

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

**IN THE MATTER OF
RELIANCE INSURANCE COMPANY**

**AND IN THE MATTER OF THE
*INSURANCE COMPANIES ACT, S.C. 1991, C.47, AS AMENDED***

**AND IN THE MATTER OF THE
*WINDING-UP AND RESTRUCTURING ACT, R.S.C. 1985, C.W-11, AS AMENDED***

B E T W E E N:

THE ATTORNEY GENERAL OF CANADA

Applicant

- and -

RELIANCE INSURANCE COMPANY

Respondent

**REPORT OF KPMG INC., THE LIQUIDATOR OF
RELIANCE INSURANCE COMPANY – CANADIAN BRANCH**

August 25, 2004

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I. THE MOTION

1. This report is respectfully filed in support of a motion by KPMG Inc., the liquidator (the “Liquidator”) of the insurance business of Reliance Insurance Company in Canada (“Reliance (Canada)”) for an Order:

- a) passing the accounts of the Liquidator for the period October 1, 2003 to June 30, 2004 (the “Three Quarters”), as reflected in the financial statements of Reliance (Canada);
- b) approving the professional fees of the Liquidator and of its counsel (the “Professional Fees”) for the Three Quarters;

- c) authorizing the Liquidator to pay up to \$25,000 on valid claims under the Meridian program; and
- d) approving and authorizing a second interim distribution of 25% of valid and allowed loss claims (the “Second Distribution”), bringing total distributions to 50% thereof, as claims are allowed.

II. OVERVIEW OF THE ESTATE

A. Policy Payments

2. Pursuant to orders of this Court, the Liquidator has paid policyholders and claimants the following benefits since the commencement of the liquidation of Reliance (Canada):

- a) defence costs;
- b) valid claims up to the greater of \$25,000 or the amount, if any, of the voluntary compensation payment of the Property and Casualty Insurance Compensation Corporation (“PACICC”) that may be paid under its Memorandum of Operations; and
- c) valid claims under the Meridian program up to the greater of \$5,000 or the amount, if any, of PACICC’s voluntary payment,

(collectively, the “Policy Payments”).

A copy of the order appointing the Liquidator and authorizing the Policy Payments is attached as Schedule “A” (the “Appointment Order”). This Court has extended the date for making the Policy Payments from time to time, the latest extension being to further order of the Court.

3. This Court further approved a first interim distribution (the “First Distribution”) to policyholders and claimants of 25% of their valid and allowed claims on June 26, 2003. The Liquidator therefore now pays policyholders and claimants the higher of the Policy Payments and the First Distribution.

B. Second Distribution

4. The Liquidator has made progress in the administration of the estate since the approval of the First Distribution. Small claims continue to be closed on an efficient basis, with the use of third party administrators where appropriate, including on programs such as Meridian, Family and Groupe PPP (described below). A number of large complex claims have also now been resolved. Reinsurance collections are improving, in part because outstanding issues with reinsurers that involve the U.S. estate are being resolved. However, the reinsurance market has generally been difficult, and collection problems are an industry wide issue.

5. Based on the Liquidator's continuing experience with the estate, the Liquidator remains confident that all policyholders will receive full payment on all valid claims. As at June 30, 2004, the surplus on the financial statements was \$42.9 million. However, there remain uncertainties in the estate and the Liquidator is not in a position to make full payment at this time. To further alleviate hardship to policyholders whose claims are not satisfied by the Policy Payments, the Liquidator proposes to make a second interim distribution of 25% of valid loss claims, bringing total distributions to 50% on all claims as they are allowed.

C. The Future

6. The Liquidator will continue the run-off of Reliance (Canada)'s business in an orderly manner, dealing with policy liabilities and collection of reinsurance on a commercially reasonable basis, seeking the approval of the Court for further interim distributions as appropriate. Given the nature of Reliance (Canada)'s business, the process can be expected to take many years. The consulting actuary estimates that the run-off will continue to 2018, but the number of payments will begin to decline after 2007. However, based on current information and assuming no unforeseen negative developments, the Liquidator is optimistic that payment of 100% of valid loss claims will be reached by 2007.

7. As previously reported, the Liquidator pursued an intensive marketing program for the policy liabilities last year, which did not result in a transaction. The market for the sale of policy liabilities now appears to be improving. Several parties have contacted the Liquidator to ask

very preliminary questions concerning the estate, and the possibility of acquiring the liabilities. Although the Liquidator believes that the improving reinsurance collections and the resolution of certain of the problematic claims will have a positive effect on their marketability, the Liquidator does not consider that the costs of a formal disposition program for Reliance (Canada)'s liabilities are warranted at this time. The Liquidator will continue to monitor market conditions and use all reasonable efforts to find innovative approaches to expedite the completion of the liquidation.

III. BACKGROUND

A. General Background

8. Reliance Insurance Company (“Reliance”) is a property and casualty insurer in the United States of America, domiciled in the Commonwealth of Pennsylvania. Reliance carried on business in Canada as a “foreign company” within the meaning of the *Insurance Companies Act* through a branch. In October, 2000, Reliance (Canada) stopped issuing new policies and began “running off” or winding down its existing business.

9. Reliance was ordered liquidated by Order of the Commonwealth Court of Pennsylvania dated October 3, 2001, under the Pennsylvania *Insurance Department Act of 1921*. M. Diane Koken, Commissioner of Insurance for Pennsylvania, was appointed liquidator (the “U.S. Liquidator”).

10. By Orders of this Court made December 3, 2001, the insurance business of Reliance (Canada) was ordered wound-up pursuant to the provisions of the *Winding-up and Restructuring Act* and KPMG Inc. was appointed provisional liquidator.

11. In the Appointment Order, this Court appointed the U.S. Liquidator and PACICC as inspectors. By order dated January 30, 2002, this Court ordered that the Superintendent of Financial Institutions of Canada (the “Superintendent”) may attend meetings of inspectors, be included in the service list, and attend and be heard in matters before this Court.

12. The inspectors and the Superintendent are not opposing this motion.

B. Reliance (Canada)'s Insurance Business

13. Reliance (Canada) wrote a very diverse set of policies. Within the classes of liability insurance that it wrote, Reliance (Canada) specialized in providing coverage for professional liability, directors' and officers' liability, pollution and environmental liability and product liability. While some of Reliance (Canada)'s policies were "claims made", meaning that claims must be reported during the term of the policy or within a defined period thereafter, a substantial portion of its policies were "occurrence" based. These policies cover liabilities incurred during the policy period that may not become manifest for years. This business is called "longtail". The policyholders themselves have no way of predicting what claims they may incur. Reliance (Canada) also wrote policies with lengthy policy periods. In addition, Reliance (Canada) acted as a reinsurer for other insurers. "Assumed Reinsurance" is treated as insurance under the *Insurance Companies Act*, and is accorded the same priority as loss claims under the *Winding-up and Restructuring Act*.

14. In October 2000, Reliance (Canada) voluntarily stopped writing new policies, effectively winding down its business. At the beginning of the liquidation, excluding the warranty programs, there were 16 policies still in force with all other policies having expired or been cancelled, and over 1100 claims. In addition, Reliance (Canada) had "incurred but not reported" ("IBNR") claims for which it will ultimately be put on notice and to which it will have to respond, primarily on the occurrence-based policies.

15. As at June 30, 2004, two policies remained in force. The term of the second policy and the last certificates in the Meridian program will expire in 2007. There were 544 open claims, excluding the warranty programs.

IV. MERIDIAN PROGRAM

16. As discussed, the Liquidator is authorized to pay the greater of \$5,000 or the amount, if any, of PACICC's voluntary payment, the maximum of which is \$250,000.

17. PACICC does not generally respond to claims on policies in force more than 45 days after a winding-up order, but agreed to do so in the case of the Meridian program because of the potential sale of the Meridian block. It has now confirmed that it will not respond to new Meridian claims.

18. Since the winding-up order was made, there have been 13 claims that exceeded \$5,000 each, by the total amount of \$28,000. The Liquidator has no reason to believe the claims under the Meridian program will increase. The \$5,000 amount was originally chosen as likely to cover the vast majority of claims, as it has, in the event that PACICC ceased responding. Given the amounts in issue and the cost of paying multiple dividends on any amounts in excess of \$5,000, the Liquidator is of the view that the Meridian claimants should now be accorded the same treatment as other policyholders and be paid up to \$25,000 (an amount not likely to be reached in any case).

V. FINANCIAL STATUS OF THE ESTATE

19. The First Distribution was based on the financial status of the estate at March 31, 2003. Copies of the Order of this Court dated June 26, 2003 approving and authorizing the First Distribution and of the Liquidator's report in support with relevant schedules are attached as Schedules "B" and "C" respectively.

20. This Court passed and approved the accounts of the Liquidator for the period from the Winding-up Order to September 30, 2003 on December 18, 2003. Attached as Schedules "D" and "E" respectively are copies of the Order of this Court and the Liquidator's report in support with relevant schedules.

21. Attached as Schedule "F" are the unaudited financial statement for the estate as at June 30, 2004, prepared in a manner consistent with the financial statements before this Court for September 30, 2003, and with the same system of internal controls to safeguard the assets and reliability of the financial reporting process.

22. In this report, the Liquidator will generally compare the financial status of the estate at June 30, 2004 to its status at September 30, 2003, but will also make relevant comparisons to the status at the time of the First Distribution.

23. The estate surplus has been reduced from \$52.9 million at September 30, 2003 to \$42.9 million at June 30, 2004. This is, in large measure, the result of an increase in the policy liabilities. A key characteristic of the Reliance (Canada) claims profile is its “lumpiness.” A significant number of its policies do not have frequent claims, but, if claims occur, they are severe. As further progress has been made in dealing with the claims and more information becomes available on which to assess them, the Liquidator has increased the policy liabilities, reflecting increases referable to these kinds of policies. This has the effect of also increasing the reinsurance recoverables since these claims are generally reinsured at significant levels. As indicated, the net result is that the surplus has decreased. Such fluctuations in the level of surplus are to be expected, given the volatility of the portfolio.

A. Assets

Vested Assets

24. Reliance operated within Canada on a branch basis, with the approval of the Superintendent of Financial Institutions. The conditions for the Superintendent’s approval of the operation of a branch in Canada include the vesting in trust with the Superintendent of assets having a prescribed value (the “Vested Assets”), and filings, at least annually, of financial information disclosing both assets for which the branch is entitled to take credit under the *Insurance Companies Act*, and liabilities that it is required to report as liabilities of the branch, also under the *Insurance Companies Act*.

25. As at the commencement of the liquidation the Vested Assets consisted of cash or near cash in the amount of approximately \$171 million. The Liquidator has been making the Policy Payments and paying the costs and expenses of the liquidation. It has collected reinsurance and subrogation proceeds. As at June 30, 2004, the cash or near cash was approximately \$155 million.

Reinsurance

26. The other major asset of Reliance (Canada) is reinsurance, consisting of:
- a) reinsurance for which Reliance (Canada) was entitled to take credit under the *Insurance Companies Act* in calculating its required assets covering only the liabilities of Reliance (Canada) (“Canadian Reinsurance”); and
 - b) reinsurance entered into through Reliance’s head office, which reinsures both Reliance (Canada) policies and policies written through the U.S. operations (“International Reinsurance”) for which Reliance (Canada) was not entitled to take credit under the *Insurance Companies Act*.

27. The percentage of Reliance (Canada)’s case reserves that are reinsured changes over time as the composition of the case reserves changes. As at March 31, 2003 approximately 51% of Reliance (Canada)’s gross case reserves were reinsured. Of this amount, approximately 89% was Canadian Reinsurance and 11% was International Reinsurance. As at June 30, 2004, approximately 65% of Reliance (Canada)’s gross case reserves were reinsured, approximately 34% of which was Canadian Reinsurance and 66% International Reinsurance. This results from the increase in case reserves, discussed below, which brings the reserves into the excess layers, generally provided under the International Reinsurance. These percentages do not reflect estimates for uncollectible reinsurance due to credit, collection or contractual risk. Over 82% of the reinsurance is with reinsurers rated “A” or higher.

28. By June 30, 2004, the Liquidator had collected approximately \$14.7 million in reinsurance since the beginning of the liquidation, \$9.2 million since March 31, 2003. The U.S. Liquidator has collected International Reinsurance in the amount of U.S.\$4.8 million on behalf of Reliance (Canada), which has not yet been remitted. In addition, reinsurance receivables (amounts billed to reinsurers), net of a provision for uncollectible reinsurance, were \$27.6 million at June 30, 2004 up from \$9.2 million at March 31, 2003. Reinsurance recoverables (amounts referable to reported claims not yet billed and to IBNR), net of a provision for uncollectible reinsurance, were \$76.6, up from \$61.7 million at March 31, 2003. Since June 30,

the Liquidator has collected an additional sum of \$5.1 million, reflecting the success of continuing collection efforts.

Summary

29. As at March 31, 2003, the value of Reliance (Canada)'s assets was \$242.5 million and cumulative claims and related expenses paid from the commencement of the liquidation to March 31, 2003 totalled \$22.4 million. As at June 30, 2004, the value of Reliance (Canada)'s assets was \$265.6 million. Cumulative claims and related expenses paid totalled \$43.3 million.

	June 30, 2004 (in millions)	September 30, 2003 (in millions)	March 31, 2003 (in millions)
Cash or near cash	\$155.1	\$156.3	\$161.3
Reinsurance receivables and recoverables net of estimate for uncollectible reinsurance	\$104.1	\$ 71.1	\$ 71.2
Miscellaneous	6.4	\$ 9.6	\$ 10.0
Total	<u>\$265.6</u>	<u>\$237.0</u>	<u>\$242.5</u>
Cumulative claims and related expenses	<u>\$43.3</u>	<u>\$31.5</u>	<u>\$22.4</u>

B. Liabilities

30. In its solicitation letter provided to prospective purchasers, the Liquidator disclosed that the total policy liabilities according to the books and records of Reliance (Canada) were approximately \$132 million, including IBNR, as at June 30, 2001. A copy of the solicitation letter is attached as Schedule "G".

31. The Liquidator has performed further actuarial and claims reviews but did not share those results at the time of the First Distribution because it did not wish to prejudice the sale. At September 30, 2003, the estimated value of the liabilities was \$174.4 million. As at June 30, 2004, the estimated value was \$213.7 million, determined as described below.

No Call for Claims to Date

32. The Liquidator has not undertaken a call for claims to date and is not recommending one at this time because the Liquidator believes such a call would be expensive and counterproductive, given the long tail nature of Reliance (Canada)'s policies. Policyholders would have no choice but to file contingent claims of a magnitude that would make the claims meaningless. At the conclusion of the process, the Liquidator would still have to rely on actuarial projections to reach a view as to the total claims exposure of the estate, and would certainly have to do so to make a distribution in a reasonable time frame.

Loss Claims

33. There are basically three categories of loss claims:

- a) claims that are settled or otherwise resolved (the "Resolved Claims"). Since the First Distribution, the Liquidator has resolved approximately 5,626 claims having a total value \$40.4 million. As at June 30, 2004:
 - (i) approximately 14,751 claims having a total value of \$64.8 million have been resolved, through settlement or otherwise, since the beginning of the liquidation;
 - (ii) of those, the Liquidator paid 5,598 claims in full for approximately \$9 million since the First Distribution, bringing the total claims paid in full in accordance with the court authorized Policy Payments to 14,723 claims having a value of approximately \$21.3 million; and
 - (iii) the remaining 28 claims either do not qualify for PACICC coverage or exceed PACICC limits. Policy Payments have been made on account of these claims in the amount of \$10.4 million but a balance of \$33.1 million remains outstanding;
- b) claims which have been reported but not yet resolved (the "Reported Claims"). As at June 30, 2004, there were approximately 544 Reported Claims outstanding, down from 757 at March 31, 2003 but outstanding gross case reserves almost

doubled, from approximately \$51.5 million, to \$100.2 million. Case reserves are adjusted as additional information on the estimated amount of a claim becomes known during the course of its settlement. As discussed earlier, this change reflects the volatility and “lumpiness” of Reliance (Canada)’s portfolio; and

- c) the provision for IBNR and for deficiencies in Reported Claims.

Non-Booked Claims

34. As described in previous reports, there may be claims not reported in the books of Reliance (Canada) that may be valid claims in its liquidation (the “Non-Booked Claims”). The Non-Booked Claims arise from policies written outside of Canada but which have some nexus with Canada, and which, arguably, should have been reported in the books of the branch and for which assets should have been deposited in Canada.

35. No new Non-Booked Claims have been identified since the First Distribution. The U.S. Liquidator has agreed that her staff will advise the Liquidator if they identify any Non-Booked Claims, including as a result of the U.S. call for claims that expired on December 31, 2003. They are performing a preliminary adjudication of all claims filed and, as indicated, none have been identified to date. The U.S. Liquidator anticipates completing the adjudication in the next several months.

36. Based on the information presently available, the Liquidator estimates that the total value of the Non-Booked Claims identified thus far, if all proved to be valid, is less than Cdn \$10 million. This would not impact the Liquidator’s ability to pay all Reliance (Canada)’s valid claims in full. However, there is no certainty as to the magnitude of the Non-Booked Claims, since they were not originally identified as being appropriately assigned to Reliance (Canada). It is important to note that the U.S. Liquidator considers the open claims identified as having a possible nexus with Canada as claims which, if valid, would participate in the U.S. estate.

37. The Liquidator will be seeking the directions of this Court with respect to giving notice to any party who believes they have a claim properly assertable against Reliance (Canada) to come

forward, and will then seek directions of this Court with respect to whether the Non-Booked Claims should be allowed in the Canadian estate.

Liability Claims Projection Process

38. The Liquidator has applied the same basic methodology in projecting the policy liabilities as for the First Distribution. The Liquidator has undertaken an extensive review of the policy liabilities, including retaining the services of the consulting actuary who acted for Reliance (Canada) before it was wound up. Representatives of the U.S. Liquidator have also reviewed the largest case reserves on which there is the greatest volatility and have shared their results, which the Liquidator has taken into account in establishing the policy liabilities.

39. Actuarial projections typically consider:

- a) the current level of reserves;
- b) the history of claims development;
- c) the nature of the liabilities underwritten and the terms of the policies;
- d) industry experience and current developments with respect to similar kinds of policies and liabilities; and
- e) the potential for adverse deviation, a provision against claims developing negatively in comparison to past experience.

40. Actuaries then reach a view as to the total policy liabilities to which the insurer will be exposed, including a provision for IBNR. While the actuaries generally provide a single best estimate, there is clearly a range for valuing the total liabilities, depending on the degree of certainty to be achieved. For instance, in some circumstances, it would be within accepted actuarial standards to indicate a best estimate with a 55% degree of confidence, meaning that the liabilities would exceed the estimate 45% of the time and be less 54% of the time. More conservative assumptions would lead to higher confidence levels. In going concern situations, this may be considered appropriate.

41. The Liquidator instructed the actuaries to confirm their best estimate of the policy liabilities in accordance with accepted actuarial standards. The Liquidator then carefully reviewed the assumptions underlying the actuarial estimates, and introduced some further elements of conservatism in reaching the estimate of \$213.7 million for policy liabilities.

VI. MAJOR ACTIVITIES OF THE LIQUIDATOR

A. Administration

42. On being appointed, the Liquidator considered Reliance (Canada)'s complex claims, and the seniority and reputation of its employees, and consulted with the U.S. Liquidator and PACICC. The Liquidator determined that the best interests of the estate would be served by maintaining continuity, to the extent possible, through retaining existing Reliance (Canada) staff and that this would result in cost savings. At the beginning of the liquidation there were seventeen employees. As at June 30, 2004, 8 employees remained.

43. Reliance (Canada) employees perform day-to-day administration, including instructing defence counsel and outside adjusters, dealing with counsel on coverage issues, administering reinsurance collections, performing accounting and financial reporting with respect to claims and reinsurance issue functions, and liaising with PACICC and employees of the U.S. estate.

44. The Liquidator maintains responsibility for the conduct of the liquidation. The Liquidator is responsible for all strategic initiatives, and major decisions and, as appropriate, is involved in supervising and augmenting, where necessary, the day-to-day activities performed by former Reliance (Canada) employees. The Liquidator performs the functions specific to the liquidation, including the development of policies and procedures for claims handling and authorities, the institution of internal controls, reporting to court and stakeholders, supervising and coordinating legal counsel, monitoring developments in the U.S. liquidation, and providing insureds with information. The Liquidator reviews all claims decisions involving claims that meet criteria established in co-operation with PACICC and the U.S. Liquidator, performs the financial reporting, is actively involved in reinsurance collections, makes all investment

decisions, instructs and consults with the actuary. A further summary of the Liquidator's activities is set out in paragraph 53.

B. Third Party Administrators

45. Reliance (Canada) also had arrangements with third party administrators who were responsible for the administration of claims in a number of programs, the major ones including:

- a) Meridian;
- b) Groupe PPP, a financial guarantee program underwritten in the U.S., covering automobile dealers in Quebec;
- c) Gap Program, a financial warranty program;
- d) Family Program, a personal lines program in British Columbia; and
- e) Environmental Program, administered by ECS Inc. in the United States.

46. Each of the programs is unique in respect of the volume, magnitude and complexity of its claims, and with respect to the discretion accorded the third party administrators. In each case, the Liquidator reviewed the program and the nature of the relationship between the administrator and Reliance (Canada). In assessing the continued use of the third party administrators, the Liquidator considered their cost, the potential prejudice if the administration were disrupted and the quality of their work. The Liquidator determined that it was appropriate to maintain the relationships, but introduced additional controls and reporting requirements, as it considered necessary, and regularly reviews the status of the administrations.

C. Stakeholders

PACICC

47. The Liquidator entered into a loan and services agreement with PACICC on December 3, 2001, approved by this Court in the Appointment Order.

48. PACICC approves payments in respect of claims in excess of \$25,000, to which it responds, in accordance with its Memorandum of Operations. The Liquidator regularly consults with PACICC concerning the progress of the estate.

U.S. Liquidator

49. As discussed, based on the information currently available, there will be a surplus after payment of all liabilities of Reliance (Canada). This will ultimately be payable to the Reliance estate. Therefore, the U.S. Liquidator has an on-going interest in the administration of Reliance (Canada). Further, before the liquidation, Reliance (Canada) depended on Reliance for many services, including information services and technology. In addition Reliance underwrote insurance policies which were later allocated to Reliance (Canada), entered into reinsurance treaties which also covered Reliance (Canada) liabilities and collected reinsurance proceeds on its behalf, and had ultimate decision-making power for setting Reliance (Canada)'s claims reserves and settlement.

50. To prevent disruption to the administration of Reliance (Canada) and in recognition of the U.S. Liquidator's financial interest in the Canadian estate, the U.S. Liquidator, the Superintendent and the Liquidator entered into the protocol dated November 28, 2001, attached as Schedule "H" (the "Protocol"), providing for cooperation with respect to use of information systems, collection of reinsurance, administration of claims, and the sale process for the policy liabilities. The Protocol remains in force and close co-operation between the liquidators continues. However, the Liquidator remains cognizant at all times of balancing the interests of all stakeholders.

Policyholders

51. The Liquidator has been in regular contact with policyholders, third party claimants and counsel concerning the financial status of the estate, particularly with respect to both the timing and quantum of future distributions. The Liquidator recognizes the difficulties the liquidation poses, particularly at the time of claims settlement discussions, and has been as open and helpful as appropriate in the circumstances.

Reinsurers

52. The Liquidator has also been in regular contact with reinsurers, not only in respect of its collection efforts, but also to make information available and to respond to their legitimate concerns respecting primarily the inter-relationship between the Canadian and U.S. estates.

D. Summary of Activities

53. In summary, the Liquidator's major activities for the Three Quarters included:

- a) Claims adjudication and administration – including:
 - (i) overseeing payment of defense and adjustment costs;
 - (ii) overseeing a comprehensive review of all claims including estimating range of possible outcomes;
 - (iii) engaging in extensive discussions with policyholders, claimants and their counsel concerning the estate, including its financial status; and
 - (iv) settling or otherwise resolving 2,949 claims having a value of \$25.8 million.

- b) Reinsurance, including:
 - (i) reconciling accounts;
 - (ii) enforcing liquidation clause;
 - (iii) clarifying set-off issues;
 - (iv) entering into agreements with reinsurers and the U.S. Liquidator to facilitate collection of both the Canadian and the International Reinsurance; and
 - (v) collecting receivables, including direct communication with reinsurers and cooperative efforts with the U.S. Liquidator;

- c) Reviewed and amended as necessary the investment policy, managed investments, considered, and continues to consider, investment options including the retention of an investment manager;
- d) Reported regularly to PACICC and the U.S. Liquidator;
- e) Performed extensive review of policy liabilities as at March 31, 2004;
- f) Maintained external website; and
- g) Moved office to new premises at expiration of lease.

VII. LIQUIDATOR'S ACCOUNTS AND PROFESSIONAL FEES

A. Financial Statements

54. The Liquidator does not consider that a traditional statement of receipts and disbursements would provide a meaningful and informative reflection of the financial position of the estate. The Liquidator has therefore prepared unaudited financial statements, attached as Schedule "F".

55. The financial statements have been prepared in a manner consistent with the statements approved by this Court on December 18, 2003. The Liquidator maintains a system of internal controls to safeguard the assets and the reliability of the financial reporting process.

B. Professional Fees

56. The Liquidator retains professional advisors to assist in the administration of the liquidation from time to time. The Liquidator is familiar with the services provided by each of the professional advisors and has reviewed their invoices. Detailed invoices were timely received and carefully reviewed in detail by senior administrative and management level members of the Liquidator's staff. The invoices were reviewed for accuracy, adequate detailed information describing the work performed and by whom, the time spent and when it was spent, the rate and amount billed, possible duplicative charges, reasonableness and overall compliance

with the terms of retention. Clarifications and adjustments of items included in the invoices were requested where it appeared appropriate.

57. The Liquidator believes that the Professional Fees of its advisors are proper, fair and reasonable and were incurred in furtherance of the best interests of the estate of Reliance (Canada).

Goodmans LLP

58. Goodmans LLP (“Goodmans”) has acted as counsel to KPMG Inc. from the commencement of the liquidation and has acted or advised on all matters described in this report. The Liquidator is familiar with its services and has reviewed its invoices in detail and with the care described above.

59. At the commencement of the liquidation, Goodmans agreed to a discount from its then current market rates of approximately 15% to 20%, with rates not to be increased for one year. In fact, rates were not increased for the first two years of the liquidation, but were raised by 4.79% since the last passing, effective October 1, 2003, reflecting the change in the Consumer Price Index over the two year period. The discount from current rates is approximately 20% to 40%.

60. Attached as Schedules “I”, “J” and “K”, respectively, are:

- a) a summary invoice from Goodmans to the Liquidator for each of the Three Quarters;
- b) a summary for each of these periods of the hours and average hourly rates of each of Goodmans’ personnel who dedicated more than 30 hours to the estate; and
- c) a brief description of the areas of concentration of each of Goodmans’ personnel who dedicated more than 30 hours to the estate.

61. Detailed supporting records, including time sheets, are available should this Court wish them produced. An affidavit attesting to the accuracy of the fees and disbursements is also being filed.

62. The Liquidator is satisfied that Goodmans' fees are proper, fair and reasonable, that time was appropriately spent and that Goodmans' fees were incurred in furtherance of the best interests of the estate.

KPMG Inc.

63. The Liquidator has kept careful and detailed records of all time spent by Liquidator personnel on the estate. The Liquidator has instituted internal controls to ensure no duplicative or inappropriate charges are made. The Liquidator applied the same standard for review to its accounts as to accounts of other professionals, described above. As discussed above, the Liquidator maximized efficiency and reduced costs by retaining former Reliance (Canada) employees and third party administrators where prudent and appropriate.

64. At the commencement of the liquidation, the Liquidator agreed to a discount from its then current market rates of approximately 15% to 20%, with rates not to be increased for one year. In fact, rates were not increased for the first two years of the liquidation, but were raised by 4.79% since the last passing, effective October 1, 2003, reflecting the change in the Consumer Price Index over the two year period. The discount from current rates is approximately 15% to 40%.

65. Attached as Schedules "L", "M" and "N", respectively, are:

- a) an invoice from the Liquidator to the estate for the Three Quarters;
- b) a summary for each of these periods of the hours and average hourly rates of each of the Liquidator's personnel who dedicated more than 30 hours to the estate; and
- c) a brief description of the areas of concentration of each of the Liquidator's personnel who dedicated more than 30 hours to the estate for each of the Three Quarters.

66. Detailed supporting records, including time sheets, are available should this Court wish them produced. An affidavit attesting to the accuracy of the fees and disbursements is also being filed.

67. The Liquidator respectfully requests that this Court pass the accounts of the Liquidator, as reflected in the financial statements, and approve the Professional Fees.

VIII. SECOND DISTRIBUTION

A. Scheme of Distribution

68. Section 161 of the *Winding-up and Restructuring Act* sets out the scheme of priorities in the liquidation of insurance companies. Since Reliance carried on business in Canada as a branch, regard must be had to the foreign insurance company provisions, subsections 161(6) through (9). Because Reliance (Canada) wrote only property and casualty insurance and not life insurance, subsections 161(7) and (8) are not relevant. For purposes of this distribution, the relevant priorities are:

- a) costs of the liquidation;
- b) policyholders for loss claims. The policies in force at the commencement of the liquidation have not been cancelled, so it is not necessary to address the ranking of unearned premium at this time; and
- c) ordinary creditors.

B. Approach to Distribution

69. As with the First Distribution, the Liquidator has introduced further elements of conservatism, beyond those in the loss projection methodology, for purposes of reaching its recommendations with respect to this distribution, including:

- a) All costs for the completion of the liquidation have been estimated on a very conservative basis;

- b) Reserves have been taken for certain policies at their full limits, and notwithstanding that claims have not been asserted at limits; and
- c) Two major sources of uncertainty remain in the estate: reinsurance and Non-Booked Claims. To deal with these uncertainties in this distribution, the Liquidator is ascribing no value to reinsurance that has not been paid, and is building into the assumptions conservative values for the Non-Booked Claims.

70. The Liquidator is also taking into account \$5.1 million collected on reinsurance since June 30, 2004.

71. Based on the foregoing and in light of the remaining uncertainties described above, the Liquidator recommends a further distribution of 25% of valid policyholder loss claims, bringing the total distributions to 50%. This distribution level is conservative. There is no realistic scenario under which this distribution would prejudice any party. Since some of the Resolved Claims that exceed Policy Payments are substantial, the Liquidator considers that this dividend is appropriate and represents a fair balancing of interests.

C. Calculation of Dividends

72. If the Second Distribution is approved by the Court, each claimant's dividend will be calculated by deducting from the amount to which it would otherwise be entitled any Policy Payments it received before the date of the distribution, in accordance with paragraph 12 of the Appointment Order. In effect, those Policy Payments are treated as advances on the distribution. The Liquidator will pay the higher of the Policy Payments and the total distributions on valid policyholder claims.


73. PACICC compensated claims are deemed to be assigned to PACICC under paragraph 15 of the Appointment Order. However, the Liquidator has made the PACICC Policy Payments, which were treated as a loan to PACICC under the loan agreement dated the 3rd day of December 2001, approved by this Court in the Appointment Order. The distributions reduce the amount outstanding thereunder.

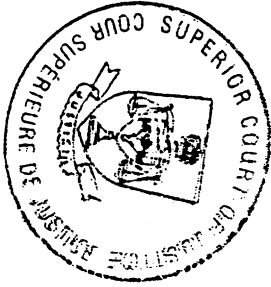
IX. RECOMMENDATIONS

74. Based on the past history of Reliance (Canada), the experience since the commencement of the liquidation, and the extensive work performed by the actuaries, the Liquidator remains of the view that Reliance (Canada) will pay all valid policyholder claims in full. However, the Liquidator is not now in a position to pay all claims in full. Accordingly, the Liquidator recommends that this Court approve the Second Distribution of 25% on all valid and allowed loss claims, to be calculated as set out above, bringing total distributions to 50%, as claims are allowed.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

KPMG INC., the Liquidator of Reliance Insurance
Company – Canadian Branch

Per: 
Robert O. Sanderson, President



**ONTARIO
SUPERIOR COURT OF JUSTICE**

COMMERCIAL LIST

THE HONOURABLE) MONDAY THE 3RD DAY
)
MR. JUSTICE FARLEY) OF DECEMBER, 2001
)
)

**IN THE MATTER OF
RELIANCE INSURANCE COMPANY**

**AND IN THE MATTER OF THE
*INSURANCE COMPANIES ACT, S.C. 1991, C.47, AS AMENDED***

**AND IN THE MATTER OF THE
*WINDING-UP AND RESTRUCTURING ACT, R.S.C. 1985, C.W-11, AS AMENDED***

B E T W E E N:

THE ATTORNEY GENERAL OF CANADA

Applicant

- and -

RELIANCE INSURANCE COMPANY

Respondent

ORDER

THIS APPLICATION made by the Applicant was heard this day without a jury at Toronto, in the presence of counsel for the Applicant, for the Respondent, for KPMG Inc., and for the Property and Casualty Insurance Compensation Corporation ("PACICC"), no one opposing.

ON READING the Notice of Application and the evidence filed by the parties, and on hearing submissions of counsel for the parties:

1. THIS COURT ORDERS that the service of the Notice of Application and the materials herein be and it is hereby good and sufficient notice thereof and that any further service of the Notice of Application and materials herein be and it is hereby dispensed with.

2. THIS COURT ORDERS that KPMG Inc. be and is hereby appointed as provisional liquidator (the "Liquidator") of the insurance business in Canada of the Respondent, including the assets in Canada of the Respondent, together with its other assets held in Canada under the control of its chief agent, including, without limitation, all amounts received or receivable in respect of its insurance business in Canada ("Reliance (Canada)").

3. THIS COURT ORDERS that the giving of security by the Liquidator upon its appointment as liquidator be dispensed with.

4. THIS COURT ORDERS that all moneys belonging to Reliance (Canada) received by or on behalf of the Liquidator and its agents shall be paid into a chartered bank to the account of the Liquidator immediately after the receipt thereof and an account or accounts shall be opened immediately, provided, however, that the Liquidator shall have the discretion to deposit funds to and use the bank accounts currently in the name of or operated by Reliance (Canada).

5. THIS COURT ORDERS that any cheques or drafts in respect of policies, issued by Reliance (Canada) prior to the making of the winding-up order herein and which are presented for payment thereafter, may be paid out of the estate and effects of Reliance (Canada).

6. THIS COURT ORDERS that the amount recoverable from, due or owed by any reinsurer to Reliance (Canada) shall be paid to the Liquidator and shall not be reduced as a result of this Order or the winding-up order, notwithstanding any terms or contractual agreement to the contrary, and that any payment made directly by a reinsurer to an insured or other creditor or claimant of Reliance (Canada) or Reliance Insurance Company shall not diminish or reduce or affect such reinsurer's obligation to Reliance (Canada).

7. THIS COURT ORDERS that the Liquidator is authorized to cure such defaults and effect such arrangements as may be required to reinstate such reinsurance affecting the operations of Reliance (Canada), as the Liquidator deems to be in the interest and for the protection of policyholders, creditors and claimants of Reliance (Canada).

8. THIS COURT ORDERS that the Liquidator may pay all valid policyholder claims, including claims in respect of unearned premiums, to the amount of \$25,000 or the amount, if any, of the voluntary compensation payment of PACICC which may be paid under the terms of its Memorandum of Operations (the "PACICC Voluntary Compensation Payment") until April 30, 2002 or such later date as this Court may order, subject to paragraph 9 hereof, and such payments shall be deemed for all purposes to have been payments made on account of claims in the course of the liquidation of Reliance (Canada).

9. THIS COURT ORDERS that the Liquidator may pay all valid claims including claims in respect of unearned premiums under the Meridian and other warranty and surety programs to the amount of \$5,000 or the amount, if any, of the PACICC Voluntary Compensation Payment until January 31, 2002 or such later date as this Court may order, and such payments shall be deemed for all purposes to have been payments made on account of claims in the course of the liquidation of Reliance (Canada).

10. THIS COURT ORDERS that the Liquidator may, after consultation with the Inspectors, make such other payments as the Liquidator in the Liquidator's discretion deems advisable in the circumstances in respect of policies of Reliance (Canada) and such payments shall be deemed for all purposes to have been payments made on account of claims in the course of the liquidation of Reliance (Canada).

11. THIS COURT ORDERS that in addition to the payments referred to in paragraphs 8 and 10, until April 30, 2002 or such later date as this Court may order, the Liquidator may pay and continue to pay all reasonable legal and other costs, incurred to and including April 30, 2002, which Reliance (Canada) is obligated to pay for defending any insureds against losses under Reliance (Canada)'s policies in accordance with the applicable policy ("Defence Costs"), subject to the applicable terms and limits of such policies. For greater certainty, all payments of Defence Costs shall be deemed for all purposes to have been payments made on account of claims in the course of the liquidation of Reliance (Canada) and to form part of the expenses of the liquidation as a first charge on the assets of the estate. However, if the applicable policy so provides, such payments shall be taken into account in determining the amount which would otherwise be distributed to the respective policyholders and claimants, or otherwise paid on account of Defence Costs, as the case may be, at such time as any further distributions or similar arrangements are made in respect of their policies.

12. THIS COURT ORDERS that any payments made by the Liquidator pursuant to paragraphs 5, 8, 9, 10 and 11 hereof, other than payments made pursuant to clerical errors (the "Payments"):

- (a) shall be deemed to be payments made on account of claims in the liquidation of Reliance (Canada) and shall be deducted from the amount which would otherwise

be distributed at such time as further distributions or similar arrangements are made in respect of such claims;

- (b) shall be deemed to have been made in accordance with this Order;
- (c) in respect of any policy shall not obligate the Liquidator to make further payments in respect thereof; and
- (d) which may have exceeded the ultimate amount which the Liquidator determines is available for distribution to the respective policyholders and claimants, or available for payment of Defence Costs, as the case may be, (collectively, the “Overpayments”) shall be deemed not to be preferences and shall not be repayable by the recipients or policyholders.

Neither the Liquidator nor the Liquidator’s agents, advisers or employees shall be liable to any person in respect of the Overpayments.

13. THIS COURT ORDERS that PACICC, which shall designate from time to time one or more persons as its representative, and the Insurance Commissioner of the Commonwealth of Pennsylvania in her capacity as Liquidator of the Respondent or her designee are appointed inspectors (collectively the "Inspectors") to assist and advise the Liquidator in the winding-up of Reliance (Canada).

14. THIS COURT ORDERS that the Inspectors may apply to this Court on motion for directions concerning any matter relating to the liquidation of Reliance (Canada).

15. THIS COURT ORDERS that each claim in respect of which PACICC makes a PACICC Voluntary Compensation Payment (a “Compensated Claim”) shall be deemed to be and

shall hereby be assigned in its entirety to PACICC without specific assignment or further steps required. PACICC shall be entitled to assert each Compensated Claim in the Liquidation. Reliance (Canada) is hereby deemed to have acquiesced to the assignment of Compensated Claims provided for herein and to have received a copy of the deed of assignment. PACICC and the Liquidator shall be deemed to be and shall hereby be released and forever discharged from any and all claims, actions, losses and liabilities which any person has or may have at present or in the future with respect to each Compensated Claim.

16. THIS COURT ORDERS that, notwithstanding the provisions of paragraph 15, the Liquidator may make funds in the estate available to PACICC from time to time to be used by PACICC to make PACICC Voluntary Compensation Payments pursuant to the terms and conditions of the loan and services agreement made effective as of the date hereof between the Liquidator and PACICC, which is hereby approved.

17. THIS COURT ORDERS that the Liquidator is authorised and empowered to act as administrator of insurance coverage on behalf of third parties who assume all or part of the insurance risk, and to be paid the fees earned by Reliance (Canada), pursuant to the terms of the contracts between Reliance (Canada) and such third parties.

18. THIS COURT ORDERS that the Liquidator is entitled forthwith to possession of all of Reliance (Canada)'s books, accounts, securities, documents, papers, computer programs and data, registers and records of any kind ("Books and Records") and that Reliance (Canada), its present and former shareholders, directors, officers, employees, salespeople and agents, accountants, auditors, solicitors, trustees, and every person having knowledge of this Order and having possession or control of such Books and Records, do forthwith deliver over to the Liquidator or to the Liquidator's agent all such Books and Records.

19. THIS COURT ORDERS that all persons, including, without limitation, employees, brokers, legal counsel, insurance agents, third party administrators, or salespeople having access to or knowledge of the affairs of Reliance (Canada) do co-operate with the Liquidator in providing information or documents necessary or incidental to the liquidation of Reliance (Canada).

20. THIS COURT ORDERS that any entity which has custody or control of any data processing information and records (including but not limited to source documents, all types of electronically stored information, master tapes or any other recorded information) relating to Reliance (Canada), shall transfer custody and control of such records in a form readable by the Liquidator to the Liquidator as of the date of this Order, unless instructed to the contrary by the Liquidator.

21. THIS COURT ORDERS that any entity furnishing claims processing or data processing services to Reliance (Canada) shall maintain such services and transfer any such accounts to the Liquidator as of the date of this Order, unless instructed to the contrary by the Liquidator.

22. THIS COURT ORDERS that Reliance (Canada) and its Chief Agent, officers, trustees, employees, consultants, agents, and legal counsel shall: surrender peacefully to the Liquidator the premises where Reliance (Canada) conducts its business; deliver all keys or access codes thereto and to any safe deposit boxes; advise the Liquidator of the combinations or access codes of any safe or safekeeping devices of Reliance (Canada) or any password or authorization code or access code required for access to data processing equipment; and shall deliver and surrender peacefully to the Liquidator all of the assets, books, records, files, credit cards, and other property of Reliance (Canada) in their possession or control, wherever located,

and otherwise advise and cooperate with the Liquidator in identifying and locating any of the foregoing.

23. THIS COURT ORDERS that all persons, firms, corporations and other entities having agreements, whether written or oral, with Reliance (Canada) for the supply of goods or services, be and they are hereby enjoined from terminating, accelerating, suspending, modifying, determining or cancelling such agreements without the written consent of the Liquidator or leave of this Court, and that all such parties shall continue to comply with their obligations under such agreements or otherwise on terms currently provided so long as the Liquidator pays the normal prices or charges for such goods or services incurred after the date of this Order in accordance with usual payment terms or as may hereafter be negotiated by the Liquidator from time to time.

24. THIS COURT ORDERS that all persons, firms, corporations and other entities be and they are hereby enjoined from disturbing or interfering with the occupation, possession or use by the Liquidator of any premises occupied or leased by Reliance (Canada) as at November 8, 2001 except upon further Order of this Court. From November 8, 2001 and for the period of time that the Liquidator occupies any leased premises, the Liquidator shall pay occupation rent to each lessor based upon the regular monthly base rent that was previously paid by Reliance (Canada) in respect of the premises so occupied or as may hereafter be negotiated by the Liquidator from time to time.

25. THIS COURT ORDERS that all persons, firms, corporations and other entities be and they are hereby enjoined from disturbing or interfering with computer software, hardware, support and data services or with utility services, including, but not limited to, the furnishing of oil, gas, heat, electricity, water, telephone service (including at present telephone numbers used by Reliance (Canada)) or any other utilities of like kind furnished to Reliance (Canada) and they

are hereby enjoined from discontinuing or altering any such utilities or services to the Liquidator except upon further order of this Court, so long as the Liquidator pays the normal prices or charges for such goods and services incurred after November 8, 2001 as the same become due in accordance with usual payment terms or as may hereafter be negotiated by the Liquidator from time to time.

26. THIS COURT ORDERS that, without limiting the generality of the foregoing, and except upon further order of this Court having been obtained on at least 7 days' notice to the Liquidator:

- (a) all persons, firms, corporations and other entities be and they are hereby restrained from terminating, cancelling or otherwise withdrawing any licences, permits, approvals or consents with respect to or in connection with Reliance (Canada) as they were on November 8, 2001;
- (b) any and all proceedings or steps taken or that may be taken, wheresoever taken, by any person, firm, corporation or entity, including, without limitation, any of the policyholders or creditors of Reliance (Canada), suppliers, co-insurers, reinsurers, contracting parties, depositors, lessors, tenants, co-venturers or partners (hereinafter, in this paragraph "Claimants") against or in respect of Reliance (Canada) shall be and hereby are stayed and suspended;
- (c) the right of any Claimant to make demands for payment on or in respect of any guarantee or similar obligation or to make demand or draw down under any letters of credit, bonds or instruments of similar effect, issued by or on behalf of Reliance (Canada), to take possession of, to foreclose upon or to otherwise deal

with any property, wheresoever located, of Reliance (Canada) whether held directly or indirectly, as principal or nominee, beneficially or otherwise, or to continue any actions or proceedings in respect of the foregoing, is hereby restrained;

- (d) the right of any Claimant to assert, enforce or exercise any right (including, without limitation, any right of dilution, buy-out, divestiture, forced sale, acceleration, termination, suspension, modification or cancellation or right to revoke any qualification or registration), option or remedy available to it including a right, option or remedy arising under or in respect of any agreement (including, without limitation, any contract, debt instrument, guarantee, option, co-ownership agreement or any agreement of purchase or sale but not including any eligible financial contract, as defined in the *Winding-up and Restructuring Act*) to which Reliance (Canada) is a party, arising out of, relating to or triggered by the occurrence of any default or non-performance by Reliance (Canada) or the making or filing of these proceedings, or any allegation contained in these proceedings, is hereby restrained; and
- (e) all Claimants are restrained from exercising any extra judicial remedies against Reliance (Canada), including, without limitation, the registration or re-registration of any securities owned by Reliance (Canada) into the name of such persons, firms, corporations or entities or their nominees, the exercise of any voting rights attaching to such securities, the retention of any payments or other distributions made in respect of such securities, any right of distress, repossession, or consolidation of accounts in relation to amounts due or accruing due in respect of

or arising from any indebtedness or obligation of Reliance (Canada) as of the date hereof.

27. THIS COURT ORDERS that no action lies against the Liquidator, any of its affiliates (the "Affiliates") any director, officer, agent, representative or employee of the Liquidator or of the Affiliates, any entity or person (or director, officer, agent, representative or employee of any such entity or person) acting under the direction of the Liquidator, or the Inspectors or any director, officer, agent, representative or employee thereof, for anything done or omitted to be done in good faith in the administration of the liquidation of Reliance (Canada) or in the exercise of the Liquidator's powers under this Order or otherwise.

28. THIS COURT ORDERS that no suit, action or other proceeding shall be proceeded with or commenced against the Liquidator, the Affiliates, any director, officer, agent, representative or employee of the Liquidator, or of the Affiliates, any entity or person (or director, officer agent, representative or employee of any such person) acting under the direction of the Liquidator, or the Inspectors or any director, officer, agent, representative or employee thereof, except with leave of this Court and subject to such terms as this Court may impose.

29. THIS COURT ORDERS that the Liquidator may, without the approval, sanction or intervention of this Court and without previous notice to the policyholders or creditors of Reliance (Canada) or any other person,

- (a) take control of the estate and effects of Reliance (Canada) or such part thereof as the Liquidator shall determine;

- (b) bring or defend any action, suit or prosecution or other legal proceeding, civil or criminal, in the Liquidator's own name as liquidator or in the name or on behalf of Reliance (Canada), as the case may be;
- (c) carry on the business of Reliance (Canada) so far as it is necessary or incidental to the winding-up of Reliance (Canada);
- (d) lease or mortgage or otherwise realize upon the undertaking, property and assets of Reliance (Canada) or any part or parts thereof;
- (e) sell the real and personal property, effects, intangibles and choses in action of Reliance (Canada), including all or any portion of Reliance (Canada)'s contracts and products and related assets, including, without limitation, Reliance (Canada)'s lists of policyholders and customers, by public auction or private contract, and transfer the whole thereof to any person or company, or sell them in parcels;
- (f) do all acts and execute, in the name of and on behalf of Reliance (Canada), all deeds, receipts, and other documents, and for that purpose use, when necessary, the seal of Reliance (Canada), and file any elections (tax or otherwise), objections or registrations, and file any notices, all as may be necessary or desirable in the opinion of the Liquidator for the better liquidation of Reliance (Canada);
- (g) prove, rank, claim and draw dividends in the matter of the bankruptcy, insolvency or sequestration of any contributory, for any sum due to Reliance (Canada) from the contributory, and take and receive dividends in respect of the bankruptcy, insolvency or sequestration, as a separate debt due from that contributory and rateably with the other separate creditors;

- (h) draw, accept, make and endorse any bill of exchange or promissory note in the name of and on behalf of Reliance (Canada);
- (i) give discharges of mortgages and other securities, partial discharges of mortgages and other securities, and pay property taxes and insurance premiums on mortgages and other securities taken in favour of Reliance (Canada);
- (j) pay such debts of Reliance (Canada) as may be necessary to be paid in order to properly preserve and maintain the undertaking, property and assets of Reliance (Canada) or to carry on the business of Reliance (Canada);
- (k) surrender possession of any premises occupied by Reliance (Canada) and disclaim any leases entered into by Reliance (Canada);
- (l) apply for any permits, licences, approvals or permissions as may be required by any governmental or regulatory authority;
- (m) re-direct Reliance (Canada)'s mail;
- (n) enter into any eligible financial contracts, as defined in the *Winding-up and Restructuring Act*;
- (o) take possession and control of all securities in which Reliance (Canada) has an interest (directly or indirectly) and exercise all rights that may be enjoyed by a holder of such securities including, without limitation, rights (i) that may arise by virtue of the holder being a party to a shareholder or similar agreement that may, by way of example, restrict the powers of the directors to manage or supervise the management of the business and affairs of the corporation, (ii) to receive

information, (iii) to attend at and cause to be held meetings of holders of such securities, (iv) to vote such securities for the removal or election of directors and approval of significant transactions (such as the sale or disposition of all or substantially all of the assets of such company or the winding-up, liquidation, rehabilitation, bankruptcy, receivership, restructuring or amalgamation of such company), and (v) to sell or otherwise dispose of such securities;

- (p) compromise all calls and liabilities to calls, debts and liabilities capable of resulting in debts, and all claims, demands and matters in dispute in any way relating to or affecting the assets of Reliance (Canada) or the winding-up of Reliance (Canada), on the receipt of such sums, payable at such times, and generally on such terms as are agreed on by the Liquidator;
- (q) make such compromise or other arrangements with creditors or persons claiming to be creditors of Reliance (Canada) as the Liquidator deems expedient; and
- (r) do and execute all such other things as are necessary for, or incidental to the winding-up of the affairs of Reliance (Canada), including without limitation entering into agreements incurring obligations.

30. THIS COURT FURTHER ORDERS that the Liquidator may, with the approval of this Court and on such notice as the Court may direct:

- (a) arrange for the transfer or reinsurance of all or a portion of the policies of Reliance (Canada); and
- (b) cancel all or a portion of the outstanding policies of Reliance (Canada).

31. THIS COURT ORDERS that the Liquidator and any of the Liquidator's agents, officers, directors, representatives or employees shall be deemed not to be an employer or a successor employer of the employees of Reliance (Canada) within the meaning of the *Pension Benefits Act* (Ontario), *Employment Standards Act* (Ontario), the *Labour Relations Act* (Ontario) or any other Federal, Provincial or Municipal legislation governing employment or labour standards or any other statute, regulation or rule of law or equity for any purpose whatsoever and, further, that the Liquidator and any of the Liquidator's agents, directors, officers, representatives or employees shall not be and shall be deemed not to be, in possession, charge or control of the property or business or affairs of Reliance (Canada) pursuant to any Federal, Provincial or Municipal legislation, statute, regulation or rule of law or equity which imposes liability on the basis of such status including, without limitation, the *Environmental Protection Act* (Ontario), the *Canadian Environmental Protection Act*, or the *Ontario Water Resources Act*, and this shall be binding on all tribunals and administrative bodies.

32. THIS COURT ORDERS that the Liquidator may retain, employ or engage such actuaries, accountants, financial advisors, investment dealers, solicitors, attorneys, valuers or other expert or professional persons as the Liquidator deems necessary or desirable to assist the Liquidator in fulfilling the Liquidator's duties, and all reasonable and proper expenses which the Liquidator may incur in so doing shall be costs of liquidation of Reliance (Canada).

33. THIS COURT ORDERS that the Liquidator may act on the advice or information obtained from any actuary, accountant, financial advisor, investment dealer, solicitor, attorney, valuer or other expert or professional person, and the Liquidator shall not be responsible for any loss, depreciation or damage occasioned by acting in good faith in reliance thereon.

34. THIS COURT ORDERS that the Liquidator shall be paid such remuneration as the Court Orders.

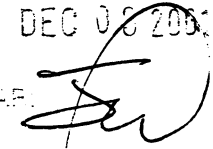
35. THIS COURT ORDERS that the Liquidator shall be at liberty to apply reasonable amounts against its remuneration, expenses and disbursements on a monthly basis and that such amounts shall constitute advances against its remuneration and expenses on, but subject to, the passing of its accounts.

36. THIS COURT ORDERS that this Order and any other orders in these proceedings shall have full force and effect in all Provinces and Territories in Canada.

37. THIS COURT SEEKS AND REQUESTS the aid and recognition of any Court or administrative body in any Province or Territory of Canada and any Canadian Federal Court or administrative body and any Federal or State Court or administrative body in the United States of America and any Court or administrative body in the United Kingdom or elsewhere to act in aid of and to be complementary to this Court in carrying out the terms of this Order.

38. THIS COURT ORDERS that the costs of this application, including the costs of the Inspectors, are to be assessed on a solicitor and his own client basis and shall be costs of liquidation of Reliance (Canada).

39. THIS COURT ORDERS that interested parties may apply to the Court for advice and directions on 7 days' notice to the Liquidator and the Inspectors, and that the Liquidator may at any time apply to this Court for advice and directions.

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PER/PAR



Registrar

**ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST**
Proceeding commenced at Toronto

ORDER

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Solicitors for the Applicant

**ONTARIO SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST**



THE HONOURABLE
MR. JUSTICE FARLEY

) THURSDAY, THE 26th DAY
)
) OF JUNE, 2003

**IN THE MATTER OF
RELIANCE INSURANCE COMPANY**

**AND IN THE MATTER OF THE
INSURANCE COMPANIES ACT, S.C. 1991, C.47, AS AMENDED**

**AND IN THE MATTER OF THE
WINDING-UP AND RESTRUCTURING ACT, R.S.C. 1985, C.W-11, AS AMENDED**

BETWEEN:

THE ATTORNEY GENERAL OF CANADA

Applicant

- and -

RELIANCE INSURANCE COMPANY

Respondent

ORDER

THIS MOTION, brought by KPMG Inc., liquidator (the "Liquidator") of the insurance business in Canada of Reliance Insurance Company ("Reliance (Canada)"), was heard this day at 393 University Avenue, Toronto, Ontario.

ON READING the Report of the Liquidator dated June 20, 2003, filed, the Order of this Court dated December 3, 2001 appointing the Liquidator (the "Appointment Order") and the Orders of this Court dated January 30, 2002, April 29, 2002, May 8, 2002, December 6, 2002

and March 26, 2003 (collectively the "Extension Orders"), and on hearing submissions of counsel for the Liquidator and counsel for Maritime Road Development Corporation, no one else appearing although properly served as appears from the proof of service filed:

1. **THIS COURT ORDERS** that the service of the Notice of Motion and materials herein is good and sufficient service of this motion, that the motion is properly returnable before this Court and that further service thereof upon any interested party other than those parties served be and is hereby dispensed with.

2. **THIS COURT ORDERS** that paragraphs 8, 9 and 11 of the Appointment Order, amended by the Extension Orders, are hereby further amended *nunc pro tunc* to extend the date of June 30, 2003 to December 31, 2003 or such later date as this Court may order.

3. **THIS COURT ORDERS** that the Liquidator is hereby authorized to pay a first interim distribution from the estate of Reliance (Canada) in the amount of 25% of valid and allowed policyholder loss claims, where such amount exceeds the payments authorized by paragraphs 8 and 9 of the Appointment Order.



Registrar

ENTERED AT/INSCRIT À TORONTO
ON/BOOK NO:
LE/DANS LE REGISTRE NO:

JUN 26 2003

PER/PAR:

NB

THE ATTORNEY GENERAL OF CANADA
Applicant

and

RELIANCE INSURANCE COMPANY
Respondent

Court File No: 01-CL-4313

**ONTARIO SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST**

Proceeding commenced at Toronto

ORDER

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

**IN THE MATTER OF
RELIANCE INSURANCE COMPANY**

**AND IN THE MATTER OF THE
INSURANCE COMPANIES ACT, S.C. 1991, C.47, AS AMENDED**

**AND IN THE MATTER OF THE
WINDING-UP AND RESTRUCTURING ACT, R.S.C. 1985, C.W-11, AS AMENDED**

B E T W E E N:

THE ATTORNEY GENERAL OF CANADA

Applicant

- and -

RELIANCE INSURANCE COMPANY

Respondent

**REPORT OF KPMG INC., THE LIQUIDATOR OF
RELIANCE INSURANCE COMPANY**

June 20, 2003

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**ONTARIO
SUPERIOR COURT OF JUSTICE**

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RELIANCE INSURANCE COMPANY

Respondent

June 20, 2003

I. THE MOTION

1. This report is respectfully filed in support of a motion by KPMG Inc., the liquidator (the “Liquidator”) of the insurance business of Reliance Insurance Company in Canada (“Reliance (Canada)”) for an Order:

- (a) extending the date for the Policy Payments, payment of Defence Costs and Meridian Payments (as hereinafter defined) to December 31, 2003, or such later date as this Court may order; and
- (b) approving a first interim distribution to policyholders and claimants of 25% of their valid and allowed loss claims (the “First Distribution”).

A. Overview

Extension of Payments

2. Pursuant to orders of this Court, the Liquidator has paid policyholders and claimants the following benefits since the commencement of the liquidation of Reliance (Canada):

- (a) defence costs (“Defence Costs”);
- (b) valid claims up to the greater of \$25,000 or the amount, if any, of the voluntary compensation payment of the Property and Casualty Insurance Compensation Corporation (“PACICC”) that may be paid under its Memorandum of Operations (the “Policy Payments”); and
- (c) valid claims under the Meridian program up to the greater of \$5,000 or the amount, if any, of PACICC’s voluntary payment (the “Meridian Payments”),

(collectively, the “Payments”).

A copy of the order appointing the Liquidator and authorizing the Payments is attached as Schedule “A” (the “Appointment Order”). This Court has extended the date for making the Payments from time to time, the latest extension being to June 30, 2003.

3. As set out in the Liquidator’s Report dated March 21, 2003, (the “March Report”), the Liquidator entered into a memorandum of understanding with respect to a reinsurance transaction (the “Assumption Arrangement”) that would result in a purchaser (the “Purchaser”) assuming all the policy liabilities of Reliance (Canada) at one hundred percent. The Assumption Arrangement would confer a substantial benefit on the policyholders by providing immediate access to their full benefits. However, the completion of the Assumption Arrangement is subject to a number of conditions and negotiations, the outcome of which is uncertain. A copy of the March Report is attached as Schedule “B”.

4. To avoid disruption to potential transactions and hardship to policyholders, the Liquidator recommends that the Court authorize it to continue the Payments until December 31, 2003, or such later date as the Court considers appropriate.

First Distribution

5. Although the Liquidator remains confident that, whether or not the Assumption Arrangement ultimately closes, all policyholders will receive full payment on all valid claims, the Liquidator is not in a position to make full payment at this time. To alleviate hardship to policyholders whose claims are not satisfied by the Payments, the Liquidator proposes to make an interim distribution of 25% of valid policyholder loss claims.

II. BACKGROUND

A. General Background

6. General background of Reliance (Canada) and this liquidation is set out in the March Report at paragraphs 2 through 7.

7. Attached as Schedule "C" is a copy of the loan and services agreement between PACICC and the Liquidator dated the 3rd day of December 2001 (the "Loan Agreement") which was approved by this Court in the Appointment Order. The Loan Agreement provides that the amounts paid by the Liquidator to policyholders on PACICC-covered claims are deemed to be loaned to PACICC, the aggregate amount of such payments being the "Amount Outstanding" from time to time under the Loan Agreement. Interest accrues on the Amount Outstanding at the prime rate.

B. Reliance (Canada)'s Insurance business

8. Prior to March, 2001, Reliance (Canada) was authorized to transact the following classes of insurance:

- property
- accident and sickness

- aircraft
- automobile
- boiler and machinery
- fidelity
- liability
- surety

9. Under the classes of liability insurance, Reliance (Canada) specialized in providing coverage for, among other things:

- (a) professional liability, such as for lawyers, engineers, architects, and dentists and for hospital programs and the health care industry;
- (b) directors' and officers' liability, for which Reliance (Canada) was a significant source in Canada;
- (c) pollution and environmental liability; and
- (d) product liability.

10. Some of Reliance (Canada)'s policies were "claims made." This means that claims must be reported during the policy period or within a defined period thereafter. However, a substantial portion of its policies were "occurrence" based. This means that the policies covered liabilities incurred during the policy period that may not become manifest for years. This kind of business is called "long tail". The policyholders themselves have no way of predicting what claims they may incur.

11. In October, 2000, Reliance (Canada) voluntarily stopped writing new policies and restricted its activities to dealing with claims on existing and terminated policies, and collecting receivables. Effectively, the company began winding down its business. As at the beginning of the liquidation, excluding the Meridian program, there were 16 policies still in force with all other policies having expired or been cancelled, and over 1400 claims. In addition, like all insurance companies, Reliance (Canada) had "incurred but not reported" claims for which

Reliance (Canada) will ultimately be put on notice and to which it will have to respond, primarily on the occurrence based policies.

III. EXTENSION OF PAYMENTS

A. Meridian Payments

12. As discussed in the March Report, the Liquidator entered into an agreement with St. Paul Guarantee Insurance Company, formerly London Guarantee Insurance Company (“St. Paul Guarantee”) pursuant to which St. Paul Guarantee would assume Reliance (Canada)’s liabilities under the Meridian program.

13. As the Liquidator reported, the consent of the reinsurers of the Meridian program is a condition of the Meridian transaction. While the majority of the Meridian Reinsurers are Canadian registered reinsurers, their decision makers are located in London, England. The Liquidator retained U.K. insurance counsel, Kendall Freeman (formerly D.J. Freeman), and is using the services of Reliance (Canada)’s reinsurance broker in London, AON, to assist in dealing with the Meridian Reinsurers. The Liquidator has met with the Meridian Reinsurers, has provided them with all information they have requested concerning the transaction and has been responsive to all concerns they have raised to date. Notwithstanding these efforts, the Meridian Reinsurers have not yet consented. The Liquidator is considering all options, including seeking assistance of this Court, and other negotiated resolutions.

14. The Liquidator recommends that this Court extend the date to which the Liquidator may make Meridian Payments to December 31, 2003. The Liquidator makes this recommendation because:

- (a) Assuming the Meridian Transaction closes, it would be counterproductive to interrupt payments. There would be significant costs both in communicating with the approximately 12,600 Meridian policyholders remaining to explain the interruption in the payment stream and with restarting payments after the transaction closes, which costs St. Paul Guarantee has not covenanted to pay; and

- (b) Even if the Meridian Transaction does not ultimately close, the Liquidator remains of the view that the cost of cancelling the Meridian policies is likely to exceed the cost of running them off. Therefore, it is still more beneficial to the estate to continue to make the Meridian Payments as part of a running off of the business.

15. As set out in the March Report, the Liquidator is confident, based on the information presently available to it, that the estate of Reliance (Canada) will pay all valid claims in full. However, for the reasons discussed more fully below, the Liquidator is not yet in a position to pay all policyholders 100%. The Liquidator is of the view that it is appropriate to continue the Meridian Payments at the present level whether or not the Meridian Transaction closes because the administrative costs of reducing and adjusting those payments would more than offset any cost differential if the ultimate dividend rate is less than 100%.

B. Policy Payments and Defence Costs

16. As also discussed in the March Report, the Liquidator sought qualified insurers to assume the liabilities under the balance of the policies (the “Policy Liabilities”) in exchange for the transfer of assets. The Liquidator engaged Scotia Capital Inc. and KPMG Corporate Finance Inc. as co-advisers in this process. The U.S. Liquidator has been extensively involved in the process as well.

17. In the March Report, the Liquidator advised this Court that, on November 21, 2002, it entered into a memorandum of understanding in respect of the Assumption Arrangement with the Purchaser. The Purchaser stipulated that the terms of the memorandum, including the Purchaser’s identity, are to be kept confidential at this time.

18. The memorandum of understanding for the Assumption Arrangement contemplated that a number of steps would be completed by certain dates, several of which were met. One of those steps was that the parties enter into definitive agreements by February 28, 2003. To date, no definitive agreements have been finalized. The process has taken longer than the Liquidator originally anticipated given, among other things, current market conditions, changes in

management at the assuming insurer, the necessity of negotiating changes to the structure to address certain regulatory concerns, and issues which result from the fact that Reliance (Canada) is a branch and not a subsidiary. The Liquidator remains of the view that a transfer of the Policy Liabilities to another carrier on appropriate terms will produce a substantial benefit to the policyholders and the estate in comparison to a more traditional liquidation. Therefore, the Liquidator does not propose to terminate discussions with the Purchaser even though the issues that have arisen are difficult and the Liquidator is not, at this point, optimistic that they will be resolved.

19. The Liquidator also considers it appropriate and in the best interest of the estate to continue Policy Payments and payment of Defence Costs. The payment of Defence Costs would facilitate the transaction to transfer the Policy Liabilities by easing any potential concerns of the Purchaser with respect to the standards of claims adjudication. Payment of Defence Costs also significantly reduces immediate hardship to policyholders.

20. The Liquidator does not recommend any change to the Policy Payments, subject to the changes which will arise from the approval of the first distribution. The Liquidator remains confident that, whether a transaction is consummated or not, all valid claims against Reliance (Canada) will be paid in full. However, as discussed below, there are uncertainties. The Liquidator is of the view that the present Policy Payment level balances the interests of all parties. The Liquidator recommends that the Policy Payments continue on the same basis until December 31, 2003 or such later date as this Court may order if they exceed the first distribution.

IV. FIRST DISTRIBUTION

A. Scheme of Distribution

21. Section 161 of the *Winding-up and Restructuring Act* sets out the scheme of priorities in the liquidation of insurance companies. Since Reliance carried on business in Canada as a branch, regard must be had to the foreign insurance company provisions, subsections 161(6) through (9). Because Reliance (Canada) wrote only property and casualty insurance and not life

insurance, subsections 161(7) and (8) are not relevant to the First Distribution. For purposes of this distribution, the relevant priorities are:

- (a) costs of the liquidation;
- (b) policyholders for loss claims. The policies in force at the commencement of the liquidation have not been cancelled, so it is not necessary to address the ranking of unearned premium at this time; and
- (c) ordinary creditors.

B. Financial Status of the Estate

Assets

Vested Assets

22. Reliance operated within Canada on a branch basis, with the approval of the Superintendent of Financial Institutions. The conditions for the Superintendent's approval of the operation of a branch in Canada include the vesting in trust with the Superintendent of assets having a prescribed value (the "Vested Assets"), and filings, at least annually, of financial information disclosing both assets for which the branch is entitled to take credit under the *Insurance Companies Act*, and liabilities that it is required to report as liabilities of the branch, also under the *Insurance Companies Act*.

23. As at the commencement of the liquidation the Vested Assets consisted of cash or near cash in the amount of approximately \$171 million. The Liquidator has been making the Payments and paying the costs and expenses of the liquidation. It has collected reinsurance and subrogation proceeds. As at March 31, 2003, the cash or near cash was approximately \$161 million.

Reinsurance

24. The other major asset of Reliance (Canada) is reinsurance, consisting of:

- (a) reinsurance for which Reliance (Canada) was entitled to take credit under the *Insurance Companies Act* in calculating its required assets covering only the liabilities of Reliance (Canada) (“Canadian Reinsurance”);
- (b) reinsurance entered into through Reliance’s head office, which reinsures both Reliance (Canada) policies and policies written through the U.S. operations (“International Reinsurance”) for which Reliance (Canada) was not entitled to take credit under the *Insurance Companies Act*.

25. As at March 31, 2003 approximately 51% of Reliance (Canada)’s gross case reserves were reinsured. Of this amount, approximately 89% is Canadian Reinsurance and 11% is International Reinsurance. However, these percentages change as the composition of the case reserves changes. The Liquidator estimates that, over time, the International Reinsurance will likely account for at least 20% of the reinsurance, the balance being Canadian. These percentages do not reflect our estimates for uncollectible reinsurance due to credit, collection or contractual risk. Over 88% of the reinsurance is with reinsurers rated “A” or higher.

26. The Liquidator has collected approximately \$5.4 million in reinsurance since the beginning of the liquidation. The U.S. Liquidator has collected International Reinsurance in the amount of \$4.1 million on behalf of Reliance (Canada), which has not yet been remitted. In addition, reinsurance receivables (amounts billed to reinsurers), net of a provision for uncollectible reinsurance, were \$9.5 million as at March 31, 2003. Reinsurance recoverables (amounts referable to reported claims not yet billed and to IBNR), net of a provision for uncollectible reinsurance, were \$61.7 million.

Summary

27. In summary, as at March 31, 2003, Reliance (Canada)'s assets consisted of:

	Millions
Cash or near cash	\$161.3
Reinsurance receivables and recoverables net of estimate for uncollectible reinsurance	\$ 71.2
Miscellaneous	<u>\$ 10.0</u>
Total	<u>\$242.5</u>

Liabilities

28. In its solicitation letter provided to prospective purchasers, the Liquidator disclosed that the total policy liabilities according to the books and records of Reliance (Canada) were approximately \$132 million, including IBNR, as at June 30, 2001. A copy of the solicitation letter is attached as Schedule "D".

29. The Liquidator has performed further actuarial and claims reviews but is of the view that it would not be in the best interest of the estate to share those results at the present time since the Purchaser is expected to arrive at its own conclusions. In this report, the Liquidator will provide as much information concerning the liabilities as possible without prejudicing the sale, and will describe the process it has followed to reach its views concerning the proposed distribution.

No Call for Claims to Date

30. The Liquidator has not undertaken a call for claims to date and is not recommending one at this time because the Liquidator believes such a call would be expensive and counterproductive, given the long tail nature of Reliance (Canada)'s policies. Policyholders would have no choice but to file contingent claims of a magnitude that would make the claims meaningless. At the conclusion of the process, the Liquidator would still have to rely on

actuarial projections to reach a view as to the total claims exposure of the estate, and would certainly have to do so to make a distribution in a reasonable time frame.

Loss Claims

31. There are basically three categories of loss claims:

- (a) Claims that are settled or otherwise resolved (the “Resolved Claims”). As at March 31, 2003:
 - (i) approximately 8,670 claims having a total value of \$22.6 million have been resolved, through settlement or otherwise, since the beginning of the liquidation;
 - (ii) of those, approximately 8,660 claims, having a value of approximately \$12.1 million, have been paid in full in accordance with the court authorized payments;
 - (iii) the remaining 10 claims either do not qualify for PACICC coverage or exceed PACICC limits. Policy Payments have been made on account of these claims but a balance of \$10.5 million remains outstanding.
- (b) claims which have been reported but not yet resolved (the “Reported Claims”). As at March 31, 2003, there were outstanding approximately 757 Reported Claims with outstanding gross case reserves of approximately \$51.5 million. Case reserves are adjusted as additional information on the estimated amount of a claim becomes known during the course of its settlement; and
- (c) the provision for claims incurred but not yet reported and for deficiencies in Reported Claims (“IBNR”).

Liability Claims Projection Process

32. The Liquidator has undertaken an extensive review of the policy liabilities, including retaining the services of the consulting actuary who acted for Reliance (Canada) for more than

12 years before it was wound up. The projections have been further reviewed by the Liquidator's own actuaries.

33. Actuarial projections typically consider:

- (a) the current level of reserves;
- (b) the history of claims development;
- (c) the nature of the liabilities underwritten and the terms of the policies;
- (d) industry experience and current developments with respect to similar kinds of policies and liabilities; and
- (e) the potential for adverse deviation, a provision against claims developing negatively in comparison to past experience.

34. Actuaries then reach a view as to the total policy liabilities to which the insurer will be exposed, including a provision for IBNR. While the actuaries generally provide a single best estimate, there is clearly a range for valuing the total liabilities, depending on the degree of certainty to be achieved. For instance, in some circumstances, it would be within accepted actuarial standards to indicate a best estimate with a 55% degree of confidence, meaning that the liabilities would exceed the estimate 45% of the time and be less 54% of the time. More conservative assumptions would lead to higher confidence levels. In going concern situations, this may be considered appropriate.

35. The Liquidator has asked the actuaries to confirm their best estimate of the policy liabilities in accordance with accepted actuarial standards. The Liquidator has carefully reviewed the assumptions underlying the actuarial estimates. The Liquidator has introduced further elements of conservatism for purposes of reaching its recommendations with respect to this distribution, including:

- (a) All costs for the completion of the liquidation have been estimated on a very conservative basis;

- (b) Reserves have been taken for certain policies at their full limits, and notwithstanding that claims have not been asserted at limits; and
- (c) As the Liquidator advised the court in the March Report, two major sources of uncertainty remain in the estate: reinsurance recoverables and non-booked claims. These are discussed in the March Report at paragraphs 26 through 31. To deal with these uncertainties in this distribution, the Liquidator is ascribing no value to the receivables, including the reinsurance recoverables, and is building into the assumptions very conservative values for the non-booked claims.

36. Based on the foregoing and in light of the remaining uncertainties described above, the Liquidator recommends a distribution of 25% of valid policyholder loss claims. This distribution level is highly conservative. There is no realistic scenario under which this distribution would prejudice any party. Since some of the Resolved Claims that exceed Policy Payments are substantial, the Liquidator considers that this dividend is appropriate and represents a fair balancing of interests.

C. Calculation of Dividends

37. If the First Distribution is approved by the Court, each claimant's dividend will be calculated by deducting from the amount to which it would otherwise be entitled any Policy Payments or Meridian Payments it received before the date of the distribution, in accordance with paragraph 12 of the Appointment Order. In effect, those payments are treated as advances on the distribution. In the future, the Liquidator will pay the higher of the Meridian Payments or Policy Payments on valid policyholder claims.

38. PACICC-compensated claims are deemed to be assigned to PACICC under paragraph 15 of the Appointment Order. However, the Liquidator has made the PACICC payments, which were treated as a loan to PACICC under the Loan Agreement. The First Distribution will, therefore, reduce the Amount Outstanding.

V. RECOMMENDATIONS

39. Based on the past history of Reliance (Canada), the experience since the commencement of the liquidation, and the extensive work performed by the actuaries, the Liquidator remains of the view that Reliance (Canada) will pay all valid policyholder claims in full. However, the Liquidator is not now in a position to pay all claims in full. Accordingly, the Liquidator recommends that:

- (a) the Payments be extended to December 31, 2003 or such other date as this Court may order; and
- (b) this Court approve the First Distribution of 25% on all valid and allowed loss claims, to be calculated as set out above.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

KPMG INC., solely in its capacity as the
Liquidator of Reliance Insurance Company -
Canadian Branch

Per: 
Robert G. Sanderson, President

Schedule "D"

Court File No. 01-CL-4313

ONTARIO SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

THE HONOURABLE) THURSDAY, THE 18th DAY
)
MR. JUSTICE FARLEY) OF DECEMBER, 2003



IN THE MATTER OF
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AND IN THE MATTER OF THE
INSURANCE COMPANIES ACT, S.C. 1991, C.47, AS AMENDED

AND IN THE MATTER OF THE
WINDING-UP AND RESTRUCTURING ACT, R.S.C. 1985, C.W-11, AS AMENDED

BETWEEN:

THE ATTORNEY GENERAL OF CANADA

Applicant

- and -

RELIANCE INSURANCE COMPANY

Respondent

ORDER

THIS MOTION, brought by KPMG Inc., liquidator (the "Liquidator") of the insurance business in Canada of Reliance Insurance Company ("Reliance (Canada)"), was heard this day at 393 University Avenue, Toronto, Ontario.

ON READING the Report of the Liquidator dated December 12, 2003 (the "Report"), filed, the Order of this Court dated December 3, 2001 appointing the Liquidator (the

"Appointment Order"), and on hearing submissions of counsel for the Liquidator, no other party appearing, although properly served as appears from the proof of service filed:

1. **THIS COURT ORDERS** that the service of the Notice of Motion and materials herein is good and sufficient service of this motion, that the motion is properly returnable before this Court and that further service thereof upon any interested party other than those parties served be and is hereby dispensed with.

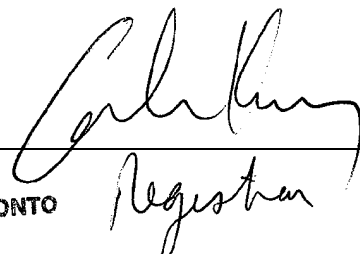
2. **THIS COURT ORDERS** that the accounts of the Liquidator for the periods December 3, 2001 to December 31, 2002 and January 1, 2003 to September 30, 2003, as reflected in the financial statements of Reliance (Canada) attached to the Report, and the fees and disbursements of the Liquidator, and of its counsel, Goodmans LLP, from the commencement of the liquidation to September 30, 2003, be and they are hereby passed and approved as submitted.

3. **THIS COURT ORDERS** that paragraphs 8, 9 and 11 of the Appointment Order, as amended by further orders of this Court, are hereby further amended *nunc pro tunc* to extend the date of December 31, 2003 to June 30, 2004 or such later date as this Court may order.

4. **THIS COURT ORDERS** that any claims payable in foreign currency shall be converted to Canadian currency at the Bank of Canada noon spot rate of exchange for exchanging such currency to Canadian currency on November 8, 2001.

ENTERED AT / INSCRIT À TORONTO
ON/BOOK NO:
LE/DANS LE REGISTRE NO:
DEC 18 2003

PER/PAR:


Register

ONTARIO SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST
Proceeding commenced at Toronto

ORDER

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Liquidator of Reliance (Canada)

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**REPORT OF KPMG INC., THE LIQUIDATOR OF
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December 12, 2003

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- and -

RELIANCE INSURANCE COMPANY

Respondent

December 12, 2003

I. NATURE OF THE MOTION

1. This report is respectfully submitted in support of a motion by KPMG Inc., the liquidator (the "Liquidator") of the insurance business of Reliance Insurance Company in Canada ("Reliance (Canada)") (as hereinafter defined) for an Order:

- (a) passing the accounts of the Liquidator for the periods December 3, 2001 to December 31, 2002 and January 1, 2003 to September 30, 2003, (collectively, the "Periods") as reflected in the financial statements of Reliance (Canada), and approving the professional fees of the Liquidator and of its counsel, Goodmans LLP (the "Professional Fees") from the commencement of the liquidation to September 30, 2003;

- (b) extending the date for the Policy Payments, payment of Defence Costs and Meridian Payments (as hereinafter defined) to June 30, 2004 or such later date as this Court may order; and
- (c) fixing the exchange rate at which claims payable in foreign currencies are to be converted to Canadian currency at the Bank of Canada noon spot rate of exchange for that currency on November 8, 2001.

II. GENERAL BACKGROUND

A. Liquidation Orders

2. Reliance Insurance Company (“Reliance”) is a property and casualty insurer in the United States of America, domiciled in the Commonwealth of Pennsylvania. Reliance carried on business in Canada as a “foreign company” within the meaning of the *Insurance Companies Act* through a branch. In October, 2000, Reliance (Canada) stopped issuing new policies and began “running off” or winding down its existing business.

3. Reliance was ordered liquidated by Order of the Commonwealth Court of Pennsylvania dated October 3, 2001, under the Pennsylvania *Insurance Department Act of 1921*. M. Diane Koken, Commissioner of Insurance for Pennsylvania, was appointed liquidator (the “U.S. Liquidator”).

4. By Order of this Court made December 3, 2001 (the “Winding-up Order”), the insurance business of Reliance (Canada) was ordered wound-up pursuant to the provisions of the *Winding-up and Restructuring Act*. A copy of the Winding-up Order is attached as Schedule “A”.

5. By further Order of this Court made December 3, 2001 (the “Appointment Order”), KPMG Inc. was appointed provisional liquidator. A copy of the Appointment Order is attached as Schedule “B”.

6. The relevant provisions of the Appointment Order for the purposes of this motion are:

- (a) paragraph 8 provides that the Liquidator may pay all valid policyholder claims, including claims in respect of unearned premiums, to the amount of \$25,000 or

the amount of the coverage limits of the Property and Casualty Insurance Compensation Corporation (“PACICC”) if any (the “Policy Payments”), until April 30, 2002 or such later date as the Court may order, subject to paragraph 9 of the Appointment Order, and that such payments are deemed to be payments made on account of claims in the liquidation;

- (b) paragraph 9 provides that the Liquidator may pay all valid claims, including claims in respect of unearned premiums, under the Meridian Warranty Program and other warranty and surety programs to the amount of \$5,000 or the PACICC coverage limits, if any (the “Meridian Payments”), until January 31, 2002 or such later date as the Court may order, and that such payments are deemed to be payments made on account of claims in the liquidation;
- (c) paragraph 11 provides that the Liquidator may pay and continue to pay all reasonable legal and other costs, incurred to and including April 30, 2002 that Reliance (Canada) is obligated to pay for defending any insureds against losses under Reliance (Canada)’s policies in accordance with the applicable policy, subject to the terms and limits of such policies (the “Defence Costs”); and
- (d) paragraph 30 provides that the Liquidator may, with the approval of this Court, arrange for the transfer or reinsurance of all or a portion of the policies of Reliance (Canada) and cancel all or a portion of the outstanding policies of Reliance (Canada).

7. By various Orders, this Court extended the date to which the Liquidator was authorized to make the Policy Payments and the Meridian Payments and to pay the Defence Costs (collectively, the “Payments”) to December 31, 2003.

B. Inspectors

8. In the Appointment Order this Court appointed the U.S. Liquidator and PACICC as inspectors. By order dated January 30, 2002, this Court ordered that the Superintendent of Financial Institutions may attend meetings of inspectors, be included in the service list, and attend and be heard in matters before this Court.

9. The inspectors and the Superintendent are not opposing this motion.

C. First Distribution

10. This Court approved a first interim distribution to policyholders and claimants of 25% of their valid and allowed claims on June 26, 2003. Policyholders and claimants therefore receive the higher of the Policy Payments, the Meridian Payments, and the first distribution.

III. OVERVIEW OF THE ESTATE

A. Summary of Current Status

11. The Liquidator has made progress in the resolution of claims and collection of reinsurance and remains confident that the estate will pay all claimants in full, although there are still many uncertainties. As at September 30, 2003, the estimated surplus on the financial statements was \$52.9 million.

12. A transfer of the policy liabilities to a solvent insurer would have expedited the payment of full benefits. However, it is now clear that this cannot be achieved in the current market and until certain issues, including those surrounding the International Reinsurance (as hereinafter defined), are resolved. The proposed assumption transaction for the Meridian program, described below, is no longer advantageous to the estate, given difficulties with the reinsurers. However, the Liquidator will remain open to opportunities to transfer the liabilities.

13. The Liquidator will continue the run-off of Reliance (Canada)'s business in an orderly manner, dealing with policy liabilities and collection of reinsurance on a commercially reasonable basis, seeking the approval of the Court for further interim distributions as appropriate. Given the nature of Reliance (Canada)'s business, the process can be expected to take many years. The consulting actuary estimates that the run-off will continue to 2018, but the number of payments will begin to decline after 2007. The Liquidator will continue to monitor market conditions and use all reasonable efforts to find innovative approaches to expedite the completion of the liquidation.

B. Financial Status of Estate

Reliance (Canada)'s Business

14. Attached as Schedule "C" is a copy of the Liquidator's report dated June 20, 2003, in support of the extension of the Payments and the approval of the first interim distribution. Paragraphs 8 to 11 of that report describe Reliance (Canada)'s business. In summary, Reliance (Canada) wrote a very diverse set of policies. Within the classes of liability insurance that it wrote, Reliance (Canada) specialized in providing coverage for professional liability, directors' and officers' liability, pollution and environmental liability and product liability. While some of Reliance (Canada)'s policies were "claims made", meaning that claims must be reported during the term of the policy or within a defined period thereafter, a substantial portion of its policies were "occurrence" based. These policies cover liabilities incurred during the policy period that may not become manifest for years. This business is called "longtail". The policyholders themselves have no way of predicting what claims they may incur. Reliance (Canada) also wrote policies with lengthy policy periods. In addition, Reliance (Canada) acted as a reinsurer for other insurers. "Assumed Reinsurance" is treated as insurance under the *Insurance Companies Act*, and is accorded the same priority as loss claims under the *Winding-up and Restructuring Act*.

15. In October 2000, Reliance (Canada) voluntarily stopped writing new policies, effectively winding down its business. At the beginning of the liquidation, excluding the Meridian program, there were 16 policies still in force with all other policies having expired or been cancelled, and over 1100 claims. In addition, Reliance (Canada) had "incurred but not reported" ("IBNR") claims for which it will ultimately be put on notice and to which it will have to respond, primarily on the occurrence-based policies.

16. As at September 30, 2003, three policies remain in force. Two are excess directors' and officers' liability policies which are currently in the extended reporting periods, during which claims incurred before the expiry of the policy may be reported. The term of the third policy and the last certificate in the Meridian program will expire in 2007.

Assets

Vested Assets

17. Reliance operated within Canada on a branch basis, with the approval of the Superintendent of Financial Institutions. The conditions for the Superintendent's approval of the operation of a branch in Canada include the vesting in trust with the Superintendent of assets having a prescribed value (the "Vested Assets"), and filings, at least annually, of financial information disclosing both assets for which the branch is entitled to take credit under the *Insurance Companies Act*, and liabilities that it is required to report as liabilities of the branch, also under the *Insurance Companies Act*.

18. As at the commencement of the liquidation, the Vested Assets consisted of cash or near cash in the amount of approximately \$171 million. The Liquidator has been making the Payments and paying the costs and expenses of the liquidation. It has collected reinsurance and subrogation proceeds. As at September 30, 2003, the cash or near cash was approximately \$156.3 million.

Reinsurance

19. The other major asset of Reliance (Canada) is reinsurance, consisting of:

- (a) reinsurance covering only the liabilities of Reliance (Canada) ("Canadian Reinsurance"); and
- (b) reinsurance entered into through Reliance's head office, which reinsures both Reliance (Canada) policies and policies written through the U.S. operations and for other entities in the Reliance Group ("International Reinsurance").

20. As at September 30, 2003 approximately 55.7% of Reliance (Canada)'s gross case reserves were reinsured. Of this amount, approximately 89.4% is Canadian Reinsurance and 11.6% is International Reinsurance. However, these percentages change as the composition of the case reserves changes. The Liquidator estimates that, over time, the International Reinsurance will likely account for at least 20% of the reinsurance, the balance being Canadian. These percentages do not reflect estimates for uncollectible reinsurance due to credit, collection

or contractual risk. Over 81.6% of the reinsurance is with reinsurers rated “A” or higher. This percentage has decreased because there have been industry wide downgrades of reinsurers.

21. The Liquidator has collected approximately \$11.8 million in Canadian Reinsurance since the beginning of the liquidation. The U.S. Liquidator has collected International Reinsurance in the amount of \$4.2 million on behalf of Reliance (Canada), which has not yet been remitted. Discussions with the U.S. Liquidator that are likely to result in an agreement with respect to this matter will be concluded in the near future. In addition, reinsurance receivables (amounts billed to reinsurers), net of a provision for uncollectible reinsurance, were \$13.9 million as at September 30, 2003. The reinsurers’ share of the provision for unpaid claims (amounts referable to reported claims and IBNR, and unearned premiums), net of a provision for uncollectible reinsurance, was \$57.1 million.

Summary

22. In summary, as at September 30, 2003, Reliance (Canada)’s assets consisted of:

	Millions
Cash or near cash	\$156.3
Reinsurance receivables and recoverables net of estimate for uncollectible reinsurance	\$ 71.1
Miscellaneous	<u>\$ 9.6</u>
Total	<u>\$237.0</u>

Liabilities

23. In its solicitation letter provided to prospective purchasers, the Liquidator disclosed that the provision for unpaid claims according to the books and records of Reliance (Canada) was approximately \$132.1 million, including IBNR, as at June 30, 2001. A copy of the solicitation letter is attached as Schedule “D”.

24. The Liquidator did not previously make public its estimates of the liabilities because prospective purchasers were being asked to reach their own conclusions based on information provided to them and the Liquidator did not want to prejudice the sale process. Given that this is

no longer a concern, the statements indicate the estimated value of the liabilities, at the respective points in time, determined as described below.

No Call for Claims to Date

25. The Liquidator has not undertaken a call for claims to date and is not recommending one at this time. The Liquidator believes such a call would not be productive at this time, given the longtail nature of Reliance (Canada)'s policies. Policyholders would likely file contingent claims of a magnitude that would make the claims meaningless. At the conclusion of the process, the Liquidator would still have to rely on actuarial estimates to reach a view as to the total claims exposure of the estate, and would certainly have to do so to make distributions in a reasonable time frame. The Liquidator will review this decision from time to time, as the estate evolves.

Claims Adjudication Process

26. The Liquidator has retained members of the Reliance (Canada) adjusting staff, who deal with claims on a day-to-day basis, regularly reporting to, and consulting with, the Liquidator and Liquidator's counsel, particularly with respect to the impact of the liquidation on claims issues, such as payment of claims in excess of PACICC limits. Defense and coverage counsel are appointed based on qualifications in particular claims areas. They report to the adjusting staff and to the Liquidator when appropriate. A process for PACICC involvement and approval of claims to which PACICC agrees to respond has been established, as well as reporting to the U.S. Liquidator, as provided for in the protocol between the two liquidators discussed later in this report.

Approved and Admitted Claims

27. At the beginning of the liquidation, there were 1,145 open claims. An additional 11,266 claims were opened to September 30, 2003, excluding certain Assumed Reinsurance. As at September 30, 2003:

- (a) Approximately 11,752 claims having a total value of \$40.34 million had been resolved, through settlement or otherwise, since the beginning of the liquidation (the “Resolved Claims”). Of the Resolved Claims:
- Approximately 526 claims were closed without payment, or had been paid but not closed prior to the liquidation;
 - Approximately 11,211 claims, having a value of approximately \$18.18 million, were paid in full in accordance with the court-authorized payments, of which approximately 10,153 were under the Meridian program and approximately 844 were under the GAP Program (described below); and
 - the remaining 15 claims either do not qualify for PACICC coverage or exceed PACICC limits. Policy Payments or the first distribution, in total \$4.89 million, have been made on account of these claims but a balance of \$17.27 million remains outstanding.

Claims Reported But Not Resolved

28. There were approximately 659 claims reported but not yet resolved (the “Reported Claims”). This does not include certain of the Assumed Reinsurance and programs such as Meridian. Case reserves are established and adjusted as information concerning the claim becomes available and based on the recommendations of the adjusting staff and defense counsel. Provision for adverse development in the case reserves is included in the IBNR.

Liability Claims Estimation Process

29. The Liquidator has undertaken an extensive review of the policy liabilities, including retaining the services of the consulting actuary who acted for Reliance (Canada) for more than twelve years before it was wound up. The estimates have been further reviewed by the Liquidator’s own actuaries.

30. Actuaries typically consider:

- (a) the current level of reserves;
- (b) the history of claims development;

- (c) the nature of the liabilities underwritten and the terms of the policies;
- (d) industry experience and current developments with respect to similar kinds of policies and liabilities; and
- (e) unexpected patterns in loss development.

31. Actuaries then reach a view as to the total policy liabilities to which the insurer will be exposed, including a provision for IBNR. While the actuaries generally provide a single best estimate, there is clearly a range for valuing the total liabilities, depending on the degree of certainty to be achieved. The Liquidator has based its estimate for policy liabilities on the actuary's best estimate. The Liquidator does not distribute on the basis of these estimates, but introduces further elements of conservatism, including taking reserves at full policy limits, notwithstanding that claims have not been asserted at those limits, and only including reinsurance actually collected in its asset values.

32. As at September 30, 2003 the Liquidator estimates total policy liabilities, including IBNR, as \$174.4 million, of which \$17.3 million is the portion of the outstanding admitted claims that will be paid as the distributions increase.

IV. MAJOR ACTIVITIES OF THE LIQUIDATOR

A. Administration

33. On being appointed, the Liquidator considered Reliance (Canada)'s complex claims, and the seniority and reputation of its employees, and consulted with the U.S. Liquidator and PACICC. The Liquidator determined that the best interests of the estate would be served by maintaining continuity, to the extent possible, through retaining existing Reliance (Canada) staff and that this would result in cost savings. At the beginning of the liquidation there were seventeen employees. As at September 30, 2003, eleven employees remained, and arrangements had been made to terminate the employment of two employees, who have since left.

34. Reliance (Canada) employees perform day-to-day administration, including instructing defence counsel and outside adjusters, dealing with counsel on coverage issues, administering

reinsurance collections, performing accounting and financial reporting with respect to claims and reinsurance issue functions, and liaising with PACICC and employees of the U.S. estate.

35. The Liquidator maintains responsibility for the conduct of the liquidation. The Liquidator is responsible for all strategic initiatives, and major decisions and, as appropriate, is involved in supervising and augmenting, where necessary, the day-to-day activities performed by former Reliance (Canada) employees. The Liquidator performs the functions specific to the liquidation, including the development of policies and procedures for claims handling and authorities, the institution of internal controls, reporting to court and stakeholders, supervising and coordinating legal counsel, monitoring developments in the U.S. liquidation, and providing insureds with information. The Liquidator reviews all claims decisions involving claims that meet criteria established in co-operation with PACICC and the U.S. Liquidator, performs the financial reporting, is actively involved in reinsurance collections, makes all investment decisions, instructs and consults with the actuary. A further summary of the Liquidator's activities is set out in paragraph 57.

B. Policy Payments and Payment of Defense Costs

36. During the control period discussed below, the Liquidator (then agent to the Superintendent of Financial Institutions) reviewed with Reliance (Canada) management and the Superintendent the financial status of Reliance (Canada). In consultation with PACICC, the Liquidator established a reasonable level for payments to policyholders and for defence costs, to prevent undue hardship, to save administrative costs associated with making dividend payments on large numbers of small claims, and to ensure that claims were properly defended to provide comfort to reinsurers, thereby expediting collection.

C. Third Party Administrators

37. Reliance (Canada) also had arrangements with third party administrators who were responsible for the administration of claims in a number of programs, the major ones including:

- (a) Meridian;

- (b) Groupe PPP, a financial guarantee program underwritten in the U.S., covering automobile dealers in Quebec;
- (c) Gap Program, a financial warranty program;
- (d) Family Program, a personal lines program in British Columbia; and
- (e) Environmental Program, administered by ECS Inc. in the United States.

38. Each of the programs is unique in respect of the volume, magnitude and complexity of its claims, and with respect to the discretion accorded the third party administrators. In each case, the Liquidator reviewed the program and the nature of the relationship between the administrator and Reliance (Canada). In assessing the continued use of the third party administrators, the Liquidator considered their cost, the potential prejudice if the administration were disrupted and the quality of their work. The Liquidator determined that it was appropriate to maintain the relationships, but introduced additional controls and reporting requirements, as it considered necessary, and regularly reviews the status of the administrations.

D. PACICC

39. The Liquidator entered into a loan and services agreement with PACICC on December 3, 2001, approved by this Court in the Appointment Order.

40. PACICC approves payments in respect of claims in excess of \$25,000, to which it responds, in accordance with its Memorandum of Operations. The Liquidator regularly consults with PACICC concerning the progress of the estate.

E. Protocol with U.S. Liquidator

41. Prior to the liquidation, Reliance (Canada) depended on Reliance for many services. For example:

- (a) Reliance underwrote insurance policies which were later allocated to Reliance (Canada);

- (b) Reliance entered into reinsurance treaties which also covered Reliance (Canada) liabilities and collected reinsurance proceeds on its behalf; and
- (c) Reliance had ultimate decision-making power for setting Reliance (Canada)'s claims reserves and settlement.

In addition, Reliance provided information services and technology to Reliance (Canada), which had no independent IT function.

42. On the making of the liquidation order in the U.S., the Superintendent of Financial Institutions took control of Reliance (Canada) under the *Insurance Companies Act*, appointed KPMG Inc. his agent to assist him in exercising his duties, and nominated KPMG Inc. to be liquidator. During the control period, the U.S. Liquidator, the Superintendent and the agent engaged in extensive discussions concerning the future administration of Reliance (Canada). The Superintendent and the agent were concerned that there be as little disruption as possible to the administration of Reliance (Canada) and that the best interests of the stakeholders of Reliance (Canada) be served. Given the dependence of Reliance (Canada) on U.S. systems, records and reinsurance, the Superintendent and agent formed the view that cooperation was clearly necessary. Further, based on all financial information available then (and now) there will be a surplus after payment of all liabilities of Reliance (Canada) which will ultimately be payable to the Reliance estate. Therefore, the U.S. Liquidator had, and has, a legitimate interest in the administration of Reliance (Canada). The Liquidator is cognizant at all times of balancing the interests of all stakeholders.

43. The U.S. Liquidator was of the view that attempts should be made to transfer the policy liabilities of Reliance (Canada) to a solvent insurer, to accelerate release of the surplus, notwithstanding that Reliance had tried to sell the branch before the liquidation, but had been unsuccessful. The Superintendent and agent agreed that such a transfer would be in the best interests of Reliance (Canada) stakeholders, and that co-operation in the sharing of information and systems was in the best interests of all stakeholders. The U.S. Liquidator, the Superintendent and the Liquidator therefore entered into the protocol dated November 28, 2001, attached as Schedule "E" (the "Protocol"), providing for cooperation with respect to use of

information systems, collection of reinsurance, administration of claims, and the sale process for the policy liabilities.

F. Attempted Sale of Policy Liabilities

44. As agreed in the Protocol, the Liquidator engaged Scotia McLeod Inc. and KPMG Corporate Finance Inc. as its financial advisors in the marketing process and cooperated in the process with the U.S. Liquidator, keeping her informed at all times, as agreed in the Protocol.

45. The Liquidator's main goals for the assumption transaction were to provide:

- (a) earlier access by policyholders and claimants to their benefits, and a greater certainty of full payment, than would be the case in a run-off by the Liquidator; and
- (b) earlier quantification of the surplus available to Reliance, and its earlier release, than in a run-off.

46. To satisfy these goals, the purchaser would have to be appropriately capitalized, so that the protection the purchaser would provide to policyholders and claimants would be at least as extensive as that provided within the estate. The cost of the assumption would also have to be at least comparable to the projected cost of a liquidation.

47. The Liquidator, with the advice of the financial advisors, engaged in extensive marketing efforts which included contacting licensed property and casualty insurers in Canada and in other jurisdictions, as well as non-traditional insurers who had shown an interest and ability to undertake run-off enterprises by providing appropriate capital, and obtaining appropriate regulatory approvals.

48. The Liquidator's clear preference was to conclude a transaction with a Canadian licensed, operating property and casualty insurer. However, no such insurer expressed interest. Three parties presented proposals. Two of them were not acceptable. The third party was partnering with a substantial participant in the insurance market that clearly had the capacity to undertake the transaction and satisfy the concerns of the Liquidator, the U.S. Liquidator and all regulatory requirements (the "Purchaser").

49. The Liquidator and Purchaser entered into extensive negotiations concerning the structure of the transaction. The Purchaser proposed a structure which included the incorporation of a new licensed insurer whose business would consist initially of the Reliance (Canada) business, with the intention to add future run-off businesses. The Liquidator and Purchaser met with and made submissions to the Office of the Superintendent of Financial Institutions in order to ascertain whether such a structure would be, at least potentially, acceptable under the provisions of the *Insurance Companies Act* since regulatory approval would be required for the transfer of the liabilities, and the proposed acquiring entity would have to be licensed under the *Insurance Companies Act*. The indications were that such a transaction and structure would be given serious consideration, and would not be rejected out of hand.

50. On November 21, 2002 the Liquidator entered into a memorandum of understanding with respect to the transaction. The Purchaser stipulated that the terms of the memorandum, including its identity, are to be kept confidential.

51. Over the course of the ensuing months, the completion of definitive agreements was delayed by a number of difficulties resulting from, among other things, market conditions, the complexity and magnitude of the remaining claims relative to the size of the estate and the fact that Reliance (Canada) is a branch and not a subsidiary, particularly with respect to the collectability of the International Reinsurance. The Liquidator reported to this Court on several occasions that it was not optimistic that the issues would be resolved, but, because of the substantial benefit to the policyholders and the estate in concluding an agreement, carried on discussions as long as there was some possibility of a deal. The Liquidator remained of the view throughout the process that the Purchaser was negotiating in good faith, that its concerns were of substance, and that serious efforts were being made by all parties, including the U.S. Liquidator and the Purchaser, to resolve the issues.

52. The parties have now agreed that there was no further realistic possibility for concluding a transaction and discussions ended.

G. Non-Booked Claims

53. One of the uncertainties in a branch is the potential that certain claims not reported in the books of the branch may be held to be valid claims in its liquidation (the “Non-Booked Claims”). Non-Booked Claims arise from policies written outside of Canada but which have some nexus with Canada, and which, arguably, should have been reported in the books of the branch and for which assets should have been deposited in Canada.

54. The Liquidator has worked co-operatively with the U.S. Liquidator to identify Reliance (Canada) Non-Booked Claims. Reliance maintains databases with historical and current policy and claim information. With directions from the Liquidator, staff of the U.S. Liquidator have searched these databases using as many query criteria as available to identify Non-Booked Claims. When the search process identifies open claims, the database details and policy files, if available, are reviewed to confirm whether the identified claims are possible Non-Booked Claims. In many cases, they are not. For example, the search may turn up a Canadian address which is not relevant. It is important to note that the U.S. Liquidator considers the open claims identified as having a possible nexus with Canada as claims which, if valid, would participate in the U.S. estate.

55. The search has thus far identified fewer than 40 potential Non-Booked Claims. About half of these claims have only nominal reserves. In addition, one policyholder that was not identified on the search has contacted the Liquidator. Based on the information presently available, the Liquidator estimates that the total value of the Non-Booked Claims identified thus far, if all proved to be valid, is less than Cdn \$10 million. This would not impact the Liquidator’s ability to pay all Reliance (Canada)’s valid claims in full. However, there is no certainty as to the magnitude of the Non-Booked Claims, since they were not originally identified as being appropriately assigned to Reliance (Canada).

56. The U.S. Liquidator has called for claims. The call expires on December 31, 2003. The U.S. Liquidator will advise the Liquidator of any further Non-Booked Claims that are identified as a result of the call. The Liquidator will then seek directions of this Court with respect to whether the Non-Booked Claims should be allowed in the Canadian estate.

H. Summary of Activities

57. In summary, the Liquidator's major activities for the Periods included:

- (a) Entered into the Protocol with the U.S. Liquidator;
- (b) Created appropriate control levels for a liquidation while ceding day-to-day operations to existing staff in an attempt to maintain operations in a manner as close as possible to a normal run-off operation;
- (c) Entered into, with court authority, the loan agreement with PACICC;
- (d) Claims adjudication and administration – including:
 - (i) oversaw payment of defense and adjustment costs;
 - (ii) repatriated administration of aviation claims;
 - (iii) undertook comprehensive review of attributes and scope of policy and extent of liability for Groupe PPP;
 - (iv) reviewed adjudication processes undertaken by Groupe PPP and amended Reliance (Canada)'s review procedures as a result thereof;
 - (v) amended review procedures on claims presented under the Meridian program;
 - (vi) educated Reliance (Canada) staff, outside counsel and third party administrators with respect to procedures in a liquidation;
 - (vii) oversaw a comprehensive review of all claims including estimating range of possible outcomes;
 - (viii) established internal controls, liquidation policies, procedures and documentation; and

- (ix) settled or otherwise resolved 11,752 claims having a value of \$40.34 million.
- (e) Reinsurance, including:
 - (i) reconciling accounts;
 - (ii) enforcing liquidation clause;
 - (iii) clarifying set-off issues, including with Lloyds;
 - (iv) entering into agreements with reinsurers and the U.S. Liquidator to facilitate collection of the International Reinsurance;
 - (v) gathering of shared reinsurance documentation, particularly in respect of International Reinsurance and policies; and
 - (vi) collection of receivables, including direct communication with reinsurers and cooperative efforts with the U.S. Liquidator;
- (f) Documented (and attempted to quantify) magnitude of exposure to Non-Booked Claims;
- (g) Established investment policy, managed investments, sold the bond portfolio, realizing on gains, considered, and continues to consider, investment options;
- (h) Assembled all the information required to set up a data room;
- (i) Retained Scotia Capital Inc. and KPMG Corporate Finance Inc. to conduct a fully marketed sale process for the business of Reliance (Canada) and engaged in the sale process, described above;
- (j) Reported regularly to PACICC and the U.S. Liquidator;
- (k) Extensive review by Liquidator and actuarial consultant of policy liabilities as at December 31, 2002, updated to June 30, 2003;

- (l) Obtained court approval of 25% dividend in June 2003;
- (m) Created and maintained external website; and
- (n) Moved office to new premises at expiration of lease.

V. LIQUIDATOR'S ACCOUNTS AND PROFESSIONAL FEES

A. Financial Statements

58. The Liquidator does not consider that a traditional statement of receipts and disbursements would provide a meaningful and informative reflection of the financial position of the estate. The Liquidator has therefore prepared unaudited financial statements. Attached as Schedule "F" are unaudited financial statements for the Periods.

59. The financial statements have been prepared in a manner consistent with each other. Assuming this Court is satisfied with this approach, further statements will also be prepared in a consistent manner so that the progress of the administration can be measured. The Liquidator maintains a system of internal controls to safeguard the assets and the reliability of the financial reporting process.

B. Professional Fees

60. The Liquidator retains professional advisors to assist in the administration of the liquidation from time to time. The Liquidator is familiar with the services provided by each of the professional advisors and has reviewed their invoices. Detailed invoices were timely received and carefully reviewed in detail by senior administrative and management level members of the Liquidator's staff. The invoices were reviewed for accuracy, adequate detailed information describing the work performed and by whom, the time spent and when it was spent, the rate and amount billed, possible duplicative charges, reasonableness and overall compliance with the terms of retention. Clarifications and adjustments of items included in the invoices were requested where it appeared appropriate.

61. The Liquidator believes that the Professional Fees of its advisors are proper, fair and reasonable and were incurred in furtherance of the best interests of the estate of Reliance (Canada).

Goodmans LLP

62. Goodmans LLP (“Goodmans”) has acted as counsel to KPMG Inc. from the commencement of the liquidation and has acted or advised on all matters described in this report. The Liquidator is familiar with its services and has reviewed its invoices in detail and with the care described in paragraph 60 above. Goodmans’ fees include services rendered since the commencement of the liquidation and in respect of the winding-up application, chargeable to the estate in accordance with the Appointment Order.

63. At the commencement of the liquidation, Goodmans agreed to a discount from its then current market rates of approximately 15% to 20%. The discount from current rates is approximately 25% to 35%.

64. Attached as Schedules “G”, “H” and “I”, respectively, are:

- (a) a summary invoice from Goodmans to the Liquidator for the periods from the commencement of the liquidation to December 31, 2002 and from January 1, 2003 to September 30, 2003;
- (b) a summary for each of the these periods of the hours and average hourly rates of each of Goodmans’ personnel who dedicated more than 50 hours to the estate; and
- (c) a brief description of the areas of concentration of each of Goodmans’ personnel who dedicated more than 50 hours to the estate.

65. Detailed supporting records, including time sheets, are available should this Court wish them produced. An affidavit attesting to the accuracy of the fees and disbursements is also being filed.

66. The Liquidator is satisfied that Goodmans' fees are proper, fair and reasonable, that time was appropriately spent and that Goodmans' fees were incurred in furtherance of the best interests of the estate.

KPMG Inc.

67. The Liquidator has kept careful and detailed records of all time spent by Liquidator personnel on the estate. The Liquidator has instituted internal controls to ensure no duplicative or inappropriate charges are made. The Liquidator applied the same standard for review to its accounts as to accounts of other professionals, described in paragraph 60. As discussed above, the Liquidator maximized efficiency and reduced costs by retaining former Reliance (Canada) employees and third party administrators where prudent and appropriate. The Liquidator's fees include services rendered since the commencement of the liquidation and in respect of the winding-up application, chargeable to the estate in accordance with the Appointment Order.

68. At the commencement of the liquidation, the Liquidator agreed to a discount from its then current market rates of 15% to 20%. The discount from current market rates is approximately 20% to 25%.

69. Attached as Schedules "J", "K" and "L", respectively, are:

- (a) an invoice from the Liquidator to the estate for the periods from the commencement of the liquidation to December 31, 2002 and from January 1, 2003 to September 30, 2003;
- (b) a summary for each of these periods of the hours and average hourly rates of each of the Liquidator's personnel who dedicated more than 50 hours to the estate; and
- (c) a brief description of the areas of concentration of each of the Liquidator's personnel who dedicated more than 50 hours to the estate for each of the Periods.

70. Detailed supporting records, including time sheets, are available should this Court wish them produced. An affidavit attesting to the accuracy of the fees and disbursements is also being filed.

71. The Liquidator respectfully requests that this Court pass the accounts of the Liquidator, as reflected in the financial statements, and approve the Professional Fees.

VI. EXTENSION OF PAYMENTS

A. Meridian Payments

72. As discussed in previous reports, the Liquidator entered into an agreement with St. Paul Guarantee Insurance Company, formerly London Guarantee Insurance Company (“St. Paul Guarantee”) pursuant to which St. Paul Guarantee would assume Reliance (Canada)’s liabilities under the Meridian program.

73. As the Liquidator reported, the consent of the reinsurers of the Meridian program was a condition of the Meridian transaction. While the majority of these reinsurers are Canadian registered reinsurers, their decision makers are located in London, England. The Liquidator retained U.K. insurance counsel, Kendall Freeman (formerly D.J. Freeman), and used the services of Reliance (Canada)’s reinsurance broker in London, AON, to assist in dealing with the Meridian reinsurers. The Liquidator has met with the Meridian reinsurers, has provided them with all information they have requested concerning the transaction and has been responsive to all concerns they have raised to date. Notwithstanding these efforts, the Meridian reinsurers did not consent. The Liquidator considered all options, including seeking assistance of this Court, and other negotiated resolutions. The Liquidator has now concluded that the completion of the Meridian transaction is no longer of benefit to the estate, given:

- (a) the primary benefit to the estate was the transfer out of the Meridian policies, the last of which expires in 2007. The Meridian liabilities are short-tail. Given that the assumption transaction has not proceeded, the estate will still be in administration; and
- (b) the Liquidator had not projected a major cost benefit to the estate from the Meridian transaction. In light of this, and in the absence of the assumption transaction, the Liquidator does not consider it appropriate to expend further costs in attempting to secure the consent of the reinsurers.

74. The Liquidator recommends that this Court extend until June 30, 2004 or such further date as this Court may order, the date to which the Liquidator may make the Meridian Payments. The Liquidator makes this recommendation because:

- (a) it is not cost-effective to interrupt payments. There would be significant costs in communicating with the approximately 10,200 remaining Meridian policyholders to explain the interruption in the payment stream; and
- (b) as stated in previous reports, the Liquidator was of the view that, given the cost of cancelling the Meridian policies was likely to exceed the cost of running them off, it was more beneficial to the estate to continue to make the Meridian Payments as part of running off the business even if the Meridian transaction did not close. The Liquidator remains of that view.

75. As discussed above, the Liquidator is confident, based on the information presently available to it, that the estate of Reliance (Canada) will pay all valid claims in full. However, the Liquidator is not yet in a position to pay all policyholders 100%. The Liquidator is of the view that it is appropriate to continue the Meridian Payments at the present level because the administrative costs of reducing and adjusting those payments would more than offset any cost differential if the ultimate dividend rate is less than 100%.

B. Policy Payments and Defence Costs

76. The Liquidator remains of the view that it is appropriate and in the best interest of the estate to continue Policy Payments and payment of Defence Costs. The payment of Defence Costs facilitates the collection of reinsurance by easing any potential concerns of the reinsurers with respect to the standards of claims adjudication. Payment of Defence Costs also significantly reduces immediate hardship to policyholders.

77. This Court approved a first distribution of 25 cents on the dollar on valid policyholder claims. Policyholders are paid the higher of the Policy Payments and the first distribution. Although the Liquidator is confident that all valid claims against Reliance (Canada) will be paid in full, uncertainties remain. The Liquidator is of the view that the present Policy Payment level balances the interests of all parties. The Liquidator recommends that the Policy Payments

continue until June 30, 2004 or such later date as this Court may order, to the extent the Payments exceed the first distribution.

78. The Liquidator is recommending June 30, 2004 because it will, in any event, be reporting back to this Court on the status of the estate by that date.

VII. CURRENCY EXCHANGE

79. Section 5 of the *Winding-up and Restructuring Act* provides that the winding-up of the business of the company shall be deemed to commence at the time of the service of the notice of presentation of the petition for winding-up, which in the case of Reliance (Canada) was November 8, 2001.

80. Because Reliance (Canada) was a branch of Reliance, some of the policies issued by Reliance (Canada) were written in U.S. dollars.

81. The *Winding-up and Restructuring Act* has no provisions relating to currency exchange. The Liquidator has been advised by counsel that there is case law that supports the position that claims should be paid in the currency of the country in which the insolvent company is resident and that any currency exchanges should be calculated as at the date of the commencement of the winding-up.

82. In addition, the Liquidator has been advised by counsel that section 275 of the *Bankruptcy and Insolvency Act* provides that a claim for a debt that is payable in a currency other than Canadian currency shall be converted to Canadian currency as of the date of the bankruptcy. The *Bankruptcy and Insolvency Act* defines the date of bankruptcy as the date when the receiving order is granted or the assignment is filed.

83. The Liquidator recommends that any claims payable in foreign currency be converted to Canadian currency at the Bank of Canada noon spot rate of exchange for exchanging such currency to Canadian currency as of November 8, 2001. The applicable exchange rate for U.S. dollars as at November 8, 2001, was \$1.5981.

VIII. RELIEF REQUESTED

84. The Liquidator therefore respectfully requests an order:

- (a) passing the accounts for the Periods, as reflected in the financial statements, and approving the Professional Fees;
- (b) extending the date for the Payments until June 30, 2004 or such later date as this Court may order; and
- (c) fixing the exchange rate at which claims payable in foreign currencies should be converted to Canadian currency at the Bank of Canada noon spot rate of exchange on November 8, 2001.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

KPMG INC., solely in its capacity as the
Liquidator of Reliance Insurance Company -
Canadian Branch

Per:



Robert O. Sanderson, President

Schedule "F"

Unaudited Financial Statements of

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

In our capacity as Liquidator, we have prepared the balance sheet of Reliance Insurance Company, Canadian Branch (in liquidation) as at September 30, 2003, December 31, 2002 and December 3, 2001, the statement of earnings and changes in surplus for the nine months ended September 30, 2003 and the thirteen months ended December 31, 2002 and the statement of cash flows for the nine months ended September 30, 2003 and the thirteen months ended December 31, 2002 in our capacity as liquidator. These financial statements have not been audited or reviewed.

In view of the uncertainties surrounding a branch in liquidation, the ultimate realization on assets and liabilities will differ from the recorded amounts and the differences may be material (see notes).

Readers are cautioned that these statements may not be appropriate for their purposes.

KPMG Inc., Liquidator.
Reliance Insurance Company, Canadian Branch

November 20, 2003

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Balance Sheet

As at September 30, 2003, December 31, 2002, and December 3, 2001

(Unaudited - \$000)	Sep 30, 2003	Dec 31, 2002	Dec 3, 2001
Assets			
Cash and short term investments (note 4)	\$156,277	\$71,835	\$56,165
Investments (note 4) (market value - \$0; 2002 - \$92,353; 2001 - \$114,392)	0	85,211	108,949
Receivable from other insurers/reinsurers	13,908	8,607	6,090
Receivable from income and premium taxes recoverable	3,070	3,265	3,446
Receivable from Reliance Insurance Company US (note 8)	4,181	686	0
Other receivables	958	1,126	1,978
Reinsurers' share of provision for			
Unpaid claims	51,761	58,371	57,536
Unearned premiums	5,430	6,838	9,670
Estimate for deductibles on unpaid claims	1,444	1,619	2,527
	\$237,029	\$237,558	\$246,361
Liabilities and Surplus			
Policy liabilities:			
Unpaid claims (note 5)	\$145,815	\$159,421	135,088
Unearned premiums (note 6)	9,177	11,413	15,189
Allowed claims (note 9)	17,269	6,393	0
Other liabilities	2,158	2,544	1,917
	174,419	179,771	152,194
Payables:			
Due to Reliance Insurance Company US (note 8)	4,848	5,151	0
Due to other insurers/reinsurers	189	181	192
Brokers	2,924	3,547	3,389
Taxes and other creditors	1,653	1,959	1,826
Reinsurance deposits	10	1,229	3,494
Total	184,043	191,838	161,095
Surplus (note 10)	52,986	45,720	85,266
Contingent liabilities (note 11)			
	\$237,029	\$237,558	\$246,361

The accompanying notes are an integral part of the financial statements

(Unaudited - See Cover Page)

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Statements of Earnings and Changes in Surplus

For the nine months ended September 30, 2003, and the thirteen months ended December 31, 2002

(Unaudited - \$000)	Jan 1, 2003 to Sep 30, 2003	Dec 3, 2001 to Dec 31, 2002
Revenue		
Gross Premiums Written	\$ (71)	\$ (437)
Less: Reinsurance Ceded	(265)	(244)
Net written premiums	<u>194</u>	<u>(193)</u>
Net premiums earned	<u>1,022</u>	<u>750</u>
Expenses:		
Claims incurred	3,036	39,281
Commissions and premium taxes	(247)	5,362
General expenses (note 13)	2,043	4,551
	<u>4,832</u>	<u>49,194</u>
Underwriting income (loss)	(3,810)	(48,444)
Investment income		
Interest on cash and short term investments	3,337	1,851
Interest on bonds	433	7,319
Investment expenses	(31)	(43)
Realized gain (loss) on disposal of investments	7,385	(140)
	<u>11,124</u>	<u>8,987</u>
Income (loss) before taxes	7,314	(39,457)
Capital taxes	<u>48</u>	<u>89</u>
Net income (loss)	<u>7,266</u>	<u>(39,546)</u>
Surplus beginning of period	<u>45,720</u>	<u>85,266</u>
Surplus end of period	<u>\$52,986</u>	<u>\$45,720</u>

The accompanying notes are an integral part of the financial statements

(Unaudited - See Cover Page)

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Statement of Cash Flows

For the nine months ended September 30, 2003 and the thirteen months ended December 31, 2002

(Unaudited - \$000)	Jan 1, 2003 to Sep 30, 2003	Dec 3, 2001 to Dec 31, 2002
Operating activities		
Premiums received	\$ (202)	\$ 120
Reinsurance collected	4,021	4,580
Salvage, subrogation & deductibles received	601	1,731
Reduction in other receivables	25	672
Total sources	4,445	7,103
Gross claims paid	9,415	13,658
Claim expenses paid	3,560	4,833
Uncashed claim/expense cheques	(96)	
Reinsurance premiums paid	(76)	(32)
General expenses		
Salaries	1,147	1,962
Office expenses	190	451
Legal/professional	99	174
Head office services	208	257
Sale of business expense	193	577
Liquidation expenses		
KPMG	1,600	1,521
Goodmans	271	614
Income & premium taxes (incl interest paid/rec'd)	(166)	144
Foreign exchange (gain)/loss	(7)	1
Total uses	16,338	24,160
Net cash provided by (used) in operations	(11,893)	(17,057)
Investing activities		
Sale (purchase) of Bonds	91,665	21,560
Investment expenses	(33)	(41)
Interest received	4,493	11,319
Increase(decrease) in accrued investment income	210	(111)
Cash provided by (used in) investing activities	96,335	32,727
Increase in cash and short term investments	84,442	15,670
Cash and short term investments, at beginning of period	71,835	56,165
Cash and short term investments, at end of period	\$156,277	\$71,835

The accompanying notes are an integral part of the financial statements

(Unaudited - See Cover Page)

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

**Notes to Financial Statements for the nine months ended September 30, 2003,
and the thirteen months ended December 31, 2002**

(unaudited – \$000)

1. Nature of the Business:

The Canadian Branch of Reliance Insurance Company, which was primarily engaged in the writing of commercial property and liability insurance in Canada, commenced a voluntary wind down of its operations in Canada effective August 2000. In May 2001, Reliance Insurance Company's U.S. operations ("Reliance US") were placed under an order of rehabilitation. On October 3, 2001, the Company was put into liquidation and declared insolvent by the Court of Pennsylvania.

On December 3, 2001, the Ontario Superior Court of Justice (the "Court"), on the application of the Attorney General of Canada, granted an order appointing KPMG Inc. as provisional liquidator (the "Liquidator") of the insurance business in Canada of Reliance Insurance Company, including the assets in Canada of Reliance Insurance Company, together with its other assets held in Canada under the control of its chief agent ("Reliance Canada"). By further order of the same date, the Court ordered that Reliance Canada be wound up.

Since August 2000, existing insurance policies in force have been allowed to expire and Reliance Canada has neither renewed nor cancelled existing policies, nor has it written any new business. Reliance Canada continues to run off the existing policy and claims liabilities in an orderly fashion.

Pursuant to Orders of the Court the Liquidator has paid policy holders and claimants the greater of: 25% of valid and allowed loss claims pursuant to the first interim distribution approved by the Court in June 2003; or the greater of \$25, or the amount, if any, of the voluntary compensation payment of the Property and Casualty Insurance Compensation Corporation ("PACICC") that may be paid under its Memorandum of Operations.

2. Basis of preparation:

The accounting policies used in the preparation of these financial statements have been selected with a view to reflecting the financial position of a company that is in liquidation.

The preparation of these financial statements requires the use of estimates and assumptions that affect the reported assets and liabilities as at the date of the financial statements and the reported amount of revenue and expenses for the reporting period. The actual results will differ from these estimates and, in view of the additional uncertainties surrounding a company in liquidation, the differences may be material. Changes in estimates are recorded in the current period.

No provision has been made for future liquidation costs. Interest income earned on the assets of Reliance Canada is likely to offset the unbooked future costs of the liquidation.

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended September 30, 2003,
and the thirteen months ended December 31, 2002

(unaudited – \$000)

3. Significant accounting policies:

(a) Investments and investment income

Bonds, including accrued interest of \$931 at December 31, 2002 and \$3,128 at December 3, 2001, are carried at amortized cost, providing for the amortization of the discount or premium on an effective yield basis to maturity. Term deposits and treasury bills are carried at cost plus accrued interest of \$424 at September 30, 2003, \$214 at December 31, 2002, and \$325 at December 3, 2001.

Investment income is recorded as it is earned. Gains and losses arising on disposal of investments are on a settlement date basis, and are calculated on the basis of amortized cost.

(b) Premium revenue and unearned premiums

Unearned premiums represent the amount of premiums written which are applicable to the unexpired terms of the policies in force or to the remaining terms of certificates issued as part of program business. Accordingly, premiums written are taken into income when earned. Although policies were generally issued for one year, Reliance Canada also wrote some multi-year policies and some program business with underlying certificates which are multi-year.

If the unearned premiums are not sufficient to pay expected claims and expenses, a premium deficiency is said to exist. Any changes in estimates of premium deficiencies are recorded as net premium earned in the accounting period in which they are determined.

The reinsurers' share of unearned premiums, net of a provision for doubtful amounts, are recognized as amounts recoverable at the same time and using principles consistent with the method for determining the unearned premium liability.

(c) Provision for unpaid claims

The provision for unpaid claims, includes adjustment expenses, and represents an estimate for all costs of investigating and settling claims incurred on or before the balance sheet date. The provision estimates do not take into account the time value of money, or make explicit provision for adverse deviation.

The provision includes case basis estimates, and an actuarially determined "best estimate" provision for claims incurred but not reported and for development on case basis estimates ("IBNR"). These estimates of future loss activity are necessarily subject to uncertainty and are selected from a wide range of possible outcomes. All provisions are periodically reviewed and evaluated in the light of emerging claim experience and changing circumstances. The resulting changes in estimates of the ultimate liability are recorded as incurred claims in the accounting period in which they are determined.

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

**Notes to Financial Statements for the nine months ended September 30, 2003,
and the thirteen months ended December 31, 2002**

(unaudited – \$000)

(d) Reinsurance ceded:

Net premiums earned and claims incurred are recorded net of amounts ceded to, and recoverable from, reinsurers. To indicate the extent of the credit, collection and contractual risks related to third party reinsurance, estimates of amounts recoverable from reinsurers are recorded separately from the estimated provisions for unearned premiums and unpaid claims.

Amounts recoverable from reinsurers, net of a provision for doubtful amounts, are estimated and recognized at the same time and using principles consistent with Reliance Canada's method for establishing the related liability.

4. Short term investments and investments

Short-term investments are readily convertible into cash and have maturities of three months or less.

Composition of investment portfolio:

	<u>Sept 30, 2003</u>		<u>Dec 31, 2002</u>		<u>Dec 03, 2001</u>	
	<u>Carrying</u>	<u>Market</u>	<u>Carrying</u>	<u>Market</u>	<u>Carrying</u>	<u>Market</u>
	<u>Value</u>	<u>Value</u>	<u>Value</u>	<u>Value</u>	<u>Value</u>	<u>Value</u>
Bonds						
Canadian government	0	0	\$ 85,211	\$ 92,353	\$ 99,949	\$105,415
Canadian corporate	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>8,990</u>	<u>8,977</u>
	<u>0</u>	<u>0</u>	<u>\$ 85,211</u>	<u>\$ 92,353</u>	<u>\$ 108,949</u>	<u>\$114,392</u>

Liquidity and Interest Rate Risk:

	<u>Under 1</u>	<u>1 to 5</u>	<u>6 to 10</u>
	<u>Year</u>	<u>Years</u>	<u>Years</u>
Maturity profile as at December 31, 2002			
Bonds (carrying value)	\$ 6,110	\$71,601	\$ 7,500
Effective interest rate: 7.31%			
Maturity profile as at December 03, 2001			
Bonds (carrying value)	\$17,626	\$52,951	\$38,372
Effective interest rate: 8.19%			

5. Unpaid claims

(a) Nature of unpaid claims:

The provision for unpaid claims and adjustment expenses (and for third party reinsurers' share thereof) are based upon estimates of the ultimate claim costs associated with claims occurring as of the balance sheet dates, including estimates for IBNR claims. These estimates are subject to variability, and the variability could be material. The variability arises because all events affecting the ultimate settlement of claims have not yet taken place and may not take

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended September 30, 2003,
and the thirteen months ended December 31, 2002

(unaudited – \$000)

place for some time. Additional factors affecting the variability include receipt of additional claim information; the continually evolving and changing regulatory and legal environment; court decisions; economic conditions; public attitudes; claims management practices; actuarial studies; the quality of the data used for projection purposes; the effect of inflationary trends on future claims handling and settlement practices; and significant changes in the severity or frequency of claims from historical trends. In addition, the longer the time required for the settlement of a group of claims, the more variable the estimates.

Reliance Canada had fronting reinsurance arrangements with other insurers and provided self-insurance facilities for selected corporate clients. Because Reliance Canada acted as the direct insurer under these arrangements, policyholders look to Reliance Canada for settlement of their claims; Reliance Canada obtains repayment from the insurers or corporations, either directly or from security deposits Reliance Canada maintains. The risk to Reliance Canada is a credit risk if claims exceed either the security deposits or the self-insured's ability to pay.

Reliance Canada accepted certain insurance risks that other insurance companies have underwritten ("assumed reinsurance"). Because of the necessary reliance on the ceding companies for information regarding reported claims, and the resulting reporting lag between the dates of occurrence and the time Reliance Canada is notified of the claims, the inherent uncertainties of estimating reserves is greater for assumed reinsurance than for direct insurance.

In the normal course of settling claims, Reliance Canada acquires rights to subrogate its claims against other parties and, in some cases, recover a portion of the loss from the policyholder as a deductible amount. Salvage and subrogation are deemed not to be material and, as such, are recorded as received. Deductible amounts, which are recoverable on liability claims, have been recognized as assets.

(b) Provision for unpaid claims:

Considerable judgement is required to evaluate claims and establish claim liabilities. The estimation of the claims provision is based on known facts and interpretation of circumstances. The basic assumptions made in establishing actuarial liabilities are best estimates of possible outcomes. Methods of estimation have been used which it is believed produce reasonable results given current information; however, the process of determining the provision necessarily involves risks that the actual results will deviate, perhaps substantially, from the best estimate made. It is also not possible to estimate the impact of the additional uncertainties surrounding a company in liquidation on the estimation process.

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

**Notes to Financial Statements for the nine months ended September 30, 2003,
and the thirteen months ended December 31, 2002**

(unaudited – \$000)

The changes in the unpaid claim provisions recorded in the balance sheet as at September 30, 2003 and December 31, 2002, and their impact on the claims and adjustment expenses for the nine months ended September 30, 2003 and the thirteen months ended December 31, 2002, are as follows:

	Jan 1/03 to Sept 30, 2003	Dec 3/01 to Dec 31/02
Unpaid claims at beginning of period	\$159,421	\$135,088
Recoverable from reinsurers at beginning of period	<u>58,371</u>	<u>57,536</u>
Net unpaid claims at beginning of period	<u>101,050</u>	<u>77,552</u>
Increase in estimated losses and expenses for claims occurring in prior years	3,036	39,281
Increase in outstanding deductibles	(175)	(915)
Paid on claims (net) occurring during current year	(603)	(774)
Paid on claims (net) occurring during prior years	<u>(9,254)</u>	<u>(14,094)</u>
Net reserves at end of period	94,054	101,050
Ceded reserves at end of period	<u>51,761</u>	<u>58,371</u>
Gross reserves at end of period	<u>\$145,815</u>	<u>\$159,421</u>

In order to show the progress of the liquidation from the date of winding-up and as it is not practicable in a winding-up to determine fair value with sufficient reliability, the fair value of the unpaid claims and adjustment expenses, gross and recoverable from reinsurers has been omitted.

6. Unearned premium:

The provisions for unearned premiums as at September 30, 2003 and December 31, 2002 include actuarially determined estimates for premium deficiencies. The process for estimating any provisions for premium deficiency involves the use of estimates concerning factors such as expected claims and expenses and future payout patterns. Any provisions are necessarily subject to uncertainty.

The provision estimates do not take into account the time value of money or make explicit provision for adverse deviation.

7. Reinsurance:

In the normal course of business, Reliance Canada sought to reduce the loss that may arise from catastrophes or other events that cause unfavourable underwriting results by reinsuring certain levels of risk, in various areas of exposure, with other insurers. Reliance Canada is not relieved of its primary obligation to policyholders as a result of its third party reinsurance. Failure of reinsurers to honour their obligations could result in losses to Reliance Canada.

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended September 30, 2003,
and the thirteen months ended December 31, 2002

(unaudited – \$000)

Reliance Canada makes specific provisions against reinsurance receivables and recoverables from companies with whom balances are in dispute or where the reinsurer is not settling balances due to Reliance Canada for reasons related to Reliance US. In addition, the company records a general allowance against reinsurance receivables and recoverables based upon the level of allowance already in place and management's judgement. The general allowance reflects the view that a company in liquidation or run-off has a greater collection risk than a going concern company. The establishment of the allowances for doubtful accounts involves judgement and therefore creates a degree of uncertainty as to adequacy at each reporting date.

Reliance Canada's reinsurance program includes i) reinsurance placed by Reliance Canada directly with Canadian licensed reinsurers and ii) reinsurance entered into through Reliance's head office which reinsures both Reliance (Canada) policies and policies of the former head office and other companies in the Reliance group.

8. Head Office:

(a) Payable to Head Office:

As at September 30, 2003, \$4,848 (2002 - \$5,151) is due to Reliance US for underwriting commissions paid to ECS Managers. The U.S. operations of Reliance settled the commissions with ECS Managers on behalf of Reliance Canada prior to the respective and separate liquidations of Reliance Canada and the U.S. Reliance US advised Reliance Canada of this balance subsequent to the date of liquidation.

(b) Receivable from Head Office:

As at September 30, 2003, on behalf of Reliance Canada, the Liquidator for Reliance US has collected \$4,181 (2002 - \$686) from reinsurers on the International Reinsurance.

(c) Further to a protocol agreement between the Liquidator and the US Liquidator, Reliance US provides various services to Reliance Canada, particularly in the areas of data processing, claims and reinsurance. For the 9 months ended September 30, 2003 the cost of the services was \$208 (2002 - \$297).

9. Allowed Claims

As at September 30, 2003, allowed claim balances are due on claims which have been settled and admitted by the Liquidator, in excess of the Court authorized payments of \$17,269 (2002 - \$6,393).

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

**Notes to Financial Statements for the nine months ended September 30, 2003,
and the thirteen months ended December 31, 2002**

(unaudited – \$000)

10. Surplus

As at September 30, 2003, Reliance Canada's estimated surplus is \$52,986 (2002 - \$45,720). This estimate is subject to revision. In view of the uncertainties surrounding a company in liquidation, the ultimate realization of the assets and liabilities will differ from the estimated results as at September 30, 2003 and the difference may be material. Any surplus available at the wind-up of the liquidation will be paid to Reliance US.

11. Contingent liabilities

There is the potential that certain claims that were not reported in the books of Reliance Canada may be valid claims against Reliance Canada ("Non-Booked Claims"). The Non-Booked Claims would arise from policies written outside Canada but which have some nexus with Canada and which, arguably, should have been reported in the books of Reliance Canada. There is no certainty as to the magnitude of the Non-Booked Claims, since they were not originally identified as being appropriately assigned to Reliance Canada. Should additional loss result from any new claims, such loss would be accounted for as a charge to earnings in the period that the claims are verified as liabilities of Reliance Canada.

12. PACICC loan agreement

PACICC and the Liquidator entered into a loan and services agreement, dated December 3, 2001, which provides that the amounts paid by the Liquidator to policyholders on PACICC-covered claims are deemed to be loaned to PACICC, the aggregate amount of such payments being the "Amount Outstanding" from time to time under the Loan Agreement. Interest occurs on the Amount Outstanding at the prime rate. In the event all policyholders and creditors receive full payment on all valid claims from the assets of the estate, the Liquidator will not demand repayment of the Amount Outstanding. The Amount Outstanding has not been accrued in the financial statements.

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

**Notes to Financial Statements for the nine months ended September 30, 2003,
and the thirteen months ended December 31, 2002**

(unaudited – \$000)

13. Supplementary Expense Information

	<u>Jan 1/03 to Sept 30/03</u>			<u>Dec 3/01 to Dec 31/02</u>		
	<u>Total</u>	<u>General</u>	<u>Claims</u>	<u>Total</u>	<u>General</u>	<u>Claims</u>
Salaries	\$ 1,154	\$ 577	\$ 577	\$ 1,509	\$ 754	\$ 755
Office Expense	189	94	95	378	181	197
Legal/Professional Services	206	103	103	104	52	52
Allowance for Bad Debts	(141)	(141)	0	33	33	0
Head Office Services	208	104	104	297	158	139
Interest (Income)/Expense	3	3	0	77	77	0
Foreign exchange (gains)/loss	(341)	(341)	0	(27)	(27)	0
Sales of Business Expense:						
KPMG Corporate Finance	0	0	0	227	227	0
Scotia Capital	0	0	0	214	214	0
Other	193	193	0	136	136	0
Liquidation Expenses:						
KPMG	1,178	1,178	0	2,002	2,002	0
Goodmans	<u>273</u>	<u>273</u>	<u>0</u>	<u>744</u>	<u>744</u>	<u>0</u>
Total Expenses	<u>\$ 2,922</u>	<u>\$ 2,043</u>	<u>\$ 879</u>	<u>\$ 5,694</u>	<u>\$ 4,551</u>	<u>\$ 1,143</u>

The claims expenses are included in Claims incurred on the statement of earnings and changes in surplus.

RELIANCE INSURANCE COMPANY
(in liquidation)

Professional Fees (including G.S.T.)

	Nov 8 '01 to Dec 31, '02	Jan 1, '03 to Sep 30, '03	Nov 8, '01 to Sep 30, '03
Core Professional			
Goodmans LLP	\$699,032	\$317,695	\$1,016,727
KPMG Inc.	2,204,053	1,294,709	3,498,762
	2,903,085	1,612,404	4,515,489
Other Professional Fees			
Blaney McMurtry	2,774		2,774
Clark Wilson	890		890
Lax O'Sullivan Cronk	13,659		13,659
Lavery, De Billy	756		756
Robinson Sheppard Shapiro	3,051		3,051
KPMG Inc.		32,598	32,598
	21,129	32,598	53,727
Actuaries			
J. S. Cheng & Partners	128,428	66,594	195,022
	128,428	66,594	195,022
PACICC	17,371		17,371
Public Relations			
Crawford Adjusters	5,562		5,562
Hill & Knowlton	1,124		1,124
	6,685		6,685
TOTAL	\$3,076,698	\$1,711,596	\$4,788,294

February 1, 2003

KPMG Inc.
Suite 3300, Commerce Court West
Stn. Commerce Court
Toronto, Ontario
M5L 1B2

Attention: Robert O. Sanderson

OUR FILE NO. KPMG/016699

Re: Reliance Insurance Company, in Liquidation ("Reliance")

TO OUR PROFESSIONAL SERVICES RENDERED in connection with the above-noted matter for the period November 8, 2001 to December 31, 2002, including the following:

Attendances with respect to the winding-up application of Reliance, including communications with OSFI, Ministry of Finance and representatives of Pennsylvania Liquidator, preparation of orders re: winding-up and appointment of liquidator, preparation for cross-examination of François Gilbert, review of Department of Justice factum, preparation for and attendance at court on winding-up application, and preparation of engagement letter and agent contract;

Attendances with respect to claims and liabilities issues, including preparation of forms of releases and procedures for adjusters, review of various claims, including aviation claims, review and analysis of GAP policies, including policies administered by Groupe PPP, applications for leave to proceed, liaison and communications with adjusters, defence counsel and plaintiffs' counsel, and providing advice on settlement of various claims and settlement documents;

Attendances with respect to reinsurance issues, including collection of reinsurance proceeds, research re assignment of reinsurance contracts and set-off issues;

Attendances with respect to liquidation issues, including strategy issues, communications with various stakeholders, including certain policyholders and PACICC, preparation of stakeholder letters, PACICC coverage issues, preparation of loan and services agreement with PACICC, employee issues, including review of employee severance and preparation of termination letters and employee contracts, tax issues, preparation of motion materials and attendance at Ontario Court for various court applications, including transfer of funds and securities on deposit with Quebec regulator to the Liquidator, approval of Meridian Transfer Agreement and extensions of dates for policy payments, payment of defense costs and Meridian payments, responding to questions raised by Maritime Road Development Corporation and their request for adjournment

of motion for approval of Meridian Transfer Agreement, and attendances re: sale of furniture and art at Reliance premises;

Attendances with respect to U.S. issues, including U.S. claims issues, communications with U.S. Liquidator, identification of non-booked claims and arrangements with respect thereto;

Attendances with respect to protocol, including preparation of protocol letter with U.S. Liquidator and communications with U.S. Liquidator; and

Attendances with respect to sale process, including preparation of engagement letter with Scotia Capital Inc. and KPMG Corporate Finance to provide financial advisory services, communications with potential purchasers, review of letters of intent and offers from potential purchasers, consulting with inspectors, financial advisors and U.S. Liquidator with respect thereto, preparation of assumption reinsurance agreement re: Meridian warranty program and preparation of confidentiality agreement.

OUR FEE: \$633,367.80

DISBURSEMENTS: \$20,024.40

GST: \$ 45,639.72

TOTAL: \$699,031.92

GOODMANS LLP

E. & O. E.

November 17, 2003

KPMG Inc.
Suite 3300, Commerce Court West
Stn. Commerce Court
Toronto, Ontario
M5L 1B2

Attention: Robert O. Sanderson

OUR FILE NO. KPMG/016699

Re: Reliance Insurance Company, in Liquidation

TO OUR PROFESSIONAL SERVICES RENDERED in connection with the above-noted matter for the period January 1, 2003 to September 30, 2003, including the following:

Attendances with respect to claims and liabilities issues, including applications for leave to proceed, liaison and communications with adjusters, defence counsel and plaintiffs' counsel, advising on settlement documents, review and analysis of GAP policies and preparation of opinion with respect thereto, preparation of motion materials and attendance at Ontario Court with respect to the appointment of litigation administrators, and administration of aviation claims;

Attendances with respect to reinsurance issues, including set-off issues and collection of reinsurance proceeds;

Attendances with respect to liquidation issues, including preparation of lease re premises of Reliance, preparation of motion materials and attendance at Ontario Court on various court applications, including extension of dates for policy payments, payment of defence costs and Meridian payments and distribution and liaison with inspectors;

Attendances with respect to U.S. issues, including U.S. claims issues, identification of non-booked claims and communications with U.S. Liquidator; and

Attendances with respect to sale process, including meetings with PACICC and U.S. Liquidator, preparation of escrow agreement and governing agreement with respect to the transfer of policyholder liabilities.

GOODMANS

-2-

OUR FEE:	\$287,370.40
DISBURSEMENTS:	\$ 9,651.88
GST:	<u>\$ 20,673.05</u>
TOTAL:	<u>\$317,695.33</u>
GOODMANS LLP	

E. & O. E.

G26\4500071.1

RELIANCE INSURANCE COMPANY

(in liquidation)

LISTING OF GOODMAN'S LLP PERSONNEL Schedule "H"

HOURS AND AVERAGE HOURLY RATE

THIRTEEN MONTH PERIOD ENDED DECEMBER 31, 2002

<u>Name</u>	<u>Rank</u>	<u>Area</u>	<u>HOURS</u>	<u>AVG. HRLY RATE</u>
Rubenstein, Gale	Partner	Insolvency	514.10	\$480
Smith, Graham	Partner	Litigation	469.20	\$404
Gormley, Daniel	Partner	Commercial	108.60	\$404
Paquette, Fanny	Sr. Clk	Insolvency	99.30	\$158
Altaras, Michele	Assoc.	Insolvency	94.10	\$336
Zimmerman, Susan	Partner	Research	81.20	\$391
Bell, Scott	Assoc.	Research	71.10	\$236
Vanderwal, Amy	Assoc.	Insolvency	51.00	\$188
Individuals with less than 50 hours			309.50	\$154
			<u>1,798.10</u>	<u>\$352</u>

RELIANCE INSURANCE COMPANY
(in liquidation)

LISTING OF GOODMAN'S LLP PERSONNEL Schedule "H"
HOURS AND AVERAGE HOURLY RATE
NINE MONTH PERIOD ENDED SEPTEMBER 30, 2003

Name	Rank	Area	HOURS	AVG. HRLY RATE
Rubenstein, Gale	Partner	Insolvency	237.00	\$480
Smith, Graham	Partner	Litigation	177.10	\$404
Gormley, Daniel	Partner	Commercial	63.80	\$404
Altaras, Michele	Assoc.	Insolvency	50.80	\$336
Individuals with less than 50 hours			283.50	\$209
			<hr/>	<hr/>
			<u>812.20</u>	<u>\$354</u>

SCHEDULE "I"

GOODMANS LLP

GENERAL LIQUIDATION RESPONSIBILITY

GALE RUBENSTEIN is a partner in the insolvency area. She oversees all legal matters and is involved in all major areas of the liquidation. Her particular areas of concentration during the periods included strategy issues, communications with various stakeholders, including certain policyholders and PACICC, and with the U.S. Liquidator. She also advised with respect to claims and liabilities issues, reinsurance issues, set-off issues, U.S. issues, protocol with the U.S. Liquidator, the sale process with respect to the Meridian warranty program and policyholder liabilities, and distribution issues, and attended before the Honourable Mr. Justice Farley of the Ontario Superior Court at various court applications.

MICHELE ALTARAS is an associate in the insolvency area. She prepared letters to stakeholders, including Meridian warranty program policyholders, prepared motion materials for various court applications, including the transfer of funds and securities on deposit with the Quebec Regulator to the Liquidator, the extensions of dates for policy payments, payment of defence costs and Meridian payments, and the appointment of independent claims administrators, and acted on the collection of reinsurance proceeds.

AMY VANDERWAL is an associate in the insolvency area. Her primary responsibilities were with respect to reinsurance issues, including research regarding assignment of reinsurance contracts and subrogation.

FANNY PAQUETTE is a senior law clerk in the insolvency area. She drafted basic court documents and prepared other materials in connection with various court applications and attended to service of motion materials. She also monitored the U.S. Bankruptcy Court website re the U.S. proceedings and had responsibility for internal accounting control and meeting the requirements of the Liquidator with respect to accounting and billings.

LITIGATION

GRAHAM SMITH is a partner in the litigation section. His primary responsibilities were with respect to litigation support. He acted as liaison with adjusters, defence counsel and plaintiffs' counsel, acted on applications for leave to proceed and provided advice on settlement of various claims and settlement documents.

COMMERCIAL

DAN GORMLEY is a partner in the commercial law section. He advised with respect to the protocol with the U.S. Liquidator and with respect to the sale process and drafted the transfer agreements with respect to the transfer of the Meridian warranty program and policyholder liabilities.

RESEARCH

SUSAN ZIMMERMAN and **SCOTT BELL** are in the research section. Susan Zimmerman is the Director of Research and Scott Bell is an associate in the research area. They provided research support with respect to reinsurance and U.S. issues.

February 1, 2003

Invoice

Reliance Insurance Company, in Liquidation
8th Floor, 800 Bay St.
Toronto, ON M5S 3A9

GST #122363153

BILL OF COSTS

To our professional services rendered in connection with the above-noted matter for the period November 8, 2001 to December 31, 2002, including:

- Initial consultation with representatives of the Office of the Superintendent of Financial Institutions ("OSFI") and discussions pertaining to the winding-up of Reliance's Canadian Branch ("Reliance Canada");
- Assisting OSFI with their preparation for the Court appearance pertaining to the issuance of a winding-up Order;
- Attendance at meetings and ongoing discussions with Reliance Canada's legal counsel;
- Attendance at meetings and discussions with OSFI, Property and Casualty Insurance Compensation Corporation ("PACICC"), and the U.S. Liquidator to review the drafting of the Appointment Order;
- Taking control of Reliance Canada's operations;
- Attendance at meeting with Reliance employees to review the Winding-Up Order and the Appointment Order and educate them as to procedures in a liquidation and in dealing with policyholder, creditor and other interested parties' telephone calls or correspondence;
- Negotiations with Crawford Adjusters and the establishment of a call centre to deal with all policyholder inquiries pertaining to the winding up of Reliance Canada;
- Development and preparation of questions and answers (Q&As) to be provided to the call centre and to Reliance employees;
- Ongoing monitoring of call centre operations;
- Preparation and issuance of notices of the winding up of Reliance's Canadian Branch to policyholders, adjusters, lawyers, medical practitioners, reinsurers, brokers, agents, general creditors and all other interested parties;

- Development of a Reliance Canada website for the benefit of policyholders, claimants and unsecured creditors to enable them to obtain access to current information as to the status of the liquidation;
- In conjunction with legal counsel, preparation of employment contracts for continuing employees, meeting with employees to explain contracts and arrange for execution of same;
- Attendance at meetings and discussion with Reliance Canada's legal counsel as to the severance packages established for employees prior to the date of liquidation;
- Preparation of a Policies and Procedures Manual which created appropriate control levels for a liquidation while ceding day-to-day operations to existing staff in attempt to maintain operations in a manner as close as possible to a normal runoff operation;
- Attendance at meetings with representatives of the U.S. Liquidator, discussions, preparation and review of documentation resulting in the entry into a Protocol Agreement with the U.S. Liquidator;
- Review existing claims bordereau in order to stratify claims as to dollar amounts, lines of business and PACICC exposure;
- Attendance at meetings with representatives of PACICC, discussions and preparation of a Loan Agreement which was subsequently Court approved;
- Review of Reliance Canada's investment portfolio and entering into a custodial agreement for the safekeeping of same;
- Attendance at meetings with information technology technicians to ensure that the Reliance Canada computer systems were properly backed up as of the date of liquidation and to liaise with Reliance U.S. to ensure that the computer operating systems which are located in the United States will continue to function for the benefit of the Canadian Liquidator and the U.S. Liquidator;
- Establishment of call centre to deal with Meridian inquiries;
- Retained Scotia Capital Inc. and KPMG Corporate Finance Inc. to conduct a fully marketed sales process for the business of Reliance Canada and engage in sales processes;
- Assembly of all pertinent information required to set up a data room;
- Attendance at meetings with significant policyholders and claimants to educate them as to the procedures and process of settlement of claims in a liquidation;

- Attendance at meetings, telephone calls and/or correspondence with lawyers, adjusters, brokers and agents to educate them as to the procedures in a liquidation;
- Review and approval of defence and adjustment costs and authorizing payment of same;
- Attendance at meetings in New York with representatives of the U.S. Liquidator to formalize the working of the Protocol Agreement as it pertained to claims and reinsurance collections;
- Attendance at meetings with third party administrators to ensure the continued processing and adjudication of claims under their control and ensuring that their procedures met with the Liquidator's requirements;
- Attendance at meetings in New York and Cranbury, New Jersey, to arrange for the repatriation of the administration of aviation claims of the Canadian branch formerly handled in the United States;
- Attendance at meetings and discussions with Reliance Canada's independent actuary to review claims reserves and reserve adjustments required due to the liquidation;
- Overseeing a comprehensive review of all claims including estimating range of possible outcomes;
- Attendance at meetings with estate legal counsel, claims adjudication personnel, and representatives of PACICC to develop appropriate releases and dividend distribution procedures for the liquidation;
- Detailed review of the Meridian Program resulting in amended review procedures on claims presented under the Meridian block of business;
- Initiated a comprehensive review of attributes and scope of policy and extent of liability for Le Groupe PPP;
- Attendance at meeting at the Group PPP offices in Quebec City to review adjudication processes undertaken and amended Reliance Canada's review procedures as a result thereof;
- Continued monitoring and supervision of claims adjudication staff, approval of reserve changes, approval of claims settlements, approval of claims settlement costs and authorization of payment of same;
- Detailed review of all reinsurance treaties noting particular the insolvency clause provisions thereof;

- Enforcing insolvency clause of reinsurance treaties to obtain collections of outstanding balances;
- Attendance at meetings with legal counsel to clarify setoff issues with reinsurers;
- Obtaining shared reinsurance documentation from the U.S. Liquidator, particularly in respect of international and reinsurance policies;
- Ongoing collection of reinsurance receivables, including direct communication with reinsurers and cooperative efforts with the U.S. Liquidator;
- Attendance at meetings with various prospective purchasers;
- Responding to due diligence requests of the various prospective purchasers;
- Advising the Inspectors of the Estate as to the status of the sales process;
- Attendance at meetings with reinsurers to discuss novation of the reinsurance treaties to a prospective purchaser;
- Attendance at meetings with legal counsel, review of documentation, and preparation of court motion material for the approval of the Meridian transaction;
- Attendance at Court to hear the above noted motion and responding to undertaking request by the Court for further information;
- Receipt and review of draft letter of intent for the assumption of the Canadian block of business;
- Negotiations with prospective purchaser, receipt and review of documentation, meetings with estate legal counsel resulting in the execution of a Memorandum of Understanding;
- Discussions and attendance at meetings with OSFI to review the regulatory approval requirements for the sale of the Canadian Branch;
- Location of new and smaller premises as at the expiration date of the lease;
- Arrange for build-out of new premises including all IT, data and voice requirements;
- Disposal of excess furniture and equipment;
- Overseeing move of operations to new premises;

- Review and approval of financial statements and related analysis as at December 31st, 2001, for the quarters ending March 31st, June 30th, and September 30th, 2002, and the year end financial statements as at December 31st, 2002;
- Review and approval of Management's Report as at December 31st, 2001, for the quarters ending March 31st, June 30th, and September 30th, 2002, and the year end Management's Report as at December 31st, 2002;
- Review and approval of money market transactions;
- Discussions, receipt and review of various court motions to extend the date to which the Liquidator was authorized to make policy payments and the Meridian payments and payments to defence costs;
- Attendance at court to hear the above noted motions;
- Receipt and review of motion material for the return of the Quebec Deposit and attendance in Court to hear same;
- Review of Reliance Canada documentation and meetings with the U.S. Liquidator to review U.S. documentation to attempt to quantify the magnitude of exposure to Canadian risks not reported on the books of Reliance Canada;
- Ongoing liaison with the U.S. liquidator including discussions as to the potential sale of the Canadian block of business, the return of surplus funds from the Canadian estate to the U.S. estate, discussions as to the status of reinsurance collections, IT systems administration, and obtaining additional information required for the proper administration of the Canadian estate;
- Receipt, review, discussion and attendance at meetings with estate legal counsel to review ongoing matters, sale of the Canadian Branch, reinsurance collection issues and various other estate matters as required;
- Monitor the Reliance staff, including providing appropriate direction and assistance;
- Preparation of appropriate accounting information and filing of appropriate non-tax statutory returns;
- Preparation and filing of the December 31st, 2001 tax returns;
- Updating of the Reliance Canada website for the benefit of policyholders, claimants and creditors to enable them to obtain access to current information as to the status of the liquidation and their claims therein;
- Providing information and analysis for the inspectors;

- Overall administration of the estate and the Reliance staff consisting of approximately 11 people, dealing with day-to-day administrative issues, responding to policyholder, claimants' and creditor inquiries and attendance at all meetings, proceedings and/or court appearances as required.

Our fee:	\$1,993,328.50
Disbursements:	<u>66,533.88</u>
	2,059,862.38
GST	<u>144,190.40</u>
TOTAL	<u>\$2,204,052.78</u>

G26\4500372.1

November 14, 2003

Invoice

Reliance Insurance Company, in Liquidation
8th Floor, 800 Bay St.
Toronto, ON M5S 3A9

GST #122363153

BILL OF COSTS

To our professional services rendered in connection with the above-noted matter for the period January 1, 2003 to September 30, 2003, including:

- Review and approval of financial statements and related analysis for the quarters ending March 31st, June 30th, and September 30th, 2003;
- Review and approval of Management Reports for the quarters ending March 31st, June 30th, and September 30th, 2003;
- Review and approval of money market transactions;
- Receipt of review of information which disclosed that the Liquidator had a potential conflict of interest in the preparation of motion material for the appointment of independent claims administrators and obtaining Court approval of same;
- Continued review of Reliance Canada documentation and meetings with the U.S. Liquidator to review U.S. documentation to attempt to quantify the magnitude of exposure to Canadian risk not reported on the books of Reliance Canada;
- Ongoing liaison with the U.S. Liquidator including discussions as to the potential sale of the Canadian block of business; the return of surplus funds from the Canadian estate to the U.S. estate, discussions as to the status of reinsurance collections, IT systems administration, runoff models, and obtaining additional information required for the proper administration of the Canadian estate;
- Receipt, review, discussion and attendance at meetings with estate legal counsel to review ongoing matters, sale of the Canadian branch, reinsurance collections issues, claims settlement issues and various other estate matters as required;
- Continued monitoring of the Reliance staff, including providing appropriate direction and assistance;
- Attendance at meetings with legal counsel, review of documentation and preparation of court motion material for the approval of the distribution motion which provided for an initial dividend of 25 cents on the dollar;

- Attendance at Court to hear the above noted motion;
- Performing detailed analysis of the bond portfolio, investigation of market conditions and trends, analysis of same, discussions with inspectors and obtaining their approval for the sale of the bond portfolio at a significant gain to the estate
- Continued negotiations with the prospective purchaser and responding to additional due diligence requests and to questions from OSFI;
- Attendance at meetings with estate legal counsel, PACICC, the U.S. Liquidator, to review the progress of the sale transaction and ultimately concluding that the transaction could not proceed;
- Meetings, discussions, review of assumptions and preparation of detailed runoff models projecting the runoff of the estate;
- Discussions, receipt and review of various court motions to extend the date to which the Liquidator was authorized to make policy payments and the Meridian payments, and payments to defence costs;
- Attendance at Court to hear the above noted motion;
- Continuing to deal with policyholder and claimants' telephone calls, e-mails, and correspondence requesting specific information pertaining to the liquidation or their specific claims;
- Continuing to deal with agents and brokers, especially trying to finalize the reconciliation of their accounts as at the date of liquidation;
- Performing a detailed analysis of all large loss claims and discussion of potential outcomes with claims staff;
- Attendance at meetings with actuarial consultant to perform an extensive review of policy liabilities as at December 31st, 2002, and to update same to June 30th, 2003;
- Receipt, review and discussion with the actuarial consultant, the results of his extensive review as performed above;
- Continued to review existing claims bordereaux in order to stratify claims as to dollar amounts, lines of business, and PACICC exposure;
- Review of new reported claims, discussions with claims adjudication staff and approving set-up of appropriate reserves;

- Continuing to liaise with Reliance U.S. IT personnel to ensure the ongoing performance of the computer systems;
- Responding to Reliance U.S. IT personnel requesting specific support due to changes in the IT environment in the U.S.;
- Continuing to deal with numerous Meridian policyholder inquiries;
- Continued review and approval of defence and adjustment costs and authorizing payment of same;
- Continued attendance with third party administrators to ensure the continued processing and adjudication of claims under their control and ensuring that claims are adjudicated and settled according to the procedures established by the Liquidator;
- Continued monitoring and supervision of claims adjudication staff, approval of reserve changes, approval of claims settlements, approval of claims settlement costs and authorization of payment of same;
- Continued follow-up on reinsurance billings and collections;
- Continued to obtain shared reinsurance documentation from the U.S. Liquidator, particularly in respect of international and reinsurance policies;
- Continued liaison with U.S. Liquidator as to international reinsurance collections and commission expenses associated therewith;
- Search for and locate new, smaller premises for the period commencing January 1, 2004;
- Negotiation and execution of a lease for new premises for a period of two years;
- Arrange for build-out of new premises including all IT, data and voice requirements;
- Providing information and analysis for the Inspectors as required;
- Preparation of appropriate accounting information and filing of appropriate non-tax statutory returns;
- Preparation and filing of the December 31st, 2002, tax returns;
- Updating of the Reliance Canada website for the benefit of policyholders, claimants and creditors to enable them to obtain access to current information as to the status of the liquidation and their claims therein;

- Overall administration of the estate and the Reliance staff consisting of approximately 11 people, dealing with day-to-day administrative issues, responding to policyholder, claimants' and creditor inquiries and attendance at all meetings, proceedings and/or court appearances as required.

Our fee:	\$1,191,507.50
Disbursements:	<u>18,500.78</u>
	1,210,008.28
GST	<u>84,700.59</u>
TOTAL	<u>\$1,294,708.87</u>

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RELIANCE INSURANCE COMPANY
(in liquidation)

LISTING OF KPMG INC. PERSONNEL
HOURS AND AVERAGE HOURLY RATE
THIRTEEN MONTH PERIOD ENDED DECEMBER 31, 2002

Schedule "K"

<u>Name</u>	<u>Rank</u>	<u>Area</u>	<u>HOURS</u>	<u>AVG. HRLY RATE</u>
Gutfreund, G.	V.P./Senior Manager	Insolvency/Claims	1,003.00	\$425
Burgess, J.	Specialist	Insolvency/Claims	1,400.80	\$200
Bossence, T.	Special Consultant	Insurance	708.50	\$525
Sanderson, R. O.	President/Partner	Insolvency/Overall Admin./Divestiture	533.80	\$550
Shivas, J.	Senior Manager	Financial Report	494.00	\$425
Murphy, E.	V.P./Senior Manager	Financial Report/Divestiture	460.00	\$425
Taylor, I.	Technician	Insolvency	130.50	\$210
Raynova, N.	Specialist	Actuarial	101.30	\$210
Cantin, C.	Partner	Actuarial	75.30	\$525
Individuals with less than 50 hours			682.60	\$188
			<u>5,589.80</u>	<u>\$357</u>

RELIANCE INSURANCE COMPANY
(in liquidation)

LISTING OF KPMG INC. PERSONNEL
HOURS AND AVERAGE HOURLY RATE
NINE MONTH PERIOD ENDED SEPTEMBER 30, 2003

Schedule "K"

<u>Name</u>	<u>Rank</u>	<u>Area</u>	<u>HOURS</u>	<u>AVG. HRLY RATE</u>
Murphy, E.	V.P./Senior Manager	Financial Report/Divestiture	855.70	\$425
Burgess, J.	Specialist	Insolvency/Claims/Admin.	837.70	\$210
Gutfreund, G.	V.P./Senior Manager	Insolvency/Claims/Admin.	608.00	\$425
Bossence, T.	Special Consultant	Insurance	230.00	\$525
Sanderson, R. O.	President/Partner	Insolvency/Overall Admin.	189.50	\$550
Dutil, R.	Manager	Actuarial	160.50	\$275
Peleshok, A.	Specialist	Actuarial	88.70	\$175
Cantin, C.	Partner	Actuarial	82.60	\$525
Raynova, N.	Specialist	Actuarial	77.70	\$210
Helewa, M-R.	Specialist	Actuarial	51.10	\$210
Individuals with less than 50 hours			206.30	\$186
			<u>3,387.80</u>	<u>\$352</u>

KPMG INC.

ROBERT O. SANDERSON – is President of KPMG Inc., a chartered accountant, fellow of the Institute of Chartered Accountants of Ontario and a trustee in bankruptcy. He has primary responsibility for the liquidation as a whole. During this period, his particular areas of concentration were with respect to the development of the overall direction, approach and strategy for the estate, co-ordinating the investment advisors and confirming the sale process and strategy, ongoing liaison with PACICC, the U.S. Liquidator, the inspectors and major stakeholders, financial projections for the estate, and responding to specific issues arising in the defense of claims.

I. GEORGE GUTFREUND – is a Vice-President of KPMG Inc. and a chartered accountant, a Certified Insurance Receiver and licensed trustee in bankruptcy. He is responsible for the general administration of the liquidation, including oversight of all financial and internal controls, human resources and office management. Mr. Gutfreund oversees the claims adjudication staff and participates as required in the formulation of the appropriate strategy, and is also responsible for the development and maintenance of the website.

EDWARD G. BOSSENCE – was a Partner of KPMG LLP and became a consultant. He is a chartered accountant whose specialty is insurance audits and liquidations. Mr. Bossence has general responsibility for determination of the actuarial liabilities, the Meridian block of business, the sales process, and management of the investment portfolio.

JANE SHIVAS – is a chartered accountant and Senior Manager. She is responsible for budgeting, financial reporting, preparation of financial statements and overseeing the accounting department.

ELIZABETH MURPHY – is a Vice-President of KPMG Inc. and a chartered accountant. During this period Ms. Murphy has general responsibility for all reinsurance matters, communications with PACICC and the U.S. Liquidator and with Mr. Bossence, management of and strategy for the sales process.

JANINE BURGESS – is a Specialist in the corporate recovery group. She assisted Mr. Gutfreund with the claims adjudication process, analysis and stratification of claim files, overseeing the Meridian call centre, preparation and distribution of notices to policyholders, claimants, lawyers, brokers, agents and creditors, reviewing defence costs and extensive claims reviews. Janine also assisted with the set up of the data room and relocation of the office including disposition of excess assets.

IVONEKE TAYLOR – is a Specialist in the corporate recovery group. She provided support with respect to the assembly of documents and creation of the data room.

CLAUDETTE CANTIN – is a Partner of KPMG LLP and the actuary who leads the Canadian P&C Insurance Actuarial Practice. Ms. Cantin is responsible for reviewing the claims reserves, assumptions used and performing sensitivity analysis on the reserves.

N. RAYNOVA – is a Specialist in the P&C actuarial practice. He assisted Ms. Cantin in performing initial analysis as required.

KPMG INC.

ROBERT O. SANDERSON – is President of KPMG Inc., a chartered accountant, fellow of the Institute of Chartered Accountants of Ontario and a trustee in bankruptcy. He has primary responsibility for the liquidation as a whole. During this period, his particular areas of concentration were with respect to the development of the overall direction, approach and strategy for the estate, co-ordinating the investment advisors and confirming the sale process and strategy, ongoing liaison with PACICC, the U.S. Liquidator, the inspectors and major stakeholders, financial projections for the estate, and responding to specific issues arising in the defense of claims.

I. GEORGE GUTFREUND – is a Vice-President of KPMG Inc. and a chartered accountant, a Certified Insurance Receiver and licensed trustee in bankruptcy. He is responsible for the general administration of the liquidation, including oversight of all financial and internal controls, human resources and office management. Mr. Gutfreund oversees the claims adjudication staff and participates as required in the formulation of the appropriate strategy, and is also responsible for the development and maintenance of the website.

ELIZABETH MURPHY – is a Vice-President of KPMG Inc. and a chartered accountant. Ms. Murphy has general responsibility for all reinsurance matters, management of the investment portfolio, providing direction to Scotia Capital in respect to the execution of the sales process and strategy, communications with PACICC and the U.S. Liquidator and determination of actuarial liabilities. She is also responsible for financial reporting, and overseeing the accounting department.

EDWARD G. BOSSENCE – is a consultant with KPMG LLP and a chartered accountant whose specialty is insurance audits and liquidations. Mr. Bossence has assisted with the determination of the actuarial liabilities, the Meridian block of business and the sales process.

JANINE BURGESS – is a Specialist in the corporate recovery group. She assisted Mr. Gutfreund with the claims adjudication process, analysis and stratification of claim files, and reviewing defence costs. Janine also developed runoff models under the direction of Ms. Murphy and Mr. Gutfreund.

CLAUDETTE CANTIN – is a Partner of KPMG LLP and the actuary who leads the Canadian P&C Insurance Actuarial Practice. Ms. Cantin is responsible for reviewing the claims reserves, actuarial assumptions used, performing sensitivity analysis on the reserves and assisting in the development of runoff models.

R. DUTIL – is a Manager in the P&C actuarial practice. He assisted Ms. Cantin in performing initial analysis as required.

N. RAYNOVA – is a Specialist in the P&C actuarial practice. He assisted Ms. Cantin in performing initial analysis as required.

A. PELESHOK – is a Specialist in the P&C actuarial practice. He assisted Ms. Cantin in performing initial analysis as required.

M-R. HELEWA – is a Specialist in the P&C actuarial practice. She assisted Ms. Cantin in performing initial analysis as required.

Schedule "F"

Unaudited Financial Statements of

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

In our capacity as Liquidator, we have prepared the balance sheet of Reliance Insurance Company, Canadian Branch (in liquidation) as at June 30, 2004, September 30, 2003 and December 3, 2001, the statement of earnings and changes in surplus for the six months ended June 30, 2004, the twenty-two months ended September 30, 2003 and the statement of cash flows for the six months ended June 30, 2004 and the twenty-two months ended September 30, 2003 in our capacity as liquidator. These financial statements have not been audited or reviewed.

In view of the uncertainties surrounding a branch in liquidation, the ultimate realization on assets and liabilities will differ from the recorded amounts and the differences may be material (see notes).

Readers are cautioned that these statements may not be appropriate for their purposes.

KPMG Inc., Liquidator
Reliance Insurance Company, Canadian Branch

August 20, 2004

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Balance Sheet

As at June 30, 2004, September 30, 2003, and December 3, 2001

(Unaudited - \$000)	Jun 30, 2004	Sep 30, 2003	Dec 3, 2001
Assets			
Cash and short term investments (note 4)	\$155,078	\$156,277	\$56,165
Investments (note 4) (market value - \$0; 2003 - \$0; 2001 - \$114,392)	0	0	108,949
Receivable from other insurers/reinsurers	27,576	13,908	6,090
Receivable from income and premium taxes recoverable	0	3,070	3,446
Receivable from Reliance US (note 8)	4,848	4,181	0
Current balance due (note 8)	870	0	0
Other receivables	600	958	1,978
Reinsurers' share of provision for			
Unpaid claims	71,704	51,761	57,536
Unearned premiums	4,847	5,430	9,670
Estimate for deductibles on unpaid claims	106	1,444	2,527
	\$265,629	\$237,029	\$246,361
Liabilities and Surplus			
Policy liabilities:			
Unpaid claims (note 5)	\$171,544	\$145,815	135,088
Unearned premiums (note 6)	8,216	9,177	15,189
Allowed claims (note 9)	33,106	17,269	0
Other liabilities	841	2,158	1,917
	213,707	174,419	152,194
Payables:			
Due to Reliance US (note 8)	4,848	4,848	0
Due to other insurers/reinsurers	142	189	192
Brokers	2,916	2,924	3,389
Taxes and other creditors	1,031	1,653	1,826
Reinsurance deposits	10	10	3,494
Total	222,654	184,043	161,095
Surplus (note 10)	42,975	52,986	85,266
Contingent liabilities (note 11)			
	\$265,629	\$237,029	\$246,361

The accompanying notes are an integral part of the financial statements

(Unaudited - See Cover Page)

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Statements of Earnings and Changes in Surplus

For the nine months ended June 30, 2004, and twenty-two months ended September 30, 2003

(Unaudited - \$000)	Oct 1, 2003 to Jun 30, 2004	Dec 3, 2001 to Sep 30, 2003
Revenue		
Gross Premiums Written	\$ (12)	\$ (508)
Less: Reinsurance Ceded	(9)	(509)
Net written premiums	(3)	1
Net premiums earned	375	1,772
Expenses:		
Claims incurred	12,539	42,317
Commissions and premium taxes	21	5,115
General expenses (note 13)	1,212	6,656
Foreign Exchange (net claims)	(656)	(62)
	13,116	54,026
Underwriting income (loss)	(12,741)	(52,254)
Investment income		
Interest on cash and short term investments	2,807	5,188
Interest on bonds	0	7,752
Investment expenses	(36)	(74)
Realized gain (loss) on disposal of investments	0	7,245
	2,771	20,111
Income (loss) before taxes	(9,970)	(32,143)
Capital taxes	41	137
Net income (loss)	(10,011)	(32,280)
Surplus beginning of period	52,986	85,266
Surplus end of period	\$42,975	\$52,986

The accompanying notes are an integral part of the financial statements

(Unaudited - See Cover Page)

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Statement of Cash Flows

For the nine months ended June 30, 2004, and twenty-two months ended September 30, 2003

(Unaudited - \$000)	Oct 1, 2003 to Jun 30, 2004	Dec 1, 2001 to Sep 30, 2003
Operating activities		
Premiums received	\$ 1	\$ (82)
Reinsurance collected	6,163	8,601
Salvage, subrogation & deductibles received	578	2,332
Reduction in other receivables	481	697
Total sources	7,223	11,548
Gross claims paid	8,663	23,073
Claim expenses paid	3,136	8,393
Uncashed claim/expense cheques	0	(96)
Reinsurance premiums paid	(14)	(108)
General expenses		
Salaries	1,364	3,109
Office expenses	369	641
Legal/professional	138	273
Head office services	210	465
Sale of business expense	0	770
Liquidation expenses		
KPMG Inc.	818	3,121
Goodmans LLP	266	885
Foreign exchange (gain)/loss	(81)	56
Income & premium taxes (incl interest paid/rec'd)	(3,405)	(22)
Foreign exchange (gain)/loss(net claims)	(273)	(62)
Total uses	11,191	40,498
Net cash provided by (used) in operations	(3,968)	(28,950)
Investing activities		
Sale (purchase) of Bonds	0	113,225
Investment expenses	(36)	(74)
Interest received	2,895	15,812
Increase(decrease) in accrued investment income	(90)	99
Cash provided by (used in) investing activities	2,769	129,062
Increase in cash and short term investments	(1,199)	100,112
Cash and short term investments, at beginning of period	156,277	56,165
Cash and short term investments, at end of period	\$155,078	\$156,277

The accompanying notes are an integral part of the financial statements

(Unaudited - See Cover Page)

RELIANCE INSURANCE COMPANY

Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended June 30, 2004, twenty-two months ended September 30, 2003

(unaudited – \$000)

1. Nature of the business:

The Canadian Branch of Reliance Insurance Company, which was primarily engaged in the writing of commercial property and liability insurance in Canada, commenced a voluntary wind down of its operations in Canada effective August 2000. In May 2001, Reliance Insurance Company's U.S. operations ("Reliance US") were placed under an order of rehabilitation. On October 3, 2001, Reliance US was put into liquidation and declared insolvent by the Court of Pennsylvania.

On December 3, 2001, the Ontario Superior Court of Justice (the "Court"), on the application of the Attorney General of Canada, granted an order appointing KPMG Inc. as provisional liquidator (the "Liquidator") of the insurance business in Canada of Reliance Insurance Company, including the assets in Canada of Reliance Insurance Company, together with its other assets held in Canada under the control of its chief agent ("Reliance Canada"). By further order of the same date, the Court ordered that Reliance Canada be wound up.

Since August 2000, existing insurance policies in force have been allowed to expire and Reliance Canada has neither renewed nor cancelled existing policies, nor has it written any new business. Reliance Canada continues to run off the existing policy and claims liabilities in an orderly fashion.

Pursuant to Orders of the Court the Liquidator has paid policy holders and claimants the greater of: 25% of valid and allowed loss claims pursuant to the first interim distribution approved by the Court in June 2003; or the greater of \$25, or the amount, if any, of the voluntary compensation payment of the Property and Casualty Insurance Compensation Corporation ("PACICC") that may be paid under its Memorandum of Operations.

2. Basis of preparation:

The accounting policies used in the preparation of these financial statements have been selected with a view to reflecting the financial position of a company that is in liquidation.

The preparation of these financial statements requires the use of estimates and assumptions that affect the reported assets and liabilities as at the date of the financial statements and the reported amount of revenue and expenses for the reporting period. The actual results will differ from these estimates and, in view of the additional uncertainties surrounding a company in liquidation, the differences may be material. Changes in estimates are recorded in the accounting period in which they are determined.

No provision has been made for future liquidation costs. Interest income earned on the assets of Reliance Canada is likely to offset the unbooked future costs of the liquidation.

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended June 30, 2004, twenty-two months ended September 30, 2003

(unaudited – \$000)

3. Significant accounting policies:

(a) Investments and investment income:

Bonds, including accrued interest of \$3,128 at December 3, 2001, are carried at amortized cost, providing for the amortization of the discount or premium on an effective yield basis to maturity. Term deposits and treasury bills are carried at cost plus accrued interest of \$334 at June 30, 2004, \$424 at September 30, 2003, and \$325 at December 3, 2001.

Investment income is recorded as it is earned. Gains and losses arising on disposal of investments are on a settlement date basis, and are calculated on the basis of amortized cost.

(b) Premium revenue and unearned premiums:

Unearned premiums represent the amount of premiums written which are applicable to the unexpired terms of the policies in force or to the remaining terms of certificates issued as part of program business. Accordingly, premiums written are taken into income when earned. Although policies were generally issued for one year, Reliance Canada also wrote some multi-year policies and some program business with underlying certificates which are multi-year.

If the unearned premiums are not sufficient to pay expected claims and expenses, a premium deficiency is said to exist. Any changes in estimates of premium deficiencies are recorded as net premium earned in the accounting period in which they are determined.

The reinsurers' share of unearned premiums, net of a provision for doubtful amounts, is recognized as amounts recoverable at the same time and using principles consistent with the method for determining the unearned premium liability.

(c) Provision for unpaid claims:

The provision for unpaid claims includes adjustment expenses and represents an estimate for all costs of investigating and settling claims incurred on or before the balance sheet date. The provision estimates do not take into account the time value of money, or make explicit provision for adverse deviation.

The provision includes case basis estimates, and an actuarially determined "best estimate" provision for claims incurred but not reported and for development on case basis estimates ("IBNR"). These estimates of future loss activity are necessarily subject to uncertainty and are selected from a wide range of possible outcomes. All provisions are periodically reviewed and evaluated in the light of emerging claim experience and changing circumstances. The resulting changes in estimates of the ultimate liability are recorded as incurred claims in the accounting period in which they are determined.

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended June 30, 2004, twenty-two months ended September 30, 2003

(unaudited – \$000)

d) Reinsurance ceded:

Net premiums earned and claims incurred are recorded net of amounts ceded to, and recoverable from, reinsurers. To indicate the extent of the credit, collection and contractual risks related to third party reinsurance, estimates of amounts recoverable from reinsurers are recorded separately from the estimated provisions for unearned premiums and unpaid claims.

Amounts recoverable from reinsurers, net of a provision for doubtful amounts, are estimated and recognized at the same time and using principles consistent with Reliance Canada's method for establishing the related liability.

4. Short term investments and investments:

Short-term investments are readily convertible into cash and have maturities of three months or less.

Composition of investment portfolio:

	<u>Dec 03, 2001</u>	
	<u>Carrying</u>	<u>Market</u>
	<u>Value</u>	<u>Value</u>
Bonds		
Canadian Government	\$ 99,949	\$ 105,415
Canadian Corporate	<u>8,990</u>	<u>8,977</u>
	<u>\$ 108,939</u>	<u>\$ 114,392</u>

Liquidity and Interest Rate Risk:	<u>Under 1</u>	<u>1 to 5</u>	<u>6 to 10</u>
	<u>Year</u>	<u>Years</u>	<u>Years</u>
Maturity profile as at December 03, 2001			
Bonds (carrying value)	\$17,626	\$52,951	\$38,372
Effective interest rate: 8.19%			

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended June 30, 2004, twenty-two months ended September 30, 2003

(unaudited – \$000)

5. Unpaid claims:

(a) Nature of unpaid claims:

The provision for unpaid claims and adjustment expenses (and for third party reinsurers' share thereof) are based upon estimates of the ultimate claim costs associated with claims occurring as of the balance sheet dates, including estimates for IBNR claims. These estimates are subject to variability, and the variability could be material. The variability arises because all events affecting the ultimate settlement of claims have not yet taken place and may not take place for some time. Additional factors affecting the variability include receipt of additional claim information; the continually evolving and changing regulatory and legal environment; court decisions; economic conditions; public attitudes; claims management practices; actuarial studies; the quality of the data used for projection purposes; the effect of inflationary trends on future claims handling and settlement practices; and significant changes in the severity or frequency of claims from historical trends. In addition, the longer the time required for the settlement of a group of claims, the more variable the estimates.

Reliance Canada had fronting reinsurance arrangements with other insurers and provided self-insurance facilities for selected corporate clients. Because Reliance Canada is the direct insurer under these arrangements, policyholders and claimants look to Reliance Canada for settlement of their claims; Reliance Canada obtains repayment from the insurers or corporations, either directly or from security deposits Reliance Canada maintains. The risk to Reliance Canada is a credit risk if claims exceed either the security deposits or the self-insured's ability to pay.

Reliance Canada accepted certain insurance risks that other insurance companies have underwritten ("assumed reinsurance"). Because of the necessary reliance on the ceding companies for information regarding reported claims, and the resulting reporting lag between the dates of occurrence and the time Reliance Canada is notified of the claims, the inherent uncertainties of estimating reserves is greater for assumed reinsurance than for direct insurance.

In the normal course of settling claims, Reliance Canada acquires rights to subrogate its claims against other parties and, in some cases, recover a portion of the loss from the policyholder as a deductible amount. Salvage and subrogation are deemed not to be material and, as such, are recorded as received. Deductible amounts which are recoverable on liability claims have been recognized as assets.

(b) Provision for unpaid claims:

Considerable judgement is required to evaluate claims and establish claim liabilities. The estimation of the claims provision is based on known facts and interpretation of circumstances. The basic assumptions made in establishing actuarial liabilities are best estimates of possible outcomes. Methods of estimation have been used which it is believed produce reasonable results given current information; however, the process of determining the provision necessarily involves risks that the actual results will deviate, perhaps substantially,

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended June 30, 2004, twenty-two months ended September 30, 2003

(unaudited – \$000)

from the best estimate made. It is also not possible to estimate the impact of the additional uncertainties surrounding a company in liquidation on the estimation process.

The changes in the unpaid claim provisions recorded in the balance sheet as at June 30, 2004, September 30, 2003, and December 3, 2001 and their impact on the claims and adjustment expenses for the fifteen months ended June 30, 2004, the twenty-two months ended September 30, 2003, are as follows:

	<u>Oct 1/03 to Jun 30/04</u>	<u>Dec 3/01 to Sep 30/03</u>
Unpaid claims at beginning of period	\$ 145,815	\$ 135,088
Recoverable from reinsurers at beginning of period	<u>51,761</u>	<u>57,536</u>
Net unpaid claims at beginning of period	<u>94,054</u>	<u>77,552</u>
Increase in estimated losses and expenses for claims occurring in prior years	12,539	42,317
Increase in outstanding deductibles	(65)	(1,090)
Paid on claims (net) occurring during current year (Gap Programs)	(577)	(1,377)
Paid on claims (net) occurring during prior years	<u>(6,111)</u>	<u>(23,348)</u>
Net reserves at end of period	99,840	94,054
Ceded reserves at end of period	<u>71,704</u>	<u>51,761</u>
Gross reserves at end of period	<u>\$ 171,544</u>	<u>\$ 145,815</u>

In order to show the progress of the liquidation from the date of winding-up and as it is not practicable in a winding-up to determine fair value with sufficient reliability, the fair value of the unpaid claims and adjustment expenses, gross and recoverable from reinsurers has been omitted.

6. Unearned premium:

The provisions for unearned premiums include actuarially determined estimates for premium deficiencies. The process for estimating any provisions for premium deficiency involves the use of estimates concerning factors such as expected claims and expenses and future payout patterns. Any provisions are necessarily subject to uncertainty.

The provision estimates do not take into account the time value of money or make explicit provision for adverse deviation.

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended June 30, 2004, twenty-two months ended September 30, 2003

(unaudited – \$000)

7. Reinsurance:

In the normal course of business, Reliance Canada sought to reduce the loss that may arise from catastrophes or other events that cause unfavourable underwriting results by reinsuring certain levels of risk, in various areas of exposure, with other insurers. Reliance Canada is not relieved of its primary obligation to policyholders as a result of its third party reinsurance. Failure of reinsurers to honour their obligations could result in losses to Reliance Canada.

Reliance Canada makes specific provisions against reinsurance receivables and recoverables from companies who are in liquidation or run-off, with whom balances are in dispute or where the reinsurer is not settling balances due to Reliance Canada for reasons related to Reliance US. In addition, the company records a general allowance against reinsurance receivables and recoverables based upon the level of allowance already in place and management's judgement. The general allowance reflects the view that a company in liquidation or run-off has a greater collection risk than a going concern company. The establishment of the allowances for doubtful accounts involves judgement and therefore creates a degree of uncertainty as to adequacy at each reporting date.

Reliance Canada's reinsurance program includes: i) reinsurance placed by Reliance Canada directly with Canadian licensed reinsurers and ii) reinsurance entered into by Reliance US which reinsures both Reliance (Canada) policies and policies of Reliance US and other companies in the Reliance group.

8. Head office:

The liquidator for Reliance US (the "US Liquidator"), subsequent to the date of liquidation, advised Reliance Canada that Reliance US had settled underwriting commissions due to ECS Managers on behalf of Reliance Canada (the "ECS Commission Payable") prior to the respective and separate liquidations of Reliance Canada and Reliance US. The US Liquidator and the Canadian Liquidator have agreed, without prejudice, that the US Liquidator will withhold payment to the Canadian Liquidator of reinsurance collected by Reliance US on behalf of Reliance Canada on the international reinsurance treaties ("Canadian Reinsurance Proceeds") up to the amount of the ECS Commission Payable of \$4,848 or US\$3,034. The parties have also agreed that Reliance US will pay to the Reliance Canada any Canadian Reinsurance Proceeds in excess of the ECS Commission Payable.

(a) Payable to Head Office:

As at June 30, 2004, \$4,848 (2003 - \$4,848; 2001 - \$0) has been set up as an amount due to Reliance US for the ECS Commission Payable.

(b) Receivable from Reliance US:

As at June 30, 2004, on behalf of Reliance Canada, Reliance US has collected \$4,848 (2003 - \$4,181; 2001 - \$0) of Canadian Reinsurance Proceeds, which is to be held by the Reliance US pending payment of the ECS Commission Payable to Reliance US.

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended June 30, 2004, twenty-two months ended September 30, 2003

(unaudited – \$000)

(c) Receivable from Reliance US – Current Balance Due:

As at June 30, 2004, on behalf of Reliance Canada, Reliance US has collected \$870 (2003 - \$0; 2001 - \$0) of Canadian Reinsurance Proceeds which is to be forwarded by Reliance US to Reliance Canada.

(d) Protocol Agreement:

Further to a protocol agreement between the Liquidator and the US Liquidator, Reliance US provides various services to Reliance Canada, particularly in the areas of data processing, claims and reinsurance. For the 9 months ended June 30, 2004 the cost of the services was \$187 (2003 - \$505).

9. Allowed claims:

As at June 30, 2004, allowed claim balances are due on claims which have been settled and admitted by the Liquidator, in excess of the Court authorized payments of \$33,106 (2003 - \$17,269; 2001 - \$0).

10. Surplus:

As at June 30, 2004, Reliance Canada's estimated surplus is \$42,975 (2003 - \$52,986; 2001 - \$85,266). This estimate is subject to revision. In view of the uncertainties surrounding a company in liquidation, the ultimate realization of the assets and liabilities will differ from the estimated results as at June 30, 2004 and the difference may be material. Any surplus available at the wind-up of the liquidation will be paid to Reliance US.

11. Contingent liabilities:

There is the potential that certain claims that were not reported in the books of Reliance Canada may be valid claims against Reliance Canada ("Non-Booked Claims"). The Non-Booked Claims would arise from policies written outside Canada but which have some nexus with Canada and which, arguably, should have been reported in the books of Reliance Canada. There is no certainty as to the magnitude of the Non-Booked Claims, since they were not originally identified as being appropriately assigned to Reliance Canada. Should additional loss result from any new claims, such loss would be accounted for as a charge to earnings in the accounting period that the claims are verified as liabilities of Reliance Canada.

12. PACICC loan agreement:

PACICC and the Liquidator entered into a loan and services agreement, dated December 3, 2001, which provides that the amounts paid by the Liquidator to policyholders on PACICC-covered claims are deemed to be loaned to PACICC, the aggregate amount of such payments being the "Amount Outstanding" from time to time under the Loan Agreement. Interest occurs on the Amount Outstanding at the prime rate. In the event all policyholders and creditors receive full payment on all valid claims from the assets of the estate, the

RELIANCE INSURANCE COMPANY
Canadian Branch (in liquidation)

Notes to Financial Statements for the nine months ended June 30, 2004, twenty-two months ended September 30, 2003

(unaudited – \$000)

Liquidator will not demand repayment of the Amount Outstanding. The Amount Outstanding has not been accrued in the financial statements.

13. Supplementary expense information:

	<u>Oct 1/03 to Jun 30/04</u>			<u>Dec 3/01 to Sep 30/03</u>		
	<u>Total</u>	<u>General</u>	<u>Claims</u>	<u>Total</u>	<u>General</u>	<u>Claims</u>
Salaries	\$ 1,079	\$ 539	\$ 540	\$ 2,663	\$ 1,331	\$ 1,332
Office Expense	318	159	159	567	275	292
Legal/Professional Services	111	56	55	310	155	155
Allowance for Bad Debts	6	6	0	(108)	(108)	0
Head Office Services	187	93	94	505	262	243
Interest (Income)/Expense	(406)	(406)	0	80	80	0
Foreign Exchange (Gain)/Loss	(31)	(31)	0	(306)	(306)	0
Sale of Business Expense:						
KPMG Corporate Finance	0	0	0	227	227	0
Scotia Capital	0	0	0	214	214	0
Other	0	0	0	329	329	0
Liquidation Expenses:						
KPMG Inc.	622	622	0	3,180	3,180	0
Goodmans LLP	<u>174</u>	<u>174</u>	<u>0</u>	<u>1,017</u>	<u>1,017</u>	<u>0</u>
Total Expenses	<u>\$ 2,060</u>	<u>\$ 1,212</u>	<u>\$ 848</u>	<u>\$ 8,678</u>	<u>\$ 6,656</u>	<u>\$ 2,022</u>

The claims expenses are included in Claims incurred on the statement of earnings and changes in surplus.

14. Foreign exchange:

Further to an order from the Court, dated December 18, 2003 and amended on June 30, 2004, the Liquidator is authorized to pay claims payable in foreign currencies either:

- a) in those foreign currencies in circumstances where the Liquidator is otherwise legally entitled to do so; or
- b) in Canadian currency, converted at the Bank of Canada noon spot rate of exchange for exchanging such currencies to Canadian currency on November 8, 2001.

Further to this, in cases where the agreed claim is determined in U.S. dollars, the rate used by Reliance Canada to calculate the Canadian equivalent is \$1.5981.

RELIANCE INSURANCE COMPANY
(in liquidation)

Professional Fees (including G.S.T.)

	Oct 1 to Dec 31, '03	Jan 1, '04 to Mar 31, '04	Apr 1, '04 to Jun 30, '04	Oct 1, '03 to Jun 30, '04
Core Professional				
Goodmans LLP	\$80,085	\$44,577	\$60,498	\$185,160
KPMG Inc.	221,961	202,354	258,308	682,623
	302,046	246,931	318,806	867,783
Other Professional Fees				
KPMG Inc.		27,245		27,245
Blaney McMurtry			465	465
	0	27,245	465	27,710
Actuaries				
J. S. Cheng & Partners	109,306			109,306
	109,306	0	0	109,306
TOTAL	\$411,352	\$274,176	\$319,270	\$1,004,799

The following memorandum was prepared by Reliance Insurance Company, KPMG Inc., Scotia Capital Inc. and KPMG Corporate Finance Inc. based on publicly available information. The information contained herein is not guaranteed as to accuracy or completeness. This memorandum is for information purposes only and does not constitute an offer to sell or a solicitation to buy the securities referred to herein.

Schedule "G"

RELIANCE INSURANCE COMPANY (Canada Branch)

OVERVIEW

Reliance Insurance Company ("Reliance") is a federally registered property and casualty insurance company headquartered in Philadelphia, Pennsylvania, United States. Reliance's Canadian branch ("Reliance Canada" or the "Branch") operates from a head office located in Toronto, Ontario, Canada. Major lines of business included property, casualty, professional liability, directors & officers, group and association programs. Reliance Canada has been in run-off since September 2000.

As an alternative to the orderly run-off of Reliance Canada, one of the options being considered is an assumption reinsurance transaction for the net insurance liabilities in consideration for cash. Scotia Capital and KPMG Corporate Finance Inc. (the "Co-Advisors") have been engaged to assist in identifying interested parties and arranging an assumption reinsurance transaction.

The key attractions of this opportunity are:

- a large block of seasoned long-tail claims - the business has been in run-off since September 2000;
- portfolio backed in part by reinsurance from highly rated reinsurers - over 80% of the reinsurance cover is with "A" rated reinsurers;
- skilled and highly experienced claims staff – collectively over 177 years of experience;
- potential expense savings by combining with an existing portfolio; and
- opportunity to manage claims and investment portfolio to maximize returns.

Excluded from this transaction is a small block of insurance liabilities and associated reinsurance and other recoverables relating to the vehicle warranty business administered by Meridian Management Inc.

DESCRIPTION OF BUSINESS

Prior to the commencement of the run-off in September 2000, Reliance Canada historically wrote mainly commercial business including property, general liability and professional liability, and was licensed to transact business in all Canadian provinces and territories.

The Branch largely operated, and continues to operate, independently of Reliance in the United States although it shares certain services, including information technology and selected reinsurance activities. The Branch currently employs 16 people. Claims are handled in Canada by 5 claims examiners with a total of 177 years of cumulative claims experience. The Company's claims staff possesses unique qualifications for dealing with the book of business and may be available for transfer with the book of business.

BACKGROUND

On October 3, 2001, Reliance consented to an Order of Liquidation by the Commonwealth Court of Pennsylvania. In part in response to the October 3, 2001 Order, Reliance agreed on December 3, 2001 to the Ontario Court of Justice ordering Reliance Canada to be wound up and KPMG Inc's appointment as provisional liquidator.

The Branch continues to service its existing clients with a highly experienced team of professionals. Reliance Canada's management has stated that the Branch remains solvent and capable of meeting its obligations as they become due. During the past year, Reliance Canada's business objectives included:

- Fully responding to its contractual and business obligations to all Canadian policyholders;
- Minimizing the costs and the length of time necessary to complete the runoff;
- Ensuring that the employees, shareholders, stakeholders and interested parties are treated in an equitable and commercially reasonable manner; and
- Maximizing the surplus of the Branch to be eventually returned to Reliance.

INSURANCE LIABILITIES

⇒ At June 30, 2001, Reliance Canada (excluding the Meridian block of business) had the following:

- Gross unpaid claims of \$132.1 million
- Net unpaid claims of \$71.9 million -
- 5 claims examiners

⇒ At June 30, 2001, the breakdown of gross unpaid claims of \$132.1 million was as follows (in \$000):

Business Line	Under \$50		Over \$50		Total	
	# Claims	Gross Case Reserves	# Claims	Gross Case Reserves	#Claims	Gross Case Reserves
Liability	790	\$9,480	81	\$25,593	871	\$35,073
Commercial Property	234	\$2,047	27	\$7,645	261	\$9,692
Commercial Automobile	47	\$484	10	\$2,274	57	\$2,758
Other	24	\$7	0	\$0	24	\$7
Total	1,095	\$12,018	118	\$35,512	1,213	\$47,530
% of total		25.3%		74.7%		
				Plus: IBNR		\$80,520
				Plus: Other Adjustments		\$4,089
						<u>\$132,139</u>

INSURANCE LIABILITIES (CON'T)

⇒ At June 30, 2001, the breakdown of net unpaid claims of \$71.9 million was as follows (in \$000):

Business Line	Number Claims	Case Reserve	IBNR	Total Reserve	% of Total
Liability					
General	445	\$13,507	\$23,478	\$36,985	51.4%
E&O	162	\$753	\$4,275	\$5,028	7.0%
D&O	34	\$1,953	\$4,313	\$6,266	8.7%
Malpractice	142	\$6,962	\$846	\$7,808	10.9%
Pollution	80	\$1,759	\$1,946	\$3,705	5.2%
Other	8	\$21	\$0	\$21	0.0%
Commercial Property	261	\$3,110	\$1,139	\$4,249	5.9%
Commercial Automobile	57	\$3,013	\$2,956	\$5,969	8.3%
Other	24	\$805	\$1,076	\$1,881	2.6%
	1,213	\$31,883	\$40,029	\$71,912	100.0%

Province or Territory	Case Reserve	IBNR	Total Reserve	% of Total
Ontario	\$19,879	\$25,235	\$45,114	62.7%
Québec:	\$4,742	\$5,728	\$10,470	14.6%
Alberta	\$3,125	\$4,096	\$7,221	10.0%
British Columbia	\$2,469	\$2,992	\$5,461	7.6%
All others	\$1,669	\$1,977	\$3,646	5.1%
	\$31,884	\$40,028	\$71,912	100.0%

REINSURANCE

⇒ At June 30, 2001, the amounts recoverable from reinsurers (excluding amounts recoverable related to the Meridian block of business) were as follows (in \$000):

Reinsurer Rating ⁽¹⁾	Unpaid Claims and Adjustment Expenses	Unearned premiums	Total	% of Total
A++	\$26,383	\$33	\$26,416	43.4%
A+	\$8,812	\$190	\$9,002	14.8%
A	\$6,829	\$208	\$7,037	11.6%
A-	\$8,290	\$13	\$8,303	13.6%
B++	\$1	\$0	\$1	0.0%
B+	\$2,738	\$6	\$2,744	4.5%
Not rated and other	\$7,176	\$155	\$7,331	12.1%
	\$60,229	\$605	\$60,834	100.0%

Notes:

(1) Ratings as determined by A.M. Best Co.

- ⇒ The top 5 reinsurers account for 41.3% of the total amounts recoverable.
- ⇒ The top 10 reinsurers account for 58.4% of the total amounts recoverable.

CONTACT INFORMATION

Please feel to contact the Co-Advisors in regards to this opportunity at the numbers listed below:

Scotia Capital Inc

Paul Hodgson (416) 945-4032
 Vikas Sharma (416) 945-4282
 Richard Smith (416) 863-7401

KPMG Corporate Finance Inc.

Christian Plumer (416) 777-8995
 Derek Sutherland (416) 777-3177

November 28, 2001

Schedule "H"

M. Diane Koken
Insurance Commissioner of the
Commonwealth of Pennsylvania,
in her capacity as Liquidator of
Reliance Insurance Company

Dear Commissioner:

RE: Reliance Insurance Company ("Reliance")

By order (the "U.S. Order") of the Commonwealth Court of Pennsylvania (the "U.S. Court") made the 3rd day of October, 2001, the Insurance Commissioner of the Commonwealth of Pennsylvania (the "U.S. Liquidator") has been appointed Liquidator of Reliance.

The Superintendent of Financial Institutions (the "Superintendent") has designated KPMG Inc. as one of his representatives in connection with his taking control of the assets of Reliance in Canada, together with its other assets held in Canada under the control of its chief agent, including, without limitation, all amounts received or receivable in respect of its insurance business in Canada (collectively, the "Canadian Insurance Business"). At the Superintendent's request, the Attorney General of Canada has applied to the Ontario Superior Court of Justice (the "Canadian Court") for an order (the "Canadian Winding-up Order") winding-up the Canadian Insurance Business under the *Winding-up and Restructuring Act*. He is recommending that KPMG Inc. be appointed as liquidator of the Canadian Insurance Business (the "Canadian Liquidator"), in a further order (the "Canadian Appointment Order"). The Canadian Winding-up Order and the Canadian Appointment Order will be referred to collectively as the "Canadian Order".

References in this agreement to "Reliance (Canada)", in the context of the period prior to the issuance of the Canadian Order, mean the Canadian Insurance Business and, in the context of the period following the issuance of the Canadian Order, mean the estate and effects under the control of the Canadian Liquidator pursuant to the Canadian Order. References in this agreement to "Reliance (U.S.)", in the context of the period prior to the issuance of the U.S.

Order, mean the U.S. operations of Reliance and, in the context of the period following the issuance of the U.S. Order, mean the legal estate under the control of the U.S. Liquidator pursuant to the U.S. Order and, for greater certainty, exclude Reliance (Canada).

The parties are in agreement that it is in the best interests of Reliance (U.S.) and Reliance (Canada) and their respective stakeholders that they agree to co-operate with one another with respect to certain matters as set out below.

1. **APPOINTMENT AS INSPECTOR**

The Canadian Liquidator will consent to the appointment by the Canadian Court of the U.S. Liquidator as an inspector in the liquidation of Reliance (Canada) under the *Winding-up and Restructuring Act*. The Canadian Liquidator will convene regular meetings of inspectors.

2. **INFORMATION**

The U.S. Liquidator will receive the financial information with respect to the operations of Reliance (Canada) which, prior to the issuance of the U.S. Order, Reliance (U.S.) typically received from Reliance (Canada). The Canadian Liquidator will further provide information concerning material developments in the Canadian estate and such other information as the U.S. Liquidator may reasonably request.

3. **DETERMINATION OF RELIANCE (CANADA) POLICYHOLDERS**

The U.S. Liquidator and the Canadian Liquidator agree to co-operate with one another in order to avoid and eliminate duplicate claims within Reliance (U.S.) and Reliance (Canada). To that end, the U.S. Liquidator and the Canadian Liquidator will consult with one another when there is a need to determine whether an individual or entity is the holder of a policy which ought properly to be considered a liability of Reliance (Canada).

4. **SERVICES**

Prior to the issuance of the U.S. Order, Reliance (U.S.) provided various services to Reliance (Canada), particularly in the areas of data processing, claims and reinsurance. The U.S.

Liquidator agrees to ensure that these services continue to be provided with the same scope and at the same level of quality both before and after issuance of the Canadian Order.

Fees for such services will be negotiated in good faith based on the actual costs incurred by the U.S. Liquidator in providing the services and a reasonable mark-up thereon for associated overhead. These services include but are not limited to:

- (a) **Data Processing.** The U.S. Liquidator will cause the employees and independent third party contractors of Reliance (U.S.) to provide to Reliance (Canada) data processing services of the same nature and scope and at the same level of quality as had been provided prior to the date hereof. Without limiting the generality of the foregoing, the U.S. Liquidator will cause the employees of Reliance (U.S.) to:
 - (i) provide the data processing services currently being provided (it being agreed by the parties that they will agree upon a definitive schedule of such services within 30 days of the date hereof);
 - (ii) provide such further data processing services as may be necessary from time to time to enable the Canadian Liquidator to meet its obligations as a liquidator and an officer of the court and as it is reasonably feasible for the U.S. Liquidator to provide;
 - (iii) carry out and implement, within a commercially reasonable timeframe, such programming and processing changes as necessary to reflect the change of Reliance (Canada)'s status and as appropriate for better management of data and operations as the Canadian Liquidator may from time to time reasonably request; and
 - (iv) develop, in conjunction with the Canadian Liquidator, a plan for the migration of Reliance (Canada)'s data to a new third party processor or a new platform. In connection with such migration, the U.S. Liquidator will use reasonable efforts to assist the Canadian Liquidator in obtaining, at the lowest possible cost, licenses and sub-licenses of the software currently

being used to provide the services described above to be granted to the Canadian Liquidator or its designee.

Notwithstanding the foregoing, if it is not reasonably feasible for the U.S. Liquidator to provide the services contemplated in this paragraph on a commercially reasonable basis at a commercially reasonable cost, the parties will negotiate in good faith commercially reasonable alternative arrangements.

Services described in this paragraph (a) will be provided by the U.S. Liquidator until at least December 31, 2004, and the Canadian Liquidator will avail himself of such services until such date, provided that:

- i. the Canadian Liquidator may terminate such services upon 30 days prior written notice at any time after December 31, 2003 if the Canadian Liquidator can demonstrate to the reasonable satisfaction of the U.S. Liquidator that it is in the financial best interests of Reliance (Canada) to have such services performed by another service provider;
- ii. the Canadian Liquidator may terminate such services if the Canadian Insurance Business is transferred as contemplated by paragraph 5;
- iii. the Canadian Liquidator may terminate such services if the U.S. Liquidator breaches a provision of this paragraph 4(a) in a material respect and fails to remedy such breach within 30 days written notice thereof, provided that the Canadian Liquidator may not terminate under this clause (iii) by reason of a failure of the U.S. Liquidator to perform her obligations hereunder which is attributable to an event of *force majeure*; and
- iv. the Canadian Liquidator may terminate such services if the U.S. Liquidator is prevented from performing such services by reason

of a force *majeure condition* or event which continues for 90 days or more.

After December 31, 2004, either party will be entitled to terminate the services provided for in this paragraph (a) without cause upon 150 days prior written notice to the other.

(b) **Claims.**

To date there has been an operational policy in effect whereunder any claim (on an occurrence basis) under a Reliance (Canada) policy in excess of U.S. \$500,000.00 (on a gross basis), has been forwarded to Reliance's U.S. head office for authorization, prior to an adjustment to the claims reserve or the establishment of a claim amount. The Canadian Liquidator, (or, if applicable, Reliance (Canada)'s employees) will seek the advice of the U.S. Liquidator with respect to such claims, and at the same time will advise the U.S. Liquidator of any proposed course of action with respect to such claim. Within ten (10) days of receipt in writing of such proposed course of action (or such shorter period as required in the circumstances), the U.S. Liquidator will provide her comments thereon in writing to the Canadian Liquidator. If the Canadian Liquidator and U.S. Liquidator disagree on a proposed course of action, each will advise the other of why it does not agree, and what alternate course of action it would propose. If the U.S. Liquidator proposes an alternate course of action, the Canadian Liquidator will either implement such proposed alternate course of action or, if it determines to proceed with a different course of action, will advise the U.S. Liquidator in writing as to its reasons for doing so (but may nonetheless proceed with such different course of action.)

The Canadian Liquidator will seek, and the U.S. Liquidator will provide, its advice on the law firms who should be chosen by the Canadian Liquidator for the defence of claims brought in the U.S. under Reliance (Canada) policies. Where the U.S. Liquidator is required to defend a claim brought in Canada under a

Reliance (U.S.) policy she will seek, and the Canadian Liquidator will provide, its advice on the law firms who should be chosen for the defence of the claim.

The services described in this paragraph (b) will be provided until the Canadian Insurance Business is transferred as contemplated in Section 5.

- (c) **Reinsurance.** A large portion of the reinsurance ceded in respect of Reliance (Canada) business was ceded under reinsurance treaties or arrangements also covering business of Reliance (U.S.), and was administered by Reliance (U.S.). The U.S. Liquidator will cause the employees of Reliance (U.S.) to continue to administer such reinsurance in a reasonable and competent manner, to collect amounts owing from reinsurers thereunder in respect of Reliance (Canada) business promptly in accordance with the terms of the applicable reinsurance documents and to promptly remit same to the Canadian Liquidator without set-off other than for amounts actually set-off by a reinsurer referable to claims in respect of Reliance (Canada). In the event a reinsurer asserts a set-off or otherwise attempts to reduce payments otherwise due from such reinsurer or a insurer becomes insolvent the U.S. Liquidator and the Canadian Liquidator will work together in good faith to maximize recoveries from such reinsurer.

The Canadian Liquidator will cause Reliance (Canada) to provide such information as is necessary to bill the reinsurers. To the extent practicable, the frequency of billings to reinsurers will be accelerated. Any such amounts collected and received by the U.S. Liquidator shall be received by the U.S. Liquidator in trust for the Canadian Liquidator and, pending prompt remittance to the Canadian Liquidator, shall be held by the U.S. Liquidator in trust for the Canadian Liquidator. There shall be no obligation on the U.S. Liquidator to hold such amounts in a segregated account. The U.S. Liquidator will provide a detailed accounting to support each remittance of proceeds. On request, the U.S. Liquidator will provide the Canadian Liquidator with such other records and accounting support so that the Canadian Liquidator can confirm that all appropriate billings have been made and remittances paid.

Subject to the final sentence of the penultimate paragraph of Section 5, the services described in this paragraph (c) will be provided until the Canadian Insurance Business is transferred as contemplated in Section 5.

5. TRANSFER OF BUSINESS

The U.S. Liquidator and the Canadian Liquidator agree that it is in the best interests of the stakeholders of both Reliance (U.S.) and Reliance (Canada) that forthwith after the issuance of the Canadian Order the Canadian Liquidator attempt to transfer the Reliance (Canada) business to one or more other carriers, most likely through one or more assumption reinsurance transactions. To this end, the Canadian Liquidator intends to engage one or more financial advisors and to initiate a bid solicitation process. The Canadian Liquidator will consult with the U.S. Liquidator regarding its choice of financial advisor(s) and acknowledges that the U.S. Liquidator has advised she considers Scotia McLeod Inc. acceptable. The Canadian Liquidator will seek the U.S. Liquidator's comments on a list of intended recipients of bid solicitation materials. The U.S. Liquidator will also be afforded the opportunity to review and comment upon all bid solicitation materials, and the U.S. Liquidator will provide such comments and information as are, in the opinion of the U.S. Liquidator, acting reasonably, necessary to afford prospective bidders true and fair disclosure in such materials. The U.S. Liquidator will assist the Canadian Liquidator in establishing a data room which provides true and fair disclosure.

During the bid solicitation process, the Canadian Liquidator will convene regular progress meetings with its financial advisor(s) and will afford the U.S. Liquidator the opportunity to participate in such meetings, either in person or via conference call. The Canadian Liquidator will instruct its financial advisor(s) to copy the U.S. Liquidator on all written communications to the Canadian Liquidator regarding the bid solicitation process.

Once bids have been received, representatives of the U.S. Liquidator may review and provide their comments on the relative merits of the bids received. The Canadian Liquidator will also afford the U.S. Liquidator the opportunity to review and comment on all transactional documentation prior to execution,

The U.S. Liquidator will, if requested by the Canadian Liquidator, enter into an agreement with any transferee of all or a substantial portion of the business of Reliance (Canada) whereunder the

U.S. Liquidator agrees to provide to such transferee, for a period not exceeding twelve months, the data processing services referred to above for the fees being charged to the Canadian Liquidator. In addition, the U.S. Liquidator will co-operate with the Canadian Liquidator in attempting to effect a novation of all reinsurance treaties currently covering both the business of Reliance (Canada) and Reliance (U.S.), such that the Reliance (Canada) business now covered thereby is covered under separate and distinct reinsurance treaties between the transferee and the reinsurers. If such a novation is not effected, it may be necessary for the U.S. Liquidator to provide certain of the services described in paragraph 4(c) to the transferee on such terms as are agreed. The U.S. Liquidator will provide such further support and services to a transferee as may be reasonably required, on such terms as are agreed.

It is acknowledged that the Canadian Liquidator will likely follow a shorter and simpler process with respect to the transfer of the Meridian block of business which would not involve the engagement of financial advisors or the formal solicitation of competitive bids, but will nonetheless keep the U.S. Liquidator apprised of all material steps in the transfer process.

6. COMMUNICATIONS

It is acknowledged that provision of the services outlined in Section 4 above will require regular interaction and communication between the employees of Reliance (U.S.) and Reliance (Canada) on the same basis as same have been conducted in the past, and the U.S. Liquidator and the Canadian Liquidator agree to continue to facilitate such communications and interactions. However, all other communications between the U.S. Liquidator and the Canadian Liquidator, whether pertaining to the subject matter of this letter agreement or otherwise, will be conducted only through their "Designated Representatives". Each of the U.S. Liquidator and the Canadian Liquidator will appoint three (3) Designated Representatives. The U.S. Liquidator's initial Designated Representatives will be Arthur Mullin, David Brietling and Robert Haberle. The Canadian Liquidator's initial Designated Representatives will be Robert O. Sanderson, Edward G. Bossence and 1. George Gutfreund. Each party may change one or more of their Designated Representatives upon forty-eight (48) hours prior written notice to the other. The U.S. Liquidator agrees to keep the Canadian Liquidator advised of significant developments in the liquidation of Reliance (U.S.) which might reasonably be expected to have a material impact upon the U.S. Liquidator's ability to perform its obligations hereunder.

7. **CONFIDENTIALITY**

The U.S. Liquidator acknowledges that the data processed by Reliance (U.S.) on behalf of Reliance (Canada) and other information provided by the Canadian Liquidator to the U.S. Liquidator hereunder includes information which is either non-public, confidential or proprietary in nature (the “Confidential Information”). The U.S. Liquidator further acknowledges that the Confidential Information is the proprietary information of Reliance (Canada). The U. S. Liquidator agrees not to use the Confidential Information for any purpose other than the performance of its services as contemplated herein, and not to transfer or disclose any portion of such data to any third party, other than upon the express direction of the Canadian Liquidator, provided that:

- a. Confidential Information may be disclosed to (i) the U.S. Liquidator’s counsel, advisors, experts, consultants, directors, officers, employees, agents (including employees and officers of its agents), (ii) any guaranty or compensation fund or association that has a reasonable need to know the Confidential Information and who has signed a confidentiality agreement containing confidentiality obligations substantially the same as those provided herein and (iii) qualified persons recording testimony involving such documents or information (e.g. court reporters) and necessary stenographic and clerical assistants thereof, and
- b. to the extent that the U.S. Liquidator may be compelled by legal or regulatory requirements to disclose any of Confidential Information to a third party, she may disclose the Confidential Information if she has used all reasonable efforts to obtain, and shall have afforded the Canadian Liquidator the opportunity to obtain, an appropriate protective order or other satisfactory assurance of confidential treatment for the information compelled to be disclosed.

This agreement shall not apply to those portions of the Confidential Information which (i) are, or prior to the time of disclosure or utilization, have become, generally available to the public other than as a result of disclosure by the U.S. Liquidator; (ii) have been made or, prior to the time of disclosure or utilization, have become, available to the U.S. Liquidator on a non-confidential basis from a source other than the Canadian Liquidator

provided that such source is not known to the U.S. Liquidator to be bound by a confidentiality agreement with the Canadian Liquidator or otherwise prohibited from transmitting the Confidential Information by a contractual, legal or fiduciary obligation; or (iii) was known to the U.S. Liquidator on a non-confidential basis prior to its disclosure to her by the Canadian Liquidator.

8. **CANADIAN ORDER**

It is acknowledged that the Attorney General of Canada has sought the issuance of the Canadian Order, the Canadian Appointment Order being substantially in the form previously provided to the U.S. Liquidator, now returnable before the Canadian Court on December 3, 2001, in accordance with the order of the Canadian Court dated November 13, 2001. The Attorney-General has advised that he will seek confirmation from the Canadian Court in the Canadian Winding-up Order that no finding of insolvency has been made by the Canadian Court. The U.S. Liquidator agrees to withdraw its opposition to the Canadian Order. The provisions of this Section 8 and Sections 4, 6, 7, 9 and 10 will take effect immediately upon execution of this agreement, and references in such paragraphs to the Canadian Liquidator shall be deemed to include the Superintendent during the period prior to the issuance of the Canadian Order. The remaining provisions will take effect immediately upon the obtaining of a Canadian Order which does not contain terms which are materially inconsistent with this agreement.

9. **GOOD FAITH CO-OPERATION**

The parties acknowledge that they cannot address in this agreement all issues which might arise between them in the course of the liquidation of Reliance (U.S.) and Reliance (Canada). They agree to discuss and resolve all such issues in good faith, and to do, or cause to be done, all such further acts and things as may be reasonably necessary or desirable to give full effect to this agreement.

10. **JURISDICTION**

This agreement and any disputes or disagreements between the parties under this agreement shall be governed by the laws of the Province of Ontario and the laws of Canada applicable therein. For the purposes of resolution of any disputes or disagreements between the parties that may

arise from or in connection with this agreement, and except as otherwise expressly provided herein, each party hereby irrevocably subjects itself to the jurisdiction of the courts of the Province of Ontario. The U.S. Liquidator agrees not to bring proceedings in any court other than the courts of the Province of Ontario.

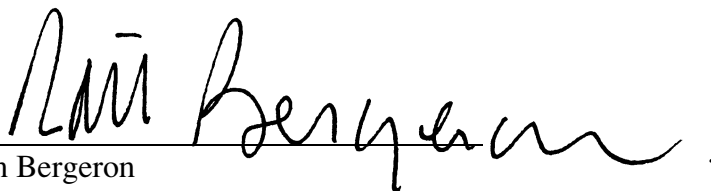
11. **ENUREMENT**

This agreement shall enure to the benefit of and be binding upon any successors to the parties hereto in their respective capacities as U.S. Liquidator and Canadian Liquidator.

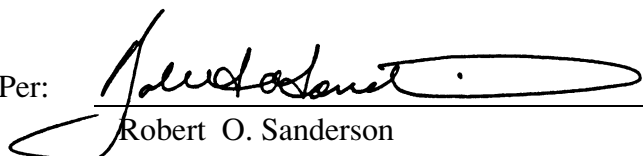
Please sign in the space provided below to indicate your agreement with the foregoing.

Yours very truly,

SUPERINTENDENT OF FINANCIAL INSTITUTIONS
prior to the issuance of the Canadian Order

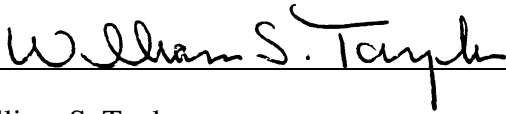
Per: 
Ron Bergeron
Senior Director

KPMG INC. solely in its capacity as Liquidator
of the Canadian Branch of Reliance Insurance Company
(and not in its personal capacity) after the issuance of the
Canadian Order

Per: 
Robert O. Sanderson
President, KPMG Inc.

ACCEPTED AND AGREED this 27 day of November, 2001.

**M. DIANE KOKEN, INSURANCE COMMISSIONER
OF THE COMMONWEALTH OF PENNSYLVANIA,**
solely in her capacity as Liquidator of Reliance Insurance Company,
and not in her personal capacity

A handwritten signature in cursive script that reads "William S. Taylor". The signature is written in black ink and is positioned above a horizontal line.

William S. Taylor
Deputy Insurance Commissioner of the
Commonwealth of Pennsylvania, solely
in his capacity as Liquidator Designee
Reliance Insurance Company (In Liquidation)

January 31, 2004

KPMG Inc.
Suite 3300, Commerce Court West
Stn. Commerce Court
Toronto, Ontario
M5L 1B2

Attention: Robert O. Sanderson

OUR FILE NO. KPMG/016699

Re: Reliance Insurance Company, in Liquidation ("Reliance")

TO OUR PROFESSIONAL SERVICES RENDERED in connection with the above-noted matter for the period October 1, 2003 to December 31, 2003, including the following:

Attendances with respect to claims and liabilities issues, including applications for leave to proceed, liaison and communications with adjusters, defence counsel and plaintiffs' counsel, providing advice on settlement of various claims and preparation of settlement documents, and review of various pleadings;

Attendances with respect to reinsurance issues, including collection of reinsurance proceeds, preparation of trust agreement and set-off issues;

Attendances with respect to liquidation issues, including strategy, communications with various stakeholders, preparation of motion materials and attendance at Ontario Court for passing of accounts, extension of date for policy payments, payment of defence costs and Meridian payments, and fixing the exchange rate at which claims payable in foreign currency are to be converted to Canadian currency, preparation of lease agreement re new Reliance premises, issues regarding third party administrators, liaison and meeting with PACICC, auto dealers issues under the Meridian warranty program and preparation of employment contract;

Attendances with respect to U.S. issues, including U.S. claims issues, identification of non-booked claims, liaison with U.S. Liquidator and monitoring U.S. liquidation.

GOODMANS

-2-

OUR FEE:	\$72,764.00
DISBURSEMENTS:	\$ 2,104.54
GST:	<u>\$ 5,216.58</u>
TOTAL:	<u>\$80,085.12</u>

GOODMANS LLP

E. & O. E.

GOODMANS\5047069.1

April 30, 2004

KPMG Inc.
Suite 3300, Commerce Court West
Stn. Commerce Court
Toronto, Ontario
M5L 1B2

Attention: Robert O. Sanderson

OUR FILE NO. KPMG/016699

Re: Reliance Insurance Company, in Liquidation ("Reliance")

TO OUR PROFESSIONAL SERVICES RENDERED in connection with the above-noted matter for the period January 1, 2004 to March 31, 2004, including the following:

Attendances with respect to claims and liabilities issues, including applications for leave to proceed, liaison and communications with adjusters, defence counsel and plaintiffs' counsel, review and preparation of settlement documents, review of third party action against Reliance, contingent claims issues and issues relating to Section 71 of the *Winding-Up and Restructuring Act*;

Attendances with respect to reinsurance issues, including collection of reinsurance proceeds and attendances re various agreements among reinsurers and Canadian and U.S. Liquidators;

Attendances with respect to liquidation issues including strategy, currency issues, privacy issues and documentation, third party administrator issues, distribution issues, and review of maternity leave and employee benefits issues.

OUR FEE:	\$40,821.50
DISBURSEMENTS:	\$ 846.08
GST:	<u>\$ 2,909.04</u>
TOTAL:	<u>\$44,576.62</u>

GOODMANS LLP

E. & O. E.

GOODMANS\5047083.1

July 31, 2004

KPMG Inc.
Suite 3300, Commerce Court West
Stn. Commerce Court
Toronto, Ontario
M5L 1B2

Attention: Robert O. Sanderson

OUR FILE NO. KPMG/016699

Re: Reliance Insurance Company, in Liquidation ("Reliance")

TO OUR PROFESSIONAL SERVICES RENDERED in connection with the above-noted matter for the period April 1, 2004 to June 30, 2004, including the following:

Attendances with respect to claims and liabilities issues, including applications for leave to proceed, liaison and communications with adjusters, defence counsel and plaintiffs' counsel, advising on and preparation of settlement documents, U.S. directors and officers claims, and stay issues;

Attendances with respect to reinsurance issues, including preparation of agreement with reinsurer and U.S. Liquidator to facilitate collection of reinsurance proceeds;

Attendances with respect to liquidation issues, including preparation of motion materials and attendance at Ontario Court re extension of dates for policy payments, payment of defence costs and Meridian payments and payment of claims in foreign currency, privacy issues, securities and investment issues, license and premium tax issues, and liaison with inspectors;

Attendances with respect to U.S. issues, including communications with U.S. Liquidator.

OUR FEE: \$55,796.00

DISBURSEMENTS: \$ 751.05

GST: \$ 3,950.61

TOTAL: **\$60,497.66**

GOODMANS LLP

E. & O. E.

GOODMANS\5047090.1

Schedule "J"

RELIANCE INSURANCE COMPANY

(in liquidation)

LISTING OF GOODMAN'S LLP PERSONNEL

HOURS AND AVERAGE HOURLY RATE

THREE MONTH PERIOD ENDED DECEMBER 31, 2003

Name	Rank	Area	HOURS	AVG. HRLY RATE
Rubenstein, Gale	Partner	Insolvency	67.90	\$505
Smith, Graham	Partner	Litigation	41.90	\$425
Paquette, Fanny	Sr. Clk	Insolvency	77.50	\$165
Individuals with less than 30 hours			49.20	\$185
			<hr/>	<hr/>
			<u>236.50</u>	<u>\$325</u>

RELIANCE INSURANCE COMPANY
(in liquidation)

LISTING OF GOODMAN'S LLP PERSONNEL
HOURS AND AVERAGE HOURLY RATE
THREE MONTH PERIOD ENDED MARCH 31, 2004

<u>Name</u>	<u>Rank</u>	<u>Area</u>	<u>HOURS</u>	<u>AVG. HRLY RATE</u>
Rubenstein, Gale	Partner	Insolvency	32.30	\$505
Smith, Graham	Partner	Litigation	30.70	\$425
Individuals with less than 30 hours			50.50	\$227
			<u>113.50</u>	<u>\$360</u>

RELIANCE INSURANCE COMPANY
(in liquidation)

LISTING OF GOODMAN'S LLP PERSONNEL
HOURS AND AVERAGE HOURLY RATE
THREE MONTH PERIOD ENDED JUNE 30, 2004

<u>Name</u>	<u>Rank</u>	<u>Area</u>	<u>HOURS</u>	<u>AVG. HRLY RATE</u>
Rubenstein, Gale	Partner	Insolvency	45.90	\$505
Smith, Graham	Partner	Litigation	48.60	\$425
Individuals with less than 30 hours			47.90	\$250
			<u>142.40</u>	<u>\$392</u>

Schedule "K"

GOODMANS LLP

GENERAL LIQUIDATION RESPONSIBILITY

GALE RUBENSTEIN is a partner in the insolvency area. She oversees all legal matters and is involved in all major areas of the liquidation. Her particular areas of concentration during the Three Quarters included strategy issues, communications with various stakeholders, including certain policyholders and PACICC, and with the U.S. Liquidator. She advised with respect to claims and liabilities issues, reinsurance issues, U.S. issues, distribution issues, issues relating to the passing of accounts, auto dealers issues under the Meridian warranty program, privacy issues, currency issues, issues re extension of policy payments, payment of defence costs and Meridian payments, investment issues, and issues regarding third party administrators.

FANNY PAQUETTE is a senior law clerk in the insolvency area. She drafted basic court documents and prepared materials in connection with applications to the Ontario Court and attended to service of motion materials. She also had responsibility for internal accounting control and meeting the requirements of the Liquidator with respect to accounting and billings.

LITIGATION

GRAHAM SMITH is a partner in the litigation section. He provided litigation support and acted as liaison with adjusters, defence counsel and plaintiffs' counsel, acted on applications for leave to proceed, and provided advice and prepared settlement documentation on the settlement of various claims.

August 10, 2004

Invoice

Reliance Insurance Company, in Liquidation
Suite 810, 4 King Street West
Toronto, ON M5H 1B6

GST #122363153

BILL OF COSTS

To our professional services rendered in connection with the above-noted matter for the period October 1st, 2003 to June 30th, 2004, including:

Review and approval of financial statements and related analysis for the quarters ending September 30th, 2003, December 31st, 2003, and March 31st, 2004;

Review and approval of Management Reports for the quarters ending September 30th, 2003, December 31st, 2003, and March 31st, 2004;

Review and approval of money market transactions;

Continued limited review of Reliance Canada documentation and meetings with the U.S. Liquidator to review U.S. documentation to attempt to quantify the magnitude of exposure to Canadian risk not reported on the books of Reliance Canada;

Ongoing liaison with the U.S. Liquidator including the return of surplus funds from the Canadian estate to the U.S. estate, discussions as to the status of reinsurance collections, IT systems administration, runoff models, and obtaining additional information required for the proper administration of the Canadian estate;

Receipt, review, discussion and attendance at meetings with estate legal counsel to review ongoing matters, reinsurance collections issues including set-off issues, claims settlement issues and various other estate matters as required;

Continued monitoring of the Reliance staff, including providing appropriate direction and assistance;

Meetings, discussions, review of assumptions and preparation of detailed runoff models projecting the runoff of the estate;

Discussions, receipt and review of various court motions to extend the date to which the Liquidator was authorized to make policy payments and the Meridian payments, and payments to defence costs;

Attendance at Court to hear the above noted motion;

- Continuing to deal with policyholder and claimants' telephone calls, e-mails, and correspondence requesting specific information pertaining to the liquidation or their specific claims;
- Continuing to deal with agents and brokers, especially trying to finalize the reconciliation of their accounts as at the date of liquidation;
- Performing a detailed claims review, discussion of potential outcomes with claims staff and attendance at meetings with the U.S. Liquidator's claims staff to review same;
- Attendance at meetings with actuarial consultant to perform an extensive review of policy liabilities as at March 31st, 2004;
- Receipt, review and discussion with the actuarial consultant, the results of his extensive review as performed above;
- Continued to review existing claims bordereaux in order to stratify claims as to dollar amounts, lines of business, and PACICC exposure;
- Review of new reported claims, discussions with claims adjudication staff and approving set-up of appropriate reserves;
- Continuing to liase with Reliance U.S. IT personnel to ensure the ongoing performance of the computer systems;
- Continuing to deal with numerous Meridian policyholder inquiries;
- Continued review and approval of defence and adjustment costs and authorizing payment of same;
- Continued attendance with third party administrators to ensure the continued processing and adjudication of claims under their control and ensuring that claims are adjudicated and settled according to the procedures established by the Liquidator;
- Continued monitoring and supervision of claims adjudication staff, approval of reserve changes, approval of claims settlements, approval of claims settlement costs and authorization of payment of same;
- Continued follow-up on reinsurance billings and collections;
- Continued to obtain shared reinsurance documentation from the U.S. Liquidator, particularly in respect of international and reinsurance policies;
- Continued liaison with U.S. Liquidator as to international reinsurance collections and commission expenses associated therewith;

- Supervision of build-out of new premises including all IT, data and voice requirements;
- Disposal of excess furniture and equipment;
- Overseeing move of operations to new premises;
- Providing information and analysis for the Inspectors as required;
- Preparation of appropriate accounting information and filing of appropriate non-tax statutory returns;
- Preparation of the December 31st, 2003, tax returns;
- Updating of the Reliance Canada website for the benefit of policyholders, claimants and creditors to enable them to obtain access to current information as to the status of the liquidation and their claims therein;
- Investigation of market conditions and trends, analysis of same, discussions with Inspectors and obtaining their approval for a new investment policy and implementation of same;
- Performed a detailed review of internal controls to ensure that the financial and operational controls are functioning as set forth in the Policies and Procedures;
- Overall administration of the estate and the Reliance staff consisting of approximately 8 people, dealing with day-to-day administrative issues, responding to policyholder, claimants' and creditor inquiries and attendance at all meetings, proceedings and/or court appearances as required.

Our fee:	\$624,408.90
Disbursements:	<u>13,556.41</u>
	637,965.31
GST	<u>44,657.57</u>
TOTAL	<u><u>\$682,622.88</u></u>

Schedule "M"

RELIANCE INSURANCE COMPANY
(in liquidation)

LISTING OF KPMG INC. PERSONNEL
HOURS AND AVERAGE HOURLY RATE
THREE MONTH PERIOD ENDED DECEMBER 31, 2003

<u>Name</u>	<u>Rank</u>	<u>Area</u>	<u>HOURS</u>	<u>AVG. HRLY RATE</u>
Sanderson, R. O.	President/Partner	Insolvency/Overall Ac	45.60	\$576
Gutfreund, G.	V.P./Senior Manager	Insolvency/Claims	224.50	\$445
Burgess, J.	Manager	Insolvency/Claims	238.00	\$288
Murphy, E.	V.P./Senior Manager	Financial Report/Rein	132.70	\$445
Individuals with less than 30 hours			102.20	\$224
			<u>743.00</u>	<u>\$372</u>

RELIANCE INSURANCE COMPANY
(in liquidation)

LISTING OF KPMG INC. PERSONNEL
HOURS AND AVERAGE HOURLY RATE
THREE MONTH PERIOD ENDED MARCH 31, 2004

<u>Name</u>	<u>Rank</u>	<u>Area</u>	<u>HOURS</u>	<u>AVG. HRLY RATE</u>
Sanderson, R. O.	President/Partner	Insolvency/Overall Ac	31.30	\$576
Gutfreund, G.	V.P./Senior Manager	Insolvency/Claims	186.00	\$445
Burgess, J.	Manager	Insolvency/Claims	184.90	\$288
Murphy, E.	V.P./Senior Manager	Financial Report/Rein	72.00	\$445
Individuals with less than 30 hours			14.00	\$106
			<u>488.20</u>	<u>\$384</u>

RELIANCE INSURANCE COMPANY

(in liquidation)

**LISTING OF KPMG INC. PERSONNEL
HOURS AND AVERAGE HOURLY RATE
THREE MONTH PERIOD ENDED JUNE 30, 2004**

<u>Name</u>	<u>Rank</u>	<u>Area</u>	<u>HOURS</u>	<u>AVG. HRLY RATE</u>
Sanderson, R. O.	President/Partner	Insolvency/Overall Ac	35.80	\$576
Gutfreund, G.	V.P./Senior Manager	Insolvency/Claims	192.50	\$445
Burgess, J.	Manager	Insolvency/Claims/Re	228.30	\$288
Murphy, E.	V.P./Senior Manager	Financial Report/Rein	128.70	\$445
Individuals with less than 30 hours			27.30	\$216
			<u>612.60</u>	<u>\$384</u>

KPMG INC.

(Quarter ending December 2003)

ROBERT O. SANDERSON – is President of KPMG Inc., a Chartered Accountant, Fellow of the Institute of Chartered Accountants of Ontario and a trustee in bankruptcy. He has primary responsibility for the liquidation as a whole. During this period, his particular areas of concentration were with respect to the development of the overall direction, approach and strategy for the estate, co-ordinating reporting to the supervising Court including passing of accounts, confirmation of continuance of payment of defence costs and small claims, ongoing liaison with PACICC, the U.S. Liquidator, the inspectors and major stakeholders, financial projections for the estate, responding to specific issues arising in the defence of claims and advising respective counsel as to projected outcomes.

I. GEORGE GUTFREUND – is a Vice-President of KPMG Inc. and a Chartered Accountant, a Certified Insurance Receiver and licensed trustee in bankruptcy. He is responsible for the general administration of the liquidation, including oversight of all financial and internal controls, human resources and office management. Mr. Gutfreund oversees the claims adjudication staff, liaises with PACICC concerning claims matters, participates as required in the formulation of the appropriate strategy, reviews and approves all significant reserve adjustments and is also responsible for the development and maintenance of the website. During this period he sought, found and negotiated a lease for new premises, oversaw the move of the Reliance operations and assisted in the passing of accounts.

ELIZABETH MURPHY – is a Vice-President of KPMG Inc. and a Chartered Accountant. Ms. Murphy has general responsibility for all reinsurance matters, management of the investment portfolio, communications with PACICC and the U.S. Liquidator and determination of actuarial liabilities. She is also responsible for financial reporting, and overseeing the accounting department. During this period she developed the financial statement format for use in the Court passing of accounts including determining issues in adhering to Canadian GAAP. She also oversaw a review of internal controls and compliance with liquidation policies and procedures.

JANINE BURGESS – is a Manager in the corporate recovery group. She assists Mr. Gutfreund with the claims adjudication process, analysis and stratification of claims, overseeing the Meridian and GAP programs, reviewing defence costs and contracted for and supervised the move of the Reliance operations. Janine also developed runoff models and a revised investment policy under the direction of Ms. Murphy and/or Mr. Gutfreund.

KPMG INC.

(Quarter ended March 2004)

ROBERT O. SANDERSON – is President of KPMG Inc., a Chartered Accountant, Fellow of the Institute of Chartered Accountants of Ontario and a trustee in bankruptcy. He has primary responsibility for the liquidation as a whole. During this period, his particular areas of concentration were with respect to the development of the overall direction, approach and strategy for the estate, co-ordinating reporting to the supervising Court including confirmation of continuance of payment of defence costs and small claims, ongoing liaison with PACICC, the U.S. Liquidator, the inspectors and major stakeholders, financial projections for the estate, responding to specific issues arising in the defence of claims and advising respective counsel as to projected outcomes.

I. GEORGE GUTFREUND – is a Vice-President of KPMG Inc. and a Chartered Accountant, a Certified Insurance Receiver and licensed trustee in bankruptcy. He is responsible for the general administration of the liquidation, including oversight of all financial and internal controls, human resources and office management. Mr. Gutfreund oversees the claims adjudication staff, liaises with PACICC concerning claims matters, participates as required in the formulation of the appropriate strategy, reviews and approves all significant reserve adjustments and is responsible for the maintenance of the website. During this period the detailed claims review was completed and reviewed with the inspectors.

ELIZABETH MURPHY – is a Vice-President of KPMG Inc. and a Chartered Accountant. Ms. Murphy has general responsibility for all reinsurance matters, management of the investment portfolio, communications with PACICC and the U.S. Liquidator and determination of actuarial liabilities. She is also responsible for financial reporting, and overseeing the accounting department.

JANINE BURGESS – is a Manager in the corporate recovery group. She assists Mr. Gutfreund with the claims adjudication process, analysis and stratification of claims, the detailed claims review, overseeing the Meridian and GAP programs, and reviewing defence costs. Janine also developed runoff models and a revised investment policy under the direction of Ms. Murphy and/or Mr. Gutfreund.

KPMG INC.

(Quarter ended June 2004)

ROBERT O. SANDERSON – is President of KPMG Inc., a Chartered Accountant, Fellow of the Institute of Chartered Accountants of Ontario and a trustee in bankruptcy. He has primary responsibility for the liquidation as a whole. During this period, his particular areas of concentration were with respect to the development of the overall direction, approach and strategy for the estate, co-ordinating reporting to the supervising Court including confirmation of continuance of payment of defence costs and small claims, ongoing liaison with PACICC, the U.S. Liquidator, the inspectors and major stakeholders, financial projections for the estate, responding to specific issues arising in the defence of claims and advising respective counsel as to projected outcomes.

I. GEORGE GUTFREUND – is a Vice-President of KPMG Inc. and a Chartered Accountant, a Certified Insurance Receiver and licensed trustee in bankruptcy. He is responsible for the general administration of the liquidation, including oversight of all financial and internal controls, human resources and office management. Mr. Gutfreund oversees the claims adjudication staff, liaises with PACICC concerning claims matters, participates as required in the formulation of the appropriate strategy, reviews and approves all significant reserve adjustments and is responsible for the maintenance of the website. During this period the detailed claims review was completed and reviewed with the inspectors.

ELIZABETH MURPHY – is a Vice-President of KPMG Inc. and a Chartered Accountant. Ms. Murphy has general responsibility for all reinsurance matters, management of the investment portfolio, communications with PACICC and the U.S. Liquidator and determination of actuarial liabilities. She is also responsible for financial reporting, and overseeing the accounting department. During this period a full actuarial review was undertaken including additional liaison with the actuary as a result of the comprehensive claims review undertaken in part with representatives of the U.S. Liquidator. In conjunction with Ms. Burgess, she reviewed the overall investment approach and selected RBC Asset Management Inc. as the asset manager.

JANINE BURGESS – is a Manager in the corporate recovery group. She assists Mr. Gutfreund with the claims adjudication process, analysis and stratification of claims, the detailed claims review, overseeing the Meridian and GAP programs, and reviewing defence costs. Janine also updated runoff models to reflect the results of the comprehensive claims review, staff reductions, projected runoff of claims and additional reinsurance characteristics, and a revised investment policy under the direction of Ms. Murphy and/or Mr. Gutfreund including RBC Asset Management Inc.