IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	)	Chapter 11
	)	
DBSI, INC., et al.	)	Case No. 08-12687(PJW)
	)	
Debtors.	)	Jointly Administered
	)	
	)	
FEDERAL INSURANCE COMPANY,	)	
	)	
Interpleader-Plaintiff,	)	
	)	
v.	)	Adv. Proc. No. 09-52031(PJW)
	)	
DBSI, INC., DBSI SECURITIES CORPORATION, FOR 1031 LLC, DOUGLAS L. SWENSON, JOHN MAYERON, CHARLES E. HASSARD, WALT MOTT, THOMAS V. REEVE, JOHN D. FOSTER, FARRELL J. BENNETT, MARK ELLISON, MERRIAH HARKINS, GARY BRINGHURST, JEREMY SWENSON, DAVID SWENSON, ALLEN V. HIRSCH, JOSHUA M. HOFFMAN, WADE THOMAS, MATTHEW DUCKETT, PARIS COLE, and PARTIES UNKNOWN,	)	
	)	
Interpleader-Defendants.	)	

MEMORANDUM OPINION

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Date: June 27, 2012

WALSH, J.

This opinion concerns the question of whether James R. Zazzali ("Zazzali") and Conrad Myers ("Myers") have standing to object to the payment of certain insurance policy proceeds in this interpleader action. After reviewing briefing (Adv. Docs. ## 540, 544, 546, 547, 548, 551, 559, 560, 561, 562) from the interpleader parties, I conclude that Zazzali and Myers do not have standing to object to the disbursal of the proceeds.

Background

In November 2008, DBSI Inc. ("DBSI") and numerous affiliates (collectively with DBSI, "Debtors") filed for bankruptcy under chapter 11 of the Bankruptcy Code, 11 U.S.C. §§ 101 et seq. Zazzali was appointed as chapter 11 trustee (the "Chapter 11 Trustee") in September 2009. (Case Doc.[3] # 4375.) Debtors' plan of liquidation was confirmed in October 2010, naming Myers as liquidating trustee ("Liquidating Trustee") of the DBSI Estate Liquidating Trust and Zazzali as litigation trustee ("Litigation Trustee," and together with Liquidating Trustee, "Trustees") of the DBSI Estate Litigation Trust. (Case Doc. # 5924.)

Prior to the commencement of the bankruptcy cases, Federal Insurance Company ("Federal") issued to DBSI ForeFront Portfolio Policy Number 8169-5543 (the "Policy") offering both

[3]Docket items from the DBSI lead bankruptcy case, Case No. 08-12687 (PJW), will be referred to as "Case Doc. # X." Docket items from this interpleader action, Adv. No. 09-52031 (PJW), will be designated "Adv. Doc. # X."

directors and officers liability coverage for certain individuals and entity coverage for certain Debtors. The Policy's insuring clauses provide, in relevant part, as follows:

> **(A) Individual Non-Indemnified Liability Coverage**
> The Company shall pay Loss on behalf of the Insured Persons[4] resulting from any D&O Claim[5] first made against such Insured Persons during the Policy Period. . . for Wrongful Acts,[6] but only to the extent the Insured

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[4]"Insured Person means any past, present or future Executive or Employee of the Insured Organization." (Adv. Doc. # 8, Directors & Officers Liability Coverage Section, II(J).)

[5]"D&O Claim means:

(1) any of the following:
(a) a written demand for monetary damages or non-monetary relief;
(b) a civil proceeding commenced by the service of a complaint or similar pleading;
(c) a criminal proceeding commenced by a return of an indictment; or
(d) a formal administrative or regulatory proceeding commenced by the filing of a notice of charges, formal investigative order or similar document; against an Insured Person for a Wrongful Act, including any appeal therefrom; or
(2) a formal civil, criminal, administrative or regulatory investigation commenced by the service upon or other receipt by the Insured Person of a written notice from the investigating authority specifically identifying the Insured Person as a target individual against whom formal charges may be commenced; or
(3) a written request received by an Insured to toll or waive a statute of limitations, relating to a potential D&O Claim as described in paragraphs (1) and (2) above."

(Id., II(D).)

[6]Wrongful Act is defined as:

"(1) any error, misstatement, misleading statement, act, omission, neglect, or breach of duty committed, attempted, or allegedly committed or attempted by:
(a) For purposes of coverage under Insuring Clauses (A) and (B): any Insured Person in his or her capacity as such, or any matter claimed against any Insured Person solely by reason of his or her status as such;
(b) For purposes of coverage under Insuring Clause (C): any Insured

> Organization[7] does not indemnify the Insured Persons for such Loss[8].
>
> **(B) Individual Indemnified Liability Coverage**
> The Company shall pay Loss on behalf of the Insured Organization resulting from any D&O Claim first made against Insured Persons during the Policy Period . . . for Wrongful Acts to the extent the Insured Organization indemnifies the Insured Persons for such Loss.
>
> **(C) Corporate Liability Coverage**
> [T]he Company shall pay Loss on behalf of the Insured Organization resulting from any Insured Organization

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> Organization; or
> (c) For purposes of coverage under Insuring Clause (D): any Executive."

(Id., II(U)(1).)

[7]"Insured Organization means the Parent Company and any Subsidiary created at any time or any Subsidiary acquired on or before the inception date as [listed in the Policy declarations]. Insured Organization shall also mean any such entity as a Debtor in Possession or an equivalent status under the law of any other country." (Adv. Doc. # 8, General Terms and Conditions Section, II(H).) Insured Organizations include DBSI as the Parent Corporation and several Debtor subsidiaries. (See id. Endorsement No. 4.)

[8]"Loss means the total amount by which any Insured becomes legally obligated to pay as a result of any Claim made against any Insured for Wrongful Acts, including, but not limited to, damages . . . judgments, settlements, pre-judgment and post-judgment interest and Defense Costs. . . ." (Id., Directors & Officers Liability Coverage Section, II(L).)

> Claim[9] first made against such Insured Organization during the Policy Period . . . for Wrongful Acts.

(Adv. Doc. # 8, Directors & Officers Liability Coverage Section, I(A)-(C).) The Policy period ran from June 1, 2008 to June 1, 2010. The Policy's maximum limit of liability for all insuring clauses is $5 million. (Id., Declarations, Item 2.) On top of the maximum limit of liability, there is an additional $500,000 earmarked solely for executives, to be tapped in the event that any insurance in excess of the Policy is exhausted. (Id., Item 3.) The Policy is a "wasting policy," in that each dollar paid for one Claim[10] reduces the remaining fund available for subsequent Claims.

After the commencement of Debtors' bankruptcy cases, Federal filed this interpleader action naming as interpleader-

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[9]"Insured Organization Claim means:

(1) any of the following:

(a) a written demand for monetary damages or non-monetary relief;

(b) a civil proceeding commenced by the service of a complaint or a similar pleading; or

(c) a criminal proceeding commenced by a return of an indictment;

against any Insured Organization for a Wrongful Act, including any appeal therefrom; or

(2) a written request received by an Insured Organization to toll or waive a statute of limitations, relating to a potential Insured Organization Claim as a described in paragraph (1) above."

(Id., II(I).)

[10]"Claim," where capitalized, means an Insured Organization Claim or a D&O Claim under the Policy, as context dictates.

defendants certain Debtors including DBSI and certain employees covered by the Policy ("Individual Insureds"). (Adv. Doc. # 1.) As of the filing of the complaint in August 2009, Debtors and Individual Insureds had submitted several claims seeking insurance coverage for multiple matters related to DBSI's sale of tenant-in-common interests to investors. (Id. at 2.) Paragraph 14 of Federal's complaint lists nine matters for which Debtors and/or Individual Insureds had requested coverage. (Id. ¶ 14(a)-(i).) In the complaint, Federal states that it "reasonably believe[d] that demands for coverage will exceed the maximum aggregate limit of liability under the [Policy]" and so brought this interpleader action "for the Court to determine allocation of the Policy proceeds among those demands." (Id.) On October 28, 2009, this Court granted Federal's motion for leave to deposit the full $5.5 million into the Court's registry. (Adv. Doc. # 51.) Federal was dismissed from this action in February 2010. (Adv. Doc. # 103.)

To facilitate the coverage determinations, this Court entered a scheduling order (the "Scheduling Order") on January 27, 2010, requiring any party who wished to seek coverage under the Policy for an existing Claim to file a motion for summary adjudication by February 16, 2010. (Adv. Doc. # 77, Ex. A.) The Scheduling Order provides, in relevant part:

> "Any Party (i) asserting a right to payment of Policy proceeds relative to any claim or matter identified in paragraph 14 of the Complaint in Interpleader herein or in any Notice of New Claim for Payment of Loss filed

> herein before February 8, 2010 ("Present Claim") and (ii) either previously (a) appearing in this adversary proceeding or (b) being duly served with the Summons and Complaint herein must file by February 15, 2010[11], a motion for summary adjudication as to coverage (but not payment) under the Policy of each such Present Claim. Failure by any such Party to so file will forever bar that Party from thereafter filing a motion for summary adjudication with respect to any Present Claim, except by leave of the Court upon a showing of good cause."

(Id. ¶ 7.) Several of the Individual Insureds filed motions for partial summary judgment asking this Court to determine whether or not their Claims were covered under the Policy. (Adv. Docs. ## 84, 87, 92, 101, 104, 107.) Individual Insureds sought coverage for, inter alia, a civil action for state securities law violations commenced on January 14, 2009 by the State of Idaho Department of Finance against Douglas Swenson (one of the Individual Insureds) and several Debtors (the "Idaho Action"); a civil action filed against several Individual Insureds and Debtors by the Myles W. and Jannelle S. Spann Trust (the "Spann Trust Action"); and a special investigation of several Individual Insureds and Debtor DBSI Securities Corporation by the Financial Industry Regulatory Authority (the "FINRA Investigation").

The Chapter 11 Trustee also filed a motion for partial summary judgment seeking coverage for "Loss and Defense Costs resulting from the Idaho Complaint, the Examiner Motion, and the

[11]Because February 15, 2010 fell on a federal holiday, the parties were permitted to file their motions on February 16, 2010.

Examiner's investigation." (Adv. Doc. # 105, ¶ 2.) The Idaho Complaint, as defined by the Chapter 11 Trustee, is the complaint filed by the State of Idaho to commence the Idaho Action. Soon after commencing the Idaho Action, the State of Idaho filed a motion (the "Examiner Motion") in this bankruptcy case seeking the appointment of an examiner (the "Examiner"). (Case Doc. # 1276.) Debtors commenced an adversary proceeding (Adv. No. 09-50190 (PJW)) in this Court seeking a stay of the Idaho Action while the bankruptcy cases were pending. Debtors and the State of Idaho subsequently agreed that the Idaho Action would be stayed if this Court appointed the Examiner. (Adv. Doc. # 105 ¶ 10.) This Court granted the Examiner Motion. (Case Doc. # 3207.) The Examiner, who was appointed to investigate transactions between Debtors, non-debtors, and certain insiders, prepared two reports for the Court and incurred more than $3.6 million in fees and expenses (the "Examiner Fees").

In his motion for partial summary judgment, the Chapter 11 Trustee asserted that the Idaho Complaint and Examiner Motion were Insured Organization Claims. Additionally, the Chapter 11 Trustee argued that the Examiner Fees "result[ed] from the Idaho Complaint and the Examiner Motion" and thus were covered Loss under the Policy. (Adv. Doc. # 105 ¶ 37.) The Chapter 11 Trustee also claimed that costs and expenses incurred in cooperating with the Examiner's investigation and in "responding to the Idaho Complaint

and opposing the Examiner Motion" were covered as Defense Costs (Id. ¶ 36, 39.) Lastly, the Chapter 11 Trustee requested coverage for costs incurred in connection with the FINRA Investigation. (Id. ¶ 40.)

On March 17, 2010, the Court heard extensive arguments from the parties relative to the coverage issues and ruled from the bench on them. The Court invited counsel to submit a detailed form of order. The Court entered an order drafted by the parties on certain of the Individual Insureds' motions and the Chapter 11 Trustee's motion on May 25, 2010 (the "May 25 Order"). (Adv. Doc. # 160.) The Order denied the Chapter 11 Trustee's and Individual Insureds' motions "to the extent that they [sought] coverage under the Policy, as either Defense Costs or Loss, for any and all fees and costs incurred in connection with the [Examiner's investigation and preparation of reports]." (Id., at 3, ¶ 1.) Further, the Order provided that the Idaho Action was an Insured Organization Claim but reserved decision on whether the Spann Trust Action and the FINRA Investigation were covered under the Policy. (Id. ¶¶ 15, 18.) Certain of the litigants, including the Chapter 11 Trustee, have appealed the May 25 Order to the District Court. (Adv. Nos. 1:10-cv-00655-GMS, 1:10-cv-00656-GMS, 1:10-cv-0067-GMS, 1:10-cv-00682-GMS.)

In February 2011, some of the Individual Insureds filed additional motions for partial summary judgment regarding later

Claims arising from two adversary actions, herein the "Avoidance Action" and the "RICO Action," commenced by the Litigation Trustee after the Policy Period terminated on June 1, 2010. (Adv. Doc. # 303.) The Litigation Trustee opposed the motion, arguing that the RICO and Avoidance Actions were excluded by the Policy and could not be covered because the Actions were commenced after the Policy Period had ended. (Adv. Doc. # 341.) This Court determined that those actions were covered with respect to certain defendants under the Policy's "related claims" provision and were not excluded by the Policy's terms. (Adv. Doc. # 386.) The Litigation Trustee filed a motion for reconsideration of the order granting coverage, which is currently pending before the Court. (Adv. Doc. # 418.)

There are several other motions for partial summary judgment on the issue of coverage pending in this Court. At a hearing on one such motion on March 7, 2012, I asked the parties to submit briefing on whether Trustees still have standing to participate in this interpleader dispute. Several of the parties (Trustees and Individual Insureds Douglas Swenson, Charles Hassard, Thomas Var Reeve, John Mayeron, David Swenson, Jeremy Swenson, and Gary Bringhurst) submitted briefing on the matter.

Following completion of briefing, Litigation Trustee submitted a request for disbursement of proceeds to cover Defense Costs incurred in defending the Idaho Complaint and the Examiner Motion. At a June 25, 2012 hearing on Litigation Trustee's

submission, I denied recovery for any Defense Costs other than those incurred in defending the Idaho Complaint and specifically denied reimbursement of fees related to the Examiner Motion. Upon review by this Court, the amount of $72,033.50 was disbursed to the estates to cover the Defense Costs for the Idaho Complaint. The Court will now consider whether Trustees, as representatives of the estate, have any remaining interest in the balance of the proceeds.

Discussion

In order for Trustees to have standing in this interpleader action, they must demonstrate some "legally protected interest that either has been adversely affected (thereby warranting judicial relief) or that is in actual danger of being adversely affected (if relief is not granted)." In re W.R. Grace & Co., --- B.R. ---, 2012 WL 2130981, at *86 (D. Del. June 11, 2012) (citation and internal quotation marks omitted). Accord In re Global Indus. Techs., 645 F.3d 201, 210 (3d Cir. 2011) (adopting the Seventh Circuit's view that a party in interest in a bankruptcy case is "'anyone who has a legally protected interest that could be affected by a bankruptcy proceeding'") (citation omitted). Put another way, Trustees must demonstrate "some injury-in-fact, i.e., some specific, 'identifiable trifle' of injury or personal stake in the outcome of the litigation." Id. at 211 (citations and internal quotation marks omitted).

Trustees proffer three bases for standing: 1) that the Policy proceeds are property of the estate; 2) that the pending appeal of the May 25 Order denying coverage for the Examiner Fees entitles them to protect the proceeds from disbursal in case this Court's order is reversed; and 3) that the Litigation Trustee's status as plaintiff in the RICO and Avoidance Actions give Trustees an interest in the proceeds, which may be used by the insured defendants in those actions to pay any judgment or settlement in favor of the Trusts. The short answer to these assertions is: 1) the remainder of the proceeds are not property of the estate because entity coverage no longer exists; 2) the request of Trustees for coverage of the Examiner's Fees has been denied, is now the law of the case, and therefore Trustees will be entitled to those proceeds only if the District Court reverses and remands with directions to rule in favor of Trustees; 3) only the insured defendants have rights of coverage in the RICO and Avoidance Actions, and Trustees have no rights in the Policy unless and until the defendants seek proceeds with respect to any judgments in favor of Trustees. I will consider each of Trustees' arguments in further detail below.

Proceeds as Property of the Estate

Trustees argue that the proceeds are property of the estate, and as they have a fiduciary duty to maximize the value of

the Litigation and Liquidating Trust assets, Trustees have standing to object to the distribution of proceeds to the Individual Insureds.

Under section 541 of the Bankruptcy Code, the estate is comprised of "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1) (2005). Most cases, including several in this District, hold that the debtor's liability insurance policy is property of the estate. See, e.g. In re Downey Fin. Corp., 428 B.R. 595, 603 (Bankr. D. Del. 2010); In re Allied Digital Techs., Corp., 306 B.R. 505, 509 (Bankr. D. Del. 2004). Whether the proceeds of the policy – as separate from the policy itself – are property of the estate is a more complicated question, and depends on the "language and scope of the policy at issue." Allied, 306 B.R. at 509. Where the policy provides direct coverage to both the debtor and to officers and directors, "the proceeds will be property of the estate if depletion of the proceeds would have an adverse effect on the estate to the extent the policy actually protects the estate's other assets from diminution." Id. at 512. The debtor must have existing covered claims under the policy, and coverage must be more than merely "hypothetical or speculative." Id. In other words, where the debtor is no longer covered by the policy, the "policy proceeds no longer constitute property of the bankruptcy estate." Id. at 511.

Trustees' central argument is that the proceeds are property of the estate because the funds may be payable to the estate in connection with several Claims against the estate, including the "more than 10,000 proofs of claim against DBSI that have not yet been resolved." (Adv. Doc. # 551, at 2.) Trustees also point to an oral ruling by this Court, made on October 19, 2009 that, at the time, the estate had an interest in the proceeds because several of the Debtors were named as defendants in the Spann Trust Action, the Idaho Complaint, and the FINRA Investigation. Trustees argue that the Spann Trust Action, the FINRA Investigation, the Idaho Complaint, and the proofs of claim are covered Claims and that any Loss incurred as a result of those Claims would be payable from the Policy proceeds.

As a preliminary matter, it must be established what qualifies a Claim for coverage. Under the Policy, a Claim must first fit the definition of an Insured Organization Claim or a D&O Claim, as applicable, and must not be excluded by any of the Policy exclusions. Second, the insured party must submit notice of the Claim. Under the Policy terms, the insured was required to notify Federal as soon as practicable after the Claim was made against the insured. (Adv. Doc. # 8, General Terms and Conditions Coverage Section, Endorsement No. 1.) Once this interpleader action was commenced, any insured party who wished to submit a Claim existing as of February 8, 2010, was required to file a motion for summary

judgment to preserve his/her/its rights under the Policy. (Adv. Doc. # 77, Ex. A, at ¶ 7.) Finally, since the Policy Period terminated in June 2010, the Policy only covers Claims made against an insured prior to that date.

In order for any of the potential Claims cited by Trustees to be covered under the Policy, such Claim must meet all three of the criteria above. I will consider each potential Claim in turn.

The Spann Trust Action

Trustees allege that, as several Debtors were named as defendants in the Spann Trust Action, the Policy proceeds may be payable for Defense Costs or any Loss resulting from the suit. In so arguing, however, Trustees omit one key fact: neither Trustee has ever sought a determination that the Spann Trust Action was a covered Insured Organization Claim in this interpleader action. Under the terms of the Scheduling Order, any party who wished to assert a right to receive Policy proceeds in connection with any Claim existing as of February 8, 2010 was required to file a motion for summary adjudication in this interpleader proceeding. (Adv. Doc. # 77, Ex. A, ¶ 7.) Failure to do so forever barred the party from asserting the right to payment at a later date. (Id.) Trustees filed only one motion for partial summary judgment in this interpleader (Adv. Doc. # 104); the motion made no mention of the

Spann Trust Action. Consequently, Trustees cannot now argue that the Spann Trust Action is a covered Insured Organization Claim.

Furthermore, according to information supplied by Douglas Swenson's counsel, the Spann Trust Action has been inactive since it was filed on October 27, 2008. (Adv. Doc. # 475.) In addition, the Spann Trust could not pursue its complaint against the estates because of the § 362 automatic stay, which stay is still in effect.

FINRA Investigation

Trustees next allege that the FINRA Investigation may entitle them to proceeds from the Policy. This argument fails for two reasons.

First, the FINRA Investigation does not fit the definition of an Insured Organization Claim and thus could not possibly be covered. The definition of an Insured Organization Claim under the Policy is:

> (1) any of the following:
> (a) a written demand for monetary damages or non-monetary relief;
> (b) a civil proceeding commenced by the service of a complaint or a similar pleading; or
> (c) a criminal proceeding commenced by a return of an indictment;
> against any Insured Organization for a Wrongful Act, including any appeal therefrom; or
> (2) a written request received by an Insured Organization to toll or waive a statute of limitations, relating to a potential Insured Organization Claim as a described in paragraph (1) above.

(Adv. Doc. # 8, Directors & Officers Liability Coverage Section, II(I)). In contrast, the definition of a D&O Claim is:

> (1) any of the following:
> (a) a written demand for monetary damages or non-monetary relief;
> (b) a civil proceeding commenced by the service of a complaint or similar pleading;
> (c) a criminal proceeding commenced by a return of an indictment; or
> **(d) a formal administrative or regulatory proceeding commenced by the filing of a notice of charges, formal investigative order or similar document;**
> against an Insured Person for a Wrongful Act, including any appeal therefrom; or
> (2) a formal civil, criminal, administrative or regulatory investigation commenced by the service upon or other receipt by the Insured Person of a written notice from the investigating authority specifically identifying the Insured Person as a target individual against whom formal charges may be commenced; or
> (3) a written request received by an Insured to toll or waive a statute of limitations, relating to a potential D&O Claim as described in paragraphs (1) and (2) above.

(Id., II(D)) (emphasis added). Unlike the definition of a D&O Claim, the definition of an Insured Organization Claim does not include a formal regulatory proceeding or an investigation, such as the FINRA Investigation. Nor can the FINRA Investigation be considered a written request for non-monetary relief, as this reading of subsection (1)(a) would make subsection (1)(d) of the D&O Claim definition redundant. Thus, the FINRA Investigation is not an Insured Organization Claim, and Trustees are not entitled to any Defense Costs or Loss reimbursement from the Policy proceeds.[12]

[12]This issue also relates to the appointment of the Examiner. At the March 13, 2009 hearing on the Examiner Motion, I stated the basis for that appointment as follows:

Second, even if the FINRA Investigation were an Insured Organization Claim, it is now too late for Trustees to seek coverage for it. The May 25 Order provided that "[t]he [Litigation] Trustee and the Movants reserve their respective positions, as set forth in their Motions and the papers filed in support of their Motions, regarding whether the Estates are entitled to have Defense Costs incurred in defending the FINRA special investigation paid from the Policy proceeds." (Adv. Doc. # 160 ¶ 18(b).) This order was entered over two years ago, shortly before the Policy Period expired. Trustees have not yet filed any motion seeking a final determination of coverage. Thus, any application for coverage is time-barred.

Idaho Action

Trustees cite the Idaho Complaint as another possible covered Claim for which they are entitled to Policy proceeds. A careful review of the facts surrounding the Idaho Complaint shows

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> I'm inclined at this point to appoint an examiner, but with a limited scope. And that scope is to address only the issue of inter-[debtor] transactions and transactions by debtors with non-debtor affiliates and with principals, and by principals I mean officers and directors. And I'm going to ask the U.S. Trustee to submit an order embodying that concept.

(Case Doc. # 4185, at 222:11-17.) The May 25 Order had as its basis that statement. (Case Doc. # 5308, at 35:3-23.) Thus, it seems clear that the appointment of the Examiner would easily fall within the purview of a "formal investigative order" which would not qualify as an Insured Organization Claim under the Policy.

that, following the disbursement of their allowed Defense Costs, Trustees have no ongoing claim to proceeds.

The Chapter 11 Trustee included a request for Defense Costs incurred in responding to the Idaho Complaint in his motion for partial summary judgment. (Adv. Doc. # 104 ¶ 4.) Subsequently, the May 25 Order provided that the Idaho Complaint was a covered Insured Organization Claim. (Adv. Doc. # 160 ¶ 18(a).) In his brief in support of the motion for partial summary judgment, the Chapter 11 Trustee did not specify the amount of Defense Costs incurred. Upon request from the Court, Trustees submitted an application for reimbursement of Defense Costs. As the Idaho Complaint has been deemed a covered Insured Organization Claim, Trustees were entitled to the Defense Costs already incurred. This amount has been determined by the Court to be $72,033.50 and has been disbursed to Litigation Trustee.

Those Defense Costs already incurred are the only Defense Costs or Loss that will ever be covered. Per the brief in support of Chapter 11 Trustee's motion for partial summary judgment, the Idaho Action has been stayed indefinitely by an agreement between Debtors and the State of Idaho since March of 2009, when the Examiner was appointed.[13] (Adv. Doc. # 105 ¶ 10; see also Case Doc.

[13]The Court directed the appointment of an Examiner at the conclusion of a hearing held on March 13, 2009. (Case Doc. # 4185, Hr'g Tr., at 222:11-17.) Several weeks later, the U.S. Trustee moved for an order requesting the appointment of Joshua Hochberg as Examiner. (Case Docs. ## 3207, 3208.) That order was entered on April 14, 2009. (Case Doc. # 3308.) Thus, the date of the Examiner's appointment is March 13, 2009, because it is at this time that all parties

2564.) Indeed, the Chapter 11 Trustee stated in May 2010 in regards to Debtors' motion for a stay of the Idaho Action:

> It is the Trustee's understanding that the Idaho Action was stayed upon the Examiner's appointment and has remained stayed since that time. Subject to the Trustee's further investigation of the status of this matter, **it appears that there is no present need to proceed and, indeed, the relief sought will likely become moot as a result of proceedings following the filing of a plan of orderly liquidation.**

(Adv. No. # 09-50190 (PJW), Doc. # 13, ¶ 7) (emphasis added.) The Plan does in fact provide that "all injunctions or stays provided for in the Chapter 11 Cases under Sections 105 or 362 of the Bankruptcy Code, the Plan, by orders of the Bankruptcy Court, or otherwise, and extant on the Confirmation Date, shall remain in full force and effect until the later of (i) entry of the Final Decree or (ii) the dissolution of the Trust." (Case Doc. # 5924, Ex. B, Art. XI, Section F.) Thus, Trustees will never incur any future Defense Costs or Loss in connection with the Idaho Complaint. Trustees were only entitled to receive proceeds for the $72,033.50 in Defense Costs already incurred. This amount has already been disbursed to Trustees, and consequently, they are no longer entitled to receive any proceeds in connection with the Idaho Complaint.

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became aware that an examiner was to be appointed. The U.S. Trustee's motion and the subsequent order served only to notify the parties of the Examiner's identity, not to notify them that an Examiner was to be appointed.

Miscellaneous Proofs of Claim

Trustees argue that there are more than 10,000 unresolved proofs of claim (including those filed by the State of Idaho and the Spann Trust), and that any one of these proofs of claim may be a covered Insured Organization Claim under the Policy. The problem with this argument is that Trustees have failed to request coverage for these proofs of claim by filing a motion for partial summary judgment, as required by the Scheduling Order. The bar dates for proofs of claim were in June and October 2009, well before the February 8, 2010 cut-off date for Present Claims under the Scheduling Order. Consequently, Trustees are forever barred from seeking coverage for any of these proofs of claim.[14]

This also applies to the State of Idaho's proofs of claim. The State of Idaho has filed over 300 proofs of claim in the various DBSI-related bankruptcy cases, seeking over $1.8 billion in each proof of claim. Unfortunately for Trustees, they did not seek coverage for any of those proofs of claim. The Chapter 11 Trustee's motion for partial summary judgment made no mention of the proofs of claim, which were filed before the Scheduling Order's deadline of February 2010 and which would undoubtedly constitute separate Claims under the Policy. The Idaho

[14]Further, I note that the Policy excludes from coverage claims based on breach of contract as well as certain securities claims. (Adv. Doc. # 8, Directors and Officers Liability Coverage Section, III(A)(9) & (C)(2)). I imagine that these two exclusions would preclude coverage of many of the proofs of claim at issue.

Complaint is "a civil proceeding commenced by the service of a complaint or a similar pleading." (Adv. Doc. # 8, Directors and Officers Liability Coverage Section, II(I)(1)(b).) The proofs of claim, on the other hand, are arguably (absent an exclusion) "written demand[s] for monetary damages," which is a different type of Insured Organization Claim. (Id., II(I)(1)(a).) The Idaho Complaint sought various forms of injunctive and monetary relief, including civil penalties of at least $40,000 and restitution of more than $9 million. In contrast, each proof of claim seeks over $1.8 billion in civil penalties and restitution. As noted above, the Idaho Complaint is essentially a nullity at this point because that action is stayed until the dissolution of the Trusts. Moreover, the proofs of claim filed by the State of Idaho are of a different nature than the Idaho Complaint. Consequently, Trustees should have sought coverage for those proofs of claim (which were filed on June 4, 2009, more than eight months prior to the cut-off date for the Scheduling Order) by filing a motion for partial summary judgment with regard to coverage. It is now too late for Trustees to claim that they are entitled to proceeds for the State of Idaho's proofs of claim. Because Trustees failed to properly seek coverage in this interpleader action, Trustees cannot now argue that any of the proofs of claim entitle them to proceeds of the Policy.

Expiration of Coverage

There will be no further covered Insured Organization Claims, since the Policy Period ended on June 1, 2010. Trustees argue that the Policy's expiration date is irrelevant because the Policy is a "claims made" policy, and all Claims against DBSI were filed before June 1, 2010. This argument misses the mark. While all of the Claims discussed above were made against a DBSI entity before the Policy expired, Trustees failed to follow the procedures for securing coverage in this action except as to the Idaho Complaint.

The Policy provides that "any Insured shall, **as a condition precedent to exercising their rights** under any Liability Coverage Section, give to the Company written notice as soon as practicable of any Claim after the CEO, CFO, Risk Manager, Department of Human Resources or Office of General Counsel of an Insured Organization . . . becomes aware of such Claim, **but in no event later than ninety (90) days after the expiration of the Policy Period**." (Adv. Doc. # 8, General Terms and Conditions Section, VII(A)(1), as amended by Endorsement No. 1) (emphasis added.) By the express terms of the Policy, a party must request coverage for any Claim made against it in order to receive any payment for that Claim, and no such request can be made after ninety days following the end of the Policy Period. Likewise, a party to an interpleader action must assert his or her claim to

proceeds in that interpleader action in a timely fashion. See 7 Federal Practice & Procedure § 1714 (3d ed. 2012). It is without a doubt that the terms of the Policy, including the Policy Period and the requirement of notification, still dictate coverage; otherwise, Trustee would not have argued earlier in this proceeding with respect to D & O coverage that the RICO and Avoidance Actions were not covered because they were filed after the end of the Policy Period:

> The claims in the RICO Action, the Avoidance Action . . . were all made on November 5, 2010, over five months after the Policy Period had expired. No policy or coverage existed at the time the Actions were filed against the Individual Insureds. Accordingly, the Individual Insureds' application for coverage on a non-existent policy must be denied.

(Adv. Doc. # 341, at 11.)

Trustees acknowledge in their briefing for this issue that once this interpleader action was commenced, "Federal was no longer a part of this proceeding and the Court was charged with making determinations regarding coverage under the Policy based upon submissions and objections from persons/entities with an interest in the Policy proceeds and how those proceeds are disbursed." (Adv. Doc. # 551, at 12.) The proper mechanism to request coverage was a motion for partial summary judgment, as dictated by the Scheduling Order. This fact is supported by the Court's order dismissing Federal from this action, which provided that "all interpleader-defendants named in this action are required

to interplead and to pursue any and all claims for coverage under the Directors and Officers Liability Coverage Section of [the Policy] in this interpleader proceeding." (Adv. Doc. # 103, at 2.) Trustee has failed to tender any Claims to this Court other than those named above. To hold that the Policy Period and the Scheduling Order do not bar a party from seeking coverage for a Claim heretofore unraised would defeat the purpose of allowing an insurer to interplead potential claimants and let the court determine whose claims are entitled to coverage under the applicable policy's terms.

In light of the foregoing, I hold that Trustees have no further interest in the proceeds, because they have already received their Defense Costs reimbursement for the Idaho Complaint. In re Allied Digital, which also involved a policy with both individual and entity coverage, is clear that where the debtor has no existing covered claims – and there is no further possibility for coverage – the proceeds are not property of the estate. Allied, 306 B.R. at 512. In Allied, no claims could be made against the debtor because the statute of limitations had run on securities claims, which were the only types of claims covered by the entity coverage. Id. at 508. Because the trustee could not point to any possible claims against the debtor, the court found that "Trustee has made no credible showing that the direct coverage of Allied Digital under [the entity coverage clause] for securities

claims has any continuing vitality." Id. at 513. As a result, the proceeds were not property of the estate. Id.

Here, there is only one existing covered Insured Organization Claim, and Trustees have received the amount due to them as Defense Costs incurred in connection with that Claim. The Policy claims period expired in 2010, so there can be no further claims coverage by the estate. All actions against Debtors, including those Claims for which Debtors sought coverage, are stayed by the Plan until the end of the cases. Further, Debtors failed to seek coverage for any other Claims aside from the Idaho Complaint, the Examiner Motion and Investigation, and the FINRA Investigation. Only the Idaho Complaint is a covered Insured Organization Claim, per the Policy terms and this Court's prior rulings. There will be no further Defense Costs or Loss incurred because the Idaho Complaint is essentially finished. Thus, like the proceeds in Allied, the proceeds here are not property of the estate. While this Court determined at the October 14, 2009 hearing that the estate had an interest in the proceeds because of the actions pending against it, there was nothing in the transcript to suggest that ruling is applicable forever.[15] In fact, circumstances have changed – all actions against Debtors have been

[15]Trustees state that "each of the more than 10,000 proofs of claim were filed prior -- and in fact formed part of the basis for -- this Court's October 14 conclusion that the Policy proceeds are property of the Estate." (Adv. Doc. # 551, at 9.) That statement is pure speculation. There is nothing in the record to support that statement.

stayed by the Plan. Additionally, the Scheduling Order in this interpleader action set the procedures for seeking coverage determinations, and the parties are bound by those procedures and this Court's determinations. The proceeds are no longer property of the estate, because the entity coverage has no "continuing vitality."

If Federal had not commenced this interpleader and left the Court to determine coverage, there would be no doubt that Trustees are only entitled to recover for those Claims which have been properly tendered to Federal and deemed covered. In the absence of a valid covered Claim, Federal would be under no obligation to pay anything to the estate. To find a different result here would be to give the estate more rights in the Policy than Debtors paid and bargained for. Trustees in this case should not be permitted to run up legal fees, which must come out of the estate, to fight over funds to which they are not entitled.

Appeal of the May 25 Order Denying Coverage for Examiner's Fees

Trustees next cite the Litigation Trustee's appeal of the May 25 Order denying coverage for the Examiner's Fees. Trustees argue that if the appeal is decided in their favor, they would be entitled to use more than $3 million of the proceeds to pay the Examiner's Fees. Consequently, according to Trustees, "so long as the appeal is pending, the Trustees have a readily identifiable

stake in preventing any improper disbursement of Policy proceeds so that sufficient funds remain to reimburse the over $3.8 million in costs incurred by the Estate." (Adv. Doc. # 540, at 7.)

As matters currently stand, the Chapter 11 Trustee's request for coverage of the Examiner's Fees has been denied. Thus, it is the law of the case that those Fees are not covered. If the District Court reverses and remands with directions to rule in favor of Trustees, then the standing could be reinstated.[16] At this point, however, this Court's May 25 Order is a valid, enforceable order. In the absence of a stay pending appeal, "the prevailing party may treat the judgment of the lower court as final notwithstanding that an appeal is pending." In re Highway Truck Drivers & Helpers Local Union No. 107, 888 F.2d 293, 297-98 (3d Cir. 1989) (citation and internal quotation marks omitted). In this case, the final order entered by this Court on May 25, 2010 held that Trustees had no right to Policy proceeds for the Examiner's Fees. Consequently, Trustees have no standing at this time to object to disbursement of the proceeds in favor of those who do have existing covered Claims.

Litigation Trustee's Status as Plaintiff in RICO and Avoidance Actions

[16]If the District Court were to reverse and remand, I note that the issue addressed in footnote 12 above would likely produce the same result as the May 25 Order.

Last, Trustees argue that they have standing because the Litigation Trustee has filed the RICO and Avoidance Actions against certain of the Individual Insureds. According to Trustees, if those actions result in a judgment against the insured defendants, those defendants will use Policy proceeds to pay the judgment. As a result, the argument goes, Trustees have an interest in preserving the proceeds to be used for the judgment, since the amount of the judgment will inure to the Trusts.

This argument fails in light of this Court's holding in Allied. In Allied, the trustee brought suit against the individuals covered by the policy and claimed that "there should be a limit on the [individuals'] defense costs because if the proceeds of the policy are substantially depleted it would defeat the purpose of his lawsuit." 306 B.R. at 509. The Court rejected this argument:

> The Trustee's real concern is that payment of defense costs may affect his rights as a plaintiff seeking to recover from the D&O Policy rather than as a potential defendant seeking to be protected by the D&O Policy. In this way, Trustee is no different than any third party plaintiff suing defendants covered by a wasting policy. No one has suggested that such a plaintiff would be entitled to an order limiting the covered defendants' rights to reimbursement of their defense costs.

Id. at 513. As in Allied, here the Trustees are attempting to use their status as plaintiffs in the RICO and Avoidance Actions – which have been deemed covered D&O Claims by this Court – to grant them standing in this interpleader. But as the court held in

Allied, this is insufficient to give Trustees a legally protected interest in the proceeds. Litigation Trustee raised this very argument when he opposed the motion to intervene in this interpleader by certain claimants who obtained judgments against some of the Individual Insureds. (Adv. Doc. # 457.) Litigation Trustee argued that the claimants lacked a "substantial legal interest in the proceeds" where their "sole interest in this interpleader action is that 'the continued depletion of the Policy's proceeds will only lessen their ability to recover' their arbitration award." (Id. at 9.) Further, Litigation Trustee cited Idaho law for the proposition that a third party has no right of direct action against an insurer for damages caused by the insured; consequently, argued Litigation Trustee, the claimants had no standing to intervene. (Id. at 12, citing Safeco Ins. Co. v. Klein, 2011 U.S. Dist. LEXIS 141897, at *5 (D. Idaho Dec. 9, 2011); Pocatello Indus. Park Co. v. Steel West, Inc., 621 P.2d 399, 407 (Idaho 1980)).

Trustees' position would allow any plaintiff suing an insured person to intervene in an interpleader action – even where, as here, there has been no judgment or settlement. Thus, I hold that the Litigation Trustee's status as a plaintiff in the RICO and Avoidance Actions is insufficient to maintain standing in this action.

Conclusion

In light of the foregoing, I hold that Trustees have no further interest in the Policy proceeds because they have no existing Insured Organization Claims covered by the Policy. Since the Defense Costs incurred for the only covered Insured Organization Claim, the Idaho Complaint, have been disbursed, Trustees have no further standing in this interpleader action. Accordingly, I need not address the following submissions filed by Trustees:

- Motion to Reconsider the Court's Opinion and Separate Order Granting Coverage for the Avoidance Action, and for a Stay of the Order Dated November 15, 2011 (Adv. Doc. # 418);
- Brief in Opposition to Motion for Partial Summary Judgment Regarding Coverage Under the D&O Policy for Defense Costs Incurred in the Kline Enterprises Case (Adv. Doc. # 424);
- Cross Motion for Summary Judgment (Adv. Doc. # 506);
- Brief in Opposition to the Swensons' Motion to Enforce Court Orders, and Brief in Support of Trustee's Cross Motion for Partial Summary Judgment for Entry of an Order Declaring the Bushman Actions as Not Covered and Directing Recoupment of Defense Costs Paid (Adv. Doc. # 507);
- Motion for Partial Summary Judgment for Entry of an Order Declaring the Bushman Actions as Not Covered and Directing Recoupment of Defense Costs Paid (Adv. Doc. # 538);

- Trustees' Memorandum of Law: (1) in Further Support of Trustees' Motion for Partial Summary Judgment for Entry of an Order Declaring the Bushman Actions as Not Covered and Directing Recoupment of Defense Costs Paid; (2) in Opposition to Douglas, David, and Jeremy Swenson's Cross-Motion for Partial Summary Judgment Declaring the Bushman Action Covered for Defense Costs Purposes and There is No Right for Recoupment; and (3) in Opposition to David and Jeremy Swenson's Cross Motion for Partial Summary Judgment Declaring the Bushman Action Covered for Indemnity Purposes (Adv. Doc. # 565).

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	)	Chapter 11
	)	
DBSI, INC., et al.	)	Case No. 08-12687(PJW)
	)	
Debtors.	)	Jointly Administered
	)	
	)	
FEDERAL INSURANCE COMPANY,	)	
	)	
Interpleader-Plaintiff,	)	
	)	
v.	)	Adv. Proc. No. 09-52031(PJW)
	)	
DBSI, INC., DBSI SECURITIES CORPORATION, FOR 1031 LLC, DOUGLAS L. SWENSON, JOHN MAYERON, CHARLES E. HASSARD, WALT MOTT, THOMAS V. REEVE, JOHN D. FOSTER, FARRELL J. BENNETT, MARK ELLISON, MERRIAH HARKINS, GARY BRINGHURST, JEREMY SWENSON, DAVID SWENSON, ALLEN V. HIRSCH, JOSHUA M. HOFFMAN, WADE THOMAS, MATTHEW DUCKETT, PARIS COLE, and PARTIES UNKNOWN,	)	
	)	
Interpleader-Defendants.	)	

ORDER

For the reasons set forth in the Court's memorandum opinion of this date, the Court finds that James R. Zazzali and Conrad Myers do not have standing to object to the disbursal of the Policy proceeds.

Peter J. Walsh
United States Bankruptcy Judge

Dated: June 27, 2012