Barton beware: Barton doctrine prevents Bermuda insurers from enforcing arbitration clause in foreign court

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The Bankruptcy Court for the Southern District of New York adopted an expansive reading of the 'Barton doctrine' as applied in the Third, Sixth, Ninth and Eleventh Circuits to bar Bermudian insurers from suing in Bermuda to enforce an arbitration clause in an insurance policy against a plan administrator under an approved Chapter 11 plan.

In a recent decision, the Bankruptcy Court for the Southern District of New York held that the protections of the 'Barton doctrine' applied to a plan administrator under an approved chapter 11 plan, and barred Bermudian insurers from suing in Bermuda to enforce an arbitration clause in an insurance policy.[1] The Bankruptcy Court's decision highlights the pitfalls and limitations of commencing actions in foreign jurisdictions to enforce arbitration provisions against debtors or their representatives while a bankruptcy proceeding is pending. The holding is therefore of interest to insurers in particular and to bankruptcy practitioners generally, as it signals a move in the Second Circuit toward the expansive application followed by the Third, Sixth, Ninth and Eleventh Circuits of the Barton doctrine, which bars suits not just against trustees, but also against other key bankruptcy players such as estate professionals, creditors' committees and plan administrators.

Background

The Bankruptcy Court's decision originated in the litigation that arose in the wake of the collapse of MF Global. Following the commencement of a Chapter 11 proceeding, the non-regulated MF Global entities obtained confirmation of a Chapter 11 plan that appointed MF Global Holdings Ltd (MFGH) as plan administrator charged with the responsibility to prosecute suits against MF Global's former officers and directors for the benefit of creditors. The plan administrator, in concert with the former customers of MF Global, commenced a multidistrict litigation against the former officers and directors asserting claims for losses arising from the firm's historic failure. After years of litigation, the parties in the multidistrict litigation reached a global settlement, which the Bankruptcy Court approved on 10 August 2016. The global settlement called for MF Global's former insurers to tender the policy limits of their coverage to fund the settlement and, with the exception of the four insurers that had issued the top layers of excess errors and

omissions (E&O) insurance policies (the 'Dissenting Insurers'), all of MF Global's directors and officers (D&O) and E&O insurers complied with the terms of the global settlement.

On 27 October 2016, MFGH and its subsidiary, MF Global Assigned Assets LLC (MFGAA along with MFGH, the 'MFG Plaintiffs'),[2] filed an adversary proceeding in the Bankruptcy Court for breach of contract and bad faith against the Dissenting Insurers alleging that they unreasonably and in bad faith failed to contribute any of their combined US$25m policy limits to the settlement, despite the fact that there was more than US$480m in damages asserted as claimed losses under the E&O policies.[3] The Dissenting Insurers, who were based in Bermuda, turned around and filed cases in the Bermuda Supreme Court, Civil Jurisdiction (the 'Bermuda Proceeding'), through which they obtained ex parte antisuit injunctions that prohibited the MFG Plaintiffs from prosecuting the adversary proceeding, effectively forcing the MFG Plaintiffs to arbitrate the coverage dispute in Bermuda pursuant to the arbitration provisions contained in the Dissenting Insurers' excess E&O policies. After commencing the Bermuda Proceeding, the Dissenting Insurers filed a motion in the Bankruptcy Court to compel arbitration in Bermuda, but the antisuit injunction issued by the Bermuda court barred the MFG Plaintiffs from opposing the motion.

The Bankruptcy Court then issued a temporary restraining order that barred the Dissenting Insurers from enforcing the Bermuda antisuit injunctions, a preliminary injunction extending the relief granted in the temporarily restraining order, and an opinion holding the Dissenting Insurers in contempt for violating the temporarily restraining order. Now free to oppose the Dissenting Insurers, the MFG Plaintiffs argued that the commencement of the Bermuda Proceedings as well as the obtaining of the antisuit injunctions violated the Barton doctrine (as well as the bar order contained in the order approving the global settlement).

The Barton doctrine

The Barton doctrine, developed from common law by the United States Supreme Court over a century ago, provides that a suit may not be brought against a bankruptcy trustee or a receiver without leave of such receiver's appointing court.[4] In *Barton v Barbour*,[5] the Supreme Court held that 'before suit is brought against a receiver leave of the court by which he was appointed must be obtained', because 'the evident purpose of a suitor who brings his action without leave is to obtain some advantage over the other claimants upon the assets in the receiver's hands'.[6] In addition to protecting a bankruptcy trustee or receiver from personal liability, 'the Barton Doctrine is intended to protect the receivership court's "overriding interest in [the] administration of the estate"'.[7] Courts have noted that the Barton doctrine also serves to 'centralize bankruptcy litigation' and 'keep a watchful eye' on court-appointed officers.[8] In addition to barring declaratory judgment actions and suits seeking damages, the Barton doctrine also extends to arbitrations and requires insurers to seek leave of the bankruptcy court before naming a receiver or trustee as a party to an arbitration proceeding.[9]

While the protections of the Barton doctrine have been demarcated by numerous court decisions in the many years since the *Barton* decision, ambiguity still exists as to which entities in a bankruptcy proceeding are protected by the Barton doctrine, and the Second Circuit has not articulated a test for determining the application of the Barton doctrine to parties other than a bankruptcy receiver or trustee. Other courts have broadly applied the protections of the Barton doctrine to various parties in a bankruptcy proceeding. For example, the Sixth Circuit has held that the Barton doctrine protects any entity that is the 'functional equivalent' of a trustee.[10] In *DeLorean*, the Sixth Circuit applied the Barton Doctrine to prevent a suit against a trustee's counsel on the basis that counsel for a trustee is the 'functional equivalent' of the trustee for purposes of estate administration and reasoned that 'the protection that the leave requirement affords the trustee and the estate would be meaningless if it could be avoided by simply suing the trustee's attorneys'.[11] The Eleventh Circuit has also adopted the 'functional equivalent' test articulated by the Sixth Circuit in finding that officers appointed by the trustee and approved by the bankruptcy court to sell estate property warranted the protection of the Barton doctrine.[12] In perhaps the most expansive application of the Barton doctrine to date, the Ninth Circuit recently held that the doctrine applied to a member of an unsecured creditors committee 'because creditors have interests that are closely aligned with those of a bankruptcy trustee, there's good reason to treat the two the same for purposes of the Barton doctrine'.[13]

The Barton doctrine and the MFG plaintiffs

The central issue presented to the Bankruptcy Court then was whether the protection of the Barton doctrine actually applied to the MFG Plaintiffs. The Dissenting Insurers argued that the Bermuda Proceedings were 'not a suit against a court-appointed officer in his/her official capacity' and thus did not constitute a

Barton violation because the Bermuda proceedings were only filed to defend a pre-existing arbitration clause.[14] The Dissenting Insurers further argued that the Barton doctrine is 'typically applied in suits against court officers in entirely different circumstances, such as where a trustee commits malpractice, breaches a fiduciary duty, or violates an individual's constitutional rights'.[15] The Dissenting Insurers posited that because the Bermuda Proceeding did not interfere with a creditor's claim or the administration of the estate, the policy concerns underpinning the Barton doctrine were not implicated. The MFG Plaintiffs argued that MFGH and MFGAA were entitled to the protections of the Barton doctrine because they were assigned the rights of the individual insureds against the Bermuda Insurers under the global settlement and the Barton doctrine protects their effort to marshal and liquidate estate assets such as the proceedings of the excess E&O insurance policies.

Adopting the reasoning of the Eleventh Circuit that the Barton doctrine protects court-appointed officers assisting a trustee in carrying out official duties, the Bankruptcy Court held that the Barton doctrine applied to the MFG Plaintiffs. Specifically, the Bankruptcy Court noted that MFGH, as the plan administrator under a Chapter 11 plan, was a court-appointed entity tasked with marshalling and liquidating assets, and by initiating an adversary proceeding against the Dissenting Insurers to pursue funds for the benefit of creditors, it was acting in its official capacity. Further, MFGAA, as the holder of the rights to collect against the Dissenting Insurers, was acting to 'functionally advance' the goals of MFGH as plan administrator.[16] The Bankruptcy Court found that 'just as the court in *Lawrence* found that the Barton Doctrine protects parties assisting a trustee in pursuing its objectives, so too does this Court find that the Barton Doctrine protects both MFGH and MFGAA in undertaking their official obligations, including the [commencing of the adversary proceeding against the Dissenting Insurers]'.[17]

The Bankruptcy Court further noted that the Bermuda Proceeding was commenced to circumvent the adjudication of issues by the Bankruptcy Court and prevent the MFG Plaintiffs from carrying out their official responsibilities. These actions 'undermined the Court's and the Plaintiffs' overriding interest in the administration of the estate' and ' resulted in disjointed and decentralized actions in multiple jurisdictions that delayed the administration of the case, and ultimately, distributions to creditors'.[18] That was the very harm, the Bankruptcy Court reasoned, that the Barton doctrine was created to prevent.

In reaching its conclusion, the Bankruptcy Court noted that the facts and circumstances of the instant case were similar to those in *ACE Insurance Co, Ltd v Smith* (*In re BCE West LP*).[19] In *BCE West*, a Bermuda-based insurance company obtained ex parte injunction orders prohibiting a plan administrator, charged with the collection of certain retained assets (including causes of action relating to insurance policies), from pursuing litigation to collect on the insurance policies issued by the Bermuda insurance company. The court in that case found that the Bermuda-based insurance company, by filing suit against the plan trustee without first seeking leave of the bankruptcy court, violated the Barton doctrine, and the district court affirmed the bankruptcy court's decision. The Bankruptcy Court found that the MFG Plaintiffs were performing the same function as the plan administrator in *BCE West* as they were charged under the Chapter 11 plan with administering certain assets, including the rights to collect on the policies issued by the Dissenting Insurers, and, accordingly, were equally protected by the Barton doctrine.

Finally, the Bankruptcy Court dismissed the argument that the Barton doctrine did not apply because the Dissenting Insurers commenced an action outside of the United States, and held that Barton doctrine requires 'a party who seeks to file suit in an international forum' to obtain leave of the appointing court.[20]

Conclusion

The Bankruptcy Court's decision reinforces the Barton doctrine's ability to prevent foreign insurers from commencing actions in foreign courts against plan administrators (and entities that serve a similar function) where the action seeks to bar enforcement actions in a US bankruptcy court. More broadly, it serves as the latest example of the bankruptcy courts taking a sceptical approach to efforts by insurers and other litigants to pursue collateral attacks against settlements by commencing actions in foreign jurisdictions. The Bankruptcy Court's ruling in *MF Global* also clarifies that bankruptcy courts within the Second Circuit will lean towards the expansive reading of the Barton doctrine as applied in the Third, Sixth, Ninth and Eleventh Circuits. As illustrated in that case, the cost of failing to seek leave of the bankruptcy court before commencing a foreign proceeding can be high and include sanctions, fee shifting and findings of contempt.

Shortly after the entry of the Bankruptcy Court's opinion, the Dissenting Insurers filed an appeal to the District Court for the Southern District of New York, so additional developments as to the application of the Barton doctrine in the Second Circuit are possible. In addition, the parties are briefing the issues of whether

the arbitration clause contained in the Dissenting Insurers' excess policies is enforceable against the MFG Plaintiffs, and the ultimate determination of this issue will be of further interest to foreign insurers who issued policies to companies in US insolvency proceedings.

Notes

1 *MF Glob Holdings Ltd v Allied World Assurance Co Ltd* (*In re MF Glob Holdings Ltd*), 562 BR 866 (Bankr SDNY 2017).
2 MFGAA was a subsidiary of MFGH that had been created after the commencement of the Chapter 11 proceeding to receive and prosecute the claims of MF Global's former customers and affiliates that had been assigned to it under the global settlement and other assignment agreements for the benefit of MFGH's creditors.
3 See n1 above, at 867.
4 *Matter of Linton*, 136 F3d 544, 545 (7th Cir 1998): 'An unbroken line of cases . . . has imposed the requirement [of obtaining leave from the bankruptcy court] as a matter of federal common law.'
5 *Barton v Barbour*, 104 US 126 (1881).
6 *Ibid*, at 128.
7 See n1 above, at 873.
8 See, for example, *Blixseth v Brown* (*In re Yellowstone Mountain Club, LLC)*, 841 F 3d 1090, 1094 (9th Cir 2016).
9 See *McIntire v China MediaExpress Holdings, Inc*, 113 F.Supp 3d 769, 773 (SDNY 2015).
10 *Allard v Weitzman* (*In re DeLorean Motor Co*), 991 F 2d 1236, 1241 (6th Cir 1993).
11 *Ibid*.
12 See *Carter v Rodgers*, 220 F 3d 1249, 1252 n 4 (11th Cir 2000); see also *Lawrence v Goldberg*, 573 F 3d 1265, 1270 (11th Cir 2009).
13 *In re Yellowstone Mountain Club, LLC*, 841 F 3d at 1095.
14 See n1 above, at 872.
15 *Ibid*.
16 *Ibid*, at 876.
17 *Ibid*.
18 *Ibid* (internal quotation marks omitted).
19 *ACE Insurance Co, Ltd v Smith* (*In re BCE West LP)*, 2006 WL 8422206 (D Ariz 20 September 2006).
20 See n1 above, at 876; see also *ibid*, at *8.