JOHN BATES, JOHNS MANVILLE, THE BOYSCOUTS OF AMERICA, AND JOHNSON & JOHNSON

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The convergence of two cases from half a century ago is allowing trial lawyer vultures to destroy our bankruptcy system in cases involving some of the most storied names in America.

The bankruptcy system feels like it is coming apart at the seams. There have been a litany of stories in recent years demonstrating how trial lawyers have turned the bankruptcy process upside down.[1] And I have written before in these pages about how mass tort trial lawyers were running a shake down inside the bankruptcy system, capturing leverage once companies enter bankruptcy.[2] But the recent events surrounding Johnson & Johnson's second failed attempt at putting its LTL subsidiary into bankruptcy in response to a wave of a tort claims over talc products is showing that mass-tort trial lawyers have also figured out how to capitalize on the bankruptcy rules and statutes to convince courts to keep companies out of bankruptcy and keep the mass-tort gravy train running when the trial lawyers deem it more to their liking.

The ability of personal-injury trial lawyers to game the system coming and going—feasting on cases in bankruptcy while blocking cases like Johnson & Johnson/LTL from bankruptcy—is an existential problem for the system. Yet there is little evidence that bankruptcy judges, practitioners, or even most companies are taking the threat seriously enough. That needs to change, especially if we are going to allow bankruptcy courts to be used to solve societal issues. We can make the bankruptcy system more resilient to this threat, giving it a chance of serving its important role and not just being a captured province of the mass-tort empire. But it is time to wake up and get moving before trial lawyers entrench themselves and gain effective control over more billion-dollar gold mines.

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[1] *See, e.g.*, Philip Goldberg, *How Mass Tort Litigation Is Gaming the Judicial System*, BLOOMBERG LAW (March 2, 2023), https://news.bloomberglaw.com/us-law-week/how-mass-tort-litigation-is-gaming-the-judicial-system; Lawrence A. Friedman, *Reforming Corporate Bankruptcies to Stop the Mass Tort Shakedown*, BLOOMBERG LAW (April 25, 2022), https://news.bloomberglaw.com/bankruptcy-law/reforming-corporate-bankruptcies-to-stop-the-mass-tort-shakedown-16; The Editorial Board, *Looting the Boy Scouts*, WALL ST. J. (March 2, 2021), https://www.wsj.com/articles/looting-the-boy-scouts-11614728612.

[2] Lawrence A. Friedman, *Corporate Bankruptcy Gets A Shakedown From Mass Tort Trial Lawyers*, HARV. J.L. & PUB. POL'Y: PER CURIAM (Spring 2022, No. 7), https://journals.law.harvard.edu/jlpp/corporate-bankruptcy-gets-a-shakedown-from-mass-tort-trial-lawyers-lawrence-a-friedman/.

I. JOHNSON & JOHNSON & LTL

Johnson & Johnson has been beset by a wave of lawsuits over talc products, with the drama featuring all the trappings one would expect of the most savage and high-stakes game of mass-tort litigation: trial lawyers piling lawsuits on top of lawsuits, the removal of talc products from the United States and global markets, a Johnson & Johnson lawsuit against doctors over studies that linked talc-based products to cancer, and nonstop media attention.[3]

Johnson & Johnson has been attempting to conclusively resolve these tort claims by spinning off their tort liabilities to a subsidiary (LTL), with the intent of putting it into bankruptcy.[4] The theory, known as the Texas two-step, involves creating a subsidiary, transferring the tort liabilities to that subsidiary, and then agreeing to fund the subsidiary with insurance proceeds and/or assets sufficient to pay tort claimants.[5] The goal, from Johnson & Johnson's perspective, has been to try and reach an end to the talc war with the mass-tort trial lawyers and to do so with less money on the table than the mass-tort lawyers might otherwise necessitate with their fully operational shake and bake machinery.

The trial lawyers weren't so pleased. But they also sensed an opportunity. If they could force dismissal of the LTL bankruptcy case, and bar the door to bankruptcy court at least for the time being, they could force Johnson & Johnson to a negotiating table on weaker terms.

And sure enough, mere hours after the United States Court of Appeals for the Third Circuit reversed the initial bankruptcy court ruling and dismissed LTL's first bankruptcy as a bad faith filing, LTL renegotiated with the various groups of trial lawyers and filed a second bankruptcy case, in which Johnson & Johnson promised to pay some $9 billion, nearly 4 times what they offered in the first case.[6] Just like the mass tort-trial lawyers effectively gamed the system in the Boy Scouts of America bankruptcy to the tune of multiple billions in their favor—something that very well could be in the cards for the LTL case if it is allowed to proceed—we now see that the LTL bankruptcy has turned into a trial lawyer plaything, with the trial lawyers driving the ship and singing the tune at key procedural turns, all while their ledgers swell and almost every other player in the drama suffers.

In short, Johnson & Johnson/LTL, coming so soon after the Boy Scouts of America debacle, lays out in full display how trial lawyers have managed to exert influence over the bankruptcy

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[3] *See, e.g.*, Suryatapa Bhattacharya, *Johnson & Johnson Sues Doctors Over Studies Linking Talc-Based Products and Cancer*, WALL ST. J. (July 13, 2023), https://www.wsj.com/articles/johnson-johnson-sues-doctors-over-studies-linking-talc-based-products-and-cancer-78ffd2a7; The Editorial Board, *Why Lawyers Love Jackpot Talc Litigation*, WALL ST. J. (September 25, 2022), https://www.wsj.com/articles/why-lawyers-love-jackpot-talc-litigation-johnson-and-johnson-talcum-powder-lawsuits-tort-lawyers-11663965125; Talal Ansari, *J&J to Stop Selling Talc-Based Baby Powder Globally Next Year*, WALL ST. J. (August 11, 2022), https://www.wsj.com/articles/j-j-to-stop-selling-talc-based-baby-powder-globally-next-year-11660258047; James R. Copland, *Johnson & Johnson Takes A Powder*, WALL ST. J. (May 22, 2020), https://www.wsj.com/articles/johnson-johnson-takes-a-powder-11590167907.

[4] *See, e.g.*, David Goldman, *Johnson & Johnson is again trying to use bankruptcy to settle talc cases for $8.9 billion*, CNN (April 4, 2023), https://www.cnn.com/2023/04/04/investing/johnson-and-johnson-talc-bankruptcy/index.html.

[5] Charlie Hu, *Court Rejects Johnson & Johnson's Use of the "Texas Two-Step" to Tackle Baby Powder Liability*, U. CHI. BUS. L. REV. (Online Edition 2023), https://businesslawreview.uchicago.edu/online-archive/court-rejects-johnson-johnsons-use-texas-two-step-tackle-baby-powder-liability.

[6] See, e.g., David Goldman, *Johnson & Johnson is again trying to use bankruptcy to settle talc cases for $8.9 billion*, CNN (April 4, 2023), https://www.cnn.com/2023/04/04/investing/johnson-and-johnson-talc-bankruptcy/index.html.

process on the front end and the back end, ensuring that mass-tort bankruptcies are starting to look like trial lawyer playthings rather than a well-functioning part of our legal system.

II. THE ROAD HERE: MANVILLE AND BATES

It seems fair to ask how we got here in the first place, and why bankruptcy judges buy into any of this chicanery. And the answers lie in part in two cases from half a century ago.

The year was 1977. A young lawyer named John Bates sought to build a practice offering low-cost services to middle America. And he set about to do so by advertising various legal offerings, such as uncontested divorces, wills, and other (primarily process-based) mass-market consumer offerings.[7]

The State Bar of Arizona objected to this and sought to discipline young Mr. Bates for violating ethics rules that prohibited lawyers from advertising. Mr. Bates argued that the ban on attorney advertising violated his first amendment rights. The Bar argued that allowing attorney advertising would be "inherently misleading," negatively affect the "administration of justice," have "undesirable economic effects," harm the quality of legal services, and be difficult to police.[8]

The State Bar of Arizona lost. The Supreme Court of the United States held that attorney speech was commercial speech protected under the first amendment. Further, the restriction on any attorney advertising had "served to burden access to legal services, particularly for the not-quite-poor and the unknowledgeable."[9]

Enter Johns Manville, a maker of construction materials that contained asbestos, subjecting them to some 16,000 lawsuits. In 1982, facing a wave of lawsuits, Johns Manville filed bankruptcy. While Johns Manville's operation was not per se insolvent, the company had a major problem: insurers had been denying coverage even as the company faced the current wave of lawsuits and those to be expected from future plaintiffs whose claims might ripen in the coming years. By filing bankruptcy, Johns Manville was able to draw those insurance policies into the bankruptcy estate and use them to help fund trusts to which future claimants would look for compensation, essentially forcing value from the insurance contracts and dealing with the problem of future claimants, thereby making confirmation of a final bankruptcy plan possible and allowing the company to move its operations past the wave of lawsuits it was facing.[10] Problem solved from Manville's perspective.

Following in the footsteps of Johns Manville, corporations now use bankruptcy to tap insurance policies to fund trusts that serve as the source of payment for current and future tort victims. But the rules of bankruptcy were not designed to address mass torts. And if you add in a healthy dose of attorney advertising you reach the point where *Manville* and *Bates* collide.

Yet this straightforward collision of *Bates* and *Manville* on its own could not cause the chaos we are seeing in the current mass-tort cases. After all, for nearly 50 years we didn't see the kinds

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[7] Bates v. State Bar of Arizona, 433 U.S. 350, 350 (1977).

[8] *See, e.g.*, *id.* at 372.

[9] *Bates*, *id.* at 376.

[10] *See, e.g.*, David Skeel, *Purdue Pharma's Bankruptcy Heads to the Supreme Court*, WALL ST. J. (August 27, 2023), https://www.wsj.com/articles/purdue-pharmas-bankruptcy-heads-to-the-supreme-court-asbestos-sackler-trust-90d810a4.

of problems that exist today. Agent Orange litigation was in the 1970s. Asbestos was in the 1980's. And these helped generate the silicone breast implant and tobacco cases in the 1990s without generating the kind of situation we see now.

III. THE QUAINTNESS OF MR. BATES: MASS TORT IN THE DIGITAL AGE

Fuel was needed to cause the explosion in claims which are now threatening our bankruptcy system. That fuel was technology.

Today we live in the digital age, and we're headed quickly into the virtual world of artificial intelligence. And mass-tort lawyers are wasting no time in enlisting the most modern methods for generating claims and pushing the envelope on attorney advertising.

The attorney advertising of the *Bates* era seems so quaint in retrospect. I grew up in the 1970s. Seat belts were only recently required (1966). Headlight dimmer switches were found on the floorboard of cars. Only 50% of radio listeners tuned into FM stations, and touch-tone phones were just showing up in homes. Key punch machines were the backbone of billing systems and personal computers were still a decade away. Attorney advertising was seen only in the classified section of your local newspaper or by those who stayed up to watch the late show after Johnny Carson, and by 2 am every TV station had signed off until morning.

Mass-tort lawyers have moved far beyond this quaint world. They use lead-generation software that integrates consumers' own information with public information to target consumers (search for anything relating to a mass tort case or topic and watch over the next few days how every search you perform, every Facebook thread you peruse, every article you look at, and every streaming service you listen to, is suddenly filled with targeted trial lawyer advertising directed specifically at you). And that is only the beginning. Once they trigger a click with one of these advertisements – you clicked because you were casually interested, perhaps – you then get the full onslaught of the seal-the-deal machinery. And if you enter the sign-up rabbit hole but then decide to head for the exit? Well, that is when the wave of "save the sale" software maneuvers come out—the same algorithms that kick in on consumer websites when you move away from a potential purchase now kick into gear to lock you in as a law firm's client, signing over a massive portion of a potential legal claim as if it were equivalent to picking out a new set of jeans.[11]

IV. CORPORATE BANKRUPTCY'S SPECIAL RULES MAKE FOR UNIQUE MASS-TORT SUSCEPTIBILITY

The success of the corporate bankruptcy process is driven in part by rules that were designed to make the reorganization process efficient. At its core the corporate reorganization process is all about restructuring the company in a manner that maximizes its value and then redistributes

[11] Judge Land of the U.S. District Court for the Middle District of Georgia was the first high-profile jurist to prominently call out these dynamics. In 2016, while administering an MDL over mesh medical devices, he found most claims stockpiled in his MDL "should never have been brought in the first place," as they were "fueled" by television solicitations, filed "with so little pre-filing preparation," and couldn't "stand on their own merit." *See* Philip Goldberg, *How Mass Tort Litigation Is Gaming the Judicial System*, BLOOMBERG LAW (March 2, 2023), https://news.bloomberglaw.com/us-law-week/how-mass-tort-litigation-is-gaming-the-judicial-system.

that value efficiently to creditors (employees, bondholders, and so on), thus staving off liquidation; the goal is a confirmed plan, with other considerations taking a backseat. To that end, bankruptcy courts rely on a concept that claims filed in a case are deemed allowed - subject to review later – and thus are eligible to vote for or against confirmation of a plan of reorganization. Typically, these claimants are unsecured creditors who have provided goods or services to the company but have not been paid. In larger cases an unsecured creditors committee is appointed to act as a voice for all unsecured creditors. These committees investigate the financial affairs of the debtor, pursue certain actions within the case, and play an important role in the reorganization of the debtor.

In the mass-tort cases, damages incurred by victims are the vast majority of unsecured claims. These unsecured claims become a numbers game. Unlike the typical corporate case where unsecured creditors are generally known and listed in the company's books, in the mass-tort case they are usually unknown at the outset of the bankruptcy proceedings. The more of these claims a party controls, the more that party can influence the direction and outcome of the case. You don't need a law degree to understand the free-for-all this creates. Control enough claims, control the case. And with no guard rails in place to determine the validity and amount of these claims, the process is especially ripe for gaming by the same people who have perfected digital claim generation and client sign-up tools for their other purposes.

The tactics the personal injury lawyers use to manipulate the bankruptcy process include sophisticated lead-generation algorithms that promise lottery-ticket sized payouts and then ensure that potential claimants stay locked into the process for as long as necessary. I reviewed a sampling of solicitations on the web for those wondering if they may have a claim against Johnson & Johnson for talc-related issues. Preliminary questions suggest that if you or a family member has been diagnosed with cancer you may have a claim.[12]

The strongest recent example of this operation in action inside a bankruptcy case is the Boy Scouts of America Bankruptcy, where mass-tort trial lawyers swamped the case and took control of much of the plan negotiation, to the benefit of themselves and to the detriment of the initial set of seemingly deserving victims.[13] When the Boy Scouts of America bankruptcy case was first filed, there were a few hundred tort cases pending. Boy Scouts of America estimated that there may be a total of some 2,000 claims which would be filed in the case. After ramping up their claims-generating machine, the mass-tort lawyers eventually filed some 80,000 claims in the bankruptcy. That ended up increasing the size of the overall pot for these lawyers to $2.4 Billion.

[12] Of particular note is the consent the consumer is required to sign agreeing to be contacted including by email, telephone (including phone calls, text messages, autodialed/auto-selected or pre-recorded calls. *See, e.g.*, Pintas & Mullins, P.R., Free ClaimReview, https://www.ovariansettlements.com/?utm_source=google&utm_medium=PPC&utm_campaign=14817830815&utm_content=SL2&PN=8007497444&gclid=CjwKCAjwrranBhAEEiwAzbhNtVXQW6F35El0btQUXbxrKncq1CeUJG-SNkcblX0gdn5ewHDb7jRZyxoCcAYQAvD_BwE.

[13] *See, e.g.*, Lawrence A. Friedman, *Reforming Corporate Bankruptcies to Stop the Mass Tort Shakedown*, BLOOMBERG LAW (April 25, 2022), https://news.bloomberglaw.com/bankruptcy-law/reforming-corporate-bankruptcies-to-stop-the-mass-tort-shakedown-16; The Editorial Board, *Looting the Boy Scouts*, WALL ST. J. (March 2, 2021), https://www.wsj.com/articles/looting-the-boy-scouts-11614728612.

And the same maneuvers are rearing their heads in the Johnson & Johnson/LTL cases, with groups of lawyers teaming up with doctors to link various cancers to the use of talc, foment a swarm of cases in private litigation, and separately gin up a pool of some 16,000 claims in order to object to the bankruptcy petition.[14]

V. THE ROAD AHEAD: STOPPING THE ABUSES AND HELPING VICTIMS

Make no mistake, there is a real problem here. Corporate bankruptcy reorganization is about dividing the limited assets of a distressed company. It cannot be allowed to remain a trial lawyer toy.

One systematic way to respond to the problem here is legislation from Congress. Congress could pass legislation to try and force disclosure of how claims are generated and otherwise more aggressively regulate the full-scale sales operations that the mass tort trial lawyers use to run their gambit in and around these bankruptcy cases. But, as recent events in Congress have demonstrated, the path forward for any substantive, non-mandatory legislation, particularly judicial reform legislation, is questionable; passing the Bankruptcy Abuse Prevention and Consumer Protection Act in 2005 took nearly 10 years during a different time in terms of congressional cooperation and ability to forge bipartisan consensus around reforms to courts.

Another potential avenue for structural reform would be action through the Judicial Conference's Committee on Rules of Practice and Procedure. The rules could be changed to require more up-front disclosure and heightened certification requirements for the lawyers (and others, as the case may be) who help file claims in the bankruptcy process on behalf of tort claimants. The Rules Enabling Act, 28 U.S.C. §§ 2071-2077, authorizes the Supreme Court of the United States to prescribe general rules of practice and procedure for the federal courts, including the bankruptcy courts. Related to this authority is the power that Bankruptcy Rule 9009 gives to the Judicial Conference to prescribe the official forms that, pursuant to the Rule, shall be used in federal bankruptcy proceedings without alteration (except as otherwise provided in the bankruptcy rules, in a particular Official Form, or in the national instructions for a particular Official Form).[15]

Changing the pertinent Bankruptcy Rules themselves to heighten oversight of the claim-generation process—for example, by requiring that third-party providers employed by mass-tort trial lawyers be retained subject to an order of the bankruptcy court (like any other professional employed in furtherance of the bankruptcy), with the estate as the locus for payment and therefore greater transparency—would be a two- to three-year process (likely as a complement

[14] *See, e.g.*, Suryatapa Bhattacharya, *Johnson & Johnson Sues Doctors Over Studies Linking Talc-Based Products and Cancer*, WALL ST. J. (July 13, 2023), https://www.wsj.com/articles/johnson-johnson-sues-doctors-over-studies-linking-talc-based-products-and-cancer-78ffd2a7; Evan Ochsner, *J&J Uses Cajoling, $9 Billion Offer to Sell New Talc Bankruptcy*, BLOOMBERG LAW (April 27, 2023), https://news.bloomberglaw.com/bankruptcy-law/j-j-uses-attorney-cajoling-8-9b-to-sell-new-talc-bankruptcy ("J&J says the settlement now has the purported support of up to 80,000 claimants, including about 16,000 who are represented by a lawyer, Mikal Watts, whose role in the case grew in recent months.").

[15] Permitted Changes to Official Bankruptcy Forms, UNITED STATES COURTS, https://www.uscourts.gov/rules-policies/about-rulemaking-process/permitted-changes-official-bankruptcy-forms [https://perma.cc/A5PS-UBUC].

to updates to the Official Forms, as discussed below).[16] The Advisory Committee on Bankruptcy would evaluate the proposal in the first instance, seek permission from the full Judicial Conference's Committee on Rules of Practice and Procedure, better known as the Federal Rules Committee, to publish a draft of any contemplated amendment that the Advisory Committee thought worth pursuing, and then choose ultimately to transmit the amendment as contemplated to the full Federal Rules Committee (or not) based on comments from the bench, bar, and general public. The Federal Rules Committee would then independently review the findings of the Advisory Committee and, if satisfied, recommend changes to the Judicial Conference itself, which in turn would recommend the changes to the Supreme Court of the United States (or not), at which point the Supreme Court would consider the proposal and ultimately be the entity to promulgate any change to the pertinent rules.

There is also a complementary path that the Federal Rules Committee could follow while full-scale rule changes were in process: changing the Official Forms for the federal bankruptcy proceedings. This is how the Federal Rules Committee tackled some meaningful reform efforts when I was an *ex officio* member during my tenure as Director of the Executive Office for United States Trustees. In the aftermath of the high-profile National Mortgage Settlement, the Federal Rules Committee revamped the official proof-of-claim form for mortgage debts, changing how the official form addressed deficiencies and how claims that might change based on contractual language are treated in the filing process—for example, mortgage claim holders must now give notice in the bankruptcy case in advance of any change in the amount of the monthly claim amount.[17] Similarly, after the Supreme Court held that the Fair Debt Collection Practices Act did not apply to the filing of a proof of claim form in bankruptcy in *Midland Funding, LLC v. Johnson*,[18] the Federal Rules Committee revamped the official proof-of-claim form to require a prominently placed clear statement disclosing that the debt may be subject to legal defenses. In both these instances, the changes to the Official Forms added additional requirements, disclosures, and detail in the initial claim-filing process to serve an information-forcing function and add transparency and trust to the system where it might have been lacking before. This same approach could be deployed in a matter of months in response to the current mass-tort problems, with real systematic benefits.

Yet another expedient and meaningful option for addressing the real concerns here would be for bankruptcy judges to increase transparency through proactive appointment of claims examiners. Bankruptcy judges can do this right away. They have the power to appoint claims examiners pursuant to 11 U.S.C. § 1104. And this would not be a wholly novel approach. The use of examiners has grown dramatically since the United States Trustee Program sought the use of them in Enron, WorldCom, and Adelphia, and the appointment of examiners for particular matters within an ongoing bankruptcy proceeding (such as examiners to shed light on fees sought by all professionals in a case) is not uncommon. Examiners can serve many purposes, but the common theme is that they do not work to fully adjudicate questions in their topic area, but

[16] About the Rulemaking Process, UNITED STATES COURTS, https://www.uscourts.gov/rules-policies/about-rulemaking-process [https://perma.cc/N42G-94EJ].

[17] *See, e.g.*, Bankruptcy Rule 3002.1, Notice Relating to Claims Secured by Security Interest in the Debtor's Principal Residence, and 2011 Committee Notes on Rules.

[18] 137 S. Ct 1407 (2017).

instead perform an investigative function and file detailed reports regarding the matters they were tasked with investigating. These reports serve many beneficial purposes. For example, they help consolidate key information, aiding with eventual discovery and other related reviews, including any involvement by other departments within agencies like the Department of Justice and the Securities and Exchange Commission. And, perhaps most importantly, the examiner reports, which can often be multi-volume affairs, pull back the curtain to shine light on what is actually happening in the bankruptcy proceedings or what precipitated the debtor's insolvency.

The appointment of claims examiners in cases where large numbers of tort claims are swirling around the initiation or conclusion of a bankruptcy proceedings would shed light on who is driving the bankruptcy and who should have a say in the resolution of the proceedings. A claims examiner is the best way to sift through the mess that mass tort trial lawyers are making of cases in and around bankruptcy. And it could be a powerful way to figure out if mass tort lawyers are running a gambit to a keep a company out of bankruptcy for their own benefit. Put simply, the increased transparency that systematic use of claims examiners would drive is exactly what is needed to help tamp down and dissuade future abuses.

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The problems creeping into corporate bankruptcy because of mass tort trial lawyers are serious. The damage to victims and other creditors is real. And it is crucial that the bankruptcy world respond in short order lest our beloved corner of the legal world succumb to the mass-tort trial lawyers and become a mere vassal state where the trial lawyers control things from start to finish and real victims get crushed in a mass-tort gold rush that imposes huge costs and takes massive value out of a system that is meant to divide the limited assets of a distressed company.

Courts, judges, and other public officials should act now to increase transparency, expose the forces behind the problems, and respond in an appropriate fashion. So far, as the Johnson & Johnson/LTL and Boy Scouts of America cases illustrate, there is little evidence that judges and practitioners are taking the threat seriously enough. That needs to change, especially if we are going to allow our bankruptcy courts to be used to solve societal issues. We can make the bankruptcy system more resilient to this threat, giving it a chance of serving its important role and not just being a captured province of the mass-tort empire. But it is time to wake up and get moving.