CLIENT UPDATE

NEWLY AFFIRMED BANKRUPTCY COURT RULING OUTLINES PATH TO BANKRUPTCY DISCHARGE FOR MASS TORT CLAIMS

NEW YORK
Jasmine Ball
jball@debevoise.com

Richard F. Hahn
rfhahn@debevoise.com

M. Natasha Labovitz
nlabovitz@debevoise.com

George E. B. Maguire
gebmaguire@debevoise.com

Maura K. Monaghan
mkmonaghan@debevoise.com

Shannon Rose Selden
srselden@debevoise.com

My Chi To
mcto@debevoise.com

Michael E. Wiles
mewiles@debevoise.com

Craig A. Bruens
cabruens@debevoise.com

Derek P. Alexander
dalexand@debevoise.com

Chapter 11 has long been used by companies to obtain relief from legacy tort liabilities. There has been a lingering question, however, as to whether chapter 11 can bar claims by tort litigants who were exposed to a hazardous material or defective product before bankruptcy but do not develop injuries until after the case is over. Some debtors have set up trusts and appointed representatives for so-called "future claimants": this approach can be effective, but may add months or years to a bankruptcy case along with significant cost, business disruption and litigation. The Southern District of New York recently affirmed a bankruptcy court ruling confirming that there is an alternate path to discharge mass tort claims by relying on a tailored and comprehensive noticing program.

Specifically, in *In re Chemtura Corp.*,[1] District Judge Jesse Furman affirmed a ruling of Judge Robert Gerber of the Bankruptcy Court for the Southern District of New York, which held that a debtor may bar tort claims for injuries from exposure to harmful materials or defective products, even if those injuries had not manifested themselves or been diagnosed as of the claims bar date in the bankruptcy case, so long as (i) the exposure occurred before the debtor filed for bankruptcy protection and (ii) the debtor provided reasonable notice of the bar date to the claimants.

---

[1] *In re Chemtura Corp.*, Case No. 13 Civ. 2023 (JMF) (S.D.N.Y. Feb. 10, 2014); *aff'g* Case No. 09-11233 (REG) (Bankr. S.D.N.Y. Feb. 7, 2013) (ECF No. 5817). Copies of the decisions are at http://www.debevoise.com/publications/dpny-24060102-v1-Chemtura Client Update Attachment.pdf. Debevoise & Plimpton LLP is counsel to Chemtura Corp. in this matter.

BACKGROUND

Chemtura sold synthetic diacetyl, a butter flavoring ingredient, to the food industry between 1982 and 2005. Beginning in 2001, food industry workers, alleging that long-term diacetyl exposure can cause respiratory illness, began filing product liability lawsuits. By the time Chemtura Corp. and a number of its subsidiaries filed voluntary petitions for relief under chapter 11 of the Bankruptcy Code in March 2009, more than fifty diacetyl plaintiffs had brought suit against Chemtura.

Diacetyl was viewed as a potential emerging area for mass tort litigation, so Chemtura took careful steps to ensure that claims for diacetyl exposure (as well as other chemical exposure) would be addressed and discharged in the chapter 11 cases. Chemtura sought and obtained bankruptcy court approval for a heightened bar date noticing program in which Chemtura supplemented publication of standard notices in national newspapers with additional plain-language notices in local newspapers covering more than a hundred locations at which diacetyl was known or alleged to have been used or at which there had been a cluster of diacetyl plaintiffs. A customized notice for each location identified the specific plants at which diacetyl may have been used, described the use of diacetyl in butter flavoring, stated that diacetyl had been alleged to cause injuries and required claims to be filed for injuries then existing or that become apparent in the future. Chemtura's noticing program was the next step in a developing trend; it followed the noticing program that was pioneered in the chapter 11 case of Solutia Inc., used in the chapter 11 case of Tronox Incorporated, and has become the state-of-the-art noticing program for discharge of mass tort liabilities.

Chemtura's bar date noticing program resulted in the filing of hundreds of additional diacetyl claims before the bar date, which were settled in the chapter 11 cases. Claims not filed were discharged upon effectiveness of Chemtura's confirmed plan of reorganization in November 2010. Nearly a year after confirmation, though, nine diacetyl claimants who had not filed claims in the chapter 11 cases filed state court lawsuits against reorganized Chemtura. After the plaintiffs refused to dismiss the lawsuits, Chemtura filed a motion asking the bankruptcy court to enforce the discharge embodied in the chapter 11 plan of reorganization by requiring the plaintiffs to dismiss their lawsuits against Chemtura.

RULING 1: TORT CLAIMS IN BANKRUPTCY ARISE UPON EXPOSURE, NOT KNOWLEDGE

The timing of when a claim arises is important to the treatment of the claim in bankruptcy. Confirmation of a plan of reorganization discharges (that is, blocks pursuit of) claims

against the debtor that arose before confirmation, including prepetition claims, unless otherwise provided. Claims that arise after confirmation are unaffected by the bankruptcy.

A claim is defined broadly in bankruptcy as a "right to payment" whether or not the right is unliquidated, contingent, unmatured or disputed. Judge Gerber followed precedent in the Southern District of New York and applied this broad definition to hold that "claims for injuries resulting from prepetition exposure to products alleged to cause tort injuries are prepetition claims… regardless of when the injury manifests or when the claimant receives a formal diagnosis." This ruling was not challenged on appeal.

RULING 2: DUE PROCESS REQUIRES REASONABLE, BUT NOT ACTUAL, NOTICE TO UNKNOWN CLAIMANTS

Discharge in bankruptcy prevents creditors from pursuing existing claims (which are property rights) against reorganized debtors, so the Due Process Clause of the U.S. Constitution requires that creditors be given appropriate notice and an opportunity to assert their claims in the bankruptcy case. Absent such notice, the discharge will be ineffective. The Supreme Court has long held that notice satisfies due process requirements if it is reasonably calculated under the circumstances to inform the parties concerned and give them an opportunity to object. For unknown parties, "indirect or even probably futile" notice may be sufficient if that "is all that the situation permits."[2]

Applying these principles, courts have followed a fact-specific approach to determine the adequacy of a debtor's bar date notice to discharge claims held by unknown claimants. In some cases, publication of notice in national newspapers may be sufficient. In cases involving mass torts, however, such a limited noticing scheme may fall short. Plaintiffs and their counsel have routinely challenged the discharge of mass-tort litigation claims, arguing that such claims cannot be discharged in the absence of an appointed future claims representative and a trust to provide recovery for late-discovered claims, but had not previously challenged a state-of-the-art noticing program in discharge litigation.

The *Chemtura* decision and its affirmation on appeal arose in the context of just such a challenge. The nine diacetyl plaintiffs argued that Chemtura's bar date notice could not be effective to discharge their claims because the plaintiffs' injuries had not been diagnosed at the time of notice, the plaintiffs did not read the notice or subscribe to the local newspaper in which it was published and no future claims representative was appointed for diacetyl claimants. Judge Gerber ruled that, under the circumstances, the diacetyl claims were

---

2 *Mullane vs. Central Hanover Bank and Trust Company*, 339 U.S. 306, 317 (1950).

discharged even though there was no future claims representative in Chemtura's chapter 11 cases. Judge Gerber found that Chemtura's enhanced noticing program for diacetyl and other tort claimants was "unusually thorough" and therefore was at least "reasonably calculated" to provide notice to unknown claimants. On appeal, District Judge Furman agreed that Chemtura's noticing program satisfied due process requirements and described the "site-specific" tailored notice as the "[m]ost important" factor in his affirmation. Judge Furman also soundly rejected the claimants' argument that a future claims representative was necessary; due process requirements had been met by Chemtura's thorough noticing process.

IMPLICATIONS

Judge Gerber's ruling in *Chemtura*, as affirmed by the District Judge Furman, marks a path in the Southern District of New York for the discharge of tort liabilities in chapter 11 using enhanced noticing schemes without the need to appoint future claims representatives or establish trusts for claims that are discovered post-reorganization.

The particulars of effective noticing will vary according to each case, but a debtor's path to an enforceable discharge against unknown claimants begins with a thorough noticing plan. By leveraging what is known – such as particular products and specific locations – debtors may develop an enhanced plan to provide better notice to potential tort claimants thereby protecting the reorganized debtor by reinforcing the effectiveness of its discharge.

Such discharge is limited, of course, to claims arising before confirmation. The claims of plaintiffs who come into contact with materials or products after confirmation of a plan will generally not be discharged, even if the materials or products were manufactured prepetition. But, as *Chemtura* confirms, prepetition exposure will render a claim for injuries prepetition, and therefore dischargeable, regardless of later diagnosis.

* * *

Please do not hesitate to contact us with any questions.

February 18, 2014