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PERSPECTIVE

Where can I do the Texas two-step in bankruptcy court?

By Catherine Bauer

It's no secret that bankruptcy attorneys have preferred venues when it comes to filing mega Chapter 11 cases. They say they like courts that are "predictable" and are familiar with the "uniqueness" of these very large cases. But I don't buy it.

Without taking away from the earned expertise of my former bankruptcy bench colleagues in the districts that handle the majority of the mega cases, there's more to it than their expertise when it comes to them getting these cases. In my opinion, counsel often file in these venues because they and their wealthy clients can get away with murder (sometimes literally). Just look at what Johnson & Johnson has tried to do.

Using the so-called "Texas Two-Step" (so appropriate a name), the very solvent Johnson & Johnson created an entity to file bankruptcy and stop all those pesky lawsuits by all those women who claim to have developed cancer (or died) because of J&J's baby powder and other talc products. The new shell entity (LTL Management; an acronym for "Legacy Talc Litigation") was divested from Johnson & Johnson, under Texas law, and then became a North Carolina entity two days before it filed a Chapter 11 bankruptcy in North Carolina. The case was eventually transferred to New Jersey on the request of various parties (that's where Johnson & Johnson has its headquarters, nearly all of its assets and its principal operations).

Head spinning, even to a bankruptcy professional.

But I'd bet big money that the choice of North Carolina for the LTL bankruptcy wasn't one that was made lightly. Debtor's counsel thought they would do better (and get away with more?) in North Carolina than in New Jersey. Many other large, asbestos-related bankruptcies had been filed in North Carolina. Those other cases gave debtor's counsel the assurances they wanted. They knew how the case would probably play out.

What does counsel in these mega cases want? They want to get paid of course. And they want a judge who's accommodating. There's a desire by many bankruptcy judges and attorneys to make their districts desirable places to file big bankruptcy cases. It's a conundrum for the bankruptcy bench: Allow what may arguably be done in bad faith and keep newsworthy mega cases, or say no and risk having debtor's counsel go elsewhere in the future.

When I was on the bench, I had many attorneys say to me, "We always get this approved in (fill in the district)." The meaning was clear enough: they wanted me to approve what they were proposing or risk having them take their dance card to another venue. It never impacted my decision, but the pressure was definitely real.

In addition to the dubious Texas Two-Step trick, third-party releases can test the resolve of bankruptcy judges. Wealthy companies and individuals ask for releases of liability through their corporate bankruptcies. The Sacklers of Purdue Pharma are a prime example. Well-healed non-debtors don't want to be inconvenienced by having to file personal bankruptcy cases. And, despite due process concerns, third-party releases are still approved in some courts. I have to wonder how often bankruptcy judges feel pressured to approve third-party releases so that mega (or just larger Chapter 11 cases) will continue to flow into their districts.

I know of one wonderful bankruptcy judge who graciously volunteered to help out in a "mega" bankruptcy court that was swamped. ("Mega" bankruptcy courts because they get the filings, not because they are specially designated as such.) That judge didn't last long on assignment. Counsel in that other district complained. They said the judge asked too many questions; the judge held too many hearings; the judge wanted to read everything; the judge didn't understand the culture of the court. In other words, the visiting judge wasn't "accommodating" enough. So, despite the district's need for more judges, this judge was sent packing.

While it may not be obvious at first glance, the Texas Two-Step cuteness and other similar bankruptcy ploys that scream bad faith are part of the larger bankruptcy venue problem. If companies had to file where they actually should (say, where they and their assets are located), bankruptcy judges wouldn't feel pressured to attract mega cases and this gamesmanship would largely be history.

This is not a good look for the administration of justice. Wealthy entities and individuals should play by the same rules as the rest of us, especially in a court of equity.

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