1994 WL 16035112 (C.A.11) (Appellate Brief)
United States Court of Appeals,
Eleventh Circuit.

David G. EPSTEIN, Legal Representative for the Future Claimants, Appellant,

v.

THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF THE ESTATE OF PIPER AIRCRAFT CORPORATION, Appellee.

No. 94-4745.
December 6, 1994.

On Appeal from the United States District Court for the Southern District of Florida

Amicus Brief

Elizabeth Warren, William A. Schnader ProfessorK, of Commercial Law at the University of Pennsylvania Law School.

***i** *TABLE OF CONTENTS*

***ii** *TABLE OF CITATIONS*

CASES

OTHER AUTHORITIES

***1** *STATEMENT OF THE ISSUES*

Amicus incorporates by reference herein the Statement of Issues Presented set forth in the Brief of Appellant, filed in the above-captioned case on October 26, 1994.

STATEMENT OF THE CASE (Interest of Amicus)

Amicus is Elizabeth Warren, William A. Schnader Professor of Commercial Law at the University of Pennsylvania Law School. I have taught Bankruptcy Law for fifteen years at the University of Texas, the University of Houston,

the University of Michigan, Harvard Law School and the University of Pennsylvania. I am the coauthor of a leading casebook on Debtor-Creditor Law, *The Law of Debtors and Creditors* (with Westbrook), and a new casebook on secured lending, *Secured Transactions: A Systems Approach* (with LoPucki). I am also a co-principal investigator of the largest empirical study of the bankruptcy system, reported in *As We Forgive Our Debtors: Bankruptcy and Consumer Credit in America* (with Sullivan and Westbrook) and a new, twenty-three district, 3,450 case study of business bankruptcies that is currently underway.

My continuing academic interest in the scope of the Bankruptcy Code and the treatment of future claimants against faltering companies causes me to submit this amicus brief to the Court. I ***2** have written on the subject as part of larger works on the bankruptcy system, and those works are cited herein. My interest is strictly academic; I have not represented any party in this or any other dispute involving future claimants. I have received no compensation for my work on this amicus, and I have no stake in the outcome of this or any other case currently before the court.

SUMMARY OF ARGUMENT

I have no doubt that every party petitioning this court for expedited consideration of an appeal from a district court ruling argues that the legal issue presented to the court is of the utmost consequence. In this case, however, the claim that the legal issue at stake relates to the very heart of an important part of the legal system is not even a slight exaggeration. How future claimants can be dealt with in the course of a business reorganization or liquidation under the bankruptcy laws is a question that goes to the essence of what bankruptcy can accomplish and the reach of the justice it may dispense to parties owed obligations by failing businesses.

The district court in *In re Piper,* 168 B.R. 434 (S.D. Fla. 1994) has sharply narrowed the range of options available to a bankrupt business to deal with all those who may claim its assets. If allowed to stand, the implications for failing businesses, for those who are trying to put the assets of those businesses back ***3** into productive use, for those who face uncompensated injuries, and for those who have other claims against the business are profound. This is not a simple case of debtor versus creditor, a decision in which favoring one party necessarily injures another. Instead, this is a question about the scope of the bankruptcy laws, about whether they provide a final opportunity to separate the activities of the debtor's pre-bankruptcy past from those of its post-bankruptcy future, and whether all claimants from that past have a right to treatment on an equal footing. When a broad question of scope has been raised by the district court, it deserves the timely attention of the Court of Appeals.

ARGUMENT AND CITATION OF AUTHORITIES

A. *Background: The Claims Process in the Bankruptcy System*

I was asked by the Federal Judicial Center to write a summary of the operation of the business bankruptcy system, explaining the most important features in non-technical language for use by the non-specialist federal courts. In the resulting book, [1] which was reviewed by judges throughout the federal system before publication, claims are featured prominently in the first ***4** substantive chapter. I explain the starting point of bankruptcy law for both liquidations and reorganizations:

A profound shift in the relationship between debtors and creditors occurs at the filing of a bankruptcy petition. A new estate is created, comprising both the legal and economic interests of the old debtor and the collective economic and legal interests of the creditors. Creditors lose their individual collection rights against the debtor, and they are forced to deal with an estate operating on behalf of all the creditors. [2]

This fundamental shift is captured most vividly in the claims process:

> The transformation of claims against a debtor into claims against an estate protects the collective nature of the bankruptcy proceeding. By converting creditors' claims against the pre-bankruptcy debtor to claims against a bankruptcy estate, the Code gives the estate manager a position to account for, to monitor, and to value each charge against the estate's assets. [3]

The extent to which the Bankruptcy Code forces all parties who may call on the debtor for payment into a collective proceeding is governed by the interpretation of the claims provisions in the Code, section 101(5). If this provision is given a narrow reading, the impact on the bankruptcy process is profound: bankruptcy will deal with less than all of the obligations arising from the pre-bankruptcy behavior of the debtor. If the provision is read broadly, then a bankruptcy case may reasonably ***5** deal with all the obligations incurred by the debtor, making a cleavage between the debtor's pre-filing past, which will be dealt with collectively, and the debtor's post-filing future, in which parties may deal individually with the surviving entity.

The practical implications of this difference are enormous. If an obligation of the debtor is not dealt with in the bankruptcy, then the obligation may survive after the bankruptcy case is completed. In some cases, this means that creditors who have a claim tied to the debtor's pre-bankruptcy past may disrupt the debtor's post-bankruptcy future. A claimant who is not dealt with in the collective bankruptcy proceedings, for example, and whose claim is therefore not processed and paid on par with other claimants, may come back to the surviving business after a plan is confirmed to assert claims for compensation that disrupt the post-filing debtor's business. In some bankruptcy cases, such as a Chapter 11 debtor's selling its assets or in all Chapter 7 cases, the party who is unable to make a clam against the estate knows that when it returns to the debtor to make its claim later, that no debtor will exist. The creditor who is required to wait will find in some cases that there is nothing left to wait for.

The question of what claims shall be covered in a bankruptcy proceeding involves the distributional issues at stake in any bankruptcy action:

> The claims process is critical to the distributional objectives of the Code. As claims are estimated, valued, and assigned certain priority rights, the distributional ***6** scheme of the bankruptcy system comes to life. Whether an obligation owed by a debtor becomes a claim -- and can thus be discharged -- raises a critical distributional question among competing creditors. Similarly, the discharge of claims or the rewriting of payment obligations over time necessarily distributes the assets of the estate among competing parties. [4]

If a creditor is denied the opportunity to participate in a final distribution by a failing debtor, the Bankruptcy Code fails to deliver its promised equality of treatment. Similarly, if a creditor can profit from being treated as a non-claimant and later collect more from the surviving business, the distributional goal of equality of treatment among creditors is again violated.

In a law review article describing the overall workings of the bankruptcy system, I focused on the importance of including all parties who may raise a claim against a debtor for its prefiling behavior in a single bankruptcy action:

> The bankruptcy system equalizes the treatment of creditors and parties affected by business failure when timing variations leave them with very different formal rights. For example, those who have been injured by a debtor's product, such as workers who have been exposed to asbestos, can bring state law actions only after their injuries are manifest. In the case of a failing company, this rule leaves early claimants paid in full, while later claimants with the same rights discover there is nothing left to collect. Bankruptcy law, however, may resolve both present and future claims at once, giving comparable outcomes to those with similar legal rights, but different ***7** timetables for reaching the courthouse. The bankruptcy court may approve a plan to pay victims over time using similar procedures and providing similar payouts regardless of when their injuries appeared. The Code generally minimizes the consequences of timing differences among the debtor's prepetition creditors as it reorders claims based on an underlying similarity of rights. [footnote omitted] [5]

One final point about the impact of a decision about claims is in order. The claims question is implicated in the most difficult cases facing the courts over the next dozen years. Environmental claims and mass tort claims, for which we have currently only seen the tip of the iceberg, are multiplying against American businesses. A significant number of those businesses will find their way into the bankruptcy courts. If hastily made judicial decisions constrain the reach of the bankruptcy system to deal with these problems, it will be no victory for judicial economy. Instead, decisions creating false boundaries that limit which claims can be collectively treated in a bankruptcy case will spawn countless more cases, as parties dispute whether their particular facts fall inside or outside the newly modified claims definition. Moreover, parties will spend the intervening time maneuvering for position in and out of the bankruptcy system rather than submit their difficulties to a single forum for a unified resolution. Only by keeping the ***8** claims definition broad, as Congress wrote it and as the Supreme Court has thus far consistently interpreted it, can bankruptcy serve as a forum to resolve multiple disputes without expending endless resources on disputes about whether the proceedings include all the disputants.

The kinds of obligations drawn into the bankruptcy process as claims against the estate powerfully affect both the collective nature of the bankruptcy proceedings and the distributional impact of bankruptcy. The lines that are drawn to determine which obligations are included within the definition of claim are the lines that determine whether the bankruptcy goals of equality of treatment among creditors and preservation of the going concern value of a business can be realized.

B. *The Piper Decision*

The district court in *In re Piper* offered only two grounds for its decision. The court acknowledged that "[o]ne of the basic policies of the Bankruptcy Code is the equal treatment of similarly situated creditors." *Piper* at 5. It concluded, however, that the Future Claimants are not similarly situated to other claimants because "Piper owed no legal obligations to them at the time of its filing." *Piper* at 5. With respect, however, I would note that the Code specifically deals with this aspect of "similarly situated," expressly including claims that are "unliquidated," "contingent," "unmatured," and "disputed." That ***9** a party could not point to a legal obligation owed to it at the time of filing was clearly irrelevant to Congress.

The district court bolstered its opinion by discussing the "formidable practical and logistical problems" of notification of Future Claimants. The court is correct that the problems are difficult. A number of academics and practitioners have wrestled with the problem of notification and suggested several solutions, [6] but the difficulty of notification does not mean that the parties should be barred from attempting to develop an adequate system for dealing with Future Claimants. Moreover, I would again suggest with respect that "practical and logistical problems" are an inadequate basis

for disregarding the language and intent of Congress and sharply constraining the scope of the bankruptcy system so that those same problems can be pushed elsewhere in the legal system.

***10** In a debate with Professor Baird, I described the bankruptcy system six years ago:

> The Bankruptcy Code clearly rejects the alternative of leaving future claimants uncompensated. It defines "claim" broadly to pull future creditors into the debtor's distribution plan and to require participation by anticipated claimants. The Code does not specifically address how to establish funds to pay future claimants and determine appropriate payout priorities, and as a result, the courts must take on the difficult task of devising workable plans. Nonetheless, it is clear that dealing with the effects of default on future claimants was intended to be a significant feature of bankruptcy's distributional scheme. [footnotes omitted] [7]

While this article has received substantial scholarly attention and some criticism for some of the ideas developed therein, to my knowledge, no one has suggested that my summary of the treatment of future claimants is inaccurate or taken issue with my conclusion that the treatment of future claimants is an essential feature of the equality of distribution devised by the Code.

The practical and logistical problems created by the district court's decision became clear within weeks after its publication. The bankruptcy court had to consider another claimant, one who was injured after the *Piper* bankruptcy filing. Notwithstanding his own earlier opinion which had made it clear that any post-filing accident victim would not have a claim in the *Piper* bankruptcy case and the district court's affirmation of ***11** that sharp line to separate pre-filing and post-filing accident victims, Judge Mark decided that the post-filing creditor should also have a claim in the *Piper* bankruptcy. Judge Mark describes his own earlier decision as "incomplete" and "the wrong legal conclusion." *Id.* at 6. Judge Mark then strains to draw a new line between claimants and non-claimants at yet another, not entirely determined point. In recognizing that a decision to distinguish pre-filing from post-filing accident victims was both impractical and contrary to bankruptcy policy, Judge Mark rejects the line embraced by the district court decision that is currently on appeal to this Court.

CONCLUSION

The decision to limit the scope of the bankruptcy system by denying access to any parties whose injuries from the debtor's pre-bankruptcy conduct are sustained after the bankruptcy filing has a powerful impact on the bankruptcy system. Such a decision will constrain the ability of the parties to settle all disputes related to a debtor's pre-bankruptcy past in a single forum. It will encourage both strategic behavior and multiple lawsuits. It will undermine the central principle of the Bankruptcy Code -- to treat like claimants alike -- leaving those with pre-filing injuries to a collective treatment in the bankruptcy proceeding while those whose injuries arise later founder alone, sometimes ***12** receiving much better subsequent treatment and other times receiving no compensation at all.

I urge this court to hear the issues raised by *In re Piper* before any steps taken by the parties may moot the appeal and to make clear that the district court decision excluding Future Claimants is not the law of the Eleventh Circuit.

Footnotes

1 Elizabeth Warren, *Business Bankruptcy* (Federal Judicial Center 1993).

2 Id. at 61.

3 Id. at 61-62.

4 Id. at 61.

5 Elizabeth Warren, *Bankruptcy Policymaking in an Imperfect World,* 92 Mich. L. Rev. 336, 358-59'(1993).

6 An extremely thoughtful analysis is offered in Ralph R. Mabey and Jamie A. Gavrin, *Constitutional Limitations on the Discharge of Future Claims in Bankruptcy,* 44 S.C. L. Rev. 745 (1993). The National Bankruptcy Conference has developed proposed statutory amendments to clarify the notification process required, working on the assumption that future claims are appropriately covered in a bankruptcy action. National Bankruptcy Conference, *Reforming the Bankruptcy Code: Final Report May 1. 1994* 281-87 (1994).

7 Elizabeth Warren, *Bankruptcy Policy,* 54 U. Chi. L. Rev. 775, 787 (1987).

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