



WORLDWIDE INSURANCE

Chesterfield House, 26-28 Fenchurch Street, London, EC3A 3DH.
 Telephone: 01-626 8744, 01-626 8758 Telex No. 686980

APPENDIX B

Exhibit 10

G.R. Wilson Esq.
 Department of Trade & Industry
 Insurance Division 1E
 Sanctuary Buildings
 20 Great Smith Street
 London SW1P 3DB

28th October 1985

Dear Mr Wilson,

RE: THE HOME INSURANCE COMPANY
ST. PAUL FIRE & MARINE INSURANCE COMPANY
TREATY DEPARTMENT REINSURANCE ARRANGEMENTS

At a recent meeting you requested further details of the special reinsurance arrangement covering the Treaty Departments of the London branches of The Home Insurance Company and St. Paul Fire and Marine Insurance Company in respect of the 1983 and prior underwriting years.

The reinsurance arrangements in question include those arranged with BAFOD Reinsurance Company, a company incorporated in Bermuda. Prior to the acquisition of AFIA by CIGNA Corporation, BAFOD was ultimately wholly-owned by the then members of AFIA. Since the acquisition of AFIA by CIGNA, BAFOD has ultimately been a wholly-owned subsidiary of CIGNA. BAFOD is authorised to carry on insurance business in Bermuda.

The History of the Arrangements is as follows:

In June 1981 with effect from 12th May 1981 and subsequently amended to have effect from 1st January 1981 an Excess of Loss Reinsurance Agreement was entered into whereby six specific treaties written by the Home Insurance Company were 100% retroceded to BAFOD.

In 1982 the general nature of the AFIA UK Treaty Department losses became apparent, and a Second Excess of Loss Reinsurance Agreement was entered into. In summary, subject to a retention of US\$95 million, all losses of the UK Treaty Departments of Home and St. Paul and certain uncollectable reinsurance is recoverable from BAFOD.

...2/-

- 2 -

For BAFCO's protection the Stop Loss Agreement was entered into which provided that in so far as BAFCO's liabilities were not covered by its accumulated funds it would be reinsured without limit by all the then members of AFIA.

On acquisition of AFIA these reinsurance arrangements passed to CIGNA and for the purpose of the acquisition Stop Loss Addendum 1, the Insurance Assumption Agreement and the Quota Share Agreement were entered into. Since that time CIGNA has taken further steps to consolidate and simplify the reinsurance arrangements by the preparation and execution of the First Supplemental Excess of Loss Reinsurance Agreement and Stop Loss Addendum.

The Present Arrangements are currently:

The First and Second Excess of Loss Reinsurance Agreements have been modified by the First Supplemental Excess of Loss Reinsurance Agreement. The Stop Loss Agreement must be read in conjunction with Stop Loss Addendum 1 and, Stop Loss Addendum 2. The Insurance Assumption Agreement and Quota Share Agreement exist independently.

The Stop Loss Agreement, as amended by Stop Loss Addendum 1 and Stop Loss Addendum 2, is now between BAFCO and Insurance Company of North America, one of CIGNA's US insurance subsidiaries. As amended, the Stop Loss Agreement reinsures BAFCO for all liability under the First and Second Excess of Loss Reinsurance Agreements (as amended) in excess of an aggregate of US\$50,000.

The Insurance Assumption Agreement was entered into on CIGNA's acquisition of AFIA. It provided that INA would assume as its direct obligation all insurance and reinsurance liabilities of each of the selling members of AFIA (including Home and St. Paul) arising out of the operation of AFIA. This agreement results in INA being legally obliged to stand directly behind the liabilities of the Home and St. Paul Treaty Departments whether formally reinsured with INA or not.

Under the Quota Share Agreement the selling AFIA members in turn reinsure INA and the other CIGNA entities for:

- (a) a 90% Quota Share of US\$265 million excess of US\$335 million of losses of the London Treaty Department; and
- (b) 50% of non-recoverable London Treaty Department reinsurance in excess of US\$45.9 million.

In conclusion I would suggest that the reinsurance now afforded by BAFCO under the First Excess of Loss Reinsurance Agreement, the Second Excess of Loss Reinsurance Agreement and the First Supplemental Excess of Loss Reinsurance Agreement and supported by the Stop Loss Agreement provide high quality protection for the United Kingdom Treaty Department of Home and St. Paul.

...3/-

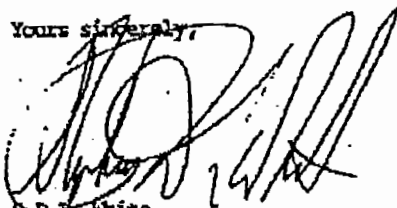
- 3 -

I hope that you now have the information which you require. If you would appreciate a meeting to clarify further the contents of this letter, I should be very happy to oblige.

I enclose the following copy documents:

- (a) First Excess of Loss Reinsurance Agreement, signed on 1st and 23rd December 1982 and taking effect on 12th May 1981.
- (b) Second Excess of Loss Reinsurance Agreement, signed on 1st and 23rd December 1982 and taking effect on 12th May 1982.
- (c) First Supplemental Excess of Loss Reinsurance Agreement, signed on 1st February 1985 and taking effect on 1st January 1981 in respect of the First Excess of Loss Reinsurance Agreement and 12th May 1982 in respect of the Second Excess of Loss Reinsurance Agreement.
- (d) Stop Loss Reinsurance Agreement, signed on various dates in 1982 and 1983 and taking effect on 30th June 1982.
- (e) Addendum number 1 to the Stop Loss Agreement signed on 31st January 1983 and taking effect on 30th June 1983.
- (f) Addendum number 2 to the Stop Loss Agreement, in draft, and taking effect on 30th June 1983.
- (g) Insurance and Reinsurance Assumption Agreement, signed on 31st January 1984 and taking effect on that date, together with a glossary of terms used but not defined in the Agreement. ✓
- (h) Quota Share Reinsurance Treaty Agreement, signed on 31st January 1984 and taking effect on 30th June 1983, together with a glossary of terms used but not defined in the Agreement. ✓

Yours sincerely,



S. D. White
General Manager
SW22/85/AE/DA14/LP

3

The St Paul

St. Paul Specialist Services Limited
 Suite 1/2
 London Underwriting Centre
 3 Minster Court
 Mincing Lane
 London EC3R 7YJ
 020 7618 6100 Tel
 020 7618 6294/5 Fax

Exhibit 11

Gareth Hughes
 Ernst & Young LLP
 Becket House
 1 Lambeth Palace Road
 London SE1 7EU

EU ERNST & YOUNG LLP LONDON	
01 SEP 2003	
Partner	GWH/MEM
Manager	

29th August 2003

Dear Sir,

Re: The Home Insurance Company (in provisional liquidation)Thank you for your letter of 31st July 2003.

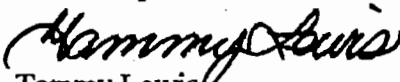
We are investigating the position of Unionamerica Insurance Company Limited (Unionamerica) with regard to its reinsurances underwritten by AFIA (including those reinsurances where The Home Insurance Company UK Branch was used to front for AFIA), which also includes collating the information requested in your letter.

We are not yet in a position to say whether or not Unionamerica will be pursuing claims under its reinsurances with AFIA as a creditor of The Home. I would however be willing to participate as a member of the proposed informal creditors committee on the understanding that my participation will not in any way bind Unionamerica in relation to whether or not it is a creditor of The Home. I would also be willing to participate in the committee as a representative of St. Paul International Insurance Company Limited (formerly St. Katherine Insurance Company Limited) on the same basis.

I look forward to hearing from you.

Yours faithfully

For and on behalf of
 St. Paul Specialist Services Limited


 Tammy Lewis
 Legal Officer

The St Paul

RECEIVED
4 AUG 2003

St. Paul Specialist Services Limited
Suite 1/2
London Underwriting Centre
3 Minster Court
Mincing Lane
London EC3R 7YJ
020 7618 6100 Tel
020 7618 6294/5 Fax

Ms B Nowak
Claims Manager
ACE INA Services UK Ltd
The London Underwriting Centre
3 Minster Court
Mincing Lane
London EC3R 7DD

1st August 2003

By Post and Facsimile 020 7173 2801

Dear Ms Nowak,

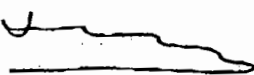
**Re: Unionamerica Insurance Company Limited
Casualty XL Loss Reinsurance
US \$50,000 xs US\$25,000 and US\$75,000 xs US\$75,000
1974 - 1980 Years of Account**

We refer to our correspondence in relation to the claims notified under the above policies by way of claims bordereaux. We are in the process of investigating Unionamerica's position in relation to these claims. Accordingly please note that Unionamerica withdraws the request for payment of the claims set out on the attached schedule with immediate effect. For the avoidance of doubt, this withdrawal does not affect the notification, which Unionamerica has already given, of all claims on these policies (including the claims in the attached schedule) under the second paragraph of the notice of loss clause. Further, this withdrawal does not affect the position of Continental Insurance Company of New York.

While our investigations are continuing please note that we reserve all our rights in relation to this matter.

Yours sincerely

For and on behalf of
St Paul Specialist Services Limited


T.P. Open

cc: Mike Durkin, ACE INA Services Limited

The St Paul

St. Paul Specialist Services Limited
Suite 1/2
London Underwriting Centre
3 Minster Court
Mincing Lane
London EC3R 7YJ
020 7618 6100 Tel
020 7618 6294/5 Fax

Ms B Nowak
Claims Manager
ACE INA Services UK Ltd
The London Underwriting Centre
3 Minster Court
Mincing Lane
London EC3R 7DD

1st August 2003

By Post and Facsimile 020 7173 2801

Dear Ms Nowak,

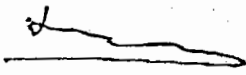
Unionamerica Insurance Company Limited
Excess of Loss Reinsurances
US\$350,000 xs US\$150,000, US\$250,000 xs US\$750,000
US\$1,000,000 xs US\$500,000 1975-1978 Years of Account

We refer to our correspondence in relation to the claims notified under the above policies through Resolutions. We are in the process of investigating Unionamerica's position in relation to these claims. Accordingly please note that Unionamerica withdraws the request for payment of its proportion of the claims as set out on the attached schedule with immediate effect. For the avoidance of doubt this withdrawal does not affect the notification, which has already been given, of all claims on these policies (including the claims in the attached schedule) under the notification of claims clause. Further, this withdrawal does not affect the position of Continental Insurance Company of New York.

While our investigations are continuing please note that we reserve all our rights in relation to this matter.

Yours sincerely

For and on behalf of
St Paul Specialist Services Limited



T.P. Open

cc: Mike Durkin, ACE INA Services Limited

9/17/03

Unionamerica Meeting:

Tammy Lewis

Barbara Nowak

Sara Elk

Alexander Gunn (Sr. Law)

- Have withdrawn claims in order to reserve rights (??)
- Want to participate on creditors committee - BUT CAN THEY ???
- Will provide EY4 with a statement of balances that they believe are owing as if they had not withdrawn claims. plus CASE RESERVES & maybe IBNR
- Requested to clarify why they believe that by withdrawing claims they somehow preserve / reserve their position.
- Can't give an exact time as to when they will tell us their intentions. Seems to be driven by HQ in the U.S.

Cashin, John

From: Denbin, Howard D TL35S [Howard.Denbin@ace-ina.com] **Sent:** Fri 9/12/2003 4:03 PM
To: Cashin, John
Cc: Durkin, Mike MMQE; Bateman, Darren MMQE; Wamser, Thomas J TL35S; 'Philip.Wilkinson@Lovells.com'; 'Joe.Bannister@Lovells.com'
Subject: Home Liquidation

Attachments:

John -

An issue has come up regarding ACE's continuing obligations to administer Home's AFIA liabilities, which we need you and your colleagues to look into ASAP.

Jonathan Rosen, who you may know, is now General Counsel of Home. He and other Home representatives have been interposing themselves into ACE's conduct of various UK matters, including arbitrations involving Ruddy pool members - Agrippina and Wurttembergische, in contravention of the Liquidator's position that ACE's obligations to administer Home's AFIA liabilities on behalf of Home under the Insurance and Reinsurance Assumption Agreement remain in full force and effect, notwithstanding Home's intervening insolvency. In particular, they have advised both Agrippina and Wurttembergische that they have no right to terminate the reinsurance contract (Contract R) between themselves and Home (as provided by Article IX(ii) upon the insolvency of Home), while ACE has been encouraging them to do so as it would be for the economic benefit of all concerned. (If the contract is terminated, the pool members will not have to look to Home as its sole security on policies issued in their names - in accordance with these pool members' positions that Home reinsures their "fronted" liabilities - but rather could look to the other solvent pool members for both the solvent pool members' shares as well as the shares of insolvent pool members which all pool members agreed to proportionally share, as well as obtain the benefits of outward reinsurances. On pool share participations, they can deal directly with ACE and get a somewhat larger recovery instead of a small distribution from the Estate. Home benefits, since no claims are filed against it, and ACE benefits by not paying its 100% reinsurance of Home's liabilities.)

At least two issues are raised:

1.- Paragraph. (p) of the order of Liquidation does permanently enjoin anyone doing business with the Home from terminating its contract(s) on account of the Home's insolvency. Does this provision prevent Ruddy pool members Agrippina and Wurttembergische from terminating its contracts with Home? Or is the provision directed toward requiring vendors to continue to render services, i.e., electricity? And does ACE have any options getting this provision lifted regarding the Agrippina and Wurttembergische actions, as termination would be to the benefit of the Estate? (Home seems to be looking to get claims admitted to the Estate so they can collect the 100% reinsurance to distribute to a larger body of creditor. But this doesn't benefit the Home Estate, it creates a liability in the first instance, and in the end is neutral.)

2 - At what point - and what activities - would the Liquidator need to engage in that would be so in contravention of its position that ACE retains the obligation to administer the AFIA liabilities - as to amount to a waiver, estoppel, repudiation, etc.? I will fax to you the correspondence regarding termination of the contracts. Additionally, Jonathan Rosen has met with each of the Ruddy pool member and various cedents to

H01918

the Ruddy pool, and has advanced positions different from those taken by ACE on behalf of Home in various arbitrations, i.e., he advised Agrippina that they would be allowed to audit various records maintained by ACE, when ACE has advised Agrippina that so long as we remain in arbitration we will not permit free, additional discovery outside of the arbitral process. I believe we may need to send a letter to the Liquidator advising them in the strongest terms that should ACE's defense of any actions on behalf of Home be prejudiced by the Liquidator's actions on behalf of Home, ACE will not provide reinsurance reimbursement for any additional liability. Said activities are also in breach of the contractual provisions allowing ACE, as reinsurer, upon the insolvency of Home, to interpose defenses on behalf of the Liquidator at its own expense.

Please call after you have reviewed this so we can discuss this in detail.

HDD

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immediately, and do not disclose its contents to any other person,

use them for any purpose, or store or copy them in any medium.

Thank you for your cooperation.

H01919

7/16/03

Exhibit 14

Meeting w/ Jackson & Mike Smith:

- (1) Agreed that he would take effect now re Nationwide
- (2) Agreed to allow Agrippina audit subject to terms requiring all that audit is w/o prejudice & can't be used in arbitration - draft of all being prepared.
- (3) Agreed to continue handling direct Primary Pool - says all being drafted confirming same to allowing R of R.
- (4) Said that LMC's would be paid by ACE subject to R of R but probably exclusive of Nationwide & that they were considering tendering Nationwide's look back to them for future handling.
- (5) I reinforced that they shouldn't do side deals w/ cedents & circumvent Home. Jackson was non-committal on ACE's intentions.
- (6) Discussed tripartite Primary Pool, ACE, Home commutation concept.
- (7) Gave him 1985 AFIA w/ describing how agreements work & indicating no BAFCO privity with QS.

H00914

STROOCK

FACSIMILE

DATE September 17, 2003

TO	COMPANY NAME	FAX NO.	PHONE NO.
Alexander Feldwebel	New Hampshire Insurance Dept.	(603) 271-1406	

TOTAL NO. OF PAGES

FROM	John R. Cashin
SENDER'S FAX NO.	212-806-1345
SENDER'S PHONE NO.	212-806-5945
SENDER'S EMAIL	JCashin@Stroock.com
ROOM NO.	3894
ATTORNEY NO.	
CLIENT/MATTER NAME	
CLIENT/MATTER NO.	000628.0003

MESSAGE

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H01920

STROOCK

September 17, 2003

John R. Cashin
Direct Dial 212-806-5945
Direct Fax 212-806-1345
JCashin@Stroock.com

Mr. Alexander Feldwebel
Deputy Commissioner
New Hampshire Insurance Dept.
56 Old Suncook Rd
Concord, N.H. 03301-5151


Dear Alex:

As we discussed in Chicago we represent ACE Group in its relationship to the Home as the acquirer of AFIA. ACE has encountered some potential difficulties in the administration of the AFIA liabilities under the Assumption Agreement and the Reinsurance Treaty and Management Agreement.

Lovells, ACE's UK counsel, has raised this issue with the attorneys for the Provisional Liquidator in London and wishes to advise the New Hampshire Department as well. Enclosed is a copy of the correspondence to counsel for the Provisional Liquidator.

We look forward to working with the New Hampshire Department to resolve these issues.

Very truly yours,



John R. Cashin

Cc: H. Denbin - ACE

H01921

Lovells

Atlantic House
Holborn Viaduct
London EC1A 2FG
Tel: +44 (0) 20 7296 2000
Fax: +44 (0) 20 7296 2001

16 September 2003

Direct line 020 7296 5942
philip.wilkinson@lovells.com
Direct fax 020 7296 2001

Our ref F1PJW/1531445.01

Clifford Chance LLP
200 Aldersgate Street
London
EC1A 4JJ

By email &
By Post

Attention: David Steinberg Esq/John Curran Esq

Dear Sirs

**THE HOME INSURANCE COMPANY (IN PROVISIONAL LIQUIDATION)
INSURANCE AND REINSURANCE ASSUMPTION AGREEMENT DATED 31 JANUARY 1984 ("THE
ASSUMPTION AGREEMENT")**

An issue has arisen relating to the administration by ACE of the AFIA Liabilities under the Assumption Agreement. We use the term "ACE" here to encompass all or any of CIRC, Century Indemnity and ACE INA Services UK Limited. It is an issue that ACE must take very seriously and in our view is one that the provisional liquidators would also take seriously.

We understand that Jonathan Rosen, as Home's Chief Operating Officer, and other representatives of Home have been intervening in the administration of various UK matters affecting the AFIA Liabilities. The detail is perhaps less important than the principle. However, we understand that through these representatives, the following has occurred:

1. Home has advised cedants (Agrippina and Wurtembergische) under the Ruddy Pool contract "R" agreements that they cannot terminate their reinsurance agreements with Home. This is contrary to the position taken by ACE on behalf of Home and, in the view of ACE, materially prejudices both Home as reinsurer of Agrippina and Wurtembergische and ACE as reinsurer of Home;
2. Home has, in connection with ongoing arbitration, indicated that the cedant may audit records maintained by ACE notwithstanding that a process of discovery is in train in the arbitration and that ACE, on behalf of Home, has refused such inspection. Such broad inspection would go well beyond the limits agreed in the proceedings;
3. Home has planned meetings with cedants to discuss commutation.

ACE had understood the position of the provisional liquidators to be that ACE would continue to have full authority (subject only to ACE not having authority finally to bind Home to agreements

Alicante Amsterdam Beijing Berlin Brussels Chicago Dusseldorf Frankfurt Hamburg Ho Chi Minh City Hong Kong London Milan Moscow
Munich New York Paris Prague Rome Shanghai Singapore Tokyo Warsaw Associated offices: Budapest Vienna Zagreb

The partners in the firm are solicitors or registered foreign lawyers or registered European lawyers. Regulated by the Law Society.
A list of the partners and their professional qualifications is open to inspection at the above address.

H01922

Clifford Chance

- 2 -

16 September 2003

without the consent of the provisional and New Hampshire liquidators) to administer the run off of Home's AFIA Liabilities under the Assumption Agreement. ACE considers that the interventions put ACE into the impossible position of serving two masters operating under what appear to be conflicting views of the role and authority of ACE and the interests of Home. ACE considers that the interventions are unhelpful, particularly in the context of the arbitrations. ACE further considers the interventions to fall outside the best interests of Home.

ACE stresses that, under the Assumption Agreement, Home must, at least for so long as it holds ACE to that agreement, act reasonably and comply with the reasonable requests of ACE. Home must also, as an insured, act reasonably not to increase the liabilities of ACE as reinsurer. Home must also allow ACE to interpose defences into proceedings against Home in respect of AFIA liabilities. ACE is concerned that the interventions cause Home to be in breach of these obligations and to increase the possible liabilities of ACE as reinsurer.

ACE hopes that the provisional liquidators will share the concerns of ACE and that the above position can be rectified by the provisional liquidators reaching a common understanding with the US liquidation staff.

In the meantime, ACE reserves all its rights under the Assumption Agreement and generally.

We look forward to hearing from you.

Yours faithfully



cc Tom Wamser/Mike Durkin

H01923

**The State of New Hampshire
Insurance Department**

56 Old Suncook Road
Concord NH 03301-7317
(603) 271-2261 Fax (603) 271-0248
TDD Access: Relay NH 1-800-735-2964



Roger Sevigny
Commissioner

Alex Feldvebel
Deputy Commissioner

September 26, 2003

Mr. Michael J. Daley, President
Century Indemnity Company
1601 Chestnut Street
Philadelphia, PA 19192

Re: The Home Insurance Company ("The Home")
Assumption Agreement dated January 31, 1984

Dear Mr. Daley:

We write as the Liquidator of The Home appointed by the Merrimack County Superior Court in New Hampshire and as Provisional Liquidators of The Home's UK Branch appointed by the High Court of Justice in London in light of the attached letter dated September 16, 2003 from Lovells and certain discussions between Jonathan Rosen, Gareth Hughes and Michael Durkin.

We are concerned that attempts may be made to circumvent the existing contractual relationships between, on the one hand, The Home and its cedants and, on the other hand, The Home as cedant and its reinsurers, with a view to enabling Home's cedants to cut directly through to Home's reinsurers.

In the circumstances, and to avoid any ambiguity, we wish to make clear that both the Liquidator and the Provisional Liquidators would regard such efforts as being unlawful and would seek strenuously to restrain them. Any such arrangements would unlawfully benefit those cedants and those reinsurers by circumventing both contractual provisions and both the United States and United Kingdom liquidation regimes, to the detriment of the remaining creditors of The Home.

As The Home's run-off agent and reinsurer, ACE-INA Services and ACE-INA, clearly have an important role to play in ensuring that claims are handled properly and that reinsurance protecting The Home is not improperly interfered with or appropriated to particular creditors. We would appreciate confirmation that:

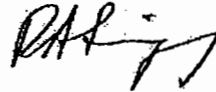
Mr. Michael J. Daley, President
September 26, 2003
Page 2

(1) the ACE group will advise us if it is presently aware of any such efforts on the part of cedants and/or reinsurers (if so, please provide details); and

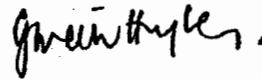
(2) no ACE group company will in any way participate in, or otherwise facilitate, any such efforts, and will notify us immediately upon becoming aware of any such efforts being made.

We look forward to hearing from you. Please direct any correspondence or questions concerning these matters to David Steinberg at Clifford Chance in London.

Very truly yours,



Roger A. Sevigny
Insurance Commissioner, as
Liquidator of The Home Insurance
Company



Gareth H. Hughes
Provisional Liquidator
The Home Insurance Company UK
Branch

cc: David Gold
Michael Durkin
Thomas Wamser
David Steinberg
Peter Bengelsdorf
Jonathan Rosen
David Leslie

H00622

16 September 2003

Direct line 020 7296 5942
philip.wilkinson@lovells.com
Direct fax 020 7296 2001

Our ref F1PJW/1531445.01

Clifford Chance LLP
200 Aldersgate Street
London
EC1A 4JJ

By email &
By Post

Attention: David Steinberg Esq/John Curran Esq

Dear Sirs

**THE HOME INSURANCE COMPANY (IN PROVISIONAL LIQUIDATION)
INSURANCE AND REINSURANCE ASSUMPTION AGREEMENT DATED 31 JANUARY 1984 ("THE
ASSUMPTION AGREEMENT")**

An issue has arisen relating to the administration by ACE of the AFIA Liabilities under the Assumption Agreement. We use the term "ACE" here to encompass all or any of CIRC, Century Indemnity and ACE INA Services UK Limited. It is an issue that ACE must take very seriously and in our view is one that the provisional liquidators would also take seriously.

We understand that Jonathan Rosen, as Home's Chief Operating Officer, and other representatives of Home have been intervening in the administration of various UK matters affecting the AFIA Liabilities. The detail is perhaps less important than the principle. However, we understand that through these representatives, the following has occurred:

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2. Home has, in connection with ongoing arbitration, indicated that the cedant may audit records maintained by ACE notwithstanding that a process of discovery is in train in the arbitration and that ACE, on behalf of Home, has refused such inspection. Such broad inspection would go well beyond the limits agreed in the proceedings;
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ACE had understood the position of the provisional liquidators to be that ACE would continue to have full authority (subject only to ACE not having authority finally to bind Home to agreements

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without the consent of the provisional and New Hampshire liquidators) to administer the run off of Home's AFIA Liabilities under the Assumption Agreement. ACE considers that the interventions put ACE into the impossible position of serving two masters operating under what appear to be conflicting views of the role and authority of ACE and the interests of Home. ACE considers that the interventions are unhelpful, particularly in the context of the arbitrations. ACE further considers the interventions to fall outside the best interests of Home.

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ACE hopes that the provisional liquidators will share the concerns of ACE and that the above position can be rectified by the provisional liquidators reaching a common understanding with the US liquidation staff.

In the meantime, ACE reserves all its rights under the Assumption Agreement and generally.

We look forward to hearing from you.

Yours faithfully



cc Tom Wamser/Mike Durkin

PB

Home Insurance Company in Liquidation

■ Agenda for ACE/INA, Liquidator & Provisional Liquidator Meeting 9/30/03

■ Attendees:

- Mr. Pete Bengelsdorf
- Mr. Gareth Hughes
- Ms. Sarah Ellis
- Mr. Thomas Wamser
- Mr. Howard Denbin
- Mr. Jonathan Rosen

Without prejudice-for discussion purposes only

The Parties Have Clear Relationships.

- ACE/INA acts as an agent of Home in processing AFIA claims.
- Only ACE/INA and Home are in privity of contract – Home has the only claim(s) against ACE/INA arising from AFIA.
- Cedants to AFIA are not in privity of contract with ACE/INA.
- Any assertion of a payment obligation against ACE/INA by an AFIA cedant constitutes a claim against Home (an assertion against the agent is an assertion against the principal).

The Parties Have Multiple Obligations.

- Home has obligations to its creditors and the supervising court.
- ACE/INA has obligations to Home, as its agent, to service the AFIA book.
- ACE/INA is obligated to continue servicing the Ruddy Pool.

Different Laws Apply to the Parties' Relationships and Obligations – In the Case of a Dispute, Different Courts Will Determine the Outcome and the Results are Therefore Unpredictable.

- We assume ACE/INA does not want litigation with Home's liquidator – the Liquidator will act to protect Home's rights and to enforce ACE/INA's obligations.
- While there are separate New Hampshire and UK liquidation proceedings there is actually only one estate. ~ The UK courts are expected to grant comity to the US Liquidation Order including its injunctive provisions.
- The ACE/INA contract is a New York contract and any disputes are to be resolved in New York.
- BAFCO money flows pursuant to UK Law under reinsurance agreement with INA.
- AFIA cedants are subject to different laws:
 - i. Agrippina, Werttembergische – UK Law
 - ii. Nationwide – US Law
 - iii. Equitas – UK Law as respects AFIA, US Law on direct book with Home
 - iv. Unionamerica – UK Law
 - v. Sphere Drake – UK Law
 - vi. Excess – UK Law
 - vii. KWELM - UK Law as respects AFIA, US Law on direct book with Home

AFIA Obligations Were Not Portfolio Transferred to ACE/INA.

- ACE/INA has handled the AFIA book directly with the cedants, as agent of Home, and reported the resulting activity to Home.
- The AFIA business was never transferred to ACE/INA; a novation was never concluded.
- On Home's Liquidation, ACE/INA pays directly to Home without diminution.

A Comprehensive Business Resolution is in the Best Interest of Home and ACE/INA. To Achieve Such a Resolution:

- ACE/INA must recognize that it has a determinable obligation to Home.
- Notwithstanding the invalidity of their legal position, AFIA cedants are expected to assert rights to reimbursement from ACE/INA so their position must be acknowledged; and,
- Home and ACE/INA will therefore need to agree on a reasonable allocation of the ACE/INA AFIA obligation as between Home and the AFIA cedants.

A Potential Transaction Might be

Structured as Follows:

- ACE/INA pays Home a discounted sum to commute all known and unknown liabilities.
- ACE/INA directly pays all AFIA cedants a percentage of their claims.
- All parties release their claims against each other pursuant to a settlement agreement approved by the supervising court(s).

A Comprehensive Business Resolution is in the Best Interest of Home and ACE/INA. To Achieve Such a Resolution:

- ACE/INA must recognize that it has a determinable obligation to Home.

National Employers' Mutual General Insurance Association Ltd (in liq) v AGF Holdings
 (UK) Ltd and others
 CHANCERY DIVISION
 [1997] 2 BCLC 191, [1997] LRLR 159
HEARING-DATES: 7, 12 November 1996
 12 November 1996

CATCHWORDS:

Insolvent insurer -- Netting -- Insolvent insurer ceding business to reinsurer -- Reinsurer settling claims of policyholders direct -- Whether actionable loss incurred by insolvent insurer.

HEADNOTE:

National Employers' Mutual General Insurance Association Ltd (NEMGIA) was a mutual insurance company limited by guarantee. It carried on an insurance business both within the United Kingdom and abroad. The UK business comprised 15% direct business, where the policyholders dealt with NEMGIA directly, and 85% broked business, where the policyholders dealt with NEMGIA through brokers. Business it carried on in Australia proved heavily loss making and eventually this led to NEMGIA becoming insolvent. In order to raise capital, NEMGIA agreed to sell the entirety of its broked business to AGF Holdings (UK) Ltd (AGF). The vehicle for this purchase was a wholly owned dormant subsidiary of NEMGIA, NEM Insurance Co Ltd (NEMIC). On 11 December 1989 NEMGIA entered into a business sale agreement with NEMIC. By that agreement, NEMIC purchased the goodwill and assets of the broked business and agreed by reinsurance to indemnify NEMGIA against the liabilities under all NEMGIA's broked business policies and against the liabilities under 50% of NEMGIA's direct business policies. When AGF became aware of NEMGIA's insolvency, a direct payment agreement was put in place in order to protect NEMIC from the risks to which it would be exposed in the event of NEMGIA's liquidation. Under the direct payment arrangement NEMIC, not on behalf of NEMGIA, but on its own behalf, would pay direct the policyholders in respect of all claims which were actually made, or which otherwise would be made, against NEMGIA, taking in return from the policyholders an assignment of their claims against NEMGIA. This prevented NEMGIA from having claims made against it or, if claims were made, from suffering a loss. NEMGIA thereby was prevented from making any claim on NEMIC. NEMIC could under the direct payment arrangement pay promptly and in full all policyholder claims but would not be obliged to make any payment under the reinsurance contracts to NEMGIA. NEMGIA ceased trading and a winding-up order was made on 3 October 1990. In an action commenced by writ in the Chancery Division NEMGIA sued AGF and NEMIC for damages for breach of contract and for their tortious conduct in setting up and implementing the direct payment arrangement. NEMGIA contended that they would have been better off if the direct payment arrangement had not been implemented prior to liquidation, because they could have decided what to do with the receipts from NEMIC and would not have had to apply such reinsurance proceeds exclusively in payment of UK policyholders, after liquidation, because the liquidators could have paid all creditors rateably, not just the UK policyholders in full, thus the other creditors which included the Australian policyholders would have received a substantially larger dividend. Because of the likely length of the trial it was decided that the issue of whether NEMGIA had suffered any loss by virtue of the direct payment arrangement which would give rise to a right to substantial damages if the conception, implementation or subsequent operation of the direct payment arrangement were held to be a breach of contract or a tort, would be determined as a preliminary issue of law. It was agreed that the court would proceed on the basis that the defendants' conduct had been deliberate so as to cause money not to be paid to NEMGIA, because they knew or feared that NEMGIA would be going into liquidation and that NEMGIA's money would not be dealt with as they would like. Therefore, instead of the money being paid to NEMGIA, they arranged payment tortiously and in breach of contract to parties to whom NEMGIA would not have made that payment.

Held -- NEMGIA had not suffered any recoverable damage or loss.)

(a) The defendants' alleged wrongdoing in the present case occasioned not a loss but a relief from claims by UK policyholders and relief from liability could not of itself be a loss. The only possible complaint was the loss of the right to an indemnity in respect of such liability. As a matter of common sense and of the law of damages, the liability to UK policyholders and the right to the indemnity from NEMIC was a single package and had unquestionably to be netted-off one against the other in accordance with the general rule that a net loss approach had to be applied. In the present case the loss of the package could not have occasioned NEMGIA any substantial damage.

(b) The loss of the ability by NEMGIA to apply the reinsurance proceeds as it thought served its purpose and in breach of the terms of their policies with the UK policyholders, did not constitute damage or loss. The entitlement on the part of NEMGIA to the receipt of the insurance policies was entirely balanced by the immediate liability to the UK policyholders and both had to be netted-off one against the other.

(c) There was no recoverable loss with regard to claims made after liquidation because the direct payment arrangement prevented liquidators from distributing all the reinsurance proceeds received from NEMIC amongst the large body of creditors *pari passu*, since NEMGIA was not worse off in money terms.

(d) The question of whether the direct payment arrangement infringed the rules laid down to ensure *pari passu* distribution in a liquidation of an insolvent company's assets to its creditors could not and should not have been raised in the guise of the action brought by NEMGIA.

CASES-REF-TO:

British Westinghouse Electric and Manufacturing Co Ltd v Underground Electric Railways Co of London Ltd [1912] AC 673, [1911-13] All ER Rep 63, HL.
 Cleadon Trust Ltd, Re [1938] 4 All ER 518, [1939] 1 Ch 286, CA.
 Edmondson v Nuttall (1864) 17 CB (NS) 280, 144 ER 113.
 Nabi v British Leyland (UK) Ltd [1980] 1 All ER 667, [1980] 1 WLR 529.
 Underwood (AL) Ltd v Bank of Liverpool and Martins [1924] 1 KB 775, [1924] All ER Rep 230, CA.
 Westwood v Secretary of State for Employment [1984] 1 All ER 874, [1985] AC 20, [1984] 2 WLR 418, HL.

CASES-CITED:

Harrington Motor Company, Re, ex p Chaplin [1927] 1 Ch 105, CA.
 Liggett (Liverpool) Ltd v Barclays Bank Ltd [1928] 1 KB 48.
 Parsons v BNM Laboratories [1963] 2 All ER 658, [1964] 1 QB 95, CA.

INTRODUCTION:

In the course of the trial of the action commenced by writ in the Chancery Division by the plaintiff, National Employers' Mutual General Insurance Association Ltd (NEMGIA) (in liquidation) against the defendants, AGF Holdings (UK) Ltd, AGF Insurance Ltd and NEM Business Services Ltd, an issue arose for the determination of the court, namely whether NEMGIA had suffered any loss by virtue of the direct payment agreement, which would give rise to a right to substantial damages if the conception, implementation or subsequent operation of the direct payment agreement were held to be a breach of contract or a tort. The facts are set out in the judgment.

COUNSEL:

M Burton QC, C Newman QC, T Howe and J Crawford for the plaintiff; J Sumption QC, R Hacker and B Isaacs for the defendants.

JUDGMENT-READ:

Cur adv vult 12 November 1996. The following judgment was delivered.

PANEL: LIGHTMAN J

JUDGMENTBY-1: LIGHTMAN J

JUDGMENT-1:

LIGHTMAN J:

A. INTRODUCTION

During the first five weeks of the joint trials of two actions, I have studied the parties' skeletons (totalling some 240 pages), read a copious selection from the 150 bundles of documents, and heard opening speeches by counsel for both parties. At this stage before the calling of any witness, I have been asked by counsel to decide an issue of law which may be determinative of the claim which is the heart of one of the actions. In the event of my deciding that issue one way, several weeks of evidence and argument will be rendered unnecessary and accordingly avoided. I have no doubt that I should take this course in the interests of expedition and economy.

B. THE BACKGROUND

I shall seek to set out in bare outline the facts necessary for an understanding of, and the resolution of, the issue now before me and in respect of which there is, as I understand it, common ground.

The National Employers Mutual General Insurance Co Ltd (NEMGIA), a mutual insurance company limited by guarantee, for many years carried on as its principal business property, motor and liability insurance (but not life insurance) both within the United Kingdom (the UK business) and abroad. The UK business broadly speaking had two principal components; (a) direct business where policyholders dealt with NEMGIA directly (the direct business); and (b) broked business where policyholders dealt with NEMGIA through brokers (the broked business). I shall refer to the direct and broked business policyholders together as 'the UK policyholders'. The broked business in 1988 accounted for some £ 120.1m of NEMGIA's total gross premium income of £ 138.8m (ie over 85%). Its foreign business was carried on in some countries as a branch of NEMGIA (eg in Australia) and in others through subsidiaries (eg in Ireland and South Africa). The business conducted in Australia prior to 1985 was enormous relative to the size of NEMGIA and proved heavily loss making. In 1985, NEMGIA ceased accepting new business in Australia, and (effectively) its only business thereafter that date was the run-off of pre-1985 business (the Australian run-off). Since this business had a long tail, the liability for claims was not only substantial, but likely to extend over a prolonged period. The cost of the Australian run-off was a constant drain on NEMGIA's resources: funds had to be transferred to Australia at a substantial rate. As a result of the liabilities of the Australian run-off by 31 December 1988 NEMGIA was (on an asset basis) insolvent and it continued to be such until its liquidation. The date when the directors of NEMGIA first learnt of such insolvency is in issue.

In view of its pressing need for further capital (which because of its mutual status could not be raised by an issue of capital), NEMGIA in May 1989 instructed Barings to invite offers for a part of its business. With the deterioration of its financial position in 1989, NEMGIA was compelled to agree to sell the entirety of the broked business to a purchaser found by Barings. On 8 December 1989 NEMGIA completed a sale to AGF Holdings (UK) Ltd (AGF) of the entire share capital of a wholly owned dormant subsidiary NEM Insurance Co Ltd (NEMIC), now called AGF Insurance Ltd, which was to be the vehicle for AGF's purchase. On 11 December 1989 NEMGIA entered into a business sale agreement with NEMIC for the sale to NEMIC of the broked business and the NEM Ireland sale agreement for the sale of the Irish subsidiary.

The terms of the business sale agreement (so far as they are material) were as follows:

(1) NEMIC was to purchase the goodwill of the broked business (including the right to solicit renewals from existing policyholders) for some £ 45.7m and the assets of the broked business at a valuation (which produced a figure of some £ 15m);

(2) NEMIC agreed (a) (in consideration of a premium to be calculated as therein provided) by reinsurance to indemnify NEMGIA against the liabilities under all NEMGIA's broked business policies; and likewise (b) (in consideration of a premium) by reinsurance to indemnify NEMGIA against the liabilities under 50% of NEMGIA's direct business policies. The reinsurance was to be effected by four reinsurance contracts (the reinsurance contracts). The premium in the event was £ 128,554,000;

(3) NEMGIA and NEMIC agreed that after completion they should use their reasonable endeavours to obtain a novation or assignment in favour of NEMIC of certain existing reinsurances (the third party reinsurances) 'to the extent that they related to the business ceded';

(4) NEMGIA agreed to sell to AGF the entire issued share capital of its service company NEM Business Services Ltd (NEMBS) for a price sum equal to its net asset value and the parties agreed that they and NEMBS should enter into a service management agency agreement (the agency agreement) under which NEMBS should provide certain agency and management services to NEMGIA, but be left free at the same time to provide services for NEMIC.

Completion was due to take place on 28 February, but had to be postponed because NEMGIA could not raise the balance due of some £ 60m by which the premiums payable by NEMGIA exceeded the purchase price payable by NEMIC for goodwill and assets and for the shares in the Irish subsidiary and NEMBS. To enable NEMGIA to complete, AGF's holding company AGF International SA (AGFISA) agreed to lend NEMGIA some £ 5.643m (the AGFISA loan) secured by a charge over NEMGIA's 73% interest in its South Africa subsidiary, National Employers General Insurance Co Ltd (NEG), and with this assistance and the commutation of certain 'time and distance' policies, NEMGIA was able to complete on 9 March 1990. On that date the parties executed the reinsurance contracts and the agency agreement, NEMGIA executed transfers of the shares in the Irish subsidiary and NEMBS and NEMGIA paid

over to NEMIC the balance due of some £ 60m. (It should be mentioned that there is an issue between the parties whether upon the true construction of the reinsurance contracts NEMIC assumed liability to make payment to NEMGIA as soon as NEMGIA became liable to make payment to the policyholder or only after NEMGIA actually paid the policyholders. For the purposes of this determination I am required to adopt the former construction.) Completion took place subject to provision for certain financial adjustments to be made at a later date. No question is raised in this action regarding the sale of the Irish subsidiary, which drops out of the picture at this stage. Immediate upon completion AGF and NEMIC took over running the broked business and NEMBS.

The board of NEMGIA knew of the insolvency of NEMGIA at some date prior to completion. Whether they knew of the insolvency at the date of the business sale agreement is in issue. There is a dispute whether AGF knew of the insolvency before completion, but most certainly they knew of it very shortly afterwards, and the most anxious consideration followed as to how to protect NEMIC from the risks to which it was exposed in the event of NEMGIA's liquidation.

The risks primarily related to the goodwill of NEMGIA's broked business bought for £ 45.7m. The subsistence of this goodwill depended upon the policyholders' claims under existing NEMGIA policies being promptly dealt with, negotiated and (when agreed or otherwise adjudicated upon) paid in full. Under the arrangements agreed to and adopted upon completion by NEMGIA, NEMIC and NEMBS, for reasons of practical convenience NEMBS on behalf of NEMGIA dealt with, negotiated and agreed claims, and when moneys were due to policyholders NEMIC on behalf of NEMGIA paid the policyholders direct. This saved the unnecessary administrative time and cost of NEMGIA paying and seeking reimbursement by NEMIC. (It may be noted that under the agency agreement, if not placed in funds by NEMGIA, NEMBS was entitled to call on NEMIC to pay such claims direct and NEMGIA did not in fact have much, if any, in the way of free funds).

This arrangement would, however, not survive the liquidation of NEMGIA. The authority of NEMBS to act as agent for NEMGIA would cease; and where claims were made by policyholders on and accepted by NEMGIA, the liquidator could (and in all likelihood would) require NEMIC to pay in full all sums due under the reinsurance agreements only to NEMGIA, and these moneys would fall into the pool of assets available for the whole body of creditors (including the Australian policyholders). Accordingly the UK broked business policyholders would only receive from NEMGIA a dividend and then only belatedly in the eventual distribution by the liquidators to creditors. If this course was followed, the likelihood of renewals by these (and indeed other) policyholders with NEMIC would be adversely affected. (It should be mentioned for completeness that the policyholders would also receive a payment from the Policyholders Protection Board under the provisions of the Policyholders Protection Act 1975, but they would remain out of pocket.)

In this dilemma, NEMIC's solicitors devised what is known as the direct payment arrangement to be put in place once the existing arrangements for payment by NEMIC on behalf of NEMGIA came to an end. Under the direct payment arrangement as so devised NEMIC, not on behalf of NEMGIA, but on its own behalf, would pay direct the policyholders in respect of all claims which were actually made, or which otherwise would be made, against NEMGIA, taking in return from the policyholders an assignment of their claims against NEMGIA. By so doing, NEMIC would prevent NEMGIA having claims made against it or (if claims were made) from suffering a loss; NEMGIA thereby would be prevented from making any claim on NEMIC: it would have no occasion to do so. NEMIC in this way would be enabled to pay promptly and in full all policyholder claims, as was necessary to preserve its goodwill, but would not be obliged to make any payment under the reinsurance contracts to NEMGIA available for the benefit of other creditors.

On 4 May 1990, NEMGIA wrote a letter to NEMBS terminating its authority to admit, negotiate or pay on NEMGIA's behalf any claims, even if they related to the broked or direct business. The letter added:

'We have no objection to your informing [NEMIC] of claims, since it may wish to make its own arrangements direct with claimants.'

What (if any) were the surviving duties of NEMBS to NEMGIA under the agency agreement after the date of this letter are in issue. NEMIC thereafter implemented the direct payment arrangement as originally devised subject to one possible variation. When payments were sent to the policyholders, there was enclosed with the cheques (or at least most of them) an indorsement. The indorsement varied during three consecutive periods of time. The construction of the indorsements is in issue. NEMIC contends that upon their true construction the payment was a voluntary payment made in full and final discharge of NEMGIA's liability to the policyholders. NEMGIA contends that upon their true construction and/or by operation of law the payments effected assignments to NEMIC of the policyholders' claims against NEMGIA. I cannot resolve this question at this stage and it is unnecessary to do so. NEMIC pursuant to the

direct payment arrangement has paid policyholders a sum which the liquidators allege amounts to some £ 290m. No policyholder has made any claim on NEMGIA and NEMGIA has not paid any claim and has received no payment from NEMIC under the reinsurance contracts.

The date at which NEMGIA became aware of the direct payment arrangement and its implementation is in issue, as is the extent (if at all) of the participation and co-operation of NEMGIA in its devising and implementation. NEMIC contends that the idea was its alone and that it went ahead with the direct payment arrangement without any regard to the views or wishes of NEMGIA, and that no expression of views or wishes and no action taken by NEMGIA would have made any difference. Their case is that the 'go-ahead' with some such scheme given to them by NEMGIA by the letter dated 4 May in these circumstances had no, or no significant, effect on them or the course adopted. These are all matters to be resolved at the trial.

Three other events subsequent to the completion require mention.

(1) On or about 6 April 1990 NEMGIA sold to NEMIC the goodwill of the direct business in consideration of the reduction of the AGFISA loan by £ 1m, and certain consequential amendments were made to the business sale agreement and the reinsurance contracts were agreed placing the parties in the same position in respect of the direct business as they already were in respect of the broked business. In particular NEMIC agreed to indemnify NEMGIA in respect of all direct business policyholders claims.

(2) NEMGIA and NEMIC agreed the terms of novation letters to be sent to the third party reinsurers providing for the novation, (substituting as a party NEMIC for NEMGIA), of the third party reinsurances (not excluding those covering business retained by NEMGIA) and for the making by the third party reinsurers of all reinsurance payments thereunder to NEMIC. NEMIC and NEMGIA also signed in April a side letter agreeing that NEMBS should apportion receipts between them according to their entitlement. The novation letters were sent to the third party reinsurers on 8 May. Some were returned signed by the third party reinsurers before, and some after, 29 May 1990. In respect of the novated reinsurances, the third party reinsurers have paid NEMIC the sum which the liquidators allege to be some £ 65m.

(3) The final adjustment of accounts between NEMGIA and NEMIC in respect of completion took place on 2 May 1990, in the course of which AGFISA was repaid the balance of its loan and accrued interest and released its charge on the NEG shares.

NEMGIA ceased trading on 26 April 1990 and the board unsuccessfully sought to promote a scheme of arrangement. A winding-up petition was presented and provisional liquidators were appointed on 29 May 1990. A winding-up order was made on 3 October 1990.

C. THE TWO ACTIONS

There are two sets of proceedings before me.

(1) In the first commenced by ordinary application in the Companies Court (the Companies Court application) the liquidators of NEMGIA sue AGF, AGFISA, NEMIC and NEMBS. They seek declarations that NEMGIA's (a) entry into and completion of the business sale agreement; (b) grant of security for the AGFISA loan and subsequent repayment of the AGFISA loan; (c) co-operation in setting up and implementing the direct payment arrangement and the payment of the UK policyholders pursuant to the direct payment arrangement; and (d) participation in the execution of the novation agreements constituted preferences within the meaning of s 239 of the Insolvency Act 1986 (the 1986 Act). In the alternative they claim that the novations constituted transactions with NEMIC at an undervalue within the meaning of s 238 of the 1986 Act and (in so far as they were completed on or after 29 May 1990) constituted dispositions after the commencement of the winding up within the meaning of s 127 of the 1986 Act. Consequential relief is then sought. In respect of the direct payment arrangement the claim is made for payment of £ 290m paid by NEMIC to UK policyholders, but credit is allowed for the dividend to which NEMIC would become entitled if it proved in the liquidation as a creditor for this sum of £ 290m. I need say no more about this action than that in view of the number of witnesses to be cross-examined and the issues of law raised the trial is likely to take at least another four weeks.

(2) In the second, commenced by writ in the Chancery Division (the Chancery action) NEMGIA sues AGF, NEMIC, and NEMBS (the defendants). The heart of this action is a claim in effect for the same £ 290m as damages for their breaches of the terms of the agency agreement and the reinsurance agreements and for their tortious conduct (eg wrongful interference with contract and conspiracy) in setting up and implementing the direct payment arrangement.

The claim is only intended to be made as a fall back in case the claim for this sum as relief for a preference in the Companies Court application fails and the same credit is allowed for the dividend. If proceeded with (as it is) this claim requires full consideration at the trial. In a word, NEMGIA complains that the UK policyholders were wrongfully prevented from making any claims against NEMGIA and seeks by way of relief in the form of damages to be placed in the same financial position it would have been in if the direct payment arrangement had not been implemented. If such claims had been made by the UK policyholders, NEMGIA would have been entitled to obtain recoveries from NEMIC equal in amount to the claims to be met. Though the price for this entitlement would have been a liability in the self same sum, it is contended that NEMGIA would have been better off, for prior to liquidation it could have decided what to do with the receipts from NEMIC and would not have had to apply such reinsurance proceeds exclusively in payment of UK policyholders; and after liquidation acting by the liquidators NEMGIA would have paid all creditors rateably, (and not the UK policyholders in full), and accordingly the Australian policyholders would have received a substantially larger dividend.

The investigation of the questions of fact and law necessary for a full trial of this claim is a very considerable exercise. Having regard to the seriousness of the allegations of conspiracy, deliberate wrongdoing and conscious misleading of the court as well as policyholders (allegations which are strenuously denied) I cannot think that the trial is likely to take less than four weeks. Enormous costs have already been incurred in the preparation for it. On my pre-reading in this case, I felt grave doubt whether (assuming all NEMGIA's contentions of law and fact were established) NEMGIA could obtain any recovery under this head, and my questioning of Mr Burton in the course of his opening confirmed, rather than removed, these doubts. In these circumstances I suggested that this question of law should be decided before further time and effort are expended on the action, and most particularly before any evidence is called. Counsel after careful consideration agreed that I should immediately do so as the first stage of the trial.

D. THE ISSUE

The issue as formulated by counsel reads as follows:-

'WHETHER NEMGIA (as opposed to the creditors other than the relevant UK policyholders) has suffered any loss by virtue of the direct payment arrangement, which would give rise to a right to substantial damages if the conception, implementation or subsequent operation of the direct payment arrangement were held to be a breach of contract or a tort.'

For the purpose of answering this question, it is agreed that I should proceed on the basis set out in para 2 of NEMGIA's skeleton argument which is in the following terms:-

'The conduct by the [defendants] the subject matter of the causes of action . . . was crafted deliberately so as to cause money not to be paid to NEMGIA, because AGF/NEMIC knew/feared that NEMGIA would be going into liquidation and NEMGIA's money would not be dealt with as they would like . . . Therefore instead of the money being paid to NEMGIA, they arranged payment tortiously and in breach of contract to a party/parties to whom NEMGIA would not have made that payment.'

In short I must proceed on the basis that (1) the defendants, foreseeing the imminent liquidation of NEMGIA, tortiously and in breach of contract deliberately brought it about that the UK policyholders made no claims on NEMGIA and that NEMGIA accordingly had no occasion or right to seek and receive payment under the reinsurance agreements; (2) any receipts by NEMGIA from NEMIC would not have been held subject to any trust or obligation to apply in favour of the UK policyholders, but prior to liquidation would have been the free assets of NEMGIA available to be dealt with as the directors determined and after liquidation would have been held by the liquidators on trust (after payment of all costs and expenses of the liquidation costs and expenses) to be distributed *pari passu* between all NEMGIA's creditors; (3) by way of damages for the tort and breach of contract NEMGIA is entitled to be placed in the position in which it would have been if there had been no direct payment arrangement, ie UK policyholders had made claims on NEMGIA and, when liability in respect of these claims was established (but before these claims were paid and even if these claims were not paid), NEMGIA was entitled to call on NEMIC for payment of a sum equal to such liability; and (4) the liquidators upon liquidation would have paid out of such receipts a dividend to all creditors and accordingly only a percentage of their claims to each UK policyholder.

The short, but perhaps novel, issue of law is whether in such circumstances NEMGIA has suffered any recoverable damage or loss. For myself I would have thought the answer was plainly and obviously in the negative and one requiring no elaboration. But in view of NEMGIA's declared intention to take this matter further, I think it right to spell out the arguments and my reasoning.

A convenient starting point is a passage in Chitty on Contracts (27th edn, 1994), vol 1, p 1198:

'Damages for a breach of contract committed by the defendant are a compensation to the plaintiff for the damage, loss or injury he has suffered through that breach. He is, as far as money can do it, to be placed in the same position as if the contract had been performed. This implies a "net loss" approach in which the gains made by the plaintiff as the result of the breach (e.g. savings made because he is relieved from performing his side of a contract which has been terminated for breach . . .) must be set off against his losses arising from the breach (after he has taken reasonable steps to minimise those losses).'

The decision of the House of Lords in *British Westinghouse Electric and Manufacturing Co Ltd v Underground Electric Railways Co of London Ltd* [1912] AC 673 at 689, [1911-13] All ER Rep 63 at 69 is authority for the adoption as a general rule of this 'net loss' approach in the field of the law of contract and the same approach is equally applicable in the law of tort (see *Nabi v British Leyland (UK) Ltd* [1980] 1 All ER 667 at 669-670, [1980] 1 WLR 529 at 531-532 and *Westwood v Secretary of State for Employment* [1984] 1 All ER 874 at 879, [1985] AC 20 at 44). For reasons of justice or history, this general rule of 'netting-off' is not of universal application: there are certain exceptions. For example in a case where a plaintiff is the victim of personal injury or wrongful dismissal and because of the wrong done to him has received insurance benefits or benevolent donations, he need not give credit for them (see *Westwood v Secretary of State for Employment* [1984] 1 All ER 874 at 878-879, [1985] AC 20 at 43); and it may be that a plaintiff who is the victim of conversion need not give credit for the application of the converted funds in the discharge of his debts unless the plaintiff or his duly authorised agent authorised such application: see *Edmondson v Nuttall* (1864) 17 CB (NS) 280 at 297, 144 ER 113 at 119-120 and consider *AL Underwood Ltd v Bank of Liverpool and Martins* [1924] 1 KB 775 at 794 and 799, [1924] All ER Rep 230 at 236 and 240 and *Re Cleadon Trust Ltd* [1938] 4 All ER 518, [1939] 1 Ch 286. But subject to limited exceptions the rule is of general application.

In the ordinary case where the question arises whether the net loss approach should be adopted, the plaintiff who is the victim of the tort or breach of contract suffers a loss and thereafter by reason of such loss receives certain benefits which (in whole or in part) relieve him of the consequences. The startling feature of this case is that the defendants' alleged wrongdoing in the first instance occasioned, not a loss, but relief from a liability, ie claims by UK policyholders. Relief from a liability of itself cannot of course of itself be a loss. The complaint (and only possible complaint) is the loss of the concomitant and knock-on effect of such relief from liability, namely the loss of the right to an indemnity in respect of such liability. As a matter of common sense and of the law of damages, the liability to UK policyholders and the right to the indemnity from NEMIC are a single package and inseparable: they are two sides of the same coin and must unquestionably be netted-off one against the other. There can be no basis for any exception to the application of the general rule to which I have referred: it must be an a fortiori case for its application. I fail to see how the loss of this package can possibly have occasioned NEMGIA any substantial damage or how this conclusion is affected, (as Mr Burton QC insists that it is), by the fact that the non-payment under the reinsurance contracts was throughout the desired and achieved objective of NEMIC.

Mr Burton argued that there was a loss to NEMGIA because, if claims had been made by UK policyholders on NEMGIA prior to liquidation, once NEMGIA accepted liability to those policyholders NEMIC would have been obliged to pay the full amount of that liability to NEMGIA, but NEMGIA prior to the liquidation, whilst insolvent and trying to keep the wolf from the door, would have been free to apply the reinsurance proceeds as it thought served its interests and in breach of the terms of their policies could have left the UK policyholders unpaid. To leave the UK policyholders unpaid after NEMGIA had accepted liability to them (leave aside after having taken advantage of that liability to extract payment from NEMIC) would have been a breach of contract. In short Mr Burton's case is that NEMGIA suffered loss because it was prevented from profiting from this wrong by withholding payment when placed in funds by NEMIC and so enabled to do so. I do not think that the loss of this opportunity constitutes damage or loss. The entitlement on the part of NEMGIA to the receipt of the reinsurance proceeds is entirely balanced by the immediate liability to the UK policyholders and both must be netted-off one against the other.

Mr Burton goes on to contend that, in case of claims made after liquidation, the liquidators would have been enabled and obliged by the Insolvency Rules 1986, SI 1986/1925 (after payment first of the costs and expenses of the liquidation) to distribute all the reinsurance proceeds received from NEMIC amongst the larger body of creditors (including the UK policyholders) *pari passu*. These proceeds are not now available for this purpose because of the direct payment arrangement and this constitutes a recoverable loss. I do not think that the withholding from the liquidators of the ability to apply the reinsurance proceeds in this matter constitutes such a loss to NEMGIA. The relevant question is: what loss did NEMGIA suffer -- ie in money terms is NEMGIA worse off? The statutory scheme for distribution of the assets of NEMGIA in the liquidation and the manner and consequences of performance of their duties by the liquidators

are irrelevant, and this is so even though the consequences of the direct payment arrangement in this regard were in the forefront of the mind of NEMIC in devising and implementing the direct payment arrangement.

In short, I can see no basis for a claim that the wrongful conduct on the part of the defendants which I must assume, if directed against a solvent company amply able to meet its liabilities as and when they arise, can in law occasion that company loss: so far as it goes, it relieves that company of the administrative and cash-flow burden of which the practical arrangements adopted on completion in this case were designed to relieve NEMGIA. The position is not changed if the company is insolvent (unable to pay its debts as they accrue due) in need (if it is to continue to trade) of the facility to 'rob Peter to pay Paul'. Nor again is it changed if the company's liquidation is seen to be imminent by those who devise and implement the direct payment arrangement and indeed liquidation ensues. The critical focus of attention must be the assets and liabilities, the rights and obligations, of the company. The consequences of the direct payment arrangement are in this respect neutral and accordingly no substantial damages can be awarded.

The reality is that the only persons who have suffered loss and can have been intended to have suffered loss are the creditors of NEMGIA other than the UK policyholders, the foremost of which must be the Australian policyholders. It is to meet situations of this character that legislation (now encapsulated in the 1986 Act) has provided means for adjusting the rights of creditors inter se and setting aside and granting other relief when transactions infringe rules laid down to ensure *pari passu* distribution in a liquidation of an insolvent company's assets to its creditors. The question whether the direct payment arrangement does infringe those rules is the subject matter of the Companies Court application: that question cannot and should not be raised in the guise of the claims now under consideration in the Chancery action at a horrendous cost and involving a substantial waste of court time.

DISPOSITION:

Order accordingly.

SOLICITORS:

Barlow Lyde & Gilbert; Lovell White Durrant.