

ENDING CORPORATE BANKRUPTCY ABUSE ACT OF 2024

The Problem

The “Texas Two-Step” is a recently developed abusive bankruptcy maneuver used by corporations to avoid paying out massive injury claims. The maneuver allows corporations to put their assets out of reach while miring the injury victims in bankruptcy proceedings that drag out for years. The Texas Two-Step proceeds as follows:

- 1) A corporation with a lot of injury/tort liabilities transforms into a Texas corporate entity.
- 2) The new Texas entity then undertakes a “divisive merger” that splits the corporation into two companies, one saddled with tort liabilities and containing few assets (BadCo) and the other one containing almost all of the assets and no tort liabilities (GoodCo).
- 3) BadCo immediately files for bankruptcy as a separate entity, but gets an automatic stay for both itself and GoodCo, stopping all pending litigation against them.
- 4) Injury victims now have to spend years challenging BadCo’s bankruptcy while GoodCo goes about business as usual.

Most prominently, Johnson & Johnson has [employed](#) this tactic to try to cap its liability in lawsuits claiming its talc powder caused cancer. Existing bankruptcy laws have not been adequate to stop this practice.

The Solution

The **Ending Corporate Bankruptcy Abuse Act of 2024 (ECBA)** would deter the Texas Two-Step and ensure injury victims have a chance to be heard in court. Specifically, ECBA:

- **Instructs courts to presume Texas Two-Step filings as bad-faith bankruptcies:** Courts would presume a bankruptcy has been filed in bad faith if it shows clear indicia of a Texas Two-Step bankruptcy, such as if: the debtor manufactured venue for the case; a purpose or effect of the bankruptcy filing is to gain a tactical litigation advantage, impose delay upon creditors, or cap the amount of liability even if the debtor or affiliate has sufficient funds to pay; the debtor was formed as result of a recent divisional merger; the debtor engaged in what would be considered a fraudulent transfer; or the debtor does not have a valid reorganizational purpose. The bill would also resolve a circuit outlier by standardizing to the prevailing standard of dismissing a bankruptcy for either subjective bad faith or objective futility.
- **Prohibits stays of litigation in Texas Two-Step cases:** Stays of litigation against a debtor’s non-bankrupt affiliates would be prohibited where the debtor engaged in a Texas Two-Step maneuver within the previous four years. The bill would add a Texas Two-Step exception to the Bankruptcy Code’s statutory litigation stay, which is normally triggered automatically when a debtor files for bankruptcy. This exception would ensure that, when the BadCo debtor formed in the Two-Step files for bankruptcy, the statutory stay will not block litigation against the GoodCo affiliate. This provision is narrowly scoped and would apply to Two-Step bankruptcies involving mass-tort/injury cases affecting more than 100 individuals. By carving out an exception to the statutory stay and prohibiting injunctions in Two-Step cases, this provision ensures that injury victims can get their day in court and deters corporations from abusing bankruptcy protections.