In the United States Bankruptcy Court

for the Northern District of Iowa

J.E. ADAMS INDUSTRIES LTD. *Debtor(s).*	Bankruptcy No. 98-00167-C Chapter 7
J.E. ADAMS INDUSTRIES LTD. and REPUBLIC CREDIT CORPORATION I *Plaintiff(s)* vs. AURORA NATIONAL LIFE ASSURANCE COMPANY *Defendant(s)*	Adversary No. 00-9056-C

Appealed to U.S.D.C. on 09-28-2000
Reversed and Remanded by U.S.D.C. 09-28-2001

RULING RE MOTIONS FOR SUMMARY JUDGMENT

On August 17, 2000, the above-captioned matter came on for hearing pursuant to assignment. The matters before the Court are competing Motions for Summary Judgment as to Count II of the Complaint. Attorney Thomas Fiegen appeared for Plaintiff J.E. Adams Industries, Ltd. and Attorney Eric Lam appeared for Plaintiff Republic Credit Corp. Attorney Jeff Taylor appeared for Defendant Aurora National Life Assurance Co. After hearing argument of counsel, the Court took the matter under advisement. The parties stipulated to all operative facts and filed prehearing briefs. This is a core proceeding pursuant to 28 U.S.C. §157(b)(2)(A), (G), and (O).

STATEMENT OF THE CASE

This adversary proceeding arises in the case of J.E. Adams Ltd., a Chapter 11 reorganization. A plan has been confirmed in the Chapter 11 reorganization. The question presented is whether the automatic stay prevents an insurance company, which carries a life insurance policy owned by Debtor, from declaring the policy lapsed for failure to pay premiums and failure to cure defaults within the grace period provided in the policy. Additional threshold questions are also presented in this context.

Debtor J.E. Adams Industries filed the pending adversary complaint on March 31, 2000, and Republic Credit Corp. joined as a party plaintiff. The complaint is in two counts. Count I is entitled "Breach of the Duty of Good Faith and Course of Dealing". This Count seeks monetary damages based upon the alleged loss of the life insurance policy in question. Count II is captioned "Violation of the Automatic Stay". In this Count, Debtor asserts a violation of the automatic stay by Defendant Aurora National Life. Only Count II is at issue in the parties competing Motions for Summary Judgment. Republic Credit Corp. moves for summary judgment on Count II, joined by Debtor J.E. Adams Indus.

Defendant Aurora National Life filed a cross-motion for summary judgment. They seek a determination of whether there was a violation of the automatic stay.

FACTS

J.E. Adams Industries, Ltd. (Debtor) purchased a whole life insurance policy covering its CEO, Jack E. Adams, from Executive Life Insurance Company (ELIC) on March 26, 1988. On September 3, 1993, as the result of ELIC's insolvency and rehabilitation plan, Aurora National Life Assurance Company (Aurora) assumed and reinsured substantially all of the life insurance policies and annuity contracts previously held by ELIC.

Debtor's policy had a March 26 anniversary date and required the payment of premiums to keep the policy in force. Debtor elected to pay the premiums in quarterly installments. According to the terms of the insurance policy, if the policyholder fails to pay a premium payment when due, Aurora would attempt to continue coverage by the application of available funds under the policy.

The policy in question contains a non-forfeiture option that converts it from a whole life policy to a term life policy, subject to cancellation, at the end of a 31 day grace period after a default in payment. The default options in the policy require Aurora to provide notice to the policy holder. Additionally, Aurora is obligated by the terms of the contract to provide notice to the policy holder of the due dates for the quarterly payments prior to the date when those payments come due.

Debtor filed a voluntary Chapter 11 petition on January 21, 1998 in the United States Bankruptcy Court for the Northern District of Iowa. After the filing, J.E. Adams operated the company as debtor-in-possession. Aurora had actual knowledge of this filing no later than December 18, 1998 by way of an overnight letter dated December 17, 1998 from counsel for Debtor disclosing the Chapter 11 filing and requesting a loan against the available cash value in the policy.

The Court confirmed Debtor's Chapter 11 Plan on March 24, 2000. In the plan, Debtor assigned its interest in the policy to Firstar, a creditor. Confirmation of the plan does not impact the resolution of this adversary proceeding.

In December 1998, Debtor requested and received a loan from Aurora for $65,802.67, the maximum amount available under the insurance policy. After the loan, the policy with Aurora had only enough remaining cash value to support the payment of the quarterly premium due on December 26, 1998. Because Debtor did not otherwise pay the December 26, 1998 premium payment, the remaining cash value in the policy converted into an automatic premium loan according to the terms of the policy. On March 5, 1999 Aurora mailed Debtor a notice stating that the next quarterly payment was due on March 26, 1999.

After Debtor defaulted on the March 26, 1999 payment, Aurora sent Debtor three additional notices. The April 16, 1999 notice was a 20-day reminder advising Debtor that the premium had not been paid, and if the premium remained unpaid at the expiration of the grace period, the policy would convert to an extended term life policy. This conversion is consistent with the non-forfeiture option in the policy. The April 26, 1999 notice informed Debtor that the grace period had expired on the policy. The June 3, 1999 notice advised Debtor that as a result of the default the policy had converted into a term life policy and the expiration date would be July 3, 1999 in the event that no additional payments were made toward maintaining the policy. Aurora's final letter dated July 3, 1999 notified Debtor that the policy had lapsed and that Aurora would provide no further coverage under the terms of the policy.

On July 9, 1999, Debtor sent Aurora a letter stating that it had not received any notice prior to the July 3 letter informing it of the cancellation of the policy. With this letter, Debtor sent a check to Aurora for the continuation of the whole life policy in an amount intended to cover the premiums for the last two quarters. The amount that Debtor sent would have been insufficient to cover the amount overdue on the whole life policy. Aurora did not file a motion for relief from the automatic stay, or to compel assumption or rejection of the policy. Jack E. Adams died on December 9, 1999.

DISCUSSION

Plaintiffs Republic Credit Corp. and Debtor assert that Aurora violated the automatic stay. They allege that violations occurred both when Aurora sent notification letters of payments due and of cancellation and when Aurora terminated the policy. They base these assertions on the premise that the insurance policy is a part of Debtor's estate and as property of the estate, it is protected by the automatic stay from action that would exert control over or otherwise remove that property from the estate.

Aurora claims that it may cancel the policy based on Debtor's failure to pay premiums. It asserts the contract is contingent on the timely payment of premiums. Aurora also argues that Debtor may not remedy the breach after the grace period expires, because the grace period for remedy is not tolled indefinitely by the application of the automatic stay. Finally, Aurora claims that it took no affirmative action against the property of the debtor, but rather the contract reached its natural end and lapsed.

Three questions are presented. First, is the insurance policy a part of the debtor's estate. Second, is the insurance policy an executory contract and, if so, what are the parties' obligations. Finally, if the policy is property of Debtor's estate, the Court must decide how the automatic stay applies, whether the grace period for default is tolled, and whether Aurora's actions constitute a violation of the automatic stay.

PROPERTY OF THE ESTATE

If the insurance policy is not a part of the debtor's estate, there can be no violation of the automatic stay. The automatic stay only applies to property that is a part of the bankruptcy estate. 11 U.S.C. § 362; In re National Cattle Congress Inc., 179 B.R. 588 (Bankr. N.D. Iowa 1995) (explaining the application of the automatic stay to property of the estate, and expansively defining what constitutes property of the estate). Section 541(a) defines the property of the estate as "all legal or equitable interests of the debtor in property as of the commencement of the case." This includes both tangible and intangible interests in property. S. Rep. No. 95-989 95th Cong., 1st sess. 82 (1978). Courts have acknowledged that insurance policies are part of the debtor's estate. See, e.g., Bursch v. Beardsley & Piper, 971 F.2d 108, 115 n.8 (8th Cir. 1992) (stating that "a debtor's interest in an insurance policy is property of the debtor's estate."); In re Titan Energy, 837 F.2d 325, 328 (8th Cir. 1988) (finding that products liability insurance is a part of the estate); Estate of Lellock v. Prudential Ins. Co., 811 F.2d 186, 189 (3rd Cir. 1987) (discussing an unmatured life insurance policy, the court stated, "We hold that an insurance policy is property of the estate . . . 'even though the policy has not matured, has no cash surrender value and is otherwise contingent.'"). The weight of authority supports the conclusion that the insurance policy in question here is an asset of Debtor's estate and this Court so finds.

EXECUTORY CONTRACT

It is critical to determine if the policy in question is an executory contract. If it is, the nature of the estate's property interest and the obligations of the parties are contingent on assumption or rejection of

the contract. 11 U.S.C. § 365. The Bankruptcy Code does not expressly define "executory contract". The Supreme Court has stated that "the legislative history to § 365(a) indicates that Congress intended the term to mean a contract 'on which performance is due to some extent on both sides.'" N.L.R.B. v. Bildisco & Bildisco, 465 U.S. 513, 522 (1984) (citing H.R. Rep. No. 95-595 p. 347 (1977)). An executory contract is defined as one where so much of the contract is unperformed that a failure to perform on the part of either party would constitute a breach that would excuse the other's performance. Vern Countryman, Executory Contracts in Bankruptcy Part I, 57 Minn. L. Rev. 439, 460 (1973). Thus, the Court must decide whether performance is due on both sides of the insurance policy.

Courts and commentators have concluded that insurance policies are executory contracts. See, e.g., Counties Contracting & Constr. v. Constitution Life, 855 F.2d 1054, 1060 (3d. Cir. 1988); In re Pester Ref., 58 B.R. 189, 191 (Bankr. S.D. Iowa 1985); In re American Medical Imaging Corp., 133 B.R. 45, 55 (Bankr. E.D. Pa. 1991). In reference to insurance policies, Colliers states "the policy is essentially an executory contract that may be assumed or rejected by the trustee. Continued coverage should be based on the trustee's assumption of the contract." 1 Collier Bankruptcy Manual ¶362.03[3][b], at 362-17 (Lawrence P. King ed.,3d ed. 1999). Debtor's policy is an executory contract. Debtor was obligated to perform by paying premiums and Aurora was obligated to pay out at the death of Jack E. Adams.

If the policy is an executory contract, the debtor-in-possession must assume the contract to enforce its terms. Bildisco, 465 U.S. at 529. The trustee or debtor-in-possession has the option, pending court approval, to assume or reject the terms of an executory contract. Id. "In a chapter 11 reorganization a debtor-in-possession has until a reorganization plan is confirmed to decide whether to accept or reject an executory contract." Pester Ref., 58 B.R. at 191 n.1. Thus, Debtor has until plan confirmation to assume or reject the policy.

The Third Circuit has rejected the notion that the chapter 11 debtor-in-possession has the option of waiting until plan confirmation to assume or reject the contract, if the contract will expire by its own terms. Counties, 855 F.2d at 1061. Counties is distinguishable because the breach was pre-petition. Counties, 855 F.2d at 1056. Here, it is post-petition. If the breach occurs post-petition, the debtor's obligation to pay the premiums is stayed, while the creditor is obligated to provide service pending acceptance or rejection of the contract. In re Feyline Presents, Inc., 81 B.R. 623, 626 (Bankr. D. Colo. 1988) (stating that "an executory contract under Chapter 11 is not enforceable against the debtor party, but is enforceable against the non-debtor party prior to the debtor's assumption or rejection of the contract."). This means that Aurora is still obligated to honor the policy, despite the debtor's failure to pay the premiums, until the policy is assumed or rejected.

The Bankruptcy Code functions to protect the interests of the estate by allowing an evaluation of the benefits and burdens of an executory contract before it must be assumed or rejected. Bildisco, 465 U.S. at 528-33. This takes into account the possibility that the debtor may default because when a debtor assumes an executory contract, the estate must pay full dollar value for the contract as well as remedy any breach that may exist. Id.at 531. Section 365(b)(1)(a) specifically provides that "[i]f there has been a default in an executory contract . . . the trustee may not assume the contract . . . unless, at the time of the assumption of such contract . . . the trustee[ ] cures . . . such default." The Supreme Court elaborated on §365(b)(1)(a) in Bildisco. "If the debtor-in-possession elects to continue to receive benefits from the other party to an executory contract pending a decision to reject or assume the contract, the debtor-in-possession is obligated to pay for the reasonable value of those services . . ." Bildisco, 465 U.S. at 531. In the event the debtor rejects the contract, the non-debtor will assume a

place in line as a general unsecured creditor under the plan. Id. Thus, in the case at bar, Aurora will be paid the total amount of the premiums that are in arrears if and when the estate assumes the contract.

The Code also effects its purpose by enforcing the contractual obligations of the non-debtor in an executory contract, thereby providing the debtor with breathing room from the claims of its creditors. Id.; In re Public Serv. Co., 884 F.2d 11, 15 (1st Cir. 1989). The policy rationale behind enabling debtors to wait until plan confirmation to assume or reject contracts is central to bankruptcy as a whole. Bildisco, 465 U.S. at 528-33 (discussing how successful reorganization depends on easing the burdens of prepetition contracts until the plan is confirmed); In re Whitcomb & Keller Mortgage Co., 715 F.2d 375, 379 (7th Cir. 1983) (while discussing the assumption of executory contracts, the court noted that "the purpose of the Bankruptcy Code" is to alter contractual relations to ease the burden on the reorganizing debtor).

As a creditor, Aurora may have sought Court intervention to compel Debtor to assume or reject the contract within a specified time frame. Public Serv., 884 F.2d at 15. "Parties who wish to know where they stand may, pursuant to §365(d)(2) seek to compel an early election: 'the court, on the request of any party to [an executory] contract . . . may order the trustee to determine within a specified period of time whether to assume or reject such contract . . . .'" Id. at 15 (quoting 11 U.S.C. § 365(d)(2)). However, the decision to grant this order is still subject to approval of the court which acts at its discretion. Id. Aurora has not petitioned the Court to compel an early election under §365(d)(2).

THE AUTOMATIC STAY

Having determined that the insurance policy is both property of the estate and an executory contract, the Court must decide whether the lapse of policy violated § 362 of the bankruptcy code. 11 U.S.C. § 362(h). Any action that violates the automatic stay is void ab initio. In re Vierkant, 240 B.R. 317, 321-23 (B.A.P. 8th Cir. 1999). Property of the estate is protected by the application of the automatic stay under § 362. The automatic stay precludes creditors from taking action against the property of the estate in the absence of a grant of relief from the court. 11 U.S.C. § 362.

In some cases, the automatic stay has prevented the cancellation of insurance policies by the insurance company. See, e.g., In re Minoco Group of Companies, Ltd., 799 F.2d 517, 520 (9th Cir. 1986) (stating that cancellation of liability insurance policies is automatically stayed by section 362(a)); Pester Ref., 58 B.R. at 191; In re J & L Transp. Inc., 47 B.R. 51, 52 (Bankr. W.D. Wis. 1985). Even the enforcement of a contractual provision against the debtor in possession is prevented until the debtor assumes the contract. Pester Ref., 58 B.R. at 191. These courts hold that after the debtor has filed for bankruptcy protection, § 362(a)(3) prevents the insurer from canceling the policy. J & L Transp., 47 B.R. at 52. The cancellation could injure the debtor in a manner that makes reorganization impossible, and essentially takes property from the estate. Id.

By the terms of the contract, the policy lapses if a default is not cured within 31 days. Aurora argues that the operation of the automatic stay will not alter the terms of the contract. Hazen First State Bank v. Speight, 888 F.2d 574, 576 (8th Cir. 1989) (stating that the automatic stay "does not enlarge the rights of individuals under a contract nor does it toll the running of time under a contract. It will not prevent the termination of a contract by its own terms."). In Hazen however, the running of time related to a statutory redemption period for a security interest, not a contract clause that required prompt payments by the debtor. Id. at 575. The court in Hazen was also referring to a time period that began running pre-petition. Id. at 576-77. In this case, the Debtor made timely payments on the contract for more than a year after filing. The time period in the cancellation clause began running post-petition.

That Debtor defaulted post-petition is critical, because after the commencement of the case, the failure to pay premiums is neither a breach that operates as a rejection of the contract nor does it excuse Aurora's performance. Bildisco, 465 U.S. at 528-33; Feyline, 81 B.R. at 626. The automatic stay tolls the grace period for executory contracts until the confirmation of the plan in a Chapter 11 case. Bildisco, 465 U.S. at 531. Aurora owed Debtor's estate performance on the policy until the debtor-in-possession rejected the contract. Aurora's cancellation of the policy is void as an act that takes a property interest from the estate and violates the automatic stay.

Aurora sent Debtor multiple letters notifying it that payments were due and that non-forfeiture options would be exercised. Section 362(a)(3) prohibits actions that exercise control over property of the estate. Money is property of the estate under § 541(a)(6). In re Southmark Corp., 49 F.3d 1111 (5th Cir. 1995). Section 362(a)(6) prohibits acts to collect claims that arose before commencement of the case. The insurance payments were current up to the default on March 26, 1999. Debtor filed for bankruptcy protection on January 21, 1998. The letters were not an attempt to collect a claim that arose pre-petition, and do not a violate § 362(a)(6). However, because each letter requested payment from the debtor, each was an act attempting to obtain possession of the property of the estate, and, as such, each letter violated § 362(a)(3). As each letter constituted a violation of the automatic stay, their effect was void ab initio.

EXTENSION OF TIME

Aurora argues that the automatic stay does not apply to its actions in this case because the policy ended on its own when the grace period to cure default ended. The question they pose is whether the automatic stay will toll the grace period until the stay is lifted. Several courts, including the 8th Circuit have held that the automatic stay will not permanently stay the running of a statutory time period, finding that 11 U.S.C. §108(b) is the controlling section. See generallyHazen, 888 F.2d 574; In re Maanum, 828 F.2d 459 (8th Cir. 1987); Johnson v. First Nat'l Bank, 719 F.2d 270 (8th Cir. 1983), cert. denied 465 U.S. 1012 (1984). Section 108(b) provides, in relevant part:

> (b) Except as provided in subsection (a) of this section, if applicable nonbankruptcy law, an order entered in a nonbankruptcy proceeding, or an agreement fixes a period within which a debtor . . . may file a pleading, demand, notice, or proof of claim or loss, cure a default, or perform any other similar act, and such period has not expired before the date of the filing of the petition, the trustee may only file, cure, or perform as the case may be, before the latter of-
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> > (1) the end of such period, including any suspension of such period occurring on or after the commencement of the case; or
> > (2) 60 days after the order for relief.

The Eighth Circuit has ruled that § 108 should be read in a manner harmonious with the automatic stay. Johnson, 719 F.2d at 277. Section 362 does not address the running of a statutory or contractual time period, while § 108 specifically provides a time frame that gives the debtor adequate temporal relief from the running of a grace or redemption period. 11 U.S.C. §§108(b), 362. The Eighth Circuit reasoned that if the automatic stay in § 362 tolls the running of a time period, then § 108 would be rendered ineffectual. Johnson, 719 F.2d at 278. Additionally, the court found that a historical analysis of the automatic stay, prior to the enactment of the current Code, supported the conclusion that the stay would not permanently toll the running of a statutory time period. Id. at 277.

Aurora relies heavily on Counties to support its argument that an insurance company may allow a policy to lapse despite the operation of the automatic stay. In Counties, the court extended Johnson, to apply to the grace period on an insurance contract, finding that the period of time could be tolled by operation of §108(b) for up to 60 days but not indefinitely. 855 F.2d at 1061. The Third Circuit noted that the Johnson decision emphasized the difference between affirmative actions in the automatic stay and the "explicit running of time" in §108. Id. at 1058. In its analysis, the court held that the expiration of a grace period to cure the debtor's default, when the debtor did not pay insurance premiums, and the subsequent cancellation of the policy, did not constitute an affirmative act by the insurer, but rather the explicit running of time. Id.

The critical distinction between Counties and the case at bar is that in Counties, the breach was pre-petition whereas in this case the breach is post-petition. Section 108(b) applies only to pre-petition claims. In re Dougherty, 187 B.R. 883, 886 (Bankr. E.D. Pa. 1995) (stating that: "it has been held that §108(b) extends the time period for asserting only pre-petition, as opposed to post-petition, claims."). Debtor was current in its premium payments for over a year after filing for bankruptcy protection. The default occurred, and the grace period began running, post-petition. Thus, § 108(b) does not apply.

OPERATION OF § 542(d)

Aurora argues that its actions were specifically authorized by § 542(d), and that on that basis, it did not violate the automatic stay. Section 542(d) contains a specific provision for the operation of non-forfeiture options in life insurance contracts. Section 542(d) authorizes the good faith transfer of property of the estate to pay premiums or to carry out non-forfeiture options that are required by the insurance contract to be carried out automatically. This provision applies only to policies held by the debtor prior to the bankruptcy filing. 11 U.S.C. § 542(d). Plaintiffs allege that the cancellation, not the non-forfeiture options, constituted a violation of the automatic stay. Section 542(d) contains no language authorizing the insurance company to cancel the policy, and there is no case law suggesting that it does. Therefore, § 542(d) may not be read to authorize cancellation.

CONCLUSION

All parties have moved for summary judgment. Under Fed.R.Civ.P. 56, the Court renders summary judgment when "there is no genuine issue as to any material fact and [ ] the moving party is entitled to a judgment as a matter of law." Because all parties concede there is no genuine issue as to any material fact, it is appropriate to grant summary judgment in favor of the party entitled to judgment as a matter of law.

The insurance policy is an executory contract and is property of the estate. The automatic stay applies to this contract, and prohibits Aurora from canceling the policy or enforcing other contractual provisions prior to confirmation of the plan. Section 542(d) enables Aurora to exercise the non-forfeiture options in the policy but does not function as an exception to the automatic stay and enable the policy to lapse. Section 108(b) only operates to toll the statutory or contractual time periods that are running at the time of filing. In this case, the grace period began to run postpetition. Allowing the insurance policy to lapse postpetition violates the automatic stay. In the absence of a genuine issue of material fact, summary judgment for Plaintiffs is warranted.

WHEREFORE, for the reasons set forth herein, Plaintiffs' Motion for Summary Judgment is GRANTED as to Count II.

FURTHER, the effect of granting Plaintiffs summary judgment as to Count II is that the cancellation of the life insurance policy in question is ineffective and void ab initio. The life insurance policy in question remains in effect according to its terms.

FURTHER, for the reasons set forth herein, the Motion for Summary Judgment by Defendant Aurora National Life Assurance Company is DENIED.

FURTHER, Count I remains unadjudicated and this matter should be set for a scheduling conference to determine how Plaintiffs intend to proceed on this Count.

FURTHER, a scheduling conference is set for

October 13, 2000 at 10:15 a.m.

by **TELEPHONIC CONFERENCE. ATTORNEY FOR PLAINTIFF J.E. ADAMS INDUSTRIES, LTD. IS TO INITIATE THE TELEPHONE CALL.** Parties should be ready and available to accept said call. The telephone number for Judge Kilburg's chambers is **(319) 286-2230**. **NOTE:** THIS HEARING WILL BE TAPED ON ELECTRONIC RECORDING EQUIPMENT.

SO ORDERED this 20th day of September, 2000.

Paul J. Kilburg
Chief Bankruptcy Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF IOWA
CEDAR RAPIDS DIVISION

J.E. ADAMS INDUSTRIES LTD. No. C00-190 MJM

J.E. ADAMS INDUSTRIES LTD. and REPUBLIC CREDIT CORPORATION I
Plaintiff(s)

vs.

AURORA NATIONAL LIFE ASSURANCE COMPANY
Defendant(s)

ORDER

The Bankruptcy Court for the Northern District of Iowa entered partial summary judgment in favor of co-plaintiffs J.E. Adams, Inc., and Republic Credit Corporation I (hereinafter Debtor). Aurora National Life Assurance Company (Aurora) appeals the decision in which the court held Aurora's cancellation of a "keyman" insurance policy held by J.E. Adams, Inc., violated the automatic stay imposed by 11 U.S.C. § 362(a)(3)[(1)]. For the following reasons, this court reverses the bankruptcy court's holding and remands the case for consideration of the remaining issues in Debtor's bankruptcy proceeding.

I. Standard of Review

The court reviews de novo the bankruptcy court's conclusions of law. *In re Commercial Millwright Service Corp.*, 245 B.R. 603, 606 (N.D. Iowa 2000). The bankruptcy court's findings of fact are reviewed for clear error. *In re Usery*, 123 F.3d 1089, 1093 (8th Cir. 1997). Summary judgment was properly entered if, assuming all reasonable inferences favorable to the on-moving party, there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(c); *Celotex Corp. v. Catrett* 477 U.S. 317, 322-23 (1986); *In re Commercial Millwright Service Corp*., 245 B.R. at 606. "'A finding is 'clearly erroneous' when although there is evidence to support it, the reviewing court is left with a definite and firm conviction that a mistake has been committed.'" *In re Hatcher*, 218 B.R. 441,445-46 (B.A.P. 8th Cir. 1998) (quoting Anderson v. Bessemer City, 470 U.S. 564, 573 (1985)).

II. FACTS

In March of 1988, J.E. Adams, Inc., purchased a whole life insurance policy (Policy), insuring its chief executive officer, Jack E. Adams. Debtor purchased the Policy from Executive Life Insurance Company (ELIC). However, in September of 1993, as a result of ELIC's insolvency, Aurora assumed the Policy. The Policy had an anniversary date of March 26 and Debtor made quarterly premium payments of $2,905.06. Debtor had a thirty-one day grace period if it did not make timely premium payments, after which provisions of the Policy dictated Debtor's and Aurora's rights and responsibilities. The Policy required Aurora to notify Debtor of approaching quarterly premium due dates if the Policy might terminate if payment was not received by the end of the grace period. In addition to the grace period, the Policy had several provisions to prevent forfeiture of the Policy. The first was a Premium Default Provision which allowed the cash value in the Policy to automatically pay a quarterly premium if the Policy holder failed to pay the premium due at the expiration of the thirty-one day grace period. If the Policy had insufficient cash value to pay the missed premium, the Policy was converted from a whole life policy to a term life policy pursuant to a Nonforfeiture Option in the Policy.

Debtor filed a Chapter 11 bankruptcy petition on January 21,1998, after which J.E. Adams operated the company as debtor-in-possession. Counsel for Debtor sent an overnight letter on December 17, 1998, nearly eleven months after the filing of the petition, notifying Aurora of the Chapter 11 filing. In addition, the letter requested a post-petition loan against the available cash value in the Policy. On December 22, 1998, Aurora loaned $65,802.67 to Debtor, the maximum amount available under the Policy. After the loan, the Policy had only enough cash value to pay one quarterly premium. Debtor did not pay the quarterly premium due on December 26, 1998, and at the expiration of the thirty-one day grace period, the remaining cash value in the policy was used to pay the premium pursuant to the Premium Default Option. Debtor was notified of this on March 6, 1999. On March 5,1999, Aurora sent Debtor a notice advising Debtor of the upcoming quarterly premium payment due on March 26, 1999. Debtor did not pay the March 26, 1999, quarterly premium. However, because of the loan against the Policy taken out by the Debtor, and the fact the remaining cash value of the Policy was applied to the December 26, 1998, quarterly premium, the Policy had no remaining available cash to apply to the missed premium.

Aurora advised Debtor by way of letter on April 16, 1999, that the Policy would be converted from a whole life to a term life policy if the premium was not paid by the end of the grace period. On April 26, 1999, Aurora notified Debtor that the grace period had expired. Then, on June 3,1999, Aurora notified Debtor the Policy was converted from a whole life to an extended term policy pursuant to the Nonforfeiture Option and that the Policy would expire on July 3, 1999. Debtor failed to make any

payment on the Policy before the expiration of the Policy and consequently, the extended term coverage ended on July 3, 1999.

On July 9,1999, Debtor sent Aurora a letter stating it had not received notice prior to the July 3,1999, letter notifying Debtor of the cancellation of the policy. Debtor attempted to pay the amount of the last two quarterly premiums. The amount was insufficient to cover the overdue premiums. J.E. Adams died on December 9,1999. The Bankruptcy Court confirmed Debtor's Chapter 11 plan on March 24, 2000. Debtor assigned its interest in the Policy to one of its creditors.

III. Discussion

The issue before the court is whether the cancellation of the Policy violates the automatic stay imposed by Debtor's filing of a Chapter 11 petition. Debtor and co-plaintiff below, Republic Credit Corporation, assert that Aurora's notification letters constitute affirmative acts "to engineer the cancellation process of a life insurance policy purchased by [Debtor]," and that such acts are in violation of the automatic stay imposed by 11 U.S.C. § 362(a)(1) and (3). Debtor suggests that J.E. Adams did not assume the Policy and, consequently, Aurora's cancellation of the Policy is in violation of 11 U.S.C. § 365. Further, Debtor urges the court to uphold the bankruptcy court's conclusion that 11 U.S.C. § 542(d) does not apply to the case at bar, and that 11 U.S.C. § 108(b) does not require J.E. Adams to have cured the default within the grace period provided for by the policy.

Aurora contends the automatic stay does not prevent a contract from expiring automatically by its terms, and that the notices provided by Aurora to Debtor were not affirmative acts within the meaning of the bankruptcy code. Aurora also urges the court to apply 11 U.S.C. § 542(d) to the cancellation of the policy. Additionally, Aurora contends that 11 U.S.C. § 108(b) prevents the automatic stay from indefinitely tolling the Policy's grace period.

A. 11 U.S.C. §362(a)

> The automatic stay provision relevant to this appeal provides:
>
> Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title . . . operates as a stay, Applicable to all entities, of--(1) the commencement or continuation including the issuance or employment of process, or 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, or to recover a claim against the debtor that arose before the commencement of the case under this title; . . . (3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate[.]

11 U.S.C. § 362(a)(1) and (3). First, the court will address section 362(a)(1). The court notes the events in question surrounding the Policy arose post-petition: the loan against the policy, the Premium Default Option, the Nonforfeiture Option, and the canceffation of the Policy for nonpayment of the March 26, 1999, quarterly premium Therefore, as Aurora points out, the events could not have Occurred pre-petition because Debtor did not default on the Policy until after fifing the Chapter 11 petition. *See Taylor V. First Federal Savings & Loan Ass'n of Monessen,* 843 F.2d 153, 153 (3rd Cir. 1986) ("Further,the automatic stay is not intended to bar proceedings for post-petition claims that could not have been commenced before the petition was filed."). In addition, the cancellation of the policy is not a proceeding, but rather a natural event flowing from the terms of the Policy. *See In re*

Vacation Villages Ltd. P'ship, 49 B.R.590, 593 (Bankr. N.D. Iowa 1984). As the *In re Vacation Villages* court stated:

> (Section] 362(a) stays an 'act,' or a 'proceeding,' or the 'enforcement' of a right. in a contract forfeiture situation, the contract vendor, once a notice of forfeiture has been served, need not act, proceed, or enforce in order to achieve forfeiture. in other words, nothing is expected or required from the contract vendor. On the other hand, it is the contract vendee who must act, proceed, or otherwise enforce its rights under the contract by curing.

Id. at 593 (citing *Johnson v. First Nat'l Bank of Montevideo*, 719 F.2d 270, 276 (8th Cir. 1983)) (footnote omitted). Therefore, Section 362(a)(1) does not have the relevance Debtor suggests.

The court prefaces its discussion of section 362(a)(3) with a general principle the Eighth Circuit has announced: "The automatic stay provided for by section 362(a) does not enlarge the rights of individuals under a contract nor does it toll the running of time under a contract. It will not prevent the automatic termination of a contract by its own terms." Hazen First State Bank v. Speight, 888 F.2d 574, 576 (8th Cir. 1989). This precept proscribes the court from reading beyond the statute imposing the automatic stay and from rewriting the Policy. Debtor seeks to have Aurora insure J.E. Adams beyond the terms of the contract because Debtor has filed a bankruptcy petition: "A contract that provides for termination on the default of one party may terminate under ordinary principles of contract law even if the defaulting party has filed a petition under the Bankruptcy Act." *Trigg v. United States*, 630 F.2d 1370, 1374 (10th Cir. 1980). The holding Debtor seeks would allow Debtor the benefit of the Policy with none of the accompanying costs or risks. Debtor wants Aurora to continue a policy that Debtor has defaulted on and drained of its cash value.[(2)] That is not the purpose of the automatic stay, nor should it be its effect:

> The automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy.

S. Rep. No. 95-989, at 54-55, *reprinted in* 1978 U.S.C.C.A.N. 5787, 5840-41; H.P. Rep. No. 95-595, at 340, *reprinted in* 1978 U.S.C.C.A.N. 5963, 6296-97.

Debtor makes the point that Aurora notified Debtor of the premium due date and that these notifications constitute affirmative acts on the part of Aurora to cancel the Policy in violation of the automatic stay. The court does not accept the finding by the bankruptcy court that Aurora's notice letters constitute affirmative acts in seeking to get property of the estate. The notice provision in the Policy states: "The Company will advise the Owner prior to the premium due date if this policy may terminate if the Premium is not received by the end of the Grace Period." (Appellant's Excerpt of Record, p. 55). The notices serve as a reminder that the Policy was still in effect and premiums were still due. The characterization of the notices as an attempt to get money from the estate is in error. The notices did not attempt to get money from the estate, nor did they cancel the Policy. The notices are required of Aurora pursuant to the terms of the Policy, and in effect, seek to prevent the situation Debtor is now in--claiming it did not know of the expiration and seeking the benefit of a lapsed Policy Debtor's failure to pay the quarterly premium and to act according to the terms of the Policy cancelled the Policy.

In *In re B & K Hydraulic*, 106 B.R. 131 (Bankr. E.D. Mich. 1989), the court was faced with a similar situation in which an insurance policy on the life of a corporate debtor's principal was cancelled, post-petition, due to nonpayment of a premium. Debtor attempts to distinguish *B & K Hydraulic* by noting that the insurer did not take action to terminate the policy. The court assumes the action Debtor intimates is Aurora's notifying the Debtor of the cancellation. The facts of *B & K* do not specify if the insurer notified the debtor of the cancellation. However, it appears there was little time to do so as the insured died six days after the policy lapsed. *Id*. at 131. The *B & K Hydraulic* court concluded "that this contract terminated on December 29, 1987, when the payment due on November 28, 1987, went unpaid." *Id*. at 134. In the appeal of *In re B&K Hydraulic*, an unpublished opinion, the Sixth Circuit stated:

> A debtor or trustee cannot overlook payment of premiums and later claim that the insurance contract is extended and still enforceable despite its terms.
>
> The same principle applies under the automatic stay provisions of § 362. The automatic stay applies to prevent the creditor from taking affirmative steps to forfeit or foreclose an interest or to collect a debt, but it does not normally impair the terms of contracts concerning expiration.

In re B & K Hydraulic Co., 1991 WL 93191 (6th Cir. 1991) (unpublished opinion). In the case at bar, the notices to the Debtor did not cancel, terminate, or cause the lapse of, the Policy. Further, it was error to characterize the notices as seeking possession of the Debtor's estate. It was Debtor's failure to make timely premium payments that led to the cancellation of the Policy.

The principle of this holding is consistent with Eighth Circuit case law as well as that of courts that have faced analogous, though not identical, facts. *See Hazen*, 888 F.2d at 570. The Seventh Circuit has stated:

> Section 362, which creates an automatic stay of certain creditor actions upon the filing of a petition in the bankruptcy court, does not help debtors here. The automatic stay does not toll the mere running of time under a contract, and thus it does not prevent automatic termination of the contract. Section 362 does not give a debtor greater rights in a contract. Thus, debtors cannot rely on section 362 to prevent termination of the contracts.

Moody v. AMOCO Oil Co., 734 F.2d 4200, 1213 (7th Cir. 1984) (citations omitted). In *In re West Pine Construction Co.*, 80 B.R. 315, 324 (Bankr. E.D. Penn. 1987), the court was faced with a situation where a debtor defaulted on a lease post-petition, and consequently, the lease, by its terms, expired automatically. *Id*. at 317. The court stated:

> There must clearly come a point in time when the parties to a lease are entitled to a legitimate expectation of finality in connection with their business dealings. It is clearly inequitable to permit a debtor to attempt to cure and remedy a contractual obligation that has already expired. To permit a debtor to attempt to assert rights under an already expired lease by resort to the equitable provisions of the Bankruptcy Code would undermine confidence not only in the certitude of contracts, but in the judicial system itself.

Id. at 324. The court's holding reflects a commitment to this principle and honors the terms of the Policy.

B. 11 U.S.C.§542(d)

Aurora contends that 11 U.S.C. § 542(d) permitted the expiration of the Policy. Section 542(d) provides:

> A life insurance company may transfer property of the estate or property of the debtor to such company in good faith, with the same effect with respect to such company as if the case under this title concerning the debtor had not been commenced, if such transfer is to pay a premium or to carry out a nonforfeiture insurance option, and is required to be made automatically, under a life insurance contract with such company that was entered into before the date of the filing of the petition and that is property of the estate.

The bankruptcy court distinguished between what section 542(d) authorizes and what Debtor alleges. The statute authorizes the good faith transfer of estate property to pay premiums or to carry out nonforfeiture options. The Debtor contends the cancellation, and not the Nonforfeiture Option, violates the automatic stay. While the distinction is important, it is not dispositive of the issue. The automatic stay does not eviscerate the terms of the contract. Nor can the statute extend the life of the contract. To give effect to the grace period, the Premium Default Option, and the Nonforfeiture Option, but not the cancellation of the Policy by its agreed to terms would be to rewrite the Policy. The Policy, pursuant to its terms, including the grace period, the Premium Default Option, and the Nonforfeiture Option, provide a roadmap for the cancellation of the Policy. This does not entail any affirmative actions on the part of Aurora. The contract in the instant case was cancelled due to Debtors failure to make premium payments. Cancellation of the policy was not effectuated through the notice letters to the Debtor, but rather through Debtor failing to make timely premium payments.

C. II U.S.C. § 108(b)

Section 108(b) provides:

> Except as provided in subsection (a) of this section, if applicable nonbankrutpcy law, an order entered in a nonbankruptcy proceeding, or an agreement fixes a period within which the debtor oran individual protected under section 1201 or 1301 of this title may file any pleading, demand, notice, or proof of claim or loss, cure a default, or perform any other similar act, and such period has not expired before the date of the filing of the petition, the trustee may only file, cure, or perform, as the case may be, before the later of--(1) the end of such period, including any suspension of such period occurring on or after the commencement of the case; or (2) 60 days after the order for relief.

Section 108(b) is inapplicable to the situation before the court. This section might apply if the Debtor was in the grace period stipulated by the Policy and then filed the bankruptcy petition. The Policy grace period did not start until Debtor failed to pay the March 26, 1999, premium, nearly 15 months after the filing of the bankruptcy petition. The statutory grace period would have expired sixty days from the filing of the bankruptcy petition on January 21,1998. In fact Debtor did not notify Aurora that it had filed for bankruptcy until nearly eleven months had passed since the filing, and nine months since the expiration of the statutory grace period. Debtor failed to cure the default

during the grace period provided for in the Policy. The Policy expired under its own terms, and not within the statutory grace period contemplated by section 108(b).

ORDER

For the foregoing reasons, the decision of the bankruptcy court is REVERSED, and this case is remanded for consideration of the remaining issues in Debtor's Chapter 11 bankruptcy proceeding.

Done and so ordered this 28th day of September, 2001.

Michael J. Melloy,
United States District Judge for the
Northern District of Iowa

1. The court has jurisdiction to hear this appeal pursuant to 28 U.S.C. § 158(a)(1).

2. It is worth noting that while J.E. Adams was acting as debtor-in-possession, J.E. Adams borrowed $65,802.67 from the policy. At the time, the Debtor had not defaulted on or forfeited the Policy. It is slightly disingenuous for Debtor, acting as debtor-in-possession, to borrow the maximum amount of cash value from the Policy in a post-petition loan and then to argue to the court it has not assumed the Policy. *See NLRB v. Bildisco*, 465 U.S. 530, 531 (1984) ("If the debtor-in-possession elects to continue to receive benefits from the other party to an executory contract pending a decision to reject or assume the contract, the debtor-in-possession is obligated to pay for the reasonable value of those serves, which, depending on the circumstances of a particular contract, may be what is specified in the contract.") (internal citations omitted). Consequently, Debtor's 11 U.S.C. §365 argument is without merit.