LAW360 Insurance Authority

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3rd-Party Release Case Looms Over Ch. 11 Mass Tort Claims

By **Abraham Gross**

Law360 (August 30, 2023, 6:25 PM EDT) -- Following the U.S. Supreme Court's decision to review the nonconsensual liability releases against the Sackler family in Purdue Pharma's Chapter 11 plan, insurance experts warn that the justices' decision could undermine a method for resolving insurance coverage issues involving mass torts.

Restricting the use of nonconsensual releases could have downstream effects for coverage disputes in mass tort cases like those that have embroiled Purdue Pharma in its Chapter 11 plan, insurance experts said. (AP Photo/Mark Lennihan, File)

The court on Aug. 10 **granted** the U.S. Trustee's Office's request to pause Purdue Pharma LP's Chapter 11 plan and asked the parties to explain whether the courts can approve a reorganization plan that includes nonconsensual releases of opioid-related claims against nondebtor third parties, like the company's former owners in the Sackler family, as part of the bankruptcy proceeding.

Third-party nonconsensual releases — which free nondebtor parties from liability to other nondebtor parties without the consent of all potential claim holders — have been controversial for decades.

The bankruptcy code explicitly authorizes these kinds of nonconsensual releases only with bankrupt entities facing claims related to harms from asbestos. Given the court majority's textualist bent, bankruptcy experts are concerned that the justices **might limit the tool's use**.

Insurance experts told Law360 that restricting the use of nonconsensual releases could have downstream effects for coverage disputes in mass tort cases like those that have embroiled Purdue, while noting that insurers had other tools at their disposal.

Mass tort claims are particularly challenging for insurers and policyholders alike. From opioids and asbestos to sexual abuse claims, mass tort claims can often stretch across multiple policy years and push limits to their breaking points. The sheer volume of individual claims can rocket costs above even the tallest policy towers.

Bert Wells of Covington & Burling LLP, who represents policyholders, told Law360 that bankruptcy often serves as the arena for aggregating mass tort claims because the costs of such claims can precipitate a company's bankruptcy. Administering rather than litigating numerous claims is often a cheaper option, he said.

"When you're dealing with mass torts, for example, where claimants are either extremely numerous — or maybe more significantly, haven't even all been identified yet — the availability of a bankruptcy-style release for third parties creates the possibility of resolving all their liabilities for a given matter in one moment," he said.

The upshot of providing insurers with a sense of finality from existing and future claims and litigation costs incentivizes carriers to participate in bankruptcy proceedings and provide payments to policyholders and others, Wells said.

"The possibility that a defendant could get a release with respect to all known and unknown claims of a certain type makes it much easier to get the insurers' agreement to fund a settlement and to provide its top dollar for the insurance that it has exposed to those risks," he added.

Nonconsensual releases do not always offer insurers a sweet deal, and can pit different insurers against each other.

In September, more than a dozen insurers **appealed** the Chapter 11 plan of the Boy Scouts of America, **telling the Third Circuit** that the plan that created a $2.5 billion settlement trust for hundreds of sexual abuse claimants impermissibly altered the carriers' contractual rights.

The insurers argued that the district and bankruptcy courts disregarded Third Circuit law by confirming a plan that failed to preserve the insurers' contractual rights to defend themselves against abuse claims, seemingly transferring the Boy Scouts' contractual rights under the policies to the trust without a similar transfer of obligations.

Inter-insurer disputes are made likelier in mass tort cases by both the volume of policies implicated and the different forms of coverages that are available — facts that further complicate bankruptcy proceedings.

Mass torts more often ensnare general liability policies, but specialty lines like directors and officers or professional liability policies are not always out of reach, said Michael Manire, a partner with Manire Galla Curley LLP, who represents insurers.

"All of these disputes can and typically do sweep around and pick up insurance coverage," he said. "It's not just who gets the money, but also whether the money is available, and if so, how much."

In an Aug. 17 ruling for North Carolina Mutual Wholesale Drug Co., U.S. District Judge Catherine C. Eagles **rejected** Federal Insurance Co.'s arguments that contract and professional services exclusions in its directors and officers policy barred coverage for opioid litigation against the company.

Policyholder attorneys have said that the decision indicates that insurers **will find it difficult** to argue for broad readings of similar exclusions that would deny coverage to policyholders facing opioid litigation.

Manire pointed out that receiverships, which often share certain similarities with bankruptcy but are overseen by district courts, have also faced challenges to the use of nonconsensual liability releases.

In February, the Sixth Circuit decided in Digital Media Solutions LLC v. South University of Ohio LLC that a district court exceeded its authority when it authorized a settlement prohibiting third parties from

pursuing claims against the directors and officers of an education nonprofit in receivership. The appeals court, however, noted that courts can control payouts from D&O policies if those proceeds were the property of entities in receivership.

Experts shared concerns that if the justices limited the use of nonconsensual releases to asbestos cases, it would remove a potent tool for insurers and policyholders to resolve mass tort claims. What remains in doubt is the extent that the court's ruling would practically alter how those claims are managed in future bankruptcy disputes.

"There's so many claims, limited assets, limited resources and so many conflicting interests with respect to those resources that, without that tool, one would think there'd be more litigation, [and] litigation takes longer to resolve," Manire said.

Wells qualified his prediction that limiting releases may make resolutions more challenging by noting that bankruptcy proceedings are a limited venue and would have little impact on entities that are not themselves in bankruptcy proceedings or affiliated with such entities.

The impact of limiting nonconsensual releases would be muted even in the bankruptcy context because insurers still have other options for insulating themselves, Todd Padnos of Sheppard Mullin, who represents insurers, told Law360.

One common method is a policy buyback, in which the insurer effectively purchases its coverage from the bankrupt entity as an asset and is released from claims under the policy in exchange for a one-time payment into a settlement fund.

If deemed an asset sale made in good faith under Section 363 of the bankruptcy code, policy buybacks can provide insurers a more expedient and potentially cheaper route to seek protection from claims against the bankrupt company than an injunction would offer.

A buyback offers more limited protection, effectively extinguishing the insurer's liability under the policy covering claims based on the policyholder's conduct, while a release of the insurer can possibly shield the insurer from liability for the insurer's own acts, such as insurance bad faith claims, according to Padnos.

"The downside or risk is that someone may attempt to bring a direct claim against the insurer after confirmation of a plan, saying that you still have exposure under those policies, but that strikes me as a relatively low risk," he said.

Still, Padnos said it is unlikely that maintaining a broad application of nonconsensual releases will alter insurer practices significantly.

"At the end of the day, would it be helpful for insurance companies, would it give greater flexibility? Possibly, yeah. Is it going to move the needle in terms of underwriting and pricing? I'm not so sure," he said.

--Additional reporting by Hope Patti, Henrik Nilsson, Daniel Tay and Ganesh Setty. Editing by Bruce Goldman and Nick Petruncio.

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