SACKLER IMMUNITY: PROBLEMS SURROUNDING NONDEBTOR RELEASES IN CHAPTER 11 BANKRUPTCY

GARNER VANCE*

ABSTRACT

When bankruptcy courts grant nondebtor, or third-party releases, they release from liability individuals and business entities that are not a party to the bankruptcy proceeding, but that are otherwise connected to the bankruptcy in some way. For example, these third-parties are often solvent executives of the company in bankruptcy that are facing large amounts of individual liability themselves. Since the practice expanded beyond its initial purpose of resolving asbestos liabilities in the 1980s, courts and legal scholars have often questioned the constitutional and statutory validity of nondebtor releases in chapter 11 reorganizations. Until recently, debates about the validity of nondebtor releases were mostly contained within legal circles, as the issue had not garnered significant attention from the press and general public. Now, with Purdue Pharma and other high-profile companies in bankruptcy seeking questionable releases for third-parties through their chapter 11 plans, the media has amplified the issue, leading many to challenge the prospective liability releases for nondebtors like members of the Sackler family.

This Article first analyzes the constitutional, statutory, and due process issues surrounding nondebtor releases in chapter 11 bankruptcies. It then focuses on the nondebtor release issue in the context of mass tort cases and proffers that, among implementing other substantive and procedural safeguards, bankruptcy courts should consider a nondebtor's willful misconduct when determining what should be required for the court to grant that nondebtor relief. Lastly, this Article discusses proposed legislation to eliminate the practice entirely and argues that other less severe solutions are more appropriate for curbing the abuse of the system being carried out by solvent nondebtors. This Article aims to contribute ideas that will increase the fairness and transparency of mass tort bankruptcy

* J.D. Candidate 2023, University of Mississippi School of Law; B.S. in Chemical Engineering 2017, University of Mississippi. He serves as Executive Articles Editor for Volume 92 of the *Mississippi Law Journal* and as Vice Chair of the University of Mississippi Moot Court Board. The author would like to thank his friends and colleagues at the *Mississippi Law Journal* and the University of Mississippi School of Law, and Professors Matthew R. Hall and Judge Neil P. Olack for their time, support, and helpful comments.

cases. Hopefully, if the system can be improved, the added efficiency of allowing bankruptcy courts to resolve third-party liability issues can be equitably retained.

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INTRODUCTION

The opioid crisis has caused great harm to the United States. The widespread addiction, overdose, and ravaging of entire communities across the country originated from the over prescription and false advertisement of opioid pain medications. Since 1999, more than 900,000 people have died from drug overdose, and in 2020 alone, close to 70,000 people died from opioid overdose.[1] Furthermore, the economic burden of prescription opioid misuse in the U.S. is estimated to be between $53-72 billion a year.[2] While several companies were involved in the manufacturing and marketing of opioids, Purdue Pharma's OxyContin product was amongst the most powerful and popular. During this time, Purdue was a closely held company owned by various members of the wealthy Sackler family.[3] The Sacklers were directly involved in Purdue's management as officers and directors, so much so that the Department of Justice labelled the Sacklers as Purdue's "de facto CEO."[4] As the opioid crisis garnered attention around the country, a wave of litigation began against opioid manufacturers for their role in misrepresenting the addictive nature of opioids and incentivizing doctors to oveSrprescribe the medications. By 2019, Purdue Pharma faced more than 2,600 civil actions brought by both private individuals and state and local governments.[5] Several lawsuits were also brought against the Sacklers, who became extraordinarily rich from Purdue's opioid business.[6] The family collected more than $10 billion in distributions and other payments from Purdue, including payments made after members of the family were well aware of their potential exposure to liability from Oxycontin.[7] In response to the tidal wave of litigation, Purdue filed chapter 11 bankruptcy in September 2019.[8] After two years of

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[1] *See* Ctrs. for Disease Control & Prevention, *The Drug Overdose Epidemic: Behind the Numbers*, DATA OVERVIEW, https://www.cdc.gov/opioids/data/index.html (June 1, 2022).

[2] U.S. Dep't of Health & Hum. Servs., Addressing Prescription Drug Abuse in the United States, *Current Activities and Future Opportunities*, 10, httpps.//www.cdc.gov/drugoverdose/pdf/hhs_ prescription_drug_abuse_report_09.2013.pdf (last visited Nov. 15, 2022).

[3] *See In re* Purdue Pharma L.P., No. 21-7532, at *11 (S.D.N.Y. Dec. 16, 2021).

[4] Brian Mann, *Critics Want Sacklers to Face Criminal Charges for Role in Opioid Crisis*, NPR, (Nov. 25, 2020, 3:05 PM), https://www.npr.org/2020/11/25/938801514/critics-want-sacklers-to-face-criminal-charges-for-role-in-opioid-crisis. *See also In re* Purdue Pharma L.P., No. 21-7532, at *28 ("This evidence [from the 2007 settlement] demonstrated that members of the Sackler family were heavily involved in decisions on how to market and sell opioids [].").

[5] Adam J. Levitin, *Purdue's Poison Pill: The Breakdown of Chapter 11's Checks and Balances*, 100 TEX. L. REV. 1079, 1104 (2022).

[6] *See In re* Purdue Pharma L.P., No. 21-7532, at *10 ("Purdue generated approximately $34 billion in revenue total between 1996-2019, most of which came from OxyContin sales []; prior to bankruptcy, OxyContin accounted for some 91% of Purdue's U.S. revenue[].").

[7] *Id.* at *4.

[8] *Id.* at *2

negotiations and plan amendments, a New York bankruptcy court confirmed Purdue's reorganization plan.[9] However, the Sackler family members' fates remain in question, as Judge Colleen McMahon of the U.S. District Court for the Southern District of New York recently vacated the bankruptcy court's confirmation order.[10]

Prior to the district court vacating the order, the confirmation of the plan seemed to be a sweet deal for the Sacklers. In return for a $4.325 billion contribution to the settlement fund over nine years, the Sacklers would receive complete immunity from all past, present, and future opioid related civil claims.[11] The releases are controversial, as not a single member of the Sackler family has filed for bankruptcy. There are obvious societal risks associated with people making and retaining billions of dollars from knowingly and fraudulently mass marketing a harmful product while victims are left without recourse due to the confirmation of a separate entity's chapter 11 bankruptcy plan. Bankruptcy is meant to be a collective remedy that mitigates the problems and conflicts that arise when debtors and creditors are free to act solely in their own interest. However, for this to work, the bankruptcy system must operate in a manner that does not confer advantages to one party over others. Without such a system, history shows that this delicate relationship between debtor and creditor bears the potential to divide society into different ranks and classes and damage the societal cohesion amongst the people of a nation.[12]

> ("Purdue's bankruptcy was occasioned by a health crisis that was, in significant part, of its own making: an explosion of opioid addiction in the United States over the past two decades, which can be traced largely to the over-prescription of highly addictive medications, including, specifically and principally, Purdue's proprietary, OxyContin.").

9 *In re* Purdue Pharma L.P., No. 19-23649, 2021 WL 4240974 (Bankr. S.D.N.Y. Sept. 17, 2021), *vacated*, No. 21-7532 (S.D.N.Y. Dec. 16, 2021).

10 *In re* Purdue Pharma L.P., No. 21-7532, at *7 ("This opinion will not be the last word on the subject, nor should it be.").

11 *See id.* at *5, *52.

12 Daniel Webster eloquently described the state of a new American nation prior to the ratification of the Constitution and the passage of uniform bankruptcy laws. *See* Ogden v. Saunders, 25 U.S. 213, 247 (1827)

> ("The relation between debtor and creditor, always delicate, and always dangerous whenever it divides society, and draws out the respective parties into different ranks and classes, was in such a condition in the years 1787, '88, and '89, as to threaten the overthrow of all government; and a revolution was menaced, much more critical and alarming than that through which the country had recently passed. The object of the new constitution was to arrest these evils; to awaken industry by giving security to property; to establish confidence, credit, and commerce, by salutary laws, to be enforced by the power of the whole community.").

The Sackler releases are "nondebtor" or "third-party" releases, and they are among the most controversial issues in chapter 11 bankruptcy. This Article proffers that this relief mechanism for third parties to bankruptcy proceedings has increasingly led to abuse of the system and a less equitable chapter 11 bankruptcy process. Part I of this Article provides the statutory framework used by bankruptcy courts to grant these releases and describes the origin of nondebtor releases in asbestos litigation. Part II then analyzes the extension of nondebtor releases to cases outside of asbestos and discusses the constitutional questions, different statutory interpretations, and due process concerns surrounding the issue.

Next, Part III of this Article examines a past overreach of the bankruptcy court's equitable power under § 105(a) and poses the question of whether nondebtor releases are another overreach of that power. Further, it analyzes whether the Supreme Court has effectively resolved the debate over the statutory power to grant nondebtor releases.

Part IV of this Article delves deeper into nondebtor releases in the context of mass tort bankruptcies and discusses the channeling injunction, a common mechanism used to effectuate nondebtor releases in mass tort bankruptcies. Next, it proposes that bankruptcy courts consider a nondebtor's willful misconduct when that nondebtor seeks release from liability through the bankruptcy court's confirmation of a chapter 11 plan. Lastly, it explores potential perverse incentives created by the prospect of liability releases for solvent nondebtors and provides examples of parties seizing upon these incentivized opportunities at the expense of claimants.

Finally, Part V of this Article discusses proposed solutions to the issues surrounding nondebtor releases. It analyzes proposed legislation to prohibit nonconsensual, nondebtor releases in chapter 11 and compares alternative solutions proposed by scholars that offer both substantive and procedural checks on the chapter 11 process.

The issues associated with nondebtor releases are complex, and each case presents both positive and negative implications to granting these releases. This Article argues that because the system has increasingly produced inequitable results, we should prioritize a solution to the problem that increases transparency and consistently produces better outcomes for claimants.

I. BACKGROUND

A. Nondebtor Releases in Chapter 11

Chapter 11 of the Bankruptcy Code enables business entities to reorganize their finances and operations and continue operating while paying creditors over time.[13] A reorganization plan is a "highly negotiated, multiparty contract between the debtor and its body of creditors."[14] Sometimes, a debtor may need nondebtor, third-party entities to assist in effectuating its reorganization.[15] Often, these nondebtors are either insiders of the debtor, like directors and officers, or entities directly affected by the reorganization, such as the debtor's insurers or major plan contributors.[16] Because these nondebtors are often solvent and are not subject to the same requirements as the debtor, they can have significant leverage over other parties in chapter 11 negotiations.[17] As the American Bankruptcy Institute ("ABI") explains, nondebtors "may be reluctant to contribute to the plan" if they are potentially "exposed to liability or will have ongoing liability despite the confirmation of the Chapter 11 plan."[18] Nondebtors hope that if they contribute enough to the plan either claimants will consensually grant them release or the bankruptcy court will find their release necessary to the reorganization even over the objection of some creditors. Not all bankruptcy courts find these releases appropriate under the Code, and courts that do find them appropriate consider a variety of factors in determining the appropriateness of any third-party release at hand.[19] The following sections discuss the statutory power governing nondebtor releases and describe the origin of nondebtor releases in asbestos litigation.

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13 Dorothy Coco, *Third-Party Bankruptcy Releases: An Analysis of Consent Through the Lenses of Due Process and Contract Law*, 88 FORDHAM L. REV., 231, 234 (2019).
14 *Id.*
15 *See* AM. BANKR. INST. COMM'N TO STUDY THE REFORM OF CHAPTER 11, 2012-2014 FINAL REPORT AND RECOMMENDATIONS (2014) ("This assistance may be in the form of service, collaboration, funding, business commitments, or other means that allow the debtor to achieve its objectives in the Chapter 11 case or in its post confirmation operations."); Coco, *supra* note 14, at 235 ("Debtors often utilize third-party releases to incentivize parties to support a plan or to influence others to contribute to and fund the plan.").
16 Coco, *supra* note 13, at 235.
17 *See, e.g.*, discussion *infra* Section V.B.1 (describing disclosure requirements imposed on debtors but not imposed on nondebtors seeking relief through the chapter 11 process).
18 AM. BANKR. INST., *supra* note 15, at 255.
19 *See infra* notes 75-81 and accompanying text.

B. Statutory Power Governing Nondebtor Releases

For a bankruptcy court to approve a chapter 11 plan, the plan must comply with the entire Bankruptcy Code.[20] The plan may include any provision not inconsistent with the Code.[21] Additionally, at least one impaired class of creditors must accept the plan.[22] The Code deems a class of creditors impaired if the proposed plan changes the legal, equitable, and contractual rights of the claimants within the class.[23] When the bankruptcy court confirms the plan, it binds all parties related to the bankruptcy, including objectors to the plan.[24] From this arises the distinction between consensual and nonconsensual nondebtor releases, a distinction that may determine the fate of the release.[25]

Scholars have long debated whether nondebtor releases comply with the powers bestowed on bankruptcy courts by the Code.[26] The debate stems from different interpretations of Sections 524(e) and 105(a). § 524(e) states that the "discharge of a debt of the debtor does not affect the liability of any other entity."[27] § 105(a) grants bankruptcy courts broad equitable power to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."[28]

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[20] 11 U.S.C. § 1129(a)(1) ("The court shall confirm a plan only if . . . [t]he plan complies with the applicable provisions of this title.").

[21] 11 U.S.C § 1123(b)(6).

[22] 11 U.S.C § 1129(a)(10).

[23] 11 U.S.C § 1124(1).

[24] *See* Coco, *supra* note 13, at 236 ("Once a plan is confirmed, the plan and all of its provisions bind the debtor, creditors, and any other related entities that benefit or are connected to the plan, regardless of impairment status or whether the entity had voted to accept or reject the plan.").

[25] *See infra* Section II.B (describing differences amongst the circuits in considering the permissibility of third-party releases); *See also infra* notes 90-93 and accompanying text (discussing varying approaches to analyzing creditor consent).

[26] *Compare* Ralph E. Brubaker, *Bankr. Injunctions & Complex Litigation: A Critical Reappraisal of Non-debtor Releases in Chapter 11 Reorganizations*, 1997 U. ILL. L. REV. 959 (1997) (arguing non-debtor releases do not fall under bankruptcy courts' injunctive powers), *and* Peter M. Boyle, *Nondebtor Liability in Chapter 11: Validity of Third-Party Discharge in Bankr.*, 61 FORDHAM L. REV 421 (1992) (arguing § 524(e) precludes the discharge of a debtor from affecting the liability of non-debtors and concluding that a discharge is only available to parties who have filed for bankruptcy), *with* Joshua M. Silverstein, *Hiding in Plain View: A Neglected Sup. Ct. Decision Resolves the Debate Over Nondebtor Releases in Chapter 11 Reorganizations*, 23 EMORY BANKR. DEVS. J. 13 (2004) (arguing Supreme Court precedent settles the debate in favor of the pro-release view), *and* Howard C. Buschman III & Sean P. Madden, *The Power & Propriety of Bankr. Ct. Intervention in Actions Between Non-debtors*, 47 BUS. LAW. 913 (1992) (arguing that because § 524(e) does not expressly bar permanent non-debtor releases, they are appropriate in some instances).

[27] 11 U.S.C. § 524(e).

[28] 11 U.S.C. § 105(a).

C. Origins in Asbestos

The origin of nondebtor releases traces back to the mass tort litigation that arose from the asbestos crisis. The onslaught of lawsuits eventually forced several firms in the asbestos industry to file bankruptcy.[29] Johns-Manville Corporation, a leading producer of asbestos, was one of those businesses.[30] Not only did the company have to think about current liabilities, but it also worried about future liabilities that might arise from injuries that manifest later.[31] As a result, the company's reorganization plan represented the first use of channeling injunctions and nondebtor releases in chapter 11.[32] The plan created litigation trusts to pay claims and effectuated a channeling injunction that required all claims to be settled against the trust rather than against the corporation or its plan contributors.[33] In effect, the channeling injunction prevented claimants from "going after the company, its subsidiaries, or its insurance carriers."[34] Therefore, the injunction effectively released nondebtor insurance companies from any asbestos-related liability.[35] After appeal, the Second Circuit confirmed the plan.[36] The court reasoned that "the Plan [sought] to ensure that health claims can be asserted only against the Trust and that Manville's operating entities will be protected from an onslaught of crippling lawsuits that could jeopardize the entire reorganization effort."[37] Congress expressed a positive view of the strategy when it amended the Code in 1994 to approve the use of channeling injunctions and nondebtor releases for insurance companies involved in asbestos litigation so long as the plan met specific requirements.[38]

Congress and the courts seemingly presume that bankruptcy courts have the constitutional authority to grant nondebtor releases. As discussed below, the Third Circuit recently wrestled with that question.[39] Furthermore, the Code does not explicitly authorize nondebtor releases outside of asbestos cases. This lack of explicit authorization creates circuit splits on whether bankruptcy courts have the statutory power to grant nondebtor releases outside of asbestos cases.[40]

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29 *See* Lindsey D. Simon, *Bankr. Grifters*, 131 YALE L.J. 1154, 1172 (2022).
30 *Id*.
31 *Id.*
32 *Id.*
33 *In re* Matter of Johns-Manville Corp., 68 B.R. 618, 621 (Bankr. S.D.N.Y. 1986).
34 Simon, *supra* note 29, at 15.
35 *See Matter of Johns-Manville Corp*., 68 B.R. at 624 ("The actions prohibited by this Injunction include: commencing, enforcing, perfecting, or setting-off any proceeding, judgment or interest against the Debtor or its subsidiaries or any settling insurance company[.]").
36 Kane v. Johns-Manville Corp., 843 F.2d 636 (2d Cir. 1988).
37 *Id.* at 640.
38 11 U.S.C. § 524(g).
39 *See infra* Section II.A.2.
40 *See* discussion *infra* Section II.B.

II. NONDEBTOR RELEASES OUTSIDE OF ASBESTOS

A. Constitutional Authority

Article III of the Constitution states, "The judicial Power of the United States, shall be vested in one Supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish."[41] Article III courts, such as the Supreme Court and Federal Courts of Appeal, are characterized by the ability to adjudicate any case or controversy so long as the court has appropriate subject matter and personal jurisdiction.[42] Further, Article III courts are comprised of judges with lifetime tenures.[43] On the other hand, bankruptcy courts are Article I courts created through Congress's power "[t]o establish … uniform Laws on the subject of Bankruptcies throughout the United States."[44] This distinction is critical; Article I courts, like the bankruptcy courts, lack the broad subject matter jurisdiction of Article III courts.[45] Bankruptcy courts may only adjudicate cases under Title 11 and core proceedings arising under Title 11 or arising in a case under Title 11.[46] They also may submit proposed findings of fact and conclusions of law to the district court in non-core proceedings otherwise related to a case under Title 11.[47]

1. Stern v. Marshall

The Supreme Court's seminal decision in *Stern v. Marshall* illustrates the limited jurisdiction of bankruptcy courts.[48] In that case, the Court held that "[t]he Bankruptcy Court below lacked the constitutional authority to enter a final judgment on a state law counterclaim that is not resolved in the process of ruling on a creditor's proof of claim."[49] In other words, the bankruptcy court had statutory

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41 U.S. CONST. art. III, § 1.

42 While litigating parties may waive personal jurisdiction, they cannot waive subject matter jurisdiction. The two primary sources of subject matter jurisdiction are diversity jurisdiction, 28 U.S.C. § 1332, and federal question jurisdiction, 28 U.S.C. § 1331.

43 *See* U.S. CONST. art. III, § 1 ("The Judges, both of the supreme and inferior Courts, shall hold their Offices during good behaviour. . . .).

44 U.S. CONST. art. I, § 8, cl. 4.

45 Federal district courts have original, but not exclusive, jurisdiction over bankruptcy matters, 28 U.S.C. § 1334(b). However, district courts "may provide that any or all cases under title 11 and any or all proceedings arising under title 11 shall be referred to the bankruptcy judges for the district." 28 U.S.C. § 157(a).

46 *See 28* U.S.C § 157(b).

47 *See* 28 U.S.C §157(b)(1) and 28 U.S.C §157 (c)(1). *But cf.* 28 U.S.C §157(b)(5) ("The district court shall order that personal injury tort and wrongful death claims shall be tried in the district court in which the bankruptcy case is pending.").

48 Stern v. Marshall, 564 U.S. 462 (2011).

49 *Id.* at 503.

authority to rule on the counterclaim because the counterclaim was technically a core proceeding; the bankruptcy court's exercise of that statutory authority in this instance, however, was unconstitutional.[50] Justice Rehnquist, writing for the majority, explained that "[w]hen a suit is made of the stuff of transactional actions at common law … and is brought within the bounds of federal jurisdiction, the responsibility for deciding that suit rests with Article III judges in Article III courts."[51] Therefore, the Court held that the lower bankruptcy court exceeded its constitutional limits when it "exercised the 'judicial Power of the United States' in purporting to resolve and enter final judgment on a state common law claim[.]"[52] Additionally the Court insinuated that the test for whether a bankruptcy court has the constitutional authority to hear and determine a proceeding is whether that proceeding is integral to restructuring the debtor-creditor relationship.[53]

2. In re Millenium Lab Holdings II, LLC

Stern reappeared recently in the Third Circuit case *In re Millennium Lab Holdings II, LLC*.[54] The Third Circuit held that bankruptcy courts have the constitutional authority to confirm a chapter 11 plan containing nonconsensual, nondebtor releases when such releases are integral to the debtor's successful reorganization.[55] The court drew three crucial points from *Stern* to guide their analysis. First, even when bankruptcy courts act in a designated core proceeding category, they still may violate Article III of the Constitution and exceed constitutional authority.[56] Second, a bankruptcy court does not act unconstitutionally when it resolves matters "integral to the restructuring of the debtor-creditor relationship."[57] Specifically, the Court in *Stern* held that bankruptcy courts had authority to decide matters stemming from the bankruptcy itself or that would necessarily be resolved in the claims allowance process.[58] Lastly, the Third Circuit interpreted *Stern* to dictate that bankruptcy courts focus

50 *See id.* at 463.
51 *Id.* at 484.
52 *Id.* at 487.
53 *See id.* at 497 ("[A] preferential transfer claim can be heard in bankruptcy when the allegedly favored creditor has filed a claim, because *then* 'the ensuing preference action by the trustee become[s] integral to the restructuring of the debtor-creditor relationship.'") (quoting *Lagenkamp v. Culp*, 498 U.S. 42, 44 (1990)).
54 *In re* Millenium Lab Holdings II, 945 F.3d 126 (3d Cir. 2019).
55 *Id.* at 133.
56 *Id.* at 135.
57 *Id.*
58 *See Stern*, 564 U.S. at 499 ("Congress may not bypass Article III simply because a proceeding may have *some* bearing on a bankruptcy case; the question is whether the action at issue stems from the bankruptcy itself or would necessarily be resolved in the claims allowance process.").

on the content of the proceedings rather than on the category of core proceedings at issue.[59]

Applying these principles from *Stern* to the facts in *In re Millenium Lab Holdings II, LLC*, the Third Circuit affirmed the confirmation of Millennium's chapter 11 plan.[60] The confirmation resulted in the release of various nondebtor entities, including Millennium's former shareholders, who faced fraud claims, affirming the bankruptcy court's view that the releases were critical to the plan's success.[61] The opposing creditor, Voya Alternative Asset Management LLC ("Voya"), argued that the centrality of the releases to the plan was irrelevant because their fraud claims against the shareholders neither stemmed from bankruptcy, nor would they be resolved in the claims allowance process. Therefore, Voya argued that the bankruptcy court's confirmation of the releases was unconstitutional under *Stern*.[62] The Third Circuit rejected such a narrow view of *Stern*, explaining that *Stern's* "integral to the restructuring" language was not limited to the claims allowance process.[63] The court reasoned that had the *Stern* court meant this language to be limited to the claims-allowance process, "it would not have said that a bankruptcy court may decide a matter when a 'creditor has filed a claim, because *then*' - adding its own emphasis to the word - 'the ensuing preference action . . . become[s] integral to the restructuring of the debtor-creditor relationship.'"[64]

The court believed that this phrasing clearly showed that bankruptcy courts may rule on matters arising in the claims-allowance process because "those matters are integral to the restructuring of debtor-creditor relations, not the other way around."[65] Voya argued that an "integral to the restructuring" rule could allow bankruptcy courts to approve releases simply because nondebtor plan contributors demand them, which may result in manipulation and abuse of the process by nondebtors.[66] The Sackler family's manipulation of the *Purdue* bankruptcy seems to validate Voya's concern.[67]

Third Circuit chapter 11 opinions, which include appeals from Delaware, certainly carry significant weight in the bankruptcy world. However, the Supreme Court has yet to address the issue. Given the publicity surrounding *Purdue* and

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59 *See In re Millennium Lab Holdings II, LLC*, 945 F.3d at 136.

60 *Id.* at 140.

61 *See id.* at 137 ("Restructuring in this case was possible only because of the release provisions.").

62 *See id.* at 137-38.

63 *See id.* at 138.

64 *Id.*

65 *Id.*

66 *See id.* at 139. The court rejected this argument, stating, "Setting too low a bar for the exercise of bankruptcy court authority could seriously undermine Article III, which is fundamental to our constitutional design."

67 *See In re* Purdue Pharma L.P., No. 19-23649, 2021 WL 4240974 at *47 (Bankr. S.D.N.Y. 2021 Sept. 17, 2021), *vacated*, No. 21-7532 (S.D.N.Y. Dec. 16, 2021).

other high-profile bankruptcies seeking third-party releases, it seems likely that the question will not remain unanswered much longer.

B. Different Statutory Interpretations

In analyzing the statutory question of nondebtor releases outside of asbestos, a tug-of-war arises between §§ 524(e) and 105(a) of the Code. On one hand, courts that favor a restrictive view of § 105(a)'s equitable powers point to the court's lack of power to modify relationships other than the one between debtor and creditors.[68] Further, these courts find § 524(e) dispositive on the matter. A plan of reorganization that purports to discharge a nondebtor necessarily affects the liability of another entity; therefore, the plan directly violates § 524(e). The Fifth Circuit explained this view of the Code in *In re Zale Corp.*: "Although we interpret § 105 liberally, a § 105 injunction must be consistent with the rest of the Bankruptcy Code" and § 524 "prohibits the discharge of debts of nondebtors"; therefore, "we must overturn a § 105 injunction if it effectively discharges a nondebtor."[69]

On the other hand, courts that prefer a more expansive view of § 105(a)'s equitable powers opine that because the plain language of § 524(e) does not in itself preclude nondebtor releases, they are permissible under the Code. These courts interpret § 524(e) to merely *explain* the effect of a debtor's discharge on the liability of other entities; therefore, they find the Code silent on the permissibility of nondebtor releases. Because they find the Code silent on nondebtor releases outside of asbestos, they find these releases not inconsistent with the Code and permissible under the court's equitable powers. The Sixth Circuit illustrated this view in *In re Dow Corning Corp.*, "§ 1123(b)(6) permits a reorganization plan to 'include any provision not inconsistent with the applicable provisions of this title'[,] and "this language [in § 524(e)] explains the effect of a debtor's discharge. It does not prohibit the release of a nondebtor."[70]

While these courts find nondebtor releases statutorily permissible, other factors discussed below are at play when courts consider granting a nondebtor release.[71]

Currently, circuits are split on the statutory permissibility of nondebtor releases due to the interpretation issues mentioned above and other considerations discussed below.[72] The distinction between consensual and nonconsensual releases

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68 Boyle, *supra* note 26, at 427.
69 Feld v. Zale Corp., 62 F.3d 746, 760 (5th Cir. 1995).
70 *In re* Dow Corning Corp. 280 F.3d 648, 657 (6th Cir. 2002).
71 *See infra* notes 75-80 and accompanying text.
72 In her order vacating the confirmation of Purdue Pharma's chapter 11 plan, Judge McMahon made a plea for the split to be resolved. *See In re Purdue Pharma.*, 635 B.R. at 37 (S.D.N.Y. 2021) ("The great unsettled question in this case is whether the Bankruptcy Court - or any court - is

usually plays a large role in the analysis. Consensual, or voluntary, releases are ones that a creditor has consented to in one way or another.[73] Nonconsensual, or involuntary releases, force objecting parties to release a nondebtor without consent.[74]

The majority of circuit courts hold that consensual nondebtor releases are appropriate if certain factors are present while nonconsensual releases should only be granted in rare circumstances.[75] The ABI agrees with the majority view and recommends that courts apply the factors from *In re Master Mortgage Investment Fund, Inc.*[76] in deciding the question of nondebtor releases.[77] The *Master Mortgage* factors to consider are:

> (1) the identity of interest between the debtor and the third party, usually an indemnity relationship, such that a suit against the nondebtor is, in essence, a suit against the debtor or will deplete assets of the estate; (2) whether the nondebtor has contributed substantial assets to the reorganization; (3) whether the injunction is essential to reorganization; (4) whether a substantial majority of the creditors agree to such injunction--specifically, whether the impacted class or classes have overwhelmingly voted to accept the proposed plan treatment; and (5) whether the plan provides a mechanism for the payment of all, or substantially all, of the claims of the class or classes affected by the injunction.[78]

None of the factors are dispositive, but they do provide courts with a framework for analysis. Some courts also require the nondebtor release to be narrowly tailored and not constitute blanket immunity.[79]

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statutorily authorized to grant such releases. This issue has split the federal Circuits for decades . . . This will no longer do. Either statutory authority exists or it does not.”).

73 Coco, *supra* note 13, at 239.

74 Brad B. Erens, *Second and Seventh Circuits Issue Decisions on Third-Party Releases*, JONES DAY: INSIGHTS (May/June 2008), https://www.jonesday.com/en/insights/2008/06/second-and-seventh-circuits-issue-decisions-on-third-party-releases#%20[perma.cc/8AU9-JCMX.

75 The circuits comprising the majority include the Second, Third, Fourth, Sixth, Seventh, and Eleventh. Coco, *supra* note 13, at 240. *But see In re* Aegean Marine Petroleum Network Inc., 599 B.R. 717, 726 (S.D.N.Y. 2019). (“Unfortunately, in actual practice the parties … often seek to impose involuntary releases based solely on the contention that anybody who makes a contribution to the case has earned a third-party release. Almost every proposed Chapter 11 Plan that I receive includes proposed releases.”).

76 *In re* Master Mortg. Inv. Fund, Inc., 168 B.R. 930 (Bankr. W.D. Mo. 1994).

77 AM. BANKR. INST, *supra* note 15, at 256.

78 *In re Master Mortg. Inv. Fund, Inc.*, 168 B.R. at 937-38.

79 The Seventh Circuit follows the majority’s view of the issue, but with a twist: nondebtor releases are acceptable where appropriate or necessary and the distinction between consensual and nonconsensual releases is irrelevant to the analysis. *See In re* Airadigm Commc’ns, Inc., 519 F.3d 640, 657 (7th Cir. 2008) (explaining that determining appropriateness is fact intensive, case specific,

The minority of circuit courts take the view that it is not necessary to even reach a factor-based analysis on the question of consensual or nonconsensual nondebtor releases.[80] This is because these courts hold that § 524(e) prohibits nondebtor releases.[81]

C. Due Process Concerns

Nonconsensual, nondebtor releases raise Due Process concerns because they involve the nonconsensual deprivation of nonconsenting creditor's property – their claims against the nondebtor. Thus, the due process issue centers around what constitutes consent and how creditor's consent must be obtained.[82]

Currently, if a debtor's proposed plan includes an injunction against conduct not otherwise enjoined under the Code, the Federal Rules of Bankruptcy Procedure requires the plan to describe in "specific and conspicuous language" the acts to be enjoined and the identity of the entities subject to the injunction.[83] Further, the debtor must provide a notice to the parties in interest of the bankruptcy that includes a conspicuous statement that the plan proposes an injunction. That statement must describe the nature of the injunction and identify the entities subject to the injunction.[84] Provided that the debtor gives proper notice, creditors then vote to approve or object to the plan. While some creditors may consent to the plan, others may object. Under normal contract law principles, nonconsenting creditors would not be bound by the terms of this contract, as their consent was not clearly expressed or manifested by conduct.[85] However, in chapter 11 bankruptcies, all parties, including nonconsenting creditors, are bound to the plan through the bankruptcy court's confirmation of the plan.[86] According to the Code, a class of claims accepts a plan if creditors who hold two-thirds of the value of the claims in

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and depends on the nature of the reorganization). The third-party release must (1) be narrowly tailored, (2) not constitute a "blanket immunity," and (3) be essential to the debtor's reorganization. *Id.*

[80] The circuits comprising the minority include the Fifth, Ninth, and Tenth. Coco, *supra* note 13, at 237-8.

[81] See *In re* Pac. Lumber Co., 584 F.3d 229 (5th Cir. 2009) (holding that § 524(e) prohibits the release of co-liable third-parties); *In re* Lowenschuss, 67 F.3d 1394 (9th Cir. 1995) (same); *In re* W. Real Est. Fund, Inc., 922 F.2d 592 (10th Cir. 1990) (same).

[82] *See* Coco, *supra* note 13, at 249.

[83] Fed. R. Bankr. P. 3016(c). "[B]old, italic, or underlined text" will satisfy the requirement. *Id.*

[84] *See* Fed. R. Bankr. P. 2002(b) & (c)(3). Courts have rejected third-party releases because the release was not properly disclosed to the creditors or the court. *See In re* Lower Bucks Hosp., 571 F.App'x 139, 143 (3rd Cir. 2014) (explaining that "[n]o use was made of underlined, italicized or boldface text to emphasize the Release or to distinguish it from the more typical releases between the parties to the settlement.").

[85] *See* RESTATEMENT (SECOND) OF Contracts. § 19 (Am. L. Inst. 1981).

[86] 11 U.S.C. § 1141.

the class and one-half of the number of the claims in the class approve the plan.[87] For plans that include nondebtor releases, the consequence of this is that a class of consenting creditors in the majority can strip the minority of their claims against the nondebtor without their consent. This presents an obvious due process issue because the dissenting creditors are stripped of their right to pursue their claims against the nondebtor.

Courts have taken various views on what makes a nondebtor release truly consensual. One view is that a creditor must provide affirmative consent by expressly opting into the release of the nondebtor.[88] Other courts find a failure to opt-out of the nondebtor release as deemed consent to the release.[89] As Dorothy Coco explains, the "opt-out approach results in third-party releases that bind (1) parties who affirmatively vote to accept the plan [and] (2) parties who affirmatively reject the plan and do not opt out of the release[.]"[90]

Notably, where the plan does not contain an option to opt-out of the release, some courts view the mere confirmation of the plan insufficient to infer objecting creditors have consented to the nondebtor's release.[91] Coco argues, and I agree, that the best practice would be for courts to require chapter 11 plans to provide an option to opt-out of a nondebtor's release and find creditor consent only where it is explicit and affirmative through the creditor's opting into the release.[92] This reasoning is in line with the majority view expressed in Part II.B of this Article which purports to hold nonconsensual releases to a higher standard than consensual

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87 11 U.S.C. § 1126(c) ("A class of claims has accepted a plan if such plan has been accepted by creditors . . . that hold at least two-thirds in amount and more than one-half in number of the allowed claims of such class held by creditors . . . that have accepted or rejected such plan.").

88 *See In re* Chassix Holdings, Inc., 533 B.R. 64, 77-81 (Bankr. S.D.N.Y. 2015) (reasoning that creditors who submit a ballot and vote in favor of the plan affirmatively consent to the release; creditors who submit a ballot and vote to reject the plan but opt in to the release affirmatively consent to the release; creditors who are entitled to vote but fail to return a ballot, thus abstaining from voting, do not affirmatively consent and are not deemed to consent to the release; creditors holding claims in classes deemed to reject the plan but who neither affirmatively consent nor are deemed to consent to the release are deemed to reject the release; and creditors holding claims that are unimpaired and are in classes deemed to accept the plan do not affirmatively consent and are not deemed to consent to the release).

89 *See In re* Indianapolis Downs, LLC., 486 B.R. 286 (Bankr. D. Del. 2013) (explaining that if a creditor does not opt-out of the release, the creditor will be bound by the release if the plan is confirmed).

90 *See* Coco, *supra* note 13, at 252.

91 *See In re* SunEdison, Inc., 576 B.R. 453, 455 (Bankr. S.D.N.Y. 2017) (explaining that, regardless of the plan's overall approval, those deemed to reject the plan still needed an opportunity to opt-out of the releases).

92 *See* Coco, *supra* note 13, at 262. ("Allowing creditors who either abstain from voting or reject a plan but fail to opt out to be bound by a release ignores the contract principle that a person cannot be deemed to accept or be bound through silence or inaction.").

releases.[93] Requiring affirmative consent would help to brighten the line between when a nondebtor release is consensual and when it is not.

However, as mentioned earlier, the majority view still finds nonconsensual releases permissible in rare circumstances where the court deems the releases necessary for the debtor's successful reorganization.[94] Absent the opportunity to opt-out of the release, it is difficult to see how this comports with the "opportunity to be heard" that due process is supposed to provide.[95] In these situations, these nonconsenting parties are losing a legitimate right of access to the courts, a right that the Supreme Court has recognized as a fundamental aspect of the First Amendment.[96] If a bankruptcy court is to confirm a plan containing a nondebtor release, creditors should have the opportunity to opt-out of the release and further pursue their claims against the nondebtor in state or federal court. On the other hand, creditors that want to opt into the release should not be precluded from doing so because other claimants made the decision to opt-out. Ideally, the process should operate like a series of contracts entered into by individual creditors with the third-party seeking relief. The decision to enter into that contract or not should be left to each creditor's sole discretion.

III. SCOPE OF BANKRUPTCY COURTS' EQUITABLE POWER

Over the years, bankruptcy courts have derived power under § 105(a) to take judicially created actions that are not explicitly supported elsewhere in the Code. One such example is the nondebtor release. Higher courts have struck down bankruptcy court rulings that were without explicit support from the Code or at odds with other sections of the Code. This section highlights one such instance, the critical vendor motion. Further, this section discusses attempts to reconcile the circuit split on third-party releases and analyzes whether the Supreme Court has already resolved the statutory debate. In chapter 11 cases, the Supreme Court has noted that it is easy to sympathize with the bankruptcy court's desire to expedite reorganization proceedings because they are frequently protracted; however, "[t]he need for expedition . . . is not a justification for abandoning proper standards."[97]

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93 *See supra* Section II.B.

94 *See, e.g.*, *In re* Purdue Pharma L.P., No. 19-23649, 2021 WL 4240974 at *47 (Bankr. S.D.N.Y. 2021 Sept. 17, 2021) (confirming Purdue's plan because the court found the nonconsensual Sackler releases to be necessary to Purdue's reorganization), *vacated*, No. 21-7532 (S.D.N.Y. Dec. 16, 2021).

95 Armstrong v. Manzo, 380 U.S. 545, 552 (1965) ("A fundamental requirement of due process is 'the opportunity to be heard.'") (quoting Grannis v. Ordean, 234 U.S. 385, 394 (1914)).

96 *See* Bill Johnson's Rests., Inc. v. NLRB, 461 U.S. 731, 741 (1983).

97 Protective Comm. for Indep. Stockholders of TMT Trailer Ferry, Inc. v. Anderson, 390 U.S. 414, 450 (1968). *See also In re* Lionel Corp., 722 F.2d 1063, 1071 (1983) (explaining that a trustee's sale of estate assets outside the ordinary course of business must be supported by some articulated

A. The Doctrine of Necessity and Critical Vendor Motions

Once such example of bankruptcy courts overreaching their equitable power is the critical vendor motion. It is an established principle in chapter 11 bankruptcies that debtors can only pay pre-petition claims at the end of a case.[98] Bankruptcy courts use the judicially created doctrine of necessity as an exception to this principle. Where bankruptcy courts find the circumstances compelling, this doctrine allows early pay-outs to otherwise ordinary creditors through the granting of a debtor's critical vendor motion.[99] In a critical vendor motion, the debtor asks the court to allow the debtor to pay a pre-petition creditor early.[100] The debtor argues if this creditor, the critical vendor, is not paid early, it will cease to do business with the debtor, jeopardizing the success of the debtor's reorganization.[101] Bankruptcy courts that grant these motions do so in reliance on their equitable power under § 105(a).[102]

In *In re Kmart Corp*., the bankruptcy court, relying on § 105(a), granted a critical vendor motion without any notice to other creditors nor any findings of fact that all creditors would benefit from the motion.[103] The Seventh Circuit applied much needed brakes to this practice.[104] Judge Easterbrook of the Seventh Circuit pointed out that "[a] doctrine of necessity is just a fancy name for a power to depart from the Code."[105] Further, he agreed with the district court's perspective that § 105(a) "allows [bankruptcy] courts to use their equitable powers only as necessary to enforce the provisions of the Code, not to add on the Code as they see fit."[106]

business justification, and that the need for expediency in Chapter 11 does not excuse the bankruptcy judge from requiring such finding of fact).

98 *See* 11 U.S.C. §§§ 1123, 1129, 1142.

99 Anthony M. Sabino, *The Death of Critical Vendor Motions & the Potential Demise of the Doctrine of Necessity: Farewell to Two Misbegotten Doctrines*, 6 TRANSACTIONS: THE TENN. J. OF BUS. L. 47, 48 (2004).

100 *See id.* at 47 (explaining that debtors justify this request by arguing these vendors will cease supplying goods and services to the debtor until the debtor satisfies its pre-petition debts).

101 *See id.* at 49.

102 *See id.* at 56.

103 *See In re* Kmart Corp. 359 F.3d 866, 868 (7th Cir. 2004).

104 *See id.* at 874 (affirming the district court's reversal of the bankruptcy court's ruling allowing the critical vendor motion). Note, however, the court left open the possibility that a critical vendor motion might be permissible in extraordinary circumstances under § 363(b)(1). The court declined to reach the issue due to the unsoundness of the bankruptcy court's order. *Id.* at 872.

105 *Id.* at 871.

106 *In re* Kmart Corp., 291 B.R. 818, 822 (N.D. Ill. 2003), *aff'd*, 359 F.3d 866 (7th. Cir. 2004) (quoting *In re* Fesco Plastics Corp., 996 F.2d 152, 156 (7th Cir. 1993)).

B. Are Nondebtor Releases Another Overreach of § 105(a)?

In 2014, the Supreme Court expressed its view of § 105(a) and stated that "[i]t is hornbook law that § 105(a) 'does not allow the bankruptcy court to override explicit mandates of other sections of the Bankruptcy Code[]' . . . 'whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of' the Bankruptcy Code."[107]

As discussed below, some scholars argue that the Supreme Court has already resolved the nondebtor release issue. However, the answer seems unclear.

1. Can the Circuit Split Be Reconciled Via Factual Distinction?

As Joshua Silverstein points out, commentators have tried to reconcile the pro- and anti-release decisions across the circuits.[108] Some scholars contend that the cases under the two lines of authority are factually distinct.[109] These commentators contend that pro-release decisions typically concern complex, mass torts where the *Master Mortgage* factors are generally met.[110] Conversely, they contend that anti-release decisions typically involve smaller disputes where the release provisions do not meet the *Master Mortgage* factors.[111] I agree with Silverstein that these reconciliation attempts are unpersuasive, as the anti-release circuits have made clear their view that § 524(e) expressly prohibits nondebtor releases.[112] The next section addresses Silverstein's argument that the Supreme

[107] Law v. Siegel, 571 U.S. 415, 421 (2014) (quoting Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 206 (1988) and 2 Collier on Bankruptcy ¶ 105.01[2], p. 105-6 (16th ed. 2013)).

[108] Silverstein, *supra* note 26, at 86.

[109] *See* John E. Swallow, *The Power of the Shield – Permanently Enjoining Litigation Against Entities Other than the Debtor – A Look at In re A.H. Robins Co.*, 1990 BYU L. REV. 707, 720-23 (arguing the pro/anti release decisions are factually distinguishable); *see also* Kate Inman, *All Debts Are Off? – Can the Bankruptcy Process Be Used to Release the Debts of Nondebtor Parties*, 49 FLA. L. REV. 631, 641-47 (1997) ("A closer review suggests that the differing outcomes between the [pro/anti release decisions] may be as much a product of different factual settings as a result of divergent interpretations of the law.").

[110] Silverstein, *supra* note 26, at 86-87.

[111] *Id.* at 87.

[112] *See In re* Am. Hardwoods, Inc. v. Deutsche Credit Corp., 885 F.2d 621, 626 (9th Cir. 1989) ("Section 524(e) . . . limits the court's equitable power under section 105 to order the discharge of the liabilities of nondebtors . . ."); *In re* W. Real Est. Fund, Inc., 922 F.2d 592, 601 (10th Cir. 1991) (concluding that § 524(e) prohibits any permanent injunction "extended post confirmation . . . that effectively relieves the nondebtor from its own liability to the creditor"); Feld v. Zale Corp., 62 F.3d 746, 760 (5th Cir. 1995) ("Although we interpret § 105 liberally, a § 105 injunction must be consistent with the rest of the Bankruptcy Code" and § 524 "prohibits the discharge of debts of nondebtors"; therefore, "we must overturn a § 105 injunction if it effectively discharges a nondebtor.").

Court, in *United States v. Energy Res. Co.*,[113] has already resolved the issue in favor of the pro-release circuits.

2. Has the Debate Been Resolved?

a. The Case

The Internal Revenue Code requires employers to withhold money from their employees' paychecks to pay employees' income and social security taxes.[114] The funds must be held in trust for the United States and are commonly known as "trust fund taxes."[115] If an employer does not pay all its trust fund taxes, the government may directly pursue the employees responsible for collecting the taxes to collect the deficiency.[116] Hence, these employees are called "responsible persons."[117] Conversely, for non-trust fund taxes which an employer fails to pay, the IRS cannot pursue responsible persons for the deficiency.[118]

When Energy Res. Co. filed chapter 11, it had outstanding trust fund tax liability.[119] After the bankruptcy court confirmed the reorganization plan, the trustee sent a payment to the IRS and requested, unsuccessfully, that the IRS apply the payment to the company's trust fund tax debt.[120] In response, the ". . . trustee successfully petitioned the Bankruptcy Court to order the IRS to apply the money to the trust fund tax liabilities."[121] The IRS failed on appeal and the Supreme Court granted certiorari. The Supreme Court affirmed the decision and held that, if it is necessary for a successful reorganization plan, bankruptcy courts may order the IRS to deem tax payments made by chapter 11 debtor corporations as trust fund payments.[122] In reaching its decision, the Court acknowledged that there was no explicit authorization in the Code for bankruptcy courts to approve reorganization plans that designate tax payments as either trust or non-trust fund.[123] However, the Court went on to explain:

The [Bankruptcy] Code, however, grants the bankruptcy courts residual authority to approve reorganization plans including "any . . . appropriate provision not inconsistent with the applicable provisions of this title." 11 U.S.C. § 1123(b)(5)

113 U.S. v. Energy Res. Co., Inc., 495 U.S. 545 (1990).
114 26 U.S.C. §§ 3102(a), 3402(a).
115 *See* 26 U.S.C. § 7501(a); Slodov v. U.S., 436 U.S. 238, 243 (1978).
116 § 26 U.S.C. § 6672.
117 *Slodov*, 436 U.S. at 245.
118 Internal Revenue Serv. v. Energy Res. Co., 871 F.2d 223, 225 (1st Cir. 1989), *aff'd*, 495 U.S. 545 (1990).
119 *See* U.S. v. Energy Res. Co., 495 U.S. 545, 547 (1990).
120 *Id.* at 547.
121 *Id.* at 547-48.
122 *Id.* at 545.
123 *Id.* at 549.

[now 1123(b)(6)]; see also § 1129. The Code also states that bankruptcy courts may "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions" of the Code. § 105(a). These statutory directives are consistent with the traditional understanding that bankruptcy courts, as courts of equity, have broad authority to modify creditor-debtor relationships.[124]

Thus, the bankruptcy court, under its equitable powers, had the authority to confirm the plan deeming the tax payments as trust fund payments.[125]

b. Boundaries of § 105(a)

Silverstein argues that the Supreme Court's opinion resolves the debate over nondebtor releases.[126] He argues that the *Energy Res. Co.* Court, by holding that the exercise of equitable power under Sections 105(a) and 1123(b)(6) need not be tied to specific Code provisions, effectively ends the debate over the scope of bankruptcy courts' equitable power in chapter 11.[127] Generally, I agree with this point. However, I also agree with Judge Easterbrook that bankruptcy courts must exercise this power in a manner that is at least consistent with the Code and that assists in enforcing the Code and the general policies and goals of bankruptcy.[128] The Supreme Court seems to agree with this view. Ten years after *Energy Res. Co.*, the Supreme Court again elaborated on its view of § 105(a): "It is hornbook law that § 105(a) 'does not allow the bankruptcy court to override explicit mandates of other sections of the Bankruptcy Code[]' . . . whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code."[129]

The implication of this statement turns on one's interpretation of "within the confines of the Bankruptcy Code". On one hand, this may be interpreted to allow the exercise of § 105(a) power so long as it does not expressly clash with other provisions of the Code. The codification of § 1123(b)(6) seems to support that view.[130] Silverstein concurs and argues that this statement of law is best

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124 *Id.* (citing Katchen v. Landy, 382 U.S. 323 (1966); U.S. Nat'l Bank v. Chase Nat'l Bank, 331 U.S. 28 (1947); Pepper v. Litton, 308 U.S. 295 (1939)).

125 *See id.* at 551 ("In this case, the Bankruptcy Courts have not transgressed any limitation on their broad power. We therefore hold that they may order the IRS to apply tax payments to offset trust fund obligations where it concludes that this action is necessary for a reorganization's success.").

126 *See* Silverstein, *supra* note 26, at 104-31.

127 *See id.* at 106-07 (explaining that several anti-release authorities believe § 105(a) must be used to implement other, specific provisions in the Code).

128 *See In re* Kmart Corp., 359 F.3d 866, 871 (7th Cir. 2004) ("[T]he power conferred by § 105(a) is one to implement rather than override."); *supra* Section III.A (discussing § 105(a) and the doctrine of necessity).

129 L. v. Siegel, 571 U.S. 415, 421 (2014) (quoting Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 206 (1988) and 2 Collier on Bankruptcy ¶ 105.01[2], p. 105-06 (16th ed. 2013)).

130 11 U.S.C. § 1123(b)(6) states that a plan may "include any other appropriate provision not inconsistent with the applicable provisions of this title". *But see In re* Purdue Pharma L.P., No. 21-

understood as "reflecting the rule that a bankruptcy court may not use §§ 105(a) and 1123(b)(6) to issue orders that are inconsistent with the Code."[131] He supports his argument by pointing out that the *Energy Res. Co.* court did not even cite the *Ahlers* case from which the "confines of the Bankruptcy Code" quote originally came; therefore, the Court must not have found it relevant to its analysis.[132]

On the other hand, one can argue that "within the confines of the Bankruptcy Code" means the exercise of equitable power must be used in conjunction with other provisions of the Code to be permissible. Notably, some anti-release courts and scholars have interpreted it this way.[133] The thrust of their view of § 105(a) is that the provisions of the Code denote a fixed set of remedies determined by Congress and that bankruptcy courts cannot use § 105(a) to "legislate to add to them."[134] Furthermore, without explicit authority from the Code, bankruptcy courts granting nondebtor releases are at the very least acting on questionable authority. Using "rare" or "unique" circumstances to justify the use of questionable authority is a risky proposition, "especially as the United States Supreme Court has recently held that there is no 'rare case' rule in bankruptcy that allows a court to trump the Bankruptcy Code."[135]

Even assuming Silverstein's view that bankruptcy courts may invoke § 105(a) without explicit support from other provisions in the Code is the correct one, nondebtor releases still may exceed other articulated limitations on § 105(a).[136] Not only must § 105(a) be used consistently with the rest of the Code, but some courts have also articulated that § 105(a) does not empower courts to "create substantive rights that would otherwise be unavailable under the Code" or other "applicable

7532, at 121 (Dec. 16, 2021) (arguing that § 1123(b)(6) is substantively analogous to § 105(a) and neither confer substantive authority).

131 Silverstein, *supra* note 26, at 109.

132 *Id*.

133 *See, e.g.,* Jamo v. Katahdin Fed. Credit Union, 283 F.3d 392, 403–04 (1st Cir. 2002) ("The authority bestowed [under § 105] may be invoked only if, and to the extent that the equitable remedy dispensed by the court is necessary to preserve an identifiable right preserved elsewhere in the Bankruptcy Code."); *In re* Myrvang, 232 F.2d 1116, 1125 (9th Cir. 2000) ("Exercise of § 105 powers must be linked to another specific Bankruptcy Code provision."); Noonan v. Sec'y of Health and Hum. Servs., 124 F.3d 22, 28 (1st Cir. 1997) ("But since section 105 itself is not a source of new substantive rights, the bankruptcy court may invoke section 105(a) only if the equitable remedy utilized is demonstrably necessary to preserve a right elsewhere provided in the Code."); Norton Bankruptcy Law & Practice 3d § 13:3.

134 Pertuso v. Ford Motor Credit Co., 233 F.3d 417, 423 (6th Cir. 2000) (quoting Matter of Kelvin Pub., Inc., No. 94-1999, 1995 WL 734481 at *4 (6th Cir. Dec. 11, 1995)).

135 *See In re* Purdue Pharma L.P., No. 21-7532, at *6 (citing Czyzewski v. Jevic Holdings Corp., 137 U.S. 973, 986 (2017)).

136 *See* Fouad Kurdi, *A Question of Power: Non-Consensual Third-Party Releases in Chapter 11 Plans*, 25 NORTON J. OF BANKR. L. & PRAC. NL 4 Art. 6 at *3 (2016).

law."[137] Because nondebtor releases prevent claimants from pursuing their claims against the nondebtor, some courts perceive the inclusion of these releases in reorganization plans as an impermissible creation of substantive rights.[138]

Nevertheless, it is well established that the equitable power in § 105(a) must be used with the purpose of effectuating successful reorganizations; it does not "authorize free-wheeling consideration of every conceivable equity, but rather only how the equities relate to the success of the reorganization."[139] Effectively, no interpretation of § 105(a)'s scope leads to the conclusion that bankruptcy courts have complete carte blanche to take any action not explicitly at odds with the Code. But should successful reorganization be the only consideration involved in the release of a nondebtor? As mentioned earlier, the ABI has recommended the *Master Mortgage* factors control courts' analysis.[140] This Article contends that other factors such as procedural protection of claimants,[141] guaranteed substantive outcomes,[142] and willful misconduct should also be considered.[143]

C. Interpretation of § 524(e)

Silverstein also uses *Energy Res. Co.* to dispense with the argument that § 524(e) prohibits nondebtor release.[144] He argues that the case establishes the Supreme Court's "plain-meaning" approach to statutory interpretation should apply when the issue is whether the use of equitable power clashes with a more specific Code provision.[145] From this, he concludes that "since the clear language

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[137] *See In re* Combustion Eng'g, Inc., 391 F.3d 190, 236 (3rd Cir. 2004) (citing U.S. v. Pepperman, 976 F.2d 123, 131 (3rd Cir. 1992)); *In re* Aquatic Dev. Group, Inc., 352 F.3d 671, 680-681 (2nd Cir. 2003); U.S. v. Sutton, 786 F.2d 1305, 1308 (5th Cir. 1986).

[138] Kurdi, *supra* note 136, at *3. Kurdi points to the Third Circuit's *In re* Combustion Eng'g, Inc., 391 F.3d 190, case to illustrate this point. In that case, the Third Circuit vacated a channeling injunction that restricted the recovery of asbestos claims against third-party affiliates because the nondebtors did not satisfy the requirements in § 524(g) for asbestos related nondebtor releases, *In re* Combustion Eng'g, Inc., 391 F.3d at 236. Because the remedy was not available under the Code in this instance, the bankruptcy court could not use § 105(a) to create a new substantive right that was otherwise unavailable, *see id.* at 236-37. Kurdi notes that while this holding is limited to "equitable injunctions issued in asbestos related contexts, its analysis is instructive in identifying when, if ever, non-consensual third-party releases are permissible." Kurdi, *supra* note 136, at *3. Judge McMahon articulates a similar line of reasoning in vacating the bankruptcy court's confirmation of Purdue's chapter 11 plan. *See In re* Purdue Pharma, L.P., No. 21-7532 at *121-22 (explaining that the Sacklers would not be able to discharge the fraud claims against them even if they themselves were debtors in bankruptcy).

[139] NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527 (1984).

[140] AM. BANKR. INST., *supra* note 14, at 256.

[141] *See* discussion *infra* Part IV.B.

[142] *See* discussion *infra* Part IV.B.

[143] *See* discussion *infra* Part IV.C.

[144] *See* Silverstein, *supra* note 26, at 122-31.

[145] *See id.* at 123 (explaining that the Energy Res. Court took the plain meaning approach to the statutes at issue).

of § 524(e) fails to prohibit or even address nondebtor releases, the statute does not bar such relief."[146]

On its face, this is probably the right stance; however, Silverstein fails to consider that the Supreme Court has shown willingness to stray from such a strict "plain-meaning" approach in bankruptcy matters where an inequitable result is at stake.

One such example is the Supreme Court's 2010 *Hamilton v. Lanning* opinion.[147] There, the court was tasked with determining the appropriate method to calculate a debtor's "projected disposable income" for the purpose of her chapter 13 plan.[148] While no definition exists in the Code for "projected," the "disposable income" definition reads, "[f]or the purposes of this subsection [§ 1325(b)], the term 'disposable income' means current monthly income received by the debtor[.]"[149] Further, the Code defines "current monthly income" as "the average monthly income from all sources that the debtor receives . . . derived from the 6-month period" prior to the commencement of the case or the date the court determines the debtor's current income.[150] The key fact in this case was that the debtor had received a large sum of money in the months prior to her filing, so the normal backwards-looking approach required by the plain meaning of the Code would skew her "projected disposable income" so high that she would be unable to make the payments under the plan.[151] To avoid this inequitable result, the Court took it upon itself to shift its emphasis from the words "disposable income" to the word "projected", crafting a meaning that would allow a forwards-looking approach in this instance.[152] Justice Scalia, remaining true to his record as a staunch plain-meaning advocate, fervently disagreed. He argued that such a construction of the statute rendered Congress's codified definition of "disposable income" meaningless.[153]

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146 *Id.*
147 Hamilton v. Lanning, 560 U.S. 505 (2010).
148 *See id.* at 509. In chapter 13 cases, an individual debtor's obligations are paid over the life of a three-to-five-year plan. *See* 11 U.S.C. § 1322.
149 11 U.S.C § 1325(b)(2).
150 11 U.S.C § 101(10a)(a).
151 *See Hamilton*, 560 U.S. at 511 ("In the six months before [the debtor's] filing, she received a one-time buyout from her former employer, and this payment greatly inflated her gross income[.]").
152 *See id.* at 513-19.
153 *See id.* at 526 (Scalia, J., dissenting)

> ("It would be pointless to define disposable income in such detail, based on data during a specific 6-month period, if a court were free to set the resulting figure aside whenever it appears to be a poor predictor. And since 'disposable income' appears nowhere else in § 1325(b), then unless § 1325(b)(2)'s definition applies to 'projected disposable income' in § 1325(b)(1)(B), it does not apply at all.").

It would not be surprising to see the Supreme Court consider utilizing similar creativity in construing § 524(e) to prohibit nondebtor releases, particularly considering widespread public opinion that the release of nondebtors like the Sacklers is inequitable.[154]

IV. MASS TORT LITIGATION AND CHAPTER 11

Since the advent of nondebtor releases in *Johns-Manville*, other companies forced into bankruptcy under the weight of mass tort litigation have looked to this legal mechanism to assist in effectuating their chapter 11 plans. What seemed to be a new, creative solution to solve the unsolvable asbestos problem proved to have a more pernicious effect in serving as a vehicle for nondebtors involved in mass tort litigation to escape liability. Particularly, when creditors have valid claims against nondebtors that played a role in the perpetuation of a mass tort, granting those nondebtors a liability release as part of the reorganization plan may reduce injured parties' overall recoveries and allow people who deserve to be held accountable to receive a windfall.

A. Nature of Mass Tort Litigation Resulting in Bankruptcy

A mass tort is a wrongful action that causes injury to many different people resulting in multiple, dispersed claims.[155] The sheer amount of litigation involved in mass torts often forces companies into bankruptcy. Litigation is expensive and broad exposure to liability can rapidly deplete any cash and insurance reserves a company might have.[156] Generally, the main factors that drive mass tort bankruptcies are (1) the "company does not have enough money to pay claimants" and (2) "the value of filing as a strategic maneuver to effectuate and/or coerce a global settlement."[157] Typically, bankruptcy exists as a last resort for struggling companies; however, companies involved in mass tort litigation have increasingly invoked chapter 11 as an effective way to deal with immense amounts of liabilities.[158] This is in part due to the procedural and substantive benefits

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[154] The Supreme Court might soon address the Sackler release issue considering the district court's recent reversal and Purdue's plan to appeal the decision. *See* Brendan Pierson, et. al., *U.S. judge tosses $4.5 billion deal shielding Sacklers from opioid lawsuits,* REUTERS, (Dec. 16, 2021), https://finance.yahoo.com/news/judge-tosses-deal-shielding-purdues-002136299.html?fr=sycsrp_catchall.

[155] Douglas Smith, *Resolution of Mass Tort Claims in the Bankruptcy System*, 41 U.C. DAVIS. L. REV. 1613, 1617 (2008).

[156] Simon, *supra* note 29, at 1162.

[157] *Id.*

[158] *Id.* at 1163. *See generally* Alan N. Resnick, *Bankruptcy as a Vehicle for Resolving Enterprise-Threatening Mass Tort Liability*, 148 U. PA. L. REV. 2045, 2046 (2000) (noting that when the Code was enacted in 1978, Congress did not expect that companies facing massive tort liability would turn to the Code for relief).

bankruptcy provides to mass tort defendants. For instance, the automatic stay freezes most all pending litigation the moment the debtor's petition is filed.[159] Substantively, mass tort defendants receive the benefit of binding absent parties and "discharg[ing] claims of countless future claimants who have not yet manifested any injury."[160] The Code makes this possible by defining a "claim" as a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured."[161] These benefits, combined with bankruptcy courts' "equitable powers of injunction and release [] have encouraged the use of bankruptcy to deal with mass torts."[162]

B. Channeling Injunctions

To assist in effectuating chapter 11 plans, bankruptcy courts have increasingly begun to extend the benefits of bankruptcy to nondebtor parties through tools such as channeling injunctions and nondebtor releases. To understand how nondebtor releases in mass tort bankruptcies work, one must understand the concept of a channeling injunction. When a court issues a channeling injunction, it channels "tort claims to a litigation trust funded by participating parties."[163] After the trust is established, all past, present, or future claimants must look exclusively to the assets in the trust to satisfy their claims.[164] Bankruptcy expert Gary Svirsky described the double-edged effect of the process: while this process often provides claimants with an "efficient claims-evaluation process that typically does not require the level of proof they would need" to prevail in court, it also "insulate[s] debtors, certain nondebtor defendants, and other participants from known current and future claims."[165] In effect, the issuance of a channeling injunction triggers a permanent liability release for certain nondebtors contributing to the trust.[166]

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159 *See* 11 U.S.C. § 362(a) (listing prohibited creditor action as a result of the automatic stay). Notable exceptions to the automatic stay include police and government/regulatory power. § 362(b)(4).

160 Simon, *supra* note 29, at 1164.

161 11 U.S.C. § 101(5)(A).

162 Simon, *supra* note 29, at 1164.

163 Gary Svirsky et al., *A Field Guide to Channeling Injunctions and Litigation Trusts*, 260 N.Y.L.J. 10 (2018); *See also supra* Section I.C. (discussing the origin of nondebtor releases and the channeling injunction issued in the *Johns-Manville* bankruptcy).

164 *Id.*

165 *Id.*

166 However, some plans that make use of the channeling injunction provide claimants the opportunity to opt-out of the trust structure and pursue their claims. To issue channeling injunctions, courts rely on §§ 363 (f) and (h), *See* Matter of Johns-Manville Corp., 68 B.R. 618, 625 (Bankr. S.D.N.Y. 1986) (explaining that these Code sections "explicitly provide for the channeling of claims in this manner" and concluding that "the court's authority to channel claims is … granted by implication, even absent statutory provisions").

Because of its efficiency and finality for debtors and others in the product's distribution chain, parties employ the channeling injunction in a multitude of mass-tort product liability bankruptcies.[167] One of the earliest non-asbestos examples of the channeling injunction came in the *Dow Corning Corp.* bankruptcy.[168] In 1995, Dow filed for bankruptcy facing billions of dollars in lawsuits alleging Dow's silicone breast implants caused auto-immune disorders in millions of women.[169] Dow's reorganization plan permanently released the company, its insurers, and its shareholders from liability on personal injury claims and channeled the claims into a litigation trust.[170] Notably, the plan offered claimants the option to opt-out of the settlement and releases and further pursue litigation.[171] If a claimant who opted into the settlement was unhappy with her payment, she could request review by the Claims Administrator and further appeal that decision to the Appeals Judge if she was still unsatisfied.[172] Also, only claimants were provided appellate rights; Dow had no right to appeal.[173]

Professor Simon uses the Dow bankruptcy and others to illustrate how claimants' experiences vary when mass tort claims are channeled through bankruptcy.[174] In particular, she details the mechanics of the Takata bankruptcy plan to provide an example of when the channeling injunction was a valuable tool for all parties involved, including claimants.[175] She identifies two key categories that make *Takata* an exemplary mass bankruptcy: procedural protections and substantive outcomes.[176]

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167 *See In re* TK Holdings Inc., No. 17-11375, 2018 WL 7051669 (D. Del. Apr. 9, 2018) (using channeling injunction that protected nondebtor automakers from mass tort liability involving air bag inflators); *In re* Blitz, Inc., Notice of (A) Entry of Order Confirming Debtors' and Official Committee of Unsecured Creditors' First Amended Joint Plan of Liquidation, And (B) Bar Dates for Filing Administrative Expense Claims and Rejection Damages Claims, Case No. 11-13603 (PJW), Doc. #2160 (Bankr. D. Del. Feb. 5, 2014) (using channeling injunction that protected nondebtor private equity investors, retailers, and insurers from mass tort liability involving gas cans); *In re* The Delaco Co., No. 04-10899, (Bankr. S.D.N.Y. Feb. 17, 2006) (using channeling injunction that protected nondebtor drug vendors, distributors, and insurers from mass tort liability involving diet pills).

168 *In re* Dow Corning Corp., 280 F.3d 648 (6th Cir. 2002).

169 Jason J. Jardine*, The Power of the Bankr. Ct. to Enjoin Creditor Claims Against Nondebtor Parties in Light of 11 U.S.C. § 524(e): In Re Dow Corning Corp.*, 2004 B.Y.U. L. Rev. 283, 283 (2004) (citing *In re* Dow Corning Corp., 280 F.3d 648 (6th Cir. 2002)).

170 Simon, *supra* note 20, at 1174.

171 Amended Joint Disclosure Statement with Respect to Amended Joint Plan of Reorganization at 8-9, *In re* Dow Corning Corporation, No. 95-20512 (Bankr. E.D. Mich., Feb. 4, 1999).

172 *Id.* at 8.

173 *Id.*

174 *See* Simon, *supra* note 29, at 1176 (explaining that "[s]ome cases offer litigation experiences that closely mirror procedural rights in state or federal court, while others put claimants through a gauntlet that severely limits process and potential recoveries").

175 *See id.* at 1176-1183 (providing a detailed description of Takata's plan).

176 Simon, *supra* note 29, at 1179.

One example she points to of a procedural protection Takata's channeling injunction provided was "the claimant's right to appeal to multiple levels, with a variety of different decisionmakers with expertise and independence."[177] This is important because channeled claims should benefit from the same multiple opportunities to appeal what they deem unjust determinations that civil procedure provides at the state and federal level.[178] Another protection was claimants' opportunity to opt out of the trust structure entirely and further pursue their claims in state or federal court.[179] This is crucial, as it helps to satisfy the due process concerns discussed in Part II.C of this Article.[180] Lastly, she notes that the Takata claimants were given several opportunities to submit additional information to decisionmakers and request special or additional review.[181] This further cements the protection of claimants' rights by providing "individualized opportunities in the mass tort process" that "offer small ways for [individualized] needs to be satisfied in an otherwise impersonal and mass-produced mechanism for justice."[182]

Simon goes on to point out a couple fundamental substantive guarantees that the Takata plan included that benefitted claimants.[183] First was the guarantee that claimants would be paid the full amount of their awarded claim because the plan contributors were required to make ongoing contributions to the trust.[184] Compared to the many trust structures where the nondebtor pays a fixed sum of money to the trust, this is a better result where the nondebtor is solvent and is not financially limited to making one isolated contribution.[185] Second, decisionmakers

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177 *See id.* at 1179; *Id.* at 1177-78 (describing the appeals process).

178 *See id.*

> ("There are few decisions in mass tort litigation more important than whether a claimant is eligible to recover against a defendant and how much that recovery will be. Civil procedure at the state and federal level provides multiple opportunities to challenge a determination that seems unjust. Channeled claims should benefit from the same opportunities, free of charge.").

179 *See id.* (noting that the Takata claimants could opt out of the trust structure and "return to state or federal court at will").

180 *See* discussion *supra* Section II.C (explaining that without the opportunity to opt out of a nondebtor release, claimants lose a legitimate right of access to the courts and the due process protection of the opportunity to be heard).

181 *See* Simon, *supra* note 29, at 1180.

182 *Id.* at 1181.

183 *See id.* at 1181.

184 *Id.*

185 *See id.* Further, Simon explains that there are times where a one-time contribution by the nondebtor might be appropriate. However, stakeholders must have access to enough information about the nondebtor to determine a sufficient contribution amount. *See also* discussion *infra* Section V.B.1 (proposing mandatory disclosure obligations for nondebtors); discussion *infra* Section IV.C (arguing solvent nondebtors that engaged in willful misconduct should pay the highest price possible for release which could include required continuing contributions).

determined the monetary value of claims in Takata by using thoughtfully calculated metrics that considered variables such as the "average out-of-court award for different injuries" and the likely arguments and defenses that might arise in litigation outside of bankruptcy.[186] Further, Simon explains that faith in the claims estimation approach was only possible "because claimants and decisionmakers ha[d] been granted access to information about the debtor and nondebtor beneficiaries, including their litigation values and legal positions."[187] Without this transparency, it's easy to see that it would be difficult for claimants to fully trust the results of the process.

While Simon gives praise where its due for Takata's bankruptcy plan, she also makes clear the reality that, until Congress or courts intervene on nondebtor relief, "the actual process and treatment of channeled claimants in Takata was as fair and transparent as one could expect."[188] In sum, if the protections of bankruptcy are to be extended to nondebtors, it should be limited to circumstances like Takata, where the process gives mass tort defendants no impactful procedural or substantive advantages.[189]

C. Considering Willful Misconduct as a Factor in Nondebtor Releases

When faced with the decision to issue a release to a nondebtor involved in a company's mass tort bankruptcy, courts should consider whether the nondebtor engaged in willful misconduct related to the mass tort claims that forced the debtor into bankruptcy. Further, the answer to that question should affect the analysis of factor two of the *Master Mortgage* factors, "whether the nondebtor has contributed substantial assets to the reorganization[.]"[190] The ABI pointed to three factors being of particular importance to the question of nonconsensual nondebtor releases: the extent of the nondebtor's contribution to the plan, the effectiveness of established mechanisms facilitating affected creditor's recoveries, and whether substantially

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[186] Simon, *supra* note 29, at 1181.
[187] *Id.* at 1182.
[188] *See id.* at 1183. ("Instead of abusing the channeling injunction to minimize liability and silence litigation risk, Takata . . . used it to create a manageable process for organizing and paying claims.").
[189] *Id.* at 1183.
[190] *In re* Master Mort. Inv. Fund, Inc., 168 B.R. 930, 937-38 (Bankr. W.D. Mo. 1994).

all of these creditor's claims will be paid.[191] The Commission recommended "specific emphasis" on the mechanisms facilitating recoveries.[192]

The standard to meet under these factors should heighten when a nondebtor's willful misconduct or gross negligence has played a direct part in the mass tort claims rendering the debtor company insolvent. This is especially true where the nondebtor aims to remain solvent after the confirmation of the plan while tort victims are forced to accept less than the value of their claims against the debtor company and nondebtor. When faced with a situation like the *Purdue* bankruptcy, where the value of the aggregated mass tort claims is virtually limitless, a difficult question arises about what sort of contribution would be substantial enough to justify the release of a nondebtor. In these cases, without the protection of a nondebtor release, these nondebtors would likely go insolvent before every past, present, and future claim against them matured. This leaves courts with a binary choice. Either (1) allow the claims against the nondebtor to go forward, which could increase individual recoveries and eventually render the nondebtor insolvent if the claimants were successful, or (2) confirm the releases, which would ensure an immediate contribution by the nondebtor to the plan and guarantee claimants a bigger pot to share as a result of the plan confirmation than they would have gotten had the nondebtor not contributed to the plan at all. When faced with this decision, and where the nondebtor has engaged in willful misconduct, courts should place the highest price tag possible on the nondebtor's release. Courts could require continuing contributions, rather than a one-time payment, to help accomplish this. While this may result in more arduous plan negotiations, fervent reluctancy to grant releases without extracting the maximum contribution from nondebtors may cause the leverage to shift from nondebtors with deep pockets to the body of creditors. It would put the ball in the nondebtor's court to either contribute to the plan as much as it can or take the chance of going broke when the claims against it move forward. Furthermore, if opt-out provisions were required to be included in these situations, nondebtors would be incentivized to make larger contributions to the plan to minimize the number of creditors who otherwise might opt-out of the release.

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191 *See* AM. BANKR. INST., *supra* note 15, at 256

> ("The Commission considered the application of each factor to different scenarios, including the relationship of the factors to nonconsensual releases. It agreed that in the context of nonconsenting creditors or classes of claims, the factors focusing on the contributions of nondebtor parties, percentage recoveries by the affected creditors, and mechanisms established to facilitate recoveries to those creditors were of particular importance, with specific emphasis on the last of these factors.").

192 *Id.*

Courts should also consider willful misconduct in analyzing whether a release is sufficiently narrowly tailored. Courts have done this in the past. The Seventh Circuit, in the *Airadigm* bankruptcy, found relevant that the release of the nondebtor entity, Telephone and Data Systems ("TDS"), did not include a release for claims arising from willful misconduct.[193] A few subsequent courts have looked to *Airadigm* when analyzing the breadth of a nondebtor release;[194] however, the consideration has not made enough of an impact on mass tort bankruptcies. For example, in the *A.H. Robins Co.* bankruptcy, the Fourth Circuit remained silent on what effect any willful misconduct on the part of the nondebtors should have on the confirmation of the plan.[195] A.H. Robins filed for bankruptcy after their Dalkon Shield IUD devices had severely injured several women who used them. Plaintiffs brought claims against the company and members of the Robins family as joint tortfeasors, charging that they had fraudulently concealed evidence of the Dalkon Shield's dangers.[196] Ultimately, the court found the nondebtor releases necessary for successful reorganization.[197]

A good argument exists that the release of dishonest and unscrupulous nondebtors should never be granted, regardless of consent or the nondebtor's contribution to the chapter 11 plan. If a debtor in bankruptcy is unable to discharge debts that arose from fraudulent or malicious conduct,[198] why then should a nondebtor receive this benefit when he has not subjected all of his assets to the court by way of filing for bankruptcy? Discharging the nondebtor in these instances

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[193] *See In re* Airadigm Commc'ns, Inc., 519 F.3d 640, 657 (7th Cir. 2008) (explaining that the release was appropriately tailored because it was limited to "claims arising out of or in connection with the reorganization itself and does not include willful misconduct"). Note, however, that this was not a case arising out of mass tort litigation.

[194] *See In re* Purdue Pharma L.P., No. 21-7532, at *121-22 (Dec. 16, 2021) (finding the Sackler releases impermissible because they included the release from claims of fraud and willful misconduct); OPS3 LLC v. Am. Chartered Bank, No. 13-cv-04398, 2017 WL 3263484 at *4-5 (N.D. Ill. Aug. 1, 2017) (holding the nondebtor release provision insufficiently narrow under *Airadigm's* analysis); *In re* Ingersoll, Inc., 562 F.3d 856, 865 (7th Cir. 2009) (granting a nondebtor release where the creditor was not also a creditor of the bankrupt because the release was sufficiently narrow under *Airadigm*).

[195] *See In re* A.H. Robins Co., 880 F.2d 694, 701 (4th Cir. 1989) (holding the nondebtor releases were valid because the plan was overwhelmingly approved and the entire reorganization hinged on the debtor being free from indirect claims like suits against parties who would have indemnity or contribution claims against the debtor).

[196] *See* Brubaker, *supra* note 26, at 963.

[197] *See In re A.H. Robins Co.*, 880 F.2d at 701.

[198] *See, e.g.,* 11 U.S.C. § 523(a)(2) (debtor cannot discharge debt for benefit obtained through misrepresentation); § 523(a)(4) (debtor cannot discharge debt for embezzlement, larceny, or fraud or defalcation while acting in a fiduciary capacity); § 523(a)(6) (debtor cannot discharge debt for willful and malicious injury); 523(a)(9) (debtor cannot discharge debt for personal injury caused by driving intoxicated); § 523(a)(13) (debtor cannot discharge debt for payment of criminal restitution order).

gives the nondebtor what Ralph Brubaker calls a "[s]uper [f]resh [s]tart"[199] that contradicts one of bankruptcy's most important policy goals of providing the honest but unfortunate debtor with a fresh start.[200] As he explains,"[t]here are two sides to the fresh start policy. The flip side of relief for the honest debtor is no relief for the dishonest or fraudulent debtor, and the bankruptcy discharge has always been conditioned, to various degrees, upon the debtor's good faith."[201]

Further, in nondebtor releases, the absence of discriminative exceptions that deny the release of a dishonest or unscrupulous nondebtor has allowed individuals to discharge debts that they could arguably not discharge through an actual bankruptcy filing.[202] Brubaker points to the *A.H. Robins Co.* case as an example.

[I]n the Robins case, the nondebtor releases left Dalkon Shield claimants with no right to seek compensatory or punitive damages from any individual, including various officers, directors, employees, and attorneys of Robins alleged to have personally participated in a scheme to defraud the public concerning the dangers of the Dalkon Shield. The nondebtor releases lifted from these individuals the prospect of staggering compensatory and punitive damages awards and the prospect that such awards might well haunt them for the rest of their lives as nondischargeable debts.[203]

In vacating the confirmation of Purdue's chapter 11 plan, Judge McMahon refused to give the Sacklers this super fresh start.[204] In doing so, she makes a very persuasive argument similar to the one above. She suggests that interpreting the Code to permit the discharge of a nondebtor from "fraud liability - something that is strictly forbidden from doing for a debtor - cannot be squared with the fact that Congress intended that the Bankruptcy Code 'ensure that all debts arising out of fraud are excepted from discharge no matter what their form.'"[205]

One can hope that other courts adopt the same reasoning in these instances.

To conclude, bankruptcy courts should not allow the release of nondebtors from claims arising from willful misconduct and the like. Even if courts continue to do so in extraordinary circumstances, they should be diligent in requiring opt-

199 Brubaker, *supra* note 26, at 999.

200 Marrama v. Citizens Bank of Mass., 549 U.S. 365, 367 (2007) ("The principal purpose of the Bankruptcy Code is to grant a 'fresh start' to the 'honest but unfortunate debtor.'") (quoting Grogan v. Garner, 498 U.S. 279, 286 (1991)).

201 Brubaker, *supra* note 26, at 999-1000.

202 *Id.* at 1000; *See also In re* Purdue Pharma L.P., No. 21-7532, at *10 (Dec. 16, 2021) (commenting that the claims against the Sacklers "could not be released if the Sacklers were themselves debtors in bankruptcy").

203 Brubaker, *supra* note 26, at 1000.

204 *See In re Purdue Pharma L.P.*, No. 21-7532, at *121-22.

205 *Id.* (quoting Archer v. Warner, 538 U.S. 314, 321 (2003)).

out provisions,[206] considering the "best interests" of claimants,[207] and extracting the highest price possible in return for the nondebtor's release.

D. Perverse Incentives

When a system provides opportunities for one party to achieve a desirable result at the expense of others, advantaged parties naturally have an incentive to position themselves in a way to seize these opportunities. Unfortunately, recent history shows that bankruptcy courts' willingness to grant third-party releases has created such perverse incentives for nondebtors. The subsequent sections highlight two such examples. First, this Article discusses the issues surrounding distributions made from Purdue Pharma to the Sackler family prior to the company's bankruptcy. Next, this Article explores the "Texas Two Step" maneuver employed by Johnson & Johnson to deal with its outsized liabilities arising from its sale of asbestos-containing talc powder.

1. Sacklers' Profit Protection

Imagine the following scenario. You are the owner of a closely held, major pharmaceutical company that made billions of dollars off of a dangerous, addictive drug by fraudulently marketing its safe and non-addictive characteristics to the public. As the years pass, public doubt about the drug's safety heightens as victims become addicted, criminal activity involving the drug increases, and communities begin to deteriorate noticeably. Because of this, you foresee the real possibility that your company might face crushing liability that could potentially put it into bankruptcy. In bankruptcy, your company must thoroughly disclose its financial condition and surrender assets to pay claimants. However, you are also aware of the possibility that, with your financial contribution to a reorganization plan, the bankruptcy might lead to the release of any personal liability you may have due to your role in promoting the drug. That possibility might incentivize you to distribute money from the company to yourself to remove that money from the bankruptcy process, thus removing it from the reach of claimants. Then, once in bankruptcy, you can offer some of the money back to claimants as consideration for releasing their claims against you.

This is part of the story of the Sackler family and Purdue Pharma. In 2007, after Purdue agreed to a $600 million payment to resolve a federal investigation into the company, members of the Sackler family debated whether it was time to

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[206] *See* discussion *supra* Section II.C.

[207] *See* discussion *infra* Section V.B.2 (suggesting extending the "best interests" test to nondebtor releases as a potential alternative to requiring opt-out provisions).

get out of the pharmaceutical business.[208] Recently unsealed emails, memos, and messages from a Sackler family group chat provide insight into the internal deliberations of the wealthy family at the helm of Purdue Pharma.[209] In one 2008 email, Purdue board member, Mortimer Sackler, wrote to his cousin and fellow board member, Richard Sackler, imploring him to consider selling the company. Mortimer wrote, "[e]ven though our prospects have improved dramatically I feel [the sale] offers us a unique opportunity to sell at a very high price and once and for all eliminate the great risks we have and continue to take and secure our families' current and future financial security."[210]

After a bankruptcy attorney advised the family to take "defensive measures" such as "overseas assets with limited transparency and jurisdictional shielding from U.S. judgments," the family decided not to sell the company and continued to market and sell its high-earning opioid, Oxycontin.[211] In the meantime, Purdue Pharma made several distributions to Sackler family members; these distributions continued until 2017 and totaled around $10.4 billion.[212] Two years later, in September 2019, Purdue filed chapter 11.[213]

When a debtor transfers assets out of the debtor's estate with the intent to hinder, delay, or defraud its creditors, fraudulent conveyance laws are supposed to allow the estate to recover the transfers.[214] Johnathan Lipson, a Temple University

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208 Meryl Kornfield, *Newly unsealed court documents reveal Sackler family's early concerns over lawsuits*, THE WASHINGTON POST (JAN. 4, 2021), https://www.washingtonpost.com/business/2020/12/22/sackler-unsealed-documents/.

209 *See id.*

210 *See id.* (quoting an unsealed document).

211 *See id.* (quoting an unsealed document).

212 *See In Re* Purdue Pharma L.P., No. 21-7532, at *4 (S.D.N.Y. Dec. 16, 2021), https://www.courtlistener.com/docket/60373325/280/in-re-purdue-pharma-lp/.

> ("As the opioid crisis continued and worsened in the wake of Purdue's 2007 Plea Agreement, the Sacklers – or at least those members of the family who were actively involved in the day to day management of Purdue – were well aware that they were exposed to personal liability over OxyContin. Concerned about how their personal financial situation might be affected, the family began what one member described as an 'aggressive[]' program of withdrawing money from Purdue almost as soon as the ink was dry on the 2007 papers. The Sacklers upstreamed some $10.4 billion out of the company between 2008 and 2017, which, according to their own expert, substantially reduced Purdue's 'solvency cushion.' Over half of that money was either invested in offshore companies owned by the Sacklers or deposited into spendthrift trusts that could not be reached in bankruptcy and off-shore entities located in places like the Bailiwick of Jersey.").

213 *Id.* at *2

214 *See* 11 U.S.C. § 548(a)(1)(A)

law professor, has suggested that the unsealed Sackler communications "feature classic language that signals an intent to hinder and delay creditors."[215] Nevertheless, attempts at recovering the Sackler distributions have been unsuccessful, as members of the family successfully argued that there was no evidence they knew the company would face an onslaught of litigation until 2017 when the distributions stopped.[216] However, the unsealed internal communications suggest otherwise. For example, the family's unsealed group chat messages reveal that members of the family, long before 2017, had discussed potential liability, surging overdose deaths, and adverse media reports about the company.[217] Adding to the suspicion, under the Code, the statute of limitations to bring a fraudulent conveyance action is two years.[218] Purdue filed bankruptcy in 2019, two years after the distributions to the family reportedly stopped in 2017.

For now, Purdue's plan has been vacated by the district court on appeal. This comes as a relief to many who found the Sackler releases to be a clear abuse of the system. However, the story is likely far from over. As Judge McMahon stated, "[t]his opinion will not be the last word on the subject, nor should it be."[219]

2. J&J's Texas Two Step

Another pharmaceutical company, Johnson & Johnson ("J&J"), is also at the center of a controversial, high-profile bankruptcy case. In 2018, revealed documents showed that J&J's raw talc and finished powders tested positive for small amounts of asbestos occasionally from the early 1970s to the early 2000s.[220] The documents further revealed that company executives, lawyers, and scientists had worried about the asbestos issue and discussed how to address it without

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> ("The trustee may avoid any transfer [. . .] made or incurred on or within 2 years before the date of the filing of the petition, if the debtor voluntarily or involuntarily — made such transfer with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted[.]").

[215] *See* Kornfield, *supra* note 208.
[216] *See id.* (The Sackler family also argues that the distributions were made because of a concern over an expiring patent for OxyContin).
[217] *Id.* (In 2007, David Sackler wrote in an email, "We will be sued. Read the op-ed stuff in these local papers and ask yourself how long it will take these lawyers to figure out that we might settle with them if they can freeze our assets and threaten us.").
[218] § 548(a)(1)(A).
[219] *See In re* Purdue Pharma L.P., No. 21-7532, at *7 (S.D.N.Y. Dec. 16, 2021).
[220] Lisa Girion, *Special Report: J&J knew for decades that asbestos lurked in its Baby Powder*, REUTERS (Dec. 14, 2018), https://www.reuters.com/article/us-johnson-johnson-cancer-special-report/special-report-jj-knew-for-decades-that-asbestos-lurked-in-its-baby-powder-idUSKBN1OD1RQ.

disclosing it to regulators or the public.[221] By 2021, J&J faced roughly 38,000 lawsuits related to the company's talc baby powder.Most of these lawsuits were filed by women with ovarian cancer or people with mesothelioma who claim the asbestos in J&J's product to be the cause of their injuries.[222]

The path chosen by J&J to deal with these liabilities illustrates another example of third-party releases creating an incentive to use chapter 11 to gain an advantage over claimants and protect assets. J&J birthed a new subsidiary, LTL Management LLC, and placed all its talc liability into the new company with the sole purpose of putting the company into bankruptcy.[223] This divisive merger, colloquially called a "Texas Two Step" in reference to the Texas statute that effectuates it,[224] forces claimants to seek recovery from this fictitious subsidiary, LTL Management LLC, rather than from wealthy and solvent J&J. J&J will fund LTL to help pay prepetition claims.[225] J&J will also create a $2 billion settlement trust for future talc claims to be channeled through in hopes that the bankruptcy court will approve the channeling injunction while allowing J&J's release from liability as a nondebtor.[226]

Whether J&J's strategy will be successful remains to be seen. Judge Craig Whitley, who presided over LTL Management LLC's bankruptcy in North Carolina, called the strategy either "brilliant" or "manifestly unfair," depending on the perspective one has.[227] The case now resides in a bankruptcy court in New Jersey, the state where most plaintiffs filed their talc lawsuits.[228] Regardless of the outcome, the situation presents a clear illustration of how solvent nondebtors seek to manipulate the bankruptcy process to provide themselves an advantage at the expense of claimants.

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221 *Id.*

222 Brian Mann, *J&J is using a bankruptcy maneuver to block lawsuits over baby powder cancer claims*, NPR (Oct.21, 2021), https://www.npr.org/2021/10/21/1047828535/baby-powder-cancer-johnson-johnson-bankruptcy.

223 Johnson & Johnson, *Johnson & Johnson Takes Steps to Equitably Resolve All Current and Future Talc Claims*, https://www.jnj.com/johnson-johnson-takes-steps-to-equitably-resolve-all-current-and-future-talc-claims (last visited Nov. 15, 2021).

224 TEX. BUS. ORGS. CODE ANN. § 1.002(55)(A) (2019) (defines a "merger" to include "the division of a domestic entity into two or more new domestic entities or other organizations.") The divisive merger must clearly identify the liabilities and assets to be allocated to each entity. *See* § 10.003 (2006).

225 Johnson & Johnson, *supra* note 223.

226 *See id.*

227 David Warfield, *Johnson & Johnson: The Texas two-step and talc-related liabilities*, THOMPSON COBURN LLP CREDIT REPORT BLOG (Nov. 3, 2021), https://www.thompsoncoburn.com/insights/blogs/credit-report/post/2021-11-03/johnson-johnson-the-texas-two-step-and-talc-related-liabilities.

228 Andrew Scurria & Johnathan Randles, *J&J Talc Bankruptcy Case Moved to New Jersey From North Carolina*, WALL S. J. (Nov. 10, 2021, 7:33 PM), https://www.wsj.com/articles/north-carolina-judge-moves-j-j-talc-bankruptcy-to-new-jersey-11636572841.

V. PROPOSED SOLUTIONS TO THE NONDEBTOR RELEASE PROBLEM

A. Nondebtor Release Prohibition Act

There is legislation in the Congressional pipeline to address nondebtor releases. In late July 2021, Congress introduced bicameral legislation to eliminate nonconsensual, nondebtor releases in chapter 11 bankruptcies.[229] After approval by the House Committee on the Judiciary on November 3, 2021,[230] Chairwoman of the Committee of Oversight and Reform Carolyn Maloney, in a press release, pointed to the *Purdue* bankruptcy to illustrate why the bankruptcy system needs this legislation. "The Sacklers amassed a multi-billion-dollar fortune by flooding communities with OxyContin and fueling an opioid crisis that has claimed the lives of more than half a million people in the United States. Through Purdue Pharma's bankruptcy, they obtained nonconsensual, nondebtor releases that have shielded them from accountability."[231] In addition to prohibiting nonconsensual third-party releases, the bill proposes specific requirements for consensual releases, providing that consent may be given "only after clear and conspicuous notice" to the releasing party.[232] Additionally, consent would be required to be affirmative and expressly given, it may not be given by merely "accepting a proposed plan," or by "failing to accept or reject a proposed plan, or any other silence or inaction."[233] The bill would also prevent the Texas Two Step maneuver described in Section IV.D.2 of this Article.[234]

Critics of the bill, such as the U.S. Chamber of Commerce, argue that the bill would make it more difficult for victims to receive compensation in a timely fashion and that it would harm legitimate claimants by forcing them into litigation.[235] They also argue that the complete elimination of nonconsensual, nondebtor releases would feed into plaintiff's attorneys' incentives to generate questionable claims to extract undeserved payouts.[236] Further, critics argue that the portion of the bill addressing the Texas Two Step will prevent financially distressed

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229 Nondebtor Release Prohibition Act of 2021, H.R. 4777, 117th Cong. (2021), https://docs.house.gov/meetings/JU/JU00/20211103/114212/BILLS-1174777ih.pdf.
230 *Press Release, H. Comm. on the Judiciary, House Judiciary Committee Passes Nondebtor Release Prohibition Act,* JUDICIARY HOUSE (Nov. 3, 2021), https://judiciary.house.gov/news/documentsingle.aspx?DocumentID=4776.
231 *Id.*
232 H.R. 4777 § 2(b)(5)(A).
233 *Id.* at § 2(b)(5)(B)(i-ii).
234 *See* H.R. 4777 § 4. The bill would require courts to dismiss any chapter 11 case if, within a decade prior to filing bankruptcy, the debtor or a predecessor of the debtor divided assets and liabilities between various subsidiaries. *Id.*
235 *See* Neil L. Bradley, *U.S. Chamber Letter on H.R. 4777, "Nondebtor Release Prohibition Act,"* U.S. CHAMBER OF COM. (Nov. 3, 2021), https://www.uschamber.com/lawsuits/u-s-chamber-letter-on-h-r-4777-nondebtor-release-prohibition-act.
236 *See id.*

companies from separating unprofitable assets from those that are more profitable; this, they argue, could cause job losses as one subsidiary's financial problems could lead to other subsidiaries becoming insolvent.[237]

There are valid concerns on both sides of the argument. Those supporting the legislation are correct that nondebtors have abused the system to gain a personal advantage. However, those opposing the legislation express system's ability to resolve complex mass tort litigation issues. In addition, the bill's effect on creditors wanting to opt into the release creates the concern that the bill would foreclose the possibility of a release being obtained via an opt-in/opt-out process at all. Specifically, as the bill is currently written, if *any* creditors voted to opt-out of the release, it would render the release nonconsensual and torpedo the settlement prospects of the creditors wanting to opt into the release.[238]

Congressional consideration of this bill is partly a result of the attention high-profile bankruptcies like the *Purdue* and *J&J* cases have garnered for abusing the system. It will be interesting to see how the situation develops now that the confirmation of Purdue's chapter 11 plan has been vacated by the district court.[239] Still, this nuclear legislation that would destroy the practice as a whole is not without negative implications. Instead, the Chamber of Commerce persuasively suggests that Congress focus its efforts on exploring reforms to increase transparency and consistently produce better outcomes for claimants.[240] The following section takes a closer look at some potential solutions that stop short of eliminating the practice of nonconsensual, nondebtor releases as a whole.

B. Other Proposed Checks on Chapter 11

This Article discusses a few ways in which bankruptcy courts could improve the fairness of chapter 11 and further protect claimants' rights in the process. First, this Article proposed that bankruptcy courts require chapter 11 plans that seek to release a nondebtor to provide an option for claimants to opt-out of the release.[241] Under this approach, the confirmation of a plan would only release a nondebtor from all liability if creditors unanimously opt into the release. However, without unanimous consent, the court could still confirm the plan and release a nondebtor from the claims of those creditors who opted into the release. Those that chose to opt-out would be permitted to prosecute their claims elsewhere. Second, this Article used the *Takata* bankruptcy to highlight desirable procedural protections and substantive outcomes that bankruptcy courts should require when

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237 *See id.*

238 *See supra* Section II.C (arguing that creditors opting out of a release should not affect the settlement prospects of those opting into the release).

239 *See In re* Purdue Pharma L.P., No. 21-7532, (S.D.N.Y. Dec. 16, 2021).

240 *See* Bradley, *supra* note 235, at 43.

241 *See* discussion *supra* Section II.C.

issuing a channeling injunction and nondebtor release.[242] Third, this Article proposed that bankruptcy courts consider a nondebtor's willful misconduct when evaluating the appropriateness of a release.[243] Lastly, the following sections explore other proposed solutions to help mitigate the problems associated with nondebtor releases.

1. Mandatory Disclosures

Disclosures made by the debtor in chapter 11 bankruptcy are fundamental to the success and fairness of the process. Throughout the process, the debtor faces scrutiny from the U.S. Trustee, the court, and stakeholders such as creditors and statutory committees.[244] The debtor's disclosure of things such as detailed schedules of its assets and liabilities and statements of its financial affairs that relate to its bankruptcy filing provide stakeholders the necessary means to evaluate the debtor.[245] As noted before, when a nondebtor seeks release from the claims against it by contributing to the debtor's reorganization plan, bankruptcy courts and claimants face a significant challenge in evaluating whether that contribution is sufficient to compensate claimants equitably and justify the release.[246] Simon argues that bankruptcy courts should impose on "bankruptcy grifters" the exact disclosure requirements imposed on debtors.[247] If nondebtors were required to produce detailed schedules of their financial affairs, claimants could evaluate the fairness of the nondebtor's contribution much more accurately.[248] Rather than negotiating while proverbially blindfolded, claimants would be able to navigate the process with a clear understanding of how much the nondebtor seeking relief could realistically afford. Bankruptcy courts would also have a clearer picture of what is and is not an equitable result. Without the nondebtor's full disclosure, bankruptcy courts are limited mainly in their equitableness analysis to looking at what benefit the nondebtor's contribution to the plan *would* provide to claimants. Requiring the

242 *See* discussion *supra* Section IV.B (highlighting, in *Takata*, the opportunity to opt out of the release; the right to appeal to multiple levels; the opportunity to provide supporting evidence to receive an individualized award rather than a flat amount; the certainty that claimant's awards will be paid in full due to ongoing contributions by the nondebtor; and the use of thoughtfully calculated metrics to value claims).

243 *See* discussion *supra* Section IV.C (arguing that willful misconduct should be considered when evaluating a nondebtor's contribution to a Chapter 11 plan and when determining whether a release is sufficiently narrowly tailored).

244 *See* Simon, *supra* note 29, at 1207.

245 *See id.* (noting that these disclosures contain an abundance of information about "the debtor's estate, including assets, liabilities, related parties, insurance coverage, insiders, litigation, and potential claimants").

246 *See* discussion *supra* Section IV.C (explaining the difficulties with determining whether a nondebtor's contribution to the plan is substantial enough to justify relief).

247 Simon, *supra* note 29, at 1207.

248 *Id.* at 1208-1209.

nondebtor's full financial disclosure would expand the ability of courts to consider what benefit a nondebtor *could* provide to claimants by way of their contribution to the plan. It would also allow for more robust implementation of the proposal in Part IV.C of this Article concerning willful misconduct. If bankruptcy courts know what the nondebtor can afford, they can place higher price tags that they know are realistic on releasing nondebtors who have engaged in willful misconduct.[249]

Simon also points to monthly operating reports as another mandatory disclosure obligation debtors have that courts should extend to nondebtors.[250] She explains that chapter 11 debtors must provide monthly reports highlighting expenditures, assets, and changes that give parties regular insight into the safety of the debtor's assets in the estate — a requirement not imposed upon nondebtors.[251] While the Code prohibits debtors from hiding assets and punishes any attempt to do so with harsh penalties, nondebtors can move assets and shield them from recovery behind the curtain of injunctions and stays imposed by the bankruptcy court.[252] Simon draws a persuasive conclusion that creditors should be able to monitor the assets of a nondebtor seeking relief through the bankruptcy process to ensure they are available for contribution, and the nondebtor should be subject to limitations on asset transfers in a similar manner as the debtor.[253]

These requirements may deter nondebtor participation, leading some to worry that nondebtors will refuse to contribute to the plan if they must disclose private information about their financial affairs. However, as in most mass tort bankruptcies, the nondebtors only alternative is to face crushing amounts of litigation. If nondebtors seek to reap the benefits of bankruptcy, they should have to play by the same rules as parties that actually file a petition.

2. Extending the "Best Interests" Test to Nondebtors

For a bankruptcy court to confirm a plan without unanimous acceptance from impaired creditors, the Code requires a debtor to show that its plan is in the "best interests of creditors."[254] To do this, debtors must show that impaired creditors are treated better under the plan than they would be treated under a hypothetical chapter 7 liquidation.[255] If liquidation would be more beneficial to creditors and all impaired classes have not voted to accept the plan, the court cannot

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249 *See* discussion *supra* Section IV.C (arguing that courts should require higher financial contributions to release dishonest and unscrupulous nondebtors).
250 *See* Simon, *supra* note 29, at 1208.
251 *See id.*
252 *See id.* (noting that the Sackler family has been accused of engaging in this type of activity which threatens public trust in the process and creditor recovery).
253 *Id.*
254 11 U.S.C. § 1129(a)(7)(A)(ii).
255 *Id.*

confirm the plan, and the court orders the debtor to reconsider its approach.[256] Another of Simon's proposals is implementing a similar requirement for nondebtors seeking a channeling injunction and nonconsensual release.[257] Although liquidation would not be at issue, Simon explains that the "best interests" test in § 1129(a)(7), in practical effect, considers two "alternative realities: where the claimant stands if the requested relief is granted, and what the claimant receives if relief is denied."[258] Extending the test to nondebtors would require them to show that channeling the claims against them will lead to at least as good of a result for claimants as would the claimants receiving a claim against the debtor and pursuing the nondebtor outside of bankruptcy.[259]

If bankruptcy courts required opt-out provisions, applying this "best interest" test would not have much practical effect, as creditors that do not want to release the third-party could opt-out and prosecute their claims in state or federal court. However, some bankruptcy courts may not want to implement such a measure because it could deter nondebtor participation and decrease willingness to contribute to the plan. Applying the "best interests" test would be a safe alternative to ensure that nonconsenting creditors are not receiving a worse deal than they would if they had the option to opt-out of the release. Suppose it is a close calculation and the possibility exists that the nondebtor is using the system to gain an advantage over claimants. In that case, bankruptcy courts could reject the plan and force nondebtors to contribute more assets to the plan.[260] After all, granting nondebtors relief from liability only becomes a problem where the relief comes to claimants' detriment.[261] As Simon explains, "[a]ssuming claimants receive approximately equal process and substantive remedies, permitting access to chapter 11 likely reduces overall litigation spending and increases the money that goes directly to claimants."[262]

CONCLUSION

Nondebtor releases are controversial. This controversy is multi-layered, as illustrated by this Article's discussion of the constitutional, statutory, due process, and fairness concerns surrounding the issue. The public's visceral reaction to the bankruptcy court's initial confirmation of the Sackler release has helped to propel the issue to discussion in the halls of Congress, but the best approach is likely not to eliminate the practice completely. While the practice has led to inequitable

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256 *See* Simon, *supra* note 29, at 1212.
257 *See id.*
258 *Id.*
259 *See id.*
260 *See* Simon, *supra* note 29, at 1214.
261 *Id.*
262 *Id.*

results, the *Takata* bankruptcy and Judge McMahon's reversal of the Sackler releases show that the system is not beyond repair and given the right protections in place, we should be able to make the chapter 11 process work for all involved. The efficiency provided by chapter 11 does not have to come at the expense of claimants. With the right guardrails throughout the process, bankruptcy courts can ensure that the benefit of a global resolution to mass tort cases in bankruptcy does not affect the rights of claimants in a negative or inequitable way. However, as long as third-parties are allowed to operate under a different set of rules in chapter 11, we can expect to see nondebtors like the Sacklers continue to play the hand they are dealt in such a way that maximizes self-interests without regard for the effect it has on claimants.