

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

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

Plaintiff,

v.

RELiance INSURANCE COMPANY,

Defendant.

No. 269 M.D. 2001

2009 DEC 29 A 11:58

RECEIVED AND FILED
COMMONWEALTH COURT
OF PA (PHILA)

RE: LIQUIDATOR'S PETITION TO SUPPLEMENT
THE FIRST AGGREGATE ORDER

ORDER

AND NOW, THIS _____ day of _____, 2010, upon consideration of the Liquidator's Petition to Supplement the Court's November 19, 2007 First Aggregate Order ("Petition") filed by Joel S. Ario, Insurance Commissioner of the Commonwealth of Pennsylvania, in his official capacity as Statutory Liquidator ("Liquidator") of Reliance Insurance Company ("Reliance"), it is hereby ORDERED and DECREED that:

1. A decrease in the 60% First Safety Factor Percentage is approved and the new Second Safety Factor Percentage of 40% is approved for any future distributions on Aggregate NODs;

2. Claimants under Aggregate Policies who received their first 20% distribution payments subject to the 60% First Safety Factor Percentage will receive another distribution payment to compensate them for the reduction in the Safety Factor Percentage and any future distribution payments made to them thereafter will be subject to the Second Safety Factor Percentage; and

3. The calculation methodology approved in the First Aggregate Order of November 19, 2007, as amended by the Second Safety Factor Percentage will continue to be applied to any distribution on claims under Aggregate Policies.

BY THE COURT:

BONNIE BRIGANCE LEADBETTER,
President Judge

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

JOEL S. ARIO, Insurance Commissioner of
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RELiance INSURANCE COMPANY,

Defendant.

No. 269 M.D. 2001

RECEIVED AND FILED
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2009 DEC 29 A 11:58

**LIQUIDATOR'S PETITION TO SUPPLEMENT
THE COURT'S NOVEMBER 19, 2007 FIRST AGGREGATE ORDER**

Petitioner, Joel S. Ario, Insurance Commissioner of the Commonwealth of Pennsylvania, in his official capacity as Statutory Liquidator ("Liquidator") of Reliance Insurance Company ("Reliance or Estate"), petitions the Court for an Order to supplement the November 19, 2007 Aggregate Order. In support of the Liquidator's Petition to Supplement the Court's November 19, 2007 Order ("Petition"), the Liquidator avers as follows:

Background Regarding the Liquidation of Reliance

1. On May 29, 2001, this Court entered a Rehabilitation Order with respect to Reliance pursuant to Article V of the Pennsylvania Insurance Department Act, 40 P.S. §§221.1 – 221.63 ("Act") and appointed the Pennsylvania Insurance Commissioner as Rehabilitator.
2. This Court subsequently terminated the rehabilitation of Reliance and, by Order dated October 3, 2001, declared Reliance to be insolvent; issued a Liquidation Order pursuant to 40 P.S. §§221.18 and 221.20; appointed the Pennsylvania Insurance Commissioner as Liquidator

of Reliance; ordered the Liquidator to take possession of all Reliance property; and authorized the Liquidator to liquidate the business and affairs of Reliance.

3. The Liquidator is statutorily charged with the duties of identifying, marshaling and liquidating assets of the Estate; processing and evaluating claims to determine the liabilities of the Estate; and distributing assets to the Claimants¹ of the Estate in accordance with the mandates set forth in the Act.

4. The Liquidator's Petition to Supplement the Court's September 9, 2002 Claims Procedures Order, filed on June 22, 2006, asked this Court for an Order requiring Claimants who had not yet received Notices of Determination ("NODs") to submit complete information about their Proofs of Claim ("POCs") within specific time frames, including annual claim reports, and authorizing the Liquidator to subordinate to class (g) priority any POCs for which the required information was not provided timely. On May 1, 2007 and November 27, 2007, this Court issued two Orders (Claims Information Orders) requiring Claimants to submit complete information regarding their POCs within specific time frames as requested by the Liquidator, and ultimately requiring the Liquidator to subordinate to class (g) priority any POC for which the information was not provided. The information submitted pursuant to those Claims Information Orders allowed the Liquidator to address several thousand pending POCs and to establish appropriate case reserves for individual claims. As of September 30, 2009, the Liquidator has now addressed more than 94% of the 159,750 POCs filed with Reliance.

5. On July 27, 2007, the Liquidator filed a Petition to Supplement the Court's December 9, 2002 Claims Procedures Order to Address Claims Under Aggregate Policies ("First

¹ In this Petition, "Claimants" will be used to refer to policyholders, insureds, third party claimants and other creditors, collectively.

Aggregate Petition”) and this Court approved the First Aggregate Petition by its Order dated November 19, 2007 (“First Aggregate Order”). The First Aggregate Order approved the methodology outlined in the First Aggregate Petition for calculating any distribution to Claimants with POCs under Aggregate Policies² and approved a percentage to be applied in any distribution to Aggregate NODs to hold back a portion of the Aggregate Limits for any future claims development (“Safety Factor Percentage”).

6. The Liquidator files quarterly status reports with the Commonwealth Court which provide detailed information regarding, among other things, the financial condition of Reliance and the claims process (“Quarterly Reports”). These Quarterly Reports are available on the Reliance Documents website at www.reliancedocuments.com.

7. Subject to the caveats regarding financial information in the Quarterly Reports and in the Notes to the Special Purpose Financial Statements attached as an exhibit to the Quarterly Reports, total estimated assets for Reliance as of September 30, 2009 were \$5.5 billion. Total estimated liabilities were \$9 billion, leaving an estimated net deficit of \$3.5 billion. The liquid investment portfolio, as of September 30, 2009, totaled \$2.0 billion which will provide sufficient cash for a reduction in the Safety Factor Percentage as proposed in this Petition.

8. In conjunction with this petition, the Liquidator is filing a petition for approval of an increase in the distribution percentage and a petition for approval of a fifth early access proposal for Guaranty Associations (“GAs”). The Liquidator has determined that neither the Petition for Second Interim Distribution nor the Petition To Approve Liquidator’s Fifth Proposal

² Many Reliance liability policies have an aggregate limit (“Aggregate Policies”). An “Aggregate Limit” is a provision in a policy that limits the maximum liability of an insurer under that policy. For example, if during the

To Distribute Assets To State Guaranty Associations will adversely affect this recommendation for a reduction in the Safety Factor Percentage. The Liquidator believes that, based on current financial information, both the early access and interim distributions are feasible, as well as a revision in the calculation methodology for distributions on claims under aggregate policies.

First Safety Factor Percentage

9. The First Aggregate Order authorized the Liquidator to continue issuing NODs (“Aggregate NODs”) to Claimants with claims under Aggregate Policies (“Aggregate POCs”) advising the Claimants that any allowed amount stated in their Aggregate NOD is subject to 40 P.S. §221.40(d) which provides, in part, that:

(d) In the event several claims founded upon one policy are filed, whether by third parties or as claims by the insured under this section, and the aggregate allowed amount of the claims to which the same limit of liability in the policy is applicable exceeds that limit, then each claim as allowed shall be reduced a proportionate amount so that the total equals the policy limit. . . .

The First Aggregate Order approved a 60% Safety Factor Percentage (“First Safety Factor Percentage”) which would provide a safety margin for any future developments with pending Aggregate POCs and any late filed Aggregate POCs with good cause, as well as any development on claims handled by GAs under Aggregate Policies. The First Aggregate Order also required the Liquidator to consider, for future distributions, whether the First Safety Factor Percentage should be adjusted.

10. The selection of the First Safety Factor Percentage was based on several factors, primarily:

policy term, there are losses totaling \$5,000,000 from several occurrences, but there is a policy aggregate limit of \$3,000,000, the insurer would not be liable for more than \$3,000,000 for that policy period.

- a. a review of the distribution scenarios for Aggregate NODs under various Safety Factor Percentages;
- b. the extent to which the Aggregate Limits had been eroded for all Aggregate Policies including related allowed amounts for Aggregate NODs;
- c. the number of pending Aggregate POCs that reflect contingent claims or for which insufficient information has been provided;
- d. the type and number of Aggregate POCs that are still being filed even after the claim filing deadline of December 31, 2003; and
- e. the number of claims under Aggregate Policies which are being handled by insureds and for which the Liquidator may have limited information.

Reduction of the First Safety Factor Percentage

11. In connection with the analysis undertaken to recommend an increase in the interim distribution percentage to this Court, the Liquidator again reviewed the factors included in the above paragraph, along with subsequent claims experience since the initial selection and current outstanding reserves, to determine whether the First Safety Factor Percentage should be adjusted.

12. At this time, based on the following factors, the Liquidator is recommending a reduction in the 60% First Safety Factor Percentage to 40% ("Second Safety Factor Percentage"):

- a. A reserve review and certification process conducted by the Reliance Claims Department during 2007 and 2008, with information obtained through the Claims Information Orders, resulted in more reliable, updated case reserves for the Aggregate POCs. Significant claims are now recertified on a regular basis.

b. The information provided by Claimants in response to the Claims Information Orders allowed the Reliance Claims Department to address many Aggregate POCs resulting in a substantial reduction in the number of open Aggregate POCs;

c. An independent actuarial review conducted as of September 30, 2008 by PricewaterhouseCoopers LLP indicated a small reduction in the overall expected ultimate liabilities and did not reveal new areas of significant concern;

d. The Pennsylvania Supreme Court confirmed the Liquidator's determination of priority classification for subrogation claims as class (g); and

e. An updated analysis of the extent to which the Aggregate Limits had been eroded for all Aggregate Policies, including related allowed amounts for Aggregate NODs, was reviewed. The analysis indicated some additional erosion of available coverage within the Aggregate Limits, but not an unexpected result.

13. Despite the factors outlined above, there is still a risk that unanticipated development on Aggregate Policies will occur, and even despite the 40% Second Safety Factor Percentage, excess distributions could occur on particular Aggregate NODs which the Liquidator would not be able to recover. New Aggregate POCs will continue to be received, despite the claims filing deadline; new information will continue to be received on pending Aggregate POCs; and unexpected developments could occur regarding the priority classification of Aggregate POCs. In addition, the GAs will continue to handle certain claims under Aggregate Policies and subsequent adverse development is possible for those claims. However, the Liquidator believes that the proposed reduction in the Safety Factor Percentage achieves a reasonable balance between the "expeditious completion of the liquidation and the protection of unliquidated and undetermined claims" set forth in 40 P.S. §221.46.


14. If this Court approves the Second Safety Factor Percentage, Claimants under Aggregate Policies who received their first 20% distribution payments subject to the 60% First Safety Factor Percentage will receive another distribution payment to compensate them for the reduction in the Safety Factor Percentage. This will result in a further distribution of approximately \$12.8 million to those Claimants as of September 30, 2009. Claimants under Aggregate Policies who receive their first distribution payments after any Order approving the Second Safety Factor Percentage will receive a distribution based on the Second Safety Factor Percentage.

15. The distribution amounts for Aggregate NODs will continue to be calculated according to the methodology approved by the First Aggregate Order, except for the change in the Safety Factor Percentage, as demonstrated in Exhibit A to this Petition.


WHEREFORE, the Liquidator respectfully requests that this Court grant this Petition and Order as follows:

- a) A decrease in the 60% First Safety Factor Percentage is approved and the new Second Safety Factor Percentage of 40% is approved for any future distributions on Aggregate NODs;
- b) Claimants under Aggregate Policies who received their first 20% distribution payments subject to the 60% First Safety Factor Percentage will receive another distribution payment to compensate them for the reduction in the Safety Factor Percentage. Any future distribution payments to them thereafter will be subject to the Second Safety Factor Percentage;
- c) The calculation methodology approved in the First Aggregate Order, as amended by the Second Safety Factor Percentage, will continue to be applied to all distributions on claims under Aggregate Policies.

Respectfully submitted:

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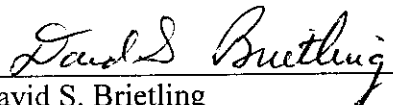
Dated: December 29, 2009

VERIFICATION

I, David S. Brietling, have been retained by the Insurance Commissioner of the Commonwealth of Pennsylvania, and am responsible for the on-site insurance and financial operations of Reliance Insurance Company (in Liquidation) as Chief Liquidation Officer. I am authorized by the Insurance Commissioner to make this verification on behalf of the Liquidator of Reliance Insurance Company. I hereby verify that the facts set forth in the foregoing Petition 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.

Date: December 29, 2009



David S. Brietling
Chief Liquidation Officer

CERTIFICATE OF SERVICE

I, Marilyn K. Kincaid, hereby certify that on or about this day, pursuant to the Court's Order of December 12, 2008, service of the foregoing Petition was provided through the transmission of a Notice of Filing and through posting of a true and correct copy in PDF file format on the Reliance Documents website (www.reliancedocuments.com) to:

The attached Master Service List

The attached Claim Objector List

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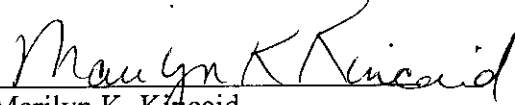
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Dated: December 29, 2009


Marilyn K. Kincaid

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v.

Reliance Insurance Company

No. 269 M.D. 2001 (Commonwealth Court of Pennsylvania)

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EXHIBIT A

EXAMPLES OF DISTRIBUTIONS ON NODS UNDER AGGREGATE POLICIES

	POLICY A NOD Allowed Amounts Erode Aggregate 100%	POLICY B Total Incurred Amounts Erode Aggregate <u>Below</u> Aggregate Allocation Amount	POLICY C Total Incurred Amounts Erode Aggregate <u>Above</u> Aggregate Allocation Amount
<p>The aggregate limits originally available under the policy are first reduced by the dollar amount of claims paid prior to liquidation to determine the Aggregate Amount Remaining for post liquidation claims. The Safety Factor Percentage of 40% is then applied to the Aggregate Amount Remaining to determine the Safety Factor Amount to be held back from the distribution. This reserved amount provides a safeguard for the development of known and unknown claims against the Estate for each policy.</p>			
a. Aggregate amount per policy term	\$10,000,000	\$3,000,000	\$10,000,000
b. Claims paid by Reliance prior to liquidation	NONE	\$350,000	\$5,900,000
c. Aggregate Amount Remaining for post liquidation claims (a – b)	\$10,000,000	\$2,650,000	\$4,100,000
d. Safety Factor Percentage	40%	40%	40%
e. Safety Factor Amount (c x d)	\$4,000,000	\$1,060,000	\$1,640,000
f. Aggregate Allocation Amount (c – e)	\$6,000,000	\$1,590,000	\$2,460,000
<p>The following section shows all Post Liquidation Amounts incurred under the policy: claims that have been paid by the GAs; all outstanding reserves on the books of Reliance which includes pending GA claims and POCs not yet evaluated; and total NOD allowed amounts, whether or not approved by the Court.</p>			
g. Claims paid by GAs post liquidation	NONE	NONE	\$90,000
h. Outstanding reserve which includes pending GA claims, pending POCs and all outstanding reserves	NONE	\$75,000	\$54,000
i. Total NOD allowed amounts	\$10,000,000	\$425,000	\$4,750,000
j. Post Liquidation Amounts (g + h + i)	\$10,000,000	\$500,000	\$4,894,000
<p>The Aggregate Allocation Amount is then divided by the Post Liquidation Amounts to determine the Aggregate Pro Rata Percentage for each policy to be applied to each Aggregate NOD under that policy. Application of the Aggregate Pro Rata Percentage effectively holds back 40% of the Aggregate Amount Remaining for Unevaluated POCs and creates a Revised Allowed Amount for each Aggregate NOD.</p>			
k. Aggregate Pro Rata Percentage to be applied to each court approved NOD allowed amount under policy (f ÷ j)	60%	result is greater than 100%, so 100% is applied	50.3%
l. NOD allowed amounts	\$10,000,000	\$425,000	\$4,750,000
m. Revised Allowed Amounts (l x k)	\$6,000,000	\$425,000	\$2,387,617
<p>Then the overall distribution percentage that will be approved by the Court is applied to the class b NOD Revised Amount to result in the First Distribution Amount for each Aggregate NOD. The First Distribution Amount for each Aggregate NOD divided by the total Aggregate NOD allowed amounts under that policy will show the actual distribution percentage for each Aggregate NOD under each aggregate policy.</p>			
n. Overall distribution percentage approved by Court	20%	20%	20%
o. First Distribution Amount (m x n)	\$1,200,000	\$85,000	\$477,523
p. Actual distribution percentage for Court approved NODs under specific aggregate policies, applying Safety Factor Percentage and depending on aggregate erosion (o ÷ l)	12%	20%	10%