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Brief of Amici Curiae Law Professors in Support of Appellees Regarding the "Abuse" Standard

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United States Court of Appeals

for the

Second Circuit

In Re: PURDUE PHARMA L.P., PURDUE PHARMA INC, PURDUE TRANSDERMAL TECHNOLOGIES L.P., PURDUE PHARMA MANUFACTURING L.P., PURDUE PHARMACEUTICALS L.P., IMBRIUM THERAPEUTICS L.P., ADLON THERAPEUTICS L.P., GREENFIELD BIOVENTURES L.P., SEVEN SEAS HILL CORP., OPHIR GREEN CORP., PURDUE PHARMA OF PUERTO RICO, AVRIO HEALTH L.P., PURDUE PHARMACEUTICAL PRODUCTS L.P., PURDUE NEUROSCIENCE COMPANY, NAYATT COVE LIFESCIENCE INC., BUTTON LAND L.P., RHODES ASSOCIATES L.P., PAUL LAND INC., QUIDNICK LAND L.P., RHODES PHARMACEUTICALS L.P., RHODES TECHNOLOGIES, UDF LP, SVC PHARMA LP, SVC PHARMA INC.,

Debtors.

(For Continuation of Caption See Inside Cover)

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF OF *AMICI CURIAE* LAW PROFESSORS IN SUPPORT OF APPELLEES REGARDING THE "ABUSE" STANDARD

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PURDUE PHARMA, L. P., PURDUE PHARMA INC, PURDUE TRANSDERMAL TECHNOLOGIES L.P., PURDUE PHARMA MANUFACTURING L.P., PURDUE PHARMACEUTICALS L.P., IMBRIUM THERAPEUTICS L.P., ADLON THERAPEUTICS L.P., GREENFIELD BIOVENTURES L.P., SEVEN SEAS HILL CORP., OPHIR GREEN CORP., PURDUE PHARMA OF PUERTO RICO, AVRIO HEALTH L.P., PURDUE PHARMACEUTICAL PRODUCTS L.P., PURDUE NEUROSCIENCE COMPANY, NAYATT COVE LIFESCIENCE INC., BUTTON LAND L.P., RHODES ASSOCIATES L.P., PAUL LAND INC., QUIDNICK LAND L.P., RHODES PHARMACEUTICALS L.P., RHODES TECHNOLOGIES, UDF LP, SVC PHARMA LP, SVC PHARMA INC.,

Debtors-Appellants-Cross-Appellees,

THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF PURDUE PHARMA L.P., et al., AD HOC COMMITTEE OF GOVERNMENTAL AND OTHER CONTINGENT LITIGATION CLAIMANTS, THE RAYMOND SACKLER FAMILY, AD HOC GROUP OF INDIVIDUAL VICTIMS OF PURDUE PHARMA, L.P., MULTI-STATE GOVERNMENTAL ENTITIES GROUP, MORTIMER-SIDE INITIAL COVERED SACKLER PERSONS,

Appellants-Cross-Appellees,

– v. –

THE CITY OF GRANDE PRAIRIE, as Representative Plaintiff for a Class Consisting of All Canadian Municipalities, THE CITIES OF BRANTFORD, GRAND PRAIRIE, LETHBRIDGE, AND WETASKIWIN., THE PETER BALLANTYNE CREE NATION, on behalf of All Canadian First Nations and Metis People, THE PETER BALLANTYNE CREE NATION on behalf itself, and THE LAC LA RONGE INDIAN BAND,

Appellees-Cross Appellants,

THE STATE OF WASHINGTON, STATE OF MARYLAND, DISTRICT OF COLUMBIA, U.S. TRUSTEE WILLIAM K. HARRINGTON, STATE OF CONNECTICUT, RONALD BASS, STATE OF CALIFORNIA, PEOPLE OF THE STATE OF CALIFORNIA, by and through Attorney General Rob Bonta, STATE OF OREGON, STATE OF DELAWARE, by and through Attorney General Jennings, STATE OF RHODE ISLAND, STATE OF VERMONT, ELLEN ISAACS, on behalf of Patrick Ryan Wroblewski, MARIA ECKE, ANDREW ECKE, RICHARD ECKE,

Appellees.

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INTEREST OF AMICI CURIAE AND SUMMARY OF ARGUMENT[1]

Amici curiae, who are identified in the attached Addendum, are law professors who teach, write, and research in the areas of bankruptcy law, commercial law, civil procedure, and business law. Their scholarship focuses on bankruptcy law, theory and policy, with special emphasis on the constitutional, structural and economic implications of the use of the corporate reorganization system created by chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). Accordingly, amici curiae have a strong interest in the correct interpretation of the Bankruptcy Code and appropriate limits on the reach of bankruptcy law.

This Court has long been concerned that a broad nondebtor release ("NDR") "lends itself to abuse" because it can "operate as a bankruptcy discharge arranged without a filing and without the safeguards of the Bankruptcy Code." *Deutsche Bank A.G. v. Metromedia Fiber Network, Inc.*, (*In re Metromedia Fiber Network, Inc.*), 416 F. 3d 136, 141 (2d Cir. 2005).

United States District Judge McMahon's thorough and carefully-reasoned opinion below should be affirmed for the reason she stated: there is no statutory authority for the nondebtor releases in this case. *In re Purdue Pharma L.P.*, 635 B.R.

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[1]No counsel for any party authorized this brief in whole or in part, and no person or entity, other than amici curiae or their counsel, made a monetary contribution to fund the preparation or submission of this brief. This brief is accompanied by a *Motion of Law Professors for Leave to File Amici Curiae Brief in Support of Appellees* as required by Fed. R. App. P. 29(a)(3).

26 (S.D.N.Y. 2021), *certificate of appealability granted*, No. 21 CV 7532 (CM), 2022 WL 121393 (S.D.N.Y. Jan. 7, 2022).

Alternatively, her opinion should be affirmed because the releases granted to the owners of the Debtors[2], the Sackler family, were "abusive" as that term has been understood in bankruptcy. The Sacklers' financial contribution to the Debtors' reorganization and the affirmative vote on the Debtors' Plan of Reorganization cannot overcome that abuse.

STATEMENT OF THE CASE

On September 17, 2021, Bankruptcy Judge Robert Drain confirmed the Twelfth Amended Joint Chapter 11 Plan of Reorganization of Purdue Pharma L.P. and Its Affiliated Debtors (the "Plan" and the "Debtors"). *In re Purdue Pharma L.P.*, 633 B.R. 53 (Bankr. S.D.N.Y.), *vacated sub nom. In re Purdue Pharma L.P.*, 635 B.R. 26 (S.D.N.Y. 2021), *certificate of appealability granted*, No. 21 CV 7532 (CM), 2022 WL 121393 (S.D.N.Y. Jan. 7, 2022).

The Plan contains a nonconsensual nondebtor release which "permanently enjoins third parties from pursuing their current claims against" the Sacklers arising from Purdue Pharma's marketing, labeling and sale of opioids. *In re Purdue Pharma,* 635 B.R. at 67 (quoting Plan § 10.7(b)).

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[2] Unless otherwise indicated, capitalized terms used without definition in this amicus brief shall have the meanings ascribed to such terms in Judge McMahon's opinion that is the subject of this appeal. *In re Purdue Pharma,* 635 B.R. 26.

The NDR would enjoin, among others, direct claims "arising under various unfair trade practices and consumer protection laws that make officers, directors and managers who are responsible for corporate misconduct personally liable for their actions." *In re Purdue Pharma,* 635 B.R. at 26.

On December 16, 2021, United States District Judge Colleen McMahon, sitting in an appellate capacity, reversed the Bankruptcy Court and vacated the order confirming the Plan. *In re Purdue Pharma L.P.,* 635 B.R. at 34. She found that the Plan's NDRs "are non-consensual; they bind the objecting parties as well as the parties who consented." *Id.* at 67. Thus, "[a]ll present and potential claims connected with OxyContin and other opioids would be covered by" the NDRs. *Id.*

Judge McMahon reversed the Bankruptcy Court because—

> the Bankruptcy Code does not authorize such non-consensual non-debtor releases: not in its express text (which is conceded); not in its silence (which is disputed); and not in any section or sections of the Bankruptcy Code that, read singly or together, purport to confer generalized or "residual" powers on a court sitting in bankruptcy.

Id. at 37-38.

Prior to her ruling, Judge McMahon had sought briefing on whether granting the NDRs was "abusive." *See* Schedule for Further Briefing, *In re Purdue Pharma L.P.*, 21 cv 08566 (CM), ECF No. 73 (S.D.N.Y. Dec. 1, 2021) (requesting briefing on issue of "abuse" in the use of NDRs). Although she received such briefing, her opinion focused solely on whether the Bankruptcy Code authorized the NDRs. She

made significant findings of fact (which the Debtors do not dispute on appeal), which would also support an alternative holding that the NDRs were abusive.

ARGUMENT

I. HIDING ASSETS AS A "DEFENSIVE MEASURE" IS A CLASSIC FORM OF BANKRUPTCY ABUSE REQUIRING AFFIRMANCE.

The United States has long had liberal bankruptcy laws, including "broad provisions for the discharge of debts." *Lamar, Archer & Cofrin, LLP v. Appling*, 138 S. Ct. 1752, 1758 (2018). The discharge of debt is bankruptcy's "greatest" power because it eliminates otherwise enforceable legal claims. *Hanover Nat'l Bank v. Moyses*, 186 U.S. 181, 186 (1902) (bankruptcy's "greatest" power "is the discharge of a debtor from his contracts."); Jonathan C. Lipson, *Debt and Democracy: Towards A Constitutional Theory of Bankruptcy*, 83 NOTRE DAME L. REV. 605, 612 (2008).

The broad discharge has led to corresponding concerns about "abuse" of the bankruptcy system. *See generally* Bankruptcy Abuse Prevention and Consumer Protection Act, Pub. L. No. 109-8, 119 Stat. 23. Thus, the *Metromedia* court was correct to link the discharge-like effect of an NDR to fears of bankruptcy abuse.

A. Acts "In Contemplation of" Bankruptcy Are Abusive.

Acts taken "'in contemplation of' bankruptcy ha[ve] long been, and continue[] to be, associated with abusive conduct." *Milavetz, Gallop & Milavetz, P.A. v. United States,* 559 U.S. 229, 240 (2010). Hiding assets from creditors—a "fraudulent

transfer"—is the prototypical act "in contemplation of bankruptcy" and a "primordial" form of abuse. Kenneth C. Kettering, *Securitization and Its Discontents: The Dynamics of Financial Product Development*, 29 CARDOZO L. REV. 1553, 1596 (2008).

Every jurisdiction in the United States proscribes transfers that hinder or delay creditors. *See, e.g.,* Unif. Fraudulent Transfer Act, 7A U.L.A. 266 (1999); 11 U.S.C. § 548. Debtors who commit fraudulent transfers before bankruptcy can be denied a discharge entirely. 11 U.S.C. § 727(a)(2). But the Bankruptcy Code's discharge rules do not apply to nondebtors, such as the Sacklers.

Fraudulent transfers are abusive because they reduce creditor recoveries. They also threaten the legal system, because they enable defendants to evade public accountability through processes such as execution on a judgment. *See* Jonathan C. Lipson & Jennifer L. Vandermeuse, *Stern, Seriously: The Article I Judicial Power, Fraudulent Transfers, and Leveraged Buyouts*, 2013 WIS. L. REV. 1161 (2013).

"[T]he law of fraudulent conveyances," Dean Clark has observed "contains a few simple but potent moral principles governing the conduct of debtors toward their creditors." Robert Charles Clark, *The Duties of the Corporate Debtor to Its Creditors*, 90 HARV. L. REV. 505, 505 (1977). It "embodies a general ideal, in connection with a debtor's transfers of property rights and incurrences of new obligations, of [n]onhindrance of creditors." *Id.* at 513.

B. The Sacklers' "Defensive Measures" Were Abusive Acts In Contemplation of Bankruptcy.

Here, there is little question that the Sacklers took "'defensive measures'" before bankruptcy by withdrawing assets from Purdue Pharma that hindered creditors' ability to recover. *In re Purdue Pharma*, 635 B.R. at 56 (quoting a confidential memo from a family financial advisor to Jonathan Sackler).

1. These Defensive Measures Were Used to Lever the Releases

In 2007, Purdue Pharma—while under the control of the Sackler family—pleaded guilty to federal felonies arising from the marketing, labeling and sale of OxyContin. *In re Purdue Pharma*, 635 B.R. at 34. The Sacklers were not charged.

Nevertheless, a "veritable tsunami" of litigation ensued, initially against Purdue, later adding the Sacklers as named defendants. *Id.* at 35. Judge McMahon observed that "almost as soon as the ink was dry" on the 2007 criminal plea "the family began what one member described as an "'aggressive[ ]' program of withdrawing money from Purdue":

> The Sacklers upstream[ed] some $10.4 billion out of the company between 2008 and 2017, which, according to their own expert, substantially reduced Purdue's "solvency cushion." Over half of that money was either invested in offshore companies owned by the Sacklers or deposited into spendthrift trusts that could not be reached in bankruptcy and off-shore entities located in places like the Bailiwick of Jersey.

Id. at 36.[3]

When Purdue went into bankruptcy, an estate was created, comprised of all of Purdue's property, including fraudulent transfer claims against the Sacklers. 11 U.S.C. § 541. The Debtors' Plan would settle these claims, which is not disputed on appeal.

But the Plan goes further, because the Sacklers have levered these defensive measures to force creditors to give up ("release") claims that have been, or could be, asserted directly against them for, among other things, unfair and deceptive trade practices that create personal liability. *In re Purdue Pharma*, 635 B.R. at 70.

If transfers that hinder creditors are abusive as to the estate, then they are *a fortiori* abusive as to creditors whose direct claims are enjoined by the NDRs. They are a "'conditioning of financial participation by non-debtors'" that is "'subject to the sort of abuse foreseen'" in *Metromedia. In re Johns-Manville Corp.*, 517 F.3d 52, 66 (2d Cir. 2008)*, rev'd & remanded sub nom. Travelers Indem. Co. v. Bailey*, 557 U.S. 137 (2009) (quoting *In re Karta Corp.,* 342 B.R. 45, 55 (S.D.N.Y. 2006)).

[3] Apparently, about 44% of the proceeds were used to pay tax obligations. *In re Purdue Pharma,* 635 B.R. at 55. The Sacklers "vehemently deny any suggestion that any of these transfers would qualify as fraudulent conveyances," but the "fact of these extensive transfers of money out of Purdue and into the family coffers is not contested." *Id.* at 58.

2. *The Sackler NDRs Are Doubly Abusive*

Indeed, they are worse than the ordinary abuse of fraudulent transfer because the underlying claims are, themselves, evidence of a kind of abuse. Just as the Bankruptcy Code denies the discharge to debtors who hide assets, so too does it except from discharge debts for various types of misconduct, including debts for "willful and malicious injury" or unpaid fines or criminal penalties. 11 U.S.C. § 523(a)(6) & (7).

Here, there has been no adjudication of the Sacklers' liability on the merits, but the allegations are serious. Purdue Pharma has now twice agreed[4] to plead guilty to federal drug crimes committed while members of the Sackler family were a majority of its board of directors. *In re Purdue Pharma*, 635 B.R. at 34-35 & 40.

Yet, the bankruptcy case itself prevented the determination of the merits of any direct claims that creditors might have had against them arising from this conduct. The Debtors commenced these cases in September 2019, shortly after the Sacklers lost "at least three" motions to dismiss lawsuits asserting direct liability. 635 B.R. at 51 (citations omitted). The next month, in October 2019, the Bankruptcy Court issued a broad preliminary injunction shielding the Sacklers from litigation outside the Bankruptcy Court. *See* Order Pursuant to 11 U.S.C. § 105(a) Granting, In Part, Mot. for Preliminary Injunction, *Purdue Pharma L.P. v. Commonwealth of*

[4] In 2007 and, as discussed *infra* at Part III.A., in 2020.

Massachusetts, Adv. Pro. No. 19-08289, ECF No. 82 (Bankr. S.D.N.Y. Oct. 11, 2019), *aff'd Dunaway v. Purdue Pharm. L.P.* (*In re Purdue Pharm. L.P.*), 619 B.R. 38 (S.D.N.Y. 2020).

The Sacklers have not declared personal bankruptcy, so we cannot know whether these direct claims would be excepted from discharge. They vehemently deny any wrongdoing.

But that is the ultimate problem: The Debtors' bankruptcy precluded any determination of the merits through the preliminary injunction. The NDRs would make that permanent.

The Sacklers' defensive measures are thus doubly abusive: on their own, and because they led ultimately to the preliminary injunction and NDRs that would prevent any adjudication or determination of the merits of the claims against them.

II. THE SACKLERS' FINANCIAL CONTRIBUTIONS DO NOT CLEANSE THE NDRS OF ABUSE.

Certain law professors have written in support of the Appellants ("Appellants' Amici") in the hope of preserving the use of NDRs in at least "rare" cases because, they argue, NDRs can be economically "efficient." *See* Br. of Amici Curiae Law Professors in Supp. of Appellants, ECF No. 403-3 (the "Appellants' Amici Brief"). Yet, they practically concede the abusiveness of the NDRs here because they "take no position on the appropriateness of the third-party releases *in this case or whether*

such releases were sufficiently supported by contributions to the bankruptcy estate to be justified." *Id*. at 1 (emphasis supplied).

The Appellants' Amici Brief argues that NDRs can be economically efficient in mass tort bankruptcies, and offers the examples of the *Manville*, *A.H. Robins* and *Dow Corning* cases. *Id.* at 3 (citations omitted). But those cases were, to many, abusive in their own ways and, in any event, readily distinguishable. The underlying liability in question there looked little like the harms alleged here. Reversing Judge McMahon would shrink, not grow, value in the long term.

A. Other Mass Tort Cases Were Bad; *Purdue Pharma* Is Worse.

The Appellants' Amici argue that *Manville, A.H. Robins* and *Dow Corning* show that nonconsensual NDRs are an "indispensable" and "necessary" tool in order to "provide value in exceptional cases." Appellants' Amici Br. 4-5.

While the cases they cite were important examples of the use of NDRs, they were deeply problematic, and highlight the abusive character of the NDRs here. They are arguments for affirming Judge McMahon, not reversing her, for three reasons.

First, those earlier cases were subject to significant criticism, including on grounds that they were examples of "outrageous misconduct" and "bending the

law."[5] *Manville* was considered sufficiently controversial that Congress amended the Bankruptcy Code in 1994 to assure that asbestos makers could take advantage of that structure only for asbestos debts, and only with special procedural safeguards. *See* H.R. Rep. 103-834, 103d Cong., 2nd Sess. 12; 140 Cong. Rec. H10765 (Oct. 4, 1994).

Second, the NDRs there were used chiefly to induce insurance companies to contribute to the reorganizations in exchange for assurance that the insurers' liability would be capped.[6] The Second Circuit later stated that the *Manville* releases affected only derivative, not direct, liability asserted against the insurance companies. *In re Johns-Manville Corp.,* 517 F.3d at 55. While the Supreme Court reversed on grounds

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[5] Katherine M. Anand, *Demanding Due Process: The Constitutionality of the S 524 Channeling Injunction and Trust Mechanisms That Effectively Discharge Asbestos Claims in Chapter 11 Reorganization*, 80 NOTRE DAME L. REV. 1187, 1203 (2005) (arguing that "524(g) does not provide adequate procedural safeguards through the representative vehicle."); Joseph A. Page, *Asbestos and the Dalkon Shield: Corporate America on Trial*, 85 MICH. L. REV. 1324 (1987) (reviewing MORTON MINTZ, AT ANY COST: CORPORATE GREED, WOMEN, AND THE DALKON SHIELD (1985) & PAUL BRODEUR, OUTRAGEOUS MISCONDUCT: THE ASBESTOS INDUSTRY ON TRIAL (1985)); RICHARD B. SOBOL, BENDING THE LAW: THE STORY OF THE DALKON SHIELD BANKRUPTCY (1991); Ralph Brubaker, *Bankruptcy Injunctions and Complex Litigation: A Critical Reappraisal of Non-Debtor Releases in Chapter 11 Reorganizations*, 1997 U. ILL. L. REV. 959, 963 (1997).

[6] As amici observe "The [Manville] court agreed the injunction was necessary to direct claims to insurance proceeds and away from the insurers, preserve value for the estate, and effectuate an equitable reorganization by solving Manville's distinct collective action problem." Appellants' Amici Br. 7 (citing *Johns-Manville Corp. v. Asbestos Litig. Grp.* (*In re Johns-Manville Corp.*), 26 B.R. 420, 436–37 (Bankr. S.D.N.Y. 1983)).

of preclusion, the Second Circuit opinion echoed the *Metromedia* Court's fear that "'a nondebtor release is a device that lends itself to abuse.'" *Id*. at 66 (quoting *In re Metromedia Fiber Network, Inc*., 416 F.3d 136, 142 (2d Cir. 2005)).

If the earlier cases were bad, the Purdue NDRs are worse: the Sacklers are nothing like the insurers in those earlier cases. There is little evidence, for example, that the insurers controlled the debtors' decision-making in those cases. The undisputed facts here, by contrast, show that the Sacklers owned and (until 2018) controlled the Debtors.

Moreover, the insurance policies in question were property of the estates of those debtors, which were exhausted in the bankruptcies; the insurers had no greater liability under those policies.[7] Here, by contrast, the Sacklers have no analogous contractual commitment to the Debtors. Nor, more importantly, have they exhausted their apparent resources. Rather, it appears that the Sacklers would retain the benefit of about $5 billion of the $10.5 billion they withdrew from Purdue in the years between 2007-2017.

[7] *In re Johns-Manville Corp*., 40 B.R. 219, 229 (S.D.N.Y. 1984) ("[I]nsurance policies and their proceeds and the claims or causes of action which are or may be asserted by Manville against its insurance carriers in pending suits, constituted "substantial property of the Manville estate which will be diminished if and to the extent that third party direct actions against the insurance carriers result in plaintiffs' judgments.").

B. The Costs of Reversing Judge McMahon.

The Appellants' Amici also argue that NDRs can "unlock" value for the benefit of creditors, including tort creditors whose direct claims would be extinguished by the NDRs. Appellants' Amici Br. 5.

They are wrong. Permitting these NDRs would destroy value in future cases.

1. The Perverse Incentives Created By Reversing Judge McMahon.

The logic of the Appellants' Amici Brief is that nonconsensual NDRs produce greater recoveries for all concerned at lower transaction and judicial costs by reducing creditors' incentives to "hold out" in plan negotiations. But that can only be true if all claimants are left no worse off by virtue of the NDRs.

There has been no valuation of the claims enjoined by the NDRs in this case. The Sacklers have offered about $5.5 billion, a significant amount of money. But much of the "added value" was the product of the very holding-out that the Appellants' Amici fear.

At the commencement of these cases, the Debtors filed with the Bankruptcy Court an unsigned "term sheet" that proposed a "settlement framework."[8] The framework had three basic elements: (i) the Sacklers would cede ownership of Purdue Pharma to or for the benefit of creditors; (ii) they would make an additional

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[8] *See* Notice of Filing of Term Sheet with Ad Hoc Committee, *In re Purdue Pharma*, 19-23649-rdd, ECF No. 257, ¶ 5 (Bankr. S.D.N.Y.).

contribution of $3 billion; and (iii) in exchange, they would receive "comprehensive releases," which ultimately took the form of the NDRs struck by Judge McMahon.[9]

The Sacklers' $3 billion "offer" has now reached $5.5 billion because creditors held out for a better deal. In summer 2021, a large group of holdout states, including New York and Massachusetts, agreed to support the settlement framework, which led to an additional $1.3 billion contribution from the Sacklers. *See In re Purdue Pharma*, 633 B.R. at 87.

More recently, nine of the appellees, also holdouts, agreed to withhold appellate briefs in exchange for the Sacklers' promise to provide an additional $1.5 billion in funding. *See* Order Pursuant to 11 U.S.C. §§ 105 and 363(b) Authorizing and Approving Settlement Term Sheet, *In re Purdue Pharma*, 19-23649-rdd, ECF No. 4503 (Bankr. S.D.N.Y.). The ability to hold out gave the NDRs whatever value they may have "unlocked" in this case.

If Judge McMahon is affirmed, the Sacklers will have to litigate or settle the direct claims outside the bankruptcy system, just like everyone else. That may cost them more, but it is not possible to know the effect on creditors, because, as explained *infra* at Part III.B, the Debtors have taken the position that the direct

[9] *See id.* ¶ 6 (providing that the Sacklers' contributions would be made "[i]n exchange for comprehensive releases in the form and manner to be agreed upon by the parties.").

claims are either "unknowable" or $0. *See* Disclosure Statement for Fifth Am. Joint Chapter 11 Plan of Reorganization of Purdue Pharma L.P. and its Affiliated Debtors, *In re Purdue Pharma*, 19-23649-rdd, ECF No. 2983, at 5 (Bankr. S.D.N.Y.) (the "Disclosure Statement").

If, instead, this Court reverses Judge McMahon, it would signal that creditors can be forced to exculpate virtually any misconduct, no matter how serious the allegations. This would, in turn, reduce the price of nondebtor releases in the future, and thus any value they might yield for creditors.[10]

2. *"Rare Case" Exceptions Invite Abuse.*

The Appellants' Amici also argue that NDRs can have economic value in "exceptional" cases. This is equally problematic.

Even if that were true as a matter of economic theory—and reversing Judge McMahon would assure it is false in the future—it is nevertheless important to note

[10] Appellants' Amici argue that "it is non-adjusting creditors who are the ones harmed most by the strategic bankruptcy behavior that third-party releases are used to prevent." *See* Appellants' Amici Br. 21 n.6 (citing Joshua Macey & Jackson Salovaara, *Bankruptcy as Bailout: Coal Company Insolvency and the Erosion of Federal Law*, 71 STAN. L. REV. 879, 887 (2019)). At best, this is questionable, where all efforts to determine the liability of the Sacklers were foreclosed by the Bankruptcy Court in the preliminary injunction granted at the start of the case. Moreover, the payments personal injury creditors would receive are miniscule, likely only several thousand dollars per creditor. *See* Disclosure Statement at 15 (personal injury claims would receive a "gross award ranging between $3,500 and $48,000").

that NDRs are not limited to "exceptional" cases.[11] Bankruptcy Judge Wiles recently observed that "[a]lmost every proposed Chapter 11 Plan that I receive includes proposed releases." *See In re Aegean Marine Petroleum Network Inc.*, 599 B.R. 717, 726 (Bankr. S.D.N.Y. 2019).[12]

This reflects a larger reality of chapter 11 practice, which is that deviations from the Bankruptcy Code, intended to be used only for "rare" cases, can become the norm.

Concerned about this, the Supreme Court announced in the *Jevic* case that there can be no "rare case" exception to fundamental rules in the Bankruptcy Code on the priority of final distributions. *Czyzewski v. Jevic Holding Corp.*, 137 S. Ct. 973, 987 (2017).

In *Jevic,* the Court held that a bankruptcy court may not approve a "structured dismissal that provides for distributions that do not follow ordinary priority rules

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[11] As one observer stated in 1994: "More and more frequently, various nondebtors, including partners, officers, directors, guarantors, and co-obligors are seeking and are being granted releases from liability under the debtor's plan of reorganization." Kenneth M. Lewis, *When Are Nondebtors Really Entitled to A Discharge: Setting the Record Straight on Johns-Manville and A.H. Robins*, 3 J. BANKR. L. & PRAC. 163 (1994). It is difficult to characterize NDRs as "exceptional."

[12] Judge Wiles's concerns were recently shared by Judge Novak, of the District Court for the Eastern District of Virginia: "The ubiquity of third-party releases in the Richmond Division demands even greater scrutiny of the propriety of such releases. And, their prevalence also undermines assertions that they are integral to the success of this particular reorganization plan." *See Joel Patterson v. Mahway Bergen Retail Group, Inc.*, __ B.R.__, No. 3:21CV167 (DJN), 2022 WL 135398, at *2 (E.D. Va. Jan. 13, 2022).

without the affected creditors' consent." *Jevic Holding Corp.*, 137 S. Ct., at 983. The Court did so because the priority-skipping distributions there "circumvent[ed] the [Bankruptcy] Code's procedural safeguards." *Id.* at 986. *Jevic* was the Court's reminder that chapter 11 cases "cannot drive through or around [chapter 11's procedural] guardrails." Jonathan C. Lipson, *The Secret Life of Priority: Corporate Reorganization After* Jevic, 93 WASH. L. REV. 631, 671 (2018).

These, however, are the very same safeguards that concerned the *Metromedia* Court in 2005, and for the same reason: deviating from Congress' baseline rules about who may use bankruptcy's "greatest power" invites abuse. If the Supreme Court refused to recognize "rare" deviations from absolute priority in *Jevic*, equally fundamental rules on the scope of the discharge of debt are no different.

III. THE VOTE ON THE PLAN DOES NOT CLEANSE THE SACKLER NDRS OF ABUSE.

Appellants also argue that the Plan enjoyed the overwhelming support of creditors, which "provide[s] evidence that the releases are not being abused." Appellants' Amici Br. 22 n.7. Here, too, they are wrong because that can be true only if the vote was fair and informed. But the vote on the Purdue Plan was, for purposes of the NDRs, neither of those things.

It is true that the Plan was supported by the vast majority of creditors who *voted*.[13] But fewer than 20% of the 618,194 claimants entitled to vote—and fewer than 50% of the subset of claimants with personal-injury claims—actually voted on the Plan.[14] The United States, in its capacity as the largest (and first priority) creditor, submitted no ballot.[15]

Bankruptcy Judge Drain stated that "an unprecedented number" of votes were cast on the plan. *In re Purdue Pharma*, 633 B.R. at 60. Even if that were true—and it appears not[16]—creditors had no practical choice and little information about the claims being released.

A. The DOJ Settlement and the "Poison Pill" Stripped Creditors of Meaningful Choice.

Purdue Pharma had the exclusive right to propose the Plan during the case (11 U.S.C. § 1121), and was committed to the settlement framework (with the NDRs) from the outset. Moreover, a controversial settlement between Purdue Pharma and

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[13] *In re Purdue Pharma*, 633 B.R. at 60-61.

[14] *See* Final Decl. of Christina Pullo of Prime Clerk LLC Regarding the Solicitation of Votes & Tabulation of Ballots Cast on the Fifth Am. Joint Chapter 11 Plan of Reorganization of Purdue Pharma L.P. and its Affiliated Debtors, *In re Purdue Pharma*, 19-23649-rdd, ECF No. 3372 (the "Tabulation"), at 5 & Ex. A (Bankr. S.D.N.Y.).

[15] *See* Tabulation. This was deemed to be an acceptance of the plan. *Id*. at Ex. A.

[16] Rather, it appears that more creditors voted in the A.*H. Robins* case. *See In re A.H. Robins Co., Inc.*, 88 B.R. 742, 750 (E.D. Va. 1988), *aff'd*, 880 F.2d 694 (4th Cir. 1989) (plan was approved by all creditors, including by over 94% of over 140,000 votes casted by Dalkon Shield claimants).

the United States included a "poison pill" which made confirmation of the Plan virtually inevitable. *See* Mot. of Debtors Pursuant to 11 U.S.C. § 105 and Fed. R. Bankr. P. 9019 Authorizing and Approving Settlements Between the Debtors and the United States, *In re Purdue Pharma*, 19-23649-rdd, ECF No. 1828, ¶¶ III.10 & III.8.f (Bankr. S.D.N.Y.) ("Purdue-DOJ Settlement").

Purdue Pharma was not chastened by the 2007 criminal plea, and continued to violate the law. As a result, in 2020 the United States asserted about $18 billion in claims against Purdue for fines, penalties and criminal forfeitures. (Again, the Sacklers were not charged.) Purdue agreed in the bankruptcy to compromise and settle these claims for about $8 billion.

But any deviation from this settlement (including conversion to a chapter 7 liquidation) would cause the United States' claim to balloon back to its full amount, and give it first-priority status, swamping all other claims.[17] As a practical matter, it would enable the United States to "gobble up" all of Purdue's assets, leaving nothing for other creditors. Adam J. Levitin, *Purdue's Poison Pill: The Breakdown of Chapter 11's Checks and Balances*, 100 TEX. L. REV. __ (forthcoming 2022).

[17] Specifically, that settlement provided that the "Debtors will not propose a Plan of Reorganization or liquidation that is inconsistent with this [Settlement] Agreement," Purdue-DOJ Settlement at ¶ III.8.e, and if a Plan of Reorganization is not confirmed that "provides for the emergence from the Chapter 11 Cases of a public benefit company (or entity with a similar mission), Purdue and the United States each have the option to rescind this Agreement." Purdue-DOJ Settlement ¶ III.8.f.

It is no answer to say that the Plan, itself, embodies a number of settlements, including a settlement between the Debtors, certain creditors, and the Sacklers. While that may be true, "a voluntary settlement . . . cannot possibly 'settle,' voluntarily or otherwise, the conflicting claims of [those] who do not join in the agreement." *Martin v. Wilks*, 490 U.S. 755, 761-62, 768 (1989). "Of course," The Supreme Court has admonished, "parties who choose to resolve litigation through settlement may not dispose of the claims of a third party . . . without that party's agreement." *Loc. No. 93, Int'l Ass'n of Firefighters v. City of Cleveland*, 478 U.S. 501, 529 (1986).

That, however, is exactly what the NDRs under the Plan do.

The Purdue-DOJ settlement was a gun to creditors' heads. Voting "no" would have been economically irrational. A vote "yes" under these conditions cannot cleanse the Sackler NDRs.

B. The Creditors' Vote Was Not Informed For These Purposes.

Nor was the vote on the NDRs informed, for at least three reasons.

First, creditors knew little about the merits of the underlying allegations against the Sacklers. As a result of the preliminary injunction granted early in this case—which remains in force[18]—all litigation against the Sacklers has been stayed

[18] *See* Twenty-Sixth Am. Order Pursuant to 11 U.S.C. § 105(a) Granting Mot. for a Preliminary Injunction, *In re Purdue Pharma*, Adv. Pro. No. 19-08289, ECF No. 338 (Bankr. S.D.N.Y. Mar. 2, 2022).

for two and a half years. Unlike earlier mass tort bankruptcies, where there had been findings of liability before bankruptcy, here the Bankruptcy Court foreclosed all efforts to have such a determination as to the Sacklers at the outset of the case.

Second, the Plan was supported by the Disclosure Statement, which said almost nothing about the merits of those allegations. *See generally* Disclosure Statement. It contains significant discussions about the *estate's* claims against the Sacklers for, *e.g.,* fraudulent transfer, as well as the efforts by counsel to various stakeholders to negotiate the settlement of those claims.

The Disclosure Statement assumed that the value of direct claims was "unknowable" and then booked those claims at $0. Disclosure Statement at 5 & App'x B at 8 ("The Liquidation Analysis assumes that all opioid-related claims asserted against the Debtors are asserted solely against Debtor PPLP."). Yet, they had to be worth more than that or they would not have engendered the dispute currently on appeal.

Third, notice of the NDRs was incomprehensible. Even Richard Sackler, for many years Purdue's leader and thus a key beneficiary of them, admitted that he did not understand them.[19]

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[19] Dr. Richard Sackler testified that although he tried to read the prior iteration of the NDRs, they were so "extremely dense," and would take such "an enormous amount of time to fully understand," that he gave up. Hr'g Trans., *In re Purdue Pharma*, 19-23649-rdd, ECF No. 3614, at 133 (Bankr. S.D.N.Y.).

Thus, the vote on the Plan shows resignation, not assent; the objections to the Plan's NDRs show resistance, not release. The Purdue-DOJ Settlement meant there would be no plausible alternatives to the Plan; the preliminary injunction meant creditors would have no chance to learn the truth about their direct claims against the Sacklers.[20]

A vote under these circumstances cannot cleanse the NDRs here.

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[20] It is no answer to say that the Plan would create a "public document repository." *In re Purdue Pharma,* 635 B.R. at 66 (citing *In re Purdue Pharma*, 19-23649-rdd, ECF No. 3440, ¶ 7 (Bankr. S.D.N.Y.)). While laudable in many ways, its contents were not available when creditors had to vote on the Plan.

Nor does it matter that an examiner was appointed in these cases. *In re Purdue Pharma*, 19-23649-rdd, ECF No. 3048 (Bankr. S.D.N.Y.). The examiner's mandate was narrow, limited to investigating whether the Sacklers interfered with a special committee of the Debtors' board after they had resigned *Id*. at 2. His budget was miniscule, $200,000. *Id.* Like the Sacklers' contributions and the Plan vote, the examiner's findings do not eliminate the abusiveness of the NDRs in this case.

Whether you call them an "outrage"[21] or "lawless"[22] or "shocking"[23] or a "grift,"[24] the bottom line is always the same: nonconsensual nondebtor releases—especially those here—are abusive.

CONCLUSION

The nondebtor releases in this case defy the Bankruptcy Code's safeguards, as Judge McMahon correctly found. But, they also derive from, and perpetuate, abuses that harm creditors and the integrity of the bankruptcy system. Judge McMahon's opinion must be affirmed.

Respectfully submitted,

Dated: March 18, 2022

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[21] Ralph Brubaker, *Mandatory Aggregation of Mass Tort Litigation in Bankruptcy*, 131 YALE L.J.F. 960, 962 (2022).

[22] Lynn M. LoPucki, *Chapter 11's Descent into Lawlessness,* 96 AM. BANKR. L. REV. __ (forthcoming 2022).

[23] Melissa B. Jacoby, *Shocking Business Bankruptcy Law*, 131 YALE L.J.F. 409, 411 (2021).

[24] Lindsey Simon, *Bankruptcy Grifters*, 131 YALE L.J. 1154, 1188 (2022).

CERTIFICATION OF COMPLIANCE

This brief complies with the type-volume limitation of Fed. R. App. P. 29(a)(5) and 2d Cir. L.R. 29.1(c) because this brief contains 5,427 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(f).

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I, Tyrone Heath, 2179 Washington Avenue, Apt. 19, Bronx, New York 10457, being duly sworn, depose and say that deponent is not a party to the action, is over 18 years of age and resides at the address shown above.

On March 22, 2022

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