

**Extra-Territorial Application of Section 524(g) of the U.S. Bankruptcy  
Code to Non-U.S. Asbestos Claims**

**In re Federal-Mogul, Inc., et al.**

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I. Background

On October 1, 2001, Federal-Mogul Corporation and 156 of its subsidiaries and affiliates filed for Chapter 11 under the United States Bankruptcy Code in the United States Bankruptcy Court for the District of Delaware. One hundred and thirty four of the Debtors were entities created under the laws of the United Kingdom. Only twenty-three were U.S. entities. Also on October 1, 2001, each of the U.K. Debtors concurrently commenced administration proceedings pursuant to Part II of the English Insolvency Act of 1986 in the High Court of Justice, Chancery Division in London, England. One additional entity, that is a Scottish rather than an English entity, obtained an administration order on April 6, 2002 from the Court of Session in Edinburgh, Scotland.

Federal-Mogul Corporation is a multi-national conglomerate manufacturing automotive and vehicle parts and systems for end-use customers in the automotive, small engine, heavy duty and industrial markets. The history of the corporate family dates back to 1899. Federal-Mogul Corporation, the parent company, is a public U.S. company incorporated in Delaware. Federal-Mogul's business operations are comparatively strong, notwithstanding some softness in the automotive and vehicle industries. The major reason for the Federal-Mogul bankruptcy filings was its exposure to significant asbestos personal injury and property damage litigation and liabilities arising out of asbestos-containing products used and manufactured by several Federal-Mogul subsidiaries and affiliates in the U.S. and abroad.

Since the filing of the bankruptcy cases, the Debtors have acted as debtors-in-possession in the United States, with management retaining control of the operations of the Debtors' varied

businesses. No such similar concept exists under U.K. insolvency law. Therefore, since the commencement of the administration proceedings, the English and Scottish Debtors have been overseen by the Joint Administrators appointed by the English and Scottish courts. Pursuant to a cross-border insolvency protocol entered by both the U.S. Bankruptcy Court and the English High Court of Justice immediately after the filing of the cases, and subsequently by the Scottish Court of Session, the Joint Administrators have agreed to cooperate with the Debtors' management to the extent allowable under U.S. and U.K. insolvency law in order to develop plans of reorganization for the businesses of the U.K. Debtors and to enable the Federal-Mogul board of directors to manage the U.K. Debtors' affairs during the pendency of the insolvency proceedings.

## II. Section 524(g) of the U.S. Bankruptcy Code

Section 524(g) was Congress's attempt in 1994 to create a model for the restructuring of companies with significant asbestos liabilities. Asbestos litigation was both overwhelming the tort systems of various states, and causing otherwise healthy companies to undergo the risks of bankruptcy to use the existing provisions of the Bankruptcy Code to manufacture some type of asbestos-claim relief. Using a model structure that came out of the *Johns-Manville Corp.* bankruptcy case in the mid-eighties, Congress added Section 524(g) to the Bankruptcy Code.

The cornerstone of Section 524(g) is the requirement that asbestos creditors, through a trust, become the owners of the debtor. In exchange for this ownership, all asbestos claims, both current and future,<sup>1</sup> are channeled to the trust for handling, and the debtors obtain a permanent injunction against any pending or future asbestos liabilities.

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<sup>1</sup> Future claims can be channeled to the trust provided certain procedures are followed, including the appointment of a futures representative.

The injunctions that can be issued under Section 524(g) are extremely broad in order to effectuate the complete restructuring of the debtor. Thus the injunction not only protects the debtors, but also buyers of assets from the debtors, lenders to the debtors, and any third parties who are identifiable from the terms of the injunction and have asbestos liability that is, in some manner, derivative of the debtors' asbestos liability. The ability to be free from the multi-jurisdictional tort system and the escalating costs of asbestos litigation defense has made chapter 11 and Section 524(g) structured plans of reorganization the preferred method of dealing with asbestos claims in the U.S.

No such equivalent restructuring method exists under applicable U.K. insolvency laws. Historically, there have been less asbestos cases in the United Kingdom than in the United States, and U.K. law and the U.K. courts have been less receptive than U.S. courts to expanded concepts of liability for asbestos claims. However, the number of asbestos personal injury claims asserted in the U.K. has been growing, and U.K. attorneys have been quick to learn from their U.S. cousins. Therefore, Federal-Mogul, in order to effectively reorganize, needed to find a global solution to its asbestos problems.

### III. The Federal-Mogul Plan

Federal Mogul filed its Second Amended Joint Plan of Reorganization, as Modified on or about May 10, 2004 (the "Plan"). The related disclosure statement was presented to the Court on May 11, 2004, and will be approved subject to certain modifications. While as of the time of the writing of this paper, certain terms of the Plan are contested by a variety of creditors, in general, the Plan effectuates a compromise between the Debtors and their major creditor constituencies. The Plan is primarily based on a compromise and agreement among the Unsecured Creditors' Committee and the Asbestos Claimants' Committee, pursuant to which 49.9% of the stock of the

reorganized Federal-Mogul Corporation will be distributed to noteholders and bondholders and 50.1% of the stock of the reorganized Federal-Mogul Corporation will be distributed to a trust established pursuant to Section 524(g) of the Bankruptcy Code for the benefit of holders of asbestos personal injury claims. Unsecured trade creditors will be paid a percentage of their claims in cash over time, and secured creditors will receive payment on their claims, either in cash or through restructured secured notes.

The Plan includes an extensive permanent injunction protecting not only the reorganized Debtors, but all their non-debtor affiliates and subsidiaries, their lenders, creditors, any person who bought assets from the Debtors during the case, certain contractual indemnification creditors and any settling insurance carrier, from all past, present and future asbestos personal injury claims. Appended to the Plan is a Trust Agreement that establishes the Trust that will take title to the stock and certain other assets of the Debtors and handle and resolve all asbestos personal injury claims post-effective date. Also appended to the Plan are a set of procedures that will be used by the Trust to determine the validity of asbestos personal injury claims, resolve them and pay them.

What is significant about the Plan Trust and Trust procedures, and the injunctions that support them, is that they are all intended to apply extraterritorially. The Plan is intended to not only resolve the bankruptcy cases and asbestos personal injury claims of the U.S. Debtors, but also of the U.K. Debtors. In order to facilitate and effectuate the U.K. Debtors' emergence from both chapter 11 and their concurrent U.K. administration proceedings, the proponents of the Plan have prepared forms of Schemes of Arrangement and Company Voluntary Arrangements for certain of the U.K. Debtors.

#### IV. The U.K. Proceedings

The Debtors have indicated that it is their intention to get the Administrators of the U.K. Debtors to apply to the English and Scottish courts for orders that meetings of certain classes of creditors be convened for the purposes of considering and, if thought appropriate by the courts, approving Schemes of Arrangement and Company Voluntary Arrangements (the “Arrangements”) in relation to F-M UK Holding Limited and those U.K. Debtors with existing or anticipated asbestos personal injury and property damage claims against them.

The Arrangements will, in all material respects, mirror the provisions of the Plan insofar as they relate to (i) asbestos-related claims against the U.K. Debtors, and (ii) bank claims, surety claims and noteholder claims against F-M UK Holding Limited. With respect to the holders of asbestos personal injury claims, the Arrangements will each propose the creation of a Trust,<sup>2</sup> which will have as its purpose the evaluation and payment of all asbestos personal injury claims for which the U.K. Debtors are liable. After hearings before the applicable U.K. courts, all creditors affected by the Arrangements will be notified of the details of the meetings of creditors which will be held for the purpose of voting on the Arrangements.

However, under U.K. insolvency law, the only persons with authority to recommend the Schemes of Arrangement and Company Voluntary Arrangements are the Joint Administrators. They have not yet agreed to proceed in the manner set forth above. Negotiations are ongoing, and the Administrators are conducting due diligence on certain of their concerns. These include the concern that certain U.K. Debtors would provide a better return to creditors if liquidated and that certain procedures for claims determination set forth in the Trust established for asbestos personal injury claims discriminate unfairly against U.K. asbestos personal injury claimants. The Administrators have also expressed concern that if these issues cannot be resolved, even if

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<sup>2</sup> The same Trust created under the Plan.

the Arrangements are proposed, the U.K. creditors might not support them and further, that the U.K. courts might refuse to approve the Arrangements for the U.K. Debtors, even as a matter of comity.

In the event the Administrators' concerns can be assuaged and they propose the Arrangements, the Administrators and the proponents of the Plan in the U.S. will seek approval of the Arrangements in accordance with English and Scottish insolvency laws. If approved by the U.K. courts, all U.K. asbestos personal injury claimants would be subject to the injunctions set forth in the Plan under Section 524(g) of the Bankruptcy Code based on the injunctions issued by the applicable U.K. courts.

In the event the Administrators refuse to propose the Arrangements, the Debtors have informed the Bankruptcy Court that they believe the same results can be obtained through a "controlled realization," which is essentially a U.K. liquidation. Under this scenario, Federal-Mogul believes that it would be the successful bidder at any sale of the businesses of those U.K. Debtors that Federal-Mogul believes constitute an integral part of its business operations. As the buyer of assets free and clear under applicable U.S. and U.K. law, the Debtors believe they still would be entitled to protection from U.K. asbestos personal injury claims in accordance with Section 524(g) of the Bankruptcy Code. Certain significant creditors of the U.K. Debtors have contested this assertion, and the actual results remain to be seen. At this time, it is anticipated Federal-Mogul's U.S. Plan confirmation hearing will be set some time in July 2004. No date has been set for any hearings in the U.K.



## Judith Elkin

Ms. Elkin is the Co-Chair of the Finance Section and a partner in the Business Reorganization and Bankruptcy Practice Group. Ms Elkin has in excess of 20 years of experience representing debtors, creditors, creditors' committees, lenders, trustees, acquirors and other parties in interest in reorganization proceedings and financial restructurings. She is also a bankruptcy litigator with particular expertise in bankruptcy appeals. She is a frequent speaker both in and outside the United States, having spoken on insolvency issues at conferences in New Zealand, India and Great Britain.

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**AREAS OF EXPERIENCE**

Representation of Debtors, Creditors, Creditors' Committees, Lenders and Acquirors in bankruptcy cases and out of court restructurings in and outside the United States  
Representation of parties in bankruptcy litigation and bankruptcy appeals

**REPRESENTATIVE CASE INVOLVEMENT**

America West Airlines  
Dailey International  
El Paso Electric Company  
Enron Corp.  
Federal-Mogul Corporation  
General Wireless, Inc.  
Mirant Corporation  
National Gypsum Corporation  
Southmark Corporation  
United States Brass Corporation

**EDUCATION**

J.D. *cum laude*, University of Wisconsin, 1981  
B.A. *summa cum laude*, Binghamton University, State University of New York, 1978

**ADMITTED TO PRACTICE**

Texas Supreme Court; U.S. Supreme Court; U.S. Court of Appeals for the Fifth, Sixth, Tenth and Eleventh Circuits; U.S. District Court for the Northern, Southern, Eastern and Western District of Texas

**Representative transactions include:**

Representation of major foreign lender and co-chair of Unsecured Creditors' Committee in Enron Corp. chapter 11 case

Representation of debtor in possession in restructuring and divestiture of certain US and foreign assets

Negotiation of major recovery for Korean company that was largest unsecured creditor in reorganization of wireless telecommunications company

Represented secured lender in arresting a large private yacht in the Jersey Islands in collection of a multimillion dollar bank obligation

Represented Unsecured Creditors' Committee in successful restructuring of \$2 billion electric utility

Assisted acquiror in acquisition of foreign assets out of TWA chapter 11 case

**MEMBERSHIPS AND PROFESSIONAL ASSOCIATIONS**

American Bar Association: Litigation Section (Co-Chair, Bankruptcy and Insolvency Litigation Committee 1997-2001), Section of Business Law (Business Bankruptcy Committee; International Subcommittee); International Bar Association: Committee J (International Insolvency); American Bankruptcy Institute; COMBAR (Honorary North American Member of Commercial Bar Association of United Kingdom); International Women's Insolvency & Restructuring Confederation (IWIRC) Secretary/Treasurer 2002-2004; Board of Directors/Executive Board/Secretary, Dallas Zoological Society; International Insolvency Institute