1-1-2021

The Settlement Trap

Lindsey Simon
Assistant Professor of Law *University of Georgia School of Law*, lindsey.simon@uga.edu

University of Georgia School of Law
Research Paper Series
Paper No. 2021-16

The Settlement Trap

LINDSEY D. SIMON*

Mass tort victims often wait years for resolution of their personal injury claims, but many who successfully navigate this arduous process will not receive a single dollar of their settlement award. According to applicable bankruptcy and state law, settlement payments may be an asset of the estate that the trustee, exercising its significant authority, administers and distributes to creditors instead of a claimant who had filed for bankruptcy. This distribution power maximizes repayment, a critical counterbalance to the robust protections and benefits that debtors receive in bankruptcy.

Setting aside the perceived unfairness of taking desperately needed money from tort victims, there is something fundamentally unsettling about the process by which bankruptcy law ensnares payment of mass tort settlements. This Article is the first to identify the problem, which it dubs the "settlement trap." Claimants in the settlement trap must seek relief from the mass tort claims administrator, the trustee, and potentially the bankruptcy court, facing costs and legal challenges at each turn. This Article explores the developing law surrounding treatment of mass tort settlements in consumer bankruptcy and identifies structural and doctrinal pressure points that impose significant confusion and costs on claimants. It supplements legal analysis with original interviews of stakeholders in the ongoing NFL concussion and pelvic mesh cases, case studies that highlight the peculiar mix of incentives that impact whether claimants receive their settlements and illustrate the potential for abuse. Finally, the Article offers a blueprint for reform.

---

* Assistant Professor, University of Georgia School of Law. I am thankful to Beth Burch, Mechele Dickerson, Pamela Foohey, Dalié Jiménez, and Bob Lawless for feedback at various stages of this project, and to the attendees at the Civil Procedure Workshop for their helpful comments. This Article benefitted from the excellent research assistance of Gretchen Edelman and Victoria Barbino. Any errors are my own.

INTRODUCTION

Susan[1] and her husband James, a former National Football League (NFL) player, had their world turned upside down when James was diagnosed with early onset Alzheimer's disease and related conditions. James died from these illnesses, and soon thereafter Susan filed for bankruptcy. While her bankruptcy case was pending, Susan joined the NFL concussion multidistrict litigation (MDL).[2] After the NFL

1. Susan's real name is not disclosed here, as portions of her case are still pending. As described in more detail below, I collected the real-life stories in this paper through phone interviews and email correspondence. I learned the specifics of Susan's case through emails from her personal injury attorney, who was outraged by the way her settlement award had been captured.

2. *In re* Nat'l Football League Players' Concussion Injury Litig., 307 F.R.D. 351 (E.D.

reached a global settlement resolving claims relating to traumatic brain injuries suffered by its players, Susan went through the various procedural examinations and evidentiary steps to secure an award of nearly $400,000. After costs, attorney's fees, and the money owed to her litigation finance company were taken out of the settlement, Susan awaited approximately $20,000 of much-needed funds, a mere 5% of her initial damages award. But Susan disclosed her bankruptcy, as required by the NFL's settlement form, and the trustee overseeing her bankruptcy case was entitled to receive the settlement and pay it out to her creditors, leaving Susan without a penny. Susan had fallen prey to the settlement trap.

Susan's case is not exceptional; rather, it is the direct result of the straightforward application of bankruptcy law. All property rights a debtor has as of the petition date—including potential lawsuit settlement payments—belong to the bankruptcy estate.[3] The trustee, acting on behalf of the estate, has sole authority to pursue and distribute settlement proceeds among creditors.[4] This vested authority exists when the lawsuit is settled while the bankruptcy case is ongoing and continues even when a bankruptcy has been closed for a decade.[5] This fact comes at a surprise to claimants as well as non-bankruptcy attorneys. As explained by one plaintiff's attorney, "once a bankruptcy is done and gone, the claimant has put that all behind them. The last thing they think is that proceeds of some award will be brought back by the trustee, and the costs would be borne by them."[6]

Consider the experience of Tammie, a woman who had pelvic mesh surgically implanted in the early 2000s to treat organ prolapse. A few years after her surgery, Tammie filed for bankruptcy, and her case was closed in 2005. More than a decade later, Tammie joined a mass litigation against the pelvic mesh manufacturer, claiming that the product caused her many health problems. Tammie was shocked when the bankruptcy trustee—a court-appointed representative of the estate in consumer bankruptcies—moved to reopen her long-dormant bankruptcy case and take control over the settlement. Even though nobody knew in the early 2000s that Tammie's pelvic mesh would cause her injuries, under some states' laws, her claims nevertheless still belong to the bankruptcy estate because the surgery implanting the mesh occurred before she filed for bankruptcy. In other states, the personal injury claim would not belong to the estate unless Tammie discovered the harm before bankruptcy or unless her cause of action accrued under state law before bankruptcy.[7] Claim accrual standards create instances where mass tort claimants are funneled back into the bankruptcy system they left long ago.

All is not lost for mass tort victims like Susan and Tammie. The Bankruptcy Code's[8] exemption provisions permit a consumer debtor to keep certain categories of their assets away from the grasp of creditors. The fundamental principles are

---

Pa. 2016).

3. 11 U.S.C. § 541.

4. 11 U.S.C. § 544.

5. *Id.*

6. Telephone Interview with Plaintiffs' Attorney 1 (Sept. 25, 2019).

7. Here, just as in many parts of discussion surrounding exemptions, choice of law analysis can have significant implications for debtors. For a more detailed discussion of the applicable laws, see *infra* Part I.C.1.

8. The Bankruptcy Code refers to Title 11 of the United States Code.

simple: consumer bankruptcy is designed to give the honest but unfortunate debtor a fresh start, and to do so the debtor must exit bankruptcy with some modest assets.[9] Exemptions cover many things, from clothes to schooling materials to retirement benefits. Section 522 of the Bankruptcy Code provides federal exemptions, but also allows individual states to create alternative exemptions that a debtor may elect.[10]

Mass tort personal injury settlement payments—the focus of this Article—may fall within a number of exemptions. The exemption framework is complicated, and minor distinctions in the arcane corners of state law can impact whether a claimant's settlement is exempt. Many debtors do not receive bankruptcy-specific advice when settling claims, and plaintiffs' attorneys are likely not aware or mindful of the potential implications until it is too late. Beyond accrual and exemption woes, the claimant may face still more challenges if he did not previously disclose the claim in his dormant bankruptcy. In that instance, mass tort defendants may argue that judicial estoppel prevents the claimant from collecting a settlement in the first place. In all, the layered doctrinal challenges relating to claim accrual, exemptions, and judicial estoppel create a harrowing and often insurmountable path to recovery for tort victims.

Powerful stakeholders like the trustee and claims administrator control the process for evaluating a claimant's settlement payment against this nuanced doctrinal framework. The compensation structure for these stakeholders creates incentives that magnify the settlement trap. Trustees are tasked with acting in the best interests of the bankruptcy estate and its creditors,[11] but in any given case the appropriate action may fall along a spectrum of potential options. For example, a claim that will be fully exempt is likely not worth the trustee's time to litigate and should be abandoned. However, a claim that could possibly return funds to the estate in excess of any potential exemption may—or may not—be worth the trustee's limited resources. Whether or when a trustee seeks to reopen a bankruptcy case to collect a mass tort settlement payment is a matter of discretion. So, too, is the decision to take an active role in a debtor's pending litigation, including negotiating the specifics of a settlement.[12] Keep in mind, though, that the often-substantial costs of pursuing a claim or settlement, including trustee and counsel fees, will be paid out of the estate's assets before any recovery goes to creditors. Thus, the trustee will be paid first for any efforts they expend to recover a claim, creating a perverse incentive to pursue claims even if the benefit to creditors is minimal.

---

9. *E.g.*, Williams v. U.S. Fidelity & G. Co., 236 U.S. 549, 554–55 (1915) (noting one of the primary purposes of the bankruptcy act is to "relieve the honest debtor from the weight of oppressive indebtedness and permit him to start fresh free from the obligations and responsibilities consequent upon business misfortunes"); *see also* ELIZABETH WARREN, JAY WESTBROOK, KATHERINE PORTER & JOHN POTTOW, THE LAW OF DEBTORS AND CREDITORS (7th ed. 2014).

10. Individual states may also opt out of the federal exemptions altogether, leaving debtors with no choice but to claim exemptions under state law. 11 U.S.C. § 522.

11. 11 U.S.C. § 704(a).

12. This paper is particularly concerned with three types of discretionary trustee behavior: pursuing settlements that are likely exempt, destroying the value of the debtor's potential surplus, and settling claims in ways that disqualify the resulting payment from exemptions. These behaviors reflect structural tension between a debtor's ability to claim settlement proceeds via exemptions or surplus and the trustee's power to control the estate's legal claims.

Claims administrators—the companies that are hired to evaluate and distribute settlement payments in mass tort cases—contribute to the settlement trap by withholding payment and requiring claimants to involve the trustee. Claims administrators must make sure that they only pay settlements to the proper party, otherwise they risk losing business or facing legal claims from mass tort defendants. Where there is any uncertainty due to bankruptcy, claims administrators require claimants to get some proof that they are entitled to the payment, such as a signed statement from the trustee or an order from the bankruptcy court.[13] Trustees therefore learn about settlement payments more often in the mass tort context than they otherwise would and are incentivized by the Code's fee structure to argue that such payments belong to the estate. The claims administrator and trustee can effectively trap settlement payments until questions about accrual and exemptions are resolved, either through settlement with the claimant or after contentious battles in court.

When asked about the settlement trap, stakeholders I interviewed all agreed that the system was inefficient and problematic. They pointed to various causes and contributing factors, from the "gang of lawyers" in mass tort cases who have too much control in the process and not enough bankruptcy knowledge,[14] to the claims administrators that increase costs "out of the claimant's pockets,"[15] to the "money-grabber" trustees who "shake down" claimants for their settlement awards.[16] There is plenty of blame to go around, but the problem remains unresolved. The settlement trap is costly, time consuming, and acutely impacts individual claimants.

Disputes regarding the treatment of settlement payments in bankruptcy have become more frequent over the past fifteen years, with a significant wave of cases in the last five years in connection with the NFL and pelvic mesh MDLs.[17] Mass tort cases pose a number of challenges that make the effects of the settlement trap more harmful and difficult to police.[18] Yet scholars have largely ignored the problem. Scholarship surrounding consumer bankruptcy exemptions and the treatment of

---

13. Telephone Interview with Claims Administrator (Oct. 1, 2019).

14. Telephone Interview with Plaintiffs' Attorney 4 (Sept. 27, 2019).

15. Telephone Interview with Plaintiffs' Attorney 2 (Sept. 28, 2019).

16. Telephone Interview with Debtors' Attorney (Oct. 1, 2019).

17. Telephone Interview with Trustee 1 (Sept. 26, 2019). *See generally* Lawrence Ponoroff, *Neither 'Twixt nor 'Tween: Emerging Property Interests in Bankruptcy*, 61 ARIZ. L. REV. 101 (2018) (describing increase in mass tort cases in bankruptcy). I suspect this is true for a few reasons. First, large mass tort settlement structures result in payments to many claimants in a relatively short window of time, increasing the likelihood that payments will be due to current or prior debtors. Additionally, mass tort injuries, such as CTE in the NFL cases, may be debilitating enough to drive claimants and their families into bankruptcy. Further, mass tort claims relating to defective products tend to have long latency periods, meaning many of the claim accrual issues will be put at issue for long-dormant bankruptcies. Finally, and most significantly, current mass tort claim forms almost always require the claimant to disclose prior bankruptcies, leading to increased scrutiny of the issue.

18. *See infra* Part II.A.2. Representation in mass tort cases is more likely to be collective, meaning attorneys tend to make decisions about litigation and settlement strategy without an individual claimant's bankruptcy exemptions in mind. Additionally, mass tort defendants are motivated to undercut the litigation against them and may agree to settle cases on terms that align with the trustee's interest but harm the debtor. And finally, many mass tort claims relate to latent harms that do not manifest for years. This delay opens the door for claimants to be caught in the web of standards for claim accrual in bankruptcy.

personal injury payments has thus far centered upon constitutional problems with uniformity in state and federal exemptions,[19] debtors' strategic use of exemptions to avoid paying judgments,[20] and issues surrounding the lien-stripping provisions in § 522(f).[21] This Article's contribution is to identify the settlement trap and ways to mitigate its harsh effects.

By interviewing stakeholders and collecting examples from the ongoing NFL concussion and pelvic mesh cases, this Article uncovers vast discrepancies in how bankruptcy trustees across the country approach mass tort settlements. This Article also uncovers systemic challenges imposed by the claims administration process that hinder claimants from receiving payments that would—or should, under rational exercise of the parties' discretion—go to claimants. This Article diagnoses the core features of a settlement trap, including complex laws, lack of control, and prohibitive costs. After identifying challenges posed by incomplete professional and fiduciary duties, broad discretionary authority, and conflicting financial incentives, this Article suggests a number of measures, both structural and procedural, that would mitigate the most pernicious features of the settlement trap.

I. Treatment of Settlement Payments in Bankruptcy

Before introducing the settlement trap, it is first important to understand both the basic operation of consumer bankruptcy law and the doctrinal issues behind the problem. This Part sets the stage.

A. The Consumer Bankruptcy Process

An individual debtor begins her case by filing a bankruptcy petition, at which time an estate is formed that contains all of the debtor's "legal or equitable interests" in property.[22] As is relevant here, property of the estate includes litigation claims and any settlements that result from such claims.[23] The debtor, within certain constraints,[24] may elect to file under one of three different chapters of the Bankruptcy Code. The vast majority of consumer debtors file either Chapter 7 or Chapter 13

---

19. *See, e.g.*, Lawrence Ponoroff, *Constitutional Limitations on State-Enacted Bankruptcy Exemption Legislation and the Long Overdue Case for Uniformity*, 88 AM. BANKR. L.J. 353 (2014); Gary E. Sullivan, *A Fresh Start to Bankruptcy Exemptions*, 2018 BYU L. REV. 335, 335 (2018) (creating a model for opt-out states to create "bankruptcy-specific exemptions").

20. *See, e.g.*, Stephen G. Gilles, *The Judgment-Proof Society*, 63 WASH. & LEE L. REV. 603, 714 (2006) (explaining how bankruptcy law undermines the ability of tort claimants to recover judgments).

21. *See, e.g.*, Paulette J. Delk, *Lien Avoidance Under Section 522(f) of the Bankruptcy Code: The Winding Road to the Supreme Court*, 26 WAKE FOREST L. REV. 879, 879–83, 893 (1991) (recommending amendments to the Bankruptcy Code that would harmonize tension between the opt-out and lien avoidance provisions of section 522).

22. 11 U.S.C. § 541(a)(1) (forming an estate comprised of "all legal or equitable interests of the debtor in property as of the commencement of the case").

23. *See* Parker v. Wendy's Int'l, Inc., 365 F.3d 1268, 1272 (11th Cir. 2004).

24. 11 U.S.C. § 707(b).

cases.[25] In Chapter 7 cases, the bankruptcy process involves liquidating the debtor's nonexempt property, distributing available assets among creditors, and then discharging the debtor's remaining unpaid debts.[26] Chapter 13 cases, by contrast, require the debtor to complete a structured repayment plan over three to five years, after which all estate property re-vests in the debtor, free from preexisting debt obligations.[27] In either instance, consumer bankruptcy seeks to achieve two goals: promote the debtor's "fresh start" in the world while still maximizing and equitably distributing assets among creditors.

To obtain the benefits and protections of bankruptcy, the debtor must in turn disclose many details about his assets and liabilities. This includes identifying property that is exempt, meaning it will be removed from the bankruptcy estate and returned to the debtor. As explained in more detail below, exemptions can originate from state or federal law depending on where the debtor is domiciled.[28] Exemptions are designed to provide the debtor with enough property to get back on his feet and prevent him from becoming reliant on the government or others for survival.

Procedurally, the debtor must outline his exemptions on Schedule C to the bankruptcy petition. This document can be freely amended and so long as the case remains open at the time the exemption is claimed the bankruptcy court should permit it.[29] Unless a party objects, the asset is presumed exempt. Any objector has the burden to show that the property should not be exempt. Bankruptcy courts across the country recognize a strong norm in favor of exemption and often interpret close cases to allow a debtor to exempt the property.[30] Even after a bankruptcy case is complete, or "closed," the court maintains limited jurisdiction over the debtor. For example, if information comes to light that the debtor had additional, undisclosed assets, an interested party may ask the court to reopen the bankruptcy case to administer the property.[31]

25. The third option, filing under Chapter 11, is usually only selected by debtors who do not want to lose their property in Chapter 7 but who have too many assets to qualify for Chapter 13. *See* 11 U.S.C. § 109(e) (setting debt limits for Chapter 13 debtors).

26. This introductory explanation does not address many nuanced exceptions and potential challenges that could arise in a debtor's bankruptcy case.

27. *See infra* Section I.C.2.

28. *See infra* Part I.C.2. In short, federal exemptions permit a debtor to keep a limited amount of a personal injury payment, while state exemptions range from allowing no exemption whatsoever for personal injury payments to exempting all amounts that the debtor reasonably needs to live his or her life. Depending on the specifics of the claims and the terms of the settlement, mass tort awards may also fall within other exemptions, such as those for lost wages or disability payments.

29. *See In re* Mendoza, 595 B.R. 849, 856–57 (B.A.P. 10th Cir. 2019) (holding that debtors may freely amend schedules in reopened bankruptcy cases to list assets and claim exemptions); *In re* Bronk, 444 B.R. 903 (Bankr. W.D. Wis. 2011) (observing that amendment may be denied if there is evidence of the debtor's bad faith and creditors would be prejudiced).

30. *See In re* Reschick, 343 B.R. 151, 156 (Bankr. W.D. Pa. 2006) ("Given the public policy behind exemptions in bankruptcy, it is of no surprise that the Bankruptcy Rules provide that 'the objecting party has the burden of proving that the exemptions are not properly claimed' by the debtor."); *see also* Sullivan, *supra* note 19, at 341–42 (explaining the bankruptcy-specific policy norms supporting exemptions and contrasting them with motivations for state exemption regimes).

31. 11 U.S.C. § 350(b); FED. R. BANKR. P. 5010.

After all assets are collected and claims against the debtor identified, the available funds are distributed to creditors.[32] The distribution scheme outlined in the Bankruptcy Code first removes exempt property and gives secured creditors the value of their collateral.[33] Next, administrative claims (including the trustee and special counsel fees)[34] and other priority unsecured claims are paid in full,[35] then unsecured creditors receive a pro rata distribution of available funds.[36] Finally, if every other claim is paid in full, any surplus goes to the debtor.[37]

B. Consumer Bankruptcy's Cast of Characters

Bankruptcy cases involve many stakeholders that do not appear in civil litigation, and each one plays an important role in the process Congress designed through the Code. These stakeholders have different powers, responsibilities, and incentives that impact the trajectory of a bankruptcy case. Understanding the various characters is a critical step to understanding why the settlement trap has such a detrimental effect on claimants.

Debtor: The debtor's role requires little explanation. They initiate the bankruptcy process to receive the benefits of bankruptcy and in return face significant oversight, limitations, and scrutiny from other stakeholders.[38] In Chapter 13 cases, the debtor remains in control of estate assets during the course of the bankruptcy and has standing to administer and resolve issues that come up with estate property. In contrast, Chapter 7 debtors have no rights to or control over estate property. Debtors are entitled to exempt certain property, and also receive any surplus from the estate after all claims and administrative expenses are paid.[39]

Judge: Bankruptcy judges are the ultimate gatekeeper for the debtor's path through bankruptcy. These Article I judges have jurisdiction over bankruptcy cases by reference from district courts,[40] and hear and decide a broad range of issues due to the bankruptcy court's vast scope of authority.[41] Bankruptcy judges exercise significant discretion over many key issues, including (as is relevant here) whether to reopen a previously closed bankruptcy case.[42] The bankruptcy bench and bar are

32. The timing of this distribution will depend on what type of bankruptcy the debtor filed.
33. 11 U.S.C. § 522.
34. 11 U.S.C. § 507(a)(1).
35. *Id.*
36. 11 U.S.C. § 726(b).
37. *Id.* § 726(a).
38. In some instances, a debtor may be pushed into an involuntary bankruptcy if three creditors so desire.
39. 11 U.S.C. § 726(a).
40. 28 U.S.C. § 157(a); Schulman v. Cal. Water Res. Control Bd. (*In re* Lazar), 200 B.R. 358, 366 (Bankr. C.D. Cal. 1996) (observing that each district court is authorized to adopt general order of reference for bankruptcy cases).
41. *See* 28 U.S.C. § 157(b)–(c). The judges are appointed for fourteen-year terms by the Circuit Court of Appeals.
42. 11 U.S.C. § 350(b); *see also In re* Ross, 548 B.R. 632, 636 (Bankr. E.D.N.Y. 2016);

relatively tight-knit groups, and the judge often plays a role in facilitating negotiation and settlement among the parties to streamline contested issues and preserve estate value.[43] Judges also shape bankruptcy practice in their districts by communicating expectations and setting boundaries of what will be accepted. Judges can significantly impact how bankruptcy operates at a local level, especially on matters involving discretionary action.

U.S. Trustee: The U.S. Trustee is appointed by statute to appear in every bankruptcy case.[44] Their role is to oversee administrative functions of the bankruptcy process while ensuring that the debtor's actions are consistent with the Bankruptcy Code.[45] The U.S. Trustee is an arm of the Department of Justice, and receives guidance from the Executive Office of the United States Trustee on core issues of bankruptcy practice and procedure.[46] One of the U.S. Trustee's jobs is to appoint and oversee Chapter 7 and 13 trustees for consumer cases. The U.S. Trustee also has standing to appear and be heard on issues within the bankruptcy case, including whether to reopen a closed bankruptcy case for purposes of administering a settlement payment.[47]

Trustee: Trustees serve different functions in Chapter 7 and Chapter 13 cases. The Chapter 7 trustee is tasked with administering the estate of a debtor and has full control over liquidating assets, evaluating claims, and determining distributions. The Chapter 7 trustee has significant discretion to pursue, or abandon,[48] claims and property for the benefit of the estate. It also is the sole party with standing to pursue the debtor's litigation claims and has authority to settle claims on behalf of the estate.[49] The Chapter 7 trustee is compensated via a fee structure outlined in the Bankruptcy Code and often employs special counsel to assist with the legal aspects of its role.[50] Chapter 13 trustees, in contrast, do not control the estate's assets. Instead they serve in an oversight role, confirming that the debtor is acting in the best interests of the estate and ensuring that the debtor proposes and completes a plan that

---

(noting the bankruptcy court's "broad discretion to determine whether a party . . . has demonstrated good cause" to reopen a case).

43. Although bankruptcy judges hear and decide many contested issues, they have a fundamental awareness that the parties are in the best position to value their dispute and reach a solution that preserves value. Stated another way, slash-and-burn bankruptcy litigation consistently benefits attorneys, not the parties.

44. 28 U.S.C. § 586(a)(3). Alabama and North Carolina do not participate in the U.S. Trustee program but have "bankruptcy administrators" that serve a near-identical function.

45. *See* Lindsey D. Simon, *The Guardian Trustee in Bankruptcy Courts and Beyond*, 98 N.C. L. REV. 1297 (2020) (explaining the various functions of the U.S. Trustee).

46. *See, e.g.*, U.S. DEPT. OF JUST., *Significant Guidance Documents*, https://www.justice.gov/ust/significant-guidance-documents [https://perma.cc/L6W3-2C8F].

47. 11 U.S.C. § 350(b); FED. R. BANKR. P. 5010.

48. 11 U.S.C. § 544.

49. *Id.*

50. 11 U.S.C. § 327(e). *See* Pamela Foohey, *A New Deal for Debtors: Providing Procedural Justice in Consumer Bankruptcy*, 60 B.C. L. REV. 2297, 2338–40 (2019) (explaining the Chapter 7 and Chapter 13 trustee compensation models and resulting incentives).

satisfies the Code requirements.[51] Still, the Chapter 13 trustee has discretion to impose requirements on the debtor and make determinations as to what repayment terms are acceptable under the circumstances. Both categories of trustees are integrally involved in consumer bankruptcy cases and the judge relies heavily on their positions and arguments when evaluating a debtor's case.[52] The ways that trustees exercise discretion will vary according to local legal culture, leading to geographical differences in how they approach their role in consumer cases.[53]

Creditors (secured and unsecured): Creditors include any party to whom the debtor owes an obligation as of the petition date. Creditors may be secured, meaning their interest is protected by a security interest that gives them special rights in the value of certain property, or unsecured.[54] For creditors, the bankruptcy process reflects the best-case procedural mechanism for a worst-case scenario. It is inherently unjust that a debtor will not pay back 100% of the creditors' debt. Without bankruptcy's strict protections, however, creditors, especially unsecured creditors, would likely not receive an equal share of the debtor's insufficient remaining assets.[55]

Plaintiffs' attorney: While not technically a bankruptcy-specific party, plaintiffs' attorneys will be involved in just about every bankruptcy case that results in a settlement trap. When a debtor comes into bankruptcy with litigation claims, those claims are usually being pursued by plaintiffs' attorneys. These attorneys may or may not be selected to continue pursuing the estate's claim after the petition date.[56] The Chapter 7 trustee has authority to select attorneys to remain on the case as "special counsel," in which case any post-petition fees due to the plaintiffs' attorney will be classified as an administrative claim, meaning that they will be repaid before general unsecured creditors.[57]

---

51. *See* John A. E. Pottow, *Fiduciary Duties in Bankruptcy and Insolvency*, LAW & ECON. WORKING PAPERS, Mar. 29, 2018, at 1, 4–5 (discussing the role of Chapter 13 trustees).

52. This is not to say that the court is beholden to trustees or is likely to take their arguments over those of the debtor; rather, they are a repeat stakeholder that the court will consistently ask for input on important matters.

53. *See, e.g.*, Pamela Foohey, *Access to Consumer Bankruptcy*, 34 EMORY BANKR. DEVS. J. 341 (2018) (identifying the impact of local legal culture in consumer bankruptcies); Jay Lawrence Westbrook, *Local Legal Culture and the Fear of Abuse*, 6 AM. BANKR. INST. L. REV. 25 (1998); Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, *The Persistence of Local Legal Culture: Twenty Years of Evidence from the Federal Bankruptcy Courts*, 17 HARV. J.L. & PUB. POL'Y 801, 804 (1994) (describing the impact of local legal culture in bankruptcy).

54. *See* Pamela Foohey, Robert Lawless & Deborah Thorne, *Driven to Bankruptcy*, 55 WAKE FOREST L. REV. 287, 298–303 (2020) (outlining the different categories and treatment of creditors in consumer bankruptcy).

55. Instead, in a world without bankruptcy the debtor would pay off preferred creditors in full while leaving nothing for other creditors.

56. Recall that, as of the petition date, the estate holds all litigation claims.

57. *See* 11 U.S.C. § 327(a).

C. Doctrinal Contours and Tension Points

Focusing once again on the bankruptcy treatment of settlement payments, the vast majority of challenges relate to three doctrinal issues: (1) whether the settlement is property of the estate based upon when it accrued, (2) whether the settlement is exempt, and (3) whether the claimant is judicially estopped to recover the payment. Procedurally, disputes over treatment of mass tort settlement payments generally arise in one of several contexts, including: at a motion to reopen a closed bankruptcy case to administer a settlement, in a trustee's motion under Rule 9019 to seek approval of a settlement, or on a party's objection to the debtor's claimed exemption. Most often, the core of these disputes involves tension between the debtor and the trustee.

1. Property of the Estate

When evaluating the bankruptcy treatment of settlement payments, the first step is deciding whether the payment is property of the estate. Simply put, if the debtor's property included the claim at issue on the petition date, then it is property of the estate.[58] When the debtor receives settlement payments or files litigation claims before filing a bankruptcy petition, there is little doubt that they are estate assets; however, claims that are not yet known to the debtor when he files for bankruptcy may still be estate property. The accrual analysis for whether litigation claims are property of the estate varies by jurisdiction, but generally falls within one of three approaches: (1) whether the debtor discovered, or should have discovered, the harm as of the petition date; (2) whether all of the elements of the claim were present before the petition date; or (3) whether the post-petition claim was "sufficiently rooted" to the debtor's pre-bankruptcy past such that it should be included as an asset of the estate.[59]

Bankruptcy courts look to state law on accrual to determine whether an asset is property of the estate.[60] Differences in state-accrual methods are especially apparent in the mass-tort context, where latent injury is a frequent issue.[61] Many states incorporate a permissive, discovery-based framework that evaluates whether, at the time of the bankruptcy petition (or during the pendency of the bankruptcy if in a

---

58. 11 U.S.C. § 541.

59. *See* Nicole Pellerin, *Undisclosed Claims and Causes of Action*, 2016 AM. BANKR. TR. J., 32, 33–34 (describing different accrual considerations); *see also In re* Ross, 548 B.R. 632 (Bankr. E.D.N.Y. 2016) (applying the elements approach and determining that medical device claim was not property of the estate).

60. *See* Butner v. United States, 440 U.S. 48, 54–55 (1979); Cusano v. Klein (*In re* Cusano), 264 F.3d 936 (9th Cir. 2001). Most states do not have a bankruptcy-specific accrual scheme, but instead look to state law on accrual for purposes of statutes of repose and limitation. *See, e.g., In re* Purcell, 573 B.R. 859, 867 (Bankr. D. Kan. 2017) (applying Kansas non-bankruptcy statute of limitations to accrual issue). State legislatures set such time periods for purposes of barring claims, not impacting exemptions.

61. *See* Ponoroff, *supra* note 12 (discussing accrual standards).

Chapter 13 case),[62] the debtor knew, or should have known, of his claim.[63] This accrual method prevents debtors who had no reason to know they had been injured, or had a claim for the injury, from having their settlement dragged back into bankruptcy.

On the other end of the spectrum, courts in product-based cases look to when the defective item left the factory or when it first made contact with the debtor.[64] These approaches may reflect state law preferences on limiting expansive statutes of repose or limitation; however, their impact when imported into bankruptcy's "asset of the estate" determination is striking. One bankruptcy judge considered the practical result of prepetition-exposure standards, concluding that:

> [s]uch analysis would expand property of the estate to include any interest so long as a trustee can tie such interest to a debtor's "pre-bankruptcy past" and would transform section 341 meetings of creditors into health examinations. Opportunistic trustees would be scrambling to latch onto every possible claim that may someday arise, however attenuated.[65]

Trustees in exposure-based accrual states embrace the ease of administration that comes from clear prepetition-exposure standards, observing that they do not waste estate assets arguing with debtors about whether settlements are property of the estate.[66] That may be correct, but administrative ease cannot be the deciding factor, especially where the substantive impact is dragging claimants with no prepetition knowledge of their injury into the settlement trap.

A majority of circuits consider a different, federally created standard in addition to (or instead of)[67] state law accrual standards.[68] These courts ask whether the claim was "sufficiently rooted in the [debtor's] pre-bankruptcy past."[69] True to form, courts have interpreted this standard to mean different things in different contexts,[70] further complicating the doctrine.

---

62. Interestingly, if a debtor converts her case from Chapter 13 to Chapter 7, any post-petition claims that would have been an asset of the Chapter 13 estate revert back to the debtor. *See In re* Love, No. 15-34977-KRH, 2019 WL 2427198, at *2, *2 n.16 (Bankr. E.D. Va. June 10, 2019) (citing 11 U.S.C. §§ 348(f)(1)(A), 1306(a)).

63. *See In re* Purcell, 573 B.R. 859, 867 (Bankr. D. Kan. 2017) (applying a discovery test).

64. *See, e.g.*, *In re* Carroll, 586 B.R. 775, 782–90 (Bankr. E.D. Cal. 2018) (determining that the implantation of the debtor's pelvic mesh was the relevant time for accrual purposes); *In re* Davis, No. 10-24836-JRS, 2018 WL 2223076 (Bankr. N.D. Ga. May 15, 2018) (same).

65. *In re* Ross, 548 B.R. 632, 640–41 (Bankr. E.D.N.Y. 2016).

66. Curiously, none of the trustees mentioned the financial upside of their state's interpretation: more assets to administer results in more fees to the trustee. *See infra* Section II.C.2.

67. *See In re* Richards, 249 B.R. 859, 861 (Bankr. E.D. Mich. 2000).

68. *See, e.g.*, Segal v. Rochelle, 382 U.S. 375, 379–81 (1966).

69. *Id.* at 380.

70. *See, e.g.*, *In re* Harber, 553 B.R. 522, 533 (Bankr. W.D. Pa. 2016) (asking whether a substantial portion of the claim accrued prepetition such that it would be inequitable to keep the asset from creditors); Underhill v. Huntington Nat'l Bank (*In re* Underhill), 579 Fed. App'x. 480, 482 (6th Cir. 2014) (concluding that without prepetition injury, the claim could

Ironing out the accrual standards in each state for each type of claim is beyond the scope of this Article, and any effort to paint a nationwide picture would be outdated just as quickly as it were published.[71] Whatever the standards may be, debtors with settlement payments—and the trustees/creditors seeking to collect or distribute them—will need to understand the law. A court's determination about whether a settlement payment is an asset of the estate has real consequences. If settlement payments are outside the estate, then the debtor can escape bankruptcy-imposed administrative costs and potentially lengthy litigation about whether the settlement is exempt. Additionally, if the bankruptcy remains open while the litigation claim is pending, then a decision that the claim belongs to the estate divests the debtor of standing to pursue it and opens the door to the trustee's discretionary resolution of the claim.[72] As this Section illustrates, identical debtors may experience starkly different experiences across state lines.

2. Exemptions

The bankruptcy estate, though vast, does not include *every* asset the debtor owns as of the petition date. Recognizing the debtor's need to survive after bankruptcy, current law permits the debtor to keep, or "exempt," certain types of property.[73] While simple in theory, the exemption doctrine is extremely complicated to apply. This Section introduces bankruptcy exemptions, outlines their origin and purpose, and explains the process for evaluating and claiming exemptions.

The Bankruptcy Code exempts certain of the debtor's settlement payments from collection, reflecting a public policy that promotes a "fresh start" after bankruptcy.[74] However, vast differences among each state's exemption standards create uncertainty that even experienced bankruptcy professionals struggle to unravel. Deciding which payments are exempt from the bankruptcy trustee's grasp can turn on what may seem like inconsequential characteristics and details of a settlement.[75]

---

not be sufficiently rooted in the debtor's prepetition life); Mueller v. Hall (*In re* Parker), No. 06–8053, 2007 WL 1376081, at *7–8 (B.A.P. 6th Cir. 2007) (framing the analysis as whether there is a strong nexus between the action and pre-bankruptcy events).

71. Additionally, it is the stuff of nightmares for research assistants or first-year associates.

72. *See* Fair v. Biogen Idec Inc., No. 11-1509, slip op. at 12–16 (Mass. Super. Ct. June 12, 2012). As described in Section II.C.2, trustees have both incentive and opportunity to settle claims in ways that eliminate the debtor's opportunity to claim an exemption.

73. *See* Sullivan, *supra* note 19 at 337–38.

74. Lawrence Ponoroff & F. Stephen Knippenberg, *Debtors Who Convert Their Assets on the Eve of Bankruptcy: Villains or Victims of the Fresh Start?*, 70 N.Y.U. L. REV. 235 (1995) ("A central feature of American consumer bankruptcy law is the 'fresh start' policy, which, through the dual mechanisms of discharge and exemption, affords debtors a certain degree of economic viability in exchange for the surrender of present assets at filing.").

75. *See* Alan N. Resnick, *Prudent Planning or Fraudulent Transfer? The Use of Nonexempt Assets to Purchase or Improve Exempt Property on the Eve of Bankruptcy*, 31 RUTGERS L. REV. 615, 621 (1978) (noting that exemptions are designed "(1) [t]o provide the debtor with property necessary for . . . survival; (2) [t]o protect the dignity and the cultural and religious identity of the debtor; (3) [t]o enable the debtor to rehabilitate himself [or herself] financially and earn income in the future; (4) [t]o protect the debtor's family from the adverse consequences of impoverishment; [and] (5) [t]o shift the burden of providing the debtor and

Both state and federal interests are implicated by exemption law, and there are parallel doctrinal frameworks both in and outside of bankruptcy. The Code's exemption provisions are designed with the realities of insolvency in mind. The benefits of the fresh start from the federal perspective are widespread, from the debtor (who is enabled to maintain his dignity) to the broader society (which will not have to bear the burden of the debtor's financial woes).[76] State-level incentives for exemption law are slightly different, as they were not created with bankruptcy in mind. Instead, state exemption standards are intended to address debtor-creditor relationships and create some basic floor to a creditor's collection efforts, regardless of a debtor's insolvency.[77] Given the different policy perspectives at the state and federal levels, Congress encountered significant conflicts when deciding how the bankruptcy exemption scheme should relate to existing state law.[78] When drafting the modern bankruptcy code in the early 1970s, Congress appointed a commission of bankruptcy experts to provide guidance on a number of issues.[79] Regarding opt-out provisions and state exemptions, the commission recommended imposing uniform federal exemptions.[80] After heated political debate, Congress went against the recommendations and included both state and federal exemption options in the legislation, at the preference and discretion of each state.[81]

To identify whether certain assets are exempt, the debtor must know which exemptions apply. Because Congress permitted the state opt-out provision in section 522, not all debtors will be eligible to use the federal exemptions. The Bankruptcy Code imposes a domicile rule on section 522, which requires debtors to use the exemptions of the state where the debtor was domiciled for the 730 days prior to the petition date.[82] If the debtor was domiciled in more than one state during that window, then the debtor takes the exemptions of the state where he lived during the 180 days prior to the 730-day period.[83] While the choice-of-law analysis generally maps on to the state where the debtor is eligible to file for bankruptcy (i.e., the forum state), the rights to exemption are personal, not geographic, and move with the debtor.[84] Once the debtor knows which state's exemption laws apply, she can evaluate what options there may be for specific property.

---

his family with minimal financial support from society to the debtor's creditors").

76. *See* Sullivan, *supra* note 19, at 341–45 (describing the policy implications of federal exemptions).

77. *See generally* Ponoroff, *supra* note 14, at 356–60 (describing tension between exemption incentives at the state and federal level).

78. *See* Sullivan, *supra* note 19, at 343–45.

79. S.J. Res. 88, 91st Cong. (1970).

80. H.R. Doc. No. 93-137, pt. 1, at 170–74 (1973). *See also* Stephen G. Gilles, *The Judgment-Proof Society*, 63 WASH. & LEE L. REV. 603, 624–25 n.84 (2006) (describing the opt-out regime).

81. 11 U.S.C. § 522(b)(2). Exemptions have long been a critical element of consumer bankruptcy and one that is consistently under review and analysis. *See* Charles J. Tabb, *The Top Twenty Issues in the History of Consumer Bankruptcy*, 2007 U. ILL. L. REV. 9, 13–14 (2007) (listing exemption issues as important in history).

82. 11 U.S.C. § 522(b)(3)(A).

83. *Id. But see In re* Pederson, 105 B.R. 622, 624–25 (Bankr. D. Colo. 1989) (applying—prior to institution of the Bankruptcy Code's domicile rule—Colorado choice of law rules to determine that Colorado law should apply and not the underlying litigation forum state).

84. *See* Daniel A. Austin, *Bankruptcy and the Myth of "Uniform Laws"*, 42 SETON HALL

As explained above, exemptions may originate at the state or federal level. The applicable law will outline the category of property that may be exempt and any conditions for eligibility (such as mandatory characteristics of property, use, or value).[85] In many instances, exemptions are not an all-or-nothing proposition. Where the Bankruptcy Code identifies exempt property on a per item basis—for example, the exemption for an automobile found in section 522(d)(2)—and the property falls within the dollar limitation, then the debtor may keep that property.[86] A valuation analysis of the property is completed as of the petition date; if the property increases in value during the bankruptcy case, then the upside goes to the debtor.[87] If, however, the value of the asset exceeds the threshold, then the asset is not fully exempt.[88] The Chapter 7 trustee is the sole party with standing to administer the asset, and the debtor will receive the value of the exemption (with excess value going to the estate).[89] In the event of a valuation dispute, the challenger has the burden to prove that the asset's valuation exceeds the exemption amount.[90] Some jurisdictions permit a debtor to layer or "stack" available exemptions up to the amount of the asset, while others require a debtor to elect an exemption and collect only that portion.[91]

Settlement payments may qualify under multiple exemptions. Relevant exemptions for mass tort settlements under federal law include exemptions for personal injury,[92] loss of wages,[93] disability benefits,[94] and the "wildcard" exemption, which may be applied to any property.[95] Whether a settlement payment

---

L. REV. 1081, 1094–96 (2012) (outlining the choice-of-law issue). The vast majority of scholarship and litigation surrounding choice-of-law issues relates to homestead exemptions, which vary greatly by state. This is, in part, due to the visibility and public condemnation of debtors purchasing million-dollar estates on the eve of bankruptcy and then exempting them, thwarting creditors.

85. *See generally* Sullivan, *supra* note 19 at 356–58 (describing different states' limitations on property exemptions).

86. *See, e.g.*, *id.* at 337 n.2 (explaining the operation of a motor vehicle exemption in different dollar-value scenarios).

87. *See, e.g.*, Polis v. Getaways, Inc. (*In re* Polis), 217 F.3d 899, 902 (7th Cir. 2000) (noting the possibility that assets appreciate over the course of the bankruptcy).

88. *See* Ponoroff, *supra* note 19 at 362 n.46.

89. *See* William T. Clarke, *A Bankruptcy Primer for Personal Injury Lawyers*, S.C. LAW. 30, 31 (2007) (describing a scenario in which a debtor's asset is sold with amounts in excess of a state exemption being returned to the estate). In Chapter 13 cases, the debtor remains in possession of estate assets that revest in the debtor when the payment plan is finalized, though, in some jurisdictions, the Chapter 13 trustee may take an interest in pending litigation and ask the court for additional assistance or oversight authority. *Id.* at 31, 33.

90. *In re Polis*, 217 F.3d at 904 (citing FED. R. BANKR. P. 4003(c)).

91. *See* Uriel Rabinovitz, Note, *Toward Effective Implementation of 11 U.S.C. § 522(d)(11)(E): Invigorating a Powerful Bankruptcy Exemption*, 78 FORDHAM L. REV. 1521, 1551–52 (2009) (explaining exemption stacking in the settlement payment context).

92. 11 U.S.C. § 522(d)(11)(D).

93. *Id.* § 522(d)(11)(E); *see also* Rabinovitz, *supra* note 90, at 1523 (explaining the possibility that mass tort payments may fall within the "lost wages" exemption depending upon how they are structured).

94. 11 U.S.C. § 522(d)(10)(C).

95. *Id.* § 522(d)(5) (permitting a debtor to exempt up to $1325, in addition to any amount up to $12,575 of the $25,150 homestead exemption that remains unused, in any type of property).

falls within any of these exemptions will turn on the facts of the case and the forum law governing their application. While federal exemptions are uniform, they are not uniformly applied; there is significant ambiguity regarding specific applications.[96]

State law exemptions relating to mass tort settlement payments fall along a wide spectrum.[97] Some states permit a debtor to retain any amount, while others offer no exemption.[98] State law may provide a set of exemptions for civil litigation that are different from bankruptcy-specific exemptions, and the debtor may be in a position to elect between the exemptions.[99] Most states permit a debtor's stake in ongoing litigation to be exempted if it falls within an available category,[100] but others require a settlement to be finalized, or *liquidated*, before the petition date to qualify for an exemption.[101] Finally, there may be instances where part of the settlement is exempt but the remaining portion is not. For example, in a state where pain and suffering may be exempt but payments for future wages are not, the settlement agreement could identify which part of the settlement falls into which category. When settlement agreements do not identify the source or a purpose for the payment, the court will be asked to decide which portion is eligible for exemption. The law is divided on which party bears the burden to show how the settlement payment is allocated.[102]

3. Estoppel

Another doctrinal challenge involving settlement payments is judicial estoppel, an equitable doctrine that prevents litigants from taking inconsistent positions in subsequent litigation. This arises in the bankruptcy context when a debtor fails to list a cause of action (or potential cause of action) on her mandatory disclosures and

---

96. *See* Rabinovitz, *supra* note 90, at 1541–43.

97. *See* WILLIAM HOUSTON BROWN, LAWRENCE R. AHERN, III & NANCY FRAAS MACLEAN, BANKRUPTCY EXEMPTION MANUAL app. B (West ed. 2020) (outlining treatment of settlement payments under state law); Joseph J. Blyskal, III, Comment, *Levying Flesh and Charging Society, Creditors, and Insurance Companies for It: The Irony of Including Personal Injury Awards in the Bankruptcy Estate*, 23 EMORY BANKR. DEVS. J. 677, 701–05 (2007) (discussing states' approaches to exempting personal injury settlements).

98. *See* Sullivan, *supra* note 19 at 338 (comparing the available exemptions in different states); MD. CODE ANN., CTS. & JUD. PROC. § 11-504(b)(2) (2014); Cerny v. Salter, 429 S.E.2d 809 (1993) (confirming the unlimited cap to exempt settlement payments under South Carolina's exemption statute).

99. *Compare* MICH. COMP. LAWS § 600.5451 (through 2020 Public Act 149) (outlining bankruptcy-specific exemptions), *with id.* § 600.6023 (providing non-bankruptcy collection exemptions).

100. *See, e.g.*, MISS. CODE ANN. § 85-3-17 (2020); NEB. REV. STAT. ANN. § 25-1563.02 (LexisNexis 2019).

101. *In re* Key, 255 B.R. 217, 84 Fair Empl. Prac. Cas. (BNA) 1010 (Bankr. D. Neb. 2000) (concluding that Nebraska's personal injury exemption, Neb. Rev. Stat. Ann. § 25-1563.02, was not available for unliquidated claims).

102. *See, e.g.*, *In re* Meyer, 433 B.R. 739, 744–46 (Bankr. D. Minn. 2010) (placing the burden on the trustee to show, by the preponderance of the evidence, that an exemption is not validly claimed, and concluding that an entire payment could be exempt despite not having clear apportionment between pain and suffering and future earnings).

receives a discharge.[103] Defendants in later proceedings argue that the claimant's omission operates as a statement in her bankruptcy that no such claim existed and, as a result, the claimant cannot later sue the defendant.[104] Judicial estoppel may apply to bar the debtor's claim[105] where (1) a party's position is clearly inconsistent with a previous one, (2) the court accepted the previous position, and (3) the non-disclosure was not inadvertent.[106] Whether or how these standards are met varies significantly in different parts of the country. In a mass tort case, the choice-of-law analysis for judicial estoppel is a matter of federal common law that looks to where the mass litigation (and not the bankruptcy case) is pending.[107]

The first two elements are easily established when the debtor received a discharge without disclosing the claim on her petition.[108] The bankruptcy court's grant of a discharge necessarily relies on full disclosure of all assets,[109] and the debtor's failure to list the claim is akin to a statement that no such claim exists. On the inadvertence requirement, multiple circuits have permitted an inference of bad faith where the debtor knew about the claim and had motive to conceal it, concluding that a debtor always has motive to conceal a settlement.[110] Thus, a debtor may only argue inadvertence if he had no knowledge of the claim. In other circuits, the debtor may amend his schedules freely to avoid judicial estoppel.[111] These courts conclude that, by giving the trustee an opportunity to administer the estate, the underlying purpose of disclosure in bankruptcy is met and the defendant would receive a windfall if judicial estoppel were imposed.[112]

---

103. *See, e.g.*, Fair v. Biogen IDEC, Inc., No. 11-1509, 2012 WL 2417722 (Mass. Super. June 13, 2012). The Bankruptcy Code only discharges claims of the debtor that were disclosed. *See* 11 U.S.C. § 727(a). Note that standards for judicial estoppel may vary between Chapter 7 and Chapter 13 cases, where the timeline for disclosure and discharge are significantly different. *See* Byrd v. Wyeth, 907 F. Supp. 2d 803 (S.D. Miss. 2012).

104. I find it somewhat ironic that judicial estoppel in bankruptcy comes from a desire to support the finality of confirmation orders, but the same logic does not prevent trustees from reopening cases that were long resolved to administer previously unknown assets after the debtor relied on the finality of confirmation.

105. The trustee, however, is not barred by judicial estoppel because it was not the party who made conflicting representations. *See, e.g.*, Parker v. Wendy's Int'l, Inc., 365 F.3d 1268, 1271–72 (11th Cir. 2004).

106. *See* Love v. Tyson Foods, Inc., 677 F.3d 258, 261 (5th Cir. 2012).

107. *See In re* Taxotere (Docetaxel) Prods. Liab. Litig., No. 16-2740, 2018 WL 5016219, at *2–3 (E.D. La. Oct. 16, 2018) (applying Fifth Circuit law on judicial estoppel to a debtor who filed for Chapter 7 in Ohio because the MDL transferee court for the underlying claim was in the Fifth Circuit).

108. Some courts have even found reliance where the bankruptcy remains open. *See, e.g.*, *Love*, 677 F.3d 258.

109. *See* Chartschlaa v. Nationwide Mut. Ins. Co., 538 F.3d 116, 122 (2d Cir. 2008) (discussing the impact of a debtor's failure to disclose assets).

110. *See* Eastman v. Union Pac. R.R. Co., 493 F.3d 1151, 1157–59 (10th Cir. 2007); Stallings v. Hussmann Corp., 447 F.3d 1041, 1048 (8th Cir. 2006) (quoting *In re* Coastal Plains, Inc., 179 F.3d 197, 210 (5th Cir. 1999)); Barger v. City of Cartersville, 348 F.3d 1289, 1294–98 (11th Cir. 2003); *In re Coastal Plains*, 179 F.3d at 210; Ryan Operations G.P. v. Santiam-Midwest Lumber Co., 81 F.3d 355, 362–63 (3d Cir. 1996).

111. *See* Dunmore v. United States, 358 F.3d 1107, 1113 (9th Cir. 2004).

112. *See id.* at 1113 n.3; *see also* Cannata v. Wyndham Worldwide Corp., 798 F. Supp. 2d 1165, 1175–76 (D. Nev. 2011) (rejecting judicial estoppel but creating equitable limitation on

II. THE SETTLEMENT TRAP IN MASS TORT CASES

Bankruptcy's treatment of settlements is imprecise and imperfect. This Part contextualizes the bankruptcy-specific challenges in one particularly troubling environment: mass tort cases. By using mass tort cases as an example, this Part introduces the paradigmatic settlement trap. It identifies three core characteristics of a settlement trap, and then explores the underlying forces that cause the trap to form.

A. Bankruptcy's Collision Course with the Mass Tort System

Consumer debtors have litigation assets in all forms, and many of the same characters (exercising the same discretion) will be asked to administer diverse claims relating to business disputes, car accident injuries, and family law issues. Why, then, does this Article focus on mass tort claims? This Section explores why mass tort cases pose a particularly severe settlement trap and explains why they also offer a useful forum to identify challenges and implement solutions.

1. Additional Characters

Mass tort cases introduce additional stakeholders to a consumer bankruptcy litigation scenario. Understanding the different role of these participants will help shape the ultimate prescription.

Aggregate-litigation counsel: In addition to individual plaintiffs' attorneys, claimants in aggregate litigation cases will also be "represented" by a lead group of lawyers who act, formally or informally, on behalf of all claimants. This may take the form of class counsel in class actions, the "plaintiff's steering committee" in MDLs, or other ad hoc committees. Whether the case involves a class action, which is binding on all claimants, or other aggregation device, which collects cases but preserves their individual status, most settlements arise out of the aggregate-litigation counsel's negotiations with defendants.[113] Additionally, assuming the defendants agree to settle, the aggregate litigation counsel is also closely involved with the defendants in defining the terms and conditions of the claim distribution program.[114]

Mass tort defendants: Every litigation claim involves at least one defendant; however, mass tort defendants are different from defendants facing individual plaintiffs because they negotiate and think of cases on a global scale. For example, due to the number of potential claims at issue, a mass tort defendant may desire settlements to have certain characteristics, such as allocation of settlement proceeds to exclude pain and suffering, inclusion of mandatory no-fault releases, and other

---

the debtor's ability to recover).

113. To be effective, such agreements outside of the class action context will require buy-in from the individual claimants and their attorneys.

114. *See* Francis E. McGovern, *The What and Why of Claims Resolution Facilities*, 57 STAN. L. REV. 1361, 1373–78 (2005) (noting that some settlement programs are formed through consensus-building efforts with stakeholders).

terms.[115] Mass tort defendants may be incentivized by different issues in different contexts but overall tend to take positions on timing, valuation, and closure.[116] Given their role in structuring settlement programs, mass tort defendants set the rules by which claimants are eligible for relief.

Claims administrator: Claims administrators are the gatekeepers for settlement payments. They oversee administration of the settlement program according to program terms negotiated by the parties. Claims administrators advise the parties on important terms to include, and their current practice is to request information about a claimant's bankruptcy history. When a claimant has a potential bankruptcy issue, claims administrators evaluate whether the settlement may be property of the estate. To do so, they do not conduct a state-specific analysis; rather, they take a conservative view of what could possibly be an estate asset.[117] If a claim is potentially impacted by bankruptcy, the claims administrator puts the funds aside in a separate bank account and will not release them until the claimant or another party provides proof of who may receive the payment and (critical to mass tort defendants) who has the authority to release the claim.[118] The consequences of mistakenly paying the wrong party are significant. The claims administration business is extremely competitive, and incorrectly distributing funds without an effective release for the defendant is a surefire way to fall behind competitors for future engagements, not to mention any indemnification obligations owed to the mass tort defendants.

Litigation finance companies: Finally, mass tort claimants and their plaintiffs' attorneys may turn to litigation finance companies to sustain themselves while waiting for a settlement payment.[119] The presence of litigation finance may impact settlement negotiations and have a broader impact on the litigation system. Litigation finance companies also have an interest in whether the claimant's payment is

---

115. *See* Claims Administrator, *supra* note 13 (describing different terms defendants have crafted in settlement documents). *See also* D. Theodore Rave, *Closure Provisions in MDL Settlements*, 85 FORDHAM L. REV. 2175, 2179–82 (2017) (outlining defendant-driven elements in MDL settlements). Mass tort defendants can take advantage of the exemption scheme by overvaluing the claim above an exemption cap so that the trustee—and not the claimant—has control over the litigation. While the claimant might be motivated to reject the settlement to pursue his claims, the trustee is more likely to settle.

116. "Some mass tort defendants are happy to pay more money to delay the process, while others want it to be streamlined to reduce the overall costs." Plaintiffs' Attorney 1, *supra* note 6.

117. The claims administrators do not evaluate whether exemptions could apply.

118. Claims Administrator, *supra* note 13. In class action cases, where releases are mandatory on a class-wide basis, this concern is less pressing, and settlement programs are usually more permissive on when to release bankruptcy-impacted claims.

119. *See* Elizabeth Chamblee Burch, *Financiers as Monitors in Aggregate Litigation*, 87 N.Y.U. L. REV. 1273, 1313 (2012) (describing the role of litigation finance companies in aggregated consumer cases); ABA Comm'n on Ethics 20/20, *White Paper on Alternative Litigation Finance*, AM. BAR ASS'N 1 (Oct. 19, 2011), https://www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111019_draft_alf_white_paper_posting.authcheckdam.pdf [https://perma.cc/TBH8-CP3H]; Byron G. Stier, *The Sale and Settlement of Mass Tort Claims: Alternative Litigation Finance and a Possible Future of Mass Tort Resolution*, 23 WIDENER L.J. 193 (2013) (describing mass tort litigation finance).

property of the bankruptcy estate; if so, the company can usually only recover to the extent the claimant has rights to an exemption or surplus.

2. Complicating Factors

The mass tort industry presents a number of factors that fuel the settlement trap. Practically, mass tort cases are relevant because they are a likely catalyst for the development of bankruptcy law in this area. Stated another way, many of the most recent doctrinal challenges described above arose out of claims in mass tort cases. There are a number of reasons why this is the case. First, mass tort claims commonly involve latent injuries, which increases the likelihood that a debtor would have filed for bankruptcy after the seeds of the claim were planted but long before the injury lawsuit was filed (i.e., the facts often lead to accrual challenges that impact the "property of the estate" determination). Second, the sheer number of mass tort claimants and the potentially disabling impact of mass tort injuries both suggest a high volume of claimants with bankruptcy issues. As described above, those issues would play out under different states' laws across the country, leading to confusion. Finally, and most importantly, many mass tort cases impose a bankruptcy notice regime that requires claimants to disclose information about any previous bankruptcies in their claim form.[120] By collecting this information and requiring claimants with a history of bankruptcy to take additional steps for payment, the mass tort process redirects significantly more settlements to the bankruptcy court for trustee approval.

Mass tort cases also have complicating characteristics that impact claimants. First, the representational structure in many mass tort cases is so distant that it's hard to imagine any decisions being made with potential bankruptcy implications in mind.[121] Second, repeat players dominate the mass tort industry, and commentators identify significant concerns about fee-seeking behavior by the various stakeholders.[122] Third, mass tort cases are often linked with litigation finance

---

120. *See, e.g.*, *NFL Concussion Settlement Claim Form for Retired NFL Football Players and Representative Claimants*, NFL CONCUSSION SETTLEMENT 10 (requesting information about any previous bankruptcy cases), https://www.nflconcussionsettlement.com/Docs/Claim_Form_for_Retired_NFL_n_Representative_Claimants.pdf [https://perma.cc/4LL3-6T65]. The pelvic mesh MDL also contains a bankruptcy disclosure requirement. Curiously, non-tort aggregate litigation cases—such as securities class actions—have not adapted a pattern of requiring bankruptcy disclosures, despite the fact that settlement awards may be significant and could be administered by the trustee just as the mass tort settlements described in this paper. *See, e.g.*, *Proof of Claim and Release Form*, CLOVIS SEC. LITIG., https://www.clovissecuritieslitigation.com/Content/Documents/Claim%20Form.pdf [https://perma.cc/8DC8-AUZT].

121. *See* Howard M. Erichson, *Beyond the Class Action: Lawyer Loyalty and Client Autonomy in Non-Class Collective Representation*, 2003 U. CHI. LEGAL F. 519, 529 (describing the lack of individualized representation in aggregate litigation); *see also* Linda S. Mullenix, *Aggregate Litigation and the Death of Democratic Dispute Resolution*, 107 NW. U. L. REV. 511, 511 (2013) (describing representational challenges in various forms of aggregate litigation); Samuel Issacharoff, *The Governance Problem in Aggregate Litigation*, 81 FORDHAM L. REV. 3165, 3167 (2013) (identifying the "agency problem" in aggregate representation).

122. *See* ELIZABETH CHAMBLEE BURCH, MASS TORT DEALS: BACKROOM BARGAINING IN

companies, which give claimants access to much-needed funding while they wait for an award. These companies become creditors that have a vested interest in the outcome of the claimant's effort to recover payment, and that interest is intensified when the payment is within the grasp of a bankruptcy trustee. Litigation finance creditors may push to resolve whether a claimant's settlement payment will be captured and administered by the trustee, as the determination will impact the creditor's ability to recover from the claimant.[123]

For these and other reasons, mass tort cases are particularly complicated and impose additional structural barriers for claimants. Making changes that improve the settlement trap in mass tort cases will also improve, or create a roadmap to improve, similar challenges in nonaggregate litigation.

3. Tales from the Litigation Trenches

> *I had one client who called up and said he got an award for $1.5 million net, and the trustee won't budge on giving the debtor just $200 thousand. I didn't know how to help him any longer, but it really stuck with me.*
>
> *This one left me scratching my head: Gentleman has been on disability and struggling for probably three decades. He was involved with a bankruptcy about two decades ago that was closed around 2005. He gets involved in the CTE case years after the closed bankruptcy and pleads that he couldn't know about his injury until now because the NFL failed to disclose anything about the diseases. I'm not a bankruptcy person, but I find it hard to believe that this poor guy has to reopen a bankruptcy, from 15 years ago, and ask around if anybody has any entitlement to his money.*[124]

In this Section, and throughout the Article, I quote from dozens of interviews I conducted with prominent stakeholders in bankruptcy and mass tort cases. I began with a list of mass tort attorneys involved in the NFL CTE MDL, prominent trustees, and bankruptcy attorneys who have represented clients in cases creating precedent

---

MULTIDISTRICT LITIGATION (Cambridge 2019) (explaining the insular relationships and conflicted decision-making in MDL negotiations); Howard M. Erichson, *Aggregation as Disempowerment: Red Flags in Class Action Settlements*, 92 NOTRE DAME L. REV. 859, 863–64 (2016) (identifying systemic challenges of aggregate litigation); David M. Jaros & Adam S. Zimmerman, *Judging Aggregate Settlement*, 94 WASH. U. L. REV. 545, 557–62 (2017) (describing incentive problems in the aggregate settlement process); Elizabeth Chamblee Burch, *Publicly Funded Objectors*, 19 THEORETICAL INQUIRIES L. 47, 51 (2018) (noting the inability of the adversary system to highlight "scurrilous behavior" in class settlements due to the shared incentives on all sides to pursue approval); Thomas D. Morgan, *Client Representation vs. Case Administration: The ALI Looks at Legal Ethics Issues in Aggregate Settlements*, 79 GEO. WASH. L. REV. 734, 741 (2011) ("The only people with a powerful bias toward particularized representation, in short, are the clients whose interests the law purports to protect. The risk is that, when lawyers and judges make the rules, clients will tend not to have their interests heard.").

123. One plaintiff's attorney disclosed that many clients cannot receive litigation funding due to the shadow of bankruptcy. Plaintiffs' Attorney 1, *supra* note 6.

124. Plaintiffs' Attorney 4, *supra* note 14.

on these issues. Interviewees then provided recommendations for additional contacts who had encountered the "bankruptcy issue" in mass tort cases. I created a list of questions that I asked each interviewee and saved my written notes from each conversation.[125] You will no doubt observe that names are not included for these individuals. I asked each person whether I could quote them, either anonymously or by name. A significant number would speak with me on background only, and those willing to be quoted insisted on anonymity. They explained that both the mass torts and bankruptcy communities are small and insular, and attorneys rely heavily on repeat engagements. The fear of retaliation, both against the attorney and their client, was palpable. As one attorney explained, "I have to work with these people; I have to help my clients. I can't have anything out there that would let them identify me." These stories bring to light the great injustice of the settlement trap.

Mass tort claimants are acutely impacted by the nuances of bankruptcy law and the way it treats settlement payments. A large part of the problem relates to lack of information and awareness, both for claimants and their attorneys. "I assure you that most practitioners have no idea of the bankruptcy implications of their settlements," said one experienced mass torts attorney.[126] As another plaintiffs' attorney explained, dealing with bankruptcy issues in mass tort cases is like "the law of two worlds that don't fit together colliding."[127] A Chapter 7 trustee gave an example of the potential risk of making mistakes in this complicated area: "I had one case where a plaintiffs' attorney misunderstood the [exemption] statute, thought a $10,000 exemption limit for personal bodily harm would apply to pain and suffering and made a point to allocate the settlement to get an exemption. Because they were wrong, debtor was left in the middle with nothing."[128]

Attorneys shared a sense of helplessness surrounding how and why bankruptcy law stands between their client and relief. One attorney who has more than eighty clients still waiting for payments explained his frustration as follows: "The nature of a mass tort is that you have clients in many jurisdictions. The people in [State A], I can advise them and counsel them on [bankruptcy settlement issues], but normally in a different jurisdiction I have to send them for help from others."[129] The frustration is particularly acute in cases where the bankruptcy was closed long ago. Claims administrators bear the brunt of this frustration. "We are usually met with resistance, consternation and complaining. Nobody knows and understands it. In closed cases, we get lots of pushback saying 'it's closed, why do we gotta worry about it now?'"[130] Even some trustees recognize the potential for absurdity when administering ancient claims: "Do you really think, nineteen years later that anybody is going to file a

---

125. After I provided a detailed summary, the University of Georgia confirmed that this project was exempt from Institutional Review Board for the Protection of Human Subjects in Research (IRB) review based upon Department of Health and Human Services (HHS) regulations published in the Code of Federal Regulations, 45 C.F.R. § 46, on March 8, 1983, and amended in the Federal Register, 56 Fed. Reg. 28001, on June 18, 1991.

126. Plaintiffs' Attorney 1, *supra* note 6.

127. Plaintiffs' Attorney 2, *supra* note 15.

128. Trustee 1, *supra* note 17.

129. Telephone Interview with Plaintiffs' Attorney 3 (Sept. 26, 2019).

130. Claims Administrator, *supra* note 13.

claim?," said one Chapter 7 trustee.[131] "I'd set the bar date and see if any claims are filed. If not, just let it go."[132]

Attorneys and trustees also described the administrative hassle they face to convince claims administrators to release payments.

> Millions and millions of dollars sit there, until what? In theory the court is supervising it. In actual fact, ten years after it's opened, the fund administrator submits a report and says we did X, Y, Z, and we're not sure what they do with the undecideds. There are just lots of bankruptcies where the claims administrator wouldn't pay it out.[133]

As another mass torts lawyer explained, "[m]ore and more administrators hold up money than they used to . . . . [T]he whole process has become so much more legalistically complicated, they have a contract that requires them to jump through eighty-two hoops instead of just getting something done."[134] For their part, claims administrators acknowledged the challenge that claimants face when trying to satisfy the various programs' standards for release. "The programs vary as to how aggressive they want us to be about cleaning this stuff up . . . in individual voluntary programs, people worry about it more because there isn't a [class-wide] release and they want to make sure it's the right person." Attorneys were particularly offended by how quickly the settlement payment was consumed with fees imposed by the process to release payment. "Everything comes out of the claimant's hide, it comes out after the fact, and there's so much money tied up that there is no efficient way to pursue this."[135]

Many plaintiffs' and debtors' attorneys shared stories about clients that were caught within the settlement trap. One NFL player's experience stood out, from beginning to end, as a cautionary tale of the worst a claimant may endure. The player filed for bankruptcy in the early 2000s as the result of a significant judgment debt. Nearly twelve years after the bankruptcy case concluded, the player filed a claim under the NFL settlement program. After the player disclosed the bankruptcy on his claim form, the claims administrator notified the player that he needed to inform the trustee about the claim. The trustee filed a motion to reopen the bankruptcy case and filed an adversary proceeding—a bankruptcy "case within a case"—seeking the court's determination that any settlement payment was an asset of the estate. The player is still challenging that argument, as he was on an NFL team both before and after the bankruptcy case closed, and applicable state law is not certain. Given the imprecise diagnostic process for CTE and the complex nature of brain injuries, it is impossible to determine whether the player's injury related to a single incident or a cumulative injury over a period of years. Assuming the bankruptcy court finds that the claim is estate property, the player's attorney will amend the claimed exemptions from state to federal to obtain a determination that the payment is exempt as a disability payment (the player has serious quality of life challenges).

---

131. *Id.*
132. Trustee 1, *supra* note 17.
133. Plaintiffs' Attorney 1, *supra* note 6.
134. Plaintiffs' Attorney 2, *supra* note 15.
135. Plaintiffs' Attorney 1, *supra* note 6.

The trustee hired counsel, who represented the trustee on a contingency basis. "Basically," said the player's bankruptcy attorney, "counsel is going to take one-third of whatever the trustee recovers. And, again, my client hasn't recovered anything."[136] The attorney recalls a crushing exchange where the trustee threatened to pursue potential cost of appellate fees if the claimant continued to challenge whether the payment belonged to the estate. "Well," the trustee said,

> you would probably win in the bankruptcy court, because I don't think the judge would rule in our favor. And you would probably be affirmed at the District Court level. But if we take it to the [Court of Appeals], depending on the panel, you will probably lose, and your client would owe all the fees.[137]

According to the attorney, it was a "complete shakedown" by a "money-grabber" trustee who has a pattern of similar behavior in the district.[138]

One claims administrator estimated that 5–10% of all claims in a case will be flagged for bankruptcy hold and the connected payment segmented in a bank account pending resolution. In the NFL settlement program, for example, current statistics show that 2721 claimants are eligible for payments that total $1.65 billion.[139] Assuming a 10% hold rate[140] and equal claim values, this means that more than 250 claimants, and more than $165 million in claims, could have fallen into the settlement trap in one case alone.

B. Elements of the Settlement Trap

What is it about settlement-trap cases that feels so problematic? Consider an illustration: Bernard, an elderly man, underwent hip replacement surgery more than fifteen years ago. He learned just recently that the artificial joint was defective and required a second debilitating surgery. Bernard joined a mass tort action, receiving a significant settlement award to redress his injuries. He was shocked, however, when the MDL claims administrator refused to turn over the award to him or his personal injury attorney. Instead, because Bernard had previously filed for bankruptcy, the claims administrator refused to distribute the funds until a bankruptcy trustee or the bankruptcy court certified that the funds were not property of the estate. Bernard was left with no choice but to hire a bankruptcy attorney to fight with the trustee about whether the claim accrued before the bankruptcy and if Bernard could claim an exemption for the settlement. For Bernard, the settlement trap led to substantially increased costs and additional time spent waiting for the settlement money he

---

136. Debtors' Attorney, *supra* note 16.

137. *Id.*

138. *Id.*

139. *See* BrownGreer PLC, *NFL Settlement Program Summary Report*, NFL CONCUSSION SETTLEMENT 8 (May 10, 2021), https://www.nflconcussionsettlement.com/Docs/5_10_21_report.pdf [https://perma.cc/SYC4-JPZB].

140. The claims administrator explained that cases are likely to be closer to 10% when the population of claimants is more likely to have filed for bankruptcy and identified the NFL case as one example where a claims administrator might hold 10% of cases for potential bankruptcy issues. Claims Administrator, *supra* note 13.

desperately needed. In the settlement trap, substantive, procedural, and structural factors in two colliding systems overlap to leave injured claimants unaware of the law, without control of the process, and paying the costs of pursuit. This Section outlines the core elements of the settlement trap.

1. Legal Complexity

At the most fundamental level, the settlement trap is possible because the underlying law on accrual, exemption, and judicial estoppel is incredibly complicated. Decisions that a claimant made in his bankruptcy decades ago may have binding effect on a newly discovered claim; similarly, characteristics of a claimant's settlement that come to light decades after a bankruptcy has closed can ultimately determine whether that settlement goes to the claimant. Hindsight may be 20/20, but claimants in these circumstances would have to be clairvoyant legal experts to escape the settlement trap. The attorneys who are involved usually do not know the full legal landscape to offer comprehensive advice, and the law may change over time to shift outcomes in unpredictable ways.

2. Loss of Control

By the time most claimants know about potential problems with their settlement payment, they have likely lost all control to guide the process. The claims administrator (according to settlement program terms) controls whether the claimant falls under, and whether he can escape, a bankruptcy hold. A trustee with even a colorable argument that a claim is estate property is the sole party in interest who may take action on the claim. In that capacity, a trustee may settle away exemptions or surplus, or accept terms a claimant would not want. The trustee may also dictate settlement terms that force the claimant to surrender property that would be hers.[141] The claimant is stuck with very little recourse.

3. Prohibitive Costs

Adding insult to injury, a claimant who is ensnared by complicated law and overtaken by loss of control is also required to pay the costs of administration and challenges over his claim. Claimants in the settlement trap may be desperate for settlement funds, but if their claim is flagged for bankruptcy hold by the claims administrator or captured by the trustee, then the only path to recovery involves spending money. The claimant may ask the trustee to abandon the payment, but if the trustee exercises its discretion to take control over the asset, then the claimant must pay for a bankruptcy lawyer, in addition to potentially being responsible for the trustee's and counsel's fees from litigating over the claim.[142] Claimants may incur

141. One debtors' attorney shared a story about a client who was initially told by a trustee that a potential NFL claim was not property of the estate, only to come back once a larger claim was awarded and demand $100,000 payment as a price for peace. Given the delay and cost of administration and the legal uncertainty, the debtor decided to take the deal even though the property was likely fully exempt. Debtors' Attorney, *supra* note 16.

142. Recall that trustee and counsel fees may be approved by the court as administrative

additional harm due to the resulting delays. Because the claims administration hold can take a long time to resolve, claimants may be pushed to take litigation finance loans or other financially unsound measures.

C. Who Sets the Trap?

> *No problem can be solved until it is reduced to some simple form. The changing of a vague difficulty into a specific, concrete form is a very essential element in thinking.* – J. P. Morgan[143]

In the settlement trap, a claimant with a settlement awarded may be forced to surrender control of key decisions, endure the cost and delay of seeking payment, and ultimately lose the payment after receiving insufficient advice on complex laws. This is possible because multiple stakeholders in both the mass tort and the bankruptcy systems have unclear or conflicted duties, too much discretion, and opportunistic incentives. While not all cases will involve every element described in this Section, collecting them will provide a useful foundation for evaluating the strategy for reform.

1. The Blame Game

When speaking with stakeholders to understand the settlement trap, my first impression was that everybody (1) agreed there was a problem and (2) had strong opinions about who was responsible. As one may have expected, there was little consensus about who the "bad actors" were and plenty of fault to go around. This Section provides a snapshot into the blame game that ensued.

Many stakeholders voiced frustration with defendants' and lead plaintiffs' counsel. One interviewee—who calls himself a "garden variety personal injury attorney" who occasionally does mass torts—was appalled by the fundamental disconnect between class attorneys and their clients. "In mass tort cases the rule of law that we teach isn't being followed. It's a free-for-all, where the defendant calls the shots and the plaintiffs' attorney lead counsel gets paid a ton, while people who need their money don't get it."[144] As another plaintiffs' attorney explained, "I think the defense side has figured out ways to increase the process so that things get slowed down, the whole idea of delaying the pay out, and then it gets checked [for bankruptcy issues], all to the detriment of the claimant who nobody really cares about."[145] A lawyer representing former NFL players complained that

> [e]verybody has gotten paid through this NFL case except the actual players who deserve to get paid. It's terrible. It was not meant to be a

---

claims, which would be paid in full out of funds that remain after a debtor exempts her property, but before unsecured creditors receive any distribution (or the debtor a surplus).

143. KAREN LAWSON, THE TRAINER'S HANDBOOK OF LEADERSHIP DEVELOPMENT: TOOLS, TECHNIQUES, AND ACTIVITIES (John Wiley & Sons, Aug. 2, 2011).

144. Plaintiffs' Attorney 3, *supra* note 129.

145. Plaintiffs' Attorney 2, *supra* note 15.

> case run that way, but that's how they are doing these mass torts, the same gang of lawyers doing it the same way, hiring the same companies to be administrators and lien administrators, etc. It's really pathetic.[146]

Other participants look to the cost of overseeing the settlement program. "In the NFL case, the administrator makes as much money as it wants to make. The way that one is set up, it behooves the lawyers and everybody involved to do as much work as possible, all out of the claimant's pocket."[147]

Plaintiffs' attorneys faced scrutiny for their unwillingness to yield to valid bankruptcy issues. One trustee bemoaned that:

> [i]t can be difficult getting information out of [plaintiffs'] attorneys, even though you hire them as "special counsel" in the bankruptcy case. They rarely have a lot of knowledge about bankruptcy, at heart. . . . They don't want to send the money to the trustee. They try to set off attorney's fees, but instead the money has to come through the estate.[148]

A claims administrator expressed similar frustration: "Lawyers representing plaintiffs, class counsel, and also defendants don't know much bankruptcy, and they don't want to talk about it, it's a 'fly in the ointment' or a 'wrench in the system' that they don't really want to deal with."[149]

Other parties—including plaintiffs' attorneys, debtors' attorneys, and judges—say that trustees are responsible. "The only ones who made any money are the trustee and the attorney for the trustee. They made all sorts of money on the bankruptcy and hold up distribution of the award to my clients."[150] A nationally recognized Chapter 7 trustee summarized the problem:

> In slow times like these, trustees may get a little more aggressive because they are losing money in their practices and are incentivized to do maybe the wrong thing. . . . I've seen trustees who are reopening cases for the "smaller" settlements, and then they have the fights on their hand. By the time they finish litigating it, what's left? Every trustee has to exercise his or her own business judgment . . . but that culture varies by region. In more rural areas, with very few bankruptcies, a $3000 judgment would be considered a big case.[151]

From a global perspective, each of these criticisms may be valid. The net sum of failures is what creates the settlement trap, not any one party's actions.

---

146. Plaintiffs' Attorney 4, *supra* note 14.
147. Plaintiffs' Attorney 2, *supra* note 15.
148. Telephone Interview with Trustee 2 (Sept. 25, 2019).
149. Claims Administrator, *supra* note 13.
150. Plaintiffs' Attorney 1, *supra* note 6.
151. Trustee 1, *supra* note 17.

2. Duties

A claimant in the settlement trap is often completely unaware that his claim is not recoverable, either because it is tied up in a claims administrator bankruptcy hold or held hostage in a battle with the trustee. In part, claimants' ignorance results from problems with the professional and fiduciary duties they are owed. In a given case, the plaintiffs' attorney, debtors' attorney, trustee, and even aggregate litigation counsel will all owe duties of some sort to a claimant. But despite this seemingly comprehensive list of stakeholders acting on behalf of the claimant, critical information about settlement payments gets lost.

First, in this context some stakeholders have conflicting duties. The trustee, for example, owes a fiduciary duty to collect and distribute funds on behalf of available creditors.[152] However, the trustee also owes a fiduciary duty to the debtor, to the extent an asset would be exempt or result in a surplus.[153] A certain conflict arises when the trustee is tasked with making decisions that would benefit one party and harm another (for example, settling a lawsuit for less money than possible in the interest of time, but thereby eliminating the debtor's ability to get a surplus).[154] Aggregate litigation counsel, too, may be conflicted.[155] Whether in a class action, multidistrict litigation, or simply when acting on behalf of many claimants, counsel negotiating an aggregate settlement owes duties to multiple parties. Due to the differences in clients' claims, counsel will likely make decisions about the settlement that will be in the best interests of one client but not another.[156] This conflict may be satisfied for professional responsibility purposes by waivers or consent.[157] However, none of those safeguards will help claimants with potential bankruptcy issues. For

---

152. This suggests that a trustee would be in violation of his fiduciary duty if he took action (and incurred costs) without returning a meaningful recovery to creditors. *See infra* note 185.

153. U.S. DEP'T OF JUST., EXEC. OFF. FOR U.S. TRS., HANDBOOK FOR CHAPTER 7 TRUSTEES 4-2 (2012), https://www.justice.gov/ust/file/handbook_for_chapter_7_trustees.pdf/download [https://perma.cc/NGD7-3VP5] ("The trustee is a fiduciary charged with protecting the interests of all estate beneficiaries – namely, all classes of creditors, including those holding secured, administrative, priority, and non-priority unsecured claims, as well as the debtor's interest in exemptions and in any possible surplus property."); *see also In re* Leavell, 141 B.R. 393, 399 (Bankr. S.D. Ill. 1992) (noting the Chapter 7 trustee owes a fiduciary duty to the debtor if it "has an interest, *e.g.*, a right of exemption in estate property, that may be harmed by the trustee's failure to preserve assets").

154. *See* Steven Rhodes, *The Fiduciary and Institutional Obligations of a Chapter 7 Bankruptcy Trustee*, 80 AM. BANKR. L.J. 147, 148–49 (2006) (outlining conflicts in the trustee's exercise of its fiduciary duties). *See generally* Pottow, *supra* note 51 (discussing the inherent conflicts in trustee representation).

155. *See* Lynn A. Baker, *Aggregate Settlements and Attorney Liability: The Evolving Landscape*, 44 HOFSTRA L. REV. 291, 295–98 (2015) (describing the different roles that settling attorneys may play depending upon the form of aggregate litigation).

156. Consider the difference between claimants with a strong claim that would rather proceed to litigation versus clients with potential proof issues that are incentivized to settle early and for lower amounts. *See id.* at 296–97.

157. *See id.* at 295; *see also* Martin H. Redish & Julie M. Karaba, *One Size Doesn't Fit All: Multidistrict Litigation, Due Process, and the Dangers of Procedural Collectivism*, 95 B.U. L. REV. 109, 140–41 (2015) (describing the ethical obligations of attorney representation and how those obligations are strained in the MDL context).

example, the client who should try and settle a claim to qualify for exemptions may not receive sufficient advocacy from an aggregate litigation attorney who knows that the settlement value for all claimants could increase by going along with the defendants' requests that would disqualify the payment from exempt status

Next, other stakeholders owe duties to the claimant, but the scope of those duties leaves a gap in critical advice. Plaintiffs' attorneys are not experts in bankruptcy law and would likely be acting in violation of their professional obligations by making misinformed bankruptcy recommendations.[158] More commonly, plaintiffs' attorneys who identify potential bankruptcy issues refer claimants to contact an experienced consumer bankruptcy attorney. Yet another group of plaintiffs' attorneys have no idea that a long-dormant bankruptcy could be reopened for settlement payments and are just as surprised as their clients to be denied payment.[159] For their part, debtors' attorneys are not well-versed in mass tort settlement protocols, and may not know the most effective way to coordinate with claims administrators or even still represent the debtor when any mass tort claim accrues. Especially in dormant bankruptcies, no single attorney has the right combination of expertise and access to the client to navigate or avoid the settlement trap. For claimants without debtors' or plaintiffs' counsel, the information disadvantage only magnifies.

3. Discretion

The settlement trap is further enabled by certain stakeholders' discretionary authority. First, the parties who draft mass tort settlement programs have discretion to set specific terms by which claimants are paid. This includes when potential bankruptcy issues are subject to the claims administrators' bankruptcy hold, and when the claimant has provided sufficient proof to escape that hold.[160] Claims administrators are bound by the terms of the settlement program in each case, even if a claimant in one case would be paid without question while that same claim would be delayed in a different case. In close cases, or if the claimants' attorney comes back with clarifying information, the claims administrator will look to the defendant to allow an exception.

The stakeholder with the most significant discretion is the trustee. As described above, in most instances a mass tort claimant will receive his settlement payment unless the trustee takes action to recover it. For example, if a bankruptcy is closed, the trustee will reopen a case to pursue the settlement. Trustees are bound to act on behalf of the estate but have discretion to identify when the estate would benefit from pursuing a settlement. Tucked within this discretion are the trustee's decisions about whether the settlement payment is property of the estate and/or exempt. Because the

158. *See supra* text accompanying note 128 (recounting an instance when attorney error led to disqualification from a significant award).

159. As one plaintiffs' attorney explained, "I have no separate duty and obligation to go back in time when someone settles a case. When I settle asbestos mesothelioma cases, I don't think I have any ethical obligation to disclose that to previous creditors." Plaintiffs' Attorney 4, *supra* note 14.

160. Most often, the defendant's counsel, in partnership with representatives from the plaintiffs' group, draft the terms of a settlement program. *See* Claims Administrator, *supra* note 13.

law surrounding each characteristic of settlement payments may be largely unsettled, the trustee has significant power over the debtor's ability to successfully claim an exemption. Trustees exercise discretion in reopening closed bankruptcy cases to pursue settlement payments; in taking over and settling pending cases; and in challenging a debtor's claim that property is exempt. The trustee's interests in settling a claim do not always align with the debtor's. As outlined in Section I.B above, whether a particular settlement qualifies for exemption may turn on nuanced elements of the settlement (such as whether the settlement is for pain and suffering versus bodily harm, or lost wages as opposed to damage to property).[161] In deciding how and when to settle cases, a trustee has the ability to seek terms that pull the resulting award away from the debtor's exemption.

It bears mentioning that this Article does *not* assert that the nation's trustees are, en masse, abusing discretion to the detriment of debtors. There is currently no data to support any empirical claim about the overall pattern of trustee behavior on this issue.[162] Anecdotally, I spoke with trustees who use the very same discretion explained above to abandon claims or not object to exemptions, thereby permitting settlement payments to flow to the debtor. Debtors' attorneys also recognize the possibility that some trustees take a limited approach to interfering with settlements.[163] At times, trustees exercise this discretion in favor of the claimant in direct contradiction to guidance from the trustee's oversight authority.[164] While the data-driven story of trustee behavior remains untold, this Article focuses on the rules that would permit a trustee to thwart the public policy of exemption and identifies structural safeguards to remove that possibility.[165] The next Section explores the incentive structure that may motivate trustees and other stakeholders to exercise discretion to the detriment of claimants.

---

161. *See supra* Section I.B.

162. The issue of whether and how trustees decide to abandon or pursue litigation and settlement payments in bankruptcy is both fascinating, and worthy of empirical assessment beyond the scope of this Article. My experience with this project suggests that the norms are highly regionalized and vary based on a mix of factors including state exemption and accrual law, the perspective of the local bench, and the overall volume and value of consumer cases in the district.

163. "In defense of the trustees, I will say there are trustees in the area who think the trustees who are going after my guys are crazy. There is definitely a split in trustees." Debtors' Attorney, *supra* note 16. This split may also explain why represented debtors are more likely to try and manipulate the random assignment system for a preferred trustee. *See* Edward R. Morrison, Belisa Pang & Jonathon Zytnick, *Manipulating Random Assignment: Evidence from Consumer Bankruptcies in the Nation's Largest Cities* 5, (Colum. Univ. Dep't Econ. Working Paper No. 614, 2019), https://scholarship.law.columbia.edu/cgi/viewcontent.cgi?article=3539&context=faculty_scholarship [https://perma.cc/8QCT-CQPZ].

164. Multiple trustees disclosed a stated policy preference from the U.S. Trustee's office about how to handle personal injury settlement payments in closed cases. Trustees also explained their willingness to go against the policy preferences when exercising their discretion.

165. Any effort for reform should prevent the more troubling abuses of discretion and balance the information disparity among claimant and trustee (or claims administrator) while maintaining core objectives of the bankruptcy and mass tort systems.

4. Incentives

Why do stakeholders exercise their discretion related to settlements in a way that often harms claimants? At its core, much of the problematic behavior is incentivized by money. Both bankruptcy and mass tort practices indulge attorneys' and other administrators' quests for fees or cost savings. Scholars have outlined in great detail how each system benefits the connected, repeat players.[166] In this context, claimants must endure both sets of incentive challenges.

i. Financial Incentives of Settlement Administration

A settlement program's terms and the manner in which it is administered are both heavily impacted by costs and fees. The terms of a settlement program, including how it addresses claims with potential bankruptcy issues, will vary based upon the fee structure. The cost of claims administration can be staggering, and different features in the fee agreement can make it more or less likely that a claimant will receive payment.

First, a bit of background on settlement programs cost structures and claims administrator fees. Usually, settlement program administrative costs are paid either directly from the settlement funds, or separately by the defendant in addition to any settlement amount. In the former scenario, the defendant has no incentive to streamline program costs because their contribution remains the same. The defendant's primary incentive, then, is to ensure as many releases as possible and reduce the claims pool via other means. In the latter circumstance, where every administration dollar is an additional cost to the defendant, the incentive structure shifts, and it is plaintiffs who are uninterested in the cost while defendants are conflicted between a desire to reduce costs and a desire to effectively reduce their current and future liability.

The claims administrator payment structure further complicates this incentive issue. Claims administrators are paid through a number of fee arrangements, each of which may incentivize different approaches to administering special handling cases (such as claims with potential bankruptcy issues).[167] One model involves paying claims administrators at an hourly rate, while another method (the unit-price model) offers a flat rate for every claim they administer. Competition is fierce in the claims administrator industry, and debtors and lead plaintiffs' counsel use that reality to push claims administrators toward more advantageous terms.

Both compensation methods may impact how claims administrators deal with bankruptcy holds. In a case with hourly compensation, the claims administrator might be motivated to conduct more investigations into claimants with bankruptcy issues, thereby increasing the fees.[168] In the unit-price model, the terms of the price

---

166. *See* BURCH, *supra* note 122 (explaining the insular relationships and fee-seeking decision-making in MDL negotiations); Pottow, *supra* note 51, at 16.

167. The information in this Section comes exclusively from my interviews with well-established claims administrators but is by no means exhaustive or universal. *See* Claims Administrator, *supra* note 13. The details of settlement fund administration and the incentives at play merit careful attention and future focus from academics.

168. The fear of losing future business may mitigate excessive hourly billing in this

could incentivize the way claims administrators treat borderline claims involving potential bankruptcy issues. For example, one claims administrator explained that sometimes, the per-claimant fee will be a flat sum (say, $500),[169] while in other cases there may be a tiered fee (perhaps $500 for regular claims and $650 for special handling claims that involve bankruptcy).[170] Under the flat-sum structure, a claims administrator is incentivized to finalize and approve claims as quickly as possible. In close cases (perhaps instances where the claimants' proof could arguably fall on either side of the program line, or where the initial payment seems potentially impacted), the claims administrator is incentivized to finalize the payment. With tiered fees, the claims administrator may be incentivized to categorize more claims within the bankruptcy hold to earn the additional fee.

When combined, the program funding source and claims administrator fee structures impose different incentives on claimants in different cases that may result in inconsistent and self-interested treatment of claims with potential bankruptcy issues.

ii. Costs of Bankruptcy

The bankruptcy process also has incentive issues arising out of fees. As explained above, the trustee's fees are paid out of the debtor's estate. This creates a "financial incentive to identify and recover non-exempt property."[171] Trustees receive a small flat fee for no-asset cases, which make up the vast majority of many districts' dockets.[172] As one debtors' attorney explained:

> The trustees, all they see are dollar signs. The whole bankruptcy system is set up so being a trustee isn't worth your while unless you can get some big asset cases. So, the trustees do this work, in hopes of being able to get a big asset case. If you see a million dollar case, and you're going to get a cut of that, it makes it worth your while to make up for all the $60 cases you've had.[173]

---

context, but given the secrecy surrounding the costs of settlement programs, there is no way to know whether the bills receive sufficient scrutiny to identify opportunistic billing.

169. While single-fee terms may seem more cost effective, the claims administrators pointed out that contracts often have a carve out for "complicating factors" that results in hidden and significant fee increases. Claims Administrator, *supra* note 13.

170. *Id.* (reporting the possibility of a 10–25% additional unit fee for special handling cases).

171. Morrison et al., *supra* note 163, at 5 ("[The trustee] is paid a $60 administrative fee for every case and, in addition, 25 percent of the first $5,000 of non-exempt property liquidated for the benefit of creditors, 10 percent of the next $25,000, 5 percent of the next $950,000, and 3 percent of any amount over $1 million. These bounties, however, are collected in a tiny percentage of cases: Cases with nonexempt assets account for only about 4 percent of all cases."). Recent scholarship highlights that represented debtors are statistically more likely to engage in "trustee shopping," likely to avoid particularly harmful exercises of discretion. *Id.* at 16.

172. *Id.*

173. Debtors' Attorney, *supra* note 16.

Trustees only receive fees on the non-exempt portion of estate assets. Thus, trustees are incentivized to nudge assets like settlement payments—which are under the trustee's control—outside the boundaries of available exemptions. This may be a valid exercise of the trustee's role, but in instances where the facts are not clear cut, it also opens up the potential for abuse. This is especially true when a trustee challenges the status of an asset that is likely exempt solely to gain leverage to extract a settlement from the debtor.[174] Multiple bankruptcy attorneys and trustees identified this issue, while also acknowledging that exemption gamesmanship is two-sided. "It can work both ways, you can have the debtor's attorneys trying to angle [for exemptions] or the trustee."[175]

The fee structure for debtors' attorneys also plays a role in this conflict. Many debtors' attorneys earn a flat fee for their representation that is not impacted by the amount of work required for a particular case.[176] They represent clients on a volume basis and have limited capacity to engage in relentless briefing and appeals on a single debtor's case. "On a flat fee basis, debtor's attorneys can't afford to fight everything, and everybody knows that."[177] Trustees take advantage of these fee limitations to push debtors and their attorneys to accept settlements on issues that would likely go to the debtor if litigated.[178]

The settlement trap is also fueled by decisions made to avoid losing money. The claims administrator, for example, insists on significant documentation to release claims potentially impacted by bankruptcy to avoid liability under its engagement with mass tort defendants.[179] Mass tort defendants, in turn, are incentivized by concerns about future litigation when they push for draconian proof mechanisms to release settlements from a bankruptcy hold. In class action cases, the proof required to release a bankruptcy hold claim may be less arduous because the settlement provides a binding release on all present or absent claimants. But in MDLs or other aggregate cases, the defendant's only repose comes from releases on an individual basis. If the settlement is an asset of the estate, then only the trustee has authority to sign the release.[180] In such cases, defendants have strong incentives to seek more certainty about which party has the authority to release claims against the defendant.

---

174. One debtors' attorney provided several examples of such behavior with a particular trustee. *Id.*

175. Trustee 1, *supra* note 17.

176. Debtors' Attorney, *supra* note 16.

177. *Id.*

178. *See, e.g.*, *In re* Boyher, 467 B.R. 672, 673 (B.A.P. 8th Cir. 2012) (describing an example where the case was reopened, the debtor scheduled a class action settlement payment, and the debtor and trustee agreed to split the proceeds fifty-fifty with the debtor waving his right to claim exemptions).

179. Claims Administrator, *supra* note 13.

180. Settlement program release forms often pose challenging issues when trustees have standing to administer the claim. Release forms commonly require secrecy, something that is completely antithetical to the open disclosure norms and requirements of the bankruptcy system. Additionally, many settlement forms have broad release and indemnification terms that the trustee is either unable or unwilling to sign. Some defendants understand the difference between what reasonable release terms may be for a claimant versus for a trustee, but others refuse to budge and place the trustee in the difficult position of deciding whether to accept the money and accept the potential personal liability that could come from signing the release. Trustee 1, *supra* note 17; Trustee 2, *supra* note 148.

This, in turn, makes it harder for claimants to escape the claims administrator's bankruptcy hold. Finally, defendants have an incentive to investigate claimants' prior bankruptcies to wage as many judicial estoppel defenses as possible. If successful, the defendant can pay one fewer claimant.

III. THE RELEASE

Not one individual interviewed for this Article was satisfied with the existing system for evaluating and resolving settlement payments to current or prior debtors. If, as outlined above, a tangled web of laws, practices, and procedures creates a settlement trap for claimants, and stakeholders uniformly see a need for reform, the obvious next step is to identify and pursue meaningful changes. Any adjustments must be in harmony with the underlying goals of the various statutory schemes. Bankruptcy, for example, balances competing interests of maximizing estate value, distributing assets equitably among creditors, and providing the debtor with a fresh start. And the mass tort system seeks to aggregate and resolve a large number of claims against a defendant (or defendants) and facilitate an orderly process for distributing recoveries. This Part outlines a number of measures that could address the more troubling parts of the settlement trap identified above. Some are directed at the mass tort system, while others fall within the bankruptcy process (where they will improve bankruptcy's treatment of litigation as an asset beyond mass tort claims). Together, the changes offer a blueprint for releasing the settlement trap.

A. Demystifying the Doctrine

Attorneys in all roles noted the doctrinal complexity surrounding the treatment of settlement payments in bankruptcy. While the bankruptcy bench and bar (including trustees, debtors' attorneys, and judges) were more likely to have knowledge of the issues, even those who routinely deal with the issue in bankruptcy found the doctrine confusing to explain or apply on a national level. The law on key issues—accrual, exemptions, and estoppel—is hyper-specific to the debtor's jurisdiction and is constantly shifting as more cases are tried. Non-bankruptcy stakeholders (including plaintiffs' and class attorneys and settlement administrators) described their knowledge of relevant bankruptcy law along a spectrum from a vague awareness to a cautious understanding.[181] This first set of modifications aims to make navigating the legal landscape easier for claimants and other stakeholders in the process.

1. Judicial interpretation

The first set of demystification efforts could be accomplished incrementally through advocacy. By continuing to challenge treatment of mass tort payments in bankruptcy courts, claimants will nudge judges to clarify open doctrinal questions.

---

181. *See, e.g.*, Plaintiffs' Attorney 1, *supra* note 6 ("I know some basic bankruptcy law."); Claims Administrator, *supra* note 13 ("Most of the time the lawyers dealing with this are not bankruptcy lawyers who don't know what should be done and don't want to do anything. We are usually met with resistance, consternation and complaining. Nobody knows and understands it.").

In the last five years, litigation on settlement issues has produced a flurry of opinions that address missing elements.[182] In the NFL CTE cases, for example, courts have conceptualized the settlement payments as disability payments, which are eligible for different and more generous exemptions.[183] This shift has adjusted the way that trustees respond to NFL settlements, including making it more likely that they abandon the settlement without challenge.[184] Relying on the courts to recalibrate existing practices, however, will take time, may lead to more inconsistency throughout the country, and will impose significant costs on claimants.[185]

2. Legislative Changes

An alternative solution involves changing the Bankruptcy Code (and/or state laws)[186] to simplify the analysis surrounding settlement payments. This legislative fix could take many forms, but two obvious improvements relate to timing of accrual and creating a uniform personal injury exemption.

First, Congress should create a uniform framework for deciding whether a litigation claim or settlement payment is an asset of the estate. State laws on claim accrual are not designed with bankruptcy in mind. Whether or when a cause of action should be time-barred (the primary purpose of accrual laws) is a profoundly different query than whether a recovery should belong to the bankruptcy estate, and blind reliance on state provisions leads to absurd results.[187] A discovery rule that turns on actual or potential knowledge of the injury comes closest to aligning with the aims

---

182. The number of bankruptcy opinions arising out of the most recent wave of mass tort cases is particularly striking when compared to the relative silence after previous cases. For example, there are very few, if any, cases discussing exemption and reopening of bankruptcy cases for Agent Orange, asbestos, or Dalkon Shield cases, even though such cases should have produced many similar claimants.

183. *In re* Williams, 586 B.R. 355 (Bankr. S.D. Fla. 2018) (overruling Chapter 7 trustee's objection to claim of exemption in National Football League player's concussion injury litigation settlement), *aff'd*, No. 18-cv-61581 (S.D. Fla. 2019).

184. This decision is economically rational due to the priority scheme of the Code. When distributing assets, the value of exempt property is removed from the estate and given in full to the debtor before any administrative costs (including the trustee's and its attorneys' fees) are paid or distributions made to creditors. If the entire settlement amount is exempt, the trustee's efforts to recover it will benefit neither creditors nor the trustee itself.

185. In addition to the obvious challenges regarding accrual, exemptions, and estoppel, claimants could pursue breach of fiduciary duty claims against the trustee who administers a settlement payment without benefit to creditors or who takes settlement actions that diminish the debtor's interest in an exemption. Such claims are certainly viable, though challenging to assert given existing precedent on trustee immunity. *See* Pottow, *supra* note 51, at 27 (outlining the current immunity doctrine relating to trustee actions); Elizabeth H. McCullough, *Bankruptcy Trustee Liability: Is There a Method in the Madness?*, 15 LEWIS & CLARK L. REV 153, 175 (2011) (exploring the trustee's fiduciary duties and the potential causes of action against the trustee).

186. Although the focus of this Section is on federal legislative reform, state legislatures could significantly improve the problem by clarifying their exemption and/or accrual provisions or incorporating federal law. *See* Sullivan, *supra* note 19 at 345 (suggesting states adopt bankruptcy-specific provisions).

187. *See supra* Section I.C.1 (describing treatment of any pre-petition placement of a device as an asset of the estate).

of the bankruptcy process. If the debtor knew or should have known about his claim or injury prior to the petition date (or during the plan in Chapter 13 cases), then the claim and any resulting settlement payment should be property of the estate.

Under this standard, the estate of a football player who knew about his concussions and degenerative disease before filing for bankruptcy would include any settlement in the NFL MDL case; it would not, however, include a settlement paid to a woman who had a hip implant prior to filing for bankruptcy but who had no injury until years after her bankruptcy closed. To the extent Congress does not have the appetite to address timing challenges for all litigation claims (including business disputes), it could narrowly tailor the revision to personal injury claims. Congress could additionally impose a maximum time period for reopening closed cases due to mass tort claims, subject to an exception for debtors who intentionally hide or delay their settlement. Permitting the trustee to grab settlement payments within five or ten years of the bankruptcy accomplishes the goal of distributing assets to creditors, while also eliminating the perpetual grasp of a bankruptcy filing.

Second, Congress could set a generous uniform exemption relating to personal injury claims and permit opt-out state exemptions for personal injury claims to apply only if they offer the same or greater exemption amounts. As identified in Section I.C.2, states have set many different levels of exemptions for personal injury claims. Imposing a uniform standard permits Congress to set a floor for how claimants are eligible to receive payments and adds clarity to an otherwise complicated legal issue. I recommend setting the personal injury claim exemption amount to mirror the current federal standards for some types of payments by imposing a "reasonably necessary for the support of the debtor and any dependent of the debtor" standard.[188] This removes the need to distinguish and allocate settlement proceeds among categories of relief (lost wages, pain and suffering, etc.). Such a standard also prevents debtors from receiving a windfall from a large settlement payment that is not necessary to the debtor's "fresh start." Under this proposed regime, states would be permitted to offer complete exemption of personal injury claim amounts, but not reduce the amount below the reasonably necessary threshold. With more predictable and blanket standards, the trustee is no longer incentivized to settle claims around exemptions and all parties can streamline their exemption analysis.

The suggestion that Congress take control of these issues highlights longstanding tension between state and federal interests in resolving property disputes in bankruptcy. Current laws (relying on state accrual standards and permitting states to opt out of the federal exemption scheme) show Congress's desire to incorporate and honor state principles. But this reality is more the result of effective lobbying and federalism concerns than constitutional necessity.[189] Congress has the right to create and enforce a uniform system of bankruptcy laws,[190] and would be well within its

---

188. 11 U.S.C. § 522(d)(11)(B), (C), (E).

189. *See* Ponoroff, *supra* note 19, at 357 (describing the history of the federal exemption scheme, including the "firestorm of opposition" to an initial recommendation for uniform federal exemptions); COMM'N ON THE BANKR. LAWS OF THE U.S., REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. 93-137 (1st Sess. 1973).

190. U.S. CONST. art. I, § 8, cl. 4; *see also* Ponoroff, *supra* note 19, at 355–56; Stephen J. Lubben, *A New Understanding of the Bankruptcy Clause*, 64 CASE. W. RSRV. L. REV. 319 (2013) (describing the relationship between bankruptcy and state courts).

bounds to narrow the influence of state law on administration of the bankruptcy estate.[191] While much of the bankruptcy process rests on "applicable non-bankruptcy law,"[192] the Code clearly overrides such law when deemed necessary,[193] including in the exemption context.[194]

3. Other Solutions

Aside from changes to the legal landscape, increasing knowledge of current legal standards relating to settlement payments would add clarity for all stakeholders. The doctrinal framework in this context is ripe for development of assistive technology. A developer could create an algorithm that could identify and categorize how the law applies to a specific claimant's settlement with a few data inputs (including information about the claim and terms of the settlement; bankruptcy dates; which state's law applies; and what applicable law holds about accrual, exemptions, and estoppel, etc.). Once built, and assuming accuracy, each stakeholder could readily identify the likely legal treatment of a claim and take action accordingly. If, for example, a settlement administrator had access to a bankruptcy treatment estimator tool, they could release settlements that clearly are not property of the estate without the cost and delay of getting trustee approval. Similarly, plaintiffs' attorneys could advise clients easily about the bankruptcy impact of settling cases, and trustees could more quickly decide whether a claim should be abandoned.

Separately, the Executive Office for U.S. Trustees (EOUST) could issue formal guidance to standardize the process among trustees.[195] Currently, Chapter 7 and 13 trustees take region-specific approaches to administering settlement payments. While trustee discretion is important, there should be some standard considerations and baseline thresholds that limit the discretion. By publishing guidance outlining factors such as the amount paid to creditors, time since the bankruptcy closed, and the likelihood of returning meaningful assets to creditors, the U.S. Trustee could set the standards by which trustees should operate and give other parties a better understanding of how a settlement will fare under bankruptcy law. Such guidance would serve the additional benefit of laying the foundation for removal of Chapter 7 trustees and trustee counsel for noncompliance.[196]

B. Structural Safeguards

Some elements of the settlement trap can only be addressed by structural shifts. Stakeholders' potential incentive conflicts are powerful because the mass tort and

---

191. Ponoroff, *supra* note 19, at 356; *see also* Stellwagen v. Clum, 245 U.S. 605, 613 (1918) (noting the *choice* of Congress to honor state law in the exemption context).

192. *See* Butner v. United States, 440 U.S. 48, 55 (1979).

193. *See, e.g.*, 11 U.S.C. § 545 (voiding certain statutory liens in conflict with state law).

194. *See* 11 U.S.C. § 522(f)(3).

195. The EOUST issues guidance on various issues involving administration of bankruptcy cases. *See Significant Guidance Documents*, U.S. DEP'T OF JUST. (May 18, 2015), https://www.justice.gov/ust/significant-guidance-documents [https://perma.cc/L8GP-KA3D].

196. *See* John A. E. Pottow, *Bankruptcy Fiduciary Duties in the World of Claims Trading*, 13 BROOK. J. CORP. FIN. & COM. L. 87, 90 n.21 (2018) (discussing removal of Chapter 7 trustees).

bankruptcy systems do not impose sufficient limitations on their exercise of discretion. Creating enhanced structural safeguards would add oversight to controlling stakeholders such as the trustee and claims administrator and could effectively curb some of the more problematic behavior that impacts claimants.

The first group of safeguards would limit the trustee's discretion to pursue and administer assets without meaningful upside to the estate. Many complaints about the settlement trap center upon the trustee's decision to pursue a claim or settlement when the nonexempt amounts would not provide a significant payment to creditors (or there were few identifiable creditors even seeking repayment). Courts could address this problem by imposing careful limitations when granting a trustee's motion to reopen a bankruptcy for the purpose of administering settlement proceeds. A bankruptcy court could draft the order to apply on a temporary basis and make administration of the asset conditional on creditors filing claims. Although this practice is not common on the bench, the text of the Code gives bankruptcy judges clear discretion to refuse to reopen cases.[197] If judges have full discretion to grant or deny relief, surely they also have discretion to impose limitations on the relief when granted.[198]

A second group of safeguards would address the trustee's ability to settle litigation to the detriment of the debtor's interest in exemptions or surplus.[199] Although the trustee has a fiduciary duty to act on behalf of the debtor when those interests are present, the reality is that the conflicting duties imposed on the trustee will likely marginalize protections to the debtor and favor creditors (or the trustee himself). With this tension in mind, I suggest three potential solutions. First, the bankruptcy court or U.S. Trustee could require inclusion of a statement summarizing potential exemption implications as part of a 9019 motion to approve settlements.[200] At minimum, this addition would improve notice to the debtor about what the impact of a settlement may be and give them a meaningful opportunity to challenge the settlement terms. Second, the court could require debtor approval of settlement offers in cases where there is potential for an exemption or surplus.[201] Canadian insolvency law, which has a similar exemption scheme, gives the debtor and trustee joint standing to pursue claims that could result in distributions to both the debtor and

---

197. *See* 11 U.S.C. § 350(b); *see also In re* Ross, 548 B.R. 632, 636 (Bankr. E.D.N.Y. 2016) (noting the court's discretion).

198. *See, e.g.*, City of Lakewood v. Plain Dealer Publ'g Co., 486 U.S. 750, 763 (1988) (observing that the government's ability to prohibit speech entirely would include its lesser power to use grant discretionary speech licenses).

199. This could happen, for example, if the trustee finalizes a settlement agreement that classifies a settlement as a category that is not eligible for exemption.

200. Unfortunately, the circuits are divided as to whether a trustee is required to seek court approval to settle litigation. *See* Linhadley Eljach, Comment, *No Seal No Deal: Amending Federal Rule of Bankruptcy Procedure 9019 to Require Judicial Approval of Settlement Agreements*, 32 EMORY BANKR. DEVS. J. 433 (2016) (outlining the split of authority on Rule 9019 and proposing reform). Whether or not the costs of requiring court approval of all settlements is justified, the case for requiring notice and approval in the personal injury context—where trustees are incentivized to settle litigation outside the grasp of the debtor's exemptions—seems very strong.

201. This idea, at least in the context of cases where a large settlement would exceed the debtor's obligations, mirrors that of an equity committee appointed in business bankruptcy cases. *See* 11 U.S.C. § 1102.

estate.[202] Finally, the court could require an independent counsel or ombudsman to review settlement of claims where the debtor has a potential exemption or surplus interest. This additional check could be from the U.S. Trustee[203] or special counsel appointed for this purpose.[204] Whatever adjustment is made, the court must consider the increased costs to ensure that it does not simply impose one more administrative drain on the claimant's settlement.

C. Preventing Disregard for Time and Money

A final category of potential reforms would specifically target the staggering cost—both in time and in money—for claimants to overcome the settlement trap. First, there should be a streamlined procedure for claimants to get their payment released from claims administrators. This could be accomplished in a number of ways, including by creating a negative notice structure for releasing payments under a certain dollar threshold. For example, a mass tort judge could establish and approve procedures that permit settlement administrators to distribute settlement amounts under a $20,000 threshold to claimants if the U.S. Trustee does not respond to notice within thirty days by either requesting more time or asserting an interest in the property. Different thresholds could provide similar relief, and the specific components of this reform should be decided with the guidance of empirical data surrounding (1) the average size of settlement awards that fall within the settlement trap; and (2) the average turnaround time for similar actions in U.S. Trustee offices around the nation. This reform would give the settlement administrators a more certain and time-limited mechanism to establish entitlement to settlement payments in the bankruptcy context. Because the dollar cap is designed to be relatively small, the impact to potential creditors is modest and there is little risk of upending fundamental principles of the bankruptcy system.

Second, the bankruptcy court could impose limitations on the trustee's litigation efforts for settlement payments.[205] Fee limitations would counteract the trustee's structural incentive to overadminister estate assets for the purpose of generating fees. Because the court must approve trustee and special counsel fees as an administrative

---

202. Robert A. Klotz, *Bankrupt Tort Victims Impact of the Fourth Dimension: Time*, 45 ADVOCS.' Q. 212 (2016) (discussing Canadian insolvency law, which imposes a shared right between trustee and debtor to pursue potentially exempt litigation).

203. The U.S. Trustee is already in place and has authority to review the trustee's settlement decisions. Perhaps the U.S. Trustee could serve this independent check function, though I suggest that additional guidance from EOUST would be necessary to deviate from existing practices that defer to trustees. The role of the U.S. Trustee is important in the bankruptcy system, but it faces a number of criticisms from the bankruptcy bar and may be too conflicted to serve in this role. *See* Simon, *supra* note 45, at 1311–14 (describing the U.S. Trustee's challenges and impact in the bankruptcy system).

204. *In re* Key, 255 B.R. 217, 221 (Bankr. D. Neb. 2000) ("The cause of action for employment discrimination should be prosecuted for the mutual benefit of the debtor and the bankruptcy estate in a cooperative effort. The trustee should consider retention of debtor's existing special counsel to represent the estate and the debtor in prosecution of the claim.").

205. This suggestion is complementary to the proposed structural safeguards surrounding motions to reopen in the previous subsection.

expense,[206] the court could impose some threshold for fees that mirrors some class action payout structures that award fees based upon actual distributions to claimants.[207] One option would be to only approve litigation fees as administrative claims up to a certain percentage of total money returned to creditors. Imagine that a 25% recovery threshold were imposed.[208] If the claimant received a $10,000 settlement, $5000 of which was exempt, then the trustee's counsel fee would be capped at 25% of the amount that was distributed to creditors. If you assume that creditors filed just $4000 in claims, then the trustee would be limited to a $1000 administrative claim. If only $2000 of claims were filed, the trustee would make $500. This structure incentivizes trustees to pursue settlement payments proportionate to the amount of funds available to creditors and the number of creditors who would claim an interest in the property.[209] Any remaining amount would be returned to the claimant.

CONCLUSION

Mass tort victims commonly face financial struggles as a result of the harm they suffered. The settlement trap imposed by bankruptcy increases that struggle and threatens the availability of a true fresh start. As the nation deals with an influx of mass tort cases over the coming years—including those involving vaping, opioids, talc, and pesticides, in addition to traumatic brain injuries and pelvic mesh—the number of settlements that fall into the settlement trap is likely to increase. The current structure, procedures, and incentives all combine to harm claimants, a crushing irony given their preexisting role as victims. These cases have hard facts and unsettling outcomes, all of which have amplified and exposed a broader problem: the current bankruptcy system has fundamental limitations for litigation claims. It is critical that we adopt measures to clarify the law, improve procedures, and realign incentives among stakeholders. The time has come to eliminate the settlement trap.

---

206. *See* 11 U.S.C. §§ 326–328.

207. *See* Elizabeth Cabraser & Andrew Pincus, *Claims-Made Class-Action Settlements*, 99 JUDICATURE 81 (2015).

208. This could mirror the compensation cap imposed on trustees in 11 U.S.C. § 326(a).

209. Recall that any recovered money that does not pay administrative expenses or creditors goes back to the debtor as a surplus. By tying administrative expenses to creditor recovery, such a proposal would guard against litigating a settlement to the detriment of the debtor's potential surplus.