

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

JOEL S. ARIO,
Acting Insurance Commissioner of the
Commonwealth of Pennsylvania,

Plaintiff

v.

RELiance INSURANCE COMPANY,

Defendant

DOCKET NO. 269 M.D. 2001

IN RE: *Commutation, Settlement Agreement and Release between
Reliance Insurance Company (In Liquidation) and Enstar (US) Inc., formerly
known as Castlewood (US) Inc., for and on behalf of Continental Casualty
Company*

Order

AND NOW, this ___ day of _____ 2008, upon consideration of the Liquidator's Petition for Approval of the Commutation, Settlement Agreement, and Release ("Settlement Agreement") between Reliance Insurance Company ("Reliance or Estate") and Enstar (US) Inc., formerly known as Castlewood (US) Inc., for and on behalf of Continental Casualty Company ("Reinsurer") submitted by the Liquidator for Reliance Insurance Company (In Liquidation):

The Court ACCEPTS the Liquidator's representations that the Settlement Agreement is in the best interest of the Reliance Estate, as the Settlement Agreement allows the Liquidator to terminate and commute the Reinsurance Agreement and the Estate will receive an economic benefit amounting to \$10,885,000;

Further, the Court accepts the Liquidator's representations that the Settlement Agreement is a fair and reasonable settlement of the Reinsurer's obligations to the Reliance Estate under its Reinsurance Agreement, and that the payment contemplated under the Settlement Agreement constitutes fair and reasonable value to the Reliance Estate;

2008 FEB 13 10 33 AM
CLERK OF COURT

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

JOEL S. ARIO	:	
Acting Insurance Commissioner of the	:	
Commonwealth of Pennsylvania.	:	
	:	CIVIL ACTION
	:	
Plaintiff	:	
	:	
v.	:	NO. 269 M.D. 2001
	:	
RELIANCE INSURANCE COMPANY,	:	
	:	
Defendant	:	
	:	

2001 FEB 14 10 18 19

21

IN RE: *Commutation, Settlement Agreement and Release between Reliance Insurance Company (In Liquidation) and Enstar (US) Inc., formerly known as Castlewood (US) Inc., for and on behalf of Continental Casualty Company*

LIQUIDATOR'S PETITION FOR APPROVAL OF COMMUTATION, SETTLEMENT AGREEMENT AND RELEASE

Petitioner Joel S. Ario, Acting Insurance Commissioner of the Commonwealth of Pennsylvania, in his capacity as Statutory Liquidator ("Liquidator") of Reliance Insurance Company (In Liquidation) ("Reliance" or "Estate"), respectfully requests that this Court enter an Order approving the Commutation, Settlement Agreement and Release ("Settlement Agreement"), attached hereto as Exhibit A, between Reliance and Enstar (US) Inc., formerly known as Castlewood (US) Inc., for and on behalf of Continental Casualty Company ("Reinsurer").

In support of this petition, the Liquidator avers the following:

1. On October 3, 2001, this Court found Reliance insolvent and appointed the Commissioner as Liquidator of Reliance pursuant to Article V of the Insurance Department Act of 1921, 40 P.S. §221.1 et seq. ("Act"). The Act confers broad powers on the Liquidator to

marshal the assets of Reliance in order to maximize the value of the insolvent insurer's estate for eventual distribution to its policyholders and creditors.

2. The Act authorizes the Liquidator to take such actions as deemed "necessary or expedient to . . . conserve or protect [the insolvent insurer's] assets or property[.]" including the power to "compromise" claims involving assets of the insolvent insurer in order to accomplish or aid in achieving the purposes of liquidation. See 40 P.S. §221.23(6, 9, and 23).

3. One way in which the Liquidator "compromises" claims and "conserves" assets is through commutation. A commutation is a settlement agreement reached between a reinsured and its reinsurer by which the reinsurance obligation is terminated through an agreement by the reinsurer to pay funds that are both due and not yet due under the reinsurance agreement.

4. Prior to entering into a commutation, Reliance takes several steps, including the following, to ensure that the commutation is fair and reasonable to the Reliance Estate and in the best interests of its policyholders, claimants and the general public:

(a) Reliance develops a complete list of reinsurance agreements to be included in the commutation;

(b) Reinsurance accounting specialists for Reliance verify balances and reconcile differences with the reinsurer;

(c) Reliance's claims department reviews ceded case reserves;

(d) Actuaries for Reliance determine the projected ultimate loss, discounted and undiscounted, taking into consideration specific contract features such as reinstatement premiums, sliding scale rates, commission adjustments and/or loss corridors¹ as well as the impact of other applicable reinsurance and off-sets;

¹ A loss corridor is a mechanism contained in certain reinsurance agreements that requires the ceding insurer to be responsible for a certain amount of the ultimate net loss that is above the company's designated retention and below the designated limit, and which would otherwise be reimbursed under the reinsurance

(e) Reliance and the reinsurer exchange commutation proposals and discuss justifications;

(f) Reliance evaluates the commutation proposal based on nominal results, the discounted results, the volatility and trends of the business, disputed issues and any administrative savings; and

(g) Reliance and the reinsurer secure any required approvals.

5. The Liquidator also has established a Commutation Working Group which performs accounting and data reconciliations, actuarial analyses, and claims reviews and analyses. The Commutation Working Group is largely comprised of several key senior management employees each of whom have over 20 years of insurance and reinsurance experience.

6. In addition, the Liquidator has established a Commutation Committee, consisting of the Chief Liquidation Officer, President, and Chief Actuary, who, along with the Vice-President for Commutations and the Executive Vice-President for Reinsurance, review all commutation proposals. Any commutation in excess of \$1,000,000 must be approved by the Commutation Committee.

7. In addition, Reliance's independent consulting actuaries, PricewaterhouseCoopers, have reviewed Reliance's commutation approach both generally and with respect to individual transactions and have concluded that Reliance's process to estimate liabilities ceded to reinsurers is reasonable for commutation purposes.

8. Commencing on December 31, 1997 and ending on December 30, 1998, 2000, Reliance and the Reinsurer entered into the "Underlying Workers Compensation Excess of Loss Reinsurance Agreement" ("Reinsurance Agreement"). Excess of loss reinsurance is

agreement. A loss corridor is usually expressed as a loss ratio percentage of the reinsurer's earned premium, or a combined ratio if the reinsurance agreement provides for a ceding commission to the company. Loss corridors are employed to mitigate the volatility of reinsurance agreements.

purchased by primary insurers to protect against individual losses that exceed a particular retention amount. This protection attaches once the primary carrier's per loss retention amount is exceeded. In this instance, the Reinsurance Agreement provides Reliance with protection in the amount of \$500,000 in excess of Reliance's \$500,000 per loss retention. Accordingly, the most that Reliance can recover under the Reinsurance Agreement for any one loss is \$500,000. However, the total amount that Reliance can recover under the Reinsurance Agreement for all losses is unlimited. Reliance entered into the Reinsurance Agreement to protect the results of workers compensation accounts written through its Commercial Lines, Large Accounts and Specialty Divisions. The policies subject to the Reinsurance Agreement include workers compensation business written in nearly every state and covering nearly every occupation.

9. Large workers compensation claims pay out over the lifespan of the claimants, which may be as long as 40 or more years from the date of the accident. As part of its due diligence, senior Reliance actuarial and claims personnel conducted a review of relevant claims under the Reinsurance Agreement in order to both verify the accuracy of the reserves and to project the timing of payments for each relevant claim. Appropriate annual medical cost escalation rates were included in these projections. Reliance's actuaries then used the results of this work to project both the payment stream of losses subject to the Reinsurance Agreement and a range of ultimate commutation values for these losses.

10. With the benefit of such due diligence, Reliance was able to negotiate a settlement for the remaining exposure under the Reinsurance Agreement and entered into the Settlement Agreement effective December 21, 2007, subject to the approval of this Court. The Settlement Agreement settles with certainty the claims against the Reinsurer for losses under the Reinsurance Agreement.

11. Specifically, the Settlement Agreement provides that the Reinsurer shall pay Reliance the sum of \$10,885,000 ("Commutation Amount") to commute the Reinsurance

Agreement. The Commutation Amount was negotiated with the Reinsurer, and the Liquidator has taken the necessary steps to determine, and has concluded, that the terms of the Settlement Agreement are fair and reasonable to the Reliance Estate and in the best interests of its policyholders, claimants and the general public. See 40 P.S. §§221.1(c), 221.23(9).

12. Based on the analysis of the terms of the Settlement Agreement, and the evaluation of the transaction as a whole by the Liquidator's staff and Reliance staff members familiar with the business dealings under the Reinsurance Agreement, the Liquidator has determined that payment of the Commutation Amount by the Reinsurer is a fair and reasonable commutation of the Reinsurer's obligations to Reliance under the Reinsurance Agreement.

13. Keith Kaplan, Executive Vice President for Reinsurance at Reliance, is responsible for all facets of ceded and assumed reinsurance at Reliance including accounting, billing, claims, commutations, coverage analysis, and dispute management. He has specific knowledge regarding the risks to the Estate of attempting to collect reinsurance through billing, negotiation or the dispute resolution process. As set forth in his Confidential Affidavit (attached as "Sealed Exhibit B"), Mr. Kaplan has identified several specific advantages to the Estate arising from the consummation of the transaction memorialized in the Settlement Agreement.

14. The Settlement Agreement will further achievement of the liquidation objectives under the Act. The commutation transaction will assist the Liquidator in marshalling and maximizing Reliance's immediately available assets while minimizing any unavoidable loss to policyholders, claimants and creditors resulting from the Reliance insolvency and hazardous financial condition. See 40 P.S. §221.1(c).

15. First, the Settlement Agreement converts future reinsurance obligations into immediate cash for the Estate. Specifically, the Reliance Estate receives \$10,885,000 which can be invested until it is distributed.

16. Second, the Settlement Agreement eliminates both the internal and external administrative costs associated with continued reporting and collection efforts, including legal fees.

17. Third, this commutation eliminates any potential future credit risk associated with collection of the reinsurance proceeds in the event that the reinsurer becomes insolvent.

18. Fourth, no person or firm has earned or will earn any contingent fee or extra remuneration of any type as a result of this transaction.

19. Under the terms of the Settlement Agreement, the Commutation will be fully consummated upon satisfaction of the following conditions: (a) execution of the Settlement Agreement by an authorized representative of the Liquidator; (b) execution of the Settlement Agreement by an authorized representative of the Reinsurer; (c) approval of the transaction by this Court; and (d) appropriate notice to the Reinsurer of Court approval.

WHEREFORE, the Liquidator respectfully requests that this Court enter an Order in the form attached hereto:

(a) Finding that the Settlement Agreement and Commutation Amount are in the best interest of the Reliance Estate;

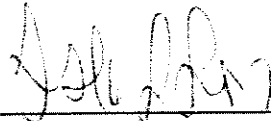
(b) Finding that the Settlement Agreement is a fair and reasonable settlement of the Reinsurer's obligations under the Reinsurance Agreement;

(c) Finding the payment contemplated by the Settlement Agreement constitutes fair and reasonable value to the Reliance Estate; and

(d) Approving the terms of the Settlement Agreement attached as Exhibit A and authorizing the Liquidator to take such actions as are necessary to consummate the Settlement Agreement as approved.

Respectfully submitted,

PEPPER HAMILTON LLP



DEBORAH F. COHEN

ISLA L. LONG

3000 Two Logan Square

18th and Arch Streets

Philadelphia, PA 19103-2799

(215) 981-4000

Attorneys for Joel S. Ario, Acting Insurance
Commissioner of the Commonwealth of
Pennsylvania, in his official capacity as Statutory
Liquidator of Reliance Insurance Company

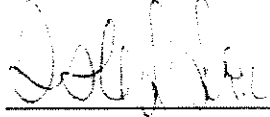
Dated: February 13, 2008

CERTIFICATE OF SERVICE

I hereby certify that on February 13, 2008 a true and correct copy of the Liquidator's Petition for Approval of Commutation, Settlement Agreement And Release was served upon the following:

Via Notice of Filing

Members of Reliance Master Service List



ISLA L. LONG

VERIFICATION

I, David S. Brietling, Chief Liquidation Officer for Reliance Insurance Company, in liquidation, am authorized by Joel S. Ario, Acting Insurance Commissioner of the Commonwealth of Pennsylvania, pursuant to 40 P.S. §221.23, to act on his behalf in his capacity as the Statutory Liquidator of Reliance Insurance Company. I hereby verify that the facts set forth in the foregoing pleading are true and correct to the best of my knowledge, information and belief.

I understand that this Verification is made subject to the penalties of 18 P.S. §4904 relating to unsworn falsification to authorities.

Executed on February 11, 2008



DAVID S. BRIETLING

COMMUTATION, SETTLEMENT AGREEMENT AND RELEASE

THIS COMMUTATION, SETTLEMENT AGREEMENT AND RELEASE ("Agreement"), made effective and entered into this 21st day of December, 2007, by and between Enstar (US) Inc., f/k/a Castlewood (US) Inc., for and on behalf of Continental Casualty Company (hereinafter known as the "Reinsurer") and Joel S. Ario, Acting Insurance Commissioner of the Commonwealth of Pennsylvania, in his capacity as Statutory Liquidator of Reliance Insurance Company (In Liquidation) (hereinafter known as the "Cedant"). David S. Brietling, Chief Liquidation Officer, is acting on behalf of Joel S. Ario, who is acting on behalf of the Cedant pursuant to the powers granted to him under Title 40, Purdon's Statutes, Section 221.20, et seq. and other applicable statutes, regulations and laws.

RECITALS

A. The Reinsurer and the Cedant entered into a certain contract of reinsurance wherein the Reinsurer obligated itself to accept from the Cedant the cession of a certain percentage of liabilities with respect to risks written or assumed by the Cedant and/or agents of the Cedant, and;

B. The reinsurance agreement referred to in Recital A above is set out on Exhibit A attached hereto and is herein referred to as "the Contract", and;

C. Pursuant to the Contract, there are loss developments, the total amount of which are not fully known, or not yet capable of determination, representing liabilities which are or may come due from the Reinsurer to the Cedant, and;

D. The parties hereto recognize and understand that, based upon current economic projections, a substantial portion of the Reinsurer's obligations to the Cedant may become payable in the future rather than at present; that the Reinsurer's future liabilities and obligations to the Cedant pursuant to the Contract have been evaluated, but cannot be determined in an amount certain at this time; and that a settlement and commutation of the Reinsurer's obligations

to the Cedant based upon present calculations of outstanding losses, including incurred but not reported losses, will eliminate the uncertainty of contingent liabilities for presently unresolved or unasserted claims, and;

E. The Reinsurer and the Cedant agree that it is in each of their best interests and in the best interests of their respective policyholders and creditors to adjust and settle their differences and to enter into this Agreement.

NOW THEREFORE, in consideration of the mutual benefits to be received by the parties hereto and the mutual covenants and agreements herein contained, the parties hereto hereby agree as follows:

Commutation of Reinsurance Agreement

1. Subject to the receipt by the Cedant of the Consideration as set out in Article 4 herein, together with any collection expenses and accrued interest due as is more particularly described in Article 8 (c) and 9 below, and in further consideration of the release contained in Article 2 herein the Cedant hereby irrevocably releases the Reinsurer, its predecessors, successors, assigns, shareholders, officers, directors, agents, sub-agents, brokers and sub-brokers from One Hundred Percent (100%) of all adjustments, obligations, liabilities, offsets, actions, causes of action, proofs of claim, suits, debts, sums of money, accounts, reckonings, bonds, bills, covenants, contracts, conversions, costs, agreements, promises, damages, expenses, judgment claims, and demands whatsoever, whether known or unknown, suspected or unsuspected, by either or both parties, fixed or contingent, arising out of, or in connection with the Reinsurer's participation on the Contract, whether or not such contract is void or voidable.

Release of the Cedant

2. In consideration of the release set out in Article 1 herein, the Reinsurer hereby irrevocably releases the Cedant, its predecessors, successors, assigns, shareholders, officers, directors, receivers, liquidators, administrators, agents, sub-agents, brokers and sub-brokers from

One Hundred Percent (100%) of all adjustments, obligations, liabilities, offsets, actions, causes of action, proofs of claim, suits, debts, sums of money, accounts, reckonings, bonds, bills, covenants, contracts, conversions, costs, agreements, promises, damages, expenses, judgment claims, and demands whatsoever, whether known or unknown, suspected or unsuspected, by either or both parties, fixed or contingent, arising out of, or in connection with the participation of the Cedant on the Contract, whether or not such contract is void or voidable.

Warranties

5. To the best information and belief of each of the parties to this Agreement, the following express warranties apply:

a. There are no pending agreements, transactions, negotiations, regulatory actions or lawsuits in which any of the parties are involved nor are there any threatened regulatory actions or lawsuits of which any of the parties are aware that would render this Agreement or any part thereof void, avoidable, or unenforceable;

b. No party hereto has transferred, assigned, or contracted to transfer or assign to any person, corporation, company or entity any of its rights, title, benefit or obligations directly arising out of or in connection with the Contract, including without limitation any balances, accounts, costs, claims, counterclaims or demands which are within the contemplation of this Agreement;

c. The Reinsurer has not commuted or otherwise settled with or contracted to commute or settle with any person, corporation, company or entity any of their respective rights, title, benefit or obligations directly arising out of or in connection with the Contract, including without limitation any balances, accounts, costs, claims, counterclaims or demands which are within the contemplation of this Agreement;

Consideration

4. The Reinsurer agrees to pay the Cedant the total sum of Ten Million Eight Hundred Eighty Five Thousand United States Dollars and No Cents (US\$10,885,000.00) ("the Consideration"). Said payment shall be made no later than ten (10) calendar days following notice to the Reinsurer by facsimile of the execution of this Agreement by the Cedant or its assignee and the approval of the Agreement by the Commonwealth Court of Pennsylvania in accordance with Article 16 herein ("the Completion Date"). Notwithstanding the foregoing, if the ten (10) day period expires on a weekend or a holiday, then the transfer must be completed by the end of the next business day. Notwithstanding anything to the contrary in this Agreement, in no event shall the payment to be made by Reinsurer to Cedant be due before February 1, 2008. Reinsurer shall transfer the Consideration to the following account:

Name of Bank:	Mellon Bank Pittsburgh, PA
ABA Number:	043000261
Credit:	Reliance Insurance Company
CHIPS No.:	044840
Account Number:	079-7806
S.W.I.F.T.:	MELN US 3P
Ref:	Kathy Lee

The parties also agree that any claim recoveries including but not limited to salvage and subrogation, any escrow funds with third party claim administrators and any unemitted cash with intermediaries that relates to the Contract is the property of the Cedant.

Successors and Assigns

5. This Agreement shall inure to the benefit of and bind the Reinsurer and its successors and assigns and the Cedant and their respective successors and assigns.

Independent Investigation

6. Each of the parties acknowledges that it has entered into this Agreement in reliance upon its own independent investigation and analysis of the Contract and its respective rights and obligations thereunder, and not on the basis of any representation made or not made by the other party hereto. Each of the parties further acknowledges that it has read this Agreement, that it has had the opportunity to discuss it with legal counsel, and that it fully understands all of the terms herein.

Integration and Waiver

7. This Agreement shall constitute the entire agreement between the parties pertaining to the subject matter hereof, and supersedes any and all prior or contemporaneous understandings or agreements. No supplement, modification, waiver or termination hereof shall be binding or enforceable unless executed in writing by the parties to be bound thereby. No delay, omission or forbearance on the part of any party to this Agreement in exercising or enforcing any right, power or remedy under this Agreement shall impair such right, power or remedy or operate as a waiver thereof. The single or partial exercise or enforcement of such right, power or remedy shall not preclude any other or further exercise or enforcement thereof or of any other right, power or remedy. The rights, powers and remedies provided in this Agreement are cumulative and not exclusive of any rights, powers and remedies provided by law.

Remedies

8. In the event that the Reinsurer fails to pay the Consideration to the Cedant by the

later of the Completion Date or February 1, 2008, the Cedant shall have all rights and remedies available at law or in equity. In addition, the Cedant shall have the express right to

a. deem the entire Agreement null and void by notice in writing to the Reinsurer per Article 11 herein and to seek recovery of all sums due or to become due under the Contract, or;

b. bring suit on the Agreement including interest on the agreed-upon but unpaid amount as set out in Article 8(c).

c. Without prejudice to the Cedant's rights to rescind this Agreement pursuant to Article 8(a) above, if Reinsurer does not pay all of the Consideration recited herein to the Cedant by the later of the Completion Date or February 1, 2008, the Reinsurer shall pay interest on any unpaid sums at a rate which is equal to one percentage point (1.00%) over the Prime Rate (the base rate on corporate loans at large U.S. money center commercial banks) as published in *The Wall Street Journal*, but in no event shall said interest be calculated at less than six percent (6%) per annum.

Expenses of Collection

9. Subject to the provisions of Article 8(c) herein, if the Reinsurer fails to pay the Consideration to the Cedant by the later of the Completion Date or February 1, 2008, Reinsurer agrees to reimburse the Cedant for all reasonable expenses including, without limitation, attorney fees which are incurred by the Cedant in the enforcement of this Agreement and collection of the consideration together with any interest accrued upon such reasonable expenses from the date of payment of such expenses at the rate set out in Article 8(c) above.

Choice of Laws

10. The performance and interpretation of this Agreement shall be governed by the laws of the Commonwealth of Pennsylvania with respect to any dispute arising under this Agreement between the Reinsurer and the Cedant;

Notices

11. All notices required under this Agreement shall be as follows:

a. Any notice or other communication under or in connection with this Agreement shall be in writing and shall be delivered personally or sent by first class post/mail (or by air mail if overseas) or by overnight courier service, to the addresses of the parties as set out in Exhibit B attached hereto or to such other person or address as any party may specify by notice in writing to the others.

b. In the absence of evidence of earlier receipt, any notice or other communication shall be deemed to have been duly served if (i) sent by first class post on the second business day after posting; (ii) sent by overnight courier on the next business day after mailing (iii) sent by air mail, six (6) days after posting, and; (iv) if delivered personally, when left during normal business hours at the address set out in Exhibit B or any alternative address specified by the receiving party.

Interpretation

12. The language of this Agreement is the result of negotiation between all parties hereto, and any ambiguities in said language shall not be presumptively construed against or in favor of any party or parties hereto.

Execution and Approval

14. Except as disclosed in Article 16, each party to this Agreement represents that it is authorized to enter into this Agreement and the transactions contemplated herein.

15. Except as disclosed in Article 16, each signatory to this Agreement represents that said signatory is authorized and empowered to execute this Agreement and the transactions contemplated herein and that any and all required corporate approval on behalf of the Reinsurer has been properly executed and that the Agreement is entered into voluntarily.

16. With respect to the Cedant, this Agreement is subject to final approval by the Commonwealth Court of Pennsylvania (the "Court"), which has jurisdiction over the liquidation of Cedant. Upon execution by all parties hereto, the Liquidator of Cedant shall promptly make application to the Court to secure said approval. In the event the Court does not approve this Agreement, then upon such notice of disapproval, the Liquidator of Cedant shall notify the Reinsurer and this Agreement will become null and void and have no further force or effect as between the Reinsurer and the Cedant.

17. This Agreement may be signed and exchanged in counterpart by facsimile and this Agreement as so signed and exchanged will constitute the binding Agreement of the parties.

IN WITNESS WHEREOF, the parties have hereunto set their hands as of the dates set forth.

RELIANCE INSURANCE COMPANY (In Liquidation)

By: *Lucas Brattley*
Title: *Chief Liquidation Officer*
Date: *1/24/08*

**ENSTAR (US) INC., f/k/a CASTLEWOOD (US) INC.,
for and on behalf of CONTINENTAL CASUALTY COMPANY**

By: *James Aragoni*
Title: *Executive Vice President*
Date: *1/14/08*

Reliance CRA Court Approval Execution

EXHIBIT A

Reinsurer	Reliance Ref.	Enstar Ref.	Treaty	Eff. Dates	Participation
Continental Casualty Company	32U	2198	WC Underlying XOL	12/31/97-12/30/98	100%

EXHIBIT B

For Reliance/The Liquidator

Keith Kaplan
Reliance Insurance Company (In Liquidation)
Three Parkway
Philadelphia, PA 19102
Tel. 215-864-4250
Fax 215-864-1077

For Reinsurer

Enstar (US) Inc.
7901 4th Street North, Suite 203
St. Petersburg, FL 33702
Attn: James Grajewski, EVP
Tel: 727-576-1632, Ext. 203
Fax: 727-576-3627