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The Significance Of Travelers V. Bailey

Law360, New York (May 08, 2009) -- A case currently before the United States Supreme Court could set the framework for asbestos litigation in the 21st century.

Specifically, the court is considering *Travelers Indemnity Co. v. Bailey*,^[1] a case that concerns the relationship between Johns-Manville Corporation and its former primary insurer from 1947 – 1976, Travelers Indemnity Company.

Although Manville is immune from suit because it filed for bankruptcy in 1982, the Bailey plaintiffs are asserting direct causes of action against Travelers alleging that Travelers tortiously conspired with Manville to prevent the dissemination of information concerning the adverse health effects of asbestos.

The court's decision could impact the areas of bankruptcy, insurance and mass torts. A decision against Travelers likely means insurers will be hesitant to settle any case because they will not have an assurance of finality, as lawsuits will never end if these types of "independent" claims against insurers are possible.

The Manville Bankruptcy

Manville was the largest producer of raw asbestos in the world by 1970. "Fundamentally, the story of asbestos health litigation is the story of Johns-Manville."^[2]

As the bankruptcy court noted at the time, "there are no industries from which claimants originate where Manville did not provide asbestos products — either manufactured or raw materials."^[3]

Given Manville's ubiquity in the asbestos business, it "was named in virtually every asbestos-related personal injury or wrongful death action filed in the United States."^[4]

Travelers paid for Manville's defense of asbestos suits until the company's bankruptcy filing in 1982. Indeed, the time and resources allocated to the defense of these suits

was so massive that Travelers formed a dedicated “Asbestos Unit” — its sole responsibility being to coordinate and “centralize all litigation against the company’s insureds [facing asbestos liability].”[5]

It is the knowledge and experience about asbestos that Traveler’s gained from defending Manville in this context that ultimately serves as the underlying basis for the tort claims in Bailey.[6]

Manville filed a Chapter 11 petition for reorganization on Aug. 26, 1982.[7] The bankruptcy court had to craft a reorganization plan for Manville that took into account all present and future asbestos victims that would have claims against the debtor’s estate “using only the broken shards of a Fortune 500 company that had been crushed by the weight of a century-long entanglement with asbestos.”[8]

One of the largest and most important assets in the debtor’s estate was the insurance policies that Manville owned, although Manville was entangled in numerous insurance coverage disputes because its insurers had denied some of the asbestos claims.

The bankruptcy court persuaded the insurance companies, including Travelers, to resolve their disputes with Manville so that the court could use the insurance monies.

To alleviate the insurers concerns about future suits, the bankruptcy court issued several injunctive orders barring future claims. The assurances by the bankruptcy court and the corollary injunctive orders allowed multiple insurers to settle with Manville for approximately \$770 million; monies that were ultimately placed in a trust and are now used to compensate present and future Manville asbestos claimants.[9]

The injunction that precluded any further direct action suits against Travelers was codified in a 1986 confirmation order, which “permanently enjoin[ed] ‘all persons’ from commencing any action against any of the settling insurance companies ‘for the purpose of directly or indirectly, collecting, recovering or receiving payment of, on or with respect to any claim ... or other asbestos obligation ...”[10]

As a result of this injunction, any suits that normally would have been brought against Manville’s insurers based on an insurance policy were enjoined and the claims were channeled to a Trust created specifically to compensate future Manville asbestos claimants.[11]

The Bailey Case

The Bailey plaintiffs asserted claims directly against Travelers, alleging that through its 29-year relationship as Manville’s primary insurer, Travelers conspired with Manville to hide the health effects of asbestos.

Travelers maintains that the 1986 Confirmation Order expressly precludes this suit. Conversely, the plaintiffs assert that direct action suits such as this are independent

causes of actions based on Travelers own tortious conduct and not directly related to the Manville insurance policies.[12]

The bankruptcy court held that the suit was barred, relying on the Second Circuit's 1988 decision in *MacArthur Co. v. Johns-Manville Corp.*, which held that a direct attack on Manville's insurers arising under the policies it underwrote was precluded because the policies were assets of the debtor's estate.

Despite the differences between the causes of action asserted by the MacArthur plaintiffs and causes of action asserted by the Bailey plaintiffs, the bankruptcy court held that it had the ability to enjoin any further suits against Travelers based on its relationship with Manville.

The court then issued a clarification order stating that any further suits predicated on Travelers' relationship with Manville were enjoined.

Plaintiffs and Travelers' co-defendants, who were sued under the same conspiracy theories, challenged the bankruptcy court's authority to enjoin any further suits against Travelers.[13]

The district court affirmed the ruling. In upholding the majority of the bankruptcy court's clarification order, the district court relied on the language of the original 1986 settlement order that stated:

All persons are permanently restrained and enjoined from commencing and/or continuing any suit, arbitration or other proceeding of any type or nature for policy claims against any or all members of the settling insurer group [which includes Travelers Indemnity Company and its affiliates] ... [14]

Based on this language, the district court concluded that "[t]he direct action suits are actions against one of the 'settling insurance companies' to receive payment on an 'other asbestos obligation' and [are] thus barred by the confirmation order as well." [15]

The Second Circuit, however, vacated the district court's affirmance on Feb. 15, 2008.[16] In so holding, the court of appeals stated that "while there is no doubt that the bankruptcy court had jurisdiction to clarify its prior [1986] orders, that clarification cannot be used as a predicate to enjoin claims over which it had no jurisdiction." [17]

In making this determination, the Second Circuit analyzed its prior holding in *MacArthur* and explained that the plaintiff's "rights as an insured vendor are completely derivative of Manville's rights as the primary insured," and thus, the coverage claim affected a principal asset of the debtor's estate.[18] Therefore, the bankruptcy court's 1986 channeling injunction precluded *MacArthur's* suit directly against Travelers.

In Bailey, however, the Second Circuit drew a distinction between the causes of action asserted in MacArthur and the causes of action asserted in the present case, as the present causes of action were independent tort claims brought against Travelers.

The Second Circuit found that the tort claims asserted in Bailey did not touch upon the insurance policies. Thus, the court believed that the question to be answered was whether the causes of action asserted against Travelers sought to recover for Manville's misconduct or were based on an independent legal duty that Travelers owed to the plaintiffs, irrespective of the factual nexus between the Manville and Travelers.[19]

The Supreme Court

The Supreme Court heard oral argument in Bailey on March 30, 2009. The Justices asked numerous questions concerning the scope of the bankruptcy court's subject matter jurisdiction. Many other questions focused on the practical effect of the court's ruling. Indeed, as Justice Breyer aptly noted in a question to the asbestos claimants' counsel:

You will never get insurance companies to go into this kind of [settlement] if they are going to be sued for the very act of helping the debtor defend the asbestos cases. And so, I can't imagine an insurance company in its right mind going into [a settlement] when in fact all these suits are still open. That is presumably what the bankruptcy judge cut off.[20]

Ultimately, the justices seemed to recognize that the bankruptcy court's authority to enjoin suits against non-debtors has its limits. That said, the causes of actions asserted against Travelers were questioned.

As Justice Stevens stated: "I don't understand — I can't figure out why anybody expects to collect from Travelers for what they did. The fact that they defended cases certainly was — was proper for them as an insurance company. This is [a] mysterious case to me." [21]

Thus, while recognizing that the bankruptcy court's subject matter jurisdiction has limits, the court also seemed skeptical of the theories asserted against Travelers to circumvent the bankruptcy court's 1986 injunction.

The Broader Implications of Affirmance

The Supreme Court's pending decision may have a sweeping impact on bankruptcy and insurance, but even more so on mass torts cases. Should the Supreme Court affirm the Second Circuit and allow these conspiracy claims to go forward, it may have opened the door to a new wave of asbestos litigation against insurers. As cogently noted by an asbestos plaintiff's lawyer:

If a plaintiff can successfully assert the conspiracy cause of action, he can hold solvent defendants liable for the sins of Manville, Raybestos-Manhattan and a host of insolvent entities. By asserting broad conspiracies with Manville, plaintiffs hope to expand the universe of asbestos defendants to hundreds of formerly peripheral companies and breathe new life into asbestos litigation in the 21st century.[22]

More generally, however, if the Supreme Court holds that a bankruptcy court does not have the power to implement an appropriate plan for reorganization, then how can a mass-tort defendant expect to ever settle a class action? In essence, if the Supreme Court affirms, it will allow plaintiffs to settle with a defendant, and then subsequently sue its insurer and other nonrelated parties under theories not yet crafted.

As a result, the relationship between insurer and insured might be placed at odds, and insurance companies may become more reluctant to amicably resolve their coverage disputes.

Few insurers would ever settle mass tort claims knowing that they could subsequently be sued by emboldened plaintiffs' lawyers asserting novel theories alleging that pursuant to an insurer's defense obligations owed to its insured, the insurer engaged in a "conspiracy."

Should the Supreme Court uphold the Second Circuit, insurers will be reluctant to settle any dispute knowing they may not be able to purchase global finality. Bailey could present a cautionary tale that could change mass tort law in the future. Asserting claims against insurers responsible for funding large settlements will only make it harder for future mass tort victims to be compensated.

Conclusion

The Supreme Court's decision in Bailey ultimately could change the asbestos litigation landscape in the 21st century, and have a lasting affect on mass tort defendants.

Aside from the immediate impact on Travelers, the court's decision could open or shut a new avenue of collection for the asbestos plaintiffs' bar. It could also embolden the plaintiff's bar to file even more new, and exotic, claims, such as conspiracy, against a wider array of defendants.

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- [1] 129 S. Ct. 761 (U.S. Dec. 12, 2008).
- [2] In re Johns-Manville Corp., 2004 WL 1876056 at *2 (Bankr. S.D.N.Y. Aug. 17, 2004).
- [3] In re Johns-Manville Corp., supra note 2, at * 3.
- [4] In re Johns-Manville Corp., supra note 2, at * 7.
- [5] In re Johns-Manville Corp., supra note 2, at * 8.
- [6] In re Johns-Manville Corp., supra note 2, at * 9.
- [7] MacArthur Co. v. Johns-Manville Corp., 837 F.2d 89, 90 (2d Cir. 1988)
- [8] In re Johns-Manville Corp., supra note 2, at * 14.
- [9] MacArthur Co., 837 F.2d at 90.
- [10] In re Johns-Manville Corp., supra note 2, at * 16.
- [11] MacArthur Co., 837 F.2d at 91.
- [12] In re Johns-Manville Corp., supra note 2, at * 17-18.
- [13] 340 B.R. 49, 56 (S.D.N.Y. 2006).
- [14] Id. at 60.
- [15] Id. at 61.
- [16] 517 F.3d 52, 55 (2d Cir. 2008).
- [17] Id. at 60-61.
- [18] Id. (citing MacArthur, 837 F.3d at 92-93)
- [19] Id.
- [20] 129 S. Ct. 761 (Oral Argument Tr. p. 28 lines 8, 10-16).
- [21] 129 S. Ct. 761 (Oral Argument Tr. p. 12 lines 12-19).
- [22] In re Johns-Manville Corp., supra note 2, at * 12 (quoting W. Mark Lanier, Conspiracy Theory: Putting New Defendants In Manville's Chair, Asbestos L. & Litig., ALI-ABA, Dec. 6-7, 2001 (Am. L. Inst. 2001))