

**IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION**

SECURITIES AND EXCHANGE COMMISSION, §

Plaintiff, §

v. §

STANFORD INTERNATIONAL BANK, LTD., §

ET AL., §

Defendants. §

Case No. 3-09-CV-0298-N

**RECEIVER'S RESPONSE TO DEFENDANT LAURA PENDERGEST-HOLT'S
EXPEDITED MOTION FOR CLARIFICATION THAT RECEIVERSHIP ORDER
DOES NOT APPLY TO D&O POLICY PROCEEDS, OR, ALTERNATIVELY,
FOR AUTHORIZATION OF DISBURSEMENT OF D&O POLICY PROCEEDS**

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TABLE OF CONTENTS

I. INTRODUCTION1

II. ARGUMENT AND AUTHORITIES2

 A. Movants Should Have Sought Leave of Court Before Making Claims to the D&O Policy.2

 B. The Stanford Entities Are Faced With Massive Claims.3

 C. Movants’ Fifth Circuit Cases Do Not Support Their Position.....4

 D. Distribution Of The D&O Proceeds To Other Parties Will Negatively Impact The Receivership Estate.8

 1. The Impact On The Receivership Estate Must Be Considered.8

 2. Other Courts Have Found D&O Proceeds Are The Sole Property Of The Estate.....9

 E. The Proceeds Are An Estate Asset Even If They Will Eventually Be Paid To Third-Party Claimants And To The Insureds’ Attorneys.10

 F. There Is No Basis To Lift The Receivership Order And Authorize Payment Of Movants’ Defense Costs.12

 1. In The Bankruptcy Cases Movants Rely Upon, There Were No Claims Against The Estate.12

 2. No Provisions In The Stanford D&O Policy Authorize Payment Of Proceeds Under These Circumstances.13

III. CONCLUSION.....14

TABLE OF AUTHORITIES

	Page(s)
CASES	
<i>A.H. Robbins Co., Inc. v. Piccinin</i> 788 F.2d 994 (4th Cir. 1986)	5
<i>Davis v. Life Investors Ins. Co. of Amer.</i> 282 B.R. 186 (S.D. Miss. 2002).....	7
<i>Executive Risk Indem., Inc. v. Integral Equity, L.P.</i> No. Civ.A. 3:03-CV-269, 2004 WL 438936 (N.D. Tex. Mar. 10, 2004)	10, 11
<i>H.L. Stansell v. Bullock</i> No. Civ.A. 01-0554, 2001 WL 245777 (E.D. La. Mar. 9, 2001).....	7
<i>In re Adelpia Comms. Corp.</i> 298 B.R. 49 (S.D.N.Y. 2003).....	3, 10
<i>In re Allied Digital Techs. Corp.</i> 306 B.R. 505 (Bankr. D. Del. 2004)	3, 9, 12, 13
<i>In re Babcock & Wilcox Co.</i> 69 Fed. Appx. 659 (5th Cir. 2003).....	6
<i>In re CHS Electronics, Inc.</i> 261 B.R. 538 (Bankr. S.D. Fla. 2001)	3, 12, 13
<i>In re CyberMedica, Inc.</i> 280 B.R. 12 (Bankr. D. Mass. 2002)	3, 12, 13
<i>In re Davis</i> 730 F.2d 176 (5th Cir. 1984)	5
<i>In re Edgeworth</i> 993 F.2d 51 (5th Cir. 1993)	5, 6, 8
<i>In re Equinox Oil Co., Inc.</i> 300 F.3d 614 (5th Cir. 2002)	6, 11, 12
<i>In re GB Holdings, Inc.</i> No. 05-42736/JHW, 2006 WL 4457350 (Bankr. D. N.J. Sept. 21, 2006).....	3, 9
<i>In re Kevco</i> 309 B.R. 458 (Bankr. N.D. Tex. 2004).....	7
<i>In re Laminate Kingdom LLC</i> No. 07-10279, BXC-AJC, 2008 WL 1766637 (Bankr. S.D. Fla. Mar. 13, 2008)	9, 12, 13

<i>In re Louisiana World Exposition, Inc.</i> 832 F.2d 1391 (5th Cir. 1987)	5, 6, 7
<i>In re Medex Regional Labs, LLC</i> 314 B.R. 716 (Bankr. E.D. Tenn. 2004)	9
<i>In re Minoco Group of Cos., Ltd.</i> 799 F.2d 517 (9th Cir. 1986)	5
<i>In re Sacred Heart Hosp. of Norristown</i> 182 B.R. 413 (Bankr. E.D. Penn. 1995)	9
<i>In re Sfuzzi</i> 191 B.R. 664 (Bankr. N.D. Tex. 1996).....	5
<i>In re Vitek, Inc.</i> 51 F.3d 530 (5th Cir. 1995)	5, 6, 7, 8
<i>In re World Health Alternatives</i> 369 B.R. 805 (Bankr. D. Del. 2007)	14
<i>Lamar Homes, Inc. v. Mid-Continent Cas. Co.</i> 242 S.W.3d 1 (Tex. 2008).....	11
<i>MacArthur Co. v. Johns-Manville Corp.</i> 837 F.2d 89 (2d Cir. 1988).....	5

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I. INTRODUCTION

Receiver Ralph S. Janvey files this Response to Defendant Laura Pendergest-Holt’s “Expedited Motion for Clarification that Receivership Order Does Not Apply to D&O Policy Proceeds, or, Alternatively, for Authorization of Disbursement of D&O Policy Proceeds.” (Doc. 538). Defendants R. Allen Stanford (Doc. 567) and James M. Davis (Doc. 560) have joined in the Pendergest-Holt motion, as has former Stanford Financial Group Treasury manager Patricia Maldonado (Doc. 582).¹

Movants seek unrestricted access to the entire proceeds of a Directors and Officers (“D&O”) liability insurance policy underwritten by Lloyds of London with limits of at least \$50 million.² This D&O policy provides coverage to a lengthy list of Stanford companies expressly

¹ The parties seeking access to the D&O Policy proceeds are referred to as “Movants.”

² The D&O policy consists of an underlying primary policy with a liability limit of \$5 million, and an excess policy that provides up to \$90 million in the annual aggregate over the Professional Indemnity, D&O, and Employment Practices Liability underlying policies. The underlying and excess Professional Indemnity and D&O policies are contained in the Appendix to the Pendergest-Holt motion (Doc. 538-2 at App. 1, 3, 137).

named in the policy,³ as well as to officers and directors of those entities. This is an extremely valuable asset of the Receivership Estate whose value will decline with every dollar paid. Movants ask the Court to rule that the entire amount of the D&O insurance policy is “not subject to the Receiver’s control,” is “not...subject to the Court’s order freezing Defendant’s assets,” and that Movants’ purported “contractual right to defense costs under the D&O Policies is not a receivership asset.” Motion at 5; Stanford Joinder at 4. According to Movants, this Court and the Receiver have no legal basis to prevent them from using the entire amount of the Stanford companies’ D&O policies to defend and resolve their criminal and civil proceedings. Movants’ position is unsupported by the law and manifestly unfair to the Receivership Estate and the thousands of persons who have made claims against the Stanford entities covered by the D&O Policy. The Receiver opposes the relief requested by Movants, but believes the Court can make an allocation as addressed below. Movants’ motion should be denied.

II. ARGUMENT AND AUTHORITIES

A. Movants Should Have Sought Leave of Court Before Making Claims to the D&O Policy.

Movants first argue that the Receiver unfairly delayed in asserting his position regarding insurance proceeds, but Movants are subject to an order of this Court prohibiting, among other things, the encumbrance, hypothecation, or dissipation of any Receivership Estate assets. As set forth in the authorities herein, the D&O policy and its proceeds are assets of the Receivership

³ The D&O policy lists more than 135 Stanford companies as named insureds. See Appendix to Pendergest-Holt motion, at “Addendum Number 1.” (Doc. 538-2, App. 19-21).

Estate.⁴ It was incumbent on Movants to obtain permission to seek payment under the policies, as is the usual procedure in bankruptcy courts when this issue arises.⁵

B. The Stanford Entities Are Faced With Massive Claims.

The Stanford corporate entities in receivership have had numerous lawsuits filed against them, with at least hundreds of millions of dollars of claims asserted. There undoubtedly will be more lawsuits filed and claims made in the future. These claims are not hypothetical or speculative, and they exceed the value of the D&O policy proceeds. The following are some of the lawsuits filed against Stanford entities covered under the D&O policy, each of which has been pled as a putative class action on behalf of many, and perhaps most, Stanford investors:

- *Hernandez v. Stanford Financial Group Co., et al.*, Cause No. 3:09-CV-487-N, in the United States District Court for the Northern District of Texas (defining the putative class as all persons who (1) purchased securities, including certificates of deposit, sold by or through defendants and affiliated persons and entities between January 1, 2000 and February 17, 2009; or (2) deposited funds with defendants to be held in deposit accounts during the same period);
- *Allen v. Stanford Group Co., et al.*, Cause No. 2:09-CV-108-JVP-PLD, in the United States District Court for the Middle District of Louisiana (defining the putative class as all persons in the United States who purchased securities and certificates of deposit sold by or through the defendant entities, or affiliated entities, between January 1, 2000 and February 17, 2009);
- *Cohron v. Stanford Int'l Bank Ltd., et al.*, Cause No. 4:2009-CV-511, in the United States District Court for the Southern District of Texas (defining the putative class as all

⁴ The Receiver is not taking a position as to the total amount of proceeds available under the D&O policy and the Financial Institutions and Professional Indemnity Policy, and reserves his rights to seek the maximum amount available under both of those policies.

⁵ See, e.g., *In re Adelpia Comms. Corp.*, 298 B.R. 49, 51 (S.D.N.Y.) (addressing directors and officers' motion seeking relief from automatic stay and to allow payment of defense costs under the D&O policies); *In re Allied Digital Techs. Corp.*, 306 B.R. 505, 507 (Bankr. D. Del. 2004) (addressing officers and directors' motion for an order authorizing reimbursement of defense costs, settlement amounts, and judgments under D&O policy); *In re CyberMedica, Inc.*, 280 B.R. 12, 13 (Bankr. D. Mass. 2002) (addressing directors' motion for relief from automatic stay, seeking payments from the D&O policy for defense costs); *In re CHS Electronics, Inc.*, 261 B.R. 538, 538-39 (Bankr. S.D. Fla. 2001) (addressing officers and directors' motion for approval to use D&O insurance policy proceeds to fund proposed settlement); *In re GB Holdings, Inc.*, No. 05-42736/JHW, 2006 WL 4457350, at *1 (D. N.J. Sept. 21, 2006) (addressing debtor's motion for order authorizing payment and advancement of defense costs on behalf of its directors and officers under a D&O policy).

purchasers of certificates of deposit from Stanford Int'l Bank, Ltd., or shares in SIBL's Stanford Allocation Strategy mutual fund wrap program, between February 19, 2004 and February 17, 2009);

- *Adams, et al. v. Stanford Group Co., et al.*, Cause No. 3:09-CV-334-N, in the United States District Court for the Northern District of Texas (defining the putative class as all persons or purchased securities and certificates of deposit sold by or through the Stanford entities, or affiliated agents, between January 1, 2000 and February 17, 2009); and
- *Kyle v. Stanford Int'l Bank Ltd., et al.*, Cause No. 4:2009-CV-525, in the United States District Court for the Southern District of Texas (defining the putative class as all purchasers of certificates of deposit from Stanford Int'l Bank, Ltd., or shares in SIBL's Stanford Allocation Strategy mutual fund wrap program, between February 19, 2004 and February 17, 2009).

Although the civil litigation against the Stanford entities is currently stayed by this Court's orders, the stay will be lifted in the future and the Receiver will have to address these claims. Allowing payments of D&O policy proceeds to these Movants and to the many other individuals claiming entitlement to benefits will deplete the D&O proceeds.⁶ If the insurance policies are depleted, the Receiver will be forced to expend funds that could otherwise go to the defrauded investors and other creditors. Allowing Movants unrestricted access to the policy proceeds during the pendency of the stay would frustrate the purpose of that stay, which was designed to protect the Receivership Estate.

C. Movants' Fifth Circuit Cases Do Not Support Their Position.

The Receiver agrees with Movants that bankruptcy cases are instructive in determining a receiver's powers over D&O insurance proceeds,⁷ and fcourts almost universally hold that

⁶ The Receiver has been informed by counsel for Lloyds that more than 60 persons have requested payment or reimbursement for legal expenses under Stanford's insurance policies, based upon their status as a former director, officer, or employee of Stanford entities.

⁷ Motion at 6 n.5; Stanford Joinder at 5 n. 5.

insurance policies constitute property of the bankruptcy estate of a corporate debtor.⁸ Whether the proceeds of those policies are property of the estate, however, must be analyzed in light of the facts of each case. *In re Sfuzzi*, 191 B.R. 664, 668 (Bankr. N.D. Tex. 1996).

Movants rely on two Fifth Circuit cases in support of their argument that proceeds of the Stanford entities' D&O policies are not property of the Receivership Estate. *In re Louisiana World Exposition, Inc.*, 832 F.2d 1391 (5th Cir. 1987); *In re Edgeworth*, 993 F.2d 51 (5th Cir. 1993). Neither case supports Movants' position.

In *Louisiana World Exposition*, unlike the policy involved here, the D&O insurance policies at issue did not afford the company itself any coverage for liability to third-party claimants. *Louisiana World Exposition*, 832 F.2d at 1398. The court distinguished the D&O policies before it from those which "provide[] coverage for judgments against or losses of the bankrupt corporation itself" in which "the estate owns not only the policies, but also the proceeds designated to cover corporate losses or liability." *Id.* at 1399-1400. It was only under these very unique facts, with a D&O policy that "d[id] not cover the liability exposure of the corporation at all, but only of its directors and officers and . . . payable only to them," that the court held that the insurance proceeds were not a part of the bankruptcy estate. *Id.* at 1401.⁹

The other Fifth Circuit case relied on by Movants did not involve a D&O insurance policy at all. *Edgeworth*, 993 F.2d at 53. Instead, the issue was whether a doctor's Chapter 7 bankruptcy estate included the proceeds of his medical malpractice liability insurance policy. *Id.* The Court found that the malpractice policy proceeds were not part of the estate because the

⁸ E.g., *In re Davis*, 730 F.2d 176, 184 (5th Cir. 1984); *In re Minoco Group of Cos., Ltd.*, 799 F.2d 517, 519 (9th Cir. 1986); *MacArthur Co. v. Johns-Manville Corp.*, 837 F.2d 89, 92 (2d Cir. 1988); *A.H. Robbins Co., Inc. v. Piccinin*, 788 F.2d 994, 1001 (4th Cir. 1986).

⁹ A subsequent Fifth Circuit case would describe the D&O policy in *Louisiana World Exposition* as being at "one extreme" end of the spectrum. *In re Vitek*, 51 F.3d 530, 535 (5th Cir. 1995). That extreme is not this case.

proceeds could only be distributed to victims of medical malpractice. *Edgeworth*, 993 F.2d at 55 n.11, 56. Thus the doctor himself, and consequently his bankruptcy estate, had “no legally cognizable claim to the insurance proceeds.” *Id.* By contrast, the Receivership Entities do have a legally cognizable claim to proceeds of the D&O policy because they are named insureds under the policy, claims have been made under the policy, and the Stanford entities are entitled to coverage.¹⁰ Unlike the physician in *Edgeworth*, the Receiver has not disclaimed an interest in the policy proceeds and the prospective insurance benefits will either enhance or decrease the Receivership Estate.¹¹

Not long after *Louisiana World Exposition*, the Fifth Circuit revisited the ownership of proceeds issue in the case of *In re Vitek, Inc.*, 51 F.3d 530 (5th Cir. 1995), regarding a D&O policy that covered both individual directors and officers and the insured entity, like the policy in this case. When the company filed for bankruptcy protection, the company and certain officers and directors were named as defendants in more than 400 lawsuits. Vitek’s bankruptcy trustee petitioned the court to approve a compromise with the company’s liability insurers in which the insurers would pay the remainder of the policies’ proceeds to the estate in return for protection from third party suits. *Id.* at 531. The company’s officers and directors objected because they would have no protection from the pending claims under the settlement. *Id.* The bankruptcy court approved the settlement, but the district court reversed, holding that individual insureds also had rights in the proceeds. *Id.* at 532. On appeal, the Fifth Circuit reversed the district court

¹⁰ See *In re Equinox Oil Co., Inc.*, 300 F.3d 614, 619 (5th Cir. 2002) (holding insurance policy proceeds were property of the estate because “the policy provides coverage for losses of the bankrupt corporation itself and provides for payment of those losses to [that corporation]”); *In re Babcock & Wilcox Co.*, 69 Fed. Appx. 659, at *1 (5th Cir. 2003) (noting that in *Equinox* the court “reasoned that, because the proceeds of the policies flowed directly to the debtor (and not to a third party), the proceeds were property of the bankruptcy estate”).

¹¹ The *Edgeworth* court found that “no secondary impact ha[d] been alleged upon Edgeworth’s estate, which might have occurred if, for instance, the policy limit was insufficient to cover appellant’s claims or competing claims to proceeds.” *Id.* As discussed *infra*, this is not the case here.

and reinstated the original settlement, thus allowing the estate exclusive use of all the insurance proceeds. *Id.* at 531.

Noting that the case involved the intersection of federal bankruptcy law and state insurance law, the court framed the issue as, “[W]hat part of the proceeds of a liability policy that covers the non-bankrupt coinsureds should enrich the estate of the coinsured debtor?” *Id.* at 533. The *Vitek* court first looked at its previous decision in *Louisiana World Exposition* and determined that the lack of any direct coverage for the debtor in that case was the basis for holding that the debtor, despite having owned the policies, had no interest in the proceeds. *Id.* at 534. The *Vitek* court concluded:

In this circuit, we are therefore in the position of knowing how to resolve cases on either end of the continuum, but we have not yet decided how to resolve cases somewhere along the continuum. On one extreme, when a debtor corporation owns a liability policy that *exclusively* covers its directors and officers, we know from *Louisiana World Exposition* that the proceeds of that D&O policy are *not* part of the debtor’s bankruptcy estate. On the other extreme, when a debtor corporation owns an insurance policy that covers its own liability *vis-à-vis* third parties, we — like almost all other courts that have considered the issue — declare or at least imply that both the policy *and the proceeds* of that policy are property of the debtor’s bankruptcy estate. But we have not yet grappled with how to treat the proceeds of a liability policy when (1) the policy-owning debtor is but one of two or more coinsureds or additional named insureds, (2) the rights of the other coinsured(s) or additional named insured(s) are *not* merely derivative of the rights of one primary named insured, and (3) the aggregate potential liability substantially exceeds the aggregate limits of available insurance coverage.

Id. at 535 (emphasis in original; citations omitted).¹²

¹² Pendergest-Holt tries to inoculate her position against the *Vitek* decision by pointing the Court to a footnote in which the Fifth Circuit discounted the precedential value of its opinion “to future Chapter 11 cases.” Motion at n.4 (citing *Vitek*, 51 F.3d at 533 n.3). The opinion’s qualification, caused by the fact that corporate debtor in that case sought protection under Chapter 7, does not limit *Vitek*’s value here. See *Vitek*, 51 F.3d at 533 n.3. *Vitek* has been cited with approval in subsequent cases. See, e.g., *In re Kevco*, 309 B.R. 458, 467 n.12 (Bankr. N.D. Tex. 2004); *Davis v. Life Investors Ins. Co. of Amer.*, 282 B.R. 186, 189 n.1 (S.D. Miss. 2002); *H.L. Stansell v. Bullock*, No. Civ.A. 01-0554, 2001 WL 245777, at *2 n.1 (E.D. La. Mar. 9, 2001).

Although affirming the estate’s use of all the D&O proceeds, the court reversed on other grounds the district court’s ruling in favor of the individuals and therefore did not set forth a general rule on the ownership of proceeds issue. *Id.* Nevertheless, the Fifth Circuit made clear that Movants’ position here — that the Receivership Estate has no ownership in the D&O policy proceeds — is untenable and not even within the realm of its considered options:

When ultimately we are faced with such a mid-continuum case, we shall have to decide which of two positions to take: either (1) the proceeds of a liability policy should be wholly included in the bankruptcy estate of the debtor that owns the liability policy — even though there are other[s] [who] . . . have some “interest” in the proceeds, or (2) the proceeds should be divided among all coinsureds, either per capita or in proportion to the potential or actual liability faced by each insured party.

Id.

D. Distribution Of The D&O Proceeds To Other Parties Will Negatively Impact The Receivership Estate.

1. The Impact On The Receivership Estate Must Be Considered.

The Court should consider the effect on the Receivership Estate from the insufficient policy limits and the competing claims to the policy proceeds. The Fifth Circuit’s decision in *Edgeworth* that the doctor’s malpractice policy proceeds were not a part of his bankruptcy estate was predicated upon its conclusion that the single case seeking to pursue a judgment against that malpractice policy would have no effect on the estate. *Edgeworth*, 993 F.2d at 56. The court noted that “no secondary impact has been alleged upon Edgeworth’s estate, which might have occurred if, for instance, the policy limit was insufficient to cover appellant’s claims or competing claims to proceeds.” *Id.* at 56. Here, by contrast, the policy limit is plainly insufficient to cover the claims, and there are competing claims to the proceeds from a very large number of parties.

2. Other Courts Have Found D&O Proceeds Are The Sole Property Of The Estate.

Although the Fifth Circuit has not yet definitively addressed whether the proceeds of a policy covering officers and directors as well as the corporate entity are the property of the entity's estate, courts in other circuits have. The United States Bankruptcy Court for the Eastern District of Pennsylvania, for example, held that because a debtor's own exposure was covered by the D&O policy, and because the proceeds available to that debtor were not segregated from those available to the officers and directors, "the Debtor is indeed an insured and has a sufficient interest in the Proceeds as a whole to bring them into the estate." *In re Sacred Heart Hosp. of Norristown*, 182 B.R. 413, 419-20 (Bankr. E.D. Penn. 1995).¹³

In the case *In re GB Holdings, Inc.*, on which Stanford relies in his Joinder, it was the debtor itself that asked the court to approve the D&O insurer's payment of defense costs to the debtor's officers and directors. No. 05-42736/JHW, 2006 WL 4457350, at *1 (Bankr. D. N.J. Sept. 21, 2006). Nevertheless, that court held that because the policy at issue also covered the debtor as a named insured, both the policy and its proceeds were the property of the debtor's bankruptcy estate. *Id.* at *3, *1. While the court ultimately allowed the officers and directors access to a portion of the policy's proceeds, it did so only after noting that the \$75,000 in defense costs they requested was "relatively inconsequential as compared to the \$15 million cap on recoveries under the policy." *Id.* at *4.

¹³ Other bankruptcy courts have also held that the proceeds of insurance policies that cover officers and directors as well as the debtor may be the sole 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." *In re Allied Techs. Corp.*, 306 B.R. 505, 510-11, 512 (Bankr. D. Del. 2004); *In re Laminate Kingdom LLC*, No. 07-10279, BXC-AJC, 2008 WL 1766637, at *2-3 (Bankr. S.D. Fla. Mar. 13, 2008); see also *In re Medex Regional Labs, LLC*, 314 B.R. 716, 721, 723 (Bankr. E.D. Tenn. 2004) (agreeing that when D&O policy covers debtor as insured and depletion of proceeds would have adverse interest on estate, proceeds are property of the estate, but allowing advancement of defense costs to officers and directors because period in which debtor could make claim to policy proceeds had already expired).

Pendergest-Holt cites *In re Adelpia Comms. Corp.*, believing it to be analogous to this matter. Motion at 8-9 (citing 298 B.R. 49 (S.D.N.Y. 2003)). It is not. In that case, the court held that Adelpia “d[id] not have a property interest in the proceeds of the insurance policies *yet*” because no debtor had made any payment for which it was entitled to indemnification coverage, and no debtor had committed itself to payments using their entity coverage. *In re Adelpia Comms.*, 298 B.R. at 53 (emphasis added). Under these facts, that court observed that “[c]laiming the debtors now have a property interest in those proceeds . . . would be akin to a car owner with collision coverage claiming he has the right to proceeds from his policy simply because there is a prospective possibility that his car will collide with another tomorrow.” *Id.* Here, as set forth above, the claims against the Receivership Entities are no mere “prospective possibility.”

E. The Proceeds Are An Estate Asset Even If They Will Eventually Be Paid To Third-Party Claimants And To The Insureds’ Attorneys.

Movants also rely on a summary judgment order entered by Judge Fish in a declaratory judgment action authorizing payment of defense costs under a liability insurance policy. In *Executive Risk Indem., Inc. v. Integral Equity, L.P.*, No. Civ.A. 3:03-CV-269, 2004 WL 438936 (N.D. Tex. Mar. 10, 2004), the court allowed payment of defense costs to an individual officer not in receivership as well as two mutual funds that were the subject of a receivership order, all of whom had been sued. Movants rely on *Executive Risk* for the proposition that, because the D&O policy proceeds will end up in the hands of third-party claimants and the attorneys defending against those claims, the Receivership Entities themselves have no interest in those proceeds. Motion at 7; Stanford Joinder at 8.

Executive Risk is distinguishable on its facts. That receiver sought a continuance to conduct discovery relating to his position that the policy was ambiguous such that the policy

limits were \$5 million per defendant, and not \$5 million in total. *Executive Risk*, 2004 WL 438936, at *3.

Moreover, the rationale in *Executive Risk* which was the basis of the decision has since been rejected by the Texas Supreme Court.¹⁴ Movants argue that the Stanford D&O policy is only triggered by payments required to be made to third-parties or to lawyers defending third-party claims, and “the proceeds therefore are not part of the receivership estate.” Motion at 8. In *Lamar Homes, Inc. v. Mid-Continent Cas. Co.*, the Texas Supreme Court held that a statute imposing a penalty on insurers who delay payment of a “first party claim” applies to defense costs under a liability insurance policy, regardless of whether the payment is to the insured or to its attorneys. 242 S.W.3d 1, 16-17 (Tex. 2008) (“The claim for defense costs is a first-party claim because the insured is the only party who will suffer loss or benefit from the claim.”).¹⁵ One of the arguments against applying the delay statute to defense costs was precisely what Movants argue here in denying that defense costs are “owed” to the insured. This proposition was rejected by the Texas Supreme Court:

Determining the statute’s application by whether the payments are made directly to the insured or to a service provider for the insured’s benefit is a distinction without a difference. . . . When the claim involves a defense benefit, the payee will always be either an insured or the insured’s attorney, and for the purposes of the prompt-payment statute, no reason supports distinguishing between the two.

Id. at 18 (internal citations omitted).

Using similar reasoning, the Fifth Circuit in *Equinox Oil* rejected the argument that because the insurance policy at issue specifically covered the cost of the work outside companies

¹⁴ The *Executive Risk* court applied Texas law in its decision. The Stanford D&O policy provides that it is to be “governed by and in accordance with” Texas law. (D&O Policy, Article XI, Doc. 538-2 at App. 18)

¹⁵ “First-party claim” is defined as an insurance claim that must be paid by the insurer directly to the insured or beneficiary.

performed to clean up debtor's oil spill, the proceeds should be excluded from the bankruptcy estate. 300 F.3d at 618. The court held the proceeds were properly part of the estate because the "policy protect[ed] Equinox from losses resulting from loss of control of a well," and was "not designed to protect losses of third parties" like those who cleaned up the spill. *Id.* at 619-20. Likewise, the purpose of the D&O policy in this case is to protect the Stanford entities and their officers and directors from loss; it is not designed to protect their defense attorneys or any other third party.

F. There Is No Basis To Lift The Receivership Order And Authorize Payment Of Movants' Defense Costs.

1. In The Bankruptcy Cases Movants Rely Upon, There Were No Claims Against The Estate.

Movants argue in the alternative that, even if the D&O policy proceeds are part of the Receivership Estate, the Court should still authorize the payment of Movants' defense costs from this estate asset. In support, Pendergest-Holt cites four opinions in which bankruptcy courts found that D&O policy proceeds were property of the estate, but nevertheless allowed portions of those proceeds to be distributed on behalf of the debtor's officers and directors.¹⁶ None of Movants' cases provides support for the access requested here.

First, while bankruptcy cases are instructive on the ownership of policy proceeds question, a key distinction between bankruptcy and a receivership proceeding is that, as Pendergest-Holt observes, "claims against a debtor entity are typically discharged in bankruptcy." Motion at 10. Movants assume that the Stanford entities will "presumably" obtain

¹⁶ Motion at 9-10 (citing *In re CHS Electronics, Inc.*, 261 B.R. 538 (Bankr. S.D. Fla. 2001); *In re Allied Digital Techs.*, 306 B.R. 505 (D. Del. 2004); *Laminate Kingdom*, 2008 WL 1766637; *In re CyberMedica, Inc.*, 280 B.R. 12 (Bankr. D. Mass. 2002)).

a “complete discharge from liability” in this case, and therefore, the Receiver’s claim to direct coverage under the D&O policy is only “theoretical.” *Id.* There is no basis for this assumption.

Second, in the cases cited by Movants, there were no claims against the estate. The basis for the decision by the *CHS Electronics* court that the proceeds of the D&O policy could be distributed to pay claims against the company’s officers and directors was that all securities claims against the entity that would have been covered by the D&O policy had already been discharged in bankruptcy. *Id.* at 241, 243. Similarly, the court in *Allied Digital* held that because the bankruptcy trustee failed to show that there was any claim remaining against the debtor that would be covered by the D&O policy, the policy’s proceeds were not a part of the estate. *Allied Digital*, 306 B.R. at 511, 513. In *CyberMedica*, although the court held the D&O insurance proceeds to be the property of the estate, it found cause to lift the automatic stay and distribute the proceeds to the debtors’ former officers and directors after balancing their potential harm against that of the debtor-estate. 280 B.R. at 17-18. While the court found that officers and directors were at risk of suffering substantial harm if payments were not made to fund their defense, the harm to the corporate debtor was speculative “given the fact that *there are presently no claims for indemnification nor entity coverage . . . there does not appear to be an immediate risk of the D&O Policy’s two million dollars being depleted.*” *Id.* at 18 (emphasis added). A more stark contrast could not possibly be presented between these cases and the facts here.

2. No Provisions In The Stanford D&O Policy Authorize Payment Of Proceeds Under These Circumstances.

Finally, some courts have allowed advancement of defense costs even when the D&O policy covers the insured entity if a specific provision of the policy renders direct coverage for the debtor itself difficult or impossible. An example is the *Laminate Kingdom* case cited by Movants, in which under the D&O policy’s “priority of payments” clause, the company could

not be paid any proceeds until after the officers and directors' costs of defense had been paid. 2008 WL 1766637, at *3. The payment of proceeds to the officers and directors did not diminish the protection the policy afforded the estate, because such protection was only available under the terms of the policy if there were proceeds remaining after paying the officers' and directors' defense costs. *Id.*¹⁷ The Stanford D&O policy contains no "priority of payments" or similar provision authorizing payments to individuals before the covered entities.

III. CONCLUSION

By asserting its ownership interest to the policy proceeds, the Receiver does not deny that Defendants also may have an interest in the proceeds. Rather, the Receiver seeks to preserve the assets until this Court has the opportunity to weigh the competing claims and interests in the proceeds. The D&O proceeds are a limited resource that will not come close to paying all the claims of defrauded investors.

Given the numerous competing claims to the D&O insurance proceeds, including claims of the individuals who are involved in criminal proceedings, the Receiver asks the Court to make an appropriate allocation of the D&O proceeds. The Receiver suggests that such an allocation should reserve the majority of the insurance proceeds for the benefit of the Receivership Estate. For the reasons set forth above, Movants' motion should be denied.

Dated: July 16, 2009

Respectfully submitted,

¹⁷ See also *In re World Health Alternatives*, 369 B.R. 805, 811 (Bankr. D. Del. 2007) (denying trustee's motion for preliminary injunction to prevent directors and officers' use of D&O proceeds in settlement of claims against them, in part because D&O policy contained priority of payments clause).

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CERTIFICATE OF SERVICE

On July 16, 2009, the foregoing document was electronically submitted with the clerk of the court of the U.S. District Court, Northern District of Texas, using the electronic case filing system of the court ("ECF"), and all counsel of record were provided copies by the ECF system.

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