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Superior Court Of California
County Of Los Angeles

JUL 02 2012

John A. Clarke, Executive Officer/Clerk
By: Robin Sanchez, Deputy

SUPERIOR COURT OF THE STATE OF CALIFORNIA
COUNTY OF LOS ANGELES - CENTRAL CIVIL WEST

INSURANCE COMMISSIONER OF THE
STATE OF CALIFORNIA,

Applicant,

v.

FREMONT INDEMNITY COMPANY,

Respondent.

CASE NO. BS083582

**EIGHTH VERIFIED APPLICATION
FOR ORDER APPROVING
LIQUIDATOR'S PROPOSAL TO
DISBURSE ASSETS TO STATE
INSURANCE GUARANTEE
ASSOCIATIONS OR FUNDS [INS. CODE
§ 1035.5]; MEMORANDUM OF POINTS
& AUTHORITIES IN SUPPORT
THEREOF**

Date: August 7, 2012
Time: 1:30 p.m.
Dept.: CCW-307
Judge: Hon. William Highberger

I.

INTRODUCTION

Pursuant to California Insurance Code section 1035.5, the Insurance Commissioner of the State of California, in his capacity as the Liquidator ("Liquidator") of Fremont Indemnity Company ("Fremont"), seeks the Court's approval of his proposal to disburse a portion of the Fremont liquidation estate's assets to the California Insurance Guaranty Association ("CIGA") and to insurance guaranty associations that perform similar functions in the other states in which Fremont conducted its workers' compensation business (collectively, the "IGAs"). The Liquidator proposes to disburse \$39,617,203, to the IGAs in accordance with their estimated reported losses through December 31, 2011, as specified in the distribution schedule attached to the application as Exhibit A.

II.

VERIFIED APPLICATION

Applicant, the Insurance Commissioner of the State of California, in his capacity as Liquidator of Fremont Indemnity Company states as follows:

1. On June 4, 2003, the Los Angeles County Superior Court ordered and appointed the Commissioner to serve as Conservator of Fremont.
2. On July 2, 2003, the same court found that Fremont was insolvent and, on that basis, terminated the Commissioner's status as Conservator and appointed the Commissioner to serve as the Liquidator of Fremont. The entry of the Liquidation Order triggered the duty of the IGAs to pay all covered policyholder claims in accordance with the IGAs' respective statutes.
3. California Insurance Code section 1035.5 provides in relevant portion that:
"Notwithstanding the provisions of Article 14 (commencing with Section 1010), with regard only to those insurers subject to this article:
"(a) Within 120 days of the issuance of an order directing the winding up and liquidation of the business of an insolvent insurer under Section 1016, the commissioner shall make application to the court for approval of a proposal to

1 disburse the insurer's assets, from time to time as such assets become available, to
2 the California Insurance Guarantee Association, or the California Life and Health
3 Insurance Guarantee Association, and to any entity or person performing a similar
4 function in another state.

4 “(b) The proposal shall at least include the following provisions for:

5 “(1) Reserving amounts for the payment of expenses of administration and
6 the payment of claims of secured creditors (to the extent of the value of the
7 security held) and claims falling within the priorities established in paragraphs (1)
8 to (4), inclusive, of subdivision (a) of Section 1033.

9 “(2) Disbursement of the assets marshaled to date and subsequent
10 disbursements of assets as they become available.

11 “(3) Equitable allocation of disbursements to each of the associations
12 entitled thereto.

13 “(4) The securing by the commissioner from each of the associations
14 entitled to disbursements pursuant to this section of an agreement to return to the
15 commissioner such assets previously disbursed as may be required to pay claims
16 of secured creditors and claims falling within the priorities established in
17 paragraphs (1) to (5), inclusive, of subdivision (a) of Section 1033 in accordance
18 with the priorities. No bond shall be required of any association.

19 “(5) A full report to be made by the association to the commissioner
20 accounting for all assets so disbursed to the association, all disbursements made
21 therefrom, any interest earned by the association on the assets, and any other
22 matter as the court may direct.

23 “(c) The commissioner's proposal shall provide for disbursements to the
24 associations in amounts estimated at least equal to the claim payments made by
25 the associations for which such associations could assert a claim against the
26 commissioner, and shall further provide that if the assets available for
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1 disbursement from time to time do not equal or exceed the amount of the claim
2 payments made by the associations, then disbursements shall be in the amount of
3 available assets. The reserves of the insolvent insurer on the date of the order of
4 liquidation shall be used for purposes of determining the pro rata allocation of
5 funds among eligible associations.

6 “(d) The commissioner shall offset the amount disbursed to any entity or
7 person performing a function in any other state similar to that function performed
8 by the California Insurance Guarantee Association, or the California Life and
9 Health Insurance Guarantee Association, by the amount of any statutory deposit,
10 premiums, or any other asset of the insolvent insurer held in that state.

11 “(e) Notice of such application shall be given to the associations in and to
12 the commissioners of insurance of each of the states. Any such notice shall be
13 deemed to have been given when deposited in the United States certified mails,
14 first-class postage prepaid, at least 30 days prior to submission of such application
15 to the court. Action on the application may be taken by the court provided the
16 above required notice has been given and provided further that the commissioner's
17 proposal complies with paragraphs (1) and (4) of subdivision (b).”

18 **PLAN APPROVAL AND PRIOR DISTRIBUTIONS**

19 4. On December 3, 2004, the Court approved the plan proposed by the Liquidator for
20 the early distribution of Fremont's assets to the IGAs as required under Insurance Code section
21 1035.5 (the “Plan”). Pursuant to the Plan, each IGA will receive an early access distribution
22 equal to a percentage of an amount based on the ratio of the IGA's paid losses (which includes
23 the amount of paid “allocated loss adjustment expense,” or ALAE, on specific claims) to the total
24 of all IGAs' paid losses (including ALAE). Statutory deposits will be netted from each IGA's
25 share to ensure that the allocation of the early access distribution remains equitably proportionate
26 to each IGA's respective share of Fremont's aggregate claim payment liability. Under the Plan,
27

1 the Liquidator also agreed to maintain a \$60 million reserve, subject to periodic adjustment, to
2 cover items listed in Insurance Code section 1035.5(b)(1) (the "Reserve").

3 5. The Court further approved the first distribution by the Liquidator from Fremont's
4 assets to the IGAs for claim payment activity reported by the IGAs from July 2, 2003, through
5 June 30, 2004. On December 14, 2004, the Liquidator disbursed Fremont's assets in the
6 aggregate amount of \$49,224,224 to the IGAs based on claim losses reported to the Liquidator,
7 after offsetting statutory deposits and other assets that were turned over to the IGAs upon
8 Fremont's insolvency.

9 6. On July 7, 2005, the Court approved a second distribution of Fremont's assets to
10 the IGAs for claim payment activity reported by the IGAs from July 1, 2004, through December
11 31, 2004. Pursuant to the Court's approval, the Liquidator disbursed Fremont's assets in the
12 aggregate amount of \$36,934,280 to the IGAs based on claim losses reported to the Liquidator,
13 after offsetting statutory deposits and other assets that were turned over to the IGAs upon
14 Fremont's insolvency.

15 7. On June 11, 2006, the Court approved a third distribution of Fremont's assets to
16 the IGAs for claim payment activity reported by the IGAs from July 1, 2005, through December
17 31, 2005. Pursuant to the Court's approval, the Liquidator disbursed Fremont's assets in the
18 aggregate amount of \$168,063,039 to the IGAs based on claim losses reported to the Liquidator,
19 after offsetting statutory deposits and other assets that were turned over to the IGAs upon
20 Fremont's insolvency.

21 8. On August 3, 2007, the Court approved a fourth distribution of Fremont's assets to
22 the IGAs for claim payment activity reported by the IGAs from January 1, 2006, through
23 December 31, 2006. Pursuant to the Court's approval, the Liquidator disbursed Fremont's assets
24 in the aggregate amount of \$144,007,213 to the IGAs based on claim losses reported to the
25 Liquidator, after offsetting statutory deposits and other assets that were turned over to the IGAs
26 upon Fremont's insolvency..

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1 9. On June 11, 2008, the Court approved a fifth distribution of Fremont's assets to
2 the IGAs for claim payment activity reported by the IGAs from January 1, 2007, through
3 December 31, 2007. Pursuant to the Court's approval, the Liquidator disbursed Fremont's assets
4 in the aggregate amount of \$49,675,212 to the IGAs based on claim losses reported to the
5 Liquidator, after offsetting statutory deposits and other assets that were turned over to the IGAs
6 upon Fremont's insolvency.

7 10. On October 5, 2009, the Court approved a sixth distribution of Fremont's assets to
8 the IGAs for claim payment activity reported by the IGAs from January 1, 2008, through
9 December 31, 2008. Pursuant to the Court's approval, the Liquidator disbursed Fremont's assets
10 in the aggregate amount of \$50,000,000 to the IGAs based on claim losses reported to the
11 Liquidator, after offsetting statutory deposits and other assets that were turned over to the IGAs
12 upon Fremont's insolvency.

13 11. On October 17, 2011, the Court approved a seventh distribution of Fremont's
14 assets to the IGAs for claim payment activity reported by the IGAs from January 1, 2009, through
15 December 31, 2010. Pursuant to the Court's approval, the Liquidator disbursed Fremont's assets
16 in the aggregate amount of \$39,905,597.00 to the IGAs based on claim losses reported to the
17 Liquidator, after offsetting statutory deposits and other assets that were turned over to the IGAs
18 upon Fremont's insolvency.

19 **ADJUSTMENT TO RESERVE**

20 12. As part of the Court's approval of the early access distribution plan on December
21 3, 2004, the Liquidator proposed to set the Reserve at \$60 million, subject to periodic adjustments
22 to ensure that the reserve is neither too great nor too small for the proper and equitable
23 administration of the estate and the protection of claimants. The Liquidator further agreed to
24 advise the Court of future changes in the Reserve at the time he files his Notices of Proposed
25 Early Access Distribution.

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13. In 2008, the Liquidator advised the Court that a reserve of \$30 million was sufficient. In 2009, the Liquidator determined that it was necessary to increase the Reserve to \$60 million, pending the completion and approval of a plan to effect a taxpayer deconsolidation of the estate from the consolidated taxpayer group of Fremont's former parent company, Fremont General Corporation. The Fremont estate has completed the taxpayer deconsolidation plan and is working to run off the balance of the reinsurance program. After making the early access distribution in 2011, the Fremont estate had approximately \$120 million in available reserves set aside. The estate also implemented limitations on future early access distributions to avoid over-distribution to certain IGAs and in consideration of the funds that ultimately will be required for an equitable distribution to other non-IGA Class 2 claimants, who were not entitled to early access distribution but are entitled to equal claim treatment. Currently, the estate has set aside \$28 million to address the non-IGA Class 2 claims.

14. In prior Early Access Distributions discussed above, the IGAs were reimbursed for all paid claims and related expenses at percentages between 85-100%. However, several years ago the Liquidator settled all major litigation involving this estate thus removing a material degree of uncertainty around the estate's potential legal expense/recovery and ultimate creditor payout. The Liquidator has continued to administer and monitor the adjustment of Uncovered Claims that will eventually share in future distributions *pari passu* with the IGAs. Based on these settlements and developments in adjusting and estimating the amount of the estate's potential liability on Uncovered Claims, the Liquidator determined that the estimated final distribution to Class 2 participants, including both IGAs and Uncovered Claims, will be in the range of 40-50%. This analysis caused the Liquidator to change the method used to make early access distributions to participating "Insurance Guaranty Associations." Effective as of the 2009 Early Access Distribution, the Liquidator established a cap on such distributions of 38% of each IGA's total incurred losses. Consistent with the 2009 protocol, if an IGA's distributions exceed the 38% cap, that particular IGA will not participate in further Early Access Distributions. In addition, the Liquidator will not make a distribution to an IGA that will cause its aggregate distributions to

exceed its total paid losses to date.

THE PROPOSED 2012 DISTRIBUTION

15. As of March 30, 2012, the Fremont estate has cash assets of \$106,840,308. After making the proposed 2012 Early Access Distribution of \$39,617,203, the Fremont estate will have an available pool of approximately \$67,223,105 remaining as a reserve for liabilities referenced in Insurance Code section 1035.5(b)(1).

16. After the IGAs reported to the Liquidator their claim payment activities for the period January 1, 2011, through December 31, 2011, and after the Liquidator applied the protocol described in paragraph 13 above, the Liquidator determined that the appropriate 2012 Early Access Distribution would be in the aggregate amount of \$39,617,203. The specific amount anticipated to be paid to each participating IGA is provided in the schedule attached as Exhibit A hereto and incorporated herein by this reference.

17. Finally, as required by Insurance Code section 1035.5(b)(4) and (b)(5), each IGA receiving a distribution has signed an Agreement for Early Access Distribution of Funds, which obligates the IGA to return to the Fremont estate any portion of an early access distribution that exceeds the IGA's ratable share of the ultimate Class 2 distributions from the liquidation estate. The agreements govern this distribution and each subsequent early access distribution of assets from the Fremont estate.

WHEREFORE, the Liquidator prays that this Application be heard and granted, and that this Court issue an Order as follows:

1. Authorizing the Liquidator to disburse approximately \$39,617,203 from the assets of Fremont Indemnity Company to the IGAs, subject to final adjustments of the disbursement amount; and

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2. Authorizing the Liquidator to take any and all action necessary to accomplish the purposes of the Order prayed for herein.

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Dated: July 2, 2012

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State of California, in his capacity as Liquidator of
Fremont Indemnity Company*


VERIFICATION

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I, Scott D. Pearce, state that I am a Senior Estate Trust Officer with the California Insurance Commissioner's Conservation and Liquidation Office and have overall responsibility for the liquidation of Fremont Indemnity Company. I have read the EIGHTH VERIFIED APPLICATION FOR ORDER APPROVING LIQUIDATOR'S PROPOSAL TO DISBURSE ASSETS TO STATE INSURANCE GUARANTEE ASSOCIATIONS OR FUNDS; and know the contents thereof. The statements contained therein are not all within my personal knowledge, and I am informed that no single officer of the Conservation and Liquidation Office has personal knowledge of all these matters. The statements are based upon information assembled by employees authorized to maintain and analyze the records of Fremont Indemnity Company in liquidation. I am informed and believe that the statements based upon that information are true. As those matters that are within my own personal knowledge, the statements herein are true.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Executed at San Francisco, California on June 28, 2012.



Scott D. Pearce

1 MEMORANDUM OF POINTS AND AUTHORITIES

2 California Insurance Code section 1035.5 states the procedural requirements regarding the
3 disbursement of an insolvent insurer's assets. The following sets forth the responsibility of the
4 Insurance Commissioner of the State of California, in his capacity as the Liquidator (the
5 "Liquidator") of Fremont Indemnity Company, to apply for the disbursements to the California
6 Insurance Guarantee Association and the Insurance Guarantee Associations in other states
7 (collectively "IGAs"):

8 Within 120 days of the issuance of an order directing the winding up and
9 liquidation of the business of an insolvent insurer under Section 1016, the
10 commissioner shall make application to the court for approval of a proposal to
11 disburse the insurer's assets, from time to time as such assets become available, to
12 the California Insurance Guarantee Association, or the California Life and Health
13 Insurance Guarantee Association, and to any entity or person performing a similar
14 function in another state.

15 (Cal. Ins. Code § 1035.5(a).)

16 California and other states have similar requirements regarding the handling of assets of
17 insolvent insurers that require the equitable distribution of an insolvent insurer's assets among all
18 IGAs. (Cal. Ins. Code § 1033(a); *Commercial Nat'l Bank v. Superior Court (Garamendi)* (1993)
19 14 Cal.App.4th 393, 398 (finding that claimants within same class are entitled to share pro rata in
20 distribution to class).)

21 As required under Insurance Code section 1035.5(b)(1), the Liquidator has established a
22 reasonable plan to reserve assets to pay secured claims and the higher or ratable priority
23 disbursement required under Insurance Code section 1033(a). Therefore, the Liquidator should
24 be allowed to make his proposed early access distribution of approximately \$39,617,203 to the
25 IGAs.

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1 Based on the foregoing, the Liquidator respectfully requests that the Court grant the
2 application and approve the proposal to disburse assets to state Insurance Guarantee Associations.

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4 Dated: July 2, 2012

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10 *Attorneys for the Insurance Commissioner of the*
11 *State of California, in his capacity as Liquidator of*
12 *Fremont Indemnity Company*

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EXHIBIT A

EXHIBIT A

Fremont Indemnity Co
Proposed 8th Early Access Distribution to IGAs
August 2012

<u>Insurance Guaranty Association</u>	<u>Proposed Current Distribution</u>
Alabama Insurance Guaranty Association	\$33,237
Alaska Insurance Guaranty Association	2,021,375
California Insurance Guarantee Association	32,680,659
Connecticut Insurance Guaranty Association	27,503
District of Columbia Guaranty Association	48,836
Georgia Insurance Insolvency Pool	309,060
Idaho Insurance Guaranty Association	658,481
Illinois Insurance Guaranty Fund	1,807,957
Kentucky Insurance Guaranty Association	100,636
Montana Insurance Guaranty Association	804,868
Nevada Insurance Guaranty Association	16,505
North Carolina Insurance Guaranty Association	73,117
Oklahoma Property & Casualty Guaranty Association	19,142
Texas Property & Casualty Insurance Guaranty Assn.	191,328
Utah Property & Casualty Insurance Guaranty Association	824,499
	<u>\$39,617,203</u>