ALM | LAW.COM

New York Law Journal

CORPORATE INSURANCE LAW

Supreme Court Expands Insurers' Rights by Holding That Insurers Are "Parties in Interest" in Bankruptcy Proceedings

By Howard B. Epstein and Theodore A. Keyes

September 27, 2024

By **Howard B. Epstein**

And **Theodore A. Keyes**

The U.S. Supreme Court wrapped up its 2023-24 term in June 2024, handing down a number of long-awaited rulings. In the insurance space, no decision was more highly-anticipated than that issued in *Truck Insurance Exchange v. Kaiser Gypsum Company*.

In *Truck Insurance Exchange*, the issue presented was whether an insurer with financial responsibility for a bankruptcy claim is considered a "party in interest" under Section 1109(b) of the Bankruptcy Code. In its June 6, 2024 opinion, the court held that such an insurer is a "party in interest," opening the door for Truck Insurance Exchange (Truck) and similarly-situated insurers to "'raise and [to] appear and be heard on any issue' in a Chapter 11 case." *Truck Ins. Exch. v Kaiser Gypsum Co.*, 144 S. Ct. 1414, 1418 (2024).

Truck's Perpetual Liability

Kaiser Gypsum Company and its parent company, Hanson Permanente Cement (collectively, Hanson), were manufacturers of building materials containing asbestos. Given the now well-known health risks associated with exposure to asbestos, Hanson faced extensive liability for the production and sale of these products, with over 38,000 lawsuits filed against it since the late 1970s and many more suits expected. The unpredictable quantum of future liability led Hanson to file for relief under Chapter 11 of the Bankruptcy Code in 2016, at which time 14,000 claims remained pending.

Truck had issued primary liability insurance policies to Hanson from 1965 to 1983 pursuant to which Truck is required to "investigate and defend each covered asbestos personal-injury claim or suit asserted against [Hanson], 'even if such claim or suit is groundless, false or fraudulent.'" *In re Kaiser Gypsum*, 60 F.4th 73, 78-79 (4th Cir. 2023). Under the policies, Truck is generally

HOWARD B. EPSTEIN *is of counsel at Schulte Roth & Zabel and* THEODORE A. KEYES *is a partner at the firm.* JULIA R. CUMMINGS, *an associate, also contributed to this column.*

required to indemnify Hanson for up to $500,000 per claim, subject to a $5,000 per claim deductible. Since the policies do not contain a maximum aggregate limit, Truck faces potential liability up to the per-claim limit for each new covered claim or lawsuit. The policies explicitly also provide that Hanson's bankruptcy or insolvency does not affect Truck's obligations thereunder, meaning that Truck's indemnification obligations survive any plan of reorganization.

Hanson's Plan of Reorganization

Under Section 524(g) of the Bankruptcy Code, a Chapter 11 debtor may establish an asbestos personal injury trust to assume the debtor's liability for asbestos-related claims. The Section 524(g) trust shields a debtor from future liabilities by requiring claimants to channel their claims to the trust, rather than pursuing claims against debtor-related entities post-reorganization. To address its unknown future liabilities for asbestos-related claims, Hanson and certain parties participating in the Chapter 11 proceeding agreed to a proposed plan of reorganization that created such a trust. The proposed plan also transferred Hanson's rights under the Truck policies to the Section 524(g) trust, including "all rights to coverage and insurance proceeds." *Truck Ins. Exch.*, 144 S. Ct. at 1422.

In the insurance space, no decision was more highlyanticipated than that issued in 'Truck Insurance Exchange v. Kaiser Gypsum Company.'

Under the proposed plan, uninsured claims would be processed directly through the trust via an administrative process. In contrast, insured personal injury claims (i.e., those covered by the Truck policies) would have to be filed as tort claims in the court system and, consistent with the insurance policies, Truck would be required to indemnify Hanson for any judgments in favor of a claimant, up to the $500,000 per-claim limit. For uninsured claims, the trust process would require claimants to submit disclosures and authorizations intended to prevent payment of fraudulent or duplicative claims. The proposed plan did not require such disclosures and authorizations in connection with insured claims.

Truck was the only participant in the Chapter 11 proceeding that objected to the proposed plan. However, the bankruptcy court overseeing the proceedings held that Truck was only permitted to challenge the proposed plan "to the extent that it was not 'insurance neutral.'" *In re Kaiser Gypsum*, 60 F.4th at 80-81. Because the proposed plan did not "alter Truck's rights or obligations under the policies," the court concluded that the proposed plan was insurance neutral and, as a result, ruled that Truck was not a "party in interest" under Section 1109(b) entitled to challenge other aspects of the proposed plan. Id. The U.S. District Court for the Western District of North Carolina, Charlotte Division and the U.S. Court of Appeals for the Fourth Circuit both agreed with the bankruptcy court and affirmed the ruling on appeal.

The Supreme Court Weighs In

In a unanimous 8-0 opinion, the Supreme Court overruled the Fourth Circuit's decision, holding that an insurer with financial responsibility for a bankruptcy claim is a "party in interest" under Section 1109(b), and that such a party may "'raise and may appear and be heard on any issue' in a Chapter 11 case," including to object

to a proposed plan of reorganization. *Truck Ins. Exch.*, 144 S. Ct. at 1418.

The court began its analysis by reviewing the text of Section 1109(b), noting that the broad language allowing "any ‹party in interest› to ‹appear and be heard on any issue›» is capacious. Id. at 1423-24. The statute provides a non-exhaustive list of certain parties that could be considered parties in interest, including the debtor, its creditors, equity holders, and certain committees. The court stated that each of the listed parties could be directly impacted by a proposed plan of reorganization, either (i) "because they have a financial interest in the estate's assets," or (ii) "because they represent parties that do." Id. at 1424. The court then examined the ordinary meaning of the words "party" and "interest," finding that the meaning of each word individually and together as a phrase confirms that the term "party in interest" should be interpreted broadly. "'Party' in this context is best understood as '[a] person who constitutes or is one of those who compose … one or [the] other of the two sides in an action or affair; one concerned in an affair; a participator; as, a party in interest,'" and "'[i]nterest' is best understood as '[c]oncern, or the state of being concerned or affected, esp[ecially] with respect to advantage, personal or general.'" Thus, taken together, the term "party in interest" means parties "that are potentially concerned with or affected by a proceeding." Id.

Next, the court turned to the historical context behind Section 1109(b)'s enactment. The court observed that over time, Congress has expanded the rights of stakeholders to participate in reorganization proceedings. While earlier bankruptcy statutes provided limited rights to creditors and stakeholders or allowed only certain types of stakeholders to participate in proceedings, laws such as Section 1109(b) aimed to enhance participation in the bankruptcy process.

Lastly, the court discussed the purpose of Section 1109(b). Recognizing the risk of a very debtor-friendly plan of reorganization in Chapter 11 proceedings with limited stakeholder participation, Congress drafted Section 1109(b) broadly to "serve … the policies of inclusion underlying the [C]hapter 11 process." Id. at 1425.

Applying this analysis, the court found that Truck and other similarly-situated insurers squarely fit into the term, "parties in interest." For example, plans of reorganization can (i) directly adversely affect certain contractual rights of insurers, such as the right to control the defense of claims and negotiate settlements; (ii) be collusive at the expense of the insurer; and (iii) abolish the debtor's obligations to "cooperate and assist" the insurer in defending covered claims. Simply put, the court explained, "[w]here a proposed plan 'allows a party to put its hands into other people's pockets, the ones with the pockets are entitled to be fully heard and to have their legitimate objections addressed.'" Id. at 1426.

The Court Rejects the 'Insurance Neutrality' Doctrine

The court next rejected the lower courts' application of the insurance neutrality doctrine. The insurance neutrality doctrine considers whether a plan of reorganization "increase[s] the insurer's pre-petition obligations or impair[s] the insurer's pre-petition policy rights." Id. at 1427. Because Truck would have retained the same coverage defenses that it had under the policies and Hanson retained its obligations to assist and cooperate with Truck in defending claims before and after Hanson's reorganization under the

proposed plan, the District Court determined that the proposed plan was insurance-neutral. As part of this determination, the District Court rejected Truck's argument that the proposed plan would breach Hanson's obligation to cooperate and assist Truck in defending covered claims. The proposed plan's disparate treatment of insured versus uninsured claims did not change the District Court's analysis, since Truck had not been contractually entitled to the additional disclosure protections under the terms of the insurance policies.

The court found that application of the insurance neutrality doctrine "is conceptually wrong and makes little practical sense." Id. By focusing on the insurer's rights and obligations pre-reorganization, the court explained, the insurance neutrality doctrine overlooks how a proposed plan might "alter and impose obligations on insurers." Id. In this case, the proposed plan would have "transformed [Hanson's] asbestos liabilities into bankruptcy claims that Truck will now have to indemnify … without the protections of disclosure requirements in place for uninsured claims filed directly with the [t]rust." Id. The court emphasized that Truck's financial exposure may be directly affected by the proposed plan, which is sufficient to give Truck a right to voice objections to the plan.

Looking Forward

The Supreme Court's opinion in *Truck Insurance Exchange* is expected to provide insurers with financial responsibility for bankruptcy claims more leverage in bankruptcy proceedings. At minimum, insurers will expect to have a seat at the table for plan negotiations. Rather than being limited to raising objections that a proposed plan of reorganization alters their pre-reorganization obligations, insurers will likely seek to negotiate more favorable outcomes that reduce their potential future liabilities.

Given the Supreme Court's emphasis on maximizing participation in bankruptcy proceedings and its broad interpretation of Section 1109(b)'s "party in interest" language, we may also see other stakeholders come forward arguing that they too are parties in interest and attempting to have their voices heard in future proceedings. While the Supreme Court noted that there are surely limits to which stakeholders could be considered parties in interest in Chapter 11 proceedings, courts will have to determine where to draw the line for more peripherally-interested parties on a case-by-case basis.