

**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**

**LIQUIDATOR'S OFFER OF PROOF**

In accordance with the Scheduling Order issued March 7, 2005, Roger A. Sevigny, Commissioner of Insurance of the State of New Hampshire ("Commissioner"), as Liquidator ("Liquidator") of The Home Insurance Company ("Home"), provides the following offer of proof with respect to the Liquidator's motion for approval of the agreement with AFIA Cedents.

Background

1. Home is a New Hampshire domiciled insurance company licensed and subject to regulation by the New Hampshire Insurance Department. 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. [Verified by Peter Bengelsdorf]

2. Home did business in the UK through its unincorporated UK branch ("Home UK Branch"), which was authorized to do business in the UK and regulated by the Financial Services Authority ("FSA") and its predecessor regulators in the UK. [Verified by Peter Bengelsdorf, Gareth Hughes]

3. On March 5, 2003, the Superior Court for Merrimack County, New Hampshire ("New Hampshire Court"), entered an Order of Rehabilitation for Home that appointed the Commissioner as Home's Rehabilitator. On June 13, 2003, the New Hampshire Court entered an

Order of Liquidation for Home. The Order of Liquidation declared that Home was insolvent and appointed the Commissioner as liquidator of Home. Among other things, the Order of Liquidation enjoined, to the full extent of the New Hampshire Court's jurisdiction and principles of comity, the assertion of 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. A copy of the Order of Liquidation is attached as Exhibit 1. [Verified by Peter Bengelsdorf]

4. 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 the Home UK Branch 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 ("Joint Provisional Liquidators") in a provisional liquidation proceeding for Home's UK Branch. A copy of the English Court's order is attached as Exhibit 2. [Verified by Peter Bengelsdorf, Gareth Hughes]

5. On December 19, 2003, the New Hampshire Court entered an Order Establishing Procedures Regarding Claims Filed With The Home Insurance Company In Liquidation ("Claim Procedures Order"). The Claim Procedures Order governs the practice and procedures in proceedings before the Liquidator, any New Hampshire Court-appointed Referee and the New Hampshire Court to provide for the orderly presentation and determination of claims against Home.<sup>1</sup> [Verified by Peter Bengelsdorf]

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<sup>1</sup> The Claims Procedures Order was amended on June 9, 2004. A Restated and Revised Order Establishing Procedures Regarding Claims Filed With The Home Insurance Company In Liquidation entered January 19, 2005.

6. AFIA business and the Assumption Agreement. Home (through the Home UK Branch) wrote insurance and reinsurance business in the UK as a participating member of the American Foreign Insurance Association, an unincorporated association of American insurers (“AFIA”). As a participating member, Home entered insurance contracts with policyholders and cedents in the UK, and Home reinsured that business with AFIA as well as a number of other reinsurers. Among other things, Home entered certain reinsurance treaties (the “AFIA Treaties”) under which a number of insurers (the “AFIA Cedents”) ceded and Home assumed insurance risk through the Home UK Branch. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

7. 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. 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. Under the Assumption Agreement, INA agreed among other things to assume the insurance and reinsurance liabilities of the Home UK Branch 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. A copy of the Assumption Agreement is attached as Exhibit 3. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

8. With the exception of the AFIA Treaties, the Home UK Branch’s AFIA insurance and reinsurance business (consisting of general direct and marine and aviation business) was formally transferred to a CIGNA subsidiary under English law in 1986, as contemplated by the Assumption Agreement. This effected a novation such that the transferred business became a

direct obligation of the CIGNA subsidiary, and Home had no further involvement with that business. The AFIA Treaties, however, were not formally transferred under English law and accordingly remained an obligation of Home, through the Home UK Branch, subject to the Assumption Agreement. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

9. The Assumption Agreement contains an “insolvency clause,” which is included as the second unnumbered paragraph within paragraph 6 of the agreement. See Exhibit 3 at 5. 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. The claims are to be paid on the basis of Home’s liability on the claims, 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 INA to interpose a defense in the determination of claims in the applicable proceeding. Id. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

10. In 1996, INA was part of a corporate restructuring pursuant to which INA’s rights and obligations under the Assumption Agreement with respect to the AFIA Treaties were transferred to INA’s successor, Century Indemnity Company (“Century”). The transfer of these AFIA liabilities to Century was confirmed in a letter from Thomas J. Wamser of ACE to Jonathan Rosen of Home dated February 1, 2001. A copy of that letter is attached as Exhibit 4. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

11. On July 2, 1999, CIGNA sold INA Corporation and its subsidiaries, including Century, to ACE INA Holdings, Inc., a subsidiary of ACE Limited. This transaction is confirmed in Note 21(C) to the Notes to Financial Statements forming part of Century’s 2004 Annual Statement. A copy of Note 21(C) is attached as Exhibit 5 at 14.12. Under the transaction, Century became part of the ACE group of companies (“ACE”). The ACE group of companies

also includes ACE Property and Casualty Insurance Company, Pacific Employers Insurance Company, and ACE American Reinsurance Company. The ACE group of companies also includes ACE-INA Services U.K. Limited (“ACE INA Services”), a company that provided claim administration services and, through certain of its designated personnel, served as the UK representative for the Home UK Branch with respect to the AFIA Treaties pursuant to the Assumption Agreement. A copy of Schedule Y to Century’s 2004 Annual Statement, which reflects the composition of the ACE group of companies, is attached as Exhibit 6 at 105.3, 105.5, 105.7. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

12. Since 1984, claims submitted by the AFIA Cedents under the AFIA Treaties have been handled on Home’s behalf by INA and its successor, Century, and their agents, including ACE INA Services, at INA’s and Century’s own expense pursuant to the Assumption Agreement. The AFIA Cedents submitted claims under the AFIA Treaties directly to ACE INA Services (or its predecessors), acting for INA and then Century, in London. Also since 1984, claims submitted by the AFIA Cedents under the AFIA Treaties have been paid on Home’s behalf as described in paragraph 14 below. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

13. The liabilities under the AFIA Treaties for which ACE is obligated are significant. ACE INA Services prepared financial statements for the Home UK Branch to be filed with the FSA reporting that the expected claims under the AFIA Treaties, and thus Century’s obligations for those treaties under the Assumption Agreement, as of December 31, 2002 (the year end immediately prior to entry of the Order of Liquidation), totaled approximately £143 million (or approximately \$231 million). A copy of pertinent pages from the 2002 Home UK Branch

statement prepared by ACE INA Services is attached as Exhibit 7. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

14. Home was also reinsured with respect to its liabilities under the AFIA Treaties under reinsurance contracts with BAFCO Reinsurance Company of Bermuda Limited (“BAFCO”), a Bermudan company. These reinsurance contracts consisted of an Excess of Loss Reinsurance Agreement signed December 23, 1982, a Second Excess of Loss Reinsurance Agreement also signed December 23, 1982 and a First Supplemental Excess of Loss Reinsurance Agreement signed February 1, 1985 (as amended, the “BAFCO Agreements”). The BAFCO Agreements provide that they are subject to English law and that disputes will be resolved by arbitration in England. They provide coverage to Home for net losses exceeding \$95 million in the aggregate. Copies of the BAFCO Agreements are attached as Exhibit 8. BAFCO’s obligations under the BAFCO Agreements have been assumed by another member of the ACE group of companies, Century Indemnity Reinsurance Company (“CIRC”). While the obligations under the BAFCO Agreements and the Assumption Agreement appear to overlap, historically, the BAFCO Agreements were used to pay the net claims of AFIA Cedents. The net claims represented Home’s gross assumed claims payable, less third party reinsurance. Copies of documents prepared by ACE INA Services illustrating this point are attached as Exhibit 9. Indeed, in describing the security supporting Home’s UK obligations, it was noted in a letter dated October 25, 1985 from the General Manager of AFIA Worldwide Insurance to the UK Department of Trade and Industry that the reinsurance afforded by BAFCO “provide[s] high quality protection for the United Kingdom Treaty Department of Home.” A copy of that letter is attached as Exhibit 10. [Verified by Gareth Hughes, Jonathan Rosen]

### Effects of Home's Insolvency and Liquidation

15. The insolvency of Home and its consequent liquidation had three effects of significance with respect to the claims of AFIA Cedents under the AFIA Treaties and the obligations of Century and/or CIRC:

16. *First*, as a result of Home's liquidation, the AFIA Cedents' claims under the AFIA Treaties must be filed with and determined by the Liquidator, as opposed to Century (through ACE INA Services), subject to review and approval by the New Hampshire Court. Under RSA 402-C:37 and RSA 402-C:57, claims against an insurer in liquidation proceedings must be submitted to the insurer's liquidator through the proof of claim process. The Order of Liquidation enjoins (to the full extent of the New Hampshire Court's jurisdiction and principles of comity) other means of asserting claims against Home. See Exhibit 1. Under RSA 402-C:41 and RSA 402-C:45, the liquidator of the insolvent insurer must investigate and determine claims, issue notices of determination (which are subject to objection by the claimant and review by a referee or the New Hampshire Court) and make recommendations with respect to the allowance of claims (which are subject to approval by the New Hampshire Court). The applicable claims procedures order provides procedures for the determination of claims against Home. [Verified by Peter Bengelsdorf, Jonathan Rosen]

17. *Second*, Century must make payments under the Assumption Agreement and/or CIRC must make payments under the BAFCO Agreements with respect to determined claims under the AFIA Treaties to the Liquidator (or the Joint Provisional Liquidators, as appropriate), not the AFIA Cedents. Home's assets, here reinsurance/indemnity recoverables, are required to be paid or turned over to the Liquidator, who is vested with title to and charged with collecting the insolvent insurer's assets. See RSA 402-C:21, I; RSA 402-C:25, VI. The Order of Liquidation directs that Home's assets be paid to the Liquidator. See Exhibit 1. The insolvency

clause in the Assumption Agreement also provides for payments directly to the liquidator of a seller (such as Home), in the event a seller becomes insolvent, based on claims allowed in the estate and without diminution because of the insolvency. See Exhibit 3 ¶ 6. [Verified by Peter Bengelsdorf, Jonathan Rosen]

18. *Third*, AFIA Cedents' claims will receive a distribution respecting their claims from the Home estate only if assets are sufficient to reach the priority class to which their claims are assigned. No distribution to the AFIA Cedents' priority class is expected. Distributions of assets on claims that have been allowed by the New Hampshire Court under RSA 402-C:45, II, will depend on the assets that are ultimately marshaled by the Liquidator and the total allowed claims in higher and the same priority class under RSA 402-C:44. Subject to any offset entitlement pursuant to RSA 402-C:34, claims of the AFIA Cedents fall in the Class V "residual priority" class. See RSA 402-C:44, V. [Verified by Peter Bengelsdorf]

19. While the ultimate collected assets of the Home estate and the total allowed claims in each class were not then known, during 2003 and early 2004 it was not expected that there would be sufficient assets for Home to make any distribution to creditors below Class II. Thus, the AFIA Cedents were not expected to receive any distribution on their claims from the Home liquidation. This expectation was shared with members of the Informal Creditors' Committee ("ICC"), all of whom are AFIA Cedents, that was created pursuant to the English provisional liquidation proceeding.<sup>2</sup> [Verified by Peter Bengelsdorf]

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<sup>2</sup> The Liquidator continues to expect that the assets of the Home estate will not be sufficient to make any distribution to priority classes below Class II.



20. Under RSA 402-C:34, a claimant is able to use its claims against Home as offsets against claims by the Liquidator against the claimant. A number of the AFIA Cedents are also reinsurers of Home under reinsurance contracts separate from Home's AFIA business. Home's claims against those AFIA Cedents could be offset by the AFIA Cedents' determined claims against Home. Home's claims against AFIA Cedents were expected to constitute a significant amount of money but only a relatively small percentage of the AFIA Cedents' total claims against Home. [Verified by Jonathan Rosen]

#### The Genesis of the Agreement

21. During September 2003, the Liquidator and the Joint Provisional Liquidators were aware that (i) Century's and CIRC's obligations to indemnify Home for its obligations to the AFIA Cedents represented a significant asset of the Home estate, and (ii) the collectibility of this asset depended on the filing and prosecution of claims by AFIA Cedents and their allowance by the New Hampshire Court. The Liquidator and the Joint Provisional Liquidators were concerned that the AFIA Cedents would not pursue their claims against the estate but would seek to negotiate some payment directly from ACE. This concern arose from the conduct and statements of both AFIA Cedents and ACE. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

22. One AFIA Cedent, Unionamerica Insurance Company ("Unionamerica"), had withdrawn its claims against Home. A copy of Unionamerica's letters concerning that withdrawal and expressing Unionamerica's uncertainty over whether it would pursue claims under the AFIA Treaties is attached as Exhibit 11. [Verified by Gareth Hughes]

23. In a meeting on September 17, 2003, between representatives of Unionamerica (Tammy Lewis and Alistair Gunn), ACE INA Services (Barbara Nowak), the Joint Provisional Liquidators (Sarah Ellis of E&Y), and the Liquidator (Mr. Rosen, Chief Operating Officer of Home), Mr. Rosen asked why Unionamerica had withdrawn its claims, and Unionamerica refused to explain beyond saying that it would reserve Unionamerica's rights. A copy of Mr. Rosen's notes of the meeting are attached as Exhibit 12. Ms. Nowak in discussions with Mr. Rosen about Unionamerica's intentions indicated that Unionamerica might seek to ignore Home in the claims submission process and attempt to deal directly with ACE. [Verified by Jonathan Rosen]

24. In several September 2003 discussions with Michael Durkin of ACE INA Services, which had acted as manager of the run-off of the AFIA business prior to Home's liquidation, Mr. Rosen and Gareth Hughes (the lead Joint Provisional Liquidator) expressed concern over potential direct dealings between ACE and AFIA Cedents to circumvent the liquidation but received only noncommittal responses. [Verified by Gareth Hughes, Jonathan Rosen]

25. During one conversation with Mr. Rosen, Mr. Durkin raised the possibility that ACE could deal directly with AFIA Cedents that were members of the Ruddy Pool and suggested that this would benefit the cedents (by giving them a larger recovery than a distribution from the Home estate would) and ACE (which would pay less than 100% of its obligations on Home's liabilities). Mr. Durkin provided Mr. Rosen with an ACE email dated September 12, 2003 that referred to these issues. A copy of the email is attached as Exhibit 13. [Verified by Jonathan Rosen]

26. Mr. Rosen met with Mr. Durkin and Michael Smith of ACE INA Services on September 16, 2003. During that meeting, Mr. Rosen stated that it would be legally inappropriate for ACE to entertain entering side deals with AFIA Cedents and attempt to circumvent Home. Mr. Durkin refused to address ACE's intentions. A copy of Mr. Rosen's notes of that meeting is attached as Exhibit 14. [Verified by Jonathan Rosen]

27. On September 16, 2003, ACE sent a letter to Clifford Chance, counsel for the Joint Provisional Liquidators, alleging that Mr. Rosen had been interfering in the administration of various UK matters affecting ACE's obligations for the AFIA Treaties under the Assumption Agreement. The letter was also sent to Alexander Feldvebel, the Deputy Commissioner of the New Hampshire Insurance Department. A copy of the letter to Clifford Chance and the cover letter to Mr. Feldvebel is attached as Exhibit 15. (Clifford Chance responded in a letter dated September 29, 2003 detailing the reasons why such interference had not occurred.) [Verified by Gareth Hughes, Jonathan Rosen]

28. In light of ACE's September 16, 2003 letter and the discussions noted above, the Liquidator and Joint Provisional Liquidators sent a letter to Century dated September 26, 2003 to express concern that attempts might be made to deal directly between Century and AFIA Cedents; advise that the Liquidator and Joint Provisional Liquidators viewed such efforts as unlawful; and request confirmation that ACE would not participate in such efforts and would notify the Liquidator and Joint Provisional Liquidators if it was aware of any efforts. A copy of the September 26, 2003 letter is attached as Exhibit 16. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

29. Century (and ACE generally) never responded to the September 26, 2003 letter. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

30. During mid-September, 2003, the Special Deputy Liquidator (Peter Bengelsdorf) and the lead Joint Provisional Liquidator (Mr. Hughes), among others, discussed issues concerning recovery of indemnity/reinsurance from Century and CIRC for the Home estate. It was determined to contact ACE and arrange to meet for exploratory discussions about a potential agreement to commute the indemnity obligations of Century under the Assumption Agreement and address other aspects of the situation, including the BAFCO Agreements and the expected assertion by AFIA Cedents of direct rights against ACE. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen] Gernot Warmuth for Agrippina Versicherung Aktiengesellschaft (“Agrippina”),<sup>3</sup> on September 12, 2003, advised Mr. Rosen that he was investigating such direct rights, among other options, and Unionamerica had intimated as much at the September 17, 2003 meeting. [Verified by Jonathan Rosen, Gernot Warmuth]

31. Mr. Rosen contacted Mr. Wamser of ACE and arranged for a meeting on September 30, 2003. [Verified by Jonathan Rosen]

32. On September 30, 2003, a “without prejudice” meeting was attended by Mr. Bengelsdorf and Mr. Rosen for the Liquidator, Mr. Hughes and Ms. Ellis for the Joint Provisional Liquidators, and Mr. Wamser and Howard Denbin for ACE. At the meeting, Mr. Bengelsdorf suggested the possibility of a three-cornered commutation transaction among Home, ACE and the AFIA Cedents, subject to court approval. A copy of the presentation materials used by Mr. Bengelsdorf during the meeting is attached as Exhibit 17. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

33. During the meeting on September 30, 2003, Mr. Denbin and Mr. Wamser of ACE asserted that direct agreements between ACE and AFIA Cedents were permissible under English

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<sup>3</sup> Zurich Versicherung Aktiengesellschaft (Deutschland) is the successor to Agrippina.

law, citing the “NEMGIA” decision (National Employers’ Mutual General Insurance Association Ltd v. AGF Holding (UK) Ltd [1997] 2 BCLC 191) as purported authority for this view. A copy of the NEMGIA decision is attached as Exhibit 18. Mr. Denbin stated his view that ACE had the right to make such direct agreements with AFIA Cedents. They stated that Lovells (UK counsel for ACE) thought there was a strong case for the legality of cut-throughs in the UK, and that Strook & Strook (US counsel for ACE) would provide ACE with an opinion on the issue under US law. A copy of Mr. Bengelsdorf’s notes of the meeting is attached as Exhibit 19. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

34. Despite follow-up discussions between Mr. Bengelsdorf, Mr. Rosen and ACE personnel concerning the suggestion of a potential comprehensive business resolution during October 2003, ACE never provided any substantive response and the discussions concerning such a resolution did not meaningfully progress. [Verified by Peter Bengelsdorf, Jonathan Rosen]

35. As authorized by English law, the ICC was established in the UK provisional liquidation proceeding to consult with the Joint Provisional Liquidators. The ICC consisted of the AFIA Cedents expected to have the largest claims against Home under the AFIA Treaties: Equitas Limited (“Equitas”), Continental Insurance Company of New York (“Continental”), Unionamerica, Excess Insurance Company Ltd. (“Excess”), English & American Insurance Company Ltd. (“English & American”), Bermuda Fire & Marine Insurance Company in Liquidation, Mentor Insurance Company (UK) Ltd., Riverstone Management Limited (as agent, for and on behalf of Sphere Drake), and Agrippina. [Verified by Gareth Hughes]

36. The first meeting of the ICC was held on October 21, 2003. It was attended by representatives of the nine ICC members and of the Joint Provisional Liquidators and the

Liquidator. A copy of the minutes of the first ICC meeting is attached as Exhibit 20. During the meeting, many points were discussed, including the filing of claims in the New Hampshire proceeding; the priority applicable to reinsureds' (cedents') claims; and the availability of setoff. Both Mr. Hughes and Mr. Bengelsdorf said that Home needed detailed information as to the amount of the AFIA Cedents' claims or potential claims to evaluate the amount of AFIA liabilities, and Mr. Bengelsdorf noted that none of the ICC members had yet presented a claim. See Exhibit 20 at H00342, 345. The ICC members asked for a comfort letter stating that any information provided would not be construed as a claim in the estate or used for a commercial resolution with ACE. *Id.* at H00344-45. The ICC members also requested confirmation that direct insurance creditors ranked above reinsurance creditors in the New Hampshire liquidation and in the UK. *Id.* at H00344-45.<sup>4</sup> [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen, Rhydian Williams]

37. During the discussion, at least three ICC members (Mr. Gunn for Unionamerica, Rhydian Williams for Equitas, and Steve Goodlud for English & American) noted that it appeared that AFIA Cedents were unlikely to receive anything from the Home estate. Exhibit 20 at H00344-45. Toward the conclusion of the meeting, Mr. Williams summarized the situation as follows:

- There was a lot of uncertainty (in particular regarding the eventual size of the estate)
- Reinsurers ranked down the priority list and would probably get nothing from the estate (save for offset against Home's claims)
- The ACE reinsurance provided the largest asset in the estate and this asset depended on claims made by creditors.

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<sup>4</sup> The Joint Provisional Liquidators subsequently provided the ICC members with, among other things (1) an analysis of the priority of reinsureds under New Hampshire law from Rackemann, Sawyer & Brewster, (2) advice from leading UK counsel concerning the applicability of the priority of direct insurance creditors over reinsured creditors under a European Union directive and regulations to Home's UK Branch, and (3) as discussed below, a proposal concerning the use of information from the AFIA Cedents.

Mr. Williams questioned what incentive there was for reinsureds to put claims into the estate. Id. at H00345. Mr. Goodlud emphasized that from the perspective of the reinsured there would be a great deal of administrative effort and cost involved with getting a claim set up and agreed, for no real benefit. Id. A discussion concerning the need for a commercial resolution of all issues followed. Id. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen, Rhydian Williams]

38. During the course of the first ICC meeting and other meetings and discussions during the fall of 2003, representatives of several AFIA Cedents, including Mr. Williams for Equitas and Ms. Lewis and Mr. Gunn for Unionamerica, informed representatives of the Liquidator and Mr. Hughes that they would not file or expend resources in pursuing claims in the Home liquidation where they were unlikely to receive a distribution on those claims, except to the extent they would be able to use the claims as offsets in relation to reinsurance claims Home has against them. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen, Rhydian Williams]

39. Mr. Williams remarked on the difficulty Equitas had experienced in getting ACE to agree and pay claims before Home's liquidation and noted that ACE's expected involvement in the claims process likely meant this would continue. [Verified by Gareth Hughes, Jonathan Rosen, Rhydian Williams]

40. Similarly, representatives of several AFIA Cedents, including Richard Leedham for Excess and Continental, Ms. Lewis and Mr. Gunn for Unionamerica, Mr. Williams for Equitas, and Mr. Warmuth for Agrippina, made clear to Mr. Hughes that they would be most unlikely to prosecute proofs of claim in the New Hampshire liquidation proceeding for the simple reason that they would not wish to incur the time and expense of prosecuting those claims

in circumstances where they would not receive a distribution for their claims. [Verified by Gareth Hughes, Rhydian Williams, Gernot Warmuth]

41. Mr. Warmuth for Agrippina asserted to Mr. Rosen, during September of 2003, that Agrippina was in a unique position among AFIA Cedents and was considering not filing a claim in the Home liquidation proceeding, terminating the so-called “Treaty R”, thereby “cutting-out” Home’s reinsurance recoveries or indemnity rights from ACE in relation thereto, and collecting directly any third party reinsurance inuring to the benefit of “Treaty R”, provided that it could make a side deal with ACE to receive consideration for relieving ACE from its reinsurance and or indemnity obligations to Home. [Verified by Jonathan Rosen, Gernot Warmuth]

42. Representatives of certain AFIA Cedents, including Mr. Williams for Equitas, also informed Mr. Rosen that they were considering attempting to “cut through” and deal directly with ACE in an effort to seek payment under the AFIA Treaties by going around Home’s Liquidator. Moreover, Mr. Williams said that Equitas was considering whether it could obtain direct rights against ACE (i.e., Century) under the Assumption Agreement because that agreement had contemplated that INA would assume the obligations under the AFIA Treaties through a novation, and that Home would be bypassed in the process. As described in paragraph 41 above, Mr. Warmuth for Agrippina asserted it was in a unique position and was considering seeking to make a side deal with ACE that involved termination of “Treaty R”, thereby “cutting out” Home and facilitating Agrippina’s direct collection of third party reinsurance for “Treaty R.” [Verified by Jonathan Rosen, Rhydian Williams, Gernot Warmuth]

43. Similarly, representatives of certain AFIA Cedents (Mr. Williams of Equitas and Mr. Leedham for Excess) made clear in discussions with Mr. Hughes that they had been considering what methods may be available to enable them to “cut through” to the reinsurances



provided to Home by ACE or otherwise negotiate a direct agreement with ACE. In particular, they had suggested that they might try to negotiate direct agreements with ACE under which ACE would make payments to AFIA Cedents, by-passing the Home estate in the process.

[Verified by Gareth Hughes, Rhydian Williams, Gernot Warmuth]

44. Based on these discussions, the Special Deputy Liquidator (Mr. Bengelsdorf) and the lead Joint Provisional Liquidator (Mr. Hughes) believed that AFIA Cedents would neither file nor expend resources in pursuing claims in the Home liquidation, except to the extent they would be able to use the claims as offsets against claims that Home has against them. It was self-evident that sensible businesses would not devote resources in time and money to pursuing claims that would not give them any benefit. It was also clear that the absence of claims, while providing ACE with a large windfall, would deprive Home of large recoveries from ACE under the Assumption Agreement and/or BAFCO Agreements described in paragraph 13, and that the AFIA Cedents were aware of this fact. [Verified by Peter Bengelsdorf, Gareth Hughes]

45. Based on these discussions, Unionamerica's withdrawal of claims, ACE's non-response to the September 26, 2003 letter, and ACE's assertions that cut-throughs were legal under English law and were being considered by ACE, the Special Deputy Liquidator and lead Joint Provisional Liquidator also believed that (i) certain AFIA Cedents were considering attempting to "cut through" and deal directly with ACE in an effort to obtain payment on their claims under the AFIA Treaties by going around Home's Liquidator, and (ii) ACE would be receptive to such efforts. This would provide the AFIA Cedents with an alternative means of recovery by obtaining payment on claims under the AFIA Treaties other than through the filing of claims in the liquidation and allow ACE to pay less than 100% on the claims. It would circumvent Home by avoiding the filing and prosecution of claims in the liquidation of Home

and thus deprive the Liquidator of the ability to collect under the Assumption Agreement and/or the BAFCO Agreements for the AFIA Cedents' claims. The Special Deputy Liquidator and lead Joint Provisional Liquidator believed that assertions of direct rights of access to indemnity or reinsurance were particularly credible in the circumstances of the Home liquidation. Century (and its predecessors, including INA), acting through ACE INA Services, and the AFIA Cedents had dealt directly with each other for almost twenty years before the liquidation, and the Assumption Agreement had contemplated that INA would use its best efforts to assume the AFIA Treaties by novation. The potential of "cut-through" agreements thus presented a serious threat that could involve litigation over the complex history of the Assumption Agreement and the course of dealings with respect to AFIA Cedents' past claims. [Verified by Peter Bengelsdorf, Gareth Hughes]

46. In these circumstances, it was considered highly risky and financially disadvantageous for Home to merely wait and see what claims were filed and prosecuted in the Home liquidation by AFIA Cedents, given the statements and positions asserted by AFIA Cedents and ACE. The Special Deputy Liquidator and Mr. Rosen believed that significant AFIA Cedents would only file and prosecute claims that could be used by the AFIA Cedent involved to offset claims by the Liquidator against the cedent, thereby depriving the Liquidator of the ability to pursue a substantial portion of an estate asset as the potential offset rights were estimated to be a significant amount of money but only a relatively small percentage of the AFIA Cedents' claims. [Verified by Peter Bengelsdorf, Jonathan Rosen]

47. The Special Deputy Liquidator also considered continuing efforts to negotiate an agreement with ACE to commute the indemnity obligations of Century under the Assumption Agreement (and the obligations of CIRC under the BAFCO Agreements). However, the

discussions with ACE over the concept of such a potential comprehensive business resolution did not meaningfully progress and ACE indicated that it could legally negotiate directly with the AFIA Cedents. Moreover, it was in ACE's interest to prolong the discussions without reaching an agreement. If the discussions lasted until after the June 13, 2004 claim filing deadline without the AFIA Cedents' filing claims, then (other than with respect to offsets asserted by AFIA Cedents) the value of the Liquidator's claims under the Assumption Agreement and/or the BAFCO Agreements would likely be nothing. The estate would not realize on these indemnity/reinsurance assets, and ACE would have reaped a great windfall. To effectively negotiate, the Liquidator needed to have credible information concerning the value of the AFIA Cedents' claims. However, the AFIA Cedents had resisted providing information and, as noted above, were not going to file and prosecute claims except potentially for offset purposes.

[Verified by Peter Bengelsdorf, Jonathan Rosen]

48. The Special Deputy Liquidator accordingly concluded that some form of an agreement with AFIA Cedents was necessary so that they would file and prosecute claims and enable the Liquidator to collect the asset of the estate represented by the Assumption Agreement (and/or BAFCO Agreements) and reported his conclusion to the Liquidator. [Verified by Peter Bengelsdorf, Jonathan Rosen]

#### Negotiation of the Agreement

49. The negotiation of the Agreement was a three month process beginning after the first ICC meeting on October 21, 2003 and running through the circulation of the final Agreement for signature on January 23, 2004. It involved representatives and/or counsel for the nine members of the ICC, the Joint Provisional Liquidators, and the Liquidator. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

50. After the ICC meeting, the Joint Provisional Liquidators, in consultation with the Liquidator, prepared a draft proposal for the members of the ICC to consider. A draft was provided to Mr. Williams of Equitas on November 10, 2003. (Mr. Williams was a leading member of the ICC.) A copy of the draft is attached as Exhibit 21. Among other things, the draft proposed that AFIA Cedents (i) provide information concerning paid losses, case reserves and IBNR to Home by November 30, 2003 for specified purposes, including attempting to reach a commercial resolution of the value of ACE's obligations, and (ii) agree to a scheme of arrangement under English law under which the AFIA Cedents would receive a portion of net proceeds (after certain deductions) received from ACE with respect to claims under the AFIA Treaties. The portion of the net proceeds proposed was 25%. Under the proposal, AFIA Cedents would also be precluded from pursuing side arrangements directly with ACE. [Verified by Peter Bengelsdorf, Gareth Hughes, Rhydian Williams]

51. Mr. Williams met with Mr. Hughes and David Steinberg, counsel for the Joint Provisional Liquidators, on November 11, 2003, and among other comments said that the 25% was far too low and would not obtain the support of the necessary percentage of the AFIA Cedents. (Under English law, a scheme of arrangement is subject to approval of a majority in number and 75% in value of creditors.) He also said that the AFIA Cedents would be unwilling to provide information concerning losses, cases reserves, and IBNR to the Liquidator (and thus lose control over the information which might be used by the Liquidator to reach an agreement with ACE) until after the agreement was made binding on the Liquidator by an order of the New Hampshire Court. Mr. Williams subsequently sent an email to Mr. Hughes on November 12, 2003, asking why – assuming that 25% was justifiable and could obtain the support of creditors –

Home should not bear 75% of the costs. A copy of the email is attached as Exhibit 22. [Verified by Gareth Hughes, Rhydian Williams]

52. Mr. Hughes provided Mr. Williams with a revised proposal on November 18, 2003, and with illustrative schedules on November 19, 2003. The draft proposal provided that the portion of net recoveries to be paid to AFIA Cedents would increase as recoveries increased: 25% for proceeds under \$150 million, 35% for proceeds from \$150 million up to \$250 million, 45% for proceeds from \$250 million up to \$350 million, and 50% for proceeds over \$350 million. (This was referred to as a “lock step.”) It also provided for the AFIA Cedents to provide claim information only after the New Hampshire Court had issued an order approving the agreement. A copy of the proposal is attached as Exhibit 23. A copy of the illustrative schedules is attached as Exhibit 24. [Verified by Gareth Hughes, Rhydian Williams]

53. After further discussions with Mr. Williams, a draft proposal was circulated to the members of the ICC on November 21, 2003. A copy of the draft is attached as Exhibit 25. The draft was substantially the same as the second draft provided to Mr. Williams. It included the “lock step” proposal that the portion of net recoveries to be paid to AFIA Cedents would increase as recoveries increased. [Verified by Gareth Hughes]

54. Members of the ICC met with Mr. Hughes and others on November 28, 2003 to discuss the proposal and illustrations as to how it would work. A copy of the presentation materials is attached as Exhibit 26. The ICC members raised numerous questions, and Mr. Hughes proposed to add language to address the situation where ACE commuted with the Liquidator based on AFIA Cedents’ claims submissions. [Verified by Gareth Hughes]

55. During discussions after the meeting, Mr. Williams advised Mr. Hughes that the “lock step” approach was not viewed by ICC members as fair, and that the ICC would more

likely accept a 50/50 sharing of net proceeds or better. A copy of Mr. Williams' December 9, 2003 email commenting on Home's illustrations is attached as Exhibit 27. [Verified by Gareth Hughes, Rhydian Williams]

56. On December 12, 2003, Mr. Leedham, counsel for Continental and Excess, circulated a marked-up draft of the proposal letter on behalf of the ICC generally, although individual Cedents still might raise issues. A copy of the draft is attached as Exhibit 28. Among other things, the mark-up used a flat 50% portion in defining net recoveries, included a 150% "multiplier" applicable to amounts received from any commutation with ACE, required the prior consent of 75% by value of the ICC before such a commutation, extended the period for providing claim information, and provided for the return of that information if the scheme was not approved. [Verified by Gareth Hughes]

57. On December 15, 2003, Philip Hertz, counsel to the Joint Provisional Liquidators, responded with a revised draft. Among other things, the draft left the percentage portion blank, removed the commutation multiplier, changed the consent requirement into a consultation provision, and deleted the information return provision. A copy of the draft is attached as Exhibit 29. To avoid the possibility of further substantive changes to a deal after agreement on a percentage, the Special Deputy Liquidator and Joint Provisional Liquidator had determined not to respond on the percentage until the letter was otherwise final. [Verified by Peter Bengelsdorf, Gareth Hughes]

58. In discussions over the next several days, Mr. Leedham advised that seven of nine ICC members would agree to the letter if the percentage were 50%, but that Unionamerica and Agrippina were not yet in agreement. [Verified by Gareth Hughes]

59. In a discussion with Mr. Rosen, Mr. Warmuth said that Agrippina had not yet completed its analysis of the options it was considering and would abstain from the ICC vote on the letter. [Verified by Jonathan Rosen, Gernot Warmuth]

60. On December 31, 2003, Unionamerica advised that it was not prepared to sign the proposal as drafted, and it provided a draft of a letter stating that it generally would be willing to support a scheme with certain features. A copy of the draft is attached as Exhibit 30. [Verified by Gareth Hughes]

61. On January 7, 2004, Unionamerica provided a marked up revision of the Joint Provisional Liquidators' proposal letter raising issues concerning terms of the scheme, costs and claims procedures. A copy of the draft is attached as Exhibit 31. [Verified by Gareth Hughes]

62. On January 15, 2004, after discussions involving representatives of Unionamerica (among others), Mr. Steinberg, counsel for the Joint Provisional Liquidators, provided Mr. Williams with a draft reflecting changes discussed with Unionamerica for circulation to the ICC. A copy of the draft is attached as Exhibit 32. [Verified by Gareth Hughes]

63. During this period, Mr. Leedham raised questions concerning a tolling agreement that had been discussed at the October ICC meeting, and a letter concerning New Hampshire claim procedures was also requested. Mr. Hertz provided a draft tolling agreement to Mr. Leedham, and it was agreed that a letter outlining claim procedures would be provided. [Verified by Gareth Hughes]

64. On January 23, 2004, Unionamerica advised Ms. Ellis that it would sign the proposal letter. [Verified by Peter Bengelsdorf, Gareth Hughes]

65. On January 23, 2004, Mr. Hughes sent packages to the ICC members consisting of (1) the agreement letter dated January 22, 2004 signed by the lead Joint Provisional

Liquidator, (2) a letter dated January 20, 2004 from the New Hampshire Attorney General's Office outlining expected claim procedures, and (3) the tolling agreement signed by the lead Joint Provisional Liquidator and the Liquidator. Copies of the claims procedures letter and the tolling agreement are attached Exhibits 33 and 34. [Verified by Gareth Hughes]

66. All of the ICC members (except Agrippina, which abstained) returned signed letter agreements (collectively, the "Agreement") on or before February 2, 2004. The lead Joint Provisional Liquidator and Special Deputy Liquidator then determined that a sufficient number of AFIA Cedents had agreed to the proposal. (This was formally acknowledged to the ICC members by letter dated February 23, 2004.) A copy of the Agreement (the letter and signature pages) is attached as Exhibit 35.<sup>5</sup> [Verified by Peter Bengelsdorf, Gareth Hughes]

67. The Liquidator served a motion requesting that the New Hampshire Court approve the Agreement on February 11, 2004. [Verified by Peter Bengelsdorf, Jonathan Rosen]

#### The Agreement

68. The Agreement provides for a compromise to be implemented by a "scheme of arrangement" between Home and all AFIA Cedents under § 425 of the English Companies Act 1985 (the "Scheme"), the principal elements of which are specified in the Agreement (Exhibit 35). [Verified by Peter Bengelsdorf, Gareth Hughes]

69. Under the Scheme, a portion of the net proceeds received from ACE (or any reinsurer of Home's AFIA business other than an ACE company) with respect to the AFIA Cedents' claims will be allocated to the Scheme for distribution to the AFIA Cedents, with the remainder to vest with the Liquidator. Agreement § 1.9. The amount to be allocated to the Scheme for the AFIA Cedents is determined by taking the amounts actually received from ACE

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<sup>5</sup> Agrippina later agreed to the Agreement.



with respect to the AFIA Treaties (i.e., the amounts due from Century and/or CIRC less the amounts that Century and/or CIRC successfully withholds as offsets on account of ACE's claims against Home) and deducting:

- (i) the costs of the UK provisional liquidation;
- (ii) collection costs;
- (iii) costs of obtaining approvals from the New Hampshire and English Courts;
- (iv) amounts received by Home on account of Home AFIA liabilities which will be settled with the AFIA Cedent by way of offset (i.e., amounts for which an AFIA Cedent that also has obligations to Home as a reinsurer will receive a credit against its obligations to Home); and
- (v) amounts received by Home on account of any costs orders entered against it in disputed claims proceedings (which otherwise will not be paid by Home).

Agreement § 1.3 (definition of "Proceeds"). Fifty percent of these net "Proceeds" (plus the previously deducted amounts received on costs orders) will be paid to AFIA Cedents as "Net Recoveries," and the remaining 50% will be retained by Home. Agreement § 1.2. [Verified by Peter Bengelsdorf, Gareth Hughes]

70. Because of the deductions, the actual portion of the amounts received from ACE that will be allocated to the AFIA Cedents under the Agreement will be less than 50%. The working of the allocation formula based on certain assumptions is illustrated on Exhibit 36. Exhibit 36 shows the allocation based on the \$231 million value of the AFIA Cedents' claims estimated by ACE INA Services as of December 31, 2002. Under those assumptions, the formula would provide the Home estate with approximately two-thirds of the amounts received from Century. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

71. Under the Agreement, the Net Recoveries are to be paid *pari passu* to all AFIA Cedents according to the value of their claims against Home under the AFIA Treaties as determined in the New Hampshire liquidation (except that amounts from any cost orders will be

paid to the cedent involved). Agreement § 1.9.1. [Verified by Peter Bengelsdorf, Gareth Hughes]

72. The Agreement provides that the compromise reflected in the Agreement is subject to the approval of the New Hampshire Court. Agreement § 1.1.2. It is also subject to the approvals required for a scheme of arrangement under English law. Under § 425 of the Companies Act, the Scheme is subject to the approval of (a) a majority in number and (b) 75% in value of the AFIA Cedents, and then sanctioned by the English Court. A copy of § 425 of the English Companies Act is attached as Exhibit 37. Once the Scheme is approved by the creditors and sanctioned by the English Court and an office copy of the English Court's order sanctioning the Scheme is filed with the English Registrar of Companies, it will be binding on all AFIA Creditors as a matter of English law. [Verified by Gareth Hughes]

73. To confirm that the Liquidator will receive Home's UK assets as envisaged in the Agreement, the Scheme is also conditioned upon an order by the English Court approving the remission of Home's assets in England and Wales (other than those becoming subject to the Scheme) to the Liquidator to be administered as part of the New Hampshire proceeding (the "Global Liquidation Order"), and the approval or non-objection of the UK insurance regulator, the FSA, to the Scheme and the Global Liquidation Order. Agreement §§ 1.1.2, 1.1.3. [Verified by Peter Bengelsdorf, Gareth Hughes]

74. In light of the multi-jurisdictional approval process and the compromise of disputes reflected in the Agreement, the Agreement provides for a Standstill Period during which signatory AFIA Cedents will not seek to agree on "cut-through" agreements with ACE. This

period ran until the earlier of the date on which a required approval is not obtained or June 1, 2004. Agreement §§ 1.6, 1.7.<sup>6</sup> [Verified by Peter Bengelsdorf, Gareth Hughes]

The Necessity, Fairness and Reasonableness of the Agreement

75. The Special Deputy Liquidator and lead Joint Provisional Liquidator believe that the Agreement is necessary, fair and reasonable because it allows the Liquidator to collect a significant asset of the estate, which would otherwise be uncollectible, for the benefit of Home's policyholders and other creditors. [Verified by Peter Bengelsdorf, Gareth Hughes]

76. The insolvency of Home and its consequent liquidation meant that the AFIA Cedents' claims under the AFIA Treaties had to be filed with and determined by the Liquidator instead of being determined by Century (through ACE-INA). Further, Century was obligated to make payments under the Assumption Agreement (and/or CIRC was obligated under the BAFCO Agreements) with respect to claims under the AFIA Treaties to the Liquidator, not the AFIA Cedents. The Assumption Agreement (and/or the BAFCO Agreements) was thus a significant asset of the Home estate. In a filing with the FSA, ACE-INA estimated the value of the AFIA Cedents' claims under the AFIA Treaties as of December 31, 2002 at approximately £143 million (approximately \$231 million), which also represented the estimated value of ACE's obligations to Home. [Verified by Peter Bengelsdorf]

77. However, the Liquidator's ability to collect under the Assumption Agreement (and/or the BAFCO Agreements) depended upon the AFIA Cedents filing and proving their claims in Home's liquidation. Without such allowed claims, the Liquidator would not be able to recover from Century (and/or CIRC), and Century (and/or CIRC) would obtain a windfall because it would not pay amounts that it would have paid absent Home's liquidation. As

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<sup>6</sup> The Standstill Period has been extended to September 30, 2005.

described above, the AFIA Cedents had no reason to file and prosecute claims in Home's liquidation (other than for offset purposes) because, as Class V claimants, it was unlikely they would receive any payment on their claims. [Verified by Peter Bengelsdorf]

78. When the Liquidator and Joint Provisional Liquidators sought to gather additional information concerning the amount of claims from the AFIA Cedents to better understand the asset, the AFIA Cedents resisted providing it. As described above, certain AFIA Cedents made two points. First, they stated that they would not file or expend resources in pursuing claims in the Home liquidation, where they were unlikely to receive a distribution on those claims, except to the extent they would be able to use the claims as offsets against claims by Home. Second, they said they were considering attempting to "cut through" and deal directly with ACE in an effort to seek payment under the AFIA Treaties by going around Home's Liquidator. The Liquidator's concern that this might be happening was supported by Unionamerica's and ACE's actions and statements made by other AFIA Cedents. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

79. The Liquidator thus faced two significant problems in collecting Century's (and/or CIRC's) obligations to Home under the Assumption Agreement (and/or the BAFCO Agreements): *First*, unless the AFIA Cedents filed and prosecuted claims, Century's obligations under the Assumption Agreement (and/or CIRC's obligations under the BAFCO Agreements) would have no value. The AFIA Cedents had credibly asserted the self-evident position that they would not file and prosecute claims without any incentive to do so, and in the circumstances of the Home estate they had no reason to file and prosecute claims except to offset the Liquidator's claims against them which were expected to be a relatively small percentage of their claims. *Second*, the AFIA Cedents and Century (or another ACE company) could enter "cut-through"

agreements under which the AFIA Cedent agreed not to file claims with the Liquidator in exchange for a payment directly from Century or another ACE company. AFIA Cedents had credibly asserted that they were considering this; one large AFIA Cedent (Unionamerica) had withdrawn its claims and refused explanation; Century had asserted such arrangements were legal and had not responded to a request for confirmation that it would not enter such agreements; and it would be difficult for the Liquidator to learn of such agreements. Further, the history of direct dealing over claims between ACE INA Services (an affiliate of Century) and AFIA Cedents meant that the possible parties to such agreements were potentially in contact and could argue that strict contractual privity requirements did not apply. While such side arrangements – if discovered by the Liquidator – would be subject to legal challenge, litigation would be costly and uncertain and might not be fully effective in preserving access to recoveries to which Home would otherwise be entitled. [Verified by Peter Bengelsdorf, Jonathan Rosen]

80. The Agreement was necessary because, if the Liquidator had not addressed these issues by agreement, then the estate would not be able to collect an asset of significant value: the obligations of Century under the Assumption Agreement (and/or CIRC under the BAFCO Agreements) for AFIA Cedents' claims in excess of amounts they could offset. [Verified by Peter Bengelsdorf]

81. The Agreement resolves this issue in a fair and reasonable way. It provides for a “scheme of arrangement” between Home and all AFIA Cedents under § 425 of the English Companies Act 1985, the principal elements of which are specified in the Agreement. The Agreement provides that a portion of the net proceeds received from ACE (or any reinsurer of Home's AFIA business other than an ACE company) with respect to the AFIA Cedents' claims will be allocated to the Scheme for distribution to the AFIA Cedents, with the remainder to vest

with the Liquidator. Agreement § 1.9. The amount to be allocated to the Scheme for distribution to AFIA Cedents is determined by taking the amounts actually received from ACE with respect to the AFIA Treaties (i.e., the amounts due from Century (and/or CIRC) less the amounts that Century (and/or CIRC) successfully withholds as offsets on account of the ACE Companies' claims against Home) and deducting certain amounts, including (i) the costs of collecting the proceeds; (ii) the costs of obtaining approvals from the New Hampshire and English Courts; and (iii) amounts received by Home on account of Home AFIA liabilities settled with the AFIA Cedents by way of offset. See Agreement § 1.3 (definition of "Proceeds"). Fifty percent of these "Proceeds" will be paid to AFIA Cedents as "Net Recoveries," and the remaining 50% will be retained by Home. Agreement § 1.2. [Verified by Peter Bengelsdorf, Gareth Hughes]

82. These contingent payments reasonably serve to provide the AFIA Cedents with reason to file and prosecute claims that they believe are valid but that they otherwise would not pursue. The Agreement will thus permit the Liquidator to collect indemnity for these claims, to the extent they are allowed, from Century under the Assumption Agreement (and/or CIRC under the BAFCO Agreements). The payments are targeted to serve the purposes of the Agreement. In particular, if the Agreement does not result in recoveries in excess of (a) amounts resulting from AFIA Cedents' that will be the subject of offset and (b) the costs of the Agreement and reinsurance or indemnity collection, there will be no payments to AFIA Cedents. [Verified by Peter Bengelsdorf]

83. Contingent payments based on "Proceeds" reflects the Liquidator's purpose in entering the Agreement of making possible increased collection under the Assumption Agreement (and/or the BAFCO Agreements). This mode of payment from recoveries after certain deductions has three desirable features: *First*, the Agreement's formula provides the

AFIA Cedents with reason to prosecute claims, but only if the cedent involved believes the claim to be valid. The mere filing of claims does not assist the Liquidator in collecting assets. Only allowed claims will support claims for recovery under the Assumption Agreement and/or the BAFCO Agreements. Prosecuting claims takes time and resources, and the formula's use of proceeds means that the AFIA Cedents will prosecute their claims. But it also means that the AFIA Cedents will only file and pursue claims they reasonably believe to be valid, because the time and expense incurred in pursuing a claim will otherwise be lost. The Special Deputy Liquidator had advised ICC members that ACE was expected to be involved in the determination of claims.<sup>7</sup> *Second*, the Agreement's formula makes the payments contingent upon success in collecting under the Assumption Agreement and/or BAFCO Agreements. Proceeds are defined as actual recoveries from ACE (less certain deductions). If the purpose of the Agreement to enable the Liquidator to collect assets is not achieved (because recoveries from ACE or its guarantor (CIGNA) are not forthcoming), then no payments will be made. *Third*, the Agreement's formula provides that amounts that the Liquidator could expect to receive without the Agreement do not give rise to payments and that costs incurred because of the Agreement are paid for out of recoveries before payment need be made. The deduction for AFIA Cedents' claims to be settled by way of offset (Agreement § 1.3.4) means that claims that likely would have been filed and prosecuted without the Agreement do not give rise to payment. The deductions of the costs of collection and the costs of the approvals from the New Hampshire and English Courts (Agreement §§ 1.3.2 and 1.3.3) provide for the Agreement to cover costs before payments need be made. [Verified by Peter Bengelsdorf]

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<sup>7</sup> This has now been formalized through the claims protocol with Century approved by the New Hampshire Court on November 12, 2004.

84. Payment of a flat amount for the filing of claims would not serve the Agreement's purposes. It would not provide the AFIA Cedents with reason to prosecute claims or to pursue only claims that are believed to be valid. It would be divorced from the actual collection of assets for the estate. It would not compensate cedents commensurately with the value brought into the estate. It would not account for the claims that would likely be filed in any event. And it would not provide for the Agreement to cover its costs before payment would need to be made. Also, given the uncertainty over the value of the AFIA Cedents' claims (which will only become certain through claim determinations), any fixed payment would not correlate with assets collected and would be extremely difficult to support or negotiate. [Verified by Peter Bengelsdorf]

85. As described above, the 50% allocation of Proceeds is the result of negotiations involving numerous parties. The Joint Provisional Liquidators and the Liquidator initially proposed a lower percentage (25%), but it was necessary to move to 50% to persuade the signatory AFIA Cedents to agree. The figure is a reasonable negotiated result. The AFIA Cedents had significant leverage because (i) they had no arguable obligation to file and prosecute claims, and (ii) it was necessary to obtain agreement of almost all the members of the ICC to have a sufficient portion of the AFIA Cedents to make approval of a scheme likely under English law, which requires a majority in number and 75% in value of creditors to approve a scheme of arrangement. [Verified by Peter Bengelsdorf, Gareth Hughes, Jonathan Rosen]

86. In fact, Mr. Warmuth advised Mr. Rosen that Agrippina continued to believe that the benefits available from a termination of "Treaty R" made it a very "close call" whether to accept a 50% share of Proceeds and, ultimately, it only reluctantly signed the Agreement after it



had been submitted to the New Hampshire Court for approval. [Verified by Jonathan Rosen, Gernot Warmuth]

87. The policyholders and other creditors of Home will benefit because the assets of the Home estate, and thus the distributions from the estate, will be increased. [Verified by Peter Bengelsdorf]

88. The exact amount of benefit involved cannot be determined because it depends on future events, including the filing, prosecution and allowance of AFIA Cedents' claims. However, the ACE-INA filing with the FSA for the Home UK Branch as of December 31, 2002 valued the AFIA Cedents' claims at approximately \$231 million, and Home's claims against AFIA Cedents were roughly estimated at approximately \$58 million. The Agreement provides reason for AFIA Cedents to file and prosecute claims in excess of that amount. [Verified by Peter Bengelsdorf, Jonathan Rosen]

89. Under the Agreement, the policyholders and other creditors of Home will benefit because the estate will receive 50% of the net proceeds recovered from ACE (Century and/or CIRC). The Home estate (and thus the policyholders and other creditors) will also benefit through two of the deductions specified in §§ 1.3.1-1.3.5 of the Agreement which provide that several specific items will be retained by the Liquidator from reinsurance and/or indemnity amounts received:

- The costs of collecting from Century and/or CIRC (some such costs would have been born by the estate without the Agreement; under the Agreement they will be paid for out of the increased amounts received from Century and/or CIRC)
- The costs of the entire UK provisional liquidation and costs of seeking approvals from New Hampshire and English Courts (without the Agreement, the costs of the UK provisional liquidation would have been born by the estate; under the Agreement they will be paid for out of the increased amounts received from Century and/or CIRC)

The Liquidator will also retain the amount of AFIA Cedents' claims settled between the cedent and Home by way of offset against Home's claims against the cedent, although the Liquidator likely would have received this amount in any event as AFIA Cedents would presumably have filed and prosecuted such claims to preserve offset rights. [Verified by Peter Bengelsdorf]

90. The working of the Agreement is illustrated on Exhibit 36. That exhibit shows that, based on certain assumptions set forth on the exhibit (including that the AFIA Cedents' claims are ultimately allowed in the amount estimated by ACE-INA as of December 31, 2002), the Home estate would receive approximately \$145.5 million (approximately two-thirds) of the expected proceeds from Century and/or CIRC. After deducting the amounts that the Liquidator would likely receive without the Agreement, the benefit to the estate, and thus to Home's policyholders and other creditors, from the Agreement is approximately \$87.5 million. (Of course the amounts to be received by Home under the Agreement are determined under the formula set forth in the Agreement, so that the amounts will depend on the actual numbers for the various elements in the formula. Those numbers will depend on future events.) [Verified by Peter Bengelsdorf]

91. The Agreement also avoids potential litigation over "cut through" agreements, i.e., litigation over attempts by AFIA Cedents and members of the ACE group of companies to circumvent the liquidation. The Agreement provides that during the "Standstill Period" the signatory AFIA Cedents will not seek to enter any agreement or arrangement with any member of ACE or any third party reinsurer under which the AFIA Cedent would receive payment in respect of the AFIA Treaties. Agreement § 1.5.1. The Agreement thus prevents the principal AFIA Cedents from entering "cut-through" or other agreements to obtain payment directly from ACE or a third party reinsurer and by-passing the Home estate. [Verified by Peter Bengelsdorf]

92. If such agreements were entered, to the extent the Liquidator was able to learn of them, the Liquidator would need to file suits to set them aside. Such proceedings could be expected to involve complex factual and legal issues that would involve considerable time and cost. In the absence of the Agreement, the Liquidator would have had to bring actions against the ACE group member, the third party reinsurer and/or the AFIA Cedents involved in such an agreement to prevent the agreement or to set the agreement aside. The jurisdictions in which such actions would be brought would depend upon the identities of the ACE company or third party reinsurer and the AFIA Cedent involved and the jurisdictions where those entities are subject to personal jurisdiction. [Verified by Peter Bengelsdorf]

93. The Agreement also facilitates remission of assets to the domiciliary New Hampshire estate. It provides that the New Hampshire Court's approval order and the scheme of arrangement are to be conditioned on entry of an order by the High Court of Justice (the Global Liquidation Order) approving the remission of the Home's assets situated in England and Wales (other than the Net Recoveries) to the Liquidator for administration and distribution as part of the New Hampshire liquidation. Agreement §§ 1.1.2(2), 1.1.3. [Verified by Peter Bengelsdorf]

94. The fairness and reasonableness of the Agreement is further supported by the "non-objection" of the UK insurance regulator, the FSA, as set forth in its letter of March 26, 2004. A copy of the letter is attached as Exhibit 38. [Verified by Gareth Hughes]

95. Further, the National Conference of Insurance Guaranty Funds, the organization of the insurance guaranty funds that are paying claims under Home insurance policies and collectively will be significant Class II creditors of the estate, authorized the Liquidator to advise the Court of its "non-objection." [Verified by Peter Bengelsdorf]

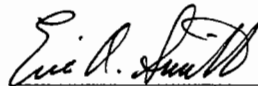
Respectfully submitted,

ROGER A. SEVIGNY, INSURANCE  
COMMISSIONER OF THE STATE OF NEW  
HAMPSHIRE, AS LIQUIDATOR OF THE HOME  
INSURANCE COMPANY

By his attorneys,

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April 28, 2005

**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**

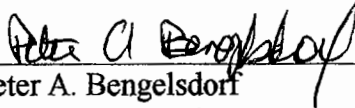
**VERIFICATION OF PETER A. BENGELSDORF**

I, Peter A. Bengelsdorf, hereby depose and say:

I was appointed as Special Deputy Liquidator of The Home Insurance Company by the Commissioner of Insurance for the State of New Hampshire, as Liquidator ("Liquidator") of Home. I submit this Verification in support of the Offer of Proof (the "Offer of Proof") to be submitted in the above-captioned matter by the Liquidator.

I am acquainted with and hereby verify the accuracy of the facts and information set forth in paragraphs 1-13, 16-19, 21, 28-30, 32-34, 36-38, 44-50, 57, 64, 66-71, 73-85, 87-93 and 95 of the Offer of Proof. Such facts and information are either within my own knowledge, gained through my involvement with this matter, in which case I confirm that they are true, or are based on information provided to me by others, in which case they are true to the best of my knowledge, information and belief.

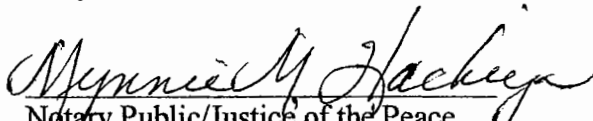
Signed under the penalties of perjury this 26<sup>TH</sup> day of April, 2005.

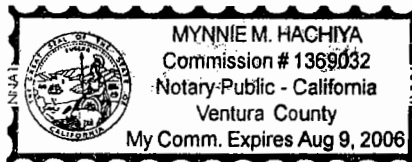


Peter A. Bengelsdorf  
Special Deputy Liquidator of The Home Insurance  
Company

STATE OF CALIFORNIA  
COUNTY OF VENTURA

Subscribed and sworn to, before me, this 26 day of April, 2005

  
Notary Public/Justice of the Peace



# IMISON & CO

NOTARIES

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Ella Imison



TO ALL TO WHOM THESE PRESENTS SHALL COME, I  
ELLA ELIZABETH IMISON of the City of London NOTARY  
PUBLIC by royal authority duly admitted and sworn DO HEREBY  
CERTIFY that on the date hereof before me personally came and  
appeared GARETH HOWARD HUGHES the deponent named and  
described in the verification hereunto annexed WHO in my  
presence by solemn oath by him taken in due form of law swore  
and deposed to the truth of the several statements matters and things  
mentioned and contained in the said verification.

IN WITNESS whereof I have hereunto set my hand and seal of  
office at London aforesaid this twenty-seventh day of April two  
thousand and five.





THE STATE OF NEW HAMPSHIRE

MERRIMACK, SS

SUPERIOR COURT

Docket No. 03-E-0106

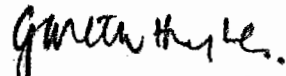
In the Matter of the Liquidation of  
The Home Insurance Company

VERIFICATION OF GARETH HOWARD HUGHES

I, Gareth Howard Hughes, of 1 More London Place, London SE1 2AF, United Kingdom, hereby depose and say:

I am a licensed insolvency practitioner and a partner in the firm of Ernst & Young LLP of the above address. I am also one of the Joint Provisional Liquidators of The Home Insurance Company ("Home"), having been appointed to such office by the High Court of Justice in London, England, on 8 May 2003. I submit this Verification in support of the Offer of Proof (the "Offer of Proof") to be submitted in the above-captioned matter by the Commissioner of Insurance for the State of New Hampshire, as Liquidator of Home.

I am acquainted with and hereby verify the accuracy of the facts and information set forth in paragraphs 2, 4, 6-14, 21, 22, 24, 27-30, 32, 33, 35-40, 43-45, 49-58, 60-66, 68-75, 78, 81, 85 and 94 of the Offer of Proof. Such facts and information are either within my own knowledge, gained through my involvement with this matter, in which case I confirm that they are true, or are based on information provided to me by others, in which case they are true to the best of my knowledge, information and belief.

  
\_\_\_\_\_  
Gareth Howard Hughes

Sworn at London, England

This 27 day of April, 2005

Before me:



[ATTACH NOTARIZATION]



**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**

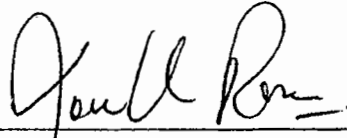
**VERIFICATION OF JONATHAN ROSEN**

I, Jonathan Rosen, hereby depose and say:

I am the Chief Operating Officer of The Home Insurance Company ("Home"), a position I have held since shortly after the liquidation commenced. Prior to that, I was Executive Vice President and Reinsurance Counsel of Home and Executive Vice President of Risk Enterprise Management Limited, a third party administrator that, among other things, administered the business of Home. I submit this Verification in support of the Offer of Proof (the "Offer of Proof") to be submitted in the above-captioned matter by the Commissioner of Insurance for the State of New Hampshire, as Liquidator of Home.

I am acquainted with and hereby verify the accuracy of the facts and information set forth in paragraphs 6-14, 16, 17, 20, 21, 23-34, 36-39, 41, 42, 46-49, 59, 67, 70, 78, 79, 85, 86, and 88 of the Offer of Proof. Such facts and information are either within my own knowledge, gained through my involvement with this matter, in which case I confirm that they are true, or are based on information provided to me by others, in which case they are true to the best of my knowledge, information and belief.

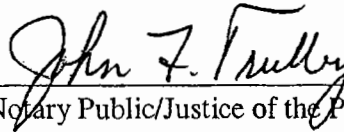
Signed under the penalties of perjury this 27<sup>th</sup> day of April, 2005.



Jonathan Rosen  
Chief Operating Officer of The Home Insurance Company

STATE OF NEW YORK  
COUNTY OF NEW YORK

Subscribed and sworn to, before me, this 27<sup>th</sup> day of April, 2005



Notary Public/Justice of the Peace

**JOHN F. TRULBY**  
**NOTARY PUBLIC, State of New York**  
**No. 43-4931270**  
**Qualified in Richmond County**  
**Commission Expires June 20, 2006**

# CHEESWRIGHT'S

NOTARIES PUBLIC

10 Philipps Lane London EC3M 8EP  
Telephones 020 7614 9477 (up) 0200 NOTARIES

Fax 020 7614 9474

E-mail [cheeswrights@bt.com](mailto:cheeswrights@bt.com)

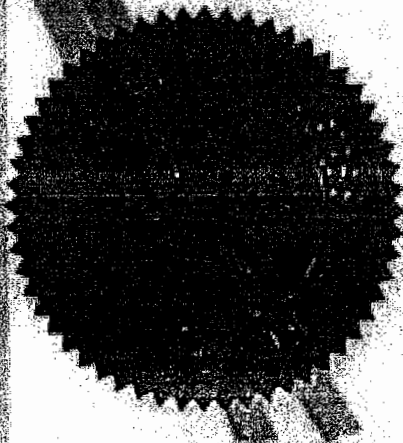
[www.cheeswrights.com.uk](http://www.cheeswrights.com.uk)

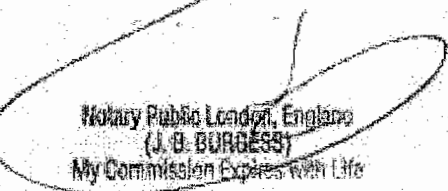
DN 6776 London 1st ECU

TO ALL TO WHOM THESE PRESENTS SHALL COME, I  
JEREMY BROOKER BURGESS of the City of London  
NOTARY PUBLIC by royal authority duly admitted and sworn DO  
HEREBY CERTIFY that on the day of the date hereof before me  
personally came and appeared RHYDIAN WILLIAMS the  
Deponent named and described in the verification hereunto annexed  
WHO in my presence by solemn oath by him taken in due form of  
law swore and deposted to the truth of the several statements matters  
and things mentioned and contained in the said verification.

IN TESTIMONY whereof I have hereunto set my hand and seal of  
Office.

LONDON the twenty eighth day of April in the year two thousand  
and five.



*J*  
  
Notary Public London, England  
(J. B. BURGESS)  
My Commission Expires with Life



N P Burgess  
Paul M Campbell J B Burgess E Gardiner  
& J Charles J A Brown

THE STATE OF NEW HAMPSHIRE

MERRIMACK, SS

SUPERIOR COURT

Docket No. 03-E-0106

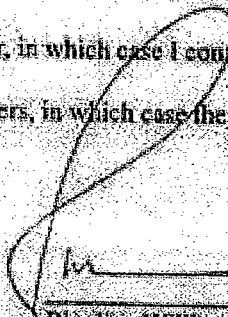
In the Matter of the Liquidation of  
The Home Insurance Company

VERIFICATION OF RHYDIAN WILLIAMS

I, Rhydian Williams, of 9 Ryves Avenue, Yateley, Hampshire, United Kingdom, GU46  
6PB, hereby depose and say:

I am an employee of Equitas Limited with responsibility for Equitas' relationships with  
insolvent reinsurers. I submit this Verification in support of the Offer of Proof (the "Offer of  
Proof") to be submitted in the above-captioned matter by the Commissioner of Insurance for the  
State of New Hampshire, as Liquidator of The Home Insurance Company.

I am acquainted with and hereby verify the accuracy of the facts and information set forth  
in paragraphs 36-40, 42-43, 50-52 and 55 of the Offer of Proof in so far as they relate to  
statements made by me. Such facts and information are either within my own knowledge,  
gained through my involvement with this matter, in which case I confirm that they are true, or  
are based on information provided to me by others, in which case they are true to the best of my  
knowledge, information and belief.

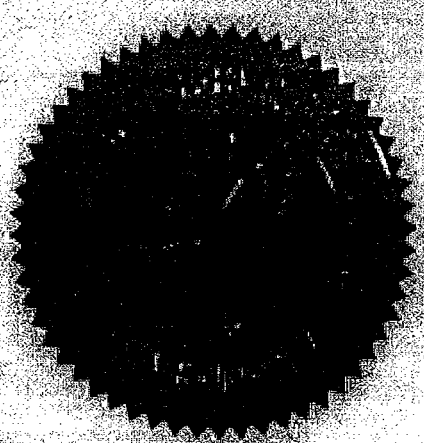
  
\_\_\_\_\_  
Rhydian Williams

Sworn at

This 23<sup>rd</sup> day of April, 2005

Before me:

  
\_\_\_\_\_  
[ATTACH NOTARIZATION]  
Notary Public London, England  
(J. B. BURGESS)  
My Commission Expires with Life



THE STATE OF NEW HAMPSHIRE

MERRIMACK, SS

SUPERIOR COURT

Docket No. 03-E-0106

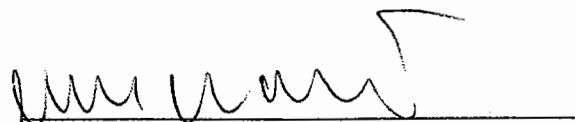
In the Matter of the Liquidation of  
The Home Insurance Company

VERIFICATION OF GERNOT A. WARMUTH

I, Gernot A. Warmuth, hereby depose and say:

1. I am an attorney at the law firm of Scheiber & Partner, Rechtsanwälte Notare, Kennedyallee 97, D-60596 Frankfurt am Main, Germany. My client is Zürich Versicherung Aktiengesellschaft (Deutschland), as successor to Agrippina Versicherung Aktiengesellschaft ("Agrippina"). I submit this Verification in support of the Offer of Proof (the "Offer of Proof") to be submitted in the above-captioned matter by the Commissioner of Insurance for the State of New Hampshire, as Liquidator of The Home Insurance Company. Reference is made in the Offer of Proof to Agrippina for ease of reference since it was the company that initially entered into the subject insurance arrangements.

2. I am acquainted with and hereby verify the accuracy of the facts and information set forth in paragraphs 30, 40, 41, 42, 59 and 86 of the Offer of Proof in so far as they relate to statements made by me. Such facts and information are either within my own knowledge, gained through my involvement with this matter, in which case I confirm that they are true, or are based on information provided to me by others, in which case they are true to the best of my knowledge, information and belief.


  
Gernot A. Warmuth

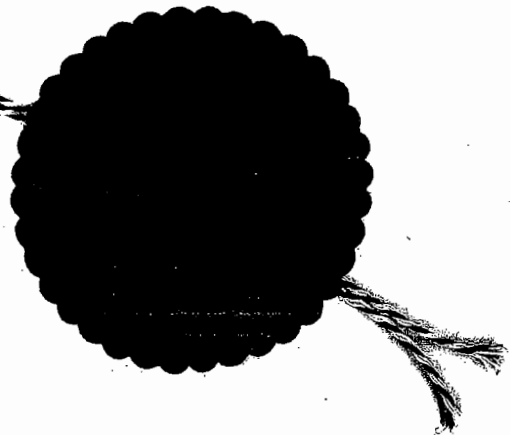
Sworn this 25<sup>th</sup> day of April, 2005  
at Frankfurt am Main (Germany)  
before me, the undersigned Notary Public Edgar Birr, with official residence at  
Frankfurt am Main (Germany)

**Protocol Registration No.** 242 /2005

I hereby officially certify, that the above signature of Gernot A. Warmuth, born July 5<sup>th</sup>, 1955, resident at Kennedyallee 97, D-60596 Frankfurt am Main, who is personally known to me and who denied any prior involvements as defined by Sec. 3 Para. 1 No. 1 of the German Official Recordings Act, has been executed in my presence.

Frankfurt am Main, April 25<sup>th</sup>, 2005

  
(Birr)  
Notary Public



Kosten:

**Geschäftswert: € 3.000,00**

Gebühr § 45 KostO

zuzüglich 16% MWSt.

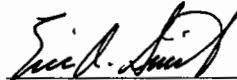
€ 10,00

(Birr)  
Notar



Certificate of Service

I hereby certify that a copy of the foregoing Liquidator's Offer of Proof was sent, this 28th day of April, 2005, by first class mail, postage prepaid to all persons on the attached service list.



---

Eric A. Smith



THE STATE OF NEW HAMPSHIRE

MERRIMACK, SS.

SUPERIOR COURT

In the Matter of the Liquidation of  
The Home Insurance Company  
Docket No. 03-E-0106

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