

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF MAINE**

In re:

MONTREAL MAINE & ATLANTIC
RAILWAY, LTD.

Debtor.

Bk. No. 13-10670

Chapter 11

**CHAPTER 11 TRUSTEE'S MOTION FOR ORDER APPROVING COMPROMISE
AND SETTLEMENT WITH TRAVELERS PROPERTY
CASUALTY COMPANY OF AMERICA**

Robert J. Keach, the chapter 11 trustee in the above-captioned chapter 11 case (the "Trustee"), moves this Court for an order, pursuant to Rule 9019 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules"), approving a compromise and settlement with Travelers Property Casualty Company of America ("Travelers") on the terms set forth in this motion (the "Motion"). The compromise and settlement resolves a dispute between the Trustee, Montreal, Maine & Atlantic Canada Co. ("MMAC") and Travelers concerning the coverage under a commercial property insurance policy which the Trustee claims provides, among certain other coverages, business interruption coverage to the above-captioned debtor (the "Debtor") as well as MMAC. The settlement results in a \$3.8 million dollar payment to the Debtor and its Canadian affiliate (with the payment being allocated as provided for herein). The Trustee believes, in the exercise of his business judgment, that approval of the compromise and settlement is in the best interest of the Debtor and its estate. The settlement avoids protracted litigation with Travelers over whether the Debtor has asserted a covered claim under the policy in the first instance and whether, assuming the Debtor has asserted a covered claim, the coverage is void due to what Travelers contends was a mutual mistake in including the coverage in the policy at issue. It also

avoids time consuming and expensive litigation concerning the amount and extent of any claim for business interruption. In support of this Motion, the Trustee states as follows:

JURISDICTION, VENUE AND STATUTORY BASIS

1. The District Court has original, but not exclusive, jurisdiction over this proceeding pursuant to 28 U.S.C. § 1334(b). Pursuant to 28 U.S.C. § 157 and Rule 83.6 of the District Court's local rules, the District Court has authority to refer and has referred the Debtor's case to this Court (the "Bankruptcy Court").

2. This matter arising under Bankruptcy Rule 9019 is a core proceeding pursuant to 28 U.S.C. § 157(b)(2) and the Bankruptcy Court has constitutional authority to enter final judgment in this proceeding.

3. Venue over this chapter 11 case is proper in this district pursuant to 28 U.S.C. § 1408, and venue over this proceeding is proper in this district pursuant to 28 U.S.C. § 1409.

4. The relief sought in this Motion is predicated upon Bankruptcy Rule 9019 and Rules 9013-1 and 9019-1 of the Bankruptcy Court's local rules.

BACKGROUND

5. On August 7, 2013 (the "Petition Date"), the Debtor filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code. The Debtor's bankruptcy filing was precipitated by a train derailment in Lac-Mégantic, Québec on July 6, 2013 (the "Derailement"). The Derailement set off several massive explosions, destroyed part of downtown Lac-Mégantic, and is presumed to have killed 47 people. The Derailement also precipitated the filing by MMAC under Canada's Companies' Creditors Arrangement Act and the appointment of Richter Advisory Group, Inc. as the monitor to those proceedings (the "Monitor").

6. On August 21, 2013, the Trustee was appointed pursuant to 11 U.S.C. § 1163.

7. Prior to the Petition Date, on or about April 19, 2013, Travelers issued a commercial property insurance policy, No. QT-630-6357L188-TIL-12, under which the Debtor and MMAC are insureds for total coverage in the amount of \$7,500,000.00 (the “Policy”). LMS Acquisition Corporation, Montreal, Maine & Atlantic Corporation and Rail World, Inc. are also named as insureds under the Policy.

8. Although the Policy provides coverage for certain types of property damage, importantly, the Debtor contends that the Policy also provides coverage for loss of business income (the “Business Interruption Coverage”) and for “Extra Expense” arising out of a disruption to business (the “Extra Expense Coverage”).

9. In relation to the Business Interruption Coverage and the Extra Expense Coverage, the Policy states as follows:

“Business Income” and “Extra Expense”

[Travelers] will pay:

- (a) The amount by which your “Business Income” is actually reduced during the “period of restoration” due to loss of or damage to Covered Property from a Covered Cause of Loss; and
- (b) Your necessary “Extra Expense” to continue normal operations following loss of or damage to Covered Property from a Covered Cause of Loss.

10. After the Derailment, the Debtor filed a claim under the Policy for resulting damages to locomotives, railcars, railroad track, and roadbed. Additionally, the Debtor asserted claims under the Business Interruption Coverage and the Extra Expense Coverage premised on the loss of revenue arising out of the Derailment and the extra expenses being incurred by the Debtor as a result of the accident. The Debtor claimed that Travelers should advance the entire Policy limit of \$7,500,000.00 premised on the asserted claims.

11. Travelers responded to the Debtor's claims for coverage by denying that coverage exists under the Policy for the type of claims asserted by the Debtor. First, in relation to Business Interruption Coverage and Extra Expense Coverage, Travelers argued that there is simply no coverage because the claimed loss of business income did not arise out of damage to "Covered Property" as such term is defined by the Policy. Second, in relation to the Business Interruption Coverage specifically, Travelers argued, to the extent coverage exists, it was provided by mistake because the parties intended to include only Extra Expense Coverage and did not intend to include Business Interruption Coverage in the Policy, and the inclusion of such coverage in the Policy occurred in error.¹

12. Premised on these contentions, on August 27, 2013, Travelers filed the Motion of Travelers Property Casualty Company of America for Relief from the Automatic Stay Pursuant to 11 U.S.C. § 362(d)(1) [D.E. 105] (the "Motion for Relief") in order to file a declaratory judgment action in the United States District Court for the District of Maine (the "Maine District Court") to seek a judicial declaration regarding the rights of the parties under the Policy, including a declaration that any Business Interruption Coverage was included in the Policy by mistake, and a declaration that the Policy as written did not provide Business Interruption Coverage for the claimed loss. Attached to the Motion for Relief is a draft of the declaratory judgment action complaint which outlines in detail the reasons why Travelers contends there is no coverage under the Policy for the vast majority of the claims asserted by the insureds.

13. The Trustee opposed the Motion for Relief, arguing that cause for relief did not exist, because although, absent agreement, a judicial declaration was necessary to determine the

¹ Travelers did agree to pay \$250,000.00 under the Policy for expenses incurred to repair or replace certain damaged railroad track and roadbed. Travelers asserted that these incurred expenses were covered only under an endorsement, and did not constitute "Covered Property" under the Policy (and therefore did not provide a basis for claiming Business Interruption Coverage or Extra Expense Coverage). The \$250,000.00 payment was received by MMAC on or about September 23, 2013. The \$3.8 million dollar settlement amount at issue in this Motion is in addition to the initial \$250,000.00 paid by Travelers.

scope of coverage provided by the Policy, the action could be filed in the Bankruptcy Court. See Trustee's Objection to Motion of Travelers Property Casualty Company of America for Relief from the Automatic Stay Pursuant to 11 U.S.C. § 362(d)(1) [D.E. 199]. On October 9, 2013, the Bankruptcy Court entered an order denying the Motion for Relief [D.E. 364], from which Travelers filed an appeal (the "Appeal"). The Appeal is currently pending before the Maine District Court. See No. 1:13-cv-00432-NT. The parties to the Appeal have filed a joint motion to stay the appeal pending consideration of the Motion, which has been granted.

14. The Trustee and MMAC have been in active negotiations with Travelers for months, which negotiations included a daylong meeting of all parties in Hartford, Connecticut. As a result of these negotiations, which have included the review of documents relating to whether the Business Interruption Coverage was provided by mistake, the Trustee and MMAC, on the one hand, and Travelers, on the other hand, have reached a compromise and settlement to resolve the issues arising under the Policy. The general terms of that compromise and settlement are as follows:

- (a) Travelers shall pay a total of Three Million Eight Hundred Thousand United States Dollars (\$3,800,000.00) to the Debtor and MMAC (the "Settlement Payment"). The Settlement Payment shall be allocated 35% to the Debtor and 65% to MMAC. Contemporaneously with the filing of this Motion, MMAC is filing a motion in the Canadian proceeding seeking similar approval of the settlement with Travelers on the terms set forth herein. The relief sought in this Motion is conditioned upon approval of the relief sought by MMAC in the Canadian proceeding. The Settlement Payment shall be paid by Travelers in immediately available funds on or before December 31, 2013, assuming that the settlement has been approved in both the U.S. and Canada, no appeal has been taken and all applicable appeal periods have expired. The Settlement Payment shall be made in two payments to account for the allocation described above: (i) one payment in the amount of \$1,330,000.00 shall be paid directly to the Debtor; and (ii) one payment in the amount of \$2,470,000.00 shall be paid directly to the Monitor.
- (b) The settlement is conditioned on LMS Acquisition Corporation, Montreal, Maine & Atlantic Corporation and Rail World, Inc. entering into any and all

documents necessary to effectuate the terms of the settlement described in the Motion, including a release form executed by these parties.

- (c) The Settlement Payment shall be in full and final satisfaction of any and all claims arising under the Policy and Travelers shall be released from any and all liability arising under or relating to the Policy.
- (d) Travelers shall cause the Appeal to be dismissed, with prejudice, within seven (7) days of payment of the Settlement Payment.
- (e) The parties shall enter into any documents reasonably necessary to effectuate the terms of the settlement described herein.

15. After substantial negotiation, the Trustee believes that entering into the settlement with Travelers as described herein is in the best interest of the estate and its creditors. Although the Policy has a policy limit of \$7,500,000.00, the terms and extent of coverage have been and will continue to be the subject of considerable litigation if the compromise is not approved, which will be costly and time consuming to the estate. Additionally, not only could the litigation to resolve the coverage disputes take years to resolve, there is a risk of an outright loss of the litigation, which would reduce the recovery to zero. Premised on the risk, time and expense of litigation, the Trustee believes, in the exercise of his business judgment, that payment of the Settlement Payment provides considerable benefit to the estate and the settlement is in the best interests of the estate.

RELIEF REQUESTED

16. The Trustee requests that the Court: (a) grant this Motion and approve the compromise and settlement as provided for by the terms hereof; (b) authorize the payment of the Settlement Payment upon the allocation percentages outlined above; (c) authorize the Trustee and Travelers, subject to review by the Monitor and MMAC, to enter into any and all documents necessary to effectuate the terms of the settlement; and (d) approve service of the Motion to the parties and in the manner set forth herein.

BASIS FOR RELIEF

17. Bankruptcy Rule 9019(a) provides that “[o]n motion by the trustee and after notice and a hearing, the court may approve a compromise or settlement.” Fed. R. Bankr. P. 9019(a). This Court has sound discretion to determine whether the proposed compromise is fair and equitable and in the best interest of the bankruptcy estate. See Jeffrey v. Desmond, 70 F.3d 183, 185 (1st Cir. 1995).

18. In making this determination, the Court should consider: (a) the probability of success in the litigation of the claim being compromised; (b) the difficulties, if any, to be encountered in the matter of collection; (c) the complexity of the litigation involved, and the expense, inconvenience and delay attending it; and (d) the paramount interest of creditors and a proper deference to their reasonable views. See id., at 184; see also In re High Voltage Eng’g Corp., 397 B.R. 579, 601 (Bankr. D. Mass. 2008). The Jeffrey factors are not, however, exclusive. See In re Healthco, Int’l, Inc., 136 F.3d 45, 50 (1st Cir. 1998). Deference should be given to the trustee’s business judgment if the trustee can demonstrate that the settlement falls within a “range of reasonableness.” In re Fibercore, Inc., 391 B.R. 647, 655 (Bankr. D. Mass. 2008).

19. The Trustee believes that the terms of the compromise and settlement are fair and equitable, and that such compromise is in the best interest of the Debtor’s estate. The factors articulated in Jeffrey warrant approval of the compromise and settlement. First, concerning the probability of success in the litigation being pursued by Travelers, although the Trustee believes that there is a reasonable probability of prevailing in the litigation, Travelers has raised considerable claims concerning the scope and existence of coverage. As outlined above, Travelers has raised issues concerning whether “Covered Property” was damaged in the Derailment, and whether such damage caused a business income loss. In the event “Covered Property” was not damaged, or such damage to “Covered Property” was negligible and did not cause a business

income loss, there is no claim under the Business Interruption Coverage or the Extra Expense Coverage. The Policy leaves open a number of issues concerning what constitutes “Covered Property” under the Policy arising out of apparent limitations contained in the declarations page of the Policy.

20. Additionally, even if the “Covered Property” issues could be overcome, as explained above, Travelers claims that it was a mutual mistake to have included the Business Interruption Coverage in the Policy in the first instance. After reviewing documents relating to this issue, there may be open issues concerning whether this coverage was in fact included by mistake, posing significant risk to the estate.

21. Importantly, assuming the Business Interruption Coverage is determined to exist and that the claims arise out of damage to “Covered Property,” there would likely be considerable disputes concerning the amount of the claim arising under the Business Interruption Coverage. The Policy contains limitations on the time periods that can be used to calculate amounts owed for loss of business. As evidenced by the language quoted above, the business loss coverage extends only through the “period of restoration.” Depending on how this time limitation to coverage is determined and premised on likely unavoidable disputes concerning simply calculating the loss of business even within the “period of restoration,” there is a real risk that the claims under the Business Interruption Coverage would not reach the limits of the Policy, making the Settlement Payment that much more attractive to the estate.

22. Although the second Jeffrey factor has little bearing on this matter since Travelers has an ability to pay claims under the Policy, the third factor is significant and leans in favor of the settlement. Litigating the coverage issues could be complex, expensive and time consuming. The negotiations between the Trustee, MMAC and Travelers have made clear that the Policy contains a considerable number of inconsistencies and, according to Travelers, mutual mistakes. Resolving

the issues of coverage would require extensive discovery at tremendous cost to the estate. Furthermore, as described above, the complexity, time and expense involved in dealing with establishing the timeframes of the Business Interruption Coverage and the amount of loss that occurred within the timeframes could be considerable. For these reasons, the complexity, expense and delay caused by litigating these issues weigh in favor of the settlement.

23. Lastly, the settlement is of paramount interest to creditors of the estate. The uncertainty of the litigation could ultimately result in the estate having no coverage under the Policy and thus receiving nothing from Travelers. Instead of facing this uncertainty and risk, the estate is receiving a payment immediately for its allocable share of \$3.8 million. The proceeds of the settlement will be used to operate the Debtor and to pay creditors of the estate. Accordingly, the Trustee believes the motion should be granted because the compromise and settlement is in the best interest of creditors.

24. As noted above, the Settlement Payment will be allocated 65% to MMAC and 35% to the Debtor. This allocation has been driven by analysis performed by the Trustee's financial advisor, Development Specialists, Inc. ("DSI"). DSI analyzed the projected loss of business suffered by both of the Debtor and MMAC as a result of the Derailment by looking at the tonnage that would have been carried across Canadian and U.S. rail lines but for the Derailment and based the allocation on this projected tonnage analysis. Based on this work, the parties believe the allocation approximates the loss of income suffered by both the Debtor and MMAC.

NOTICE

25. Notice of this motion was served on the following parties on the date and in the manner set forth in the certificate of service: (a) the United States Trustee; (b) the Debtor's counsel; (c) the non-insider holders of the twenty (20) largest unsecured claims against the Debtor or, if applicable, the lawyers representing such holders; (d) applicable federal and state taxing

authorities; (e) the holders of secured claims against the Debtor, or if applicable, the lawyers representing such holders; (f) counsel for the committee appointed pursuant to 11 U.S.C. § 1102(a)(2); (g) counsel for Travelers; (h) the named insureds under the Policy, or if applicable, the lawyers representing the named insureds; (i) others who have, as of the date of the motion, entered an appearance and requested service of papers in the chapter 11 case. In light of the nature of the relief requested in the Motion, the Trustee requests that the Court approve notice to, and service of the Motion on, the parties set forth above as adequate and sufficient notice under the circumstances.

WHEREFORE, the Trustee requests that the Court enter an Order: (a) granting this Motion; (b) approving, pursuant to Bankruptcy Rule 9019, the compromise and settlement and authorizing the parties to enter into any and all settlement documents needed to effectuate the terms of the settlement as reflected herein; (c) finding that notice to and service upon the parties and in the manner set forth is appropriate; and (d) granting such other further relief as may be appropriate.

Dated: December 9, 2013

ROBERT J. KEACH,
CHAPTER 11 TRUSTEE OF MONTREAL
MAINE & ATLANTIC RAILWAY, LTD.

By his attorneys:

/s/ Sam Anderson
Michael A. Fagone, Esq.
Sam Anderson, Esq.
BERNSTEIN, SHUR, SAWYER & NELSON, P.A.
100 Middle Street
P.O. Box 9729
Portland, ME 04104
Telephone: (207) 774-1200
Facsimile: (207) 774-1127
E-mail: sanderson@bernsteinshur.com

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF MAINE**

In re:

MONTREAL MAINE & ATLANTIC
RAILWAY, LTD.

Debtor.

Bk. No. 13-10670
Chapter 11

**ORDER APPROVING CHAPTER 11 TRUSTEE'S MOTION FOR ORDER
APPROVING COMPROMISE AND SETTLEMENT WITH TRAVELERS
PROPERTY CASUALTY COMPANY OF AMERICA**

This matter came before this Court on the Chapter 11 Trustee's Motion for Order Approving Compromise and Settlement with Travelers Property Casualty Company of America (the "Motion")¹ and this Court having held a hearing to consider the Motion on December 18, 2013, and upon consideration of any and all objections to the Motion, if any, it is hereby **ORDERED, ADJUDGED** and **DECREED** as follows:

1. The Motion is granted.
2. Travelers shall pay a total of Three Million Eight Hundred Thousand United States Dollars (\$3,800,000.00) to the Debtor and MMAC (the "Settlement Payment"). The Settlement Payment shall be allocated 35% to the Debtor and 65% to MMAC. The Settlement Payment shall be made in two payments to account for the allocation described above: (a) one payment in the amount of \$1,330,000.00 shall be paid directly to the Debtor; and (b) one payment in the amount of \$2,470,000.00 shall be paid directly to the Monitor.
3. The Settlement Payment shall be paid by Travelers in immediately available funds on the later of (a) December 31, 2013; or (b) the date that this Order and the Order relating to motion to approve the settlement in relation in MMAC become final, non-appealable Orders.

¹ Capitalized terms used, but not defined in this Order, have the meanings ascribed to such terms in the Motion.

4. The Settlement Payment shall be in full and final satisfaction of any and all claims arising under the Policy and Travelers shall be released from any and all liability arising under or relating to the Policy.

5. Travelers shall cause the Appeal to be dismissed, with prejudice, within seven (7) days of payment.

6. The Debtor, MMAC and Travelers are authorized to enter into any documents reasonably necessary to effectuate the terms of the settlement described herein.

7. The relief granted herein is conditioned upon entry of an Order approving the settlement between MMAC and Travelers as set forth herein and reflected in the parallel motion filed by MMAC in the Canadian proceeding seeking approval of this settlement. The relief granted herein is conditioned upon LMS Acquisition Corporation, Montreal, Maine & Atlantic Corporation and Rail World, Inc. entering into any and all documents necessary to effectuate the terms of the settlement described in the Motion, including a release form executed by these parties.

Dated:

The Honorable Louis H. Kornreich
United States Bankruptcy Judge