Products Liability Law Daily Wrap Up, TOP STORY—MOTOR VEHICLES—S.D. N.Y. Bankr.: $7 to $10 billion in claims related to GM ignition switch defect barred, (Apr. 16, 2015)

Products Liability Law Daily Wrap Up

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By John W. Scanlan, J.D.

The U.S. Bankruptcy Court handling the case of General Motors has barred an estimated $7 to $10 billion in claims brought by plaintiffs in ignition switch defect litigation against General Motors seeking damages for purely economic losses, such as the diminution of value of their vehicles (Economic Loss Plaintiffs), as well as those brought by plaintiffs who bought their vehicles and who had been in accidents before the creation of post-bankruptcy New GM (Pre-Closing Accident Plaintiffs). However, the court allowed the Economic Loss Plaintiffs to pursue claims against New GM based solely on New GM's independent post-bankruptcy sale acts and not on any acts by Old GM and to file late claims; but refused to modify Old GM's reorganization plan or to allow the plaintiffs to tap the assets of a Trust set up to compensate Old GM creditors (*In re Motors Liquidation Co.*, April 15, 2015, Gerber, R.).

Background. In March 2009, the U.S. Treasury gave General Motors 60 days to develop a viable restructuring plan or it would be forced to liquidate. Because the company was unable to do so, GM and three affiliates filed for Chapter 11 bankruptcy on June 1, 2009. GM also filed a motion to sell its assets pursuant to Sec. 363 of the U.S. Bankruptcy Code, which would allow it to free itself of most of its prepetition liabilities. The bankruptcy court approved GM's proposed Sale Order, which authorized the sale of the assets of "Old GM" to new entity "New GM" free and clear of all successor liability claims except for those liabilities contractually assumed, with the result that litigation claimants were prohibited from asserting claims against New GM or the purchased assets.

The court also issued a Sales Procedures Order that provided for actual notice of the sale (the Sale Notice) to 25 categories of persons or entities and for notice by publication in a number of publications. A number of parties objected to the proposed Sale Order; the court observed that generally they objected to the Free and Clear Provisions that limited successor liability or asserted that New GM should assume certain additional types of claims. Certain successor liability objectors argued that Bankruptcy Code Sec. 363(f) did not permit New GM to avoid potential successor liability because this section authorized sales free and clear of interests in property to be sold, not *in personam* claims against New GM under successor liability theories. However, the court rejected those arguments.

Under the Sales Agreement, which GM filed with the Sale Motion, New GM would assume responsibility for all accidents or incidents giving rise to death, personal injury, or property damage taking place after the date of the closing of the sale, regardless of whether the vehicle in question was manufactured by Old GM or New GM. However, products liability claims arising from accidents or incidents before the closing date, as well as liabilities for prepetition claims based in tort, would be retained by Old GM. The final Sale Order contained five provisions protecting New GM from successor liability. Upon closing of the sale, New GM gave shares of New GM securities to Old GM to be distributed to creditors of Old GM.

In September 2009, the court set November 30, 2009, as the deadline for proofs of claim to be filed against Old GM (the Bar Date) and approved the form and manner of notice. This Bar Date Order allowed for publication notice to holders of unknown claims; the plaintiffs in the present case received publication notice only.

On March 31, 2011, the bankruptcy court confirmed Old GM's Plan, and the parties stipulated that it was substantially consummated on that date. The confirmation order authorized the creation of the Old GM General Unsecured Creditors Trust (GUC Trust), which held the New GM securities given to Old GM to be distributed

to beneficiaries of the GUC Trust. Beneficiaries were limited to: holders of allowed general unsecured claims against Old GM that existed on the effective date; holders of claims asserted against GM that were disputed on the effective date but which were later allowed; holders of potential general unsecured claims that might arise in connection with a lien avoidance action related to a mistakenly released financial statement; and the holders of units of beneficial interest in the GUC Trust.

By May 2011, 75 percent of the New GM securities and 30 million GUC Trust Units were distributed to those who had made allowed claims as of the effective date; the remaining GM securities were held to fund claims that were still in dispute and Trust administrative costs. By September 2014, more than 89 percent of New GM securities and nearly 32 million GUC Trust units had been distributed. After the Trust administrator disclosed another planned distribution in November 2014, plaintiffs' counsel advised the administrator not to make additional distributions until adequate reserves had been set aside for the plaintiffs' potential claims. The administrator refused; the plaintiffs decided for "admitted strategic reasons" not to seek a stay of the distribution, and it took place as planned. As of December 2014, the GUC Trust had assets of about $773.7 million. A provision of the Sale Agreement requires New GM to provide additional securities to the GUC Trust if total allowed general unsecured claims against Old GM exceed $35 billion.

After New GM announced in March 2014 that it would begin recalling vehicles due to ignition switch defects, a number of class actions were filed against it. New GM filed a motion to enforce the Sale Order, asserting that most of the claims in the various class actions were prohibited by the Sale Order's Free and Clear Provisions and the provisions limiting successor liability. MDL 2543 was established to handle the cases, and following an August case management conference, lead counsel for the plaintiffs in the MDL filed a pre-sale consolidated complaint for those who had bought vehicles with an ignition switch defect before the sale closing date, as well as a post-sale consolidated complaint for those who bought vehicles with ignition switch defects after the sale. The parties identified four threshold issues for the court: due process, remedies, Old GM claims, and equitable mootness.

Due process/entitlement to notice. Owners of GM cars with ignition switch defects were denied notice of the 363 sale to which they were entitled by due process, as well as notice before expungement of claims. The court first determined that the plaintiffs were entitled to due process for both the Sale Order and the Claims Bar Order. The court disagreed with New GM's arguments that successor liability claims belonged to Old GM rather than to the Economic Loss Plaintiffs and the Pre-Closing Accident Plaintiffs, observing that the plaintiffs were suing to advance their own personal interests rather than for the benefit of Old GM creditors generally.

The court next found that the plaintiffs were denied the notice required by due process. Under Second Circuit precedent, the issue was whether Old GM "acted reasonably in selecting means likely to inform persons affected," giving "the best notice practical under the circumstances." Publication by notice to owners of Old GM vehicles owners not known by Old GM to have been in an accident was sufficient, given the urgency of the circumstances surrounding the 363 sale. However, the court found that owners of vehicles with an ignition switch defect that had not been in an accident had "known" claims. Although it was a "close question," the court found significant the fact that at least 24 Old GM employees knew of the defect and the need to send out recall notices and that Old GM knew the names and addresses of the owners of affected Old GM vehicles. Because of the known safety risk requiring the recall, all of these owners were entitled to notice.

Due process/prejudice. Even though adequate notice was not given, the court stated that it was still necessary to consider whether the plaintiffs had been prejudiced before it could find that they were denied due process.

Both groups of plaintiffs were prejudiced regarding the Bar Date for filing claims. Unlike the 363 sale process, which took place under circumstances requiring a great deal of urgency regarding time, the deadline for filing claims was less urgent and the denial of the opportunity to file a claim was the classic example of prejudice. The failure to send out ignition switch defect recall notices clearly resulted in the denial of notice required by due process and prejudiced the plaintiffs concerning any claims they might have filed against Old GM.

The Economic Loss Plaintiffs and the Pre-Closing Sale Plaintiffs were not prejudiced when it came to the Free and Clear Provision of the Sale Order and successor liability—although the plaintiffs did not get adequate notice

of the 363 sale hearing, over 4 million people had received notice, including many who had vigorously contested the Free and Clear Provisions. Further, the plaintiffs did not show that the court's 2009 ruling barring successor liability was in error; their assertions that they could have defeated these provisions by means of public pressure or public outrage rested on speculation. The court noted that it had previously rejected arguments similar to those advanced by the plaintiffs here, and that neither plaintiff group made any new arguments.

However, the Economic Loss Plaintiffs had made a new argument that they had not previously had the opportunity to make: that they should have been allowed to bring claims regarding Old GM vehicles as long as the claims were based only upon conduct by New GM. They were prejudiced to the extent that they were not given the opportunity to make this argument in 2009. Therefore, the Economic Loss Plaintiffs, but not the Pre-Closing Accident Plaintiffs, were prejudiced by the failure to give proper notice of the 363 sale.

Remedies. Because they had been prejudiced by the lack of proper notice, the Economic Loss Plaintiffs were entitled to a remedy, even though the court found "great merit" in New GM's argument that taking away asset purchasers' property rights strikes at the heart of the understandings important to the bankruptcy system, because remedying a constitutional violation is more important than this concern.

The court rejected both the plaintiffs' argument that the proper remedy was to deny enforcement of the Sale Order as to the plaintiffs and New GM's argument that the plaintiffs' remedy, if any, was against the proceeds of the 363 sale, which had to be enforced as a whole or vacated as a whole. Regarding the Free and Clear provisions concerning successor liability, no remedy was required because there had been no prejudice and, thus, no due process violation. Regarding the Sale Order, the Economic Loss Plaintiffs were entitled to a remedy because they were not given the opportunity to argue that the Sale Order was too broad. As a result, the court concluded that it could exclude the Economic Loss Plaintiffs, but not the Pre-Closing Accident Plaintiffs, from compliance with the Sale Order regarding their overbreadth objections without voiding the Sale Order in its entirety. As such, the Sale Order's nonseverability provisions did not bar relief.

Regarding the denial of notice relating to the Bar Date Order, the court said that it may grant leave from the Order's deadline to file claims.

Successor liability. The court said that it would continue to enforce prohibitions against successor liability. New GM would be liable for any wrongful conduct of its own, but would not be liable for any wrongful conduct by Old GM. As a result, to the extent that the plaintiffs in this case sought to impose successor liability upon New GM, they actually were asserting claims against Old GM, the court said.

Equitable mootness. The plaintiffs' recovery against Old GM—the GUC Trust—was barred by the doctrine of equitable mootness. The court said that while a return of past distributions from all of Old GM's creditors was "unthinkable," it originally believed that the plaintiffs could share in assets remaining in the GUC Trust. However, the Trust pointed out that granting them this relief would require modification of the confirmation order and, thus, impairment of the rights of the Trust unitholders.

Applying Second Circuit precedent—the "*Chateaugay* factors"—for determining whether substantial consummation moots an appeal, the court found that three of the five factors weighed against overcoming the presumption in favor of mootness: (1) the GUC Trust's limited remaining assets could not be used to satisfy the plaintiffs' claims, (2) allowing $7 to $10 billion in additional claims at this point would be unjust to the purchasers of GUC Trust units after confirmation, and (3) the plaintiffs' strategic decision not to oppose additional distributions from the GUC Trust amounted to a failure to diligently pursue claims against the Trust. Thus, the equitable mootness doctrine protected the unitholders from modification of the Plan. The bankruptcy court observed that this would materially (and perhaps completely) impair the plaintiffs' ability to collect on any allowed claims against the GUC Trust, but the rights of the GUC Trust beneficiaries could not be impaired at this late date.

The next step. The bankruptcy court certified the decision for direct review by the Second Circuit, finding that the matter was one of considerable public importance, there were no controlling decisions of the Second Circuit, and an immediate appeal would be likely to advance proceeding both in the present case and in the MDL.

The court directed the parties to caucus and determine whether other issues remained to be decided by the bankruptcy court, and, if not, to attempt to agree on the form of a judgment.

The case is No. 09-50026 (REG).

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Companies: Motors Liquidation Co.; Wilmington Trust Co.; United States Trustee; GCG, Inc.; Official Committee of Unsecured Creditors of General Motors Corp.; Official Committee of Unsecured Creditors Holding Asbestos-Related Claims

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