Section 524(g) Without Compromise: Voting Rights and the Asbestos Bankruptcy Paradox

S. Todd Brown

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SECTION 524(g) WITHOUT COMPROMISE: VOTING RIGHTS AND THE ASBESTOS BANKRUPTCY PARADOX

S. Todd Brown*

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I. INTRODUCTION

Given a choice, many people would be inclined to pay an undocumented debt to a local loan shark ahead of a secured loan from their bank. After all, the consequences of failing to pay the loan shark could make losing a house or car seem mild by comparison. Once debtors enter bankruptcy, however, they are no longer free to make this choice; the Bankruptcy Code\(^1\) recognizes only legal rights to payment and establishes a firm system for allocating priorities among claims. Practical extra-legal incentives and consequences do not modify this reality—there is no “pay it or sleep with the fishes” exception to the bankruptcy priority scheme.

Even this most fundamental bankruptcy principle has been corrupted in the equitable netherworld of asbestos defendant Chapter 11 reorganizations. Legislative and judicial efforts to make asbestos-driven bankruptcies more efficient, maximize assets available to compensate current and future asbestos victims, and preserve viable businesses have, over time, provided a small group of law firms\(^2\) a de facto veto power over any asbestos bankruptcy plan. Given the common presumption that this veto power is absolute, most asbestos defendant-debtors and bankruptcy courts have been extremely deferential to the Controlling Firms’ demands; even to the point of approving schemes that violate black-letter bankruptcy law and raise significant professional responsibility concerns.

The result is an unusual paradox—the only way for debtors to obtain the asbestos plaintiff votes required to have a reorganization plan confirmed is to accept terms that will

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\(^2\) These law firms are hereinafter referred to as the “Controlling Firms.”
render the plan unconfirmable or, at least, unable to withstand a sustained challenge on appeal. Even if asbestos defendant-debtors ultimately overcome the paradox, they may be discouraged from pursuing a timely bankruptcy filing or choose increasingly risky alternatives outside of bankruptcy, thereby depleting their assets and reducing their ability to reorganize when they ultimately file Chapter 11. Under any scenario, whatever assets remain for future victims will be insufficient to compensate them for their injuries.

This Article begins with an overview of the interwoven histories of asbestos tort and bankruptcy law. Against this backdrop, the second section questions the basic policy and administrative assumptions that produced the asbestos bankruptcy paradox. Finally, I suggest several basic, yet critical, judicial responses that will help restore the integrity of asbestos bankruptcy administration, preserve due process for future victims and advance bankruptcy law's key goals of efficiency, fairness and finality.

II. ASBESTOS TORT AND BANKRUPTCY: THE DOWNWARD SPIRAL

A. A Brief History of Asbestos Tort and Bankruptcy

The history of asbestos in America is a history of failure—failure of asbestos producers to protect their employees and the public, of physicians and researchers to sound the alarm and of federal and state governments to acknowledge and address asbestos-related illness. For more than half a century, senior asbestos industry executives carefully orchestrated a systematic campaign to conceal the dangers of asbestos exposure. The success of this campaign over such
an extended period is due not only to the long latency period between exposure to asbestos fiber and the appearance of symptoms, but also to the acquiescence of medical professionals, regulators and politicians. These failures allowed producers to delay the introduction of asbestos safety programs and ensure that the financial burdens associated with asbestos disease remained squarely on the shoulders of the victims.

This history of failure did not end once the dangers of asbestos became widely known, as early asbestos cases failed to provide meaningful recovery to victims due to scorched earth defense tactics and victim compensation systems that were ill-suited to the unique nature of asbestos illness. Even after the previously unfathomable scope of the asbestos industry's deception was uncovered, the inherent difficulties created by the long latency period of asbestos disease—including the evidentiary barriers to proving exposures that occurred decades earlier—continued to undermine asbestos personal injury cases.


5 See Bowker, *supra* note 3, at 131-44, 161-85 (discussing litigation and settlement tactics of W.R. Grace); Anthony Z. Roisman et al., *Preserving Justice: Defending Toxic Tort Litigation*, 15 FORDHAM ENVTL. L. REV. 191, 213 (2004) ("The history of asbestos litigation is a lesson in the costs of intransigence. In the early days of asbestos litigation, like the early days of tobacco litigation, defendants successfully resisted claims. Even after it became obvious to the world that both asbestos and tobacco claims had merit, defendants continued to resist the claims. That intransigence is the principal cause of the high transaction costs and not the toxic tort litigation system.").


7 Id. at 260.
Eventually, the pendulum started to swing in favor of plaintiffs and, when it did, defendants were faced with crushing asbestos liabilities. Although state and federal governments were disinclined to regulate the asbestos industry, state courts and legislatures played an active role in modifying the tort system to make it more "plaintiff-friendly." At the same time, the emerging evidence of the asbestos industry's scheme to mislead the public and its aggressive litigation practices made courts and juries far more receptive to plaintiffs' requests for large compensatory and punitive awards. After decades of deception, obfuscation and indifference to the personal costs the industry inflicted on the public, the industry's days were numbered.

B. Asbestos Defendant Bankruptcies

When Johns-Manville petitioned for bankruptcy protection in 1982, stunned lawyers and victims' rights advocates were up in arms. As the largest bankruptcy in history at the time, Manville's Chapter 11 was an easy target. Critics railed against the filing as an abuse of the bankruptcy process and an unconscionable tactic to delay payment to the sick and dying. On the surface, these


9 Hensler, supra note 6, at 278.


11 White, supra note 3, at 194.

12 Elmer W. Lammi, Asbestos Victims Denounce Firm's Bankruptcy Tactic, PHILA. INQUIRER, Feb. 11, 1983, at A8; Larry Reibstein, Manville's Move Turns Hopes to Dust in Asbestos Lawsuits, PHILA. INQUIRER, Aug. 27, 1982, at C12 (noting plaintiffs' counsel's characterization of the Manville bankruptcy filing as "a ploy to delay the suits while buying time for congressional action on a compensation fund for asbestos victims").

13 Warren Brown, Surviving 'Creative' Bankruptcy; As A Business Strategy, Firms Find that it Exacts a Heavy Price, WASH. POST, Nov. 6,
criticisms reflected a basic, common-sense concern: how could a seemingly healthy company with assets in excess of $2 billion and fixed liabilities of roughly $1 billion possibly be a candidate for bankruptcy?

Unlike its predecessor, however, the new bankruptcy law did not require imminent or actual insolvency for a debtor to be eligible for relief. This was no mere oversight; the insolvency requirement was omitted to serve the goals of "preserving going concerns and maximizing property available to satisfy creditors" by ensuring timely access to the bankruptcy process. And as the principal asbestos personal injury litigation defendant, Manville faced potentially limitless liability—a fact that its auditors emphasized in issuing qualified opinions of the company's operating reports for two years prior to its bankruptcy.

1988, at H1 ("Manville's filing shocked the nation and sparked an explosion of charges that the company was trying to avoid its legal and moral responsibilities through a reworded bankruptcy statute."); Mark Clayton, Manville Pulling Out of the Asbestos Quagmire, CHRISTIAN SCI. MONITOR, Oct. 3, 1988, at 12 ("Immediately after Manville filed, lawyers for those harmed by asbestos charged a 'perversion' of the bankruptcy laws and castigated the company for ducking its responsibility."); Judge Criticizes Johns-Manville, BOSTON GLOBE, Feb. 14, 1986, at 71 (quoting U.S. District Judge H. Lee Sarokin, "History will record that the Johns-Manville Corp. manipulated the judicial system so as to delay to thousands of claimants and possibly deny completely to some their day in court to present asbestos-related injuries . . .").


15 As explained in the Report of the Commission on the Bankruptcy Laws of the United States: "The process should encourage resort to it, by debtors and creditors, that cuts short the dissipation of assets and the accumulation of debts. Related commencement of a case may kill an opportunity for reorganization or arrangement." REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. Doc. No. 93-137, pt. 2, at 75 (1973); H.R. Rep. No. 95-595, at 220 (1977); see also In re SCL Carbon Corp., 200 F.3d 154, 163 (3d Cir. 1999) ("It also is clear that the drafters of the Bankruptcy Code understood the need for early access to bankruptcy relief to allow a debtor to rehabilitate its business before it is faced with a hopeless situation.").

16 Tamar Lewin, Asbestos Now Company Peril, N.Y. TIMES, Aug. 10, 1982, at D2; see also Brown, supra note 13, at H1 (quoting former Manville
Thus, in denying a motion to dismiss Manville's Chapter 11 case, Bankruptcy Judge Lifland reasoned:

[T]he drafters of the Code envisioned that a financially beleaguered debtor with real debt and real creditors should not be required to wait until the economic situation is beyond repair in order to file a reorganization petition. The “Congressional purpose” in enacting the Code was to encourage resort to the bankruptcy process. This philosophy not only comports with the elimination of an insolvency requirement, but also is a corollary of the key aim of Chapter 11 of the Code, that of avoidance of liquidation . . . .

In the instant case, not only would liquidation be wasteful and inefficient in destroying the utility of valuable assets of the companies as well as jobs, but, more importantly, liquidation would preclude just compensation of some present asbestos victims and all future asbestos claimants. This unassailable reality represents all the more reason for this Court to adhere to this basic potential liquidation avoidance aim of Chapter 11 and deny the motions to dismiss. Manville must not be required to wait until its economic picture has deteriorated beyond salvation to file for reorganization.17

Of course, like other Chapter 11 debtors, early asbestos bankruptcy debtors were concerned less with remaining under bankruptcy protection than their ability to emerge from bankruptcy as financially healthy companies. However, the long latency period for asbestos disease that facilitated decades of concealing the dangers of asbestos now worked against these asbestos defendant-debtors; they could resolve known claims in bankruptcy, but a potentially overwhelming number of new claims could arise well into the

C.E.O W. Thomas Stephens as saying “[t]here were not a hell of a lot of choices available when the board made that decision [to file bankruptcy] in 1982.”.

future. This fact complicated the early asbestos debtors' efforts to reorganize as both a practical and legal matter—Chapter 11 debtors can reorganize only if they establish that they will not be forced back into bankruptcy, and most asbestos plans that fail to resolve future asbestos liabilities could not satisfy this requirement.

Even if the Bankruptcy Code authorized courts to enjoin future claimants from suing the reorganized companies, due process ordinarily requires giving parties an opportunity to contest the modification of their rights, and it is not possible to provide this opportunity to those who may not become aware of their injury until months or years after plan confirmation. And as much as bankruptcy may vary from

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18 Bankruptcy Code § 1129(a)(11) (A reorganization plan may only be confirmed if it "is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan . . . "); see also In re UNR Industries, Inc., 725 F.2d 1111, 1119 (7th Cir. 1984) ("If future claims cannot be discharged before they ripen, UNR may not be able to emerge from bankruptcy with reasonable prospects for continued existence as a going concern."); In re Johns-Manville Corp., 36 B.R. 743, 757 (Bankr. S.D.N.Y. 1984) (noting the need to address future claims in order for reorganization to occur).

19 See Taylor v. Sturgell, 128 S.Ct. 2161, 2175 (2008) ("[O]ur decisions emphasize the fundamental nature of the general rule that a litigant is not bound by a judgment to which she was not a party. Accordingly, we have endeavored to delineate discrete exceptions that apply in 'limited circumstances.'") (citations omitted); Lankford v. Idaho, 500 U.S. 110, 120-21 (1991) (noting "the importance that we attach to the concept of fair notice as the bedrock of any constitutionally fair procedure."); Hansberry v. Lee, 311 U.S. 32, 40 (1940) ("It is a principle of general application in Anglo-American jurisprudence that one is not bound by a judgment in personam in a litigation in which he is not designated as a party or to which he has not been made a party by service of process."); Grannis v. Ordean, 234 U.S. 385, 394 (1914) ("The fundamental requisite of due process of law is the opportunity to be heard."); Vale Chem. Co. v. Hartford Accident & Indem. Co., 516 A.2d 684, 688 (Pa. 1986) ("Essential to the adversary system of justice, and one of the basic requirements of due process, is the requirement that all interested parties have an opportunity to be heard.").

20 In re Waterman Steamship Corp., 141 B.R. 552, 559 (Bankr. S.D.N.Y. 1992) ("[N]o future Asbestosis Claimant who, by definition, had yet to manifest any detectible injury prior to confirmation, could be deemed to have relinquished substantive rights when, even if that
ordinary litigation, the mere happenstance that proceedings occur in a bankruptcy forum does not eliminate the obligation to satisfy the dictates of due process.\textsuperscript{21} On the

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\textsuperscript{21} Martin v. Wilks, 490 U.S. 755, 762 n.2 (1989) (Bankruptcy proceedings may terminate preexisting rights of absent parties only "if the scheme is otherwise consistent with due process.") (emphasis added); N. Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 117 (1982) ("Bankruptcy proceedings remain . . . subject to all of the strictures of [the Due Process Clause].") (White, J., dissenting); Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 589 (1935) ("The bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment."); In re Hanson, 397 F.3d 482, 487 (7th Cir. 2005) (noting that the unique nature of bankruptcy does not remove the need to satisfy due process); Educ. Credit Mgmt. Corp. v. Repp (In re Repp), 307 B.R. 144, 149 (B.A.P. 9th Cir. 2004) (concluding that student loan discharge in Chapter 13 plan failed to provide sufficient notice to satisfy due process); In re Ruehle, 296 B.R. 146, 164-5 (Bankr. N.D. Ohio 2003) (discussing due process in a student loan discharge bankruptcy dispute and concluding "Due process is not to be sliced, diced and disguised with sauce. Due process must be served whole, without garnish"); In re Kewanee Boiler Corp., 198 B.R. 519, 536-37, (Bankr. N.D. Ill. 1996) ("The Bankruptcy Code encourages businesses to reorganize through rewriting debt. However, the Code cannot justify disregarding due process concerns and bankruptcy notice requirements to the detriment of persons affected and benefit businesses seeking to eliminate liability and their known creditors who receive notice."); Laura B. Bartell, \textit{Due Process for the Unknown Future Claim in Bankruptcy—Is This Notice Really Necessary?}, 78 Am. Bankr. L.J. 339, 347-48 (2004) ("The Constitution has thus given us two fundamental policies: one policy requiring that property not be taken without due process of law, and another policy allowing Congress to provide for uniform bankruptcy legislation. If possible, we must interpret the laws that Congress has enacted under its constitutional authority in a way that meets the requirements of the Due Process Clause."). As the First Circuit explained, the distinction drawn between ordinary cases and bankruptcy proceedings is a narrow one:

There are specialized proceedings, such as bankruptcy, reorganization, or probate proceedings, where a party may be barred from future litigation by his mere failure to intervene. Cases in that category would seem limited, however, to ones where by statute, rule or practice,
other hand, the inability to address future asbestos liability could force an otherwise viable company into liquidation and thereby undermine future victims’ prospects for recovery.\textsuperscript{22} The preservation of customary due process would come at the cost of the very property rights due process is intended to protect. Thus, binding future claimants in spite of their absence would be to their benefit, as it presumably would be to other constituencies.\textsuperscript{23}

Against this backdrop, the so-called “futures problem” was less one of determining whether modified due process was appropriate than one of determining the form that it should take. The recognition that liquidation could doom recovery prospects for future claimants did not, of course, strip these claimants of the right to a fair, equitable process to guard against encroachment upon their individual interests any more than it did other parties whose recoveries could be threatened by liquidation. Any substitute process, then, needed to ensure that current creditors would not gorge themselves at the expense of future claimants.

In \textit{Manville}, the focal point of this modified framework was the appointment of a legal representative for future victims, who played the role of the “honest broker”\textsuperscript{24} among the conflicting current interests and ensured that any negotiated resolution was not purchased at the expense of future victims. With substantial contributions from the legal representative, Manville and its creditors ultimately adopted what has become known as the “trust-injunction” approach. Put simply, asbestos plaintiffs were enjoined from initiating intervention, after notice, is invited, or at least where the affected parties have reason to understand that their rights will be foreclosed unless timely asserted in the original proceeding.

Griffin v. Burns, 570 F.2d 1065, 1071 n.7 (1st Cir. 1978).


litigation against Manville and certain others, the plaintiffs' claims were channeled to a trust funded by these parties and the trust became responsible for processing and satisfying these claims.25

In spite of the considerable financial contributions to the early trusts, it soon became apparent that new asbestos plaintiffs would receive, at best, pennies on the dollar for their claims.26 The dramatic expansion of asbestos tort litigation drove defendants into bankruptcy. These bankruptcies left the remaining defendants with considerably greater liability27 and sent lawyers searching for new defendants.28 This cycle continues to this day.29


26 See Stephen Labathon, The Bitter Fight Over the Manville Trust, N.Y. TIMES, July 8, 1990, at F1 (noting how the Manville Trust was effectively "looted" within two years after its inception); see also Richard A. Nagareda, MASS TORTS IN A WORLD OF SETTLEMENT 75 (2007) ("The Manville trust proved to be a perilous institution . . . with large numbers of claims quickly overwhelming its initial capitalization.").

27 Anup Malani & Charles Mullin, The Effect of Joint and Several Liability on the Bankruptcy Rate of Defendants: Evidence from Asbestos Litigation 14 (Working paper, May 27, 2004), available at http://ssrn.com/abstract=552081 ("[If no companies had gone bankrupt between 1990 and 2002, the asbestos liabilities of solvent, major asbestos defendants might have been as small as two-fifths their present size."); Nagareda, supra note 26, at 167 (noting the domino effect of the Manville bankruptcy).

28 See Patrick Hanlon & Anne Smetak, Asbestos Changes, 62 N.Y.U. ANN. SURV. AM L. 525, 547 (2007) (noting that the dramatic rise in asbestos claim filings during the 1990s "led to an unprecedented wave of asbestos bankruptcies" and resulted in a broader search for defendants); White, supra note 3, at 196-97.

29 Lester Brickman, On the Theory Class's Theories of Asbestos Litigation: The Disconnect Between Scholarship and Reality, 31 PEPP. L. REV. 33, 55 (2003) ("[Manville's bankruptcy] posed a severe problem for plaintiff attorneys, setting off a concerted effort to find other deep pockets to supplant and supplement Manville, a process which inures to this day as seventy companies have joined Manville in entering bankruptcy."); see also Victor E. Schwartz, Mark A. Behrens & Rochelle M. Tedesco,
C. The New Asbestos Bankruptcy Landscape

The legal foundations for the trust-injunction mechanism in *Manville* and other early cases—the court’s equitable authority and largely unsettled interpretations of key provisions of the Code—were, at best, unstable. Although courts sitting in bankruptcy may “issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code]” and enjoy considerable equitable authority to address the situations that come before them, this power is very limited and may not be used to circumvent or rewrite the express requirements of the Code. The resulting uncertainty

Addressing the “Elephantine Mass” of Asbestos Cases: Consolidation Versus Inactive Dockets (Pleural Registries) and Case Management Plans that Defer Claims Filed by the Non-Sick, 31 PEPP. L. REV. 271, 280 (2003). As one author summarized:

Once again, evidence that a serious problem of “too many defendants” exists is reflected in what presumably sympathetic critics say about the situation. Thus, Senior U.S. District Court Judge Weinstein has observed: “If the acceleration and expansion of asbestos lawsuits continues unaddressed, it is not impossible [to foresee] that every company with even a remote connection to asbestos may be driven to bankruptcy.” And prominent plaintiffs’ lawyer Richard Scruggs observes that asbestos litigation has become an “endless search for a solvent bystander.”

James A. Henderson, Jr., *Asbestos Litigation Madness: Have the States Turned a Corner?*, 20-23 MEALEY’S LITIG. REP. ASBESTOS 19 (2006) (modification in original). Indeed, it appears that searching out new asbestos defendants has become a cottage industry in itself. See, e.g., *Asbestos Litigation: Fire in the Courts; Bankruptcies Explode as the Asbestos Inferno Rages On*, TRIAL LAWYERS INC., 2007, http://www.triallawyersinc.com/html/part05.html (private company’s report on the general state of asbestos litigation, supporting and bolstering the search by asbestos plaintiff lawyers for new defendants, including any company that has ever used asbestos in its products).

Bankruptcy Code, § 105(a).

Raleigh v. Ill. Dep’t of Revenue, 530 U.S. 15, 24-25 (2000) (“Bankruptcy courts are not authorized in the name of equity to make wholesale substitution of underlying law controlling the validity of creditors’ entitlements, but are limited to what the Bankruptcy Code itself
weighed on the stock of the reorganized companies to the
detriment of the trusts established to pay asbestos claims and
discouraged companies from adopting similar
approaches until after their litigation costs depleted
significant assets that would have otherwise been available
for victims.

To address these concerns, Congress amended the
Bankruptcy Code in 1994 to include Section 524(g), which
largely codified the approach utilized in Manville, and

provide.

140 CONG. REC. S4521, S4523 (daily ed. Apr. 11, 1994) (statement of
Sen. Brown) ("Without a clear statement in the code of a court's
authority to issue such injunctions, the financial markets tend to discount the
securities of the reorganized debtor."); see also Elihu Inselbuch, Some Key
Issues in Asbestos Bankruptcies, 44 S. TEX. L. REV. 1037, 1040 (2003) ("The
enactment of Section 524(g) removed the uncertainty surrounding Johns-
Manville and made it possible to transmute the equity value of that
company into money so that claimants could be paid.").

140 CONG. REC. H10752, H10765 (daily ed. Oct. 4, 1994) ("The
procedure is modeled on the trust/injunction in the Johns-Manville case,
which pioneered the approach a decade ago in response to the flood of
asbestos lawsuits, it was facing."); Andrew W. Caine & Thomsen Young,
Need Post-Confirmation Injunctive Relief? Get Some Class, 14 AM. BANKR.
Section 524(h), which retroactively authorized the trust-injunction mechanisms used in plans confirmed prior to the amendments. As Senator Heflin explained:

Mr. President, this statutory affirmation of the court's existing injunctive authority is designed to help asbestos victims receive maximum value. It does so by assuring investors, lenders, and employees that the reorganized debtor has indeed emerged from Chapter 11 free and clear of all asbestos-related liabilities other than those defined in the confirmed plan of reorganization, and that all asbestos-related claims and demands must be made against the court-approved trust. This added certainty will ensure that the full value of such a trust's assets—the securities upon which it relies in order to generate resources to pay asbestos claims—can be realized.

1. The Structure of Section 524(g)

Section 524(g) authorizes an asbestos bankruptcy reorganization plan "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 [an asbestos trust established in accordance with Section 524(g)]" under

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34 Bankruptcy Code, § 524(h).

35 140 CONG. REC. S14461, S14464 (daily ed. Sept. 12, 1994). Senator Brown also described Section 524(g)'s role in a similar fashion:

Without a clear statement in the code of a court's authority to issue such injunctions, the financial markets tend to discount the securities of the reorganized debtor. This in turn diminishes the trust's assets and its resources to pay victims. The amendment is intended to eliminate that speculation so that the marketplace values the trust's assets fairly.

140 CONG. REC. S4521, S4523 (daily ed. Apr. 11, 1994).
specified conditions. Among other things, these conditions include the appointment of a "legal representative for the purpose of protecting the rights of persons that might subsequently assert [asbestos-related] demands" and the establishment of a trust that treats similar current and future claims in "substantially the same manner." In addition, at least 75% of any class or classes of current asbestos claimants must vote in favor of the plan.

Although Section 524(g) establishes a supplemental mechanism for the reorganization of asbestos defendants, it does not supplant the Code's other requirements. As the Third Circuit explained:

Section 524(g) provides a special form of supplemental injunctive relief for an insolvent debtor facing the unique problems and complexities associated with asbestos liability. Channeling asbestos-related claims to a personal injury trust relieves the debtor of the uncertainty of future asbestos liabilities. This helps achieve the purpose of Chapter 11 by facilitating the reorganization and rehabilitation of the debtor as an economically viable entity. To achieve this relief, a debtor must satisfy the prerequisites set forth in § 524(g) in addition to the standard plan confirmation requirements.

2. The Right to Vote and the Power to Veto

Like any other class of creditors, asbestos tort creditors are entitled to vote for or against any plan of reorganization that impairs their claims. Understanding how asbestos

36 Bankruptcy Code, § 524(g)(1)(B).
37 Id. at § 524(g)(4)(B)(i).
38 Id. at § 524(g)(2)(B)(ii)(V).
39 Id. at § 524(g)(2)(B)(ii)(IV)(bb).
40 In re Combustion Eng'g, Inc., 391 F.3d 190, 234 (3d Cir. 2004) (emphasis added).
41 Bankruptcy Code Section 1124(1) provides that most claims will be considered impaired unless the plan "leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder"
creditor voting rights have given rise to a unique veto power requires an appreciation of how these rights differ from ordinary voting rights and the manner in which asbestos claimants' votes are cast in Chapter 11.

a. Voting Rights Generally

Section 1129 outlines the necessary conditions that any plan of reorganization must satisfy in order to be confirmed. Among these, the Bankruptcy Code requires certain minimum evidence of creditor support, which is gauged by soliciting and processing creditor votes for or against the plan. As the Third Circuit explained, "By providing impaired creditors the right to vote on confirmation, the Bankruptcy Code ensures the terms of the reorganization are monitored by those who have a financial stake in its outcome."3

In most instances, individual creditors or creditor groups will find it difficult to transform their voting rights into a veto power. First, Section 1129(a)(8) requires only the acceptance of each impaired class, not of each impaired creditor. Under Section 1126(c), an impaired class is deemed to accept a plan if it is approved by eligible creditors "that hold at least two-thirds in amount and more than one-half in number of the allowed claims of such class held by creditors . . . that have accepted or rejected such plan." In a class with several distinct, perhaps conflicting interests, forging a cohesive unified voting block can be the bankruptcy equivalent of herding cats. Moreover, skillful plan proponents may be able to shatter this voting block after it is

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of such claim or interest . . . ." Thus, even changes that arguably improve a creditor's rights may constitute impairment under the Code. In re L & J Anaheim Assocs., 995 F.2d 940, 942-43 (9th Cir. 1993); In re Rhead, 179 B.R. 169, 177 (Bankr. D. Ariz. 1995) ("[A]ny change of a creditor's rights, whether for the better or for the worse, constitutes impairment . . . .").

42 In re SM 104 Ltd., 160 B.R. 202, 218 & n.35 (Bankr. S.D. Fla. 1993) ("Section 1129(a)(10) was intended not to give [an individual] lobby a veto power, but merely to require 'some indicia of creditor support' for confirmation of a proposed Chapter 11 plan.").

43 In re Combustion Eng’g, Inc., 391 F.3d at 244.
forged by making modest concessions to discrete creditors or groups within the class.

Even if these obstacles are somehow overcome, plan proponents will often be able to structure the plan to allow them to "cram down" the plan under Section 1129(b). Under this provision, a plan may be confirmed over its rejection by an impaired class "if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan." This power is only available, however, if "at least one class of claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any insider." 44

The emphasis on class acceptance in Sections 1129(a)(8) and 1129(b) means that the ability of an individual creditor to block a plan through the voting process depends, in part, on how claims are classified. And since plan proponents enjoy considerable discretion in classifying claims, 45 recalcitrant creditors generally find it difficult to garner sufficient votes within their class and ensure that the plan will not be "crammed down" over the objection of that class.

b. Section 524(g) Voting Rights

If a plan that includes asbestos claims does not invoke Section 524(g), the asbestos creditors' ability to block confirmation through voting is the same as any other creditor's under Section 1129. As noted previously, if the plan attempts to invoke the trust-injunction authorized under Section 524(g), the injunction may issue only if the court determines, among other things, "a separate class or classes of [asbestos] claimants... votes, by at least 75

44 Bankruptcy Code, § 1129(a)(10).

45 Id. at § 1122(a) requires only that claims within a class be "substantially similar." Thus, courts have long recognized that "[a] debtor in bankruptcy has considerable discretion to classify claims and interests in a chapter 11 reorganization plan." In re Wabash Valley Power Ass'n, 72 F.3d 1305, 1321 (7th Cir. 1995).
percent of those voting, in favor of the plan. . . ." Section 524(g) does not include the ability to "cram down" an injunction if fewer than 75% of asbestos creditors vote in favor of the plan.\textsuperscript{47}

The absence of a "cram down" option under Section 524(g) removes a significant obstacle to transforming voting rights into a veto power, but it does not resolve the practical difficulties associated with gaining control over enough claims to block a Section 524(g) injunction. This obstacle, however, is far less significant for asbestos creditor claims than other types of claims; over the years, control over the overwhelming majority of asbestos claims has been consolidated in the hands of a small number of law firms.\textsuperscript{48} In bankruptcy, these firms assert the power to speak and cast large blocks of votes on behalf of their clients.\textsuperscript{49}

An additional difficulty arises due to the fact that the voting conditions under Sections 1129 and 524(g) are wholly independent—acceptance by 75% of those in an asbestos creditor class for the purposes of Section 524(g) may not be sufficient to qualify as "acceptance" under Sections 1126(c) and 1129. As Judge Bernstein recognized in Quigley, given the wide disparity among the potential values of asbestos claims, it is possible that a large block of low-value claimants will vote in favor of a plan (thereby satisfying the super-

\textsuperscript{46} Id. at § 524(g)(2)(B)(ii)(IV)(bb).

\textsuperscript{47} Century Indem. Co. v. Congoleum Corp. (In re Congoleum Corp.), 426 F.3d 675, 680 n.4 (3d Cir. 2005) ("Pre-packaged bankruptcies employing a channeling injunction are not eligible for the "cram down" provision contained in 11 U.S.C. § 1129(b)(1) which allows the bankruptcy court to confirm a plan of reorganization over creditors' objections in certain circumstances.").

\textsuperscript{48} Id. at 679 ("A unique feature of asbestos personal injury litigation is the fact that a small group of law firms represents hundreds of thousands of plaintiffs."); see also Frances McGovern, Asbestos Legislation II: Section 524(g) without Bankruptcy, 31 PEPP. L. REV. 233, 247-48 (2004) (noting concentration of representation among a small group of lawyers).

\textsuperscript{49} In re Congoleum, 426 F.3d at 680 ("The realities of securing favorable votes from thousands of claimants to meet the 75% approval requirement forces debtors to work closely with the few attorneys who represent large numbers of injured claimants.").
majority "number of claimants" requirement of Section 524(g)) while a much smaller number of high-value claimants will vote against the plan (thereby preventing the plan from satisfying the two-thirds "value of claims" requirement of Section 1126(c)). Thus, the failure to obtain this level of support may be fatal to any plan seeking to employ the trust-injunction mechanism under Section 524(g).

This combination of factors creates a considerable barrier to confirmation of any asbestos bankruptcy plan: lawyers representing both a large number of claimants and those representing claimants with large value claims must be accommodated. Although representation of most asbestos claimants is consolidated under a handful of law firms—each arguably in position to block plan confirmation—no one lawyer or firm controls enough claims to ensure a plan will be confirmed. This effectively gives each of them the ability to veto any Section 524(g) plan.

D. The Paradoxical Nature of Modern Asbestos Bankruptcies

1. Redefining “Compromise” Under the Asbestos Veto Threat

Against this backdrop, it should come as no surprise that the Section 524(g) “veto power” over asbestos reorganization plans has fundamentally altered the consensus-building model of Chapter 11. Consensus is now more about the satisfying the demands of the Controlling Firms than

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51 Plevin, supra note 25, at 285 ("The inventory-holding law firms claim a power of attorney for all of their claimants, which they can vote en masse, giving them huge blocks of potential creditor votes for approval of any asbestos bankruptcy plan and, at the other extreme, veto power over any such plan.")
obtaining mutual sacrifices among constituencies.\textsuperscript{52} The resulting "negotiations" have thus been plagued by three basic traits: attorney dominance; concealment of critical information; and exclusion of dissenting voices. Each of these traits is inconsistent with the traditional bankruptcy negotiation model.

a. Attorney Dominance and Self-Dealing

The presumption that the Controlling Firms hold an unassailable veto power leaves debtors and other parties in interest with the classic Hobson's choice—reorganization on the Controlling Firms' terms or no reorganization at all. In the interest of building this single-constituency-driven consensus, debtors have been extremely deferential to the Controlling Firms' demands. Recent bankruptcies were largely driven (and in some cases originally suggested) by one or two Controlling Firms, who, at times, demanded and received direct\textsuperscript{53} and indirect\textsuperscript{54} financial and other incentives to settle their clients' claims and reach out to their

\textsuperscript{52} Todd R. Snyder & Deanne C. Siemer, \textit{Reply To Barliant: Asbestos Pre-Packaged Bankruptcies: Apply The Brakes Carefully And Retain Flexibility For Debtors}, 13 AM. BANKR. INST. L. REV. 801, 803 (2005) (arguing that Congress intended to give plaintiffs' lawyers greater control over asbestos bankruptcies).

\textsuperscript{53} See \textit{In re Congoleum Corp.}, 362 B.R. 167, 187 n.14 (Bankr. D.N.J. 2007) (noting that the debtor paid lawyers at two Controlling Firms $1 million each and then "buried" a provision precluding any avoidance actions to recover these funds in the plan with "no explanation for this munificence"); see also \textit{In re Combustion Eng'g, Inc.}, 295 B.R. 459, 476 (Bankr. D. N.J. 2003) ($20 million payment to asbestos attorney Joe Rice from the parent of the debtor); Ronald Barliant, Dimitri G. Karcazes & Anne M. Sherry, \textit{From Free-Fall to Free-For-All: The Rise of Pre-Packaged Asbestos Bankruptcies}, 12 AM. BANKR. INST. L. REV. 441, 468 (discussing conflicts of interest arising from payments to asbestos counsel in Combustion Engineering and Congoleum).

\textsuperscript{54} \textit{Congoleum}, 362 B.R. at 186 n.12 (noting that two cases presented by one Controlling firm were settled pre-petition at $8 million each while most other mesothelioma claims in another class would be capped at $265,000); In \textit{Century Indemnity}, the Third Circuit also noted the preferred treatment afforded select claimants in the Congoleum case. \textit{In re Congoleum.}, 426 F.3d at 680.
colleagues in the bar. In some cases, the Controlling Firms enjoyed largely unchecked control over key settlement terms and the selection of critical players in the process, including the appointment of the future claimants' legal representative and certain of the debtors' counsel.

In most cases, the claims brought by key asbestos counsel (or their co-counsel) were promised higher distributions and faster payment than could be obtained in tort or a "free-fall" bankruptcy. Among other things, the claims of favored law firms would be settled and granted security interests in advance of any bankruptcy filing. Some claims were settled without any review, and the criteria used to review other claims were largely dictated by the lawyers themselves. Moreover, claim reviewers were often hand-picked by or

55 Baron & Budd, P.C. v. Unsecured Asbestos Claimants Comm., 321 B.R. 147, 160 (D.N.J. 2005) ("Of particular relevance, is evidence that the Motley Rice and Weitz & Luxenberg firms, which together purport to 'speak for' over 75 percent of all asbestos claimants against Congoleum, may not in fact 'represent' individual claimants in the traditional sense of an attorney-client relationship, but rather, they represent other attorneys who, in turn, represent individual claimants.").

56 Congoleum, 362 B.R. at 196 ("[T]he claimants [sic] representatives were the architects of the Claimants Agreement, which provided for uneven treatment of asbestos creditors and created many of the confirmation problems that have plagued this case.").

57 A "free-fall" bankruptcy is one in which most, if not all, of the critical negotiations take place after the debtor is under bankruptcy protection.


59 Barliant, supra note 53, at 454-58.

affiliated with some of the law firms submitting claims. In some cases, one or more of the Controlling Firms also demanded a share of less influential lawyers' fees as a condition of obtaining preferred status for their clients' claims.

A critical component of this approach was to structure the settlements as "pre-packaged" bankruptcies. These cases tend to be confirmed quickly because support is effectively locked up beforehand, thereby reducing the uncertainty associated with a free-fall bankruptcy case. In an asbestos bankruptcy, this can be particularly helpful because it provides the debtor some comfort that the super-majority voting requirement can be satisfied before it leaps into Chapter 11.

Unlike traditional pre-packaged bankruptcies, recent asbestos pre-packs were driven largely by the Controlling Firms' desire to circumvent the Bankruptcy Code's equal treatment provisions. As noted at the outset of this article,

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63 Pre-packaged bankruptcies are cases in which solicitation and voting occur before the case commences. See, e.g., In re United Artists Theatre Co., 315 F.3d 217, 224 n.5 (3d Cir. 2003); In re Pioneer Fin. Corp., 246 B.R. 626, 630 (Bankr. D. Nev. 2000).

64 John D. Ayer et al., Out-of-court Workouts, Prepacks and Pre-arranged Cases: A Primer, AM. BANKR. INST. J. Apr. 2005, at 16 ("Unlike a traditional chapter 11 case, the prepackaged bankruptcy is negotiated and accepted by creditors before a proceeding is commenced in the bankruptcy court. In theory, therefore, the prepackaged bankruptcy itself can be quick (sometimes as fast as 30-45 days), and therefore less costly and damaging to the restructuring company."); Robert K. Rasmussen & Randall S. Thomas, Timing Matters: Promoting Forum Shopping by Insolvent Corporations, 94 NW. U. L. REV. 1357, 1375 (2000) ("The prepackaged bankruptcy thus provides the firm with the benefit of class-wide voting to minimize holdout problems, while simultaneously minimizing the time the firm spends in bankruptcy.").

65 In fact, in one asbestos pre-pack, the asbestos plaintiffs' lawyer who largely controlled its design and structure testified that "there's no reason
the Bankruptcy Code includes clear default rules—including those governing the assessment, valuation, priority and payment of claims—that may not be ignored for convenience or perceived necessity once the debtor files bankruptcy. Moreover, steps taken in the ninety days prior to the petition date may be unwound after the case is filed.\textsuperscript{66} Thus, in order to provide the incentives necessary to obtain the Controlling Firms' support and ensure that those incentives would not be unwound easily once the case was filed, the parties needed to finalize these critical steps at least ninety days before commencing Chapter 11 proceedings.

for -- for this pre-pack to have occurred unless the [preferred asbestos claims] were receiving their security interest . . . .” \textit{In re Congoleum Corp.,} 362 B.R. 167, 185 n.10 (Bankr. D.N.J. 2007) (quoting the deposition of Perry Weitz). As Plevin et al., explained:

\begin{quote}
The now-common structure used in asbestos pre-packs—a pre-petition trust that pays a subset of current claimants nearly full value for their claims, followed by a post-petition trust that pays other current claimants and future claimants a much smaller percentage of their claims, with significantly more stringent qualifying requirements—financially benefits the lawyers for the preferred claimants, since they typically receive, as contingent fee payments, as much as 40 cents of each dollar paid to their claimants. Because their clients get paid more, and sooner, than other claimants, these lawyers personally benefit when the plan is structured in such a fashion. If the plan treated all claimants the same, paying all current claimants through the mechanism of a post-petition trust, the lawyers for the current claimants would make less money—even assuming the bankruptcy court or the trust made no effort to restrict the portion of a trust beneficiary's payment that could be paid as a contingent fee. This, as much as anything, explains why asbestos pre-packs are structured in such a byzantine fashion that is so different than any "conventional" asbestos bankruptcy case.\end{quote}


\textsuperscript{66} Bankruptcy Code § 547(b)(4)(A) (ninety-day preference period).
b. Concealment of Critical Information

The Controlling Firms' ability to provide sufficient asbestos votes to guarantee confirmation is only as strong as (a) the validity of the underlying claims and (b) the Controlling Firms' authority to control the votes of those claims. Put differently, if either element is successfully challenged, the law firms' support may no longer provide sufficient assurance that a plan negotiated with those firms will succeed. Even if the law firms are able to establish both elements, any litigation over these significant points may delay confirmation significantly. To that end, pre-pack proponents have found it desirable to avoid inquiry into these issues to the extent possible.

c. Authority to File and Vote on Behalf of Asbestos Victims

The Controlling Firms' legal authority to appear and vote in asbestos bankruptcy cases is purely representative; they nominally speak for victims, not themselves. Under the Federal Rule of Bankruptcy Procedure 2019(a), attorneys are ordinarily required to substantiate their authority to represent multiple creditors. Although this basic...

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67 In relevant part, Bankruptcy Rule 2019(a) provides:

In a . . . chapter 11 reorganization case, except with respect to a committee appointed pursuant to § 1102 or 1114 of the Code, every entity or committee representing more than one creditor . . . shall file a verified statement setting forth (1) the name and address of the creditor or equity security holder; (2) the nature and amount of the claim or interest and the time of acquisition thereof unless it is alleged to have been acquired more than one year prior to the filing of the petition; (3) a recital of the pertinent facts and circumstances in connection with the employment of the entity or indenture trustee, and, in the case of a committee, the name or names of the entity or entities at whose instance, directly or indirectly, the employment was arranged or the committee was organized or agreed to act; and (4) with reference to the time of the employment of the entity, the organization or formation of the committee, or
requirement might suggest that parties in interest are able to scrutinize the Controlling Firms' authority in asbestos bankruptcy cases, most bankruptcy courts have required Controlling Firms only to file "sample" authorizations and allowed Controlling Firms to withhold "co-counsel" and similar agreements altogether. In short, in most cases, it is impossible to discern who a given law firm represents or the scope of that representation, notwithstanding Bankruptcy Rule 2019(a).

d. Claim Filings and Support

Given the dollar values involved and the inherent difficulties in establishing an enforceable asbestos personal injury claim,\(^6\) those parties in interest that oppose an asbestos pre-pack—primarily insurers and creditors who believe they have been disenfranchised—may have substantial financial incentives to pursue claim-by-claim objections.\(^9\) In practice, these potential "spoilers" enjoy the appearance in the case of any indenture trustee, the amounts of claims or interests owned by the entity, the members of the committee or the indenture trustee, the times when acquired, the amounts paid therefor, and any sales or other disposition thereof. The statement shall include a copy of the instrument, if any, whereby the entity, committee, or indenture trustee is empowered to act on behalf of creditors or equity security holders.

FED. R. BANKR. P. 2019(a).

\(^6\) For example, many claimants struggle to identify the source of exposure by the time they are diagnosed. Lawrence Martin, Asbestos Lung Disease: A Primer for Patients, Physicians, and Lawyers, J. CONTROVERSIAL MED. CLAIMS, Nov. 2001, at 15, 17 (2000) ("[I]n about half the [mesothelioma] cases, there is no history of asbestos exposure, and the cause is unknown."). This may be even more difficult with second- and third-tier defendants who now make up a far larger portion of the pool of asbestos defendants. See Jeffrey M. Davidson, Theories of Asbestos Litigation Costs—Why Two Decades of Procedural Reform Have Failed to Reduce Claimants' Expenses, 7 NEV. L.J. 73, 91 (2006).

\(^9\) Even the extremely lenient Manville Trust medical audit revealed that the trust may have paid $190 million for fraudulent or inflated claims from 1996 to 2001. Roger Parloff, Mass Tort Medicine Men, AM. LAw., Jan. 3, 2003, at 97. Thus, those inclined to challenge claims may reasonably
little, if any, opportunity to do so because courts routinely excuse counsel from filing proof of claim forms and supporting documentation. The debtors’ schedules contain sparse information, if any, and even the minimal information provided to asbestos claim processors is rarely subjected to independent scrutiny. In those rare cases, the parties investigating the claims are required to execute strict confidentiality agreements (or are bound by confidentiality orders), so the prospects that any dramatic discoveries will become public are limited. This is true even where the discovery has little to do with the asserted bases for confidentiality; for example, evidence that a law firm has filed claims on behalf of long-deceased victims or asserted claims for clients that have no idea who the attorneys are may remain outside public scrutiny.

Although the potential for fraud is obvious, the suggestion that a particular lawyer or law firm is guilty of misconduct in a given case is not one to be made lightly. In fact, courts regularly bar inquiry without specific evidence of fraud in the cases before them. This is true even when the known facts suggest, at a minimum, that the firms could not have performed even a cursory investigation of the claims filed before dumping them on a bankruptcy settlement processor. Moreover, because basic information about

believe that the costs of doing so are justified by potential savings in claims paid.

See, e.g., In re Congoleum Corp., 2008 Bankr. LEXIS 303, at *12-13 (denying request to set a bar date for asbestos claims because, among other reasons, doing so would open the door to an avalanche of claim objections); In re Quigley Co., 346 B.R. 647, 653 (Bankr. S.D.N.Y. 2006) (“Many asbestos cases, including this one, excuse asbestos claimants from the requirement to file claims because of the practical difficulties involved.”).

Bankruptcy Rule 1007(c) requires debtors to file schedules of assets and liabilities within fifteen days after the filing of a voluntary Chapter 11 petition. Although Official Forms 6D (Schedule D—Creditors Holding Secured Claims) and 6F (Schedule F—Creditors Holding Unsecured Nonpriority Claims) require only minimal information about claims—the name and address of the claimant, the dollar amount, and the date the claim was incurred—even this information is largely omitted from the debtors’ schedules in many asbestos bankruptcy cases.
asbestos claims is not available, it is ordinarily impossible for opponents to cross-reference claims across bankruptcy trusts and cases to unearth wholly inconsistent representations. In short, parties in interest face a conundrum—fraudulent claims cannot be investigated unless they are discovered, but they cannot be discovered unless they are investigated.

e. Exclusion of Dissenting Voices

In many recent asbestos pre-packs, two litigious blocks—insurers (who are usually expected to provide most of the funding for the trusts) and disfavored creditors (including some asbestos claimants)—were generally excluded from pre-petition negotiations. These parties have considerable interests that are contrary to the Controlling Firms. Concessions to these parties would weaken recoveries for Controlling Firms; and involving these other parties without providing any significant concessions could provide dramatic evidence that any proposed plan was collusive and fundamentally unfair, in contravention of the Code. Moreover, allowing these parties to participate would require giving them additional information as negotiations evolved—information that could be used against the plan proponents in the likely event that the disfavored parties rejected any deal that the Controlling Firms demanded.

The efforts to exclude insurers gained considerable ground following the Fuller-Austin bankruptcy. In that case, the insurers' objections to confirmation were rejected on standing grounds because the plan included a "super-peremptory" clause that nominally preserved all of the insurers' rights in coverage litigation. After the plan was confirmed, however, the bankruptcy trust switched course and claimed that the plan was binding on the insurers. The

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72 See Plevin et al., supra note 65, at 889.
74 As the California Court of Appeals later noted in reversing the trial court's order, the plan proponents advised the bankruptcy court:
trial court agreed with the plan proponents; although the insurers were actively excluded from challenging the plan in the bankruptcy case, its confirmation required them to pay the full value of their policies immediately.\textsuperscript{75} After Fuller-Austin, one of the leading architects of asbestos pre-packs characterized his resulting leverage over insurers in these cases as god-like,\textsuperscript{76} so the decision to actively exclude

Fuller-Austin Insulation Co. v. Highlands Ins. Co., 38 Cal. Rptr. 3d 716, 725 (Cal. Ct. App. 2006). Once the state court litigation resumed following Fuller-Austin's confirmation, however, "Fuller-Austin adopted a position it did not take in the bankruptcy proceedings; it asserted that its confirmed Plan was a final adjudication that established its liability to asbestos claimants and therefore obligated appellants to pay the full ALV established by the bankruptcy court with respect to each asbestos claim." \textit{Id.} at 726.

\textsuperscript{75} As explained by the California Court of Appeals:

The trial court agreed with Fuller-Austin's new position, ruling that "Fuller-Austin's confirmed bankruptcy plan is a binding federal court judgment and adjudication that establishes Fuller-Austin's liability and its legal obligations to pay damages to all pending and future asbestos claimants." It found that the bankruptcy proceedings constituted an "actual trial" of Fuller-Austin's liability; alternatively, it reasoned that the Plan constituted a "settlement" for which appellants' consent was unnecessary because appellants had received notice of and an opportunity to participate in the bankruptcy proceedings.

\textit{Id.}

\textsuperscript{76} In characterizing this leverage at a conference in June 2003, Scott Gilbert analogized the pre-pack proponents' and insurers' positions to the lead character and a gang of thugs, respectively, in a scene from the film \textit{Bruce Almighty}. In this scene, Bruce demands an apology from the gang. After the lead thug responds, "When a monkey comes out of my butt, you'll
insurers from negotiations following *Fuller-Austin* is hardly surprising.

2. Case Study: *Congoleum*'s Difficult March Through Bankruptcy

Congoleum Corporation and its predecessors in interest produced asbestos-containing flooring products until the early 1980s. During its first two decades as an asbestos personal injury defendant, the company successfully defended the overwhelming majority of its lawsuits. Like many other second-tier asbestos personal injury defendants, however, the number of lawsuits filed against Congoleum increased dramatically during the first part of this decade. During negotiations concerning two mesothelioma personal injury cases with Perry Weitz, a key member of one of the Controlling Firms, he suggested that the company consider pursuing a pre-packaged bankruptcy case.

Congoleum's subsequent bankruptcy planning and filing followed the same model that other confirmed and then-

get your sorry;” Bruce, now holding divine powers, makes precisely that happen. (Author notes).

77 Congoleum Corp., Quarterly Report (Form 10-Q), at 10 (Sept. 30, 2002).

78 Most of the cases against Congoleum were dismissed during this period, and the company's aggregate defense and settlement costs during this time were roughly $13.5 million, which was paid by the company's primary insurer. See Id. at 10-11.

79 For example, as of December 31, 2002, Congoleum faced twenty-four times more asbestos personal injury lawsuits than it faced just three years earlier (including a nine-fold increase in the number of plaintiffs naming Congoleum as a defendant). Congoleum Corp. Annual Report (Form 10-K), at 51 (Dec. 31, 2002) (noting that there were approximately 16,156 known asbestos personal injury lawsuits on behalf of 56,567 individuals pending against the company as of December 31, 2002); Congoleum Corp. Annual Report (Form 10-K), at 10 (Dec. 31, 1999) (approximately 670 asbestos personal injury lawsuits on behalf of 6,246 individuals were pending against the company as of December 31, 1999).

pending asbestos bankruptcies used. Unfortunately for Congoleum, critical elements of its asbestos pre-pack strategy had not been tested to final judgment; many disputes had been settled before appeals were final, and disputes over other significant issues were still being litigated during Congoleum's pre-bankruptcy planning period. By the time that courts started condemning the asbestos pre-pack model, Congoleum was firmly committed to this strategy. Thus, Congoleum's experience provides a framework for discussing many critical legal developments in asbestos bankruptcies and also illustrates the Controlling Firms' and other parties' respective perceptions of the process as these developments occurred.

a. Basic Process and Structure

The basic elements of asbestos pre-packs before Congoleum—control, exclusion, and preferential treatment—are easy to identify in Congoleum's case. First, consistent with the control demanded by key lawyers in other cases, two lawyers from Controlling Firms directed the Congoleum process as self-styled "Claimants Counsel." For the debtors, a significant portion of the bankruptcy planning and early settlement negotiations were handled by Gilbert Heintz & Randolph, the firm recommended by one of the Claimants Counsel. Kenesis Group, LLP, an affiliate of Gilbert Heintz, was hired to review and process claims. Kenesis, in turn, "subcontracted its work to The Clearinghouse LLC, an organization owned by an individual who was on leave of absence from a position as a paralegal at [Claimant Counsel] Joseph Rice's law firm."

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81 Id. at 680 ("The pre-petition activity that occurred in [Congoleum] is fairly typical of that in a number of asbestos pre-packaged plans.").
82 Id. at 680-81.
83 Id. at 681 (reversing order retaining debtor's law firm).
84 Id. at 683.
85 Id. at 684 n.11. Kenesis ultimately agreed to acquire The Clearinghouse prior to the filing of Congoleum's Chapter 11 petition. Id.
Second, the parties largely followed the script for excluding those who might object to the terms of the deal. Insurers were excluded from any meaningful input in the pre-bankruptcy planning and negotiations, and the pre-petition future claimants' representative was not hired until after the deal was essentially done. Although initially left out of discussions, attorneys representing a block of the most seriously ill asbestos victims were ultimately brought into the pre-petition discussions, apparently in response to this group's successful tactics in other cases.

Third, and most significant, the parties structured the pre-petition settlements and the bankruptcy plan such that comparable claims were divided into subclasses, and these separate classes were secured at different levels. Thus, asbestos plaintiffs with similar injuries would be entitled to substantially different recoveries under the plan.

On December 31, 2003, after the preference period passed, Congoleum commenced its Chapter 11 case. However, significant problems for the Congoleum pre-pack were percolating even before its filing. Among other things, the company used by Congoleum to process asbestos claims had been roundly criticized for its conduct in another asbestos case just a few months earlier, and the Congoleum plan proponents' hard-line strategy against its insurers had not yielded any significant insurance settlements. To the contrary, it backfired badly, as most of these insurers dug in for a long, arduous battle.

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86 Stroumtsos Order, supra note 58, at 10-11.
87 Plevin et al., supra note 25, at 306-7.
88 For example, one of the lead attorneys for the "Cancer Claimants" in the Combustion Engineering bankruptcy, Steve Kazan, was added to the pre-petition asbestos claimants' committee in Congoleum. See Proposed Disclosure Statement With Respect to Tenth Modified Plan at §3.3, In re Congoleum Corp., No. 03-51524 (KCF), Dkt. No. 4565.
89 Id. at 680-81.
b. The ACandS Confirmation Order

Perhaps the most staggering early blow to the Congoleum case came less than one month after Congoleum filed its petition: Judge Newsome’s opinion and order denying confirmation of a similar asbestos pre-pack plan in the ACandS bankruptcy case. Congoleum’s pre-pack was designed in large part on the ACandS model, involved many of the same key players, and even allowed claimants to rely on claim eligibility determinations from the ACandS case. Judge Newsome’s opinion went further than merely questioning the legality of the plan; he criticized its fundamental assumptions and the equities involved, limiting Congoleum’s ability to distinguish ACandS in any significant way.

First, although the ACandS plan may have satisfied the super-majority voting requirement of Section 524(g)(2)(B)(ii)(IV), Judge Newsome concluded that the approach used to obtain the lawyers’ support made it impossible to “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,” as required by Section 524(g)(2)(B)(ii)(V):

The trust established in ACandS’ plan of reorganization does nothing of the kind. Not only does the plan discriminate between present and future claims, it pays similar claims in a totally disparate manner by giving preferential treatment to certain claimants who are secured by insurance proceeds. Those security interests were not granted based upon the medical condition of those claimants, but rather because, for whatever reason, they were first in line and able to carve out seemingly unassailable security interests. Nothing could be further from what the drafters of Section 524(g) intended.91

Judge Newsome further concluded that the debtors gave far too much authority to opposing counsel in the claim review process, contrary to Section 1129(a)(3)'s "good faith" requirement:

The plan under consideration falls short of this [good faith] standard in nearly every respect. Although ACandS was represented during the course of the prepackage negotiations, the correspondence among plaintiffs' asbestos counsel presented at trial indicates that the plan was largely drafted by and for the benefit of the prepetition committee. It was the prepetition committee that drafted (or more likely directed debtor's counsel in drafting) the prepetition trust, and apparently chose the trustee for the trust; it was the prepetition committee that decided how the security agreement would be crafted and how many classes of security interests would be formed; and it was the prepetition committee that decided who was going to get what. ACandS was there to do their bidding, having been thrown overboard by Irex to keep what was left of that company afloat. Given the unbridled dominance of the committee in the debtor's affairs and actions during the prepetition period, its continued influence flowing from its majority status on the post-petition creditors committee, and the obvious self-dealing that resulted from control of the debtor, it is impossible to conclude that the plan was consistent with the objectives and purposes of the Bankruptcy Code.\(^\text{92}\)

Finally, because the arrangement differentiated claims based on extra-legal factors (i.e., the influence of the lawyers bringing the claims and timing) rather than the "legal character" of the claims, its classification scheme would be particularly prejudicial to some of the most seriously ill asbestos claimants:

Although the plan may meet the technical classification requirements of § 1122 and § 1129(b), it is fundamentally unfair that one claimant with non-

\(^{92}\) Id. at 43 (citation omitted).
symptomatic pleural plaques will be paid in full, while someone with mesothelioma runs the substantial risk of receiving nothing. Both should be compensated based on the nature of their injuries, not based on the influence and cunning of their lawyers. The court is informed that other judges have confirmed plans with such discriminatory classifications. This judge cannot do so in good conscience.93

All of these issues plagued the Congoleum case at least as much as they had in ACandS. Still, the Controlling Firms balked at any significant departures from the asbestos pre-pack model, generally, or the terms of the deal in Congoleum, specifically. Moreover, because Judge Newsome’s opinion also reinforced previous case law limiting insurer standing, the Congoleum plan proponents may have reasonably believed that the ACandS ruling would effectively allow them to exclude insurers from the confirmation hearings in Congoleum, thereby removing the only parties that were likely to raise significant challenges to the plan in that case.

c. Combustion Engineering

Later that year, the Third Circuit reversed an order confirming the plan in another similar asbestos pre-pack case, Combustion Engineering. Much like Judge Newsome’s opinion in ACandS, the Combustion Engineering opinion was highly critical of the asbestos pre-pack strategy and its emphasis on form over substance. After rejecting the lower court’s decision to enjoin asbestos actions against the debtor’s non-debtor affiliates,94 the court zeroed in on the inequitable treatment of claims under the scheme:

The pre-petition transfer in this case also implicates the fundamental bankruptcy policy of “equality of distribution among creditors.” In this regard, we consider the bankruptcy scheme as an integrated whole in order to evaluate whether Plan confirmation

93 Id.
94 In re Combustion Eng’g, Inc., 391 F.3d 190, 233-38 (3d Cir. 2004).
is warranted. Viewing the Combustion Engineering pre-pack bankruptcy as a whole, the record reveals that it may lack the requisite equality of distribution among creditors. The Plan, as it relates to asbestos claimants, consists of two elements: the pre-petition CE Settlement Trust and the post-petition Asbestos PI Trust. Under this interdependent, two-trust framework, the Certain Cancer Claimants, the future asbestos claimants, and other non-parties to the pre-petition settlement appear to receive a demonstrably unequal share of the limited Combustion Engineering fund.95

The panel further questioned the disparate treatment for (a) current impaired and unimpaired claims and (b) favored current claims and future demands.96 Finally, the court concluded that the pre-petition manipulation of claims was designed for the improper purpose of buying critical votes:

Here, Combustion Engineering made pre-petition payments to current asbestos claimants that exceeded any recovery obtainable by other current asbestos claimants (such as the Certain Cancer Claimants) in bankruptcy. As a result, the CE Settlement Trust participants, many of whom received as much as 95% of the full liquidated value of their claims pre-petition, had little incentive to scrutinize the terms of the proposed Plan. Rather, their incentive appears to have been otherwise, given that the favorable pre-petition settlements were conditioned, at least implicitly, on a subsequent vote in favor of the Plan.97

With respect to the representation of future claimants, the Third Circuit expressed concern about the absence of a future claimants' representative during the critical early stages of the negotiations.98 As a result, the modifications

95 Id. at 241-42 (citations omitted).
96 Id. at 242.
97 Id. at 244 (citations omitted).
98 Id. at 245 ("Here, the first phase of the integrated, global settlement—the establishment of the CE Settlement Trust—included
made during this stage undermined the facially overwhelming vote in favor of the plan:

Had the future and other non-participating asbestos claimants been adequately represented throughout the reorganization process, including the CE Settlement Trust negotiations, then perhaps the corresponding stub claims would demonstrate the “indicia of support by affected creditors” required under § 1129(a)(10). But they were not. Instead, as discussed, a disfavored group of asbestos claimants, including the future claimants and the Certain Cancer Claimants, were not involved in the first phase of this integrated settlement. The result was a Plan ratified by a majority of “stub votes” cast by the very claimants who obtained preferential treatment from the debtor. As noted, an estimated 99,000 of the approximately 115,000 “valid” confirmation votes appear to have been stub claim votes. Given this structural inadequacy, the Plan may have lacked the requisite “indicia of support” among creditors.99

Practically speaking, however, Combustion Engineering may have inadvertently reinforced the pre-pack strategy in Congoleum. Although the court found numerous flaws with the approach, it also effectively limited the right to appeal these issues to the “Cancer Claimants” who were excluded from negotiations in that case but included in the Congoleum negotiations. With the only group with standing to appeal these issues firmly in support of the Congoleum pre-pack, then, the plan proponents may have reasonably believed that the plan could survive any challenge in spite of its many flaws. To that end, most of Congoleum’s subsequent plan amendments involved several modest, superficial changes but did not address the fundamental concerns identified in Combustion Engineering.100

99 Id. (citations omitted).
100 See discussion infra Section I.D.2.f.
d. Century Indemnity v. Congoleum Corp.

Another blow to Congoleum's pre-pack arose within the case: the disqualification of Gilbert Heintz, the debtors' counsel in its pre-petition planning stage and its post-petition "special insurance counsel." After receiving repeatedly favorable rulings limiting insurers' standing to litigate and appeal critical aspects of asbestos pre-packs, the plan proponents may have believed that the appeal of the firm's retention would fail regardless of the significant ethical and substantive problems that the firm's activities raised. In stark contrast to its discussion of insurer standing in *Combustion Engineering*, however, the Third Circuit concluded that insurers and their counsel had standing to appeal the firm's retention:

Here, the insurers are entitled to standing even under the more restrictive standard applied to bankruptcy proceedings. The retention of special insurance counsel is an important preliminary matter that will profoundly affect the determination of the validity of a proposed plan *ab initio*. It is an issue based on procedural due process concerns that implicate the integrity of the bankruptcy court proceeding as a whole. The retention of Gilbert as special insurance counsel will affect the resolution of issues that may directly affect the rights of insurers and fairness to the asbestos claimants.\(^1\)

After concluding that the firm's role in the bankruptcy required its application to be evaluated under Section 327(a) rather than the far less restrictive standards of Section 327(e),\(^2\) the court noted the firm's repeated refusals to

\(^{101}\) Century Indem. Co. v. Congoleum Corp. (*In re Congoleum Corp.*), 426 F.3d 675, 685 (3d Cir. 2005).

\(^{102}\) Section 327(a) applies to professionals retained "to represent or assist the trustee [or debtor in possession] in carrying out [its] duties under this title", 11 U.S.C. § 327(a), while Section 327(e) authorizes the retention of attorneys "for a specified special purpose . . . ." 11 U.S.C. § 327(e). Attorneys retained under either provision must not hold or represent an "interest adverse to the estate", but attorneys retained under Section 327(a) must also be "disinterested." 11 U.S.C. § 327. Among other
disclose critical information about its relationship with Perry Weitz and asbestos plaintiffs with claims against Congoleum.\textsuperscript{103} Even without this additional information, however, the panel readily concluded that the firm was not “disinterested” under Section 327(a).\textsuperscript{104}

After the Gilbert Heintz firm’s retention was reversed, additional documents that were not disclosed in connection with its retention or in response to numerous applicable document requests (and omitted from its privilege logs) during the case demonstrated that the firm’s contractual relationships with claimants’ counsel were far more sweeping than previously realized.\textsuperscript{105} Of particular relevance to this discussion, the firm was recommended to Congoleum by Perry Weitz—and settled two of his clients’ asbestos personal injury claims against Congoleum for $8 million each—less than one month after Weitz and Gilbert Heintz entered into a previously undisclosed global asbestos fee-sharing agreement.\textsuperscript{106} Even if it is in any way conceivable that this global relationship somehow slipped the minds of the attorneys at the time that Gilbert Heintz agreed to the $16 million settlement—an amount exceeding the company's reasons, the Third Circuit concluded that the firm “continues to participate actively in formulating and revising the plan” and reasoned that its efforts to distinguish its advice concerning insurance recovery and other matters “might be likened to attempts at using a scalpel to carve a bowl of soup.” In re Congoleum, 426 F.3d at 692. Accordingly, the court readily concluded that the firm's retention had to be considered under the heightened standard of Section 327(a).

\textsuperscript{103} Id. at 690.

\textsuperscript{104} Id. at 692 (“Our discussion of the Rules of Professional Conduct demonstrates that Gilbert also cannot meet the Bankruptcy Code’s requirement of disinterestness contained in section 327(a). Its status as co-counsel with Weitz and its ownership interest in Kenesis represent factors which prevent Gilbert from being completely loyal to Congoleum’s interests.”).

\textsuperscript{105} Declaration of Kerry A. Brennan Relating to Debtors’ Objection to Motion of Gilbert, Heintz & Randolph LLP for a Stay Pending Appeal with Respect to the GHR Disgorgement Order, In re Congoleum Corp., No. 03-51524 (KCF), Dkt. No. 3971 (Bankr. D.N.J. 2006).

\textsuperscript{106} Id. (“Relationship Letter” from Scott Gilbert to Perry Weitz, dated Sept. 3, 2002).
aggregate asbestos defense and settlement costs throughout its history—as Congoleum's nominal counsel, the ongoing concealment of such a fundamental conflict of interest over a period of years raises, at best, serious questions about the firm's claims that it acted in good faith in that case.\textsuperscript{107} As the bankruptcy court noted from the bench, "the conflict at issue here existed from the outset of the case and was of such a nature that it necessarily permeated every aspect of [Gilbert Heintz]'s decision-making."\textsuperscript{108}

e. Coverage Litigation

Given the extensive role that Gilbert Heintz played in the Congoleum pre-pack and the firm's widely-criticized conflicts of interest in the case, few were surprised when the trial court overseeing the lawsuit between Congoleum and its insurers ruled against the company on May 18, 2007. Still, notwithstanding the various plan proponents' efforts to downplay the significance of the ruling, Judge Stroumsilos' opinion undermined whatever rationalizations might have remained available to support confirmation of a plan that relied upon key elements of the pre-pack. In addition to the practical impact of the order, barring recovery from the only substantial source of funds for the trust, many of the legal and factual justifications for the order—pervasive conflicts of interest, payment of claims that would not be paid in the tort system, inflated claim values and weak exposure and medical criteria—were relevant to plan confirmation.\textsuperscript{109} Sounding a now familiar refrain, the court reserved its harshest criticism for Gilbert Heintz's "actual conflict of interest because of its relationship with Weitz and his law firm, including their joint representation of claimants with


\textsuperscript{108} Transcript of February 7, 2007 Hearing at 19, \textit{In re Congoleum Corp.}, No. 03-51524, Dkt. No. 3582.

\textsuperscript{109} Stroumsilos Order, \textit{supra} note 58, at 10-11.
claims against Congoleum”\textsuperscript{110} and its “collu[sion]” with that firm to manufacture liability.\textsuperscript{111}

f. Congoleum’s Response to Date

To date, Congoleum’s original “pre-pack” plan has been amended a dozen times, with many of those amendments evincing the company’s struggle to address the flaws identified by the various courts without alienating the Controlling Firms. Indeed, the one amendment that contemplated the elimination of the preferential treatment demanded by Claimants Counsel’s pre-petition—the sixth amended plan—was subsequently withdrawn by the debtors when they learned that one of the Claimants Counsel, Perry Weitz, would not support it.\textsuperscript{112} After repeated amendments that were, at best, superficially responsive but substantively insufficient to address the courts’ concerns, the bankruptcy court stressed that the continued separate classification of comparable asbestos claims would render any plan

\textsuperscript{110} Id. at 11-12.

\textsuperscript{111} Id. at 11. Less directly, the court’s reservations about the manner in which the firm and Claimants Counsel “negotiated” with insurers are also apparent:

GHR, Rice and Weitz invited the insurers to meetings on March 13, 2003 in South Carolina and March 20, 2003 in New York; however, no real negotiations took place at that meeting. One meeting was delayed while Scott Gilbert and Joe Rice were enjoying the afternoon looking at custom made motorcycles. In addition at each of the meeting the insurance carriers were told discussions would advance only after they agreed to tender their policies. The insurers did not receive a draft of the Claimant Agreement until March 7, 2003. Congoleum later provided the insurers with revised drafts of the settlement documents, but only after an agreement in principle had been reached with Weitz and Rice without consulting the insurers.

\textsuperscript{112} See Proposed Disclosure Statement with Respect to Tenth Modified Plan at §5.13, \textit{In re} Congoleum Corp., No. 03-51524(KCF), Dkt. No. 4565.
"unconfirmable on its face." As the bankruptcy court explained:

In this case, the fact that the Debtors granted pre-petition security interests to certain favored creditors and then purposefully waited more than 90 days to file in order to protect those security interests evinces a scheme designed to circumvent the Code's equal distribution requirements. As a result, confirmation of a plan that in any way recognizes those pre-petition security interests is not permissible.

The legal conditions of confirmation may ultimately be satisfied in Congoleum, but its example is understandably discouraging for other companies that may benefit from a bankruptcy filing. Even if the Controlling Firms embrace a legally-sufficient plan in Congoleum at this late stage, history suggests that they will continue exercising the asbestos veto power to press the boundaries of the Code in other cases. Moreover, the asbestos veto threat may discourage companies from filing until after the Controlling Firms have stripped considerable assets from the estate through the tort system—if they cannot front-load recoveries in bankruptcy, they can use the threat of liquidation to prevent bankruptcy filings and continue front-loading recoveries in tort. Thus, rather than advancing the reorganization goal of bankruptcy law, the asbestos veto may be employed to prevent companies from pursuing timely restructuring plans.

3. Prospects for Future Asbestos Bankruptcies

Following the Third Circuit's rejection of the Combustion Engineering plan, asbestos defendants understandably became uncomfortable with the asbestos pre-pack strategy. Crane Co., for example, expressly noted the opinion as "a material change in the case law regarding Section 524(g) transactions" and terminated its Master Settlement

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114 Id. at 186.
Agreement with the Controlling Firms.\textsuperscript{115} The company remains embroiled in asbestos litigation in the tort system and recently increased its pre-tax asbestos provision to more than $1 billion to account for asbestos liability through 2017.\textsuperscript{116}

The precise number of pre-pack negotiations that may have been derailed by the Combustion Engineering reversal or other recent developments in asbestos bankruptcies is difficult to quantify because of the secretive nature of these negotiations. Moreover, recent state tort reform efforts, Judge Janis Jack's blistering condemnation of client recruiting screenings in the silica MDL, and other developments in asbestos personal injury tort cases have given many asbestos defendants considerable breathing room; so at least some defendants may be taking a wait-and-see approach to asbestos bankruptcy planning. At present, however, considerable uncertainties remain.

III. A CRITICAL EXAMINATION OF THE ASBESTOS BANKRUPTCY PARADOX

The difficulties encountered by Congoleum highlight the degree to which bankruptcy law is guided by a number of distinct, sometimes conflicting principles.\textsuperscript{117} As noted previously, one of the key goals of the Bankruptcy Code is to promote reorganization—a goal that Section 524(g) is clearly intended to advance. Practically speaking, however, the super-majority vote requirement may be impossible to satisfy without providing asbestos creditors significant financial incentives, which, as demonstrated in ACandS and

\textsuperscript{115} Crane Co., Annual Report (Form 10-K), at 17 (Dec. 31, 2006).
\textsuperscript{116} Crane Co., Annual Report (Form 10-K), at 18 (Dec. 31, 2007).
\textsuperscript{117} Patrick J. Borchers, Choice of Law Relative to Security Interests and Other Liens in International Bankruptcies, 46 AM. J. COMP. L. 165, 171-72 (1998). \textit{But see In re Greene}, 103 B.R. 83, 89 (S.D.N.Y. 1989) (in a different context, noting that "the need to ensure the integrity and fairness of the process while at the same time providing assurance to the debtor that the fresh-start goal will be reasonably and timely realized, barring complications, if the process is utilized in good faith" are "neither competing nor incompatible.").
Combustion Engineering, will violate provisions that serve other fundamental goals of bankruptcy law: equal treatment and fundamental fairness. If a party whose interests are impaired objects, even the overwhelming support of creditors as a whole or those within the objecting party's class will not render the plan confirmable.

Accepting this paradox at face value will condemn increasingly tangential asbestos defendants to failure—Chapter 11 may be the only option for many of these companies, and the paradox may prevent them from reorganizing—to the detriment of most, if not all, of their creditors and other constituencies. This reality may explain why few openly acknowledge the asbestos bankruptcy paradox or suggest that it is absolute. Yet ignoring the

118 Howard Delivery Serv. v. Zurich Am. Ins. Co., 547 U.S. 651, 655, (2006) ("[T]he Bankruptcy Code aims, in the main, to secure equal distribution among creditors."); Begier v. IRS, 496 U.S. 53, 58 (1990) ("Equality of distribution among creditors is a central policy of the Bankruptcy Code."); Young v. Higbee Co., 324 U.S. 204, 210 (1945) ("Historically one of the prime purposes of the bankruptcy law has been to bring about a ratable distribution among creditors of a bankrupt's assets; to protect the creditors from one another."); Clarke v. Rogers, 228 U.S. 534, 548 (1913) ("Equality between creditors is necessarily the ultimate aim of the bankrupt[cy] law, and to obtain it we must regard the essential nature of transactions . . . ."); In re Lakeside Cmty. Hosp., 151 B.R. 887, 893 (N.D. Ill. 1993) ("Congress designed the Bankruptcy Code to provide for equal and consistent treatment among similarly situated creditors."). In Howard Delivery, the Supreme Court further noted the "complementary principle that preferential treatment of a class of creditors is in order only when clearly authorized by Congress." 547 U.S. at 655 (emphasis added).

119 Eisenberg Bros. v. Clear Shield Nat'l (In re Enviroydne Indus.), 214 B.R. 338, 349 (N.D. Ill. 1997) ("The goal of bankruptcy is to provide fairness among creditors and thereafter to give a debtor a fresh start.").

120 In re Texaco, Inc., 84 B.R. 893, 899 (Bankr. S.D.N.Y. 1988) (holding that a plan supported by 96% of the only impaired class must still satisfy the other requirements of the Code to be confirmed).

121 Georgene Vairo, Mass Torts Bankruptcies: The Who, The Why and The How, 78 AM. BANKR. L.J. 93, 128 (2004) ("[G]iven the failure of the Amchem and Ortiz class action settlements and the failure of Congress to act on a general level, bankruptcy may well be the only option available to defendants seeking peace in an intractable litigation.").
paradox is not an answer; even in a system that promotes pragmatic solutions, the conflict that gave rise to the paradox must ultimately be addressed if the law is to serve its intended purpose.

A solution to the problem, however difficult, requires an assessment of the conflict between asbestos veto demands and the other requirements of the Bankruptcy Code, on the one hand, and the assumptions underlying the existence and control of the asbestos veto, on the other. Thus, this section begins with a critical analysis of the practical justifications for the current approach to asbestos bankruptcy cases. Following this discussion, it addresses the prevailing approach under the legal framework of Section 524(g). As this inquiry unfolds, the paradox reveals its origins are less in bankruptcy law than in the accepted norms of legal practice. This section concludes with a summary of the consequences of the current approach to asbestos bankruptcies.

A. Practical Justifications for the Asbestos Veto

As noted previously, an important goal of bankruptcy law is "to secure a prompt and effectual administration and settlement of the estate of all bankrupts within a limited period."122 To advance this goal, the Code substantially modified the design of its predecessor, the Bankruptcy Act of 1898, to not only encourage timely bankruptcy filings but also encourage consensus-building among parties in interest.123 Accordingly, consensual Chapter 11 plans evolve through negotiation among parties with diverse and

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122 Katchen v. Landy, 382 U.S. 323, 328-29 (1966) (internal quotation marks and citation omitted).
123 In re Polytherm Indus., Inc., 33 B.R. 823, 835 (W.D. Wis. 1983) ("The authors of the Bankruptcy Reform Act of 1978 sought both to simplify the procedures for reorganizing a debtor by lessening the court's role in arranging a satisfactory reorganization scheme and to facilitate negotiation and consensus between the debtor and creditors in devising a reorganization plan.").
conflicting interests,\textsuperscript{124} and courts tend to give parties considerable leeway to design pragmatic solutions to complex problems. Indeed, the original asbestos bankruptcy cases are vivid examples of this design in action.

The prospects for a universally-accepted plan are weakened, however, as the number of parties and the divide among their respective interests grow. Parties frequently rationalize their litigation and negotiation stances to the point of absurdity,\textsuperscript{125} so these divisions can be considerable where the legal merits and priority of one or more large blocks of claims are contested, critical legal questions are

\textsuperscript{124} Plevin et al., supra note 25, at 294 ("Bankruptcy, particularly Chapter 11 bankruptcy, is often seen as a process within which interested parties hammer out agreements under the rules established by the Bankruptcy Code, bringing appropriate concerns and legal conflicts to the court's attention for resolution only as necessary. Consensual resolution is at the core of modern bankruptcy practice.").

\textsuperscript{125} Coleman v. Comm'r, 791 F.2d 68, 69 (7th Cir. 1986) ("Some people believe with great fervor preposterous things that just happen to coincide with their self-interest.") (Easterbrook, J.). Indeed, the concepts of self-serving and confirmation bias are well-recognized in the literature. See, e.g., Robert Prentice, Enron: A Brief Behavioral Autopsy, 40 AM. BUS. L.J. 417, 424 (Winter 2003) ("[P]eople tend to be subject to the confirmation bias in that they seek out and process information in such a way as to confirm pre-existing beliefs rather than in a more optimally neutral manner."); Max H. Bazerman et al., Environmental Degradation: Exploring the Rift Between Environmentally Benign Attitudes and Environmentally Destructive Behaviors, in CODES OF CONDUCT: BEHAVIORAL RESEARCH INTO BUSINESS ETHICS 256, 265 (David M. Messick & Ann E. Tenbrunsel eds., 1996) ("When people are personally involved in a situation, judgments of fairness are likely to be biased in a manner that benefits themselves."). As Prentice explains:

A growing body of behavioral research indicates that acting contrary to one's self interest is not a natural or easy thing. It is not just that people consciously say: "I'm looking out for me; screw the other guy," although they sometimes do. Rather, a menu of cognitive biases and limits on rationality affect how people perceive, process, and remember information, and, consequently, how they choose among alternative actions, assess risk, and make many other types of decisions.

Prentice, at 428.
unsettled or the parties have a long history of conflict. All of these barriers are present in asbestos bankruptcies, and the asbestos veto makes the "prompt and effectual administration" of these cases unlikely in a free-fall bankruptcy. Thus, the asbestos pre-pack strategy may be viewed as an efficient way to overcome these obstacles.

Just as good intentions and the desire to promote efficiency escalated the asbestos tort crisis, asbestos pre-packs made the resolution of some asbestos Chapter 11 cases less efficient and even more perilous for all parties in interest. The same biases that fuel litigation may help explain why so many lawyers justify inequitable distributions that favor themselves and some clients ahead of others and why debtors cling to fundamentally flawed plan terms in spite of facially clear statutes, rules, and opinions.

1. Procedural Efficiencies and Claim Filing

   a. Basic Efficiency Assumptions

   Conceptually, it is easy to reason that reducing the delays associated with proving claims will make the bankruptcy process more efficient. The time and expense associated with litigating individual claims may be overwhelming, so a process that expedites claim review and payment should, in theory, preserve considerable financial and judicial resources.

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127 Bazerman, *supra* note 125, at 266 ("Ambiguity enables individuals to make self-serving interpretations of the situation and to judge as fair distributions of resources that favor themselves."); George Loewenstein, *Behavioral Decision Theory and Business Ethics: Skewed Trade-Offs Between Self and Others*, in *Codes of Conduct: Behavioral Research into Business Ethics* 214, 221 (David M. Messick & Ann E. Tenbrunsel eds., 1996) ("[P]eople tend to conflate what is personally beneficial with what is fair or moral.").
The asbestos pre-pack strategy addresses these issues by developing and gaining the approval of distribution procedures prior to any bankruptcy filing. The procedures are frequently incorporated into a "master settlement agreement" and establish minimal evidentiary, diagnostic and other criteria for approval and ultimate payment of claims. The firms responsible for processing claims are selected, begin processing, and often complete their analysis of most or all of the claims that are filed before the bankruptcy case commences. Late-filed claims or those that arise after the pre-petition settlement deadline may be settled individually or processed under similar procedures (which are also negotiated pre-petition) that will be used by the asbestos trust established under the plan.

As a result, tens of thousands of asbestos personal injury claims that may take years or decades to resolve in the tort system or customary bankruptcy claim review procedures may be swept into a case, approved, and paid in a matter of months. This approach has obvious appeal to the lawyers presenting these claims for payment and the courts that might otherwise find their dockets overwhelmed by hundreds or thousands of claim objections. Even critics should agree that this process, if successful, may be exceptionally prompt and efficient.

b. Waste and Abuse

Reluctance to investigate asbestos claims may be understandable, but the belief that it is more efficient does not make it appropriate or, for that matter, necessarily improve efficiency. Turning a blind eye to questionable screening, filing and other practices of some among the plaintiffs' bar has undoubtedly reduced recoveries for legitimate claimants and further undermined the integrity of

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128 Stroumtosos Order, supra note 58, at 11-13.
129 These trusts will generally have similarly weak mechanisms for weeding out fraudulent or weak claims. Brickman, supra note 29, at 76.
the tort system. Lawsuits are frequently filed with inadequate or highly questionable medical and exposure evidence, and the sheer volume of claims filed against any individual defendant often makes meaningful inquiry into this evidence unlikely.

Although the Bankruptcy Code is designed to provide the debtor and other parties in interest with the ability to ferret out fraud, this potential remains largely unrealized. Debtors are unlikely to stir the pot against the very attorneys whose support is necessary to obtain sufficient votes to confirm any plan, and courts rarely allow other parties in interest to examine and object to asbestos claims. Moreover, because many asbestos bankruptcy

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130 Matthew Mall, Derailing the Gravy Train: A Three-Pronged Approach to End Fraud in Mass Tort Medical Diagnosing, 48 WM. & MARY L. REV. 2043, 2053 (2007) (abuse of mass screening has led to a dilution of legitimate asbestosis claims).


132 See Robin Jones, supra note 127, at 557.

133 Bankruptcy Code § 502(a) (allowing any party in interest to object to claims).


135 See In re Quigley Co., 346 B.R. 647, 653 (Bankr. S.D.N.Y. 2006). (concluding that requiring submission of sufficient supporting information “is cumbersome and best postponed for submission to the post-confirmation trust” and noting the practice of allowing counsel to cast votes for unsubstantiated claims on “master ballots”); Brickman, supra
settlements are reached and signed before the debtor's Chapter 11 case commences, the claims are viewed as present contractual obligations and may not receive the same scrutiny that they might encounter as contingent, unverified tort claims. The courts' repeated refusals to allow meaningful inquiry into the factual and legal bases for the claims and the attorneys' unsubstantiated assertions of authority to bring the claims and vote on the claimants' behalf effectively undermine any realistic prospect for preventing fraud and abuse.

In addition, by enabling attorneys to elevate their negotiating position solely on the number of claims they bring, Section 524(g) further encourages attorneys to file as many claims as possible. The upside is considerable: an attorney can obtain a considerable negotiating position and sizeable fees by simply dumping their asbestos claim "inventory" on a debtor. The downside is all but nonexistent: a low risk of having claims thrown out and little to no prospect of sanctions for filing even grossly fraudulent or, at best, wholly unsubstantiated claims.

With the risks of being discovered so dramatically reduced, attorneys may be encouraged to file unsupported
Experience demonstrates that these incentives may be more significant than commonly realized—attorneys that may have filed very few (if any) cases against a company will often throw a large percentage (if not all) of their "inventory" of asbestos claims against a company once its bankruptcy is announced. Of course, some of these claims may be filed even without additional incentives, but it is equally clear that the perceived gains in efficiency from the current approach are, at a minimum, partially offset by the additional time required to administer more claims.

2. Procedural Efficiencies of Attorney Dominance

a. Basic Efficiencies of Control

Removing obstacles to compromise among known parties should also improve efficiency both by avoiding litigation among those parties and discouraging dissent by minor creditors and tangential parties in interest. In Chapter 11, building consensus among those with the strongest legal and financial positions will often be sufficient to bring recalcitrant creditors in line or, at least, narrow the field of objecting creditors to those that lack the votes or legal claims necessary to block confirmation of a reorganization plan. Even creditors holding the strongest legal and financial positions will, in most cases, make concessions; bankruptcy involves risks and uncertainties for all parties, and those

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139 See David M. Setter et al., Why We Have to Defend Against Screened Cases—Now Is the Time For Change, 18-20 MEALEY'S LITIG. REP. Asb. 23 (Nov. 12, 2003) (arguing that asbestos trusts that conduct few audits or use minimal medical criteria create incentives for unscrupulous parties to "manufacture claims"); see also John M. Wylie, The $40 Billion Scam, READER'S DIGEST, January 2007, available at http://www.rd.com/content/printContent.do?contentId=32514.

140 White, supra note 137, at 1330; see also, Francis E. McGovern, The Tragedy of the Asbestos Commons, 88 VA. L. REV. 1721, 1749-50 (2002) (detailing the "field of dreams" effect resulting from plaintiffs' lack of cooperation resulting in large and disparate groups of plaintiffs pooling resources in order to maximize compensation).
that refuse to come to the table on important issues may find
the playing field tilted against them as the case proceeds.
Among other reasons, a recalcitrant creditor's claims may
suffer a concerted attack from debtors and other creditors
and courts may be more amenable to embracing these
challenges if the creditor is viewed as an obstacle to
reorganization. Chapter 11 case law is littered with
shattered claims of creditors who overplayed their hands.
Such creditors may lose bargaining power and, ultimately,
significant financial recoveries in the process.

In addition to these practical realities, asbestos pre-packs
present a bankruptcy court with an extremely appealing
starting point: arguably the most difficult issue in an
asbestos case—satisfaction of the super-majority voting
requirement—has already been resolved. Other parties in
the case are cast in the recalcitrant creditor (or party in
interest) role at the outset; they are seen less as
disenfranchised parties with significant individual rights at
stake than as spoilers pursuing their own self-interest. And
once cast in the role of the recalcitrant creditor, parties may
struggle to overcome this perception.

By embracing asbestos pre-packs, warts and all, courts
may reasonably believe that they are fulfilling their mandate
of making the overall process more efficient and cost-
effective. The outcome of litigation in bankruptcy is
frequently less significant in framing the ultimate rights of
the parties than it is in framing the negotiating postures the
parties take going forward. Once objecting parties get an
opportunity to make their case and lose, they may be less
likely to continue their litigious posture. If those parties
obtain even small victories, on the other hand, they may be
encouraged to forgo settlement in the belief that they can
improve their bargaining positions further. Given the
historical practices of some that may attempt to use
litigation to harass and delay confirmation, this is no small
concern.

Looking beyond the influence on litigation strategy,
asbestos pre-packs promise considerable additional
efficiencies. Many of the up-front costs of administration—
including the need to identify asbestos creditors, provide notice, design and manage the voting process, and evaluate claims—are largely accomplished by private parties in asbestos pre-packs. The difficult tasks of translating critical events in a case to those unfamiliar with the complexities of bankruptcy may also be handled by attorneys. In short, those presumably hired by asbestos claimants to represent them, and governed by clear rules of professional conduct, will do precisely what they are hired to do. And in the absence of evidence of impropriety in how that job is done, judicial second-guessing may serve only to delay a facially acceptable compromise and undermine the potential efficiencies of the asbestos pre-pack.

b. Practical Incentives and Lost Efficiencies

On the other hand, as recent cases suggest, the financial incentives associated with Section 524(g) may not only lead to a flood of new claims but also encourage plaintiffs' attorneys and other parties, such as insurers, to engage in extensive litigation. The small circle of plaintiffs' lawyers that control asbestos litigation have not been reluctant to fully exploit their presumed veto power, and traditional factors that may counter a "my-way-or-the-highway" mentality are either not present in bankruptcy or collapse due to considerations external to any individual bankruptcy case. Indeed, even after a plan is rejected, these lawyers may be more willing to see the debtor liquidate than accept the changes necessary to make the plan confirmable.\(^\text{141}\) On the other side of the aisle, insurance companies faced with the global prospect of attorney-dominated asbestos

\(^{141}\) For example, following the Third Circuit's rejection of Claimants Counsels' self-dealing and manipulation of the bankruptcy process, one of the Claimants Counsel dismissed the ruling and blamed the company's insurers for the failure of the plan and, in his view, the likely liquidation of this "mom-and-pop company." Margaret G. Tebo, Philadelphia Freedom, 93 A.B.A. J. 1, 21-22 (2007) ("The insurance companies have been successful in preventing Congoleum from reorganizing and saving this little mom-and-pop company. [Congoleum] will probably now go into liquidation . . . .") (quoting Joseph Rice).
bankruptcies manufacturing potentially unlimited liability have strong incentives to contest even those cases where their financial exposure may not be significant. 142

By leaving the parties to their own devices, and placing few substantive boundaries on their conduct or the resulting plans, 143 many (though, to be certain, not all) bankruptcy courts have unwittingly created the conditions necessary for the asbestos bankruptcy paradox. In authorizing even the parties' most outlandish attempts to advance their own self interest, courts have fueled additional litigation both within the cases before them and, by providing a measure of judicial approval to these schemes, in similar pending and future cases. Every decision—even those that are not reported or, for that matter, reduced to a written order—is introduced in these other cases across the country and becomes a stepping stone for ever more aggressive practices. Indeed, most of the problems identified in ACandS and Combustion Engineering became widespread long before those bankruptcies were filed. To that end, these cases are remarkable less for their legal conclusions than the fact that such fundamental violations of bankruptcy law became so engrained in the process before they were ultimately rejected.

Moreover, as the Fuller-Austin debacle demonstrates, even facially benign court orders can fundamentally alter the parties' conduct. First, the bankruptcy and the trial courts treated the underlying problems with the global arrangement more as judicial "hot potatoes" than as issues demanding resolution. The bankruptcy and district courts' acceptance of the Fuller-Austin plan placed the California trial court in an impossible position—a ruling in favor of the

142 See Davidson, supra note 68, at 95-96 (noting insurers and defendants have incentives to gamble on risky litigation as they approach insurance policy limits and insolvency).

143 Brickman, supra note 60, at 865 (noting that bankruptcy courts, "with rare exception, accept, adopt and otherwise ratify whatever is needed to satisfy plaintiff lawyer demands, which typically include adoption of trust structures and trust distribution procedures that allow claims to be paid even if they lack valid evidence of actual injury and proof of actual exposure to the debtor's products").
insurers could dramatically reduce possible recoveries for victims and effectively undermine a plan already approved in federal court, whereas a ruling against the insurers required turning a blind eye to the obvious legal and equitable problems that plagued the arrangement. The trial court's approach, albeit subtle, shifted responsibility for any obvious problems back to the bankruptcy court.

The practical impact of Fuller-Austin should not be overlooked. In the four years between the trial court's order in favor of the trust and its reversal on appeal, much of the damage had already been done—plan proponents relied on the Fuller-Austin cases during this time to rationalize away the risks that insurers might undermine their plans and, in the absence of other significant obstacles, dominate negotiations. Given the global dimensions of asbestos bankruptcy, however, the hope that other parties would simply yield across the board was, at best, unrealistic. Thus, by avoiding critical, albeit difficult, questions, the bankruptcy, district, and state trial courts unwittingly created a far more litigious environment in asbestos bankruptcies, threatening the promised efficiencies of asbestos pre-packs.¹⁴⁴

¹⁴⁴ Plevin et al., supra note 65, at 889 ("[P]arties in interest who were not included in the pre-petition plan negotiations, and whose interests are therefore not reflected in the proposed plan, may delay or derail confirmation by objecting to the plan, thereby depriving the debtor of some or all of the anticipated benefits of the pre-pack."). This, in fact, is precisely what happened in recent asbestos pre-packs:

Companies facing tens of thousands of asbestos claims may view pre-pack bankruptcies as a panacea, in that they seem to provide a mechanism for quick and inexpensive relief from the asbestos litigation nightmare. However, experience has shown that this is not the case because such bankruptcies have drawn vigorous objections by persons claiming that pre-packaged asbestos bankruptcies, as currently practiced, violate the Bankruptcy Code and Rules, improperly treat some claimants more favorably than others, and disregard the contractual rights of the insurers expected to fund the payments under the plan.

Id. at 923.
B. Section 524(g) in Context

Practical rationalizations aside, courts that have approved asbestos pre-packs in recent years have relied on fundamentally flawed statutory interpretations that, much like those offered by the plan proponents in ACandS, Combustion Engineering, and Congoleum, elevate form over substance. The increasing predominance of this mentality in asbestos bankruptcies corresponds, not surprisingly, to the adoption of Section 524(g). Once the trust-injunction process was codified, the emphasis of the parties shifted from its underlying equitable and constitutional bases to fashioning colorable interpretations of the statutory language that maximized their own goals and interests.

The form over substance approach may be superficially appealing and improve chances for reorganization, but it rests on the flawed assumption that the singular goal of Section 524(g) is reorganization. As evidenced by the legislative history, however, the central goal of Section 524(g) is the protection of future claimants; even the supplemental injunction against future litigation was authorized to serve this purpose:

The Committee remains concerned that full consideration be accorded to the interests of future claimants who, by definition, do not have their own voice. Nevertheless, the Committee also recognizes that the interests of future claimants are ill-served if Johns-Manville and other asbestos companies are forced into liquidation and lose their ability to generate stock value and profits that can be used to satisfy claims.\(^{145}\)

Thus, this approach mirrors the creditor protection model of traditional bankruptcies: although creditors sacrifice some of their individual collection rights under non-bankruptcy law, creditors as a whole should benefit if the process results in a greater pool of assets available for distribution and those

assets are distributed to creditors equitably according to the nature of their claims.

The emphasis on protecting future victims permeates the terms and structure of Section 524(g). Some protections, such as the requirement that the court appoint a legal representative, are readily apparent even if viewed in isolation. This requirement, however, is not the sole protection for future claimants:

The concept of a legal representative is embedded in § 524(g) as part of a framework for dealing with massive asbestos liabilities in bankruptcy. The statutory prerequisites are specifically tailored to protect the due process rights of future claimants. The appointment of a legal representative is only one of the many procedural safeguards that protect future claimants, who will be bound by terms of the channeling injunction. Other elements of Section 524(g), such as the obligation to ensure that current and future claims will receive substantially similar treatment and super-majority voting condition serve this purpose only if viewed collectively: futures are protected where they share a substantial identity of interest with current claimants and the current claimants overwhelmingly support the plan. The two primary alternative due process protections for future claimants—the appointment of a legal representative and the super-majority vote/substantially similar treatment requirements—are discussed in turn.

1. The Perversion of the Legal Representative Requirement

Although Section 524(g) conditions the application of a channeling injunction against future claimants on the

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146 In re G-I Holdings, Inc. v. Bennet, Jr. et al., 328 B.R. 691, 696-97 (D.N.J. 2005) (internal citations and quotations omitted). Indeed, legal representatives lack sufficient bargaining leverage to adequately protect future victims' interests against overreaching by Controlling Firms. See Nagareda, supra note 26, at 175-76 & 182.
appointment of "a legal representative for the purpose of protecting the rights of persons that might subsequently assert demands of such kind," the Code does not provide any direct guidance on the criteria for making such an appointment. Courts that have considered the question have focused more on how their different options may delay confirmation than which of these options will best protect future claimants. To that end, although the statute and


148 Boe W. Martin, Solution Or Setback For Mass-Tort Bankruptcies?, COM. LENDING LITIG. NEWS, vol. 7, no. 19 (Mar. 24, 1995) ("In short, Congress acknowledged the need for a legal representative in the [524(g)] injunctive process; however, it failed to give the courts any guidance as to such legal representative's capacity, duties, powers, qualifications, or compensation.").

149 Tung, supra note 24, at 65.

With the power to decide whether and whom to appoint, the judge will wish to select a "safe" FCR, one who subscribes to the common goal of reorganization. The FCR, the judge, and other parties in interest will understand this role for the FCR, and their respective expectations of the FCR's conduct will be affected accordingly. The FCR's latitude to champion future claimants' cause may be circumscribed. She is not negotiating on a clean slate, as she would be if her appointment did not depend on this collective precommitment to reorganization.

Id. at 64 ("As an institution for the representation and protection of future claimants, the FCR device is underinclusive. Its use suggests not so much a concern for otherwise unrepresented claimants, but instead a need to provide due process cover in order to bind future claimants to a reorganization plan."). The Supreme Court long ago recognized similar concerns in the class action context:

Such a selection of representatives for purposes of litigation, whose substantial interests are not necessarily or even probably the same as those whom they are deemed to represent, does not afford that protection to absent parties which due process requires. The doctrine of representation of absent parties in a class suit has not hitherto been thought to go so far. Apart from the opportunities it would afford for fraudulent and collusive sacrifice of the rights of absent parties, we think that the
legislative history appear to contemplate the selection of an independent representative selected by the court, the prevailing practice in recent years has been for courts to appoint the representative that is hand-picked by counsel for current claimants and the debtor—the very parties who stand to lose the most if a strong, independent representative is appointed.

After an appointment is made, judicial attention to the adequacy of futures representation rarely receives more than a passing reference, and bankruptcy plans routinely shield legal representatives from liability to future claimants for all but the most egregious misconduct. Some legal representatives have been paid jaw-dropping fees, and the

representation in this case no more satisfies the requirements of due process than a trial by a judicial officer who is in such situation that he may have an interest in the outcome of litigation in conflict with that of the litigants.

Hansberry v. Lee, 311 U.S. 32, 45 (1940) (internal citations omitted).

See Plevin et al., supra note 25, at 273 ("Congress plainly envisioned an FCR who was independent of the other parties in the bankruptcy, aggressively representing future claimants’ interests, standing as a bulwark against abuse of those absent parties.").

See id. at 301-14 ("In almost every asbestos bankruptcy case to date, the bankruptcy court has granted the debtor a presumptive right to select the FCR, often approving the appointment of an FCR who has already been selected by the debtor and pre-determined to be acceptable to the current claimants.").

McGovern, supra note 48, at 248 ("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."); accord In re Kensington Int’l Ltd., 368 F.3d 289, 304 (3d Cir. 2004) (acknowledging conflict between present and future asbestos claimants and need for separate representation).

Brickman, supra note 60, at 868 n.144 (extraordinary Halliburton fees); see also, In re Mid-Valley, 2004 Bankr. LEXIS 1553 at 21 (Bankr. W.D. Pa. 2004); Russel Gold, Halliburton Finalizes Settlement for $5.1 Billion Over Asbestos, WALL ST. J., Jan. 4, 2005, at A3; Halliburton Asbestos Settlement Wins Approval, N.Y. TIMES, Nov. 30 2004, at C4; Judge Rules Insurers Have No Standing In Halliburton Units’ Bankruptcy Petition, BESTWIRE (Feb. 11, 2004) (noting that Halliburton's pre-petition futures representative was paid $9,000 per day—nearly $5 million in all—
resulting plans often expressly provide for the continued employment of the legal representative post-confirmation.\textsuperscript{155} Under these plans, the legal representatives will report to the very attorneys that both controlled their appointment and, in theory, were their adversaries in the bankruptcy process. Moreover, much like the attorneys that control their appointment, legal representatives are repeat performers in asbestos bankruptcies.\textsuperscript{156} Thus, in addition to case-specific incentives, legal representatives for future victims have strong global incentives against taking positions in any one case that may alienate these same attorneys.\textsuperscript{157}

It is difficult to imagine any principal knowingly employing an agent with such extensive dependence on its adversaries; of course, future claimants are principals that do not have the ability to make this choice. As Professor Tung explained:

> [S]evere agency problems exist with the FCR mechanism [i.e., the appointment of a legal representative to protect future claimants]. The fundamental and unavoidable problem is that the purported principals play no part in choosing or monitoring their agent or even in deciding whether to retain one at all. Instead, other parties in interest—the debtor and other creditors—initiate the process,

\textsuperscript{155} \textit{In re Congoleum Corp.}, No. 03-51524 (Bankr. D.N.J. July 6, 2004).


\textsuperscript{157} See Nagareda, \textit{supra} note 26, at 177 (discussing the "punch-pulling" incentive for legal representatives who wish to be "repeat players"); Plevin et al., \textit{supra} note 25, at 292-93 ("Further compromising the pseudo FCR's independence, prospective debtors have tended to choose the pseudo FCRs from a small stable of repeat FCRs. Such persons are most likely to be chosen repeatedly if they are viewed by prospective debtors and claimants as reliable negotiating partners who can be counted on to not 'rock the boat.'").
and the judge decides whether and whom to appoint, as well as the terms of the agency. All these actors have interests that will conflict with those of future claimants. Ultimately, the FCR mechanism may not assure zealous representation of future claimants' interests. The FCR has principals only as a conceptual matter. The terms and quality of the FCR's representation are not subject to oversight by her ostensible "clients." A significant potential exists, therefore, for divergence between the respective interests of principal and agent.\[158\]

The net result is that a process designed to protect future claimants against overreaching by current parties serves the opposite purpose: protecting deals expressly designed to prefer current parties from subsequent challenges by future claimants.

Such an approach is inconsistent with the Supreme Court's recent decision in Taylor v. Sturgell. In that case, the Court stated the following:

"[I]n certain limited circumstances," a nonparty may be bound by a judgment because she was "adequately represented by someone with the same interests who [w]as a party" to the suit. Representative suits with preclusive effect on nonparties include properly conducted class actions, and suits brought by trustees, guardians, and other fiduciaries.\[159\]

Although Taylor did not involve "other fiduciaries" like the Section 524(g) legal representative, the unanimous Court recognized that the mere presence of a "representative" is not sufficient; a nonparty is "adequately represented" only if "the interests of the nonparty and her representative are aligned . . . ."\[160\] And given the Taylor Court's insistence on a

\[158\] Tung, supra note 24, at 60.
\[160\] Id. at 2176 ("A party's representation of a nonparty is 'adequate' for preclusion purposes only if, at a minimum: (1) the interests of the nonparty and her representative are aligned, and (2) either the party
"constrained approach to nonparty preclusion" and insistence on "crisp rules with sharp corners," the suggestion that the appointment of a conflicted Section 524(g) legal representative will pass constitutional muster strains credulity.

2. The Asbestos Veto Reconsidered

a. The Super-Majority Vote in Context

The place to begin any statutory inquiry is the text of the statute. Unfortunately, Section 524(g) is not always a model of clarity, and its legislative history is sparse. Nonetheless, it is possible to understand the purpose of the super-majority vote requirement by viewing its role in Section 524(g)(2)(B)(ii) and by reference to the overall goals of Section 524(g) generally. As noted previously, Section 524(g)(2)(B)(ii) conditions the issuance of the channeling injunction on a series of court determinations, including the determination that 75% of asbestos creditors approve the plan. The first three

understood herself to be acting in a representative capacity or the original court took care to protect the interests of the nonparty." (internal citations omitted).

161 Id. at 2176.

162 Id. at 2177 (quoting Bittinger v. Tecumseh Prods. Co., 123 F.3d 877, 881 (6th Cir. 1997)).

163 Caminetti v. United States, 242 U.S. 470, 485 (1917) ("It is elementary that the meaning of a statute must, in the first instance, be sought in the language in which the act is framed, and if that is plain ... the sole function of the courts is to enforce it according to its terms.").

164 See In re Congoleum Corp., 362 B.R. 167, 176 (Bankr. D.N.J. 2007). Of course, as noted previously, even this sparse history clearly establishes the focus of Section 524(g) is to protect future claimants.

165 See id. (looking to the "overall purpose of § 524(g)" to interpret the statute).

166 Section 524(g)(2)(B)(ii) requires that the court determine if:

(I) the debtor is likely to be subject to substantial future demands for payment arising out of the same or similar
components of this section focus on the threat to equal treatment posed by current and future claims—substantial future demands must be likely, it must be difficult to predict the scope of these future demands, and the pursuit of these demands will likely undermine the prospects for equitable treatment of current claims and future demands if the trust-injunction approach is not used. Given that these concerns must already be present, reading the fourth component—the super-majority voting requirement—in a way that would serve only to increase the disparity among current claims and future demands seems, at best, out of place. In light of the long-acknowledged competition between current and
future claimants for estate assets,¹⁶⁷ and the fact that current claimants already enjoy significant protections under the traditional voting procedures in Chapter 11, the conclusion that the super-majority voting requirement was intended for the singular benefit of current claimants is untenable.

A contextual analysis not only demonstrates what interests the super-majority vote is not intended to advance, it also provides insight into the important function it is designed to serve—like the rest of Section 524(g), the super-majority vote exists to protect future claimants. The fifth component of Section 524(g)(2)(B)(ii) requires a plan to be designed so that similar current claims and future demands receive valuations and payments that are the same considerably or to a large degree,¹⁶⁸ or without material

¹⁶⁷ As the Supreme Court vividly recognized in a class action case that, other than the nominal legal foundation, bears remarkable resemblance to asbestos pre-packs: “Most saliently, for the currently injured, the critical goal is generous immediate payments. That goal tugs against the interest of exposure-only plaintiffs in ensuring an ample, inflation-protected fund for the future.” Amchem Prods., Inc. v. Windsor, 521 U.S. 591, 626 (1997). The Court subsequently noted the same concern when it rejected a comparable settlement framed as a "limited fund" class action in Ortiz v. Fibreboard Corp., 527 U.S. 815, 856 (1999). Indeed, the Second Circuit rejected one claimant's efforts to speak on behalf of Manville's future claimants in that case due to similar concerns:

Kane's interest in these proceedings is potentially opposed to that of the future claimants. Both Kane and the future claimants wish to recover from the debtor for personal injuries. To the extent that Kane is successful in obtaining more of the debtor's assets to satisfy his own claims, less will be available for other parties, with the distinct risk that the future claimants will suffer. Thus, we cannot depend on Kane sincerely to advance the interests of the future claimants.


¹⁶⁸ Toyota Motor Mfg., Ky., Inc. v. Williams, 534 U.S. 184, 196 (2002) (“[S]ubstantially’ in the phrase ‘substantially limits’ suggests ‘considerable’ or ‘to a large degree.’” (quoting WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 2280 (1976); see also 17 OXFORD ENGLISH DICTIONARY 66-67 (2d ed. 1989) (defining “substantial” as “relating to or
qualification.\textsuperscript{169} If their interests are so aligned, providing current claimants with all relevant information and requiring their overwhelming approval mirrors a long-recognized substitute form of due process in situations where notice and an opportunity to appear are not possible.\textsuperscript{170} As one court explained:

Where the identities of the actual takers of a future interest are unascertainable or otherwise difficult to determine with certainty, joinder of the presumptive takers of that interest as of the time of the commencement of the action will, in appropriate circumstances, be sufficient to enable any judgment entered therein to be binding upon all persons, whether in being or not, in the class of potential takers of that interest. While the members of that class may not be individually ascertainable at the time of the action, they are identifiable as a class and their interests as such cognizable. The presumptive takers are persons who would be the actual takers of the future interest if the contingency occurred at the time of the commencement of the proceeding affecting the property in which the future interest exists. They are permitted to represent the entire class of potential takers, but only in the absence of any demonstrable conflict of interest or other hostility between the presumptive takers and the other members of the class sought to be represented.\textellipsis Utilization of virtual representation enables the court to act upon the interests of proceeding from the essence of a thing; essential;" and "of ample or considerable amount, quantity, or dimensions").

\textsuperscript{169} Heublein, Inc. v. United States, 996 F.2d 1455, 1465 (2d Cir. 1993) ("'Substantially' is defined as 'without material qualification;' and as 'in a substantial manner.'") (quoting BLACK'S LAW DICTIONARY 1428-29 (6th ed. 1990)).

\textsuperscript{170} In re Estate of Lange, 383 A.2d 1130, 1140 (N.J. 1978) ("The assumption underlying the doctrine of virtual representation is the existence of a relationship between the presumptive takers and the class of potential takers sufficiently close to guarantee an identity of interest between the representatives and the class and thus to assure that the representation will be adequate.").
unascertainable contingent remaindermen to the same effect as if they all had been *sui juris* and parties to the action without any infringement of their right to due process.\(^{171}\)

Indeed, in its recent rejection of the expansion of the nebulous concept of "virtual representation," a unanimous Supreme Court remarked that this form of preclusion is available only if "(1) the interests of the nonparty and her representative are aligned, and (2) either the party understood herself to be acting in a representative capacity or the original court took care to protect the interests of the nonparty."\(^{172}\)

The most significant condition, and the most difficult to satisfy, is that there be a sufficient identity of interest shared by a party to the suit and the nonparty whose suit may be precluded.\(^{173}\) As we have seen, standing alone, the legal representative device is ill-suited to provide a meaningful check on overreaching by current parties,\(^{174}\) so the alignment of current and future interests may be the only practical manner in which courts may protect the interests of future victims.

This condition is not satisfied in the recent wave of asbestos pre-packs, which are premised on the assumption that the components of Section 524(g)(2)(B)(ii) operate in

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\(^{171}\) *Id.* (emphasis added) (internal citations omitted).


\(^{173}\) *Chase Manhattan Bank, N.A. v. Celotex Corp.*, 56 F.3d 343, 346 (2d Cir. 1995) ("The question thus is whether NYPBC had an interest in pursuing a property damage claim against the asbestos manufacturers sufficiently similar to Chase's interest in pursuing the same claim as to have created virtual representation. Absent such an identity of incentives, the application of claim preclusion against Chase would violate concepts of elemental justice and probably due process."); *Delta Air Lines v. McCoy Rest.*, 708 F.2d 582, 587 (11th Cir. 1983) ("This principle applies, however, only when the respective interests are closely aligned and the party to the prior litigation adequately represented those interests.").

\(^{174}\) See discussion *supra* Section II.B.1. Indeed, some have argued that the legal representative device is fundamentally incapable of protecting the interests of future claimants. See also discussion *infra* III.B.
isolation. By ignoring their context, as well as their purpose, lawyers claim a power that fundamentally alters the collective compromise model of Chapter 11. As a result, rather than maximizing the identity of interest between current and futures—the focus of Section 524(g)(2)(B)(ii)(V)—and protecting the interests of future claimants—the key aim of Section 524(g)—asbestos pre-packs ensure that current claimants will obtain far more than future claimants and therefore have considerably different interests under the plan. To that end, a critical element of the substitute due process design has not only been lost; it has been corrupted to the detriment of the very parties it was constitutionally required to serve.

b. Attorney Block Voting

Following the lead of ACandS and Combustion Engineering, some courts have taken a hard line on asbestos pre-packs that insist on elevating preferred current claims above similar current and future claims. This is a promising step, but, standing alone, it is insufficient. The underlying problem with asbestos pre-packs remains: not only are current claimants’ interests far removed from their future counterparts, they do not, by and large, make the critical voting decisions:

The near unbridled power of Controlling Firms is further compounded by the virtually unregulated voting process. Plaintiff lawyers claiming appointment as attorney-in-fact for their asbestos clients, deliver their votes in a block—listing the names of those they claim to represent and the total vote for and against. While there is, in theory, a limitation on who is eligible to vote on approval of a Section 524(g) trust, in practice, there are no controls over who gets

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175 In re Congoleum Corp., 362 B.R. 167, 182 (Bankr. D.N.J. 2007) (concluding that such an approach would render a plan “unconfirmable on its face”). Moreover, Judge Ferguson recently reiterated that “it is not enough to have mere technical compliance with the trust funding requirements” of Section 524(g); the plan proponents must establish that the plan is fair and equitable and proposed in good faith. In re Congoleum Corp., 2008 Bankr. LEXIS 2375, at *32 (Bankr. D.N.J. Sept. 2, 2008).
to vote. The absence of any auditing process to confirm that the claimants have exposure to the debtor's product, that counsel represents them, that counsel has authority to cast their ballots, and even that the listed claimants actually exist, is indicative of the control that plaintiff lawyers exercise over asbestos bankruptcy proceedings.\textsuperscript{176}

As a result, it is not even possible to characterize modern asbestos bankruptcy class voting as representative of their own views, much less of future claimants. As Judge Weinstein observed:

A second factor inhibiting the courts [sic] inclination to obtain a vote is the practice of permitting attorneys to vote on behalf of their clients. This does not seem appropriate in the context of asbestos litigation, particularly with respect to the Trust. The fee and solicitation positions of attorneys in this specialized and concentrated litigation amount to vested interests quite distinct in some circumstances from those of injured claimants. Moreover, conflicts among the masses of clients each major attorney represents arise because of vast differences in exposures, kinds of diseases, ages and needs of clients and the like. Any position taken by an attorney is bound to place him or her or one of the clients at a relative disadvantage or advantage. This has been true for the last decade in asbestos litigation.

Treating this mass litigation as if each claimant had an individual voice and an individual attorney devoted only to that client's interest is, in the case of most claimants, a romantic notion based on dreams of the law's past, having no relationship to the reality of asbestos lawyering as a business in the present.\textsuperscript{177}

\textsuperscript{176} Brickman, \textit{supra} note 60, at 866-67. This mirrors the attorney-client dynamic outside of bankruptcy. \textit{See, e.g.}, John C. Coffee, \textit{Class Wars: The Dilemma of the Mass Tort Class Action}, 95 \textit{Columbia L. Rev.} 1343, 1346 (1995) (recognizing that "individual plaintiffs have weak to nonexistent control over their attorneys across the mass tort context").

\textsuperscript{177} \textit{In re} Joint E. & S. Dist. Asbestos Litig., 129 B.R. 710, 838 (E.D.N.Y. & S.D.N.Y. 1991); \textit{accord In re Congoleum Corp.}, 362 B.R. 167,
To that end, regardless of the practical considerations that make attorney block voting on behalf of current claimants appealing, it does not provide a sufficient basis for denying future claimants their day in court.

Beyond due process concerns, block voting presents immediate practical barriers to satisfying the basic requirements of bankruptcy law. Attorneys may threaten to veto confirmation in order to preserve sweetheart deals or to deter current and future debtors from auditing claims. Thus, even if a claim audit is wildly successful in rooting out fraudulent claims, a Controlling Firm may prevent the debtor from obtaining the benefit of Section 524(g) by casting its remaining votes against the plan. Of course, a negative vote may be against the voting clients' best interests in the case, but, as the circumstances surrounding Congoleum's sixth amended plan demonstrate, that is hardly a guarantee that the vote will reflect the clients' immediate interests.  

3. The Limits of Compromise and Section 524(g)

As with any other provision of the Code, the courts' authority to enjoin actions under Section 524(g) is limited. In Combustion Engineering, for example, the injunction protected some of the debtors' non-debtor affiliates, who might otherwise be sued due to their own distinct asbestos manufacturing histories, in exchange for their shared parent company's contributions to the trust. The Third Circuit, however, properly recognized that bankruptcy jurisdiction does not extend to a plaintiff's independent cause of action against any of the non-debtor affiliates. Thus, the court concluded:

194 (Bankr. D.N.J. 2007) ("Moreover, many of the claimant's representatives are using master ballots. The conclusion that claimants who did not submit an individual ballot gave their unambiguous consent to this release [in the proposed plan] hangs at the end of a shaky limb.").

178 See discussion supra Section I.D.2.f.

179 In re Combustion Eng'g, Inc., 391 F.3d 190, 228 (3d Cir. 2004).

180 Id.
Although [the parent corporation's] contributions to the Asbestos PI Trust may depend on freeing [the non-debtor affiliates] of asbestos liability, and these contributions may inure to the benefit of certain Combustion Engineering asbestos claimants, these factors alone do not provide a sufficient basis for exercising subject matter jurisdiction. If that were true, a debtor could create subject matter jurisdiction over any non-debtor third-party by structuring a plan in such a way that it depended upon third-party contributions. As we have made clear, "subject matter jurisdiction cannot be conferred by consent of the parties. Where a court lacks subject matter jurisdiction over a dispute, the parties cannot create it by agreement even in a plan of reorganization." Although federal bankruptcy jurisdiction is "deliberately expansive" and "conspicuous for its breadth," it is not without limitation. As such, the boundaries of bankruptcy jurisdiction cannot be extended simply to facilitate a particular plan of reorganization, even if we perceive the plan to be in the public interest.\textsuperscript{181}

In February 2008, the Second Circuit reached a similar conclusion concerning the scope of the channeling injunction issued in the Manville case more than two decades earlier.\textsuperscript{182} This injunction enjoined "all persons' from commencing any action against any of the Settling Insurance Companies 'for the purpose of, directly or indirectly, collecting, recovering or receiving payment of, on or with respect to any Claim . . . or Other Asbestos Obligation . . . ."\textsuperscript{183} In the intervening years, asbestos plaintiffs sued some of these insurers under various state insurance regulations and common law tort theories that centered on, among other things, their role in assisting Manville and others in concealing the dangers of asbestos.\textsuperscript{184} The district court noted that, in spite of the broad language

\textsuperscript{181} Id. at 228-29 (internal citations omitted).

\textsuperscript{182} Johns-Manville Corp. v. Chubb Indem. Ins. Co. (In re Johns-Manville Corp.), 517 F.3d 52, 57 (2d Cir. 2008).

\textsuperscript{183} Id. at 57-58.
of the injunction, "[t]he Bankruptcy court has no jurisdiction to bar a suit alleging tortious conduct by Travelers on behalf of a non-Manville insured, conduct that is unrelated to Manville and not based on any knowledge of asbestos gained from Manville, and that did not involve Manville asbestos or asbestos products."  

With that caveat, however, the court concluded that the injunction applied. On appeal, the Second Circuit disagreed:

Plaintiffs seek to recover directly from a debtor's insurer for the insurer's own independent wrongdoing. Plaintiffs aim to pursue the assets of Travelers. They raise no claim against Manville's insurance coverage. They make no claim against an asset of the bankruptcy estate, nor do their actions affect the estate. The bankruptcy court had no jurisdiction to enjoin the Direct Action claims against Travelers.

In other words, "global finality is only as 'global' as the bankruptcy court's jurisdiction" and "[t]he bankruptcy court's desire to facilitate global finality... may not be used as a jurisdictional bootstrap when no jurisdiction otherwise exists."

The Second and Third Circuits' recent opinions serve as stark reminders of the limits of compromise and the courts' authority in bankruptcy. Debtors and other parties in interest ignore these limits at their own peril; turning a blind eye to these problems during bankruptcy may expedite confirmation, but the inherent flaws in any resulting "final" order may largely undermine some or all of the expected benefits of the process years or, as shown in Manville, decades later. For courts, recognition of these limits and forcing parties to work within them—regardless of self-serving claims that any overreaching is necessary to achieve

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185 Id. at 60 (quoting the district court opinion).
186 Id. at 59-60.
187 Id. at 65 (internal citations omitted).
188 Id. at 66.
189 Id. at 68.
a confirmable plan—a may thus avoid the far more complicated task of managing the fallout of such a failure down the road.

C. The Costs of Failure

With so much maneuvering around legal and practical justifications, the fundamental purpose of Section 524(g) may be overlooked. From the perspective of actual future claimants, however, these are no legal or constitutional niceties. In addition to the devastating physical and personal consequences of the disease, they learn that whatever modest consolation their day in court might have provided is now lost due to bankruptcy. In the worst-case scenario, these victims may face a future where the known parties’ own self-interests were so engrained and unyielding that the companies responsible for their injuries were ultimately forced into liquidation, leaving nothing to offset the financial burdens of their diseases. Of course, this also has significant consequences for individual communities and families, just as it does in any other corporate liquidation.

In the best-case scenario under prevailing practices of recent years, lawyers the future claimants never knew, much less hired, decided that their injuries were less worthy of compensation. The legal representative appointed to prevent disparate treatment had financial or other significant relationships with these same attorneys and was promised lucrative employment, paid out of the funds set aside for

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190 In Combustion Engineering, for example, the plan proponents asserted: “If the channeling injunction does not extend to claims against [the non-debtor affiliates], there is no plan; it is that simple.” In re Combustion Eng’g, Inc., 391 F.3d 190, 228 (3d Cir. 2004). Once this option was foreclosed by the Third Circuit, however, Combustion Engineering reformulated its plan, which was confirmed less than one year later.

191 See S. Todd Brown, Non-Pecuniary Interests and the Injudicious Limits of Appellate Standing in Bankruptcy, 59 Baylor L. Rev. 569, 615 (2007) (arguing that the failure to ensure that the requirements of Section 524(g) are satisfied “will place a greater burden on judicial resources in the long term”).
future claimants, upon the approval of the deal. Of the hundreds of millions, if not billions, of dollars collected from insurers and other defendants, forty percent or more ultimately found its way into the pockets of these professionals. As a result, future claimants are paid at a fraction of the rate fixed in the plan; a rate that was already lower than comparable then-current claimants received.

Under either scenario, future claimants lose significant personal and financial rights; the primary benefits of success flow to those involved in the bankruptcy case. On the flip side, rampant claim inflation ensures that those with weak medical or causal evidence obtain significant windfalls. Thus, in addition to the depletion of assets by unimpaired claims, those with strong evidence establishing a causal link to a particular defendant must compete for a limited pool of assets against those with weak or non-existent ties to the defendant.

Cynically speaking, a claimant with strong claims against a debtor whose asset pool is depleted by weak claims under this system may have a similarly weak basis for asserting a claim against a subsequent debtor. If that subsequent debtor's case also has weak barriers to payment, the claimant may ultimately make up the difference or even obtain more recovery in the long run. As a mass tort
rationalization that would make Charles Ponzi proud, of course, it assumes that there will be similar standards in future bankruptcies and that the individuals making the decision to file claims will not be limited by the technical fact that their claims have little or no merit as against those future debtors.

Ultimately, the development of a system that adequately compensates all victims of asbestos exposure may, as the Supreme Court noted, rest in the hands of Congress. However good the intentions, decades of trying to do so through the tort and bankruptcy systems have undermined the integrity of both and left too many victims without recovery. Where recovery is obtained, it comes only after extraordinary delays and at great expense. These problems did not begin with bankruptcy law, but bankruptcy need not be a way to simply pass financial burdens onto future victims.

196 See Ortiz v. Fibreboard Corp., 527 U.S. 815, 819 (1999) ("The elephantine mass of asbestos cases . . . defies customary judicial administration and calls for national legislation.").

197 As one commentator reasoned:

[B]ecause of a lack of scrutiny with respect to information utilized to substantiate an individual claimant's claim, in some cases, the claim is based on questionable pulmonary function tests and x-ray interpretations. Undoubtedly, the result has been that numerous claimants who are currently asymptomatic, or only mildly impaired, have been overcompensated for their injuries at the expense of seriously ill claimants, as well as future claimants.

William J. Warfel, Ph.D, Asbestos Litigation Reform: An Identification of Problematic Issues, CPCU eJOURNAL, Nov. 2004 at 5. This is no mere hypothesis; as the filing of screening-based claims declined in the aftermath of Judge Jack's scathing criticism of similar practices in silica litigation, "[t]he average malignant claim settlement amount rose as defendants moved away from settling claims in groups, which had depressed average payments for malignant injuries." Austern & Bhagavatula, supra note 58, at 75.

198 See James Surowiecki, Asbestos, Inc., NEW YORKER, Mar. 6, 2006, available at http://www.newyorker.com/archive/2006/03/06/060306ta_talk_surowiecki (noting that "roughly sixty per cent of all the money spent on [asbestos] litigation has gone to attorneys").
IV. RESTORING THE PURPOSE AND PROMISE OF ASBESTOS BANKRUPTCY LAW

"How wonderful that we have met with a paradox... Now we have some hope of making progress."199

In the rush to manufacture consensus, the most notable compromises in recent asbestos bankruptcies have been to the integrity and underlying fairness of the system.200 Of course, some may reason that avoiding liquidation is ultimately better for future claimants, so the flaws in the process are justified. Such a rationalization, while practically inadequate for future victims, also assumes that there are not other viable alternatives and is based on policy judgments that are inconsistent with practical experience and the purposes of the Bankruptcy Code. The degree to which participants and courts have been willing to look past the extreme manner in which the system has been compromised is based less on indifference than mistaken, often self-serving rationalizations. As demonstrated, these rationalizations do not withstand scrutiny.

As long as asbestos litigation continues, some defendants will ultimately be forced to risk bankruptcy, uncertainties and all. For these companies, the asbestos veto may not only discourage a timely filing; it may make it impossible to obtain a truly final resolution of asbestos liability in bankruptcy. The ultimate outcomes for these companies and asbestos victims depend on whether recent developments serve as a wake-up call and lead to fundamental changes to the way that asbestos bankruptcies are negotiated, overseen by courts and structured. Above all, just as attitudes and negotiating postures have become distorted by failures in the system, they may be corrected by more aggressive judicial


200 Barliant et al., supra note 53, at 441 (noting that recent asbestos bankruptcies "refined the mechanics, and strayed from the purpose, of the Bankruptcy Code and particularly of section 524(g)").
oversight and structural protections designed not only to address discrete issues as they arise but also the global incentives that have, to date, driven asbestos bankruptcy cases.

Consensual resolution may be the normative priority in Chapter 11, but this does not justify judicial acceptance of proposals that compromise the very provisions intended to protect those who are not at the negotiating table. Parties are, of course, free to negotiate away their own rights; the statutory protections of the rights of others, however, are not theirs—or the courts’—to compromise.\textsuperscript{201} Steadfast adherence to this fundamental principle should be the norm in any bankruptcy case, but it has not been the norm in recent asbestos bankruptcies:

\textit{Between Johns-Manville and ACandS are numerous asbestos cases in which the purpose and language of the Bankruptcy Code have been disregarded in favor of expediency. That expediency is rationalized as necessary to save the debtor company and compensate asbestos victims. But by departing from the provisions of the Bankruptcy Code, the engineers of these cases too often compromise the rights of others, including the victims of asbestos exposure whose interests are not represented.\textsuperscript{202}}

\textit{Congoleum} and other recent cases, however, illustrate that plans that rely on compromising the protections of

\begin{footnotesize}
\textsuperscript{201} See Local No. 93 v. City of Cleveland, 478 U.S. 501, 529 (1986) (“Of course, parties who choose to resolve litigation through settlement may not dispose of the claims of a third party, and \textit{a fortiori} may not impose duties or obligations on a third party, without that party’s agreement. A court’s approval of a consent decree between some of the parties therefore cannot dispose of the valid claims of nonconsenting intervenors; if properly raised, these claims remain and may be litigated by the intervenor.”).

\textsuperscript{202} Barliant et al., \textit{supra} note 53, at 442; Boe W. Martin, \textit{Solution Or Setback For Mass-Tort Bankruptcies?}, COM. LENDING LITIG. NEWS, April 7, 1995, at 4. (“In short, Congress acknowledged the need for a legal representative in the [524(g)] injunctive process; however, it failed to give the courts any guidance as to such legal representative’s capacity, duties, powers, qualifications, or compensation.”).
\end{footnotesize}
Section 524(g) are unconfirmable; so it is no longer efficient or practical for bankruptcy courts to turn a blind eye to these compromises. In these circumstances, courts, as the only participants empowered to take decisive action, have an obligation to the parties before them and the integrity of the judicial process to do so.\textsuperscript{203}

To be clear, this assessment of judicial practice in this area to date is not a condemnation of the judges involved, their competence, or their willingness to ensure that the rule of law is followed. Bankruptcy judges must balance a wide array of competing legal and practical considerations, often with poor guidance from Congress and other courts, and with little time to do so. They properly focus on the matters before them, and decisions that may seem clearly misguided from a global perspective may be entirely reasonable when considered in isolation. This is particularly true when those challenging the courts' wisdom do so with the benefit of hindsight. However, today we have the benefit of this hindsight, and the unfolding image that it presents demands that courts take a much more active, critical role in overseeing asbestos cases than has been the norm to date. It is time to revisit the practices that gave rise to the asbestos paradox and have consistently undermined the goals of Section 524(g).

\textsuperscript{203} \textit{In re} Martin, 817 F.2d 175, 180 (1st Cir. 1987) (recognizing the "bankruptcy court's fundamental responsibility to monitor the integrity of the proceedings before it"); \textit{In re} Narod, 138 B.R. 478, 481-82 (Bankr. E.D. Pa. 1992) ("It is within the discretion of the bankruptcy court, and indeed it is the court's obligation, to prevent flagrant abuse of the Bankruptcy Code.") (emphasis added); MBNA Am. Bank, N.A. v. Panem (\textit{In re} Panem), 352 B.R. 269, 278 (Bankr. D. Colo. 2006) ("The inherent powers of this Court, embodied in 11 U.S.C. § 105(a), impose a duty on this Court to ensure that the provisions of the Code are carried out and to prevent an abuse of process."); \textit{In re} Bruno, 68 B.R. 101, 103-04 (Bankr. W.D. Mo. 1986) ("[T]he bankruptcy court has a paramount obligation to prevent such abuses as will bring the great goals of bankruptcy into disesteem and disrepute.").
A. Aligning the Interests of Current and Future Claimants

Section 524(g), as noted previously, may be read to require an identity of interest between current and future claims by demanding "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." Ensuring that current and future claimants have an identity of interest sufficient to satisfy the demands of due process is no simple task, but the failure to do so will have considerable implications for future victims. This failure leaves the Controlling Firms with little incentive to challenge overreaching by their counterparts as long as the pool of assets available for asbestos claims (current and future) is sufficient to pay their respective current claims to their satisfaction. If they must share the potential burden imposed by over-claiming with future claimants evenly, however, these disagreements may force these concerns to the forefront of negotiations. Accordingly, over-claiming stands a far greater likelihood of being addressed in a meaningful way before significant trust assets are wasted to satisfy frivolous or unsupported claims.

Alignment of current and future claims may be achieved by taking into account reasonable estimates of the long-term assets and liabilities of the asbestos trust—recognizing the likelihood that these estimates have historically been higher and lower, respectively, than they proved to be in practice. If these adjusted estimates reflect a reasonable prospect of a long-term shortfall, payment of current claims should be reduced to the extent necessary to make anticipated current and future payments for similar claims equal to future demands. Unpaid amounts may be escrowed for a fixed period, at least until such time as the anticipated shortfalls are no longer a concern (which may be established by evidence that trust assets are demonstrably higher or actual expenses of the trust are demonstrably lower than estimated), and then paid at that time. At a minimum, and in accordance with the conclusions in Combustion Engineering and other asbestos bankruptcy opinions, a true
"identity of interest" demands an end to front-loading payments to current claimants through "stub claims" or other contrivances.

Critical questions arise, however, about whether current claims are legitimate proxies for future victims and whether the individuals casting votes do so in a manner that reflects the interests of current claimants (and, by proxy, future victims). These issues are discussed in turn.

1. The Legitimacy of Current Claimants as Proxies for Future Victims

Throughout the history of bankruptcy law, transparency has been viewed as an essential element in maintaining confidence in the system. Although "[t]here is a strong presumption and public policy in favor of public access to court records" generally, "[t]he public interest in openness of court proceedings is at its zenith when issues concerning the integrity and transparency of bankruptcy court proceedings are involved . . . ." Of course, transparency is not only a question of access to public records but also the open disclosure of critical information in those records. As Judge Bohm recently noted, "in order for the bankruptcy system to function . . . every entity involved in a bankruptcy proceeding must fully disclose all relevant facts." This

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205 In re Food Mgmt. Group, 359 B.R. 543, 553 (Bankr. S.D.N.Y. 2007); see also In re Bell & Beckwith, 44 B.R. 661, 664 (Bankr. N.D. Ohio 1984) ("This policy of open inspection, established in the Bankruptcy Code itself, is fundamental to the operation of the bankruptcy system and is the best means of avoiding any suggestion of impropriety that might or could be raised.").

206 Sanchez v. Ameriquest Mortgage Co. (In re Sanchez), 372 B.R. 289, 297 (Bankr. S.D. Tex. 2007) (citing several cases); see also In re Davis, No.
mirrors the First Circuit's emphasis on full disclosure by debtors in bankruptcy:

The [bankruptcy] statutes are designed to insure that complete, truthful, and reliable information is put forward at the outset of the proceedings, so that decisions can be made by the parties in interest based on fact rather than fiction. As we have stated, the successful functioning of the bankruptcy act hinges both upon the bankrupt's veracity and his willingness to make full disclosure. Neither the trustee nor the creditors should be required to engage in a laborious tug-of-war to drag the simple truth into the glare of daylight.²⁰⁷

In short, the integrity of the bankruptcy process demands transparency—both in disclosure and open public records.

Like so many other provisions of bankruptcy law, Section 524(g) cannot serve its fundamental purpose without transparency. Votes cast in the names of fraudulent creditors protect current and future victims no more than votes cast on account of a random sampling of the phone book. Without transparency, however, enormous blocks of fraudulent or fundamentally flawed claims may be filed and alter critical asbestos creditor voting results.

Even if such claims are entitled to a presumption of validity notwithstanding the overwhelming historical evidence of asbestos claim fraud and other questionable conduct,²⁰⁸ the refusal to allow other parties in interest to

²⁰⁷ *In re Tully*, 818 F.2d at 110 (internal citations and quotations omitted).

²⁰⁸ See, e.g., Brickman et al., supra note 127.
test this presumption in any meaningful way is inexcusable. Given this history and the potential prejudice to asbestos victims, bankruptcy courts should not just allow but require spot audits of the supporting information for claims either filed against a debtor or settled pre-petition. Secondary audits should also be required for firms whose sample claims fare poorly in an initial audit. And, given that firms have been remarkably consistent in their practices (if not their factual assertions) across cases, particularly demanding scrutiny should be the norm for claims submitted by firms with a history of filing weak or unsupported claims.

Of course, the primary drawback of transparency is that investigation will delay the case. Practically speaking, the delays associated with initial investigations alone are minimal. The real threat is that widespread fraud or other misconduct will be discovered, thereby delaying a case for months or years, if a plan will ever be confirmed. Yet this is precisely the risk that debtors, lawyers, and other professionals assume when they play fast and loose with claims, even when practical experience shows that the risk is virtually non-existent. By making this risk a reality, courts may finally start deterring such conduct and bring some semblance of sanity to the claim filing process.

Moreover, courts and parties are entitled to know who attorneys represent and the nature of their representation in bankruptcy. As demonstrated in the Gilbert Heintz disqualification in Congoleum, there is considerable risk involved with allowing relationships to remain concealed over a prolonged period. This is no less true for parties who assert, but are often unwilling to substantiate, the authority to speak for large blocks of asbestos claimants. If claimants’ rights are going to be modified by a bankruptcy, it is hardly unreasonable to ensure that they are aware of the case and have specifically authorized counsel to speak and vote on their behalf in that case.

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Unfortunately, experience demonstrates that courts and parties may not be able to rely on rules governing professional conduct to guard against abuse. This was true in asbestos cases nearly two decades ago, and it remains true in bankruptcy today. As an initial matter, the systems that regulate attorney misconduct are far from adequate. Clients are rarely able to supervise their attorneys throughout the litigation and settlement process, and attorneys frequently underestimate their personal risks.

210 See Raymark Indus., Inc. v. Stemple, No. 88-1014-K, 1990 U.S. Dist. LEXIS 6710, at *5-6 (D. Kan. May 30, 1990) ("For all purposes, Raymark and this court reasonably assumed, given the defendant attorneys' professional responsibilities and Rule 11 compliance, that they would only submit claims of at least some merit, but surely would not recklessly acquiesce in the filing of a constant, steady flow of faulty claims. As this opinion will demonstrate, such is apparently the case. As stated at the time of hearing on the motions, this claim process appears to be a 'professional farce!' The process makes a mockery of the practices of law and medicine! Indeed, if this court were now to acquiesce in any of them it would make a 'laughingstock' of the court!").

211 David B. Wilkins, Who Should Regulate Lawyers?, 105 HARV. L. REV. 799, 867 (1992) ("By condemning only the most flagrant departures from the client service model, the current disciplinary system leaves a regulatory void that may encourage lawyers for individual clients to exploit the indeterminacy of legal rules in ways quite inconsistent with either client or public understandings of professional independence. Sociologists have repeatedly documented instances in which these lawyers have sacrificed the interests of their unsophisticated clients to avoid the powerful embedded controls exerted by colleagues, state officials, or others with whom they share a long-term relationship. Although it is possible that these embedded interests will coincide with a lawyer's independent professional judgment, it is as least at likely that lawyers may wield a power they have over individual clients in a manner that benefits no one so much as themselves."). (quoting Stephen Ellmann, Lawyers and Clients, 34 UCLA L. REV. 717, 720 (1987)).

212 See Brickman, supra note 60, at 838 ("Even egregious violations of rules of ethics usually generate disinterest from bar disciplinary counsel and state supreme courts when the subject is asbestos litigation."); Roger C. Cramton, Asbestos Litigation & Tort Law: Trends, Ethics, & Solutions, 31 PEPP. L. REV. 175, 178 (2003) ("Individual clients, who could raise the issues, have neither the time nor the resources to pursue these issues.").

Indeed, as Professor Regan's recent book concerning the rise and fall of attorney John Gellene highlights, lawyers are as susceptible to self-serving justifications as anyone else. Moreover, because the law firms that submit claims for payment may have no direct contact with the claimants, screening companies, or doctors involved, the system conveniently offers lawyers multiple layers of deniability in the event that the claims are ultimately found to be wholly unsupported in fact. Thus, just as some courts appear content to rely on state bar associations to keep attorneys in check, attorneys may claim that they relied on these parties' professional or other obligations rather than investigating critical elements of the claims themselves.

Bankruptcy courts hold significant options in sanctioning fraudulent claim filings and other misconduct. Much like the other options discussed previously, however, this potential remains unrealized. Lawyers who submit unsupported or fraudulent claims, regardless of their actual knowledge of any misconduct on the part of other professionals or claimants, are responsible for the claims that they submit for payment. The courts' general judgments affects attorneys as well. No attorney believes disbarment or civil liability for securities fraud is in her long-term interest, but overconfidence, undue optimism, the illusion of control, and related decision-making errors can cause attorneys to jeopardize their long-term reputational interest by taking unwise risks.


215 See, e.g., Adair v. Sherman, 230 F.3d 890, 895 n.8 (7th Cir. 2000) ("Rule 9011(b) explicitly requires all filings with the court to present only facts which the party reasonably believes to have evidentiary support; debtors facing fraudulent proofs of claim could seek sanctions under that section."); Caldwell v. United Capital Corp. (In re Rainbow Magazine, Inc.), 77 F.3d 278, 284-85 (9th Cir. 1996) (recognizing bankruptcy courts' inherent power to sanction misconduct).

216 Bankruptcy Rule 9011 requires a "reasonable" inquiry into any claim submitted for payment in bankruptcy. See, e.g., Timmons v. Cassell (In re Cassell), 254 B.R. 687, 691 (B.A.P. 6th Cir. 2000) (noting "a continuing responsibility to review and reevaluate" the basis for the claim, thus, the attorney presenting the claim cannot merely rely on others in fulfilling this duty); Sramek v. Jacobsen (In re REJ Props.), No. 07-41274
unwillingness to investigate is understandable—opponents may abuse the process, among other reasons—but the firm application of a standard of conduct in asbestos claim submissions is a necessary element of deterring misconduct. As Professor Hylton reasoned in the asbestos tort context:

> In light of the apparent incentive to include fraudulent claims in mass tort settings, a policy of sanctioning plaintiffs’ attorneys who bundle fraudulent claims would be desirable. The plaintiffs’ attorney should be considered responsible for the quality of claims he represents. If an attorney is permitted to avoid responsibility by arguing that he had no knowledge of the fraudulent claims, then attorneys who knowingly bundle fraudulent claims will find no obstacles in their way.²¹⁷

The Gellene matter demonstrates the degree to which even one case can alter legal cultures. Although the conduct involved and Gellene’s ultimate criminal conviction may have been extreme examples, the courts’ strict application of bankruptcy disclosure requirements forced practitioners and law firms to reevaluate their bankruptcy disclosure processes and played a significant role in the adoption of the “when in doubt, disclose”²¹⁸ approach at law firms across the

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²¹⁸ In re LSS Supply, Inc., 247 B.R. 280, 283 (Bankr. D. Ariz. 2000) (“The standard is really quite simple, disclose one’s connection and, if there is any doubt what should be disclosed, one must err on the side of disclosing information and not withholding information.”); Michael Richman, Disclose (Publish) or Perish, Revisited: Disclosing Business “Connections” between Bankruptcy Counsel and Other Professionals, AM. BANKR. INST. J., APR. 2006, at 18 (2006) (noting the “cardinal principle
country. This is not to suggest that the lawyers involved in asbestos bankruptcies have committed bankruptcy fraud or need be convicted of criminal misconduct. Rather, it reflects the fact that, in the relatively small world of corporate bankruptcy practice, uncompromising judicial responses to clear misconduct and an unyielding policy of investigating questionable conduct are likely to influence attitudes toward disclosure. Of course, as the Gilbert Heintz example demonstrates, some firms may still be willing to press their luck. When they do, however, courts have an obligation to the process, and to those who fulfill their own obligations within that process, to respond with nothing less than decisive sanctions.

2. Ensuring that Votes Represent the Correct Interests

The degree to which previous asbestos bankruptcies have been plagued by attorney conflicts of interest has been the focus of intense academic discussion recently. Moreover, one of the most significant and least discussed elements of the Third Circuit's reversal of Gilbert Heintz's retention in Congoleum was the panel's harsh admonition to lower courts about their obligation to scrutinize the roles played by professionals in asbestos bankruptcies:

[I]n class actions, particularly settlement-only suits, the district court has a duty to protect the members of the class . . . from lawyers for the class who may, in derogation of their professional and fiduciary obligations, place their pecuniary self-interest ahead of that of the class. . . . [W]e caution that here, as in

'when in doubt, disclose,' and the "remarkable . . . prominent examples of failures that uniformly provoke the response, 'what were they thinking?'". However, given the current state of play in asbestos pre-packs, it seems doubtful that even criminal misconduct would be discovered in most cases.

See, e.g., Brickman, supra note 60.
situations of settlement-only class litigation, careful and comprehensive scrutiny is required.\textsuperscript{221}

This focus is not mere professionalism for professionalism's sake; the courts' failure to scrutinize the relationships and conflicts of interest that permeate asbestos bankruptcies strips away significant protections of the statute and undermines the legitimacy of any plan that may be confirmed.\textsuperscript{222} Block voting by conflicted counsel fails to provide the "indicia of creditor support" that the voting requirements of Sections 524(g) and 1129 are designed to obtain. At best, it demonstrates that attorneys, whose interests may conflict with some or all of the claimants whose votes they are casting, support the plan.

Conversely, the failure to reign in attorney conflicts may unreasonably delay, or even completely undermine a case. As demonstrated in Congoleum, attorneys may cast all of their clients' votes against a plan based on their dissatisfaction with the treatment afforded to some claims, even though that treatment benefits most of their clients.

To be clear, the Controlling Firms and other counsel are important components of any realistic process for managing asbestos claims in bankruptcy. Attorneys can play an invaluable role in facilitating communication to plaintiffs, and their presence is usually the primary safeguard against overreaching by other powerful, well-financed parties. Moreover, managing the complexities of Chapter 11 can be difficult for even seasoned practitioners, much less unsophisticated individual creditors. Thus, the advice of experienced counsel may be necessary for most asbestos claimants to make anything resembling educated judgments at key stages of the process.

\textsuperscript{221} Century Indem. v. Congoleum Corp. (\textit{In re Congoleum}) 426 F.3d 675, 693-94 (3d Cir. 2005) (internal citations and quotations omitted).

\textsuperscript{222} \textit{Id.} at 692 ("We do not approve of a bankruptcy court applying less than careful scrutiny to pre-petition procedures in pre-packaged plans. The parties here seek the court's imprimatur of a reorganization that will free the debtor of all current and future asbestos liability. The legitimacy of such a transaction is dependent on the stature of the court.").
Acknowledging that attorneys have a critical role to play, however, does not mean that asbestos bankruptcies are necessarily unworkable. Rather, it suggests that greater vigilance is required to balance this necessity against its inherent risks. Clearly defining the parameters of that involvement will allow courts and other parties to restore due process for future claimants and, practically speaking, provide an important check on the asbestos veto power. Two fundamental approaches to addressing these concerns are readily apparent: insist upon individual asbestos claimant voting or adopt procedures that better protect against conflicts of interest.

Although block voting may provide some administrative convenience, it also lends itself to self-dealing and manipulation by conflicted attorneys. Moreover, there is no principled reason that asbestos claimants must vote in blocks through their attorneys. Many asbestos bankruptcies already involve claim and noticing agents who specialize in handling mass claimant issues in bankruptcy, and large bankruptcy cases frequently involve large blocks of creditors who vote individually. In short, given the experience and technological sophistication of these organizations, it is both practical and reasonable to require individual voting in asbestos bankruptcy cases.

Even where claimants expressly allow their attorneys to vote on their behalf, this consent will not be sufficient if it is not informed. The fact that many of these clients may not be sophisticated does not mean that they are incapable of understanding the basic issues that concern them most, and straightforward disclosure of the factors that may influence those casting their votes will at least give them the opportunity to make informed decisions. If a claimant continues to agree that the attorney may vote their claim after full, current disclosure, and that vote does not otherwise violate professional responsibility obligations, then the vote may be sufficient.

Of course, attorneys are subject to state bar investigations for misconduct, but, for the reasons discussed previously, the expectation that this risk will provide adequate assurance that these disclosures will occur is no substitute for diligent oversight. To that end, mandatory disclosure of information that will enable claimants to evaluate these conflicts—among other things the attorney's other representations, personal interests, and financial compensation received (or to be received) in connection with the case—should be required.

3. Ensuring the Alignment of Interests in Practice

The practical elements of aligning current and future interests are deceptively simple:

1. All assets available to pay current and future claims should be swept into a single fund, not separate trusts;
2. The same claim criteria should be used to validate and value current and future claims; and
3. Current individual claim payments should be capped at a percentage that, under conservative estimates, maximizes the likelihood that similar current and future claims will be paid on a pro rata basis.

In theory, such an arrangement would force current parties to address the very difficult disputes over the basic standards of proof required to establish a valid claim, the relative values of different types of asbestos injuries, and the aggregate amount of funding available to the trust. In the two decades since the Manville trust was established, dozens of similar approaches both in and out of bankruptcy have been established, so we have tremendous empirical resources available to guide the estimation of how different criteria will affect the aggregate payments under a trust over its lifetime and gauge the total assets that we may expect to be available to a trust during this time. And, as time goes on and additional information becomes available, these estimates should improve.
In practice, however, these guidelines may be difficult to administer. The estimation of future liabilities and assets is extremely complex and subject to manipulation. Even good faith estimates may not account for critical, as yet unknown, scientific and legal developments that may fundamentally alter the dynamics of the process. Moreover, current claimants may reject any scheme that withholds a portion of their recoveries on principle alone. At the very least, this process may intensify intra-class disputes among asbestos claimants and delay or undermine plan confirmation.

Although these problems are significant, they are not unique to this proposal. Recent cases avoid them not by resolving important questions about the burden of proof required to establish claims or the relative value of different types of claims but by allowing each distinct current claimant group to maximize its own recovery prospects. As long as sufficient assets are available to pay a current claimant group however much they believe to be satisfactory, they have no financial incentive to intervene in the decisions affecting the treatment of other claims. Those whose claims will be impacted by those provisions—future victims—do not have a meaningful voice in the process at the outset and, by the time they are involved, there may be too little left of the trust assets to justify a battle over the inequities built into the trust’s administration.

B. Reframing Section 524(g) Legal Representatives’ Role in the Protection of Future Claimants

Professor Nagareda makes a compelling case that Section 524(g) legal representatives lack the necessary bargaining leverage to be “robust protector[s]” of future claimants’ interests. And, as Professor Nagareda suggests, the emphasis on the appointment of a legal representative to protect future victims’ interests distracts us from pursuing a far more promising approach—adjusting the incentives for

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224 Nagareda, supra note 26, at 182; see generally, id. at 179-82.
those with considerable leverage in negotiations in a manner that may better protect future victims.\textsuperscript{225}

Professor Nagareda's well-reasoned assessments, however, highlight the inadequacies of the Section 524(g) legal representative when it is the only source of protection for future victims—as has been the case in recent asbestos bankruptcies—not its potential utility as part of a larger system of protection. Statutory legal representatives undoubtedly have standing to challenge provisions of a plan that undermine Section 524(g)'s protections, which, in itself, can be a valuable tool in negotiations. Indeed, bankruptcy courts will be hard-pressed to recommend confirmation of a plan over a legal representative's well-reasoned objections, particularly with respect to the critical questions of voting manipulation, questionable liability estimates, front-loaded payments, and lowball trust funding arrangements.

To date, however, this potential remains largely unrealized. To be certain, some legal representatives have been aggressive in matters concerning trust funding, but few have forced significant alterations to matters that put them at odds with the Controlling Firms who may veto their appointment in future cases and deny them lucrative positions with any asbestos trust established by a plan of reorganization. Whether this punch-pulling effect is conscious or not, it suggests that greater vigilance is required in ensuring that legal representatives' interests are fully aligned with those of future victims.

1. Selection and Appointment

As in other areas of law, the divide between legal scholarship concerning Section 524(g) and prevailing practice is considerable. With respect to the condition that a legal representative be appointed, however, the two may as well be discussing entirely different statutes. For scholars, the absence of any express statutory criteria for such an appointment requires an assessment of the purpose of the appointment and leads to additional investigation into

\textsuperscript{225} Id.
comparable mechanisms in other areas of law. In court, as with so many other aspects of Section 524(g), colorable technical compliance with the statutory language—in this case, the appointment of someone, anyone, as a nominal legal representative without more—is generally sufficient, even where the appointee is burdened by numerous conflicts of interest.

To be sure, simply continuing the pre-petition legal representative’s role after the commencement of the case has its advantages. A new legal representative and her professionals may require weeks or months to get up to speed, which will be more expensive and, most likely, delay consideration of important issues in the early stages of the case. Moreover, the new legal representative may have very different views on critical elements of the plan, which may erase the efficiencies obtained by negotiating the deal pre-petition.

On the other hand, a strong, independent legal representative will best ensure that any confirmed plan reflects the best interests of future claimants and provide the debtor with a greater assurance of finality. Moreover, such an appointment may ultimately prove more efficient than the current process because uncertainty should caution the parties against overreaching during pre-petition negotiations. If the plan proponents are truly dedicated to a short stay in Chapter 11, they will not want to propose a plan that will invite an objection from a reasonable legal representative. If, on the other hand, a pre-packaged plan is designed more along the lines of previous asbestos pre-packs, or the Controlling Firms refuse to work with an independent legal representative, the bankruptcy court will see, at a very early stage in the case, that a more aggressive approach in its dealings with these recalcitrant parties is required.

2. Stripping Away Prospective Conflicts of Interest

Although legal representatives may be agents without a principal as a practical matter, they are not agents without rigid duties. Among these, perhaps the most significant is
the duty of undivided loyalty; if for no other reason, precisely because their constituency is not able to protect itself from its agent’s misconduct. Even the appearance of conflict may undermine the integrity of the proceedings, encourage wasteful litigation, and open the door to future challenges to the Section 524(g) injunction.

One subtle yet potentially significant conflict arises when the legal representative is promised lucrative ongoing work for the bankruptcy trust established under Section 524(g). As noted previously, this promise provides the legal representative with strong personal interests both in ensuring that the plan is approved and in avoiding actions that might put them at odds with the Controlling Firms that will serve as trustees over the trusts. Unequivocal rejection of the appointment of legal representatives to these and other post-confirmation roles will thus help ensure that their judgments are not colored by self-interest.

Moreover, courts should be careful to clearly define the role when appointing a legal representative. Some legal representatives appear to have no clear picture of who they represent and operate on the faulty assumption that they fulfill their obligations solely by maximizing assets that are paid into the trust. As the rapid depletion of the Manville and other asbestos trusts vividly demonstrate, this is just one factor relevant to future victims’ ultimate recoveries; no matter how well-funded a trust may be at the outset, allowing minimal checks on weak or fraudulent claims will significantly undermine these future recoveries. And though weak evidentiary barriers to payment may make it easier for future claimants to file their own claims, this primarily benefits the law firms responsible for submitting claims (who are paid large contingency fees for doing so) and will be of little comfort if the trust lacks sufficient resources to satisfy those claims.

V. CONCLUSION

Asbestos pre-packs to date have widely incorporated the worst aspects of asbestos litigation: pervasive conflicts of interest, relaxed judicial oversight, wasted resources, and
under-compensated victims. In stressing the value of compromise and encouraging asbestos pre-packs, courts have overlooked the basic elements of these schemes that are fundamentally inconsistent with compromise—single-constituency dominance, concealment of critical information, and exclusion of parties with significant interests at stake. The superficially reasonable justifications for these failures do not withstand scrutiny or even a cursory reference to practical experience. Indeed, this experience shows that, however noble or understandable the goals, judicial efforts to facilitate asbestos pre-packs have dramatically undermined the potential of Section 524(g).

As demonstrated, the most egregious abuses of asbestos bankruptcy law to date stem less from inherent flaws in the statutory scheme than the manner in which courts and participants in the process approach the law. Of course, a comprehensive global solution to the ills that plague asbestos litigation may not be possible without congressional action. But an uncompromising adherence to the dictates of bankruptcy law generally, and Section 524(g) specifically, will improve the prospects that viable companies will survive, victims will be compensated, and the integrity of the process will be preserved.