IN THE SUPREME COURT OF BERMUDA

CONSOLIDATED ACTION

Civil Jurisdiction
2003: No. 26

BETWEEN:

MUTUAL HOLDINGS (BERMUDA) LIMITED

Plaintiff

And

(1) AMERICAN PATRIOT INSURANCE AGENCY INC
(2) KENNETH A HENDRICKS
(3) DIANE M HENDRICKS

Defendants

Civil Jurisdiction
2004: No. 196

BETWEEN:

(1) AMERICAN PATRIOT INSURANCE AGENCY INC
(2) KENNETH A HENDRICKS
(3) DIANE M HENDRICKS

Plaintiffs

And

(1) MUTUAL INDEMNITY (BERMUDA) LIMITED
(2) MUTUAL RISK MANAGEMENT LIMITED
(3) COMMONWEALTH RISK SERVICES L.P.
(4) GLENN PARTRIDGE
(5) DAVID ALEXANDER
(6) RICHARD TURNER
(7) ANDREW S. WALSH

Defendants

JUDGMENT

Dates of Hearing: 5 to 12, 14 to 18, 26 to 31 May 2010

Date of Judgment: 9 July 2010

Mr. Andrew Martin, Mello Jones & Martin, for the Plaintiffs

Mr. Paul Smith and Mr. Ben Adamson, Conyers Dill & Pearman, for the 1st, 2nd and 4th to 7th Defendants

Introduction

1. This judgment follows from the trial of consolidated proceedings dating back to 2003 and 2004. The plaintiffs in the 2004 proceedings were treated as the plaintiffs in the consolidated proceedings. At the core of the original dispute between the parties is an allegation of fraud in relation to the renewal of an insurance programme in early 2000, said to have had its genesis at a meeting which took place at the offices of the first plaintiff ("American Patriot") in the state of Illinois in the United States, in February 2000. This meeting was attended by the third plaintiff ("Mrs. Hendricks"), and Lysa Saran, the president and chief operating officer of American Patriot on the one hand, and James Agnew and Eric Bossard, both of whom at the material time were either employed by or held office in the third defendant ("Commonwealth") on the other. Mr. Bossard also held a position at the material time as vice president of underwriting at Legion Insurance Company ("Legion"), a company within what I will loosely refer to at this stage as the Mutual Group, which I will cover in more detail shortly. Mr. Bossard described himself in his witness statement as an employee of Legion.

2. Although the meeting in Illinois could be described as the start of the alleged fraud, the real fraud is alleged by American Patriot and Mrs. Hendricks to have been decided upon at a meeting which took place at the offices of the fourth defendant, Glenn Partridge. Messrs. Agnew and Bossard said in their witness statements that they received instructions at this meeting to misrepresent the true position in relation to American Patriot's and Mrs. Hendricks' obligations under

the insurance programme. I will come back to the details of the alleged fraud, but will first give more detail about the various parties.

3. American Patriot was at all material times a licensed insurance brokerage agency incorporated in Wisconsin in the United States, with its principal office in Illinois. It was owned by the second plaintiff and Mrs. Hendricks, although the former died in December 2007 and did not play any part in the material events. In her witness statement, Mrs. Hendricks described how American Patriot had established an insurance programme ("the Programme" or "the American Patriot Programme") named "the Roofers' Advantage", in order to offer workers' compensation, employer's liability, auto liability and general liability insurance coverage to roofing contractors who were customers of a related business owned by the Hendricks. Mrs. Hendricks described these various types of insurance as being part of the Programme, which she said was designed to provide roofing contractors with an alternative market to commercial insurance products. The Programme also served as an investment vehicle for American Patriot.

4. I now turn to the Mutual Group. At the top of the corporate structure was the second defendant ("MRM"), whose chairman and chief executive officer throughout virtually all of the material time was Robert Mulderig. I use the words "virtually all of" because Mr. Mulderig's involvement did not extend to the finalisation of the commutation agreement referred to subsequently. The MRM operations were essentially divided into offshore and onshore entities, and all of the witnesses for the defendants stressed the importance for tax purposes of ensuring that none of the offshore companies carried on business within the United States. Below MRM in the offshore corporate chain was Mutual Holdings (Bermuda) Ltd ("Mutual Holdings"), which in turn owned the first defendant ("Mutual Indemnity"). The latter company was not incorporated until 1993. Onshore companies within the Mutual Group included two insurance companies which ultimately went into liquidation or rehabilitation in the United States, Legion, and Villanova Insurance Company ("Villanova"). Both Legion and Villanova were owned by MRM. Commonwealth operated as the marketing/sales production arm of Legion and other companies within the Mutual Group,

although it was neither a licensed broker nor a licensed insurance company. There is an issue as to whether Commonwealth ever acted for MRM or Mutual Indemnity. I should add here that Commonwealth has taken no part in these proceedings.

5. Turning to the individual defendants, Glenn Partridge was at the material time executive vice president of Legion, in charge of underwriting. He had originally been employed by Commonwealth, but that had not been the case since 1987. He was also a member of the board of MRM. David Alexander was at the material time a vice president of Mutual Holdings, and the president of Mutual Indemnity; he was also an AVP of MRM, which is the company that he described as his employer. Richard Turner was president of Commonwealth from 1984 until 2002, and was also a senior or executive vice president of MRM and a director of MRM, Mutual Indemnity and Legion. Andrew Walsh indicated in his witness statement that he was the general counsel for the onshore subsidiaries of MRM, although in fact employed by a company named Legion Management Corporation. He said that he acted as general counsel for Legion, Villanova, Commonwealth and other onshore entities within the Mutual Group. Mr. Walsh indicated that there were probably 30 or 40 different such onshore entities at one time or another during his employment. The plaintiffs' case is that Mr. Walsh acted for both the onshore and offshore companies within the Mutual Group. Finally, in relation to Messrs. Partridge and Turner, they, with Mr. Mulderig, were three of the top four executives within the Mutual Group.

The Programme

6. As Mr. Agnew indicated in his witness statement, at all material times, MRM marketed and advertised its ability to provide "rent-a-captive" insurance programmes in the United States through its network of subsidiaries. The rent-a-captive facility was marketed by Commonwealth with a standard programme proposal to prospective clients which was modified in certain respects to fit the needs of the different clients. In his witness statement, Mr. Alexander described the two distinct categories of rent-a-captives offered by the Mutual offshore companies, which he divided into corporate business and agency business. The

American Patriot Programme fell into the latter category. The Programme was described by Mr. Alexander by the use of the term "IPC", which was a marketing term meaning insurance profit centre. Within the Mutual Group offshore companies there was an IPC team, and Mr. Alexander referred in his witness statement to the IPC product which offered benefits to the IPC client by means of cheaper insurance, through the return of investment income generated on the particular programme, and the possibility of underwriting profits if loss pay-outs were low. However, the possibility of profit carried with it the risk of loss, something which the IPC client should have known.

7. In the case of agency business, the IPC client would not be the ultimate insured (as was the case in corporate business), but would typically be an insurance broker or agency which controlled a book of similar risks. In this case, American Patriot was the IPC client. Legion issued insurance policies to the underlying insureds, the roofing contractors who were customers of the Hendricks' other businesses. Legion itself would retain a small part of the first layer of cover, for regulatory purposes, but Mr. Alexander essentially ignored this in his description of the Programme, and it has no relevance for the purpose of this case.

8. Having issued insurance policies, Legion would cede the risk to the IPC reinsurer, which in this case was Mutual Indemnity, and the IPC client (in this case American Patriot) would undertake to indemnify the IPC reinsurer against losses on the Programme in exchange for receipt of any underwriting profit realised. That exercise was undertaken indirectly, by a shareholder agreement between the IPC client and Mutual Holdings. I shall refer to the agreement between American Patriot and Mutual Holdings dated 23 March 1997 as the Shareholder Agreement. This was subject to regular amendments upon renewal of the Programme. Under the Shareholder Agreement, if there was an underwriting profit, Mutual Indemnity would declare a dividend to Mutual Holdings, and the latter would pass such profit on to the IPC client. Hence the IPC client would take on the risk and rewards of the reinsurance undertaken by Mutual Indemnity, and would also earn fees by way of commission on the initial placement of business.

9. Mr. Alexander described how the risk on programmes such as the Programme was divided into layers. The first layer constituted the loss fund, which was calculated by reference to a specified proportion of written premium, and was ceded to Mutual Indemnity as the IPC reinsurer. Claims within the retention covered under the policies fell first to be paid out of the loss fund.

10. If losses exceeded the loss fund, they would be covered by the reinsurance provided by the IPC reinsurer, but the IPC reinsurer would in turn be secured by security deposits of collateral provided by the IPC client, so that it was effectively the IPC client, American Patriot in this case, which was at risk rather than Mutual Indemnity as the IPC reinsurer. This second layer was referred to as "the Gap", which was the layer between the loss fund and a cap known as the aggregate attachment point ("the AAP"). The AAP would be set as a percentage of gross written premiums when the particular IPC client entered into the programme for the year, and the percentage would differ according to the individual programme, the line of business, and overall market conditions.

11. Mr. Alexander described how the Gap was the principal area of risk/reward for the IPC client; the client would typically expect to lose the loss fund, and would profit if losses did not enter the Gap. If losses did enter the Gap, the IPC reinsurer would pay claims, and in turn recover from the IPC client under the indemnity provisions contained in the Shareholder Agreement. In this regard the IPC reinsurer's risk was normally collateralised, either by way of letters of credit or by cash collateral. In this case, there were some four letters of credit in place, in respect of which there arose disputes between the two sides, which led to injunctions being granted within the United States, and indeed at an earlier stage of these proceedings an application was made to me to restrain Mutual Indemnity from drawing down upon two specified letters of credit. By a ruling dated 1 December 2005 I declined to grant the relief sought. In the United States, there was litigation in Illinois, Michigan and California, with injunctions being obtained in Michigan and California; Mutual Indemnity was ultimately able to obtain the discharge of the Michigan injunction, and at this point, only one letter of credit, in the amount of $3,072,107.50 remains frozen.

12. Above the AAP was a layer of risk covered by independent third party reinsurance. Mr. Alexander indicated that for a typical IPC programme, Legion would purchase approximately $5 million of reinsurance coverage for each programme, although this figure would vary. If the IPC client wished to reduce its exposure, the AAP could be set at a lower figure, with more third party reinsurance.

13. Mr. Alexander described how the original IPC model had these three layers of risk, being the loss fund, the Gap, and the third party reinsurance, but he indicated that that model had changed in 1993 with the introduction of a new, higher layer. I should interject here that there is an issue between the parties both as to the existence of this fourth layer and whether such existence was ever communicated to the plaintiffs. The introduction of this fourth layer came about because the Pennsylvania insurance authorities (which regulated Legion) did not think that there was sufficient risk transfer in the Programme, thereby creating regulatory issues for Legion. The reality, of course, was that the IPC reinsurer was not supposed to retain risk, and Legion's retention was covered by the loss fund, but in any event the IPC model was restructured in 1993 (though the arrangements were made effective "as of 1 January 1991"), and the relevant treaty was amended to provide for an additional layer of reinsurance coverage, which was provided in the first instance by three Mutual Group companies. Mutual Indemnity had not been incorporated until 1993, and so was not one of these three, but was added (or apparently added) to the treaty by amendment at a later date. This late addition subsequently gave rise to an argument which was put forward in the commutation discussions between MRM on the one hand and the Pennsylvania Insurance Commissioner in her capacity as rehabilitator of Legion and Villanova on the other, that Mutual Indemnity had not been bound by clause 3A of treaty 103, the relevant provision. The parties agreed the terms of a commutation agreement which was ultimately approved by the Commonwealth Court of Pennsylvania, and the plaintiffs rely upon those terms as part of their case. They do so because the argument, accepted by the Pennsylvania Insurance Commissioner, was that Mutual Indemnity did not have any liability beyond the AAP, by reason of not

being at risk in this higher layer because it had not been a party to the amendment to the treaty.

14. It is to be noted that, according to Mr. Alexander and the other defendant witnesses, until the American Patriot Programme, there had been no instances of any programme losses exceeding the third party reinsurance layer, and it appears to have been relatively unusual for that layer to have been reached.

15. Finally, for completeness, I should refer to the position in the event that losses were to go beyond the fourth layer. In such a case (according to Mr. Alexander) the risk would remain with Legion, and would not pass to the IPC client; this was because the risk would not be covered by the reinsurance treaty between Legion and the IPC reinsurer, which meant that the IPC client (American Patriot) had no liability under the particular shareholder agreement to indemnify the IPC reinsurer (Mutual Indemnity), because the IPC reinsurer was not itself on risk beyond the fourth layer.

Claims Management

16. I shall refer to this relatively briefly. Claims handling for the IPC programme was carried out by professional claims managers referred to as third party adjusters or TPAs. There was originally an issue as to the independence of the TPA appointed in respect of the American Patriot Programme, a company named Cunningham Lindsey Claims Management Inc ("Cunningham Lindsey"). The defendants' position was that Cunningham Lindsey was an independent TPA over which none of the Mutual Group companies had any oversight or responsibility. For the plaintiffs there was originally a claim that MRM had responsibility for the alleged poor performance of Cunningham Lindsey in terms of its claim management, and particularly in relation to under-reserving. The plaintiffs have taken proceedings against Cunningham Lindsey in the Commonwealth of Pennsylvania, and have now indicated that they will give credit in respect of any amounts recovered in those proceedings, and do not pursue such claims against MRM.

The Pleadings

17. The amended statement of claim was dated 31 March 2010, following leave which I granted to make amendments which deleted the claim based upon the alleged failures by Cunningham Lindsey, and sought a declaration that Mutual Indemnity was not bound by clause 3 A of the reinsurance agreement (this being the clause which had added the fourth layer referred to in paragraph 13 above), and which also sought declarations in relation to the draw-downs of the letters of credit. A further amendment was made at the commencement of trial (in fact in the form of a re-amended defence and counterclaim to proceedings number 26 of 2003) in relation to the issue of the preference share which constituted the mechanism for underwriting profit to be returned to the IPC client. There had been a discovery dispute relatively late in the day in relation to this aspect of matters, since a search of the share register had suggested that the preference share had never been issued. There were more detailed complaints in relation to this aspect of matters, which came to be referred to as the corporate law issues. This late amendment led Mr. Smith to make an application at the start of his clients' case to bifurcate the corporate law issues to a separate hearing, on the grounds that he had not had time to make a full enquiry in relation to the facts, or to consider the law. In the event, the need for bifurcation was postponed in the first instance, and ultimately not pursued. I shall address the detail of the corporate law issues in due course.

18. Going back to the original pleadings, the first real area of dispute raised in the pleadings is in relation to the different Mutual Group companies, and more particularly their inter-relationship, and the responsibility of one for the acts of another. The plaintiffs plead that MRM was responsible for a wide variety of services in relation to the Programme, whether undertaken on its own behalf or by other companies within the Mutual Group. It is pleaded that Commonwealth acted both as MRM's agent and intermediary, and that it was MRM which negotiated the Shareholder Agreement which provided for an indemnity to be given by the IPC client to the IPC reinsurer, Mutual Indemnity. The description of MRM's activities contained in the pleading led to an averment that MRM

entered into an implied collateral contract with each of the participants in the Programme which included an obligation on the part of MRM to:

(i) manage the Programme generally;

(ii) manage the underwriting rates and guidelines to ensure that only appropriate accounts were written, that premiums were set at a level sufficient to cover expected losses, and that claims were properly managed;

(iii) manage the claims process to ensure adequate reserving and adjustment;

(iv) ensure that the reinsurance protection offered by Mutual Indemnity was sufficient to meet the expected loss experience on any individual programme; and

(v) disclose any relevant information in respect of the estimating of premiums and loss experience and projected premium and loss experience which could or would affect the liability of the client under the programme.

19. The pleading refers to the common membership of certain members of the board of Legion and the board of MRM and the reports given by subsidiaries to the board of MRM, and continues to aver that the management of each company within the Mutual Group was directly controlled by MRM, so that MRM effectively ran the businesses of its subsidiaries, and ignored the distinct legal personality of each subsidiary company.

20. In relation to the American Patriot Programme, reliance is placed upon the general representations said to have been made by Mr. Agnew and one Randall Siko of Commonwealth, which were contained in a written proposal dated 24 March 1997. The plaintiffs seek to rely upon the principle of *contra proferentem* in relation to the interpretation of the relevant documents.

21. The pleading then refers to the reinsurance treaty entered into between Legion and three companies within the Mutual Group dated 1 January 1991. There is

then a plea that clause 3A of the treaty did not bind Mutual Indemnity (which had not been incorporated at the date of the original treaty), and in this regard, the plaintiffs rely upon the terms of the commutation agreement referred to in paragraph 13 above (hereafter "the Commutation Agreement").

22. It is then pleaded that Commonwealth acted as agent on behalf of MRM and/or Legion and/or Mutual Indemnity in relation to the marketing and sale of the Programme. In relation to the administration and management of claims by Cunningham Lindsey, there is a plea that MRM and/or Mutual Indemnity and/or Commonwealth discovered the under-reserving problem in late 1999, but did not advise American Patriot or Mr. or Mrs. Hendricks about this problem for several months. It is then said that the problem but not its effect was brought to the knowledge of American Patriot and the Hendricks by Mr. Bossard in December 1999 or January 2000. In this same vein, it is said that MRM, Legion, Commonwealth and Mutual Indemnity were all seriously concerned about under-reserving and the possibility that premiums from the Programme would not cover expected losses, but did not communicate those concerns to American Patriot or the Hendricks. As well as the under-reserving problem, there was said to be a problem in the estimation of the projected loss ratio in relation to each Programme year.

23. The pleading then deals with the February 2000 meeting which took place at the offices of American Patriot in Illinois between Mrs. Hendricks, Ms. Saran, Mr. Bossard and Mr. Agnew, the purpose of which was to discuss the status of the Programme and consider renewal for the upcoming year. I will refer to that meeting, as the defendants did, as "the Renewal Meeting". It is pleaded that Mrs. Hendricks was not prepare to renew the Programme on the pricing terms offered by Messrs. Agnew and Bossard. At the same time, the pleading refers to Mrs. Hendricks having expressed a concern over the liability (which by then had been transferred from American Patriot to Mr. and Mrs. Hendricks personally) to indemnify Mutual Indemnity, particularly in light of the under-reserving of claims. It is pleaded that Messrs. Agnew and Bossard gave reassurances, but more particularly that they did so on behalf of MRM and/or Mutual Indemnity as well as on behalf of Commonwealth. Lastly, it is

pleaded that at this meeting, Mrs. Hendricks asked whether American Patriot's liability (in real terms hers and her husband's) extended to amounts in excess of the AAP, up to Legion's and/or Villanova's policy limits. It is pleaded that Messrs. Agnew and Bossard were unable to answer that question at the time of the meeting but undertook to check and revert.

24. That issue was then said to have been raised by Messrs. Agnew and Bossard in a meeting with Mr. Partridge and Mr. Turner which Mr. Walsh joined by telephone. I will refer to this meeting, as both parties did, as "the Coverage Meeting". It is then pleaded that Mr. Walsh advised that in relation to losses in excess of the AAP:

    (i) these were not obligations reinsured by Mutual Indemnity; and therefore

    (ii) not obligations in respect of which the Hendricks had any obligations to indemnify Mutual Indemnity; but

    (iii) remained the liabilities of Legion or Villanova up to policy limits.

25. The pleading then states that Mr. Partridge asked Mr. Walsh if it was possible to amend the reinsurance agreement retroactively as so as to place additional liability with the Hendricks. Mr. Walsh is said to have advised that this was not directly possible, but that the addenda to the reinsurance agreement which related to the Programme could be altered so as to change the Hendricks' obligations.

26. It is then pleaded that Mr. Alexander was joined to the meeting by conference telephone link, and as a result of the discussion between those four participants (the implication is that Messrs. Agnew and Bossard listened but did not participate), the decision was reached that MRM, Mutual Indemnity, Legion and Commonwealth should take advantage of the lack of understanding on the part of the Hendricks as to the true nature of the reinsurance obligations of Mutual Indemnity, and hence the indemnity obligations of the Hendricks, by advising them that they were responsible for losses up to Legion's or Villanova's policy limits pursuant to the Shareholder

Agreement, when each knew that this was not the case. It is pleaded that that decision was followed by a discussion as to what amount the Hendricks were willing to pay to limit or cap their perceived exposure, following which there was discussion with one James Eaton, an employee of MRM Hancock, a London broker within the Mutual Group, and it is pleaded that as a result of that conversation it was agreed that US $1 million was the maximum amount that could be claimed as the cost of procuring reinsurance to cap the perceived, but non-existent, liability of the Hendricks in relation to the Programme.

27. Such reinsurance protection was never in fact acquired, but the gravamen of the pleading is that there never was any intention on the part of the relevant MRM personnel to do so, but rather an intention to charge premium to the Hendricks without providing further reinsurance coverage.

28. It is then pleaded that the object of this fraud was to eliminate risk to Mutual Indemnity, allowing MRM, Legion and Mutual Indemnity to decrease the cost of the Programme and at the same time meet Mrs. Hendricks' demands as to the pricing of the Programme.

29. The pleading continues with details as to how the fraud continued to be perpetrated, both in relation to the payment of premium and the revision to the Shareholder Agreement, all of which Mr. Alexander set out in a letter to Ms. Saran dated 20 April 2000. This letter is said to have been false and misleading to Mr. Alexander's knowledge.

30. In the event, the Hendricks accepted the need for the phantom reinsurance, accepted its cost, and agreed to renew the Programme for the next underwriting year. Letters of credit were provided to collaterise the obligation on the part of the Hendricks to indemnify Mutual Indemnity, such that total security of US $8,248,107.50 was provided.

31. The pleading then deals with the various proceedings in the United States. It seeks declarations against Mutual Indemnity that that company is not entitled to recover damages for alleged breaches of the Shareholder Agreement on the grounds that Mutual Indemnity was not a party to that agreement, and

provided no consideration, and also seeks declarations that any such obligation has been vitiated by the deceit pleaded. By the recent amendment there is also a declaration sought that Mutual Indemnity was not bound by clause 3A of the reinsurance agreement, the clause by which Mutual Indemnity acted as an IPC reinsurer. There are further declarations sought relating to the Shareholder Agreement and the letters of credit.

32. As against MRM, damages are sought as a result of the alleged deceit and/or negligent misrepresentation of Messrs. Partridge, Turner, Alexander and Walsh, all of whom are said to have acted as agents for MRM. Damages are sought both in relation to the $1 million premium for reinsurance which was not secured, and for losses incurred as a result of taking proceedings in the United States to prevent draw-down on the letters of credit. Credit is offered in respect of any recovery in the Pennsylvania proceedings against Cunningham Lindsey, and relief is also sought against Messrs. Partridge, Alexander, Walsh, Mutual Indemnity and Commonwealth, arising in broad terms from the fraud.

33. The defence in the consolidated action contains denials in relation to the roles of the various companies within the Mutual Group and particularly denials of responsibility on the part of the offshore group for the activities of any of the onshore companies or their employees. The defendants also deny that Cunningham Lindsey ever acted as the agent of MRM or Mutual Indemnity.

34. In relation to the business within the Programme, it is admitted that Mutual Indemnity was concerned about the size of the Gap, which it is pleaded arose because American Patriot produced far more business and collected far more premium than had been anticipated at the outset of the Programme, when the amount of collateral had initially been agreed. The increased business created increased risk, which in turn led to the need for increased security. In relation to the under-reserving and other problems in relation to Cunningham Lindsey's activities, Mutual Indemnity pleads that it was unaware of these.

35. The defence acknowledges that Messrs. Agnew and/or Bossard (who it is pleaded were not at any time acting on behalf of MRM or Mutual Indemnity)

came up with the idea of reinsuring or capping the liability of the Hendricks and/or American Patriot, but essentially pleads that this was in respect of a real rather than a perceived liability. In relation to the renewal of the Programme for the fourth year, the defence pleads that the terms were onerous, but avers that the Hendricks were keen that the Programme should be renewed with a view to trading out of the losses on the first three years. In particular, it is pleaded that Mr. Turner spoke by telephone to Mrs. Hendricks, expressing his doubts as to whether the potential underwriting profits were worth the financial risk under the terms proposed for the 2000 Programme year.

36. The defence denies that Messrs. Partridge, Turner, Walsh and/or Alexander made any of the statements attributed to them, and further maintains that they did not authorise onward transmission to American Patriot and the Hendricks of the statements in fact said to have been made by Mr. Bossard at the direction of Messrs. Partridge, Turner, Alexander and Walsh. There is a denial that the Hendricks and/or American Patriot did rely upon any such alleged statements or that it was reasonable for them to do so.

37. In relation to the critical issues as to the extent of Mutual Indemnity's exposure to Legion, it is pleaded that such exposure (and hence the obligation to indemnify on the part of American Patriot and the Hendricks) did exceed the AAP. The reinsurance then contemplated was intended for the purpose of capping the exposure of American Patriot and the Hendricks to the AAP (and not beyond) for the first three years of the Programme. It is pleaded that the renewal for the fourth year gave the Hendricks an opportunity to generate profits which would cover losses on the first three years.

38. As to the statement alleged to have been made by Mr. Bossard to Mrs. Hendricks at the Renewal Meeting, it is pleaded that the statements made by Mr. Bossard were true, even if he believed them to be false, and there was thus no misrepresentation.

39. As to the failure to obtain the reinsurance proposed from third party reinsurers, Mutual Indemnity pleads that it was unable to obtain such

reinsurance and therefore acted as self-insurer by retaining the liability for its own account, and thereby removed those liabilities from American Patriot and/or the Hendricks, in return for the premiums set out in the letter of 20 April 2000.

40. There are then what I might refer to as predictable responses in relation to the letters of credit, and Mutual Indemnity closes by repeating its claims in action number 26 of 2003, in which it claimed the sum of US $8,804,102 as well as an accounting and specific performance of the Shareholder Agreement.

41. All of the above pleadings relate to what was originally the plaintiffs' action, in proceedings number 196 of 2004. Earlier, Mutual Holdings had issued its proceedings in 2003, in which it had sought recovery under the Shareholder Agreement. The 2003 proceedings referred to the American Patriot Programme, recited the relevant clauses of the Shareholder Agreement and its amendments, the provisions of the various letters of credit, the Commutation Agreement, and originally made a claim for $8,804,102, which was the amount then said to be payable pursuant to the Commutation Agreement, representing losses on the American Patriot Programme.

The Witness Statements – an Overview

42. I will deal with these relatively briefly at this stage, and indeed have referred to some of these in part in setting out the general background to the case. The key area of dispute concerns the true nature of the obligations owed by American Patriot and Mrs. Hendricks to Mutual Holdings and Mutual Indemnity. Following on from this is the nature of the representations made by Messrs. Agnew and Bossard to American Patriot and Mrs. Hendricks, and indeed on whose behalf those representations were made.

43. I have already referred to the fact that Mr. Agnew and Mr. Bossard were at the material time employed by Commonwealth and Legion respectively. Mr. Agnew referred in the most general terms to MRM marketing and advertising its ability to provide rent-a-captive insurance programmes in the United States through its network of subsidiaries. But that is as far as Mr. Agnew went in his witness statement; Mr. Bossard went further, insofar as he maintained that

Villanova and Mutual Indemnity were at the relevant times acting as one in the marketing and implementation of the Programme. He carried on to say that with respect to at least some of the dealings set forth relating to the Programme, decisions were made and/or controlled by executives by MRM, and he lumped the various companies together, referring to them as "the Mutual Entities". The individual defendants all stressed the importance of none of the offshore companies carrying on business within the United States. That would obviously have been the case if either Mr. Agnew or Mr. Bossard were acting on behalf of the offshore entities when meeting with American Patriot and Mrs. Hendricks.

44. I next turn to the different layers of coverage within the Programme which I have set out in paragraphs 9 to 15, largely taken from Mr. Alexander's witness statement. Mr. Agnew set out his understanding of the structure, taking as his starting point a letter dated 18 February 1997 written by William McPherson of Commonwealth to Ms. Saran. That letter, which is of course not part of the contractual documentation, seems to suggest that the indemnification obligations of the IPC client extend only as far as the AAP. Certainly, Mr. Agnew made no reference in his witness statement to the position in relation to reinsurance coverage, either at the third layer (third party reinsurance) or the fourth or additional layer where in relation to the Programme, Mutual Indemnity was on risk. Mr. Agnew referred in his statement to the fact that he and Mr. Bossard both understood that American Patriot and Mrs. Hendricks had no exposure over the AAP. Hence there is a fundamental conflict with Mr. Agnew's understanding of the risk to Mutual Indemnity and the consequential obligation on the part of American Patriot and Mrs. Hendricks, and that of Mr. Alexander. Mr. Bossard referred in his witness statement to Legion's reinsurers only in the most general terms, and agreed with Mr. Agnew that Mutual Indemnity's obligation to Legion/Villanova in respect to the Programme was never greater than the AAP.

45. I will in due course come to and make findings in regard to the true nature of Mutual Indemnity's risk and American Patriot's and Mrs. Hendricks' indemnification obligations. However, I would just note at this stage that the

understanding which Mr. Agnew and Bossard had could colour their view of the discussions at the Coverage Meeting with Messrs. Partridge and Turner, to which Messrs. Walsh and Alexander were said to have been joined by telephone for differing periods of the meeting.

46. In relation to Mr. Alexander, his understanding was that there was nothing specific in the Shareholder Agreement, but that the risk should fall with the IPC client unless ceded to a third party reinsurer. In the case of the Programme, that would mean that if Mutual Indemnity had any exposure to risk above the AAP, that exposure would be passed on to American Patriot and Mrs. Hendricks. Mr. Walsh similarly understood that Mutual Indemnity came back on risk for this fourth layer, and that any losses falling within this top layer would by reason of the indemnification provisions in the Shareholder Agreement be passed on to American Patriot and the Hendricks. Mr. Partridge had a similar understanding, and his knowledge went back to 1993 when the additional layer had been provided for in the treaty. Finally, Mr. Turner's witness statement seems to indicate that he did not have a position prior to the discussion which took place at the meeting, but that he recalled that following that discussion, the conclusion of those at the meeting was that the exposure did indeed exist.

47. So, on the basis of the witness statements, Messrs. Agnew and Bossard were of the view that American Patriot and the Hendricks had no liability beyond the AAP, whereas Messrs. Partridge, Walsh and Alexander all said that they understood Mutual Indemnity to have exposure at the fourth layer level, such that if losses reached into this level, Mutual Indemnity's exposure would in turn give rise to the indemnification obligations of American Patriot and the Hendricks.

48. I will not at this stage go into detail as to the nature of the conversations which took place at the Coverage Meeting. Suffice to say that both Messrs. Agnew and Bossard believed that the remaining members of the meeting had the same understanding as did they. This meant that they understood that the discussion which followed about the possibility of securing reinsurance

coverage necessarily meant fictitious reinsurance, for which a premium would be dishonestly charged. The defendant members of the meeting believed there to be a real risk, and hence a real need for reinsurance coverage if the liability of American Patriot and the Hendricks for the first three years of the Programme were to be capped.

49. The above is very much a précis of the witness statements, and I will now turn to consider the evidence as a whole, including the witness statements which of course represented the evidence in chief of the various witnesses at trial.

The Evidence – Ms. Saran

50. The evidence of two witnesses was taken before trial, and both a transcript and a DVD of that evidence made available. First was Ms. Saran, whose evidence was taken on 12 April 2010. Ms. Saran was the only witness who had not given a witness statement. Ms. Saran described the operation of the Programme. In relation to the Renewal Meeting, Ms. Saran confirmed that this meeting had been attended by Mr. Bossard and Mr. Agnew on the one hand, and herself, Mrs. Hendricks and Scott Thomas (another employee of Mrs. Hendricks) on the other. (There had in fact been an earlier, preliminary meeting in Illinois attended for the most part by the same players). Ms. Saran referred to the concerns which Mrs. Hendricks expressed at that meeting both to renew the Programme based on the high loss ratio, and in regard to the exposure which she believed she had above the AAP. This, said Ms. Saran, was despite the fact that Mr. Agnew and Mr. Bossard, as well as she herself, had told her that she did not have such exposure. Mr. Thomas, on the other hand, believed that she did. She said that the meeting finished with Mr. Agnew and Mr. Bossard saying that they would go back to Philadelphia and discuss finding a way to relieve Mrs. Hendricks of her additional exposure. Ms. Saran said that either Mr. Bossard or Mr. Agnew had come back to her in relation to the renewal proposal with reference to the purchase of "a $1 million dollar buy-out" for Mrs. Hendricks' perceived additional exposure. Ms. Saran reiterated that she saw no need for such a buy-out because she did not believe that American Patriot or Mrs. Hendricks had such exposure, and

said that she had communicated that view to Mrs. Hendricks. Ms. Saran said that there was further discussion, but that she could not answer questions in relation to them because to do so would involve privileged communications.

51. Ms. Saran then referred to a conversation she had had with Mr. Bossard, after the expiration of the fourth year when the Programme had not been renewed. Mr. Bossard had told her that he needed her to travel to Philadelphia and that he and Mr. Agnew had something to tell her. She said that she met with the two of them, and that due to Mrs. Hendricks and Mr. Thomas (and their counsel) being adamant that they had additional exposure above the AAP, "American Patriot had in essence walked into being defrauded". She referred to the fact that counsel had then been brought in, and that both Mr. Bossard and Mr. Agnew had said that they were willing to come forward on American Patriot's behalf if they were compensated. She said that they were seeking compensation because their future in the insurance community would be put in jeopardy by testifying on behalf of American Patriot.

52. Ms. Saran also referred to the fact that she was by then in litigation with Mrs. Hendricks.

53. In cross-examination, Ms. Saran confirmed her earlier testimony that Mr. Bossard and Mr. Agnew required compensation before giving testimony for American Patriot, and said that there had been an agreement in writing concerning that compensation, although she had not known specifically what it said.

Mr. Eaton

54. Mr. Eaton was asked about the mainframe reinsurance treaty, for which he said MRM Hancock had acted as reinsurance intermediary. He was not able to describe the treaties in any detail, but knew that the reinsured was Legion. Mr. Eaton had given a witness statement, in which he had said that MRM Hancock had been asked by Commonwealth to secure retrospective aggregate stop loss cover for losses above the AAP, and in relation to pricing said that he could not remember any conversations. In his deposition evidence, he confirmed that when he had referred to "losses" in his witness statement, he

was referring to losses which Legion would sustain on the American Patriot book of business.

Mr. Bossard

55. The first witness at trial for the plaintiffs was Mr. Bossard. Mr. Bossard had been involved with the Programme from the outset, having attended a meeting at American Patriot's offices in Illinois with William McPherson in March 1997. He described how his role had shifted from being an underwriter at Legion to being an account executive at Commonwealth after the third Programme year had been completed.

56. In his witness statement, Mr. Bossard set out his understanding as to how the Programme worked. It was Mr. Bossard's view that Mutual Indemnity's obligations to Legion or Villanova (which became the original insurer in the third Programme year) was never greater than the AAP, and he said that this feature of the Programme never changed. He referred to the fact that Legion/Villanova procured separate reinsurance to protect against losses exceeding the AAP, but reiterated that Mutual Indemnity's liability was limited to the amount of the AAP, and thus the Hendricks' liability in any Programme year was similarly limited, since their liability tied in directly to that of Mutual Indemnity.

57. Mr. Bossard then moved to the events of late 1999, when he became aware from Ms. Saran that American Patriot had conducted its own audit of claims files being adjusted by Cunningham Lindsey which had raised issues in relation to reserving. Mr. Bossard did refer to having learned that an audit report had been prepared a year before which had identified reserving problems, and the implication from Mr. Bossard's witness statement was that this earlier audit had either been conducted within Legion, or had come to its attention. Mr. Bossard said that he had consulted with Mr. Agnew, who was then the Commonwealth producer with responsibility for the American Patriot account, and they had discussed the best way of dealing with this problem. This had led to arranging a meeting with Ms. Saran and Mrs. Hendricks. Mr. Bossard had indicated Mr. Scott Thomas, whom he described as an insurance

consultant to American Patriot, had attended the client meeting, and that Mr. Turner had been on the trip but had attended the client dinner and not the meeting.

58. Following that meeting, Mr. Bossard described how he had had discussions with the Legion underwriter in relation to an adjustment to the retention levels, which led to Mr. Bossard taking the problem to Mr. Partridge, who told him to seek quotes through Mr. Eaton. Subsequently, Mr. Bossard made arrangements for he and Mr. Agnew to return to American Patriot's offices with a view to reviewing the renewal terms for the Programme. This meeting, the Renewal Meeting, was attended by Mrs. Hendricks, Ms. Saran and Mr. Scott, and Mr. Bossard described how Mrs. Hendricks' "jaw hit the table" when Mr. Agnew explained the requirement for additional collateral, because that was a very substantial number. It was at this point in the meeting that there was discussion, according to Mr. Bossard, between Mr. Thomas and Mrs. Hendricks as the existence of liability beyond the AAP. Mr. Bossard described it as Mr. Thomas's advice that there was such exposure, and he then said that both Mr. Thomas and Mrs. Hendricks incorrectly believed that the obligation of the Hendricks to reimburse or indemnify Mutual Indemnity extended to liability above the AAP.

59. Mr. Bossard then described how he knew that there was no such exposure, and he said that he did not raise the issue because he did not know how Mr. Agnew would respond, and deferred to him as the account producer. However, even at this stage, Mr. Bossard viewed the mistaken belief on the part of Mr. Thomas and Mrs. Hendricks as an opportunity to increase the likelihood that renewal could be secured, because he believed that the perceived but non-existent exposure was not in fact a problem, so that a "solution" could be provided to Mrs. Hendricks.

60. Mr. Bossard's statement then moved to the Coverage Meeting, at which he and Mr. Agnew reported to Mr. Partridge and Mr. Turner. His witness statement evidence was that they went first to Mr. Partridge's office, and Mr. Bossard explained what he perceived as a misunderstanding about the

Hendricks' exposure on the Programme. His evidence was that Mr. Partridge then asked "Are you sure they think they are on above the aggregate excess? Can you sell them retro reinsurance?" Mr. Bossard referred to the fact that Mr. Agnew answered, indicating that he thought that this was possible and said that at this point Mr. Partridge called Mr. Turner into his office, and it seems the initial conversation was repeated. Mr. Partridge then called Mr. Walsh on the telephone, repeating what had originally been told to him by Mr. Bossard. Mr. Bossard said that Mr. Partridge then asked Mr. Walsh "On the reinsurance agreement, does the client assume the risk above the aggregate stop loss?". He said that when Mr. Walsh replied "No". Mr. Partridge asked "Can't we change it?" to which Mr. Walsh replied "No", but added, after a pause "But we can change the amendment to the reinsurance agreement to say that they are responsible above the aggregate attachment point". Mr. Bossard apparently inferred that this last statement was a reference to the Shareholder Agreement.

61. Mr. Bossard's witness statement continued that at the end of the conversation with Mr. Walsh, Mr. Partridge had asked him and Mr. Agnew how much they thought "we can get them to pay for it?", presumably a reference to the earlier possibility of securing retrospective reinsurance. Mr. Bossard commented in his witness statement that the price had to make sense, because Mr. Thomas would need to be convinced that it was tied to something like the rate on line for the business, and said that at this point he went downstairs and worked out that $1 million would represent an appropriate premium for this reinsurance because it would relate to the $12 million aggregate policy. He said that having done his calculations, he went back to Mr. Partridge's office and explained his rationale for coming up with this number. He said that Mr. Partridge agreed it sounded logical and that Mr. Thomas would be persuaded, and Mr. Bossard said that at this point Mr. Partridge called Mr. Alexander in Bermuda. In this conversation, according to Mr. Bossard, Mr. Partridge had explained to Mr. Alexander the misunderstanding which Mrs. Hendricks had as to her exposure above the AAP and explained that he had come up with a proposal to offer retro cover "for $1 million", which Mr. Bossard said would

in fact be used to try and buy additional reinsurance for the benefit of Legion, not for the benefit of American Patriot or the Hendricks, whose indemnification obligation of course depended upon liability on the part of Mutual Indemnity. Mr. Bossard described how Mr. Alexander had agreed with this approach, and referred to Mr. Partridge's advice that Mr. Bossard would prepare and send to Mr. Alexander a letter intending to give American Patriot and the Hendricks the appearance that Mutual Indemnity would purchase the cover by way of reinsurance. Mr. Bossard said that he did prepare such a draft letter, but that in doing so was annoyed because he knew it was wrong.

62. Mr. Bossard further indicated that he was then instructed by Mr. Partridge to go back to Ms. Saran and falsely confirm that the Hendricks did have exposure above the AAP, and Mr. Bossard says that he did this. He described how he had placed a number of calls (he thought three), the first of which involved telling Ms. Saran that the Hendricks did have exposure, the second telling Ms. Saran that it looked as if they had found a market (for retrospective reinsurance), and giving her a rough price range, and with the third call confirming that coverage had been obtained. In truth, of course, coverage never was obtained.

63. Mr. Bossard then turned to how he had come to tell Ms. Saran of these events in early 2002, after Ms. Saran had called him to ask questions about the aggregate excess. He said that was when he was put in touch with the Hendricks' attorneys, and that those were the circumstances under which he swore an affidavit in April 2002, prepared for the purpose of applications in US proceedings which were then under way. Mr. Bossard also referred to the evidence which he gave in arbitration proceedings between Legion and John Hancock Life Insurance Company. Mr. Bossard suggested that he was "ambushed" by the Legion attorney involved in those proceedings, who asked him questions designed to demonstrate that he did not understand the way that the Programme worked. However, Mr. Bossard concluded that the full transcript shows that he did not misunderstand the working of the treaty.

64. I now turn to Mr. Bossard's cross-examination, and I first refer to the questions put to Mr. Bossard concerning the reasons which had been put in evidence by Mr. Garrood of Mello Jones & Martin, in support of the application which had been made on the last working day before the trial was due to commence, with a view to securing an adjournment. The reason given, according to Mr. Garrood, was that Mr. Bossard had taken objection to the level of disclosure either sought or given in relation to an investment made on behalf of Mrs. Hendricks in a business then operated by Mr. Bossard. Mr. Garrood's affidavit indicated that Mr. Bossard had made it known to those advising the plaintiffs in the United States that he regarded such disclosure as an unnecessary interference with his right to privacy in respect of his business affairs, and had indicated that he would not then travel to Bermuda to give evidence. I had allowed the adjournment on the basis that letters of request for Mr. Bossard's evidence would issue, and as I understand it the Pennsylvania court granted the application made by the plaintiffs. Mr. Bossard did of course come to Bermuda, but the trial started two days late. Mr. Bossard's evidence was that he did not know of the application to adjourn the trial, and that the reason for his unwillingness to travel so as to be in Bermuda for the start of the scheduled trial related to his family commitments.

65. Mr. Bossard was then referred to the investment made in the business he operated by Mrs. Hendricks, and was referred to Ms. Saran's evidence that he had required compensation in return for his testimony. Mr. Bossard denied that that was the case. However, he did agree that the affidavit which he had sworn for the purpose of the US proceedings was dated 9 April 2002, and that the cheque for the investment by Mrs. Hendricks of $400,000 in his business was dated 8 April 2002. Mr. Bossard said that there was no connection between these two dates, and that it was not true that he would have not sworn the affidavit without receipt of the investment. Various documents were put to Mr. Bossard both in relation to the investment in his business, and in relation to a defence and funding agreement and covenant not to sue. In relation to the former, Mr. Bossard seemed reluctant to, but did eventually,

accept that the documents were what they appeared to be and had been signed by him.

66. Next, Mr. Bossard was cross-examined in relation to the length of the Coverage Meeting which had taken place at Mr. Partridge's office in Philadelphia. He gave slightly different times, both of which were different from the time which he had previously given in his deposition in November 2003 in the Legion/John Hancock arbitration.

67. Next Mr. Bossard was asked as to the position in relation to the Programme once losses pierced the AAP. Mr. Bossard stood by his earlier deposition testimony that once losses pierced the AAP, they fell back on to Legion. He agreed that Legion had reinsurance with third party (non Mutual Group) reinsurers, pursuant to what Mr. Bossard referred to as the mainframe treaty, but said that once the limits of the mainframe treaty were exceeded, the losses would fall back to Legion. Mr. Bossard also confirmed his earlier testimony that it was Mrs. Hendricks' understanding that once the limit was exhausted the liability would fall back to her.

68. Mr. Bossard was questioned in relation to the figure of $1 million suggested at the meeting with Mr. Partridge as an appropriate premium for reinsurance. It was put to him that his witness statement suggested that he himself had come up with this figure, but he said that Mr. Partridge had come up with the figure, and had instructed him to go back and to confirm if that number would work.

69. There was a minor issue as to whether Mr. Bossard and Mr. Agnew had attended on Mr. Turner or Mr. Partridge first. Mr. Bossard said that his witness statement (where he said they saw Mr. Partridge first) was correct, and that if Mr. Agnew said differently, that was a matter for him. In relation to the discussion at the meeting, Mr. Bossard agreed that the comments which had been attributed to Messrs. Partridge and Walsh in his witness statement had not been given in the earlier affidavit.

70. A more critical issue was then raised in relation to what Mr. Walsh had said at the meeting. I have referred in paragraph 60 to the fact that Mr. Bossard's witness statement said that after Mr. Walsh had responded in the negative to

Mr. Partridge's question as to whether the risk position could be changed, Mr. Walsh had added the words "But we can change the amendment to the reinsurance agreement to say that they are responsible above the aggregate attachment point". Mr. Bossard was referred to his 2002 affidavit, which did not include the additional words; that affidavit simply said "Mr. Walsh indicated that such a change was not possible". In his November 2003 deposition in the Legion/John Hancock arbitration, the position was put more clearly, in the following terms:

> "Answer: The next question that was asked by Glenn was – and I don't know if Glenn was saying it jokingly or not. I don't recall – 'Can we change the agreement?' And Andy said 'No'. And that was it as far as Andy's involvement.
>
> "Question: At that point Andy gets off the phone?
>
> "Answer: Yes."

Mr. Bossard said that that statement was accurate according to his recollection at that point in time, and accepted the fact there was an inconsistency between that earlier position and his witness statement. Finally, Mr. Bossard was taken to his evidence in the arbitration, given in May 2004. I also set out that evidence, which is in the following terms:

> "Q. Now, after Mr. Walsh related his answer to Mr. Partridge's initial question, did Mr. Partridge ask another question?
>
> A. Yes, he did.
>
> Q. And what was that question?
>
> A. Can we change the agreement.
>
> Q. And did he want to change the agreement retroactively?
>
> A. I don't know the answer to that.
>
> Q. Who did he pose that question to?
>
> A. He posed the question to Mr. Walsh.

Q. And what was the answer?

A. No, we can't.

Q. What happened next?

A. We kind of chuckled.

Q. After it was decided that the agreement couldn't be changed, was there a further conversation regarding who had the exposure once the aggregate treaty was exhausted?

A. With Mr. Walsh?

Q. Yes.

A. No, there was not.

Q. At that point did Mr. Walsh hang up the phone?

A. Yes."

Mr. Bossard accepted that his earlier evidence, when given, had been correct, but was unable to explain the inconsistency.

71. Mr. Bossard was then questioned in regard to what had been said at the Renewal Meeting with regard to Mrs. Hendricks' exposure above the AAP. In his witness statement Mr. Bossard had said that he had not said anything at the time. He was referred to what Ms. Saran had said in her deposition, namely that he had made a positive statement that Mrs. Hendricks had no exposure above the AAP. Mr. Bossard's response was that that had been directed to Ms. Saran during the meeting, and that he had said nothing to Mrs. Hendricks in this regard. Mr. Bossard was again taken back to his evidence in the Legion/John Hancock arbitration, where it had been put to him that when Mrs. Hendricks had said that there might be exposure above the AAP, he had said that that was possible. Mr. Bossard confirmed that that evidence had been correct when he said it. He accepted that the two statements were inconsistent.

72. In relation to this same issue of Mrs. Hendricks' exposure, Mr. Bossard said that he had discussed the matter with Mr. Agnew on the trip back to

Philadelphia, and that the two had "agreed to disagree". Mr. Bossard said that Mr. Agnew's position was that he was not sure, and that was why they had gone back to Mr. Turner and Mr. Partridge to discuss the matter.

73. Next, there were questions in relation to the conversation with Mr. Alexander, made on speaker phone at the Coverage Meeting. Mr. Bossard's earlier deposition evidence on this subject had been that he could not recall how Mr. Alexander had become involved.

74. Next, Mr. Bossard was referred to the statement made in his witness statement, to the effect that he had been instructed by Mr. Partridge to go back to Ms. Saran "to falsely confirm that the Hendricks did have exposure above the aggregate attachment point". Again, Mr. Bossard was referred to his evidence in the arbitration, where he had said that the instructions given to him were "float the idea by American Patriot from the standpoint that we might be able to secure excess reinsurance for about $1 million to see how they would respond to the number." Mr. Bossard confirmed that that evidence had been correct.

75. Mr. Bossard was then referred to his evidence in those proceedings in which he referred to Mr. Agnew and himself having called Ms. Saran to advise that there was the potential to secure reinsurance above the aggregate limit for approximately $1 million. He was then referred to his witness statement, where, as I have set out in paragraph 62 above, Mr. Bossard referred to having thought there had been three conversations. Mr. Bossard said that there had been a number of conversations.

Mr. Agnew

76. Mr. Agnew started by dealing with the nature of the Programme, from inception, and he described how the volume of business in the second year had increased the Gap. Mr. Agnew said that because of a concern that American Patriot may have been under-capitalised to meet its liability, following discussion with Mr. Alexander, he had asked that Mr. and Mrs. Hendricks be substituted for American Patriot. He was aware that they had a substantial net worth, and said the change was made without difficulty. He

then referred to being told of the under-reserving problem by Mr. Bossard. Following discussion with Legion's claims people, he and Mr. Bossard spoke to Mr. Turner. He described the problem as being that the loss reserves had to be significantly increased, which had the effect of doubling the Gap, and similarly doubling the required collateralisation. Mr. Agnew described how he, Mr. Bossard and Mr. Turner had met with Mrs. Hendricks and Ms. Saran in Illinois, and Mr. Agnew described the meeting having ended on a good business-like footing.

77. He then described how he and Mr. Bossard had put together the renewal and arranged a second meeting at American Patriot's offices, which meeting now included Mr. Thomas, this being the Renewal Meeting. Mr. Agnew said that it was Mr. Thomas who had raised the concern that Mrs. Hendricks had an exposure over and above the AAP. Mr. Agnew indicated that he knew Mr. Thomas to be wrong in this regard, but said that he kept this to himself because it would be a distinct advantage to be used in securing the renewal. He said that both he and Mr. Bossard understood that Mrs. Hendricks never had any exposure over the AAP, and he said that they realised that Mr. Thomas did not understand the Programme, and that Mrs. Hendricks was not aware that she did not in fact have any liability over and above the AAP. He described how in later discussions with Mr. Bossard they had no doubt that Mr. Thomas was completely wrong, and he said that their understanding was the same as that of everyone in the Legion organisation with knowledge of a rent-a-captive facility. Mr. Agnew indicated that at the same meeting Mrs. Hendricks had advised that she would not continue with the Programme for the fourth year without assurances that there was an ultimate cap on liability on the first three years of the Programme, and that she also required other changes to be made to the Programme structure.

78. Turning to the Coverage Meeting, Mr. Agnew described having met with Mr. Turner to advise what had taken place at the Illinois meeting and said they subsequently went to Mr. Partridge's office to bring him up-to-date. He described how Mr. Turner had informed Mr. Partridge of the update that he had been given, and said that both Mr. Turner and Mr. Partridge looked at

Mrs. Hendricks' mistaken understanding of her exposure as an opportunity, and Mr. Partridge had asked "Can we get something for it?". Mr. Agnew then described how he had not been looking to secure anything beyond the renewal, and said that he and Mr. Bossard had asked "Like what?", and Mr. Partridge had responded with detail as to the cost to Legion's own reinsurance protection, and said that he wanted to charge them something for that, carrying on to ask "What do you think they would pay?". Mr. Agnew said that at this point Mr. Bossard had suggested "About a million dollars", that Mr. Partridge had asked if they thought they could sell that, and they had responded that they could try. He said that Mr. Bossard had then come up with the notion of making the further premium more palatable by having a trigger point which could give the appearance of not necessarily reaching the top level of premium. Mr. Agnew said that at this point Mr. Partridge had asked how they were going to put the client on an exposure which the client did not otherwise have, and said that Mr. Partridge had then dialed Mr. Walsh and put him on speaker phone. Having giving the background as to the misunderstanding on the part of Mrs. Hendricks in relation to her exposure on the treaty, he said that Mr. Partridge asked Mr. Walsh "Could we put the exposure back on them? Can we change the treaty?" He said that Mr. Walsh had responded "No, we cannot change the treaty" and had then added "We would have to change the amendment for that specific client". Mr. Agnew had indicated that he had not seen the treaty between Legion and Mutual, but that everybody understood that in talking of changing the exposure of the client, that would be done under the Shareholder Agreement.

79. In this regard Mr. Agnew said that it was necessary to get Mr. Alexander involved, and that Mr. Partridge had sent Mr. Bossard to get the underwriting file and that Mr. Walsh had then come up to Mr. Partridge's office. Mr. Partridge had then dialed Mr. Alexander in Bermuda, again on speaker phone, and Mr. Agnew had confirmed that at that point Messrs. Partridge, Walsh, Turner, Bossard and himself were all present. He described how Mr. Partridge had summarised the position, explaining that the Hendricks misunderstood their exposure and the need to change the Shareholder

Agreement. Mr. Partridge was said to have stated that Mr. Walsh would prepare the documents from the Legion side to "retroactively adjust the Shareholder's Agreement". Mr. Partridge is said to have stated that this was an opportunity and that Mr. Alexander has said "OK", and that Mr. Walsh would prepare the amendments and send them to Mr. Alexander for approval and execution. He carried on that Mr. Partridge had said that "We think we can sell one million dollars for the reinsurance", meaning that to be the amount of money to be paid for fictitious reinsurance to cover an exposure which the Hendricks did not have but believed they had. He said that Mr. Alexander had agreed. He then described how there had been a discussion about trying to buy reinsurance, not for the Hendricks, but for Legion, and that at this point a call had been put through to Mr. Eaton. There was further discussion in regard to adjustments to the Programme.

80. Mr. Agnew then said that he had backed away from the renewal at this point because he did not wish to be directly involved. He had received copies of subsequent correspondence, and confirmed that the marketing proposals that he had provided to American Patriot reflected that American Patriot and later the Hendricks would be collateralising only Mutual Indemnity's exposure. He closed his witness statement by saying that at no time during his conversation with Messrs. Partridge, Turner, Walsh or Alexander had anyone suggested that any provision of the reinsurance treaty operated to expand the obligations on the part of American Patriot and/or the Hendricks in any Programme year beyond the level of the AAP.

81. In cross-examination Mr. Agnew was also asked questions in relation to indemnity from the Hendricks, and confirmed the terms of the defence and funding agreement and the covenant not to sue. He described how his affidavit had been sworn about the time that those two agreements had been executed, and then dealt with discussions he had had with one Patrick Reardon of the Mutual Group, in which he had asked Mr. Reardon for an indemnification from the Mutual Group. He described himself as under pressure from both sides, and said that he had looked at the credibility of both parties and selected American Patriot, and carried on to say that this decision

on his part was also based on his prior experience with the Mutual Group's management and that "Legion and Mutual hung me out to dry in the middle".

82. Mr. Agnew was then asked questions in relation to minor matters where his witness statement differed from Mr. Bossard's evidence. Mr. Agnew confirmed that they had been to see Mr. Turner before going to Mr. Partridge, and that in relation to the trip to Illinois which Mr. Turner had gone on, he had been at the business meeting as well as the client dinner. In relation to the arrangements for travel to Bermuda for the start of the trial, Mr. Agnew broadly confirmed Mr. Bossard's evidence.

83. The questioning then turned to what had been said by Mr. Walsh at the Coverage Meeting, and Mr. Agnew said that Mr. Walsh had not been asked to advise whether there was any liability above the aggregate attachment limit for Mutual. In regard to the terms of Mr. Walsh's witness statement (in which he said he had advised as to liability on the part of the client above the aggregate attachment limit), Mr. Agnew said that was absolutely false and that Mr. Walsh had never said it. In regard to the exchange between Mr. Partridge and Mr. Walsh, Mr. Agnew confirmed his witness statement.

84. The questioning then turned to Mr. Agnew's understanding of the client's liability, and particularly he was asked to comment on Mr. Bossard's evidence that he, Mr. Agnew, had been open minded on the question of whether there was liability above the AAP. Mr. Agnew responded that he was non - committal to the client, but that he did not think that there was any such liability, and that was the basis upon which he had been taught to sell the product. He denied having indicated to Mr. Bossard that there might be such exposure. Mr. Agnew was referred to Mr. Bossard's evidence in the Legion/John Hancock arbitration, but his position did not change. Mr. Agnew was adamant that above the AAP, if losses exceeded the third party reinsurance, the exposure went back to Legion.

85. In relation to the effect of substantial losses in this layer of third party reinsurance, Mr. Agnew indicated that it was a big concern to Legion, because it cost the company, insofar as it drove up the loss ratio, and that affected the

treaty on renewal, so that while it was not a cost for the policy year, it was such for the future.

86. Mr. Agnew was asked about who had raised the $1 million figure as a suggested premium, and confirmed his witness statement to the effect that it was Mr. Bossard, and not Mr. Partridge. Mr. Agnew also confirmed what had been said in his witness statement about Mr. Walsh being present when Mr. Alexander had been telephoned. He was then referred to Mr. Bossard's earlier evidence as to the point at which Mr. Walsh had finished giving his advice, and said that Mr. Bossard's earlier evidence had been wrong.

87. Mr. Agnew closed by reference to the third and fourth layers, as described by Mr. Alexander. He said that Mr. Partridge was seeking to recover something from the Hendricks to compensate for the hit which Legion had taken at the third layer, as described in paragraph 12 above. Mr. Agnew said that Mr. Partridge was using losses in that layer as the basis for charging American Patriot and the Hendricks $1 million for another layer, which layer he said did not exist. Mr. Agnew was adamant that to his knowledge and understanding there was no genuine layer excess of the third layer.

Mrs. Hendricks

88. Mrs. Hendricks started her witness statement by referring to the solicitation of American Patriot by what she referred to as representatives of "Mutual Entities"; but the particular representatives were not identified and I find the use of that term (also used by Mr. Bossard) to be unhelpful. But I will continue to use it where Mrs. Hendricks did so in her witness statement.

89. She carried on to set out her understanding of the manner in which the Programme operated, indicating that Legion, as the issuer of the underlying insurance policies, would be indemnified against losses up to an agreed percentage of gross written premium, referred to as the "aggregate attachment point", by its captive reinsurer, Mutual Indemnity. She said that her understanding was that above the AAP, Legion was reinsured by non-captive reinsurers. Her understanding of American Patriot's obligation was to indemnify Mutual Indemnity against any losses which it suffered on the

Programme in excess of premium received, up to the AAP. She said that it was her understanding (based on information provided to her by unidentified persons) that the AAP was the maximum exposure that Mutual Indemnity, American Patriot or she herself faced in connection with the reinsurance of Legion.

90. Mrs. Hendricks described how in early 2000, American Patriot had discovered that Cunningham Lindsey had both mishandled claims and under-reserved. She said it was her understanding that since Legion was responsible for underwriting the Programme, Legion had ultimate claims handling authority. Mrs. Hendricks referred to the litigation taken by American Patriot against Cunningham Lindsey in the United States, various legal proceedings relating to the draw down on the letters of credit, and proceedings taken by the liquidator of Legion against American Patriot. Mrs. Hendricks went on to say that as the renewal of the Programme approached, she became concerned about the effect of the under-reserving, particularily as it would affect premium rates. She said that she had requested a meeting, and this was the Renewal Meeting which took place in February 2000, attended by herself, Ms. Saran, and Messrs. Bossard and Agnew. Mrs. Hendricks did not refer to the earlier meeting, or to Mr. Thomas being present at the later one. She said that she had specifically asked Messrs. Bossard and Agnew at this meeting whether her (and presumably American Patriot's) liability extended beyond the AAP up to Legion's policy limits, and said that she explained the need to have an answer to that question before she and American Patriot committed to renew the Programme. Mrs. Hendricks used the first person plural to refer to the exposure, and I take it that she was referring to the exposure of herself and her husband, and American Patriot. She said that the response from Messrs. Agnew and Bossard was that "it was possible" that they bore such liability, but that they would check and revert.

91. She then stated that shortly thereafter, Ms. Saran informed her that she had heard from Mr. Bossard that they were responsible for "all un-reinsured Programme losses above the aggregate attachment point up to Legion's policy limits". She then referred to what Mr. Bossard was said to have told Ms.

Saran in relation to procuring new reinsurance, which she understood would relieve them of liability and cap potential exposure for the first three Programme years. She referred to the proposal first being documented in a 28 March 2000 email from Ms. Bossard, and then referred to the representations made by Messrs. Agnew and Bossard to Ms. Saran, as confirmed in their witness statements, and continued that in reliance on the representations of Messrs. Bossard, Agnew and Alexander (the latter as the writer of the 20 April 2000 letter), she had agreed to the proposal to pay up to one million dollars to extinguish what she perceived to be a substantial but then unquantifiable potential liability for losses under the Programme for the first three years. She confirmed that that amount had been paid to Mutual Indemnity, and also confirmed that based on the representations, and the lack of Programme documentation expressly allocating this liability to "one of the Mutual Entities", she had also agreed to execute amendment number five to the Shareholder Agreement.

92. Mrs. Hendricks then referred to the understanding which she subsequently acquired (without identifying the source of that understanding) that principals of the Mutual Entities knew when Mr. Bossard presented the proposal to them that Legion was responsible for un-reinsured Programme losses up to policy limits. She also referred to having been made aware long after the event of the instructions given to Messrs. Bossard and Agnew, no doubt on the basis of information given to her by them. She continued that had she known that their potential losses were capped at the AAP for the first three Programme years, well below Legion's policy limits, she would never have agreed to pay for the purported reinsurance. She also says that she would never have renewed the Programme for the fourth year, would not have posted new letters of credit, and would not have executed the amendment to the Shareholder Agreement. Mrs. Hendricks contended that she had suffered loss and damage as a result of the deceit and/or negligent misrepresentations, and sought relief in relation to liability under the Shareholder Agreement, setting aside amendment number 5, and the renewal for year four of the Programme. She also sought the return of the $1 million in reinsurance premium, and finally

referred to substantial legal expenses, in excess of $4 million, said to have been a direct result of the deceit and/or negligent misrepresentation.

93. In her oral evidence, after Mrs. Hendricks had confirmed the accuracy of her witness statement, she was asked to confirm the amount, and more particularly the detail, of the claim for legal expenses. She referred to a binder of material, and confirmed that that was the allocation of the legal expenses referred to in her witness statements, which expenses amount to US $4,232,260.87.

94. In cross-examination Mrs. Hendricks was asked questions in relation to the status of American Patriot, and the position in relation to the delayed start of the trial. In relation to the legal expenses to which Mrs. Hendricks and American Patriot had been subjected in the United States, Mrs. Hendricks had said that she had not reviewed the material in the binder which had just been put in, supporting the claim in the amount $4,232,260.87.

95. Mrs. Hendricks was then questioned about the financial assistance provided particularly to Mr. Bossard, and denied having paid compensation to Mr. Bossard or Mr. Agnew for their evidence. However, her evidence was to the effect that this would have been something handled by her attorneys, with Ms. Saran. Mrs. Hendricks was asked questions with reference to the defence and funding agreement and covenant not to sue, with particular reference to some correspondence with Mello Jones & Martin. In a letter from that firm dated 23 March 2010, they had said on instructions that there were no documents evidencing a defence agreement, to which Mr. Agnew had referred in his witness statement. Mrs. Hendricks said that she had not given such instructions, but said again that they would have been by her US lawyers or the people now running her business. When directed to the documents, Mrs. Hendricks agreed that, contrary to the terms of the letter from Mello Jones & Martin, there was in fact a written defence agreement, and that agreement had been signed by Mrs. Hendricks.

96. Mrs. Hendricks was then referred to a letter from Mello Jones & Martin dated 21 April 2010, referring to “a capital advance in an insurance business said to have been operated by Mr. Bossard and Mr. Agnew”, and stating that there

was no written agreement in respect of this advance. Mrs. Hendricks said that she had not given those instructions, that she did not know who had, and that the statement was not true. In relation to the detail of the investment, Mrs. Hendricks said that she did not remember the precise details of the investment, but that at the time she had been looking for a market to replace the Programme, and had invested "a few million dollars" in other companies trying to find markets. Mrs. Hendricks did not know whether any dividend had been paid on her investment, or whether the money had been paid back, although she did not think that it had been. Mrs. Hendricks denied that this was a payment for the benefit of Mr. Bossard for the giving his evidence, as opposed to a normal commercial transaction.

97. Mrs. Hendricks was then questioned about the Renewal Meeting at American Patriot's offices in February 2000, attended by herself, Ms. Saran, and Messrs. Bossard and Agnew. Mrs. Hendricks confirmed that by that time she had become aware of the under-reserving problem. She referred to her previous understanding that her liability or exposure was capped at the AAP, but then said that something was said during the meeting which caused her to have a concern that she might have exposure, and indeed unlimited exposure, beyond the AAP.

98. I would pause at this point to remind myself that there were two meetings in preparation for the fourth year renewal of the Programme; both were attended by Mrs. Hendricks, Ms. Saran, Messrs. Bossard and Agnew, but the first may also have been attended by Mr. Turner (depending whether Mr. Agnew's or Mr. Bossard's evidence is correct) and the second was attended by Mr. Thomas.

99. In any event, Mrs. Hendricks' evidence was that she was then being told that there could be exposure beyond the AAP, and that Messrs. Bossard and Agnew would have to go back and check. She said it was "a bad day", and confirmed that she had indicated reluctance to renew the Programme in those circumstances, although she could not remember the detail of the conversation.

100. Mrs. Hendricks indicated that Messrs. Agnew and Bossard had next been in contact with Ms. Saran, and that eventually they had come back with a proposal. She said at this point that she was not going to go forward because "the pricing was ridiculous", but that eventually Messrs. Agnew and Bossard had come back to say that they thought they could get reinsurance, this communication coming via Ms. Saran. Mrs. Hendricks made it clear that she had no direct involvement in these discussions, but when the proposal did come back that she could secure reinsurance coverage on the first three years of the Programme for $1 million, she thought that she had no choice but to buy that coverage, since otherwise she believed her exposure to be unlimited. However, she was not able to say whether Mr. Bossard or Mr. Agnew had said this, since their channel of communication had been through Ms. Saran. Even when it came to having her own lawyer look at the issue before going ahead, she did not know whether that had happened, on the basis that it would be Ms. Saran who would do that. However, Mrs. Hendricks was then reminded of the terms of a deposition she had given in February 2006, in litigation between the liquidator of Legion/Villanova and American Patriot, and having been taken to her evidence, she accepted that her attorney Mr. Leo had looked at matters. Mrs. Hendricks agreed that the renewal terms for the fourth year were onerous, but did not recall any conversation with Mr. Turner in relation to that aspect of matters.

101. In response to questions from me, in relation to what Mr. Bossard and Ms. Saran had said about the meeting at which Mrs. Hendricks first became aware of the possibility of exposure above the AAP, Mrs. Hendricks indicated that the version of events given by Mr. Bossard in his deposition for the Legion/John Hancock arbitration and by Ms. Saran in her deposition evidence was wrong in both cases.

102. In relation to the expenses, Mrs. Hendricks indicated that she did not know what one set of proceedings was concerned with, but said that she was sure that if they were in the book they had to do with this litigation. I should note at this point that there then followed discussion with counsel in which Mr. Smith reserved the right to ask further questions of Mrs. Hendricks once he

had had an opportunity to review the relevant binder, but in the event, the issue was not pursued. The completion of Mrs. Hendricks' evidence completed the evidence for the Plaintiffs.

Mr. Partridge

103. Again, I start with Mr. Partridge's witness statement, in which he started by setting out the relevant background, which I will not set out where it represents duplication. He indicated that the American Patriot Programme was a large one, and that Mr. Agnew had a direct financial interest in the renewal of the Programme. Mr. Bossard had no such direct interest, but could receive a bonus which was less directly tied to the revenue generated by a particular programme. Mr. Partridge indicated that American Patriot earned some $8.8 million in commission in total on the Programme.

104. Mr. Partridge then turned to the Coverage Meeting, which he said took place in his office in February or March 2000, with Messrs, Turner, Agnew and Bossard present, Mr. Walsh present either in person or on the telephone, and Mr. Alexander on the telephone. Mr. Partridge described how the question arose as to who was responsible for losses if they did indeed burst through the AAP and third party reinsurance, with a supplemental question as to the renewal of the Programme. Mr. Partridge said that his understanding was that the Hendricks had exposure "to losses $5 million above the aggregate attachment point and the third party reinsurance by reason of Article 3A of treaty 103". Mr. Partridge referred to the fact that he had signed that when it had been put in place in 1993 for the purpose of transferring additional risk to the Mutual offshore companies from Legion, and that he also knew that Mutual Indemnity had become a party to treaty 103 subsequently. That of course was the opposite position to the argument later made to and accepted by the Legion/Villanova liquidator.

105. Mr. Partridge then indicated that he did not recall Mr. Walsh giving the advice set out in the plaintiffs' pleading, to which I have referred in paragraph 24 above, but said that he would be most surprised if Mr. Walsh gave such advice since he had been involved in the drafting of Treaty 103 and article 3A, and

said that he would have remembered if Mr. Walsh had given such advice, since it was contrary to his own understanding of the position. Mr. Partridge said that he had no recollection of Mr. Walsh advising that the addenda to the reinsurance agreement could be altered so as to change the Hendricks' obligation and did not believe that had happened. Mr. Partridge also said that what was set out in paragraph 19.3 of the statement of claim (set out in paragraph 26 above) was an incorrect statement of what had happened during the meeting. He said that no decision had been made to take advantage of the Hendricks' alleged lack of understanding or knowledge about the reinsurance obligations of Mutual Indemnity, although he said that they had recognised that the Hendricks were liable for losses in excess of the AAP.

106. In relation to the discussion as to the amount that the Hendricks might be willing to pay to limit or cap their perceived exposure (again referred to in paragraph 26 above), Mr. Partridge said that they had had a discussion about the cost of relieving the Hendricks of their liability, but he did not remember when that had taken place and did not think that it had been the meeting in question. He did not remember the actual terms of the arrangements to relieve the Hendricks of their liability, other than that it was retroactive cover.

107. In relation to the conversation with Mr. Eaton, Mr. Partridge did not think that this had happened as set out in the pleading, and had no recollection either of talking to Mr. Eaton about the retroactive aggregate reinsurance, or being present when any particular number was determined for premium. Mr. Partridge indicated that he had not instructed Mr. Bossard or Mr. Agnew to lie to the Hendricks, that he had not acted dishonestly or recklessly, and his view was that the Hendricks were liable to indemnify Mutual Indemnity for losses in excess of the AAP. Mr. Partridge dealt with the further pleadings arising from this meeting in much the same way; he believed that the Hendricks and American Patriot had exposure for losses $5 million in excess of the AAP, there was no misrepresentation of the position, he denied that those at the meeting had decided to lie to the Hendricks, to misrepresent the position and take advantage of their misunderstanding, and no instructions had been given

to Messrs. Agnew or Bossard to relay false and untrue information to the Hendricks.

108. Mr. Partridge made further denials in relation to subsequent claims in the statement of claim, and particularly did not accept that Mr. Alexander's letter of 20 April 2000 was false and misleading.

109. In his oral evidence, Mr. Partridge was first taken to the proposal documentation, and gave evidence in relation to his understanding of those documents. He was then taken to an amended registration statement filed with the Securities and Exchange Commission ("SEC") on 12 May 1999. This document was filed on behalf of MRM, and although Mr. Partridge agreed that he was likely to have signed it, he felt it unlikely that he had read it. Mr. Partridge agreed with the general matters which were put to him in relation to the operation of the Programme. Mr. Partridge was then taken to reinsurance treaty 103, a document which he had signed on behalf of Legion. Mr. Partridge said that he certainly knew about it but he felt that the words "very familiar" to describe his knowledge were a little strong. He was then taken to amendment number 1, which introduced the new article 3A. Mr. Partridge confirmed that to the best of his recollection this had been effected for regulatory purposes, in order to create risk transfer. Mr. Partridge confirmed his understanding that at that time it was not expected that the additional layer of reinsurance cover effected by article 3A would be used.

110. Mr. Partridge was then taken back to the proposal documentation, and the wording under the first section containing a description of the reinsurance programme. The last part of that section contained the words "Mutual's retention in the aggregate will be increased by $5,000,000 in aggregate stop loss reinsurance for total aggregate retention of $6,400,000." It was put to Mr. Partridge that this was a reference to the 3A additional limit of liability, but his response was that it looked to him to be the third party reinsurance which would represent the third layer. When it was put to him that this could not be third party reinsurance because of the reference to Mutual's retention, Mr. Partridge's response was that it didn't make sense to him, and he agreed that it

was consistent with clause 3A, although he was still unable to say why the words "Mutual's retention" had been used, and eventually came to the position that he was not sure what the words in question were referring to.

111. Mr. Partridge was then taken to the renewal proposal dated 17 February 1998. In relation to part of that document headed "Program Development", Mr. Partridge was questioned on the headings and numbers, and in relation to a heading reading "Mutual Captive Expenses, Aggregate Reinsurance" Mr. Partridge agreed that appeared to be a reference to Mutual's aggregate reinsurance, but said that he did not recall the Programme having been written that way, and did not think that that was what it represented. He was taken to further proposal documents, but did not agree that the references were indeed references to the US $5 million layer of reinsurance introduced under article 3A.

112. Mr. Partridge was then questioned in relation to the risk transfer aspect of matters. It was put to him that it was never intended that the IPC client would be liable under the indemnity, because there was a true assumption of risk by Mutual Indemnity, taken on because of regulatory requirements. Mr. Partridge did not accept that conclusion, and thought that the reference in the documentation was to the aggregate third party reinsurance charge, and Mr. Partridge was not dissuaded from this view by the suggestion that on his interpretation, the reference would be to Legion rather than Mutual Indemnity.

113. Mr. Partridge was then questioned in relation to the concern expressed in his witness statement in relation to losses on the Programme being high, such that it had become apparent by the time of renewal that losses were threatening to burst through the AAP and mainframe (third party) reinsurance. Mr. Partridge agreed that the concern arose because it was recognised that Legion had an additional exposure to liability if the development on the Programme continued to deteriorate. His witness statement then referred to the Coverage Meeting described in the pleading and referred to at paragraph 24 above. Mr. Partridge said that he recalled the meeting, but not who had arranged it. He was by that time aware in general terms of the under-reserving problem, and

agreed that the level of collateralisation was also discussed, saying that there was a concern at exposure in excess of the aggregate attachment limits, by which Mr. Partridge meant both the AAP and third party reinsurance. He agreed that this would likely lead to a large collateral requirement for the fourth Programme year.

114. Mr. Partridge was then asked about having been told by Messrs. Bossard and Agnew that Mrs. Hendricks and American Patriot were operating under the understanding that they had an unlimited exposure to liability above the aggregate attachment limits. He said that he did not remember the word "unlimited", but did remember that they thought the Hendricks had liability above the aggregate limits; Mr. Partridge said that he did not recall Mr. Agnew regarding that as an opportunity to be used in relation to the renewal. He said that he was pleased to learn that it was their impression that the Hendricks and American Patriot were responsible for what he referred to as "losses in excess", which he said was a situation that they had never come across before, and he added that if they had not seen it that way, they would obviously have had different conversations. Mr. Partridge did not understand the concern on the part of the Hendricks and American Patriot to relate to an unlimited exposure, and said he was under the impression that there had been no discussion in relation to "unlimited" as opposed to the $5 million representing the fourth layer.

115. Mr. Partridge was then asked about his understanding at the time of the Coverage Meeting, and said that it had not been his understanding that the Hendricks had exposure to $5 million above the aggregate attachment point, saying that he did not appreciate what the limits were in layer 3A. When asked in relation to the exposure being for $5 million or unlimited, Mr. Partridge said that he could not recall thinking either way on that, but that the focus had been more on their liability, and not on the limit. Mr. Partridge confirmed that he did not know the exact limitations or specific terms of clause 3A, but said that he knew that it was there. When asked why he had not examined the terms of the treaty, Mr. Partridge responded that that was what he had asked Mr. Walsh to do. He reiterated that he had assumed that

the Hendricks were liable to indemnify Mutual Indemnity for its exposure in the $5 million layer being discussed. When it was put to Mr. Partridge that Messrs. Agnew and Bossard had disagreed with the position that the Hendricks had exposure in excess of the third party reinsurance, Mr. Partridge said that he only became aware of that later, and the he did not remember any discussion in which it was suggested that the Hendricks did not have that liability.

116. Questioning then turned to the advice given by Mr. Walsh, and Mr. Partridge confirmed that the indemnity provisions were contained in the Shareholder Agreement, so that Mr. Walsh could not express a view as to the Hendricks' liability with reference only to the reinsurance treaty. Mr. Partridge agreed that the latter document would deal only with liability owed by Mutual Indemnity to Legion, and said that was the reason that Mr. Alexander had been linked to the meeting by telephone. Mr. Partridge was asked as to his recollection of what Mr. Alexander had said as to the position under the Shareholder Agreement, and said that he had no specific recollection of this. Having read what Mr. Alexander himself had said on the matter in his witness statement, Mr. Partridge said that he had no reason to disagree with what Mr. Alexander said.

117. Mr. Partridge was then questioned in relation to the Shareholder Agreement and the amendments subsequently made to it. He said that he was familiar with the former document, although that was not a document he would have retained in his office. Mr. Partridge was then referred to the amendments made to the Shareholder Agreement on an annual basis, and was then taken to amendment number 5 (which was the amendment drafted by Mr. Alexander some time after the Programme had been renewed for the fourth year). Mr. Partridge did not accept that amendment number 5 made a radical or fundamental change to the terms of the Shareholder Agreement, as was put to him. Mr. Partridge was also asked the reason for the reference to "INSURANCE COMPANY" appearing in the amendment, a reference to Legion/Villanova, and said that he could not explain that.

118. Questioning then turned to the purchase of reinsurance protection, and Mr. Partridge said that this was to be purchased for the Programme, that there could be no reinsurance protection as such for the Hendricks, so that the reinsurance had to be in respect of either Legion's or Mutual Indemnity's liabilities.

119. Mr. Partridge was then referred to an email sent to himself and Mr. Turner, copied to Mr. Agnew, by Mr. Bossard, dated 27 March 2000. That email attached a spreadsheet analysis of losses, and it was suggested to Mr. Partridge that this would have been prepared in consequence of his request. Mr. Partridge did not feel that this would have been the case, not least because the spreadsheet contained a reference to Mr. Turner.

120. Mr. Partridge was then questioned in relation to Mr. Bossard's spreadsheet, and he agreed that provided the numbers described as the Tillinghast Developed Losses were correct, there were sufficient funds available to meet losses at those numbers. Mr. Partridge cautioned that numbers changed, and while those numbers suggested that at the time Legion was "marginally safe", he did not accept that they were in fact reliable. Mr. Partridge did not accept that because Mr. Bossard had put the reference to removing American Patriot from historical development of losses above the aggregate limit in quotation marks, this meant that this was not in fact being done. In answer to my question, Mr. Partridge said that they had enough experience in aggregate development to know that the margin of error was very close, and he felt it was a probability that further losses would develop.

121. Mr. Partridge was then questioned in relation to an email sent by Mr. Bossard to Ms. Saran on 28 March 2000, and copied to various others within the Mutual Group, but not to Mr. Partridge. Mr. Bossard said in this email that there was a market interested in removing American Patriot from an excess aggregate exposure position in the prior years, that is to say writing the retroactive reinsurance, and Mr. Bossard gave a price quote of "$350k to $650k". Mr. Partridge had no knowledge in regard to that issue. Mr.

Partridge was then referred to subsequent emails of 31 March 2000 and 4 April 2000, but again had no knowledge in relation to these.

122. Next, Mr. Partridge was questioned in relation to an email from Mr. Bossard to himself and Mr. Turner dated 14 April 2000, which reported that American Patriot had agreed to renew the Programme for the fourth year. In detailing the terms, Mr. Bossard said "The 2000 proposal clearly illustrates that they are back on after the aggregate limits." Mr. Partridge said that this was simply making the position clear to the customer.

123. Mr. Partridge was then cross-examined in relation to the 20 April 2000 letter, and what he had said in regard to that letter in his witness statement. Although Mr. Partridge was cross-examined comprehensively in relation to this part of his witness statement, dealing with his view of the 20 April 2000 letter, nothing of consequence came out in cross-examination. Mr. Partridge indicated that in his view the purpose of the proposed reinsurance was to eliminate the Hendricks from any further liability in respect of the first three years of the Programme, whether that was limited or unlimited. Although it was put to Mr. Partridge that the reinsurance was reinsurance of Legion, he felt it to be reinsurance of Mutual Indemnity, but accepted that the losses were Legion losses, whether reinsured or un-reinsured.

124. Questioning then turned to the Coverage Meeting, and Mr. Partridge reiterated what had been said in his witness statement. With particular reference to the telephone conversation with Mr. Alexander, what Mr. Bossard has said in his statement was put to Mr. Partridge, and Mr. Partridge responded that he did not think that Mr. Bossard's version was accurate, and that it was a mischaracterisation to say that there had been a misunderstanding on the part of the Hendricks.

125. Mr. Partridge was then asked about the commutation negotiations, and said it would surprise him to learn that Mutual Indemnity had taken the position with the Legion rehabilitator that Mutual Indemnity was not liable for losses falling within the 3A level. On the issue of transfer of risk, Mr. Partridge said that

the indemnity arrangements contained in the Shareholder Agreement did not affect the transfer of risk as between Legion and Mutual Indemnity.

126. There were many detailed questions asked in relation to the reinsurance documentation, but I do not think that any of the evidence given by Mr. Partridge in response is relevant for the purpose of these proceedings.

Mr. Turner

127. I have already made reference to the fact that in relation to the Coverage Meeting, Mr. Turner said that he could not recall it as it was referred to in the pleading, but he did recall discussions on their side about the Hendricks' exposure in excess of the aggregate, and clearly those discussion must have taken place at the meeting in question. He had no recollection of the advice given by Mr. Walsh, and was able to say very little more than that there had been a conclusion that exposure above the AAP and third party reinsurance did exist and they should try to address it. He also recalled discussion concerning obtaining reinsurance to protect the Hendricks. He believed that their exposure existed and was real.

128. Mr. Turner did refer in his witness statement to the onerous nature of the renewal deal proposed to American Patriot, and said that at some stage he had advised Mrs. Hendricks that this was not a deal that he would be comfortable doing if he were her, because the reward offered did not match the risk. Mr. Turner made denials in relation to the critical parts of the pleading, and said that he was not party to any plot, and there was no fraud.

129. In relation to a letter dated 4 February 2002 sent to American Patriot by Thor Bjornson of Mutual Indemnity, Mr. Turner said that the letter was not misleading, even though it had by then been a considerable time since Mutual Indemnity had been unable to obtain reinsurance protection in the market. He said the additional premium requested was simply an application of the formula contained in Mr. Alexander's letter, which he described as being properly due and payable, on the basis that Mutual Indemnity had been forced to provide the cover itself, having been unable to find it in the market. I pause to comment that that seems on its face to be a strange conclusion, although it

has to be recalled that prior to renewal, Mr. Bossard had been misrepresenting the position in relation to the availability of retroactive reinsurance coverage. However, Mr. Alexander's letter said no more than that Mutual Indemnity had agreed to purchase reinsurance coverage.

130. In cross-examination, the first issue addressed to Mr. Turner was the inter-relationship of companies within the Mutual Group. Mr. Turner accepted that Commonwealth marketed and sold the IPC programme on the basis that this was a package that MRM offered, and although Mr. Turner said that many of their markets would have focused on the name of Legion rather than that of MRM, which was a holding company, he accepted that in marketing the product, clients would not draw a distinction between the different companies within the Mutual Group, and so far as the client was concerned, it was all one company and all one product.

131. Mr. Turner was then taken to the original proposal made by Mr. McPherson on 18 February 1997, and accepted that the explanation given in the original letter could have applied equally to corporate business as to agency business. Particularly, Mr. Turner was referred to the wording referring to Mutual Indemnity's retention being increased by US $5 million in aggregate stop loss reinsurance; Mr. Turner did not think this to be a reference to the additional liability undertaken by Mutual Indemnity under clause 3A of treaty 103, but the reference to reinsurance which would be in the third layer. Mr. Turner added that it was irrelevant so far as the client was concerned whether it was Mutual Indemnity or Legion on risk in that layer. Mr. Turner was asked questions in relation to the numbers appearing in the subsequent proposal of 24 March 1997, he responded that the proposal had changed since Mr. McPherson's proposal. Mr. Turner was then taken through the proposals for the three Programme years, and agreed that these were the documents which the client would have seen. Mr. Turner did not regard it as relevant for the client to know, as he put it, the different facets of the Mutual Indemnity risk. He accepted that the client would have no knowledge as to how reinsurance charges would have been allocated as between Legion and Mutual Indemnity.

132. Mr. Turner was then taken to amendment number 1 to Reinsurance Treaty 103. He said that he was aware in broad terms that there was an amendment of some sort which was tied into risk transfer between Legion and Mutual Indemnity.

133. Questioning then turned to the Coverage Meeting, although Mr. Turner did not remember it being in Mr. Partridge's office, and in fact thought there had been a series of meetings, but he did remember the four of them, himself, Mr. Partridge, Mr. Agnew and Mr. Bossard being together and discussing the American Patriot renewal. Mr. Turner said that he was vaguely aware of clause 3A at this point, but was not sure that he had "connected the dots" in relation to the liability of American Patriot/the Hendricks. Mr. Turner said that it was for that reason that the question of what would happen if losses went through the third layer came up, and that that discussion had led to communication with Mr. Walsh. Mr. Turner said that at that point he was not focusing on the extent of the exposure if losses went into the next layer, so much as to where the exposure lay. Mr. Turner said that he felt that when the question was put to Mr. Walsh, the latter had indicated that he would look into it and revert, and Mr. Turner thought that he had got back to them later, and could not recall whether he found out directly from Mr. Partridge or from Mr. Walsh. In relation to the issue of reinsurance to protect the Hendricks from exposure to losses in excess of the AAP and third party reinsurance, Mr. Turner accepted that the Hendricks' liability arose under the indemnity provisions of the Shareholder Agreement, and not under any reinsurance agreement, so that in talking of reinsurance, they had been talking about obtaining reinsurance for Legion or Mutual Indemnity.

134. In relation to the premium of $1 million, Mr. Turner thought that that number had come from Mr. Agnew or Mr. Bossard.

135. Mr. Turner was then taken to Mr. Bossard's email of 17 March 2000, and said that he was not at that time sure of the extent of Mr. Bossard's knowledge of whether the Hendricks were on risk for layer 3A. Mr. Turner reiterated that he did not know what the reinsurance, if obtained, would cost. Mr. Turner

was then taken to the subsequent email from Mr. Bossard of 28 March 2000, and reiterated that he had a concern at the level of collateral required for renewal of the Programme in year four, which he did not feel represented a good risk. Mr. Turner had no knowledge of the suggested cost of reinsurance referred to in that email, but said that in relation to the process of obtaining approval at a higher level, there would need to be a quote before that step could be taken. Next Mr. Turner was taken to Mr. Bossard's email of 31 March 2000, which referred to a firm quote from reinsurers; he was not able to say on what basis Mr. Bossard had made that statement. Next was the email from Mr. Bossard of 4 April 2000 to Ms. Saran, attaching a revised sample letter, to be sent by Mr. Alexander. Mr. Turner had no recollection of the conversation with Mr. Alexander, referred to by others. He was then taken to the final form of Mr. Alexander's letter of 20 April 2000, and the reference to "any losses" appearing in the first paragraph, and agreed that was different from the position in relation to losses pursuant to clause 3A.

136. Mr. Turner was taken to an email sent to him by Mr. Eaton, covering the excess of loss terms and the retroactive aggregate for the first three Programme years. He said that it would be perfectly normal for him to be following up with Mr. Eaton to see what the position was. Mr. Turner did not agree that Mr. Eaton was trying to place the reinsurance cover for Legion, as opposed to Mutual Indemnity. Mr. Turner was referred to Mr. Eaton's deposition, with reference to placing retroactive cover for Legion, and thought that Mr. Eaton was mistaken.

137. Mr. Turner was then taken to Mr. Bjornson's request of 4 February 2002 for $520,000 in premium due to Mutual Indemnity. Mr. Turner agreed that at this time no reinsurance had been purchased, but referred to Mutual Indemnity being "on the hook" for all of those losses, and said that they wished they had been able to buy reinsurance, because that would have saved the company a lot of money. I pause to note that that might have been the position as Mr. Turner understood it at one stage, but was not the position following execution of the Commutation Agreement. Mr. Turner accepted that the letter made no reference to Mutual Indemnity being on risk as opposed to

reinsurance protection having been purchased, but said that the client had suffered nothing by reason of no reinsurance having been purchased.

138. Mr. Turner was then taken back to the Coverage Meeting, with reference to what Mr. Agnew had said in his witness statement. Mr. Turner was referred to and accepted his earlier evidence that he may have shared Mr. Agnew's understanding that Mrs. Hendricks was not responsible for losses above the AAP, but he did not agree that Mr. Partridge shared that understanding. He thought the latter was more cognisant of it because it was something that he had actually worked on, in terms of putting it together. It was suggested to him that on this basis Mr. Partridge would have given his view as to the existence of exposure, but Mr. Turner thought it more likely that he would simply call Mr. Walsh to find out what the position was. Mr. Turner did not recall or accept that matters had happened at the meeting as contended for by Mr. Agnew, and indeed suggested that Mr. Agnew had compressed discussion from various meetings into discussion at the one meeting. Mr. Turner did not recall the question to Mr. Walsh as to exposure being put on the basis that the Hendricks had a misunderstanding as to their exposure; he accepted that the meeting understood the Hendricks to believe they had an exposure over the AAP. Mr. Turner did not recall any discussion in relation to having to "change the amendment" for the specific client, as suggested by Messrs. Agnew and Bossard in their witness statements.

139. Mr. Turner was again taken to the subject of the telephone conversation with Mr. Alexander, and reiterated that he did not recall that, but did not think that had happened as suggested by Mr. Agnew in his witness statement. But he had no recollection of participating in any conversation with Mr. Alexander.

140. In relation to the obligation upon the Hendricks in relation to clause 3A, Mr. Turner did not accept that premium was charged for a liability that did not accrue to the Hendricks, but instead resided either with Legion or Mutual Indemnity.

Mr. Walsh

141. Mr. Walsh set out in his witness statement his understanding as to how the "rent-a-captive" concept operated generally, and then referred to the various documents containing the terms of the American Patriot Programme. He referred to the terms of treaty 103, and the amendment of that treaty in 1993 by article 3A. He said that because the indemnification provisions in the Shareholder Agreement followed the provisions of the reinsurance treaty between Legion and Mutual Indemnity, the customer or shareholder such as American Patriot/the Hendricks was responsible for losses falling within this top layer of reinsurance. That statement of course coincided with what Mr. Alexander had set out in his witness statement, to which I have referred in paragraph 13 above. Mr. Walsh indicated that he had drafted treaty 103 and article 3A, and confirmed that article 3A had been introduced in order to transfer an additional layer of risk to the offshore Mutual companies, in order to satisfy regulatory requirements regarding transfer of risk.

142. Mr. Walsh recalled that he had had some discussions in relation to the renewal of the American Patriot Programme for the fourth year on an unrelated matter, and recalled that during the 2000 renewal process he had received a telephone call from Mr. Partridge, with Messrs. Turner, Agnew and Bossard on speaker phone. He said they had told him that the American Patriot renewal was coming up and that the losses on the Programme looked as if they would blow through the AAP and third party reinsurance. He said that they wanted to know who would be responsible for the losses if they did break through the aggregate. He said that it was the first time such an issue had arisen, that it was not an issue he had thought about, and that previously everyone had thought that there was enough third party reinsurance that there would be no need to worry about this question.

143. Mr. Walsh's recollection was that he needed to look into the position and revert. He said his recollection of the telephone call was not particularly good, but he did not believe that any one had asked him if the contract could be changed retrospectively. He said he might have been asked whether, if the

liability were there, a change could be made. He said his response to this was that the only way to do this was to change the reinsurance agreement retrospectively, but that could not be done, and he confirmed that this was the correct advice.

144. Mr. Walsh confirmed that his recollection was that there was a period of time before he got back to the group with an answer, and felt he had done a reasonably thorough job of looking thorough the contracts. He said that his view following that exercise was that Mutual Indemnity was liable for the fourth layer of losses, and that the Hendricks were liable under the Shareholder Agreement to indemnify Mutual Indemnity in respect of losses in that fourth layer. Mr. Walsh confirmed that he did not give the advice as pleaded in the statement of claim.

145. Mr. Walsh did recall that following his advice as to the Hendricks being on risk the idea had come up to offer them protection from their exposure, but he was not sure whose idea that was. He did not recall being involved in any telephone conversation with Mr. Eaton, but did recall learning at some stage that Mr. Eaton doubted that it would be possible to purchase such reinsurance, and that if available, the cost would be high. Mr. Walsh's understanding of the proposed premium was that at this point this would likely be more than the Hendricks could reasonably be asked for, so that the figure was decided upon at the price it would have cost before losses had been incurred.

146. Mr. Walsh made it clear that he did not instruct Mr. Bossard or Mr. Agnew to do anything, or to tell the Hendricks the position in relation to their responsibility for losses in excess of the AAP. He did recall that Messrs. Bossard and Agnew were to go back to the Hendricks and offer reinsurance.

147. Mr. Walsh reiterated his view that the exposure of the Hendricks above the AAP existed, and that there was nothing false or untrue in any representations to this effect. He denied being fraudulent or reckless as alleged in the statement of claim. Mr. Walsh said he had not been involved in the discussion on a variable premium, had not been involved in the drafting of the 20 April

2000 letter or the subsequent amendment to the Shareholder Agreement, and had not been involved in the negotiation of the Commutation Agreement.

148. In cross-examination, Mr. Walsh was taken to article 3A, and asked questions in relation to the transfer of risk issue, said to have been the reason for the introduction of this clause. It was put to Mr. Walsh that there was no actual transfer of risk, and Mr. Walsh said that there was a distinction to be drawn between the transfer of risk and the retention of risk, or, put another way, assumption of risk and maintenance of risk. Mr. Walsh continued that there had been a transfer of risk analysis which had been undertaken at the time. He would not accept that there could be no transfer of risk unless Mutual Indemnity assumed an unfunded risk.

149. Mr. Walsh was then taken to amendment number 4 to treaty 103, which he confirmed he had drafted. He agreed that the intent of the amendment was to add Mutual Indemnity as a reinsurer, but added that it did not appear that that was the result. In relation to amendment number 5, when asked as to its purpose, Mr. Walsh said that the effect was to add Mutual Indemnity and Mutual Indemnity (Dublin) Ltd ("Mutual Dublin"). When it was put to him that the purpose was to add Mutual Dublin, Mr. Walsh said that as well as that, the reason was to "clean up the Bermuda issue". It is not clear from the copy of the document in the bundle, but this amendment was apparently signed by Mutual Dublin.

150. Mr. Walsh was then questioned in relation to the Coverage Meeting, with reference to his witness statement. He did not recall being told what others had thought in relation to the liability of the IPC client above the AAP. Mr. Walsh did not recall being told what Mrs. Hendricks thought her exposure might be, but he accepted that the question asked of him had been in the context of the American Patriot renewal approaching, so that the question had no doubt arisen in that context. Mr. Walsh was sure that he had said that he would look at the matter and get back to the meeting.

151. Mr. Walsh was then questioned about the description in his witness statement of the response to the question as to how the reinsurance agreement might be

changed retrospectively, so as to impose a liability above the AAP on a client when none previously existed. He had said that this could not be done, and that that was the correct advice, and when pressed agreed that it might be technically possible, given the number of previous retrospective amendments to the reinsurance agreement, but not so where the economic interests of the shareholder would have been affected.

152. Mr. Walsh confirmed that he had reverted with the answer, probably the same day or the next, but did not recall to whom he had spoken, although he accepted that it was likely to have been to Mr. Partridge and Mr. Turner. He did not know whether he had called Mr. Bossard and Mr. Agnew. Mr. Walsh did think that he had looked at the master copy of the Shareholder Agreement which he kept in his office. He did not believe that he spoke to Mr. Alexander about the issue. He accepted that one of the reasons for his conclusion was his view that the indemnity provisions in the Shareholder Agreement extended to what has been referred to in these proceedings as the fourth layer. He did accept that it was probably true that the Hendricks never had copies of the reinsurance agreement and its amendments. Mr. Walsh did not recall being consulted for advice in connection with the proposed purchase of reinsurance, and did not think that likely.

153. Mr. Walsh was then questioned concerning the decision to charge the Hendricks $1 million for the reinsurance, which had been referred to in his witness statement. He had no detailed recollection, save that he did not believe that the protection being sought was unlimited.

154. Mr. Walsh was then questioned in relation to the Commutation Agreement, which he had not been concerned with at the time, and had learned of relatively recently. He accepted that the position taken in those negotiations was inconsistent with the advice that he had given as to how the reinsurance treaty worked, and said that had he been involved in representing Legion when Mutual Indemnity took the position described, he would have disagreed with them.

155. Mr. Walsh was then taken to amendment number 5 to the Shareholder Agreement, which he had not drafted, and agreed that the effect of clause 1, as drafted, was to seek to impose an obligation on Legion/Villanova as well as Mutual Indemnity. Mr. Walsh's view was that it would have been preferable to change the reinsurance agreement rather than the Shareholder Agreement. He did not accept that the amendment to the Shareholder Agreement imposed liability on the shareholder to Legion, which was not a party to the Shareholder Agreement or the amendment.

Mr. Alexander

156. Mr. Alexander gave an overview of the structure of the Mutual Group, and emphasised the need to keep the operations of the onshore and offshore companies separate. He said that while MRM controlled the overall strategy at a group level for the MRM companies, it did not manage the day to day actions of each group company.

157. Mr. Alexander's witness statement dealt with the role of Commonwealth, the issue of claims management and Cunningham Lindsey, and gave an overview of rent-a-captive business, with reference to both corporate and agency business, and I have referred to the operation of agency business already. As I have said, it was Mr. Alexander who had described the different layers of risk for programmes generally. He then dealt with the history of the relationship between companies within the Mutual Group and American Patriot, and then turned to the renewal of the Programme for the fourth year.

158. Mr. Alexander recalled being telephoned, and although he could not recall the date or the time of year, he accepted it might well been in February 2000. He recalled the call involving Mr. Partridge and Mr. Walsh, but was not sure of anybody else. His recollection was that Mr. Partridge had explained that the American Patriot Programme was developing adversely, something that Mr. Alexander said that he had already been aware of in general terms. He said that Mr. Partridge wanted to know if there was anything in the Shareholder Agreement as to who was responsible for the payment of losses in the event that losses exceeded the third party reinsurance layer, the third layer in his

description of risk. Mr. Alexander believed that he probably explained what he then understood to be the case, namely that there was nothing specific in the Shareholder Agreement, but that the risks should fall to the IPC client unless ceded to a third party reinsurer. That he said was his understanding at the time, and had always been his understanding.

159. Mr. Alexander could not remember what Mr. Walsh had said, but indicated that if Mr. Walsh had said anything different from his own understanding, he was sure that he would have remembered that. He did remember having further conversations with Mr. Walsh regarding the issue. He also recalled signing the letter of 20 April 2000 (which he said he had not drafted) and referred to the earlier emails. Mr. Alexander referred to the first instalment of premium in the sum of $480,000 and said that after his email enquiry of Mr. Agnew in mid May, he did not think he had thought anything more about matters.

160. In relation to the allegation that the placement was a fraud, Mr. Alexander described this as nonsense, and said that he and his colleagues had been trying to accommodate a client's concern about an exposure in a programme which was performing very badly. He denied being a party to any conspiracy to charge money for a liability which he did not believe existed, saying that he believed at the time, as he felt they all did, that the IPC client was liable for all losses not covered by third party reinsurance. Mr. Alexander did not draw a distinction between fourth layer losses and losses above that layer. He said that the payment of the reinsurance premium remained on Mutual Indemnity's books as a payable, because he believed that the money would eventually be paid to a third party to purchase reinsurance. Mr. Alexander said that he believed that the request for the second instalment of premium, made by Mr. Bjornson, had been calculated in accordance with the agreed formula.

161. Mr. Alexander then turned to amendment number 5 to the Shareholder Agreement, which he said that he had drafted without legal help, as he typically did, seeking to combine the renewal and the 20 April 2000 letter into a single document. Mr. Alexander said that he thought that the best way of

recording the position which had been reached at that time was to state that American Patriot would be liable for losses in excess of the second layer, not covered by Legion third party reinsurance, and excluding years one to three. He said that he intended the reference to "additional reinsurance purchased by Legion" to be a reference to the third party layer, and not to the additional layer of reinsurance to be procured according to the terms of the April 2000 letter, which would be the fourth layer according to Mr. Alexander's description. Mr. Alexander said in his statement that he now appreciated that the effect of his amendment number 5 was to make the American Patriot parties liable for losses above the fourth layer, whereas the amendment should have made the American Patriot parties liable for losses in the fourth layer for the fourth Programme year. Mr. Alexander stated that this error was due to his misunderstanding of the true contractual position, and said that he honestly believed that the IPC client was liable for all risks not ceded to third party reinsurers, i.e. for losses in the fourth layer and beyond. Mr. Alexander did contend that the April 2000 letter had given the American Patriot parties a real benefit, insofar as it gave the American Patriot parties cover for a liability that did exist for the first three Programme years, and was real because the losses did end up in the fourth layer.

162. Mr. Alexander stated that he did not know until "much later" that the reinsurance proposed in the April 2000 letter had not been placed, but said that while he assumed that it had been, it would not have altered matters if it had not; as far as he was concerned, the Mutual Group had agreed to relieve the American Patriot parties from all further risk for years one to three, and he believed that amendment number 5 formally set out this reduction in the liabilities on their part.

163. In relation to the fact that MRM Hancock were never able to place the reinsurance, Mr. Alexander believed that the purchase of reinsurance was realistic, that Legion had modeled the pricing and that he did not have the experience to dispute their underwriting capabilities, and he referred to having been assured by Mr. Agnew that the placement could be made at the prices

quoted. Mr. Alexander then set out various arguments for his contention that he would not have been a party to a fraud.

164. Mr. Alexander then turned to the Commutation Agreement, which he said covered some 112 programmes, of which one was the American Patriot Programme. This had started with a letter agreement dated 3 July 2002, and the sums payable in respect of each individual programme were arrived at with assistance from consulting actuaries on both sides. Mr. Alexander referred to the benefits for both Legion and Mutual Indemnity of a commutation, and then described how Legion's rehabilitator had taken some form of objection which had led to litigation in the Pennsylvania court, resulting in an increase of $5 million from the original figure agreed.

165. Mr. Alexander described how he had been involved in the negotiations along with Mr. Mulderig and Paul Watson, his predecessor, and described how Mr. Mulderig made the strategic decisions while he and Mr. Watson had taken care of the technical side. He referred to the argument that Mutual Indemnity had not been a party to the 1993 amendment to the treaty (the clause 3A argument), taken on advice from US attorneys, and described the outcome as being "a great one" for Mutual Indemnity, particularly in relation to the Programme, where losses had in fact entered the fourth layer. Mr. Alexander set out a table in his witness statement demonstrating that the commutation figures were either at the AAP or below. However, Mr. Alexander referred to the fact that the settlement sum of $8,595,361 paid by Mutual Indemnity to Legion in respect of losses on the Programme meant that Mutual Indemnity had suffered a loss on the Programme. He referred to the four letters of credit which had been re-issued in 2001, representing collateral, of which three had been drawn down, totaling $5,176,000. The fourth letter of credit which remained frozen by the California Court was in the sum of $3,072,107.50, but Mr. Alexander advised that the total due from American Patriot/the Hendricks to Mutual Indemnity was $3,419,361, representing the amount of the commutation of the Programme, less the draw downs effected.

166. Mr. Alexander did then produce a supplemental witness statement dealing with the factual position underlying the corporate law issues which arose late in the day. Mr. Alexander referred to how in his capacity as president of Mutual Holdings, he liaised with Commonwealth and Legion in relation to potential new clients. He described how Commonwealth would finalise programme details directly with the IPC client, once Legion had indicated its satisfaction with the underwriting, and he had been satisfied with the collateral arrangements in respect of Mutual Holdings' Gap. In due course he would expect to hear from Legion to advise that the programme terms had been agreed. The next stage was the creation of the share series relating to the particular programme, and the appointment of an account executive, who would usually arrange for the shareholder agreement to be finalised in respect of the relevant share series.

167. Mr. Alexander advised that he had not realised until a few weeks ago that in the case of the American Patriot Programme, designated C30, neither American Patriot nor the Hendricks had been recorded in the register of members of Mutual Holdings, and no share certificate had ever been issued for the contemplated preference share. Mr. Alexander thought at first that this must have been due to the fact that the $1,000 required under the Shareholder Agreement had not been paid, but recent enquiry had disclosed that no request had been made of the corporate administrators. Mr. Alexander described the process of setting up the new share series, and advised that he had understood that he had the authority to do this, and he believed that he was following the same process as his predecessor. He had not been aware that until 1997 there had been an IPC committee dealing with such matters on behalf of the company.

168. Cross-examination of Mr. Alexander began with a series of questions in relation to the Mutual Group companies and Mr. Alexander's role within the group, and he was taken through the SEC registration statement filed by MRM, in some detail. That covered the operation of treaty 103, and Mr. Alexander described how Mutual Indemnity invested premium on behalf of programmes collectively. He described how assets were pooled and given to

various investment managers, and the amounts of $1,000 for each preference share were dealt with similarly.

169. In relation to the declaration of dividends, Mr. Alexander confirmed that dividends would be declared across the whole of the company's underwriting business, taking into account profits and losses in relation to all programmes that had been underwritten. Mr. Alexander confirmed that in relation to losses, Mutual Indemnity would pay these out of its own funds, and then recover from the collateral held in respect of the individual programmes. If there was not enough money in the collateral account, a claim would be made of the IPC client under the indemnity provisions in the relevant shareholder agreement. Hence while Mutual Indemnity could suffer an underwriting loss, the effect of the indemnification provisions was that it did not ultimately suffer a loss.

170. In relation to a new programme, Mr. Alexander said that it would be unusual if he were to see the programme proposals, since those were between Commonwealth and the onshore IPC client. He said that he received the information for the preparation of the shareholder agreement from a document called the account summary sheet, prepared by Commonwealth.

171. Mr. Alexander was taken though the operation of Legion's treaty providing coverage at the third layer with unrelated reinsurers. He confirmed that the phrase "the third layer" was his, and that at the material time he knew the treaty as the mainframe or cessions treaty. Mr. Alexander confirmed that his understanding of these arrangements was vague and he was not aware of the detail. In relation to the fourth layer, Mr. Alexander was taken back to that part of his witness statement in which he had said "the whole point was the IPC client took on the risk and rewards of the underlying insurance policies". Mr. Alexander conceded that above the fourth layer, the risk went back to Legion, so that the IPC client did not take on all of the risk.

172. Mr. Alexander was taken to various corporate documents in terms of bye-laws and minutes. In relation to the Mutual Holdings minute book, Mr. Alexander had not reviewed this, and so was unable to answer questions as to the

existence or non-existence of a particular resolution, and cross-examination on that aspect of matters was deferred until such time as he had had an opportunity to review the minute book.

173. Mr. Alexander was then taken to the provisions of treaty 103 and questioned in relation to article 3, and the first amendment which had added article 3A. Mr. Alexander confirmed that he had not been involved at the time that clause 3A was added to the treaty, and that his understanding of what the clause was designed to achieve was based on what he had been told by others. Mr. Alexander was asked a question in relation to Mutual Indemnity's liability in the fourth layer, taking the year 2000 as an example. His response was that at that time no calculation had been undertaken to determine the extent of Mutual Indemnity's liability under this clause. Mr. Alexander said that he had never discussed how the calculation would be undertaken because for many years the question had never arisen. He described how it had become an issue in 2002, when Legion had sent down spreadsheets detailing a number of programmes that had gone through the third layer, and said that they had never actually determined how the losses would be divided across the relevant programmes. He was pressed as to the appropriate mechanism, but his response was "we never got that far".

174. Mr. Alexander was then taken to the Shareholder Agreement, and taken through the clauses covering calculation of underwriting gain or loss, and the consequent provisions for indemnity and declaration of dividend, and was then taken to amendment number 1 relating to the transfer of the preferred share from American Patriot to the Hendricks. Mr. Alexander did not have a particularly clear recollection of this document, although he did understand the purpose being "to put Mr. & Mrs. Hendricks on to the Shareholder Agreement and take American Patriot off". Mr. Alexander confirmed the claim was maintained against American Patriot on legal advice.

175. Mr. Alexander was asked questions in relation to the accounting undertaken, particularly with reference to the different lines of business, but did not regard

that as pertinent for the purposes of the Shareholder Agreement. He dealt with general questions in relation to the preparation of the accounts.

176. Questioning then turned to the Coverage Meeting. Mr. Alexander said that it had not been a long call, and he did not remember Mr. Walsh making any particular contribution, but had a clear recollection of Mr. Partridge asking if there was anything in the Shareholder Agreement as to who was responsible for losses above the third party reinsurance layer. Essentially, Mr. Alexander repeated the position as set out in his witness statement. He said that he had not referred to the Shareholder Agreement before his response to Mr. Partridge that there was nothing specific in it governing the position. Mr. Alexander said that he knew the Shareholder Agreement well enough to know that it did not cover matters such as the AAP. Mr. Alexander confirmed that his answer was not based upon any understanding that clause 3A applied.

177. Mr. Alexander did recall speaking to Mr. Agnew in regard to the proposed April letter, and as well as being informed that the price of the reinsurance had gone through the Legion pricing model, recalled an assurance from Mr. Agnew that there was a chance of securing the reinsurance.

178. It was put to Mr. Alexander that when he received the draft of what became the 20 April 2000 letter, he was aware that the AAP represented Mutual Indemnity's maximum liability, and Mr. Alexander initially accepted that, before referring to the fact that the shareholder came back on after the third layer. He regarded the proposal to purchase reinsurance as a mechanism for Mutual Indemnity to take over American Patriot's liability, but agreed that the letter did not literally make sense.

179. Mr. Alexander was then taken to Mr. Bjornson's email to Mr. Agnew of 29 October 2001. This email showed the losses penetrating above the $3 million threshold to be only $1,624,251, which produced a figure less than the provisional premium of $480,000, so that Mr. Bjornson concluded that no further for billing for premium could be made at that point. Mr. Alexander agreed that Mr. Bjornson's calculation was correct. Mr. Alexander was then taken to Mr. Bjornson's letter of 4 February 2002 to Ms. Saran, in which he

sought further premium of $520,000. The calculation in the latter document was undertaken somewhat differently than in the former. Mr. Alexander accepted that the demand for premium in the 4 February 2002 letter did not appear to have been calculated in accordance with the formula contained in the April 2000 letter. Mr. Alexander was then taken to the subsequent correspondence with Ms. Saran in which the numbers at issue were disputed, and he accepted that that dispute had never been resolved. Mr. Alexander accepted that by this time he knew that no reinsurance had been purchased, but said that he did not know that the premium calculation had been wrong. In relation to the non-placement of the reinsurance, Mr. Alexander said that had felt no need to advise Ms. Saran of that, because Mutual Indemnity had already relieved them of any obligation. It was put to Mr. Alexander that the reinsurance referred to in the April 2000 letter could only have been Legion's reinsurance, not Mutual Indemnity's. Mr. Alexander said his mind-set at the time was that it was Mutual Indemnity which had agreed to take the liability from the Hendricks. He thought they were going to get reinsurance, and accepted that once it turned out that they could not get it, that was going to give him (Mutual Indemnity) a problem. Mr. Alexander accepted that the $1 million total represented by Mr. Bjornson's calculations was too much, and also recognised that in consequence of the Commutation Agreement this was to be set off against the $3 million plus due from the Hendricks. But Mr. Alexander accepted that his position in relation to the $1million had not been disclosed to the Hendricks at the time, although ultimately it was.

180. Mr. Alexander was then taken to amendment number 5 to the Shareholder Agreement, which he had drafted without, he believed, getting legal advice. Mr. Alexander said he was trying to achieve in that document what had been agreed in the April 2000 letter, but acknowledged that he had not done so. The particular wording came from the fact that Mr. Alexander wanted to make it clear that the shareholder was responsible for losses in the fourth layer for the fourth Programme year, but taking out that responsibility for the first three Programme years. Mr. Alexander denied that the document was drafted with an intent to deceive anybody.

181. Mr. Alexander was then taken to the letter sent by Mr. Bjornson to Ms. Saran of 3 November 2000 in which he sought execution of the amendment. The letter referred to the reinsurance purchased by Mutual Indemnity, and Mr. Alexander agreed that should have been a reference to the reinsurance purchased by Legion, ie the third layer.

182. Mr. Alexander was then taken to the subject of the Commutation Agreement. He said that he had not remembered about the operation of clause 3A until about the middle of March 2002, and that had caused him to make a mistake as to how the Programme worked. Mr. Alexander was taken to the details of the commutation figure, and accepted that there was no separate calculation in the agreement detailing the calculation in relation to individual programmes, but said that there was such a calculation elsewhere. Mr. Alexander confirmed that the figure of $8,123,888 (which had been referred to in an affidavit he had sworn on 22 May 2003) was the figure payable under the Commutation Agreement in respect of the American Patriot Programme at that time. The affidavit did make it clear that the expectation was that this number was likely to increase to approximately $8.6 million. Mr. Alexander was taken to correspondence detailing the dispute that had arisen between the parties in relation to the degree of collateralisation required. Mr. Alexander confirmed that that was a dispute which had never been resolved, because it had been overtaken by events.

183. Mr. Alexander was then taken through a calculation by Mr. Martin with a view to demonstrating that the amount referable to the commutation of the American Patriot Programme was not the number that he had given. This exercise was done with reference to Mr. Alexander's commutation calculation, which had been exhibited to an affidavit he had sworn on 22 May 2003. Mr. Martin suggested to Mr. Alexander that it was impossible to derive his figure as to the extent of American Patriot's obligation under the Shareholder Agreement from the numbers in that document, and received a response that that was so when undertaking the calculation Mr. Martin's way. Mr. Alexander was taken through the audited financial statements for the

Programme. Mr. Alexander accepted that the figures in those statements did not tie back to his calculation of the appropriate commutation figure.

184. Mr. Alexander did refer to the fact that by this stage of matters, there had been a number (he referred to 5 or 6 being "the big ones") which had gone through the third layer and were now into the fourth layer which would be covered by treaty 103, clause 3A. Mr. Alexander said that that was the point at which he had taken the matter to the board. Mr. Alexander accepted that in order to determine which programme would ultimately be responsible for which portion of that fourth layer, one would need to know the full loss development on all programmes, although he pointed out that they had not got to that stage, and of course the Commutation Agreement meant that the calculation was never undertaken.

185. Mr. Alexander was then questioned in relation to his review of the Mutual Holdings minute book. He accepted that there were no minutes of any shareholder meeting until 13 May 2010 showing that the shareholders had had a meeting in respect of the issue of any shares to IPC clients. Mr. Alexander further accepted that the shareholders had waived presentation of the accounts in the years 1997 to 2001, that there were no records of any preferred shareholder meetings, no records of any waivers of any presentation of accounts, and no records showing that the board had resolved to declare and pay dividend.

186. Mr. Alexander was then taken to the directors' and shareholder's resolutions dated 13 May 2010. He confirmed that it was his understanding that all corporate action necessary to issue the C30 preferred share had now been taken. Mr. Alexander accepted that part of the directors' resolutions had been inaccurate, insofar as it referred to the C30 preference share having been issue. Mr. Alexander was then taken through the accounts of Mutual Indemnity, which he explained. He confirmed that for the year ended 31 December 1997, there had been no dividend paid to the common shareholder, but a dividend of $8,413,172 to the preferred shareholders. Mr. Alexander was taken through the corresponding provisions in subsequent years. He was

then taken to the correspondence with the corporate administrator in relation to the issue of the preferred shares; he agreed that the $1,000 had not been paid by American Patriot, and that there had been no follow-up in relation to that failure.

187. Mr. Martin closed his cross-examination by putting the terms of the discussion at the Coverage Meeting as pleaded, and received the predictable denial.

188. In re-examination, Mr. Alexander was questioned in regard to the basis upon which premium was to be calculated pursuant to the April 2000 letter. He could not indicate the basis of charge in respect of losses above $1.5 million and below $3 million. In relation to the figure claimed pursuant to the Commutation Agreement, Mr. Alexander was confident that the figure given in the exhibit to his affidavit previously referred to was correct, not least because numerous people in Legion had checked his calculation and signed off on it. Mr. Alexander confirmed that the way his commutation calculation had been done was different from the way it had been put to him by Mr. Martin.

Mr. Mulderig

189. Mr. Mulderig's evidence in his witness statement was that he had no personal involvement in the American Patriot programme, but was involved in the negotiations with Legion's US rehabilitator which ultimately led to execution of the Commutation Agreement. Mr. Mulderig described the commutation as having led to a dramatic decrease in Mutual Indemnity's liabilities to Legion, and in consequence a decrease in the IPC clients' liabilities under the indemnity. Mr. Mulderig advised that in relation to the negotiations, MRM was advised by US lawyers, and during the process came to appreciate that Mutual Indemnity had not been an original signatory to the amendment to treaty 103 introducing clause 3A. He said that on advice this led to MRM taking the position that Mutual Indemnity was not bound by clause 3A, and he said that this argument was accepted by Legion's liquidator, which discounted entirely any potential additional exposure to Mutual Indemnity above the AAP. Mr. Mulderig said that before advice from their US attorneys, if he had

been asked whether the IPC client was liable for insurance losses above the AAP not covered by third party reinsurance, he would certainly have answered affirmatively.

190. In his cross-examination, Mr. Mulderig was taken to the amendment introducing article 3A, and he recalled that this was introduced to increase the transfer of risk. Mr. Mulderig was taken to the proposal for the 1998 Programme year, with particular reference about the page headed "Programme Development", and was asked, as other witnesses had been, about the reference to "specific and catastrophe reinsurance" following the reference to Legion expenses, and to "aggregate reinsurance" following the reference to Mutual Captive Expenses. Mr. Mulderig did not think the document was correct as written, and said that the reference to "aggregate reinsurance" would have been to reinsurance purchased by Legion, and not Mutual Indemnity.

191. Mr. Mulderig was then taken to the various amendments to reinsurance treaty 103. Mr. Mulderig accepted that the purpose of amendment number 4 was to add Mutual Indemnity to the agreement, and the purposes of amendment number 5 was to add Mutual Dublin to the agreement. Mr. Mulderig was asked why in his witness statement he had referred only to Mutual Indemnity, as opposed to Mutual Dublin, when the latter had also not been an original signatory to amendment 3A. Mr. Mulderig said that he did not recall if there were any programmes with Mutual Dublin which would have been relevant.

192. Mr. Mulderig was then taken to the letter which he had written on behalf of MRM to the Legion/Villanova rehabilitator, dated 25 April 2002. Mr. Mulderig was asked whether he accepted that when writing this letter he was under a duty to make full disclosure of all relevant matters relating to the commutation proposal; Mr. Mulderig did not accept that. He did accept that the letter did not give any explanation as to why it was said that Mutual Indemnity was not covered by clause 3A. Mr. Mulderig did accept that another part of the letter suggested that Mutual Dublin was a party to treaty 103. Mr. Mulderig did not accept that if Mutual Indemnity had taken the

position with its IPC clients that it was not exposed to liability under clause 3A, that would necessarily be inconsistent with the position taken in the 25 April 2002 letter. He drew a distinction between the commercial agreement and the position as it might be legally.

193. Mr. Mulderig was also asked about his understanding as to the operation of clause 3A in the event that there were substantial losses in other programmes. Mr. Mulderig accepted that liability in the clause 3A layer from one programme could affect the position in the same layer in relation to different programmes. He did not recall any discussion as to how the allocation might be undertaken on a programme by programme basis.

194. Mr. Mulderig did recognise that there could be an inconsistency insofar as only Legion had signed amendment 3A (not Villanova or Legion Indemnity), but said that a position had not been taken with the Legion rehabilitator in regard to those latter companies as had been taken with regard to Mutual Indemnity.

195. I put a question to Mr. Mulderig in relation to amendment 4, which had not been signed by Mutual Indemnity, because I had inferred that the lack of signature on the amendment was the basis for the advice from the US attorneys. Mr. Mulderig said that as far as he recalled, the basis of the advice related to the lack of Mutual Indemnity's execution of amendment number 1, rather than the same position in relation to amendment number 4.

Evidential Conflicts

196. I have set out the evidence given in this case in considerable detail because of the very serious nature of the allegations which I described at the outset as being at the core of this dispute. True it is that there are now a number of alternative ways in which the case has been, but the fraud allegation was the crux of the case at the outset, and remains a very serious matter which has to be resolved on the basis of the evidence.

197. It is to be expected that there will be conflicts between the witnesses on both sides, and it is also to be expected that there might well be conflicts between

the witnesses on the same side. In broad terms, the factual matters in dispute occurred ten years ago, so that it is natural that parties will have differing recollections of those events. The importance of the event in question is no doubt to be borne in mind; witnesses are more likely to make mistakes (and less likely to lie) in relation to matters which are not at the heart of the dispute between the parties.

198. That said, I would propose to start by looking at the inconsistencies which appear to me to have arisen on the evidence, whether or not the evidence is on a topic that is important in the case. At the same time, it has to be recognised that very minor inconsistencies demonstrate no more than that recollections fade with the passage of time.

199. I start by referring to inconsistencies raised in the evidence on behalf of the plaintiffs only. There are two which are so minor that I do not draw any conclusion from them; these are in relation to whether Mr. Turner attended the client meeting on the occasion of the first visit to American Patriot's offices, and whether or not Mr. Bossard and Mr. Agnew, in relation to the Coverage Meeting, went first to Mr. Partridge's office or first to Mr. Turner's office. Then there is the question of whether Mr. Walsh attended the meeting by telephone, or in person as well. Mr. Bossard referred only to Mr. Walsh having been on the telephone. Mr. Agnew referred to Mr. Walsh having joined the meeting in time for the telephone call to Mr. Alexander. Mr. Walsh's own evidence seems to support Mr. Agnew's. In his witness statement he said that when the question was first put to him, his recollection was that he needed to look at the contracts, and that there was a period of time before he got back to the meeting with the answer. In his evidence he was unclear when he got back to them, stating that it was either some time later that day or the next. Mr. Partridge was not clear in his evidence as to when Mr. Walsh's advice had been given, and did not recall whether he had been physically present in the office. Mr. Turner was also vague on the issue, so that at the end of the day the position is by no means clear. However, the three Mutual Group witnesses were quite unclear in their recollection, whereas Mr. Agnew was relatively positive, and I suspect that his version is the correct

one. But again, I draw no conclusions, adverse or otherwise, from the difference of view of these various witnesses.

200. Another minor area where the evidence of the American Patriot witnesses was not in complete agreement related to the circumstance under which American Patriot came to the view that it had been the victim of a fraud. Ms. Saran said that she had had a telephone conversation with Mr. Bossard, in which he had said that she needed to travel to Philadelphia, because he and Mr. Agnew had something to tell her. Ms. Saran recalled there having been a subsequent meeting, and the conversation having been between the three of them. Mr. Bossard referred in his witness statement to the disclosure of the fraud as having taken place in the telephone conversation, making no reference to a meeting in Philadelphia, or to Mr. Agnew. In cross-examination, Mr. Bossard said that after Ms. Saran had travelled to Philadelphia "it was just the two of us". For his part, Mr. Agnew made no reference to the meeting at all.

201. I mention this relatively minor conflict only as an indication of the extent to which recollections differ after a relatively long period.

202. Then there was the nature of the instruction said to have been given to them by Mr. Partridge at the Coverage Meeting. In his witness statement, Mr. Bossard had said "I was then instructed by Glenn (Partridge) to go back to Lysa (Saran) to falsely confirm that the Hendricks did have exposure above the Aggregate Attachment Point." Mr. Bossard was again taken back to what he had said in his evidence in the arbitration, which was:

> "We were instructed to float the idea by American Patriot from the standpoint that we might be able to secure excess reinsurance for about a million dollars to see how they would respond to the number".

Mr. Bossard's response when it was put to him that the latter was "not quite an instruction to lie" was that it was an instruction "to tell what I was told to tell".

203. Then there was the relatively minor matter of how long the meeting in Mr. Partridge's office had taken. When Mr. Bossard was first asked the question

in cross-examination, he said "No longer than an hour and a half max, maybe two. No longer than an hour and a half". When further questioned, Mr. Bossard said that the meeting "probably didn't go longer than an hour or an hour and a half". When asked which was correct, Mr. Bossard went with the latter figure, and he was then taken to his deposition in the Legion/John Hancock arbitration, when his answer to the same question had been "no more than a half hour".

204. When challenged as to the discrepancy, Mr. Bossard said, with reference to the meeting "How long it took, I do not specifically recall, looking at you right here this day".

205. The point is a relatively minor one, and I certainly would not criticise Mr. Bossard for being unable to recall the length of a meeting which had taken place many years before. But what this cross-examination does demonstrate, in my view, is that Mr. Bossard was perfectly prepared to give a clear answer to a question when in truth he could not recall the true position. The length of the meeting has no real significance. Mr. Bossard's responses do, for the reasons just given. They make this part of his evidence unreliable, and that inevitably leads to a concern that other parts of his evidence might be equally unreliable.

206. Another area of disagreement between Mr. Bossard and Mr. Agnew related to their view, at the time of the client meeting in Illinois and just thereafter, as to whether American Patriot/the Hendricks had exposure beyond the AAP. Mr. Bossard's position was that he knew that Mrs. Hendricks and Mr. Thomas were incorrect in their view that there was exposure above the AAP. However, when he was asked whether Mr. Agnew agreed with that view, he said that the two had discussed the matter on the trip back to Philadelphia and had "agreed to disagree at that time". Mr. Agnew was quite clear that he took the same view as did Mr. Bossard, saying that was the way he had always understood the Programme to work. When he was referred to Mr. Bossard's evidence that he, Mr. Agnew had been open-minded on the question, he said that he had been non-committal to the client, but that did not affect the

understanding which he had always had. And Mr. Agnew was then taken to Mr. Bossard's deposition in the arbitration, where the latter had indicated that Mr. Agnew had not been sure. Mr. Agnew said that he did not think that Mr. Bossard had it correct.

207. And finally, in relation to events at about the time of the Renewal Meeting, Mr. Bossard was asked as to what he had said on the issue of exposure at this meeting. In his witness statement, he had said that he had not said anything at the time. He was then referred to Ms. Saran's deposition, in which she had said that his response had been that Mrs. Hendricks had no exposure above the AAP. Mr. Bossard said that that was something that he had said to Ms. Saran, but that he had not said anything to Mrs. Hendricks in this regard. Mr. Bossard was then taken back to his evidence in the arbitration, when Mr. Bossard agreed that when Mrs. Hendrick had said that there might be exposure above the AAP, he had said "that's possible". And there is not just a conflict between Mr. Bossard and Ms. Saran here. Mrs. Hendricks said that both had got it wrong.

208. Then there was the question of Mr. Bossard being compensated for his evidence, and in this regard it is important to remember what Ms. Saran said in her deposition. Having referred to the meeting in Philadelphia, she was asked if she recalled anything else that Mr. Bossard or Mr. Agnew had told her, and her response was "that they were willing to come forward on American Patriot's behalf if they were compensated". In cross-examination, Ms. Saran had confirmed the accuracy of that, and had also said that that agreement to compensate was in writing, and was the reason they had sworn affidavits in previous proceedings. So that was evidence given for the plaintiffs. Mr. Bossard was referred to Ms. Saran's evidence that he had required compensation for coming forward, and said that she had her facts wrong. Mr. Bossard accepted that the affidavit which he had sworn in US proceedings was dated 9 April 2002, and he was then asked whether it was on 8 April 2002 that the Hendricks had made an investment in his business. He said that he did not know the exact date, but that it was some time in April, and confirmed that the amount of the investment was $400,000. Mr. Bossard

accepted the date when shown the cheque, but said that there was no connection at all between his swearing the affidavit and the receipt of the investment.

209. I find that answer inherently unlikely, and I prefer Ms. Saran's version of events, with regard to the basis upon which Mr. Bossard (and Mr. Agnew) were prepared to come forward, namely compensation.

210. Another matter of concern to me is the matter identified by the defendants in relation to Mr. Bossard's recollection of Mr. Alexander's involvement in the Coverage Meeting. In the deposition which Mr. Bossard gave in 2003, he made no reference at all to Mr. Alexander when describing the Coverage Meeting. Then he referred to what Mr. Agnew said to him after the meeting. When Mr. Agnew referred to giving information to Mr. Alexander, Mr. Bossard continued by saying "I'm sorry. I'm a little vague on this. At that point in time how Mr. Alexander got involved, I do not recall".

211. This recollection is very different from the version of events which Mr. Bossard gave in his witness statement of October 2006, when he referred to Mr. Alexander agreeing with the approach suggested by Mr. Partridge and later said "David was told exactly what was going on and his response to Glenn was "*let me know the number and that is fine, that's okay*." It seems unlikely that Mr. Bossard's recollection would have improved without someone having prompted him, and his explanation for the difference on the two occasions made little sense.

212. These various discrepancies may seem minor, but I find them troubling in the context of these serious fraud allegations, and I now turn to one which seems to me to be rather more serious, and that is the position in relation to where the proposed premium figure of $1 million came from.

213. In his witness statement, Mr. Bossard said "I worked out that $1 million would represent an appropriate premium". I had inferred from this statement that it was indeed Mr. Bossard who had first suggested that figure. I did so because he had referred in his witness statement to going down to the floor below to get the American Patriot file, carrying on to make the statement

which I have quoted above. He then said that "having done this methodology", he went back to Mr. Partridge's office and explained it to him, and "explained my rationale for coming up with this number". In his oral evidence, Mr. Bossard said that this was not the correct inference to be drawn, and that Mr. Partridge had come up with the $1 million number, and had then instructed Mr. Bossard to go back to confirm if the number would work.

214. Mr. Agnew, on the other hand, said in his witness statement that it was Mr. Bossard who had suggested "about a million dollars" in response to Mr. Partridge's question of "What do you think they would pay?" In cross-examination Mr. Agnew was asked whether he was sure that it was Mr. Bossard who had suggested the premium, and he responded that it was Mr. Bossard who had suggested that, and when he was referred to Mr. Bossard's evidence of the previous day to the effect that it was Mr. Partridge who had come up with the figure, said "I don't think he is correct", carrying on to say that Mr. Bossard was mistaken, because that was not the way he, Mr. Agnew , recalled it.

215. I do find Mr. Agnew's version of events inherently much more likely, given the terms of Mr. Bossard's own witness statement, and the fact that before his reference to having worked out that $1 million would represent an appropriate premium, Mr. Partridge had asked what Messrs. Agnew and Bossard thought "we can get them to pay for it?" So I am satisfied that in regard to this aspect of matters, Mr. Bossard's recollection is wrong, and I feel bound to go further and say that it seems to me that Mr. Bossard's evidence, to the effect that Mr. Partridge had come up with the number of $1 million, is unlikely to have been an error on his part. First, the error does not make sense, particularly when compared with his witness statement. It seems much more likely that Mr. Bossard put forward that version of events without any genuine recollection as to its truth. And no doubt in giving that evidence, Mr. Bossard would have been aware that the Court, if it accepted that evidence, would draw inferences adverse to Mr. Partridge. In short, this evidence was either an ill-conceived lie, or given with a reckless disregard for the truth. And neither Mr. Bossard

nor Mr. Agnew supported the pleaded case referred to in paragraph 26, that the number had been reached after consultation with Mr. Eaton.

216. The next evidence which I will address is Mr. Bossard's evidence as to what Mr. Walsh had said at the Coverage Meeting, referred to in paragraph 70 above. The starting point is Mr. Bossard's witness statement, and I have set out the relevant passage at the end of paragraph 60 above. As Mr. Smith said when putting the issue to Mr. Bossard, it was the additional wording attributed to Mr. Walsh, and those words only, which founded the allegation of fraud against him.

217. In my view it is quite clear that Mr. Bossard's answers to the very clear and quite careful questions put to him in relation to this aspect of matters in the Legion/John Hancock arbitration, both in his November 2003 deposition and his May 2004 evidence, can only mean that in relation to the issue of changing the agreement retroactively, Mr. Walsh's answer was quite simply "No", with nothing further said. Mr. Bossard confirmed in his evidence that what he had said in the deposition and his earlier evidence was correct when he gave it. It cannot have changed since, and he had no explanation for the inconsistency. Only one of the two versions can be true, and it is not credible that one version should represent the truth and the other be an error. This suggests that Mr. Bossard either lied in his testimony to the arbitration, or lied to the Court. Either one is extremely damaging to his credibility. But given Mr. Bossard's confirmation that his evidence in the arbitration was correct when he gave it, I would conclude that Mr. Bossard's evidence, in his witness statement and in cross-examination, that Mr. Walsh had added the further words is not the truth, and I so find. It is inconceivable to me that Mr. Bossard could have a better recollection of these matters in 2006 and 2010 than he did in 2003 and 2004, and as I have said, the questions in 2003 and 2004 could not possibly have left any room for confusion.

218. That necessarily takes me to Mr. Agnew's evidence on the same subject. Mr. Agnew used different and less detailed wording than Mr. Bossard did, although the words "change the amendment" are common. In any event, I am

satisfied that the evidence which Mr. Bossard gave in 2003 and 2004 was indeed correct, and in relation to Mr. Agnew's evidence I say no more than that he must have been in error in regard to that evidence, perhaps because, as I indicated in paragraph 45 above, if Mr. Bossard and Mr. Agnew had a mistaken understanding as to the workings of the Programme, for whatever reason, it would not be surprising that such understanding would, with the passage of time, colour their recollection of events.

219. There are, of course, differences in the evidence given by the witnesses for the defendants. But these are for the most part very minor, and I find nothing in relation to the evidence of the defendants' witnesses remotely comparable to the various differences which I have set out above in relation to the evidence given for the plaintiffs.

Credibility

220. Having dealt in some detail with the conflicts in the evidence on behalf of the plaintiffs, I will now deal with the general issue of credibility, and would start by making a general comment in relation to the demeanour of the witnesses. With the exception of Mr. Bossard, I found nothing in the demeanour of the witnesses which would lead me to conclude that one witness was telling the truth where another was lying. I should stress that, particularly in relation to the Coverage Meeting in Mr. Partridge's office, the version of the two sides cannot be reconciled. However, I found Mr. Bossard's demeanour to be combative and at times he was evasive; even in relation to what should have been uncontroversial matters, Mr. Bossard's approach was adversarial, such as where he was asked early in his cross-examination whether he had authority to sign for Mutual Indemnity. He seemed more interested in jousting with counsel than answering the question. But I am much more influenced by the inconsistencies between Mr. Bossard's and Mr. Agnew's evidence and, more particularly, the inconsistencies between Mr. Bossard's evidence at this trial, and that which he had given previously, notably in his deposition and evidence in the Mutual/John Hancock arbitration.

221. I would just make the comment at this point that arguably the first dishonourable, if not dishonest, acts were those of Messrs. Agnew and Bossard at the Renewal Meeting, when they believed that Mrs. Hendricks had misunderstood what they thought to be the true position, and yet did not say so, preferring to see if they could use that mistake to their advantage as leverage for the renewal of the Programme for the fourth year. Had they been honest in relation to their understanding at that time, the likelihood is that events would have unfolded very differently. I recognise of course that silence cannot establish the tort of deceit. Messrs. Agnew and Bossard are not accused of such. But silence was hardly the course an honourable man would have followed.

222. Next, I would refer to Mr. Bossard's emails of late March 2000, which were not referred to in his witness statement, and on which he was not cross-examined. In his email of 28 March 2000 to Ms. Saran, Mr. Bossard said:

> "On a positive note, we have a market that is interested in removing American Patriot from an excess aggregate exposure position in the prior years. The price should be in the range of $350k to $650k. There would be no limit to this protection."

There was no evidence from anyone, and certainly not from Mr. Eaton, who would no doubt have been the only person who could report on this matter, that there was ever a market interested in removing American Patriot from exposure in the range of $350,000 to $650,000.

223. And in Mr. Bossard's email to Ms. Saran of 31 March, he said:

> "Retro Buy Out – this is a firm quote from the reinsurers that participate on our aggregate excess layer".

There was no evidence that there was ever such a quote, and these communications from Mr. Bossard appear to have been fictitious, designed to encourage Ms. Saran to believe that the perceived problem for the first three Programme years was soluble, with a view to securing a commitment for the fourth Programme year.

224. Mr. Martin submitted that these emails were consistent with the plan agreed upon at the Coverage Meeting, and that the failure to cross-examine him on these emails suggests that Mr. Bossard had not made up the contents. But the reality is that the contents were not true, and there was no evidence to suggest that in writing them Mr. Bossard was acting on instructions from anyone else. I am bound to conclude that Mr. Bossard as the author of the emails was responsible for conveying false information to Ms. Saran.

Conclusion on Credibility

225. In summary, I am satisfied that there were many instances when Mr. Bossard did not tell the truth, and others where it seemed to me that he was not taking care to ensure that his answers represented the truth. In relation to other areas, Mr. Bossard may simply have "got it wrong". Whatever the reason, I am satisfied that Mr. Bossard's evidence is not reliable, and where it conflicts with the evidence given by the witnesses for the defendants, particularly in regard to the Coverage Meeting, I reject it. So far as Mr. Agnew is concerned, I recognise that in relation to him there were not the series of conflicts which existed in relation to Mr. Bossard's evidence. But again, the critical evidence covers the events of the Coverage Meeting, and I am quite satisfied that Mr. Agnew's evidence in relation to the events of this meeting is wrong. The starting point here is no doubt Mr. Walsh's evidence, and I should say that, quite apart from the fact that I found Mr. Walsh to be an impressive witness, I necessarily had to ask myself "why on earth would Mr. Walsh give the advice and make the statements Messrs. Bossard and Agnew attribute to him?" Such statements on his part would be comparable to the "motiveless dishonesty" referred to by Rix LJ in *The Kriti Palm* [2006] EWCA Civ 1601. Having seen and been impressed by Mr. Walsh, I cannot believe that he would have acted as alleged. And once I accept Mr. Walsh's evidence, as I do, I necessarily have to reject Mr. Agnew's, which, again, I do. I would add that the manner in which Mr. Agnew's recollection accorded with Mr. Bossard's – for instance, in relation to what was said by Mr. Walsh, suggests to me that the two must have discussed matters (as Mr. Bossard essentially admitted, though Mr. Agnew denied it), and for whatever reason Mr. Agnew has tailored his

evidence so as to match that given by Mr. Bossard. The witness statements of the two were given on the same day back in October 2006, after they had travelled to Bermuda together. So I must make it clear that I do not accept that Mr. Agnew's evidence as to the events of the Coverage Meeting is the truth. By the same token, I do accept the evidence in relation to that meeting given by the four witnesses for the defendants, Mr. Partridge, Mr. Turner, Mr. Walsh and Mr. Alexander.

The Failure to Advise That No Reinsurance Had Been Purchased

226. A number of the defendants' witnesses were cross-examined in relation to this issue, and the Court was invited to draw adverse inferences, particularly in relation to Mr. Alexander. It was suggested that the failure to notify American Patriot/the Hendricks that no such reinsurance had in fact been procured supported the pleaded case (see paragraph 27 above) that there was never any intention to purchase the reinsurance in question, but rather an intention to charge premiums to the Hendricks without providing such reinsurance cover.

227. Certainly, there came a stage long after it was known to the Mutual Group witnesses that it had not proved possible to secure reinsurance, that that fact was not communicated to American Patriot/the Hendricks. For instance, when Mr. Bjornson sent his letter to Ms. Saran on 4 February 2002 seeking the additional "premium" said to be due to Mutual Indemnity of $520,000, one would have thought it appropriate to make mention of the fact that no such reinsurance had been obtained, so that the use of the word "premium" was misleading for the circumstance then existing, of self-insurance on Mutual Indemnity's part. But this was of course long after the events of the Coverage Meeting, and I find communications closer to the date of the Coverage Meeting to be more telling when considering the plaintiffs' conspiracy theory. Notable is the email which Mr. Alexander sent to various Mutual Group personnel, including Mr. Agnew, when the provisional premiums of $480,000 had been received. He asked the question "where do we stand on the reinsurance placement?" As Mr. Smith submitted, it would be "beyond Machiavellian" to suggest that Mr. Alexander wrote such an email if

there had genuinely been no intention to buy reinsurance. And it is also to be noted that the $480,000 was held by Mutual Indemnity as a payable, as Mr. Alexander indicated in his witness statement, on the basis that he believed initially that these monies would eventually be paid to a third party to purchase reinsurance.

228. In their closing submissions, the plaintiffs stated that Mr. Alexander's explanations were "simply dishonest". For the avoidance of doubt, I reject that characterisation, and I should make it clear that I accept Mr. Alexander's evidence in relation to the proposed purchase of reinsurance and Mutual Indemnity's treatment of the premium. Similar allegations of dishonestly were made in relation to Mr. Alexander's drafting of amendment number 5 to the Shareholder Agreement, and I have dealt with those below.

Finding on the Issue of Fraud

229. I do, therefore, find that the fraud in relation to the Coverage Meeting has not been proved, and I find that the position of Messrs. Partridge and Turner, and, to the extent that they were involved, Messrs. Walsh and Alexander, was that all of them believed that American Patriot/the Hendricks did have a liability beyond the third layer. I reject the case for the plaintiffs that those gentlemen, or any of them, had no such belief, and were seeking to charge a dishonest premium to relieve American Patriot/the Hendricks from exposure where none existed. There are two aspects of this finding on which I should make further comment. The first of these is in relation to the shifting emphasis which Mr. Smith for the defendants complained had the effect of changing the allegation of fraud, such that the case had not been properly put to the defendants' witnesses.

230. The basis for the changing nature of the alleged fraud was the shift in emphasis from the existence of exposure above the AAP to the extent of such exposure, and particularly whether that exposure was limited (as it no doubt would have been had the exposure properly depended upon the application of treaty 103 and clause 3A) or unlimited, as some of the later documents suggested. Mr. Martin sought to place reliance upon these documents in

relation to the establishment of the fraud. I suggested to him during the course of argument that I necessarily had to start by making findings as to what had been said at the Coverage Meeting. I do accept that the nature of the alleged fraud has to be looked at in the context of the pleaded case, and the pleaded case for the plaintiffs is predicated upon the advice said to have been given by Mr. Walsh at the Coverage Meeting, that losses in excess of the AAP were not obligations reinsured by Mutual Indemnity, and hence did not give rise to indemnification obligations on the part of American Patriot/the Hendricks under the Shareholder Agreement. So at least in theory, the case was always put on the basis that Messrs. Partridge, Turner, Walsh and Alexander resolved to take advantage of the Hendricks' lack of knowledge and understanding of the reinsurance obligations of Mutual Indemnity by telling them that they were responsible for losses "up to Legion's/Villanova's policy limits" pursuant to the Shareholder Agreement.

231. So in reality, I am not sure that the shift in emphasis of which Mr. Smith complained is real. But I do still think that it is necessary for me to consider how the Mutual Group personnel viewed matters at the Coverage Meeting, and here I go back to my summary of the relevant evidence. Mr. Partridge had said that there had been no discussion in relation to unlimited exposure, as opposed to the $5 million representing the fourth layer, and referred to the fact that the focus had been more on liability than on limit (see paragraphs 114 and 115 above). Mr. Turner said that at the meeting he was not focusing on the extent of the exposure if losses went into the next layer, so much as to where the exposure lay (paragraph 133 above). Mr. Walsh's evidence was directed to the advice which he said that he had given, which was that the exposure of the Hendricks above the AAP was based on Mutual Indemnity's exposure. Mr. Alexander does not appear to have participated in that part of the conversation.

232. So, for the avoidance of doubt, I should make it clear that I reject the allegation that the defendants' witnesses conspired to defraud the Hendricks in relation to unlimited exposure above the AAP. I recognise that there are various subsequent documents which suggest, directly or indirectly, that the

Hendricks had unlimited exposure. First is the letter of 20 April 2000, which uses the words "for any losses" that exceed the AAP. Similar language, not surprisingly, found its way into amendment number 5 to the Shareholder Agreement.

233. Mr. Martin submitted that the answer which Mrs. Hendricks had received following the Renewal Meeting was that she had unlimited exposure, and this message was said to have come from Mr. Bossard to Ms. Saran, who relayed it to Mrs. Hendricks. In fact, Ms. Saran declined to answer the question as to the nature of the communication that she had received from Mr. Bossard on purported privilege grounds. Mr. Bossard's witness statement simply referred to going back to Ms. Saran, in accordance with Mr. Partridge's instructions, to say that the Hendricks did have exposure above the AAP; his witness statement does not indicate whether that liability was fixed or unlimited, and the issue was not clarified in cross-examination. As for Mrs. Hendricks, she had certainly expressed a concern that she might have unlimited exposure at the Renewal Meeting, and in relation to the information said to have been passed by Messrs. Bossard and Agnew to Ms. Saran, Mrs. Hendricks' evidence on this issue is somewhat confusing, but she did indicate that Ms. Saran had called her and said "there is exposure there", without indicating the extent of that exposure.

234. So I do find that there is no evidence to support the contention that American Patriot and/or Mrs. Hendricks were advised following the Renewal Meeting (and after the Coverage Meeting) that their/her exposure was unlimited. The evidence for the defendants seems to be consistent with that for the plaintiffs, namely that their concern was in regard to the existence of exposure, rather than the extent of it. And of course the message passed via Ms. Saran to Mrs. Hendricks in relation to the existence of exposure was consistent with the conclusion of the Mutual Group personnel reached at the Coverage Meeting.

The Burden of Proof in Fraud

235. Having made that finding, I should clarify how I approached the issue of the burden of proof. Mr. Martin relied upon the case of *Equitas Limited v R & Q*

Reinsurance Co. (UK) Limited [2009] EWHC 2787 (Comm) for the proposition that once an asserting party discharges the burden of advancing a prima facie case, the burden shifts to the opposing party to show that the asserting party's positive case is incorrect as a matter of fact. Mr. Smith relied upon the traditional authorities as to the extent of the burden of proof in cases of fraud, with particular reference to the issue of the balance of probability standard. He referred to a passage in the judgment of Lord Nicholls in *H (Minors), Re* [1996] AC 563, which is set out in paragraph 6-55 of the 17th edition of Phipson on Evidence. I will not repeat that paragraph, since I think practitioners are well familiar with it, but I will set out the last sentence, which is in the following terms; "The more improbable the event, the stronger must be the evidence that it did occur before, on the balance of probability, its occurrence will be established". That was the test for the burden of proof which I applied in reaching my conclusion above. However, I would add this; if I were to be wrong in applying that standard, and Mr. Martin were to be correct in regard to the need to apply the standard referred to in the *Equitas* case, then I would hold that the alleged fraud would still not have been made out. My view is that the plaintiffs have failed to establish even a prima facie case in relation to the alleged fraud. But I do not think that the *Equitas* case affects what was said by Lord Nicholls in *H (Minors), Re*.

Fraudulent Misrepresentation

236. There is an alternative plea of fraudulent and/or negligent misrepresentation, based first on Mr. Bossard's email to Ms. Saran of 28 March 2000, then on Mr. Alexander's letter of 20 April 2000, and lastly upon Mr. Bjornson's letter of 4 February 2002, seeking the additional premium of $520,000. Mr. Smith referred to the claims for fraudulent misrepresentation as being "a different legal label" for the same allegations of fraud.

237. There is no question but that Mr. Bossard's email was both false and misleading, as indeed was the subsequent email of 31 March 2000, to which I referred to in paragraphs 222 and 223 above. But Mr. Bossard was an employee of Legion, and there is no evidence to suggest that in sending these

emails he was acting on behalf of any of the defendants. I will come back to the issue of agency and the inter-relationship of the companies within the Mutual Group.

238. In relation to Mr. Alexander's letter of 20 April 2000, it is pleaded that the facts set out in this letter were false and misleading in that:

(i) no additional reinsurance had in fact been purchased;

(ii) no additional reinsurance was in fact necessary; and

(iii) no amendment to the Shareholder Agreement was necessary

239. First, the April 2000 letter did not say that the additional reinsurance had been purchased; it simply said that Mutual Indemnity had agreed to purchase reinsurance to limit American Patriot's obligations for the first three Programme years. Later in the letter reference was made to the reinsurance "to be purchased" by Mutual Indemnity. There is nothing to this point. In relation to the allegations that the additional reinsurance was not necessary and that no amendment to the Shareholder Agreement was necessary, this does go back, as Mr. Smith submitted, to the principal allegation of fraud. Given the finding that I have made in relation to the alleged fraud, I agree that these last two allegations of misrepresentation fall with the allegation of fraud, and I so find.

240. I should at this point make reference to Mr. Bjornson's calculations in regard to the second instalment of premium, on which Mr. Alexander was cross-examined. It was suggested that this letter demonstrated the earlier fraud. Mr. Bjornson had first sent an email to Mr. Agnew on 29 October 2001, copied to Mr. Alexander, when he calculated the two aggregates above the $3 million threshold to be only $1,624,251, which gave a provisional premium of $259,880, less than the premium of $480,000 which had already been billed to American Patriot. Then, on 4 February 2002, Mr. Bjornson had written to Ms. Saran, indicating that the loss penetration above the total aggregate was then $4,139,437, and seeking the further premium of $520,000.

241. Mr. Alexander had accepted in cross-examination that Mr. Bjornson's numbers appeared to be wrong, and did not appear to be in accordance with the formula set out in the April 2000 letter. Mr. Alexander did not recall whether he had seen Mr. Bjornson's letter before it had been sent. He did accept, however, that the correct figure was likely to be less than the $480,000 premium which had already been charged and paid, and that even on an alternative basis of calculation, the maximum premium would not have exceeded $662,000 in total.

242. So the evidence is clearly that Mr. Bjornson's figures were wrong, and that the additional premium charged of $520,000 was charged in error. However, the case for the plaintiffs was that the figure was made up, and is a further indication of the fraudulent scheme. I reject that characterisation, and find that while the calculation of the premium was in error, as Mr. Alexander's evidence indicates, the issue is academic now that the defendants accept that the full amount of the premium is due to American Patriot/the Hendricks, or at least is to be applied for set off purposes. Even if I were wrong in that view, there is nothing to link Mr. Alexander to Mr. Bjornson's error, on the basis that there was no evidence that he had seen the letter before it had been sent out. So there can be no question of the letter operating so as to draw in Mr. Alexander to the alleged fraudulent conspiracy.

Negligent Misrepresentation

243. In fact, Mr. Martin drew a distinction between negligent misrepresentation and negligent misstatement, saying that strictly the former was relevant only in respect of assessment of damages. As I understand his position, he relies in relation to negligent misrepresentation upon the matters raised under the heading of fraudulent misrepresentation, on the basis that the damages claimed in the tortious claim for deceit or fraudulent misrepresentation apply in the event that it is established that the misrepresentation was negligent rather than fraudulent. Hence my finding that there was no fraudulent misrepresentation means that the claim by way of negligent misrepresentation

fails, if there is a lack of misrepresentation. I hold that there was no misrepresentation, so that the claim under this heading fails.

Negligent Misstatement

244. The position in relation to negligent misstatement, as I understand it, turns on a different factual scenario, and a claim is made on the basis of the representations said to have been made by Mr. Partridge, Mr. Turner and Mr. Alexander in relation to the exposure under the Shareholder Agreement, which representations are said to have been negligent.

245. I have referred in paragraphs 232 and 233 above to the somewhat unclear circumstances in which the representation was communicated to Mrs. Hendricks, but there is no doubt that Messrs. Partridge and Turner intended the representation to be so communicated, and Mr. Alexander's April 2000 letter was predicated on the basis that American Patriot and/or the Hendricks had exposure at the fourth layer. That exposure was of course (on the case for the defendants) based upon the advice which Mr. Walsh had given. I pause to note that treaty 103 is to be construed according to the laws of Pennsylvania, and no doubt the same is true in respect of amendment number 5, by virtue of which clause 3A was added to the treaty. There is no expert evidence as to Pennsylvania law, although obviously Mr. Walsh was qualified to opine on matters of Pennsylvania law. His evidence was that having reviewed the relevant documents, he had formed the view that Mutual Indemnity was liable for the fourth layer of losses, and that the Hendricks were liable under the Shareholder Agreement to indemnify Mutual Indemnity in respect of losses in the fourth layer. Subject to one issue to which I will now come, I would see no reason to dissent from that view. But that one issue relates to the construction of the Shareholder Agreement, which is of course an agreement to be construed as a matter of Bermuda law.

Exposure above the AAP

246. For the defendants it was put that this issue had relevance in two respects; first, it could have a bearing on the factual assessment as to the advice given by Mr. Walsh, and secondly, it is submitted that if there was exposure above

the AAP, then American Patriot/the Hendricks suffered no loss and cannot claim in tort.

247. In relation to the first matter, I have no doubt in relation to the nature of the advice given by Mr. Walsh, and have already made my finding in that regard. In relation to the second question, I bear in mind the effect of the Commutation Agreement, and the fact that, as Mr. Alexander said in his witness statement, the settlement sum represented in the Commutation Agreement was calculated by reference to Gap losses, and any losses above the AAP were effectively excluded.

248. In these circumstances, it does not seem to me to be appropriate to go into this aspect of matters in detail. Suffice it to say that I would agree with the view expressed by Mr. Walsh at the Coverage Meeting.

The Corporate Law Issues

249. These can essentially be broken down into two broad areas. The first relates to the failure on the part of Mutual Holdings to issue the preferred share to either American Patriot or the Hendricks, and the second relates to the entire structure of the various IPC programmes operated by the companies within the Mutual Group. This latter is not dependent upon any factual situation, but is rather aimed at the concept, and in particular the basis upon which dividends are declared in a particular programme, if an underwriting profit is realised on that programme. I will deal with this latter argument first, because it does seem to me to be a relatively straightforward issue to which there is a relatively straightforward answer.

250. Mr. Martin did refer to various factual matters in relation to his argument on this point, including the fact that capital contributions made to Mutual Holdings by preferred shareholders had been contributed to Mutual Indemnity and then pooled within Mutual Indemnity; similarly, premium received by Mutual Indemnity was also pooled. Finally, Mr. Martin referred to the fact that dividends to be paid to preferred shareholders of Mutual Holdings were not in fact dividended up by Mutual Indemnity to Mutual Holdings and declared as dividend by the latter, but instead were distributed directly by

Mutual Indemnity to Mutual Holding's preferred shareholders. None of that seems to me to be relevant to the conceptual argument that it was not legally possible in the light of the legal principles applicable to declaration of dividend from profit for Mutual Indemnity and Mutual Holdings to comply with the relevant legal requirements.

251. It seems to me that the argument put forward for the plaintiffs depends upon the notion that Mutual Indemnity made underwriting profits on some programmes and sustained losses on others. This goes back to a point made by Mr. Alexander in his evidence (paragraph 169) that while Mutual Indemnity could suffer an underwriting loss, the effect of the indemnification provisions was that it did not ultimately suffer a loss on the particular programme which had made an underwriting loss. There was of course no evidence as to which programmes were profitable and which were not in any particular year, but the theory of the scheme was that Mutual Indemnity would not suffer a loss by reason of the collateralisation arrangements. No doubt there would be cases when Mutual Indemnity experienced difficulties in realising its security, but the attack is a theoretical one, not dependent on a particular factual background, and it does not seem to me to have been made out. The scheme was designed such that Mutual Indemnity would declare a dividend to its shareholder Mutual Holdings in respect of the profits made on profitable programmes; Mutual Holdings would then similarly declare dividends to its preferred shareholders in accordance with the formula contained in the various shareholder agreements. As Mr. Smith submitted, there was not one global scheme, but a number of separate ones. And losses did not form part of the calculation of profit, using that term as being referable to IPC clients as a group. If there were to be a loss because of difficulties experienced by Mutual Indemnity in realising its collateral, that was Mutual Indemnity's loss, which it had to make good. It was not a loss for the preferred shareholders, the IPC clients.

252. The other argument in relation to the corporate law issues depends on a number of facts which are not in dispute, and which I now set out.

253. At the statutory meeting of members of Mutual Holdings held on 25 May 1993, an increase in the company's authorised share capital was authorised, and the increased value of $11,998,000 was classified as non-voting, non-convertible redeemable preference stock. No par value for the additional share capital was specified, and the meeting authorised the board to establish the par value of the shares to be issued from time to time. That appears to be as far as matters went, at least until 13 May 2010, when attempts were made by Mutual Holdings to remedy the position.

254. So Mutual Holdings failed to create the C30 preferred share, or to issue or allot that share, and failed to enter the names of American Patriot or Mr. and Mrs. Hendricks on the share register. Those deficiencies led to a plea that the consideration for the indemnification obligation contained in the Shareholder Agreement and its amendment had wholly failed, and it was pleaded that the Shareholder Agreement was void, although the pleading was not clear whether this was based upon the failure to issue shares, or the argument as to the failure of the structure, to which I have already referred.

255. The written submissions for the plaintiffs at times seemed to confuse the failure to issue the preferred share and the alleged failure of the concept of the structure, and in this regard complaint is made as to the failure on the part of Mutual Indemnity to follow the structure, and make distributions of underwriting profit directly to the IPC clients whose programmes were profitable. I do not see that that has any relevance in relation to the American Patriot Programme, where there was never an underwriting profit which might have led to a declaration of dividend. Neither do I see that I should be concerned with failures to implement the scheme as planned in respect of other programmes. In their submissions as to the effect of the shareholder and board resolutions of Mutual Holdings of 13 May 2010, the plaintiffs referred to the problem as being a greater one than the failure to comply with the statutory formality for the creation of the relevant classes of share, and say that the problem stems from the manner in which money actually flowed from Mutual Indemnity to the Mutual Holdings' preferred shareholders, adding that Mutual Holdings and Mutual Indemnity are not now capable of putting the

clock back and rectifying the maladministration of the scheme. I do not see that such failures have any relevance when considering the position of the C30 preferred share which should have been issued to American Patriot and, later, the Hendricks; the flow of money on other programmes does not seem to me to have any relevance to this issue, and it seems to me that the point is a relatively narrow one, and is whether the resolutions of 13 May 2010 succeed in correcting the past failures in relation to the issue of the preferred share.

256. And it is important to remember that there was no complaint ever made by American Patriot or the Hendricks in relation to the failure to issue the preferred share. This was an issue which was only focused on in the context of these proceedings, and even then very late in the day. In relation to consideration, the analysis given by the defendants in their closing submissions seems to me to be valid; obviously the preferred share had to be issued before American Patriot/the Hendricks could purchase it, but I see nothing in the Shareholder Agreement which would have prevented Mutual Holdings from issuing and allotting the preferred share whenever American Patriot (or later, the Hendricks) proferred the agreed purchase monies of $1,000. The provision in the Shareholder Agreement referred to redemption "on" the redemption date, but that must mean "on or after"; the notion that redemption could only occur on one particular day is not commercially sensible. In the event, that was not done, and it seems to me an extraordinary proposition that in those circumstances American Patriot/the Hendricks should now be able to make complaint of the failure to issue the preferred share so as to avoid a liability of more than $8 million.

257. There was an argument made in submissions that the passing of the redemption date meant that the share could not now be issued. But all that the redemption provisions did was to provide a date at which Mutual Holdings was obliged under the terms of the agreement to repurchase the preferred share, upon presentation of the share certificate duly endorsed for cancellation. That did not happen either, which means no more than that there was no repurchase, and hence no obligation to cancel the preferred share.

That must, surely, have left Mutual Holdings in a position to issue the preferred share should it so choose.

258. Against that background, let me turn to the terms of the two resolutions. First, the directors' resolution starts with recitals in relation to the increase in the authorised share capital of Mutual Holdings, and the par value of the shares represented by the increase in capital. In fact, part of the plaintiffs' complaint is that Mutual Holdings did not fix the amount of the new shares, said to be in breach of section 45 (1) of the Companies Act 1981. The resolution seems to have been drafted on the basis that the new shares were designated with a par value of $1,000 each. Next, there are resolutions ratifying the authority to issue, so the point seems to have been dealt with there. Next, the execution of the Shareholder Agreement is authorised and approved, and next, the resolution approves the designation of the C30 preference share. The resolution then deals with the allotment and issue of that share, first in relation to American Patriot and then in relation to the Hendricks, and finally, the resolutions cover confirmation of the directors' past acts.

259. In relation to the resolutions passed by Mutual Holdings' sole member, MRM Holdings, the same or corresponding issues are covered.

260. In my view, the resolutions of 13 May 2010 do operate to correct the previous defects in relation to the C30 preferred share, and I so find.

Estoppel by Convention

261. Were I to be wrong in relation to the pure corporate law issues, the defendants submit that the plaintiffs are estopped by reason of the fact that both parties to the Shareholder Agreement have conducted their business on the common assumption that it was effective, and have further operated as if American Patriot and the Hendricks were the holders of the C30 preferred share, notwithstanding that the $1,000 had not been paid and the share itself had not been issued.

262. The defendants relied upon a passage for the judgment of Lord Steyn in the case of *The Indian Endurance* [1998] AC 878 at 913, in the following terms:

> "A general review of the requirement of these estoppels is not necessary. It is settled that an estoppel by convention may arise where parties to a transaction act on an assumed state of facts or law, the assumption being either shared by them both or made by one and acquiesced in by the other. The effect of an estoppel by convention is to preclude a party from denying the assumed facts or law if it would be unjust to allow him to go back on the assumption."

263. I have already referred to the fact that in my view it would be extraordinary if American Patriot/the Hendricks were now to be able to avoid their substantial liability on the basis of a failure to issue the requisite preferred share. There is no doubt in my mind that it would be monstrously unjust to allow American Patriot/the Hendricks to go back on the common assumption of the parties that they were indeed the allottee of the preferred share.

264. The defendants concede that there is an argument as to whether an estoppel by convention as to the legal effect of an agreement can replace the requirement of consideration. I have found below that valid consideration was provided for the Shareholder Agreement. If I were wrong in that regard, the defendants accept that the failure cannot be remedied by an estoppel – see *Johnson v Gore Wood & Co.* [2002] 2 AC 1.

265. In the alternative, the defendants rely upon an estoppel by representation, that representation being that the plaintiffs did not require the issue of the preferred share to them, by reason of their not have proferred payment, while proceeding with the operation of the Programme. Alternatively, it is said that the plaintiffs acquiesced in the non-issue of the share, which has the same effect. It seems to me that the representation and acquiescence are very close to the common assumption of the parties, but had it been necessary for me to find on the basis on estoppel by representation, as opposed to estoppel by convention, I would have done so.

Primary Conclusion on the Plaintiffs' Case

266. To summarise the findings set out above, I find that the plaintiffs have failed on their primary case of fraud, fraudulent or negligent misrepresentation, and

negligent misstatement. I also find that the plaintiffs have failed in their case on the corporate law issues, both on the law and on the facts, and in relation to the factual issues, I find against the plaintiffs on the alternative ground of estoppel.

Mutual Holdings' Claim

267. The claim which is now put forward on behalf of Mutual Holdings is that which appears from Mr. Alexander's witness statement, to which I have referred in paragraph 165, namely $3,419,361.

Construction of the Shareholder Agreement

268. The first issue which needs to be resolved here is not one which Mr. Walsh would have considered when he was asked to opine at the Coverage Meeting as to the exposure of American Patriot/the Hendricks above the AAP and third party reinsurance, and turns on the argument for the defendants in relation to the meaning of the indemnification provision contained in the Shareholder Agreement. The indemnification covers Mutual Indemnity's underwriting loss, calculated in accordance with the formula set out in the Shareholder Agreement. That agreement makes no reference to the Gap, the AAP, or losses incurred at the fourth layer pursuant to the operation of clause 3A of treaty 103. The plaintiffs' case is that they were not aware of the treaty, and more particularly clause 3A, and so were unaware of their exposure at the fourth layer.

269. What troubles me in relation to this aspect of matters is that the evidence confirmed that neither American Patriot nor Mrs. Hendricks in fact saw the treaty, and so would indeed have been ignorant of its terms.

270. Mr. Martin relied upon the proposal documents, and during the course of argument I indicated my concern at such reliance, but I should nevertheless refer to them. First was a letter dated 18 February 1997 from Mr. McPherson, to which I have referred in paragraph 44 above. That letter was apparently based upon the use of a captive insurance company, but Mr. Agnew sent out a proposal letter on 24 March 1997, which essentially set out the basis on which

the Programme would operate. That letter made no reference to the fourth layer of cover, reinsured by Mutual Indemnity, which was hardly surprising given Mr. Agnew's evidence that he was unaware of it. The proposal was the subject of changes by Ms. Saran, and the proposal appears, following amendment, to have been signed by Mr. Agnew and Mr. Siko on behalf of Commonwealth, and Ms. Saran on behalf of American Patriot. So on the face of matters, if the accepted proposal did constitute a contract, it was not one to which Mutual Holdings or Mutual Indemnity was a party, in the absence of an agency being established.

271. But there can be no doubt but that any agreement reached on the basis of the proposal documentation was intended to be, and was, subsumed into the Shareholder Agreement and its related documents. These included the underlying insurance policies issued to the customers of American Patriot's related business, and the treaty between Legion and Mutual Indemnity, which referred to their having entered into "one or more" reinsurance agreements. The Shareholder Agreement contained a recital referring to the agreement, the policies and the treaty being a "uniquely negotiated single contract".

272. The pleading for the plaintiffs makes reference to the role of Commonwealth, in terms of it acting as agent on behalf of MRM and/or Legion and/or Mutual Indemnity in relation to the marketing and sale of the Programme. It continues to plead that the representations and statements made to American Patriot and the Hendricks were made as their agents. But while Mr. Agnew did refer to his understanding as to how the Programme was marketed and sold, any representation as to the extent of Mutual Indemnity's reinsurance of Legion can only be found in the letter of 24 March 1997.

273. The pleaded case for the plaintiffs does not seek rectification of the Shareholder Agreement on the basis that it was the intention of the parties that the indemnification obligation was to be limited to losses below the AAP. I confess that I do not find that the position as clear as I would wish, but I have come to the conclusion that since the Shareholder Agreement calls for indemnification in respect of Mutual Indemnity's underwriting losses, and the

agreement itself refers to "one or more" reinsurance agreements, the position must be that underwriting losses include those sustained by reason of the effect of clause 3A of treaty 103.

274. That said, it does seem to me that the issue is an academic one. At the end of the day, the effect of the Commutation Agreement was to exclude losses in the fourth layer. Mr. Alexander's witness statement set out a table showing that all the commuted losses were below the AAP. Hence there is no claim for losses in the fourth layer occasioned by the application of clause 3A. Had American Patriot or the Hendricks been responsible for losses in the fourth layer, then there might have been an unjust result caused by my findings. But in the end that has not happened, so that the losses incurred on the Programme, and now represented by the terms of the Commutation Agreement are losses which American Patriot and/or the Hendricks are liable for, and always understood they would be liable for.

Consideration

275. This issue was raised by the plaintiffs in their opening submissions, with reference to the relationship between the Mutual Indemnity and the Hendricks. I am not sure that the point was pressed in closing, but for the defendants, the issue was addressed from the perspective of Mutual Holdings. I think it is sufficient for me to say that there clearly was consideration furnished by Mutual Holdings in relation to the Shareholder Agreement which it seeks to enforce.

The Commutation Agreement as an Aid to Construction

276. This is no doubt an appropriate point at which to deal with the pleading based upon the position successfully taken by MRM on behalf of Mutual Indemnity in its negotiations with Legion's rehabilitator. The pleading maintains that clause 3A of the reinsurance agreement did not bind Mutual Indemnity, and relies upon the Commutation Agreement. The first problem that I have with that argument is the notion that a position taken three years after the event can be relevant when considering the state of mind of the Mutual Group personnel at the Coverage Meeting. And it is important to bear in mind that the effect of

the Commutation Agreement was to take away any liability in the fourth layer from American Patriot and/or the Hendricks. It is for this reason that the $1 million in premium paid for the purpose of relieving American Patriot/the Hendricks from liability above the AAP (whether by the purchase of reinsurance, the original concept, or by Mutual Indemnity itself taking the risk, as the Mutual Group defendants say they did when reinsurance could not be purchased) is now said to be held for the benefit of American Patriot/the Hendricks, and retained by way of set off. Because of this concession, it does not fall to me to construe the effect of clause 3A, but had it been necessary for me to do so, I would have ignored the effect of the Commutation Agreement by reference to the first of the principles of interpretation set out by Lord Hoffman in his judgment in the *Investors Compensation Scheme* case [1998] 1WLR 896, where he referred to the meaning which the document in question would convey "to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were **at the time of the contract**" (emphasis added). I bear in mind here Mr. Walsh's evidence that if he had been involved in the commutation negotiations on behalf of Legion, he would have disagreed with the position taken by Mutual Indemnity. Similarly, Mr. Mulderig had said in his witness statement that prior to the negotiations, he would have taken the position, if asked, that the IPC client was liable for insurance losses above the AAP not covered by third party reinsurance.

Estoppel by Record

277. This is no doubt also an appropriate point at which to deal with Mr. Martin's argument that the judgment of the Commonwealth Court of Pennsylvania in relation to the Commutation Agreement establishes an estoppel by record, on the basis that it is a foreign judgment *in rem*. Mr. Martin referred to a list of judgments which could properly by characterised as being judgments *in rem*, appearing in paragraph 43-14 of the 17th edition of Phipson on Evidence, and although he accepted that an order in a US Chapter 11 bankruptcy was not expressly referred to, he submitted that it was *ejusdem generis*, and therefore should be seen as similarly determinative of the state of the thing.

278. I can quite see that an order for the bankruptcy of a person or the liquidation of a company might properly be characterised as a judgment *in rem*, but that is not at all what this order of the Commonwealth Court of Pennsylvania is about. It is no more than an order of the Pennsylvania court which approves the terms of the Commutation Agreement, and authorises Legion's rehabilitator to take all appropriate action to perform the agreement. It is, if you will, the Pennsylvania court blessing the agreement reached by the parties, and it is not an adjudication of any type, much less an adjudication such as to constitute a judgment *in rem*. In my view there is nothing extra-territorial about the order of the Pennsylvania court, and I do not think that it can properly be taken into account for the purpose of construing the effect of clause 3A to treaty 103. I so find.

Transfer of Risk

279. I mention this subject, because Mr. Martin put to a number of the Mutual Group witnesses that the purpose of clause 3A being (as those witnesses had said) a result of a regulatory requirement to transfer risk to Mutual Indemnity, such requirement was not met if the Shareholder Agreement transferred the risk to the IPC client, rather than leaving it with Mutual Indemnity. Hence it was suggested that the purpose of clause 3A was to leave the risk with Mutual Indemnity, and not pass it on to the IPC client.

280. The first point to be made here is that there is no evidence for the plaintiffs to support the contention that Mr. Martin was putting to the defendants' witnesses. The second point is that the proposition was in any event rejected, and the defendants' witnesses (notably Mr. Turner and Mr. Walsh) said that Mr. Martin was confusing assumption of risk with retention of risk. So I do not think that the transfer of risk issue has any relevance for the purposes of this case.

The Effect of Amendment Number 5 to the Shareholder Agreement

281. A considerable amount of time was spent, particularly in relation to the cross-examination of Mr. Alexander, as to the effect of amendment number 5 to the Shareholder Agreement. As I have indicated, Mr. Alexander accepted that the

drafting, which he had undertaken without the benefit of legal advice, did not achieve the purpose for which it had been intended. Part of the reason for that was that Mr. Alexander's drafting was based upon the April 2000 letter, which itself was confusing in relation to the extent of losses covered. But amendment number 5 compounded the problem by purporting to create an obligation to indemnify Legion and/or Villanova, rather than Mutual Indemnity.

282. The plaintiffs contend that Mr. Alexander's explanations in relation to the preparation of amendment number 5 are not to be believed, and the substitution of Legion/Villanova for Mutual Indemnity was described in their written submissions as being "obviously fraudulent". I should no doubt have referred to amendment number 5 in relation to my finding on the fraud, because the case for the plaintiffs is that the amendment represents clear documentary evidence of the carrying into effect of the fraudulent scheme discussed and agreed at "the Coverage Meeting."

283. I reject that characterisation. I am quite satisfied that the drafting inadequacies of amendment number 5 to the Shareholder Agreement were indeed genuine errors, and not part of the theory of fraudulent conspiracy which I have already rejected. Whereas the Shareholder Agreement referred to there being an obligation to indemnity both Mutual Holdings and Mutual Indemnity, amendment number 5 referred to Mutual Holdings and/or "INSURANCE COMPANY", which while not defined was clearly a reference to Legion/Villanova.

284. But that could never have been the intention of the parties, for the reasons identified by Mr. Smith in his closing submissions. The reality is that both sides were operating on the basis that:

- American Patriot/the Hendricks were exposed to losses in the fourth layer, by reason of the operation of clause 3A of treaty 103.

- For the first three Programme years, Mutual Indemnity had agreed to seek reinsurance protection for American Patriot/the Hendricks for an agreed premium of $1 million.

- In the event, when reinsurance could not be procured, Mutual Indemnity regarded itself as effectively self-insuring the risk, in recognition of the agreement to relieve American Patriot/the Hendricks of exposure in the fourth layer for the first three Programme years.

I am satisfied that that was the common intention of the parties, so that amendment number 5 does have to be construed with a view to achieving that result. It was not intended (despite the bad drafting) to provide for unlimited exposure to American Patriot/the Hendricks, because that would have involved indemnifying Legion for its losses above the fourth layer, and there is no question but that the obligation of American Patriot/the Hendricks under the Shareholder Agreement was to indemnify Mutual Indemnity's underwriting losses, and not those of Legion.

Whether Liability (if Established) Attaches to American Patriot

285. In describing issues of liability in relation to exposure above the AAP, I have referred to both American Patriot and the Hendricks collectively or in the alternative; in their opening submissions, the defendants used the term "the AmPat parties" and did not indicate the basis for their pleaded case that the claim was maintained against both American Patriot and the Hendricks.

286. The point is a short one. It was American Patriot that entered into the Shareholder Agreement, and thereby took on the obligation to indemnify Mutual Indemnity. Under the Shareholder Agreement, American Patriot agreed to purchase one preferred share from Mutual Holdings for the sum of $1,000. American Patriot was then entitled to receive dividends on the dates specified in the appendix to the agreement, and was entitled to redemption of its preferred share on the redemption date upon presentation of the share certificate representing the preferred share, duly endorsed for cancellation. It

is to be noted that the indemnification provisions of the Shareholder Agreement were structured so as to survive both the redemption of the preferred share and the termination of the agreement.

287. The Hendricks took on personal liability in relation to the indemnification obligations by virtue of amendment number 1 to the Shareholder Agreement, executed in July 1998, but with an effective date 23 March 1997, the effective date of the Shareholder Agreement. The change came about because of a concern on Mr. Agnew's part, occasioned by the fact that the volume of business in the second Programme year had grown significantly, thus increasing Mutual Indemnity's exposure, and in this regard Mr. Agnew was concerned that American Patriot might be under-capitalised. Because Mr. and Mrs. Hendricks were high net worth individuals, the amendment was put in place. The amendment recited the issue of the preferred share (when in fact none had been issued), the desire to transfer the preferred share from American Patriot to the Hendricks, and the agreement to cancel the share purported to have been issued and to issue a share to the Hendricks. The Hendricks undertook to assume all the rights duties and obligations of American Patriot under the Shareholder Agreement, but nothing in the amendment released American Patriot from its indemnification obligations, which under the Shareholder Agreement were designed to survive redemption, and which in my view must have been intended to survive cancellation. I therefore find that the claim made by Mutual Holdings in respect of the indemnification obligations owed to Mutual Indemnity are, subject to the further arguments to which I will come in due course, claims which can be maintained both against American Patriot and Mrs. Hendricks.

The Ability of Mutual Holdings to Enforce the Shareholder Agreement

288. The first point made on behalf of the plaintiffs is that Mutual Holdings has suffered no loss under the relevant formula in the Shareholder Agreement, and cannot itself make a claim for indemnification in respect of a loss suffered by Mutual Indemnity. This is followed by an argument based on the effect of amendment number 1 to the Shareholder Agreement, pursuant to which the

preferred share issued to American Patriot was to be cancelled, and a substitute issued in favour of the Hendricks. I have dealt with that argument in paragraph 287 above. The argument is continued with reference to the effect of amendment number 5 to the Shareholder Agreement.

289. Let me start with the first argument, which is that Mutual Holdings has suffered no loss, and of course Mutual Indemnity not being a party to the Shareholder Agreement either in its original or amended form, cannot claim directly. But the claimant in the original proceedings was Mutual Holdings.

290. It does seem to me that the facts of the case before me are identical to those in the case of *Mutual Holdings v Stateco Inc* (Civil Jurisdiction number 380 of 2005), in which Ground CJ delivered a short judgment on 26 September 2007. That case was concerned with a calculation of loss stemming from the Commutation Agreement, which the Chief Justice held fell within the definition of losses contained in the relevant paragraph of the shareholder agreement in that case. Although the losses were those of Mutual Indemnity, the Chief Justice expressed himself satisfied that Mutual Holdings was entitled to claim the shortfall under the indemnity provisions of the shareholder agreement in that case.

291. Mr. Smith also relied upon the statement of general principle set out in the 28th edition of Chitty on Contracts at paragraph 28 – 045, and both sides took me through the leading authority of *Beswick v Beswick* [1968] AC 58.

292. Chitty concluded that it did not follow from *Beswick v Beswick* that the promisee can in all cases of contracts for the benefit of a third party obtain an order of specific performance in favour of the third party. Particularly, it was noted that the case is not direct authority for the availability of such a remedy in all cases. However, Chitty concluded that:

> "As a general principle, it is submitted that the promisee should be able to obtain specific performance in favour of the third party whenever that is the most appropriate method of enforcing the contract which was actually made".

In this case, it clearly is the most appropriate method of enforcing the contract, so I would hold that Mutual Holding is entitled to rely upon the relevant provisions of the Shareholder Agreement so as to enforce a claim against American Patriot and the Hendricks in respect of the indemnification obligations in the Shareholder Agreement in favour of Mutual Indemnity.

293. The plaintiff also relied upon the effect of amendment number 5 to the Shareholder Agreement, and in this regard they submit that no claim can be made either by Mutual Holdings or by Mutual Indemnity because the effect of amendment number 5 was to remove Mutual Indemnity as an indemnified party and to replace it with the defined "insurance company", which the plaintiffs contend is a reference to Legion or Villanova.

294. It was accepted by Mr. Alexander that amendment number 5, which he drafted on the basis of the April 2000 letter, did not achieve what it had been intended to achieve. However, it does have to be remembered that the purpose of the amendment, and as I understand it the joint intention of the parties, was to make it clear that the Hendricks continued to have indemnification obligations for any losses in excess of the combination of the AAP and the third party reinsurance purchased by Legion. And in my view there is no basis for concluding that the effect of amendment number 5 was to remove Mutual Indemnity and to replace it with Legion or Villanova; the relevant provision provided that the Hendricks agreed to indemnify Mutual Holdings and/or Legion/Villanova. Amendment number 5 did not remove the obligation on the part of American Patriot/the Hendricks to indemnify Mutual Indemnity in respect of underwriting losses as defined in the Shareholder Agreement. I therefore hold that amendment number 5 does not have the effect for which the plaintiffs contend.

The Proper Amount of Mutual Holdings' Claim

295. At about the time that Mr. Bjornson had sent his request for the premium through to Ms. Saran, there was a continuing dispute between the parties as to the proper amount due, which amount covered the losses up to the AAP which had not been fully collateralised. It is accepted that this dispute between the

parties was never resolved. The case for the plaintiffs is that the Court is not in a position to determine the actual amount of collateral due, and that Mr. Alexander's calculation as to Mrs. Hendricks' share of liability based on the Commutation Agreement is "fundamentally flawed". The plaintiffs carry on to submit that the Hendricks are entitled to be discharged from liability under the indemnity on the basis that their position had been materially adversely affected by the Commutation Agreement.

296. It seems to me that the problem for the plaintiffs is that while Mr. Alexander was challenged in regard to his calculation, he stood by his figures, and I do not regard his calculation as having been undermined in anyway in cross-examination. One then comes to the position that there was no alternative evidence put forward by the plaintiffs to establish any other figure as the appropriate commutation figure. In these circumstances, I do accept Mr. Alexander's calculations, and hold that the amount due from American Patriot/the Hendricks to Mutual Indemnity/Mutual Holdings pursuant to the Commutation Agreement is the sum of $8,595,361 identified by Mr. Alexander.

297. This is also no doubt the appropriate place to deal with the argument made for the plaintiffs that the losses evidenced by the Commutation Agreement have not been established so as to fall within the definition of Mutual Indemnity's losses leading to the indemnification obligation under the Shareholder Agreement.

298. As the defendants submitted, this was not an internal accounting transfer, it was an actual payment of cash which caused an actual underwriting loss. There was nothing in the Shareholder Agreement which suggests that a loss made under these circumstances should be excluded, and again the judgment of the Chief Justice in *Mutual Holdings v Stateco* appears to be on point. I do not think that the losses evidenced by the Commutation Agreement can be discounted as the plaintiffs have sought to do. I should add that I reject the contention that American Patriot/the Hendricks were adversely affected by the Commutation Agreement. The table produced by Mr. Alexander in his

witness statement shows that for the fourth year of the Programme, the commuted losses were substantially below the AAP figures for which American Patriot/the Hendricks would otherwise have been liable.

Conclusion on Mutual Holdings' Case

299. It follows from my findings set out above that I am satisfied that Mutual Holdings is able to enforce the Shareholder Agreement as against both American Patriot and the Hendricks, and succeeds in its claim of $3,419,361, representing the sum of $8,595,361 paid under the Commutation Agreement, less the draw downs on the letters of credit of $5,176,000. The $1 million in premium which Mutual Indemnity recognises is held as a set off is to be deducted from the figure of $3,419,361, to leave a balance of $2,419,361.

Alternative Findings - Agency and Piercing the Corporate Veil

300. I have referred to the fact that Mrs. Hendricks and Mr. Bossard did not differentiate between the different companies within the Mutual Group. The factual matters on which the plaintiffs relied were, first, that Mr. Partridge and Mr. Turner were both directors of and held senior positions in MRM, and secondly, the amended registration statement filed by MRM with the SEC. The plaintiffs contend that it is clear from the statements made in that registration statement that "the MRM product" was being sold and marketed through subsidaries in the United States. The plaintiffs also contended in their closing submissions that Mr. Alexander had accepted that Mutual Indemnity was in position to control whether Legion or Commonwealth bound any particular programme.

301. I will deal with that last point first, because I think it overstates what Mr. Alexander said in his evidence. His comments followed his description of how a new programme was put in place, and it was put to him that Legion would not bind a programme without Mr. Alexander or somebody from Mutual Indemnity signing off. Mr. Alexander agreed that he was signing off on the collateral at the last level of sign off. It was then put to Mr. Alexander that if he had not been satisfied by the terms being proposed by Legion, he would have had the right on Mutual Indemnity's behalf to say that Mutual

Indemnity would not reinsure the Programme, which in turn meant that Legion could not bind it. Mr. Alexander had agreed with the first part of the proposition, but also said that he did not have any expertise to comment on Legion's underwriting.

302. The fact of it is that any programme required different obligations to be taken on by different companies within the Mutual Group; Legion underwrote the issue of the original insurance policies, and Mutual Indemnity provided the reinsurance, in respect of which it needed to be satisfied that the collateral provided was adequate. Any new programme required both Legion and Mutual Indemnity to be satisfied, so that I do not think it is an appropriate characterisation to say that Mutual Indemnity was in a position to control whether Legion bound a particular programme. Mutual Indemnity was concerned with the terms of the contracts which it was going to enter into, and if it was not satisfied, the consequence was that Legion could not proceed with its part of the proposed programme. That does not mean that Mutual Indemnity was controlling Legion.

303. And neither does the fact that an individual is, for instance, a director of multiple companies mean that when he acts as a director of one, he does so as a director of all. More difficult questions no doubt arise in relation to the issue of knowledge, but the mere fact that Messrs. Partridge and Turner were directors of MRM does not mean that when they were attending the Coverage Meeting in Philadelphia in early 2000 in their capacity as employees of Legion and Commonwealth, they were also acting on behalf of MRM.

304. Mr. Smith referred to the plaintiffs' heavy reliance upon the SEC registration statement, but said that this document did no more than describe the operations of the Mutual Group, and that it was common ground that MRM was a holding company operating through subsidiaries. He carried on to say that the SEC registration statement did not mean that MRM was personally liable for the operation of each of its subsidiaries, or that the subsidiaries acted as agents of MRM, or that the corporate veil between the separate companies in the group should be pierced, and he carried on to comment that it mattered

not that Ms. Saran and Mrs. Hendricks did not choose to distinguish between the different subsidiaries within the Mutual Group.

305. I agree with Mr. Smith's submissions, and would quote part of the extract on which he relied from the case of *Adams v Cape Industries Plc* [1990] 1 Ch 433 at 544, and the judgment of the Court of Appeal delivered by Slade LJ, in the following terms:

> "…we do not accept as a matter of law that the court is entitled to lift the corporate veil as against a defendant company which is the member of a corporate group merely because the corporate group structure has been used so as to ensure that the legal liability (if any) in respect of particular future activities of the group (and correspondingly the risk of enforcement of that liability) will fall on another member of the group rather than the defendant company. Whether or not this is desirable, the right to use a corporate structure in this manner is inherent in our corporate law. Mr. Morison urged on us that the purpose of the operation was in substance that Cape would have the practical benefit of the group's asbestos trade in the United States of America without the risks of tortious liability. This may be so. However, in our judgment, Cape was in law entitled to organise the group's affairs in that manner and (save in the case of A.M.C. to which special considerations apply) to expect that the court would apply the principle of *Salomon v. A. Salomon & Co. Ltd.* [1897] A.C. 22 in the ordinary way."

306. Hence I do not accept that, if the various matters complained of were to have been established, MRM would be vicariously liable for the alleged deceit, misrepresentations or negligent misstatements said to have been made by any of Messrs. Partridge, Turner, Walsh or Alexander. I would just add that there was no evidence to support the pleading referred to in paragraph 19 above. The general assertions made by Mr. Bossard (referred to in paragraph 43 above) are inadequate in this regard.

307. All of that said, I would just deal with the position of Commonwealth, with particular reference to its role as producer of the business known within the

Mutual Group as the IPC programmes. There was no evidence as to how Commonwealth was compensated for its role as producer, but it is quite clear that it was not operating for its own account; the business which it produced was business on which Legion, Mutual Holdings and Mutual Indemnity were the contracting parties, from which they had the profit opportunity. So Commonwealth can only have been acting as an agent in producing this business, and it must have been acting as agent for Legion, Mutual Holdings and Mutual Indemnity. But I do not believe anything turns on this. The representations made by Messrs. Bossard and Agnew were true, save those made by Mr. Bossard in his emails, which were clearly not. But they misrepresented the position with regard to the purchase of reinsurance, not as to the need for the protection which Mrs. Hendricks sought. And in relation to the former, there was no difference so far as American Patriot/Mrs. Hendricks were concerned between the purchase of third party reinsurance and Mutual Indemnity self-reinsuring.

Collateral Contract

308. I referred to this in my summary of the pleadings. In the event, while the issue was not formally withdrawn, Mr. Martin confirmed during the course of Mr. Smith's closing submissions that the issue was not pursued.

Further Alternative Findings

309. There are two further points which it is appropriate to consider at this stage. The first is Mr. Martin's position as to the effect of fraud, if established. He submitted that the rule "fraud unravels everything" means that a fraud in relation to the fourth Programme year would absolve American Patriot and the Hendricks from any liability in respect of the first three Programme years. I would not accept that argument, and I indicated my difficulty with it to Mr. Martin in the course of his submissions. The reality is that each of the Programme years was the subject of a new contractual arrangement, evidenced by amendments to the Shareholder Agreement. The indemnification obligations for the first three Programme years arose before the alleged fraud. In my view, even if the fraud were to have been

established, it would not affect the obligations for those first three Programme years.

310. Another question which falls to be decided is the liability for the fourth Programme year, if indeed this was entered into on the basis of fraudulent misrepresentation as to the exposure in relation to the first three Programme years.

311. It is important to look at the evidence in relation to this aspect of matters, and no doubt to remember that part of the background to renewal for the fourth year was that by virtue of the under-reserving, substantial sums were required in respect of the collateral for the first three Programme years. In one sense, it could be thought that the arrangements to cap losses for the first three Programme years and the renewal of the Programme for the fourth year were different matters. But Mrs. Hendricks' evidence was clear in this regard. In her witness statement, Mrs. Hendricks said that had she known of the misrepresentations in relation to the exposure above the AAP, she would not have renewed the Programme for year four. In cross-examination, Mrs. Hendricks was asked what the position would have been in relation to the fourth year renewal if she had in fact had exposure above the AAP. She said that Ms. Saran was handling the matter, and she had been advised to buy the reinsurance coverage for $1 million, and "to go forward that next year with the rates". But Ms. Saran's evidence was that Mrs. Hendricks had said "that if they could not make her exposure above the aggregate attachment point go away there would be no renewal".

312. So from that it would follow that if the fraud were to be established, American Patriot and/or the Hendricks would be in a position to set aside the renewal for the fourth Programme year.

Damages - Costs of the US Proceedings

313. Mrs. Hendricks said at the conclusion of her witness statement that she had incurred some substantial expenses in obtaining relief in what she described as "related proceedings in the United States", all of which she said were the direct result of the deceit and/or negligent misrepresentations made by "the

Mutual Entities" and their related officers. She put all those expenses at the time of her witness statement as being in excess of $4 million, and at the start of her oral evidence put in a binder breaking down those expenses, with a total of $4,232,260.87. Mrs. Hendricks indicated that she herself had not reviewed the documents in the binder, and in answer to my question in relation to one set of proceedings, Mrs. Hendricks could not even identify the parties to the proceedings. So apart from anything else, there are evidential difficulties with the amount claimed.

314. For my part, I do not even know what the issues were in the US proceedings, although obviously I am aware that there were extensive proceedings in relation to the draw down of the letters of credit. But even then, the breakdown is not fully documented. For instance, there is a tab within the binder which appears to cover four separate sets of proceedings, for which the amount claimed is in excess of $2.5 million. Further, part of the amount claimed is in respect of the fees of US lawyers in these proceedings. Indeed, the entirety of the redacted bills under this head appear to relate to these proceedings; I saw no references to the other proceedings which appear in the schedule in the front of the binder, but it seems to me that there is a sensible way of dealing with these legal fees, in respect of which an award would only be made if the fraud were to be established. The major problem which I see from the plaintiffs' perspective is that matters relating to the fraud and the draw downs on the letters of credit are in substance issues which follow from the indemnification obligations contained in the Shareholder Agreement. Not only is that agreement governed by the laws of Bermuda, but there is an exclusive jurisdiction clause requiring any disputes concerning the agreement to be resolved by the courts of Bermuda. If American Patriot and/or the Hendricks had wished to restrain the draw down on the letters of credit, their remedy was to seek injunctions against Mutual Indemnity in Bermuda, something which they did ultimately seek to do, albeit unsuccessfully. That is what they should have done from the outset, and I would not award damages in respect of those US proceedings when the US courts have presumably

declined to make costs orders themselves, even if the fraud were to have been established.

315. In relation to the costs of US lawyers in these proceedings, that is a matter which can and should be dealt with on an application for costs at the end of the day in these proceedings. There is Bermuda authority on the costs of foreign lawyers – see the ruling on costs of Ground J in the *EMLICO* case on 19 February 1997.

316. There are other difficulties with this claim, not least the fact that in a number of instances the plaintiffs were not successful in them. Further, it appears from an extract that I was given from McGregor on Damages (17th edition, paragraph 17-004) that:

> "Costs incurred in earlier proceedings brought in another jurisdiction cannot be recovered as damages in a later action in England between the same parties in respect of the same claim: it was so held in *The Ocean Dynamic*".

317. That would appear to put an end to the matter.

Damages – Exemplary Damages

318. The claim for exemplary damages arises only if the plaintiffs succeed on their primary case of fraud. Reliance is placed on the case of *Kuddus v Chief Constable of Leicestershire* [2002] 2 AC 122. That case was concerned with misfeasance in public office, and considered the availability of an award of exemplary damages in the context of a strike out. The County Court judge and the Court of Appeal had held that exemplary damages were not recoverable for the tort of misfeasance in public office. The House of Lords allowed the appeal, but made it clear that the availability of exemplary damages should not be extended beyond the tort of misfeasance in public office. So if my primary finding is wrong and the plaintiffs are entitled to damages for fraud, I would not make an order increasing the award of damages by an additional figure in respect of exemplary damages.

Damages – Interest on the Sum due to Mutual Holdings

319. I will start by identifying the periods over which interest should be calculated. The Commutation Agreement was made "as of" 23 April 2003, but there was then a dispute as to its efficacy which led to the order of the Pennsylvania court approving it on 8 May 2003. It is that latter date which should operate as the date from which interest should be calculated. But that calculation only runs in part, to the time of the different draw downs on the different letters of credit. In paragraph 98 of his witness statement, Mr. Alexander gave the amounts of the three draw downs, but not the dates. Hopefully, those can be agreed, so that effectively the calculation needs to be undertaken in respect of each draw down, calculated with reference to the principal amount drawn down, from 8 May 2003 until draw down.

320. Then there is the fact that Mutual Indemnity has had the benefit of the $1 million which it accepts is to be set off against the monies due to it. Mutual Indemnity received the $480,000 on 18 May 2000, and it appears from an email sent by Ms. Saran on 27 February 2002 the payment of the $520,000 was to be made on 5 March 2002.

321. So payment of these amounts was made before the operative date of the Commutation Agreement, at a time when Mutual Indemnity believed it was self-insuring in relation to the removal of exposure from American Patriot/the Hendricks for the first three Programme years. It seems to me that the appropriate way to deal with this amount is to make no order in respect of interest between the dates of payment and the operative date of the Commutation Agreement, but to hold that from that operative date, interest should not accrue on the $1 million, on the basis that this was due to American Patriot/the Hendricks by virtue of the terms of the Commutation Agreement.

322. I recognise that there are still dates to be agreed and calculations to be undertaken, but hopefully the position can be agreed between counsel, and in the event that it is not, I grant liberty to apply.

323. As to the rate of interest, I would order that this be at the statutory rate of 7% per annum.

Summary

324. The consequence of my various findings set out above is that neither American Patriot nor Mr. or Mrs. Hendricks are entitled to the relief sought against Mutual Indemnity, MRM and the four individual defendants, in terms of the declarations and damages sought. Neither are they entitled to damages as against Commonwealth in respect of the alleged deceit, negligent misrepresentation or negligent misstatement in respect of the statements made by Messrs. Bossard and Agnew, on the basis that their representations and statements were true, notwithstanding that they believed them to be false.

325. And in relation to the claims made by Mutual Holdings against American Patriot and the Hendricks, I make an award of damages in the sum of $2,419,361 identified in paragraph 299 above, on the basis that Mutual Holdings is entitled to the benefit of the $1 million held by Mutual Indemnity.

Costs

326. I would expect that costs should follow the event, but it may be that some form of alternative order should be considered, to cover the position if the dismissal of the fraud allegation and its related matters were to be upheld, but I were to be held wrong in relation to the corporate law issues. As I indicated, these were raised very late in the day, and for many years this case was concerned with the fraud allegation only, so that if I were to be right in relation to the fraud and wrong in relation to the corporate law issues, I would still anticipate making an order for costs in favour the defendants up to the time that the corporate law issues were first fully pleaded, which I believe would be a date in April 2010. But that said, I will hear counsel on costs.

Dated this day of July 2010

Hon. Geoffrey R. Bell
Acting Puisne Judge