UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

AGWAY, INC.

Debtor

CASE NO. 02-65872 through 02-65877
Chapter 11
Jointly Administered

IN RE:

AGWAY GENERAL AGENCY, INC.

Debtor

IN RE:

BRUBAKER AGRONOMIC CONSULTING SERVICE LLC

Debtor

IN RE:

COUNTRY BEST ADAMS, LLC

Debtor

IN RE:

COUNTRY BEST-DEBERRY LLC

Debtor

IN RE:

FEED COMMODITIES INTERNATIONAL LLC

Debtor

APPEARANCES:

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Hon. Stephen D. Gerling, Chief U.S. Bankruptcy Judge

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MEMORANDUM-DECISION, FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER

The Court has under consideration a motion filed on March 14, 2008, on behalf of ACE American Insurance Company, Bankers Standard Fire and Marine Insurance Company, Illinois Union Insurance Company, Insurance Company of North America, Pacific Employers Insurance Company and other members of the ACE USA group of companies (collectively "ACE").

ACE requests an Order (a) allowing them to withdraw their prepetition claim (No. 4091), as amended (No. 4770), "subject to ACE's right to draw upon the collateral for Pre-Petition Obligations, and dismiss as moot the Liquidating Trustee's Motion to Fix the Pre-petition Claim,

(b) dismiss[ing] as moot the Liquidating Trustee's Motion to Fix any future Post-Petition Claim based on ACE's waiver of its right to an Administrative Claim for Post-Petition Obligations that fall due after the bankruptcy case is closed, subject to ACE's rights to draw upon the collateral for such Post-Petition Obligations, and (c) compel[ling] arbitration, under the parties' Program Agreement, of the remaining dispute concerning the amount of collateral held by ACE pursuant to the parties' Program Agreement."

Originally scheduled to be heard on April 29, 2008, ACE requested an adjournment to June 24, 2008, by letter filed April 24, 2008, in order to continue settlement discussions. On June 19, 2008, D. Clark Ogle, liquidating trustee ("LT") for the above-referenced debtors, filed opposition to ACE's motion.

The motion was heard at the Court's regular motion calendar in Utica, New York, on June 24, 2008. The Court afforded the parties an opportunity to file memoranda of law. The matter was submitted for decision on August 1, 2008.

JURISDICTIONAL STATEMENT

The Court has core jurisdiction over the parties and subject matter of these contested matters pursuant to 28 U.S.C. §§ 1334 and 157(a), (b)(1), (b)(2)(A), (B) and (O).

FACTS

Agway, Inc., along with several of its wholly-owned subsidiaries (collectively, the

"Debtors"), filed for bankruptcy protection pursuant to chapter 11 of the U.S. Bankruptcy Code, 11 U.S.C. §§ 101-1330 ("Code"), on October 1, 2002. According to ACE, "beginning on June 30, 2000, ACE issued various high deductible and restrospectively rated workers compensation policies, as well as high deductible automobile and general liability insurance policies on behalf of Agway and its debtor and non-debtor subsidiaries." *See* Motion to Compel Arbitration, filed July 17, 2006, at ¶ 22. Pursuant to a combined multi-line program agreement ("Program Agreement"), Agway provided ACE with a surety bond and certain letters of credit as security, which ACE argues are not property of the bankruptcy estates.

On May 21, 2003, the Court signed an Order pursuant to Rule 9019 of the Federal Rules of Bankruptcy Procedure approving a Settlement Agreement executed by the parties on April 17, 2003. According to ACE, the Settlement Agreement required the Debtors "to satisfy their obligations in full under the insurance policies and Program Agreements from September 30, 2002 going forward, and to satisfy their obligations under the same agreements from June 30, 2002 to September 30, 2002 up to a cap of $2.5 million." *Id.* at 28, citing to ¶1(a) of the Settlement Agreement. The Settlement Agreement recognized ACE's rights to draw upon certain collateral[1] in the event that the Debtors failed to satisfy their obligations under the Policies and Program Agreements.

On March 6, 2003, the Court entered an Order establishing May 30, 2003, as the final date

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[1] Attached as Exhibit "B" to the Settlement Agreement is a list of collateral: (1) Surety Bond issued by Fidelity and Deposit Company of Maryland in the amount of $10,374,458; (2) Letter of Credit issued by General Electric Capital Corporation in the amount of $5,000,000; (3) Letter of Credit issued by General Electric Capital Corporation in the amount of $4,251,074, and (4) Letter of Credit issued by General Electric Capital Corporation in the amount of $5,374,468. According to ACE, it has released the $5 million letter of credit and is holding collateral of $14,636,064, consisting of a surety bond in the remaining amount of $5,803,713 and letters of credit in the remaining amount of $8,832,351.

for filing proofs of claims against the Debtors. ACE filed what it describes as a "protective proof of claim," on May 30, 2003, indicating an unliquidated claim estimated to be "in excess of $7,400,000," and collateral valued at $24,502,442. It filed an amended proof of claim, dated February 28, 2006, identifying collateral, in the forms of letters of credit and surety bond, in excess of $21 million. In its Addendum to Amended Proof of Claim, it states that "ACE consents only to this Court's jurisdiction to determine the amount of ACE's allowed claim against the bankruptcy estate and not for any other purpose, including without limitation, the sufficiency of the collateral held by ACE.

On April 14, 2004, ACE filed an objection to the Debtors' First Amended Joint Plan of Liquidation (Dkt. No. 4986) based, *inter alia*, on its contention that the Plan did not address the Settlement Agreement. Debtors' Second Amended Joint Plan of Liquidation (the "Plan") was approved by Order of the Court on April 28, 2004 (Dkt. No. 5062), made effective May 1, 2004, and, *inter alia*, provided that the LT assumed the Debtors' rights and obligations under the Settlement Agreement, including the Program Agreement first executed on June 30, 2000. The Plan also provided that the Settlement Agreement, the ACE Insurance Policies and the Program Agreement were to remain in full force and effect. *See* Plan at Art. VII, ¶ 7.01(n)(i).

> The Plan also addresses tort claims. Specifically, it provides that
> [t]o the extent that any holder of a Tort Claim has recourse to any insurance policy issued to or for the benefit of the Debtors, for amounts in excess of the Debtors' deductible and self-insured retention amounts, if any, the holder of such Claim must first, to the satisfaction of the Debtors or the Liquidating Trustee, use its best efforts to collect that portion of its Allowed Claims in excess of the Debtors' deductible and self-insured retention amounts from the Insurance Carrier. Any remaining unpaid portion of such Tort Claim shall be treated as an Allowed General Unsecured Claim. Any liquidated and determined Tort Claim shall be the obligation of, and satisfied, by any applicable insurance agreement providing coverage for the Tort Claim in excess of any applicable Debtors' deductible or self-insured retention. The holder of such a Tort Claim may not recover from the Insurance Carrier the difference

> between the amount of any distribution paid to the holder of such Claim pursuant to the Plan and the balance of the Debtors' deductible and self-insured retention amount. Any allowed Tort Claim which falls within the Debtors' deductible and self-insured retention amounts shall be asserted solely against the Liquidating Trust and not against any Insurance Carrier.

Art. V, ¶ 5.06(c) (emphasis supplied).

On August 26, 2004, the LT filed a motion to fix ACE's prepetition claim. In ACE's motion currently under consideration, it states that during oral arguments in 2006 in connection with the LT's 2004 motion to fix ACE's claim "it became clear that the LT disputed the amount of collateral that ACE was holding under the Program Agreement. * * * For this reason, ACE filed a separate Motion to Compel Arbitration of the collateral amount pursuant to the Program Agreement. . . . ACE also moved to stay the LT"s Motion to Fix pending the arbitration. *See* ACE's Motion, at ¶¶ 56-57.

By Order, dated September 14, 2006, the Court denied ACE's motion to compel arbitration, as well as its motion to stay the LT's motion to fix ACE's prepetition claim pending arbitration. The Court later agreed to stay the LT's motion pending the appeal of its denial of ACE's motion to compel arbitration. On February 5, 2008, the Hon. Lawrence E. Kahn, United States District Judge for the United States District Court for the Northern District of New York, affirmed the decision of this Court insofar as it "concluded that the LT's motion to fix ACE's claim was properly before it and not subject to arbitration . . . ." Judge Kahn also ordered that "ACE may make an application to the Bankruptcy Court requesting arbitration of the amount of collateral only . . ."

In Judge Kahn's Decision and Order of February 5, 2008, he observed,

> [t]he Court understands that, under the Program Agreement, ACE may be entitled to hold collateral that takes into account future loss development and future losses. As a practical matter, however, it is curious why it is important to ACE to determine

> collateral outside the bankruptcy proceeding because the bankruptcy proceeding may well fix and determine the debtor's and, thus, ACE's exposure to future claims. If future claims against the debtor are precluded, then ACE's potential exposure is fixed and the amount of collateral necessary to secure its interests becomes a known certainty.

Judge Kahn's Decision and Order at Footnote 3.

ARGUMENTS

ACE acknowledges that Agway and the LT have been paying the postpetition obligations on a current basis as required by the Settlement Agreement and the Plan, making it unnecessary to draw upon the collateral to satisfy those particular obligations. *See* ACE's Motion at ¶ 62. According to ACE, it is willing to withdraw its prepetition claim and rely solely on its collateral, which it contends is not property of the estate. ACE acknowledges that if the Court grants ACE's motion to withdraw its claim and the collateral proves insufficient to satisfy Agway's prepetition obligations, it is willing to waive a recovery from the assets of the bankruptcy estate as a general unsecured creditor. *Id.* at ¶¶ 87-88. ACE also notes that it has not filed a motion for payment of any administrative claim for the postpetition obligations and, therefore, there is no postpetition claim for this Court to "fix." ACE also expresses its willingness to rely on the collateral to satisfy any postpetition obligations that may fall due after the case is closed provided that the LT continues to pay the postpetition obligations as they become due on a current basis until the case is closed. *Id.* at ¶ 71, ¶ 98. It is ACE's position that the only remaining dispute concerning the amount of collateral would be subject to arbitration under the terms of the Program Agreement. According to ACE, an arbitrator would project losses and expenses in its determination of the value of the

collateral necessary to protect ACE's claim going forward, but it would not be necessary for the arbitrator to fix ACE's claim. "ACE vehemently disputes that there is any relation between any allowed estimated amount of its claim under the Bankruptcy Code and the amount of the collateral required under the relevant agreements between ACE and Agway, Inc." *See* ACE's Motion to Compel Arbitration, filed July 17, 2006, at ¶ 17. ACE's concern is that the LT wants to use the allowed estimated amount of ACE's claim to limit ACE's rights to draw upon the collateral by disallowing or expunging a portion of ACE's claim. It is ACE's view that once the Court has ruled on the LT's motion to fix ACE's claim, the LT will file a motion seeking to reduce the amount of collateral required under the Program Agreement. *Id.* at ¶ 11, citing March 7, 2006 transcript at 14-15.

The LT argues that ACE does not meet the standard for withdrawing its proof of claim. The LT points out that four years have passed since confirmation of the Debtors' Plan. During that time, ACE has actively participated in the case, including negotiating various rights under the Settlement Agreement. According to the LT, the Court has jurisdiction to determine ACE's claim regardless of whether the collateral securing the claim is property of the estate. LT points out that the Debtors purchased the collateral and have pledged dollar for dollar assets of the estate to collateralize the letters of credit. The LT argues that every dollar that comes back to the estate has a positive effect on the distribution to creditors.

DISCUSSION

A creditor that files a proof of claim submits itself to the summary jurisdiction of the

bankruptcy court. *In re CBI Holding Co., Inc.*, 529 F.3d 432, 466 (2d Cir. 2008). It is the act of filing a proof of claim that triggers the process of allowance and disallowance of claims. *Id.* Rule 3006 of the Federal Rules of Bankruptcy Procedure ("Fed.R.Bankr.P.") allows a creditor to withdraw its proof of claim unless "an objection is filed thereto or a complaint is filed against that creditor in an adversary proceeding, or the creditor has accepted or rejected the plan or otherwise has participated significantly in the case. . . ." Fed.R.Bankr.P. 3006. In those scenarios, withdrawal is only possible on "order of the court after a hearing on notice . . . ."

ACE's participation in this case basically began with its execution of a Settlement Agreement on April 17, 2003, as approved by the Court on May 21, 2003. On May 30, 2003, ACE filed its proof of claim, indicating an unliquidated claim estimated to be "in excess of $7,400,000," and collateral valued at $24,502,442. On February 20, 2004, it filed a limited objection to the Debtors' Disclosure Statement, dated January 16, 2004, (Dkt. No. 3800). On April 14, 2004, it filed a limited objection to the Debtors' First Amended Joint Plan of Liquidation, dated February 26, 2004 (Dkt. No. 4986). On April 20, 2004, ACE also filed a motion seeking an administrative claim with respect to postpetition insurance obligations (Dkt. 5039), which it later withdrew by Stipulated Order, signed on June 17, 2004. In the interim, on May 25, 2004, the LT also sought an Order fixing workers' compensation claims of ACE, as well as Reliance Insurance Company (Dkt. No. 5176) to which ACE filed an objection on June 30, 2004 (Dkt. No. 5305). On August 26, 2004 the LT filed a motion seeking an order fixing the claim filed by ACE (Dkt. No. 5506) to which ACE filed an objection on October 25, 2004 (Dkt. No. 5704). By Order dated May 19, 2005, ACE was also permitted to intervene in a hearing concerning the LT's motion, filed on August 26, 2004, to expunge the claims of The Travelers Indemnity Company pursuant to Code § 502(e)(1)(B).

Approximately a year later, on July 17, 2006, ACE filed a motion seeking to compel arbitration and to stay consideration of the LT's motion for an order fixing ACE's claims (Dkt. No. 6499) to which the LT filed his objection on July 27, 2006 (Dkt. No. 6516). On September 14, 2006, following a hearing held on August 1, 2006, the Court signed an Order denying ACE's motion (Dkt. No. 6590). In turn, ACE filed an appeal of the Court's September 14, 2006 Order on September 25, 2006 (Dkt. No. 6602), as amended October 16, 2006 (Dkt. No. 6634). As indicated in the Facts, on appeal Judge Kahn affirmed the decision of this Court insofar as it "concluded that the LT's motion to fix ACE's claim was properly before it and not subject to arbitration . . . ." On March 14, 2008 ACE filed the motion which is the subject of this decision.

Not only has the LT objected to ACE's claim by seeking to have it fixed by this Court, ACE has also accepted the Debtors' Plan. It is also the opinion of this Court that the pleadings and other documents filed by ACE, as described above, constitute its significant participation in the case. Accordingly, the Court must consider whether to allow ACE to withdraw its proof of claim at this juncture of the case.

The LT suggests that the Court consider factors found in the case of *Zagano v. Fordham Univ.*, 900 F.2d 12 (2d. Cir. 1990). In *Zagano* the court considered plaintiff's motion pursuant to Rule 41(a) of the Federal Rules of Civil Procedure ("Fed.R.Civ.P.") seeking to dismiss her complaint against her former employer. The court considered the following factors in ultimately affirming the district court judge's denial of plaintiff's motion:

> plaintiff's diligence in bringing the motion; any "undue vexatiousness" on plaintiff's part; the extent to which the suit has progressed, including the defendant's effort and expense in preparation for trial; duplicative expense of relitigation; and the adequacy of plaintiff's explanation for the need to dismiss.

Id. at 14. These same factors have also been considered in the context of a motion pursuant to

Fed.R.Bankr.P. 3006. *See In re 20/20 Sport, Inc.*, 200 B.R. 972, 979 (Bankr. S.D.N.Y. 1996). In this case, the factors clearly do not favor ACE. As discussed above, ACE certainly has not been diligent in seeking to withdraw its proof of claim, which was filed some five years ago. The Debtors' Plan was confirmed more than four years ago. Both parties have incurred substantial time and expense in attempting to resolve various issues relating to said claim both in this Court and the District Court. As for ACE's explanation for the need to withdraw its claim at this juncture, it is clear that it wishes to exercise its rights under the Program Agreement. It again prefers to seek arbitration in connection with the determination of the value of its collateral based on projected losses. It simply does not want this Court to determine its claim based on provisions of both the Code and the Plan.

The Court agrees with ACE, however, that in ruling on its motion, the real issue to be considered is whether the LT and/or the estate would be legally prejudiced by the withdrawal of the proof of claim. *See In re Ogden New York Servs., Inc.*, 312 B.R. 729, 732 (S.D.N.Y. 2004); *In re Kaiser Group Intern., Inc.*, 272 B.R. 852, 855 (Bankr. D.Del. 2002). This entails an examination of whether granting the motion would result in prejudice "to some legal interest, legal claim or legal argument" of the LT. *See id.*, citing *Westlands Water Dist. v. U.S.*, 100 F.3d 94, 97 (9th Cir. 1996).

In his motion seeking to fix the claim of ACE, the LT relies on provisions of the Bankruptcy Code, as well as provisions of the Plan. In this regard, ACE disputes that Code § 502(e) is a basis to expunge its claim arising out of the workers compensation policies as to prepetition occurrences. It is ACE's position that as an insurer with a direct contractual relationship with the Debtor to pay workers compensation claims, it is not a co-debtor within the meaning of Code § 502(e)(1). ACE also disputes the LT's contention that the claim is contingent, as required under Code §

502(e)(1)(B). In addition, ACE takes the position that even if the Court were to disallow all or a portion of its prepetition claim arising under the workers compensation policies, it would not limit ACE's ability to draw upon the collateral for any payments that it makes and expenses it incurs.

ACE also takes issue with the LT's attempt to limit the amount of ACE's secured prepetition claim under the automobile and general liability policies by relying on the Plan provision that requires Tort Claimants to assert their claims against the LT and not against insurers such as ACE where their claims fall within the deductible and retention amounts of the policies. According to the LT, "ACE has not, and will not, disburse any funds and/or incur any defense costs with respect to claims which fall within the deductible and/or self-insured retention amounts; as a result, ACE has no basis for a claim under the policies for the period prior to June 29, 2002." *See* LT's Motion for and Order Fixing Claim, filed August 26, 2004 (Dkt. No. 5506) at ¶ 33. ACE argues that despite the provision in the Plan, ACE is not prevented from exercising its rights to pay claims within the deductible limits. According to ACE, "there could be numerous claims that are not subject to the Plan's provision." *See* ACE's Response in Opposition to LT's Motion for an Order Fixing Claim, dated October 25, 2004 (Dkt. No. 5704) at ¶ 81.

These are legal issues/arguments for which this Court clearly has the jurisdiction to decide, as affirmed by the District Court. Whether or not the LT is correct in his arguments concerning ACE's claim and ACE's entitlement to the remaining collateral is for this Court to determine. They are not issues or arguments that would be given any consideration by an arbitrator. ACE has participated in not only the execution of the Program Agreements and the Settlement Agreement, it also participated in the confirmation process. Having received an unfavorable ruling in this Court and the District Court, it apparently believes its best approach is to "take its ball and go home" in

the top of the ninth inning before the LT has had its final opportunity at bat. Both parties should have an opportunity to make their legal argument before this Court in the context of the LT's motion seeking to fix ACE's claim based on Code § 502(e) and the provisions of the Plan. Without that opportunity, the Court concludes that the LT's interests would be legally prejudiced.

Based on the foregoing, it is hereby

ORDERED that ACE's motion pursuant to Fed.R.Bankr.P. 3006(a), seeking withdrawal of its proof of claim, is denied; it is further

ORDERED that ACE's motion to the extent that it seeks dismissal as moot of the LT's Motion to Fix its Claim is denied; and it is finally

ORDERED that ACE's motion asking that the Court compel arbitration of the issue of the amount of collateral held by ACE is denied without prejudice to its renewal once the Court has ruled on the LT's Motion to Fix its claim.

Dated at Utica, New York
this 16th day of December 2008

STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge