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The Rising Use of Subchapter V Filings to Attempt to Avoid Current and Future Mass-Tort Liability

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Future asbestos claimants [individuals who have been exposed to asbestos but who have not yet been diagnosed with an asbestos-related disease] are in an untenable catch-22 situation of having to file proofs of claim — simply to share in a $50,000 distribution that may be paid on the effective date — without any manifested injuries to permit allowance of their claims.[1]

This statement from the Bankruptcy Appellate Panel (BAP) for the U.S. Court of Appeals for the Ninth Circuit in the Ben Nye subchapter V appeal highlights a new question in mass-tort bankruptcy: To what extent can the streamlined subchapter V process be used to resolve not only existing mass-tort liabilities but also liabilities arising from future undiagnosed claims? This inquiry implicates core concerns of fairness, due process and the limits of subchapter V as a mechanism for resolving latent harms. This article examines the *Ben Nye* case,[2] the evolving definition of an asbestos "claim" in bankruptcy, the use of subchapter V to manage asbestos liabilities, and the unresolved challenges of discharging future asbestos claims under subchapter V.

Ben Nye's Subchapter V Filing: A Test Case

In March 2024, Ben Nye, a Los Angeles-based theatrical cosmetics manufacturer, filed for subchapter V relief. The filing cited escalating litigation costs arising from alleged asbestos contamination in the company's talc-based cosmetic products. With limited insurance and declining revenues, the company argued that bankruptcy, particularly subchapter V, offered the only viable path to reorganize its operations while addressing both present and potential liabilities.

As part of the proceeding, the bankruptcy court approved Ben Nye's bar date order requiring all asbestos claimants, whether known or unknown, to file proofs of claim by a certain deadline. The order warned that failure to file would permanently enjoin recovery against the debtor, even for individuals who had not yet been diagnosed with an asbestos-related disease. In effect, the company sought to not only resolve existing lawsuits but also to cut off all latent injury claims in exchange for a modest $50,000 pot plan distribution.

The Appeal: Ninth Circuit BAP Pushes Back

On appeal, the Ninth Circuit BAP corrected key portions of the bar date order, striking the channeling injunction and revising it to clarify that the bar date order itself could not determine whether all future asbestos claimants were subject to the order.[3] The BAP reasoned that a bar date order is an administrative device used to facilitate participation in the bankruptcy case; it is not a substitute for the discharge or an injunction.[4] As the BAP explained:

> [E]njoining nonfiling asbestos litigants from seeking any future recovery from [the] Debtor is improperly broad; it would apply equally to those that do not have a 'claim' for purposes of bankruptcy. More importantly, it would improperly impose an injunction apart from a confirmed chapter 11 plan or the discharge injunction.[5]

By drawing this line, the BAP emphasized that bankruptcy procedure cannot be used to decide the substantive rights of people who might not yet know they are injured. The decision left unresolved whether such future claimants still hold "claims" that were discharged by the confirmed plan — a question with significant consequences for both the debtor and potential victims.

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1 *Ben Nye Co. Inc.*, BAP Nos. CC-24-1161, CC-24-1162, 31 (B.A.P. 9th Cir. June 17, 2025) (unpublished).

2 The BAP opinion has no precedential effect. It is an unsigned memorandum opinion that specifically states: "This disposition is not appropriate for publication. Although it may be cited for whatever persuasive value it may have, *see* Fed. R. App. P. 32.1, it has no precedential value, *see* 9th Cir. BAP Rule 8024-1." Although the BAP opinion has no precedential value, it is a thoughtful, well-reasoned evaluation of these issues, and bankruptcy courts in the Ninth Circuit have looked to it as a guidepost.

3 Paragraphs 8 and 9 of the bar date order were corrected to read:

8. The Asserted Asbestos Claims Bar Date applies to any person or entity that asserts a claim as defined by 11 U.S.C. § 105(5) against the Debtor based on the alleged exposure to the Debtor's products prior to the Petition Date. Notwithstanding the foregoing, nothing in this Order will prejudice current and/or future claimants' rights as set forth in Rule 3003(c)(3) of the Federal Rules of Bankruptcy Procedure.

9. Any person or entity that is required, but fails, to file a proof of claim against the Debtor for an asbestos claim, in accordance with this Order on or before the Asserted Asbestos Claims Bar Date, will not be treated as a creditor with respect to such claim in this case, including for the purposes of voting and distribution with respect to any chapter 11 plan of reorganization that may be filed in this bankruptcy case.

4 *Ben Nye Co. Inc.* at 22-23.

5 *Id.* at 25.

What Is a "Claim"? The Ongoing Debate

The *Ben Nye* decision illustrates the difficulty of applying the Bankruptcy Code's broad definition of "claim" to latent injury cases. Under § 101(5), a "claim" includes any "right to payment," whether contingent, unliquidated or disputed. Courts agree that this definition sweeps widely, but its application to asbestos exposure cases remains unsettled.

Some courts, such as the Third Circuit in *In re Grossman's Inc.*,[6] have held that a claim arises at the time of exposure to the harmful product, regardless of when illness manifests. By this reasoning, asbestos exposure alone is enough to create a pre-petition claim. At least one court in the Second Circuit has concluded that exposure-based claims might be treated as pre-petition, even if the illness emerges later, reflecting a broad reading of the statute.[7]

In the Ninth Circuit, the prevailing framework is the "fair contemplation" test. In *In re Jensen*,[8] the Ninth Circuit adopted the fair-contemplation test to determine when a claim exists under the Bankruptcy Code. Under *Jensen*, claims arise only when they can be fairly contemplated by the debtor and creditor. Individuals who have been exposed to a defendant's asbestos-containing products, but who will likely never develop an asbestos-related disease, cannot fairly contemplate that they have a claim against the debtor.

Under this standard, as reaffirmed and articulated by the Ninth Circuit in *Goudelock v. Sixty-01 Ass'n of Apartment Owners*,[9] "a claim arises when a claimant can fairly or reasonably contemplate the claim's existence even if a cause of action has not yet accrued under nonbankruptcy law." However, applying this test to asbestos exposure has proven difficult, since individuals exposed to asbestos often cannot reasonably contemplate the eventual development of an illness decades later.

Courts in the Ninth Circuit have broadly applied *Jensen* and the fair-contemplation test. For example, in *In re Hexcel Corp.*, the debtor sought to discharge an indemnification claim stemming from the debtor's pre-petition conduct.[10] The debtor argued to the district court on appeal that *Jensen* should not apply and "that outside the [Comprehensive Environmental Response, Compensation, and Liability Act] context, the debtor's conduct test must be applied, and claims stemming from pre-petition conduct must be discharged, even if this would result in the discharge of a claim that the parties had no way of contemplating prior to the bankruptcy."[11]

The *Hexcel* court disagreed, stating that "nothing in the *Jensen* decision support[ed] this extreme conclusion. In fact ... the [*Jensen*] court explicitly stated 'that nothing in the legislative history or the Code suggests that Congress intended to discharge [the] creditor's rights before the creditor knew or should have known that its rights existed.'"[12]

In *Ben Nye*, the BAP acknowledged Ninth Circuit precedent, but avoided a definitive ruling on whether individuals exposed to asbestos but not yet ill hold claims subject to discharge. Instead, the panel noted that "[a] debtor generally may not discharge future or nonexistent 'claims.'"[13] This uncertainty leaves future asbestos victims in a precarious position: If courts ultimately hold that exposure alone creates a claim, such claims could be discharged without the claimants ever receiving notice or compensation. If, on the other hand, courts require manifestation, debtors might face open-ended liability long after reorganization.

Subchapter V: An Inappropriate Vehicle for Mass Torts?

Ben Nye also raises the broader question of whether subchapter V is an appropriate vehicle for addressing mass tort liabilities. Enacted in 2019, subchapter V was designed to provide small businesses with a streamlined reorganization process, offering such debtor-friendly features as accelerated timelines and the elimination of the disclosure statement requirement. It was not intended to address the complex issues presented by latent asbestos claims.

> **Having to pay sick people who you made sick hurts the bottom line of these companies, so they are spending hundreds of millions of dollars in a sophisticated and elaborate attempt to close the mass-tort spigot.**

By contrast, § 524(g) was specifically created to manage asbestos liabilities and requires the establishment of a trust, the appointment of a representative for future claimants, and judicial findings that the trust is fair and equitable. These protections recognize that asbestos-related diseases often do not manifest until decades after exposure, making it impossible for many victims to assert claims during the debtor's bankruptcy.

In attempting to use subchapter V, *Ben Nye* effectively sought to replicate the protections afforded by a § 524(g) injunction — permanently barring both present and future claims — without meeting the statutory safeguards that Congress deemed essential. Hon. **Robert J. Faris** highlighted this concern during oral argument, asking the debtor: "Aren't you getting the same thing as the § 524(g) injunction without satisfying the requirements in that section?"[14] The answer is an emphatic "yes." Had the BAP not corrected the bar date order, Ben Nye would effectively have obtained the benefits of a § 524(g) injunction without extending any of the protections designed to safeguard future claimants.

Debtors like *Ben Nye* circumvent the approximately $3 million debt limit for subchapter V by filing before

6 607 F.3d 114, 125 (3d Cir. 2010).
7 *In re Johns-Manville Corp.*, 552 B.R. 221, 237 (Bankr. S.D.N.Y. 2016).
8 995 F.2d 925, 930 (9th Cir. 1993).
9 895 F.3d 633, 638 (9th Cir. 2018).
10 239 B.R. 564, 566-67 (N.D. Cal. 1999).
11 *Id.* at 170.
12 *Id.* (quoting *Jensen*, 995 F.2d at 930).
13 *Ben Nye Co. Inc.*, n.10.
14 Oral Argument at 28:42, *Ben Nye Co. Inc.*, BAP Nos. CC-24-1161, CC-24-116 (B.A.P. 9th Cir. April 24, 2025).

continued on page 112

from page 79

enough mass-tort judgments have been entered. By filing before the judgments reach the subchapter V threshold, the debtor can take advantage of the streamlined processes available to "small" debtors, even if they are not actually a small debtor. They simply call the debts "contingent," and seek to discharge both the current liabilities and, as in *Ben Nye*, future unliquidated liabilities as well.

The *Ben Nye* case thus exposes a fundamental policy tension. Subchapter V provides debtors with a faster, less costly path to reorganization and liability limitation, making it an appealing option for parties facing mass-tort exposure. For claimants, it carries a serious risk: Without the procedural safeguards of § 524(g), future or latent claims could be extinguished before individuals even have notice or an opportunity to assert them.

In *Ben Nye*, the trustee objected to every claim of both current and future (undiagnosed) claimants. The current claimants supplemented their proofs of claim with more detailed information about their exposure and diagnosis, and the trustee withdrew his objections. The claims of the current claimants were allowed, and they shared *pro rata* $50,000 from the pot plan.

The claims filed by future claimants were disallowed.[15] In light of the BAP's decision and the Ninth Circuit's decision in *Jensen*, future undiagnosed individuals do not have claims under § 105(5) of the Bankruptcy Code. Such potential future claims cannot be discharged before an individual receives a diagnosis. In other words, a dischargeable claim under the Code does not arise until an individual who has been exposed to a harmful substance actually gets sick. Until then, all they have is the possibility of a claim.

Questions

The *Ben Nye* decision leaves several important questions unresolved. Chief among them is whether latent asbestos injuries constitute claims under the fair contemplation test in the Ninth Circuit. Until that question is clarified, both debtors and claimants face significant legal uncertainty, leaving future victims vulnerable to having their rights extinguished before they even manifest injury.

Another open issue is whether other debtors may attempt similar subchapter V strategies in jurisdictions more favorable to the exposure-based definition of "claim," raising the specter of forum-shopping. If they do, another issue becomes whether other jurisdictions will look to the BAP opinion to hold that a debtor may not discharge future or nonexistent claims unless they fully comply with § 524(g).

The case also raises practical questions for smaller entities that cannot afford to meet the requirements of § 524(g): What options exist for such debtors to address latent asbestos liability without violating claimant rights? Finally, the decision reinforces the broader policy challenge of balancing bankruptcy efficiency and finality with the due process rights of individuals who might not yet know they are injured, a tension that courts must carefully navigate to ensure that the rights of latent mass-tort victims are protected.

Conclusion

Ultimately, while subchapter V offers debtors speed, efficiency and lower costs, it should not be used to sidestep the procedural safeguards that Congress designed for future asbestos claimants under § 524(g). Courts must recognize that efficiency and finality in bankruptcy cannot come at the expense of due process for victims whose injuries may emerge decades later.

Moving forward, bankruptcy judges, legislators and policymakers must carefully balance the interests of distressed businesses with the constitutional and equitable rights of future claimants, ensuring that mechanisms like subchapter V do not become a vehicle for extinguishing claims before justice can be meaningfully sought.

Zooming out, the *Ben Nye* case is the elephant's toenail of an elephantine problem. Mass-tort defendants nationwide have been engaged in a decades-long effort to unload their future liabilities. These are companies that used asbestos in their products, such as brake pads, gaskets, joint compounds, roofing materials and various kinds of insulation, as well as some cosmetics and other products that contain talc (which often contains asbestos). These are also companies that manufacture and distribute quartz countertops containing toxic silica that can cause silicosis. Mesothelioma and silicosis are terminal.

Having to pay sick people who you made sick hurts the bottom line of these companies, so they are spending hundreds of millions of dollars in a sophisticated and elaborate attempt to close the mass-tort spigot. They are repackaging liabilities with some cash and selling the new entity (or the old entity stripped of all the meaningful assets, or some other creative corporate maneuvering) to private equity. This is the Texas Two-Step. Or the Texas Side-Step. Or the Texas Two-Step with a Time Bomb. Regardless of what it's called, these companies would prefer to keep these externalities off their books and onto the collapsing health care system that weighs on our nation's economic health like an anvil.

These efforts should be opposed and rejected, as they were in *Ben Nye*. May it be a Bat signal in the night. Being wealthy does not make it right. If you make people sick, you should pay. abi

15 "To the extent that proofs of claim have been filed for latent asbestos injuries that do not qualify as claims, they remain subject to disallowance through the claim objection process." BAP Opinion, p. 30.

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