1995

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NOTE

WHEN A CLAIM ARISES UNDER THE BANKRUPTCY CODE

I. INTRODUCTION

In 1978, Congress enacted the Bankruptcy Reform Act in an effort to improve the effectiveness of the United States Bankruptcy Code ("Code"). There has been an ever increasing use of chapter 11 bankruptcy filings by manufacturers in an effort to discharge undiscovered, contingent and unmatured products liability claims. Debtors have proposed and sought to confirm plans establishing product liability trusts as a means of providing equal but impaired distributions to the largest possible pool of claimants and future claimants. The efforts by manufacturing debtors to enjoin and pay only a fraction of the measure of compensation to which the claimant would otherwise be entitled has led to efforts by claimants to seek rulings that pursuit of their claims outside of the bankruptcy court are not stayed. These conflicting positions have led to substantial litigation over when a particular claim arises for bankruptcy purposes and the related question of whether the claim is subject to the automatic stay which prevents the claimant from pursuing judicial remedies outside of the bankruptcy court.

The Bankruptcy Code's automatic stay is the fundamental protector of the debtor's estate and has been considered essential to the achievement of the Code's policy of providing a breathing spell for the debtor in possession en route to a "fresh start." The discussion of the automatic

2. See In re Correct Mfg. Corp., 167 B.R. 458, 459 (Bankr. S.D. Ohio 1994) (finding that problems with manufactured equipment led Correct Manufacturing to file for bankruptcy after reports of injuries and deaths resulting from the equipment); see also In re Piper Aircraft Corp., 162 B.R. 619 (Bankr. S.D. Fla.) (finding that Piper Aircraft filed for reorganization under chapter 11 with the knowledge that future problems with their products were unavoidable), aff'd, 168 B.R. 434 (S.D. Fla. 1994).

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stay in this Note is confined to 42 U.S.C. § 362(a)(1) which operates as a stay against the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title.

While the automatic stay is very broad, it is not without limitation. The scope of the stay and its application in a given case turns on the definition of "claim." The Code defines a claim as a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured." Accordingly, the key question in determining whether a particular lawsuit is subject to the automatic stay provision of 11 U.S.C. § 362(a)(1) is whether or not the claim arose prior to the petition date. The Second Circuit has stated that the legislative history of § 101(5) "surely points us in a direction, but provides little indication of how far we should travel." The issue is complicated by the interplay between bankruptcy and non-bankruptcy law—non-bankruptcy law determines the nature and existence of the right to payment, while bankruptcy law is applied to determine when that claim arose.

Recently, three dominant approaches or tests have emerged and been applied by the courts to determine when a claim arises under the Code and the applicability of the automatic stay in a given case: the non-bankruptcy law accrual test, the pre-petition conduct test, and the pre-petition relationship test.

The issue of when a claim arises is typically litigated in actions for

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5. For a more thorough discussion of the automatic stay, see 2 WILLIAM M. COLLIER, COLLIER ON BANKRUPTCY, ¶ 362.01 at 362-8 to -33 (Lawrence P. King et al. eds., 15th ed. 1991).
8. Id.
10. In re Pettibone Corp., 90 B.R. 918, 931 (Bankr. N.D. Ill. 1988) (holding that the existence or nonexistence of a claim should be determined by non-bankruptcy law); see also Vanston Bondholders Protective Comm. v. Green, 329 U.S. 156, 161 (1946).
indemnification or contribution under a contractual relationship, actions for personal injury or wrongful death in the context of products liability, and actions for regulatory compliance or to impose a penalty.

The use of three different tests leads to cross-contextual inconsistency and is analytically unnecessary because one coherent theory to determine debtor liability could be used.

Part II of this Note explores the statutory framework of the Code and argues that a coherent theoretical approach for determining when a claim arises is needed. Part III discusses and explains the common judicial approaches which have been employed to define when a claim arises under the Code. Part III also analyzes the deficiencies in each one of these approaches. Part IV proposes the following new approach which I call the Liability Rule:

(1) A claim "arises" when the right to payment first exists, as determined by non-bankruptcy law. Except:
(2) Where the non-bankruptcy law upon which the claim is predicated does not confer immediate access to the courts to enforce such right because accrual depends upon an event which is incidental to the liability, and/or which is within the control of the claimant or a third party (i.e. when there is not an "immediate" right to payment), the claim is said to be based upon a right to payment that is "unmatured" or "contingent."

The Liability Rule draws from each of the three tests currently being employed by the courts. It combines the three tests into a single coherent approach that provides a framework which leads to consistent and logical results in the contract, tort, and regulatory contexts.

Part IV also tests the Liability Rule against the existing case law and demonstrate why it is the only approach that leads to predictable results in all cases and comports with the legislative intent of the Code.

II. A STATUTORY APPROACH TO THE FRAMING OF THE QUESTION: WHEN DOES A CLAIM ARISE?

A. The Broadest Possible Definition of Claim: 11 U.S.C. 101(5)

In 1978 Congress implemented a wide variety of changes to the Code including a new definition of “claim” which is currently codified at 11 U.S.C. § 101(5). With its new definition of “claim,” Congress opted for expansive treatment, thereby eliminating the provability and allowability requirements of the Bankruptcy Act of 1898 (“Act”). The legislative history of § 101(5) makes it clear that Congress intended that all legal obligations of the debtor be subject to administration in the bankruptcy case.

The appropriate construction of § 101(5) is at the center of both the dischargeability and automatic stay debates. Much of the controversy centers around creation of a workable definition for what constitutes a contingent right to payment sufficient to constitute a claim.

While the concept of a contingent claim was not new in the 1978 amendments, analytical difficulties result when the classic definition of contingent claims litigated under the Act is applied to tort and regulatory liability. The paradigmatic example of a contingent claim

16. According to the legislative history:

The effect of the definition is a significant departure from [previous] law. . . . The definition is any right to payment, whether or not reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured. . . . By this broadest possible definition, and by use of the term throughout the title 11, . . . the [statute] contemplate[d] that all legal obligations of the debtor, no matter how remote or contingent, will be able to be dealt with in the bankruptcy case. It permits the broadest possible relief in the bankruptcy court.


18. See Elmer, supra note 17, at 274 (citing 3A WILLIAM M. COLIER, COLIER ON BANKRUPTCY § 63, at 1751-52 (James W. Moore et al. eds., 14th ed. 1975)).
19. This is not only because the definition of “claim” is broader than the definition of the term “debt” or “claim” under the former Bankruptcy Act, WEINTRAUB & RESNICK, supra note 15, ¶ 5.02,
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involves a contractual claim against the debtor by a surety, indorser, or guarantor. In this context, contingent liability becomes rooted or arises when the guarantor contracts to pay or perform when the principal defaults. The right to payment is said to be contingent because its existence depends upon the failure of the primary obligor to meet its obligation as the triggering event. In the absence of a Code definition of what constitutes a contingent claim, the courts have created a variety of definitions.

The Code defines a “claim” as any right to payment regardless of whether that right to payment is contingent, unmatured, or unliquidated. The legislative history describes the definition of a § 101(5) claim as encompassing all legal obligations of the debtor. These definitions lead to a surprisingly simple framework for understanding when a claim exists.

A claim certainly exists when the basis for the liability is fully ripe for adjudication or when there is an immediate “right to payment.” This occurs where there are no procedural or substantive impediments to adjudication in non-bankruptcy court. It is axiomatic that the right to payment exists in the contract context where the breach and damages have occurred, in the tort context where there is a fully manifested injury, and in the regulatory context where the release of the hazardous substance has occurred and response costs have been incurred by the agency.

However, a claim can exist prior to the time that the immediate right to payment exists. This occurs where the claim is based upon a

but also because the types of claims most litigated under the Act were claims by parties secondarily liable for the debtor’s obligations. Elmer, supra note 17, at 275.

20. Elmer, supra note 17, at 277.

21. Id. at 276.

22. One frequently cited definition in the contract context is:

[C]laims are contingent as to liability if the debt is one which the debtor will be called upon to pay only upon the occurrence or happening of an extrinsic event which will trigger the liability of the debtor to the alleged creditor and if such triggering event or occurrence was one reasonably contemplated by the debtor and creditor at the time the event giving rise to the claim occurred.

In re All Media Properties, 5 B.R. 126, 133 (Bankr. S.D. Tex. 1980), aff’d per curiam, 646 F.2d 193 (5th Cir. 1981).

23. See supra text accompanying note 7.


25. In re Chateaugay Corp., 944 F.2d 997, 1004 (2d Cir. 1991) (“When such costs are incurred, EPA will unquestionably have what can fairly be called a ‘right to payment.’”).
contingent, unmatured, or unliquidated right to payment.\textsuperscript{26} Under this scenario, the claim exists before the right to payment exists because the claim is one for a right to payment which will come into existence when a triggering event occurs.

Accordingly, the appropriate question in determining whether a claim exists is: At what point does the contingent or unmatured right to payment come into existence? The reason the courts have struggled with the issue is that they have failed to frame the question in this way and to understand a contingent or unmatured right to payment as a "legal obligation\textsuperscript{27} of the debtor.

The term "legal" modifies the obligation and complicates the problem because it requires the obligation to be grounded or rooted in non-bankruptcy law.\textsuperscript{28} Courts have had difficulty creating a workable analytical framework because the legal grounding in any given case is factually dependant on the substantive law which provides the basis for the claim.\textsuperscript{29} For instance, we look first to the substantive law of contract to determine the issue in that context. In the environmental regulatory context, the substantive provisions of the Comprehensive Environmental Response, Compensation, and Liability Act ("CERCLA")\textsuperscript{30} will be consulted to determine the rights and obligations created by the statute. Finally, in the tort context, we look to the substantive law upon which allegations of tort are predicated.

The term "obligation\textsuperscript{31}" makes up the second part of the definition and the point at which it comes into existence becomes the determinative factor in cases involving contingent or unmatured claims. The point at which the debtor's obligation comes into existence also must be determined by reference to the non-bankruptcy law that grounds or roots the obligation.

The contractual obligation undertaken by the surety or guarantor, for example, becomes a contingent right to payment at the time that the

\textsuperscript{27} Chateaugay Corp., 944 F.2d at 1003.
\textsuperscript{28} This term is defined as "construed or governed by the rules and principles of law, in contradistinction to rules of equity." BLACK'S LAW DICTIONARY 892 (6th ed. 1990).
\textsuperscript{29} See, e.g., In re Pettibone Corp., 90 B.R. 918, 931 (Bankr. N.D. Ill. 1988); Vanston Bondholders Protective Comm. v. Green, 329 U.S. 156 (1946).
\textsuperscript{31} Defined broadly, an obligation is a bond with a condition annexed and a penalty for non-fulfillment. See BLACK'S LAW DICTIONARY 1075 (6th ed. 1990). It can also be defined as an obligating factor that binds one to a course of action, a formal and binding agreement with an acknowledgment of liability, or something that one is bound to. Id.
obligation to pay in the event of a default on the part of primary obligor occurs.\textsuperscript{32} However, in the tort context, the legal obligation does not exist until there is an injury, even if the injury is as yet unmanifested.\textsuperscript{33} This is so because, in order for there to be an obligation that is rooted in tort law, there must be at least some injury.\textsuperscript{34} Similarly, in the regulatory context, the obligation exists with reference to the statute itself. CERCLA, for example, imposes liability upon those who release or threaten to release hazardous substances.\textsuperscript{35} Accordingly, the obligation becomes rooted in the law at the time that the potentially responsible party\textsuperscript{36} violates the constraints imposed by the statute and not at some later time, for example, when the Environmental Protection Agency ("EPA") incurs response costs.\textsuperscript{37} Defining a claim in the manner noted above strikes a balance between the legislative intent\textsuperscript{38} to define "claim" as broadly as possible, while maintaining some rational line-drawing ability that can provide the foundation of an analytical framework that can be used with consistency in the contract, tort, and regulatory contexts.

\textbf{B. 11 U.S.C. § 362(a)(1) and the Need for a Judicial Determination of When a "Claim" "Arises"}

Unlike 11 U.S.C. § 101(5), which defines "claim" without reference to timing, 11 U.S.C. § 362(a)(1) uses the petition date as a focal point for determining the applicability of the automatic stay. Close examination of the automatic stay provisions of 362(a)(1) provides further statutory

\begin{itemize}
\item \textsuperscript{32} See, e.g., In re All Media Properties, 5 B.R. 126, 133 (Bankr. S.D. Tex. 1980), aff'd per curiam, 646 F.2d 193 (5th Cir. 1981).
\item \textsuperscript{33} See, e.g., Insurance Co. of N. Am. v. Forty-Eight Insulations, Inc., 633 F.2d 1212, 1220 (6th Cir. 1980) (stating that it is the injury and not its discovery that makes the manufacturer liable in the underlying tort suit), cert. denied, 454 U.S. 1109 (1981).
\item \textsuperscript{34} The difference between the contract context and the tort context may be described as the distinction between an obligation and a duty. An obligation implies an immediate constraint imposed by circumstances, while a duty is more general. The duty that exists in the tort context is not sufficiently rooted in tort law to give rise to an obligation, and it is only when a breach of that duty results in an injury that an immediate constraint is imposed by the essential elements of tort law: duty, breach, and injury.
\item \textsuperscript{35} 42 U.S.C. § 9607(a) (1988).
\item \textsuperscript{36} See id.
\item \textsuperscript{37} See, e.g., In re Chateaugay Corp., 944 F.2d 997, 1005 (2d Cir. 1991) (holding unincurred CERCLA response costs to be claims where the release or threatened release occurs pre-petition).
\end{itemize}
guidance for the determination of when a claim comes into existence.  

Section 362(a)(1) is broken down into two distinct parts. First, a petition operates as a stay against any "action or proceeding against the debtor that was or could have been commenced" prior to the filing of the petition. This section only applies to claims that were fully ripe for adjudication or had accrued under non-bankruptcy law prior to the petition date. A petition operates as a stay against actions of this type regardless of whether the actions were pending at the time of the petition. Second, a petition operates as a stay against any action or proceeding "to recover a claim against the debtor that arose" prior to the filing of the petition. It is this broader section of the stay provision that has created much of the debate in this developing area of law.

The second facet of § 362(a)(1) is important because it adds a new and important aspect to the debate with its use of the word "arise" in connection with the petition filing date as the focal point for timing purposes. Simply stated, "claim[s]," defined as "any right[s] to payment," which "arose" prior to the filing of the petition are stayed and those that did not are outside the scope of the automatic stay. Having, already examined the meaning of "claim" and when it comes into existence, the next task is to determine when a claim arises for the purposes of the automatic stay.

It is fairly well settled that a claim arises when it first comes into existence. If this is so, the statutory relationship between §§ 101(5) and 362(a)(1) becomes apparent. A claim which is based upon an immediate right to payment will be stayed under all circumstances where it is fully ripe or is said to have accrued prior to the petition date. In

39. The author assumes that a claim arises at the same time under a given set of factual circumstances regardless of whether the inquiry is being done to determine the scope of the stay, issues of discharge, or issues of treatment.
42. 2 HOWARD J. STEINBERG, BANKRUPTCY LITIGATION §§ 12.1, 12.2 (1989).
44. The precise effect of a violation of the automatic stay in terms of whether it renders the action or proceeding "void" or "voidable" is outside the scope of this Note.
45. See, e.g., In re Thomas, 12 B.R. 452, 453 (Bankr. S.D. Iowa 1981) ("The existence of a 'claim' turns on when it arose."). But see In re Piper Aircraft Corp., 169 B.R. 766, 775-76 (Bankr. S.D. Fla. 1994) (holding that post petition pre-confirmation injury gives rise to a claim which "arose" or is deemed to have 'arisen'' prior to the petition date).
46. Under the theory advanced, the terms "acccrual" and "arise" have distinct meanings. Specifically, "acccrual" refers to the existence of an immediate right to payment under non-bankruptcy law that also constitutes a claim under § 101(5). "Arises" refers to the definition of "claim," but
the more difficult scenario, a contingent, unmatured, or unliquidated claim arises at the earliest time that the legal obligation first comes into existence, which is determined by non-bankruptcy law. It is this determination that has given courts and commentators the most difficulty and has led to the development of three different judicial analytical frameworks for determining if a "claim" exists and if so when it "arose."

III. EXPLORING THE EXISTING JUDICIAL FRAMEWORKS FOR RESOLVING THE PROBLEM

Judicial attempts to provide an analytical framework for resolving who holds a § 101(5) claim as of a given date have been created on what seems to be an ad hoc basis with courts adopting tests that either achieve a desired result or that seem to fit the facts of a particular type of case. While three tests have clearly emerged, none is adequate in and of itself. Moreover, a combination of the three is inadequate because the ability to obtain an accurate and predictable result in a given case will depend upon which version of which test is applied. Surprisingly, no standards have been clearly presented indicating which test should apply in a given substantive area much less under specific factual scenarios within a given area.

A. The Accrual Test

In re M. Frenville Co. is frequently cited as an example of a case applying the accrual test. In Frenville, the court held that the automatic stay did not apply to a third party cause of action against the debtor for contribution or indemnity that could not be filed before the

\[47. \text{Robert R. Niccolini, Note, The Voidability of Actions Taken in Violation of the Automatic Stay: Application of the Information-Forcing Paradigm, 45 VAND. L. REV. 1663, 1668 (1992) (arguing that many courts assume that the protective purposes of the stay are always "paramount"). For a glaring example, see Rick Brand, Lawyers Square Off with Fla. Judge, NEWSDAY, Jan. 5, 1994, at 18 (describing how a plaintiff and her attorney faced a $250 million sanction after refusing to drop a state court action against Piper Aircraft Corp. that was based on a post-petition crash). See Piper Aircraft, 169 B.R. at 766.}

\[48. \text{These tests are the accrual test, the conduct test, and the relationship test.}

\[49. \text{744 F.2d 332 (3d Cir. 1984), cert. denied, 469 U.S. 1160 (1985).}

\[50. \text{In re M. Frenville Co. has been cited 191 times. Search of LEXIS, Shepard's (Sept. 5, 1995).}
petition's filing date. The court distinguished the third party action at issue in the case from the classic example of a contingent claim in surety relationships. The court reasoned that in the surety context the contingent right to payment exists when the contract is signed by the parties. The court further reasoned that "while federal law controls which claims are cognizable under the Code, the threshold question of when a right to payment arises 'is to be determined by reference to state law.'" This accrual analysis which determines the issue by reference to non-bankruptcy law has been urged in the mass tort and regulatory contexts as well. Nevertheless, Frenville and the accrual test have been widely criticized. There are two major criticisms of the accrual theory to determine when a claim arises. First, the courts and commentators that have adopted the accrual test focus on the right to payment language in § 101(5) without regard to the words that modify it, e.g., contingent, unmatured, unliquidated. This focus mistakenly leads to the conclusion that a claim comes into existence at precisely the same moment that the right to payment accrues under non-bankruptcy law. For example, the court in Frenville reasoned that non-bankruptcy law determines the "threshold question" of when the right to payment arises. This ignores the fact that a claim can exist before a right to payment exists where the claim is contingent, unliquidated, or unmatured. Second, the accrual theory conflicts with the language and

51. Frenville, 744 F.2d at 335.
52. See id. at 337.
53. See id.
54. Id. (citing Vanston Bondholders Protective Comm. v. Green, 329 U.S. 156, 161 (1946)).
55. See, e.g., United States v. Union Scrap Iron & Metal, 123 B.R. 831, 836 (D. Minn. 1990) (holding that a claim for response costs under CERCLA "arises" when the EPA expends funds as a result of the discharge); In re Amatex Corp., 30 B.R. 309 (Bankr. E.D. Pa. 1983), aff'd, 37 B.R. 613 (Bankr. E.D. Pa. 1983), rev'd on other grounds, 755 F.2d 1034 (3d Cir. 1985) (consulting state law requiring manifestation of injury for accrual of cause of action in tort); Bibler, supra note 17, at 158 (urging that a tort claim must arise at the time that it accrues under non-bankruptcy law).
58. See, e.g., Bibler, supra note 17, at 161 (arguing for the application of the accrual test in the toxic tort context).
59. While the Frenville court recognized the potential of a contingent right to payment in the context of surety contract, it ruled indemnity and contribution claims with no contract to be
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obvious intent of § 362(a)(1) which stays both those proceedings which could have been commenced pre-petition and those proceedings on a claim which arose pre-petition, i.e., contingent or unmatured rights to payment which existed pre-petition. Accordingly, the accrual theory would render the second and arguably the most important aspect of § 362(a)(1) superfluous.

Because a bankruptcy claim normally comes into existence at the same time it accrues under non-bankruptcy law, the accrual theory works well in most cases. However, in circumstances where accrual of the non-bankruptcy law cause of action is in some way contingent upon a future event, the accrual theory leads to the wrong result. Delayed accrual of the non-bankruptcy cause of action can occur in the contract, regulatory, and mass tort contexts.

B. The Conduct Test

To deal with the shortcomings of the accrual test many courts have employed what has come to be known as the conduct test. A classic statement of the conduct test was made in In re Johns-Manville:

Procedural and extraneous factors such as the timing of the filing of a summons and complaint by a third party [in the case of an indemnity claim], which is not associated with the underlying nature of the cause of action . . . simply should not determine the existence or nonexistence of a “claim.” Rather the focus should be on the time when the acts giving rise to the alleged liability were performed . . . Thus, for federal bankruptcy purposes, a pre-petition “claim” may well encompass a cause of action that, under state law, was not cognizable until after the bankruptcy petition was filed.

distinguishable. 744 F.2d 332, 337 (3d Cir. 1984). This crucial distinction is where the court’s reasoning derailed. The contingent right to payment in the surety context does not exist until there is a failure of the primary obligor to perform, not at the signing of the contract, as the Frenville court decided. See Pettibone Corp. 90 B.R. at 926 (citing In re Yanks, 49 B.R. 56, 58 (Bankr. S.D. Fla. 1985)). Accordingly, the distinction between the surety case and non-contractual indemnity case makes little sense. See In re Food Barn Stores, No. 93-40012-2-11, 1994 WL 702640 (Bankr. W.D. Mo. Dec. 15, 1994).

60. Claims which could have been commenced pre-petition must have accrued under state law pre-petition. 11 U.S.C. § 362(a)(1) (1994).

61. Such claims cannot have accrued under state law until the triggering event occurs, whether it is the institution of a third party action, manifestation of an injury into a disease, or incurring of response costs in the regulatory context. See, e.g., Grady v. A.H. Robins, Co., 839 F.2d 198 (4th Cir. 1988); In re Edge, 60 B.R. 690, 700 (Bankr. M.D. Tenn. 1986).


63. Id. at 690.
The conduct test is well suited to the mass tort context where the pre-petition conduct on the part of the debtor causes an injury that does not manifest itself until post-petition or post-confirmation. Nevertheless, the conduct test has been applied outside the mass tort context. The advantage that the conduct test has over the accrual test is that, in keeping with the legislative intent of the Code, it allows for far more of the debtor's legal obligations to be administered in the bankruptcy proceeding. One drawback of the conduct test is that it does not lend itself well to line drawing on the hard cases. The criticism of the conduct test cases is that they seem to focus on the contingent, unmatured, language in the definition of "claim" without requiring that some legal obligation must exist. It could be argued that these courts are focusing on the pre-petition conduct of the debtor without regard to whether that pre-petition conduct gives rise to a legal obligation on the part of the debtor.

The only real problem with the conduct test lies in its application and failure to capture the essence of the problem which it purports to

64. See, e.g., Grady, 839 F.2d at 201-202 (tort claim arises "when the acts constituting the tort of breach of warranty . . . occurred."); In re UNR Indus., 725 F.2d 1111, 1119 (7th Cir. 1983) (no particular amount of injury is necessary to create tort liability); Insurance Co. of N. Am. v. Forty-Eight Insulations, Inc., 633 F.2d 1212, 1223 (6th Cir. 1980) (holding that there exists a clear distinction between when bodily injury occurs and when it becomes compensable), cert. denied, 454 U.S. 1109 (1981); In re Waterman Steamship Corp., 141 B.R. 552, 556 (Bankr. S.D.N.Y. 1992) (conduct in exposing employee to asbestos pre-petition gives rise to a pre-petition claim), vacated on other grounds, 157 B.IL 220 (Bankr. S.D.N.Y. 1993).

65. See, e.g., In re Jensen, 995 F.2d 925 (9th Cir. 1993) (applying the conduct test analysis to the regulatory context).

66. See criticism of accrual test supra part III.A.

67. The potential drawback of the conduct test was considered by the Second Circuit's bridge hypothetical:

Defining claims to include any ultimate right to payment arising from pre-petition conduct by the debtor comports with the theoretical model of assuring that all assets of the debtor are available to those seeking recovery for pre-petition conduct. But such an interpretation of "claim" yields questionable results. Consider, for example, a company that builds bridges around the world. It can estimate that of 10,000 bridges it builds, one will fail, causing 10 deaths. Having built 10,000 bridges, it becomes insolvent and files a petition in bankruptcy. Is there a "claim" on behalf of the 10 people who will be killed when they drive across the one bridge that will fail someday in the future? If the only test is whether the ultimate right to payment will arise out of the debtor's pre-petition conduct, the future victims have a "claim." Yet it must be obvious that enormous practical and perhaps constitutional problems would arise from recognition of such a claim.

68. But see In re Pettibone Corp., 90 B.R. 918, 932 (Bankr. N.D. Ill. 1988) (holding that "[t]he mere manufacture and sale of a defective product" does not give rise to a claim because that "act does not give rise to liability to that ultimately injured person").
solve. The conduct test leads to correct results in the mass tort context not only because the pre-petition conduct in question formed the basis of the liability, but because the contingent right to payment was created by a confluence of conduct and injury all occurring pre-petition. The conduct test in this context should more appropriately be called the tortious conduct test. Understood this way, only the pre-petition conduct of injuring the claimant gives rise to a claim that can be said to be a contingent or unmatured right to payment where the triggering event is the manifestation or discovery of the disease. Pre-petition conduct that may cause an injury in the future, such as manufacturing bridges or aircraft, lacks significant rooting in the law absent any injury at the time the pre-petition conduct takes place.

C. The Relationship Test

Finally, the recent trend is toward the use of the relationship test, where pre-petition conduct is viewed as a threshold requirement and further inquiry into the relationship between the debtor and the claimant is required. The courts which apply the conduct test appear to require some pre-petition contact, privity, impact, or exposure between the debtor and the claimant. Not surprisingly, the courts have been unclear in articulating what sort of relationship is required in a given context. This is so because the pre-petition relationship is only legally significant in a given case if it gives rise to a legal obligation on the part of the

69. See Elmer, supra note 17, at 278 (stating the All Media Properties definition, but failing to recognize the distinction between pre-petition negligent conduct giving rise to a contingent claim and the bridge hypothetical in Chateaugay).

70. By focusing on the specific type of conduct necessary to create a legal obligation, the courts applying the conduct test would have avoided much misunderstanding.

71. Conceived of in this way, the bridge hypothetical in Chateaugay is easily resolved. The pre-petition conduct of building the bridge only becomes relevant if that conduct leads to an injury pre-petition.


74. This test holds that in order for a claim to exist there must, at the very least, exist some pre-petition relationship between the debtor and the claimant. Id.


76. See Pettibone, 90 B.R. at 931-932; Piper Aircraft, 162 B.R. at 627; Lemelle v. Universal Mfg. Corp, 18 F.3d 1268, 1276 (5th Cir. 1994) (pre-petition conduct only relevant if claimant had some type of specific relationship with the debtor).

77. Pettibone, 90 B.R. at 932 ("[J]udicial construction of the breadth of § [101(5)] must be based on specific fact situations in cases presented.").
debtor at the time of the relationship. Therefore, pre-petition privity only has legal significance in the contract context where the pre-petition privity between the now debtor and guarantor provides the basis for the legal obligation. The legal obligation is the contingent right to payment which will become an immediate right to payment at the time the debtor fails to perform. Likewise, the significance of a relationship involving pre-petition exposure only applies in the tort context where the exposure is to an inherently injurious product creating a legal obligation which is a contingent or unmatured right to payment. In this context, the right to payment is contingent upon manifestation of the injury which occurred upon exposure into a disease or injury cognizable under state law. Here, the claim appropriately exists only when the exposure occurs and the exposure simultaneously creates the injury. The accrual of the immediate right to payment exists when the contingent event, manifestation of injury, occurs. Accordingly, relationship is only relevant to the extent that the relationship gives rise to a legal obligation. However, by focusing on the relationship between the parties, which by definition will include a relationship at the point that the obligation comes into existence, and not on the nature of the liability, there exists a lack of clarity in the analytical approach to resolving the § 101(5) and § 362(a)(1) issue. The result is completely ad hoc decision making without any grounding in the Code. This type of decision making will

78. Id. (where the court expressly left open the issue of "whether a party endangered by defective product pre-petition contract privity, use, or otherwise but not injured until post-petition has an unaccrued claim . . . ").
79. See In re Piper Aircraft Corp., 168 B.R. 434, 438 (S.D. Fla. 1994) ("There is absolutely no evidence in the record, nor can the Court conceive of circumstances wherein a prepetition exposure to an allegedly defective Piper aircraft or parts will result in a prepetition injury that does not manifest itself until post-petition.").
80. But see supra text accompanying note 58.
81. See the discussion of legal obligation supra text accompanying notes 28-31.
82. Compare In re Correct Mfg. Corp., 167 B.R. 458, 459 (Bankr. S.D. Ohio 1994) (explaining that the requirement of pre-petition relationship applies whatever test is used to define liability on a claim and holding pre-petition manufacture of product causing post-petition injury does not give rise to a claim pre-petition) with In re Piper Aircraft Corp., 169 B.R. 766, 775 (Bankr. S.D. Fla. 1994) (offering a modified test looking to post-petition pre-confirmation injury to conclude that a sufficient relationship existed pre-petition giving rise to claim which is stayed by 11 U.S.C. § 362(a)(1)).
83. See Piper Aircraft, 169 B.R. at 775 (applying the following ad hoc test to reach the conclusion that post-petition pre-confirmation accident victims of Piper aircraft held claims that were stayed by the automatic stay but future claimants, defined as those with injuries occurring post confirmation, did not: "an individual has a § 101(5) claim against a debtor manufacturer if (1) events occurring before confirmation create a "relationship" between the claimant and the debtor's product; and (2) the basis for liability is the debtor's prepetition conduct in designing, manufacturing and
continue until "a precise test applicable to the vast landscape of rights and interests which may be within the scope of treatment in a plan of reorganization" is articulated. 84

IV. THE LIABILITY RULE

The accrual, conduct, and relationship tests are each problematic for the reasons discussed above. The application of these tests has led to inconsistency because the adoption of one test may be satisfactory in a given context, but does not fit well when the claim issues arise in a new context. For example, the traditional concept of a contingent claim is not easily transferable to the tort and statutory context. 85 Each test fails to capture the essence of what is at issue regardless of the context. What is needed is one test that can lead to predictable and logical results in the contract, tort, and regulatory contexts. The Liability Rule can be stated as follows:

(1) A claim "arises" when the right to payment first exists, as determined by non-bankruptcy law. Except:

(2) Where the non-bankruptcy law upon which the claim is predicated does not confer immediate access to the Courts to enforce such right because accrual depends upon an event which is incidental to the liability, and/or which is within the control of the claimant or a third party (i.e. when there is not an "immediate" right to payment), the claim is said to be based upon a right to payment that is "unmatured" or "contingent."

The Liability Rule comports with the language and purpose of § 101(5) and § 362(a)(1), allowing the broadest possible definition of "claim" in furtherance of the fresh start policy, while also preventing the courts from "adopt[ing] the perspective of the character in Alice in Wonderland who opined that words meant what he intended them to mean." 86 One way to read the Liability Rule is that it is a combination of the best parts of the other three tests discussed above. The first part of the Liability Rule is essentially borrowed from the accrual test’s focus on non-bankruptcy law creating the rights and obligations while bankruptcy law determines if and how those rights and obligations are to be handled in selling the allegedly defective or dangerous product" (emphasis added)).

84. Id.
the bankruptcy case. So in the majority of the cases, where the breach of contract simultaneously results in actionable damages, or in the tort context, where the conduct causes a harm which is cognizable as a cause of action under non-bankruptcy law at the time the conduct takes place, the bankruptcy claim will “arise” when it accrues under non-bankruptcy law. The claim arises for bankruptcy purposes when the cause of action accrues not because non-bankruptcy law controls the timing of when a claim arises as it does under the accrual test, but because bankruptcy law dictates that the claim is based upon an immediate right to payment. It bears repeating that a claim can exist under the Code before an immediate right to payment exists under non-bankruptcy law because under the Code a claim can be based upon a contingent, unmatured, or unliquidated right to payment.

Accordingly, under section 1 of the Liability Rule, a claim arises when the right to payment first exists under non-bankruptcy for a majority of the cases.

Section 2 of the Liability Rule is designed to determine under what circumstances a claim should arise at a different time than when it accrues under non-bankruptcy law. In other words, section 2 addresses the “contingent and unmatured” language of § 101(5).

In the tort context a contingent or unmatured claim will arise when there is an exposure to an inherently injurious product that causes an injury, even if that injury is only microscopic and has yet to manifest itself. In the surety/indemnity context a contingent claim will “arise” before it accrues under non-bankruptcy law at the moment the primary obligor or the indemnitor fails to perform its obligations under the contract or commits the acts creating an obligation to a third party. In the regulatory context, such as under CERCLA, the claim will “arise” at the time that the release or threatened release of the hazardous substance occurs and not when response costs have been incurred. A contingent or unmatured claim arises at a different time than the cause of action accrues under non-bankruptcy law. Accordingly, pre-petition conduct is only relevant if it forms the “basis for the liability.”

87. See supra text accompanying notes 54-55.
88. This would include the bridge hypothetical in Chateaugay, the accident victims of Piper Aircraft, and the unanswered question in Pettibone.
89. See supra text accompanying notes 17-26.
91. See supra text accompanying note 30.
A. The Liability Rule in the Delayed Manifestation
Tort Cases

Although injury is an essential element of the liability conferring a right to payment on a personal injury claim, manifestation or discovery of an injury is required only to prove liability or to know of the right to recover. Because Congress has eliminated the requirement of provability,92 manifestation is reasonably considered a “contingent” event, or a “maturation” of the original injury. The injury itself, however, cannot be characterized as a “contingent” event, because no tort has occurred until the victim has suffered an injury.93 Courts employing the conduct test have recognized that a tort is composed of two elements: (1) breach of a duty by the tort-feasor resulting in (2) harm to a victim.94 They have also recognized that state laws designed to toll the running of the statute of limitations by providing a form of delayed accrual should not be dispositive of when a claim arises for bankruptcy purposes.95

In fact, many states have adopted a “discovery rule,” which delays access to the court system to enforce tort liability until such time as the extent of the damages can be proven (even where all of the elements of the liability exist or are scientifically certain to occur), and thus toll the running of the statute of limitations.96 By contrast, because Congress has eliminated the requirement of “provability” in replacing the former Bankruptcy Act with the Bankruptcy Code,97 and in light of Congress’s intention to define “claim” broadly by including “contingent” and

92. See Weintrub & Resnick, supra note 15.
93. But see In re Piper Aircraft Corp., 169 B.R. 766 (Bankr. S.D. Fla. 1994) (holding that injury occurring only post-petition arises pre-petition if it occurs pre-confirmation).
[It is the injury and not its discovery that makes the manufacturer liable in the underlying tort suit . . . . It should make no difference when the bodily injury happens to become compensable . . . . There exists a clear distinction between when bodily injury occurs and when bodily injury which has occurred becomes compensable.]
Id. at 1220-23.
95. See Keene Corp. v. Insurance Co. of N. Am., 667 F.2d 1034, 1042 (D.C. Cir. 1981), cert. denied, 455 U.S. 1007 (1982); In re UNR Indus., 725 F.2d 1111, 1119 (7th Cir. 1984).
97. In re Jensen, 995 F.2d 925, 930 (9th Cir. 1993).
“unmatured” rights to payment in the definitions of “claim,” there is not a commensurate delay in the time when a “claim” arises under the Code.

In contrast to the Frenville non-bankruptcy law accrual test, the Liability Rule, used to determine whether a claim exists pre-petition, is a perfectly logical interpretation of the meaning of claim to cover “all legal obligations of the debtor, no matter how remote or contingent.” Without stretching the meaning of a “right to payment” which “arose” prior to the filing of the bankruptcy petition to the point of absurdity, the Liability Rule affords the word “claim” its “broadest possible” interpretation, as Congress intended.

Therefore, in the delayed manifestation tort context the liability rule would yield identical results to the conduct test cases where the courts concluded that the focus should be on the conduct forming the “basis of the liability.” For example, in In re Waterman Steamship Corp. the court ruled that former Waterman employees who were exposed pre-petition to asbestos, but manifested asbestos-related diseases only post-petition, had pre-petition claims. This decision was based on the conclusion that “the claims arose at the moment the Asbestosis Claimants came into contact with the asbestos.” Thus, the “acts giving rise to the alleged liability” in Waterman consisted not simply of the improper purchase, storage or use of asbestos products, or even the employment of individuals in situations where there was a risk of exposure to the asbestos, but rather, the actual exposure of its employees to asbestos.

The Waterman court specifically did not hold that the claims arose

98. Id. at 928.
100. See id.
101. Id.
102. Id.
104. In re Johns-Manville, 57 B.R. 680, 690 (Bankr. S.D.N.Y. 1986) (“[T]he focus should be on the time when the acts giving rise to the alleged liability were performed. . . . Thus, for federal bankruptcy purposes, a pre-petition ‘claim’ may well encompass a cause of action that, under state law, was not cognizable until after the bankruptcy petition was filed.”).
106. Id. at 556.
107. See id. When the conduct test is understood as being focused on liability as opposed to conduct in and of itself, it is not susceptible to the criticism of the bridge hypothetical in Chateaugay.
at the moment Waterman negligently employed individuals in a situation in which there was a likelihood of exposure to asbestos, but rather "the moment the Asbestosis Claimants came into contact with the asbes-
tos."\textsuperscript{108} The timing of the contact was crucial in the asbestos cases because exposure to asbestos is inherently injurious.\textsuperscript{109}

Likewise, the court in \textit{In re A.H. Robins Co.}\textsuperscript{110} applied the conduct test in precisely the same manner as it was applied in \textit{Waterman}. Applying this definition to the \textit{A.H. Robins Co.} case, the court held that the right to payment arises at the time the Dalkon Shield claimant had the Dalkon Shield inserted.\textsuperscript{111} In affirming the bankruptcy court, the Fourth Circuit found that the tort claim arose "when the acts constituting the tort or breach of warranty . . . occurred."\textsuperscript{112}

However, in \textit{Grady}, the claim arose pre-petition only because all acts constituting the tort, including impact on the victim, had occurred prior to the filing of the petition.\textsuperscript{113} At the time of the petition, the plaintiff's right to payment depended solely upon manifestation, a contingent event.\textsuperscript{114}

The holding in \textit{In re Edge}\textsuperscript{115} is also consistent with the Liability Rule. The \textit{Edge} court rested its analysis on the timing of the injury.\textsuperscript{116} The fact that the injuries in \textit{Edge} occurred at the same moment as the tortious conduct on the part of the dentist-defendants should not obscure the basis of the \textit{Edge} holding: a tort claim arises when an injury occurs as a result of tortious conduct.\textsuperscript{117} Thus, because the victim's not-yet-discovered rights existed pre-petition as a result of the pre-petition injury, and despite the fact that these existing rights "were unmatured under applicable state law at the time of the petition," the \textit{Edge} court held that

\textsuperscript{108} \textit{Id.} at 556.
\textsuperscript{109} \textit{See In re Pettibone Corp.} 90 B.R. 918, 928 (Bankr. N.D. Ill. 1988) (discussing the reasoning of the delayed manifestation tort cases).
\textsuperscript{111} \textit{A.H. Robins Co.}, 63 B.R. at 993.
\textsuperscript{112} \textit{Grady v. A.H. Robins Co.}, 839 F.2d 198, 203 (4th Cir. 1988).
\textsuperscript{113} \textit{See id.} at 202-03.
\textsuperscript{114} \textit{In re Pettibone Corp.}, 90 B.R.918, 928 (Bankr. N.D. Ill. 1988).
\textsuperscript{115} \textit{In re Edge}, 60 B.R. 690, 701 (Bankr. M.D. Tenn. 1986) ("[A] claim arises at the time of the negligent act, notwithstanding that access to other courts or the running of a statute of limitation[s] may be timed from some other point in the relationship between tortfeasor and victim.").
\textsuperscript{116} \textit{Id.}
\textsuperscript{117} \textit{Id.} at 205.
the claim arose pre-petition.118

All of the claims in these tort cases “arose” at the moment the events forming the basis of the “right to payment” had occurred, even though the victims in those cases did not have immediate access to non-bankruptcy courts to vindicate their “rights to payment” because the pre-petition injuries were not yet “manifest” (i.e. not yet “provable”). Applying the Liability Rule to tort cases yields predictable results and provides a rational theoretical explanation for the divergence between state and federal law.

B. The Liability Rule in Regulatory Contexts

In Chateaugay,119 the court of appeals employed a mode of analysis similar to that used in the common law tort cases cited above. Specifically, it held that pre-petition releases of toxic chemicals by the debtor gave rise to pre-petition claims, notwithstanding the fact that those releases had not yet been discovered by the EPA.120 Notably, the court declined to hold that post-petition releases caused by the improper pre-petition storage of the toxins could give rise to a pre-petition claim.121

However, the obligation in Chateaugay is statutory and bears some similarity to the contractual obligation in the indemnity cases. In the indemnity cases, the liability of the indemnitor to the indemnitee does not create an immediate right of action in favor of the indemnitee until the latter is sued by an injured third party.122 According to the Liability Rule in CERCLA cases, the EPA cannot sue the discharger for damages until it actually incurs costs in cleaning up the discharge. In both contexts, the claim arises pre-petition when the harm giving rise to the legal obligation occurs pre-petition. Under CERCLA, the harm in question is the pre-petition release or threatened release of toxic substances.123 In the indemnity cases, the harm is the injury sustained pre-petition by the third party to whom the indemnitee is vicariously liable for the wrongful acts of the indemnitor. However, in both cases, the event which triggers the right to sue is incidental to the obligation and hence “contingent.”

118. Pettibone, 90 B.R. at 925.
119. 944 F.2d 997 (2d Cir. 1991).
120. Id. at 1000.
121. Id. at 1005.
123. In re Chateaugay, 944 F.2d at 999.
In both contexts, once the harm creating the contingent right to payment has occurred, the "trigger" which permits access to the courts to enforce the obligation is within the control of the claimant (EPA) or, in the indemnity cases, a third party. Rather than leaving the timing of a claim to manipulation by claimants or third parties, where the only remaining predicate for a right of access to the courts is incidental to the basis of the liability, a "contingent" or "unmatured" claim arises.

Thus, the Liability Rule is equally applicable to the CERCLA and indemnity cases. To the extent that the remaining condition as of the petition date (assertion of a right by a third party or clean-up undertaken by the EPA) is incidental to the liability caused by the harm, and to the extent that such condition is within the control of the claimant or a third party, a contingent or unmatured claim arises pre-petition.

V. CONCLUSION

The Liability Rule provides a coherent and analytical approach to resolve the issue of when contingent or unmatured claims arise under the Code. It resolves the logical deficiencies of the current judicial approaches. These approaches often result in inconsistent and ad hoc decisions, many of which are in direct contravention of § 101(5) and § 362(a)(1) of the Code. Application of the Liability Rule to the leading cases in each context provides principled results and demonstrates the analytical strength of the Rule relative to the other three rules currently being used.

Nevertheless, the Liability Rule may raise as many new questions and difficulties as it resolves. For example, the precise distinction between a contingent tort claim based upon common theories of negligence, and an action arising out of the same set of facts based upon breach of warranty, remains unclear. The Liability Rule seems to imply that the same transaction or occurrence could give rise to a variety of claims, each subject to different treatment under the Code. This result would certainly be undesirable as it would lead to the manipulation of pleadings for the purposes of meeting the plaintiff's objectives. Such a state of affairs would create the same uncertainty that currently exists. Nevertheless, the Liability Rule represents the best approach in light of the current statutory framework. Understanding what that framework actually is and how it works is the first step in determining whether it works the way Congress intended. During the next two years the Bankruptcy Commission will be evaluating the current statutory framework and making suggestions to Congress. It is the author's hope...
that Congress will address the issues raised in this Note and provide much needed clarity to an extremely important and complex problem.

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