THE STATE OF NEW HAMPSHIRE

MERRIMACK, SS. SUPERIOR COURT

Docket No. 03-E-0106

In the Matter of the Liquidation of
The Home Insurance Company

# ACE COMPANIES' REQUEST FOR FINDINGS OF FACT AND RULINGS OF LAW

Respondents Century Indemnity Company, ACE Property and Casualty Insurance Company, Pacific Employers Insurance Company and ACE American Reinsurance Company (collectively, the "ACE Companies"), by their attorneys, Lovells and Orr & Reno P.A., respectfully submit this request for findings of fact and rulings of law as follows:

## Summary

1. The cases cited by the New Hampshire Supreme Court in its September 13, 2004 Order (the "September 13 Order") set forth an objective standard for determining the issues of fairness and reasonableness, noting that undue deference should not be given to the Liquidator's views on whether the criteria are met.

2. The Court rules that Roger A. Sevigny, Commissioner of Insurance for the State of New Hampshire (the "Commissioner"), as liquidator (the "Liquidator") of Home Insurance Company ("Home"), has failed to carry his burden of demonstrating by a preponderance of the evidence that the Agreement is fair and reasonable.

3. The cases cited by the Supreme Court in its September 13 Order apply to settlements of litigation and they make it clear that certain criteria must be met for a finding of fairness and reasonableness.

4. As conceded by the Liquidator, the Agreement is not a settlement of a dispute; instead, it does nothing more than provide an incentive for the AFIA Cedents to file and

prosecute their claims. Because no litigation is being settled, the Liquidator cannot meet his burden under the Supreme Court's test, which is predicated on the existence of a settlement.

5. Even assuming that the Agreement may be fairly characterized as a settlement, none of the alleged threats cited by the Liquidator — when viewed under the objective standard mandated by the Supreme Court — provides any justification for the huge expenditure of estate funds that is contemplated under the Agreement.

6. For the reasons set forth below, the Court finds and rules that no reasonable liquidator would have perceived there was any realistic and credible threat that the AFIA Cedents would attempt to bypass the estate or collect directly from ACE through a ring fencing of assets, cut through litigation or side deals with ACE.[1] The Court further finds and rules that no reasonable insurance executive in the position of the AFIA Cedents would have pursued the ring fencing, cut through or side deal options.

7. The same conclusion applies to another argument allegedly threatened by the AFIA Cedents, which is that there was a novation based on ACE's course of dealing with the AFIA Cedents or its prior commitment to novate certain business. The absence of any support for the novation arguments shows that no reasonable executive in the position of the AFIA Cedents would bring an action based on such a theory and that the Liquidator would have no reasonable basis to perceive a novation-based action as a realistic or credible threat.

8. Because the Court finds that the Agreement is not fair or reasonable (which is the sole issue remaining after the Order on Remand dated October 8, 2004 (the "October 8 Order")), the Court need not reach the issue of whether the Agreement is necessary.

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[1] As used in these findings of fact and rulings of law, the term "cut through" refers to litigation in which the AFIA Cedents seek a court ruling that they have direct rights against ACE as the reinsurer. The term "side deal" refers to an arrangement between the AFIA Cedents and ACE, not involving court approval, in which the AFIA Cedents obtain the right to collect directly from ACE.

9. If, however, a ruling on that issue is required, the Court finds and rules that the Agreement is not necessary because the AFIA Cedents would have filed and fully prosecuted claims even in its absence. Thus, there was no reason for the estate to commit to paying tens of millions of dollars to the AFIA Cedents as an incentive for the filing and prosecution of their claims against the estate.

## Findings of Fact

### I. Relevant Background

#### A. Home's Liquidation And Joint Provisional Liquidation

10. Home is a New Hampshire domiciled insurance company and is subject to regulation by the New Hampshire Insurance Department. (ACE Companies' Admissions at ¶ 1.)

11. Home was incorporated in New Hampshire in 1973, and its predecessor insurance companies were established as long ago as 1853. Home and its subsidiaries wrote property and casualty insurance and reinsurance in the United States and in certain other countries, including the United Kingdom. (*Id.*, at ¶¶ 2-3.)

12. Home did business in the U.K. as a member of the American Foreign Insurance Association, an unincorporated association of American insurers ("AFIA"). AFIA wrote insurance and reinsurance business using Home's stamp (among others). (*Id.*, at ¶ 4.)

13. Home was regulated in the U.K. by the Financial Services Authority ("FSA") and its predecessor regulators in the U.K. Home considered the business it did in the U.K. as its "U.K. Branch." (*Id.*, at ¶ 4.) The U.K. Branch, however, has no legal identity separate from Home. (*Id.*; ACE Trial Ex. T at H00552.)

14. On March 5, 2003, the Court entered an Order of Rehabilitation for Home that appointed the Commissioner as Home's Rehabilitator. (ACE Companies' Admissions at ¶ 5.)

15. On May 8, 2003, the Commissioner (as Rehabilitator of Home) petitioned the High Court of Justice in London ("English Court") to appoint joint provisional liquidators for

Home under English law. That same day, the English Court appointed Gareth Hughes and Margaret Mills, licensed insolvency practitioners and partners of Ernst & Young LLP ("E&Y"), as joint provisional liquidators (the "JPLs") in a provisional liquidation proceeding for Home. (*Id.*, at ¶¶ 7-8.)

16. On June 13, 2003, this Court entered an Order of Liquidation for Home. The Order of Liquidation, among other things, declared that Home was insolvent and appointed the Commissioner as Liquidator. The Order of Liquidation enjoined the assertion of all claims against Home, except by the filing of proofs of claim with the Liquidator. The Order of Liquidation also set the last day for the filing of claims against Home as one year from the date of the order, *i.e.*, June 13, 2004. (ACE Companies' Admissions at ¶ 6; ACE Trial Ex. III at ¶¶ (n)(6) and (bb).)

17. The provisional liquidation proceeding in the U.K. is ancillary to the main New Hampshire liquidation. There is only one estate, under the exclusive jurisdiction of this Court, and the affairs of Home are treated on a unitary basis. (ACE Trial Ex. III; ACE Trial Ex. T at H00552; ACE Trial Ex. C at H00662; Rosen, Vol. 1-B, at 151:6-9; Ellis, Vol. 2-A, at 102:1-3; Hughes, Vol. 3-A, at 3:21-4:23, 8:18-9:8; 89:11-14, 91:6-92:3.)

18. The Liquidator expects the U.K. courts to grant comity to the Liquidation Order, including its injunctive provisions. (ACE Trial Ex. C at H00662; Bengelsdorf, Vol. 3-B, at 166:13-167:2.) The granting of comity is typical where, as here, the English liquidation proceeding is ancillary to a foreign proceeding. (Hacker, Vol. 5-A, at 75:21-76:5.)

19. On June 30, 2003, the Court appointed Peter Bengelsdorf as the Special Deputy Liquidator of Home. (ACE Trial Ex. HHH.) The Court's order states that the Special Deputy Liquidator "shall have all the powers and immunities of the Liquidator as set forth in RSA 402-C and the Liquidation Orders entered in these cases on June 13, 2003." (*Id.*, at ¶ 2.)

**B. ACE's Reinsurance of AFIA Treaties**

20. As a participating member of AFIA, Home entered into insurance and reinsurance contracts with policyholders and cedents. Home reinsured the AFIA business through certain reinsurance treaties, including treaties (the "AFIA Treaties") that Home entered into with cedents located in the U.S. and U.K. (the "AFIA Cedents"). (ACE Companies' Admissions at ¶¶ 11-12.)

21. Pursuant to certain agreements dated December 30, 1983, entitled Purchase Agreement No. 1 and Purchase Agreement No. 2, CIGNA Corporation ("CIGNA") and certain of its subsidiaries purchased AFIA. (*Id.*, at ¶ 13.)

22. As part of that transaction, one of the CIGNA subsidiaries, Insurance Company of North America ("INA"), entered an Insurance and Reinsurance Assumption Agreement dated January 31, 1984 (the "Assumption Agreement") with Home and other companies, which are described in the Assumption Agreement as the "Sellers." (*Id.*, at ¶ 14; ACE Trial Ex. L at 1.) The "Sellers" include Home and St. Paul Fire and Marine Insurance Company, the parent company of Unionamerica, one of the AFIA Cedents ("St. Paul"). (*Id.*)

23. Under the Assumption Agreement, INA agreed, among other things, to reinsure the insurance and reinsurance liabilities of Home's AFIA business, administer that business, and bear the related costs and expenses. INA's obligations included responsibility to adjust claims and indemnify Home through payment of Home's losses under the AFIA Treaties. (ACE Companies' Admissions at ¶ 15.) Each of the Sellers also agreed to cooperate with INA in the administration of the AFIA-related liabilities. (ACE Trial Ex. L at ¶ 5.)

24. In connection with the sale of the AFIA business, the Sellers (including St. Paul) also provided reinsurance to INA that begins paying when the AFIA liabilities exceed $335 million. (Hughes, Vol. 3-A, at 60:13-61:3.)

25. With the exception of the AFIA Treaties, the Home's interest in AFIA insurance and reinsurance business written in the U.K. (consisting of general direct and marine and aviation business) was formally transferred to a CIGNA subsidiary under English law in 1986. The transferred business became an obligation of the CIGNA subsidiary. The AFIA Treaties were not formally transferred under English law and accordingly remain an obligation of Home, subject to the Assumption Agreement. (ACE Companies' Admissions at ¶¶ 16-17.)

26. The Assumption Agreement contains, as the second unnumbered paragraph within paragraph 6, a clause that describes certain of the parties' rights and duties upon an insolvency of Home (the "insolvency clause"). (*Id.*, at ¶ 18.)

27. Subject to other relevant terms of the Assumption Agreement and any rights of setoff, the insolvency clause requires INA to pay obligations under the Assumption Agreement directly to Home or Home's liquidator in the event of Home's insolvency. Subject to other relevant terms of the Assumption Agreement, the claims are to be paid on the basis of Home's liability, without diminution because of Home's insolvency or because Home's liquidator has failed to pay all or part of a claim. The insolvency clause also permits, *inter alia*, INA to interpose any defenses in the determination of claims in the applicable proceeding. (*Id.*, at ¶ 19.)

28. The insolvency clause further states that the reinsurance shall be payable to Home or its liquidator except "(a) where this Assumption Agreement specifically provides another payee of such reinsurance in the event of the insolvency of a Seller, and (b) where INA with the consent of the direct insured or insureds has assumed such policy obligations of such Seller as direct obligations of INA to the payees under such policies and in substitution for the obligation of such Seller to such payees." (ACE Trial Ex. L at ¶ 6; emphasis added.)

29. The Assumption Agreement provides that "[n]othing in this Assumption Agreement, either express or implied, is intended, or shall be construed, to confer upon or to give

to any person, firm or corporation (other than the parties hereto and their permitted successors and assigns) any rights or remedies under or by reason of this Assumption Agreement ... ." (*Id.*)

30. The Assumption Agreement is governed by, and construed and enforced in accordance with, the laws of the State of New York. (*Id.*, at ¶ 10.)

31. In 1996, INA was part of a corporate restructuring pursuant to which Century Indemnity Company ("Century") became successor to INA with respect to INA's rights and obligations under the Assumption Agreement with respect to the AFIA Treaties. (ACE Companies' Admissions at ¶ 20.)

32. On July 2, 1999, CIGNA sold INA Corporation and its subsidiaries, including Century, to ACE INA Holdings, Inc., a subsidiary of ACE Limited. Under the transaction, Century became part of the ACE group of companies ("ACE"). (*Id.*, at ¶¶ 22, 24.)

**C. Administration of Claims By ACE-INA Services**

33. From in or about 1993, INA and Century have delegated (pursuant to the Assumption Agreement) the handling of the claims submitted by AFIA Cedents to their agents, including ACE-INA Services U.K. Limited ("ACE-INA Services"). (*Id.*, at ¶¶ 29-30.)

34. In general and in keeping with London market custom and practice, the AFIA Cedents have submitted their claims to ACE-INA Services through brokers. Such brokers are paid a fee by the cedents for whom they work, and their services included the submission of claims to reinsurers on behalf of the cedents. (Hughes, Vol. 3-A, at 28:8-29:4; Durkin, Vol. 4-B, at 168:14-169:14.) In other words, AFIA Cedents would incur no additional cost in presenting claims (tantamount to prosecution in this case) because they have already paid a fee to a broker to present such claims to Home.

35. On many of the contracts under which the AFIA Cedents have submitted claims, Home is one of several reinsurers who participate on (or "subscribe to") the risk. Therefore, the brokers will present the same claims to many reinsurers in the London market, not just Home.

(Hughes, Vol. 3-A, at 29:5-30:5; Durkin, Vol. 4-B, 168:14-169:14.) This is also true for the AFIA Cedents, such as Equitas Limited ("Equitas"), that employ internal and external brokers for the presentation of their claims. (Williams, Vol. 4-A, at 104:17-106:6.)

**D. Claims Procedures in Liquidation**

36. The Order of Liquidation provides that the AFIA Cedents who assert claims against Home under the AFIA Treaties must file proofs of claim in the New Hampshire liquidation proceeding, even if they are located outside of the United States. (ACE Companies' Admissions at ¶ 43.) Such claims are subject to review and approval by the Liquidator and this Court. (*Id.*)

37. The Court has issued several orders regarding the procedures for the review and approval of proofs of claim filed with Home. On November 12, 2004, the Court approved an agreed-upon Claims Protocol between Home and ACE dated August 6, 2004. (ACE Companies' Admissions at ¶ 46; ACE Trial Ex. FFF.) On January 19, 2005, the Court also entered a Restated and Revised Order Establishing Procedures Regarding Claims Filed with The Home Insurance Company in Liquidation (the "Restated Claims Procedures"). (ACE Companies' Admissions at ¶ 9; ACE Trial Ex. JJJ.)

38. Under the Order of Liquidation, Claims Protocol and Restated Claims Procedures, any payments under the Assumption Agreement with respect to the AFIA Treaties are made to the Liquidator, not to the AFIA Cedents. (ACE Companies' Admissions at ¶ 46.) Those payments, as well as the prosecution of claims, are in the New Hampshire liquidation proceeding. (Rosen, Vol. 1-A, at 91:13-22; Ellis, Vol. 2-A, at 101:2-8; Hughes, Vol. 3-A, at 4:5-10.)

39. The insolvency clause in the Assumption Agreement also requires that payments with respect to the AFIA Treaties must be made to the Liquidator, not the AFIA Cedents. (ACE Companies' Admissions at ¶ 50; ACE Trial Ex. C at H00663; Rosen, Vol. 1-A, at 90:23-91:12,

Vol. 1-B, at 203:19-204:19; Ellis, Vol. 2-B, at 129:15-21; Hughes, Vol. 3-A, at 19:7-19, 54:22-55:4; Bengelsdorf, Vol. 3-B, at 173:18-20; Durkin, Vol. 4-B, at 173:14-16.)

**E. Post-Liquidation Events**

**1. Information on AFIA Cedents' Claims**

40. In or around May 2003, ACE-INA Services filed with the U.K. Financial Services Authority ("FSA") Home's financial statements for the year ended December 31, 2002. The FSA return estimated that the claims of the AFIA Cedents, as of December 31, 2002, totaled approximately £143 million. (ACE Companies' Admissions at ¶¶ 32-33.) This estimate includes outstandings and IBNR. The figures in the FSA return were based on a comprehensive review and analysis by an actuary who had been involved with the AFIA business for many years. (Durkin, Vol. 4-B, at 191:14-23.)

41. Even after the JPLs were appointed in May 2003 and the Order of Liquidation was entered in June 2003, brokers continued to present claims to ACE-INA Services on behalf of the AFIA Cedents. (Durkin, Vol. 4-B, at 173:22-174:3.) In the summer of 2003, ACE-INA Services confirmed with the Liquidator that it still had the authority to administer such claims on behalf of Home, even though it could not pay the claims unless and until the claims procedures outlined in paragraphs 36-39 above had been followed. (*Id.*, at 173:10-21.)

42. Following the appointment of the JPLs and the selection of E & Y as auditors, ACE-INA Services made available to E & Y the books and records relating to Home's AFIA-related business (which included the FSA return for the year ended December 31, 2002). (*Id.*, at 174:16-175:11, 190:11-191:7, 194:4-9; Ellis, Vol. 2-A, at 113:3-5.) In addition, ACE-INA Services provided E & Y with a copy of a report on the AFIA business prepared by Milliman, an independent actuarial firm. (Durkin, Vol. 4-B, at 190:11-19; Ellis, Vol. 2-A, at 113:6-16.)

43. During the same time period, ACE-INA Services also provided several briefings to representatives of E & Y on the AFIA business. (Durkin, Vol. 4-B, at 174:16-175:11, 190:20-

191:1; Hughes, Vol. 2-B, at 161:2-5.) Gareth Hughes of E & Y described ACE-INA as "very helpful" in connection with E & Y's effort to gain an understanding of the AFIA business. (Hughes, Vol. 2-B, at 161:13-21; Durkin, Vol. 4-B, at 194:14-23.)

44. In July 2003, E & Y contacted certain AFIA Cedents and requested information regarding the amount of their claims. E & Y also asked the AFIA Cedents whether they intended to file proofs of claim against Home. (Ellis, Vol. 2-A, at 86:8-19, 92:8-19.)

45. Three AFIA Cedents — Riverstone Management Limited, Mentor Insurance Company (UK) Limited, and English & American Insurance Company Limited — confirmed in writing that they would be filing proofs of claims and two of those three provided estimates of their claims. (ACE Trial Exs. E, F and G.) A fourth AFIA Cedent, Continental Insurance Company of New York, also provided a written estimate of its claims. (ACE Trial Ex. GGG.)

46. None of the four AFIA Cedents ever withdrew their letters, nor did they ever inform representatives of Home that they would not be filing proofs of claim. (Ellis, Vol. 2-A, at 108:3-20, 109:15-18, 110:17-111:2.) Each of the four AFIA Cedents is a member of the Informal Creditors' Committee ("ICC") in the provisional liquidation. The total amount of their claims is at least tens of millions of dollars. (ACE Trial Exs. E, F, G and GGG.)

**2. Unionamerica's Response to E & Y's Request for Information**

47. In two letters dated August 1, 2003, T.P. Open of St. Paul Specialist Services Limited ("St. Paul Services") stated that Unionamerica Insurance Company Limited ("Unionamerica") was withdrawing its requests for payment of claims pending an investigation of its position. (ACE Trial Ex. DD at H01012, H01022.) By letter dated August 29, 2003, Tammy Lewis of St. Paul Services confirmed that Unionamerica was continuing to investigate its position with respect to the AFIA-related claims, but would be willing to serve on the ICC for the provisional liquidation. (*Id.*, at H01011.)

48. As of the end of August 2003, Unionamerica had not yet filed a proof of claim in Home's liquidation. Under the terms of the Order of Liquidation and the Assumption Agreement described above, Century could not have honored Unionamerica's requests for payment of claims. (Rosen, Vol. 2-A at 12:11-16, 15:23-16:4; Hughes, Vol. 3-A, 19:14-19.)

49. On September 17, 2003, Barbara Nowak of ACE-INA Services wrote to Mr. Open and requested, among other things, information on Unionamerica's withdrawal of its requests for payment. (ACE Trial Exs. EE and FF.) Unionamerica did not provide an explanation for the withdrawal and continued to reserve its rights. (Durkin, Vol. 4-B, at 184:9-11, 188:2-6.)

50. Unionamerica never informed representatives of Home or ACE that it did not intend to file a proof of claim. (Ellis, Vol. 2-A, at 107:23-108:2, Bengelsdorf, Vol. 3-B, at 176:14-20; Durkin, Vol. 4-B, at 183:10-14.)

### 3. Home's Discussions with Two AFIA Cedents and Representatives of ACE in August and September 2003

#### a) Discussions with Agrippina

51. On September 12 and 17, 2003, Jonathan Rosen of Home met with Gernot Warmuth, an attorney for Zürich Versicherung Aktiengesellschaft (Deutschland), which is the successor to Agrippina Versicherung Aktiengesellschaft ("Agrippina"). Agrippina is a member of the M.E. Rutty Underwriting Pool (the "Rutty Pool"). During the meetings, Mr. Warmuth stated that one of the options being considered by Agrippina was to terminate the contract of reinsurance between Home and Agrippina (known as "Treaty R") in order to gain access to certain third-party reinsurance covering the Rutty Pool. (Rosen, Vol. 2-A, at 24:9-17; Warmuth, Vol. 3-B, at 208:13-21, 211:21-212:1.)

52. ACE did not participate in the discussions between Mr. Rosen and Mr. Warmuth, and its representatives were specifically excluded from the September 12 meeting. (Hughes, Vol. 3-A, at 78:23-80:7; Warmuth, Vol. 3-B, at 209:14-18; Durkin, Vol. 4-B, at 177:15-17; ACE Trial Ex. QQQ at ZURICH00030.) At the time of the September 2003 meetings between Mr. Rosen

and Mr. Warmuth, Agrippina and ACE (on behalf of Home) was involved in a very contentious arbitration in which ACE was seeking to avoid any payments under the Assumption Agreement by asking the panel for a rescission of Treaty R. In that proceeding, ACE alleged fraud on the part of Agrippina. (Durkin, Vol. 4-B, at 171:15-172:9, 176:20-177:14; Wamser, Vol. 5-B, at 153:18-21.)

53. The termination of Treaty R is not a cut through to the Assumption Agreement. (Rosen, Vol. 2-A, at 23:11-13.) The termination would have meant that Home had no obligation to Agrippina and could not recover from Century under the Assumption Agreement. (Rosen, Vol. 2-A, at 23:17-24:8; Durkin, Vol. 4-B, at 172:1-9.)

**b) Discussions with ACE-INA Services**

54. On September 16, 2003, Mr. Rosen met with Mr. Durkin and asked Mr. Durkin for a commitment that ACE would not enter into future side deals with AFIA Cedents. (Durkin, Vol. 4-B, at 188:7-12, 220:20-221:16.) Mr. Durkin was noncommittal, and he testified at the evidentiary hearing that he lacked the requisite authority to provide any commitment about ACE's intentions. (*Id.*, at 188:13-189:1, 209:2-5.)

55. As of September 2003, ACE was not in discussions with any AFIA Cedents regarding a side deal. (*Id.*, at 181:3-5, 182:1-8; O'Farrell, Vol. 5-A, at 10:3-11:22; Wamser, Vol. 5-B, at 155:4-16.)

56. No AFIA Cedent had advised Home it was in discussions with ACE regarding a side deal. (Hughes, Vol. 3-A, at 72:5-20, 83:20-84:1, 127:16-128:6; Bengelsdorf, Vol. 3-B, 172:14-18.)

57. As of September 2003, ACE had not informed Home (or suggested in any way) that it was in discussions with any AFIA Cedents regarding a side deal. (Durkin, Vol. 4-B, at 181:6-9; Hughes, Vol. 3-A, at 83:20-84:1; Bengelsdorf, Vol. 3-B, at 177:18-23.)

### c) Discussions with Unionamerica

58. On September 17, 2003, Mr. Rosen of Home met with Unionamerica to discuss Unionamerica's withdrawal of its requests for payment pending further investigation. In that meeting, Unionamerica stated that it would continue to reserve its rights. (Rosen, Vol. 1-B, at 128:20-129:1.) Unionamerica did not inform Mr. Rosen that it would be seeking to enter into a side deal with ACE. (Rosen, Vol. 2-A, at 14:4-10.)

59. As of September 2003, ACE was not in discussions with Unionamerica regarding a side deal and Unionamerica had not told representatives of ACE that it wanted to discuss a side deal. (Durkin, Vol. 4-B, at 182:23-183:9; Wamser, Vol. 5-B, at 155:21-156:6.)

60. As of September 2003, ACE had not informed Home (or suggested in any way) that it was in discussions with Unionamerica regarding a side deal. (Rosen, Vol. 2-A, at 14:11-13; Ellis, Vol. 2-B, at 128:18-20; Hughes, Vol. 3-A, at 56:17-19; Bengelsdorf, Vol. 3-B, at 177:14-17.)

### 4. ACE's Letter of September 16, 2003 and the Liquidator's Letter of September 26, 2003

61. ACE sent a letter to the Liquidator on September 16, 2003 regarding the meetings that Mr. Rosen had with Agrippina without representatives of ACE being present. (ACE Trial Ex. KK at H01922-23.) ACE was concerned that Mr. Rosen was discussing Home's substantive defenses in the arbitrations with Agrippina and other Rutty Pool members or was potentially seeking to settle the cases without ACE's participation. (Durkin, Vol. 4-B, at 176:18-178:8; Wamser, Vol. 5-B, at 153:9-154:15.) ACE also noted that Mr. Rosen's actions might interfere with its obligation to administer the AFIA business. (ACE Trial Ex. KK at H01923.)

62. The September 16, 2003 letter does not assert that ACE had the right to enter into side deals with the AFIA Cedents. (Wamser, Vol. 5-B, at 154:16-19; ACE Trial Ex. KK at H01922-23.) At the time of the letter, ACE was not seeking to enter into side deals with any

AFIA Cedents and was not in discussions with any AFIA Cedents regarding a side deal. (Wamser, Vol. 5-B, at 154:20-155:3.)

63. The Liquidator and Mr. Hughes wrote to Century on September 26, 2003. They stated that the September 26, 2003 letter was in response to ACE's letter of September 16, 2003 and "certain discussions between Jonathan Rosen, Gareth Hughes and Michael Durkin." (ACE Trial Ex. LL at H00621.) The Liquidator and Mr. Hughes also stated that they were "concerned that attempts may be made to circumvent the existing contractual relationship" between Home and Century with a view to allowing the AFIA Cedents to cut directly through to Century. (*Id.*) The Liquidator and Mr. Hughes asked ACE to advise them of any ongoing attempts by AFIA Cedents to enter into side deals and requested confirmation that ACE would notify them upon becoming aware of such efforts. (*Id.*, at H00622.)

64. As of September 26, 2003, ACE was not engaged in any discussions with any of the AFIA Cedents regarding side deals. (Wamser, Vol. 5-B, at 159:15-21.) Home had not been advised by any AFIA Cedent of such discussions. (Hughes, Vol. 3-A, at 72:5-20, 83:20-84:1, 127:16-128:6; Bengelsdorf, Vol. 3-B, 172:14-18.)

### 5. Liquidator's Discussions with Representatives of ACE on September 30, 2003 and October 16, 2003

65. During September 2003 and before the letter of September 26, 2003 to Century, Mr. Rosen had requested a meeting with representatives of ACE to discuss a commutation (*i.e.*, a settlement) relating to the AFIA business. (Rosen, Vol. 1-B, at 140:5-19; Hughes, Vol. 2-A, at 33:6-12; Bengelsdorf, Vol. 3-B, at 179:18-180:16.)

66. In preparation for the meeting, which took place on September 30, 2003, the Liquidator prepared a series of slides setting forth the items to be discussed, which included a "comprehensive business resolution" and commutation between Home and ACE. (ACE Trial Ex. C at H00664-666.) The slides stated that the information being presented was "without prejudice" and "for discussion purposes only." (*Id.*, at H00659-666.) Mr. Bengelsdorf's notes of

the September 30, 2003 meeting similarly state that it was on a "without prejudice" basis. (ACE Trial Ex. M at H00650.)

67. Representatives of Home and ACE testified at the evidentiary that their clear understanding of "without prejudice" discussions is that nothing said in such talks will be used in a later proceeding between the parties. (Hughes, Vol. 3-A, at 37:12-21, 41:23-42:5; Durkin, Vol. 4-B, at 219:14-19; Wamser, Vol. 5-B, at 161:4-20.)

68. ACE was represented at the September 30, 2003 meeting by Thomas Wamser and Howard Denbin. (ACE Trial Ex. M at H00650.) The Liquidator was represented by Messrs. Bengelsdorf, Hughes and Rosen as well as Sarah Ellis of E & Y. (*Id.*) The parties discussed the commutation proposals outlined in the Liquidator's slides and ACE stated that it was "very receptive" to a commercial resolution. (*Id.*, at H00653.)

69. One of the settlement options discussed at the September 30, 2003 meeting was to develop an overall number for the reinsurance of the AFIA business and then split the proceeds 50-50 between the AFIA Cedents and Home. (Wamser, Vol. 5-B, at 165:3-166:17; ACE Trial Ex. M at H00650, H00652.) This was the exact percentage split that Home agreed with the AFIA Cedents, as embodied in the Agreement. ACE subsequently informed Home that it wanted to continue with commutation talks on a straight ACE-Home commutation basis. (Wamser, Vol. 5-B, at 173:7-174:8.)

70. At the September 30, 2003 meeting, Home took the position that there was a large discrepancy between the estimates that each side had for the AFIA Cedents' expected claims. (ACE Trial Ex. M at H00651.) ACE was relying on the figures from the 2002 FSA return. (Durkin, Vol. 4-B, at 191:2-23.) The Liquidator, based on "high level" information that had been received from some AFIA Cedents, estimated that the claims were at least double the figures being used by ACE. (ACE Trial Ex. M at H00651, H00653; Ellis, Vol. 2-A, at 92:14-94:4.)

However, no part of the information received by the Liquidator from AFIA Cedents had been verified and remains unverified and unsupported to this day. (Hughes, Vol. 3-A, at 44:5-20.)

71. The parties agreed at the September 30, 2003 meeting that E & Y would seek to obtain additional information to explain the difference between the estimates and that they would meet again in approximately two weeks to discuss commutation further. (ACE Trial Ex. M at H00651, H00653; Wamser, Vol. 5-B, at 167:6-14, 168:6-17.)

72. The issues of cut through and side deals were also discussed at the September 30, 2003 meeting. With regard to the former, Mr. Denbin cited the decision in *National Employers' Mut. Gen'l Ins. Ass'n v. AGF Holding (UK) Ltd.*, [1997] 2 BCLC 191 ("*NEMGIA*"), for the proposition that cut throughs were permissible under English law. (ACE Trial Ex. M at H00651; Wamser, Vol. 5-B, at 170:14-171:1.) The ACE representatives noted, however, that it was "unclear" whether the cut through issue would be decided under U.S. or English law. (ACE Trial Ex. M at H00651; Bengelsdorf, Vol. 3-B, at 181:21-182:1.)

73. Mr. Wamser had a follow-up telephone conversation on October 16, 2003 with Messrs. Bengelsdorf and Rosen. Mr. Wamser noted that ACE was "anxious" to continue the commutation discussions and that ACE was doing so in "good faith." (ACE Trial Ex. CC at H00647; Bengelsdorf, Vol 3-B, at 183:15-22, Wamser, Vol. 5-B, at 172:8-15.)

74. During the October 16, 2003 conference call, Mr. Wamser agreed that ACE would not enter into any discussions with AFIA Cedents regarding side deals while the commutations discussions with Home were ongoing. (ACE Trial Ex. CC at H00647; Wamser, Vol. 5-B, at 174:22-175:8, 188:3-11, 191:10-20; Hughes, Vol. 3-A, at 86:14-21.) The parties further agreed that they would not enter into any side deals with AFIA Cedents without disclosing those arrangements to the other party. (ACE Trial Ex. CC at H00647; Wamser, Vol. 5-B, at 175:8-13, 188:11-3, 191:21-192:3; Bengelsdorf, Vol. 3-B, at 185:5-23.) Mr. Wamser gave the

commitments after consulting with, and gaining the approval of, William O'Farrell of ACE. (Wamser, Vol. 5-B, at 175:14-18.)

75. The Liquidator never requested that Mr. Wamser reduce to writing the commitments that were given during the October 16, 2003 conference call. (Wamser, Vol. 5-B, at 176:22-177:10.) ACE, however, honored those commitments. (*Id.*, at 177:11-12.) From the time of the Order of Liquidation until February 11, 2004, ACE never discussed a side deal with any of the AFIA Cedents and none of the AFIA Cedents ever raised the issue with ACE. (Durkin, Vol. 4-B, at 181:10-183:9; O'Farrell, Vol. 5-A, at 10:3-11:22, 19:16-20:6; Wamser, Vol. 5-B, at 155:4-16.)

76. Home asked for confirmation that Mr. Wamser had authority to discuss a commutation with Home. Mr. Wamser sought and obtained that approval and gave that confirmation to Home. (Wamser, Vol. 5-B, at 170:8-13, 172:13-18.)

77. Mr. Rosen, during the October 16, 2003 conference call, presented his views on why the *NEMGIA* decision does not provide for cut throughs. (Wamser, Vol. 5-B, at 171:12-22.) Mr. Wamser testified at the evidentiary hearing that he agreed with Mr. Rosen's assessment of *NEMGIA*, but that he did not express his agreement because the parties were involved in settlement negotiations and the *NEMGIA* decision might provide some bargaining leverage. (*Id.*, at 171:23-172:7.)

78. During the October 16, 2003 call, the parties also agreed to continue with the process of reconciling the difference between their estimates of the AFIA Cedents' claims. (*Id.*, at 174:9-21.) The reconciliation process and commutation discussions continued thereafter, but E& Y had not provided any further information to ACE by October 21, 2003, or by the time the Agreement was signed in February of 2004. (Ellis, Vol. 2-A, at 114:23-115:3; Hughes, Vol. 3-A, at 45:20-46:8.) In fact, to this day the information has not been provided. (Rosen, Vol. 2-A, at 40:15-20.)

79. The ACE representatives never communicated to Home that ACE was no longer interested in pursuing the commutation discussions. (Bengelsdorf, Vol. 3-B, at 184:15-18.) Home never indicated in any way that the commutation discussions were not ongoing. (Rosen, Vol. 2-A, at 48:6-49:3; Hughes, Vol. 3-A, at 53:23-54:14; Wamser, Vol. 5-B, at 179:8-180:1.)

### 6. ICC Meeting in October 2003 and The Liquidator's Decision to Pursue The Agreement with AFIA Cedents

80. At the first ICC meeting on October 21, 2003, representatives of Home conferred and decided to pursue a commercial resolution with the AFIA Cedents. (Rosen, Vol. 1-B, at 154:3-13; Ellis, Vol. 2-A, at 115:8-16; Bengelsdorf, Vol. 3-B, at 158:6-159:11.) They informed the AFIA Cedents that a proposal would be sent shortly. (*Id.*, at 158:15-18.)

81. The evidence suggests that even before the first meeting with the AFIA Cedents, the Liquidator was considering a proposal. As discussed below (*see infra*, at ¶¶ 154-155), Mr. Warmuth of Agrippina had requested in September 2003 that Home pay an incentive. Home responded by saying that a proposal would be forthcoming.

82. The Liquidator also assured the AFIA Cedents at the October 21, 2003 meeting that Home would not use any information obtained from the AFIA Cedents in order to commute with ACE. (Rosen, Vol. 2-A, at 46:21-47:20; Hughes, Vol. 3-A, at 52:9-53:12.) Accordingly, while Home was purportedly in good faith settlement negotiations with ACE, it had effectively and completely determined not to negotiate with ACE by agreeing not to use claims information from the AFIA Cedents it undertook to provide to ACE for that very purpose. No one informed ACE of this agreement with the AFIA Cedents. (*Id.*, Vol. 3-A, at 53:23-54:14.)

### 7. Negotiations on Sharing of Reinsurance Proceeds

83. Approximately one month after beginning negotiations, Mr. Williams (as the *de facto* chair of the ICC) agreed to the concept of a 50-50 split of the reinsurance recoveries. (Williams, Vol. 4-B, at 136:20-137:17.) This was the same percentage split discussed at the September 30, 2003 meeting between ACE and Home.

84. In the course of the negotiations over the terms of the Agreement, Mr. Williams expressed the concern of the ICC that the Agreement was a "material departure" from the New Hampshire statutory scheme. (ACE Trial Ex. GG at H02997.)

**8. Submission and Prosecution of Claims**

85. The costs of submitting and "prosecuting" claims in Home's liquidation are minimal (if they exist at all).

86. As discussed above (*see supra*, at ¶¶ 33-35), brokers are handling the AFIA Cedents' claims and they are submitting the same claims to other reinsurers who participate on the reinsurance with Home. Therefore, little or no additional work is required to prove up the claims in Home's estate. Mr. Durkin pointed out that in other liquidations, "prosecuting the claim isn't a huge exercise because we would rely on the brokers to do most of the work for us." (Durkin, Vol. 4-B, at 195:21-23; *see also* Craig, Vol. 5-A, at 109:14-110:1.)[2]

87. The Liquidator has suggested that opposition to claims by the estate would increase the costs of prosecution. The evidence, however, does not support the Liquidator's contention.

88. Several witnesses testified that they have never had to do anything more, over the course of several if not dozens of insurance insolvencies, than present their claims for them to be allowed. Neither Home nor Equitas (the world's largest run-off organization) has ever been involved in a dispute over its liquidation claims. (Rosen, Vol. 1-B, at 170:5-9; Williams, Vol. 4-A, at 114:11-14.) This case is no different. Mr. Rosen testified at the evidentiary hearing that there have been no claims disputed, even though approximately $10 million of AFIA Cedent claims have been determined by the Liquidator. (Rosen, Vol. 2-A, at 66:14-23.)

89. Moreover, as noted above, there is a Claims Protocol in this proceeding that streamlines the determination process. (*See supra*, at ¶¶ 37-38; ACE Trial Ex. FFF.) The

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[2] Mr. Durkin also testified that brokers have continued to bring claims to ACE-INA Services post-liquidation. (*See supra*, at ¶ 41.)

Liquidator also has an incentive to ensure that valid claims are paid so that he may seek to collect reinsurance proceeds.

90. The Liquidator's assertions about the alleged burden of prosecuting claims is further belied by the fact that no analysis was ever done to determine what the costs of prosecuting the AFIA Cedents' claims against the estate would be. (Ellis, Vol. 2-A, at 111:3-11; Hughes, Vol. 3-A, at 27:8-21; Bengesldorf, Vol. 3-B, at 188:3-7.)

## II. Agreement with AFIA Cedents

### A. Rationale for Agreement

91. On February 11, 2004, the Liquidator served a motion (the "Motion") requesting that the Court approve the Agreement. (ACE Trial Ex. H.) In support of the Motion, the Liquidator submitted (among other things) the following: Affidavit of Peter Bengelsdorf dated February 10, 2004 ("Bengelsdorf Aff."); Affidavit of Jonathan Rosen dated March 26, 2004 ("Rosen Aff."); Affidavit of Gareth Hughes dated March 31, 2004 ("Hughes Aff."), Affidavit of Rhydian Williams dated April 1, 2004 ("Williams Aff."); and Affidavit of Gernot Warmuth dated March 31, 2004 ("Warmuth Aff.").

92. The Motion, citing the Bengelsdorf Affidavit, states that the Liquidator entered into the agreement with the AFIA Cedents for three reasons:

(1) "[C]ertain AFIA Cedents have previously suggested that UK assets should be 'walled off' from United States creditors and distributed only to Home UK Branch creditors." (ACE Trial Ex. H at 5-6.) The Liquidator stated that "this issue does raise the prospect of costly and time-consuming litigation over whether there should be separate US and UK liquidations or a global New Hampshire proceeding." (ACE Trial Ex. H at 6.)

(2) "[C]ertain of the AFIA Cedents have been exploring alternative means of realizing recovery with respect to the business protected by the AFIA Treaties, including possible circumvention of Home by entering into side arrangements with ACE Group." (*Id.*, at 5.)

(3) The threat that the AFIA Cedents would not file claims in Home's liquidation on the basis that they "may well receive only a small (if any) distribution" as Class V creditors. (*Id.*)

93. The other affidavits submitted by the Liquidator elaborated on the "alternative means of realizing recovery" cited in the Motion. In addition to side deals, the affidavits stated that certain AFIA Cedents were considering cut throughs or an argument that ACE's dealings with the AFIA Cedents since 1984 constituted a "constructive novation" of the AFIA Treaties (which would, in their view, permit a direct recovery from ACE). (Williams Aff. at ¶ 12; Warmuth Aff. at ¶ 9.) Mr. Warmuth further stated that Agrippina was thinking of arguing that ACE is "effectively obliged" to accept a novation because of commitments that CIGNA gave at the time of the transactions in 1984. (*Id.*)

### B. The Alleged "Threats" That Lead to the Agreement Were Non-Existent Or Were Not Objectively Credible

94. The evidence shows that the five alleged "threats" cited by the Liquidator in the Motion and supporting affidavits as the rationale for the Agreement did not exist or were not credible (when viewed objectively). The facts instead demonstrate the following:

#### 1. Ring Fencing

95. There is no basis for the Liquidator's statement in the Motion that an effort by the AFIA Cedents to "wall off" (*i.e.*, ring fence) assets in the U.K. would lead to "costly and time-consuming litigation." (ACE Trial Ex. H at 6.)

96. The Liquidator has attempted to withdraw ring fencing as a justification for the Agreement, but the fact remains that the threat of ring fencing was a central contention in the Motion. (ACE Trial Ex. H at 6.) The Liquidator has not amended the Motion or withdrawn any statements in the supporting affidavits. A consideration of the ring fencing issue is also relevant to the Court's assessment of the credibility of Messrs. Bengelsdorf, Rosen, Hughes, Williams and Warmuth, each of whom submitted sworn affidavits referring to the alleged ring fencing threat.

(Bengelsdorf Aff. at ¶ 8; Rosen Aff. at ¶ 9; Hughes Aff. at ¶ 15; Williams Aff. at ¶ 12; and Warmuth Aff. at ¶ 9.)

97. The issue of ring fencing was initially raised by Rhydian Williams of Equitas. (Williams, Vol. 4-A, at 115:17-21.) In response, the Liquidator sought advice from Robin Knowles QC and Professor Ian Fletcher on ring fencing under English law. (Williams, Vol. 4-A, at 116:3-6, Vol. 4-B, at 118:8-12; Hughes, Vol. 2-B, at 163:12-164:2, Vol. 3-A, 7:5-23, 88:2-89:10, 92:4-19.)

98. Mr. Knowles and Prof. Fletcher, in a Note of Advice dated October 19, 2003, stated that: "[Home's U.K.] Branch has no legal identity separate from the company to which it belongs, and for English law purposes the affairs of the Home are to be treated on a unitary basis. ... The settled position under English law is that even in the case of concurrent insolvency proceedings the English winding up is considered to be of universal application, and there is no possibility for the winding up of a foreign company to be limited to its activities and assets in England." (ACE Trial Ex. T at H00552.) Mr. Knowles and Prof. Fletcher unequivocally concluded that:

> English law will not allow for the UK Branch assets to be ring-fenced for the benefit of UK Branch creditors, at the expense of according equality of treatment to the non-UK creditors in the course of the administration of the worldwide estate of Home.

(*Id.*, at H00553.)

99. The JPLs and Home never received any advice to the contrary. (Hughes, Vol. 3-A, at 10:5-11, 89:18-23.)

100. At the ICC meeting on October 21, 2003, Mr. Hughes relayed the substance of the Note of Advice to the AFIA Cedents and informed them that Clifford Chance concurred with the opinion of Mr. Knowles and Prof. Fletcher. (Liquidator's Trial Ex. 27 at H00343-44; Hughes, Vol. 3-A, at 88:23-89:4.)

101. Mr. Hughes provided the ICC members with a copy of the Note of Advice around the time of the ICC meeting. (Hughes, Vol. 3-A, at 89:5-10; Bengelsdorf, Vol. 3-B, at 168:15-22.)

102. David Steinberg of Clifford Chance also stated at the October 21, 2003 meeting that although ring fencing might be possible if creditors in the U.K. were disadvantaged, "there was no disadvantage to UK Branch creditors of one US liquidation." (Liquidator's Trial Ex. 27 at H00344.) Mr. Hughes had reached the same conclusion on the issue as early as August 2003. (Hughes, Vol. 3-A, at 6:15-7:5.)

103. The ACE Companies' expert, Richard Hacker QC, testified at the evidentiary hearing that when "viewed objectively" any concerns about ring fencing "are fundamentally misplaced." (Hacker, Vol. 5-A, at 77:2-8.) Mr. Hacker added that:

> The position in relation to ring-fencing is so clear under English law that there really is no scope for any credible suggestion of ring-fencing in the circumstances of this case, and in those circumstances, I think that a well-advised Liquidator should appreciate that there really is no scope for expensive, costly or perhaps any other [litigation] in relation to the issue.

(*Id.*, at 77:9-15.)

104. Mr. Hacker further noted (and the Liquidator has acknowledged) that the losing party in an English proceeding pays the attorneys' fees of the prevailing party. (*Id.*, at 78:18-21; Hughes, Vol. 3-A, at 73:18-74:10.) This notwithstanding, Home's representatives never conducted an analysis of the costs that would be incurred in opposing any ring fencing attempt by the AFIA Cedents. (Bengelsdorf, Vol. 3-B, at 170:19-171:2.)

105. Ring fencing was no longer an issue after the October 21, 2003 meeting of the ICC. Mr. Williams testified that, as of the date of the meeting, he had concluded that it was not possible to ring fence any U.K. Branch assets. (Williams, Vol. 4-B, at 118:13-21.) Remarkably, Mr. Warmuth testified that he only considered the ring fencing issue for about "fifteen or twenty minutes" during the ICC meeting and did not consider the issue thereafter. (Warmuth, Vol. 4-A,

at 17:1-12, 18:12-18, and 19:5-11.) Mr. Bengelsdorf testified that the only time he could recall ring fencing being raised as an issue was at the ICC meeting. (Bengelsdorf, Vol. 3-B, at 169:23-170:3.) The Liquidator still included the ring fencing argument in the Motion and none of the affiants, including Mr. Williams and Mr. Warmuth, withdrew their statements.

**2. Constructive or Forced Novation**

106. There is no evidence to support the contentions in the Williams and Warmuth Affidavits that there was any threat of a "constructive novation" based on the fact that ACE (through ACE-INA Services) made payments directly to the AFIA Cedents. There is also no evidence to support the additional contention in the Warmuth Affidavit that ACE could be forced to accept a novation based on commitments made in 1984.

107. The claims payments that ACE-INA Services made on behalf of Home were pursuant to the Assumption Agreement, which did not effect a novation of the liabilities under the AFIA Treaties. (Williams, Vol. 4-B, at 130:20-23; ACE Trial Ex. C at H00660, H00663.) Instead, the AFIA Treaties remained the obligation of Home. (ACE Companies' Admissions at ¶ 17.) Mr. Durkin testified that the checks were issued in the name of Home. (Durkin, Vol. 4-B, at 169:15-170:9.)

108. Prior to the October 21, 2003 meeting of the ICC, Mr. Williams asked Mr. Hughes to determine the validity of the novation argument. (Williams, Vol. 4-B, at 129:20-130:8.) Mr. William accepted the advice provided by Mr. Hughes that Home retained the obligations under the AFIA Treaties, that Century was a reinsurer of Home under the Assumption Agreement, and that no novation had taken place. (Williams, Vol. 4-B, at 130:13-131:2.) Mr. Williams did not take any other advice on the novation argument. (*Id.*, at 125:6-11.)

109. At the October 21, 2003 meeting, Mr. Steinberg of Clifford Chance also outlined the legal advice that Home had received on forced novation, which concluded that such action was time barred. Mr. Steinberg added that, even if the FSA still had the power to force a

novation, it was "very unlikely" the FSA would do so. (Liquidator's Trial Ex. 27 at H00341.) Indeed, Home's representatives never conducted an analysis of the costs opposing any novation attempt by the AFIA Cedents. (Hughes, Vol. 3-A, at 73:9-12.)

110. Mr. Warmuth testified that he gave no consideration to the novation issue post-liquidation. (Warmuth, Vol. 4-A, at 40:23-41:8.) Mr. Warmuth further testified that he did not discuss the novation issue with Home or ACE after Home went into liquidation. (*Id.*, at 41:8-12, 42:9-43:6.) And yet neither he nor Mr. Williams withdrew the statements made in their affidavits that they knew had no merit.

**3. Cut Through Under Assumption Agreement**

111. There was no credible threat of cut-through litigation by any of the AFIA Cedents against ACE.

112. At the evidentiary hearing, counsel for the Liquidator conceded that cut throughs are not a basis for the Agreement. (Vol. 5-A, at 23:4-8.) However, as with the ring fencing issue, the Liquidator has never amended the Motion or the supporting affidavits to omit the references to cut through. Also, a consideration of the cut-through argument goes to the credibility of the affiants who cited it as a threat. (Rosen Aff. at ¶ 7; Hughes Aff. at ¶ 14.)

113. Representatives of Home believed that cut through by the AFIA Cedents was not permissible because the Assumption Agreement lacks any clause allowing a party to cut through to Century or any of the ACE Companies. (Hughes, Vol. 3-A, at 62:16-63:12; Rosen, Vol. 1-B, at 206:2-14.) At least one AFIA Cedent, Equitas, had legal advice to the same effect. (Williams, Vol. 4-B, at 125:9-22, 126:10-14; ACE Trial Ex. CCC at 000940.)

114. There are also at least two clauses in the Assumption Agreement that forbid a cut through. The first is Paragraph 12, which expressly states that nothing in the Assumption Agreement confers rights upon any third party. (ACE Trial Ex. L. at ¶ 12.). The second is the

"insolvency clause," which states that, in the event of insolvency, any payments under the AFIA Treaties must be made to Home or the Liquidator. (*Id.*, at ¶ 6.)

115. In *Nationwide Mut. Ins. Co. v. Home Ins. Co.*, 150 F.3d 545 (6th Cir. 1998), *cert. denied*, 525 U.S. 1140 (1999), the Court of Appeals for the Sixth Circuit ruled on the effect of the disclaimer language in Paragraph 12 of the Assumption Agreement. It held that the language is "clear and unequivocal" and precludes a cut through under the Assumption Agreement. *Id.*, at 548-49. The Court also held that regardless of whether the CIGNA defendants directly assumed Home's reinsurance obligations to Nationwide, "Nationwide is a stranger to the Assumption Agreement" and therefore "cannot bring suit directly against the CIGNA defendants." *Id.*, at 549.

116. Representatives of Home were well aware of the *Nationwide* decision as of the fall of 2003 and were familiar with its holding. (Rosen, Vol. 1-B, 207:10-212:21.) Mr. Rosen testified that Home's insolvency could affect the analysis in *Nationwide*, but he conceded that it was the CIGNA defendants — not Nationwide— who sought a ruling on whether Nationwide would be able to cut through in the event of insolvency. (*Id.*, at 212:9-21.)

117. Representatives of Home recognized that the insolvency clause in the Assumption Agreement precludes cut throughs. (Rosen, Vol. 1-A, at 91:4-12, Vol. 1-B, at 203:19-205:19, Vol. 2-A, at 12:8-16, 15:15-18, 16:14-20; Hughes, Vol. 3-A, at 19:7-19; Bengelsdorf, Vol. 3-B, at 140:17-23, 173:18-23. *See also* Williams, Vol. 4-B, at 128:7-16; Warmuth, Vol. 4-A, at 37:13-18.) Therefore, any attempt to cut through to ACE post-liquidation would be even weaker than the pre-liquidation cut through attempted by Nationwide (and rejected by the Sixth Circuit).

118. Indeed, representatives of Home had concluded that the AFIA Cedents could not cut through under the Assumption Agreement. (Rosen, Vol. 1-B, at 207:1-4; Hughes, Vol. 3-A, at 63:7-12.) Those representatives informed the AFIA Cedents in the fall of 2003 that they were not legally entitled to cut through, and that the Liquidator would strenuously oppose any cut-

through attempts. (Rosen, Vol. 1-B, at 206:9-14; Hughes, Vol. 3-A, at 63:19-64:1.) The AFIA Cedents never provided Home or JPLs with anything in writing or any legal advice stating that cut throughs are permissible. (Rosen, Vol. 1-B, at 206:18-23; Hughes, Vol. 3-A, at 64:2-5.)

119. In fact, both of the AFIA Cedents that testified at the evidentiary hearing had received legal advice concluding that cut throughs were impermissible. On October 20, 2003, U.S. counsel advised Equitas that a cut through was not permissible under controlling New York law. (Williams, Vol. 4-B, at 124:9-15, 127:6-10; ACE Trial Ex. CCC at 000940.) U.S. counsel similarly informed Agrippina that he could not find any legal authority to support a cut through attempt under the Assumption Agreement. (Warmuth, Vol. 4-A, at 37:19-23.) In a letter dated September 8, 2003, Agrippina's attorney stated that he could not "in good conscience" advise Mr. Warmuth to encourage the board of Zurich (as successor to Agrippina) to commit to litigation on the cut through issue. (ACE Trial Ex. QQ at ZURICH00388.)

120. Mr. Rosen testified at the evidentiary hearing that, in the fall of 2003, he was concerned about a cut through holding in *Koken v. Legion Ins. Co.*, 831 A.2d 1196 (Common. Ct. Pa. 2003), *aff'd sub nom. Koken v. Villanova Ins. Co.*, No. 204 MAP 2003, 2005 Pa. LEXIS 1479 (Pa. July 19, 2005). Mr. Rosen conceded, however, that the facts in *Legion* were materially different. First, the insolvency clause in *Legion* was worded differently so as to allow direct access to reinsurers in case of insolvency. (Rosen, Vol. 1-B, at 213:9-214:7, 215:22-216:16.) Second, the entity in *Legion* that became insolvent was, in contrast to Home, a new entity with relatively modest capital. (*Id.*, at 215:11-16.) Third, the entity in *Legion* did not participate in the program administration and did not assume a true underwriting risk; here, Home participated in the reinsurance as a risk bearer. (*Id.*, at 217:5-218:12.)

121. The Liquidator's alleged concern about cut-through litigation is further belied by the fact that the Home and the JPLs never did any analysis of the costs associated with opposing

an attempt to cut through, nor did they assess the likelihood of success of such litigation. (Rosen, Vol. 2-A, 3:16-21; Hughes, Vol. 3-A, 72:21-73:2, 73:9-12.)

**4. Side Deals Between AFIA Cedents and ACE**

122. The evidence does not support one of the Liquidator's primary contentions, which is that the threat of side deals between the AFIA Cedents and ACE justifies the Agreement. The evidence shows that no such threat existed. In fact, Home's representatives did not perform any analysis as to what costs the estate would incur in relation to side deal litigation. (Hughes, Vol. 3-A, at 73:9-17.)

123. As noted above, ACE committed during the October 16, 2003 conference call that (1) it would not have discussions with the AFIA Cedents while the commutation negotiations between ACE and Home were ongoing and (2) even if the ACE-Home commutation talks ceased, ACE would not enter into any side deals with the AFIA Cedents without providing notice to Home. (*See supra*, at ¶ 74.) Mr. Bengelsdorf noted that commitment in his contemporaneous meeting notes. (ACE Trial Ex. CC.) Mr. Hughes confirmed at the evidentiary hearing that he was told by Mr. Bengelsdorf that ACE had made such a commitment. (Hughes, Vol. 3-A, at 86:14-21.)

124. Notice of a side deal between ACE and any of the AFIA Cedents would have permitted Home to ask a court to set aside or enjoin the arrangement. (Wamser, Vol. 5-B, at 176:16-21.) Any side deal would involve ACE, which is clearly within the jurisdiction of this Court and other U.S. courts. Representatives of Home acknowledged that any litigation over a side deal would take place in the U.S. (Hughes, Vol. 3-A, at 65:19-67:2.) At the September 30, 2003 meeting, Home's representatives specifically warned ACE that Home would mount a legal challenge to any attempt by ACE to enter into side deals with AFIA Cedents. (Wamser, Vol. 5-B, at 163:14-22; Hughes, Vol. 3-A, at 70:13-20; *see also* ACE Trial Ex. M at H00651 (asserting

that side deal by ACE would constitute fraud or tortious interference with contractual relationship).)[3]

125. Mr. Wamser testified at the evidentiary hearing that ACE provided the two commitments to Home during the October 16, 2003 call as a good-faith gesture and in order to further the commutation discussions. (Wamser, Vol. 5-B, at 174:22-176:1.) Mr. Wamser also noted that ACE "had no intent to enter into any side deal discussions" with AFIA Cedents and was "not involved in any side deal discussions at that point in time." (*Id.*, at 176:2-4.)

126. To the contrary, ACE was very concerned that any side deal would expose it to "double liability" if a court later ordered ACE to pay the Liquidator the full amount of the cedent's claim (in addition to payments made under the side deal). (*Id.*, at 176:6-15.) Home's representatives similarly noted that the potential for double liability was a significant obstacle to a side deal between ACE and any of the AFIA Cedents. (Rosen, Vol. 2-A, at 4:22-6:6; Hughes, Vol. 3-A, at 70:21-71:6.) Home took the position that if that an AFIA Cedent asserted a payment obligation against ACE, Home would deem it to be a claim against the estate. (Rosen, Vol. 2-A, at 4:22-6:1; Bengelsdorf, Vol. 3-B, at 174:22-175:3; ACE Trial Ex. C at H00660.)

127. There were several other significant impediments to side arrangements:

(1) The New Hampshire statutes and Order of Liquidation would bar payments to anyone other than Home or the Liquidator. (Bengelsdorf, Vol. 3-B, at 172:23-173:17; Bengelsdorf Aff. at ¶ 7; Wamser, Vol. 5-B, at 157:6-14.)

(2) The insolvency clause in the Assumption Agreement requires payment to Home or the Liquidator and precludes payment to the AFIA Cedents directly. (Rosen, Vol. 1-A, at 91:4-12, Vol. 1-B, at 203:19-205:19, Vol. 2-A, at 12:8-16, 15:15-18, 16:14-20; Hughes, Vol. 3-A, at 19:7-19; Bengelsdorf, Vol. 3-B, at 140:17-23, 173:18-23; Bengelsdorf Aff. at ¶ 7; ACE Trial Ex. C at H00663; Williams, Vol. 4-B, at 128:7-21; Warmuth, Vol. 4-A, at 37:13-18.)

[3] Mr. Bengelsdorf testified at the evidentiary hearing that the Liquidator, as of September 2003, had legal analysis backing up his claim that side deals are impermissible. (Bengelsdorf, Vol. 3-B, at 178:10-179:4.)

(3) There is no privity of contract under the Assumption Agreement between ACE and the AFIA Cedents. (Rosen, Vol. 2-A, at 16:8-13; Bengelsdorf, Vol. 3-B, at 174:10-21; ACE Trial Ex. C at H00660.)

(4) A side deal would result in a loss of the AFIA Cedent's setoff rights — potentially worth tens of millions of dollars. (Hughes, Vol. 3-A, at 68:6-11; Durkin, Vol. 4-B, at 184:21-185:5; ACE Trial Ex. M at H00651.)

128. Home has claimed that three cedents — Unionamerica, Equitas and Agrippina — were threatening to enter into side deals with ACE or were actually engaged in such discussions as of the fall of 2003. Those assertions, however, have no basis in fact.

129. At the evidentiary hearing, ACE's representatives consistently and unequivocally testified that during the relevant period there were no discussions with any AFIA Cedents regarding side deals. (Durkin, Vol. 4-B, at 181:10-183:9; O'Farrell, Vol. 5-A, at 10:3-11:22, 19:16-20:6; Wamser, Vol. 5-B, at 155:4-16.) Both the Special Deputy Liquidator and Mr. Hughes, one of the JPLs, admitted that no AFIA Cedents told Home during the relevant period that such discussions were taking place. (Hughes, Vol. 3-A, at 64:6-17; Bengelsdorf, Vol. 3-B, at 172:14-18.)

130. Mr. Hughes also testified at the evidentiary hearing that the members of the ICC agreed not to enter into a side deal with ACE while Home and the AFIA Cedents were negotiating the terms of the Agreement (which began shortly after the October 21, 2003 meeting). (Hughes, Vol. 3-A, at 84:8-23.)

131. With regard to the three cedents specifically identified by Home, the Court finds as follows:

**a) Unionamerica**

132. The sole bases of Home's contention that Unionamerica might have been interested in a side deal with ACE are (1) the fact that Unionamerica withdrew its request for payment of claims, under a reservation of rights; and (2) speculation that Unionamerica might

have withdrawn the request because it wanted to discuss a side arrangement. There is no competent evidence to support a finding that Home had an objectively reasonable fear of a side deal between ACE and Unionamerica.

133. As noted above, ACE was precluded from honoring Unionamerica's requests for payment of the claims under New Hampshire law, the Order of Liquidation and the insolvency clause in the Assumption Agreement. Unionamerica's claims (like the claims of other AFIA Cedents) may only be paid through the procedures outlined by the Court, which include the filing of a proof of claim. (Bengelsdorf, Vol. 3-B, at 176:10-13.) Unionamerica only withdrew its requests for payment and never stated that it would not be filing a proof of claim against Home. (Bengelsdorf, Vol. 3-B, at 176:14-20; Durkin, Vol. 4-B, at 183:10-14.)

134. There is no direct evidence as to Unionamerica's possible motive for withdrawing the request for payment. The statement attributed to Ms. Nowak, an ACE-INA Services claims handler, that Unionamerica might have withdrawn the request for payment so that at some later date they would discuss a side deal, is nothing more than idle speculation. Ms. Nowak's deposition was not taken and she was not called as a witness at the evidentiary hearing.

135. Even if Ms. Nowak did engage in such speculation, it had no factual basis. Ms. Nowak's statement was not based on anything that Unionamerica had told her. (Rosen, Vol. 2-A, at 19:20-23.) Her supervisor, Mr. Durkin, testified at the evidentiary hearing that he was unaware of Ms. Nowak ever discussing a potential side deal with Unionamerica and that it would not be part of her responsibilities to have those discussions. (Durkin, Vol. 4-B, at 186:7-12.)

136. In addition, the testimony adduced at the evidentiary hearing conclusively shows that ACE was not involved in any side deal discussions with Unionamerica and no one ever told representatives of Home that such discussions were taking place. (Rosen, Vol. 2-A, at 14:4-13, 20:1-8; Ellis, Vol. 2-B, at 128:15-20; Hughes, Vol. 3-A, at 56:9-19, 71:7-21; Bengelsdorf, Vol. 3-B, at 176:21-177:17; Durkin, Vol. 4-B, at 182:23-183:9; Wamser, Vol. 5-B, at 155:17-156:6.)

137. The most likely explanation for Unionamerica's withdrawal of the payment requests is that St. Paul, which owns Unionamerica, was attempting to determine whether the amount received from Home as a result of the Unionamerica claims would be greater or lesser than the amount St. Paul would have to pay Century under the reinsurance provided by the sellers of the AFIA business (as described above in paragraph 24). (Hughes, Vol. 3-A, at 60:6-61:20; Durkin, Vol. 4-B, at 184:15-186:6.) Mr. Rosen and Ms. Ellis were informed during the September 2003 meeting with Unionamerica that Unionamerica was taking its instructions on the AFIA-related claims from St. Paul, and Home's representatives understood that Unionamerica may have withdrawn its payment requests because of St. Paul's reinsurance obligations. (Ellis, Vol. 2-A, at 90:2-17; Hughes, Vol. 3-A, at 60:6-61:20.)

**b) Equitas**

138. The Liquidator has sought to justify the Agreement on the grounds that Equitas and ACE were involved in side deal discussions concerning the AFIA liabilities. The evidence, however, shows that (1) contrary to some of the testimony offered by the Liquidator, Mr. Williams of Equitas never informed Home of such discussions; (2) Equitas had agreed that it would not enter into discussions on a side deal with ACE while the Agreement was being negotiated; and (3) Equitas and ACE were not involved in talks regarding a side deal on the AFIA business.

139. Mr. Hughes testified at the evidentiary hearing that, during the relevant time period, Equitas never told Home about an Equitas-ACE side deal regarding the AFIA liabilities. (Hughes, Vol. 3-A, at 72:9-12, 82:7-10.) Mr. Williams confirmed that he had not done so. (Williams, Vol. 4-B, at 135:1-4.)

140. Mr. Rosen testified at the evidentiary hearing that Mr. Williams had "intimated" that Equitas and ACE were in discussions regarding a side deal on the AFIA liabilities. (Rosen, Vol. 2-A, at 9:6-10:4.) Mr. Rosen conceded, however, that he had not received any specifics

from Mr. Williams on the alleged deal. (Rosen, Vol. 2-A, at 10:5-7.) Even more significantly, Mr. Bengelsdorf's description of the conversation between Messrs. Rosen and Williams illustrates that it would not be reasonable to rely on it as evidence of discussions between ACE and Equitas: "[Mr. Rosen] inferred that there was an intimation that Equitas might be talking to ACE. ... [T]hat's all it was[,] an intimation, a discussion heard of someone else that may have heard something." (Bengelsdorf, Vol. 3-B, at 145:8-11.)

141. Mr. Williams testified at the evidentiary hearing that he was not involved with the ACE-Equitas discussions, which were being handled by others at Equitas. (Williams, Vol. 4-B, at 132:22-133:22.) Mr. O'Farrell, who was involved in the commutation talks, repeatedly testified at the evidentiary hearing that the potential commutation had nothing to do with the AFIA liabilities and that ACE could not commute those liabilities without Home's involvement. (O'Farrell, Vol. 5-A, at 13:3-14:16, 16:23-17:16, 64:5-10.)

142. Moreover, even if Mr. Rosen had inferred (incorrectly) in September 2003 that Equitas and ACE were in discussions about an AFIA-related side deal, it would not be reasonable for Mr. Rosen or the Liquidator to believe that such discussions were continuing after October 21, 2003 in light of Equitas' commitment that it would not enter into side deals with ACE while Home and the AFIA Cedents were negotiating the Agreement.

143. Ms. Ellis' testimony on her discussions with Mr. Williams suffers from the same infirmities. Ms. Ellis initially testified at the evidentiary hearing that Mr. Williams actually told her, in the October-November 2003 time period, that Equitas and ACE were discussing a side deal regarding the AFIA business. (Ellis, Vol. 2-A, at 99:17-21, 119:2-8.) On cross-examination, Ms. Ellis admitted that she testified differently at her deposition and that, at best, Mr. Williams had "implied" (without giving any specifics) that Equitas and ACE were engaged in such discussions. (Ellis, Vol. 2-B, at 125:16-23; 140:6-141:15.) Ms. Ellis also acknowledged

that Mr. Williams was not the negotiator for Equitas and that others at Equitas were handling the discussions with ACE. (Ellis, Vol. 2-B, at 126:21-127:1.)[4]

144. Even if Ms. Ellis' testimony were credible, it would not have been reasonable for the Liquidator to rely on the alleged conversation between Ms. Ellis and Mr. Williams as a motivation for the Agreement.

145. Equitas agreed that it would not enter into a side deal with ACE while Home and the AFIA Cedents were in negotiations over the Agreement. (Hughes, Vol. 3-A, at 81:20-82:6.) Ms. Ellis testified that the conversation with Mr. Williams occurred during the negotiations over the Agreement (Ellis, Vol. 2-A, at 120:4-18), which was after Equitas had provided its commitment.

146. In addition, the decision to pursue the Agreement had already been made by that point. Ms. Ellis testified that she took Mr. Williams' comment into account in determining the appropriate percentage payment to the AFIA Cedents, and not in deciding whether a deal with the AFIA Cedents should be pursued. (*Id.*)

**c) Agrippina**

147. As with Unionamerica and Equitas, there was no evidence of a reasonable threat of a side deal between Agrippina and ACE during the relevant time period.

148. Mr. Rosen testified at the evidentiary hearing that Agrippina (and the other Rutty pool members) were differently situated from the other AFIA Cedents and were in a unique position because of the termination provisions in Treaty R. (Rosen, Vol. 2-A, at 21:1-22:2.)

149. Mr. Rosen also testified that Home would have opposed any effort by Agrippina to terminate Treaty R as a violation of New Hampshire law, and that Home would have sued ACE for tortious interference if ACE agreed to pay Agrippina any consideration as an

[4] It is telling that the alleged discussion between Ms. Ellis and Mr. Williams was not included in the Liquidator's Offer of Proof. There was also no testimony that any of the Home's U.S. representatives — including Mr. Bengelsdorf, who had the day-to day responsibility for running the estate and was aware of the major developments affecting Home (Bengelsdorf, Vol. 3-B, at 164:14-165:6) — were ever told about the conversation prior to February 11, 2004.

inducement for termination. (*Id.*, at 22:3-5, 24:18-21; Warmuth, Vol. 3-B, at 211:19-212:6.) Agrippina had received advice that a side deal with ACE would expose ACE to double liability, that Treaty R could not be terminated under New Hampshire law and that an order of this Court barring termination would apply abroad to Agrippina. (Warmuth, Vol. 4-A, at 29:15-30:3, 31:4-12; Warmuth, Vol. 4-A, at 32:18-21; 60:5-18, 62:15-63:20.)

150. Mr. Warmuth never told Home during the relevant time period that he had asked ACE for consideration in exchange for termination of Treaty R or that ACE had offered such consideration to Agrippina. (Rosen, Vol. 2-A, at 25:18-20, 27:8-12; Warmuth, Vol. 4-A, at 4:7-11, 7:20-8:2, 51:17-23.)

151. Mr. Rosen testified at the evidentiary hearing that there was an "intimation" of direct dealings between ACE and Agrippina during a telephone conversation between Mr. Warmuth and Mr. Durkin. (Rosen, Vol. 2-A, at 25:18-26:3.) In fact, as discussed below, the conversation did not include any discussion about side deals. Mr. Warmuth also testified that — based on the self same conversation in September 2003 — he believed ACE might be interested in a side deal with Agrippina. (Warmuth, Vol. 3-B, at 216:10-221:2.)

152. On the basis of any rational examination, however, there is no support for Mr. Warmuth's speculation nor the testimony of Mr. Rosen regarding a side deal between Agrippina and ACE. According to Mr. Warmuth, who claimed that side deal discussions were "in the air," Mr. Durkin asked him whether there was "something we should be talking about." (Warmuth, Vol. 3-B, at 219:16-19, Vol. 4-A, at 20:7-12.) Mr. Warmuth's vague suggestions cannot reasonably support his conclusion that ACE was interested in a side deal — particularly given the pending and hotly contested arbitration between the parties.

153. Mr. Durkin, on the other hand, testified at the evidentiary hearing unequivocally that the issue of side deals never came up in any conversation with Mr. Warmuth and he did not hint in any way during the September 2003 telephone conversation that ACE was interested in

doing a side deal. (Durkin, Vol. 4-B, at 180:5-22.) Mr. Durkin added that he did not tell Mr. Rosen (or hint in any way) that ACE was involved in discussions with Agrippina regarding a side deal. (*Id.*, at 179:20-180:4.)

154. Indeed, the only side deal that was being negotiated in September 2003 was between Home and Agrippina. Mr. Warmuth told Home's representatives in September 2003 that unless Home came back with an incentive not to terminate Treaty R (which had to be a "substantial offer") Agrippina would terminate the treaty no later than December 15, 2003. (Warmuth, Vol. 3-B, at 215:13-21; Warmuth, Vol. 4-A, at 64:4-12, 66:11-67:23; Hughes, Vol. 3-A, at 77:1-6.)

155. Home's representatives responded by saying Home would be looking for a commercial resolution and would come back to Agrippina with an offer. (Warmuth, Vol. 3-B, at 216:8-9; Warmuth, Vol. 4-A, at 67:14-23; Hughes, Vol. 3-A, at 78:1-3.) Agrippina, in turn, agreed that it would not seek a deal with ACE while it was waiting for Home's proposal. (Warmuth, Vol. 4-A, at 64:13-15; 65:6-18.) This occurred over a month before the first ICC meeting which allegedly triggered the discussion over the need for the Agreement.

156. Thus, as of September 2003, there was no threat of a side deal between Agrippina and ACE because Home was formulating an incentive for Agrippina not to terminate Treaty R.

**5. Incentive for Filing and Prosecuting Claims**

157. There is no evidence to support the Liquidator's final argument that without the incentives set forth in the Agreement, the AFIA Cedents would not file and fully prosecute their claims against Home.

158. Several witnesses testified at the hearing that it is standard procedure for reinsurance creditors who are in the same class as the AFIA Cedents to file proofs of claim in insurance liquidations. (Rosen, Vol, 1-B, at 169:3-18; Williams, Vol. 4-A, at 112:2-23; Durkin,

Vol. 4-B, at 195:4-16; Craig, Vol. 5-A, at 102:12-103:4.) None of the AFIA Cedents told Home that they would not be filing claims. (Ellis, Vol. 2-A, at 110:17-111:2.)

159. Those claims are typically in excess of the potential setoff and creditors will file the largest claim possible. (Rosen, Vol. 1-B, at 169:19-170:4.) Indeed, in this proceeding, several non-AFIA Cedents who are also Class V creditors have submitted proofs of claim well in excess of their potential setoff. (Rosen, Vol. 1-B, at 175:15-180:14; ACE Trial Ex. HH.)

160. Prior to the October 21, 2003 ICC meeting and the discussion of an incentive for the filing and prosecution of claims, several AFIA Cedents indicated that they would be filing proofs of claims. (ACE Trial Exs. E, F, G and GGG.) Certain cedents also submitted claims information to Home, which clearly included amounts beyond their potential setoff. (*Id.*)

161. It is undisputed that creditors who are asserting setoff, including the AFIA Cedents who have setoff positions, must prosecute their claims at least up to the amount of the setoff. (Rosen, Vol. 1-B, at 185:10-19; Ellis, Vol. 2-B, at 132:21-133:6; Hughes, Vol. 3-A, at 32:15-33:11;Williams, Vol. 4-A, at 107:10-13; ACE Trial Ex. B.) At the October 21, 2003 ICC meeting, counsel for the JPLs described setoff as a "strong incentive" for the AFIA Cedents to present claims. (ACE Trial Ex. U at H01828.)

162. In addition to setoff, Home's representatives identified other reasons why the AFIA Cedents would file claims against Home. Mr. Bengelsdorf noted in a September 17, 2003 meeting that the AFIA Cedents would file claims because the "estate return could be good" and for "tax preservation purposes." (ACE Trial Ex. B.)

163. Mr. Hughes explained at the evidentiary hearing that several of the AFIA Cedents are U.S. companies and it was his understanding that they would need to file claims in order to take advantage of bad debt tax relief under U.S. law. (Hughes, Vol. 3-A, at 30:16-31:12.)

164. Mr. Bengelsdorf testified that uncertainty about the eventual distribution by the estate is a further reason to file claims. (Bengelsdorf, Vol. 3-B, at 189:12-19.) Home's

representatives also noted that the assets and liabilities of the estate were uncertain as of the fall of 2003. (Rosen, Vol. 2-A, at 34:20-23; Ellis, Vol. 2-A, at 104:2-8, 105:8-12; Bengelsdorf, Vol. 3-B, at 190:23-191:4.)[5] They remain uncertain to this day, and Ms. Ellis testified that: "I don't think we know now whether Class V creditors will received a dividend. It is within the scope of possibility that they might receive a dividend." (Ellis, Vol. 2-A, at 107:13-18.)

165. As a practical matter, the AFIA Cedents would not be able to stop prosecuting their filed claims once the level of their setoff is reached. Home's representatives conceded that the amount of setoff will not be known until claims are admitted into the estate, which is likely to be many years in the future. (Rosen, Vol. 1-B, at 186:17-20; Hughes, Vol. 3-A, at 34:18-36:12; Bengelsdorf, Vol. 3-B, at 186:5-11; Williams, Vol. 4-A, at 110:1-112:1.)

166. It is also clear that, as discussed above (*see supra*, at ¶¶ 33-35), the prosecution of claims is not as difficult or costly as the Liquidator alleges. Much of the burden is handled by brokers, who are paid a fee to present claims, and the claims submitted to Home were often the same claims that had been submitted to other reinsurers on the risk. Once claims are presented to Home, the Claims Protocol places most of the adjudication responsibility on the Liquidator and sets forth a streamlined determination process. To date, the presentation and determination of claims has involved minimal work by the claimants.

167. Moreover, even if there were any resistance to providing information to the Liquidator (which would allow for the proving up of the claim), Mr. Rosen acknowledged at the evidentiary hearing that the Liquidator has the power to compel the production of the information via subpoena. (Rosen, Vol. 2-A, at 64:2-11, 65:3-7.) To the extent the AFIA Cedents claimed they were beyond the Court's jurisdiction, the JPLs have the same power of compulsion. (Hughes, Vol. 3-A, at 117:12-18; Hacker, Vol. 5-A, at 80:11-18.)

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[5] When Ms. Ellis met with the AFIA Cedents in the summer and fall of 2003, she told them they should put in claims because it was not yet known whether Class V creditors would receive a distribution. (Ellis, Vol. 2-A, at 102:23-103:17.)

168. Perhaps the most significant evidence is the testimony from several witnesses that they are unaware of any other liquidation where creditors received an incentive payment to file and prosecute their claims. (Rosen, Vol. 1-B, at 175:11-14; Hughes, Vol. 3-A, at 16:22-17:7; Williams, Vol. 4-A, at 113:1-8; Durkin, Vol. 4-B, at 196:1-4; Craig, Vol. 5-A, at 107:18-21.) The Liquidator has not presented any evidence showing why this liquidation proceeding should be the first one to allow such a payment.

## III. Administrative Cost Findings[6]

169. The ACE Companies' expert, Robert Craig, testified at the evidentiary hearing that administrative costs typically include post-liquidation costs incurred by the Liquidator, such as legal fees, accounting fees and the like. (Craig, Vol. 5-A, at 107:22-108:8.)

170. The Liquidator took a similar view to administrative costs in his November 28, 2003 presentation to the ICC members. The slides used during that presentation refer to the legal and administrative costs of the proposed Agreement, and describe the payments to AFIA Cedents under the Agreement as a "dividend" rather than as an administrative cost. (Liquidator's Trial Ex. 32 at H00396-99; Bengelsdorf, Vol. 3-B, at 193:2-194:12.)

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[6] The ACE Companies believe the Court should not make any additional findings on the administrative cost issue. The Court's October 8 Order determined that payments under the Agreement might constitute administrative expenses. (October 8 Order, at 6-10.) The Court also authorized the ACE Companies and Benjamin Moore & Co. to appeal the Court's ruling on the administrative expense issue at a later date. (*Id.*, at 14.) That ruling did not save the Agreement, as the Court, in accordance with the New Hampshire Supreme Court's instructions, ordered a hearing to determine whether the Proposed Agreement is fair and reasonable. (*Id.*, at 13.) The ACE Companies have limited their findings of fact and rulings of law to the issue of whether the Proposed Agreement is fair and reasonable. This is in accord with the following statements made at the evidentiary hearing:

> Lee: I want to be clear that none of the five issues that were sent back from the Supreme Court with the exception of the question of reasonableness and fairness are what's going to be addressed in the findings of facts and conclusions of law.
>
> Court: Right.

(Vol. 5-B, at 206:23:4-207:5). This is also in accordance with New Hampshire practice. *See* RICHARD V. WIEBUSCH, 5 NEW HAMPSHIRE PRACTICE, CIVIL PRACTICE AND PROCEDURE § 49.02 (2d ed. 1997) ("Requests for findings and rulings should be kept to a minimum and should focus on only those issues that will dispose of a case.") In the event, however, that the Court wishes to enter findings on administrative cost issue, the ACE Companies have requested certain findings of facts regarding this topic. (*See infra*, at ¶¶ 169-172.)

171. The evidence also shows that payments contemplated under the Agreement are in fact on account of, and directly relate to, the AFIA Cedents' pre-liquidation claims against the estate. (Ellis, Vol. 2-B, at 135:10-12; Williams, Vol. 4-B, at 138:10-23.)

172. Mr. Craig testified at the evidentiary hearing that he is unaware of any other liquidation where reinsurance creditors were paid as Class I claimants. (Craig, Vol. 5-A, at 105:3-11.) Messrs. Rosen and Williams similarly testified that, in the many liquidations in which they have been involved (effectively every major U.S. and U.K. insolvency over the past decade or more), their companies were never paid as Class I creditors. (Rosen, Vol. 1-B, at 173:8-10, 173:14-20; Williams, Vol. 4-A, at 113:9-14.) Mr. Rosen added that he is unaware of any reinsurance creditor in those cases being paid as a Class I creditor. (Rosen, Vol. 1-B, at 174:15-21.)

## Rulings of Law

### I. Legal Standard

A. Pursuant to the September 13 Order, this Court must, on a complete evidentiary record, determine whether the Agreement is a fair and reasonable settlement of a dispute. (September 13 Order at 1-2.)

B. The Liquidator must persuade this Court that the Agreement is objectively fair and reasonable by a preponderance of the evidence. *See, e.g., In re GHR Companies, Inc.*, 50 B.R. 925, 931 (Bankr. D. Mass. 1985) (citation omitted) ("The burden of persuading the court that the compromise should be approved rests with the parties proposing the compromise."); *In re Liquidation of American Mut. Liab. Ins. Co.*, 632 N.E. 2d 1209, 1216 (Mass. 1994) ("[The] receiver should demonstrate that the settlement ... is fair and reasonable."). The Liquidator has acknowledged that he bears that burden. (Vol. 1-A, at 19:3-8.)

C. The Liquidator may not carry his burden through conclusory statements; the full factual record must show that the Agreement is objectively fair and reasonable. *See Protective*

*Comm. for Indep. Stockholders of TMT Trailer Ferry, Inc., v. Anderson*, 390 U.S. 414, 424 (1968); *In re American Mut.*, 632 N.E. 2d at 1217; *In re Harvard Pilgrim Health Care, Inc.*, 746 N.E.2d 513, 521-22 (Mass. 2001).

D. The Court must play a "quasi-inquisitorial" role and not give undue deference to the Liquidator's position; the Court "ha[s] a duty to apprise itself of all facts necessary for an intelligent and *objective* opinion of the probabilities of ultimate success should the potential claims ... be litigated." *In re Boston & Providence R.R. Corp.*, 673 F.2d 11, 12 (1st Cir. 1982) (emphasis added) (citing *Protective Comm.*, 390 U.S. at 424 (same)). The Court's independent analysis must be sufficiently detailed to allow a reviewing court to distinguish it from "'mere boilerplate approval'" of the Liquidator's purported justifications for the Agreement. *Id.*

E. In determining whether the Agreement is fair and reasonable, the Court must look to the following factors:

i. As a threshold matter, whether a reasonable liquidator would have believed that the threatened litigations would take place.

ii. Whether a reasonable liquidator would have believed that the threatened litigations would be complex.

iii. The costs and expenses that a reasonable liquidator would have believed the estate would incur.

iv. The likelihood that Home would prevail in such litigations, as perceived by a reasonable liquidator.

*See In re Estate of Indian Motorcycle Mfg., Inc.*, 299 B.R. 8, 20 (D. Mass. 2003) (citing *Jeffrey v. Desmond*, 70 F.3d 183, 185 (1st Cir. 1995)); *see also In re Boston*, 673 F.2d at 12; *In re GHR*, 50 B.R. at 931.

F. The Liquidator's actual, subjective belief is irrelevant; the reasonableness and fairness of the Agreement is held to an objective standard. *See, e.g., In re Boston*, 673 F.2d at 12;

*Protective Comm.*, 390 U.S. at 424. Thus, the dispositive "state of mind" for determining the fairness and reasonableness of the Agreement is the state of mind of an objectively reasonable liquidator. (Vol. 1-A, at 97:21-23.)

G. The Court will examine whether a reasonable liquidator would have entered into the Agreement under the circumstances.

## II. Application of Standard to Facts

### A. No Dispute Is Being Settled or Compromised

H. As a threshold matter, the Court rules that the Agreement cannot meet the standard set forth by the Supreme Court in the September 13 Order.

I. The standard applies to disputes that are being settled or compromised. Here, representatives of Home have admitted that the Agreement is not a settlement of a matter in actual or threatened litigation. Instead, it sets forth an incentive to be paid to the AFIA Cedents for the filing and prosecution of claims. (Ellis, Vol. 2-A, at 117:12-118:4.) Accordingly, the Liquidator has failed to carry his burden of proof on the issue of fairness and reasonableness.

### B. The Liquidator Has Not Met the Criteria for Fairness and Reasonableness

J. The Court has described above the four alleged threats of litigation that, according to the Liquidator, were justifications for entering into the Agreement. An application of the Supreme Court's objective standard to each of these alleged threats demonstrates that, as a matter of law, the Agreement is neither fair nor reasonable because the "threats" were either non-existent or not realistically credible.

#### 1. Ring Fencing

K. As noted above, the Liquidator has withdrawn ring fencing as one of the reasons for the Agreement. (*See supra*, at ¶ 96.) That fact, by itself, warrants a ruling that the alleged ring fencing threat does not meet the Supreme Court's objective standard for fairness and reasonableness.

L. Even assuming, however, that ring fencing is still a part of the Liquidator's case, the Court rules that a reasonable liquidator would not have considered ring fencing to be a realistic or credible threat. The Court further rules that no reasonable insurance executive in the position of the AFIA Cedents would have pursued the ring fencing option.

M. Both parties have presented legal advice that English law would not permit ring fencing under the circumstances present in this case. The arguments in favor of ring fencing are so weak that, as Mr. Hacker pointed out, there would be no credible risk of costly litigation over ring fencing. To the contrary, the party bringing such an action would clearly expose itself to an award requiring it to pay the prevailing party's attorneys' fees.

N. The evidence also shows that the AFIA Cedents' consideration of ring fencing was very brief and that it ceased to be an issue after the October 21, 2003 ICC meeting.

**2. Constructive or Forced Novation**

O. The Court rules that a reasonable liquidator would not have considered constructive or forced novation to be a realistic or credible threat. The Court further rules that no reasonable insurance executive in the position of the AFIA Cedents would have pursued an argument based on constructive or forced novation.

P. It is undisputed that the obligations under the AFIA Treaties were never novated and remained with Home.

Q. Counsel for the Liquidator considered the viability of an argument that ACE's direct dealings with the AFIA Cedents or its prior commitments would provide a basis for an argument based on constructive or forced novation. The conclusion, which was not challenged, was that such an argument had no support in the law.

R. There is no evidence that Equitas or Agrippina (the only AFIA Cedents that raised the novation issue) ever took additional steps in the relevant time period to consider, let alone pursue, a novation argument.

### 3. Cut Through Under Assumption Agreement

S. As with ring fencing, the Liquidator has abandoned any argument that the threat of cut through litigation is a basis for the Agreement. (*See supra*, at ¶ 112.) For that reason alone, the threat of cut through does not meet the standard for fairness and reasonableness.

T. Even if, however, the Liquidator still contends that the threat of cut through litigation was a justification for the Agreement, the Court rules that a reasonable liquidator would not have considered cut through to be a realistic or credible threat. The Court further rules that no reasonable insurance executive in the position of the AFIA Cedents would have pursued cut through litigation.

U. The legal impediments to cut through are significant. The Assumption Agreement lacks the requisite language permitting a cut through and, to the contrary, contains two clauses that expressly forbid cut through. Even more importantly, the *Nationwide* case acts as a complete bar to any attempt at a cut through under the Assumption Agreement.

V. The evidence shows that Home and at least two of the AFIA Cedents, in considering the cut through issue, came to the conclusion that a cut through under the Assumption Agreement is not permissible. Agrippina's counsel, in particular, stated that he could not "in good conscience" recommend that the board of Zurich (as Agrippina's successor) pursue cut through litigation.

W. At the evidentiary hearing, the Liquidator attempted to rely on the *Legion* case for the proposition that cut through presented a threat in the fall of 2003. For the reasons cited above (*see supra*, at ¶ 120), the Court rules that the unusual facts in *Legion* easily distinguish it from this proceeding. *Legion*, therefore, provides no support for the Liquidator's argument.

### 4. Side Deals Between AFIA Cedents and ACE

X. The Court rules that a reasonable liquidator would not have considered side deals to be a realistic or credible threat. The Court further rules that no reasonable insurance executive

in the position of ACE or the AFIA Cedents would have pursued a side deal on the AFIA liabilities.

Y. The primary reason that side deals presented no threat to the Liquidator is that he had negotiated a series of agreements by October 2003 eliminating any true risk of a side deal. ACE committed that it would not engage in discussions with the AFIA Cedents while the ACE-Home commutations talks were ongoing. Moreover, even if the commutations had ended (and the evidence shows that they continued during the relevant time period), ACE also committed to provide notice to Home of any side deal with the AFIA Cedents. Such notice would have given the Liquidator the opportunity to enjoin or set aside a side deal. The likelihood of the Liquidator prevailing in such litigation would be very high, given that a side deal would clearly violate New Hampshire law and the terms of the Assumption Agreement.

Z. In addition to the agreements with ACE, the Liquidator had a commitment from the ICC members that they would not enter into side deals with ACE while the Liquidator and the AFIA Cedents were negotiating the Agreement. The Liquidator also had a specific agreement along the same lines from Equitas and Agrippina.

AA. The evidence further shows that there were disincentives to entering into a side deal (in addition to the fact that side deals are legally impermissible). ACE was concerned that a side deal would expose it to double liability if a court ordered it to pay the Liquidator and the AFIA Cedents with whom ACE had entered into an agreement. For their part, the AFIA Cedents were concerned that a side deal would result in a loss of their substantial setoff claims.

BB. Finally, the Court finds that the Liquidator's concerns about potential side deals between ACE and Unionamerica, Equitas or Agrippina had no reasonable basis. Other than the "intimations" and unsupported inferences discussed above, there is no evidence that ACE was engaged in side deal discussions with any of these cedents or that Home had credible information that such discussions were taking place during the relevant time period.

CC. In sum, the Agreement is neither fair nor reasonable because there was no realistic or credible threat of the litigation cited by the Liquidator as the rationale for the Agreement.

**III. The Agreement is Not Necessary**

DD. Even if the Agreement were fair and reasonable under the Supreme Court's objective standard, the Court finds that it was not necessary.

EE. In assessing the necessity of the Agreement, the Court will examine whether the AFIA Cedents, in the absence of the Agreement, would have filed and prosecuted their claims.

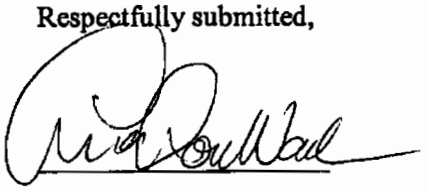
FF. The undisputed evidence adduced in this proceeding demonstrates that the AFIA Cedents, regardless of the Agreement, had a strong incentive to file and prosecute their claims to take advantage of their significant setoff positions. It is not reasonable or practical to believe that the AFIA Cedents would (or could) cease the prosecution of the claims once their level of setoff was reached. All parties agree that setoff will not be determined until all claims are admitted into the estate, which will be well into the future.

GG. There are also other reasons for the AFIA Cedents to file claims, including the potential for a distribution from the estate (which is still possible) and the preservation of tax claims. Once a claim is filed, the prosecution of claims is not nearly as onerous as the Liquidator asserts. The evidence shows that many AFIA Cedents employ brokers for the submission of claims and that the same claims will be presented to other reinsurers. Several witnesses testified that litigation or disputes over those claims in liquidations is very rare.

HH. Under the circumstances, there was no reason for the Liquidator to conclude that he should agree to pay the AFIA Cedents tens of millions of dollars to encourage them to file and prosecute claims. The evidence shows that the Liquidator acted precipitously and had other options, including the use of his subpoena power to require the submission of claims information.

II. The Court is unaware of any other liquidation where a similar incentive has been paid, and it rules that such a payment here would be unnecessary as a matter of law.

Respectfully submitted,



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The undersigned certifies that a copy of the foregoing pleading has been served on Roger A. Sevigny, Commissioner of Insurance, Peter Bengelsdorf, Special Deputy, and the following counsel via First Class mail on August 12, 2005:

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