faith negotiation that could be guaranteed by a bond or other financial commitment.

If the prerequisites were met, the court would issue an injunction staying all asbestos litigation during the pendency of the negotiations. This stay could apply either to one defendant or to a larger group of entities, but only if the same prerequisites were met for each of those additional entities. The length of the stay could be defined—ninety days or six months, for example—or could be subject to the discretion of the court, but in no event should be longer than one year. Furthermore, the opportunity for the defendant to utilize this procedure would be limited to one occasion.

Upon obtaining jurisdiction, the court would then appoint a committee of plaintiffs' counsel to negotiate on behalf of the current plaintiffs. This appointment process would be similar to the methodology used by transferee judges in multi-district litigations.¹⁰³ In addition, the committee of plaintiffs' counsel and any experts they might need would be compensated from a common benefit fund created by the defendant entities and awarded by the court.

The court would also appoint a futures representative in a manner similar to the appointment of a futures representative in bankruptcy cases.¹⁰⁴ There would be a motion by the debtor supported by the plaintiffs'

103. See MANUAL FOR COMPLEX LITIGATION (THIRD) § 20.22 (1995).

104. See 11 U.S.C. § 524(g)(4)(B)(i).

committee. Agreement of the futures representative would be required in order for the defendant to achieve the protections afforded by the legislation.

In the event that the defendant has insurance for any portion of its asbestos personal injury liabilities, the court would also form a committee to represent those insurers in the negotiations in a manner similar to the manner in which insurers' interests are represented in all major insurance coverage litigation.¹⁰⁵

The two most critical aspects of the negotiations among the defendant, its insurers (if applicable), the current plaintiffs, and the futures representative would be (1) the amount and form of resources necessary to fund the trust that would compensate asbestos claimants, and (2) the approach used to distribute that fund. The court would need to supervise expeditious discovery designed to obtain adequate information on the following: (1) the asbestos litigation and settlement history of the corporate defendant, perhaps on a state-by-state basis; (2) the full financial situation of the defendant; and (3) the details of any available insurance coverage. In the event that experts were needed to deal with financial or litigation issues, they would be hired and paid just as they would be in a multi-district litigation.

Needless to say, the devil is in the details. Because the ultimate outcome would be negotiated rather than adjudicated, the merits and demerits of any plan would be subject to bargaining among all the parties. At the end of the day, the court would need to have a fairness hearing and make a finding that both the amount and method of funding were adequate and secure in order for the plan to meet the requirements mandated by the statute. Rather than an up-front payment in full, the negotiations might lead to an evergreen trust. Alternatively, contributions to the trust could be in the form of notes or stock rather than cash. The key factors would be adequacy and reliability of funding, not form.

Although these negotiations would be difficult, they have been accomplished in many different contexts and there is little doubt that, in the appropriate circumstances, they could be successful. This is not to say that each asbestos defendant would or should avail itself of the provisions of such an act. Particularly solvent defendants might find the statute unnecessary, and many plaintiffs would agree that it is unneeded in that situation. On the other hand, a "free-fall" bankruptcy might be more appropriate than this proposed act for asbestos defendants who are financially overburdened.

The statute would also contain preferable tax treatment for certain aspects of the trust funding. The income from the fund would not be taxable, and every contribution made by a defendant would be treated as an ordinary business expense. Despite substantial litigation to require the federal government to participate financially in any resolution of the

105. See MANUAL FOR COMPLEX LITIGATION (THIRD) § 20.22 (1995).

asbestos claims because of its substantial involvement with asbestos, particularly during World War II, there has been no substantial contribution by the government. The federal government has agreed, however, to forego its subrogation rights against asbestos plaintiffs under the Federal Employers' Liability Act and other federal statutes.¹⁰⁶

The applicable court would also need to maintain continuing oversight to ensure the viability of the fund. In the event of a shortfall, the statute would provide for a pro-rated reduction in benefits similar to those found in trust funds created under current bankruptcy proceedings. The fund would never be reconstituted because any reopening of the proceedings would defeat the purposes of providing financial certainty to participating defendants. This finality would also provide an incentive to the court to make its findings with substantial certainty.

Part of the judicial supervision would be an annual audit of the fund. The precise management of the fund, however, could be left to the negotiation process because its governance would need to follow the precise nature of the currency or currencies. For instance, the administrative requirements for an evergreen trust would be quite different than for a trust funded with stock. In all cases, there would need to be administration with at least the same level of responsibility as an administrator of an employee benefit plan under the Employee Retirement Income Security Act.¹⁰⁷

The treatment of the trust distribution plan (TDP) would be quite complex. The following discussion raises most of the difficult issues in a TDP, but it is debatable how many of these issues should be addressed in the legislation and how many should be left to the negotiation process. For example, most parties would favor the inclusion of the requirement of at least a rough equivalency between current and future claimants in the TDP, but it may not be necessary to have a precise definition of "equivalency." Similarly, most parties would favor an alternative dispute resolution mechanism, but it would probably not need to be prescribed in any detail. Certain other potential provisions in the statute would be more controversial. Examples include a provision imposing a "collar" on malignancy and non-malignancy payments and a provision setting the precise nature or composition of a trust advisory committee made up of plaintiffs' counsel or insurance carriers.

The statute would probably mirror § 524(g) in mandating that present and future claims be valued and paid in substantially the same manner.¹⁰⁸ Liquidation values would probably be based on a grid with faster and lower payments for those who present less extensive evidence of physical harm and exposure. There would be, however, precisely defined minimum medical and exposure criteria required for any payment. For the more seriously injured and exposed, there would be higher payments and more individualized review. The threshold levels, grid amounts, ratios, and

106. See 45 U.S.C. §§ 51-60 (2000).

107. See 29 U.S.C. §§ 1001-1461 (2000).

108. See 11 U.S.C. § 524(g)(2)(B)(ii)(v).

flexibility in payment ranges would probably be left to the negotiations. It would be possible, however, to establish certain statutory requirements. For example, the statute might mandate that malignancies be paid before non-malignancies or that medical monitoring be available for everyone exposed, or perhaps that anyone suffering a more severe harm at a later date could return to receive a second payment.

The TDP would be managed by an administrator and would be subject to a variety of safeguards including internal fraud protection, financial and medical audits, and annual oversight by the court. The defendant, plaintiffs' committee, futures representative, and insurers, if applicable, would have at least minimal access to the administrator's records in order to maintain their confidence in the implementation of the TDP.

Under the proposed statute, payment to a claimant would be treated as a settlement for purposes of calculating contribution and taxes. Any claimants dissatisfied with their offers from the fund could avail themselves of ADR, including arbitration. The statute would provide that, if a case was not resolved, the claimant could access the tort system. The statute would preclude the claimant from receiving punitive damages and would require a payment schedule that would render the compensation of the opt out plaintiff comparable to that of participants in the fund.

The insurance aspects of the proposed statute would probably be among the most controversial and contentious provisions. The intent is to have an even playing field, but the implementation of this intent would be challenging, if not impossible. Most insurers have written their insurance policies based upon assumptions about the tort system. If claims are subject to less rigorous filters or are processed more quickly under the statute than in normal litigation, there could be dire repercussions for the capitalization of the entire insurance industry. Resolving the total potential liability of an insured at the time the statute applies, and then utilizing a claims resolution facility rather than a court to process claims creates a major disadvantage for insurers. An insured that files for bankruptcy, for example, can argue that the entire amount of the insurance coverage is due and payable on the effective date of a plan of reorganization. In addition, as indicated above, the insured has additional bargaining leverage because it can offer the insurer a § 524(g) release if the insurance disputes are resolved prior to the effective date.¹⁰⁹

How, then, can there be sensible treatment of insurers? First, the criteria that determine the amount of payments to claimants and the application of those criteria would probably need to be comparable to the existing tort system of litigation and settlement. The TDP cannot constitute precedent regarding the validity of claims, but there would need to be some security for any future insurance funding. Second, the velocity of payments would

109. See 11 U.S.C. § 524(g).

not be accelerated by virtue of the statutory settlement. The court should attempt to determine, based on history and experience, what the “normal” velocity of the case would be without the statutory acceleration. Third, the insurance carriers would not use the typical litigation delays involved in insurance coverage cases to calculate the timing of their contractual obligations. Fourth, any legal decisions regarding insurance contracts or agreements could be made by a judge not overseeing the negotiations. On balance, the goal is to minimize any deviation from the normal payment of insurance proceeds. The court could not approve the protections afforded by the statute in a way that would disadvantage either the insured or the insurer in the total amount to be paid, its availability, or the velocity of the payment.

Each situation would be different and a statute cannot define with specificity what the guidelines would require in any given setting. Thus, the court would need to have wide discretion to decide whether the proposed settlement between the defendant and tort claimants adversely impacts the insurance status quo. This decision by the court would need to be made within the statutory time frame allowed for the completion of a settlement. Thus, the insurers would have a seat at the table to increase their bargaining power in the negotiations, but would not have the ability to veto a settlement unless the court ruled that the proposed settlement undercut their contractual rights.

Another of the more problematic sections of the proposed statute relates to voting procedures; both the quantum and the qualifications present difficulties. Under § 524(g), at least seventy-five percent of all the asbestos claimants must vote in favor of the plan of reorganization.¹¹⁰ Under traditional bankruptcy standards, there must be a positive vote of at least fifty percent in number and two-thirds in value of the members of a class of claimants.¹¹¹ Neither one of these models is completely satisfactory because each is based upon the assumptions that there is a financially bankrupt debtor and that it is appropriate to give superior bargaining power to creditors. In the § 524(g) without bankruptcy scenario, that assumption is incorrect. The corporate defendant is solvent and has a desire to liquidate and pay its asbestos liabilities in full.

The normal bankruptcy approach to the qualifications for voting is to give each entity and each dollar a vote.¹¹² As a practical matter, each asbestos personal injury claimant is given one vote, and each claim is valued at \$1, in accordance with the relative disease payment outlines in the TDP. The assumption behind these decisions is that the process of evaluating each personal injury claim to establish its validity and its value would simply take too long and be too expensive to accomplish prior to a vote. In a normal bankruptcy, the total value of all asbestos personal injury claims is estimated first; the time for liquidating claims comes after the effective date and is

110. 11 U.S.C. § 524(g)(2)(B)(ii)(iv)(bb).

111. 11 U.S.C. § 1126(c) (2000).

112. *See id.*

accomplished by a claims resolution facility in accordance with the plan of reorganization.

Both the quantum and qualification issues would need to be resolved in the statute. Leaving these issues to the court would not provide the level of predictability necessary to negotiate under the act; these issues are simply too critical to be left open. One way to promote the negotiation process would be to establish strong filters for the voting process by creating an administrative process that could establish a threshold for the right to vote; this threshold would be similar to the threshold which must be met to receive payment under some of the asbestos bankruptcy trusts. For example, a medical report, based upon a medical examination, and an affidavit or other proof of exposure could be required in order for a claimant to vote. Alternatively, the Manville Trust criteria or other established medical and exposure criteria could be applied as a prerequisite to the right to vote.¹¹³

Another alternative would be to eliminate the need for a vote altogether by expanding the court's role to include authority over the issues that might have been resolved by negotiation. If a court were to find that current and future plaintiffs will be paid equivalently and in full, then the court could order all asbestos plaintiffs to participate in the statutorily designed compensation system.¹¹⁴

Finally, the form and scope of an injunction or other relief terminating the defendant's asbestos personal injury liability must be provided by the statute. The statute would need to define what entities could be covered by the permanent injunction and their required levels of contribution. Parent companies, financial entities, insurers, and others similarly situated could be covered by the injunction, but their participation would be based upon contributions similar to those required under § 524(g).¹¹⁵ The court would provide the form of the injunction and the parties would negotiate the entities to be covered, subject to the court's approval.

In order for Congress to pass this type of statute, there would probably need to be at least passive agreement among labor unions, the plaintiffs' asbestos bar, affected corporations, and insurance carriers that such a statute would be favorable. It is likely that claimants would find this statute attractive. Defendant corporations would agree only if they felt that there was a sufficiently even playing field upon which they could negotiate with the plaintiffs' bar. Their focus would be on the number and the quality of those plaintiffs eligible to vote and the total financial contribution required by the TDP. Defendants would compare that amount with their anticipated costs under the existing litigation system and choose the lowest cost

113. See *In re Joint E. & S. Dists. Asbestos Litig.*, 878 F. Supp. 473, 581-601 (1995).

114. See *The Fairness in Asbestos Injury Resolution Act of 2003: Hearings before the United States Senate*, 108th Cong. (2003).

115. See 11 U.S.C. § 524(g).

alternative. Insurers would focus not only on the amount of money required by the plan, but also on the velocity of the payments. The simple fact that under the statute there might be more settlements earlier by more defendants than anticipated would probably lead them to find the current litigation system preferable to the statute. Therefore, for the proposed statute to succeed, the key parties will need to compromise on all these issues.

IV. CONCLUSION

Over sixty companies have filed for bankruptcy because of asbestos litigation. The average length of time that these companies have stayed in bankruptcy has been over four years. There have also been over five prepackaged asbestos bankruptcies. These corporations' length of time in bankruptcy has been less than a year. The total value of the resulting trusts from these bankruptcies is over \$10 billion. The amount currently in controversy is over \$20 billion. There has to be a better way to deal with a national tragedy.

Legislators, judges, and lawyers have concluded that the only appropriate end game for asbestos litigation must be provided by legislation. The existing legal mechanisms are simply inadequate. The task is to find a legislative proposal that can achieve the political support necessary for passage by Congress.

One of the potential solutions is to allow companies to achieve a final resolution of the asbestos claims filed against them by entering into a court-sanctioned negotiation with all the relevant stakeholders. Marketplace bargaining against the backdrop of litigation can provide a more level playing field and achieve socially acceptable finality to these potential liabilities. The concept is to give claimants the same relief that is obtainable in bankruptcy under § 524(g) and use the same protections provided by bankruptcy proceedings, but eliminate the necessity of putting entire enterprises into bankruptcy. The § 524(g) without bankruptcy proposal is a legitimate contender for congressional approval and has the potential to create a statutory end game for asbestos litigation.