

WEIL'S SCOTUS TERM IN REVIEW

June 6, 2024

Supreme Court Supports Standing for Insurers in Chapter 11 Bankruptcy Cases

By Zack Tripp, Josh Wesneski, and Shai Berman

This morning, the Supreme Court decided *Truck Insurance Exchange v. Kaiser Gypsum Co.*, which clarifies that any party with a “direct financial stake in the outcome” of a reorganization has standing as a “party in interest” to object to a Chapter 11 plan. 11 U.S.C. § 1109(b). Writing for a unanimous Court, Justice Sotomayor held that the debtor’s insurer has standing to object even if the plan purports to preserve the insurer’s legal rights and thus is said to be “insurance neutral.”

Truck is the primary insurer for Kaiser Gypsum, a company that manufactured asbestos-containing products and that had filed for Chapter 11 bankruptcy. Kaiser’s plan proposed to create a personal injury trust to pay individual tort claims, many of which Truck was obligated to insure. The plan included “insurance neutrality” language providing that the plan did not alter Truck’s legal obligations, but Truck sought to object on the ground that the plan lacked adequate protections against the filing of fraudulent claims.

The Fourth Circuit held that Truck was not a “party in interest” in the bankruptcy and therefore lacked standing to object under 11 U.S.C. § 1109(b). The Fourth Circuit reasoned that Truck lacked an interest in the plan because the plan did not alter any of Truck’s pre-existing legal obligations or impair any of its pre-existing legal rights.

The Supreme Court reversed. The Court concluded that a “party in interest” includes any party with a “direct financial stake in the outcome” of a reorganization. This broader interpretation, the Court held, coheres with the purposes of the Bankruptcy Code and the “party in interest” provision, which promote both “greater participation in reorganization proceedings” and a “fair and equitable reorganization process.”

The Supreme Court further held that Truck was a party in interest because it was “[a]n insurer with financial responsibility for bankruptcy claims.” The Court explained that insurers can have a direct financial stake in the outcome of a reorganization because the reorganization can “affect an insurer’s interests in myriad ways,” including by leaving the insurer as the only party with the responsibility to cover many claims. The Court further explained that

the Fourth Circuit's narrower approach, which focused on whether the plan impaired Truck's pre-existing rights or obligations, wrongly conflated the merits of Truck's objection—whether Truck *should be* entitled to the additional protections it sought—with Truck's standing to raise the objection in the first place.

The Supreme Court's decision establishes that "insurance neutrality" language will not deprive an

insurer of standing to object to a bankruptcy plan. By putting an end to that common practice, the Court strengthened insurers' ability to have their rights and interests fully considered in Chapter 11. More broadly, the Court also made clear that statutory standing under Chapter 11 should be understood to reach any party with a financial interest in the overall outcome of a reorganization.

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WEIL'S SCOTUS TERM IN REVIEW

June 28, 2024

Supreme Court Rejects Non-Consensual Third-Party Releases in Chapter 11 Plans

By Zack Tripp, Ronit Berkovich,
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In *Harrington v. Purdue Pharma LP*, in a 5-4 decision, the Supreme Court held that the Bankruptcy Code does not authorize bankruptcy courts to confirm a Chapter 11 bankruptcy plan that discharges creditors' claims against third parties without the consent of the affected claimants. The decision rejects the bankruptcy plan of Purdue Pharma, which had released members of the Sackler family from liability for their role in the opioid crisis. Justice Gorsuch wrote the majority decision. Justice Kavanaugh dissented, joined by Chief Justice Roberts and Justices Kagan and Sotomayor.

Purdue Pharma, which was run by the Sackler family, began marketing OxyContin in the mid-1990s. As Purdue began to face substantial liability relating to its sale of OxyContin, the Sackler family withdrew approximately \$11 billion from the company, driving it into bankruptcy. The case centers on a provision in Purdue's Chapter 11 bankruptcy plan that released the Sackler family from civil liability for any future opioid-related lawsuits. The plan did so even though the Sacklers were not debtors—that is, the Sacklers did not declare bankruptcy. The Sacklers had, however, agreed to contribute approximately \$6 billion dollars to Purdue's bankruptcy estate in exchange for a broad civil-liability release provision. Under the plan, a substantial amount of Purdue's bankruptcy estate would be distributed to more than 100,000 opioid victims, along with Purdue's other creditors. The plan enjoyed substantial support: over 95% of voting creditors approved the plan, as did 50 states, and thousands of other entities such as cities, counties, and hospitals.

The Supreme Court held that the Bankruptcy Code categorically foreclosed this kind of non-consensual third-party release. Writing for the majority, Justice Gorsuch focused on the text of Section 1123(b)(6) of the Code, which provides that a bankruptcy plan may "include any other appropriate provision not inconsistent with the applicable provisions of" the Code. Purdue argued that this subsection broadly permits bankruptcy plans to include "any term not expressly forbidden by the Bankruptcy Code as long as a bankruptcy judge deems it 'appropriate' and consistent with the broad purposes of bankruptcy"—including non-consensual third-party releases. The Court disagreed. It reasoned that the other subsections in Section 1123(b) address the debtor—which indicates that subsection (6) should likewise be construed to address only the debtor, and not

to authorize releases for third parties who are not debtors. The Court emphasized that the Bankruptcy Code provides substantial benefits to debtors—most notably a discharge—but only if they file for bankruptcy and put all of their assets on the table. The Sacklers had not done so, and thus could not effectively obtain a discharge.

In dissent, Justice Kavanaugh wrote that the majority's "decision is wrong on the law and devastating for more than 100,000 opioid victims and their families," who had "overwhelming[ly]" supported the plan. According to the dissent, Section 1123(b)(6)'s use of the broad term "appropriate" should "empower[] a bankruptcy court to exercise its discretion to deal with complex scenarios"; and third-party releases are "often appropriate—indeed are essential—in such circumstances." The Court's narrower construction of Section 1123(b)(6), the dissent warns, "jettisons a carefully circumscribed and critically important tool that bankruptcy courts have long used and continue to need to handle mass tort bankruptcies going forward." The dissent cites examples of other large bankruptcies—such as Dalkon Shield and the Boy Scouts—that utilized third-party releases.

Justice Kavanaugh also emphasized how Purdue's "indemnification agreement covered judgments against the Sacklers and related legal expenses." As a result, a "suit against the non-debtor is, in essence, a suit against the debtor"—as the nondebtor suit can draw down the debtor's estate. According to Justice Kavanaugh, this relationship between Purdue (the debtor) and the Sacklers (the nondebtor) reinforced why a third-party

release was "appropriate" under Section 1123(b)(6) in the specific context of this case.

The Court's decision brings certainty to bankruptcy law by resolving a major question that had divided the circuit courts of appeals and the lower courts: whether courts can issue non-consensual third-party releases outside the narrow context of asbestos cases, where Congress has expressly allowed such relief. The answer is no, courts cannot enter such releases.

The broader impact of this decision on bankruptcies going forward, particularly those precipitated by mass tort claims, remains to be seen. The decision should not impact the ability of third parties to settle and receive the benefit of obtaining so-called "debtor releases"—releases of claims held by the debtor against such parties. These typically include claims such as fraudulent transfer, breach of fiduciary duties, and veil piercing. In addition, section 524(g) of the Bankruptcy Code continues to permit non-consensual third party releases in asbestos cases. For non-asbestos cases, third parties seeking broad releases can still use the Chapter 11 process as a settlement mechanism, but will have to allow individual creditors to opt out of any release of direct (non-debtor) claims individual creditors may hold. Or they will have to file Chapter 11 themselves to obtain the benefit of the discharge. In all events, the Purdue bankruptcy plan will now be remanded and the parties will now have the opportunity to craft a new plan in light of the Court's decision.

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