UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

TPG GROUP, WILLIAM HUTCHISON	:	No. 08 Civ. 11244 (SHS)
Plaintiffs,	:	
-against-	:	
ALTERNATIVE RE HOLDINGS LIMITED, ALTERNATIVE RE LIMITED, ARCH INSURANCE COMPANY	:	
Defendants.	:	

PLAINTIFFS' OPPOSITION TO DEFENDANTS' MOTION TO STAY AND REQUEST FOR LEAVE TO TAKE DISCOVERY AS TO FACTUAL ISSUES RELEVANT TO DEFENDANTS' MOTION

Dated: March 16, 2009

THORP REED & ARMSTRONG LLP
Ira B. Silverstein, No. 17658
2005 Market Street, Suite 1910
Philadelphia, PA 19103
Tel: 215-640-8500
Fax: (215) 640-8501

Attorneys for Plaintiffs

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MEMORANDUM OF LAW IN SUPPORT OF PLAINTIFFS' OPPOSITION TO DEFENDANTS' MOTION TO STAY AND REQUEST FOR LEAVE TO TAKE DISCOVERY AS TO FACTUAL ISSUES RELEVANT TO DEFENDANTS' MOTION

I. INTRODUCTION

In their Motion to Stay, the Defendants Alternative Re Holdings Limited ("ARH") and Alternative Re Limited ("Alt Re") assiduously avoid any analysis or even repeated mention of the agreement that is the basis of Plaintiffs' Complaint and their request for relief from this Court.[1] This Settlement Agreement ("Settlement"), entered into by ARH, the Plaintiffs and others, on December 30, 2005, was fraudulently induced in that, without disclosure, it more than doubled the Plaintiffs' participation in and liability for the reinsurance of a program that was already in deficit and had no chance of future profitability. *See* Affidavit of William Hutchison, ("Hutchison"), Exhibit E. Defendants, the managers and operators of all aspects of the NBG program ("Program"), induced the Plaintiffs to join in the Settlement through omissions and misrepresentations of material facts

[1] As Defendant Arch Insurance Company has joined Defendants ARH/Alt Re's motion to stay and its separate motion offers no substantively different arguments, the Plaintiffs respond to both motions in this single opposition.

regarding the quality of the underlying business, the financial condition of the reinsurance captive, and the value and purpose of the Settlement.

The Settlement leaves no doubt that a remedy for these misrepresentations exists and that the forum for pursuing the remedy is this Honorable Court. The Settlement explicitly provides that:

> A party shall indemnify and hold harmless any other party injured hereto or incurring or suffering any loss, damage or injury as a result of or connected to failure of any representation or warranty or breach of this Agreement by that Party. Hutchison Ex. E at 3.

And it further provides:

> This Agreement shall be interpreted in accordance with the law of the State of New York without giving effect to any choice or conflict of law provision or rule that would cause the application of the laws of any jurisdiction other than New York....The exclusive forum and venue for the resolution of disputes regarding the other Parties [including TPG and Hutchison] shall be the U.S. District Court for the Southern District of New York. *Id.* at 8.

Despite this fairly unequivocal language, ARH and Alt Re have moved this Court to stay the present action and compel a Bermuda arbitration relying on an arbitration clause contained in shareholders agreements executed in April 2007. They offer no explanation as to why the Settlement's dispute resolution clause should be ignored nor do they confront the fact that ARH's affiliated accomplices in the fraud, Alt Re (manager of the captive) and Arch Insurance Company ("Arch") (manager of the underlying insurance), are not parties to any shareholder agreements with Plaintiffs that might require the arbitration of disputes.[2] Moreover, even were this Court to conclude that some ambiguity exists as to the appropriate forum and that such ambiguity should not be resolved against the Defendants, if only because they were the drafters of both agreements, there are questions of fact that need to be resolved as predicates to choosing the appropriate venue. These issues include (i) the beneficiary relationship between the three Defendants (ii) the mechanism by which the Plaintiffs, as ARH shareholders, became liable for Alt Re losses; and (iii) the efficacy of

[2] Throughout the Opposition we refer to Arch, Alt Re, and ARH collectively as the "Arch Cap companies."

the agreements that Defendants rely upon in demanding arbitration.

Ultimately, the pending motions turn not, as Defendants seemingly wish this Court to believe, on a debate about the scope and applicability of an arbitration clause. The scope and applicability of the arbitration clause, *even if the dubious bona fides of the 2007 Agreements are ignored*, is irrelevant to this proceeding. Rather, at issue is the scope and applicability of the Settlement's clear and unequivocal dispute resolution clause. Plaintiffs submit that the Complaint, amended as well as originally filed, sets forth claims that are solidly grounded in the Settlement and the Defendants' role in its negotiation.

II. BACKGROUND

A. The Structure of the Program

Arch Capital Ltd., a Bermuda corporation, through its subsidiaries, including ARH, specializes in structuring and managing "alternative market solutions," such as off-shore reinsurance captives. Alt Re is a wholly-owned subsidiary of ARH operating as a Bermuda segregated accounts company ("SAC").[3] An SAC holds or manages segregated accounts or cells that contain assets and liabilities that are legally separated from the assets and liabilities of the SAC's general account as well as from other cells. The purpose of this statutory scheme is to protect the assets of one cell from the liabilities of another, thereby taking the concept of limited liability to a micro level. ARH utilizes this SAC structure to facilitate investor participation in the financial experience of U.S. insurance risks initially assumed by Arch Capital's wholly owned subsidiary, Arch. This participation is effected through the purchase of ARH "shares" that are somehow related to Alt Re's segregated cells. *See* Affidavit of Ira Silverstein ("Silverstein"), Ex. J. By such means, Arch offers investors in ARH financial participation in specific programs, or types of risk, written on Arch paper

[3] Alt Re operates pursuant to the "Alternative Re Limited Consolidation and Amendment Act 2004," a private act

and reinsured by Alt Re. The three companies, all owned by Arch Capital, are separate in form only. In the instant case, Arch was the producer, manager, and the beneficiary of the entire scheme, including the Settlement.[4]

As explained more fully in the Complaint, Plaintiffs were persuaded to invest in the Program after an investment meeting with Thomas Kozal of Arch. *See,* Original Complaint at ¶ 20-24. National Benefits Group ("NBG"), Arch's managing general agent, wrote domestic workers compensation business on Arch paper for three separate years, from April 2001 through October 2003. At first, Arch was a *fronting* carrier on the Program *i.e.*, it retained no risk at the ceding level. NBG sold the Arch policies, collected the premiums, and paid the claims. Arch and NBG each took a percentage of the gross written premium as commission and ceded the remaining 68.5% (of premium) along with 100% of the risk to Alt Re. All the liabilities and assets of the business ceded by Arch to Alt Re were limited to its cell 13B. Investors participated in the reinsurance of the Program through the purchase of ARH shares. In addition to the purchase of shares, investors were required to post collateral proportionate to their share of participation. Hutchison Ex. E, Trudeau Ex. B. Shareholder collateral, in combination with the net premium, constituted the capital Alt Re used to pay reinsurance claims on the Program.[5] Alt Re ostensibly maintained 13B's books and records, paid its taxes, administered the reinsurance, and managed the investment of the net premium and the investors' collateral; like Arch, it retained no risk in the transaction. If losses, or claims, on the Program exceeded the net premium held by Alt Re they would erode the investors' collateral. Such possible losses were to be off-set by investment income and ultimately, the

[4] ARH and Alt Re, two Bermuda legal entities, consist of the same handful of clerical employees housed in the same office space in Bermuda. Plaintiffs, when inquiring about 13B, were routinely directed to personnel in Arch's New York offices. Hutchison at ¶ 14, Trudeau at ¶ 12.

[5] 13B's assets were held in trust for Arch in order that it meet statutory requirements for credit for reinsurance.

attachment of other, specific and aggregate, stop loss reinsurance ("Other Reinsurance").[6] Hutchison Ex. B. As represented to the Plaintiffs, in the worst case, they might lose their collateral.

As required by the Shareholder Agreements, Plaintiffs posted collateral for the first two years of the Program. Hutchison posted $200,000 reflecting a 19.05% participation in year one and $175,000 reflecting a 21.85% participation in year two. TPG posted $250,000 reflecting a 23.81% participation in year one and $100,000 reflecting a 12.48% participation in year two. Both Plaintiffs declined to participate in year three. As would be expected, NBG participated in all three years of the Program as this was "captive" reinsurance. NBG posted $100,000 reflecting a 9.52% participation in year one and $226,000 reflecting a 28.21% participation in year two. Hutchison Ex. D. Plaintiffs are uncertain of NBG's percentage participation in year three or other investors' participation, generally.[7]

In October 2003, Arch terminated the Program six months prior to the completion of the third year, without explanation. In January 2004, Arch terminated its Managing General Agency Agreement ("MGA Agreement") with NBG and moved the claims handling for the Program to a different administrator. Hutchison, Ex. A. The Program was now in run-off. All applicable claims had been made and all premiums collected. As a closed book of business, the value the Program as well as the 13B investment might now be calculated with some certainty. Only ARH/Alt Re, however, had the ability to make that calculation.

B. The Shortfall in Collateral Funding

For nearly two years after the business they reinsured had closed, the Plaintiffs heard nothing about their investment. On February 11, 2005, for the first time, ARH advised Plaintiffs and other

[6] In the first and second years of the Program Arch purchased specific excess reinsurance of $750,000 xs 250,000 per loss and $5,000,000 of aggregate stop loss cover that attached at 90 percent of gross written premium. Hutchison, Ex. B.

[7] Arch had a 50% participation in year two. Although Arch is a 13B shareholder it did not sign or participate in the Settlement and no information regarding Arch's participation or investment income has ever been shared with Plaintiffs.

investors that there was a $1,107,584 "shortfall" in funding for cell 13B. Hutchison Ex. D. The investors, ARH claimed, would have to post additional collateral proportionate to their share of participation, in accordance with the Shareholder Agreements.[8] ARH provided no explanation for the alleged shortfall (*e.g.*, a catastrophic loss or dramatic change in reserving requirements) or the reason for the sudden and late notice of such a large sum. This urgent demand quickly turned into heated negotiations between NBG, on the one hand, and Arch, Alt Re, and ARH, on the other (the "warring parties"). It was clear that the shortfall, whatever its origin, had nothing to do with Plaintiffs. The Plaintiffs, as passive but concerned investors, awaited the outcome of the struggle between the warring parties over *their* dispute and *their* shortfall.

In December 2005, Plaintiffs were presented with the Settlement that was the result of the eleven months of negotiation between the warring parties' legion of lawyers. At no time were Plaintiffs represented by counsel as they had fulfilled all of *their* obligations under the Shareholder Agreements. Indeed, there was no real necessity to include the Plaintiffs in any settlement the warring parties might enter into. Arch could have assumed NBG's "shares" or found other investors, *if* the shares had value. Instead, however, the Arch Cap companies attempted to sell the Settlement to Plaintiffs with a mixture of promises and threats. Plaintiffs were told that the Settlement would collateralize 13B, remove quarrelsome participants, and enable 13B investors to make a profit. Should they refuse, Plaintiffs were told they would remain liable for their proportionate share of the unexplained shortfall. The Arch Cap companies' representatives sweetened their offer, and seemingly confirmed their sanguine representations, by promising

[8] The assertion by the Defendants and their counsel, *nee* threats, that the Plaintiffs were liable for NBG's collateral funding is completely erroneous. Plaintiffs were shareholders in the "profits and losses" of 13B. Both Profits and losses are defined terms in the Shareholder Agreements, and the failure of a separate shareholder to post collateral under any reading of the agreements is not a loss.

Plaintiffs $100,000 each in "profit" upon execution of the Settlement. Believing these representations, and fearing the consequences of a failed settlement, the Plaintiffs signed.

C. The Settlement Is the Basis of Plaintiffs' Action and The Locus of Defendants' Fraud

The Defendants attempt to cast the disputes that gave rise to the Settlement as one between "shareholders", but those disputes were solely and unequivocally between the Arch Cap companies (manager of the Program and reinsurance captive) and Arch's managing general agent, NBG (producer of the business and the captive's captee). However, through their misrepresentations and material omissions regarding the value of the Settlement and the financial state of 13B, Defendants shifted the entire burden of *their* settlement to Plaintiffs.

The settlement included a Settlement and a series of actual or putuative collateral agreements that were to implement the Settlement's terms. These settlement documents included: (i) the Settlement, (Hutchison Ex. E); (ii) two separate Shareholder Amendment Agreements ("Amendments") (Hutchison Ex. F, G); (iii) the Second Shareholder Amendment Agreement (Hutchison Ex. H); (iv) two Power of Attorney agreements ("POAs") (Hutchison Ex. I and Trudeau Ex. J); and (v) two Shareholders Agreements (the "2007 Agreements" that were executed via the questionable use of the POAs) (Hutchison Ex. J and Trudeau Ex. L) (collectively, the "Settlement Documents").[9] These Settlement Documents, all purportedly effective December 30, 2005, are explicitly referred to as part-and-parcel of a single settlement.[10]

The "Parties" to some or all of the Settlement Documents are NBG, National Comp America, Inc., Alan Hoover, Ken Harrison, Rodney Threatt (collectively, the "NCA Parties"), ARH, TPG,

[9] Defendants allege in their Motion to Stay that the Second Shareholder Amendment was never executed. Plaintiffs deny this assertion; however, the binding authority of the Second Amendment is not germane to the current motion.

[10] Plaintiffs suspect that there are other settlement documents entered into between Arch and NBG that have not been disclosed but are material to the current dispute.

Hutchison, Decker HIO, LLC ("Decker"), Gordon Ogden ("Ogden"), and Henry De Francesco ("De Francesco").[11] Hutchison F-H at 1. The Settlement and the Amendments further define TPG, Hutchison, Decker, Ogden and De Francesco as "Current Shareholders" and TPG, Hutchison, and Decker as the "New Shareholders." *Id.* at 2.[12]

1. The Settlement Was the Means By Which Defendants Fraudulently Imposed Liability on the Plaintiffs and All Disputes In Connection With the Settlement Are to Be Resolved in New York Under New York Law

a. The Settlement is Governed by New York Law and ARH/Alt Re Irrevocably Submitted to the Jurisdiction of this Court

The Settlement is unequivocal about the applicable law as well as the exclusive jurisdiction of this Court over any dispute arising therefrom. The Settlement's jurisdiction clause in full reads:

> Applicable Law. This Agreement shall be interpreted in accordance with the law of the State of New York without giving effect to any choice or conflict of law provision or rule that would cause the application of the laws of any jurisdiction other than New York. The exclusive forum and venue for resolution of the disputes arising from this Agreement regarding the NCA Parties shall be the federal or state courts located in Mecklenburg County, North Carolina. The exclusive forum and venue for the resolution of disputes regarding the other Parties shall be the U.S. District Court for the Southern District of New York. **Each party irrevocably submits to the exclusive jurisdiction (both subject matter and personal) of such applicable courts and irrevocably and unconditionally waives (i) any objection they may now or hereafter have to venue in such court, and (ii) any claim that any action or proceeding brought in such court has been brought in an inconvenient forum.** Hutchison Ex. E at 8 (emphasis in the original).

New York law unequivocally governs the Settlement. The clause makes a distinction, however, between the forum and venue for disputes for the "NCA Parties" and the "other Parties." The exclusive forum and venue for the resolution of any disputes for the NCA Parties "shall be the federal or state courts in Mecklenburg County, North Carolina." Id. The "other Parties" are the

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[11] The Settlement Documents refer to Alternative Re Holdings Limited as Alt Re, whereas I have used ARH. In order to be clear as well as consistent with other court filings, I have continued to use ARH throughout this brief.

[12] NBG and NCA are or were closely related entities, and all of NCA Parties were employed by, or were owners in, one or both of these entities. The role of some of the NCA Parties in the Settlement or the Program is unclear to Plaintiffs. The remaining non-NCA Parties, except ARH, are or were investors in cell 13

non-NCA Parties *i.e.*, the shareholders in 13B, including Plaintiffs. The exclusive forum and venue for the resolution of any disputes arising from the Settlement regarding the Plaintiffs "*shall* be the U.S. District court for the Southern District of New York." Id. (emphasis added). Moreover, ARH/Alt Re and Plaintiffs irrevocably submitted to the jurisdiction (both subject matter and personal) of this Court and unconditionally waived any objection they "may now or hereafter have to venue" in this Court. Id.

Strangely, the Defendants' Motion to Stay does not quote or even reference the Settlement's jurisdiction clause. Instead, Defendants have chosen to rely on the purported breadth of the arbitration clause contained in the 2007 Agreements, executed by the Arch controlled attorney-in-fact without Plaintiffs' knowledge or permission, in an attempt to divert this Court's attention as to the nature of the Plaintiffs' claims. Defendants' expert, Mark Chudleigh, also fails to mention the Settlement, its jurisdiction clause, or discuss how it might affect his reading of the various shareholder agreements. *See* Declaration of Mark Chudleigh. This despite the fact the Settlement references, defines, and incorporates the original Shareholder Agreement and, thereby, its arbitration clause.

The Settlement does not shy away from the authority of the original Shareholder Agreements and neither do Plaintiffs at this point. The Shareholder Agreements means those agreements

> entered into between the Parties evidencing the collateral funding requirements and responsibilities of the parties with regard to the Account [13B]. The Shareholder Agreements are incorporated herein by reference. Hutchison Ex. E at 2.

Moreover, Plaintiffs, as New Shareholders, explicitly ratified the existing Shareholder Agreements in Settlement. The Settlement, therefore, acknowledges and contains two jurisdictions clauses; however, they are not competing clauses. They are two different clauses with two different fora. Each jurisdiction clause has its own integrity and its own sphere of applicability. Even if the Plaintiffs were to accept Defendants' characterization of the arbitration clause as "broad," which we

do not, any disputes between ARH and Plaintiffs would be subject to Bermuda law and Bermuda arbitration, *except* those disputes between ARH and Plaintiffs in connection with the Settlement.[13]

The Defendants have only sparingly quoted the arbitration clause that is basis of their Motion to Stay. It reads, in part:

> All disputes between the Company and the Shareholder which are not settled between the Parties will be submitted to arbitration in Bermuda by a panel of three arbitrators…To the extent that any such dispute is not subject to arbitration, and unless otherwise required by law, the courts of the Islands of Bermuda will have exclusive jurisdiction of such dispute. Hutchison Ex. J at 4.

This excerpt from the 2007 Agreement's arbitration clause anticipates and acknowledges the possibility of non-arbitral disputes, including those that may, by force of law, come under the law of another jurisdiction. No finer example of the meaning of this exception can provided than the current action which, by means of the Settlement and its terms, is explicitly exempt from arbitration and the laws of Bermuda. ARH, for its own reasons, chose to resolve all disputes with Plaintiffs in connection with the Settlement in this Court under New York law. Nothing in the Shareholder Agreements, the Amendments, or any of the Settlement Documents changes that fact.

b. Defendants Fraudulently Imposed Liability On The Plaintiffs as New Shareholders By Means of the Settlement

Although the Arch Cap companies benefited in untold ways from the Settlement it cost them nothing, save their forbearance in bringing unknown legal proceedings against NBG. The Arch Cap companies, through ARH, shifted its entire burden in Settlement with NBG to the Plaintiffs through multiple misrepresentations and material omissions. In the Settlement, NBG agreed to assign "any and all rights and benefits that may be derived from shares in the Account to New Shareholders to *divide* between them as they shall solely determine." Hutchison Ex. E at 4 (emphasis added). While ARH, in turn, accepts

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[13]

> that all the liability and rights of the Account shall be solely vested with and in the New Shareholders, and [ARH's] obligations under the Shareholder Agreements will be due to New Shareholders. *Id.* at 4.

The New Shareholders

> hereby ratify The Shareholder Agreements and agree to undertake all of the duties and the obligations of the shareholders pursuant to The Shareholder Agreements with regard to the Account. *Id* at 5.

The New Shareholders, hereby, not only assumed the duties and obligations of NBG but the duties and obligations of the shareholders pursuant to the original Shareholder Agreements in regard to "the Account" (*i.e.*, 13B). As New Shareholders, Plaintiffs, *per* the Settlement, were now fully liable for the entirety of the reinsurance for the first two years of the Program.

As part of the Settlement, the parties entered into Shareholder Amendment Agreements, effective December 30, 2005, that divided liability *between* the New Shareholders and formally released departing shareholder collateral. Hutchison Ex. F-H, Trudeau Ex. G-I. The Amendments do not contain a jurisdiction clause nor an arbitration clause; they do contain an applicable law clause, which reads:

> This Agreement shall be interpreted in accordance with the laws of the Bermuda without giving effect to any choice or conflict of law provision or rule that would cause the application of the laws of any jurisdiction other than Bermuda. The parties hereto agree to consolidated arbitration proceedings in the event of any dispute under the terms of the Shareholder Agreements, *as amended.* Hutchison Ex. F, G at 7, Ex. H at 6 (emphasis added).

The Amendments are to be interpreted under Bermuda law and their applicable law clause applied to the original Shareholder Agreements, as amended *i.e.*, exclusively with respect to the terms of the Amendments. The Amendments applicable law clause does not establish an independent basis for jurisdiction but merely amends the original Shareholder Agreements' arbitration clause, providing for "consolidated proceedings."

Like the original Shareholder Agreements, on which they depend, the Amendments do not infringe upon the established authority of the Settlement's jurisdiction. The Amendments are, in fact, part of the Settlement. This is acknowledged both by ARH's reaffirmation, in the Amendments, of its "Settlement covenants" as well as the Amendments' the final paragraph:

> IN WITNESS WHEREOF, the undersigned have executed this Settlement Agreement and hereby warrant that they have read the foregoing, understand its contents, and that they are fully properly authorized to execute this document. *Id.* at 8.

The Amendments provide that the "Settlement Agreement means the Confidential Settlement Agreement entered into by the Parties and NBG to resolve a dispute between Alt Re and NBG in connection with collateral on the Account." Hutchison Ex. F-H at 2. This definition and concluding paragraph appear in identical form in the Settlement (Hutchison Ex. E), the Amendments (Hutchison Ex. F, G), and the Second Shareholder Amendment (Hutchison Ex. H).

2. Plaintiffs' Action Is Grounded in Defendants' Material Omissions and Misrepresentations in Settlement

a. The Disputes that Gave Rise to the Settlement were Never Disclosed to Plaintiffs and Were Material to the Business Reinsured

The dispute that gave rise to the Settlement is repeatedly defined in the Settlement Documents: "The Dispute means the *disputes* between [ARH] and the NCA Parties over the collateral funding for The Account or the Alleged Investment." *Id* at 2 (emphasis added). This definition appears in all of the Settlement Documents. Despite the definition, the Settlement's covenants reveal that the disputes, whatever their subject matter, involved more than these two parties. NBG covenants to

> "pay $761,385.03 and $15,000 to [ARH's] counsel's trust account, to be disbursed only when the Letters of Credit posted by the NCA Parties have been duly released...and the NCA Parties have received a signed Covenant Not To Initiate Proceedings from *Arch Insurance Company.*" Hutchison Ex. E at 4 (emphasis added).

NBG's covenant is contingent upon receiving a separate covenant from Arch, a non-signatory to the Settlement. Arch, of course, would have no cause of action against NBG regarding the collateral funding as that was a requirement of the Shareholder Agreements. Only ARH, the issuer of the 13B securities, could sue for a failure to perform under those agreements. ARH, for its part, covenants to

> indemnify, save and hold NBG, NCA, Hoover, Harrison and Threatt harmless from and against any claim, suit, action or court proceeding by *Arch Capital, Inc.*, or any parent, subsidiary or affiliate thereof, concerning the Account or The Dispute or the Alleged Investment." *Id.* at 4 (emphasis added).

Again, if the disputes were related solely to the collateral funding an indemnification from Arch Capital, Inc., a Bermuda holding company, would be unnecessary.

In his declaration, Gavin Collery, an officer of Alt Re and ARH, proffers two e-mails as evidence of Plaintiffs direct involvement in negotiating the Settlement and their full awareness of the numerous of disputes between the warring parties. Collery Declaration at ¶13-15. The first is an e-mail, dated November 3, 2005, authored by Donald Trudeau, the owner of TPG, wherein, acting as go-between, he seeks confirmation from ARH's outside counsel regarding ARH's settlement terms before forwarding them to NBG's outside counsel. Collery Declaration Ex. C. The second e-mail, dated December 13, 2005, consists of a series of exchanges between these same counsel that mentions, without describing, the existence of a separate dispute between Arch and NBG. *Id* at Ex. D. The Plaintiffs are copied on the final exchange between counsel. On the basis of these two e-mails, Mr. Collery finds it "inconceivable" that Plaintiffs were unaware of the numerous disputes between NBG and the Arch Cap companies. *Id* at ¶ 14.

The issue, however, is not whether the Plaintiffs were involved in any settlement negotiations or if they knew of the *existence* of disputes between Arch and its agent, NBG. The Settlement made Plaintiffs -- who each held less than a 20% participation in 13B prior to December 30, 2005 -- fully liable for the reinsurance of an $8m insurance Program. ARH's ability to

successfully shift this liability to Plaintiffs would necessarily involve their "participation". The pertinent issues, with respect to the disputes on the eve of the Settlement, are (i) did Plaintiffs fully know the nature and substance of the disputes between Arch and its agent, NBG; (ii) did those disputes in any way affect the business that the Arch Cap companies induced Plaintiffs reinsure 100%; and (iii) if so, did each of the Arch Cap companies fulfill their duties, both fiduciary and contractual, in disclosing that vital information at the time they induced the Plaintiffs to agree to the Settlement. We already know the answers to nos. (i) and (iii). Plaintiffs knew nothing of the details of the disputes between Arch and NBG. And Mr. Collery, in his affidavit, does not even suggest that the Arch Cap companies made any such disclosures to Plaintiffs. Discovery will reveal if Arch's disputes were material to the business reinsured by Plaintiffs.

b. Defendants Failed to Properly Disclose the Value of the Settlement and 13B, Thereby Wrongfully Inducing Plaintiffs to Accept the Settlements and its Terms

At the time of the Settlement, Defendants had an obligation to accurately disclose (i) the financial status of the Program; (ii) the financial status of 13B; and (iii) the value the Settlement for the Plaintiffs, as New Shareholders. The Defendants, however, either misrepresented or concealed this vital information and thereby induced Plaintiffs to accept the Settlement. The Defendants' obligations to Plaintiffs did not arise because the Plaintiffs were Current Shareholders but arose due to Plaintiffs' status as New Shareholders under the Settlement. If, prior to December 30, 2005, Plaintiffs had no interest in 13B the Defendants would have owed them the exact same duties of disclosure in Settlement.

At the time the Arch Cap companies' made its misrepresentations and omissions, both the Program and cell 13B were susceptible to valuation. The book of business reinsured by Plaintiffs had been closed for nearly three years (*i.e.*, no new premium and no new claims). After the initial deposit of net premium, 13B's only income derived from the investment of that premium, which

never even equaled Alt Re's annual management fee. The cell, however, did have a continuing stream of outgoing payments for taxes, management fees, and, most importantly, reinsurance claims on the underlying workers compensation business. The financial assessment of a mature, run-off book of uniform (workers comp) claims should have been a relatively straight forward arithmetical exercise. One need only measure the actuarial development of the claims and the captive's (13B's) fixed expenses against the captive's assets and the attachment of the Other Reinsurance. This type of valuation is the business of the Arch Cap companies; it is the expertise they sell to investors.

The Arch Cap companies had almost certainly undertaken such a financial evaluation for their own purposes prior to the settlement. Arch, Alt Re, and ARH, each had a distinct, proprietary interest in any agreement that would release the captive's only captee, NBG. The Arch Cap companies certainly knew the value of the Program (Arch), the value of the 13b (Alt Re), and the value of 13B shares (ARH) before compromising NBG's funding requirements and other contractual obligations through Settlement. The affidavits submitted to this Court by the Arch Cap companies are silent as to the value of the Settlement, the value of the 13B shares, and the financial status of 13B on December 30, 2005. The Defendants did not have the luxury of such silence when they induced Plaintiffs to accept the Settlement and its terms. Arch was the manger of the Program *and* manager of NBG; Alt Re was the manager of the captive, 13B; and ARH was the issuer of the shares in 13B, and counterparty with Plaintiffs as well as NBG. As we have seen, each of these Defendants explicitly benefited from the Settlement. These Defendants -- as managers, as counterparties, as fiduciaries, and beneficiaries of the Settlement -- had multiple obligations to Plaintiffs, the New Shareholders, that were breached in signing Plaintiffs up for what they knew, or should have known, was a certain loss.

3. There is No Evidence That the 2007 Agreements, the Basis of Defendants' Arbitration Demand, Ever Came Into Existence; If The 2007 Agreements did Lawfully Come into Existence, They Have no Bearing on Plaintiffs' Action

Prior to the Settlement, Defendants engaged Graham Collis of Conyers, Dill to draft Power of Attorney agreements for 13B shareholders that would enable ARH/Alt Re to implement the Settlement through a single representative of the investors.[14] Hutchison Ex. I, Trudeau Ex. J. Plaintiffs entered into the Settlement, the Amendments, and the POAs at roughly the same time, all as part of the Settlement Documents. A POA for each Plaintiff was signed on February 13, 2006. The POAs provide that Mr. Collis, as lawful agent for Plaintiffs, may "make, sign, or otherwise enter into the Shareholders Agreement dated December 30th, 2005...which *shall be provided to the [Plaintiffs] in advance of execution.*" Hutchison Ex. I (emphasis added). These shareholders agreements were intended to be part of the Settlement, the final addition to the Settlement Documents. Defendants, however, did not issue new shares nor seek to enter into any new shareholder agreements with Plaintiffs during the entirety of 2006.

In June 2006, only six months after the Settlement, Plaintiffs were made aware of a "new" deficit in 13B. This news generated surprise, frustration and inquiries from Plaintiffs. Based on Plaintiffs' response, the Defendants, especially Mr. Collery, understood that he might have difficulty in collecting on this "new" deficit. Turning to the Settlement and the Amendments, however, could not have provided Mr. Collery with much comfort. The Settlement Documents make clear that the Plaintiffs had only assumed the "liabilities and obligations" of the departing shareholders; they were not actually holders of the departing shareholders' shares. Hutchison Ex. E. Any lawsuit by ARH/Alt Re against Plaintiffs would lead directly back to, and be based on, their assumption of liability in the Settlement. Undoubtedly more alarming for Mr. Collery was the fact that the

[14] Conyers Dill was hired and paid by ARH/Alt Re. Conyers Dill regularly represent Arch Capital, Inc.

Settlement unequivocally provided that disputes in connection with the Settlement were to be resolve in New York under New York law.

Therefore, on April 3, 2007, now 16 months since the execution of the Settlement and more than 48 months since the close of the business reinsured, the Defendants undertook to "issue" shares in the known losses of 13B. Under the purported authority of the POAs, ARH instructed Mr. Collis to authorize the 2007 Agreements on behalf of the Plaintiffs. Defendants, however, were not content to merely update the original Shareholder Agreements to reflect Plaintiffs' new participation *per* the Settlement. Instead, Defendants undertook a wholesale revision of the original Shareholder Agreements, including: (i) sec. 6 "Indemnification of the Company"; (ii) sec. 7 "Investments"; (iii) sec. 9 "No Reliance on the Company"; and, significantly, (iv) sec. 12 "Arbitration". Defendants continued their revisions with respect to the Shareholder Agreements' "Addendum 1", which defines shareholder profits and losses: (i) "Profits and Losses"; (ii) "Earned Reinsurance Premium"; (iii) "Distributions"; and (iv) "Acceptable Security", are all substantively and materially changed. (A black-lined comparison of these documents is attached as Silverstein Exhibit K).

The POAs only gave authorization for the creation of shareholder agreements in order to effectuate the terms of the Settlement. Plaintiffs, had they been presented with the 2007 Agreements, would have had every expectation the new agreement would be on the same terms as the original but for Plaintiffs' increased level of participation. The POAs explicitly require that any new agreements be provided to Plaintiffs prior to execution for their approval. Defendants' unauthorized wholesale revision of the original agreements' terms was quite simply unlawful. Neither in their motion nor in their affidavits have Defendants offered proof that the 2007 Agreements (i) were ever sent to or received by Plaintiffs prior to April 3, 2007, as required by the POAs; (ii) were ever approved by Plaintiffs prior to April 3, 2007, as required by the POAs; (iii)

ever resulted in new shares being issued to Plaintiffs; (iv) ever resulted in Plaintiffs being registered holders of such new shares; or (v) resulted in Plaintiffs paying for such shares. Neither Mr. Hutchison nor Mr. Trudeau, President of TPG, ever remembers having spoken with or met Mr. Collis. Hutchison at ¶ 16, Trudeau at ¶ 14. And Mr. Collery, in his affidavit, neither acknowledges the revisions nor indicates that he disclosed them to Plaintiffs prior to "issuing" these shares. Significantly, there is no affidavit from Mr. Collis regarding his communications with Plaintiffs or the revisions in the 2007 Agreements.

Had the 2007 Agreements lawfully come into existence they would form part of the Settlement Documents, the documents implementing the Settlement's terms. As such, the 2007 Agreements would sit along side the other Settlement Documents -- the original Shareholder Agreements and Amendments -- providing a different forum for different disputes *i.e.*, those disputes not covered by the explicit grant of jurisdiction contained in the Settlement.

III. ARGUMENT

A. Plaintiffs' Complaint Falls Squarely Within The Parameters of Settlement's Jurisdiction Clause And Its Claims Predominate The Disputes Between The Parties

The Federal Arbitration Act ("FAA") provides for the stay of "any suit or proceeding brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration...*upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement.*" 9 U.S.C. § 3 (2007). The Defendants seek this Court's determination that the current action is referable to arbitration. Normally, a court entertaining such a request would have to first address two issues: (i) whether the parties agreed to arbitrate, and, if so, (ii) whether the scope of the agreement encompasses plaintiffs' claims. *Rosen v. Mega Blocks, Inc., et al,* 2007 WL 1958968 at 4 (S.D.N.Y.) These initial steps have already been undertaken by the parties. The parties agreed in writing to litigate certain disputes

(those arising from Settlement), and arbitrate others. The Defendants, curiously, avoid any mention, let alone analysis, of the Settlement's jurisdiction clause. Instead, they focus all their efforts on arguing for the absolute breadth of an arbitration clause in an agreement that does not form the basis of Plaintiffs' claims. As already stated, the arbitration clause, no matter how broad, cannot divest the Settlement's jurisdiction clause of its authority and scope. A proper legal analysis, therefore, should focus on the Complaint's allegations and claims, and whether those allegations and claims arise from the Settlement. We believe they unequivocally do.

1. Plaintiffs' Claims and Allegations Arise From The Settlement In Accordance With This Court's Test In *Rosen*

This Court's decision in *Rosen v. Mega Bloks, Inc.*, is instructive for the instant case both on the facts and the law. *Rosen,* 2007 WL 1958968 In *Rosen*, the parties entered into a stock purchase agreement ("SPA") wherein the defendants ("Mega") acquired plaintiffs' ("Rosens") companies. The parties simultaneously entered into employment and non-compete agreements that were exhibited to the SPA. The SPA and the non-compete agreements contained a forum selection clause; the employment agreements contained identical arbitration clauses. This series of agreements were all "integral parts" of a "single transaction." The exhibited agreements, however, were not "incorporated" into the SPA. *Id* at 4.

The Rosens eventually sued Mega for breach of the SPA. Mega filed a motion to compel arbitration, alleging that the parties had agreed to "arbitrate all disputes." *Id* at 9. Mega argued that the each provision of the employment agreements were incorporated by reference into the SPA and, therefore, all disputes were subject to their arbitration clause. Mega also made use of the SPA's merger clause and the simultaneity of the execution of the agreements. *Id* at 4. The court rejected these arguments. "The mere fact that a document is an 'integral part' of a larger transaction does not mean that any provision contained in that document must be applied to all other documents that are

part of the same transaction." As for the merger clause, the court found it "simply irrelevant." *Id* at 5 ("the mere fact that a contract refers to another contract does not mean it has incorporated the other contract"). The court's real task, it said, was to determine "whether the Rosens' lawsuit seeking payment under the SPA implicates issues of construction of the employment agreements." *Id* at 6. The court found that, at least on its face, the Rosens' suit did not.

The court then proceeded to focus on the factual allegations in the complaint in addition to the legal causes of action asserted. The locus of the dispute was the SPA's section 2.6 that provided for graduated payments to the Rosens' based on their compliance with defined "commitments." *Id* at 8. The employment agreements required explicit compliance the SPA's section 2.6. Mega argued, therefore, that the Rosens would have to prove their compliance both SPA 2.6 and the their employment agreements in order to prevail. Mega further argued that its central defense was going to be the Rosens' failure to comply with the employment agreements. The court rejected this reasoning, finding that a resolution of the Rosens' dispute did not require the "construction" of the employment agreements. "Nor will it require the interpretation of the 'the parties' rights and obligations under' them," as the genesis of the case stemmed from section 2.6 of the SPA. *Rosen,* 2007 WL 1958968 at 9; *see also Collins & Aikman Prods. Co. v. Bldg. Sys., Inc.,* 58 F.3d 16, 23 (2d Cir.1995). The court denied Mega's motion to compel arbitration and allowed the litigation to proceed.

The current action is on all fours with *Rosen.* The parties entered into a series of agreements that compromised a single transaction. The primary agreement, the Settlement, is the instrument of the Defendants' fraud against the Plaintiffs. The Plaintiffs' action charges Defendants with breaching multiple duties owed Plaintiffs at the time of the Settlement. None of these duties, save one (fiduciary duty), derive from any of the shareholder agreements nor Plaintiffs capacity as

shareholders. The duties Defendants' owed Plaintiffs arose at the time of Settlement. If Plaintiffs had not been shareholders at the time of the Settlement the current action would stand.

In *Rosen*, the court was faced with an explicit agreement to arbitrate and a mere forum selection clause. The latter, the court said, "suggest[ed]" that the "parties assumed the claims arising under these agreements would be heard in a court, not as part of an arbitration." *Rosen,* , 2007 WL 1958968 at 4. *See also Rosenblum v. Travelbyus.com Ltd.,* 299 F.3d 657, 663 (7th Cir.2002). However, cognizant of the strong federal policy in favor of arbitration, the court acknowledged that "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is *the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability.*" (emphasis added). *Rosen,* , 2007 WL 1958968 at 4, citing *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.,* 460 U.S. 1, 24-25, 103 S.Ct. 927, 74 L.Ed.2d 765 (1983) No such problem exists in the instant case.

Plaintiffs have not argued that the Defendants waived their right to arbitrate nor have they challenged the breadth of the arbitration clause, save the Settlement's explicit limitation of its scope. The Plaintiffs' action, unlike in *Rosen*, is firmly grounded on an explicit grant of jurisdiction that has not and cannot be challenged by Defendants. The Plaintiffs' action charges Defendants with the breach of multiple duties owed Plaintiffs at the time of the Settlement. Like *Rosen*, the "parties' rights and obligations under the Settlement are not assisted by constructing the shareholder agreements. Should the Court need to construct the terms of the shareholder agreements in order to ascertain "the parties' rights and obligations," however, it is free to does without any affect on choice of forum. For unlike *Rosen*, the Settlement incorporates the terms of the shareholder agreements. The Plaintiffs' action is not a shareholder action for breach of the shareholder agreements or breach of its rights thereunder. The Complaint is firmly grounded in the Settlement

and the Defendants' action in making of the Settlement. Defendants' own demand for arbitration, while ostensibly based on the 2007 Agreements, seeks merely to confirm Plaintiffs' obligations and duties under the Settlement.

2. The Plaintiffs' Complaint, Including its Allegations, Causes of Action, and Remedies, Arises Out of the Settlement And Defendants' Actions in Relation Thereto

As this Court has noted a presumption of arbitration "does not alter the fact that the ultimate purpose of the Court's inquiry is to determine whether the parties intended that the particular claims at issue here be arbitrated." The "case law contemplates the examination of the arbitrability of each 'particular claim' separately." *Rosen,* 2007 WL 1958968 at 7. Whether a claim falls within the scope of the parties' arbitration agreement, is determined by an examination of the "factual allegations in the complaint rather than the legal causes of action asserted." *Rosen,* 2007 WL 1958968 at 7 citing *Smith/Enron Cogeneration Ltd. P'ship, Inc. v. Smith Cogeneration Int'l, Inc.,* 198 F.3d 88, 99 (2d Cir.1999) (quoting *Genesco, Inc. v. T. Kakiuchi & Co., Ltd.,* 815 F.2d 840, 846 (2d Cir.1987)), *cert. denied,* 531 U.S. 815 (2000). The Defendants' actions prior to the Settlement were so nefarious that they themselves have mistaken these facts, rather than their own actions in connection with the Settlement, as the basis of the Plaintiffs' Complaint. Had the Defendants undertaken an analysis of the original Complaint they would have concluded that its allegations, causes of action, and remedies are all arise from the Settlement.

The Plaintiffs' original Complaint asserts ten causes of action, nine are substantive and the tenth requests this Court to enjoin the Defendants from further action with an arbitration. Of the remaining nine allegations, six of the causes are, or can be, tied exclusively to the Defendants' actions in connection with the Settlement:

- For its second cause of action, recission common law fraud, the Complaint alleges that the Defendants' entered into a scheme to defraud Plaintiffs by misrepresentations and material

omissions regarding, *inter alia*, the value of Settlement. In reliance upon the fraudulent misrepresentations and omissions, Plaintiffs agreed to the Settlement.

- For its third cause of action, intentional misrepresentation, the Complaint alleges that the Defendants intentionally made misrepresentations to Plaintiffs that were false and material to Plaintiffs' acceptance of the Settlement. The misrepresentations were made with the intent to defraud Plaintiffs and induce them to accept a known loss through the Settlement.

- For its fourth cause of action, negligent misrepresentation, the Complaint alleges that the Defendants knew, or should have known, that the Settlement did not improve the financial condition of 13B and obligated Plaintiffs to a known loss through the Settlement.

- For its sixth cause of action, fraudulent inducement, the Complaint alleges that the Defendants entered into a scheme where by they fraudulently induced Plaintiffs, with cash and other promises, to accept a known loss through Settlement.

- For its seventh cause of action, breach of implied covenant of good faith and fair dealing, the Complaint alleges that the Defendants fraudulently induced the Plaintiffs to agree to the Settlement by their misrepresentations and material omissions regarding the value of the Settlement and the financial condition of 13B, thereby breaching the Settlement's implied covenant of good faith and fair dealing.

- For its eighth cause of action, civil conspiracy, the Complaint alleges that Defendants conspired at the time of the Settlement to misrepresent multiple facts and withhold other facts that were material to the Plaintiffs acceptance of the Settlement and its terms.

These allegations, however in-artfully pled they might be, are firmly grounded in the Defendants' actions that led to the Plaintiffs' acceptance of the Settlement. None of these causes of action depends upon the duties or the obligations that may have existed between the parties *per* the original Shareholder Agreements, the Amendments, or the 2007 Agreements.

The Plaintiffs' ninth cause of action for breach of fiduciary duty, as pled in the original Complaint, is arguably arbitral. The fiduciary duty Defendant ARH owes Plaintiffs arose from the original Shareholder Agreements. That fiduciary duty was breached on December 30, 2005 when ARH misrepresented the value of the Settlement and withheld other material information that was relevant to the Plaintiffs' acceptance of the Settlement and its terms. Plaintiffs have sharpened this cause of action, and the allegations that underlie it, in the Amended Complaint. The two remaining

two causes of action, the securities violation under 10(b)5 and the breach of contract have been removed in the Amended Complaint.

B. Should The Court Look Favorably On Defendants' Motion To Compel Arbitration And Stay Litigation, Plaintiffs Request Additional Discovery In Order To Oppose The Motion To Stay

Plaintiffs' counsel have submitted an affidavit in support of additional discovery should the Court look favorably on Defendants' Motion to Stay. Where a motion is brought to compel arbitration, the court must apply a standard similar to that applicable for a "motion for summary judgment in that it must determine whether there is 'an issue of fact as to the making of the agreement for arbitration.'" *Rosen,* 2007 WL 1958968 at 3. *See also Bensadoun v. Jobe-Riat*, 316 F.3d 171, 175 (2d Cir. 2003) "[t]he summary judgment standard is appropriate in cases where the District Court is required to determine arbitrability.").

The party resisting summary judgment based on a need for additional discovery must submit an affidavit describing: (1) what facts are sought to resist the motion and how they are to be obtained, (2) how those facts are reasonably expected to create a genuine issue of material fact, (3) what effort the affiant has made to obtain them, and (4) why the affiant was unsuccessful in those efforts. *Meloff v. New York Life Ins. Co.,* 51 F.3d 372, 375 (2d Cir. 1995). The denial of access to relevant information weighs in favor of the party opposing a motion for summary judgment because the nonmoving party must be given an "opportunity to discover information that is essential to his opposition of the motion." *Burlington Coat Factory Warehouse Corp. v. Espirit De. Corp*, 769 F.2d 919, 925 (2d Cir. 1985); *Trebor Sportswear Co. Inc. v. The Limited Stores, Inc.*, 865 F.2d 506, 511 (2d Cir. 1989).

Plaintiffs and their counsel have submitted affidavits that detail their unsuccessful efforts to obtain even routine corporate and financial information from the entities in whom the Plaintiffs allegedly hold shares. Moreover, Defendants have made clear to this Court their intention to limit

that discovery. In order to properly resist Defendants Arch's and ARH/Alt Re's Motion to Stay, Plaintiffs would need document and deposition discovery on several topics, including: (i) Arch's disputes with NBG; (ii) ARH/Alt Re's disputes with NBG; (iii) financial records for the Program from 2001 through 2008, including any filings with the Bermuda Monetary Authority; (iv) ARH's relationship to Alt Re with respect to investors in 13B; (v) Arch's participation as a 13B shareholder; and (vi) the creation and execution of the 2007 Agreements that are the basis of Defendants' current motions.

IV. CONCLUSION

Based on the foregoing, Plaintiffs respectfully requests a hearing on the pending motion or that this Court enter an order enjoining the Defendants from any further instigation of an arbitration and forthwith set a schedule for discovery.

THORP REED & ARMSTRONG LLP

s/s silver86
Ira B. Silverstein, No. 17658
2005 Market Street, Suite 1910
Philadelphia, PA 19103
Tel: 215-640-8500
Fax: (215) 640-8501
isilverstein@thorpreed.com
Attorneys for Plaintiffs

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

TPG GROUP, WILLIAM HUTCHISON	:	No. 08 Civ. 11244 (SHS)
Plaintiffs,	:	
-against-	:	
ALTERNATIVE RE HOLDINGS LIMITED, ALTERNATIVE RE LIMITED, ARCH INSURANCE COMPANY	:	
Defendants.	:	

CERTIFICATE OF SERVICE

I, Carol Lydon, certify that on this 16th day of March, 2009, I served the attached document electronically via the Court's ECF System on:

Robert E. Wilder, Esqurie
Mound Cotton Wollan & Greengrass
One Battery Park Plaza
24 Whitehall Street
New York, NY 10004

Lawrence W. Pollack, Esquire
Dewey & Leboeuf, LLP
1301 Avenue of the Americas
New York, NY 10019

Carol D Lydon
CAROL LYDON