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UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW JERSEY

In re:	Chapter 11
DURO DYNE NATIONAL CORP., *et al.*,[1]	Case No. 18-27963 (MBK)
Debtors.	Jointly Administered
	Hearing Date: October 1, 2018 at 11:00 a.m.

OBJECTION OF THE UNITED STATES TRUSTEE TO DEBTORS' MOTION FOR AN ORDER APPOINTING LAWRENCE FITZPATRICK AS REPRESENTATIVE FOR FUTURE ASBESTOS CLAIMANTS

The United States Trustee, by his undersigned counsel, hereby objects to the Debtors' motion for an order appointing Lawrence Fitzpatrick as the legal representative of future asbestos claimants (the "FCR") in the above-captioned cases under 11 U.S.C. § 524(g)(4)(B)(i) (the "Motion").

[1] The Debtors in these chapter 11 cases are: Duro Dyne National Corp., No. 18-27963-MBK; Duro Dyne Corporation, No. 18-27968-MB;, Duro Dyne Machinery Corp., No. 18-27969-MBK; Duro Dyne MidWest Corp., No. 18-27970-MBK; and Duro Dyne West Corp., No. 18-27971-MBK (collectively, the "Debtors").

The United States Trustee does not object to the Debtors' general request that the Court appoint an FCR, which is appropriate relief in cases that will likely result in a section 524(g) asbestos injunction. But the United States Trustee does object to the appointment of Mr. Fitzpatrick unless the Debtors can and do provide additional information to demonstrate that Mr. Fitzpatrick is free of disqualifying conflicts of interest and that he is capable of serving as an independent fiduciary who can adequately represent the interests of future claimants. Mr. Fitzpatrick has been selected by the very parties that he will be required to negotiate with or litigate against and who retained and compensated him prior to bankruptcy. Mr. Fitzpatrick's own disclosures reveal numerous potentially disqualifying connections with adverse parties and attorneys in these cases, which have not been adequately disclosed and which the United States Trustee has not yet had an opportunity to investigate through discovery. For these reasons, the United States Trustee requests that the Motion be denied unless these concerns can be resolved.

PRELIMINARY STATEMENT

1. Appointment of a future claims representative is not a routine matter and should not be treated as such. The appointment of an FCR is one of the most consequential orders that will be entered by the Court in these cases. In a typical chapter 11 bankruptcy, the only persons whose rights will be affected by the plan

are current creditors and equity holders. Those parties are entitled to receive notice of the bankruptcy case, *see* Fed. R. Bankr. P. 2002(a), and they have the ability to appear and raise objections to vindicate their rights. *See* 11 U.S.C. § 1109(b). Even though creditors are often represented by committees and other fiduciaries, they generally have the ability to monitor the performance of their fiduciaries and may seek relief if they are not adequately represented. *See* 11 U.S.C. § 1102(a)(2), (4).

2. But this is not so in a chapter 11 case that seeks an asbestos channeling injunction under 11 U.S.C. § 524(g), as the Debtors' proposed plan does. *See* Dkt. 19. The section 524(g) injunction is unique in the Bankruptcy Code because it binds not only present creditors, but also potential future asbestos victims who have not yet manifested harm from the Debtors' products and who may not even be aware of these bankruptcy cases. For those victims—who may not show signs of illness for years or even decades after the plan is confirmed—the section 524(g) injunction will discharge any right they may have to recover against the reorganized Debtors, the Debtors' insurers, and certain related parties and will force them to look exclusively to a post-bankruptcy trust for compensation. *See In re Federal-Mogul Global, Inc.*, 684 F.3d 355, 357 (3d Cir. 2012) (section 524(g) injunction "channel[s] all current and future claims based on a debtor's asbestos liability to a personal injury trust"). The Debtors' plan—including the various trust

documents that will be incorporated as exhibits to the plan—will dictate which future claims will be eligible to be paid by the trust, as well as the formulas for determining the amount of compensation for particular types of claims. Most importantly, the Debtors' plan will also determine whether sufficient funds will be reserved to pay for claims that arise in the future. But despite the enormous impact that these cases will have on their lives, future asbestos victims have no ability to appear in these cases, no ability to object to unfair treatment, and no ability to participate in the negotiations that will ultimately determine their fate. *See In re W.R. Grace & Co.,* 729 F.3d 311, 323 (3d Cir. 2013) (noting that future asbestos victims "lack the ability to protect their own interests during the bankruptcy proceeding").

3. In an attempt to ensure that future claimants receive due process, Congress enacted section 524(g)(4)(B) of the Bankruptcy Code, which requires that before entering a section 524(g) asbestos injunction, "the court appoints a legal representative for the purpose of protecting the rights of persons that might subsequently assert [asbestos] claims." 11 U.S.C. § 524(g)(4)(B)(i). Other than stating that the court must make the appointment, section 524(g) is silent as to the procedure for appointing an FCR and does not explicitly state the standards that the FCR must satisfy to be eligible for appointment. But there is little question that those standards should be high: because the role of the FCR is to protect the rights

of absent parties, the FCR's appointment and selection should be transparent, he should be free from conflict, and he should be held to the highest possible standard of independence.

4. The selection of Mr. Fitzpatrick by the Debtors and an ad hoc committee of certain current asbestos plaintiffs (the "Ad Hoc Committee") meets none of these requirements. The Debtors would have the Court quickly approve the selection of an FCR who was vetted and selected by the very parties he will supposedly be negotiating against. Although Mr. Fitzpatrick undoubtedly has significant experience in asbestos cases, those very same past and current engagements give rise to numerous connections and potential conflicts that have neither been fully disclosed nor investigated.

5. The need for a truly independent and effective FCR is especially pertinent in light of recent court findings regarding the asbestos claims process. *See In re Garlock Sealing Technologies, LLC*, 504 B.R. 71, 86 (Bankr. W.D.N.C. 2014) (finding "startling pattern of misrepresentation" in sample of asbestos claims). Because future claimants are the parties who will be most directly harmed by payment of fraudulent or invalid present claims, the FCR should play a leading role in investigating present claims and in ensuring that the plan contains sufficient safeguards to ensure that only meritorious claims will be paid. But it is difficult to imagine how this function can be performed by an FCR

who is subject to conflicts of interest and divided loyalties, particularly where those conflicts involve the very same law firms he should be investigating or against whom he should be negotiating.

6. For all of these reasons, the Court should decline to appoint Mr. Fitzpatrick as FCR based on the present record.

APPLICABLE AUTHORITY

A. Under Section 524(g), the FCR Represents Interests That Are Adverse Both to the Debtors and to Current Asbestos Claimants.

7. Although section 524(g) does not specify the duties of the FCR, courts have long recognized that the FCR is expected to represent interests that are equally adverse both to the debtor and to all current asbestos claimants. *See Federal-Mogul*, 684 F.3d at 362 (noting "competing interests of present and future claimants"); *In re Amatex Corp.*, 755 F.2d 1034, 1043 (3d Cir. 1985) ("[B]ecause of the adverse interests of the other parties, it would appear that future claimants require their own representative").

8. This double adversity can best be understood by considering some of the major issues that will be encountered in the course of an asbestos chapter 11 case. A threshold issue in an asbestos case will usually be the amount of funding that must be placed into the trust by the asbestos defendants (typically the debtor,

its affiliates, and its settling insurers) in exchange for the injunction that will resolve their asbestos liability. During this part of the negotiations, the interests of future claimants will be generally aligned with present claimants but adverse to those of the defendants, who will usually wish to purchase the protections of the injunction as inexpensively as possible. *See In re Pittsburgh Corning Corp.*, 308 B.R. 716, 727 (Bankr. W.D. Pa. 2004) (noting that prior to confirmation, debtor has an interest in minimizing liability and is adverse to both the present claimants and the FCR).

9. But once funding to the trust has become fixed, the interests of present claimants (and their attorneys) become directly opposed to those of the future asbestos victims represented by the FCR. Under section 524(g)(2)(B)(ii)(V), the court must make a finding that present and future claims will be paid "in substantially the same manner," and present claimants may likely disagree with the FCR on whether this requirement has been met. In particular, present claimants would favor trust procedures that pay present claims as fully and as rapidly as possible and that make a minimal allowance for future claims, even at the risk of depleting the fund; future claimants, on the other hand, would favor a procedure that pays claims conservatively in order to preserve trust assets for claims that might arise in the future. For this reason, as one bankruptcy court has noted,

present and future claimants "have a natural antagonism." *In re Quigley Co., Inc.*, No. 04-15739, 2009 WL 9034027, at *5 (Bankr. S.D.N.Y. Apr. 24, 2009).

10. The defendants, present claimants, and future claimants also may have conflicting interests regarding the appropriate level of safeguards to be applied against invalid or fraudulent claims. Once the plan is confirmed and the trust is funded, the defendants are usually indifferent to how the trust funds are distributed: because the injunction ensures that their own liability will in no way be affected, it should make no difference to them what proportion of those funds is paid to meritorious claimants, to fraudulent claimants, or for trust expenses and administration. *See Pittsburgh Corning Corp.*, 308 B.R. at 727. So long as there is no threat that the fund will be exhausted before their own claims can be paid, first-in-line present claimants also may be indifferent to whether fraudulent claims are being allowed along with their own—but they may object to an overly vigilant claims review process that would delay or reduce their own distributions. By contrast, future claimants will have a vital interest in ensuring that the plan contains strong protections against fraud because unchecked payment of non-meritorious claims could well exhaust the trust before some valid future claims can be paid, and they therefore bear a disproportionate share of the harm that will result if the trust is depleted through fraud or mismanagement.

11. In short, the process set out in section 524(g) envisions, in its simplest form, a three-sided litigation or negotiation, where all three sides have distinct interests and are represented by fiduciaries who vigorously and independently protect the rights of their constituencies. The absence or ineffectiveness of any one of these parties in those negotiations may lead to perverse and unfair results. Left to their own devices, a debtor and present claimants may well negotiate a settlement that pays inflated compensation to selected present claimants in return for a lower overall debtor contribution to the trust; both the present claimants and the defendants would benefit under this deal at the expense of the future claimants, who would not receive the treatment offered to the favored present claimants and would be forced to look to an underfunded trust as their sole source of compensation. This, in fact, is exactly what appears to have happened in various asbestos plans negotiated without the full participation of an effective FCR. *See In re ACandS, Inc.*, 311 B.R. 36, 43 (Bankr. D. Del. 2004) (denying, as fundamentally unfair, approval of pre-packaged asbestos plan whose terms reflected "unbridled dominance" of certain present claimants' attorneys).

B. Because the FCR is a Fiduciary, He Must Demonstrate a High Level of Independence and Undivided Loyalty.

12. Both the history and function of section 524(g) make clear that the FCR must necessarily be subject to the ethical requirements applicable to other

types of independent fiduciaries who are appointed to represent the interests of parties who are unable to defend themselves.

13. As the Third Circuit has noted, the FCR "act[s] as fiduciary for the interests of future claimants." *In re Combustion Eng'g, Inc.*, 391 F.3d 190, 237 (3d Cir. 2004), as amended (Feb. 23, 2005). Courts have long recognized that fiduciary status imposes inherent duties of undivided loyalty and impartial service—and that persons who are unable to meet those stringent standards are disqualified from serving as fiduciaries. *Woods v. City Nat'l Bank & Trust Co.*, 312 U.S. 262, 268 (1941) (holding that a member of a bondholders committee has a duty of loyalty); *In re Mountain States Power Co.*, 118 F.2d 405, 407 (3d Cir. 1941) (fiduciary in bankruptcy case has duty of "undivided loyalty"); *In re Mesta Machine Co.*, 67 B.R. 151, 156 (Bankr. W.D. Pa. 1986) ("fiduciaries … have obligations of fidelity, undivided loyalty and impartial service in the interest of creditors they represent") (citation omitted). As a result, the Court may not appoint or approve an FCR unless that FCR can demonstrate that he is capable of meeting the duties that are inherent in his status as a fiduciary, including the duty of undivided loyalty.

14. Similarly, when enacting section 524(g), Congress did not write on a blank slate. The FCR mechanism of section 524(g) was closely modeled on two earlier asbestos bankruptcy cases, *In re Johns-Manville Corp.*, 68 B.R. 618 (Bankr.

S.D.N.Y. 1986), and *In re UNR Industries, Inc.*, 46 B.R. 671 (Bankr. N.D. Ill. 1985), which had appointed similar fiduciaries to protect the rights of future claimants. As the legislative report for what would eventually become section 524(g) explains, Congress intended to "strengthen the Manville and UNR trust/injunction mechanisms" and expected that features of section 524(g)—including the FCR appointment mechanism—would "simulat[e]" the results of those cases. *See* H.R. Rep. No. 103-835 at 41, *reprinted in* 1994 U.S.C.C.A.N. 3340, 3348.

15. The *UNR* and *Manville* rulings on which section 524(g) is modeled involved an independent FCR appointment process not controlled by the debtors or present asbestos claimants. Indeed, the appointment of the FCR in *Manville* was opposed and appealed by both the committee of present asbestos claimants and the equity committee, *see In re Johns-Manville Corp.*, 52 B.R. 940 (S.D.N.Y. 1985), while the court in *UNR* ordered an appointment process in which it granted the United States Trustee leave to "suggest a disinterested party to serve as Legal Representative for putative asbestos disease victims" and stated that it would consider "suggestions of parties in interest" only if the United States Trustee failed to act. *UNR*, 46 B.R. at 676.

16. Those courts, in turn, expressly based the asbestos FCR on various well-established models for fiduciaries representing absent parties. *Manville*

determined that there were three possible models for the proposed FCR: the guardian ad litem, the court-appointed amicus curiae on behalf of an absent party, and the section 1104 examiner. *See Manville*, 36 B.R. at 758 n.7; *UNR*, 46 B.R. at 675 (stating agreement with *Manville*). In each of these models the fiduciary is required to be completely independent of adverse parties and is subject to a stringent duty of undivided loyalty and disinterestedness. *See, e.g., Meeker v. Kercher*, 782 F.2d 153, 155 (10th Cir. 1986) (guardian ad litem owes "undivided loyalty" to minor); *United States v. Michigan*, 940 F.2d 143, 164-65 (6th Cir. 1991) (orthodox view of amicus curiae "was, and is, that of an impartial friend of the court"); *In re Big Rivers Elec. Corp.*, 355 F.3d 415, 433 (6th Cir. 2004) (section 1104 examiner may not "in the slightest degree … have some interest or relationship that would color the independent and impartial attitude required by the Code").[2] These are the same requirements for fiduciaries that were discussed by the Supreme Court in *Woods* and by the Third Circuit in *Mountain States*, and there is no reason to hold the conduct of an FCR to any lesser of a standard than that of the fiduciaries in those cases.

[2] The subsequent history of *Manville* does not make clear which of these models was ultimately used, except insofar as the FCR's powers were later described as "nonbinding." *See In re Johns-Manville Corp.*, 52 B.R. 940, 943 (S.D.N.Y. 1985); *G-I Holdings, Inc. v. Bennet (In re G-I Holdings, Inc.)*, 328 B.R. 691, 698 (D.N.J. 2005) (discussing *Manville*). For purposes of the present discussion, it is sufficient to note that all three of the models considered in *Manville* require a similarly high level of undivided loyalty and independence.

17. The requirement for a fully disinterested FCR with undivided loyalty also emanates from the function and purpose of section 524(g). Because nearly all asbestos plans depend on the ability to channel future as well as present claims, section 524(g) would be meaningless without the ability to bind unknown future claimants. But any such alteration of the rights of future litigants must be done in a manner consistent with constitutional due process. *See In re Combustion Eng'g.*, 391 F.3d at 234 n. 45 (noting that statutory requirements of section 524(g) are "specifically tailored to protect the due process rights of future claimants"). In similar circumstances, courts have recognized that due process not only requires that the absent litigants be represented, but that their representative be free from conflicting duties to other parties. *Id.* at 245 (noting that future claimants "must be adequately represented throughout the process"); *In re Johns-Manville Corp.*, 551 B.R. 104, 114 (S.D.N.Y. 2016) (trust mechanism that did not provide future claimants with adequate representation would not satisfy due process). As a result, it is not enough under section 524(g) for this Court simply to appoint an FCR; the Court must determine that the FCR will provide representation that is effective, disinterested, and independent. *See generally In re Pillowtex, Inc.*, 304 F.3d 246, 255 (3d Cir. 2002) (holding that bankruptcy court erred when it approved retention of professional before fully evaluating alleged conflict).

ARGUMENT

A. The Court Should Not Give Deference to the Selection of Mr. Fitzpatrick by the Debtors and the Ad Hoc Committee.

(1) 11 U.S.C. § 524(g) authority to select the FCR is vested in the Court and not in the Debtors or other adverse parties.

18. Section 524(g)(4)(B)(i) directs the Court to appoint the FCR, and nothing in the statute permits the debtor or any committee of creditors to assume that authority for themselves—as the Debtors and the Ad Hoc Committee appear to have presumed here. *See* Motion at 10 ("Mr. Fitzpatrick is the parties' first choice to continue as legal representative"). Nor is the idea of an adversary-selected FCR consistent with the legislative purpose of section 524(g) or the experience of the *Manville* and *UNR* cases on which section 524(g) is based, which contemplate an open and unbiased selection process. Had Congress intended to grant any other person the power to select the FCR or to give the debtors or present asbestos claimants a right to make an initial selection subject to court approval or disapproval, Congress presumably would have said so directly, as it has done with other types of fiduciary selections under the Bankruptcy Code. *Compare* 11 U.S.C. § 702(b) (creditors "may elect one person to serve as trustee" in chapter 7 case if certain conditions are met). This absence of any statutory role for the debtor or present claimants in the selection of the FCR is consistent with the highly

sensitive role of the FCR and his need for complete independence and must be regarded as intentional.

(2) Because the FCR does not represent the Debtors, the Debtors' request that Mr. Fitzpatrick be appointed is entitled to no deference.

19. The selection of an FCR raises entirely different concerns than does the selection of an estate professional under 11 U.S.C. § 327. In the latter case, courts will typically approve the debtor's selection of a professional. *See In re Huntco Inc.*, 288 B.R. 229, 232 (Bankr. E.D. Mo. 2002) (bankruptcy court should give "significant deference" to debtor-in-possession's choice of counsel); *but see In re Wheatfield Business Park LLC*, 286 B.R. 412, 418 (Bankr. C.D. Cal. 2002) (debtor "does not have absolute right to counsel of its choice"). But there is no reason for the Court to give any deference at all to the Debtors' choice of the FCR because the FCR does not represent the Debtors.

20. The United States Trustee is unaware of any other circumstance in bankruptcy in which it would be appropriate for a party to select the fiduciary representing the very interests against which it will negotiate or litigate. The request of the Debtors and the Ad Hoc Committee to have an FCR of their own choosing is comparable to the target of an investigation being allowed to choose the section 1104 examiner who will conduct that investigation, to the debtor-in-possession being allowed to appoint the members of a creditors' committee, or to a

creditor with a disputed claim being allowed to select the chapter 7 or 11 trustee against whom his claim will be litigated. *See In re TBR USA, Inc.*, 429 B.R. 599, 629 (Bankr. N.D. Ind. 2010) ("Congress did not intend to allow creditors who had disputed claims against the estate to participate in an election and choose their opponent"); *In re Williams*, 277 B.R. 114, 118 (Bankr. C.D. Cal. 2002) (noting that "any creditor with a disputed claim would love to select her future opponent"). Given the critical role that the FCR plays in acting as a check on the Debtors and on present claimants, the Debtors' request that the Court ratify their nominee is equally unreasonable.

B. Approving the Appointment of Mr. Fitzpatrick Could Create a Conflict of Interest and Undermine Confidence in the Integrity of the Bankruptcy Process.

21. "The conduct of bankruptcy proceedings not only should be right ***but must seem right***." *In re Bohack Corp.*, 602 F.2d 258, 263 (2d Cir. 1979) (*quoting In re Ira Haupt & Co.,* 361 F.2d 164, 168 (2d Cir. 1966) (emphasis added). Because this case involves a pre-negotiated plan that was formulated without court oversight, there is nothing in the record that would allow the Court to evaluate objectively Mr. Fitzpatrick's performance so far. But even assuming that he has acted (and will continue to act) in the most diligent and ethical manner possible, the conflicts inherent in his appointment may cast a permanent cloud over his service and may undermine public confidence in the bankruptcy case as a whole.

22. The circumstances of Mr. Fitzpatrick's selection and hiring by the Debtors and the Ad Hoc Committee have not been disclosed fully. But the very nature of his employment by his purported adversaries and terms of his engagement indicate that the Debtors and the Ad Hoc Committee exerted considerable leverage over his performance during the prepetition negotiations—and they may continue to do so during the bankruptcy case. The conditions of Mr. Fitzpatrick's engagement would have created enormous pressure to yield to the wishes of the Debtors and the Ad Hoc Committee. If the Debtors were unsatisfied with any of the demands made by Mr. Fitzpatrick, they could have terminated him

during the prepetition negotiations. Motion Ex. B at 4-5 (providing that Mr. Fitzpatrick could be terminated on seven days' notice for "cause," which is not defined in the engagement letter). The power to hire and fire is the power to control. Furthermore, as his own resume demonstrates, Mr. Fitzpatrick is a repeat player in asbestos bankruptcies who has frequently been hired by debtors and committees in connection with pre-packaged and pre-negotiated asbestos plans. His ongoing ability to secure such lucrative employment depends, in a very real sense, on his ability to please the plaintiffs' and debtors' attorneys who hire him—and this employment could easily be placed at risk if he advocated too aggressively for the future claimants.

23. Even if it is assumed that Mr. Fitzpatrick has acted at all times in good faith and as a vigorous advocate for future claimants notwithstanding these pressures, this potential for divided loyalties may be, by itself, reason to deny his appointment. As the Third Circuit has noted, under appropriate circumstances, the court has discretion to disqualify a professional based on the potential for a conflict alone. *See In re Marvel Entertainment Gp., Inc.,* 140 F.3d 463, 476 (court may, within its discretion disqualify professional "who has a potential conflict of interest"); *In re Congoleum Corp.*, 426 F.3d 675, 692 (3d Cir. 2005) (same).

24. Mr. Fitzpatrick is not the Debtors' professional, and the Court owes no deference to the Debtors' suggestion that he be appointed. The future asbestos

claimants are entitled to representation that is free from conflict. Unless and until Debtors can establish the absence of a conflict of interest, the Motion should be denied.

C. Past Practice Does Not Justify the Appointment of an Adversary-Selected FCR.

25. Although the Debtors' request to be allowed to choose their own FCR is inconsistent with both the text and the purpose of section 524(g), the United States Trustee acknowledges that it is a practice that has been followed, usually without opposition, in many previous asbestos bankruptcy cases.[3] But this simply underscores the need for a truly independent FCR. Apart from the future claimants—who have no actual ability to contest an FCR's appointment—there is no party in the bankruptcy case with a vested economic interest in ensuring a strong and effective FCR.[4] It is thus unsurprising that the FCR appointment often has been treated as a routine, non-controversial motion.

26. But the practice of approving adversary-selected FCRs has had generally negative results for future claimants. As several studies have pointed

[3] *See, e.g., In re Metex Corp.*, No. 12-14554, Dkt. 93 (Bankr. S.D.N.Y. Jan. 16, 2013) (order granting unopposed motion appointing Mr. Fitzpatrick as FCR).

[4] In a few cases, insurance companies have challenged FCR appointments as part of a broader challenge to the terms of a plan. *See, e.g., Chicago Insurance Co. v. Thorpe Insulation Co.*, No. CV 08-1020-DSF, 2008 WL 11338766 (C.D. Cal. July 14, 2008) (dismissing insurance companies' appeal of FCR order as interlocutory and due to appellees' lack of standing). Of course, because they may eventually be called on to contribute to an asbestos trust, insurance companies also arguably benefit from a weak FCR—and as such, they may be particularly ineffective advocates for the interests of future claimants on this issue.

out, future claimants have not fared well in asbestos trusts: "[A]lthough trusts are established on the promise to pay all current and future victims equitably, this promise has already been broken at all but a few trusts. The threat to future victims has become pressing given the dramatic growth of the bankruptcy trust system." S. Todd Brown, *How Long is Forever This Time? The Broken Promise of Bankruptcy Trusts*, 61 BUFF. L. REV. 537, 538-39 (2013).

> The bankruptcy trust system is long past the point where participants can look at the rapid depletion of newly established trusts as unanticipated and unintended consequences of generous compensation criteria . . . . If we can be reasonably assured of anything, it is that a trust that employs the same criteria and follows the same practices as its predecessors is extremely unlikely to "value, and be in a financial position to pay, present claims and future demands that involve similar claims in substantially the same manner" as required by section 524(g).

Id. at 538-39. According to one more recent study, between 2008 and 2018, 60% of asbestos trusts were forced to reduce their "payment percentages," which is the mechanism that determines the actual payment that a claimant with a particular disease or settlement will receive. *See* Peter Kelso and Marc Scarcella, *Dubious Distribution: Asbestos Bankruptcy Trust Assets and Compensation,* U.S. Chamber of Commerce, March 2018, at 9. For those trusts, an asbestos claim is today worth, on average, 46% less than it would have been worth a decade earlier. *Id.* This erosion of trust assets—which disproportionately prejudices future claimants—is the precise harm that the FCR was meant to prevent.

27. And far from providing the strong and independent voice that Congress intended, in many bankruptcy cases these FCRs have often done little more than echo the views of the parties who appointed them. A particularly noteworthy example is *ACandS*, a case in which Mr. Fitzpatrick served as FCR. In that case, the debtors and certain plaintiffs' firms negotiated a prepackaged plan under which the bulk of the debtors' insurance assets were diverted through a series of prepetition transactions to pay mass groups of alleged claims of the clients of a few favored law firms, leaving little for all other claimants, including future claimants. *See ACandS*, 311 B.R. at 40 (noting that "a claimant in Category A who has some evidence of asbestos exposure but who is not sick would have been paid in full prepetition, while someone with mesothelioma, who was not included (for whatever reason) in Categories A through D, in all probability will never receive anything."). Despite the fact that it would be difficult to imagine a plan structure more prejudicial to the interests of future claimants, Mr. Fitzpatrick supported the plan and "vouch[ed] for its fairness." *Id.* at 41. Notwithstanding Mr. Fitzpatrick's support, the bankruptcy court recommended against confirmation of the plan, specifically finding that it did not satisfy section 524(g)(2)(B)(ii)(V) because it discriminated against future claimants and would not pay present and future claims in the same manner. *Id.* at 42. In addition, the court found the plan to be so fundamentally unfair that it lacked good faith. *Id.* at 43. Despite these findings in

favor of the very claimants he purportedly represented, Mr. Fitzpatrick immediately joined the debtors and the present claimants' committee by filing a notice of appeal against the bankruptcy court's ruling. *See ACandS Inc. v. Travelers Casualty*, No. 04-cv-00123-JJF (D. Del.).[5]

28. Similarly, other cases in which Mr. Fitzpatrick has participated reveal a near-total alignment between the positions of the supposedly independent FCR and the interests of current asbestos claimants and their attorneys. Most recently, in *In re Motions Seeking Access to 2019 Statements*, 585 B.R. 733 (D. Del. 2018), *notice of appeal filed sub nom. In re ACandS, Inc., et al.,* No. 18-1951 (3d Cir.), the court considered a request to unseal Rule 2019 statements filed in several asbestos cases in which attorneys were required to list the names of the claimants they purported to represent. *Id.* at 738. Among other purposes, the movants sought those documents in order to investigate fraud in the claims process. *Id.* Mr. Fitzpatrick, in his capacity as FCR for one of the trusts, opposed the request on the grounds that the movants' purpose in seeking the information was improper. *Id.* After the bankruptcy court granted the movants a limited form of access, which would have permitted them to examine Rule 2019 statements for fraud but would not allow them to retain the statements or use them for other purposes, Mr.

[5] The Debtors in *ACandS* ultimately elected to file an amended plan of reorganization that presumably mooted the appeal of the bankruptcy court's ruling. No. 04-00123-JJF, Dkt. 35 (D. Del. Jul. 7, 2007).

Fitzpatrick was among the parties who appealed that order, and he argued that using a Rule 2019 statement "as an aid to ferret out fraud" was an improper purpose and that the movants should have been denied access to the statements altogether. *See* Appellees'/Cross-Appellants' Opening Brief, No. 16-1078, Dkt. 22, at 60 (D. Del. Aug. 1, 2017).

29. Even assuming that Mr. Fitzpatrick's argument—which was rejected by the district court—had merit, it is difficult to understand why he, in particular, would have had an interest in raising it on behalf of future claimants. The Rule 2019 motions in question involved disclosure of the identities of present claimants in certain historic asbestos cases—and not, by definition, the unknown future claimants whom Mr. Fitzpatrick supposedly represented. Moreover, it is unclear how those future claimants would benefit from squelching an investigation into fraud because they are the primary victims of claims fraud and would presumably benefit to the extent any fraud by present claimants was to be uncovered. As with the earlier *ACandS* case, a neutral observer may well question which interests Mr. Fitzpatrick was truly representing in the *2019 Statements* litigation. The Court should require an explanation before considering him for FCR in this case.

D. Debtors Have Not Demonstrated That Mr. Fitzpatrick is Disinterested.

30. Even were the Court to defer to the selection of Mr. Fitzpatrick by the Debtors and the Ad Hoc Committee, they have not demonstrated his

disinterestedness—an issue on which the Debtors, as the parties seeking Mr. Fitzpatrick's appointment, bear the burden of proof. *See In re Champagne Servs., LLC*, 560 B.R. 196, 201 (Bankr. E.D. Va. 2016) ("The burden is on the proponent of the application to show that proposed counsel satisfies all requirements, including that he is disinterested. It is not the United States trustee's burden to show that he is not disinterested").

31. The Debtors appear to acknowledge that, at a minimum, Mr. Fitzpatrick must be disinterested in order to be appointed FCR. *See* Motion ¶ 36. A "disinterested person," in turn, is one who "was not . . . within 2 years before the date of the filing of the petition . . . [an] employee of the debtor," and who "does not have an interest materially adverse to the interest of the estate or of any class of creditors or equity security holders, by reason of any direct or indirect relationship to, connection with, or interest in, the debtor, or for any reason."
11 U.S.C. § 101(14)(B), (C).

32. Although the Motion contains a boilerplate representation that Mr. Fitzpatrick is disinterested—because he "has no connection with the Debtors, the twenty (20) largest unsecured creditors, the secured lender, other parties-in-interest, the Company's current attorneys or professionals, or the United States Trustee or Bankruptcy Judge assigned to this case, and he does not represent any entity having an adverse interest to the Debtors in connection with the Debtors'

chapter 11 cases," *see* Motion ¶ 38—Mr. Fitzpatrick's own disclosures and the record of this case reveal numerous other connections and interests that may constitute a conflict of interest. Mr. Fitzpatrick has made insufficient disclosure, and discovery should be required.

33. Specifically, there are four interests and connections that potentially render Mr. Fitzpatrick not disinterested on which further disclosure or discovery is needed: (1) his status as an employee of the Debtors within two years of the petition date; (2) his personal financial interest in the Debtors' proposed bankruptcy plan, given the requirement that he be appointed as legal representative for the Debtors' eventual asbestos trust; (3) his connections with the numerous plaintiffs' law firms involved in the negotiation of the plan, including by reason of his role in several other asbestos trusts for which those same firms serve in a supervisory role; and (4) his continuing role as a fiduciary in other bankruptcy cases and for other bankruptcy trusts, which may subject Mr. Fitzpatrick to conflicting fiduciary duties.

(1) <u>There has been insufficient disclosure regarding Mr. Fitzpatrick's prepetition employment by the Debtors.</u>

34. Prior to the petition date, Debtors paid Mr. Fitzpatrick for his services. *See* Motion Ex. C. Although Mr. Fitzpatrick's engagement letter recites that his services "would not render him an employee" of the Debtors, the engagement letter

appears to have given the Debtors at least some ability to terminate his services and to impose a cap on the fees to be charged by him and his professionals. *See Id.* Ex. B at 2. In addition, the engagement letter references a two-week period in which Mr. Fitzpatrick and his attorneys appear to have provided services prior to the execution of the engagement letter. *Id.* at 3 (engagement letter "shall retroactively cover all fees and expenses Mr. Fitzpatrick and YCST have incurred since May 31, 2017").

35. There remain significant unanswered questions regarding Mr. Fitzpatrick's prepetition service to the Debtors. In particular, the Motion and its supporting documents contain no information whatsoever about Mr. Fitzpatrick's actual activities during the prepetition period. It is unclear whether his services were limited merely to providing the Debtors with a fairness opinion for their proposed transaction or whether and to what extent he was responsible for formulating, evaluating, or responding to proposals concerning the bankruptcy plan.[6] It is also unclear what understanding, if any, the parties had of the "cause" that would entitle the Debtors to terminate Mr. Fitzpatrick's services or to authorize payment for services in excess of the monthly cap. Finally, there is no

[6] Debtors paid Mr. Fitzpatrick approximately $19,000 before the petition date. Based on Mr. Fitzpatrick's rate of $500 per hour, as recited in the engagement letter, it appears that Mr. Fitzpatrick worked fewer than two hours per month for much of his prepetition engagement and that he worked fewer than seven hours total in the month leading up to the bankruptcy filing. The United States Trustee notes that these low hourly totals are far more consistent with a consultant retained to perform a perfunctory review of documents than what might be expected of an independent fiduciary who is an adversary in a complex negotiation.

information about the circumstances and nature of Mr. Fitzpatrick's employment for the period between May 31, 2017 (the earliest date for which his fees would be payable), and June 12, 2017 (the date of the engagement letter).

36. These questions, and others, are important for two reasons. First, full disclosure of Mr. Fitzpatrick's activities is relevant to the issue of whether his services were more in the nature of those of an employee than an independent fiduciary, which in turn would determine whether he is automatically not disinterested under 11 U.S.C. § 101(14)(B). Second, a further investigation is necessary to determine the true nature of Mr. Fitzpatrick's prepetition duties and obligations and whether they would conflict in any way with his proposed post-petition duties. As the Third Circuit has noted, this question is of paramount importance in prepackaged asbestos bankruptcy cases, which require "careful and comprehensive scrutiny" because the shifting roles of professionals may lead to ethical conflicts and abuses. *See In re Congoleum Corp.*, 426 F.3d 675, 694 (3d Cir. 2005) (finding that proposed law firm for debtor did not satisfy disinterestedness requirement under section 327 where it had acted as co-counsel to tort plaintiffs during prepetition negotiations). To the extent this Court finds that Mr. Fitzpatrick's true client prepetition was the Debtors or the Ad Hoc Committee, this Court would be required to disqualify Mr. Fitzpatrick based on the Third Circuit's guidance in *Congoleum*, and for that reason it is premature for the

Court to approve Mr. Fitzpatrick's appointment until his prepetition conduct has been thoroughly investigated.

(2) Mr. Fitzpatrick may not be disinterested because he may hold a personal financial interest in the outcome of the plan.

37. Mr. Fitzpatrick also likely lacks disinterestedness because he may personally benefit from confirmation of the proposed pre-negotiated plan. Under the Trust Agreement that forms part of the proposed plan, Mr. Fitzpatrick will be the initial Future Claims Representative of the post-bankruptcy trust—an appointment that creates potentially lifetime employment at Mr. Fitzpatrick's customary billing rates.[7] *See* Plan Ex. A ¶ 6.1, 6.2. At the very least, this promise of a well-paying sinecure creates a powerful personal inducement for Mr. Fitzpatrick to support confirmation of the plan. *See generally* Plevin, Epley, and Elgarten, *The Future Claims Representative in Prepackaged Asbestos Bankruptcies: Conflicts of Interest, Strange Alliances, and Unfamiliar Duties for Burdened Bankruptcy Courts,* 62 N.Y.U. ANN. SURV. AM. L. 271, 326 (2006) (noting "lucrative" nature of post-bankruptcy FCR employment).

38. But this guarantee of employment also means that Mr. Fitzpatrick is unlikely to be able to be an objective and disinterested representative of future

[7] Section 6.1 of the Trust Agreement states that "[t]he initial FCR shall be the individual identified on the signature pages hereto." The signature pages of the Trust Agreement list Mr. Fitzpatrick as FCR—in fact, one of only two trust fiduciaries to be designated by name.

claimants. For this reason, courts have not hesitated to disqualify fiduciaries who have a personal stake in the outcome of a bankruptcy case. Thus, in *Big Rivers*, the appellate court disqualified a chapter 11 examiner, and ordered him to disgorge nearly a million dollars in compensation, after it was revealed that the examiner had entered into an oral agreement with a creditor that would have paid him a bonus based on the amount of the creditor's recovery. *Big Rivers Elec. Corp.*, 355 F.3d at 434. The conflict here is no less serious. The fact that Mr. Fitzpatrick may benefit personally from one proposed plan, but may not benefit from another, undermines his ability to serve as a disinterested and objective advocate for future claimants. *Id.* ("That self-interest *might* lead examiners to act in these ways suffices to disqualify them, because the Code does not merely prohibit trustees and examiners from *acting* upon materially adverse interests, it prohibits trustees and examiners from *having* them") (emphasis in original). Further, there has been no disclosure of how, why, or at whose insistence Mr. Fitzpatrick's appointment as post-bankruptcy FCR was written into the plan. To the extent this was negotiated by Mr. Fitzpatrick, this may constitute a form of self-dealing that would raise serious questions about his eligibility to serve in this and other bankruptcy cases. Unless and until Debtors can provide more information that establishes there is no conflict, the Motion should be denied.

(3) Discovery should be required of Mr. Fitzpatrick's dealings with attorneys for current asbestos claimants.

39. Although Mr. Fitzpatrick's declaration states that he has "no connection with" the creditors in this case or their attorneys, his list of prior engagements includes numerous cases that prominently featured many of the same firms making up the Ad Hoc Committee in this case. Just as in this case, many of those firms appear to have been involved in the selection or approval of Mr. Fitzpatrick as prepetition FCR in those earlier cases, and in other cases members of those same firms serve on Trust Advisory Committees for asbestos trusts in which Mr. Fitzpatrick also serves.[8]

40. Although the mere repeated interaction of law firms and professionals in different cases is not necessarily grounds for disqualification, additional disclosure is necessary here because of the unique power that these firms have had (and will continue to have) over Mr. Fitzpatrick's employment, both as a section 524(g) FCR and as a post-bankruptcy trust fiduciary. Mr. Fitzpatrick should fully

[8] Mr. Fitzpatrick's experience with the firm of Weitz & Luxenberg, which is a member of the Ad Hoc Committee in this case, may be typical. Weitz was a leading member of the prepetition committees in both *ACandS* and *Metex*, two of the cases in which Mr. Fitzpatrick was selected to serve as FCR. *ACandS,* 311 B.R. 39 (listing members of prepetition committee); Disclosure Statement with Respect to the Plan of Reorganization of Metex Mfg. Corp., No. 12-14554, Dkt. 438 (Bankr. S.D.N.Y. Feb. 25, 2014) (describing Weitz as one of three members of the prepetition committee at the time of Mr. Fitzpatrick's selection). Though not a pre-negotiated plan, Weitz also negotiated a prepetition term sheet with the debtor in the recently filed case of *In re The Fairbanks Co.*, No. 18-41768, Dkt. 33 (Bankr. N.D. Ga.), in which a motion has been filed to appoint Mr. Fitzpatrick as FCR. On information and belief, Weitz also serves (or formerly served) as a member of the Trust Advisory Committee for at least four of the post-bankruptcy asbestos trusts for which Mr. Fitzpatrick has been hired: ACandS, North American Refractories, Pittsburgh Corning, and Metex.

disclose the circumstances of his hiring, both in this case and in each of the previous cases in which he has served. In particular, Mr. Fitzpatrick should disclose whether his hiring in this or any other case was done at the recommendation of, or was required as a condition of settlement by, any of the law firms on the Ad Hoc Committee and whether there exist any agreements and understandings regarding his employment. Furthermore, Mr. Fitzpatrick should fully disclose all relevant facts concerning the post-bankruptcy trusts for which he is currently employed, including the identities and affiliations of all Trust Advisory Committee members for such trusts, and whether and to what extent those Trust Advisory Committees control or have the ability to influence Mr. Fitzpatrick's continued employment and compensation.

(4) Mr. Fitzpatrick should disclose potential conflicts arising from his employment by post-bankruptcy asbestos trusts.

41. It is common for asbestos claimants to seek payment from more than one trust, and as a result many of the present claimants in this case—whose interests are adverse to those of the future claimants—may also be beneficiaries of other trusts in which Mr. Fitzpatrick serves in a fiduciary role. Mr. Fitzpatrick should be required to disclose and explain his duties to these trusts and those claimants in the event that a dispute arises over such claims, particularly as they may relate to an investigation of fraud or abuse, so that the Court may evaluate

whether there is a possibility that Mr. Fitzpatrick will owe conflicting fiduciary duties. In addition, as *Garlock* demonstrates, there is a possibility that the bankruptcy estates in these cases will find it necessary to seek discovery or take other actions that are adverse to the previously established trusts on which Mr. Fitzpatrick serves. *See Garlock*, 504 B.R. at 84.[9] Accordingly, he should provide further disclosure about his understanding of his duties to those trusts, including specifically whether he believes he would be obligated to resist a discovery request from this Court or from a party in this case in such capacity, and he should describe the procedures, if any, that are currently in place to address any such conflicts should they arise.

WHEREFORE, the United States Trustee requests that the Court deny the Motion without prejudice and give Debtors additional time to provide the necessary information to demonstrate that Mr. Fitzpatrick is free of disqualifying conflicts of interest and that he is capable of serving as an independent fiduciary who can adequately represent the interests of future claimants. This should include the time necessary for the United States Trustee and other parties to conduct Rule 2004 examinations and other discovery on Mr. Fitzpatrick's ability to be a fiduciary for the future claimants. In the alternative, the United States Trustee

[9] In *Garlock*, a chapter 11 debtor sought discovery of various asbestos trusts in an effort to determine the extent to which its own historic asbestos liabilities had been tainted by fraud. *Id.* at 84. Garlock's discovery requests were vigorously resisted by the trusts from which discovery was sought, including a number of the trusts on which Mr. Fitzpatrick serves.

requests that the Court deny the Motion without prejudice to the Debtors' right to file an amended motion that addresses the concerns expressed in this objection by ensuring the appointment of a fully independent FCR.

Respectfully submitted,

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