



CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

August 25, 2005

S. 852

Fairness in Asbestos Injury Resolution Act of 2005

As reported by the Senate Committee on the Judiciary on June 16, 2005

SUMMARY

S. 852 would establish the Asbestos Injury Claims Resolution Fund (the Asbestos Fund) to provide compensation to individuals whose health has been impaired by exposure to asbestos. Under the bill, the Administrator of a new Office of Asbestos Injury Claims Resolution (the Office) within the Department of Labor would administer the Asbestos Fund and manage the collection of federal assessments on certain companies that have made expenditures for asbestos injury litigation prior to enactment of this legislation. A separate Asbestos Insurers Commission would allocate other payment obligations among insurers with asbestos-related obligations in the United States. The Asbestos Fund also would absorb all private asbestos trust funds already existing at enactment. Under the bill, individuals affected by exposure to asbestos could no longer pursue awards for damages in any federal or state court and would submit claims to the Administrator, who would then evaluate such claims and award compensation according to criteria and amounts specified in the legislation.

CBO estimates that net receipts and expenditures of the Asbestos Fund would increase projected budget deficits over the 2006-2015 period by about \$6.5 billion (excluding debt service costs).

We expect that sums paid into the fund would be treated in the budget as federal revenues and that amounts expended to pay claims and administer the fund would be considered new federal direct spending. During periods when surplus amounts would be collected by the fund, CBO assumes that most of its assets would be invested in nongovernmental securities. The net cash flows associated with such investments would also be direct spending.

Over the 2006-2015 period, we estimate that payments to eligible claimants, start-up costs, investment transactions, and administrative expenses would total nearly \$70 billion. Over the same 10-year period, we estimate that the fund would collect about \$63 billion from firms and insurance companies with past asbestos liability and certain private asbestos trust funds.

Consequently, we expect the Administrator of the fund would need to exercise the borrowing authority authorized under the bill to meet the fund's obligations during this period. Assuming enactment of S. 852 by the end of calendar year 2005, CBO estimates that almost \$8 billion would be borrowed during the first 10 years.

To evaluate the long-term financial viability of the fund, CBO projected cash flows over the life of the fund—assumed to be about 50 years—using a variety of assumptions about the number, type, and timing of future claims likely to be submitted to the fund, and alternative assumptions about future inflation and interest rates. The legislation is designed to produce collections totaling about \$140 billion over the first 30 years. CBO expects that the value of valid claims likely to be submitted to the fund over the next 50 years could be between \$120 billion and \$150 billion, not including possible financing (debt-service) costs and administrative expenses. The maximum actual revenues collected under the bill would be around \$140 billion, but could be significantly less. Consequently, the fund may have sufficient resources to pay all asbestos claims over the next 50 years, but depending on claim rates, borrowing, and other factors, its resources may be insufficient to pay all such claims.

A more precise forecast of the fund's performance over the next five decades is not possible because there is little basis for predicting the volume of claims, the number that would be approved, or the pace of such approvals. Epidemiological studies of the incidence of future asbestos-related disease and the claims approval experience of private trust funds set up by bankrupt firms can be used to indicate the range of experience of the federal asbestos trust fund might face, but those sources cannot reliably indicate the financial status of the fund over such a long time period.

CBO estimates that the fund would face more than half of all anticipated claims expenses in its first 10 years, while it would receive roughly constant collections from insurers and defendant firms over its first 30 years. This conclusion is consistent with other forecasts that we have reviewed. Because expenses would exceed revenues in many of the early years of the fund's operations, the Administrator would need to borrow funds to make up the shortfall. The interest cost of this borrowing would add significantly to the long-term costs faced by the fund and contributes to the possibility that the fund might become insolvent. Under the provisions of section 405, the fund would have to stop accepting new claims (a process known as "sunset") if its current and future resources become inadequate to fulfill all existing and anticipated obligations, including its debt obligations.

Pursuant to section 407 of H. Con. Res. 95 (the Concurrent Resolution on the Budget, Fiscal Year 2006), CBO estimates that enacting S. 852 would cause an increase in direct spending greater than \$5 billion in at least one 10-year period from 2016 to 2055.

S. 852 contains two intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA), but CBO estimates that the cost of complying with those mandates would be insignificant and well below the threshold established in that act (\$62 million in 2005, adjusted annually for inflation).

S. 852 would impose new private-sector mandates, as defined in UMRA, on certain individuals filing claims for compensation for injuries caused by exposure to asbestos; certain companies with prior expenditures related to asbestos personal injury claims; certain insurance companies; trusts established to provide compensation for asbestos claims; health insurers; and persons involved in manufacturing, processing, or selling certain products containing asbestos. Based on information from academic, industry, government, and other sources, CBO concludes that the aggregate direct cost to the private sector of complying with all of the mandates in the bill would well exceed the annual threshold established by UMRA (\$123 million in 2005, adjusted annually for inflation).

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of S. 852 over the 2006-2015 period is shown in Table 1. The effects of this legislation fall within budget functions 600 (income security) and 900 (interest). CBO estimates that the bill would have little net effect on the budget over the first five years but would add about \$6.5 billion to deficits from 2011 through 2015. (The long-term budgetary impact of the bill is discussed in the section following the “BASIS OF ESTIMATE” section.)

BASIS OF ESTIMATE

For this estimate, CBO assumes that S. 852 will be enacted by the end of calendar year 2005. Based on information from the Department of Labor, we expect that the Asbestos Fund could become fully operational during fiscal year 2007 and that certain pending exigent asbestos claims would be paid by the fund in 2006.

CBO expects that the fund’s assessments on firms and insurers would be treated in the budget as revenues and that payments to satisfy claims would be considered direct federal spending. In addition, because the Administrator would be authorized to invest the fund’s balances, certain cash flows associated with investments in nongovernmental financial instruments also would be reflected in the budget. Specifically, under the Administration’s current procedures for budget presentation, government funds invested in nongovernmental financial instruments are recorded as expenses (outlays), and the redemption of such investments is recorded as a receipt (negative outlay). Under the bill, any noncash assets received from

existing private asbestos bankruptcy trust funds (such as the Manville Trust) would have no budgetary impact until they were liquidated by the Administrator. At that point, both the assets and any gains or dividends on those assets would be recorded on the budget as revenues.

TABLE 1. ESTIMATED BUDGETARY IMPACT OF S. 852

	By Fiscal Year, in Billions of Dollars									
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
CHANGES IN DIRECT SPENDING										
Claims and Administrative Expenditures of the Asbestos Fund										
Estimated Budget Authority	8.7	21.9	11.1	5.3	5.3	5.3	5.0	4.9	4.7	4.6
Estimated Outlays	8.7	5.6	8.4	9.5	10.8	6.7	5.2	5.1	5.0	4.8
Investment Transactions of the Asbestos Fund										
Estimated Budget Authority	0	1.1	0	0	-1.0	-0.2	0	0	0	0
Estimated Outlays	0	1.1	0	0	-1.0	-0.2	0	0	0	0
Total Direct Spending										
Estimated Budget Authority	8.7	23.0	11.1	5.3	4.3	5.1	5.0	4.9	4.7	4.6
Estimated Outlays	8.7	6.7	8.4	9.5	9.8	6.5	5.2	5.1	5.0	4.8
CHANGES IN REVENUES										
Collected from Defendant Firms	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
Collected from Insurer Participants	1.3	4.1	5.0	5.0	5.0	1.1	1.1	1.1	1.1	1.1
Collected from Bankruptcy Trusts ^a	4.5	0	0.4	1.6	1.6	0	0	0	0	0
Total Estimated Revenues	8.7	7.0	8.4	9.5	9.6	4.0	4.0	4.0	4.0	4.0
CHANGES IN THE DEFICIT										
Estimated Net Increase or Decrease (-) in the Deficit from Changes in Revenues and Direct Spending										
	0	-0.3	0	0	0.3	2.5	1.2	1.1	0.9	0.8

NOTE: Numbers in the table may not add up to totals because of rounding.

a. CBO estimates the total value of cash and financial assets of the asbestos bankruptcy trust funds would be \$7.5 billion in 2006 and \$8.1 billion when liquidated. The federal budget would record the cash value of those trust assets when they are liquidated by the Administrator to pay claims. CBO estimates that assets of asbestos bankruptcy trust funds would not be fully liquidated until 2010.

To estimate the cost of processing claims, CBO reviewed prior government experience with similar compensation funds and operations of privately run asbestos funds. We also discussed the potential costs of administering the fund with the Department of Labor. To estimate the number and types of claims the Asbestos Fund would receive and when they would be received, CBO reviewed a number of projections of asbestos injury claims that were prepared for different purposes by several private groups and individuals, including those developed by the Asbestos Study Group, Navigant Consulting, the National Association of Manufacturers, and Legal Analysis Systems during consideration of this bill and of similar legislation considered by the 108th Congress. In addition, we studied the history of claims paid and projections of those anticipated to be paid by the Manville Trust and considered the inaccuracy of past projections of future asbestos injury claims. Finally, to determine whether the Asbestos Fund could be expected to collect the amount of assessments from defendant companies and insurance companies that are anticipated in the legislation, CBO examined financial information for some of the public companies that would likely be contributors to the fund and the reserves held by insurance companies for asbestos claims.

Direct Spending

To estimate the amount and timing of new direct spending under S. 852, CBO considered the cost of administering the Asbestos Fund and the length of time it would take following enactment for the fund to be fully operational and processing claims. We projected the number of claims that would be submitted to the fund over the 2006-2015 period, including those claims that have been filed or will be filed in federal or state courts or with existing trusts but not settled by the time the bill is enacted (these claims are known as pending claims). To estimate the cost of paying valid claims submitted to the fund, we considered the number of claims likely to be submitted by persons with malignant and nonmalignant medical conditions due to asbestos exposure. We also estimated the net disbursements and receipts associated with the fund's investment activity. Finally, we considered the borrowing that might be required in each year in order for the fund to pay claims.

Administration and Start-up of the Asbestos Fund. Based on the cost of operating existing government compensation funds, the operation of privately run asbestos trusts, and information from the Department of Labor, CBO estimates that administration of the Asbestos Fund would require a staff of over 700 employees for the 2006-2015 period, costing a total of nearly \$1 billion over 10 years. Such administrative costs would be paid from the Asbestos Fund and would not require further appropriation action. For this estimate, CBO expects that the Office would start accepting claims in 2006, shortly after enactment. During the first three years of operation, CBO estimates that the Office would receive around

185,000 claims per year, but that this number would fall to an average of around 60,000 for the next seven years, once all currently pending claims are resolved by the fund.

Individuals seeking compensation from the Asbestos Fund would need to file a claim with the Office within the time specified by the legislation (five years from the date of enactment for pending claims or five years from the date of diagnosis for future claims). The Administrator would then have 90 days to present a proposed decision concerning the appropriate award according to the medical criteria and awards values specified in the legislation. If the claimant chooses to accept the award, the Administrator would issue a final decision, and the Asbestos Fund would pay the claimant over the next one to four years. A claimant could appeal a decision by the Administrator within 90 days of its issuance by requesting either a hearing or a review of the written record. In those cases, a decision on the appeal would be required within either 180 days or 90 days, respectively.

Under the bill, any claim pending on the date of enactment would be stayed, unless it were already before a court. Of the stayed claims, exigent claims (defined by S. 852 as those claims brought by a living claimant with either mesothelioma or less than one year to live, or by the spouse or child of a claimant who died after either filing of his or her claim or enactment of the bill) would receive the earliest attention by the Administrator. Within 60 days of receipt, the Administrator would be required to either approve or disapprove such a claim as exigent. The bill would require the Administrator to pay exigent claims within one year for cases of mesothelioma, and in no more than two years for all other exigent claims.

CBO expects that the fund would not be fully operational until at least a year following enactment of the legislation. Even after appointing an Administrator and Insurers Commission, this start-up period would be needed to promulgate detailed operating rules and procedures and to recruit, hire, and train personnel to process claims and manage the fund's operations. (The Energy Employees Occupational Illness Compensation Program—a similar federal fund serving a much smaller population—took slightly more than a year to become fully operational.) During this start-up period, the Administrator and the Insurers Commission would also need to collect financial information from thousands of firms and insurers that have made prior expenditures for asbestos injury claims to set appropriate assessment rates for those insurers and firms.

Payments to Claimants. To estimate the cost of paying compensation claims under the bill, CBO reviewed projections of asbestos injury claims that were presented to the Senate Committee on the Judiciary during its consideration of S. 852 and for similar legislation considered by the 108th Congress. Such projections were based on a combination of epidemiological data, projections of disease incidence for the affected population, historical experience of bankruptcy trusts, and projections of the number of injured that would apply for compensation given the bill's medical criteria and compensation award values.

S. 852 defines nine levels of medical impairment that persons exposed to asbestos have suffered and specifies a dollar amount of compensation that the fund would pay to individuals who demonstrate both adequate exposure to asbestos and specified medical conditions. Over time, those award values would be adjusted for inflation. For the lung cancer levels, the bill stipulates different awards, depending on whether a claimant, currently or in the past, does or does not smoke tobacco. (For example, claimants having lung cancer with asbestosis would qualify for compensation under level VIII; awards at this level would range from \$600,000 to \$1.1 million, depending on the claimant's history of tobacco use.)

To estimate the cost to the fund of compensating claimants, CBO considered four categories—future claims that would be made by individuals with malignant conditions, future claims that would be made by those with nonmalignant conditions, and claims pending on the date of enactment of the bill for both malignant and nonmalignant conditions. As detailed below, CBO used information from available projections and studies to estimate the number of claims in each category that would qualify for compensation under the medical conditions specified in the bill. Individuals who are eligible for an award would receive payments from the fund over a one- to four-year period. For this estimate, we assumed that payments for nonexigent claims would be spread equally over a four-year period. We assume that claims pending for mesothelioma at the time the bill is enacted would represent the exigent claims and would be paid in 2006.

Table 2 summarizes the number of claims and total award value for those claims that CBO projects for each category of claims under the legislation.

Pending Claims. Individuals who have an outstanding claim with any firm filed in a court on the date of enactment of S. 852 would have five years to submit a claim for compensation from the fund. CBO estimates that, over the first five years that the fund is operational, more than 320,000 pending claims would receive an award from the fund.

There is no comprehensive information regarding the numbers and types of asbestos injury claims that individuals have filed in federal and state courts or with existing trusts under current law. Nor is there reliable information on the numbers and award values of such claims that are settled each year. In 2003, Navigant Consulting prepared an estimate of the number and type of asbestos injury claims then pending in federal and state courts. That information was collected to inform the consideration of legislation similar to S. 852 in the 108th Congress.

TABLE 2. SUMMARY OF ESTIMATED ASBESTOS CLAIMS AND AWARD VALUES

	<u>Initial 10-Year Period</u>		<u>Life of Fund</u>	
	<u>Number of Claims</u>	<u>Award Value of Claims (in billions of dollars)</u>	<u>Number of Claims</u>	<u>Award Value of Claims (in billions of dollars)</u>
Pending Claims for:				
Malignant Conditions	21,000	14	21,000	14
Nonmalignant Conditions	<u>301,000</u>	<u>11</u>	<u>301,000</u>	<u>11</u>
Total Pending Claims	322,000	25	322,000	25
Future Claims for:				
Malignant Conditions	42,000	34	78,000	74
Nonmalignant Conditions	<u>620,000</u>	<u>16</u>	<u>1,184,000</u>	<u>32</u>
Total Future Claims	662,000	51	1,262,000	106
Total for All Claims	984,000	76	1,585,000	132

For this estimate, CBO used the information collected by Navigant in 2003 and adjusted the data to reflect developments since then. Using projections about the number of claims expected to be filed in 2004 and 2005 and assumptions about the pace of settlements for asbestos injury cases, we concluded that the number of pending cases in 2006 is likely to be larger than estimated in 2003—about 7 percent larger.

For this estimate, CBO did not take into account the number of claims that are still technically pending with at least one company but have been inactive for several years. If the claimants' lawyers actively seek out those individuals to file a claim against the fund, the number of claimants seeking compensation from the fund in the first four years could be significantly higher. An award from the Asbestos Fund for such individuals would be reduced by the value of any other awards received for a given claim. CBO estimates that the average award from the fund over the 2006-2015 period for pending malignant claims would be about \$650,000 and that awards for such claims would total \$14 billion. We estimate that awards for pending nonmalignant claims would average around \$38,000; total awards for those claims would be \$11 billion over the next 10 years.

Future Claims for Malignant Conditions. CBO examined several projections of malignancies associated with asbestos exposure. While all of those projections included claimants with asbestos exposure and lung cancer but with no evidence of pleural disease or asbestosis, such claimants would receive no compensation under S. 852. CBO assumes that the total number of claims for malignant conditions that would be compensated by the fund would be near the average of the various projections we examined (excluding those lung

cancer claimants who would not be eligible for compensation). Adjusting for the time that has elapsed since the performance of the studies that we examined, those studies varied from 65,000 to 100,000 claims for malignant diseases that would be compensated by the Asbestos Fund. This estimate assumes that there would be about 78,000 such claimants. We distributed those cases across the categories of malignant diseases specified in the bill based on the various projections and on the historical distributions of such claims received by the Manville Trust. On this basis, CBO estimates that the average award for malignant conditions over the next 10 years would be \$800,000 and that the total value of awards for such conditions over that period would reach \$34 billion.

Future Claims for Nonmalignant Conditions. The different projections available to CBO of the number of nonmalignant cases and their distribution among the categories specified in the bill vary greatly. CBO expects that the ratio of nonmalignant claims to malignancies under the bill would be similar to the historical ratio of claims compensated by existing bankruptcy trusts. For example, since 1995, the Manville Trust has received an average of eight claims for nonmalignant conditions for every claim for a malignant condition. Based on those historical data and because nonmalignant claimants could receive larger awards under S. 852 than those provided by existing trust funds, CBO estimates that during the first 10 years after enactment, the fund would compensate, on average, 10 new claims for nonmalignant conditions for every new malignancy (including claimants exposed to asbestos with lung cancer who would not be eligible for compensation under the bill). CBO expects that this ratio would decrease over time because of reductions in the use of and exposure to asbestos. (Other analysts have estimated the ratio of claims for nonmalignant conditions to malignancies to be as low as 7:1 or as high as 17:1.) In total, CBO anticipates about 1.2 million future claims for nonmalignant conditions.

CBO estimates that around 85 percent of claims for nonmalignant conditions filed with the Asbestos Fund would be eligible for medical monitoring reimbursement (level I) from the fund. Such reimbursement, roughly \$1,000, is the lowest rate of payment specified for nonmalignant conditions. This claims estimate is based on available research involving a sample of the exposed population with nonmalignant conditions and the history of claims filed with the Manville Trust. To evaluate the history of such claims, CBO reviewed the trust's estimate of how claims received under its 1995 trust distribution process (TDP) would have been compensated under the 2002 TDP. (The later TDP contains categories for nonmalignant conditions more similar to those under S. 852.) Overall, CBO estimates that, over the next 10 years, the average payment for nonmalignant conditions would be about \$26,000 and total awards for such conditions would amount to \$16 billion.

Investments of the Asbestos Fund. Section 222 would authorize the Administrator to invest amounts in the fund to ensure that there are sufficient sums to make payments to claimants. That section appears to imply that the fund's Administrator could invest surplus

amounts in private securities. For this estimate, CBO assumes that the managers of the fund would keep 20 percent of the investments in Treasury securities and 80 percent in non-Treasury securities. The current budgetary treatment of federal investments in non-Treasury instruments is specified in the Office of Management and Budget's (OMB's) Circular A-11, which states that the purchases of such securities should be displayed as outlays and the sales of such securities and returns, such as dividends and interest payments, should be treated as offsetting receipts or collections.

CBO estimates that investing 80 percent of fund balances in private securities would result in net receipts of \$200 million over the 2006-2015 period. The fund would make net investments in 2007, when its collections would exceed its expenditures. In subsequent years when expenditures would exceed collections, the difference would be made up by drawing down assets from the fund, starting with any assets received from other asbestos trust funds. Liquidated assets and earnings from private trust funds would be considered revenue in the federal budget, while the value of assets privately invested by the Administrator would be recorded as offsetting receipts upon liquidation.

For this estimate, CBO used its projections of the return on Treasury securities to predict investment earnings of the fund for both private securities and government securities. Although private securities may well yield higher gains over the long term, such investments carry much greater risk than government securities. The difference between projected returns on private securities and government bonds can be seen as the cost investors must be paid to bear the additional risk of holding private securities instead of government bonds. Thus, adjusted for the additional cost of risk associated with private securities, the net expected returns on private securities are the same as those on government securities.

Revenues

Receipts to the fund would come from three sources: defendant companies that have spent more than \$1 million on asbestos injury litigation, insurance companies that have made more than \$1 million in such payments, and existing private trust funds formed to settle asbestos claims. Over the life of the fund, defendant companies would be expected to contribute \$90 billion, less any credits granted for the establishment of private bankruptcy trust funds set up after July 31, 2004 (known as bankruptcy trust credits); insurance companies would be called upon to contribute just over \$46 billion, less bankruptcy trust credits. CBO is aware of one bankruptcy trust that would be eligible for such credits—the Halliburton Bankruptcy Trust. CBO estimates that the bankruptcy trust credits of defendant companies would total \$2.4 billion over the 30-year period, or \$80 million per year, with the credits being apportioned to all defendant companies based on their share of the total amounts of payments for the year. Insurers would have an estimated \$1.5 billion in bankruptcy trust

credits; those credits would go to the insurers who paid into trusts set up after July 31, 2004. All assets of existing asbestos trusts (about \$7.5 billion) would be transferred to the fund.

Defendant companies. Section 202 would specify \$90 billion, less any bankruptcy trust credits under section 222, as the amount to be collected from defendant companies. The minimum aggregate annual payment would be \$3 billion, less any bankruptcy credits. CBO estimates that annual payments would total \$2.9 billion over 30 years. For the purpose of determining each firm's contribution, each one is assigned to a tier based on its prior asbestos expenditures and whether it is in bankruptcy proceedings.

The actual amounts paid by firms might differ from that implied by their tier assignments because the bill would allow certain exemptions for small businesses and modifications of assessments, based on financial distress or inequity or based on whether a firm meets the criteria for being classified as a distributor. The bill also would allow the Administrator to increase the amount that defendants would pay if the total payments fall short of the minimum aggregate annual payment amount.

The defendants' contributions could decline over the 30-year period for two reasons. First, if more defendant companies exist and make payments than CBO estimates, the payments in the earlier years would exceed the minimum required payment. Because the aggregate payments cannot exceed \$90 billion less bankruptcy credits (or a net of \$87.6 billion), any excess amounts paid in earlier years would reduce the amounts needed to be paid in the future years. Second, the required total payments could decline in later years if the Administrator determines that full payment is not required, and each company's assessment would decline proportionately.

The amount the fund would collect from defendant companies depends on a number of unknown factors:

- The number of subject companies and the tiers into which they would fall;
- Which of those companies would be subject to exemption or modification of their contributions and whether some affiliated entities would elect to be treated separately or jointly;
- The size and nature of the assets of firms in liquidation;
- The number and characteristics of subject firms that may go into bankruptcy during the assessment period; and
- How much funding is needed to satisfy claims and other expenses of the fund.

Some sources have indicated that as many as 8,400 firms may have paid sufficient prior asbestos claims to be covered by the legislation. CBO could not verify this figure. Based on information that CBO could obtain about firms that have incurred asbestos litigation expenses, we estimate that about 1,700 defendant firms would be required to make contributions to the fund under the bill. It was possible to determine the likely tiers for about 500 of those firms. The remaining firms were assigned equally to the two lowest tiers, based on the assumption that firms with unknown tier assignments were those with lower asbestos claims payments. No reduction in the number of firms was made for those exempt due to size. Similarly, CBO made no upward adjustment to account for defendant firms not identified.

Tier I firms are firms that have filed for bankruptcy. Revenues for tier I firms expected to emerge from bankruptcy were obtained, where possible, from public sources. No reliable information could be obtained about the possible contributions of tier I firms that are likely to liquidate. Firms that securities analysts expect to earn revenues in 2006 were assumed to make the required payments, and no reduction in contribution was made for firms that would receive hardship or inequity adjustments in their contributions or for consolidated payments made by affiliated groups.

Insurers. Section 212 would specify just over \$46 billion, less any bankruptcy trust credits, as the amount to be collected from insurers over a 28-year period. In the case of insurers, no allocation or formula for payments is specified in the legislation, although the legislation does specify how much in aggregate would be collected for each of the 28 years. The bill would create an Asbestos Insurers Commission to determine an allocation among the insurance companies. The bankruptcy trust credit would represent a dollar-for-dollar reduction in the amount of liability an insurer would pay under the bill for any contributions to bankruptcy trusts established after July 31, 2004. CBO estimates that the value of the bankruptcy trust credits would be \$1.5 billion. Either the allocation determined by the Asbestos Insurers Commission or one agreed upon by the subject companies would determine how much each insurer would pay of the \$46 billion total.

S. 852 would direct insurers to contribute an aggregate initial payment of no more than 50 percent of the first year's required \$2.7 billion within 90 days after enactment. The bill would authorize the Administrator to calculate the initial payment obligations of insurers and handle other matters related to the collection of the funds. However, the initial payment amounts would not be considered final until the Insurers Commission has been formed, promulgated its allocation methodology, and issued its final determination of liability of the insurers. Based on the procedural steps specified in the bill, CBO expects that such determination would be made in fiscal year 2007.

The participating insurers would pay interest on any difference between their ultimate liability and the amount of the interim payment. Any insurers who paid more than their ultimate liability would receive interest on the excess amount. The bill specifies that the interest rate on any overpayments or underpayments would be the same rate. CBO estimates that the fund would be able to collect the initial payment from insurers by the end of fiscal year 2006 and that the demands on the fund for payments would prompt the Administrator to seek to collect the maximum allowed for the initial payment—50 percent of the first year obligation. CBO further assumes that the remaining 50 percent of the first year's payment would be collected in the second year with the associated interest and the second year's contribution.

Existing Asbestos Trust Funds. Based on publicly available information, CBO determined that the existing private trust funds set up to compensate claimants currently contain about \$7.5 billion in assets. Under the bill, those assets would be transferred to the new Asbestos Fund in the first year following enactment. Until that transfer occurs, we assume that claims paid by these funds would roughly equal investment income. The assets of existing trusts are invested in a variety of financial instruments, and only the cash and U.S. obligations in these trusts would be recorded in the federal budget as revenues of the government when transferred. The private securities in the trusts (together with any earnings) would be recorded as revenues only when converted to cash or U.S. obligations.

Based on the financial reports of the Manville Trust, CBO estimates that 56 percent of transferred trust assets (about \$4.5 billion) would be recorded as revenues in 2006. For this estimate, we assume that the remainder of the assets would only be sold as needed to finance spending in later years. The proceeds of those sales would be recorded as revenues to the fund at that time.

Offsets and Guaranteed Payment Surcharge. The bill would allow firms and insurers to reduce their individual assessments by the value of any asbestos claims paid after the enactment date of S. 852 and before 2007, when CBO expects the fund's full operations would start. It also would authorize certain payments by subject companies to guarantee collection of the mandated amounts. For the purpose of this estimate, CBO assumes that these provisions would have no net effect on annual payments by firms and insurers.

Offsets for Exigent Claims Paid During Start-up of the Fund. In the interim between enactment of S. 852 and the time when the fund would begin full operations, defendants and insurers may settle or face judgments on exigent asbestos claims that the fund is unable to process or pay. Firms and insurers could use those settlement amounts as a dollar-for-dollar offset against their assessments, reducing the payments required to be made to the fund.

Guaranteed Payment Surcharge and Guaranteed Payment Account. The Administrator of the fund could impose on each defendant participant a surcharge to offset any shortfalls in the annual aggregate payment amounts. If the payments by defendant participants exceed the minimum aggregate annual payment of \$3 billion, less bankruptcy trust credits, the excess amount, up to \$300 million, would be set aside in the guaranteed payment account as a form of self-insurance by the fund, with any excess funds being carried forward to the next year. For this estimate, CBO assumed that the Administrator would assess a surcharge on all firms when necessary. If the funds in the guaranteed payment account are insufficient to ensure that the minimum annual payment is raised in any year, the Administrator of the fund would be able to levy a guaranteed payment surcharge on the defendant participants on a pro rata basis.

Secondary Effects on Other Revenue Sources. The payments made by defendants and insurers and the sums received by claimants could affect taxable income under the federal corporate and individual income tax systems. This cost estimate includes no effects of those transactions on federal income taxes paid by claimants or businesses. Those secondary effects are likely to be insignificant in any event.

Payments made into the fund would be tax-deductible and would thus reduce the corporate income tax liability of participating firms. But in the absence of this legislation, firms would have to pay asbestos damages set in the courts, which would also be tax-deductible. It is impossible to say with any confidence whether the amounts that would be paid out by defendant firms and insurers under this legislation would be higher or lower than what they would expend in its absence through the tort system. The best assumption under the circumstances is that the bill would have no significant effect on corporate taxable income or on the government's receipts from corporate income taxes.

Similarly, the tax treatment of payments received by claimants would be unchanged from what it is now—effectively excluded from taxable income and therefore having no effect on taxes paid by individuals. There might be some reduction in income tax receipts if a significantly larger proportion of payments goes to claimants rather than to their attorneys, who would pay tax on the income. But this would depend on whether more claimants think they can navigate the new system set up under the legislation without legal assistance than is the case under the existing one—a circumstance that cannot be known. CBO expects that any change in the allocation of awards between attorneys and claimants would be too small to significantly affect income tax receipts.

BUDGETARY IMPACT OF THE ASBESTOS FUND AFTER 2015

To assess the long-term financial viability of the Asbestos Fund, CBO considered several possible projections of the fund's cash flows beyond the normal 10-year estimate of the legislation's budgetary impact. When estimating such cash flows, the provisions of section 405 are critical. That section of the bill would sunset the fund's operations by directing the Administrator to reject new claims if the fund's resources (including borrowing authority) prove inadequate to pay additional obligations. Under S. 852, claimants could seek compensation in federal courts if the fund were to sunset. In determining whether or not to sunset, the Administrator would consider the unpaid costs of any approved claims and previous borrowing against future revenues. Section 405 also would require the Administrator to return remaining assets to certain nongovernmental trust funds—but only in the event of a sunset.

CBO estimates that total receipts to the Asbestos Trust Fund over its lifetime would amount to about \$140 billion, including a small amount of interest earnings on its balances. We estimate that the fund would be presented with valid claims worth between \$120 billion and \$150 billion in addition to any financing (debt-service) costs and administrative expenses. Under the legislation, receipts to the fund would be fairly evenly distributed over its first 30 years. However, even if receipts exceed claims, CBO estimates that more than half of the fund's expenditures for claims would be paid in the first 10 years of its life. Such an imbalance between when the fund's anticipated claims payments would be made and when receipts would be collected would require the Administrator to borrow to pay claims. Under the bill, the borrowed amounts (including interest costs) would have to be repaid from the fund's own budgetary resources.

Depending upon the precise timing and value of claims presented to the fund as well as the exact revenue collected, investment returns, and interest rates, the fund might or might not have adequate resources to pay all valid claims. For example, if the value of valid claims totaled \$130 billion, interest costs on the fund's borrowing might amount to \$10 billion, and interest earned on investments could approach \$2 billion, while administrative costs would add another \$1 billion to \$2 billion. If the value of such claims were significantly more than \$130 billion, the fund's revenues might be inadequate to pay all claims.

Because of the uncertainty and sensitivity of the variables that affect the fund's balances, any long-term projection over five decades must be viewed with considerable caution. Operating the Asbestos Fund would be an entirely new governmental task, and CBO and other analysts have little basis for judging how the Administrator would implement the legislation. The discretion available to the Administrator and insurance commission with respect to the allocation of costs, provision of adjustments, and levying of surcharges makes the flows into and out of the fund hard to predict with much reliability. Furthermore, the projections that

have been made in recent decades of the number of asbestos claims likely to be filed were, in hindsight, much too low, suggesting that there might be a significant risk of underestimating the number of future asbestos claims. In addition, receipts to the Asbestos Fund would depend on the continued viability of the firms required to pay into it, which is also uncertain.

The Asbestos Fund's Operations Are Uncertain

Contributing to the uncertainty of the cost to resolve claims under the bill are some significant features of the claims process that would only be defined after enactment of the legislation. For instance, the bill would require the Institute of Medicine of the National Academy of Sciences to conduct a study to examine the causal link between asbestos exposure and cancers other than lung cancer or mesothelioma. If that study were to determine no causal link between asbestos exposure and any of those cancers, the number of claims for such conditions (level VI under the bill) could decline significantly. The bill would also require the Agency for Toxic Substances and Disease Registry (ATSDR) to conduct a study to determine if any other contaminated sites pose dangers similar to those observed in Libby, Montana. Because claimants from Libby would receive higher minimum awards than other claimants and because the bill would mandate similar treatment for any sites so identified, the costs could rise depending upon which sites might be judged similar to Libby and on how many claimants would be affected. Also, this estimate does not take into account the impact of approving any exceptional medical claims, which are claims that do not fit into the defined criteria but which might still receive compensation depending upon the findings of specific panels of physicians. It is difficult to assess how many such claims might be filed and how liberally those panels might rule on the claims.

Past Estimates of the Number and Value of Asbestos Claims Have Been Inaccurate

Forecasts of asbestos claims made over the past decade have failed to accurately predict the magnitude, scope, and evolution of asbestos claims. According to one witness that testified on similar legislation previously before the committee, "in every instance where companies or trusts have attempted to project future asbestos claims, they have always seriously underestimated."¹ Most estimates of future claims rely on a combination of epidemiological information and statistical estimation techniques using historical data. Such models contain a number of potential sources of error in forecasting.

1. Statement of Professor Eric Green, Boston University School of Law, before the Senate Committee on the Judiciary, June 4, 2003.

In 1988, experts estimated that the number of future claims against the Manville Trust would range from 50,000 to 200,000. By January of 1991, the trust had already received more than 171,000 claims. Through the summer of 2005, the Manville Trust had received 690,000 claims. The most recent claims forecast performed for the trust estimated that the trust may receive up to 1.4 million additional claims.

CBO's estimates of the number and distribution of claims that would be compensated by the Asbestos Fund under S. 852 are based on forecasts similar to those that have been prepared for the Manville Trust. Therefore, it is possible that the number of claims that would be compensated under S. 852 could deviate in significant respects from our estimates in terms of cost, timing, or both.

Revenue Collections Are Uncertain

The revenue stream that would be generated by the legislation is highly uncertain. Although the aggregate amount of the levy on defendant firms and insurers is fixed over the first 30 years, a number of factors described earlier make it difficult to project the annual receipts with much reliability.

First, identifying the defendant participants and where they would fall in the different payment tiers is difficult, if not impossible, without legislation requiring the information to be disclosed. (Tier placement directly affects the amount a defendant company would pay into the fund.) Many of the prior asbestos settlements were made outside of the court system and, as such, are not public record. This lack of information means that the number of defendant companies in each tier and the resulting payments could be either higher or lower than the numbers used in preparing this estimate.

If the number of defendants is significantly higher than assumed in this estimate and if claims remain at or about the level estimated, the likelihood of insufficient funding available to settle claims would be reduced. At the end of the first 10 years, if excess monies existed, the Administrator could decrease the payments required by the defendants by up to 10 percent. Similar stepdowns in payments could also occur after 15, 20, and 25 years should funding exceed claims levels sufficiently to warrant such a reduction.

To determine the impact of a significantly higher number of defendant companies making payments, CBO estimated the revenues and the resulting effects on cash flow if there were an additional 650 companies in each of the two lowest tiers. This scenario would result in approximately 3,000 defendant companies paying into the fund and, assuming that the number of claims projected by CBO is correct, the fund would be able to pay all claims projected by CBO and there would be no early sunset due to lack of funds to pay claims.

Conversely, significantly fewer defendant participants who meet the criteria for payments under this bill would result in higher levies on the existing defendant participants to ensure the minimum aggregate annual payment of \$3 billion less bankruptcy trust credits. This continuing drain on firms' resources could lead to more bankruptcies and even higher levies on the remaining firms.

Thirty years is a long time-span for a business. Even under ordinary conditions, economic circumstances lead many firms to liquidate over time. Normal attrition will be exacerbated by the costs of dealing with asbestos liability—either under the current system of litigation or under the legislation itself. The legislation's provisions for adjustments based on inequity or financial distress might mitigate business bankruptcies, but at the cost of even greater uncertainty in the value of the fund's future revenue stream. The legislation also would allow the Administrator to impose a surcharge to guarantee payment of amounts that some firms would be unable to pay. The success of this surcharge depends, in turn, on estimating the attrition among firms.

The bill proposes no absolute deadlines concerning the establishment of the Asbestos Insurers Commission. Some of the tasks involved in promulgating a methodology and producing final billings to the insurers are well defined and have specific time frames, while time frames for other activities are not clearly specified. CBO expects that appointing and confirming the five members and establishing the final allocation methodology for participating insurers would take at least 12 months. If the process were to take longer, it could delay the payments from insurers and possibly necessitate more borrowing than CBO has projected.

Federal Liability if the Trust Fund's Resources are Inadequate to Pay Claims

So long as the fund's Administrator does not borrow from the U.S. Treasury beyond the means of the fund to repay such borrowing, the government's general funds would not be used to pay claims. Furthermore, section 406 states that the legislation would not obligate the federal government to pay any part of an award under the bill if amounts in the Asbestos Fund are inadequate.

ESTIMATED LONG-TERM DIRECT SPENDING EFFECTS

Pursuant to section 407 of H. Con. Res. 95 (the Concurrent Resolution on the Budget, Fiscal Year 2006), CBO estimates that enacting S. 852 would cause an increase in direct spending greater than \$5 billion in at least one 10-year period from 2016 to 2055.

ESTIMATED IMPACT ON STATE, LOCAL, AND TRIBAL GOVERNMENTS

S. 852 contains two intergovernmental mandates as defined in UMRA. First, it would preempt state laws relating to asbestos claims and prevent state courts from ruling on those cases. Second, the bill would require state governments to comply with requests for information from the Asbestos Insurers Commission. CBO estimates that any cost associated with this mandate would be insignificant and well below the threshold established in that act (\$62 million in 2005, adjusted annually for inflation).

The bill would authorize \$15 million from the Asbestos Trust Fund for state, local, and tribal governments to monitor and remedy naturally occurring asbestos. Any related costs to those governments would be incurred voluntarily as a condition of receiving federal aid.

ESTIMATED IMPACT ON THE PRIVATE SECTOR

S. 852 would impose new private-sector mandates, as defined in UMRA, on:

- Certain individuals filing claims for compensation for injuries caused by exposure to asbestos;
- Certain companies with prior expenditures related to asbestos personal injury claims;
- Certain insurance companies;
- Trusts established to provide compensation for asbestos claims;
- Health insurers; and
- Persons involved in manufacturing, processing, or selling certain products containing asbestos.

Based on information from academic, industry, government, and other sources, CBO concludes that the aggregate direct cost to the private sector of complying with all of the mandates in the bill would well exceed the annual threshold established in UMRA (\$123 million in 2005, adjusted annually for inflation) during the first five years those mandates would be in effect. CBO cannot determine the direction or magnitude of the net impact of the bill's mandates on claimants, defendant companies, or insurance companies over the long term.

Asbestos Injury Claims

The bill would prohibit an individual from bringing or maintaining a civil action alleging injury due to asbestos exposure. Currently, individuals can file asbestos injury claims against any number of defendants in state or federal court. Under S. 852, individuals would only be able to receive compensation for asbestos-related injury by filing a claim with the federal Asbestos Fund established by the bill. A claimant would be able to recover from the fund if that person could meet the bill's medical criteria, which are based on the severity of the asbestos-related disease. Claims pending as of the date of enactment would be stayed, except for certain pending civil actions.

Some individuals who would receive compensation under current law would not be qualified to receive compensation under the bill. Further, some individuals would receive more compensation for their asbestos injury claims under current law, while others would receive

more if S. 852 is enacted. The direct cost of the mandate to claimants would be the difference between the total settlements and judgments that would be obtained under current law and the compensation that would be obtained by claimants under S. 852.

Based on information from academic, industry, and other sources, CBO assumes that claimants who would be deemed ineligible for compensation under the bill would be predominantly from the "unimpaired" category. Because comprehensive data relating to asbestos exposure, litigation, and compensation are not available, it is difficult to predict the number of claimants who would receive compensation and the amount of the settlements they would receive under current law. Unimpaired claimants historically receive multiple settlements of a few thousand dollars each from as many as half-a-dozen defendants. According to several expert sources, settlements for unimpaired claimants may range in value from \$3,000 to \$50,000 per claimant. Also, according to several sources, a large proportion of claims currently pending could have their settlements precluded or delayed under the bill. Further, experts predict that many individuals would probably receive less compensation in the first five years under S. 852 than under current law. Consequently, CBO expects that the direct cost to claimants of complying with this mandate could amount to hundreds of millions of dollars over the 2006-2010 period.

Assessments on Defendant Companies

Section 202 would impose a new mandate on defendant participant companies, defined in the bill as certain companies with prior expenditures related to asbestos personal injury claims. Such defendant companies would be required to pay an annual assessment to the Asbestos Fund totaling a minimum of \$3 billion in each of the first five years, less any bankruptcy trust credits. Defendant participants would be required to pay over the life of the fund a total of not more than \$90 billion, less any credits.

Section 204 would require the Administrator of the Asbestos Fund to impose a surcharge on each participant required to pay contributions into the fund to make up for any shortfalls in a given year due to nonpayment by some participants. The amount of surcharge to be paid would be determined by the Administrator. CBO expects that the Administrator would assess a surcharge on all firms sufficient to compensate for this loss and that the surcharge would be imposed differentially on defendant companies to reflect their different risks and to maintain their roughly equivalent contributions. However, CBO expects that there would be no surcharge on defendant companies during the first five years of the mandate.

The amount the fund would receive from defendant companies would depend on a number of factors, including the number of subject companies and the tiers into which they would fall. Based on data from industry and other sources, CBO estimates that the defendant

companies would pay \$2.9 billion per year into the fund over the 2006-2010 period. According to industry and academic sources, defendant companies in aggregate currently pay asbestos litigation and settlement costs on an annual basis close to the amounts that would be required by the bill in the next five years. Thus, CBO estimates that the incremental costs, if any, for those companies to comply with those mandates would not be significant over the first five years the mandates would be in effect.

Assessments on Insurance Companies

Section 212 would impose a mandate on insurers with asbestos-related obligations. The bill would require those insurance companies to contribute to the fund, and specifies that their contribution would satisfy their contractual obligation with the defendant companies to compensate claimants for injuries caused by asbestos. The bill does not, however, specify any allocation or formula for such payments to the fund. The amount of the contribution to the fund for individual insurance participants would be determined by the Asbestos Insurers Commission established under the bill.

The aggregate contributions to the fund of all participating insurers would average \$2.7 billion in the first and second year and \$5 billion in years three through five. Participating insurers would be required to pay over the life of the fund a total of \$46 billion, less any bankruptcy trust credits. Based on information from industry sources, CBO estimates that insurers would pay a total of about \$20.4 billion into the fund during fiscal years 2006 through 2010. According to industry information on asbestos liability costs, insurance companies in aggregate would have expected costs for asbestos claims under current law close to the amounts that would be required by the bill over the next five years. Thus, CBO estimates that the incremental costs for those insurance companies to comply with the mandates would not be significant over the 2006-2010 period.

Asbestos Settlement Trusts

Section 402 would require asbestos settlement trusts, established to provide compensation for asbestos claims, to transfer their assets to the Asbestos Fund no later than 90 days after the enactment of the bill. Such a requirement is an enforceable duty, and therefore, a mandate under UMRA. Based on information from the trusts and industry sources, CBO expects that such trusts would transfer approximately \$7.5 billion in assets to the fund in 2006. The cost to the trusts of the mandate for the trusts in that year would be the value of the assets net of amounts that the trusts would otherwise pay for compensation and administrative costs in that year.

Health Insurance

Section 409 would impose a private-sector mandate by prohibiting health insurers that offer a health plan from denying, terminating, or altering coverage of any claimant or beneficiary on account of participation in a medical monitoring program under this bill or as a result of any information discovered as a result of such monitoring. This mandate would have no direct cost because such a medical monitoring program does not exist under current law.

Ban on Products Containing Asbestos

Section 501 would prohibit persons from manufacturing, processing, or distributing in commerce certain products containing asbestos. The bill would require the Administrator of the Environmental Protection Agency, not later than two years after the enactment of the bill, to promulgate final regulations prohibiting commerce in such products (with some exceptions). In addition, the bill would require persons who possess a product for the purpose of commerce that is subject to the prohibition, not later than three years after the enactment of the bill, to dispose of that product by means that meet federal, state, and local requirements. A number of products and processes still use asbestos, including brake pads and linings, roofing materials, ceiling tiles, garden materials containing vermiculite, and cement products. According to industry and government sources, products are readily available to replace products containing asbestos, and the disposal of such asbestos products would not be difficult. Therefore, CBO expects that the direct cost of complying with this mandate would not be large.

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