

Client Update

Breaking Ranks: Garlock Reaches Unprecedented Deal with Future Claims Representative on Value of Trust for Asbestos Claims

NEW YORK

Mark P. Goodman
mpgoodman@debevoise.com

Robert D. Goodman
rdgoodman@debevoise.com

M. Natasha Labovitz
nlabovitz@debevoise.com

Maura Kathleen Monaghan
mkmonaghan@debevoise.com

Shannon Rose Selden
srselden@debevoise.com

My Chi To
mcto@debevoise.com

In another major development in a case that continues to redefine the standard procedures in asbestos-related bankruptcy proceedings, on January 13, 2015, Garlock Sealing Technologies LLC announced that it had reached an agreement with the representative for future asbestos claimants that would settle all present and future asbestos claims for \$358 million. The current net present value of the settlement is reportedly \$205 million – considerably higher than the bankruptcy court’s liability estimate of \$125 million, but well below the \$1.3 billion plaintiffs had been seeking.

The settlement appears to be the first time that a Future Claims Representative (“FCR”), which represents the interests of future asbestos claimants, has broken rank with the Asbestos Claimants Committee (“ACC”), which represents current asbestos claimants. Although it may be too early to assess how the settlement will impact the confirmation of Garlock’s reorganization plan, the first-ever settlement between a debtor and the FCR independent of the ACC – especially one for substantially less than the amount plaintiffs had been seeking – is a significant development that may add a new page to the asbestos defendants’ playbook.

BACKGROUND

Garlock produced and sold asbestos gaskets, sheet gasket material and packing used in pipes and valves. Its products were generally wrapped with asbestos thermal insulation produced by other manufacturers. Originally, Garlock was highly successful in settling claims brought by victims of asbestos-related diseases. However, by the early 2000s, the thermal insulation defendants had filed for bankruptcy, thus removing them from the tort system and leaving companies like Garlock facing the risk of enormous adverse verdicts in

mesothelioma wrongful death cases. In June 2010, Garlock filed for bankruptcy protection.

2014 DECISION REJECTS "SETTLEMENT" APPROACH FOR DETERMINATION OF AGGREGATE LIABILITY

In order to determine the amount of Garlock's asbestos liability for purposes of creating a sufficiently funded asbestos trust under Section 524(g) of the Bankruptcy Code, the bankruptcy court held an estimation hearing. Relying on a "settlement" approach focused on Garlock's history of settling mesothelioma claims, the ACC and FCR argued that Garlock's liability was between \$1 billion and \$1.3 billion. Relying on a "legal liability" approach focused on the merits of the claims, Garlock argued that its liability for present and future mesothelioma claims was approximately \$125 million.

On January 10, 2014, Judge George Hodges of the Bankruptcy Court for the Western District of North Carolina rejected the plaintiffs' "settlement" approach and held that \$125 million would be sufficient to satisfy Garlock's liability.¹ The court found that Garlock's settlement history did not accurately reflect fair settlements for two main reasons. *First*, plaintiffs' attorneys had withheld evidence that their clients had been exposed to other asbestos products, thereby making it appear that Garlock's product was the sole or major source of the plaintiffs' exposure. At the same time as they were withholding evidence of their clients' exposure, plaintiffs' attorneys were filing claims seeking compensation from the bankruptcy trustees of the companies that made the products their clients denied encountering. (Earlier in the case, Garlock had prevailed in a discovery dispute and gained access to the trust applications of plaintiffs who had previously sued Garlock in the tort system.) *Second*, Garlock's settlement data represented, in significant part, defense costs rather than its actual liability.

Turning to the merits of the claims against Garlock, the court found that the aggregate liability for present and future claims totaled \$125 million – \$25 million for present claims and \$100 million for future claims. The court's conclusion was informed by evidence of the claimants' exposure to other asbestos products (thus reducing Garlock's share of liability), and the fact that Garlock's product was unlikely to cause long-term high levels of asbestos exposure.

¹ *In re Garlock Sealing Technologies, LLC*, 504 B.R. 71 (Bankr. W.D.N.C. 2014).

POTENTIAL IMPLICATIONS OF GARLOCK'S DEAL WITH THE FCR

One year after the court's decision on liability, Garlock announced its deal with the FCR and filed a revised plan of reorganization. Under the terms of the plan, which the FCR agreed to support, \$250 million would be contributed up front, and \$77.5 million would be contributed over the following seven years.² An additional \$30 million would be contributed to cover litigation costs that would arise if claimants elect to forgo settlement options and litigate their claims in court.³

Although it may be years before the Garlock bankruptcy saga finally reaches its conclusion, Garlock's deal with the FCR – and the proceedings that led up to the deal – may provide the framework for substantial changes in how asbestos claims are negotiated. *First*, the deal shows that the ACC and the FCR do not always stick together. Following the Garlock precedent, future debtors might consider focusing their negotiation efforts on the FCR, especially if the ACC proves recalcitrant. *Second*, the deal underscores the importance of seeking discovery of duplicative claims filings. By obtaining discovery, Garlock was able to present evidence that contributed to the court's finding that future claims account for *four times* as much of Garlock's aggregate liability as current claims – \$100 million versus \$25 million. That finding may have provided the impetus for the FCR to break rank and argue in favor of confirmation of a Plan that has the approval of the representative of four-fifths of the claims. And third, if the reorganization plan is confirmed – over what is likely to be strong opposition from the ACC – Garlock's decision to agree to fund the Trust at more than the amount the court already ruled was sufficient (although far less than sought by the ACC) may prove to be a wise choice that is followed by future debtors.

As with many of the developments in the Garlock bankruptcy, it remains to be seen how the deal between Garlock and the FCR will impact the landscape of future negotiations between asbestos claimants and defendants. At a minimum, however, asbestos defendants should consider the possibility of independent negotiations with the FCR – especially in cases where future claimants account for a substantial majority of the trust.

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Please do not hesitate to contact us with any questions.

² See Debtors' Second Plan of Reorganization, *In re Garlock Sealing Technologies, LLC*, No. 10-31607, Dkt. No. 4306 (Bankr. W.D.N.C. Jan. 14, 2015), at §§ 7.3.1-7.3.2.

³ See *id.* at § 7.3.1.