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HEARING ON THE FURTHERING ASBESTOS CLAIMS TRANSPARENCY ACT OF 2012

HOUSE JUDICIARY COMMITTEE:
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Chairman Coble, Ranking Member Cohen, and members of the committee, thank you for this opportunity to testify in support of H.R. 4369, the Furthering Asbestos Claims Transparency Act (the FACT Act) of 2012.

I am Todd Brown, Associate Professor of Law and Director of the Center for the Study of Business Transactions at SUNY Buffalo, where I teach Bankruptcy, Business Restructuring, Torts and Mass Torts. My research focuses on the intersection of mass torts and bankruptcy law, with an emphasis on identifying and preventing practices that undermine the integrity of the judicial process. Prior to becoming a law professor, I worked with the Business Restructuring and Reorganization practice at Jones Day from 1999 to 2003, where I served primarily as debtor's counsel in several large corporate chapter 11 cases. I subsequently worked at WilmerHale from 2003 to 2007, where, among other things, I represented individuals, corporations, banks and insurers in bankruptcy and class action matters.

The views offered here are mine alone, not those of my current or former employers or clients. I am not being compensated for my testimony today, and I do not accept any compensation or funding from any party that is involved in asbestos personal injury or asbestos bankruptcy litigation or legislation.

Introduction

As a matter of bankruptcy policy, the very idea that a bill intended to advance transparency would be in any way controversial is striking. If history teaches us anything about bankruptcy law and practice, it is that transparency and safeguarding the interests of absent parties go hand-in-hand. In 1929, for example,

the corruption that had become common under the Bankruptcy Act of 1898 came to a head when twelve bankruptcy attorneys in the Southern District of New York were indicted for theft of bankruptcy estate assets. The subsequent Donovan Report, which looked at bankruptcy administration in six cities, determined that, "fundamental defects in administration are not restricted to New York, but exist generally throughout the country."[1] This report recommended, among other things, greater uniformity in bankruptcy administration and emphasized the need for more empirical data and studies on bankruptcy administration. A full recitation of the history between the Donovan Report and the adoption of the Bankruptcy Code of 1978 is beyond the scope of my testimony today; it is sufficient to note that the modern emphasis on transparency and oversight in bankruptcy administration are grounded in our experience with practices that emerged without these safeguards.

The need for comparable transparency in the asbestos bankruptcy trust context is compelling. As the assets under trust control approach $40 billion – a considerable portion of which might remain available in the tort system in the absence of Section 524(g) – other defendants, many of whom were peripheral defendants until recently, find themselves exposed to far greater defense costs and tort liability. Early trusts were flooded with specious unimpaired claims, and though state courts and legislatures have taken steps to reign in the perceived abuses in asbestos litigation, new trusts continue to be flooded with unanticipated claim volumes. We know that dubious claims continue to slip through the cracks,

[1] *See* House Comm. on the Judiciary, Report on the Administration of Bankruptcy Estates, 71st Cong., 3d Sess. 3-4 (1931).

and the lack of communication between the trusts and state tort systems fuels concerns that some lawyers may be gaming the system to obtain unwarranted recoveries either in state court or from the trusts. The extent to which these complaints may reflect pervasive problems, however, remains uncertain in large part because trust operations are largely shielded from public scrutiny. These are significant policy questions, and the need to advance intelligent and informed debate on asbestos bankruptcy policy strongly favors adoption of the FACT Act.

I begin this discussion with a brief history of asbestos litigation and bankruptcy trusts. From there, I outline the current state of asbestos bankruptcy trust administration and its relationship to the tort system. I conclude with an analysis of the arguments for and against the disclosures required under the FACT Act.

A Brief History of Asbestos Litigation and Bankruptcy Trusts

Asbestos personal injury litigation – the largest and longest running mass tort litigation in history – may be viewed as progressing across distinct stages. Initially, asbestos litigation was unremarkable; a series of discrete cases brought on behalf of plaintiffs with both substantial histories of exposure to airborne asbestos fibers and the most severe forms of asbestos related disease. Given the difficulties associated with establishing a connection between asbestos disease and exposure to specific defendants' products, many of these early cases failed. Some courts adopted modifications to tort law and procedural rules in an effort to lower the barriers to compensation and reduce the transaction costs of litigation. These changes, and the discovery of evidence suggesting a conspiracy to conceal the risks associated with

asbestos exposure, dramatically altered the litigation exposure of first line asbestos defendants.[2]

By the early 1980's, it became clear that some of these first line asbestos defendants would not survive over the long term; leading to the first asbestos bankruptcies in 1982. Many plaintiffs' attorneys and commentators were particularly critical of the bankruptcy of Johns Manville, the most commonly named asbestos personal injury defendant at the time, but the bankruptcy court concluded that the inevitable alternative – liquidation – "would preclude just compensation of some present asbestos victims and all future asbestos claimants" in contravention of bankruptcy policy.[3] To preserve this value for the benefit of both current and future victims, the parties to the Manville bankruptcy established a groundbreaking solution: establishing and channeling all asbestos claims against Manville to a trust intended to process claims and compensate victims in a prompt, efficient and equitable manner over time.

Even as the Manville bankruptcy wound its way toward conclusion, a segment of the asbestos plaintiffs' bar recognized an opportunity to recruit and advance large volumes of "unimpaired claims"[4] through litigation-focused screenings. The unanticipated influx of these new claims quickly overwhelmed the

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[2] For the sake of brevity and clarity, I refer to the defendants who were most active in the asbestos industry and, accordingly, named most frequently in asbestos litigation at this early stage as "first line asbestos defendants."

[3] In re Johns-Manville Corp., 36 B.R. 727, 736 (Bankr. S.D.N.Y. 1984).

[4] Findley v. Trs. of the Manville Pers. Injury Settlement Trust (In re Joint E. & S. Dists. Asbestos Litig.), 237 F. Supp. 2d 297, 306 (E.D.N.Y. 2002)("A characterizing feature of the recent acceleration in asbestos litigation is the number of claims being filed by plaintiffs who are functionally unimpaired.").

Manville Trust,[5] taxed the resources and imagination of the state courts that struggled to manage the emerging "elephantine mass"[6] of asbestos claims, and "led to an unprecedented wave of asbestos bankruptcies."[7] Just as other first line defendants shouldered greater liability in state court following the Manville bankruptcy, second and third line defendants shouldered greater liability in state court when the remaining first line defendants left the tort system.[8] As the dominoes fell and the volume of new claims continued to rise, plaintiffs' lawyers searched for "other deep pockets"[9] in what one former plaintiffs' attorney called an "endless search for a solvent bystander."[10]

As this second era of asbestos litigation – an era dominated by unimpaired asbestos claims – reached full stride, Congress passed the 1994 amendments to the Bankruptcy Code, which included 11 U.S.C. §§ 524(g) and 524(h). Sparked by concerns over the validity of the trust-injunction mechanism employed in the Manville plan of reorganization, and the resulting effect of these concerns on future

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[5] *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.").

[6] Ortiz v. Fibreboard, 527 U.S. 815, 821 (1999).

[7] *See* Patrick Hanlon & Anne Smetak, *Asbestos Changes*, 62 N.Y.U. ANN. SURV. AM. L. 525, 547 (2007).

[8] *See* NAGAREDA, *supra* note 5, at 167.

[9] *See* Lester Brickman, *On the Theory Class's Theories of Asbestos Litigation: The Disconnect Between Scholarship and Reality*, 31 PEPP. L. REV. 33, 55 (2003).

[10] See James A. Henderson, Jr., *Asbestos Litigation Madness: Have the States Turned a Corner?*, 20-23 MEALEY'S LIT. REP. ASB. 19 (2006)(quoting Dickie Scruggs).

asbestos victims,[11] Section 524(h) amounted to a Congressional blessing of existing asbestos trusts, while Section 524(g) expressly authorized the growing number of companies facing enterprise-threatening asbestos liability to establish their own bankruptcy trusts.

At the same time, some leading plaintiffs' attorneys, defendants and insurers attempted to address the increasingly unmanageable asbestos claim volumes through global class action settlements under Rule 23 of the Federal Rules of Civil Procedure. In its 1996 opinion in the *Amchem* case, the Supreme Court rejected one such settlement under Rule 23(b)(3) on the grounds that the class could not satisfy the requirements of common issue predominance and adequacy of representation.[12] Three years later, in *Ortiz*, the Court likewise rejected a similar settlement under Rule 23(b)(1)(B).[13] In both cases, the Court stressed, among other things, the conflicts of interest inherent in any settlement involving current and future claims.

A small group of leading asbestos lawyers – including some of the key plaintiffs' lawyers behind the failed class action settlements – subsequently turned their attention to establishing global settlement plans under Section 524(g) that

[11] The Manville Trust was funded, in part, by stock in Reorganized Manville. Lingering concerns about the validity of the trust-injunction mechanism weighed heavily on the value of this stock to the detriment of asbestos claimants seeking compensation from the trust. 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.").

[12] Amchem Prods., Inc. v. Windsor, 521 U.S. 591 (1996).

[13] Ortiz v. Fibreboard Corp., 527 U.S. 815 (1999).

were substantively the same as those rejected by the Court in *Amchem* and *Ortiz*. Under the prepack asbestos bankruptcy model that emerged, a defendant could obtain peace from future asbestos litigation – usually without sacrificing much, if any, of equity's position in the company – in return for giving plaintiffs' counsel effective control over the design and operation of the resulting trust. Leading plaintiffs' lawyers thus obtained control of every critical aspect of these cases, including the appointment of the legal representative demanded under Section 524(g) and the parties who would be responsible for processing and paying claims going forward. The only parties likely to object to this arrangement – the insurers whose policies with defendants were to be the primary source of funding for most of these trusts – were frequently denied standing to appeal orders confirming the resulting plans due to the unique prudential standing rules applied to bankruptcy matters.[14] Where the class action settlement approach failed, efforts to establish comparable settlements under Section 524(g) have yielded an astounding 44 asbestos bankruptcy trust since 2000.[15]

Around the time that these asbestos bankruptcies were gaining traction, a number of news reports,[16] medical experts,[17] and legal experts[18] increasingly

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[14] I discussed the evolution of these rules and their application in asbestos bankruptcy cases in: S. Todd Brown, *Non-Pecuniary Interests and the Injudicious Limits of Appellate Standing in Bankruptcy*, 59 BAYLOR L. REV. 569 (2007).

[15] Asbestos Injury Compensation: The Role and Administration of Asbestos Trusts, United States Government Accountability Office, Sept. 2011 (noting that the number of asbestos personal injury trusts rose from 16 in 2000 to 60 in 2011)[hereinafter, "GAO Report"].

[16] *See, e.g.*, Eddie Curran, *Diagnosing for Dollars?*, MOBILE REGISTER, Apr. 4, 2004, at A1; Stephen Hudak & John F. Hagan, *Asbestos Litigation Overwhelms Courts*, CLEVELAND PLAIN DEALER, Nov. 5, 2002, at 1; Roger Parloff, *The $ 200 Billion*

focused on evidence that the practices used to generate this "elephantine mass" of unimpaired claims were, at best, suspect. Relying upon this wealth of information – including data that, until recently, was voluntarily disclosed by the Manville Trust – Professor Lester Brickman published a series of articles that revealed the extent to which litigation screenings were flooding asbestos tort litigation and bankruptcy trusts with "specious claims."[19] And in 2005, following an extensive review of the litigation screening practices employed to develop a majority of the claims presented in the Silica MDL – practices largely borrowed from, and carried out by regular participants in, asbestos litigation screenings – Judge Janis Jack issued a detailed and scathing opinion that, among other things, aptly characterized the resulting claims as "manufactured for money."[20]

Miscarriage of Justice; Asbestos Lawyers Are Pitting Plaintiffs Who Aren't Sick Against Companies that Never Made the Stuff - and Extracting Billions for Themselves, FORTUNE, Mar. 4, 2002; Pamela Sherrid, *Looking for Some Million Dollar Lungs*, U.S. NEWS & WORLD REP., Dec. 17, 2001, at 36.

[17] *See*, *e.g.*, David Egilman & Susanna Rankin Bohme, *Attorney-Directed Screenings Can Be Hazardous*, 45 AM. J. OF INDUS. MED. 305 (2004); Joseph N. Gitlin et al., *Comparison of "B" Readers' Interpretations of Chest Radiographs for Asbestos Related Changes*, 11 ACAD. RADIOLOGY 843 (Aug. 2004); David Egilman, *Asbestos Screenings*, 42 AM. J. OF INDUS. MED. 163 (2002).

[18] *See, e.g.,* Griffin B. Bell, *Asbestos & The Sleeping Constitution*, 31 PEPP. L. REV. 1, 5 (2003).

[19] Lester Brickman, *Ethical Issues in Asbestos Litigation*, 33 HOFSTRA L. REV. 833 (2005); Lester Brickman, *On the Theory Class's Theories of Asbestos Litigation: The Disconnect Between Scholarship and Reality*, 31 PEPP. L. REV. 33 (2003); Lester Brickman, *Lawyers' Ethics and Fiduciary Obligation in the Brave New World of Aggregative Litigation*, 26 WM & MARY ENVTL. L. & POL'Y. REV. 243 (2001).

[20] 398 F. Supp. 2d 563, 635 (S.D. Tex. 2005)("[T]hese diagnoses were about litigation rather than health care. And yet this statement, while true, overestimates the motives of the people who engineered them. The word 'litigation' implies (or should imply) the search for truth and the quest for justice. But it is apparent that truth and justice had very little to do with these diagnoses--otherwise more effort

Asbestos Bankruptcies Today

These combined events bring asbestos litigation and bankruptcy to an important crossroads. In the aftermath of the Silica MDL and a variety of state reforms intended to correct the perceived abuses of repeat players in asbestos litigation, unimpaired claim filings – which once accounted for more than 9 out of every 10 new asbestos claims – have fallen dramatically and remain well below their peak.[21] At the same time, "the number of asbestos personal injury trusts increased from 16 trusts with a combined total of $4.2 billion in assets in 2000 to 60 with a combined total of over $36.8 billion in assets in 2011."[22] Collectively, these factors suggest that we should be entering an era in which asbestos trusts are finally able to predict future claiming patterns effectively and the victims of asbestos personal injury have access to full and speedy recoveries for years to come.

Unfortunately, claim filings continue to exceed projections and trust assets continue to be depleted rapidly, so much so that it appears unlikely that any of the trusts operating today "will value, and be in a financial position to pay, present claims and future demands that involve similar claims in substantially the same manner."[23] In its 2010 report on asbestos bankruptcy trusts, RAND Corporation found that only one of the 29 trust-claim-class combinations it analyzed, the T.H.

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would have been devoted to ensuring they were accurate. Instead, these diagnoses were driven by neither health nor justice: they were manufactured for money.").

[21] *See* Snapshot or Recent Trends in Asbestos Litigation, NERA Economic Consulting, July 21, 2011.

[22] GAO Report, *supra* note 15, at 3.

[23] 11 U.S.C. § 524(g)(2)(B)(ii)(V).

Agriculture & Nutrition Trust (THAN Trust), applied a 100% payment percentage,[24] and that trust had not paid any claims through 2008.[25] Indeed, claims against the then newly established THAN Trust exceeded projections so quickly that it was forced to reduce its payment percentage to a mere 30% in 2011.[26] Another trust that previously applied a 100% payment percentage, the Shook & Fletcher Asbestos Settlement Trust, likewise reduced its payment percentage to 70% on March 1, 2012.[27] Recent adjustments to the payment percentage in other trusts reflect a similar pattern:[28]

- The C. E. Thurston & Sons Asbestos Trust *increased* its payment percentage from 40% to 80% in January 2011, only to suspend new offers altogether in January 2012 after experiencing "claims filings significantly in excess of levels projected" following the adjustment.[29]
- In November 2011, the NGC Bodily Injury Trust, noting that filings from 2007 through October 2011 were 308% higher than projected, reduced the payment percentage to 18%. The trust previously reduced the payment percentage from 55.6% to 41% in July 2011.[30]

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[24] The "payment percentage" is the percentage of the value assigned to a claim that will actually be paid to a claimant. Thus, a claim that is assigned a value of $100,000 by a trust applying a 30% payment percentage will be paid $30,000.

[25] Lloyd Dixon, Geoffrey McGovern & Amy Coombe, ASBESTOS BANKRUPTCY TRUSTS: AN OVERVIEW OF TRUST STRUCTURE AND ACTIVITY WITH DETAILED REPORTS ON THE LARGEST TRUSTS 36-38 (2010) (range from 1.1% to 100%, with a median payment percentage of approximately 25%).

[26] http://www.thanasbestostrust.com/Files/20110321_THAN_Payment_Percentage_Notice.PDF.

[27] http://www.mfrclaims.com/shook_PP.pdf.

[28] This survey is not exhaustive; it reflects only the payment percentage adjustments for some of the trusts that I follow regularly in the course of my research.

[29] http://www.claimsres.com/documents/CET/Notice%20of%20Offer%20Suspension%20-%20January%202012.pdf.

[30] https://www.ngcbitrust.org//.

- The Babcock & Wilcox Asbestos PI Trust reduced its payment percentage to 11.9%, or roughly one-third of the payment percentage in place in July 2009.[31]
- The payment percentage for the United States Gypsum Asbestos Personal Injury Settlement Trust, which was reduced from 45% to 35% in April 2009, was further reduced to 30% in January of last year.[32]
- The Celotex Asbestos Settlement Trust reduced its payment percentage from 14.1% to 9.4%.[33]
- Citing an "unanticipated significant increase in claim filings," the UNR Asbestos-Disease Claims Trust reduced its payment percentage to 0.82% in March 2011.[34]

What accounts for this continuing pattern? If, as we are told, the unimpaired claims that once dominated asbestos dockets are no longer recruited through screening mills of the sort exposed in the Silica MDL, how are we to account for the fact that even recently established trusts are overwhelmed with tens of thousands of new claims from parties who never pursued them or even suggested that they had a basis for pursuing them in the tort system? Are we seeing old claims recycled for new bankruptcy trusts, or have we seen a dramatic shift in recruiting tactics to generate far more cancer claims? If the former, why have so many named new defendants years after the statute of limitations should have run? If we are simply seeing far more cancer claims than in the past, why are we only now seeing so many new filings when asbestos-related cancer rates have been steady or declining?

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[31] http://www.bwasbestostrust.com/files/B%20W%20Payment%20Percentage%20Notices%20to%20claimants%20counsel%20and%20pro%20se%20claimants%20(P0224314).PDF.

[32] http://www.usgasbestostrust.com/files/USG%20TAC_FCR%20Consent%20letter%20on%20payment%20percentage%201_06_11%20P0191773.PDF.

[33] http://www.celotextrust.com/files/Celotex%20Pmt%20Percentage%20Change%20Letter%2012_20_2010.pdf.

[34] http://www.cpf-inc.com/upload/temp/UNRPaymentPercentageDecreaseMarch2011.pdf.

The answers to these questions are exceptionally difficult to establish with certainty given the opacity of trust submission and payment data today. Asbestos trusts aggressively contest efforts by third parties to obtain information that may allow them evaluate and identify filing trends, even though this information is undoubtedly useful in designing new trusts so that they avoid the rampant oversubscription and unduly optimistic projections that have persistently plagued their predecessors. It remains unclear how often, if at all, individual trusts share information that may allow them to identify inconsistent factual representations, and the current framework allows lawyers to avoid disclosure of trust submissions altogether by delaying filing.[35]

What we do know notwithstanding this veneer of secrecy is troubling. In addition to financial information showing that claims continue to exceed projections, anecdotal reports suggest that trusts continue to pay specious claims. In the well-publicized *Kananian v. Lorillard Tobacco Company*[36] case, for example, one plaintiffs' firm apparently attempted to exploit the secrecy of trust submissions to make factual representations under penalty of perjury that not only conflicted with each other but also with the plaintiff's representations in the state court proceedings.[37] Similar discrepancies between factual representations in state court

[35] LLOYD DIXON & GEOFFREY MCGOVERN, ASBESTOS BANKRUPTCY TRUSTS AND TORT COMPENSATION (2011).

[36] Order & Opinion, Case No. CV 442750 (Ohio Ct. Com. Pl Cuyahoga Cty., Jan. 18, 2007).

[37] *Id*. at 5-6.

and on claims submitted under penalty of perjury to asbestos trusts have been reported.[38]

In another matter, the daughter of a stomach cancer victim who died in 1966 obtained more than $130,000.00 from four bankruptcy trusts beginning in 2003.[39] Setting aside the fact that the claim was first brought nearly four decades after her father's death,[40] this case presents a number of questions about settlement practices at some trusts. First, it was unclear whether Ms. Garner was the appropriate representative of her father's estate.[41] Second, there was no medical diagnosis of mesothelioma, nor could there be given the enormous passage of time since his death; the only medical evidence supporting the claim was a speculative evaluation based on a photo of an X-ray.[42] Third, although the Manville arbitrators rejected the

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[38] Written Statement of James L. Stengel, Esq., Hearing on Asbestos Litigation Fraud and Abuse, House Judiciary Committee, Sept. 9, 2011, at 17-18 (discussing inconsistencies in factual representations in cases litigated in Baltimore).

[39] *See Garner v. DII Industries, LLC Asbestos Trust*, No. 08-06191 (W.D.N.Y. Apr. 25, 2008)(Complaint and exhibits including correspondence with bankruptcy trust administrators and checks from the Manville, Celotex, and Eagle-Picher trusts totaling $131,426.00)[hereinafter *Garner Complaint*]. The H.K. Porter trust also offered a settlement of $40,000.00 to Ms. Garner. *See Garner v. DII Industries, LLC Asbestos Trust*, No. 08-06191 (W.D.N.Y. Sep. 29, 2008)[hereinafter *Garner Plaintiff's Response*].

[40] *See Garner v. DII Industries, LLC Asbestos Trust*, No. 08-06191 (W.D.N.Y. Aug. 26, 2009)(Brief in support of defendant's motion to dismiss highlighting numerous statute of limitations issues).

[41] *See Garner v. DII Industries, LLC Asbestos Trust*, No. 08-06191 (W.D.N.Y. Oct. 17, 2008)(order concluding that Ms. Garner had not established her power to sue on behalf of her father's estate). Indeed, it remains unclear how Ms. Garner, as opposed to her mother (who was still living) or someone else, was the proper estate representative, and it does not appear that any of the trusts questioned her authority to represent her father's estate.

[42] *See Garner Plaintiff's Response*, *supra* note 39 (noting physician's report that it was "quite possible" that Ms. Garner's father had mesothelioma and Manville Trust arbitrator's initial rejection of this statement as speculative). Indeed, the doctor

claim three times, it was finally approved by an "extraordinary claims panel", which approved a payment – in spite of acknowledging its weaknesses – far in excess of the scheduled value for mesothelioma claims.[43]

It remains difficult to evaluate the extent to which these examples are representative of the claim submission, review and payment practices across trusts precisely because the trusts have become so opaque. Our collective experience in asbestos litigation and bankruptcy trust administration, however, strongly suggests that the trend toward less transparency will create opportunities for manipulation and abuse. Some trusts may be extremely vigilant in reviewing claims, and others appear to be far less so. If we are to have a system that holds all trusts to the policy objectives of Section 524(g), however, greater transparency is essential.

Asbestos Bankruptcy Trusts and Transparency

Transparency has been a critical component of reforms aimed at unwinding and preventing abuse; allowing creditors, the United States Trustee, courts, other parties in interest and, ultimately, Congress to identify and address these shortcomings and preserve the integrity of the bankruptcy process. The absence of comparable transparency in asbestos bankruptcy proceedings and trust

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involved also noted the poor quality of the photograph he was reviewing in the next sentence, and the plaintiff acknowledged this fact in her pleading. *Id.* In short, it is unimaginable that this "evidence" would have been remotely sufficient to satisfy medical and scientific standards in civil litigation, and it is unclear how it was sufficient under the applicable trust distribution procedures.

[43] *See Garner Complaint*, *supra* note 39 (Manville extraordinary claim panel decision); *Garner Plaintiff's Response*, *supra* note 39 (noting that the $75,000.00 received from Manville far exceeds the scheduled amount).

administration necessarily raises concerns about whether these funds are, in practice, administered in a manner consistent with the objectives of Section 524(g).

The question, then, is whether there is some unique consideration with respect to asbestos personal injury trusts that justifies the abandonment of this policy favoring transparency. This section addresses potential justifications for abandoning the bankruptcy preference for transparency.

A. The FACT Act is an Appropriate Exercise of Legislative Authority.

The vision of asbestos bankruptcy trusts as beyond bankruptcy oversight conflates and thereby confuses the means of organizing asbestos trusts with their function in the asbestos bankruptcy process. Any trust established to fulfill the objectives of Section 524(g), just like a reorganized debtor incorporated as a new entity under the terms of a plan, will be organized under state law. But this necessity is merely a product of the fact that the specific steps of corporate or trust formation are left to state law; it does not obviate the need for these entities to comply with their obligations under the plan, the Bankruptcy Code or other applicable federal law.[44]

The Bankruptcy Code's recognition of the distinction between state law organization and the obligations that arise under federal bankruptcy law is consistent with even the most restrictive conception of the Bankruptcy Power. Although the precise reach of this power remains poorly defined, it is well settled that it applies to questions concerning the restructuring of a debtor's relations with

[44] Indeed, section 1142(a) of the Code recognizes that "the debtor and *any entity organized or to be organized for the purpose of carrying out the plan* shall carry out the plan and shall comply with any orders of the court."

its creditors.[45] When trusts are established under Section 524(g), they assign critical aspects of this power to private entities going forward, but this assignment does not strip Congress of its power to regulate these entities to ensure that they are acting in a manner consistent with the objectives they are established to advance.

B. The FACT Act is Consistent With Disclosure Obligations in Bankruptcy.

The characterization of trust claim submissions as "settlement negotiations" that should be confidential stretches credulity when contrasted with the general disclosure obligations in bankruptcy.

Filing a claim form with a trust – just like the filing of a complaint in civil litigation[46] or a proof of claim in bankruptcy – is the assertion of a legal right and requires representations under penalty of perjury. Debtors provide information about their creditors' claims and payments made to their creditors in the year preceding the bankruptcy filing under Section 521. Official Form B10 (the proof of claim) requires creditors to disclose their names, addresses, email addresses, telephone numbers, the legal and factual foundations for their claims, and "copies of any documents that support the claim[s]" – including previously non-public documents – and other personal information. Although debtors and asbestos plaintiffs have structured asbestos bankruptcy cases to avoid proof of claim filings – apparently to avoid potential objections to individual asbestos claims under Section

[45] *See*, *e.g.*, N. Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 71 (1982)(characterizing "the restructuring of debtor-creditor relations" as being "at the core of the federal bankruptcy power").

[46] *See, e.g.,* Ferguson v. Lorillard Tobacco Co., 2011 U.S. Dist. LEXIS 135183 (E.D. Pa. Nov. 22, 2011)("a claim submitted to a bankruptcy trust is more akin to a complaint than to an offer of compromise")(citing cases).

502 of the Bankruptcy Code[47] – this information is readily produced by most creditors in bankruptcy.

If negotiations take place thereafter, the various offers and counter-offers are generally entitled to confidential treatment in litigation and bankruptcy, but final settlement terms must be disclosed. Private settlements between the estate and a creditor require court approval, after full disclosure of their terms and providing parties in interest notice and the opportunity to be heard.[48] This makes sense in a traditional bankruptcy case, where multiple creditors are most often asserting claims against an estate with insufficient funds to pay all claims in full. If the debtor in possession or trustee is too generous in accepting and assigning value to competing claims, the assets available to compensate the rest of the claim pool are necessarily reduced. In the absence of this transparency, powerful repeat players could readily distort the process, walk away with distributions far beyond their statutory entitlement, and leave the rest of the claim pool with little or no recovery.

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[47] *See* S. Todd Brown, *Section 524(g) Without Compromise: Voting Rights and the Asbestos Bankruptcy Paradox*, 2008 COLUM. BUS. L. REV. 841 (2008).

[48] Fed. R. Bankr. P. 9019(a) ("On motion by the trustee and after notice and a hearing, the court may approve a compromise or settlement. Notice shall be given to creditors, the United States trustee, the debtor, and indenture trustee as provided in Rule 2002 and to any other entity as the court may direct."). The policy behind Bankruptcy Rule 9019 is to prevent the debtor from entering into secret agreements and provide interested parties the ability to review the proposed settlement and object. Motorola, Inc. v. Official Comm. of Unsecured Creditors (In re Iridium Operating LLC), 478 F.3d 452 (2d Cir. 2007); In re Masters, Inc., 141 B.R. 13, 16 (Bankr. E.D.N.Y. 1992) ("The clear purpose of Rule 9019 is to prevent the making of concealed agreements which are unknown to the creditors and unevaluated by the court.").

Creditors lose the potential for secret settlements in bankruptcy, but the trade off is that they are protected against secret agreements and manipulation by other creditors. These risks, as seen throughout the history of asbestos bankruptcies, is likewise present with respect to claims paid with the limited funds controlled by bankruptcy trusts.

C. The FACT Act is Necessary and Cost-Effective.

Even modest mandatory disclosure requirements, such as those found in the FACT Act, will inevitably draw complaints that they are unnecessary and a waste of resources. In the case of asbestos bankruptcy trusts, after all, trustees and future claimants representatives have fiduciary duties to preserve trust assets for the benefit of claimants. Moreover, nearly all of the trust distribution procedures covering active asbestos bankruptcy trusts incorporate some form of authorization for claim audits,[49] though most of these provisions require the advance consent of the trust advisory committee (TAC),[50] to verify that the claims submitted are not fraudulent and otherwise comply with the terms of the TDP. Finally, trust officials frequently note that they will comply with a valid subpoena demanding production of individual claimant information. Thus, it may be argued that the FACT Act will not protect trust assets or allow defendants to obtain relevant trust information any more than the current framework. I will address each of these concerns in turn.

[49] GAO Report, *supra* note 15, at 22.

[50] As noted in the GAO Report and the 2010 RAND Report, TAC's represent the interest of current claimants and tend to be comprised of leading plaintiffs' lawyers.

1. Fiduciary Duties of Trustees and Future Claimants Representatives.

During a typical asbestos bankruptcy case, the leading plaintiffs' lawyers will enjoy "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."[51] The Bankruptcy Code does not provide direct guidance on the criteria for appointing a claimants' representative, and "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."[52] The work performed by futures representatives during the case or post-confirmation is not supervised by the court or otherwise subjected to scrutiny. Indeed, "bankruptcy plans routinely shield legal representatives from liability to future claimants for all but the most egregious misconduct."[53]

In sum, lawyers for current claimants and debtors have strong incentives to appoint "a weak futures representative,"[54] and those who are appointed are well compensated and face little risk if they are, in fact, poor representatives of future claimants' interests. Thus, as one commentator noted, "As an institution for the

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[51] Brown, *supra* note 47, at 862, 899 ("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").

[52] *Id.* at 898.

[53] *Id.* at 899.

[54] Francis E. McGovern, *Asbestos Legislation II: Section 524(g) without Bankruptcy*, 31 PEPP. L. REV. 233, 248 (2004) ("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.").

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."[55]

The legal representative who is so appointed during the bankruptcy case most often serves in the same role in the resulting asbestos bankruptcy trust. Here, too, the future claimants' representative "has principals only as a conceptual matter"[56] both as a result of the protections against liability provided in the reorganization plan and the limited public information available to individual claimants. Indeed, given the secrecy of trust operations today, it is implausible that even a representative who is grossly negligent or actively colludes with counsel to loot the trust will be discovered and held accountable.

Moreover, once Trustees and future claimants' representatives are in place, TDP terms that govern distributions have already been finalized. TDPs provide the plaintiffs' lawyers who sit on trust advisory committees with veto power over key decisions – including any proposed amendments to TDP standards and criteria and proposed audit plans – that may effectively undermine the efforts of even the most diligent trustee or future claimants representative. Indeed, the Manville Trust's experience with its efforts to audit claims in the late 1990's and the stern rebuke it

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[55] Frederick Tung, *The Future Claims Representative in Mass Tort Bankruptcy: A Preliminary Inquiry*, 3 CHAP. L. REV. 43, 64 (2000).

[56] *Id.*, at 60 ("The terms and quality of the FCR's representation are not subject to oversight by her ostensible 'clients.'").

received as a result of this effort,[57] suggests that fiduciaries that take their duties too seriously will find more resistance than support for their efforts.

This may also explain why, in spite of the warnings concerning the legitimacy of claims generated in asbestos litigation screenings, the trusts' knowledge that a large percentage of claims were generated by them, and the involvement of numerous repeat players – including trustees, future claimants representatives, and claim processors – whose roles might suggest a duty to be proactive in derailing these practices, several thousand claims that were "manufactured" through the practices criticized by Judge Jack in the Silica MDL were accepted and paid by asbestos bankruptcy trusts for more than a decade. Only *after* Judge Jack's indictment of these practices did the trusts take steps to blacklist the doctors and screening companies involved. And notwithstanding these blacklists, the available evidence does not suggest that the institutional weaknesses that allowed litigation screenings to drain trust assets over such an extended period of time have been resolved.

2. Defendant Access to Information and Efficiency.

Although defendants may be able to obtain trust claim forms plaintiffs filed prior to the close of discovery, the current discovery-centered model is both inefficient and subject to manipulation. To date, many jurisdictions do not require

[57] Brickman, *supra* note 9, at 128-37 (discussing the Manville Trust audit, mobilization of the plaintiffs' bar against the audit, the resulting litigation and rebuke from the district court). Professor Brickman also suggests that this failure emboldened lawyers and screening companies, and thus contributed to the surge in specious claim filings against bankruptcy trusts in the early part of the last decade. *Id.*, at 135.

plaintiffs to file claims with trusts prior to the close of discovery, which creates opportunities for firms to delay filings and thereby defeat efforts to discover inconsistent factual representations made to trusts. Even if claims have been filed prior to the close of discovery, defendants must either predict where they were filed and submit a subpoena to each trust individually or blanket each trust with a subpoena.[58] After receiving a subpoena, a trust must devote time to determining whether the plaintiff submitted a claim and, in most cases, will then contact the filing firm for instructions.

As one might expect, this approach to discovering relevant bankruptcy trust claim submissions leaves trusts responding to many inquiries concerning claims that have not been submitted. Although the volume of such unnecessary claim inquiries is not publicly disclosed, the GAO Report noted that at least one trust's annual reports include plaintiff names and payments precisely to avoid these costs.[59] Many other trusts, however, take the position that their TDP's – either as a result of terms put in place prior to confirmation of the relevant bankruptcy plan or as part of post-confirmation efforts to thwart discovery – do not allow them to make such disclosures.

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[58] My understanding is that defendants target trust inquiries according to their understanding of the plaintiff's work history, but this approach assumes that there have not been any of the "mistakes" of the sort discovered in *Kananian*.

[59] GAO Report, *supra* note 15, at 25 ("Of the annual reports we reviewed, one trust reported information on the amount paid to each individual and listed these individuals' names. According to officials from this trust, they included individual's names to reduce the number of external requests for claimant payment information and, therefore, reduce the trust's operating expenses associated with addressing such requests.").

As we have seen in asbestos litigation and elsewhere, the expectation of secrecy encourages the rapid development of claim recruiting and development practices that exploit weaknesses in the system. Although we cannot be certain how far the FACT Act might have gone toward deterring or uncovering the claim patterns that depleted trust assets so rapidly through the 1990's and early 2000's, it is clear that, without such requirements, those who were inclined to manipulate the system were largely effective at doing so without significant risk of discovery. Avoiding the modest costs associated with the going forward disclosures required by the FACT Act are, at best, penny-wise but pound-foolish. At worst, rejecting the effort to shine a light on asbestos trust operations may not even be penny-wise.

Conclusion

In 1929, revelations of serious abuses in the administration of bankruptcy cases in the Southern District of New York ultimately led to the investigations that formed the basis for the Donovan Report. Then, as now, supporters of the *status quo* opined that these glimpses of institutional failures were isolated and anecdotal – there was no empirical evidence of widespread corruption, fraud or other abuse across other jurisdictions. Then, as now, it may have been convenient to assume that further inquiry would prove to be a fruitless waste of resources; and the underlying risk was that the inquiry would prove these failures to be pervasive and demand far-reaching change. The risk of preserving the secrecy that prevails today is likewise the same as it was then: the further erosion of the integrity of the bankruptcy process at the expense of absent and less influential stakeholders.

Our predecessors had the courage and resolve to look behind the curtain, and the bankruptcy process has benefited greatly for it. The FACT Act continues this tradition and, if adopted, will reinforce our nation's and this esteemed body's commitment to preserving the integrity of the bankruptcy process.

Thank you again for the invitation to appear today. I hope this summary has been useful, and I am happy to address any questions.