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

BENJAMIN MOORE & CO.'S POST-TRIAL MEMORANDUM

Benjamin Moore & Co. ("BMC"), through its undersigned counsel, submits this Post-Trial Memorandum based upon the evidence introduced at the evidentiary hearing held on July 25-29, 2005. BMC joins in the Requests for Findings of Fact and Rulings of Law submitted by the ACE Companies on the issue of whether the proposed agreement fair and reasonable, and if so, whether it is necessary. BMC submits this Memorandum in support of the limited proposed Findings and Conclusions it is submitting, which are addressed to the separate issues of whether: (1) the proposed administrative expense payments to AFIA cedents are "actual and necessary" cost of administration, and (2) whether the AFIA agreement is fair to other creditors of Home.

I. Introduction

As BMC told the Court in its opening statement at the evidentiary hearing, the evidence shows that the AFIA agreement before the Court for approval is the product of efforts by a very sophisticated group of insurance and reinsurance professionals to circumvent the mandatory priority rules in the New Hampshire liquidation statute in order to obtain priority payment on the Class V reinsurance claims of AFIA cedents. There is evidence before the Court (ACE Ex. GG) that shows the largest AFIA cedent (Equitas) knew as it was negotiating the agreement that it was a "material departure" from the statutory scheme. There is also evidence before the Court, in the form of both lay and expert testimony, that the proposed agreement is unprecedented in that no other Liquidator has ever paid a group of reinsurance creditors an incentive to file and

prosecute claims against an insolvent reinsurer. Despite the unprecedented nature of the agreement and the "far reaching consequences" of approval of the agreement for statutory liquidation priority rules in New Hampshire and around the country,[1] the Liquidator made the proposed agreement without seriously assessing any of the risks to the estate said to be avoided by the agreement—risks shown by the evidence to be illusory at worst, and at best not substantial enough to warrant payment of a $70+ million fee to AFIA cedents. The Liquidator's failure to make any meaningful assessment of the risks he asserts will be avoided by the agreement is reason enough to deny approval of the agreement. Even if the Court conducts the assessment the Liquidator should have made, based on the evidence adduced at the evidentiary hearing, it will conclude that it the evidence is insufficient to support approval of the agreement as fair and reasonable, much less essential to protection of the estate's interests.

I. Because The Liquidator Proposes To Pay AFIA Cedents A Large Administrative Expense Payment Under the Agreement, It Cannot Be Approved Absent Proof That The Payment Is Essential To Recovery Of Assets By The Estate.

Under R.S.A. 402-C:44, I, only certain "costs and expenses of administration" can be given first priority payment. The Liquidator asserts that the proposed payments to AFIA cedents are "actual and necessary costs of preserving or recovering the assets of the insurer." The term "necessary" is not defined in the statute, so it should be given its plain and ordinary meaning. State v. Nelson, 150 N.H. 569, 572 (2004)(when a particular term is undefined, the Court assigns to it its plain and ordinary meaning). The plain and ordinary meaning of the term "necessary" is defined in Webster's Dictionary as follows:

> 1. Being such in its nature that it must exist, occur, or be true; inevitable. 2. Absolutely needed to accomplish a desired result.

[1] Interlocutory Appeal Statement, p. 5 (Nov. 5, 2004)

Webster's Concise Dictionary of the English Language, p. 484 (Int'l Enc. Ed. 1998). Other courts have given the term "necessary" it ordinary dictionary definition absent some other statutory or contractual definition. See United Savings Ass'n v. Timbers of Inwood Forest, 484 U.S. 365, 375-76 (1988)(the term "necessary to an effective reorganization" in Section 362(d)(2) of the Bankruptcy Code means "essential for an effective reorganization"); Abraham v. Insurance Co. of North America, 117 Vt. 75, 80 (1951)(the term "necessary" in a livestock insurance policy means "indispensable" or "unavoidable").

A strict and narrow construction of the term "necessary" is supported by the policy underlying Section 44,I, and other provisions of the New Hampshire Liquidation statute. The administrative expense provisions of the federal Bankruptcy Code, from which the language of Section 44,I is derived,[2] have been construed narrowly in order "to keep fees and administrative costs at a minimum." Otte v. United States, 419 U.S. 43, 53 (1974); In re United Trucking Service, Inc., 851 F.2d 159, 164 (6th Cir. 1988); In re O.P.M. Leasing Services, Inc., 23 B.R. 104, 121 (Bankr. S.D.N.Y. 1982); see also 3 Collier on Bankruptcy, ¶ 503.04, at 503-23 (15th ed. 1988). Reduction and minimization of administrative costs and expenses is central to the goal of protecting the policyholder and other creditors of the estate, whose recovery is diminished by every dollar paid in administration costs. See In re Mammoth Mart, 536 F.2d 950, 953 (1st Cir. 1976); In re Dant & Russell, 853 F.2d 700, 706 (9th Cir. 1988).

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2 The New Hampshire Insurers Rehabilitation and Liquidation Act, R.S.A. §§ 402-C:1-61, is based on the 1967 Wisconsin Insurers Rehabilitation and Liquidation Act. The legislative history of the Wisconsin Act states that Section 645.68(1) of that law, which is identical to Section 402-C:44,I of the New Hampshire Act, "is freely adapted from the first priority provision in Federal Bankruptcy Act s. 64a." Section 64a of the Federal Bankruptcy Act is the basis for the current version of the administrative expense provision of the Bankruptcy Cide, 11 U.S.C. § 503(b), enacted in 1978. See Senate Report No. 95-989, 11 U.S.C. § 503. Thus, federal bankruptcy authority construing Section 503(b) of the Bankruptcy Code is highly relevant in the interpretation of the language of Section 402-C:44,I.

Moreover, other parts of the New Hampshire liquidation statute indicate a clear legislative intent to give the term "necessary" in Section 44,I a narrow meaning that excludes costs and expenses that are merely expedient. For example, Section 25 of the liquidation statute uses the term "necessary" twice, each time within the phrase "necessary or expedient." R.S.A. 402-C:25, VI, XXII. Thus, the Legislature clearly meant "necessary" to mean something other than "expedient;" otherwise it would not have used both words in the disjunctive. Unlike Section 25, Section 44 does not use the phrase "necessary or expedient." It uses the phrase "actual and necessary" instead. This is unmistakable legislative intent that the term "necessary" in Section 44 should be read to mean essential or indispensable, and not merely expedient.

Thus, administrative expense payments to AFIA cedents that are the centerpiece of the agreement cannot be approved unless the Liquidator demonstrates to the Court's satisfaction that the payments as proposed are essential or indispensable to recovery of reinsurance from the ACE Group.

II. The Liquidator Has Failed To Demonstrate That The Payment Of 1/3 Of The Reinsurance Recovery To AFIA Cedents As An Administrative Expense Is Essential To The Recovery Of Reinsurance From The ACE Companies.

The evidence shows that Liquidator made a hasty and ill-considered decision to enter into a sharing agreement with the AFIA cedents, without pursuing other available alternatives for recovering from the ACE Companies that would not involve sharing of one-third of the reinsurance recovery with one group of preferred Class V creditors. The Liquidator knew that, as of October 16, 2003, ACE was interested in pursuing commutation discussions aimed at reaching an agreement that would provide payment[3] to the estate of an agreed amount by ACE. [ACE Proposed Findings 73, 74]. Instead of pursuing in good faith this opportunity to commute

[3] In contrast to this, the AFIA agreement does not result in payment of a liquidated sum by ACE, but instead involves recovery from ACE over a number of years as claims are allowed into the estate.

with ACE, the Liquidator elected five days later, at the conclusion of the October 21, 2003, meeting with AFIA cedents and their representatives, to deal exclusively with the AFIA cedents. This decision effectively precluded any further commutation negotiations with ACE, as the Liquidator had agreed as of October 21, 2003, not to use any information obtained from AFIA cedents in order to commute with ACE. [ACE Proposed Finding 82].

The Liquidator's asserted justification for breaking off commutation discussions with ACE was that he could not effectively negotiate a commutation with ACE without more accurate information concerning the valuation of the AFIA cedent claims, which information was in the possession of the AFIA cedents. Special Deputy Liquidator Bengelsdorf testified that obtaining claims information from the AFIA cedents was a primary reason for making a sharing agreement with the AFIA cedents. [Bengelsdorf, Vol 3-A, 197:10-21]. What the Liquidator's representatives overlooked, however, is that AFIA cedent claims information could have readily been obtained by the Liquidator in the ordinary course, with or without the cooperation of the AFIA cedents.

The undisputed evidence is that at least seven of the nine members of the ICC would have filed claims to protect their offset rights against the estate. [BMC Proposed Findings, ¶ 2]. These seven cedents (Equitas, Continental, Unionamerica, Excess, English and American, Bermuda Fire and Marine, and Riverstone) represent the large majority of AFIA cedent claims. Jonathan Rosen testified that Equitas, Excess, and Agrippina alone represented 50% of all AFIA cedent claims. [Rosen, Vol. 1-B, at 165:13-18]. One other member of the ICC (Mentor) had also indicated in writing that it would file a proof of claim,[4] and the ninth member of the ICC (Agrippina) had significant incentive to file a claim for at least administrative costs it claimed

[4] Benjamin Moore Ex. S.

from the Home estate.[5] Thus, all nine members of the ICC could have been expected to file proofs of claim against the estate by the bar date of June 1, 2004.

As the Liquidator's witnesses acknowledged, filing a proof of claim subjects a claimant to the Court's jurisdiction as respects that claim, and also subjects them to the Liquidator's subpoena power under R.S.A. 402-C:25, V,[6] which empowers the Liquidator to:

> Hold hearings, subpoena witnesses and compel their attendance, administer oaths, examine any person under oath and compel any person to subscribe to his testimony after it has been correctly reduced to writing, and in connection therewith require the production of any books, papers, records or other documents which he deems relevant to the inquiry.

Thus, the Liquidator could have readily compelled AFIA cedents to produce claims information once they filed proofs of claim, if necessary. And as for any AFIA cedent that resisted production of information based upon its lack of contacts with the State of New Hampshire, the Joint Provisional Liquidator testified that he would have subpoena power in the UK over any AFIA cedent located there.[7] However, the evidence indicates that the Liquidator never even considered using his statutory powers to obtain claims information from AFIA cedents.[8] Instead, he apparently accepted at face value, without any critical scrutiny, the assertion that AFIA cedents could withhold claims information despite having filed proofs of claim.

In short, the Liquidator's proffered justification for breaking off commutation discussions with ACE does not withstand scrutiny. The Liquidator had every reason to believe that each and every member of the ICC would file a proof of claim, thereby giving the Liquidator access to

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5 Agrippina's proof of claim was admitted as ACE Exhibit MM, and lists an unspecified amount of claimed administrative costs.

6 ACE Proposed Finding 167.

7 Id.

8 Special Deputy Liquidator Bengelsdorf testified that, in his view, the estate had no options for obtaining claims information from AFIA cedents other than making a sharing agreement with them. [Bengelsdorf, Vol. 3-B, at 198:7-15].

claims information, by compulsion if necessary. And yet the Liquidator either overlooked or deliberately ignored this option for obtaining the information he says was needed to negotiate effectively with ACE. Instead of pursuing in good faith an agreement with the ACE Companies that would have raised no issues under the statutory priority rules, he made an agreement with the AFIA cedents that is both unnecessary and violates of those rules. Since a commutation agreement with the ACE Companies has been and continues to be a viable means for recovery of reinsurance on AFIA cedents' claims, the Liquidator has failed to establish that the proposed pay-off to AFIA cedents is essential to recovery of that asset.

III. The Liquidator Has Also Failed To Show That Payment Of An Incentive To AFIA Cedents Was Essential For The Recovery Of Reinsurance From ACE.

A commutation agreement with the ACE Companies is not a certainty, but even in the absence of such an agreement, the Liquidator has not shown that the proposed payment to AFIA cedents was an essential step in recovery of reinsurance from ACE. Absent a commutation with ACE, the recovery of reinsurance would be dependent on the allowance of AFIA cedent claims into the estate. It is undisputed that claims would have been filed by most of the AFIA cedents holding large claims, since they all had significant set-off positions to protect. [Rosen, Vol. 2-A, at 60:16-63:16]. The AFIA cedents needed no additional financial incentive to file claims for set-off purposes, as the Liquidator must acknowledge. The Liquidator has estimated the amount of these set-off claims at different times from as high as $120 million[9] to some amount approximating $58 million.[10] So it is beyond dispute that the estate would be in a position to recover reinsurance from ACE up to the amount of claims pursued by AFIA cedents for set-off, without having to pay any monetary incentive to AFIA cedents.

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[9] Rosen, Vol. 1-B, at 160:19.

[10] Hughes, Vol. 3-A, at 38:1-12.

The Liquidator contends that an incentive payment to AFIA cedents is necessary to cause them to pursue claims over and above their set-off positions. There are a number of fallacies in this position exposed by the evidence introduced at trial.

First, the Liquidator's position is based on the false premise that AFIA cedent set-off positions are known quantities, when in fact these positions are based on offsetting unliquidated claims in both directions that are capable of determination only over a period of years, and perhaps decades. The Liquidator's witnesses testified that AFIA cedents have largely unliquidated claims against the estate under reinsurance contracts, the amount of which will not be determined for years as claims are made against AFIA cedents, and AFIA cedents seek indemnity from the estate. [ACE Proposed Finding 165]. The nature of the risks covered by these contracts are such that it could take numerous years for this process to unfold. [Id.] Conversely, it could also take years for the extent of the estate's claims against the AFIA cedents to be determined. As a result, the offset positions of AFIA cedents cannot be determined in most cases until all claims are liquidated in both directions, at an undetermined point in the future. In the face of this uncertainty, it is reasonable to expect that AFIA cedents would pursue allowance of claims to the maximum extent possible in order to maximize offset potential.

The Liquidator's position that there is significant cost and expense to AFIA cedents in obtaining allowance of claims, which they would not incur absent an economic incentive to do so, is also undermined by the evidence. First, neither the Liquidator nor the AFIA cedents ever even attempted to quantify these alleged costs. [ACE Proposed Findings 90]. Second, many of the AFIA cedents would not even incur any additional expense in pursuing claims, as brokers would be expected to present claims as part of their duty under their pre-paid brokerage contracts. [Id. Nos. 86, 166]. Third, any AFIA cedent reinsurance claim supported by proper

documentation and covered by the relevant Home contract would have to be allowed in the ordinary course, absent some good faith basis for objection by the Liquidator. Indeed, upwards of $10 million in AFIA cedent claims have been allowed to date, without a single objection having been filed. [Id. No. 88]. The Liquidator has failed to introduce any credible evidence that AFIA cedents would incur significant additional expense to obtain allowance of valid reinsurance claims against the estate. If there is no such evidence, the Liquidator cannot show it was essential to pay AFIA cedents a $70+ million incentive, in the form of an administrative expense priority, to do what they could be expected to do in the ordinary course.

Thus, the specter of AFIA cedents failing to pursue claims to the detriment of the estate suffers from the same lack of evidentiary support as the Liquidator's other justifications for the agreement. The Liquidator has not demonstrated that this asserted risk to the estate was any more real that the once-asserted, but now forgotten (by the Liquidator)[11] risk of ring-fencing. The Liquidator has not produced credible evidence that would allow the Court to conclude that the showing required by Section 44 has been made: that the proposed incentive payment to AFIA cedents was essential to recovery of reinsurance from ACE.

IV. The Liquidator Has Not Demonstrated That The Agreement Is Fair To Other Creditors Of The Estate.

As set forth in BMC's Proposed Conclusion of Law, the Liquidator must also demonstrate that the AFIA agreement is fair in the sense that it respects the principle of equality of treatment for creditors in each class, and does not infringe on the rights of senior creditors

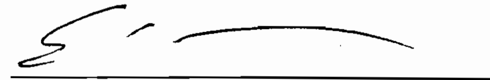
[11] The Court should not forget that the threat of ring-fencing started out as one of the principal justifications for the AFIA agreement, as this bears directly upon the credibility of the Liquidator's position as respects the arguments that remain.

who object. The Court should conclude that the Liquidator has not made the required showing on this point for the reasons set forth in BMC's Proposed Conclusions.

Respectfully submitted,

August 12, 2005

DOWNS RACHLIN MARTIN PLLC

By: 

Andre D. Bouffard (*pro hac vice*)
Eric D. Jones
Attorneys for Benjamin Moore & Co.
199 Main Street
P.O. Box 190
Burlington, VT 05402-0190
(802) 863-2375

CERTIFICATE OF SERVICE

I hereby certify that on this day 12th of August, 2005, a copy of Benjamin Moore & Co.'s Memorandum in Support of Requests for Findings of Fact and Conclusions of Law was served by first class mail, postage prepaid to the following:

Suzanne M. Gorman, Esq.
Senior Assistant Attorney General
Environmental Protection Bureau
Department of Justice
State of New Hampshire
33 Capitol St.
Concord, NH 03301-6397

J. David Leslie, Esq.
Eric A. Smith, Esq.
Rackemann, Sawyer & Brewster
One Financial Center
Boston, MA 02111

Ronald Snow, Esq.
Orr & Reno, PA
One Eagle Square
PO Box 3550
Concord, NH 03302-3550

Gary Lee, Esq.
LOVELLS
900 Third Ave., 16th FL
New York, NY 10022

Paula T. Rogers, Esq.
Case Administrator
Office of the Liquidator Clerk
The Home Insurance Company
286 Commercial Street
Manchester, NH 03101

Burlington, Vermont.

August 12, 2005

DOWNS RACHLIN MARTIN PLLC

By:

Eric D. Jones
199 Main Street
P.O. Box 190
Burlington, VT 05402-0190
Telephone: 802-863-2375
Fax: 802-862-7512

Attorneys for Benjamin Moore & Co.

BTV.448894.1