UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF NORTH CAROLINA
Charlotte Division

In Re:	Chapter 11
GARLOCK SEALING TECHNOLOGIES LLC, et al.[1]	Case No. 10-31607
Debtors.	Jointly Administered

MOTION OF THE OFFICIAL COMMITTEE OF ASBESTOS PERSONAL INJURY CLAIMANTS FOR A PROTECTIVE ORDER DETERMINING THAT COMMUNICATIONS MADE PURSUANT TO PLAN NEGOTIATIONS DO NOT FALL WITHIN THE PROPER SCOPE OF DISCOVERY IN THE CONFIRMATION PROCEEDING

The Official Committee of Asbestos Personal Injury Claimants (the "**ACC**"), by and through its undersigned counsel, hereby moves this Court for a protective order determining that communications undertaken in the course of plan negotiations are not a proper subject for discovery in the contested confirmation proceeding now underway (the "**Motion**"). In support thereof, the ACC respectfully submits as follows.

BACKGROUND

Almost from the day when Debtors filed their Chapter 11 petitions more than five years ago, the parties' principals and counsel have engaged in discussions and negotiations with a view to achieving a consensual plan of reorganization. Also from the outset, the Debtors, their parent Coltec Industries Inc. ("**Coltec**"), the ACC, and the Future Asbestos Claimants' Representative

[1] Debtors consist of Garlock Sealing Technologies LLC, Garrison Litigation Management Group, Ltd., and The Anchor Packing Company.

(the "**FCR**") all participated on the basis that negotiations plan negotiations ought to be and remain confidential.

Unfortunately, efforts to produce a fully consensual plan have fallen short so far. In January 2015, however, Debtors put forth their Second Amended Plan of Reorganization (the "**Plan**") and announced the FCR's agreement to support it.

The Confirmation Issues

The ACC opposes the Plan. Confirmation objections are not due to be filed until October 6, 2015. In a voluntary non-binding preliminary statement, however, the ACC has noted its intention to object to confirmation of the Plan as failing to satisfy subsections (1), (3), (7), and (11) of Bankruptcy Code section § 1129(a), and as violating the Absolute Priority Rule embodied in sections 1129(b)(1) and 1129(b)(2)(B). *See* Preliminary Confirmation Objections of the Official Committee of Asbestos Personal Injury Claimants to the Debtors' Second Amended Plan of Reorganization at 7-12, dated April 30, 2015 [Dkt. No. 4586] (cited below as "**Prelim. Conf. Objs.**"). These objections focus on the Plan and the effects it would have on claimants.

The confirmation objections are worth noting here because the scope of discovery ought to be delineated in such a way as to encompass the disputed issues for confirmation without bringing in matters that have no reasonable bearing on the disputes. The principal objections include:

- Section 1129(a)(1) of the Bankruptcy Code prevents confirmation because the Plan fails to comply with other applicable sections of the Code, including by channeling asbestos claims without complying with prerequisites for that relief as prescribed by section 524(g) (Prelim. Conf. Objs. at 8 ¶ 1.d), and releasing and discharging Debtors' non-bankrupt affiliates of derivative liability for "GST Asbestos Claims and Anchor Claims" (as defined in the Plan), contrary to sections 524(e) and 524(g) (*id.* at 8 ¶ 1.g).

- Section 1129(a)(3) prevents confirmation because the Plan has not "been proposed in good faith" within the meaning of that statute. That is, "[i]f the Plan took effect, it would impose results inconsistent with the Code" (Prelim. Conf. Objs. at 9 ¶ 2). The effects of the Plan that run counter to the purposes and policies of reorganization include, among other things, using a set of Claims Resolution Procedures and a Case Management Order to override applicable non-bankruptcy law and devalue claims in ways that "could not be accomplished legitimately through normal processes of litigation and resolution outside of bankruptcy" (*id.* ¶ 2.c); "rendering meaningless the right to jury trial for some Asbestos Claimants" (*id.* ¶ 2.d), in particular, those who could not get their claims to trial before the capped Litigation Fund is exhausted by judgments and defense costs[2]; "violating the priority of creditors' claims over equity holders' interests" (*id.* ¶ 2.f); "purporting to extinguish and enjoin potential claims, rights, and remedies, which are derived from" GST Asbestos Claims or Anchor Claims as against Debtors' nonbankrupt affiliates (*id.* ¶¶ 2.h & 2.i); and "attempting to confer upon the FCR a power he does not possess to bind Future Asbestos Claimants through a ballot" (*id.* ¶ 2.l).

- Section 1129(a)(11) prevents confirmation because the Plan is not feasible. It would impose "unworkable burdens on" the District Court and the Bankruptcy Court in this district and "inordinate delays" on Asbestos Claimants, portending a need for further reorganization, or even liquidation, of the Settlement Facility and Reorganized Garrison (Prelim. Conf. Objs. at 10 ¶ 3).

- The Absolute Priority Rule would prevent the Plan from being confirmed by way of cramdown, even if the FCR's ballot were legally effective to create an assenting impaired class. This is so because the Plan does not assure "each holder of an Asbestos Claim in Class 4" of payment in full of the "Allowed Amounts" prescribed by the Plan, but provides for Garlock's ultimate parent, EnPro Industries Inc., to retain its valuable indirect equity interest (Prelim. Conf. Objs. at 11-12 ¶ 8).[3]

The legal objections to confirmation point, of course, to key factual issues:

- whether the Plan provides sufficient funding for asbestos claims;

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[2] *See* Prelim. Conf. Objs. at 7 ¶ 1.a.

[3] The foregoing summary is not a full restatement or paraphrase of the ACC's Preliminary Confirmation Objections, and both it and the Preliminary Confirmation Objections themselves are without prejudice to the formal objections that are due to be filed on October 6, 2015. The purpose of the summary, rather, is to convey the nature and tenor of principal issues that are anticipated subjects of dispute in the confirmation proceeding.

- whether the Plan improperly saddles asbestos claimants with the risk that the funding will not suffice to pay the allowed amounts of asbestos claims, while enabling Debtors' parent company to keep a stake worth hundreds of millions of dollars;

- whether the interplay of the "Settlement Option" and the "Litigation Option," under the hard and fast liability cap, would exert undue duress on claimants and subvert jury trial rights that Debtors' bankruptcy cannot lawfully undermine (*see* 28 U.S.C. § 1411(a));

- whether the Parent Settlement is unfair, tainted by Coltec's control over Debtors, and contrary to law; and

- whether the Claims Resolution Procedures and Case Management Order on which the Plan is based would be unfair to claimants, confer windfalls on Debtors and Coltec, and present the courts of this District with unworkable burdens.

See Prelim. Conf. Objs. at 2-7.

Another set of important questions concern the idea that the FCR is entitled to cast a ballot for his constituency. The parties disagree about whether Future Asbestos Claimants may be considered a voting class, when by definition they cannot be identified and their as-yet unasserted claims cannot be subjected to meaningful criteria for temporary allowance for voting purposes. The parties also dispute whether the FCR has the legal capacity and authority to cast a ballot accepting the Plan, so as to enable Debtors to request cramdown.[4] And the Plan itself frames the question whether the "the FCR has adequately represented Future GST Asbestos Claimants," an affirmative determination which the Plan makes an express condition of confirmation. Debtors' Second Amended Plan of Reorganization at 53 § 7.8.1(g).[5]

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[4] *See* the FCR's response to the ACC's Preliminary Confirmation Objections, and the ACC's reply thereto. These papers were filed as Docket Nos. 4618 and 4659 respectively.

[5] The Plan is on file as Exhibit A to Debtors' Disclosure Statement.

In the ACC's view, a proper focus on the disputed issues makes clear that evidence of what communications the parties exchanged in plan negotiations and what positions they took in the bargaining are simply not relevant: such evidence cannot be probative of any material issue in the confirmation proceeding, nor can discovery into those matters plausibly lead to relevant evidence. The FCR, however, disagrees, while Debtors and Coltec's position on this question remains unclear.

Fact discovery for the confirmation proceeding is underway. The Case Management Order establishes an ambitious schedule under which written discovery and the deposition of fact witnesses are to be completed by November 17, 2015. It will promote efficiency and proper focus in the discovery process for the Court to determine at this stage whether plan negotiations fall outside the proper scope of discovery in this matter.

The Meet-and-Confer Process Regarding Written Discovery Has Sharpened the Issue of Scope

In the first round of written discovery, the ACC requested that the FCR produce "[a]ll documents upon which you based your decision to support the Plan or upon which you rely to justify that decision." Exh. A at 7 (Request for Production No. 4).[6] The FCR objected on the grounds, among others, that this request is "not relevant" and "not reasonably calculated to lead to the discovery of admissible evidence." *Id.* at 8. Nevertheless, without waiver of these objections, his written response stated that the FCR would search for and produce responsive non-privileged documents.

[6] Exh. A is a copy of Future Claimants' Representative's Responses and Objections to Official Committee of Asbestos Personal Injury Claimants' First Request for Production of Documents. It sets for the ACC's document requests and the FCR's objections and answers thereto.

Notably, the ACC's request of the FCR did not call for plan-negotiation communications as such. Faced, however, with the plan proponents' contentions that the FCR's agreement obviated any conflict of interest affecting the Parent Settlement, the ACC did serve Debtors and Coltec with interrogatories and document requests concerning Debtors' investigation and evaluation of the claims that would be discharged by that proposed arrangement. Thus, the ACC called upon Debtors to identify each claim that would be released if the Parent Settlement took effect, and also to identify the individuals who conducted Debtors' investigation into those claims, the individuals questioned in the course of the investigation, and all documents "setting forth or discussing questions posed, issues identified, observations made, evidence compiled, analyses conducted, inferences drawn, or conclusions reached in or as a result of the investigation." Exh. B at 11-12 (Interrogatory No. 10).[7] In a document request paralleling that interrogatory, the ACC also asked Debtors to produce "[a]ll Documents reviewed as part of the investigation and any Communications between or among the Debtors (or their representatives), any Non-Debtor Affiliates (or their representatives), any former affiliates of the Debtors or Coltec (or their representatives), or the FCR (or his representatives) concerning the investigation." Exh. C at 22 (Request for Production No. 35).[8] Debtors objected to the interrogatory on the basis of "the attorney-client privilege and attorney work product privilege"

[7] Exh. B is a copy of Debtors' Responses to Official Committee of Asbestos Personal Injury Claimants' First Set of Interrogatories Directed to the Debtors Regarding Confirmation Issues. It sets for the ACC's interrogatories and Debtors objections and answers thereto.

[8] Exh. C is a copy of Debtors' Responses to Official Committee of Asbestos Personal Injury Claimants' First Requests for Production of Documents Directed to the Debtors Regarding Confirmation Issues. It sets for the ACC's document requests and Debtors objections and answers thereto.

and incorporated that objection in their response to the production request.[9] In answer to the interrogatory, they provided general information about their investigation into derivative claims, but took the position that "[t]he detail of the Debtors' and the Debtors' attorneys' legal research, conversations, and questions are privileged and/or constitute protected work product." Exh. B at 13.

The ACC conducted a meet-and-confer process with the FCR and separately with Debtors. The FCR took the position that, in deciding to support the Plan, he relied on the negotiations among the parties. His counsel therefore expressed his intention to produce all documents reflecting such communications, save only communications received from Debtors that they wish to protect as work product immune from discovery. The ACC pointed out that plan negotiations were meant to be kept confidential, as all parties had agreed. The ACC also disclaimed any intention to force the FCR to produce documents revealing plan negotiations, and explained that the request for the materials the FCR relied upon in deciding to support the Plan was not meant as an invitation to abrogate undertakings of confidentiality. Yet the FCR insisted that communications exchanged in plan negotiations are responsive to the ACC's request. In context, it seems clear that the FCR himself wishes to inject plan negotiations as a subject for evidence in the confirmation hearing.

Upon considering the FCR's position, the posture of the matter, and relevant precedent, the ACC determined to seek the guidance of this Court as to whether or not the contents of plan negotiations fall within the proper scope of discovery for the confirmation proceeding. The ACC informed the FCR and the other parties that it would move for such a ruling and, without

[9] Exh. B at 12; Exh. C at 22.

prejudice pending the outcome of that motion, would suspend any discovery requests (including the above-mentioned requests directed to Debtors) to the extent that the requests either call for information or documents that would reveal the contents of plan negotiations or are interpreted by the responding parties as calling for such information or documents. Debtors appear to have accepted that protective and conditional withdrawal of requests, on the explicit understanding that the ACC reserves the right to press those inquiries if the Court determines that discovery into plan negotiations is appropriate. The FCR, by contrast, chose to make his full intended production available to the ACC via an internet-based "drop box." In an abundance of caution, not wishing to pierce the confidentiality of confidential communications until the Court determines the question now presented, the ACC has refrained from downloading, inspecting, or otherwise accessing the FCR's production, and has so informed the FCR's counsel.

Summary of the ACC's Position

Under the reasoning and precedents discussed in the Argument below, communications about the substance of plan negotiations — all of which the parties undertook on the basis of strict confidentiality — are not relevant to any confirmation issue and would not be reasonably calculated to lead to the discovery of other admissible evidence. The disputed issues for confirmation should be litigated and decided on the basis of what the Plan says and what the Plan would do if it took effect — not on what any party said in the course of negotiations. That negotiations took place is of course undisputed. But it is the contents of the Plan itself, not the contents of negotiations, that are probative of the factual and legal issues the Court must decide in order to determine whether or not to confirm the Plan.

It thus falls well within the discretion of the Court to shield from discovery the substance of the negotiations and the communications through which the negotiations were carried out.

There are compelling reasons for the Court to exercise that discretion so as to focus the litigation on the issues that truly matter, vindicate justified reliance upon the confidentiality of negotiations, prevent costly and unnecessary detours in discovery, and avoid unnecessary privilege disputes and other collateral matters. Notably, most of the negotiations directly involved not only the parties' principals, but also their respective counsel. It is difficult to see how opening up plan negotiations for discovery and proof could fail to make witnesses out of the lawyers. And if that were permitted, it would greatly complicate the litigation of confirmation issues and magnify the associated expense, for little if any benefit to the adjudicatory process.

On the other hand, if the Court rules that plan negotiations fall outside the scope of appropriate discovery, the ACC's confirmation objections, as well as the responses of Debtors, Coltec, and the FCR, will have to focus on the Plan and its effects. The ACC is fully prepared to go forward on that basis.

Of course, it is important that the litigation be conducted fairly, and no party should have to fear a "whipsaw." For example, if the Court determined that Plan negotiations are "fair game," Debtors would not be entitled to shield as "work product" communications they voluntarily shared with a counter-party, the FCR, in the course of the negotiations. A broader and vary important privilege issue would also arise. In investigating derivative claims against Coltec and negotiating the Parent Settlement to extinguish all such claims, Debtors purport to have acted in their capacity as debtor-in-possession – in other words, as a trustee for creditors. As discussed below, under what has come to be known as the "fiduciary exception" to the attorney-client privilege, it is doubtful whether their asserted privilege can stand against the statutory committee for their principal creditors with respect to an investigation and negotiation that Debtors undertook as the creditors' trustee. Such contentious privilege issues need not arise

if the entire subject of plan negotiations is ruled out of bounds for discovery and evidence in the confirmation proceeding.

If the contents of plan negotiations fall within the reasonable scope of discovery as delineated by this Court, the ACC will have a great deal to say on that subject, even apart from satellite litigation concerning privilege issues. The Argument below, however, will demonstrate that the most persuasive authorities in point, and the genuine needs of these Chapter 11 cases, should lead the Court to exclude plan negotiations from the scope of discovery and proof in the confirmation proceeding.

JURISDICTION AND VENUE

The captioned cases fall within the bankruptcy jurisdiction of the district courts pursuant to 28 U.S.C. § 1334, and venue properly lies in this district pursuant 28 U.S.C. § 1409. The District Court has properly referred these cases to the Bankruptcy Court, and proceedings on the instant Motion constitute a core matter falling within the adjudicatory authority of the Bankruptcy Court. *See* 28 U.S.C. § 157(b)(2)(L).

RELIEF REQUESTED AND STATUTORY BASIS THEREFOR

The Motion seeks a protective order pursuant to Fed. R. Civ. P. 26(c), made applicable by Fed. R. Bankr. P. 7026 and 9014. The contents of plan negotiations, and the communications through which such negotiations were carried out, fall outside the proper scope of discovery for the confirmation hearing because (1) these matters are neither relevant nor "reasonably calculated to lead to the discovery of admissible evidence" (Fed. R. Civ. P. 26(b)(1)), and (2) alternatively, "the burden and expense" of discovery into plan negotiations and related communications "outweighs its likely benefit, considering the needs of the case, the amount in

controversy, the parties' resources, the importance of the issues at stake in the action, and the importance of the discovery in resolving the issues" (Fed. R. Civ. P. 26(b)(2)(C)).

ARGUMENT

I. Plan Negotiations Are Not Relevant to Confirmation Issues, and Discovery of the Negotiations Is Not Calculated to Lead to Admissible Evidence

Under the weight of authority, communications exchanged by the parties in the course, and for the purposes of, plan negotiations are not relevant to the findings and conclusions a bankruptcy court must make in a contested confirmation hearing. Nor would discovery into such communications be "reasonably calculated to lead to the discovery of admissible evidence." Fed. R. Civ. P. 26(b)(1). To permit discovery of settlement communications would thus violate one of the fundamental boundaries circumscribing discovery in federal practice, notwithstanding the liberality of the discovery rules in other respects. *See id.*

To be confirmed, a Chapter 11 reorganization plan must be "proposed in good faith and not by any means forbidden by law." 11 U.S.C. § 1129(a)(3). The leading case on the meaning of this standard is *In re Madison Hotel Associates*, 749 F.2d 410 (7th Cir. 1984), which teaches as follows:

> Though the term "good faith," as used in section 1129(a)(3), is not defined in the Bankruptcy Code, the term is generally interpreted to mean that there exists "a reasonable likelihood that the plan will achieve a result consistent with the objectives and purposes of the Bankruptcy Code. " Similarly, in the context of a Chapter 13 reorganization, this court has interpreted the identical "good faith" language contained in 11 U.S.C. § 1325(a)(3) to require the bankruptcy court to review the proposed plan for accuracy and "a fundamental fairness in dealing with one's creditors." Thus, for purposes of determining good faith under section 1129(a)(3), as well as section 1325(a)(3), the important point of inquiry is the plan itself and whether such plan will fairly achieve a result consistent with the objectives and purposes of the Bankruptcy Code.

> According to the good faith requirement of section 1129(a)(3), the court looks to the debtor's plan and determines, in light of the particular facts and circumstances, whether the plan will fairly achieve a result consistent with the Bankruptcy Code. The plan "must be 'viewed in light of the totality of the circumstances surrounding confection' of the plan [and] . . . [t]he bankruptcy judge is in the best position to assess the good faith of the parties' proposals."

Id. at 424-25 (citations and footnote omitted);[10] *see* also *In re PWS Holding Corp.*, 228 F.3d 224, 242 (3d Cir. 2000) (explaining that "the important point of inquiry is the plan itself"); *In re City of Detroit*, 524 B.R. 147, 248 (Bankr. E.D. Mich. 2014) (when conducting the § 1129(a)(3) inquiry, "[t]he Court's focus must be on the plan itself," in light of the "totality of the circumstances" and "the court's own 'common sense and judgment.'").

The Fourth Circuit has not directly addressed the applicable standard for section 1129(a)(3). In *Behrmann v. National Heritage Foundation*, 663 F.3d 704 (4th Cir. 2011), the Court of Appeals affirmed as not clearly erroneous a bankruptcy court's determination that a negotiated plan was proposed in good faith, where the lower court took a "totality of the circumstances" approach and found that the debtor "'proposed its Plan with the legitimate and honest purpose of reorganizing and maximizing both the value of [NHF's] Estate and the recovery to Claimants.'" *Id*. at 709-10. Among the circumstances noted in the opinion was the fact that the plan was the product of negotiations. *See id.* at 709. But the Court of Appeals made no mention of the substance of the negotiations, as distinct from the fact that they took place, nor

[10] The "good faith" required to confirm a plan should not be confused with the good-faith standard that applies when testing the propriety of a bankruptcy petition. The two tests are not the same. *See Madison Hotel Assocs.*, 749 F.2d at 425.

of any communications exchanged by the parties in the course of the bargaining. There is no indication in the opinion that the legal standard had been a subject of dispute below.

Plan objectors have sometimes attempted to look beyond objective circumstances in contesting good faith for confirmation purposes. Although the caselaw is less than uniform, the most apposite and persuasive precedents have rejected such efforts and have ruled plan negotiations out of bounds for discovery and proof in contested confirmation hearings. The precedents most directly relevant to the cases at bar are the decision of the Third Circuit in *In re W.R. Grace & Co.*, 729 F.3d 332, 346 (3d Cir. 2013) (*Grace II*), and the bankruptcy court's decision in *Mt. McKinley Insurance Co. v. Pittsburgh Corning Corp.*, 518 B.R. 307, 325-26 (W.D. Pa. 2014), *appeal filed*, No. 14-4329 (3d Cir. Nov. 6, 2014). Both illustrate that the touchstone for evaluating the good faith of a plan is the plan itself.

In *Grace II*, an insurance company objected to a section 524(g) plan of reorganization agreed upon between an asbestos debtor, the statutory committee of asbestos claimants, the court-appointed future asbestos claimants' representative, and others. The insurer contended that the plan was the product of improper collusion; it demanded discovery about the plan negotiation process and insisted that testimony from the debtor's general counsel was "required to demonstrate Grace's honesty and good intentions in proposing the Plan." *Grace II*, 729 F.3d at 338. The bankruptcy court refused such discovery, and the district court affirmed that ruling on appeal of the confirmation order. *In re W.R. Grace & Co.*, 475 B.R. 34, 88 (D. Del. 2012) (*Grace I*). The Court of Appeals also affirmed, observing that the debtor's "[s]ubjective intent, to the extent that it is one factor in determining that a Plan is not being used for purposes contrary to the Code's objectives, is routinely established by circumstantial evidence." *Grace II*, 729 F.3d at 348. That Court went on to uphold the confirmation order, relying solely on

objective criteria to approve the lower court's finding that there was "[n]othing in the record" to suggest that the debtor had proposed the plan in bad faith. *Grace I*, 475 B.R. at 86. That "the Joint Plan was the result of years of litigation and extensive arms-length negotiations" (*id*. at 89) were not facts that necessitated or warranted an excursion into the back-and-forth of the bargaining or scrutiny of the contents of discussions among the negotiators.

Bankruptcy Judge Judith Fitzgerald, whose rulings in *Grace* withstood the appeals, made a similar decision in the asbestos-driven bankruptcy of Pittsburgh Corning. There, too, faced with an objecting insurer's requests to probe plan negotiations in discovery, Judge Fitzgerald ruled that such discovery was not warranted. The district court agreed on the basis that "the substance of settlement negotiations was not reasonably calculated to lead to admissible evidence." *Pittsburgh Corning Corp.*, 518 B.R. at 325-26.[11]

In *Grace II* the Third Circuit underscored the evidentiary and privilege-related pitfalls of relying on testimony about plan negotiations to determine subjective intent. *See Grace* II, 729 F.3d at 348. In particular, the Court cautioned that "divining the subjective intent of a corporate actor through the testimony of the negotiators and other key people will often prove problematic

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[11] Also instructive is a recent decision in the bankruptcy of the City of Detroit. Objectors there alleged bias in the plan mediation process, contending that proof thereof would show that the plan failed the test of good faith for confirmation. *In re City of Detroit*, 2014 WL 8396419, at *10 (Bankr. E.D. Mich. Aug. 28, 2014). After reviewing various formulations of the good-faith test, the court found that one key point was "not debatable": "[T]he sole focus of the good faith inquiry, whatever that inquiry may be, are the plan and the debtor. No case law supports extending the good faith inquiry to the conduct of third parties." *Id.* The "mandate" to examine the totality of the circumstances, the court explained, "identifies only where to look to determine the debtor's good faith. It does not identify what to look for and *it does not authorize a broad-based examination into the motives and intentions of everyone in the case*." *Id.* (emphasis added). The court therefore ruled that the totality of the circumstances test "does not make [the objector's] challenge to the mediation and the mediators relevant to its objection that the City did not propose its plan in good faith." *Id.*

and less than enlightening." *Id.* The inherent flaws in this type of evidence led the Court to conclude that "it would be an extraordinary circumstance where an objectively fair plan must be set aside because of mere suspicions concerning the subjective intent of the parties." *Id.*

The same conclusion applies in reverse with equal or greater force: A plan that is objectively *un*fair will not be salvaged by bolstering the alleged good intentions of the plan proponents and supporters through evidence going to the contents of the negotiations. In short, the proof is in the pudding. It is the plan itself that fully manifests the intentions of the debtor and allied parties. The terms and effects of the plan, viewed in the totality of the debtor's circumstances, form the proper basis for a judicial determination as to whether or not the plan is proposed in good faith and is likely to achieve the legitimate reorganization purposes of the Bankruptcy Code.

Here, Debtor's Second Amended Plan is the product of extensive negotiations tracing back more than five years to the very beginning of these Chapter 11 cases. That the Plan has antecedents in prior versions proposed by the Debtor, and that it emerged from negotiations among Debtors, Coltec, and the FCR, are undisputed matters. Also beyond dispute is that the same parties negotiated at length with the ACC. But it is neither necessary nor appropriate to delve into the course of those negotiations, to explore what positions the respective parties took or abandoned therein, or to scrutinize communications that passed between or among parties in that process.

Under the foregoing authorities, this Court should rule that plan negotiations and the communications involved in such negotiations fall outside the proper scope of discovery in the confirmation proceeding. As *Grace II* instructs, such matters have no tendency to prove or disprove good faith within the meaning of section 1129(a)(3). Nor do any of the other

confirmation tests or issues disputed in Debtors' cases fairly call for discovery forays into the contents of plan negotiations. Evidence of positions taken and communications exchanged in the course of bargaining would have no probative value for the adjudication of plan feasibility, the "best interests" test, or the Absolute Priority Rule. Nor would such evidence have any tendency to prove whether future claimants have been adequately represented. It is undisputed that the FCR engaged in negotiations with all of the other parties. But retracing the course of those negotiations cannot establish whether or not the FCR has adequately protected the collective interests of his constituency. Rather, it is the Plan he has agreed to — more particularly, how it would treat future claimants and provide for their claims — that will form the basis for that determination.

Plan negotiations are thus irrelevant. Of course, "[i]rrelevant evidence is not admissible." Fed. R. Evid. 402. Furthermore, as the bankruptcy court and the district court both held in *Pittsburgh Corning*, discovery of plan negotiations is not reasonably calculated to lead to the discovery of evidence admissible for the confirmation hearing. It follows that, under basic principles governing the scope and limits of federal discovery practice, plan negotiations and related communications are not discoverable in this proceeding. *See* Fed. R. Civ. P. 26(b)(1) (providing that parties may obtain discovery only of nonprivileged matters that are "relevant to any party's claim or defense" or that "appear[] reasonably calculated to lead to the discovery of admissible evidence").

II. Alternatively, Discovery Into Plan Negotiations Should Be Prohibited Because Any Marginal Utility Such Discovery Might Have Is Decisively Outweighed By the Costs and Disruptions It Would Entail

Even if one can conjure up some way in which plan negotiations might be, or lead to, marginally relevant evidence, discovery thereof would still transgress the reasonable bounds of

discovery in the confirmation hearing. "All discovery is subject to the limitations imposed by Rule 26(b)(2)(C)." Fed. R. Civ. P. 26(b)(1). Among those limitations is this basic principle:

> On motion or on its own, *the court must limit the* frequency or *extent of discovery* otherwise allowed by these rules or local rule *if it determines that*: . . .
>
> (iii) *the burden or expense of the proposed discovery outweighs its likely benefit, considering the needs of the case*, the amount in controversy, the parties' resources, the importance of the issues at stake in the action, and the importance of the discovery in resolving the issues.

Fed. R. Civ. P. (b)(2)(C) (emphasis added). *Cf.* Fed. R. Evid. 403 (providing that the court may exclude even relevant evidence if its probative value is substantially outweighed by countervailing factors, such as unfair prejudice, wasting time, *etc*.).

Here, substantial counterweights militate against permitting discovery and proof of plan negotiations and communications exchanged in that process. In the cases at bar, negotiations have taken place over more than five years — and should be encouraged to continue. If the bargaining is deemed a proper subject of inquiry, fairness and the rule of completeness would expose the entire course of negotiation to scrutiny, not just those parts that one side or the other might find advantageous to display. The time and expense of fully exploring the subject would be very great, while, as the Third Circuit recognized in *Grace II*, the "yield" in terms of reliable proof would be scant. *See Grace II*, 729 F.3d at 348. Moreover, discovery of the negotiations would violate the confidentiality of discussions and communications, which has been a fundamental premise of the bargaining throughout. Parties conduct negotiations on a confidential basis precisely to ensure that they can speak frankly, and even bluntly, so as to gain the clearest understanding of their respective positions and thereby maximize the prospects for achieving a consensus despite their intensely competing interests and clashing legal positions.

To permit discovery of their confidential communications would thus defeat the justified expectations of the parties, seriously chill discussions in this bankruptcy going forward, and set a precedent inimical to settlement in other cases as well, contrary to the well-established public policy favoring the settlement of disputes.

The complications and collateral issues that would follow from throwing open plan negotiations for discovery include significant privilege and work-product disputes that would not otherwise arise. The FCR has informed the ACC that it has withheld from his intended production certain communications that Debtors assert to be immune from discovery as work product. If, then, the Court determines that plan negotiations fall within the reasonable scope of discovery, the ACC will be constrained to challenge whether any such immunity exists as to materials Debtors voluntarily shared with a party that was squared off against them in negotiations.

If plan negotiations are deemed discoverable, satellite litigation will also be necessary over privilege and work-product claims Debtors have raised to shield their analysis and evaluation of the derivative claims they hope to bargain away and extinguish pursuant to the Parent Settlement and related Plan provisions. In taking it upon themselves to negotiate the Parent Settlement, Debtors acted in the fiduciary capacity of debtor-in-possession ─ that is, as trustee for the very creditors whose statutory committee, the ACC, would be entitled to scrutinize the negotiations if discovery properly encompasses that subject matter. A well-established doctrine teaches that a fiduciary may not interpose a claim of privilege against the interest of its beneficiaries when good cause exists for exposing otherwise privileged matters to discovery. This "fiduciary exception" to privilege originated in *Garner v. Wolfinbarger*, 430 F.2d 1093, 1103-04 (5th Cir. 1970), where the Fifth Circuit held that a corporation's attorney-client

privilege in a derivative suit is "subject to the right of the stockholders to show cause why [privilege] should not be invoked in the particular instance" to shield alleged breaches of the corporation's fiduciary duty to the stockholders. *Id.* at 1103-04. The exception rests on the mutuality of interest between a fiduciary and the beneficiaries in whose best interest the fiduciary is duty-bound to act. *See id.* at 1103.

Given that logic and rationale, it is not surprising that the fiduciary exception has been applied to prevent a debtor and debtor-in-possession from thwarting discovery into alleged derivative claims very like those Debtors and Coltec hope to scotch by means of the Parent Settlement. *Official Comm. of Asbestos Claimants of G-I Holding, Inc. v. Heyman*, 342 B.R. 416 (S.D.N.Y. 2006). In *Heyman*, the asbestos claimants' committee brought suit against the corporate debtor's sole stockholder to avoid and recover a fraudulent transfer whereby the stockholder had caused the company to transfer a subsidiary to himself by way of a dividend. The committee sought discovery of various communications over which the debtor asserted attorney-client privilege. Applying the *Garner* doctrine, District Judge Sweet found "good cause" to override the corporation's privilege claim, noting among other considerations that the committee had a substantial need for the requested materials to "rebut[] affirmative defenses," including the stockholder's alleged defense that the underlying conduct was conducted for valid business reasons. *Id.* at 425-26. Coltec has articulated that same defense to avoidance claims that it and Debtors have thus far avoided litigating but now hope to "settle" as part of the Plan. As noted above, Debtors have asserted privilege objections to discovery requests the ACC propounded but has withdrawn without prejudice pending a ruling on this Motion.

The ACC is willing for the Parent Settlement to stand or fall on the basis of its own terms and the objective circumstances surrounding it and thus to forego a challenge to Debtors'

claimed privilege regarding that matter. But if the Court deemed plan negotiations to be discoverable, the ACC would have no choice but to challenge that privilege claim on any available ground, including the fiduciary exception. Debtors no doubt would vigorously resist. That litigation would be costly and time-consuming; it would lead the parties and the Court into a thicket of issues that would not arise if the confirmation contest were to be waged solely on objective grounds.

Privilege disputes are certainly not the only subject that would spark collateral litigation if plan negotiations were opened up to discovery. Most of the negotiations conducted over the course of five years in Debtors' cases have involved direct participation by lawyers for those parties ─ the same lawyers who speak for them in the Bankruptcy Court. If the negotiations are permitted to become matters for evidence, those lawyers will be witnesses. Rule 3.7(a) of the North Carolina Rules of Professional Conduct, known as the "Lawyer as Witness" rule, provides: "A lawyer shall not act as advocate at a trial in which the lawyer is likely to be a necessary witness unless: (1) the testimony relates to an uncontested issue; (2) the testimony relates to the nature and value of legal services rendered in the case; or (3) disqualification of the lawyer would work substantial hardship on the client." Even apart from the ethical conundrums, the complications and inconveniences that would result from turning the lawyers into witnesses should not be underestimated.

In sum, the burdens, complications, and the cost in effort and money that would follow from throwing open plan negotiations for discovery and proof would substantially outweigh any probative value they might have in the confirmation proceeding. This Court should therefore exclude that subject matter from discovery, along with all communications exchanged in the course of the negotiations. Fed. R. Civ. P. 26(b)(2)(C). It would run counter to the genuine

needs of these cases to allow the discovery process to veer off into negotiations that have been conducted on a confidential basis. As the most apposite caselaw instructs, "the important point of inquiry is the plan itself." *PWS Holding Corp.*, 228 F.3d at 242. The confirmation issues can and should be litigated on the basis of what the Plan says and the objective circumstances in which Debtors have proposed it. *Grace II*, 729 F.3d at 346; *Madison Hotel Assocs.*, 749 F.2d at 424-25; *Pittsburgh Corning*, 518 B.R. at 325-26.

CONCLUSION

For all of the foregoing reasons, the Motion should be granted. The Court should make an order prohibiting discovery into plan negotiations and related communications.

Dated: August 24, 2014

Respectfully submitted,

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CERTIFICATION OF COMPLIANCE WITH
<u>FEDERAL RULE OF CIVIL PROCEDURE 26(c)</u>

I certify that movant, the Official Committee of Asbestos Personal Injury Claimants, has complied with the requirements of Rule 26(c) of the Federal Rule of Civil Procedure 26(c) by conferring in good faith with the Future Asbestos Claimants' Representative and Debtors in an effort to resolve the issues addressed in the foregoing Motion without court action.

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