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Resolution of Mass Tort Claims Using Bankruptcy in Jeopardy

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In the past ten years, the US bankruptcy courts have been used with increasing frequency to resolve mass tort and sexual abuse liabilities, including cases such as the Catholic Archdioceses of Milwaukee, Stockton and Minneapolis (among others), Boy Scouts of America and USA Gymnastics. Large solvent companies are now attempting to use bankruptcy to resolve products liability and personal injury claims. These cases are stretching the limits of the law, with bankruptcy courts being asked to approve plan settlements that provide broad injunctions barring all claims against the owner in exchange for a contribution to a trust established for creditors. These high-profile cases have led to public criticism and Congressional attention, and that scrutiny has not gone unnoticed by the courts.

Solvent companies are creating subsidiaries to which personal injury claims against the parent company are assigned by way of a Texas "divisional merger," followed by a bankruptcy (colloquially called a "Texas two-step"). In these cases, the subsidiaries propose that existing and future personal injury claims be estimated by the bankruptcy court, that a trust be formed to pay the claims, and that all claims against the parent company be enjoined in exchange for funding the trust. Critics complain that this process bypasses the traditional legal systems for adjudicating personal injury claims, depriving injured parties of "their day in court" and putting claimants (particularly future claimants) at risk that the bankruptcy court's claims estimate is too low and that the trust's assets will be insufficient to pay all claims.

The use of the Texas two-step was pioneered in 2017 in the Bestwall case (a Georgia Pacific subsidiary created to take assignment of its asbestos liabilities), followed in 2019 by DBMP (a CertainTeed subsidiary that was assigned its asbestos liabilities), in 2020 by Aldrich Pump and Murray Boiler (Trane Technologies subsidiaries, again asbestos-related) and most recently LTL, a Johnson & Johnson subsidiary created in 2021 to take assignment of talcum powder-related personal injury claims. Although the bankruptcy courts appear to be receptive to a claims estimation process and an injunction protecting the parent company, these cases are years away from resolution, and their ultimate outcomes (and of any appeals) are uncertain.

Moreover, on August 26, 2022, the bankruptcy court in Aearo Technologies (a 3M subsidiary facing personal injury claims arising from defective combat earplugs) refused to grant an interim injunction preventing thousands of lawsuits against 3M from proceeding even though those claims are proposed to be addressed as part of Aearo's restructuring. Interim injunctions protecting affiliates have been granted in many mass tort bankruptcy cases including LTL, where a federal appeals court is now reviewing the bankruptcy court's interim injunction, so the Aearo case may signal a growing hesitancy to protect solvent parent companies.

No matter the outcome of the LTL appeal and these bankruptcy cases, the use of bankruptcy to protect solvent owners from mass tort claims is under attack. Whether the practice will survive remains to be seen.

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