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 MOTION FOR APPROVAL OF 2005 COMPENSATION PLANS

Roger A. Sevigny, Commissioner of Insurance for the State of New Hampshire, as Liquidator ("Liquidator") of The Home Insurance Company ("The Home"), hereby moves that the Court enter an order approving three integrated compensation plans for the employees of The Home in 2005 consisting of a Retention Incentive Plan, an Annual Incentive Plan and a Collection Incentive Plan (the "Plans"). Summaries of the Plans are attached as Exhibits A to C. The Plans are intended to reward performance and reinforce retention of essential employees. The Plans and their estimated 2005 cost have been reviewed with the National Conference of Insurance Guaranty Fund's Subcommittee on The Home which has advised that it has no objection to the Plans. In support hereof, the Liquidator respectfully represents as follows:

1. Liquidation Staff for The Home. As described in the Liquidator's reports and the Liquidator's Motion for Approval of Compensation Plans dated April 5, 2004 (concerning the 2004 compensation plans) (the "2004 Compensation Motion"), shortly after the liquidation proceeding began in June 2003, the Liquidator determined that the most efficient way to organize the liquidation process was to hire the most critical Risk Enterprise Management ("REM") employees. This permitted the Liquidator to benefit

from the continued involvement of experienced employees with prior involvement with The Home runoff. The Liquidator hired 93 employees to handle the liquidation of The Home (and of USI Re). During 2004, four employees voluntarily terminated their employment with Home. The liquidation is presently staffed by 90 employees, 73 of whom are located at The Home's former headquarters in New York City and 17 in Manchester, New Hampshire. The Liquidator has also appointed the Special Deputy Liquidator to manage the operations of the liquidation. The Special Deputy Liquidator is a consultant to the Liquidator, not an employee of The Home, and is not covered by the proposed Plans. Affidavit of Peter A. Bengelsdorf, Special Deputy Liquidator, in Support of Approval of 2005 Compensation Plans ("Bengelsdorf Aff.") ¶ 3.

2. The Retention of Experienced Employees Benefits Creditors. The Home operated internationally and specialized in affording complex forms of insurance to large enterprises. Due to the sophisticated nature of The Home's insurance products, operations and supporting reinsurance programs, an experienced and stable liquidation staff will materially contribute to the efficient collection of assets. This is illustrated by the increase in The Home's liquid assets from the day the Order of Rehabilitation was entered, approximately $3 million, to approximately $640 million at November 30, 2004. Most of this increase is attributable to a combination of reinsurance recoveries and other financial settlements negotiated by The Home's experienced staff. Maximizing the prompt collection of assets is one of the principal statutory goals of the liquidation. RSA 402-C:25, VI. The Liquidator believes that this objective can be facilitated through an alignment of creditor interests with the interests of The Home's employees. Bengelsdorf Aff. ¶ 4.

3. Performance Based Compensation Plans Are Appropriate for Large Insurer Receiverships. As set forth in the 2004 Compensation Motion, the Liquidator engaged nationally recognized compensation consultants to assist in the design of employee compensation plans for 2004. The consultants had extensive experience in the design of compensation plans for large insurers, like The Home, in liquidation. The consultants concluded that The Home's base salaries were approximately at the 50th percentile among comparable companies and recommended that total direct compensation (base salary and incentive bonuses) range between the 50th and 75th percentile. Bengelsdorf Aff. ¶ 5.

4. The Three 2004 Compensation Programs. The Liquidator accordingly developed and requested approval for three integrated compensation plans for 2004: a Retention Plan for non-exempt full time employees, an Annual Incentive Plan for exempt full time employees including executives, and a Collection Incentive Plan for executives. As set forth in the 2004 Compensation Motion, the Liquidator's consultants advised that the plans represented best practices with respect to compensation in insurance company liquidations, provided competitive annual and long-term earnings opportunities, and balanced performance-based rewards with short term and long-term retention. The individual programs were integrated across employee levels and would provide, if performance goals were met or exceeded, total direct compensation between the 50th and 75th percentile market levels. This was the level of compensation recommended by the Liquidator's consultants in order to retain experienced employees. The Court approved the compensation plans for 2004 by order issued April 21, 2004. Bengelsdorf Aff. ¶ 6.

5. <u>The Three 2005 Compensation Plans</u>. After consulting with Ernst & Young LLP, the Liquidator proposes to implement essentially the same compensation plans for 2005:

a. The Retention Incentive Plan ("Retention Plan") will provide a cash incentive to The Home's fifteen non-exempt (Federal Wage and Hour Law) full time employees as of January 1, 2005 to stay with The Home. Subject to continuing employment, these employees would receive three additional bonus checks, one each in June, September and December. If an employee voluntarily leaves or is terminated for cause, then no Retention Plan payment would be made. In the event of death, disability or an involuntary termination, the employee will be entitled to the pro rata portion of the payment that would next be made. The estimated 2005 cost for the Retention Plan is approximately $56,700 (compared to $79,000 in 2004). Bengelsdorf Aff. ¶ 7.

b. All seventy-five exempt (Federal Wage and Hour Law) full time employees as of January 1, 2005, would be eligible to participate in the Annual Incentive Plan ("Annual Plan"). This plan is designed to provide additional cash compensation based on the overall performance of The Home's liquidation and the individual employee during the annual plan cycle. The Liquidator will determine the annual goals, performance measures and payouts. Annual cash payments will be made after the close of the performance year (no later than March 15, 2006). If an employee voluntarily leaves or is terminated for cause, then no Annual Plan payment would be made. In the event of death, disability or an involuntary termination, the employee will be entitled to a pro rata share of any Annual Plan payment. The estimated 2005 cost for the Annual Plan is approximately $2.3 million (compared with $3.2 million in 2004). Bengelsdorf Aff. ¶ 8.

c. At the discretion of the Liquidator, the ten senior executives of The Home would be eligible to participate in the Collection Incentive Plan ("Collection Plan"). The Collection Plan is designed to provide focused incentives for the collection of assets. Awards under this plan will be based on the accomplishment of annual collection targets but may also vary, at the discretion of the Liquidator, based on achievement of individual performance goals. The twin goals of the Collection Plan are to maximize the collection of assets and retain senior and experienced executives as long as deemed necessary by the Liquidator. Therefore, any Collection Plan award will be deferred and funded into a trust account. The employee will actually receive those funds only upon the termination of the liquidation proceeding, involuntary termination of employment other than for cause, or at the discretion of the Liquidator if an interim payout is deemed appropriate (e.g., an interim 40% payout at July 2007 and 60% payout at July 2009). If an employee voluntarily terminates or is terminated for cause, then all Collection Plan amounts are forfeited. In the event of death or disability, the Collection Plan amounts will be distributed. Collections beyond goals in 2004 will carry forward into 2005. The estimated 2005 cost for the Collection Plan is approximately $1.5 million (compared with $1.4 million in 2004). Bengelsdorf Aff. ¶ 9.

6. There will be no salary increase program in 2005, and thus employee base salaries will continue to be at approximately the 50^{th} percentile. Because Home is a company in liquidation, its employees have less career potential than they would if they were to leave Home and become employed with a "healthy" insurance company.

Further, previously available perquisites and company-sponsored portions of benefits plans have been restructured or reduced. The Home has no retirement plan or company-matched 401(k) plan (as discussed in paragraph 8, a safe harbor 401(k) plan will be effective in 2005). To address these issues, the Liquidator proposes to continue to provide incentive/retention compensation to all The Home's employees. Each of the three proposed 2005 plans is annually renewable and is therefore subject to prospective modification or termination by the Liquidator. Bengelsdorf Aff. ¶ 10.

7. The Liquidator seeks to continue to provide compensation consistent with best practices with respect to compensation in insurance company liquidations, provide competitive annual and long-term earnings opportunities and balance performance-based rewards with short term and long-term retention. The individual programs are integrated across employee levels and, if performance goals are met or exceeded, will provide total direct compensation between the 50th and 75th percentile market levels. This is the level of compensation recommended by the Liquidator's consultant in order to retain experienced employees. Bengelsdorf Aff. ¶ 11.

8. The total incentive compensation budget (assuming performance goals are met) for 2005 has been reduced to reflect a safe harbor payment to permit full participation by employees in The Home's 401(k) plan. As described in the Liquidator's reports, The Home adopted a non-contributory 401(k) plan effective October 1, 2004. Further, effective January 1, 2005, The Home adopted the safe harbor provision under Internal Revenue Service rules so that all employees who wish to do so may contribute the maximum amount to the 401(k) plan. The cost of adopting the safe harbor provision is three percent of employees' earnings (up to an individual employee earnings cap of

$205,000). The cost for 2005 is estimated at $298,000, which has been applied to reduce the budget for the Annual and Collection Plans to the amounts set forth above. Bengelsdorf Aff. ¶ 12.

9. The Liquidator also determined to extend the present severance benefit program (which was in place only until June 30, 2005) until June 30, 2007. That program excludes executives eligible for the Collection Plan, which addresses severance issues for them. Under the severance program, eligible employees may receive three or six months of severance benefits. The estimated costs of the severance program have previously been applied against the total 2004 incentive compensation budget to reduce incentive payments under the 2004 Annual Plan. Bengelsdorf Aff. ¶ 13.

10. <u>The Liquidator's Consultant Advises That The Proposed Plans are Appropriate</u>. The Liquidator's consultant, Ernst & Young, advises that the 2005 compensation proposal is appropriate and consistent with typical market practices among insurance companies in liquidation. It further advises that the individual plan designs and mechanics are based upon commonly accepted compensation practices for insurance companies in liquidation, and that the levels of pay provided by the individual plans, as well as the overall total compensation, represent market competitive compensation levels. A copy of Ernst & Young's advisory letter dated December 3, 2004 is attached as Exhibit D. Bengelsdorf Aff. ¶ 14.

11. The Liquidator believes that without the adoption of these three plans that the liquidation effort would be harmed because key employees would seek better, more long-term career opportunities elsewhere. See Bengelsdorf Aff. ¶ 15.

12. The Liquidator has authority under RSA 402-C:25, II, and paragraph (r) of the Order of Liquidation issued June 13, 2003, to engage employees and set the terms of their compensation "subject to the control of the court." The Liquidator also has authority pursuant to RSA 402-C: 25, IV, to use the property of The Home and to defray the costs of collecting its assets and liquidating its property and business.

13. For the reasons described above and in the Bengelsdorf Affidavit, the Liquidator submits that the Plans are fair and reasonable and in the best interests of the liquidation and of the policyholders and other creditors of The Home. See Bengelsdorf Aff. ¶ 16.

WHEREFORE, the Liquidator requests that the Court enter an order in the form submitted herewith approving the Plans and grant such other and further relief as may be just.

Respectfully submitted,

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

By his attorneys,

KELLY A. AYOTTE
ATTORNEY GENERAL

Suzanne M. Gorman
Senior Assistant Attorney General
Civil Bureau
New Hampshire Department of Justice
33 Capitol Street
Concord, N.H. 03301-6397
(603) 271-3650

Eric A. Smith

J. David Leslie, pro hac vice
Eric A. Smith, pro hac vice
Rackemann, Sawyer & Brewster
One Financial Center
Boston, MA 02111
(617) 542-2300

January 12, 2005

Certificate of Service

I hereby certify that a copy of the foregoing Motion for Approval of 2005 Compensation Plans, the Affidavit of Peter A. Bengelsdorf, Special Deputy Liquidator, and the proposed form of order were sent, this 12th day of January, 2005, by first class mail, postage prepaid to all persons on the attached service list.

Eric A. Smith

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SERVICE LIST

Ronald L. Snow, Esq.
Orr & Reno
One Eagle Square
P.O. Box 3550
Concord, New Hampshire 03302-3550

Gary Lee, Esq.
Pieter Van Tol, Esq.
Lovells
16th Floor
900 Third Avenue
New York, New York 10022

Gail M. Goering, Esq.
Adam Goodman, Esq.
Eric Haab, Esq.
Lovells
One IBM Plaza
330 N. Wabash Avenue, Suite 1900
Chicago, Illinois 60611

Andre Bouffard, Esq.
Eric D. Jones, Esq.
Downs Rachlin Martin PLLC
199 Main Street
P.O. Box 190
Burlington, Vermont 05402-0190