SO ORDERED,

Judge Katharine M. Samson
United States Bankruptcy Judge
Date Signed: January 26, 2016

The Order of the Court is set forth below. The docket reflects the date entered.

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF MISSISSIPPI

IN RE: MISSISSIPPI PHOSPHATES CORPORATION, *et al* — **CASE NO. 14-51667-KMS**

DEBTORS — **CHAPTER 11**

ORDER DENYING EMERGENCY MOTION TO ENFORCE AUTOMATIC STAY

This matter came on for hearing on October 21, 2015, on the Emergency Motion to Stay (Dkt. No. # 1033) filed by Mississippi Phosphates Corporation, *et al* ("MS Phosphates"). At the hearing, J. Mitchell Carrington and Paul S. Murphy appeared on behalf of MS Phosphates, and Clark R. Hammond and Tristan Armer appeared on behalf of McCain Engineering Company, Inc. ("McCain Engineering"). The Court heard argument regarding the application of the Section 362(a) automatic stay to a fraud action pursued in state court against non-debtors by McCain Engineering, and both parties submitted additional briefs on the issue.

After considering argument and case law, the Court finds that the automatic stay should not extend to prohibit the fraud suit filed by McCain Engineering.

I. JURISDICTION

The Court has jurisdiction over the parties to and the subject matter of this proceeding pursuant to 28 U.S.C. § 1334. This matter is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A), (K), (L) & (O).[1]

II. FINDINGS OF FACT

MS Phosphates filed its petition for Chapter 11 bankruptcy on October 27, 2014. On December 17, 2014, McCain Engineering filed its proof of claim alleging a claim in the amount of $153,968.31 secured by a construction lien for work, materials, and labor related to the pre-petition installation of a boiler. Claim 64-1. On September 14, 2015, McCain Engineering sued Robert P. Kerley and Randall L. Wieck, employees of MS Phosphates at the time of the McCain transaction, in the Circuit Court of Jackson County for fraud. Dkt. No. 1033 p. 21-26. MS Phosphates filed its emergency motion to enforce the automatic stay on September 29, 2015. Dkt. No. 1033. On October 21, 2015, the Court heard argument at a hearing on the motion and ordered the parties to submit additional briefing. Dkt. No. 1061. Having received those briefs, the motion is ripe for decision.

III. CONCLUSIONS OF LAW

MS Phosphates stated in their briefing that they are not seeking an injunction, but only the extension of the existing automatic stay to cover the action against Kerley and Wieck. "The Fifth Circuit has repeatedly held that section 362 does not automatically apply to non-debtors." *Cmty. Home Fin. Servs., Inc. v. Edwards Family P'ship, LLP*, No. 3:12cv252, 2013 WL 1336505, at * 2 (S.D. Miss. Mar. 29, 2013). Neither Kerley nor Wieck are debtors in bankruptcy; the Court, however, may invoke the stay to shield non-debtors "where there is such identity between the debtor and the third-party defendant that the debtor may be said to be the real party

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[1] Pursuant to Federal Rule of Civil Procedure 52, made applicable here by Federal Rules of Bankruptcy Procedure 9014(c) and 7052, the following constitutes the findings of fact and conclusions of law of the Court.

defendant" so that any judgment would in effect be a judgment against the debtor. *Reliant Energy Servs., Inc. v. Enron Canada Corp.*, 349 F.3d 816, 825 (5th Cir. 2003) (quoting *A.H. Robins Co., Inc. v. Piccinin*, 788 F.2d 994, 999 (4th Cir. 1986)) (internal quotation marks omitted). Courts generally recognize two exceptions to the rule that the automatic stay does not apply to actions against non-debtor third parties: where there is absolute indemnification[2] of the third party by the debtor and where allowing the suit would cause irreparable harm to the debtor's reorganization. *See Gulf Coast Hotel-Motel Ass'n v. Miss. Gulf Coast Golf Course Ass'n*, No. 1:08cv1430, 2010 WL 972248, at *2 (S.D. Miss. Mar. 12, 2010). "The two exceptions to the rule permitting suit against third parties are closely related." *In re Fernstrom Storage & Van Co.*, 938 F.2d 731, 736 (7th Cir. 1991). MS Phosphates bears the burden of proving either exception. *See In re Divine Ripe, LLC*, 538 B.R. 300, 302 (Bankr. S.D. Tex. 2015) ("The party invoking the stay has the burden to show that it is applicable."); *Calpine Corp. v. Nev. Power Co. (In re Calpine Corp.)*, 354 B.R. 45, 49 (Bankr. S.D.N.Y. 2006) ("When the stay does not apply automatically, the debtor then bears the burden of demonstrating that circumstances warrant extending the stay.").

First, Kerley and Wieck are not entitled to absolute indemnity here. MS Phosphates' bylaws provide indemnification for actions taken in good faith, and McCain Engineering is only suing for fraud. *See* Dkt. No. 1033 at 5 (quoting Third Amended and Restated Bylaws of Mississippi Phosphates Corporation, Article VIII, Section 8.8, the indemnity provision).[3] At the

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[2] Some courts have held that the indemnification clause need not be absolute. *See, e.g., In re Jefferson Cnty.*, 491 B.R. 277, 289 (Bankr. N.D. Ala. 2013) (holding that "the 'possibility' of a right of indemnification is sufficient").

[3] The full text of the indemnity provision is provided here:

> Any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit, or proceeding, whether civil, criminal, administrative or investigative (other than an action by or in the right of the corporation), by reason of the fact that he is or was a director, officer, employee, or agent of the corporation, or is or was serving at the request of the

hearing, counsel for MS Phosphates argued that the suit states that Wieck and Kerley were acting in their official capacities at all times and therefore their actions require indemnification. Counsel later conceded that MS Phosphates would "perhaps not" pay a fraud judgment against Wieck or Kerley but did not want to speak to the scope of the indemnification clause. Although the scope of the indemnification clause is not directly before the Court, the Court will address it tangentially. The MS Phosphates indemnification clause covers actions taken by officers, directors, employees, or agents *in good faith*. And the definition of good faith includes the "absence of intent to defraud or to seek unconscionable advantage." *Good Faith*, *Black's Law Dictionary* (10th ed. 2014); *see also Am. States Ins. Co. v. Glover*, 960 F.2d 149 (table), 1992 WL 78786, at *5 (6th Cir. Apr. 16, 1992) ("Since the indemnity agreement called for reimbursement of all payments made in good faith, the indemnitor could attack the payments only by pleading and proving fraud or lack of good faith by the surety." (internal quotation marks omitted)). Because the definition of good faith excludes fraud, the Court finds it unlikely that the indemnity clause would cover a finding of fraud by Kerley or Wieck; therefore, the Court finds that this exception does not apply here.

Even if something less than absolute indemnification met this exception, some property of the estate must be at risk. *See In re Xenon Anesthesia of Tex., PLLC*, 510 B.R. 106, 110 (Bankr. S.D. Tex. 2014) (holding that section 362 does not extend to criminal contempt action against managing member of debtor entity because "the Debtor has failed to establish that assets

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> corporation as a director, officer, employee, or agent of another corporation, partnership, joint venture, trust, or other enterprise, shall be indemnified by the corporation against expenses including attorneys' fees), judgments, fines, and amounts paid in settlement actually and reasonably incurred by him in connection with such action, suit, or proceeding *if he acted in good faith* and in a manner he reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe his conduct was unlawful.

Dkt. No. 1033 at 5 (emphasis added).

of the bankruptcy estate would be at risk in allowing the state court to proceed"). MS Phosphates maintains a D & O policy to cover losses of this type. *See* Dkt. No. 259 (approving motion to pay post-petition insurance premiums); Dkt. No. 18 (listing a Directors, Officers and Corporate Liability Policy among insurance policies to be maintained post-petition). And the proceeds of that policy may not be property of the estate. *See JNA-1 Corp. v. Uni-Marts, LLC (In re Uni-Marts, LLC)*, 404 B.R. 767, 781 (Bankr. D. Del. 2009). Because the amount sought in the fraud suit does not even exceed the premium[4] paid for the D & O coverage "and the fact that any claim against the Debtor would be a pre-petition claim[,] it is difficult to see how [MS Phosphates] would sustain any loss . . . ." *Id.*

Second, there is no reorganization to harm in this case. At the hearing, counsel for MS Phosphates described its "prospects for reorganization" as "not likely."[5] *See Le Metier Beauty Inv. Partners LLC v. Metier Tribeca, LLC*, No. 13 Civ. 4650, 2014 WL 4783008, at *4 (S.D.N.Y. Sept. 25, 2014) ("[A]llowing Plaintiffs to continue their action against [the non-debtor defendant] cannot pose a serious threat to the Debtor's reorganization efforts because there is no reorganization to threaten."). As for the current obligations of Kerley and Wieck to MS Phosphates, Kerley was the CFO and is now involved in the management of MS Phosphates' assets, and Wieck no longer works for MS Phosphates. *See* Dkt. No. 1033 at 8 n.10 ("Randall Wieck ceased being the Controller of the Debtors as of April 6, 2015."). While it might be argued that Kerley would be "distracted" from his involvement in the bankruptcy, the same cannot be said of Wieck. *See Le Metier Beauty Inv. Partners*, 2014 WL 4783008, at *4 (holding

[4] In *Uni-Marts*, the Court found it persuasive that the amount of the recovery sought in the suit was "relatively modest" in comparison to the debtor's D & O coverage limit. 404 B.R. at 781. Here, the Court is not aware of the policy limit on MS Phosphates' D & O coverage and uses the amount of the premium, which is surely dwarfed by the policy limit, as its comparator.

[5] In fact, the majority of the proceedings before this Court have been related to MS Phosphates' efforts to obtain a purchaser for its assets and/or business.

that the non-debtor defendant "cannot plausibly claim to be a 'principal player' in Debtor's bankruptcy proceedings because he is no longer a manager or employee of Debtor"). Further, the Court has previously approved the employment of a financial consulting firm and Chief Restructuring Officer (at the rate of $25,000 per week) to assist in the winding down of MS Phosphates. Dkt. No. 318. MS Phosphates has not established that there will be a reorganization or that Kerley would be integral to a reorganization if one were on the horizon. The Court, therefore, finds that this exception does not apply.

MS Phosphates also argues that the suit seeks to recover for a pre-petition debt because the amount sought in the suit is identical to McCain Engineering's proof of claim. McCain Engineering lost the same amount of money whether through services rendered to MS Phosphates or through the alleged fraud of Kerley and Wieck to obtain those services.[6] That the amount sought is the same in both bankruptcy and circuit court is not proof by itself that the action should be stayed. *See In re Divine Ripe*, 538 B.R. at 312 (holding that "the presence of identical allegations against the debtor and non-debtor defendants is an insufficient ground to extend the stay. . . .").

The Court lastly addresses the argument advanced by MS Phosphates at the hearing that denying its motion would "contradict and violate the express provisions of the Bankruptcy Code, as well as, undercut the policies of the Bankruptcy Code" and create a "damaging precedent." While the creation of bad precedent is a concern of all prudent jurists, "applying precedent does not somehow create bad precedent." *U.S. v. $22,050.00 U.S. Currency*, 595 F.3d 318, 325 (6th Cir. 2010) (finding that "Chicken Little would be proud of" similar arguments). The Court does

[6] A plaintiff can seek compensation for a single injury under multiple legal theories but is only entitled to one recovery. *Aspen Tech., Inc. v. M3 Tech., Inc.*, 569 F. App'x 259, 271 (5th Cir. 2014).

not believe that its ruling today will encourage a torrent of fraud claims because this ruling does not make allegations of fraud any easier to state or to prove.

IV. CONCLUSION

Having found that neither of the exceptions allowing extension of the automatic stay to actions against non-debtors apply, the Court denies MS Phosphates' emergency motion. The exceptions used to extend the automatic stay to non-debtors are not intended to block suits supported by legal theories entirely independent of the proof of claim. *See A.H. Robins*, 788 F.2d at 999 (recognizing that "the automatic stay would clearly not extend" to a non-debtor defendant that was "independently liable").

IT IS THEREFORE ORDERED AND ADJUDGED that the Emergency Motion to Stay is DENIED.

##END OF ORDER##