

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

**THE WESTERN TRUST'S OBJECTION TO  
THE LIQUIDATOR'S ALLOWANCE AND TREATMENT OF CERTAIN  
CLAIMS OF THE CALIFORNIA INSURANCE GUARANTEE ASSOCIATION**

**I. INTRODUCTION AND SUMMARY OF ARGUMENT**

The Western Asbestos Settlement Trust (the "Western Trust") exists for the sole purpose of compensating asbestos victims injured by the business operations of Western Asbestos Company, Western MacArthur Company and MacArthur Company (the "Western Companies"). Every dollar the Western Trust pays in expenses reduces the amount of money available to pay these victims.

The Western Trust settled its claim with the liquidator ("Liquidator") of the Home Insurance Company ("Home") for an allowed claim of \$242.5 million (the "Allowed Claim"). That amount, however, is far less than the total amount of Home's actual liability to the Western Companies under its policies, had Home remained solvent. The Western Trust, therefore, is seeking to recover the balance of Home's liability from the California Insurance Guarantee Association ("CIGA"). To that end, the Western Trust filed a lawsuit for declaratory relief against CIGA in California state court in 2013 (the "Alameda Action").

The Liquidator is indemnifying CIGA against the expenses CIGA is incurring in the Alameda Action ("CIGA's Expenses or the "Expenses"). In turn, the Liquidator is reducing the value of the Western Trust's Allowed Claim on a dollar-for-dollar basis to the extent of its reimbursement of CIGA's Expenses. As of June 2015, that reduction totaled \$311,660 and will

increase (absent intervention by this Court) with each interim distribution to claimants with allowed Class II claims (like the Western Trust), beginning with the distribution expected this quarter.<sup>1</sup> The Western Trust is therefore funding the real-time defense of its litigation adversary.

Further, the Liquidator has not even permitted the Western Trust to review or contest the reasonableness of the Expenses incurred by CIGA that are reducing the value of the Western Trust's Allowed Claim. This is particularly troubling, considering that CIGA has retained *two* law firms to defend against the Alameda Action.

This state of affairs is also against the law of New Hampshire. It runs contrary to the near universal adoption of the "American rule" in the United States, including in California, under which the parties to litigation expect to pay their own legal fees and expenses. It is also bad public policy because it rewards and intensifies natural insurance-related defense incentives to stall, delay and assert every imagined legal argument in the absence of any downside risk of doing so. Indeed, under the circumstances created by the Liquidator in this matter, CIGA's generation of excessive costs is a single-edged tactical sword pointed at the asbestos victims for whose benefit the Western Trust exists. It also frustrates the intent of Congress to bring closure to America's largest mass tort challenge. It smothers in a mass of irrelevancies, funded by the Western Trust, the resolution of the relatively few pivotal legal issues that could clarify the important question whether asbestos bankruptcy trusts created under federal law can access state insurance guaranty funds consistent with the statutory directive that they maintain funds for the benefit of claimants that may not presently know they are entitled to compensation.

The Alameda Action is nowhere near resolution, despite being on file for nearly three years, owing to CIGA's litigation strategy of aggressively denying *any* responsibility for

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<sup>1</sup> Affidavit of Jeffrey W. Moss in Support of The Western Trust's Objection to the Liquidator's Allowance and Treatment of Certain Claims of the California Insurance Guarantee Association ("Moss Affidavit"), ¶ 2, Ex. A.

insolvent insurers' liability to asbestos bankruptcy trusts and, in particular, for Home's liability to the Western Companies. As a result, the Western Trust is incurring significant legal expenses in the Alameda Action *in addition to* the reduction in the value of its Allowed Claim caused by the Liquidator's indemnification of CIGA's Expenses in that lawsuit. Thus, the Western Trust is paying *three sets of lawyers* in the Alameda Action – its own lawyers, and the two law firms that CIGA has employed.

The Liquidator asserts that he is entitled to reduce the Western Trust's Allowed Claim dollar-for-dollar not as a matter of statutory law – no such statute exists – but rather under the terms of the settlement agreement between the Liquidator and the Western Trust. The Western Trust made no such agreement. It agreed only that its indemnity recoveries from insurance guaranty associations and costs incurred by insurance guaranty associations *defending the Western Companies against third party liability claims* could reduce the value of its Allowed Claim against the Home estate. The Western Trust did not agree to fund its litigation opponent's efforts to establish that it owes no obligation whatsoever to the Western Trust.

It is undisputed that the Western Trust has *never* submitted a claim arising under the Home insurance policies to CIGA for defense or indemnification. Consequently, no basis exists for the Liquidator to have reduced the value of the Western Trust's Allowed Claim by a single dollar, let alone the hundreds of thousands of dollars in reductions that already have occurred and will continue to occur unless this Court orders the Liquidator to discontinue this practice. Until that happens, money that should compensate asbestos victims instead will be paid to the two law firms that CIGA hired to litigate against the Western Trust in California. This result is contrary to law, contrary to the agreement between the Western Trust and the Liquidator, contrary to basic equitable principles and contrary to the basic "American Rule" of litigation across the

country that parties pay their own legal expenses unless a contract or statute expressly provides otherwise.

The parties agree that this Court is the exclusive venue for any dispute arising out of their settlement agreement (hereinafter, the "Agreement"). Accordingly, the Western Trust respectfully moves the Court for an order disallowing CIGA's claims for reimbursement of its Expenses in the Alameda Action and/or directing the Liquidator to pay the Western Trust's Allowed Claim without any reduction for these Expenses.

## **II. FACTUAL BACKGROUND**

### ***A. The Western Trust.***

The Western Trust was created as a result of the bankruptcy reorganization of the Western Companies. *See In re W. Asbestos Co.*, No. 02-36284 (Bankr. N.D. Cal.). As a result of the reorganization, the Western Trust is responsible for, and holds all rights to insurance policies covering, the asbestos bodily injury liabilities of the Western Companies, including those insurance policies issued by Home (the "Policies") encompassed by the Agreement.

The Western Trust filed a claim in these proceedings seeking in excess of \$1 billion of insurance proceeds for asbestos bodily injury liabilities. The Western Trust's claim was settled for an allowed amount of \$242.5 million (the "Allowed Claim"), an amount far less than Home's actual liability to the Western Companies had Home remained solvent. The Allowed Claim is accorded Class II priority under Section 402-C:44(II) of the New Hampshire Revised Statutes.

In accordance with Section 524(g) of Chapter 11 of the United States Bankruptcy Code, the Western Trust (an asbestos claimants' trust) is funded in pertinent part by the proceeds of the Western Companies' insurance policies. Much like Section 402-C:44 of the New Hampshire Revised Statutes, Section 524(g) requires the Western Trust to reserve funds received from the

Western Companies' insurers to compensate future asbestos claimants in a manner and amount that is substantially similar to the manner in which current claimants have been paid. *See* 11 U.S.C. § 524(g)(2)(B). After taking into account the monies received by the Western Trust as a result of settlements with the Western Companies' insurers, together with the Western Trust's anticipated receipt of funds as a result of its Allowed Claim, the Western Trust currently is able to compensate its beneficiaries at less than 50% of the value of their allowed claims, and has substantial unfunded liabilities for asbestos bodily injury claims that fall within the coverage afforded by the Policies (the "Unfunded Claims").

***B.     The Alameda Action.***

In light of the Unfunded Claims, in February 2013, the Western Trust commenced the Alameda Action wherein it seeks a declaration that it is entitled to obtain payments from CIGA for asbestos bodily injury liabilities (including defense costs) that are covered under the Policies (the "Unfunded Claims," *see supra* § II.A), including reimbursement of amounts that would have been paid on covered claims to date had the Western Trust had access to the Policies. CIGA disputes its statutory obligation to pay the Unfunded Claims on at least the following grounds:

- Western Trust lacks standing to seek funding from CIGA for the Unfunded Claims;
- The funds held in reserve by the Western Trust constitute "other insurance" that preclude a claim against CIGA; and
- CIGA is insulated from liability under its operating statute because Western Trust's settlements with the Western Companies' insurers were for less than policy limits.

*See Snyder v. Cal. Ins. Guar. Ass'n*, 229 Cal. App. 4th 1196, 1205 (2014). Thus, the Alameda Action concerns the construction of CIGA's operating statute (Cal. Ins. Code § 1063) as well as certain characteristics of the Western Trust governed by Section 524(g) of Chapter 11 of the

United States Bankruptcy Code. Significantly, the Western Trust is not seeking a declaration regarding its rights under the Policies. In fact, to date, the Western Trust has not submitted a single claim arising under the Policies to CIGA for reimbursement.<sup>2</sup> *Id.* at 1211. Accordingly, CIGA has incurred no claims handling expenses.

### III. ARGUMENT

#### A. CIGA's Expenses Are Not Claims Handling Expenses.

"[E]xpenses to evaluate and defend against claims for coverage by a policyholder" have been treated as Class I claims in these proceedings (*see In the Matter of the Liquidation of the Home Ins. Co.*, No. 03E0106, 2014 WL 7644664, at ¶ 17, n.3 (N.H. Super. Ct. Sep. 9, 2014)), ostensibly because of Section 404-B:11 of the New Hampshire Revised Statutes, which instructs: "The expenses of [insurance guaranty funds] *in handling claims* shall be accorded the same priority as the liquidator's expenses," which are Class I claims. N.H. Rev. Stat. § 404-B:11(II) (emphasis added); *see also* N.H. Rev. Stat. § 402-C:44(I). The Liquidator has taken the position that CIGA's Expenses in the Alameda Action constitute such claims handling expenses.

The Western Trust disagrees. As discussed above (*see supra* § II), at issue in the Alameda Action is the proper construction of CIGA's operating statute (Cal. Ins. Code § 1063) and certain characteristics of the Western Trust (governed by 11 U.S.C. § 524(g)), not construction of the Policies. *See Snyder*, 229 Cal. App. 4th at 1205. In fact, the record in the Alameda Action (specifically, its appeal to the First District Court of Appeals of the State of California) makes clear that the Western Trust *has not yet submitted a single claim to CIGA arising under the Policies*. *Id.* at 1211 ("There is no specification in [the] complaint of any

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<sup>2</sup> "To preserve a claim for coverage by CIGA, an insured must give CIGA notice of its potential claim by the deadline for filing a claim in the insolvent insurer's liquidation proceedings [which Western Trust has done here] . . . . The time within which the insured must submit its claim for payment, however, does not commence until the insured possesses a 'covered claim' within the meaning of the statute." *Snyder*, 229 Cal. App. 4th at 1213.

amount that Western Trust alleged to be a covered claim, much less any particular asbestos claim giving rise to a liability of The Western Trust covered by a Home policy for which The Western Trust demanded payment from CIGA”); *see also Benson, M.D. v. N.H. Ins. Guar. Ass'n*, 864 A.2d 359, 363 (N.H. 2004) (“Where a plaintiff seeks a declaratory judgment, he is not seeking to enforce a claim against the defendant, but rather a judicial determination as to the existence and effect of a relation between him and the defendant”). Because the Alameda Action does not concern a claim under the Policies, CIGA’s Expenses were not incurred “in handling claims” and therefore do not constitute a proper claim against the Home estate.

**B. CIGA’s Expenses Do Not Reduce the Western Trust’s Allowed Claim.**

Even if CIGA’s Expenses are to be reimbursed from the proceeds of the Home estate (which the Western Trust vigorously disputes), such Expenses do not reduce the Western Trust’s Allowed Claim. To begin, no law permits the Liquidator to make such a reduction. Rather, the Liquidator has taken the position that Section 9B(1) of the Agreement grants him the requisite authority. The Western Trust disputes the Liquidator’s interpretation as contrary to the language of the Agreement as well as the objectives of the priority statute (N.H. Rev. Stat. § 402-C:44).

Section 9B(1) of the Agreement provides:

Claimants acknowledge that, *in the event they pursue any claim under the Policies against any Insurance Guaranty Association, the Insurance Guaranty Association’s expenses of addressing the claim and any recovery may become a claim by the Insurance Guaranty Association in the Home liquidation.* Claimants agree that any judgments, settlements, or other recoveries by claimants from any Insurance Guaranty Association with respect to the Policies (“Recovery” or “Recoveries”) and the Insurance Guaranty Association’s Policies-related expenses incurred after the Effective Date of this Agreement (“Expenses”) shall be deducted from the Recommended Amount [*i.e.*, the Allowed Claim]. In the event of such Expenses or Recovery, the amount allowed as a Class II claim in the Home liquidation shall be the Recommended Amount minus both (i) the Expenses, and (ii) any Recoveries.

Moss Affidavit at ¶ 3, Ex. B (§ 9B(1)) (emphasis added). Thus, under Section 9.B(1) of the Agreement, the Western Trust consented to the Liquidator's reduction of its Allowed Claim to the extent of (i) the Western Trust's Recoveries and (ii) the Insurance Guaranty Association's claims handling expenses – not *all* expenses incurred by an Insurance Guaranty Association. There is certainly nothing in the Agreement that requires the Western Trust to pay the legal fees of a litigation opponent that has chosen for its own purposes to hire two law firms to litigate against the Western Trust.

Reduction of an Allowed Claim to the extent of the Western Trust's receipt of funds from insurance guaranty associations for "covered claims" is consistent with the governing statutory scheme. Subsection 1063.4(b) of the California Insurance Code provides: "Any insured or claimant entitled to the benefits of [Article 1063] who elects to proceed under this article shall be deemed to have assigned to [CIGA] his or her rights against the estate of the insolvent insurer." Cal. Ins. Code § 1063.4(b). Subsection 404-B:11(II) of the New Hampshire Revised Statutes further provides that claims asserted by insurance guaranty associations in their capacity as assignee of the rights of insureds or claimants of insolvent insurers against the assets of the insolvent insurer's estate are accorded "priority equal to that which the claimant would have been entitled . . . against the assets of the insolvent insurer." N.H. Rev. Stat. § 404-B:11(II).

Thus, if the Western Trust's Allowed Claim were not reduced to the extent of its indemnity recoveries from CIGA, the Home estate could be called upon to distribute in duplicate funds pertaining to the same liability arising under the Policies. The agreed-to reduction for "Recoveries" reflected in Section 9B.1 of the Agreement resolves this concern.

The same is true of reductions for "Policies-related expenses," an undefined term. Like indemnity payments, costs incurred by insurance guaranty associations defending insureds



against *third party liability claims* constitute a claim against the Home estate that are accorded “priority equal to that which the claimant would have been entitled . . . against the assets of the insolvent insurer.” N.H. Rev. Stat. § 404-B:11(II).<sup>3</sup> “These two policy benefits, a defense if sued and indemnity for loss, are *policy* obligations of the guaranty association.” *Tex. Prop. & Cas. Ins. Guar. Ass’n v. Webb*, No. 03-99-00293-CV, 2000 Tex. App. LEXIS 905, at \*19-20 (Tex. Ct. App. Feb. 10, 2000) (emphasis in original).

The legal expenses CIGA is incurring in the Alameda Action stand in stark contrast. Unlike costs incurred defending against third-party liability claims, the Expenses were not incurred by CIGA in fulfilling insuring obligations under the Policies. To the contrary, they were expended by CIGA in an effort to *avoid* any obligation to defend or indemnify the Western Trust for claims that would be covered by the Policies but for Home’s insolvency. In fact, because CIGA’s Expenses do not relate to “handling claims,” they do not even constitute a proper claim against the Home estate, let alone a basis for reduction of the Western Trust’s Allowed Claim.

These facts notwithstanding, the Liquidator asserts that CIGA’s Expenses – which the Liquidator has or will reimburse as a *Class I* priority claim (*i.e.*, at 100%) – reduce the Western Trust’s *Class II* priority Allowed Claim even though they are not “Policies-related expenses.” In order to so argue, the Liquidator ignores the mandates in the priority statute to (i) respect the delineation among different classes of claims and (ii) treat all claimants in a given priority class the same. *See* N.H. Rev. Stat. § 402-C:44; *see also* Affidavit of Peter A. Bengelsdorf, Special Deputy Liquidator, in Support of Motion for Approval of Interim Distribution to Claimants with

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<sup>3</sup> Various insurance guaranty associations (including CIGA) contested the Liquidator’s treatment of defense costs as Class II claims, arguing that such expenses should be accorded Class I priority. Ultimately, this dispute was resolved by a court-approved settlement agreement whereby the parties agreed that 90% of defense costs (submitted after March 2013) would be accorded Class II priority, leaving the remaining 10% of defense costs to be treated as Class I claims. *See* Liquidator’s Motion for Approval of Settlement Agreement with Guaranty Funds (dated 6/17/13), ¶ 9 (approved by court on 7/15/13).

Allowed Class II Claims, dated 2/9/12 (“Bengelsdorf Aff.”), ¶ 18 (“the priority statute requires that all claimants in a priority class receive equal treatment”).

In accordance with the priority statute, the Western Trust agreed only that Policies-related expenses would be treated in the same manner as all other Class II claims. Because defense costs are “part of the policyholder benefit” (along with Recoveries), the Western Trust agreed – to the extent an insurance guaranty association incurred costs defending the Western Trust against a third party liability claim arising under the Policies – to allow such costs to reduce its Allowed Claim. *Cf. Application of Va. Prop. & Cas. Ins. Guar. Ass’n*, 2007 S.C.C. Ann. Rept. 72, 2007 WL 831497, at \*8 (Mar. 15, 2007) (“Policy defense costs are typically part of the policyholder benefit”). Had the Western Trust not so agreed, it may have received an unfair advantage vis-à-vis other Class II claimants who did not retain the right to pursue insurance proceeds from insurance guaranty associations.

The Western Trust, however, did not agree to put itself in a worse position than the other Class II claimants. The Liquidator’s construction of the Agreement does just that in requiring amounts that are not part of the policyholder benefit to reduce the Western Trust’s Allowed Claim, while making no similar reduction to other Class II claims. In doing so, the Liquidator effectively seeks to establish a subclass within the Class II claimants in direct contravention of the priority statute. *See* N.H. Rev. Stat. § 402-C:44; *see also* Bengelsdorf Aff. At ¶ 18.

In sum, the Western Trust agreed to allow those amounts insurance guaranty associations claimed against the Home estate *as assignee of the Western Trust* to reduce its Allowed Claim. CIGA, however, has decided to deny that it has any liability at all to the Western Trust, and is asserting a number of statutory defenses in a declaratory relief lawsuit. Because the Western Trust has not obtained any recovery against CIGA under the Policies, and is not seeking a

defense from CIGA under the Policies – in fact, the Western Trust has yet to submit even a single claim against CIGA under the Policies – CIGA could not have been assigned any rights of the Western Trust against the Home estate. *See* Cal. Ins. Code § 1063.4(b). CIGA’s Expenses, according to the Liquidator’s own classification, are not “Policy Related Claims” (Class II) but rather “Administration Costs” (Class I) under the priority statute. Likewise, these amounts are not “Policies-related expenses” under the Agreement and therefore not properly applied to reduce the Western Trust’s Allowed Claim.

**IV. CONCLUSION**


Because CIGA’s Expenses do not constitute a proper claim in these proceedings or Policies-related expenses under the Agreement, the Western Trust respectfully moves the Court for an order disallowing CIGA’s Expenses and/or directing the Liquidator to pay the Western Trust’s Allowed Claim without any reduction for CIGA’s Expenses.

**REQUEST FOR HEARING**

The Western Trust respectfully requests a hearing on this motion.

Respectfully submitted,


WESTERN ASBESTOS SETTLEMENT TRUST  
By Its Attorneys,

  
\_\_\_\_\_  
Jeffrey W. Moss, NH Bar No. 7918  
Morgan, Lewis & Bockius LLP  
One Federal Street  
Boston, Massachusetts 02110  
Tel: 617.341.7700  
Fax: 617.341.7701  
Email: [jmoss@morganlewis.com](mailto:jmoss@morganlewis.com)

Dated: January 27, 2016

**CERTIFICATE OF SERVICE**

I hereby certify that a copy of *The Western Trust's Objection to the Liquidator's Allowance and Treatment of Certain Claims of the California Insurance Guarantee Association* was sent this 27th day of January 2016 by regular mail to all persons on the attached service list.

  
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Jeffrey W. Moss

## SERVICE LIST

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

Gary S. Lee, Esq.  
James J. DeCristofaro, Esq.  
Kathleen E. Schaaf, Esq.  
Morrison & Foerster  
1290 Avenue of the Americas  
New York, New York 10104-0050

Robert A. Stein, Esq.  
The Stein Law Firm, PLLC  
One Barberry Lane  
P.O. Box 2159  
Concord, New Hampshire 03302-2159

David M. Spector, Esq.  
Dennis G. LaGory, Esq.  
Schiff Hardin LLP  
6600 Sears Tower  
Chicago, Illinois 60606

Michael Cohen, Esq.  
Cohen & Buckley, LLP  
1301 York Road  
Baltimore, Maryland 21093

David H. Simmons, Esq.  
Mary Ann Etzler, Esq.  
Daniel J. O'Malley, Esq.  
deBeaubien, Knight, Simmons,  
Mantzaris & Neal, LLP  
332 North Magnolia Avenue  
P.O. Box 87  
Orlando, Florida 32801

Robert M. Horkovich, Esq.  
Robert Y. Chung, Esq.  
Anderson Kill & Olick, P.C.  
1251 Avenue of the Americas  
New York, New York 10020

Martin P. Honigberg, Esq.  
Suloway & Hollis, P.L.L.C.  
9 Capitol Street  
P.O. Box 1256  
Concord, New Hampshire 03302-1256

Richard Mancino, Esq.  
Willkie Farr & Gallagher, LLP  
787 Seventh Avenue  
New York, New York 10019

Joseph G. Davis, Esq.  
Willkie Farr & Gallagher, LLP  
1875 K Street, N.W.  
Washington, D.C. 20006

Albert P. Bedecarre, Esq.  
Quinn Emanuel Urguhart Oliver  
& Hedges LLP  
50 California Street, 22nd Floor  
San Francisco, California 94111

Gerald J. Petros, Esq.  
Hinckley, Allen & Snyder LLP  
50 Kennedy Plaza, Suite 1500  
Providence, Rhode Island 02903

Christopher H.M. Carter, Esq.  
Hinckley, Allen & Snyder LLP  
11 South Main Street, Suite 400  
Concord, New Hampshire 03301

Steven J. Lauwers, Esq.  
Michael S. Lewis, Esq.  
Rath Young Pignatelli  
One Capital Plaza  
Concord, New Hampshire 03302-1500

Andrew B. Livernois, Esq.  
Ransmeier & Spellman, P.C.  
One Capitol Street  
P.O. Box 600  
Concord, New Hampshire 03302-0600

John A. Hubbard  
615 7th Avenue South  
Great Falls, Montana 59405

Paul W. Kalish, Esq.  
Ellen M. Farrell, Esq.  
Timothy E. Curley, Esq.  
Crowell & Moring  
1001 Pennsylvania Avenue, N.W.  
Washington, D.C. 20004-2595

Harry L. Bowles  
306 Big Hollow Lane  
Houston, Texas 77042

Kyle A. Forsyth, Esq.  
Commercial Litigation Branch/Civil Division  
United States Department of Justice  
P.O. Box 875  
Washington, D.C. 20044-0875

Joseph C. Tanski, Esq.  
John S. Stadler, Esq.  
Nixon Peabody LLP  
100 Summer Street  
Boston, Massachusetts 02110

Robert E. Murphy, Esq.  
Michael J. Tierney, Esq.  
Wadleigh, Starr & Peters, PLLC  
95 Market Street  
Manchester, New Hampshire 03101

Mark J. Andreini, Esq.  
Jones Day  
North Point  
901 Lakeside Avenue  
Cleveland, Ohio 44114-1190

J. David Leslie, Esq.  
Eric A. Smith, Esq.  
Rackemann, Sawyer & Brewster, PC  
160 Federal Street  
Boston, Massachusetts 02110-1700

J. Christopher Marshall, Esq.  
New Hampshire Attorney General's Office  
Civil Bureau  
33 Capitol Street  
Concord, New Hampshire 03301-6397

W. Daniel Deane, Esq.  
Nixon Peabody LLP  
900 Elm Street, 14th Floor  
Manchester, New Hampshire 03861