

# INSURANCE IN THE BANKRUPTCY WORLD

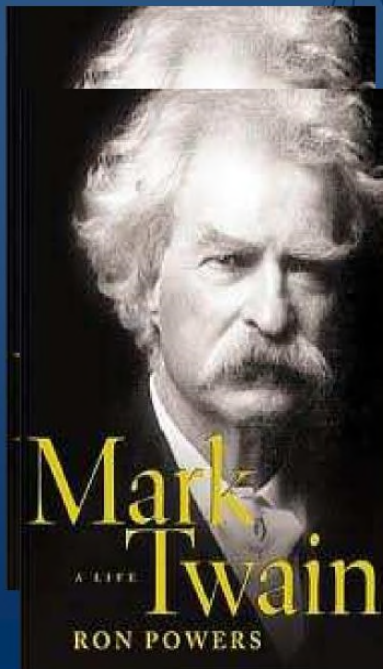
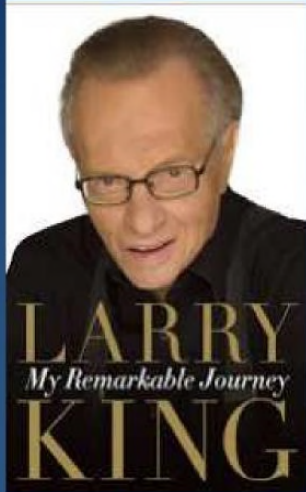
A faint, stylized image of a pair of scales of justice is visible in the background, positioned on the right side of the slide. The scales are rendered in a light blue color, matching the background, and are slightly out of focus.

**Presented by:  
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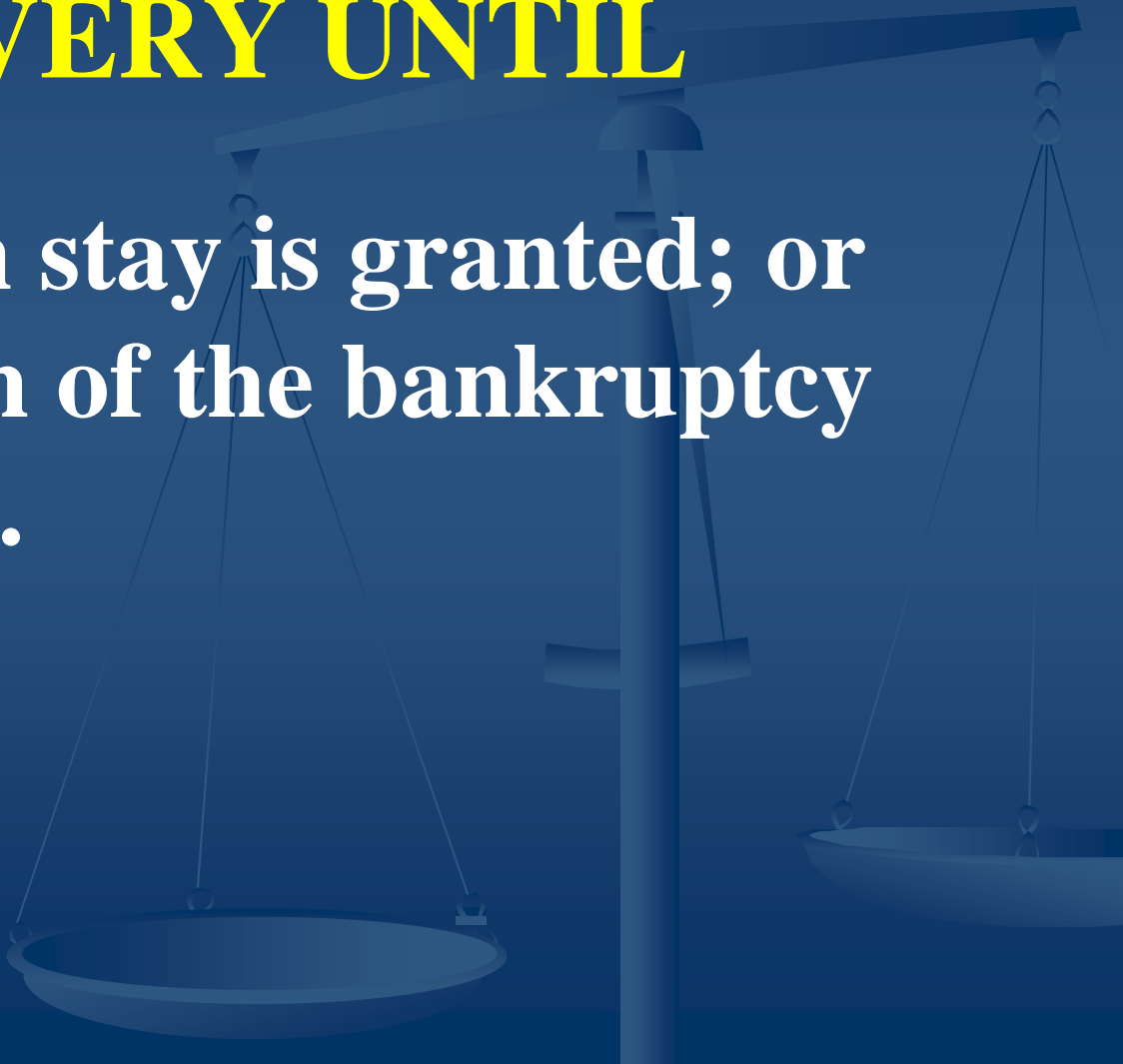
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**CHANCES ARE HIGH THAT YOU  
WILL HAVE A BANKRUPTCY  
CLAIM IN YOUR CAREER**



# **ONCE AN INSURED FILES BANKRUPTCY, THERE IS NO RECOVERY UNTIL**

- 1. Relief from stay is granted; or**
  - 2. Completion of the bankruptcy proceeding.**
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# THE AUTOMATIC STAY



## ▶ Stops:

- All requests for payment
- All collection efforts
- All litigation by non-debtors
  - The Debtor is not stayed....
  - But, most state courts will stay everything until it receives a “comfort order” from the Bankruptcy Court

# WHAT CAN YOU DO?



- **Dismiss the debtor from the litigation**
- **Sever the debtor from the litigation and continue with non-debtor parties**
- **If oral judgment has been rendered, move for entry of a judgment**
- **Move to lift, terminate, modify, or condition the automatic stay**

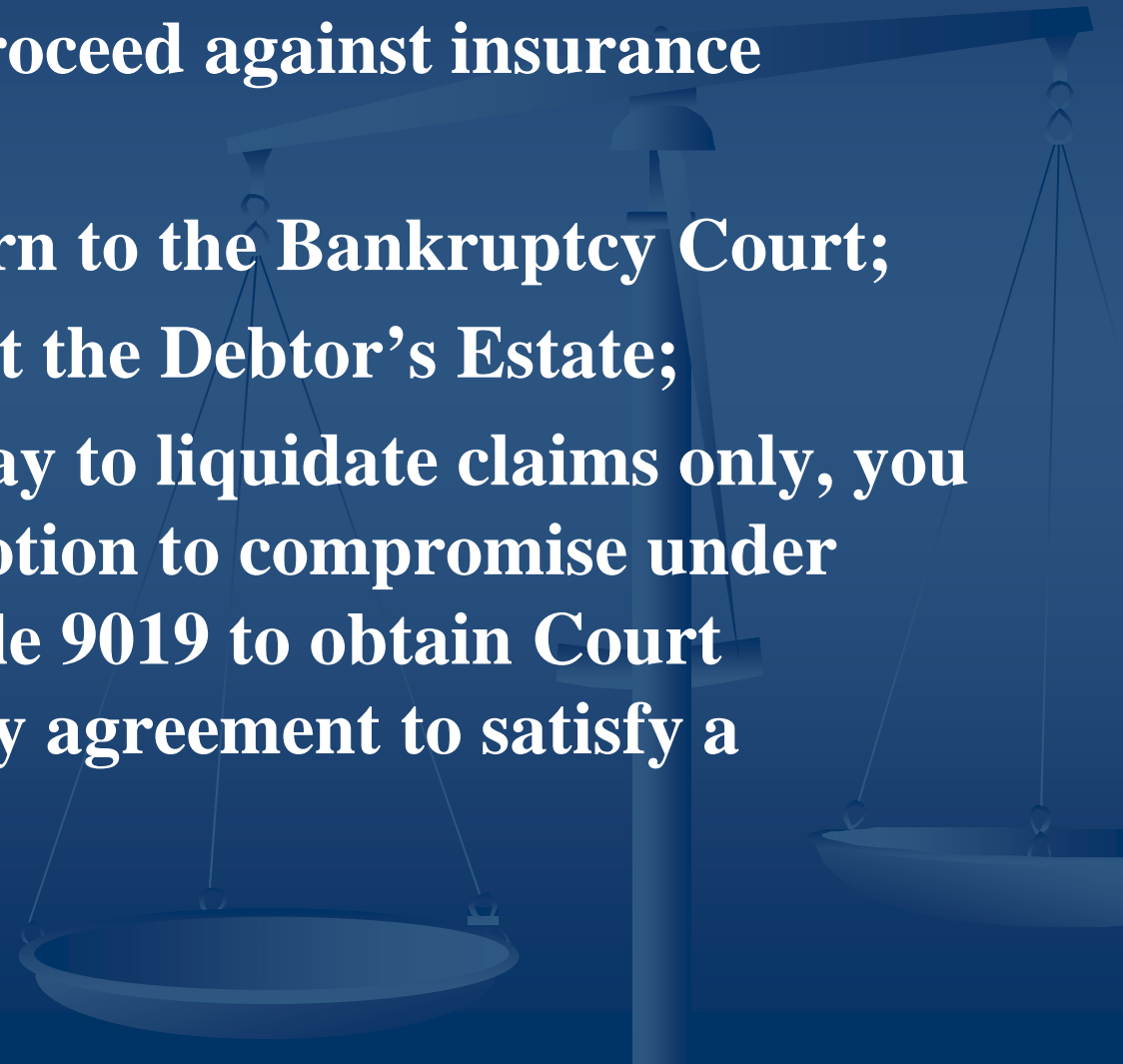
# WHAT IS NOT STAYED?

- ▶ Establishing paternity;
- ▶ Request child support;
- ▶ Stop domestic violence;
- ▶ IRS audits;
- ▶ The determination by an insurer of its obligations under a policy and acts accordingly – withdrawal of defense if the causes of action are not covered under the insurance policy

*In re Benz*, 368 B.R. 861 (9<sup>th</sup> Cir. 2007)

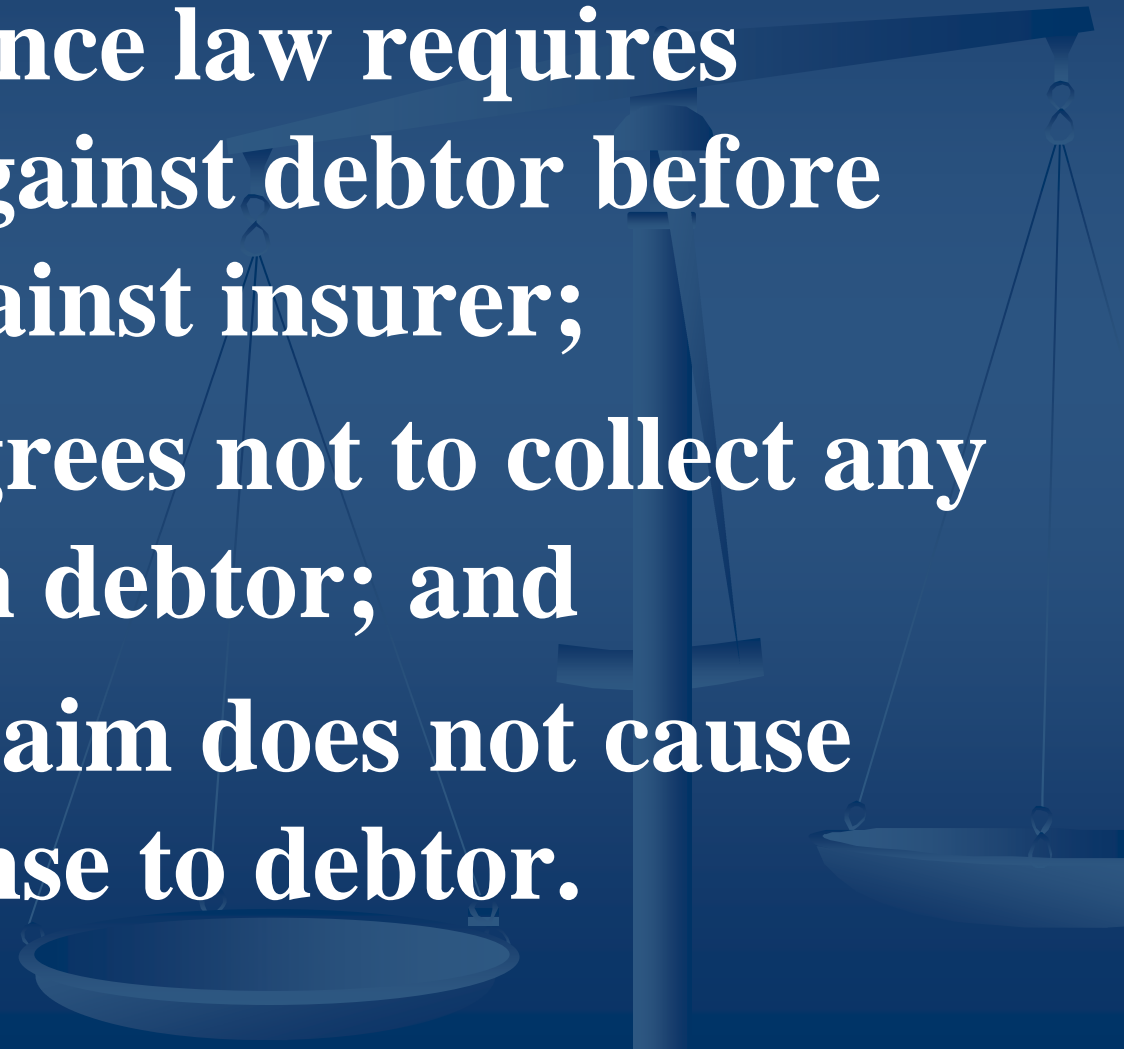
▶ For a complete listing, please review 11 U.S.C. §362(b).

# LIFTING THE STAY & INSURANCE

- Usually lifted to proceed against insurance proceeds only –
    - No need to return to the Bankruptcy Court;
    - No claim against the Debtor's Estate;
    - If you lift the stay to liquidate claims only, you have to file a motion to compromise under Bankruptcy Rule 9019 to obtain Court approval for any agreement to satisfy a judgment.
- 



# **RELIEF FROM STAY**

- 1. State insurance law requires judgment against debtor before recovery against insurer;**
  - 2. Claimant agrees not to collect any monies from debtor; and**
  - 3. Pursuit of claim does not cause undue expense to debtor.**
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# UNLIQUIDATED CLAIMS



**An unliquidated claim is one that has not been calculated or established as a specific amount**



# ADVERSARY PROCEEDING

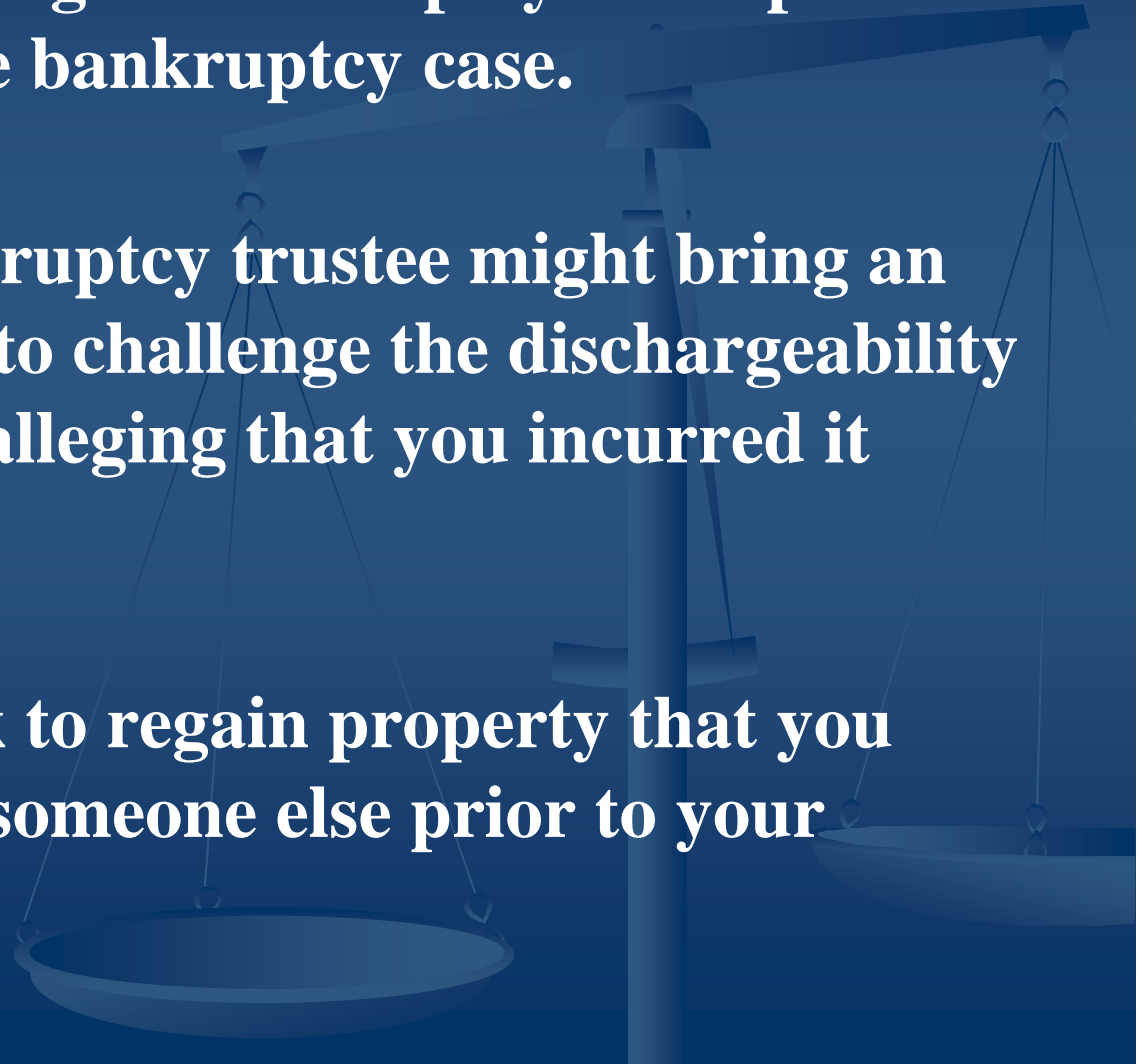


# **ADVERSARY PROCEEDING**

**An adversary proceeding in bankruptcy is a separate lawsuit filed within the bankruptcy case.**

**A creditor or the bankruptcy trustee might bring an adversary proceeding to challenge the dischargeability of a particular debt – alleging that you incurred it through fraud.**

**The trustee might seek to regain property that you transferred or sold to someone else prior to your bankruptcy.**





# **BANKRUPTCY AND *STOWERS***

253 F.3d 807  
United States Court of Appeals,  
Fifth Circuit.

In the Matter of David Lee DAVIS, Debtor.  
Safeway Managing General Agency, Inc. for State and County Mutual Fire Insurance  
Co., Appellant,  
v.  
Randolph Osherow, Trustee; James Baker, Individually and as Temporary Guardian of  
the Estate of David Baker, an Incapacitated Person; and Lele Baker, Appellees.

**Automobile insurer, whose insured had filed bankruptcy petition after being sued on claims arising from automobile accident, filed adversary proceeding, seeking declaratory judgment that no *Stowers* claim against insured under Texas law for negligently failing to settle a claim within policy limits existed or would exist in bankruptcy estate.**

253 F.3d 807  
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In the Matter of David Lee DAVIS, Debtor.  
Safeway Managing General Agency, Inc. for State and County Mutual Fire Insurance  
Co., Appellant,  
v.  
Randolph Osherow, Trustee; James Baker, Individually and as Temporary Guardian of  
the Estate of David Baker, an Incapacitated Person; and Lele Baker, Appellees.

**The United States Bankruptcy Court for the  
Western District of Texas entered judgment  
declaring that a *Stowers* claim existed and was  
part of bankruptcy estate.**



253 F.3d 807  
United States Court of Appeals,  
Fifth Circuit.

In the Matter of David Lee DAVIS, Debtor.  
Safeway Managing General Agency, Inc. for State and County Mutual Fire Insurance  
Co., Appellant,  
v.  
Randolph Osherow, Trustee; James Baker, Individually and as Temporary Guardian of  
the Estate of David Baker, an Incapacitated Person; and Lele Baker, Appellees.

**Insurer appealed, and the United States District Court held that: (1) *Stowers* claim was not part of bankruptcy estate, since no judgment was entered against debtor in underlying action until more than three years after debtor's bankruptcy case was commenced, and (2) insured did not suffer injury sufficient to support *Stowers* claim, since bankruptcy discharge relieved him from liability in excess of policy limits.**

A faint, stylized image of a balance scale is visible in the background, centered behind the text. The scale has two pans hanging from a horizontal beam, and a vertical post supports the beam. The entire scene is set against a dark blue gradient background.

**DOES THE INSURANCE  
POLICY BELONG TO  
THE BANKRUPTCY  
ESTATE?**

# Does Insurance Belong to Estate?

- When the owner of an insurance policy goes bankrupt, the policy becomes the property of the bankruptcy estate.
- Often, an insurance policy can often be considered the most important asset of the bankruptcy estate. Therefore, courts generally hold that a debtor's insurance policy becomes part of the bankruptcy estate's property upon commencement of bankruptcy proceedings.

**OWNERSHIP OF THE  
POLICY MAY NOT  
MEAN OWNERSHIP OF  
THE PROCEEDS**



# WHO OWNS THE POLICY PROCEEDS?

- While the issue of whether the policy itself becomes the property of the bankruptcy estate is relatively straightforward, less clear is the question of whether the proceeds of the policy also belong to the estate.
- In Louisiana World where a corporation formed for the purpose of organizing the 1984 World's Fair purchased directors' and officers' ("D&O") policies for personal liabilities and expenses of its directors and officers, as well as indemnification coverage for the corporation itself. *Id.* at 1393.

# WHO OWNS THE POLICY PROCEEDS?

- After the corporation filed for bankruptcy, a creditors' committee was formed and given the authority by the bankruptcy court to bring suit against the corporation, and its directors and officers. *Id.* at 1394.
- Ultimately the committee brought suit against various directors and officers of the bankrupt corporation. The committee then brought suit against the D&O insurers as well seeking a stay against payment of the directors' and officers' legal fees, claiming that such funds were part of the estate. *Id.*

# WHO OWNS THE POLICY PROCEEDS?

The Fifth Circuit held that the proceeds of the D&O coverage were not part of the estate, despite the fact that the bankrupt corporation had purchased the policy, because the policy benefited only the directors and officers, not the corporation. Therefore, the bankrupt corporation did not have any direct interest in the policy proceeds. *Id.* at 1401.

