

**ONTARIO
SUPERIOR COURT OF JUSTICE
- COMMERCIAL LIST**

**IN THE MATTER OF NORTHUMBERLAND
GENERAL INSURANCE COMPANY;**

**AND IN THE MATTER OF THE
CANADIAN AND BRITISH INSURANCE COMPANIES ACT,
R.S.C. 1970, c. I-15, as amended;**

**AND IN THE MATTER OF THE
WINDING-UP ACT, R.S.C. 1970, c.W-10, as amended.**

BETWEEN:

THE ATTORNEY GENERAL OF CANADA

Applicant

- and -

NORTHUMBERLAND GENERAL INSURANCE COMPANY

Respondent

**REPORT DATED MAY 10, 2010
(Motion Returnable May 20, 2010)**

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I. THE MOTION

1. This Report is filed in support of a motion by PricewaterhouseCoopers Inc. ("PwC Inc."), as Agent (the "Agent") to the Superintendent of Financial Institutions (the "Superintendent"), in her capacity as provisional liquidator (the "Liquidator") of Northumberland General Insurance Company ("Northumberland").

2. This motion is for an Order:

- (a) passing the accounts and approving the activities of the Agent and the Liquidator for the period July 24, 1985 to January 31, 2010 (the "Period");
- (b) approving the professional fees of the Agent and of its counsel for the Period;
- (c) approving and authorizing a sixth interim distribution ("Proposed Distribution"), namely (i) payment to Her Majesty the Queen in right of Canada ("Her Majesty") of the Industry-Funded Expenses (as defined below) in connection with the Northumberland liquidation in respect of the period April 1, 2002 to January 31, 2010, and interest thereon to the date of payment, at the rate that has been specified by the Superintendent pursuant to statute; and (ii) compensation to the Superintendent's office in the amount of \$167,000.00 in respect of the liquidation;
- (d) approving and authorizing the release to Her Majesty of the Industry Interest Holdback (as described below), including the interest earned thereon;
- (e) continuing the appointment as representative counsel of James H. Grout for the Included Creditors, Ronald N. Robertson for the Included Policyholders, and Lyndon A. J. Barnes for the Assessed Insurance Companies (all as hereinafter defined);
- (f) approving the stepping down of, and discharging, the Superintendent as Liquidator, and dispensing with any requirement that she pass further accounts, ordering that further passings will be the responsibility of the Permanent Liquidator (as defined below);
- (g) appointing the Agent as permanent liquidator (the "Permanent Liquidator");
- (h) approving the amendment of the agreements dated July 17, 1989 and August 5, 1994, described further below, to replace the Superintendent as a party thereto with the Permanent Liquidator; and
- (i) discharging the representative counsel for the Assessed Insurance Companies upon the granting of the Order requested.

II. BACKGROUND

A. The Company

3. Northumberland was a property and casualty insurance company, licensed to do business in Canada under federal legislation. Northumberland was engaged in the underwriting of, among other products, significant liability insurance policies, including many with "long-tail" coverage (where exposures may not be manifest until long after the expiry of the policy term), and complex coverage including asbestos, alcohol, tobacco and environmental exposures.

4. In the late 1970's, Northumberland also began to sell policies to companies in the United States, on an "excess and surplus lines" basis. This meant that, in times of limited insurance capacity in the marketplace, Northumberland could sell insurance to policyholders in the United States that was not being offered by domestic insurers. Pursuant to Regulation 41 of the *Insurance Law* of the State of New York (the "*New York Insurance Law*"), Northumberland deposited funds in trust for the protection of its U.S. policyholders and beneficiaries resident in the United States (the "Regulation 41 Trust Funds").

5. In January 1983, Northumberland opened a branch for doing business in the State of New York (the "U.S. Branch"). Pursuant to the *New York Insurance Law*, Northumberland's U.S. Branch deposited further assets for the protection of its policyholders and creditors in the United States (the "U.S. Branch Deposit").

B. The Insolvency Proceedings

(i) Liquidation Orders

6. By Orders of this Court made July 24, 1985, Northumberland was ordered wound-up pursuant to what is now the *Winding-up and Restructuring Act* (“WURA”), and the Superintendent of Insurance (Canada) was appointed provisional liquidator of Northumberland. Copies of the July 24, 1985 Orders are attached as Schedules “A” and “B.”

7. The Superintendent of Insurance appointed Coopers & Lybrand Limited (now PwC Inc.) as his Agent to conduct the liquidation. By Order of this Court dated October 8, 1987, the Superintendent of Insurance was replaced as provisional liquidator of Northumberland by the Liquidator. A copy of the October 8, 1987 Order is attached as Schedule “C”.

8. By Order of the Supreme Court of the State of New York (the “New York Court”) made on August 2, 1985, the Superintendent of Insurance of the State of New York (the “New York Superintendent”) was appointed liquidator of the U.S. Branch and was directed to take possession of the property of the U.S. Branch, including the U.S. Branch Deposit, and to liquidate its business under Article 74 of the *New York Insurance Law*.

9. By Order of the New York Court made on February 24, 1988, the New York Superintendent was appointed as Conservator of, and was directed to take possession of and conserve, the Regulation 41 Trust Funds, and to take such other steps as may be required to protect those policyholders and beneficiaries for whose benefit Northumberland had deposited the Regulation 41 Trust Funds (the “Regulation 41 Claimants”).

(ii) Regime for Industry-Funded Expenses

10. Under the provisions of the *Insurance Companies Act* (and its predecessor legislation) that apply to the Northumberland liquidation, with the Superintendent as the Liquidator the expenses of the liquidation (the "Industry-Funded Expenses") are borne by the Superintendent on behalf of Her Majesty. These are, in turn, assessed against and paid by those members of the insurance industry that carry on a similar business to that of Northumberland (the "Assessed Insurance Companies").¹

11. Over the course of the liquidation, the Superintendent has assessed the Assessed Insurance Companies in respect of the Industry-Funded Expenses relating to the Northumberland liquidation, and they have thereby effectively funded the Industry-Funded Expenses. (As of April 1, 2001 the liquidity of the estate was such that the liquidation expenses, excepting the Agent's fees, were paid directly from the estate. The Agent's fees have continued to be funded by the Superintendent on behalf of Her Majesty.)

12. Under the priority provisions of the *WURA* as they apply to the Northumberland liquidation, the Industry-Funded Expenses (with interest) are to be repaid to Her Majesty, subsequent to policyholder claims being paid in full. These recovered Industry-Funded Expenses, and interest thereon, either are applied by Her Majesty to reduce assessments that would otherwise be made against the Assessed Insurance Companies or are actually repaid to the Assessed Insurance Companies.

¹ This statutory regime for funding expenses of the liquidation was originally implemented to provide a benefit to policyholders before consumer compensation funds were established. Once a compensation fund was established for the property and casualty insurance industry, however, and funds were thereby made available to qualified policyholders up to specified limits, the funding of expenses by the industry was considered no longer necessary, and, as a result of statutory amendments in 1996 that prevented the Superintendent from being appointed as a liquidator, the liquidation expenses for liquidations commenced post-amendments are funded directly from the estate as a first charge.

(iii) Two Initial Interim Distributions

13. On November 1, 1989, this Court approved the payment of a first interim dividend of 15¢ on the dollar on policy claims against Northumberland. On December 7, 1990, this Court approved the payment of a second interim dividend of 25¢, bringing the cumulative interim distribution paid on these claims to 40¢ on the dollar. Copies of the November 1, 1989 and December 7, 1990 Orders are attached as Schedules "D" and "E", respectively.

(iv) Resolution of U.S. Creditor Issues

14. Early in the liquidation, the Liquidator had made demands on the New York Superintendent for the return of the Regulation 41 Trust Funds and the U.S. Branch Deposit under what was then section 165 (now section 164) of the *WURA*. The New York Superintendent refused. The Liquidator, therefore, took the position that the claims being administered by him excluded the claims of policyholders of the U.S. Branch (the "U.S. Branch Policyholders"), the ordinary creditors of the U.S. Branch (the "U.S. Branch Ordinary Creditors") and the Regulation 41 Claimants. The New York Superintendent disputed this position.

15. Accordingly, in June 1993, the Liquidator brought a motion (the "Distribution Motion") seeking the approval of this Court to his proposed scheme for the distribution of the estate being administered by the Liquidator (the "Canadian Estate"). The Liquidator sought approval to distribute the Canadian Estate in the following order of priority:

- (a) to the policyholders of Northumberland other than the Regulation 41 Claimants and the U.S. Branch Policyholders (the "Included Policyholders");
- (b) to Her Majesty, in respect of Industry-Funded Expenses incurred on or after April 1, 1986, together with interest thereon;

- (c) to the ordinary creditors of Northumberland other than the U.S. Branch Ordinary Creditors (the "Included Ordinary Creditors"); and
- (d) to Her Majesty, in respect of Industry-Funded Expenses incurred before April 1, 1986, together with interest thereon.

In addition, the Liquidator sought a declaration that the Regulation 41 Claimants, the U.S. Branch Policyholders and the U.S. Branch Ordinary Creditors were deemed to have forfeited all rights and claims against the Canadian Estate.

16. This Court declared that the following were the classes of parties affected by the Distribution Motion, and appointed the following as their respective representative counsel:

- Included Policyholders - Ronald N. Robertson, Q.C.;
- Included Ordinary Creditors - Paul S.A. Lamek, Q.C.;
- Regulation 41 Claimants - William G. Horton;
- U.S. Branch Policyholders - Geoffrey B. Morawetz; and
- Assessed Insurance Companies - Lyndon A.J. Barnes.

Copies of the Orders of this Court dated June 24, 1993, September 20, 1993 and September 28, 1993 in this regard are attached as Schedules "F", "G" and "H", respectively.

17. A settlement was reached in the Distribution Motion with respect to the issues relating to the U.S. Branch Policyholders and Regulation 41 Claimants. The settlement was approved by this Court. Under the settlement, the Liquidator agreed to make certain payments from the Canadian Estate to the New York Superintendent in respect of claims of the Regulation 41 Claimants and the U.S. Branch Policyholders, in exchange for a release from the New York Superintendent with respect to issues raised on the Distribution Motion.

18. As noted in the Report in support of the fourth interim distribution (described below), the grandfathered provisions of the *WURA* which deal with the payment of Industry-Funded Expenses contemplate that interest thereon shall have the same priority as the Industry-Funded Expenses to which it relates. The Superintendent and the Assessed Insurance Companies accordingly took a position consistent with this. However, at the time of the Distribution Motion, the Representative Counsel on behalf of the Included Policyholders raised a concern as to the priority of the interest portion of this claim.

19. To facilitate the settlement of the Distribution Motion therefore, the Superintendent agreed, with the concurrence of the Assessed Insurance Companies, that the statutory claim for interest on the Industry-Funded Expenses would be subordinated to the allowed claims of the Included Policyholders and Included Ordinary Creditors.

20. The Superintendent specified, in accordance with the *WURA*, the rate that would apply to the claim for interest on the Industry-Funded Expenses.

(v) Third Interim Distribution

21. Pursuant to an Order dated September 9, 1994, this Court:

- (a) approved the settlement regarding the U.S. creditors;
- (b) discharged the representative counsel on behalf of the Regulation 41 Claimants and the U.S. Branch Policyholders;
- (c) authorized the Liquidator to pay a third interim dividend of 60¢ on the dollar of the claims of Included Policyholders, bringing their cumulative distributions to 100¢ on the dollar; and
- (d) ordered that the balance of the Distribution Motion regarding the application for approval of the proposed scheme of distribution be adjourned *sine die*, to be brought on notice to the representative counsel on behalf of the Included

Policyholders, the Included Ordinary Creditors and the Assessed Insurance Companies.

A copy of the September 9, 1994 Order is attached as Schedule "I".

22. The September 9, 1994 Order was made subject to the approval of the settlement by the New York Court with respect to both the liquidation proceedings for the U.S. Branch and the conservation proceedings for the Regulation 41 Trust Funds. These approvals were granted on November 15 and 28, 1994, respectively. Copies of the Orders of the New York Court in this regard are attached as Schedules "J" and "K".

(vi) Fourth Interim Distribution

23. By Order dated October 1, 1996, this Court approved the payment of a fourth interim dividend of 100¢ on the dollar of the claims of:

- (i) the Included Ordinary Creditors;
- (ii) Her Majesty in respect of the principal amount of the Industry-Funded Expenses from April 1, 1986 to March 31, 1996; and
- (iii) Her Majesty in respect of the principal amount of the Industry-Funded Expenses from July 24, 1985 to March 31, 1986.

These have been paid. A copy of the October 1, 1996 Order is attached as Schedule "L".

(vii) Fifth Interim Distribution

24. After the payment of the fourth interim distribution, the Representative Counsel on behalf of the Included Policyholders advised that he would not oppose the position of the Superintendent and the Assessed Insurance Companies with respect to the priority of the interest payable on Industry-Funded Expenses.

25. However, to facilitate the payment of the fifth interim distribution, the Assessed Insurance Companies agreed:

- (a) that the Liquidator would hold back 30% of the interest component on the Industry-Funded Expenses (the "Industry Interest Holdback"), being \$8.1 million², to be available to be used to meet existing outstanding claims; and
- (b) that a portion (up to \$2.5 million) of the interest on the Industry-Funded Expenses, which would otherwise be payable to Her Majesty, would be available, if needed, to pay post-liquidation pre-judgment interest claims ("PJI Claims") for which Northumberland's insureds were liable. To date, the sum of \$1.48 million was so applied to PJI Claims. In light of the liquidity in the liquidation at this point, the Liquidator proposes to pay any further PJI Claims from the general assets in the Canadian Estate, and estimates that these will total less than \$1 million.

26. By Order dated February 13, 2003, this Court approved the payment of a fifth interim distribution as follows:

- (a) payment to Her Majesty of the portion of the Industry-Funded Expenses assessed and paid by the Assessed Insurance Companies relating to the period April 1, 1996 to March 31, 2002, and interest thereon at the rate that was specified by the Superintendent pursuant to statute;
- (b) payment to Her Majesty of interest on the portion of the Industry-Funded Expenses that had already been paid to Her Majesty relating to the period July 24, 1985 to March 31, 1996, also at the specified rate;
- (c) payment of an amount equal to 5% of the allowed claims of the Included Policyholders and Included Ordinary Creditors of Northumberland, on account of post-liquidation interest on such claims.

² Amounts expressed as "million" in this Report have been rounded.

A copy of the February 13, 2003 Order is attached as Schedule "M". This distribution was made, after deduction of the Industry Interest Holdback, referred to above, from the interest amounts in (a) and (b) referenced immediately above.

III. ACTIVITIES OF THE LIQUIDATOR AND STATEMENT OF RECEIPTS AND DISBURSEMENTS OVER THE PERIOD

A. Activities

27. Since the commencement of its appointment, the Agent has engaged on behalf of the Liquidator in the following activities in connection with the winding-up of Northumberland:

- administration of all claims-related matters, including adjusting claims, defending claims on behalf of policyholders, and disputing coverage where applicable;
- conducting the call for claims for both policyholders and claimants and ordinary creditors (claims totalling approximately \$131 million and contingent claims totalling approximately \$9 billion were filed);
- negotiating and collecting reinsurance of over \$81 million;
- ongoing negotiations and arrangements with the New York Superintendent regarding shared reinsurance collections and commutations, and claims administration for the Regulation 41 claims;
- investment of assets and administration of all investments;

- the making of five interim distributions, each to in excess of 48,000 policyholders and claimants;
- preparation and filing of corporate income tax returns, in a timely fashion; and
- reporting to the Superintendent as Liquidator and the New York Superintendent.

B. Receipts and Disbursements

28. Attached as Schedule "N" hereto is a statement of receipts and disbursements for the estate over the Period. The Agent is of the view that the receipts and disbursements are proper and reasonable.

C. Ongoing Reporting

29. The Agent reported on a quarterly basis to the Superintendent as Liquidator. Each report contained a Statement of Affairs and a Statement of Receipts and Disbursements. In the early part of the liquidation, the Superintendent also met with the Assessed Insurance Companies on a regular basis, and continued thereafter to regularly report to them.

D. Budgets

30. Annual budgets were prepared and updated by the Agent and provided to the Liquidator, who reviewed and approved each of the budgets and, in the early years, reviewed these with the Assessed Insurance Companies.

E. Professional Fees

31. The Agent provided its own professional services to the Superintendent as Liquidator and retained counsel - namely, Goodmans LLP and its predecessors ("Goodmans") - to assist and advise in the administration of the liquidation, including with respect to resolution of certain claim litigation matters.

32. The services of the two main professional advisors are discussed more particularly below.

(i) Goodmans

33. Goodmans have acted as counsel to the Agent from the commencement of the liquidation, and have acted or advised on most of the matters described in this Report. The Agent is familiar with Goodmans' services. Detailed invoices were received on a timely basis and carefully reviewed by senior members of the Agent's staff. The invoices were reviewed for accuracy, adequate detailed information about the work performed and by whom, the time spent and when it was spent, the rate and the amount billed, possible duplicative charges, reasonableness and overall compliance with the terms of retention. Clarifications and adjustments of items included in Goodmans' invoices were requested where it appeared appropriate.

34. A summary of the invoices for Goodmans is attached as Schedule "O" hereto. A summary of the hours and average hourly rates of Goodmans personnel is attached as Schedule "P" hereto.

35. The hourly billing rates charged by Goodmans have not been increased since the commencement of the liquidation and reflect a very significant discount from regular rates over the course of the liquidation.

36. The Agent is satisfied that Goodmans' fees are proper, fair and reasonable, that time was appropriately spent, and the Goodmans' fees were incurred in furtherance of the interest of the estate.

(ii) PwC Inc.

37. The Agent applied the same standard of review to its own accounts as to the accounts of counsel described above. The accounts of the Agent were provided to the Superintendent on a monthly basis for review and approval, and the supporting documents were examined by the Superintendent on a periodic basis.

38. A summary of the invoices for the Agent is attached as Schedule "Q" hereto. A summary of the hours and average hourly rates of the Agent's personnel is attached as Schedule "R" hereto.

39. The hourly billing rates charged by the Agent have not been increased since the commencement of the liquidation, with the exception of a cumulative annual increase equal to the annual increase in the Consumer Price Index for the immediately preceding year, and reflect a very significant discount from regular rates over the course of the liquidation.

40. The Agent is satisfied that its fees are proper, fair and reasonable, that time was appropriately spent, and that its fees were incurred in furtherance of the interest of the estate.

41. The Agent's accounts and the accounts of Goodmans have been approved by the Liquidator.

IV. FINANCIAL STATUS OF THE ESTATE

A. Assets

42. The assets of the Canadian Estate as at January 31, 2010 consist of cash or near cash in the amount of \$64.8 million. The majority of reinsurance has now been collected, including through commutation of reinsurance treaties. The Canadian Estate maintains a contingent interest in any surplus in the conservation proceedings of the Regulation 41 Claims. However, as a conservative measure the Liquidator is not, at this time, ascribing a value to this contingent interest.

B. Liabilities

43. At the commencement of this liquidation, the books and records of Northumberland reflected claims known to Northumberland with a claim value in excess of \$100 million.

44. In addition to the known claims reflected in the books and records of Northumberland, 190 policyholders filed 403 contingent claims, having an aggregate claimed value of approximately \$9 billion. These contingent claims related to potential occurrences during the respective policy periods for which claims had not yet been reported.

45. Over the course of the liquidation, all but 17 of the filed contingent claims were withdrawn or settled, with these 17 claims having a total claimed value of \$14 million.

46. To permit distributions on settled claims while still maintaining appropriate reserves for the remaining unsettled claims and the filed contingent claims, the Agent retained the services of a firm of consulting actuaries - Tillinghast, a Towers Perrin Company ("Tillinghast") - to perform actuarial projections of the policy liabilities. Tillinghast has performed reviews at least as frequently as annually since 1989. The Liquidator has made all distributions relying both on the opinion of Tillinghast and the Agent's own internal reviews.

47. The outstanding policy claims as at January 31, 2010 are comprised of:

- (a) unclaimed dividends of \$5.5 million for policyholders who cannot be located;
- (b) reserves of \$19.3 million for:
 - (i) known unsettled claims of \$5.3 million for policyholders, comprised of corporations and insurers that Northumberland reinsured. In addition to Tillinghast, Liquidator has retained an experienced claims consultant as needed in establishing these reserves, which include a factor for both related adjusting and defence costs, and a provision for adverse development; and
 - (ii) the 17 contingent claims totalling \$14 million, filed by three policyholders. For this component of the reserves, the Liquidator has conservatively used the amount of the filed claims and has made no judgment on the value of the claims.

V. POST-LIQUIDATION INTEREST

48. Part III of the *WURA* (both in its "grandfathered" pre-1996 version as it applies to this liquidation, and its amended version as it applies to liquidations commenced after the 1996 amendments) does not address post-liquidation interest on policy loss or ordinary creditor claims in this liquidation, or the ranking, if any, to be given thereto.

49. However, subsection 95(2) in Part I of the *WURA*, enacted in 1996, provides for post-liquidation interest on claims to be paid from a surplus at the rate of 5% *per annum*, but it does not state whether, or how, it applies to the liquidation of an insurance company.

50. In the liquidation of Confederation Trust Company this Court held that subsection 95(2) applies even though the subject liquidation began (as did the Northumberland liquidation) prior to the enactment of subsection 95(2). In July 2009, in the liquidation of the Canadian branch of Reliance Insurance Company, this Court ruled on the effect of subsection 95(2) in the liquidation of a property and casualty insurance company (the “Reliance Ruling”).

51. In brief, the Reliance Ruling held that post-liquidation interest under subsection 95(2) of the *WURA* is payable on policyholder loss and ordinary creditor claims that were not paid-in-full immediately as the claims were settled and allowed during the liquidation: i.e., it is payable on claims where the liquidation caused a delay in their being paid-in-full (*vis-à-vis* when they would have been paid contractually, absent a liquidation). The Reliance Ruling specified that the post-liquidation interest is to be calculated as simple interest at an annual rate of 5%, on the unpaid portion of each such claimant’s allowed claim, from the time such claim was settled and allowed, and that any payments by way of interim dividends during the course of the liquidation are to be treated as being allocated first toward any post-liquidation interest payable on the claim and then to the “principal” portion of the claim.

52. As discussed above, by virtue of the fifth distribution in this liquidation in 2003, 5% of the principal amount of allowed claims (or approximately 0.3% interest per annum) was paid to claimants on account of post-liquidation interest, without there being a final determination as to the applicability of ss. 95(2) of the *WURA*. As it was uncertain at that time

whether, or how, ss. 95(2) interest applied in the liquidation of an insurance company, with the Court's approval the 5% distribution was made "across the board", including on those claims that had been settled and allowed after the 100¢ dividend rate had been reached (and which claims were accordingly paid-in-full on a timely basis, without delay by virtue of the liquidation).

53. Accordingly, in a very few cases, a distribution (totalling less than \$400,000.00) was authorized on claims that had been paid-in-full without any delay because of the liquidation, which distribution likely would not have been authorized had the Reliance Ruling been in place at that time.

54. On a go-forward basis, in light of the Reliance Ruling, it is proposed, and in due course it will be recommended, that post-liquidation interest only be payable on claims that were not paid-in-full upon their being settled and allowed, consistent with the Reliance Ruling.

VI. REPRESENTATIVE COUNSEL

55. By Order dated January 16, 2003, this Court appointed James H. Grout to replace the late Paul S.A. Lamek, Q.C. as representative counsel on behalf of the Included Ordinary Creditors. A copy of the January 16, 2003 Order is attached as Schedule "S".

56. The respective representative counsel on behalf of the Included Policyholders, the Included Ordinary Creditors and the Assessed Insurance Companies are being served with the materials in respect of this motion. The representative counsel will advise this Court as to their positions with respect to the Proposed Distribution and the release of the Industry Interest Holdback.

57. The Agent understands that the representative counsel support or do not oppose the Proposed Distribution and the stepping down of the Liquidator (discussed below).

VII. PROPOSED SIXTH INTERIM DISTRIBUTION

(i) *Statutory Priority Scheme*

58. In summary, the following is the priority of claims in the estate of Northumberland by virtue of Part III of the *WURA*, as it applies to the Northumberland liquidation:

- (a) claims of policyholders for loss (or, if there is no claim for loss, unearned premiums);
- (b) the claim of Her Majesty in respect of the post-March 31, 1986 Industry-Funded Expenses, together with interest at such rate as is specified by the Superintendent;
- (c) claims of ordinary creditors and certain policyholders of Northumberland, which did not receive priority as set out in (a) above; and
- (d) the claim of Her Majesty in respect of the pre-April 1, 1986 Industry-Funded Expenses, together with interest at such rate as is specified by the Superintendent.

59. As noted above, by agreement a portion of Her Majesty's claims in respect of interest on Industry-Funded Expenses was subject to the Industry Interest Holdback.

(ii) *Canadian Estate Financial Status/Overview of Effect of Proposed Distribution*

60. In considering whether the Proposed Distribution (being a sixth interim distribution) should be paid at this time, the Agent has taken into account the assets available for distribution, the estimated claims exposure to both known and contingent claims, future investment income and estimated future costs including income taxes.

61. There would remain in the Canadian Estate a surplus of approximately \$24.4 million following the making of the Proposed Distribution, given the reserves for future liabilities. The Agent is of the view that this represents a conservative estimate of the surplus, and that the remaining surplus of distributable assets provides an adequate cushion for potential future adverse development.

(iii) *Proposed Distribution to Her Majesty for Current Industry-Funded Expenses and Interest*

62. The Liquidator proposes to pay to Her Majesty the Industry-Funded Expenses for the period April 1, 2002 to January 31, 2010 in the amount of \$2,253,286.98 and the interest thereon for the period April 1, 2002 to the date of the distribution (being approximately \$367,459.00 assuming a distribution in June 2010). This amount is calculated on a simple interest basis, at the rate specified by the Superintendent.

(iv) *Proposed Release of Industry Interest Holdback*

63. The Industry Interest Holdback of \$8.1 million, described above, was not needed to pay outstanding claims in the winding-up, and those claims have been paid or will be paid out of the general funds remaining in the Canadian Estate. The Industry Interest Holdback was invested separately from the general assets and has earned interest.

64. The Agent therefore proposes, and recommends, that the Industry Interest Holdback plus the interest earned thereon be released to Her Majesty, to be used to make whole the Assessed Insurance Companies in respect of the Industry-Funded Expenses that they funded for the period up to March 31, 2002.

(v) Proposed Compensation to Superintendent

65. The Superintendent has fixed a reimbursement amount of \$167,000.00 in respect of all costs incurred by the Superintendent's office in connection with the liquidation. In accordance with the practice approved by this Court in other insurance company liquidations where the Superintendent has contributed substantial resources to the liquidation, it is recommended that the Superintendent be compensated accordingly.

(vi) Summary

66. The total of the Proposed Distribution is \$13.7 million.

67. Attached as Schedule "T" is a summary of the Proposed Distribution.

68. Following the Proposed Distribution, \$51.1 million will remain in the Canadian Estate, of which \$24.4 million will be surplus over the remaining claims reserves. It is anticipated that a further distribution to policyholders in respect of post-liquidation interest will be recommended in 2010.

VIII. STEPPING DOWN AND DISCHARGE OF LIQUIDATOR

A. Appointment of the Superintendent as Provisional Liquidator

69. The provisions of the *Insurance Companies Act* as it read at the commencement of the winding-up of Northumberland permitted the Superintendent (and previously the Superintendent of Insurance) to act as liquidator of an insurance company which was ordered wound-up under the *WURA*. In fact, the Superintendent (and previously the Superintendent of Insurance) was appointed liquidator in respect of all the liquidations of insolvent insurance companies and branch operations under federal jurisdiction in Canada until 1996, when the

WURA and the *Insurance Companies Act* were amended to provide that the Superintendent could no longer be appointed as liquidator of insurance companies.

B. The Role of the Agent

70. The *Insurance Companies Act* also provided in section 690 that, where the Superintendent has been appointed liquidator of an insurance company, the Superintendent may appoint an agent to assist in the liquidation. As noted, in the case of Northumberland, the Superintendent appointed PwC Inc. as his Agent for the administration of the liquidation.

71. The Agent has been responsible to the Liquidator for the day to day operations and administration of the liquidation. The Liquidator has provided oversight and control functions.

C. Regulation 41 Agreement and Settlement Agreement between Liquidator and New York Superintendent

72. The Liquidator and the New York Superintendent, as Conservator of Northumberland, entered into an agreement dated July 17, 1989 (the "Regulation 41 Agreement") which was approved by Order of this Court dated November 1, 1989 and by Order of New York Court dated December 1, 1989, copies of which are attached as Schedules "U" and "V", respectively. The Regulation 41 Agreement provided, inter alia, for the Liquidator to administer the claims of the Regulation 41 Claimants.

73. The Liquidator and the New York Superintendent, in his capacity as both Conservator and as liquidator of Northumberland's U.S. Branch, entered into an agreement dated August 5, 1994 which was approved by this Court on September 9, 1994 and by the New York Court on November 15, 1994 and November 28, 1994 (Schedules "I", "J" and "K").

74. The New York Superintendent has throughout the liquidation dealt with the Agent in respect of all matters relating to the Canadian Estate and the interests of the Regulation 41 Claimants and U.S. Branch Policyholders. The New York Superintendent does not object to the replacement of the Superintendent by the Agent.

D. Passing of Accounts

75. The Liquidator has not previously passed Northumberland's accounts. The accounts and the Liquidator's activities have been reviewed and accepted by the Superintendent during the course of the liquidation, and by way of reports in respect of the interim distributions, the Court has been kept apprised of the activities and developments in the liquidation.

76. The financial affairs of the estate are complex. As noted above, the Agent reported on a quarterly basis to the Superintendent as Liquidator. Each report contained a Statement of Affairs and a Statement of Receipts and Disbursements. In the early part of the liquidation, the Superintendent also met with the Assessed Insurance Companies on a regular basis, and continued thereafter to regularly report to them. If this Court approves the Liquidator's stepping down and discharge, the Liquidator also respectfully seeks the Court's dispensing with a requirement that she pass further accounts, and instead confirming that the Period is the last period for which the Liquidator will be responsible for passing accounts and that further passings will be the responsibility of the Permanent Liquidator. The Superintendent has and will continue to provide oversight and control functions to the date of her stepping down, and will provide any comments thereon to the Court at the application for passing of accounts for the subsequent period from February 1, 2010 to the stepping-down.

77. The professional fees of the Agent and Goodmans have been charged at significantly discounted rates. A discount will continue to be applied to the professional fees, but such fees will be increased to those which are more reflective of current market conditions. The rates and professional fees will be subject to Court approval.

E. Discharge of the Superintendent as Provisional Liquidator and Appointment of PwC Inc. as Permanent Liquidator

78. Significant progress has been made in the liquidation of the Northumberland estate. The Superintendent considers it appropriate that she step down as Liquidator at this time, considering:

- (a) policyholders and creditors have been paid 100¢ the dollar, with some post-liquidation interest;
- (b) the Industry-Funded Expenses are being repaid 100¢ on the dollar, with interest;
- (c) the New York Superintendent does not object; and
- (d) the amendments to *WURA* and to the *Insurance Companies Act* indicate that the Superintendent can no longer be appointed as liquidator of insurance companies.

79. The Liquidator recommends that the Agent be appointed as Permanent Liquidator, effective on the date of the Superintendent's discharge, since:

- (a) as Agent, PwC Inc. has in practice been responsible to the Liquidator for the administration of Northumberland since the commencement of the winding-up proceedings. The Agent has the knowledge of the estate that it would have had it been liquidator. It will not require any additional time to become familiar with

the operations of Northumberland and to assume the role of Permanent Liquidator;

- (b) the Agent has worked directly with all of the significant stakeholders in the Northumberland estate, including policyholders, reinsurers, ordinary creditors and other insurers on subscription policies; and
- (c) the Agent has been involved with all litigation involving or affecting the estate, is familiar with the issues and can ensure consistency in the approach to dealing with both ongoing and future disputes or litigation.

80. The Liquidator is of the view that the stepping down of the Liquidator and the corresponding appointment of the Agent as Permanent Liquidator will not disrupt or prejudice the administration of the liquidation.

81. Subsection 23(2) of the *WURA* requires that the person to be appointed as liquidator of a company must be a licensed trustee under the *Bankruptcy and Insolvency Act*. The Agent is a licensed trustee under the *Bankruptcy and Insolvency Act*. A copy of its consent to act as Permanent Liquidator is attached as Schedule "W" to this Report.

82. The Liquidator recommends that upon the Superintendent stepping down as Liquidator, the representative counsel appointed to represent the interests of the Assessed Insurance Companies be discharged, subject to the assessment of his accounts as provided in the Order dated September 20, 1993 appointing him.

IX. RECOMMENDATION

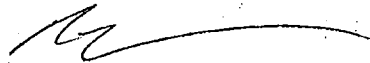
83. The Agent therefore respectfully recommends an Order be granted for the relief claimed in the within motion.

ALL OF WHICH IS RESPECTFULLY SUBMITTED,

PRICEWATERHOUSECOOPERS INC.,
Agent for the Superintendent of Financial
Institutions, Provisional Liquidator of
NORTHUMBERLAND GENERAL
INSURANCE COMPANY

Date: May 10, 2010

Per:



Robert T. Chapman
Senior Vice-President

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