ORDER PREPARED BY THE COURT

SUPERIOR COURT OF NEW JERSEY
MERCER COUNTY
CHANCERY DIVISION-GENERAL EQUITY
DOCKET NO. C-57-06

I/M/O THE REHABILITATION OF
EAGLE INSURANCE COMPANY

CIVIL ACTION

ORDER

This matter having been presented to the Court by way of a notice of motion to enforce the settlement agreement filed by Defendants, Eagle Insurance Company and The Robert Plan Corporation, Gerard Brew, Esq. appearing; and an order to show cause for an order of liquidation having been filed by Plaintiff, the Commissioner of the Department of Banking and Insurance of New Jersey, Emerald Kuepper, Deputy Attorney General appearing; and the court having reviewed the submissions of counsel; and having heard oral argument on May 16, 2007; and for the reasons attached hereto; and for good cause having been shown;

IT IS ON THIS 26th DAY OF JULY 2007,

ORDERED that Defendants' motion to enforce the settlement agreement is DENIED; and it is further

ORDERED that the Commissioner's order to show cause seeking an order of liquidation is GRANTED. The Commissioner shall submit an appropriate order of liquidation.

Neil H. Shuster, P.J.Ch.

I/M/O THE REHABILITATION OF EAGLE INSURANCE COMPANY	SUPERIOR COURT OF NEW JERSEY CHANCERY DIVISION GENERAL EQUITY PART MERCER COUNTY

DOCKET NO. C-84-06

EAGLE'S MOTION TO ENFORCE SETTLEMENT AGREEMENT; THE COMMISSIONER'S ORDER TO SHOW CAUSE FOR AN ORDER OF LIQUIDATION[1]

This matter arises from an order to show cause and verified complaint filed on July 10, 2006 by the Commissioner of the Department of Banking and Insurance of New Jersey ("Department" or "Commissioner"), against Eagle Insurance Company ("Eagle") and the Robert Plan Corporation ("RPC") seeking an Order of Rehabilitation. An amended verified complaint was filed on August 16, 2006. RPC is the corporate parent of Eagle, a New Jersey domiciled property and casualty insurer. Through its ownership of Eagle, RPC is also the ultimate corporate parent of Eagle's subsidiaries, Newark Insurance Company ("Newark"), GSA Insurance Company ("GSA") and National Consumer Insurance Company ("NCIC") (collectively the "Eagle Insurance Group"). Since June 20, 2001, Eagle and Newark have been under consensual Administrative Supervision pursuant to N.J.S.A. 17:51A-1 et seq.[2] Eagle and Newark have been in

[1] From a procedural standpoint, Eagle filed its motion to enforce the Consent Order prior to the Commissioner filing its order to show cause seeking an order of liquidation. As a practical matter, Eagle's motion operates as its opposition to the Commissioner's order to show cause, and vice versa.

[2] Eagle consented to the Department placing it under Administrative Supervision pursuant to N.J.S.A. 17:51A-1, as a result of its declining financial condition. Subsequently, the Commissioner entered a consent order on July 31, 2002 providing that Eagle and its subsidiaries would continue under the Administrative Supervision of the Department. Pursuant to the consensual Administrative Supervision, the Department oversaw all major transactions of Eagle and its subsidiaries to ensure that actions were not taken which would have an adverse impact on Eagle's policyholders, creditors and the general public.

runoff status since November 16, 2003. Currently, Eagle and Newark do not have any in-force policies.[3] After hearing argument on the Commissioner's order to show cause seeking an order of rehabilitation on September 26, 2006, the parties, at the Court's urging, entered into settlement discussions resulting in a settlement placed on the record on January 18, 2007 and codified by order dated January 29, 2007, which resulted in a Consent Order of rehabilitation, among other provisions (to be discussed further infra). Eagle's present motion concerns enforcement of this settlement agreement.

Central to the order to show cause seeking an order of rehabilitation, and central to the present order to show cause seeking an order of liquidation is the previous business relationship, and subsequent dispute, between Eagle and the American International Group ("AIG").[4] In or around January 1998 and January 1999, Eagle entered into reinsurance agreements with affiliates of AIG, whereby AIG agreed to reinsure Eagle on specified insurance policies. AIG ceased performing, allegedly in bad faith, on the agreements in September 2000. Eagle subsequently initiated arbitration proceedings against AIG, in which the Commissioner participated, based on its role as Administrative Supervisor. Eagle and AIG eventually settled the claim on December 31, 2001. Pursuant to the terms of the settlement, which is memorialized in two Commutation and Release Agreements (the "Commutation Agreements"), AIG agreed to pay Eagle $148 million[5], which represented Eagle's projected reinsurance losses, less a $109 million credit, which Eagle held in a trust account for AIG's benefit against the termination of the reinsurance

[3] GSA and NCIC are also currently under consensual Administrative Supervision, currently in runoff status, and do not have any in-force policies.

[4] The Court's discussion of the previous business relationship, and the formation of the Farley Report, is based on the parties' previous submissions to the Court in the Commissioner's order to show cause seeking an order of rehabilitation.

[5] Specifically, AIG agreed to pay $24.3 million to Newark and $124.6 million to Eagle.

agreements. Additionally, the Commutation Agreements were executed in conjunction with a master agreement, dated January 1, 2002, between RPC and AIG and their respective affiliates (the "Master Agreement"). The Master Agreement provided that AIG would have significant management and control over certain RPC affiliates in exchange for AIG's promise to provide Eagle with financial support in an amount up to $150 million, which would be achieved through various surplus notes.

On February 1, 2002, the Commissioner approved the Master Agreement by entering Administrative Order A02-109 ("the Approval Order"). In entering the Approval Order, the Commissioner stated:

> Following the consummation of the Consolidation Agreement as embodied in the Transaction Documents, Eagle and [its subsidiaries] should be sufficiently capitalized so that they are likely to succeed in effecting a solvent run-off, thereby eliminating the need for Eagle [and its subsidiaries] to be placed in receivership by the Department.
>
> . . . .
>
> In the event that AIG fails to comply with the terms of this Order and/or any provision of the Transaction Documents regarding the capital support of up to $150 million, [or] the payment of the commutation payments . . ., the Commissioner reserves the right to require a special deposit or deposits from AIG in the future until such time as the liabilities of the RPC insurance subsidiaries no longer exist.

(Rehabilitation Cert. of Jasper J. Jackson, ¶¶ 31, 33, Exh. "E".)

Shortly after the Commissioner entered the Approval Order, a dispute arose between Defendants and AIG as to whether AIG accurately reported certain of its financials in calculating the $148 million commutation balance to be paid to Eagle by AIG. As a result of this dispute, the Commissioner directed Eagle's Administrative Supervisor, Alexander Farley ("Mr. Farley"), to conduct an in-depth examination to

verify the commutation balance. On April 14, 2005, after Mr. Farley submitted a draft report, and the Department allowed both AIG and Defendants to submit comments regarding the draft report, the Department wrote to RPC and AIG. (Id. at ¶ 49, Exh. "M".) Specifically, the letter stated, in pertinent part:

> This is to advise you that the Department does not accept the explanations provided by AIG to address the discrepancy in reserves on the commuted treaties. However, we note that the parties remain in discussions regarding their continued performance of services provided for under the terms of [the Agreement] between AIG and [RPC].
>
> This is to advise you that, at this time, the Department will not take any action regarding the concerns noted in the draft report, pending the outcome of said discussions. However, this decision should not be construed as a waiver of the Department's right to take action in this manner at a future date.

(Ibid.) Mr. Farley issued his final report (the "Farley Report") on September 20, 2005, and the Department notified RPC and AIG that it had accepted the Farley Report on September 27, 2005. Relevant portions of the Farley Report stated:

> *The primary interest of the Department [in entering the Approval Order] was the solvent runoff of RPC's New Jersey domiciled insurance companies. . . . Various terms of the Agreement were to provide for their solvent runoff with a reasonable degree of probability though not guaranteed.* The financial projections, developed to determine the adequacy of economic support to be primarily provided by AIG through the Agreement, showed that Eagle . . . would have $5 million in surplus at the end of the projection period in 2013. *Given the level of reserves with potential further development and other unknown factors including actual value of assets to be sold [such as Eagle's subsidiaries], the $5 million surplus margin left little room for variance.* [(emphasis added) (Background, at p. 1)]
>
> . . . .
>
> *In conclusion, while the AIG booked balances pertaining to the commutation have been verified, potential*

> *issues exist with respect to the accuracy and reasonableness of those balances* [based on the limited scope of the target review and limitation of data available], which could adversely impact RPC and the Companies' successful runoff. The impact on Eagle is the lost opportunity of investment income presently estimated to be $3.6 million and should a successful runoff occur the surplus note liability carried by Eagle will be $56.5 million less or a total of $93.5 million versus $150 million. [(Executive Summary, at p. 10)]

(Id. at Exh. "N".) Moreover, the Farley Report indicated that while Eagle is carrying a surplus note of $150 million, rather than $93.5 million, might indirectly affect the runoff of Eagle and its subsidiaries, the larger impact of such discrepancy would be felt by RPC and the amount it owed AIG under the profit sharing terms of the Master Agreement. (Ibid. (Executive Summary, at pp. 8-9).)

Subsequent to the September 28, 2006 hearing, on the Commissioner's order to show cause seeking an order of rehabilitation, the parties engaged in settlement conferences over the course of several months. On January 18, 2007, the parties entered into a settlement, which was placed on the record before the Court, and subsequently memorialized in a consent order entered by the Court on January 29, 2007 (the "Consent Order"). Pursuant to the terms of the Consent Order, the Court also entered an order of rehabilitation. Mr. Farley was appointed Deputy Rehabilitator.

Paragraph 2 of the Consent Order states, "The Department agrees to use its *best efforts* to effectuate, by April 16, 2007, the sale of two of Eagle's wholly owned subsidiaries, Newark and GSA, to American International Group ("AIG") under terms reasonably anticipated (taking into account potential adverse loss development) to achieve a solvent runoff of Eagle and its subsidiaries." (Emphasis added.) Essentially, Paragraph 2 of the Consent Order memorializes the intent to effectuate a transaction

originally contemplated, and negotiated, between RPC and AIG while the parties were in settlement negotiations pertaining to the Commissioner's order to show cause seeking an order of rehabilitation. According to the Commissioner, these previous negotiations failed due to RPC's insistence upon the inclusion of certain terms and conditions that were unacceptable to AIG and/or the Department.

Despite such failure, in and around December 2006, AIG indicated that it was still interested in pursuing a transaction to purchase Newark and GSA. AIG conditioned its interest, however, on first obtaining a determination of the size of Eagle's deficit (i.e. the dollar amount necessary to effectuate a solvent runoff that would determine the purchase price for the contemplated transaction). In order to determine Eagle's deficit, the Commissioner directed Mr. Farley to obtain the necessary financial data to make this determination. After obtaining and analyzing the pertinent information, it was determined that Eagle's deficit exceeded $24 million, an amount significantly larger than had been anticipated.

Nevertheless, Mr. Farley developed a presentation and presented such to AIG in the hopes that AIG would still be interested in completing the transaction based on other economic benefits—specifically certain tax advantages—the transaction would provide to AIG.[6] On March 1, 2007, retired past president of AIG, and consultant to AIG on the contemplated transaction, Mr. Hansen, indicated to Mr. Farley that AIG was not likely to be interested in pursuing the transaction. On March 1, 2007, the Commissioner spoke with the president of AIG's commercial lines division, Anthony DeSantis ("Mr.

[6] The estimated funding cost to AIG under the contemplated transaction was $9,458,231. It was believed by the Commissioner that AIG would be able to recoup its investment and earn a profit within a reasonable time through the premium tax advantages available to Newark and GSA, depending on the volume of business transferred from existing AIG subsidiaries to Newark and/or GSA.

DeSantis"), who confirmed that AIG was no longer interested in pursuing the contemplated transaction. According to the Commissioner, Mr. DeSantis indicated that the reasons for no longer having an interest in pursuing the transaction were threefold: Eagle's deficit had significantly increased since the beginning of discussions; concern that the premium tax advantages available to GSA and Newark would be eliminated within the near future by the New Jersey Legislature, and concern over the potential significant administrative costs involved in the transfer of business to Newark and GSA. AIG memorialized its discontinued interest in a March 8, 2007 letter from Mr. DeSantis to the Commissioner. Specifically, the March 8, 2007 letter stated, "AIG has seriously looked at all the available information and has concluded there is no interest in pursuing a transaction." (Cert. of Donald Bryan, Exh. "A".)

Based on AIG's representations, the Commissioner now brings the present order to show cause seeking an order of liquidation. Pursuant to Paragraph 7 of the Consent Order, "[i]n the event that the Department is unsuccessful in effectuating the sale of Newark and GSA as contemplated in Paragraph 2 above, the Department shall proceed to take such actions as the Department shall determine in its discretion shall best accomplish the statutory objectives and requirements of rehabilitation." According to the Commissioner, Eagle's rapidly deteriorating financial condition, and lack of other reasonable alternatives, renders additional efforts to rehabilitate Eagle useless.

With respect to other reasonable alternatives, it is set forth that Mr. Farley contacted an investment banking firm, experienced in the sale of New Jersey tax advantaged insurance companies. According to Mr. Farley, the investment banking firm represented that based on prior transactions recently completed, one might estimate sale

proceeds for another such company in the $5 million to $7 million range provided the company either had no liabilities or in-force business, or sold with indemnification from a financially secure parent. The Commissioner asserts that since both GSA and Newark still have claim reserve liabilities and a parent that is not financially secure to indemnify a buyer, the sale of GSA and Newark would either be difficult to consummate and, even if a sale could be consummated, it would be for an amount significantly less than the $5 million to $7 million indicated by the investment banking firm.[7] Therefore, the Commissioner maintains that it has exerted its "best efforts" in seeking all available avenues for rehabilitating Eagle. Moreover, the Commissioner asserts that seeking to compel AIG to pay the $60.1 million is not a reasonable alternative because AIG will vigorously defend any such demand, the result of which will be lengthy litigation, which would be detrimental to the public, the policyholders, and Eagle's creditors.

With respect to Eagle's rapidly deteriorating financial condition, the Commissioner asserts that Eagle is insolvent, as defined by N.J.S.A. 17:30C-1(a). Specifically, the Commissioner asserts that, as of December 31, 2006, Eagle and Newark have a combined negative surplus of $21,499, 534. According to the Commissioner, this, on its own, establishes the necessary grounds for a declaration of insolvency and grounds for liquidation pursuant to N.J.S.A. 17:30C-8 and N.J.S.A. 17:30C-6(a). Moreover, it is the Commissioner's position that further attempts to rehabilitate Eagle will be useless and substantially increase the risk to policyholders, creditors, and the public, as per N.J.S.A. 17:30C-7(b).

[7] The Commissioner has also determined that there are no other apparent or readily available sources of funds to provide adequate operating capital to Eagle and Newark to pay claims even on a partial basis while other avenues of rehabilitation are pursued.

In opposing the Commissioner's order to show cause, and in support of Eagle's motion to enforce the Consent Order, Eagle contends that the Department has failed to exert its "best efforts", and has instead engaged in a course of conduct designed to place Eagle in liquidation from the very start. To evidence this, Eagle relies on the deposition testimony of Mr. Farley, and the Director of Insurance, Donald Bryan ("Director Bryan").

Specifically, deposition testimony revealed that Director Bryan only organized one internal meeting to implement the Consent Order. While Director Bryan appointed a three person "point team" at that meeting for the purpose of negotiating with AIG, only Mr. Farley had any direct negotiations with AIG. The Commissioner did not attend the internal meeting, and neither attended or convened a meeting with AIG for the purpose of negotiating the contemplated transaction. This is so despite the fact that Director Bryan and the Commissioner attended a meeting with Mr. DeSantis on January 26, 2007 to discuss other matters. While Director Bryan did testify that at the conclusion of the meeting, he mentioned to Mr. DeSantis that AIG should devote resources to the Eagle transaction, Director Bryan also testified that Mr. DeSantis indicated that he was unfamiliar with the transaction. Regardless, Eagle contends that this did not amount to "best efforts", as Director Bryan never mentioned to Mr. DeSantis the possible ramifications to AIG if it did not agree to complete the deal with Eagle.

With respect to the actual negotiations with AIG, Eagle contends that the deposition testimony revealed that they were minimal at best. Mr. Farley characterized his initial meeting with the Chief Financial Officer of AIG's commercial lines division, Glen Pfiel ("Mr. Pfiel") as an "exploratory discussion", which resulted in Mr. Farley

passing on to Mr. Pfiel a two-page memorandum containing certain financial projections. Mr. Farley also called Mr. Hansen on March 1, 2007 to arrange to send him a one-page cost/benefit analysis, which purportedly detailed the net funding AIG would have to invest in GSA and Newark to achieve the solvent runoff of Eagle. At that time, Mr. Hansen indicated to Mr. Farley that AIG's personal lines division was not interested in the transaction. Mr. Hansen and Mr. Farley had dinner that evening, at which time Mr. Hansen confirmed the substance of their earlier conversation. This was the only face-to-face negotiation with AIG. As already stated, earlier that day Mr. DeSantis conveyed to Director Bryan that AIG was no longer interested in pursuing the transaction.

Eagle further contends that the Department has devoted more time pursuing liquidation of Eagle than exerting its "best efforts" to effectuate the contemplated transaction with AIG. To evidence this, Eagle relies on the timesheets of Mr. Farley and his assistant, which, according to Eagle, clearly indicate that Mr. Farley and his assistant spent minimal time preparing the "pitch" for the dinner meeting in March. Moreover, the time sheets indicate that much of the time spent by Mr. Farley and his assistant concerned the ongoing operation of Eagle, meetings with the Department or Attorney General, and/or preparation of the Department's petition for liquidation.

Eagle also contends that the Department and Mr. Farley have taken measures that are actually adverse to Eagle's interests, the effect of which seriously impedes the likelihood of a sale to AIG, or any other potential buyer for that matter. Moreover, Eagle contends that such actions are detrimental and contrary to the Department's obligation to rehabilitate Eagle. For instance, Eagle contends that while collecting a salary in excess of $70,000 per month for he and his staff, Mr. Farley has directed Eagle to terminate a

significant number of its regular staff and employees, including several employees with years of expertise handling and processing Eagle's claims of the other insurance companies that Eagle services. Additionally, Mr. Farley has directed that Eagle reduce the fees charged for servicing claims. According to Eagle, a reduced staff and reduced fees will cause Eagle to have limited prospects of financial success once GSA and Newark have been sold to AIG, or if otherwise rehabilitated.

Eagle also takes the position that, although the Department may have confirmed that it is unable to effectuate the sale of GSA and Newark to AIG, Eagle contends that prior to entering an order of liquidation the Department should still be required to effectuate the ultimate goal of the Consent Order by compelling the Department to either enforce the Farley Report or the "special deposit" provision of the Approval Order. Eagle contends that the Department's approval of the Farley Report equates to a final determination by the Department. Eagle contends that the Department is obligated to pursue action against AIG to compel them to make proper commutation payments. Eagle takes the position that the Farley Report clearly indicates that Eagle should have received $56.5 million more than the amount Eagle originally received ($148 million) under the Commutation Agreements. Eagle further takes the position that because of the understated commutation balance, Eagle also suffered $3.6 million in lost investment income. Therefore, Eagle contends that, consistent with the public policy of this State, the Department should be ordered to exercise its authority to collect the $60.1 million to remedy AIG's fraudulent understatement of the commutation balance.

In connection with this contention, Eagle maintains that offsetting the $56.6 million against the surplus notes is no longer a permissible method of addressing AIG's

understatement of the commutation balance. To evidence this, Eagle relies on AIG's restated 2004 Form 10-K annual report. Specifically, AIG restated its accounting treatment of the surplus notes:

> -*The Robert Plan*: AIG has restated the accounting for surplus notes purchased as part of a litigation settlement in 2002 with the Robert Plan Corporation (The Robert Plan). Pursuant to the settlement agreement, the surplus notes were to be repaid through profits received from a managing reinsurance general agency relationship with the Robert Plan. When AIG deemed that repayment under the surplus notes was unlikely, AIG recorded the impairment charge as realized capital losses rather than underwriting losses. AIG now believes that this accounting treatment was an error and has restated the impairment charges as underwriting losses.

(Cert. of Allison C. O'Sullivan, Exh. "G".) Eagle contends that this change is significant because it amounts to an admission that the surplus notes are not collectible as debt instruments. Moreover, the surplus notes could not be repaid unless and until profit sharing was triggered under the terms of the Master Agreement. Because this never happened, and never will happen based on AIG's write off, Eagle contends that the Court should compel the Department to collect the full amount of the understatement, plus the lost investment income, as it represents "property" of Eagle. Additionally, Eagle contends that because profit sharing was never triggered, and never will be, any possibility of the $56.5 million being utilized as an offset for surplus notes is expressly prohibited by N.J.S.A. 17:30C-27, as AIG's right to repayment under the surplus notes is not ripe.[8] Moreover, in Eagle's view, the Department has already tacitly acknowledged as much in an April 10, 2007 demand letter from Director Bryan to AIG seeking to collect the $3.6 million in lost investment income.

[8] Eagle also contends that, even if the surplus notes were collectible, they would only be assessed as a general unsecured claim at the conclusion of these proceedings.

Alternatively, Eagle contends that the Court should compel the Department to enforce the "special deposit" provision of the Approval Order. Under the Approval Order, the Department expressly reserved the right to require a special deposit from AIG should AIG fail to pay the appropriate commutation balance or otherwise breach the terms of the Approval Order. Eagle contends that AIG has breached the Approval Order through its falsely representing the commutation balance as only $148 million, when in fact it should have been $204.5 million. Therefore, Eagle maintains that before the Court can properly enter an order of liquidation, it should direct the Department to enforce the "special deposit" provision pursuant to N.J.S.A. 17:30C-7(a).

Lastly, Eagle takes the position that there are substantial issues of fact pertaining to whether the Department exerted its "best efforts" to effectuate the transaction with AIG, whether further efforts to rehabilitate would be useless, and why the Department has failed to either enforce the Farley Report or enforce the "special deposit" provision. Therefore, Eagle contends that at the very minimum a plenary hearing should be held prior to the Court determining that the appropriate course of action is to enter an order for liquidation.

The immediate issue is whether to grant the Commissioner's order to show cause seeking an order of liquidation, or Eagle's motion to enforce the Consent Order. It has historically been held that "the Commissioner is presumed to have expertise in the field of insurance, and that expertise must be given great weight by the court." IFA Ins. Co. v. New Jersey Dept. of Ins., 195 N.J. Super. 200, 207 (App. Div. 1984). It is with consideration of this deference that the Court addresses, in turn, Eagle's motion and the Commissioner's order to show cause.

It is well settled that settlement of litigation ranks high in New Jersey's public policy. Nolan v. Lee Ho, 120 N.J. 465, 472 (1990) (citing Jannarone v. W.T. Co., 65 N.J.Super. 472 (App. Div. 1961). Generally, "[a]n agreement to settle a lawsuit is a contract which, like all contracts, may be freely entered into, and which a court, absent a demonstration of 'fraud or other compelling circumstances' shall honor and enforce as it does other contracts." Pascarella v. Bruck, 190 N.J. Super. 118, 125 (App. Div. 1983) (quoting Honeywell v. Bubb, 130 N.J. Super. 130, 136 (App. Div. 1974)). In enforcing settlement agreements, courts must ascertain the intention of the parties from the language of the agreement, and once such intentions are ascertained, the parties are bound by those intentions. See Jacobs v. Great Pacific Century Corp., 104 N.J. 580, 582 (1986) (positing that "[t]he polestar of contract construction is to discover the intention of the parties as revealed by the language used by them"); Schor v. FMS Financial Corp., 357 N.J. Super. 185, 191 (App. Div. 2002) (stating that "a party to a contract is bound by the apparent intention he or she outwardly manifests to the other party"). While courts must determine the intention of the parties to the settlement agreement, "[w]here the terms of the contract are clear and unambiguous there is no room for interpretation or construction and the courts must enforce those terms as written." Kampf v. Franklin Life Ins. Co., 33 N.J. 36, 43 (1960). Therefore, where the language of an agreement is clear and unambiguous, courts "have no right to rewrite the contract merely because one might conclude that it might well have been functionally desirable to draft it differently." Schor, supra, 357 N.J. Super. at 192.

Initially, the Court notes that neither the Commissioner nor Eagle dispute whether the language of the Consent Order is "clear and unambiguous" as to the issue of "best

efforts"; rather the parties' dispute centers on whether the Commissioner has in fact complied with the obligations set forth in the Consent Order. Therefore, the Court limits its analysis of Eagle's motion to the issue of whether the Commissioner exerted its "best efforts" in attempting to negotiate the sale of GSA and Newark to AIG, and whether the other steps—if any—taken by the Commissioner were consistent with the statutory objectives and requirements of rehabilitation.

Pursuant to Paragraph 2 of the Consent Order, the Department must use its "best efforts" to effectuate the sale of GSA and Newark. While Eagle contends that the Commissioner failed to exert its "best efforts", the Court disagrees. As a practical matter, Eagle's argument on this point, when stripped to its basics, centers on the exact same issue in dispute in the Commissioner's order to show cause for an order of liquidation, and is the exact same issue disputed throughout the Commissioner's order to show cause for an order of rehabilitation—that the Department has failed to invoke any of the purported legal rights and remedies it has against AIG regarding its failure to pay the $60.1 million due to Eagle as set forth in the Farley Report. In other words, Eagle takes the position that the Commissioner failed to "us[e] its muscle to effectuate the sale" (i.e. failed to apprise AIG of the legal recourse the Department may have against AIG). (See Eagle Opposition Brief, at 9.)

Whether the Commissioner failed to "us[e] its muscle to effectuate the sale," does not appear to be relevant to a determination of whether the Commissioner exerted its "best efforts" in negotiating the contemplated transaction. In fact, it appears to the Court from the evidence presented, including the depositions taken in preparation for the hearing on the motion and order to show cause, that AIG likely decided to discontinue its

interest in the contemplated transaction prior to the Commissioner having the opportunity to exert to the full extent its "best efforts". When AIG expressed its renewed/continued interest in pursuing the purchase of GSA and Newark, it conditioned such interest on the amount of Eagle's deficit. Upon learning, in the very early stages of negotiations following entry of the Consent Order, that Eagle's deficit exceeded $21 million AIG discontinued its interest in the contemplated transaction. Moreover, AIG indicated that even if the contemplated transaction provided other benefits, it did not believe such benefits outweighed the detriment of Eagle's deficit. Specifically, AIG expressed concern that the New Jersey Legislature would repeal, in the near future, the premium tax advantages afforded to GSA and Newark.

Additionally, the irrelevance of the Commissioner's failing to apprise AIG of any liability it may have if AIG chose not to consummate the contemplated transaction is evidenced by AIG's April 19, 2007 response to Director Bryan's April 10, 2007 demand letter to AIG seeking the $3.6 million in lost investment income:

> [Among other things,] AIG Companies will not comply with the demand [because] . . . [a]s set forth in our letters of August 13, September 20, and October 29, 2004 . . ., the Farley Report does not constitute a basis for Eagle to seek funds from AIG Companies beyond the nearly $400 million it has already received in payments pursuant to the Master Agreement.

(Cert. of Emerald Erickson Kuepper, Exh. "A".) Moreover, AIG's response is consistent with its position on the alleged understatement of the commutation balance throughout the history of this dispute. To suggest that a different outcome would have resulted had the Department apprised AIG of its legal liability if it did not follow through on the contemplated transaction simply ignores the realities of the situation; that AIG has firmly

entrenched its position that such monies are not owed to Eagle. Consequently, it does not appear to the Court that the inability to effectuate the sale of GSA and Newark to AIG was the result of a failure to put forward "best efforts"; nor does it appear to the Court that there are disputed issues of material fact pertaining to whether the Commissioner complied with its obligation under Paragraph 2 of the Consent Order.

However, this does not end the inquiry, as Paragraph 7 of the Consent Order provided that if effectuating a sale is unsuccessful, the Department must take whatever actions *it deems necessary* to best accomplish the statutory objectives and requirements of rehabilitation. The parties dispute whether the Department has taken the necessary actions, separate and apart from the sale of GSA and Newark to AIG, to best accomplish the objectives of rehabilitation. Resolution of this dispute turns on whether the Court should compel the Commissioner to either enforce the Farley Report or the "special deposit" provision of the Approval Order. As a practical matter, Paragraph 7 of the Consent Order essentially mirrors N.J.S.A. 17:30C-7(a), which provides that "[a]n order to rehabilitate . . . shall direct the commissioner . . . to take such steps toward removal of the causes and conditions which have made rehabilitation necessary, as the court may direct." The exception of course being that Paragraph 7 of the Consent Order appears to give the Commissioner the unilateral authority to take additional action, as evidenced by the "as it deems necessary" language, whereas N.J.S.A. 17:30C-7(a) permits the Court to direct that the Commissioner take additional action.[9] Under either scenario, the Court still retains the authority to pass on whether the Commissioner has acted consistently with the goal of rehabilitation—to exert the necessary efforts to remove the reasons for

[9] Presumably, even with such a grant of authority, the Court would still heed to the expertise of the Commissioner if the circumstances required such.

placing Eagle into rehabilitation in the first instance.[10] Because of this parallel between Paragraph 7 of the Consent Order and N.J.S.A. 17:30C-7(a), the Court consolidates its analysis of whether the Department has complied with Paragraph 7 of the Consent Order in the context of the Commissioner's order to show cause seeking an order of liquidation.

Pursuant to N.J.S.A. 17:30C-3, only the Commissioner may make an application for an order of liquidation. Presumably, this authority is rooted in the Commissioner's presumed expertise in the field of insurance. Consistent with this presumed expertise, N.J.S.A. 17:30C-7(b) provides, "If at any time *the commissioner* deems that further efforts to rehabilitate the insurer would be useless, *he may apply* to the court for an order of liquidation," provided the Commissioner can satisfy one of the grounds for liquidation set forth in N.J.S.A. 17:30C-8. (Emphasis added.) Here, the Commissioner has determined that further efforts to rehabilitate Eagle would be useless.

Specifically, the Commissioner asserts that Eagle is insolvent pursuant to N.J.S.A. 17:30C-1(a).[11] "The Court will grant an order of liquidation if the insurer is indeed insolvent." In re Integrity Ins. Co., 147 N.J. 128, 135 (1996). According to the Commissioner, as of December 31, 2006, Eagle's net admitted assets total $21,405,555 and its liabilities total $38,141,400, resulting in a negative surplus of $16,735,844. Additionally, Newark's admitted assets total $6,002,610 and its liabilities total $10,766,300, resulting in a negative surplus of $4,763,690. Eagle and Newark's combined negative surplus is $21,499,534, and therefore, the Commissioner asserts that it has clearly set forth a ground for seeking liquidation. See N.J.S.A. 17:30C-8, N.J.S.A.

[10] The Court recognizes that the parties consented to an order of rehabilitation as part of the Consent Order.
[11] N.J.S.A. 17:30C-1(a) provides that an insurer is insolvent "when such insurer is not possessed of assets at least equal to all liabilities and required reserves together with its total issued and outstanding capital stock."

17:30C-6(a). Even if Eagle is not in fact insolvent, the Commissioner, pursuant to N.J.S.A. 17:30C-8 may move for an order of liquidation if it is determined that Eagle is in a "hazardous financial condition."

Our courts have also posited that the Commissioner's determination that an insurance company's further transaction of business would be "hazardous" within the meaning of N.J.S.A. 17:30C-6(f) is a finding of fact. Samuel F. Fortunato, Comm'r of Ins. of the State of N.J. v. New Jersey Life Ins. Co., 254 N.J. Super. 420, 425 (App. Div. 1991). Such a finding "is an informed prediction that [the insurance company's] financial condition, even if it is technically solvent, substantially threatens the justifiable interests of policyholders, stockholders, creditors, or the public. These are interests whose protection the legislature has confided to the Commissioner of Insurance." Ibid. Therefore, even if Eagle is not technically insolvent, an order of liquidation may still be properly entered if it is found that Eagle is in a "hazardous financial condition".

Eagle contends that it is neither insolvent nor in a "hazardous financial condition", as it is entitled to recover $60.1 million in understated commutation balances. Therefore, Eagle contends that the Court should compel the Commissioner to either enforce the Farley Report or enforce the "special deposit provision" in the Approval Order. With respect the "special deposit" provision in the Approval Order, it is clear from the language of the Approval Order that the Commissioner only reserved the right to require "special deposits." Moreover, the Approval Order only covered the original commutation balance of $148 million, and not the additional $60.1 million found to be owing to Eagle in the Farley Report. While the Court agrees with Eagle's contention that it could direct the Commissioner, pursuant to N.J.S.A. 17:30C-7(a), to enforce the

"special deposit" provision, the Court does not agree with Eagle that it is a viable option in the present matter, as the plain language of the Approval Order only encompasses the $148 million in commutation balances, and not the additional $60.1 million.

With respect to the Farley Report, Eagle contends that the Court should compel the Commissioner to enforce the Farley Report, prior to there being an order of liquidation, as enforcement of the Farley Report would likely remove Eagle from insolvency and/or a hazardous financial condition. The question arises for the Court whether the Commissioner is obligated to enforce the Farley Report. While the parties do not address in detail whether the Commissioner is obligated to do so, the parties addressed this issue in detail on the Commissioner's order to show cause seeking an order of rehabilitation. Presumably, the arguments remain the same.

While the Commissioner is expressly authorized to conduct an examination of an insurance company's affairs pursuant to N.J.S.A. 17:23-22, and the Commissioner is subsequently required to either adopt, reject or call an investigatory hearing with regard to the examination report pursuant to N.J.S.A. 17:23-24(c), the Commissioner is not required to take action against any violations revealed from such report. N.J.S.A. 17:23-24(c)(1) states that, in the event of the Commissioner's approval of an examination report, "the commissioner *may* . . . take any action the commissioner considers necessary and appropriate to cure [any violations revealed by the examination report]." (emphasis added) The clear language of this statutory provision indicates that the Commissioner has the discretion to determine the appropriate action to take. The "necessary and appropriate" language of this provision reinforces the Commissioner's expertise in these matters, and further echoes the deference that courts should give the Commissioner when

scrutinizing his actions. Therefore, because of the discretionary nature of the Commissioner's duties with respect to enforcing the findings of an examination report, the Court will not usurp the Commissioner's discretionary powers by finding that the Commissioner was obligated to enforce the Farley Report.

The inquiry does not end here, however, as Eagle is currently in rehabilitation, and as already stated, the Commissioner is obligated, pursuant to N.J.S.A. 17:30C-7, "to take such steps toward removal of the causes and conditions which have made rehabilitation necessary." Moreover, a reasonable reading of N.J.S.A. 17:30C-7, allows for courts to direct the Commissioner to take certain actions under certain circumstances. Here, compelling the Commissioner to enforce the Farley Report against AIG is intriguing given Director Bryan's April 10, 2007 demand letter to AIG, as it appears that the Department has now adopted or accepted that AIG understated the commutation balances, and that Eagle is entitled to the additional $60.1 million. This is evidenced by Director Bryan's seeking to obtain the $3.6 million in lost investment income. The import of this is that the Commissioner would not demand that AIG turn over the $3.6 million in lost investment income if it did not believe that it was entitled to the corpus—the $60.1 million. Therefore, it could reasonably be argued that this Court, consistent with its statutory requirements, could require the Commissioner to first attempt to enforce the Farley Report prior to entering an order of liquidation. Yet, to what end.

The Commissioner has determined that Eagle is now not only in a "hazardous financial condition", but is insolvent as defined in N.J.S.A. 17:30C-1. There is no factual dispute as to this issue. The Court is concerned over the time it would take for the Commissioner to enforce the Farley Report against AIG, as AIG has taken a steadfast

position that it is not liable for the additional amounts set forth in the Farley Report. The role of the Commissioner during rehabilitation is to "step into the shoes" of the insurance company and actively manage the company and pursue any claims or rights deemed by the Commissioner to be in the best interests of the policyholders, shareholders and the public. Here, based on Eagle being in a hazardous financial condition, now insolvent, a condition that will likely not improve with the passing of time, the Commissioner has determined that pursuing such claims are not in the best interests of the policyholders, shareholders and the public.

The Court finds the position of the Commissioner to be reasonable at this time. The Commissioner has determined, in his wisdom and with his level of expertise, that pursuing these claims at this time would not be in the best interests of preserving Eagle in its presently insolvent condition. Eagle argues that it is almost a "slam dunk" while the Commissioner clearly looks at it differently – that any litigation has its risks and the costs would be substantial. Even if the litigation (administrative or court) were successful, it is not clear that it would ultimately change Eagle's hazardous insolvent financial condition. If the litigation was unsuccessful, the shareholders would most likely be in no worse a position; however, the unsuccessful litigation could worsen the positions of the policyholders, creditors and the public. Where the risk to the policyholders, creditors and the public is so substantial and where it is undisputed that Eagle is presently in a hazardous and insolvent financial condition satisfying the criteria of the statute, the Court does not believe it should force the Commissioner into an uncertain litigation with uncertain results.

Eagle is correct in citing LaVecchia v. HIP of New Jersey, 324 N.J. Super. 85 (Ch. Div. 1999) for the proposition that the Court's obligation in reviewing an application for rehabilitation as opposed to one for liquidation is considerably different. As. Judge Lintner explained:

> As Rehabilitator, the Commissioner has the discretion to determine the manner in which rehabilitation will proceed and must submit a plan which is subject to approval, disapproval, or modification by the court based upon its judgment as to what is fair and equitable to all parties concerned. *N.J.S.A.* 17B:32-43(e). Thus, while the Commissioner's plan for rehabilitation cannot be implemented without a court finding that it is fair and equitable, deference is given to the means the Commissioner chooses to utilize in going forward with rehabilitation. As such, the Rehabilitator's determination concerning the manner in which to proceed will not be set aside unless it is shown to be arbitrary or unreasonable. *Fortunato v. New Jersey Life Ins. Co.*, 254 *N.J. Super* 420, 603, *A*.2d 964 (App. Div.1991). Likewise, the Rehabilitator's decision to reject the plan submitted by HIPNJ is also entitled to deference and is not subject to review unless it is arbitrary or unreasonable.
>
> *N.J.S.A.* 17B:32-45(a) gives the Commissioner the discretion to file a petition for liquidation when she believes that further rehabilitation would be futile or substantially increase the risk of loss to the policyholders, creditors or the public. By requiring that deference be give to the Commissioner's decision to seek a change in status of the insurer from rehabilitation to liquidation by the filing of a petition, *N.J.S.A.* 17B:32-45(a) is consistent with *N.J.S.A.* 17B:32-43(e), which gives the Commissioner the discretion to determine the manner in which rehabilitation will proceed.
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> While deference is to be given the Commissioner's decision to seek liquidation under *N.J.S.A.* 17B:32-45(a), such is not the case when it comes to entry of an order for liquidation in accordance with *N.J.S.A.* 17B:32-46. An order for liquidation is preceded by the filing of a petition setting forth grounds for liquidation. The petition filed under *N.J.S.A.* 17B:32-46 is subject to the insurer's right to plead defenses as granted by *N.J.S.A.* 17B:32-45(a). Once a defense is raised, the court must resolve any issues of fact in determining whether

> or not grounds exist for the entry of an order of liquidation. For these reasons, the Commissioner's position that an order of liquidation must be entered absent a finding that her determination to seek liquidation is unreasonable or arbitrary is rejected. The defendant is entitled to a hearing on any issues of fact that exist concerning the grounds for liquidation.

324 N.J. Super. at 91-92.

There is no question that HIP requires the Court to have a plenary hearing on any issues of fact concerning the grounds for liquidation as opposed to the standard of review by a court when the Commissioner seeks rehabilitation. Yet, here no factual dispute has been submitted to the Commissioner's basis for seeking liquidation – that is that pursuant to N.J.S.A. 17:30C-8 Eagle is presently in an insolvent condition.

The financials that the Commissioner has presented are not refuted. Rather, it is Eagle's claim that the Commissioner did not use its "best efforts" to obtain the sale of Newark and GSA to AIG in accordance with the settlement of January 18, 2007 or did not proceed on the Farley report or that the "special deposits" should be pursued prior to liquidation. The Court has previously discussed that these three components cannot be considered at this time to forestall the liquidation order. Nor is there any factual issue which requires a plenary hearing. As set forth earlier, the components upon which Eagle relies are components that must be evaluated by the Commissioner under a risk/benefit/cost analysis to determine what action should be taken. The Commissioner has determined that it is not in the best interests of the policyholders, creditors and the public at this time – a decision the Court will not presently disturb based upon the unrefuted financials presented. Discovery and a hearing would not change this result.

This Court will defer to the "litigation" strategy of the Commissioner as to these three components.

Therefore, for the abovementioned reasons, Eagle's motion to enforce the settlement is DENIED, and the Commissioner's order to show cause seeking and order of liquidation is GRANTED.