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NEWSLETTER

Ohio Bankruptcy Court: D&O Policy Proceeds Are Not the Property of Bankrupt Corporation's Estate

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The United States Bankruptcy Court for the Northern District of Ohio has held that an insurer's payment of litigation costs to the directors and officers of a bankrupt corporation did not violate the automatic bankruptcy stay because the proceeds of the directors and officers policy are not the property of the bankruptcy estate. *Youngstown Osteopathic Hosp. Assoc. v. Ventresco (In re Youngstown Osteopathic Hosp. Assoc.)*, Adv. No. 01-4059, 2002 Bankr. LEXIS 30 (Bankr. N.D. Ohio Jan. 4, 2002).

A Chapter 11 Trustee filed an adversary proceeding against directors and officers alleging breach of fiduciary duties, negligence, fraud, misappropriation, conspiracy, misrepresentation, and civil RICO violations. The directors and officers sought coverage under their directors and officers liability policy. The insurer sought to make payments for the directors' and officers' litigation costs. In response, the debtor filed a motion seeking to enforce the automatic stay against the insurer. The debtor claimed that because the D&O policy proceeds are property of the bankruptcy estate and the debtor has a pecuniary interest in the proceeds, the insurer's payment of litigation costs would violate the automatic stay. The directors and officers opposed the motion and maintained that they own the proceeds of the policy.

The court agreed with the directors and officers, relying on *Louisiana World Exposition, Inc. v. Federal Insurance Co. (In re Louisiana World Exposition Inc.)*, 832 F.2d 1391 (5th Cir. 1987). While the bankruptcy estate may own the policy, the court determined that the proceeds of the policy are the property of the directors and officers because the company had no direct interest in those proceeds. The court distinguished *In re The Leslie Fay Companies, Inc.*, 207 B.R. 764 (Bankr. S.D.N.Y. 1997), and *Circle K Corp. v. Marks (In re Circle K Corp.)*, 121 B.R. 257 (Bankr. D. Ariz. 1990), because there was no indemnification claim, nor the possibility of such a claim arising in the *Youngstown* case. Similarly, the court distinguished *In re Sacred Heart Hospital of Norristown*, 182 B.R. 413 (Bankr. E.D. Pa. 1995), because the policy at issue in *Youngstown*, unlike *Sacred Heart*, did not provide entity coverage. The court noted, without elaboration, that the existence of entity coverage would change the court's analysis.