EXPANDING THE AUTOMATIC STAY TO A DEBTOR'S OFFICERS AND DIRECTORS

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I. INTRODUCTION

Under section 362(a)(1) of title 11 of the United States Code (the "Bankruptcy Code"), the filing of a petition for relief pursuant to the Bankruptcy Code automatically stays "the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding *against the debtor* that was or could have been commenced before the commencement of the case under this title." (emphasis added) In general, the requirement that an action be against a debtor in order for the automatic stay to apply is strictly construed, and even codefendants in the same action may not be protected by the automatic stay if they have not filed for bankruptcy protection themselves. Teachers Ins. and Annuity Ass'n of America v. Butler, 803 F.2d 61, 65 (2d Cir. 1986); see also 2 Collier on Bankruptcy ¶ 362.03 (15th ed. rev. 2008) ("[the automatic stay] does not protect separate legal entities, such as corporate directors, officers or affiliates").

There is, however, a limited exception to this general principle in certain circumstances. One leading case has held that the stay may be extended to non-bankrupt entities that have an identity of interests with the debtor. A.H. Robins Co. v. Piccinin, 788 F.2d 994, 999-1000 (4th Cir. 1986), cert. denied, 479 U.S. 876 (1986). Another test courts have used is whether the debtor's estate would be adversely affected by allowing the claims to proceed. In re United Health Care Org., 210 B.R. 228, 232 (S.D.N.Y. 1997). This extension of the automatic stay is generally accomplished through the invocation of the bankruptcy court's equitable powers under section 105(a) of the Bankruptcy Code. See id. In particular, claims against officers and directors of the debtor have been stayed pursuant to this exception. See, e.g., Lomas Fin. Corp. v. Northern Trust Co. (In re Lomas Fin. Corp.), 117 B.R. 64, 66-68 (S.D.N.Y. 1990), remanded on other grounds, 932 F.2d 147 (2d Cir. 1991).

II. THE A.H. ROBINS TEST

The leading case extending the automatic stay to entities closely associated with the debtor is A.H. Robins Co. v. Piccinin, 788 F.2d 994 (4th Cir. 1986), cert. denied, 479 U.S. 876 (1986). In particular, A.H. Robins articulated the "unusual circumstances" test which is often cited as a reason for extending the automatic stay to a debtor's officers and directors. See 2 Collier on Bankruptcy ¶ 105.03[2][b] (15th ed. rev. 2008). The court held that "in order for relief for . . . non-bankrupt defendants to be available under [section 362(a)(1) of the Bankruptcy Code], there must be 'unusual circumstances.'" A.H. Robins, 788 F.2d at 999 (quoting Johns-Manville Corp. v. Asbestos Litig. Group (In re Johns-Manville Corp.), 26 B.R. 405, 410 (Bankr. S.D.N.Y. 1983), aff'd, 40 B.R. 219 (S.D.N.Y. 1984). These "unusual circumstances" exist when "there is such identity between the debtor and the third-party defendant that the debtor may be said to be the real party defendant and that a judgment against the third-party defendant will in effect be a judgment or finding against the debtor." A.H. Robins, 788 F.2d at 999. The court went on to say that

> An illustration of such a situation would be a suit against a third-party who is entitled to absolute indemnity by the debtor on account of any judgment that might result against them in the case. To refuse application of the statutory stay in that case would defeat the very purpose and intent of the statute.

Id.

In A.H. Robins, the debtor was the manufacturer of the Dalkon Shield intrauterine device. Id. at 996. The Dalkon Shield was found to be defective and A.H. Robins became exposed to enormous tort liability as a result. Similar to many asbestos companies, A.H. Robins filed for chapter 11 protection in order to control its exposure to tort liability. Id. Several of the plaintiffs in pending lawsuits, however, had joined as defendants not only the A.H. Robins Company, but also A.H. Robins's liability insurer or some of A.H. Robins's directors and officers. Id. at 996-97.

The debtor sought an extension of the automatic stay to cover the directors and officers and the liability insurer. Id. at 996-97. Although the opinion does not state the debtor's reasoning for seeking to extend the stay, it likely was due to the fact that the debtor was still controlled by the directors and officers who were the defendants in the third-party suit, and since these lawsuits were likely to deplete the liability insurance covering the directors and officers, the directors and officers would be personally responsible for any costs or legal liabilities exceeding the total amount of coverage under the policies.

In developing the "unusual circumstances test," the court looked to the analysis in an action involving extremely similar facts that had been litigated through multiple decisions in multiple courts and had held that some non-debtor defendants were entitled to a stay of the proceedings against them, while others were not. Id. at 999 (discussing the opinion in Johns-Manville, 26 B.R. 405. The court interpreted the Johns-Manville opinion as making a distinction between non-debtors that shared a sufficient "identity" with the debtor, and those that did not. A.H. Robins, 788 F.2d at 999. The court then went on to hold that the "unusual circumstances" test stated above warranted extending the application of the automatic stay to the insurance company and officers and directors who had been co-defendants in the lawsuits prior to Robins's bankruptcy filing. Id.

Interestingly, the Fourth Circuit in A.H. Robins held that the bankruptcy court had the power to stay the proceedings against the third-party defendants on four separate grounds: (i) the automatic stay of section 362(a)(1) of the Bankruptcy Code, (ii) the automatic stay of section 362(a)(3) of the Bankruptcy Code (with respect to the insurers, because unused portions of an insurance policy are "property of the estate"), (iii) the equitable power conferred on bankruptcy courts by section 105(a) of the Bankruptcy Code, and (iv) the bankruptcy court's "inherent power . . . under [its] general equity powers and in the efficient management of the dockets to grant relief." (internal quotation marks omitted) A.H. Robins, 788 F.2d at 999-1004. Although the court could have seemingly relied on sections 362(a)(1) and (3) of the Bankruptcy Code to justify the extension of the automatic stay to non-debtor third parties, the court instead specifically affirmed the district court's finding of sufficient grounds to enjoin the third-party actions under section 105(a) of the Bankruptcy Code. Id. at 1008. This has created some confusion in later cases, as it is not always clear whether a court is holding that (i) the automatic stay included the non-debtors' proceedings at the time the bankruptcy petition was filed or (ii) section 105(a) of the Bankruptcy Code allows the court to issue a stay of the third-party proceeding in order to accomplish the purposes of the automatic stay under section 362(a) of the Bankruptcy Code.

In developing its test, A.H. Robins extensively discussed the facts of Johns-Manville and explicitly relied on its reasoning. A.H. Robins, 788 F.2d at 1003-08. Johns-Manville dealt with a remarkably similar set of facts. The debtor was an asbestos producer that, though operationally quite profitable, was subjected to a large number of tort claims for a large amount of damages. Johns-Manville, 26 B.R. at 407-08. It filed for bankruptcy protection, and in a different proceeding it sought to extend the protection of the automatic stay to its directors, its officers, other employees, and its insurers and sureties, whether or not each still held the respective relationship with the debtor. Johns-Manville Corp. v. Asbestos Litig. Group (In re Johns-Manville Corp.), 26 B.R. 420, (Bankr. S.D.N.Y. 1983) ("Johns-Manville II"). The court found that the debtor had demonstrated "an identity of interests between itself and [the relevant] officers and employees." Id. at 426. Although the court did not elaborate on the features of this identity of interests in the case before it, it reviewed other similar cases that emphasized the fact that a finding of liability against a non-debtor might harm the debtor's estate by subjecting the debtor to liability for contribution or indemnification, or collaterally estopping the debtor from making certain assertions in later proceedings. Id. at 426-27. After this review, the court granted the extension of the stay, declaring that "the interests of all concerned will be most ably protected by permitting this short breathing spell so as to remove the obstacle to a consensual plan of reorganization that the continuance of these suits against these specific employees and agents presently represents." Id. at 427.

In the wake of the Johns-Manville decisions and A.H. Robins, many other circuits adopted the A.H. Robins exception. See In re Zale Corp., 62 F.3d 746, 761 (5th Cir. 1995) (granting a preliminary injunction protecting debtor's insurer from the continuance of claims); Okla. Federated Gold and Numismatics, Inc. v. Blodgett, 24 F.3d 136, 141-42 (10th Cir. 1994) (applying A.H. Robins test but denying stay because the claims against the debtor's president); Am. Imaging Servs. v. Eagle-Picher Indus., 963 F.2d 855, 860-61 (6th Cir. 1992) (affirming the preliminary injunction protecting two of the debtor's officers); Int'l Bus. Mach. v. Fernstrom Storage & Van Co. (In re Fernstrom Storage & Van Co.), 938 F.2d 731, 736 (7th Cir. 1991) (applying A.H. Robins but refusing to first construe claim against debtor as claim against debtor's insurer, and then extend automatic stay to debtor's insurer). However, others have declined to do so. See Stephen Inv. Sec. v. Sec. & Exch. Comm'n, 27 F.3d 339, 342 n.5 (8th Cir. 1994) (declining to adopt or reject the A.H. Robins test while denying to extend the automatic stay to an assignee of debtor's economic rights); Chugach Timber Corp. v. Northern Stevedoring & Handling Corp., 23 F.3d 241, 247 (9th Cir. 1994) (explicitly declining to adopt or repudiate A.H. Robins in denying the extension of the automatic stay to cover the foreclosure of a lien on a boat chartered by the debtor and carrying cargo covered by the automatic stay).

The courts have been somewhat inconsistent in applying the A.H. Robins test. Most significantly, it remains unclear if the "unusual circumstances" test set forth in A.H. Robins acts as the sole inquiry a court must conduct prior to extending the stay, or if such test is only a threshold inquiry prior to performing the analysis typically used prior to exercising general equitable powers under section 105(a) of the Bankruptcy Code. See infra Section III (discussing more thoroughly the test courts apply when determining whether a preliminary injunction under section 105(a) of the Bankruptcy Code is appropriate).

Some courts have applied the extension of the automatic stay under the A.H. Robins test as one of two alternative bases for the grant of a stay, along with section 105(a) of the

Bankruptcy Code. See, e.g., Nev. Power Co. v. Calpine Corp. (In re Calpine Corp.), 365 B.R. 401, 408-09 (S.D.N.Y. 2007) ("I will not address whether the section 362 stay was properly ordered in this case because the Bankruptcy Court's grant of a stay under section 105 is affirmed."). Other courts have treated the A.H. Robins test as part of the "irreparable harm" test in determining whether to grant a preliminary injunction under section 105(a). See, e.g., Eagle-Picher, 963 F.2d at 861 (finding that the debtor and its officers satisfied the A.H. Robins test and "[t]hus, the lower courts did not err in determining that without the preliminary injunction, Eagle-Picher would suffer irreparable harm"). Still other courts are more ambiguous about the relationship between the A.H. Robins test and the test for granting injunctive relief under section 105(a). See, e.g., Lomas Fin. Corp., 117 B.R. at 66-68 (analyzing two of the four factors required to obtain relief pursuant to section 105 of the Bankruptcy Code, then examining the A.H. Robins "unusual circumstances" test without commenting on whether it would be necessary to satisfy the section 105 test).

When it comes to determining whether the A.H. Robins test is satisfied, the courts again are somewhat inconsistent, although some themes can be discerned. The first point to note was expressly set forth in A.H. Robins itself. If a defendant in a claim filed by a third party is entitled to indemnity under the debtor's corporate charter or bylaws for the claim, then the identity of interests between the debtor and the third-party defendant is likely sufficient to satisfy the test. A.H. Robins, 788 F.2d at 999; see also In re MCSi, Inc., Securities Litigation, 371 B.R. 270, 272 (S.D. Ohio 2004) (emphasizing that indemnity was "limited" in determining that the A.H. Robins test was not satisfied); Am. Film Tech. v. Taritero (In re Am. Film Tech.), 175 B.R. 847, 851-52 (Bankr. D. Del. 1994); In re Lomas Fin. Corp., 117 B.R. at 68. But see Algemene Bank Nederland, N.V. v. Hallwood Indus., Inc., 133 B.R. 176, 180 n.3 (W.D. Penn. 1991) ("I specifically reject the dictum stated by the Fifth [sic] Circuit in A.H. Robins Co., Inc., 788 F.2d at 999-1000, holding a stay permissible under [11 U.S.C. § 362(a)(1)] based solely on the existence of an indemnification agreement."); CAE Indus., Ltd. V. Aerospace Holdings Co., 116 B.R. 31, 34 (S.D.N.Y. 1990) (denying the extension of the automatic stay in favor of the debtor's former chairman, despite the existence of an indemnification agreement, because there was no "evidence which demonstrate[d] any impact upon the debtor's reorganization effort").

In addition to the 'unusual circumstances' test relied upon by the A.H. Robins court, some courts have found that a third-party claim against a non-debtor that will significantly interfere with the debtor's reorganization is likely to support a finding that the debtor and third-party defendant have a sufficient identity of interests to warrant extending the stay to cover the claim against the non-debtor. See Queenie, Ltd. v. Nygard Int'l, 321 F.3d 282, 287-88 (2d Cir. 2003). In Queenie, Queenie, Ltd., a closely-held distributor of women's garments had filed a copyright infringement claim against another distributor, and the other distributor had counterclaimed against it, its sole owner, and two other parties not owned or employed by Queenie who were involved in the copyright matter. Id. at 284. After the other distributor prevailed at trial, while the matter was on appeal, Queenie's owner filed for chapter 11 bankruptcy protection. Id. at 287.

In determining whether one party's bankruptcy stayed the appeal against the other parties to the action, the Second Circuit explained that "[t]he automatic stay can apply to non-debtors, but normally does so only when a claim against the non-debtor will have an immediate adverse economic consequence for the debtor's estate." Id. It then held that allowing the claim to continue against Queenie would have such an adverse economic consequence to the debtor,

"because it is wholly owned by [the debtor], and adjudication of a claim against the corporation will have an immediate adverse economic impact on [the debtor]." Id. at 288. The court did not explain the nature of this adverse economic impact on the debtor, but presumably it consisted of the decrease in the value of the ownership interest in Queenie, resulting in a decrease in the value of the estate. The court refused to extend the stay to the other non-debtors, as there was no immediate adverse economic impact to them. Id. It also rejected the contention that the threat of possible future use of collateral estoppel by the third-party plaintiffs to foreclose legal issues to the debtor created enough of an identity with the debtor to satisfy the A.H. Robins test. Id.

In a case illustrating the type of situation where a debtor and its officers and directors in particular would have a mutual interest in seeking to extend the automatic stay to cover claims brought only against officers and directors, the Southern District of New York granted a stay of the proceedings. In Lomas Fin. Corp., Northern Trust brought two postpetition claims against corporate officers of the debtor, for negligent or fraudulent misrepresentation regarding the health of the debtor. Northern Trust alleged that the debtor's directors' and officers' misrepresentations caused it to advance $20 million to the debtor prior to its bankruptcy filing. Lomas Fin. Corp., 117 B.R. at 65. The court applied the "unusual circumstances" test from A.H. Robins, holding that since the Lomas charter contained an indemnification clause, requiring the debtor to indemnify its officers for all legal claims arising out of their position as officers, the test was satisfied, and the bankruptcy court could order a preliminary injunction staying the third-party proceeding, if the other requirements for equitable relief were met. Lomas Fin. Corp., 117 B.R. at 68.

But a similar case in the Southern District of Ohio came out the opposite way. MCSi, 371 B.R. 270. In MCSi, claims for fraud and securities law violations were brought against the debtor and two of its former officers. Id. at 270-71. In denying the application of a stay to the two former officers, it distinguished other cases granting such stays based on the facts that (1) indemnity provisions were "limited" in that indemnity was not provided for if liability arose out of "acts or omissions committed in bad faith, or as a result of active and deliberate dishonesty," id. at 272; (2) securities law claims allow for the independent liability of officers, without requiring the liability of the corporation to be established, id.; (3) the officers were no longer providing services with respect to the debtor's reorganization, id. at 273; and (4) the debtor was not concerned enough about collateral estoppel to move the court to expand the stay (the former officers themselves filed the motion). Id. at 275.

The holding in MCSi is interesting, especially with respect to its treatment of the indemnity provisions as substantially different from the "absolute indemnity" referred to in A.H. Robins. See A.H. Robins, 788 F.2d at 999. This is because states generally do not allow a corporation to indemnify its directors and officers for situations similar to the carve-outs in the provision at issue in MCSi. See, e.g., DEL. CODE ANN. tit. 8, § 145(a) (requiring that the current or former director or officer have "acted in good faith and in a manner the person reasonably believed to be in or not opposed to the best interests of the corporation," and also that the director or officer "had no reasonable cause to believe [his] conduct was unlawful" with respect to criminal actions, in order that the corporation have the authority to indemnify the director or officer for any amounts for which he is liable in the action or expenses incurred in the action). Thus, there may be no lawful instances of "absolute indemnity" under MCSi's interpretation of that term. The reasoning in this decision seems to be problematic for former directors and

officers interested in extending the automatic stay, especially if the debtor is not concerned enough about collateral estoppel effects of the action against the former directors and officers to seek an application of the stay on the former directors' and officers' behalf. In such instances, there does not seem to be an identity of interests between the debtor and its former officers and directors. This is because any action against individuals not associated with the debtor would seem to have little effect on the bankruptcy estate, unless there is possible indemnity by the estate or collateral estoppel effects against the estate.

III. PRELIMINARY INJUNCTIONS UNDER BANKRUPTCY CODE SECTION 105

When a court imposes a stay on litigation or claims between non-debtors, it usually relies on its general equitable powers granted under section 105(a). Section 105(a), however, does not grant unlimited equitable power, only equitable power to implement the provisions of the Bankruptcy Code: "The court may issue any order, process, or judgment that is *necessary or appropriate to carry out the provisions of this title*." (emphasis added). 11 U.S.C. § 105(a). Therefore, courts typically rely on section 105(a) of the Bankruptcy Code in conjunction with the automatic stay granted pursuant to section 362(a)(1) as a way to extend the automatic stay to the directors and officers of a debtor. See, e.g., Homestead Holdings v. Broome & Wellington (In re PTI Holding Corp.), 346 B.R. 820, 825-27 (D. Nev. 2006).

In order to stay proceedings against its officers and directors, a debtor must first prove that an injunction to that effect would indeed help to implement the automatic stay of Bankruptcy Code section 362. The debtor would also need to establish all the prerequisites for preliminary equitable relief in the bankruptcy context, namely: (1) there is a reasonable likelihood that the debtor will prevail on the merits; (2) irreparable harm would result if relief is not granted immediately; (3) the balance of harms tips decisively in favor of the debtor; and (4) the public interest is generally favorable. In re Monroe Well Serv., Inc., 67 B.R. 746, 752-53 (Bankr. E.D. Pa. 1986); see also Calpine Corp., 365 B.R. at 409; 2 Collier on Bankruptcy ¶ 105.02[2] (15th ed. rev. 2008).

The cases in this section analyze whether a preliminary injunction under section 105(a) of the Bankruptcy Code is warranted to extend the effects of the automatic stay to non-debtors.

1. Likelihood of Success on the Merits

This requirement has been interpreted inconsistently, even in different cases before the same court. Compare Calpine Corp., 365 B.R. at 410 (interpreting test as a determination of the likelihood of a successful reorganization), with Lomas Fin. Corp., 117 B.R. at 68 (interpreting test as an analysis of whether the debtor should be successful in its motion to extend the automatic stay). In most cases, courts reason that the purpose of the injunction is to preserve the status quo prior to the chapter 11 reorganization, and therefore, require a showing that there is a substantial likelihood that the debtor will be able to reorganize or liquidate successfully. See, e.g., United Healthcare, 210 B.R. at 234; see also 2 Collier on Bankruptcy § 105.02[1][a] (15th ed. rev. 2008). In United Healthcare, a creditor of two of the officers of the debtor United Healthcare Organization had sought to recover on the debt, and the court had enjoined the action by extending the automatic stay to the officers pending resolution of United Healthcare's reorganization. Id. at 231. Based on the creditor's motion for relief from the automatic stay, the

court evaluated whether the extension of the stay under section 105(a) of the Bankruptcy Code was proper. Id. at 232-35. The court examined whether the debtor had a reasonable likelihood of reorganization or liquidation under chapter 11. Id. at 234. Although the court expressed reservations about whether the two officers would be able to provide the funds to the debtor's estate required by a settlement reached in the bankruptcy proceeding, it applied a liberal standard to determine if the United Healthcare Organization had a likelihood of effecting a successful reorganization. Id. at 234 ("I am less than sanguine that [the officers] will in fact find willing creditors to finance this settlement. Nevertheless, I find there is a reasonable likelihood of success in this case.").

Other courts have treated the requirement as necessitating a showing merely that the stay would be appropriate to apply, presumably based on the other elements of the inquiry. See, e.g., Lomas Fin. Corp., 117 B.R. at 68 (holding that it was appropriate to apply the stay when the lawsuit against the debtor's officers was clearly an attempt to circumvent the automatic stay with respect to the debtor); see also American Film Tech., 175 B.R. at 849 (explicitly collapsing the "likelihood of success on the merits" inquiry into the "irreparable harm" requirement). Notably, however, in Lomas, the court did not apply the standard test under section 105(a) as to whether a preliminary injunction should be granted, but instead examined only whether there would be irreparable harm if an injunction were denied and whether there was a likelihood of success on the merits. Lomas Fin. Corp., 117 B.R. at 66-68. When examining the likelihood of success on the merits, the court explicitly stated that "the issue on the merits is whether Lomas' application for an order . . . enforcing the automatic stay . . . should be granted." Id. at 68. This is in contrast to the courts following the common approach, which maintain that the issue on the merits is whether the debtor is entitled to an order for relief in the relevant chapter 11 proceeding.

With either treatment, this requirement is not likely to be much of a barrier to a debtor seeking to extend the automatic stay to non-debtor third parties. In the more common interpretation of the test, the courts tend to apply the standard liberally, as shown above. Under the alternate interpretation of the requirement, the court seems to be merely asking whether it should be granting the motion at issue, without looking at the state of the bankruptcy proceedings as a whole, in which case one of the other tests (e.g., irreparable harm, balance of harms) will need to be dispositive.

In addition, there is a line of cases in the Second Circuit holding that in lieu of a showing of a likelihood of success on the merits, the debtor may show that there is "a sufficiently serious question regarding the merits to make it a fair ground for litigation, with the balance of the hardships tipping decidedly in the movant's favor." Calpine Corp., 354 B.R. at 48; see also Alert Holdings, Inc. v. Interstate Protective Servs. (In re Alert Holdings, Inc.), 148 B.R. 194, 200 (Bankr. S.D.N.Y. 1992) (citing Tucker Anthony Realty Corp. v. Schlesinger, 888 F.2d 969, 972 (2d Cir. 1989)); Kaplan v. Bd. of Educ., 759 F.2d 256, 259 (2d Cir. 1985). The Second Circuit generally does not rely on this exception in analyzing whether there is a likelihood of success on the merits, but this may signal that the Second Circuit is less likely to deny a preliminary injunction based on this element.

2. Threat of Irreparable Injury

In general, when a claim is filed against a director or officer for actions taken on behalf of the corporation, there are three types of irreparable harm that might be found. First, the debtor might be subjected to collateral estoppel of claims. See, e.g., Lomas Fin. Corp., 117 B.R. at 67 ("[t]he threat of collateral estoppel would force [the debtor's officers] to participate in the . . . lawsuit"); see also Am. Film Tech., 175 B.R. at 851 ("To avoid the collateral estoppel effect, [the debtor] must participate in the defense of the state court case. That requires [the debtor] to do precisely what the automatic stay is intended to excuse it from doing.").

Second, the debtor may be forced to indemnify the third-party defendant if liability is found (forcing the third-party defendant to face the possibility of inconsistent judgments, since it likely will not recover fully from the bankruptcy estate), see, e.g., North Star Contracting Corp. v. McSpedon (In re North Star Contracting Corp.), 125 B.R. 368, 371 (S.D.N.Y. 1991) ("[the third-party defendant] has a right of indemnification with respect to North Star and thus any recovery by [the third-party plaintiff] in the state court action will adversely affect North Star's assets").

Third, the reorganization effort may be hampered by the claims. This may be due to the amount of the third-party defendant's attention diverted to defending the lawsuit, rather than attending to the reorganization. See, e.g., Lomas Fin. Corp., 117 B.R. at 66-67 ("key personnel would be distracted from participating in the reorganization process causing Lomas and its creditors both immediate and irreparable harm" (internal quotation marks omitted) (quoting Lomas Fin. Corp., No. 89-12471, slip op. at 10 (Bankr. S.D.N.Y. Jan. 11, 1990) (transcr. of hearing))); see also PTI Holding Corp., 346 B.R. at 827 ("[a]ny material diversion of [the non-bankrupt defendants'] time or energies would result in a loss to the estate"). The reorganization may also be harmed because the non-bankrupt defendant had intended to contribute funds or property to the estate to effect the reorganization, and the claims against him threaten the availability of the funds or property. See, e.g., United Healthcare, 210 B.R. at 233 (finding that the third-party defendants "do not currently have sufficient liquid assets to contribute to the [bankruptcy] estate as required under the proposed settlement agreement").

In addition, there is an exception to the irreparable harm requirement recognized in the Southern District of New York, when an action "threatens the reorganization process," in a way that is "imminent, substantial and irreparable." Calpine Corp., 365 B.R. at 409-10 (quoting Hawaii Structural Ironworkers Pension Trust Fund v. Calpine Corp., Inc., No. 06-5358, 2006 WL 3755175, at *4 (S.D.N.Y. 2006)). In Calpine Corp., an energy supplier had entered into the necessary agreements to supply electricity in Nevada through the construction and operation of two power plants. Calpine Corp., 365 B.R. at 405. After the supplier refused to honor its obligation to construct either plant, actions for breach of contract, breach of good faith and fair dealing, specific performance and declaratory relief were brought against the supplier, as well as its insurer. Id. at 406. Soon after this, the supplier filed for chapter 11 bankruptcy protection. Id. In temporarily enjoining the continuance of the suit against the insurer, the court found that the lawsuit would require a substantial portion of the sole remaining transmission engineer's time to assist the insurance company in defending the case, and that a successful reorganization would also require a substantial amount of the transmission engineer's time, making it difficult for him

to do both. Id. at 411-12. Thus, the court reasoned, there was a threat of irreparable harm if the proceedings against the chief transmission engineer were allowed to proceed. Id. at 412.

3. Balance of Harms

The balance of harms test weighs the harm to the claimant if the injunction were issued against the harm to the third-party defendant if it were not issued. 2 Collier on Bankruptcy ¶ 105.02[2] (15th ed. rev. 2008). This generally comes out on the side of granting the stay, because a relatively minor delay in receiving judicial relief is, as a matter of law, not a serious harm. Calpine Corp., 365 B.R. at 413 ("[t]he inability of Nevada Power to obtain a hypothetical recovery sooner . . . is not a harm—and is certainly not an irreparable harm sufficient to outweigh the irreparable harm that Calpine will suffer if the . . . litigation were permitted to proceed"). Since the general test for whether a preliminary injunction pursuant to the bankruptcy court's power under section 105(a) of the Bankruptcy Code requires that each of the prongs of the test be satisfied, including a finding of irreparable harm, see 2 Collier on Bankruptcy ¶ 105.02[2] (15th ed. rev. 2008), the 'balance of harms' prong can only be dispositive if there is irreparable harm threatened to the debtor's estate. But see Eagle-Picher, 963 F.2d at 859 (holding that the section 105 test requires balancing the four factors, rather than satisfying each one). When the court weighs the possibility of irreparable harm to the estate on the one hand versus a small delay in the proceedings on the other hand, the decisions strongly favor the finding of an advantage in the public interest analysis for the extension of the stay.

4. Public Interest

Similar to the balancing of harms, weighing the public interests also seems to be a factor favorable to the debtor. This is because there is a strong public interest in promoting reorganizations. See A.H. Robins, 788 F.2d at 1008 (referring to "the unquestioned public interest in promoting a viable reorganization of the debtor"); see also Calpine Corp., 365 B.R. at 413. Thus, if allowing a claim to proceed will threaten the debtor's reorganization, a stay will be favored. In addition, there is a strong public interest in treating the various creditors fairly vis-à-vis one another. So if a claim threatens to enrich one creditor at the expense of others, allowing the claim to proceed will be disfavored. While there is also a public interest in the speedy recovery on obligations, Calpine, 365 B.R. at 413, this will often be outweighed by the other considerations. For example, in Calpine, the court acknowledged that there is an interest in allowing a creditor to recover on a debt, but then explicitly referred to the irreparable harm prong of the section 105 test to find that the interest in recovery of debts does not outweigh the interests weighing in favor of the debtor. Id.

IV. PRACTICAL CONSIDERATIONS

While the importance of the ability to extend the automatic stay to cover third-party actions against the debtor's directors and officers cannot be doubted, there are a few facts that render attempts to extend the stay unnecessary in certain situations. First, many suits against the directors and officers are prosecuted pursuant to state statutes that allow for shareholder derivative suits. In such suits, the claim is ostensibly brought by the corporation itself. Thus, these claims are property of the estate, so long as they could have been brought prior to the petition date. This makes them subject to the automatic stay. But care must be taken, because

these claims are generally brought in state court, and while the automatic stay applies, a state court may not recognize this without an order from the bankruptcy court enjoining the action.

In addition, recent developments in securities law makes it much more difficult for a plaintiff in a securities fraud case to withstand a motion to dismiss. This deters potential plaintiffs from bringing securities fraud claims against officers and directors of any corporation, alleviating the need to extend the protection of the automatic stay to the officers and directors of a debtor. But the majority of securities fraud claims that are filed do survive a motion to dismiss, and these claims tend to be relatively strong, often meriting discovery or involving a protracted battle with the liability insurance carrier over coverage.

Finally, the existence of the director and officer liability policies softens the need for extension of the automatic stay in most instances, because neither the debtor nor the directors and officers themselves will be forced personally to pay any money to any claimants. On the other hand, some debtors are forced to file for bankruptcy protection precisely because of liabilities that extend to their directors and officers, in which case the liabilities are likely to exceed the total amount of coverage under the insurance policy. In addition, when the coverage limit is exceeded on a director and officer liability insurance policy, or when the liability insurer denies coverage, a debtor will likely be unable to indemnify its directors and officers for any liabilities, and any amounts for which a director or officer is liable will be forced to come from his personal assets. Lastly, a debtor may wish to seek extension of the automatic stay to its directors and officers, notwithstanding the existence of liability insurance policies, in order to ensure these individuals are able to devote their attention to promulgating a successful reorganization strategy to exit bankruptcy without the distraction of defending a lawsuit.

V. CONCLUSIONS

Generally, corporate directors and officers of a debtor are not protected by the automatic stay. Although an exception exists to permit the extension of the automatic stay to a debtor's directors and officers, the seminal case on the application of this exception - A.H. Robins - has been applied inconsistently by the courts. Despite this inconsistency, however, courts have generally been willing to grant an injunction under section 105(a) of the Bankruptcy Code staying proceedings against a debtor's officer or director when allowing the claims to proceed would cause harm to the debtor's estate. This will often apply when the proceedings target key personnel of the debtor, who are instrumental in the debtor's reorganization, when the defendants in the proceedings are entitled to indemnity from the debtor for any liability and when the proceeding could later subject the debtor to collateral estoppel.