Academy of Court Appointed Neutrals
ANNUAL MEETING

Loews Coronado Bay Resort
San Diego, CA
March 11, 2023
2:45 p.m.

The Existential Threat from Mass Cases – Why It Happens, How to Address It and What's Next to Cure It

PANELISTS:

The Honorable R. David Proctor

Deborah Greenspan, Esq.

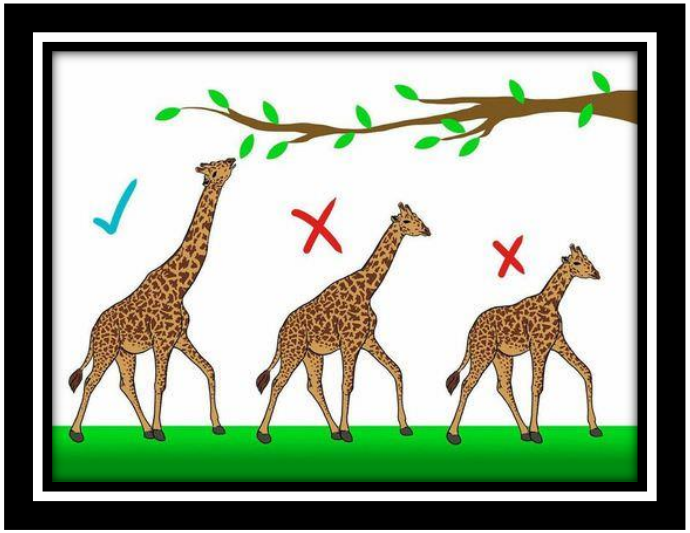
Anne Andrews, Esq.

James L. Patton, Jr., Esq.

Moderator: Ed Gentle

"I will now open the floor to questions. Bye bye!"

A. Why:



The MDL Problem and the Bankruptcy Defendant Panacea

- **Too Many Claims?**
  - MDL 926 (Breast Implant) – Dow Corning, overwhelmed by hundreds of thousands of breast implant claims files for bankruptcy in 1995. Dow Corning said that bankruptcy was the only way it could devise a plan to deal with the billons of dollars of claims against it.
  - J&J Talc MDL – Attempts the Texas two-step. $4.7 billion judgment in favor of 22 Plaintiffs in a 2018 Missouri trial. 20,000 lawsuits.
  - 3M Earplug MDL – Aero, a sub, files for bankruptcy. 230,000+ claims, more than 30% of the total number of all cases pending in Federal Courts and the world record for MDL claims, and twice as many claims as in all other pending MDLs combined
  - Under the MDL system what is the prospect for these Defendants to survive, for the wheat to be separated from the chaff, or for all like claimants to be paid alike?

- **MDL Gate Keeping Problems: Do many cases lack factual support? Can MDLs efficiently separate good from bad cases?**

- **MDL or Bankruptcy Court, who has the best case resolution tools?**

MDL vs Bankruptcy – Which Best Resolves Mass Cases?

Rights or Powers	MDL	Bankruptcy Court
a. Automatic stay	In part	Yes
b. Discovery coordination	Yes	Yes
c. Jurisdiction over related claims	Partial	Yes
d. Separating wheat from chaff and estimation of claims to facilitate resolution	Off-ramps, like dispositive motion practice and threat of remand of bad cases. Early vetting?	Yes
e. Due process concerns	No	Yes
f. Trial by jury preserved	Yes	No/Yes
g. Protect Claimants from each other (Litigation Lottery)	No	Yes

(a) Automatic Stay

(1) **Bankruptcy:** 11 USC §362(a) imposes the automatic stay, halts prepetition litigation against the Debtor and shifts the focus to the Bankruptcy Court.

But, in the related **MDL**, Transferee Judge who originally had the case may continue to preside over litigation against codefendants and the Debtor who have not filed for Bankruptcy, and over fact issues applicable to the Debtor:

Dow Corning Bankruptcy (E.D. MI Feb. 4, 1999): Debtor requested that the MDL Judge "preside over all breast implant and non-breast implant personal injury claims arising out of the reorganization of the Dow Corning Corporation in cases against the shareholders of the Dow Corning Corporation that have been transferred to the Eastern Dist. of Michigan."

(2) **MDL:** a stay of cases for discovery (or Settlement), but often with bellwether trials and eventually sometimes remanding the cases back to their Federal districts. Defendant doesn't escape the claims, but they are deferred for completion of discovery.

Bankruptcy: Court stay results in Plan of Reorganization, under which all claims are paid and the Debtor may survive and emerge from the Bankruptcy shed of the claims.

(b) Discovery Coordination and Other Pre-trial Proceedings

- Available in both Courts, with the MDL Court under 28 U.S. 1407 facilitating discovery and other pre-trial proceedings, and the Bankruptcy Court having §157 to consolidate all related claims for resolution in a single proceeding in a single form, which results in coordinated discovery.

- "The bankruptcy filing itself largely accomplishes this consolidation and coordination with respect to the mass tort claims against the debtor company." Judicial Management of Mass Tort Bankruptcy Cases, p. 17, S. Elizabeth Gibson (Fed. J.C. 2005).

- Bankruptcy Rule 2004, stating that "on motion of any party in interest, the Court may order the examination of any entity," may be used for rapid and liberal discovery. In the Purdue Bankruptcy, it was used successfully to mine millions of pages of documents in a short period of time that may have taken years to produce in a typical MDL setting. The Rule allowed the Parties to get the information much faster than the Federal Rules alone might have done. This Rule may be used to cut through the typical red-tape discovery encountered in MDLs and Bankruptcies alike.

(c) Jurisdiction Over Related Claims

Bankruptcy Court has broad jurisdiction over Federal and State claims under §1334(b), which grants "comprehensive jurisdiction to the Bankruptcy Courts so that they might deal efficiently and expeditiously with all matters connected with the bankruptcy estate." Celotex (U.S., 1995).

The MDL Court may resolve common discovery and pre-trial claims in the Federal System but not in the State Courts, but cannot put all the claims in one bucket.

By contrast, the **Bankruptcy** Court's sweeping ability to resolve claims includes consolidating all claims in one court, precluding collateral litigation in other courts, identifying the universe of existing claims, ensuring appropriate representation of future claims, establishing a Committee of Claimants' Counsel, disallowing invalid claims, litigating objections to claim validity, establishing the criteria to be used in settling claims, creating and funding a trust with criteria and procedures for evaluating and paying valid claims, and enjoining claimants from bringing future claims against the Debtor or its affiliates while channeling all claims to a post-confirmation trust.

Clearly in this context, the **MDL** is the black knight.

(d) Separating Wheat from Chaff and Claims Estimation

Is there anything formal in the **MDL**? Yes, there are off-ramps for bad cases – like dispositive motion practice, remand of bad cases, but no orderly all-inclusive procedure.

The **Bankruptcy** Code provides an orderly and all-inclusive set of procedures for first bringing the asserted claims with a bar date, assessing the validity of the claims and the defenses thereto, and then to the extent claims remain, estimating their value to set a fixed outer limit on the Debtor's potential liability. Code §502, 1129, 157, 558 and 1129.

See Union Bank v. Wolas (U.S. 1991): The primary goals of reorganization under the Bankruptcy Code are to provide "equality of distribution to similar creditors and a collective proceeding while ameliorating the devastating effect that a huge liability may have on the worth of a business and, correspondingly, the compensation available to all victims."

"Unlike an MDL, the Bankruptcy Code can bind all Mass Torts claimants, including claims in State and Federal Court and those held by both current and future claimants." The New Mass Torts Bargain, by Parikh.

(e) Due Process Concerns

Taking together the Supreme Court's decisions in Mullane, AmChem and Ortiz, the "cram down" aspects of Bankruptcy are a potential due process threat, in stark contrast to the MDL, where claims are either resolved or live to fight another day.

However, the Bankruptcy Court seems to have the edge in protecting future claimants, with an established Future Claimants Representative mechanism to satisfy AmChem and Ortiz.

There is an argument that the claims estimation process in Bankruptcy is artificially suppressed due to a debtor friendly forum. Also, there may be claims piling on in Bankruptcy, because bring a claim in Bankruptcy is much easier than in the tort system, which can dilute claims values.

(f) Home Forum Option and Trial by Jury

Yes: **MDL**: Lexecon v. Millberg Weiss (U.S. 1998) – MDL transferee Judge is without authority to try cases that originated in another district without the permission of the Parties.

No: Let the Big Dog Eat – **Bankruptcy**: §157(b) allows the District Court to transfer the related claims to the Bankruptcy Court, where they are resolved.

MDL preserves the trial by jury right hands down.

Bankruptcy: trial by jury only upon consent of the Parties and **only for core proceedings**. Bankruptcy Code §157(e) and Daewoo, 32 B.R. 308, 314 (C.D. Ca. 2003). **BUT**, right to trial by jury can be preserved with good lawyering. For example, the Asbestos Trusts have a right to trial by jury but only after exhausting other remedies.

(g) Protect Claimants from Each Other (Litigation Lottery)

MDL has nothing to do with this, being a way station for discovery or settlement, and not to pay claims.

The **Bankruptcy** inherently does this, with the Bankruptcy Court paying like claimants alike.

B. How (Short of Chapter 11): (1) TEXAS TWO-STEP

- Defendants seeking Bankruptcy shelter from a potentially fatal MDL have designed creative ways to seek Bankruptcy protection without destroying the business by actually taking the Bankruptcy plunge.
- Company reincorporates in Texas and conducts a divisive merger, dividing it into two entities, one assigned the operating assets and the other, usually with less assets, having the assigned liabilities.
- The liability company reincorporates in a favorable jurisdiction like North Carolina and files for Bankruptcy.
- May cap liabilities to what's in the liability company and seeks to shelter operating assets in the operating company.
- Most famous is the Johnson & Johnson Legacy Talc Litigation ("LTL") divisive merger followed by Bankruptcy in North Carolina.
- Judge Michael Kaplan, presiding over the LTL Bankruptcy, contends that the Texas Two-Step did not shelter assets from claimant liability, because J&J has agreed to provide funding up to $60 billion, the estimated value of the claims at the time of Bankruptcy.
- If the Two-Step arrangement provides the same value to the tort claimants, why do it? The answer is the certainty of going forward with the operating company unincumbered by tort liability. Caveat: The piling on problem for claimants.
- **REVERSED By The Third Circuit:** Maybe J&J was too helpful in standing behind the liability of the Liability Company: "J&J's triple A-rated payment obligation for LTL's liabilities…weakened its case to be in bankruptcy."
- **But** "we mean not to discourage lawyers from being innovative."

How (Short of Chapter 11): (2) 3M Attempted Liability / Asset Sharing Approach

- Aearo, which designed the Combat Arms earplug, petitioned in Bankruptcy in July 2022.
- 3M acquired Aearo in April 2008 and acquired the earplug business in 2010. 3M manufactured earplugs from 2010 to 2015, and then stopped. 80% of earplugs sales were before 3M made them.
- In April 2019 700 earplug lawsuits were consolidated in an MDL. Aearo and 3M are co-Defendants in 2,000 lawsuits.
- 3M is the biggest MDL in history. There have been 16 bellwether trials, 12 for Plaintiff and 4 for Defendant with the prevailing trials having awards between $1.7 million and $77.5 million. Negotiation attempts have failed. Trial Lottery.
- Prior to the petition in Bankruptcy, 3M entered into a Funding Agreement with Aearo in which 3M agreed to pay for earplug liabilities on an uncapped basis, with no real repayment obligation of Aearo.
- There are two insurance programs which may cover the plugs, one for $550 million and one for $1.05 billion.
- 3M sought §362(a) stay protection because there is co-liability, 3M and Aearo are co-insured and Aearo is obligated to indemnify 3M for earplug exposure.
- The MDL Court believes that Aearo is a co-Defendant with 3M in name only.
- The Bankruptcy Court found that a stay is not necessary because, ultimately, 3M is fully responsible for all earplug liabilities.
- The Court did note that 3M's actual ability to honor its commitments to pay for all the earplug claims is very much the elephant in the room. One expert, Dr. Heaton, said the 3M exposure is at least $100 billion, exceeding 3M's reserves and taking 3M 17 years to pay. If this is true, 3M, itself, may be insolvent.
- If there is $100 billion of exposure to 3M, the Court agreed that the continuation of actions against 3M would have a significant and disastrous effect on Aearo's bankruptcy.
- Bankruptcy protection of 3M was denied. A close call? It could be this simple: perhaps 3M should have filed a petition in Bankruptcy in Texas, North Carolina or New York, which are much more favorable fora, than in Indiana, where the Court never saw such a case before and the state of the law in the Circuit is much less developed.

(3) Common Issues Combines

Although a transfer under Bankruptcy Code §157 has the benefit of offering finality, it can undermine or delay creditor claims against non-debtors.

- **Sometimes the secret sauce** – Both Dow Corning and Dow Chemical received releases, which allowed the business enterprise to go forward post-petition.
- Non-debtor releases in the Bankruptcy Plan, of affiliates, officers, directors, employees, family members, doctors, hospitals and distributors of Dalkon Shield contraceptive device, A.H. Robins, 131 B.R. 292, 302(E.D.B.a 1991).
- Purdue would release numerous non-debtors. Will be resolved on appeal. A split in the Circuits, the Supreme Court may ultimately decide this case.
- Dow Corning, used §157(b)(5) to transfer to the Bankruptcy Court thousands of claims against non-debtor breast implant manufacturers to resolve threshold scientific issues of whether silicone breast implants caused disease through a "consolidated trial on the issue of causation."

C. Buffering/Curing:

Reform Thyself In the MDL?

- Rigorous MDL **early vetting**, so that only good claims remain. Parties split the cost, but with loser pays if a bad case.
- Separate the Claims vetting function from the individual claimant representation function (have lawyers with no claimants grade the claims).
- Don’t use live grenades so you don’t blow up the bank: bellwether mock trials instead of live trials.
- Have a MDL Future Claimants Representative, who may be adverse to Texas Two-Steps or other Defendant asset protection devices as reducing the pie for future claimants.

D. WHAT NEXT?

(1) Plaintiffs' Perspective: Make Defendant MDL to Bankruptcy Escape Hatches More Difficult?

- To make Texas Two-Step harder, consider allegations against multiple divisions and entities in the Defendant target (may backfire under §362 by allowing affiliates to be sheltered under the stay as being interrelated) .
- Was the Bankruptcy petition valid or only to obtain a tactical litigation advantage? (Bad faith?) May be decided in LTL appeal. It may have been brought in "bad faith," this may "chill" the two-step/3M approaches in the future.
- Pursue two-steps as an "impairment", fraudulent conveyance. Cordlandt Street Recovery, 42 A.D. 2d 837 (N.Y. 2016).
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(2) Possible "Neutral" Alternatives:

- **Let the expert Judge do his job:** In Dow Corning, the original plan was to have Judge Pointer preside over the Bankruptcy claims resolution process.
- **Happy together:** In the early dietary supplement cases (Twin Labs, Metabalife and Hydroxycut), Judge Rakoff oversaw the MDL. When several of the companies filed for bankruptcy he withdrew the reference and sat in tandem with Bankruptcy Judge Drain. There were then parallel proceedings in the MDL and the Bankruptcy, such as Daubert. As a result, this Article 3 Judge and Bankruptcy Judge worked closely together in designing and confirming several joint plans.
- By analogy, Judge Proctor in the Total Body MDL worked in tandem with Judge Wong in the Georgia State Court that had the non-Federal Cases, in designing, approving and implementing a joint settlement.
- MDL to Bankruptcy Prepack. Before making the transition from MDL to Bankruptcy, agree on a claimant payment program, provide adequate notice to all the claimants compiled in the MDL, and have a plan for the Defendant's survival?
- New MDL case resolution teeth statute?
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