

ALERT

Court Grants Relief from Automatic Stay Finding that Coverage Dispute Is Not a Core Proceeding

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The United States Bankruptcy Court for the District of Nebraska, applying federal law, granted an insurer's motion for relief from an automatic stay allowing the insurer's declaratory judgment action to proceed in federal court in New York. *In the Matter of QA3 Financial Corp.*, 2011 WL 2619572 (Bkrtcy. D.Neb. July 1, 2011).

The insured, a broker/dealer engaged in the sale of securities throughout the United States, purchased a Broker/Dealer and Registered Representative Professional Liability Policy (Policy) from the insurer. Prior to its chapter 11 filing, the insured tendered a number of claims to the insurer from disgruntled investors. The insurer and insured disputed the Policy's limits. In 2010, the insured filed a declaratory judgment action against the insurer in Florida, which was later dismissed for lack of subject matter jurisdiction. In November of 2010, the insurer filed a declaratory judgment action against the insured in the United States District Court for the Southern District of New York. Shortly after answering the complaint, the insured filed for chapter 11 bankruptcy in the District of Nevada. The insurer then filed this motion for relief from an automatic stay to obtain an order allowing it to continue its pending declaratory judgment action.

In its motion, the insurer argued that New York law governed the rights of the parties under the Policy, and that the declaratory judgment action was not an attempt to obtain property or affirmative monetary relief, but solely to obtain judicial interpretation of the Policy. The court found that although "cause" is not defined in § 362(d)(1) of the Bankruptcy Code, it includes allowing litigation to proceed in another forum under appropriate circumstances.

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The insurer argued that there was cause for relief because the New York lawsuit was filed prior to the bankruptcy; the insured agreed that venue and jurisdiction were proper in New York in its answer and counterclaim; and the matter was moving toward resolution in New York. The Official Unsecured Creditors Committee (Committee) argued that the bankruptcy court was the proper venue for any litigation concerning the Policy because the Policy became property of the bankruptcy estate, and all of the individuals and entities who have an interest in the coverage have a right to notice of litigation concerning the Policy and an opportunity to intervene. The Committee argued that the interested parties will most likely not be able to intervene in the New York litigation, and therefore it is most fair to them that the litigation go forward in bankruptcy court. The debtor and the Committee also argued that an adversary proceeding, which the debtor filed in the bankruptcy court against the insurer requesting an interpretation of the contractual language, would allow for proper adjudication of the matter.

The court granted the insurer's motion for relief from the automatic stay because the litigation in New York relates to the interpretation of Policy language controlled by New York law. Furthermore, the insurer was the first to file and the Nebraska proceeding is duplicative of the New York action. The court also noted that the Policy provides that the debtor is the representatives of all parties with an interest in the Policy. Moreover, the court held that the litigation concerns a state law contract dispute, which is not a core proceeding. Lastly, the court found that the question of whether coverage exists is a separate and distinct issue from all bankruptcy issues.