IN THE CHANCERY COURT FOR THE STATE OF TENNESSEE
TWENTIETH JUDICIAL DISTRICT, DAVIDSON COUNTY

STATE OF TENNESSEE, ex rel., LESLIE A. NEWMAN, Commissioner for Commerce and Insurance for the State of Tennessee,

v.

DOCTORS INSURANCE RECIPROCAL (Risk Retention Group), a Tennessee domiciled insurance company.

No. 03-294-IV

LESLIE A. NEWMAN, Commissioner of Commerce and Insurance for the State of Tennessee, as Liquidator for Doctors Insurance Reciprocal, Risk Retention Group;

Plaintiff,

v.

GENERAL REINSURANCE CORPORATION, a Delaware corporation; JOHN WILLIAM "BILL" CREWS; MILLIMAN USA, INC., a Washington corporation; PRICE WATERHOUSECOOPERS LLP, domiciled in Tennessee; CREWS & HANCOCK, P.L.C., a Virginia limited liability company; KENNETH R. PATTERSON; WACHOVIA BANK, NATIONAL ASSOCIATION (f/k/a FIRST UNION NATIONAL BANK), a Virginia corporation; CAROLYN B. HUDGINS; JUDITH A. KELLEY; THOMAS M. REINDEL; VICTORIA J. SEEGER; CHRISTOPHER MIGEL; THOMAS N. KELLOGG; ROBERT L. SANDERS; GARY STEPHANI; RICHARD W. E. "DICKY" BLAND; GORDON D. MCLEAN;

Defendants.

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PETITION TO RECOVER DAMAGES

JURISDICTION

1. This court has original jurisdiction based upon the domiciles of the RRGs and the Tennessee Insurers Rehabilitation and Liquidation Act, Tenn. Code Ann. § 56-9-101, *et. seq*.

a. The RRG, on whose behalf Commissioner Newman brings claims against the Defendants, is domiciled within Tennessee and did business within the State of Tennessee by providing coverage for Tennessee policyholders.

b. Furthermore, under Tennessee's insurance statutory scheme all matters pertaining to delinquency proceedings rest solely within the subject matter jurisdiction of the Chancery Court of Davidson County, Tennessee. Tenn. Code Ann. § 56-9-104(e). The Plaintiff estates in this proceeding are currently in liquidation as ordered by this Court on June 3, 2003. The Liquidation Orders issued by the Tennessee Chancery Court on June 3, 2003, fall clearly within the purview of delinquency proceedings as they established receiverships for the explicit purpose of liquidating the RRGs. (Exhibits A, B, C). Accordingly, the governance of delinquency proceedings under the Tennessee Insurance Code applies to the case at hand and dictates the jurisdiction of this Court in hearing such matters.

c. An MDL proceeding was filed in the United States District Court for the Western District of Tennessee, however, that court dismissed the Plaintiffs' federal RICO claim with prejudice and declined to exercise supplemental jurisdiction of the state law claims. Accordingly, the Sixth Circuit judge dismissed the state law claims without prejudice and ordered that those claims be filed within thirty days of the dismissal to preserve the statute tolled in the MDL. This filing falls within the mandated thirty day period and constitutes the Plaintiff's filing of its state law claims.

d Doing Business In Tennessee: Plaintiff avers that the following Defendants and co-conspirators during the relevant time period were doing business on a regular and systematic basis, in Tennessee or with entities situated in Tennessee: Gen Re; PwC; Crews & Hancock; Bland; Crews; Milliman; Sanders; various of the Management Defendants including without limitation Kelley, Hudgins, Patterson and McLean. In addition, Plaintiff alleges that various Defendants (including Gen Re and PwC) have been doing business in Tennessee by reason of their own respective modes of conduct and brand name advertising, as well as by reason of their controlled subsidiaries and affiliates.

e. Commission of Tort in Tennessee: Jurisdiction exists under Tennessee's Long Arm Statutes, T.C.A. §§ 20-2-201 and 20-2-223. Each Defendant caused tortious damage by act or omission in this state under the Long Arm Statute tests set forth further below. The allegations of the Fact Section of this Complaint are incorporated by reference under the Long Arm Statutes grounds. Without limiting the generality of the foregoing, and as shown by the paragraphs of this Complaint that are cited and incorporated in this jurisdiction section, each Defendant either directly or through agents, who were at the time acting with actual and/or apparent authority and within the scope of such authority, separately but also acting in concert or conspiracy and materially aiding each other in respects set forth herein, has, within the meaning of the Tennessee Long Arm Statutes:

- transacted business in this state;
- contracted to supply services or things in this state;
- caused tortious damage by act or omission in this state;
- caused tortious damage by act or omission in and outside this state, while such defendant regularly does or solicits business in and from this state or engages in other persistent course of conduct or

derives substantial revenue from goods used or consumed or services rendered or capital raised in and from this state;

- contracting to insure any person, property, or risk located within this state at the time of contracting; or
- conduct as a director or officer of a domestic corporation or the conduct of a domestic corporation while the person held office as a director or officer.

f. Non-Applicability of Federal Legislation and Non-Removability of this Action From State Court. Every form and amount of relief which the Plaintiff needs or seeks is afforded to the Plaintiff by the expressly-pleaded state law causes of action set forth in this Complaint; and Plaintiff does not plead, and disclaims, any claim under any federal statute. This case does not directly or indirectly assert any claims federal statute, and instead this Complaint only pleads valid and meritorious claims under the Tennessee law meritorious common law fraud and other state law causes of action. Nor is this a case which arises in, or is related to, any bankruptcy case: no bankrupt is or ever has been a party hereto; no relief is sought herein directly or indirectly against any bankrupt or bankruptcy estate.

g. Further, there is neither diversity of citizenship nor any federal question jurisdiction. Without limiting the preceding sentence, the Plaintiff is a citizen of Tennessee and the partnership defendant PwC has partners resident in Tennessee, which under applicable law is sufficient to constitute them as a Tennessee citizen for purposes of the federal diversity jurisdiction statute. Each such accounting firm's citizenship for purposes of 28 U.S.C. § 1332 is determined by the residence of its partners, *Carden v. Arkoma Assoc.*, 494 U.S. 185, 110 S.Ct. 1015 (1990), and such firm must be deemed to be a citizen of any state in which a partner resides, including Tennessee. No federal statutory or constitutional claim is asserted herein, and the plaintiff disclaims any assertion of a federal subject matter claim.

h. Each of the defendants herein conspired to defraud the plaintiff. Their agreements to do so may be formal and/or informal. Each defendants conspirator committed overt acts subjecting each other to jurisdiction in Tennessee and the acts of each conspirator are attributable to each other co-conspirator. The co-conspirators directed their overt acts toward entities in Tennessee (namely the plaintiff) resulting in injuries to the plaintiff arising out of the conspiracy activities.

PARTIES

2. This action is brought by the Plaintiff, Leslie A. Newman, Commissioner of Commerce and Insurance for the State of Tennessee, as Liquidator for Doctors Insurance Reciprocal, Risk Retention Group ("DIR"), a company in liquidation pursuant to Tennessee Code Annotated §§ 56-9-307, *et. seq*. DIR is duly licensed and domiciled under the laws of the State of Tennessee. Leslie A. Newman, as Commissioner of Commerce and Insurance for the State of Tennessee, brings this action in her capacity as Liquidator for DIR and on behalf of each creditor, policyholder and subscriber of DIR. (Over 10,000 policyholders).

3. Defendant General Reinsurance Corporation , also d/b/a "General Re," "GeneralCologne Reinsurance," and "GeneralCologne Re" (hereinafter "Gen Re"), is a corporation organized and existing under the laws of the state of Delaware and doing business in the State of Tennessee. Gen Re is liable for the actions of its executives, officers, directors, employees and agents under the doctrines of agency, respondeat superior and/or other doctrines.

4. Defendant Thomas M. Reindel was at all times relevant a Vice President of Gen Re.

5. Defendant Tom N. Kellogg was at all times relevant a Vice President of Gen Re.

6. Defendant Victoria J. Seeger (f/k/a Victoria J. Wixtead) was at all times relevant a Vice President of Gen Re.

7. Defendant Christopher J. Migel was at all times relevant an Executive Vice President of Gen Re.

8. Defendant Milliman USA, Inc. ("Milliman") (f/k/a Milliman & Robinson) is a corporation organized and existing under the laws of the State of Washington and doing business in Tennessee. Milliman is liable for the actions and omissions of Robert L. Sanders ("Sanders") and its other employees and agents under the doctrines of agency, respondeat superior and/or other doctrines.

9. Defendant Sanders was at all times relevant a principal of Milliman.

10. Defendant PricewaterhouseCoopers LLP ("PwC") is a limited liability partnership organized and existing under the laws of the State of Delaware and doing business in Tennessee by way of partners of said LLP domiciled in Tennessee. PwC is a citizen of the state of Tennessee. PwC is liable for the actions and omissions of Defendant Gary Stephani and its other employees and agents under the doctrines of agency, respondeat superior and/or other doctrines.

11. Defendant Gary Stephani ("Stephani") was at all times relevant a partner with PwC and was responsible for audits of Reciprocal of American and the RRGs.

12. Defendant Crews & Hancock, P.L.C. ("Crews & Hancock") was at all times relevant a limited liability company organized and existing under the laws of the Commonwealth of Virginia, with its principal place of business in Richmond, Virginia. At all relevant times, Crews & Hancock served as general counsel to Reciprocal of American ("ROA"), The Reciprocal Group ("TRG"), DIR, ANLIR, TRA, and First Virginia Re ("FVR"). Crews &

Hancock is liable for the actions and omissions of its members, employees, and agents under the doctrines of agency, respondeat superior and/or other doctrines.

13. Defendant John William "Bill" Crews ("Crews") was at all times relevant an officer and/or director of ROA, TRG, and FVR. He was Executive Vice President for ANLIR's attorney-in-fact.[1] He was Executive President of DIR's attorney-in-fact. He was Executive Vice President of TRA's attorney-in-fact. He also served as General Counsel to all of these entities. He was a member of Defendant Crews & Hancock. He was Executive Vice President of Tennessee domiciled DIR and availed and subjected himself to Tennessee laws, Tennessee insurance regulations and authority. Due to his positions and control over DIR, he maintained consistent contact with Tennessee.

14. Defendant Richard W. E. "Dicky" Bland ("Bland") was at all times relevant a Member with Crews & Hancock. At certain relevant times, Bland was also an officer of ROA and of the attorney-in-fact for DIR in Tennessee. He was Assistant Secretary of the attorney-in-fact of DIR in Tennessee. Due to these positions, he availed and subjected himself to Tennessee laws, insurance regulations and authority. Due to these positions he maintained consistent contact with Tennessee.

15. Defendant Gordon D. McLean ("McLean") was a member of the Boards of Directors of both TRG and ROA from 1990 to 1994. McLean was President of ROA from 1991 to 1994 and President of TRG from 1990 to 1995. On information and belief, at all times relevant after 1995, McLean was "President Emeritus" of ROA and participated actively in the management of the Companies, regardless of whether he had a formal title or position.

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[1] As set forth below, reciprocals are required by law to have an attorney-in-fact. Accordingly there also existed three corporations each holding a general power of attorney from one of the RRGs. All of the officers of the attorneys-in-fact were from either the "Management Defendants" or the "Officer and Director Defendants," as hereinafter defined.

16. Defendant Kenneth R. Patterson ("Patterson") was at all times relevant an officer of ROA, TRG, FVR, DIR, ANLIR, and TRA. Patterson was President and Chief Executive Officer of ROA, President and Chief Executive Officer of TRG, President and Chief Executive Officer of FVR, Chief Executive Officer and Executive Vice Chairman of DIR, Senior Vice President and Chief Financial Officer of ANLIR, President and Chief Executive Officer of TRA, Senior Executive Vice President and CFO of the attorneys-in-fact for DIR and ANLIR, and Executive Vice Chairman of the attorney-in-fact for TRA. Patterson was also a Certified Public Accountant. Due to these positions, he availed and subjected himself to Tennessee laws, insurance regulations and authority. Due to these positions he maintained consistent contact with Tennessee.

17. Defendant Carolyn B. Hudgins ("Hudgins") was at all times relevant an officer of ROA, and TRG. She was Vice President for Financial Services of ANLIR, Executive Vice President for ANLIR's attorney-in-fact, Executive Vice President for DIR's attorney-in-fact, Senior Vice President of TRA, and Executive Vice President of TRA's attorney-in-fact. On information and belief, at certain relevant times Hudgins was also an officer of FVR. Hudgins was also a Certified Public Accountant. Due to these positions, she availed and subjected herself to Tennessee laws, insurance regulations and authority. Due to these positions she maintained consistent contact with Tennessee.

18. Defendant Judith A. Kelley ("Kelley") was at all times relevant an officer of ROA, TRG, and FVR. She was Senior Vice President and Chief Operating Officer of ANLIR, President and Chief Executive Officer of ANLIR's attorney-in-fact, President and Chief Executive Officer of DIR, President and CEO of DIR's attorney-in-fact, Executive Vice President of TRA, and Executive Vice President of TRA's attorney-in-fact. Defendant Kelley

was also a Chartered Property & Casualty Underwriter, Society of Chartered Property & Casualty Underwriter. Due to these positions, she availed and subjected herself to Tennessee laws, insurance regulations and authority. Due to these positions she maintained consistent contact with Tennessee.

19. Defendant Wachovia Bank, National Association ("Wachovia") (f/k/a First Union National Bank) is a corporation organized and existing under the laws of the Commonwealth of Virginia and doing business in Tennessee. Wachovia is liable for the actions and omissions of its employees and agents under the doctrines of agency, respondeat superior and/or other doctrines.

20. Collectively, Defendants Patterson, Crews, Hudgins, McLean, and Kelley may be referred to herein as the "Management Defendants."

21. Collectively, Defendants Patterson, Crews, Hudgins, Kelley, and Bland may be referred to herein as the "Director and Officer Defendants."

22. Collectively, Defendants Patterson, Crews, Hudgins, Kelley, Bland, Kellogg, Seeger, Migel, Reindel, McLean, Gen Re, and Crews & Hancock, Milliman, Sanders, PwC, Stephani and Wachovia may be referred to herein as the "Conspiracy Defendants."

23. Collectively, Defendants Milliman and Sanders may be referred to herein as the "Milliman Defendants."

FACTS

I. THE HISTORY OF THE ENTITIES AND THEIR RELATIONSHIP

24. Reciprocal of America ("ROA") is a Virginia unincorporated association and reciprocal insurer. The Reciprocal Group ("TRG") is a Virginia non-stock corporation. TRG ostensibly served as the management company and attorney-in-fact for ROA. Under

Virginia law, reciprocal insurance organizations must operate through a designated attorney-in-fact. On January 29, 2003, the Circuit Court of the City of Richmond, Virginia, found that "ROA and TRG, as attorney-in-fact for ROA, operate as, and comprise, a single insurance business enterprise." As used in this Complaint "ROA/TRG" refers to the combined single insurance business enterprise.

25. ROA was formed in 1977 as Virginia Hospital Insurance Reciprocal. Over the years, ROA underwent two name changes, becoming known as Reciprocal of America in 2001. ROA initially provided insurance only to hospitals. Later, ROA also began to insure physicians and lawyers and provide reinsurance coverage to DIR, ANLIR, and TRA. Defendant Crews was instrumental in the creation and management of ROA from inception.

26. First Virginia Reinsurance ("FVR") was incorporated in Bermuda in 1984. FVR was initially capitalized by issuing stock to approximately 32 Virginia acute care hospitals. On information and belief, Crews was instrumental in the creation of FVR, which was to serve as a reinsurer of all of ROA's retained share of risk on the physician and lawyer malpractice insurance business. From the inception of FVR until about 1990, ROA ceded premiums directly to FVR. ROA was secured by a trust fund and this was necessary because FVR was an unauthorized reinsurer. This trust fund was established with Wachovia Bank between FVR and ROA. Around 1990, however, Gen Re offered to be the middle entity whereby ROA would cede the physician and lawyer business to Gen Re and then Gen Re would (retro)cede to FVR. This was done to accommodate ROA because the credit risk of FVR was passed to Gen Re and this arrangement also had the benefit of limiting regulatory oversight. This arrangement existed until late December 2001 when Gen Re became concerned with the volume of business passing through it compounded with the growing diminution in FVR's surplus. FVR's surplus was

substantially diminished as a result, in part, of significant underwriting losses experienced by DIR during 2001. Gen Re proposed to execute a loss portfolio transfer ("LPT") which will be discussed herein. Upon information and belief, the initial purpose of FVR, however, was to allow ROA's lawyer and physician insureds to defer the payment of federal income taxes. Upon information and belief, FVR was considered a non-controlled foreign corporation, i.e., not a U.S. tax payor. This had the further effect of limiting regulatory oversight of the various transactions entered into by the Defendants.

27. FVR was referred to by certain of the Defendants by the code name "Gen Re II" or "GR2."

28. On information and belief, FVR was originally owned 25% by ROA and 75% by certain Virginia hospitals and health care systems who were direct subscriber/insureds of ROA through the stock issuance discussed above. In early 1989, the 75% owners of FVR purchased ROA's 25% minority interest. On information and belief, this transfer was engineered by Patterson, Crews, Hudgins, Kelley, Bland, and Crews & Hancock, who feared that Virginia insurance regulators might determine that ROA and FVR constituted an insurance holding company system, which would require adherence to additional rigorous regulations and subject the companies to additional regulatory scrutiny.

29. On information and belief, Patterson, Crews, Hudgins, Kelley, Bland, McLean, and Crews & Hancock devised a plan further to remove FVR from potential regulatory scrutiny. Pursuant to this plan, ROA's FVR-reinsured risk would be reinsured first by Gen Re and then be retroceded to FVR. ROA would then report, and would claim a reinsurance credit for, the reinsurance with Gen Re, and thereby be relieved of the requirement to report the reinsurance with FVR, thus distancing it from the scrutiny of the regulators of ROA. This plan

had the further effect of passing FVR's credit risk from ROA to Gen Re. On information and belief, this plan was implemented beginning in 1989, when Gen Re began to pass ROA risk, both direct and reinsurance, through to FVR pursuant to retrocession agreements between Gen Re and FVR (the "Gen Re-FVR Retrocession Agreements").

30. FVR and Gen Re were also parties to certain trust agreements for the purpose of holding assets in Bermuda financial institutions as security for the performance of FVR's obligations under the Gen Re-FVR Retrocession Agreements (the "FVR Bermuda Trusts").

31. On information and belief, the Management Defendants asked Gen Re to act as an intermediary between ROA and FVR. This was a condition to Gen Re's continuing to participate in the very profitable supposed reinsurance of ROA's business.

32. In 1989 or 1990, the board of Directors of ROA authorized the management of TRG to form Doctors Insurance Reciprocal, Risk Retention Group. DIR was to insure ROA's physician line of insurance business. Under the legal direction of Crews & Hancock, and under the control of Crews and Patterson, DIR was formed in 1990 and domiciled and licensed in Tennessee on January 30, 1990. In January of 1990 Physicians Management Corporation ("PMC"), attorney-in-fact for DIR, advanced $3,400,000.00 to DIR as surplus advances under terms of a loan agreement and promissory notes. After a period of transition, DIR began directly writing the insurance for the physician line of insurance business previously insured by ROA.

33. In 1992, the Board of Directors of TRG authorized the management of TRG to form American National Lawyers Insurance Reciprocal, Risk Retention Group. ANLIR was to insure ROA's lawyer line of insurance business. Under the legal direction of Crews &

Hancock, and under the control of Crews and Patterson, ANLIR was formed in 1992 and was domiciled and licensed in Tennessee in 1993. After a period of transition, ANLIR began directly writing the insurance for the lawyer line of insurance business previously insured by ROA.

34. In 1995, the Board of Directors of TRG authorized the management of TRG to form The Reciprocal Alliance, Risk Retention Group. TRA was to insure health care providers in markets that ROA was unable to reach due to regulatory restrictions. Under the legal direction of Crews & Hancock, and under the control of Crews and Patterson, TRA was formed in 1995 and was domiciled and licensed in Tennessee.

35. By law, each of DIR, ANLIR, and TRA was required to have an attorney-in-fact to take all actions on behalf of its principal. Coincident with the formation of each RRG, and at the suggestion of Crews and Patterson, ROA's Board of Directors authorized the management of TRG to take the necessary steps to form a corporate attorney-in-fact for each RRG.

36. The attorneys-in-fact were formed by the management of TRG, with legal assistance from Crews & Hancock. DIR's attorney-in-fact was PMC, a Tennessee non-profit corporation. ANLIR's attorney-in-fact was Lawyers Management Corporation ("LMC"), a Virginia non-stock corporation. TRA's attorney-in-fact was The Reciprocal Alliance Services Corporation ("TRASCO"), a Virginia non-stock corporation.

37. The structure of a reciprocal insurance company is that the attorney-in-fact acts on behalf of the reciprocal to perform the duties of management under the direction of the board of directors of the reciprocal company. In contrast, by the terms of the RRG governing instruments, which were prepared by Crews & Hancock, each of the RRGs was controlled by, rather than managed by, its attorney-in-fact. In addition, by the terms of their governing

instruments, which not coincidentally were prepared by Crews & Hancock, each of PMC, LMC, and TRASCO was controlled by TRG.

38. On or about January 26, 1990, DIR, PMC, and TRG executed a management and insurance services agreement pursuant to which TRG would serve as their exclusive management and insurance services company, and would provide the management and technical insurance and administrative services necessary for the operations of DIR and PMC.

39. On or about November 5, 1992, ANLIR, LMC, and TRG executed a management and insurance services agreement, effective upon the subsequent date when ANLIR was issued a license by the Tennessee Department of Commerce and Insurance (the "TDCI"). Pursuant to this agreement, TRG served as ANLIR's exclusive management and insurance services company, and would provide the management and technical insurance and administrative services necessary for the operations of ANLIR and LMC.

40. On or about September 8, 1995, TRA, TRASCO, and TRG executed a management and insurance services agreement, effective upon the subsequent date when TRA was issued a license by the TDCI. Pursuant to this agreement, TRG served as TRA's exclusive management and insurance services company and would provide the management and technical insurance and administrative services necessary for the operations of TRA and TRASCO.

41. TRG served as the management company for all of the RRGs and for ROA, performing all the duties and functions normally associated with the business of insurance for each of the three Reciprocals, including claims administration. TRG management operated ROA and the RRGs as a totally integrated enterprise. The attorneys-in-fact for the RRGs were mere shells, without offices, employees, or assets, and their functions were wholly delegated to, and controlled by, TRG.

42. TRG's control of the RRGs was further enabled by the structure of the RRGs, each of which was organized with two classes of directors, one class of which consisted of well-known professionals whose images enhanced the likelihood that others would purchase insurance, but who were deprived of the ability to properly direct the RRGs as a direct and proximate result of the fraud, deceit and suppression practiced upon them by the Defendants.

43. TRG management controlled ROA and the RRGs through an interlocking network of common officers and directors. Despite their independent fiduciary duties to the RRGs and the inherent conflicts of interest presented, TRG management executed agreements between and among ROA and the RRGs without commercially reasonable terms and arms-length negotiation. Defendant Kelly was Executive Vice President of ROA, President and CEO of DIR, President and CEO of ANLIR and Executive Vice President and Board Member of TRA at the same time. Defendant Crews was for many years a senior officer and general counsel for TRG. He was also a founder and senior partner of Crews & Hancock, LLP, a firm which provided very substantial, if not virtually exclusive, corporate, employment, regulatory, claims and other legal services to each of ROA, DIR, ANLIR and TRA through TRG and to TRG directly. Defendant Crews engaged in these conflicting roles notwithstanding the different and conflicting interests that each of those entities had vis-à-vis the other. Defendant Patterson and other Management Defendants signed reinsurance and other agreements on behalf of both the RRGs and ROA, their supposed reinsurer.

44. Through surplus "loans" and written agreements, ROA/TRG and their affiliates provided the RRGs with the capital they needed to do business. The following advances or "loans" were made to ANLIR: (a) $3,700,000.00 from TRG on December 30, 1992; (b) $1,250,000.00 from TRG on December 30, 1997; and (c) $1,500,000.00 from LMC on

March 1, 2000. The following advances or "loans" were made to DIR: (a) $3,400,000.00 from PMC in January 1990; (b) $1,750,000.00 in May 1993; and (c) $5,000,000.00 from PMC in December 1998. PMC funded the advances or "loans" from amounts borrowed under a "Loan Agreement" with FVR who had numerous directors and officers in common with PMC and DIR. TRA received a total of $27,000,000.00 in advances or "loans" from six different lenders. Under the terms of the management agreements, as long as these "loans" were outstanding, TRG could not be removed as the RRGs' management company, and TRG-approved directors could not be removed from the RRGs' Boards of Directors. TRG management admitted and argued to regulators that these surplus loans should be treated as capital investments in the RRGs, more like equity than debt. The so-called "loans" were unsecured, no payments were anticipated, and due dates were routinely continued for no consideration.

45. Between ninety and one hundred percent of the RRGs' insurance risks was transferred to ROA, effectively preventing the RRGs from ever operating independently or retaining sufficient premium dollars to pay off such surplus "loans" and remove TRG as their management company. Defendant Crews has admitted that the RRGs were not structured as freestanding independent reciprocals. In a June 4, 2002 letter from Crews to Gerald D. Wages, Chairman of the Board of ROA, Crews stated "when we drafted the structural and organizational documents for Doctors Insurance Reciprocal we created and included certain control features for the benefit of ROA/TRG which would not be found in an independent free standing reciprocal." Crews added the following in his June 4, 2002 letter to Mr. Wages:

> The unique structure [between ROA, DIR, and TRG] provides for control by TRG without having the disadvantage of having to register under the Virginia Insurance Holding Companies Act, which requires numerous and continuous regulatory approvals with respect to transactions between DIR and ROA. They would include everything from reinsurance transactions, management transactions, and numerous other transactions between ROA, DIR, and TRG. The

net effect of the structure provides for the 'benefits' of a holding company without having the burdensome regulatory obligations associated with an insurance holding company. Thus, to describe DIR as an independent, stand alone autonomous and independent entity would be a complete misnomer. In reality, the final decisions by DIR governance are subject to the approval or disapproval of TRG senior officers. NOTE: TRG senior officers are also ROA senior officers. The TRG control features in the DIR structure do exist and have been in existence since DIR's inception in 1990.

This structure was the same for all of the RRGs. At a November 22, 2002 ANLIR Board of Directors Meeting, Crews stated that "ANLIR's first obligation is to make sure that ROA remains a viable entity to protect the interests of the current insured's." In other words, ANLIR and the other RRGs were structured in a manner that they could not survive without ROA.

46. When convenient, TRG management ignored the corporate form and separateness of ROA and the RRGs, and disregarded trust agreements designed to protect the RRGs and their insureds, by shifting funds between and among the various entities and their trust accounts.

47. The Management Defendants used the RRGs as mere tools to secure monetary benefits for ROA and for themselves individually, in the form of executive salaries and other benefits.

48. The Management Defendants knew that the basic survival of the RRGs depended on the continued survival of ROA. Indeed, the Management Defendants and Crews & Hancock created and fostered this dependence. Moreover, A.M. Best rated the RRGs on the financial condition and operating performance of ROA due to the common management between the entities.

49. The actions and/or omissions alleged against the Defendants caused the insolvencies of each RRG and caused damages to each RRG equal to that portion of the RRGs' pre-January 1, 2002, liabilities ceded to ROA, as well as a diminution of the ability of each RRG

to provide assets to properly fund the liabilities retained by each RRG. These combined amounts are hundreds of millions of dollars.

50. Moreover, the fraud, conspiracy, deceit, misrepresentations, and/or negligence committed by the Defendants, including but not limited to failures, whether intentional or negligent, to disclose material facts to the TDCI, caused the RRGs to continue in existence and to spiral deeper into insolvency. Each RRG, therefore, has been independently and separately damaged in the amount by which its insolvency deepened due to the culpable acts of the Defendants.

II. THE RECEIVERSHIPS

51. On or about January 29, 2003, the Circuit Court of Richmond County, Virginia, found that "ROA and TRG, as Attorney-in-Fact for ROA, operate as, and comprise, a single insurance business enterprise," and placed the combined entity ROA/TRG into receivership under the control and direction of the Commonwealth of Virginia State Corporation Commission ("SCC").

52. On June 20, 2003, the SCC found that ROA/TRG was insolvent under Virginia law, and ordered that ROA/TRG be liquidated.

53. On or about January 31, 2003, in the Chancery Court of the State of Tennessee, Twentieth Judicial Circuit, Davidson County, three consent orders were entered appointing Paula A. Flowers, Commissioner of Commerce and Insurance for the State of Tennessee, as the Receiver for DIR, ANLIR, and TRA[2].

54. On June 3, 2003 the Chancery Court for Davidson County, Tennessee entered a Final Order of Liquidation; Final Order of Insolvency; and Permanent Injunction (the "Liquidation Orders") for each of the three Tennessee domiciled RRGs, DIR, ANLIR and TRA.

[2] Leslie A. Newman has now been appointed as the Commissioner of Commerce and Insurance for Tennessee.

These Liquidation Orders declared each of the RRGs to be insolvent, appointed the Commissioner as Liquidator of each RRG and directed the liquidation of each RRG pursuant to the Tennessee Insurance Receivership statute.

55. In addition to all others rights and powers enumerated in the Tennessee receivership statute, the Liquidation Orders specifically empowered the Commissioner as follows:

> C. Pursuant to Tenn. Code Ann. ' 56-9-307, the Commissioner, as liquidator, is authorized and directed (1) to take and continue in possession of all accounts, assets, monies, and property (both tangible and intangible) belonging to, held by and/or in the name of [RRG] both within and without the State of Tennessee, (2) to continue to be vested by operation of law with the title to all of the property, contracts and rights of action, and all of the accounts, assets, monies, books and records of the insurer, wherever located, as of the date of entry of the rehabilitation order, and any further title or rights in property gained by the Commissioner by virtue of such receivership, and (3) to continue to have the right to recover the same and reduce the same to possession and to administer then under the general supervision of the Court.
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> N. The liquidator *shall have the power* to continue to prosecute and to institute in the name of the insurer or in the liquidator's own name *any and all suits and other legal proceedings*, in this state or elsewhere, and to abandon the prosecution of claims the liquidator deems unprofitable to pursue further.
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> O. The liquidator *shall have the power to prosecute any action at law* or in equity which may exist on the liquidator's behalf, *and/or on behalf of the creditors, members, policyholders or shareholders of the insurer* against any person or entity . . .

(emphasis added).

56. The Liquidation Orders are final orders, entitled to full faith and credit in the state and federal courts of each of the United States pursuant to Article IV, ' 1 of the United States Constitution and 28 U.S.C. §1738.

57. Pursuant to the Liquidation Orders, the Commissioner has the exclusive right *and obligation* to obtain and recover all assets of the companies for the benefit of policyholder, claimants, subscribers, and creditors. Additionally, the Liquidation Orders mandate that the Commissioner *shall have the power* to prosecute any actions at law for the benefit of the RRGs. Thus, the Commissioner enjoys the exclusive right and burden of pursuing the claims made the basis of her suit for the benefit of the RRGs. The Commissioner may and must pursue all claims common to the policyholders, shareholders and creditors of the RRGs. These claims are assets of the RRGs receivership estate and the Commissioner has the exclusive right and obligation to pursue such claims. All such claims are asserted herein by the Commissioner in her capacity as Liquidator and on behalf of all policyholders, shareholders, creditors and claimants of the RRGs.

III. THE ROLE OF OUTSIDE AUDITORS, OUTSIDE ACTUARIES AND GENERAL COUNSEL

58. Insurance regulators, including the Tennessee Department of Commerce and Insurance ("TDCI") and the Virginia SCC (including the Virginia Bureau of Insurance, a division of the SCC), rely on insurers and their internal and/or outside professionals to certify the fairness and accuracy of the financial statements filed by all insurers authorized to conduct insurance business in their states.

59. As required by law, insurers rely on authorized management to prepare their required financial statements in conformity with statutory accounting practices ("SAP"). SAP differs from Generally Accepted Accounting Practices ("GAAP") in that SAP generally requires a more conservative accounting treatment for insurance companies than would be permitted for other types of business enterprises. Insurers rely on their certified public

accountants to certify that financial statements represent the company's financial condition fairly and free from material misstatement and in conformity with SAP.

60. As required by law, insurers rely on their independent certified public accountants to file an audited financial report as a supplement to the annual statement. This report must include a reconciliation of differences, if any, between the audited statutory financial statements, and the annual statement filed with the domiciliary insurance Commissioner, along with a written description of the nature of these differences.

61. An insurer's independent certified public accountants are required to conduct audits of the insurer's financial statements in accordance with generally accepted auditing standards ("GAAS"), governing *inter alia*, the auditor's qualifications, independence and professionalism, the planning and performance of the audit, and the resulting reports.

62. As further required by law, the independent certified public accountant must also give consideration to such other procedures described in the Financial Condition Examiner's Handbook promulgated by the NAIC as the auditor deems necessary.

63. Pursuant to Virginia law and Tennessee Reg & Rule Ch. 0780-1-65, an independent certified public accountant is required to report in writing within five business days to the board of directors or its audit committee any determination by the auditor that the insurer has materially misstated its financial condition as reported to regulatory authorities as of the balance sheet date under examination, or that the insurer does not meet its minimum statutory capital and surplus requirements as of that date pursuant to applicable law. An insurer who has received such a report is required to forward a copy of report to the domiciliary insurance Commissioner within five (5) business days of receipt of such report, and to provide the independent certified public accountant with evidence of the report being furnished to the

domiciliary insurance Commissioner. If this is not received, the independent certified public accountant is required to furnish to the domiciliary insurance Commissioner a copy of its report within the next five (5) business days.

64. If an independent certified public accountant, subsequent to the date of an Audited Financial Report, becomes aware of facts that might have affected its report, the independent certified public accountant has the obligation to take such action as prescribed by the Professional Standards of the American Institute of Certified Public Accountants.

65. Insurers rely on their actuaries to verify that management's estimates of reserve liabilities for the payment of future claims are reasonable, by providing statements of actuarial opinion regarding the adequacy of loss reserves to the proper regulatory officials. Insurers also rely on their actuaries to ensure that management's reporting of reductions in liabilities due to reinsurance is reasonable.

66. Pursuant to the National Association of Insurance Commissioners ("NAIC") Property and Casualty Annual Statement Instructions:

> The insurer required to furnish an actuarial opinion shall require its appointed actuary to notify its Board of Directors or its audit committee in writing within five (5) business days after any determination by the appointed actuary that the opinion submitted to the domiciliary Commissioner was in error as a result of reliance on data or other information (other than assumptions) that, as of the balance sheet date, was factually incorrect. The opinion shall be considered to be in error if the opinion would not have been issued or would have been materially altered had the correct data or other information been used.

67. Insurers also may rely on legal counsel, whether internal or outside, to ensure that management complies with all applicable laws, including insurance laws regulating minimum capital and surplus, Risk Based Capital ("RBC") levels, reinsurance, required reports, and required regulatory approvals.

68. If financial statements filed and certified by management overstate the value of an insurer's assets (including reinsurance recoveries), or understate its liabilities (including reserves), the insurer's Total Adjusted Capital (and, therefore, surplus as regards policyholders and consequently its RBC percentage), will be misrepresented and overstated. Misrepresenting and overstating an insurer's Total Adjusted Capital, surplus as regards policyholders, and RBC level percentage, exposes policyholders, creditors, members, subscribers, stockholders, and/or the public to economic injury. An insurance company that appears to be, but is not, financially sound continues to attract new and renewing policyholders and continues amassing ever-greater liabilities. The financial condition of the insurer thus can continue to deteriorate, often until such time as the insurer's true financial condition can no longer sustain its operations. By that time, however, the insurer's true liabilities may far surpass its true admitted assets, or the insurer may no longer be able to pay its obligations as they become due in the usual course of business and the insurer may be insolvent.

IV. THE ROLE OF REGULATION OF REINSURANCE AND RETROCESSION

69. Reinsurance is a common arrangement whereby one insurance company (commonly called the assuming company or reinsurer), for consideration, agrees to indemnify another insurance company (the ceding company or reinsured) against all or part of a loss the latter may sustain under a policy or policies it has issued. Retrocession is a transaction whereby a reinsurer, for consideration, cedes to another reinsurer all or part of its obligation to indemnify the original ceding company.

70. Reinsurance and retrocession can be, and usually are, legitimate methods for insurers to spread risk and limit an individual insurer's potential liability to policyholders. When the reinsurer assumes a substantial risk of loss, the ceding company may qualify for a

"credit" against its outstanding loss reserves for the reinsurance on its financial statements. The reinsurance receivable under a qualified reinsurance agreement is an asset and reduces the ceding company's claim liabilities to a net liability which may result in an increase in its Total Adjusted Capital. An increase in Total Adjusted Capital can result in an increase in the RBC level percentage. As a result, an insurer therefore may be able to improve its financial rating, and the marketability of its policies, by reinsuring its policies with a well-respected and financially strong reinsurer.

71. The TDCI and the Virginia SCC are required by law to disallow any credit for reinsurance found to have been arranged for the purpose principally of deception or distortion of an insurer's financial condition, or contracts that do not meet other requirements for preferential treatment as reinsurance recoverable.

72. In some cases, complicated reinsurance treaties appear to transfer risk and merit a credit but, in fact, the transfer of risk is fraudulent or illusory. Reinsurance under which the assuming reinsurer bears no substantial insurance risk of net loss to itself is fraudulent and arranging such reinsurance for the purpose principally of deception or financial statement distortion is common law fraud, is a violation of the National Association of Insurance Commissioners' Statement of Statutory Accounting Practices 62 ("SSAP 62"), and is a violation of Tennessee statutory insurance reporting requirements.

73. Under Tennessee statutory insurance reporting requirements, an insurer is required to disclose, in the annual statement filed with TDCI, whether the insurer has reinsured any risk with any other company under a reinsurance contract and must disclose any provision that would limit the reinsurer's losses below the stated percentage (*e.g.*, a deductible, a loss ratio corridor, a loss ratio cap, an aggregate limit, release, or any similar provision). Insurers are also

required to disclose in the annual statement whether the insurer has released a reinsurer from liability, in whole or in part, for any loss that may occur on a reinsured risk.

74. Under Virginia law, no domestic reinsurer may enter into or modify a reinsurance treaty without prior written approval of the state regulatory authority if for any twelve-month period the reinsurance premium or anticipated change in the ceding insurer's liabilities equals or exceeds 50% of the insurer's surplus to policyholders as of the immediately preceding December 31. A domestic insurer must report all reinsurance and retrocession agreements to the applicable state authority.

V. REINSURANCE RELATIONSHIPS AMONG ROA AND THE RRGs

75. In addition to providing direct insurance to its subscribers, ROA entered into purported contracts of reinsurance with DIR, TRA, and ANLIR.

76. Effective January 1, 1993, ROA and DIR entered into Agreement of Reinsurance No. A1993, pursuant to which DIR ceded between 90% and 100% of its risk to ROA.

77. Effective January 1, 1993, ROA and ANLIR executed Agreement of Reinsurance No. B 1993, pursuant to which ANLIR ceded between 90% and 100% of its risk to ROA.

78. Effective September 8, 1995, ROA and TRA executed Agreement of Reinsurance No. A1995, pursuant to which TRA ceded between 90% and 100% of its risk to ROA.

79. Soon thereafter, the risk that ROA reinsured for DIR, ANLIR, and TRA was retroceded to Gen Re which, in turn, retroceded to FVR.

80. From its inception, ROA entered into a reinsurance arrangement with Gen Re, whereby ROA ceded to Gen Re a portion of ROA's risk under ROA's insurance policies. After the RRGs were formed, ROA entered into a retrocession arrangement with Gen Re further to transfer the insurance risk of DIR, ANLIR, and TRA that had been ceded by the RRGs to ROA. All of this transfer of risk to Gen Re, including risk ceded to ROA by DIR, ANLIR, and TRA, was encompassed within the reinsurance arrangement with Gen Re.

81. As originally structured and disclosed to regulators, the reinsurance treaties between ROA and Gen Re appeared to have constituted a legal, legitimate business practice. As a result of ROA's reinsurance treaties with Gen Re, ROA received a considerable financial reporting credit that had material favorable impact on its financial statements. After the RRGs entered into reinsurance treaties with ROA, they similarly received a credit that had a material favorable impact upon each of their financial statements.

82. The reinsurance treaties among and between ROA, DIR, ANLIR, TRA, and Gen Re were disclosed to regulators and to the public and were disclosed in <u>Best's Insurance Reports</u>. However, as discussed further below, the Management Defendants did not disclose to regulators or to <u>Best's Insurance Reports</u>, and did not obtain prior written approval from Tennessee or Virginia regulators of, certain "non-contractual understandings," "side letters," and other agreements purporting to modify the reinsurance treaties between the companies and Gen Re, and the Gen Re-FVR Retrocession Agreements. The non-disclosures were fraudulent and, in some cases, violated Tennessee and Virginia statutes requiring prior written approval of certain transactions. The non-disclosures were the proximate cause of economic damages to each of the RRGs.

83. At all times before January 31, 2003, TRG maintained and controlled virtually all of the assets of DIR, ANLIR, and TRA. When the companies were put into receivership, the books and records of the RRGs were located in Richmond, Virginia, under the care, custody, and control of the Deputy Receiver for ROA/TRG.

84. Virginia Insurance Commissioner Alfred Gross conducted an investigation that resulted in the filing of a Complaint on behalf of ROA/TRG. In his Complaint, Commissioner Gross alleges a conspiracy among the Defendants, as well as other wrongful acts engaged in by several of the Defendants, all of which resulted in the ultimate financial failure of ROA/TRG.

85. In his Complaint, Commissioner Gross alleges that ROA/TRG had become insolvent well before January 29, 2003. On information and belief, documents demonstrate that Conspiracy Defendants and others engaged in a complex conspiracy of fraudulent schemes to conceal ROA/TRG's financial deterioration from subscribers, members, insureds, policyholders, creditors, regulators, and the public. As a consequence, the Management Defendants were able to cause ROA/TRG to continue issuing new policies and undertaking additional debt, thereby exacerbating ROA/TRG's financial impairment to the point of, and driving ROA/TRG ever deeper into, insolvency.

86. The series of transactions and occurrences described herein caused direct and significant injury to the RRGs, and their policyholders, subscribers, claimants, and creditors.

A. **The Conspiratorial Relationship: Rebates paid to ROA**

87. On information and belief, Gen Re's reinsurance of ROA through 1990

had been so lucrative that Defendant Crews succeeded in demanding rebate of a portion of Gen Re premiums from prior reinsurance contracts as a condition of renewing or entering into new reinsurance treaties with Gen Re.

88. On December 11, 1991, Crews sent Kellogg a draft "comfort" letter (the "1992 Unreported Side Agreement"), as an addition to the ROA-Gen Re Stabilization Treaty. Crews sent the proposed draft to Gen Re so that Gen Re could transfer the letter to Gen Re letterhead, and Kellogg could sign the letter and return it to Crews.

89. On January 6, 1992, Crews sent another draft of the 1992 Unreported Side Agreement to Kellogg.

90. Although the 1992 Unreported Side Agreement purported to be a "legally binding agreement," it stated that it was intended "FOR [CREWS'] EYES ONLY" and was "not to be shared with anyone" at ROA, TRG, or DIR except in Crews' sole discretion. It recited that Gen Re would rebate at least $9.5 million of ceded premiums back to ROA, because such payment was "required to help stabilize the [ROA/Gen Re] relationship." As consideration for "the continued cession of reinsurance business to [Gen Re] on terms mutually acceptable to [ROA and Gen Re]," Gen Re would rebate an additional $6 million of ceded premiums back to ROA or to whomever ROA directed Gen Re to pay, for a total rebate of $15.5 million from 1991 to 1996.

91. On information and belief, the 1992 Unreported Side Letter Agreement was executed by Gen Re and Crews (on behalf of ROA), and payments were made by Gen Re to ROA pursuant to the Agreement.

92. Commissioner Gross alleges in his Complaint that $3.5 million of those

rebates were never deposited in any ROA account. Commissioner Gross further alleges that ROA did not correctly report the rebates received from Gen Re in its financial statements.

93. The 1992 Unreported Side Agreement was the beginning of a long pattern by the Conspiracy Defendants of engaging in unreported transactions in order to evade regulatory scrutiny and maximize benefits to themselves, which ultimately led to injury to the RRGs and their policyholders.

B. Gen Re Loans to FVR Misrepresented as Reinsurance

94. The Management Defendants, with the complicity and active cooperation of Reindel, Wixtead, Kellogg and Migel at Gen Re, and of Richard Witkowski at Atlantic Security, Ltd. ("ASL")[3], engaged in a scheme to make loans from Gen Re to FVR, but to disguise and misrepresent those loans as reinsurance. The "reinsurance" agreements were intended to inflate artificially and improperly FVR's surplus for the business originally written by the RRGs, reinsured by ROA, and then retroceded to Gen Re. This is so-called "pass-through" reinsurance. That is, this is the portion of the RRG ceded reinsurance that was ceded from the RRGs to ROA and in turn "passed through" to Gen Re and was in turn retroceded ("passed through" again) to FVR. The intent of these "reinsurance" agreements was to deceive regulators regarding FVR's ability to satisfy its obligations as a reinsurer of Gen Re.

95. On information and belief, the parties to these "reinsurance agreements" also intended that Gen Re would incur no substantial insurance risk of net loss to itself, in that FVR's obligations under the Gen Re loans would be guaranteed by ROA, and Gen Re's purported "reinsurance" of ROA for this pass-through business was merely an accommodation. The Management Defendants, Gen Re, Milliman, and PwC concealed from Tennessee and

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[3] Atlantic Security, Ltd. was the managing agent for FVR and Witkowski was a principle and agent of Atlantic Security.

Virginia insurance regulators ROA's guaranty of FVR's obligations to Gen Re, thereby misrepresenting and falsely stating the financial condition of ROA. If the regulators had known the true financial condition of ROA, ROA would not have been permitted to continue to operate and, because of the dependence of the RRGs on ROA, the RRGs also would not have been permitted to operate.

96. The RRGs paid premiums which were held in trust by FVR for the payment of claims. Each RRG's pool of premiums paid was held in separate accounts for the benefit of each RRG by FVR. The Management Defendants, particularly Crews, represented to RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage that losses suffered by one RRG would have no impact on monies held by FVR for the benefit of another RRG. Specifically, Crews told the ANLIR and TRA Boards of Directors that losses suffered by DIR would have no effect on ANLIR or TRA. These statements and assurances by Crews and the other Management Defendants were false. All of the Management Defendants were aware of the falsity of these statements and assurances and were under a duty to so inform the Board of Directors for each RRG. Gen Re, and its officers Migel, Kellogg, Reindel, Wixtead had actual knowledge that the Management Defendants had misrepresented to the Boards of ANLIR and TRA that losses suffered by DIR would have no effect on ANLIR or TRA. Gen Re and its officers were further aware that the off-balance sheet loans made to FVR and disguised as reinsurance enabled the Management Defendants to perpetuate this fraud on the ANLIR and TRA Boards.

97. As DIR began to suffer serious losses in the mid 1990s, Crews and the

Management Defendants concocted schemes to artificially inflate the surplus of DIR held by FVR. On information and belief, Gen Re actively encouraged and assisted in the formulation of these fraudulent schemes. The purpose of the schemes as described herein was to create the appearance of reinsurance so that the DIR monies held by FVR would be artificially inflated with no corresponding liability entry on the books of DIR. The purpose of the subterfuge and mischaracterization of the transactions was as follows: (1) to deceive Tennessee and Virginia insurance regulators, (2) to deceive the Board of Directors of each RRG, (3) to deceive the public, including but not limited to policyholders and subscribers of the RRGs, ratings agencies including A.M. Best, all entities to whom the RRGs, TRG and ROA were marketing etc., and (4) to induce MHP (Missouri Hospital Plan) to invest in ROA. The Management Defendants, Director and Officer Defendants and Conspiracy Defendants knew that there was little or no transfer of risk in these transactions and they could not be appropriately booked as an asset nor could they be appropriately characterized as reinsurance. In fact, they were loans and there was an obligation to repay them to Gen Re.

98. Later, in 1998, the Conspiracy Defendants again conspired to use schemes using "loans" misrepresented as reinsurance. In late 1998, certain of the Conspiracy Defendants (including at least Gen Re, Kellogg, Reindel, Seeger, Patterson and Hudgins) caused ROA to enter into agreements with Gen Re and FVR that were variously referred to as "aggregate stop loss/funding cover," "loans," "FVR Cover," "FVR Stop Loss," and "finite contracts" (referred to herein as the "Gen Re Loans"). On information and belief, these agreements took the appearance of risk-transferring reinsurance agreements between Gen Re (as reinsurer) and FVR (as reinsured). As modified by "non-contractual understandings," however, these transactions were actually loans from Gen Re to FVR (*i.e.*, a type of financial reinsurance), guaranteed by

ROA. Financial reinsurance can be deceptive or illusory when it is utilized to create an inaccurate appearance that substantial insurance risk of net loss has been transferred from the reinsured to the reinsurer, thereby inflating the reinsured's surplus to policyholders. Such arrangements (sometimes also called "Surplus Relief Insurance") are typically structured so that risk does indeed appear to be transferred, but the risk is so remote or improbable of occurrence as to be insubstantial. In such cases, even assuming all aspects of the arrangement are available for review, extensive actuarial or financial analysis is normally required in order to ascertain whether the risk being transferred is, in fact, material.

99. On information and belief, these deceptive reinsurance agreements (*i.e.*, guaranteed loans) were executed to inflate FVR's surplus for the pass-through business retroceded from Gen Re to FVR, with the intent of deceiving Gen Re's regulators regarding FVR's ability to satisfy its obligations under the Retrocession Agreements. On information and belief, the parties also intended that Gen Re would incur no substantial insurance risk of net loss to itself, in that FVR's obligations under the Gen Re Loans would be guaranteed by ROA, and in that Gen Re's purported "reinsurance" of ROA was merely an accommodation.

100. On November 30, 1998, by communication, Reindel [on behalf of Gen Re] sent Patterson [on behalf of ROA and the RRGs] an "updated proposal for the aggregate stop loss/funding cover." The letter was copied to Gen Re's Migel and Seeger. This proposal indicated that there would be "Contractual Terms and Conditions" modified by "Assumptions and Non-Contractual Understandings." Pursuant to the proposed contracts, 1998 premiums of $1 million would be ceded for $2 million of coverage attaching at 135% of the Net Subject Premium, 1999 premiums of $2 million would be ceded for $10 million of coverage attaching at

100% of Net Subject Premium. However, this purported reinsurance would be modified by "Non-Contractual Understandings" so that:

> If cover gets hit, the expectation is that Company will renew at higher attachments to help make the reinsurer whole. Long term understanding is that Reinsurer makes Fee and that contract balance is zero or positive by 12/31/03.

CONTRACT BALANCE:	Equals Premium Ceded less Fee less Incurred Losses (including IBNR) plus interest debits and credits on Cash Balance
INTEREST:	Equals Premium Ceded less Fee less Paid Losses plus Interest credits and debits
FEE:	Option 1: 6% of Ceded Premiums Option 2: 4% of Ceded Premiums plus 5% of any negative contract balance calculated quarterly

These proposed transactions were to be in the manner of guaranteed loans, not risk-transferring reinsurance. On information and belief, this proposal was further negotiated before the terms were finalized.

101. On February 8, 1999, in an email to Patterson, Reindel indicated that his notes on the "FVR Cover Non-Contractual Understandings" indicated that:

> 1. Fees are 6% of losses/premium.
> 2. The 2M 'loan' in 1998 needs to be paid back by 12/31/00. The 3M 'loan' needs to be paid back by 12/31/01. All losses need to be paid back plus Fees.
> 3. You will need to pay us back through TVIR [ROA] surplus if FVR surplus is inadequate.

This email was copied to Gen Re's Migel, and Seeger and Kellogg, as well as to Hudgins.

102. A February 16, 2000, communication from Reindel to Patterson, copied to Gen Re's Migel, Seeger and Kellogg, confirms that these finite agreements were, in reality, lines

of credit "to be noncontractually paid back." Reindel indicated that Gen Re was committed to providing "the previously agreed 3M in limits for 1999 which follow the 2M provided in 1998" and discussed the possibility of an additional $3 million loan for 1999, to raise the line of credit to $8 million total. The November 30, 1998, February 9, 1999, and February 16, 2000, correspondence, read together, suggests that repayment of the "loans" would take the form of a commutation of the purported reinsurance agreements, with Gen Re refunding FVR the ceded "premiums" minus (a) a fee of 6% the ceded "premiums," (b) interest debits and credits on the cash balance, and (c) any losses that Gen Re might actually be called upon to pay under the purported reinsurance (*i.e.*, "hits" on the "cover"). As the February 16, 2000, communication explained:

> The original intent of this cover is to provide a booking benefit and not a cash loan. It is designed to be paid back or commuted before we are out of cash.

103. An October 18, 2002, communication from Witkowski to ROA personnel discloses: "FVR paid a premium of 120,000 for the 2,000,000 cover in 1998 and a further 360,000 for 6,000,000 cover in 1999." This suggests that FVR was able to inflate its surplus by booking a "reinsurance" benefit for the Gen Re Loans, the repayment of which was guaranteed by ROA.

104. A June 15, 2000, communication, together with others on June 14 and 15, 2000 suggests that Gen Re was experiencing problems reconciling Milliman's reserve numbers for FVR with numbers that Gen Re was reporting to Gen Re's regulators in order to claim a credit for its purported retrocession of risk to FVR. The Gen Re Loans were said to "play into this also," apparently referring to the fact that a portion of FVR's claimed surplus was attributable to Gen Re Loans.

105. By communication to Patterson and Hudgins dated April 23, 2001, Reindel referred to moving forward with "an ROA 2001 accident year stop loss cover as a way of balancing our experience on the finite covers on the DIR and ANLIR books," and noted that the premium for the cover would be $706,667 with a limit of $2 million. On information and belief, the phrase "balancing our experience on the finite covers" referred to the "If cover gets hit" provision of the Gen Re Loans (*i.e.*, ROA's obligation to make good any loss that Gen Re might actually be called upon to pay under the deceptive reinsurance agreements between Gen Re and FVR). In fact, ROA paid the $706,667 "premium" for the "ROA 2001 accident year stop loss cover," which, on information and belief, really was ROA's reimbursement to Gen Re for losses Gen Re had paid under its 1998 $2 million off-balance sheet loan disguised as reinsurance of FVR losses. On information and belief, based on communications from October 21, 2002 and October 18, 2002, ROA sought reimbursement from FVR, and Witkowski was told, in response to his questioning, that: "Gen Re incurred the $706,667 and then was reimbursed by ROA for reasons of expediency." In effect, this disguised "reinsurance" transaction between ROA and Gen Re was intended to secure ROA's obligation to repay the $2 million off-balance sheet loan made in 1998 by Gen Re to FVR. This separate "payback cover" was specifically calculated by Gen Re and the Management Defendants to obtain Gen Re's desired security while concealing the transaction from the ROA Board.

106. In a communication dated December 20, 2001, Reindel informed Patterson and Hudgins that certain of the "Finite contacts" would be commuted as part of the "LPT" transaction. This was the "repayment" of the Gen Re Loans anticipated by the November 30, 1998, February 9, 1999, and February 16, 2000, correspondence.

107. Gen Re's willingness to provide the Gen Re loans was made contingent

upon ROA's signing of Endorsement 12 to Reinsurance Agreement A264 between ROA and Gen Re ("Endorsement 12"). On information and belief, Endorsement 12 was executed on February 5, 1999.

108. Endorsement 12 provided, effectively, that if Patterson ceased to be President and CEO of ROA at any time prior to October 1, 2001, Gen Re would have the option of increasing the risk charge to ROA. On information and belief, Gen Re insisted upon Endorsement 12 because of Patterson's complicity in, and necessity to, the non-contractual understandings.

109. Note 10 to the ROA annual statement for the year 1998 asserted falsely that ROA had no material contingent liabilities arising from "litigation, income taxes, and other matters," even though ROA had "non-contractually" agreed to reimburse Gen Re for up to $8 million if Gen Re were actually required to pay any losses under the $8 million of deceptive reinsurance (and if FVR did not have adequate surplus to reimburse Gen Re).

110. Patterson and Hudgins made similar false statements in ROA's annual statements for 1999, 2000, and 2001.

111. These statements were false because Patterson and Hudgins had obligated ROA to guarantee up to $8 million of FVR obligations to Gen re under the Gen Re Loans.

112. On information and belief, contemporaneously with filing ROA's 1998, 1999, 2000, and 2001 annual statements, Patterson and Hudgins mailed copies to Gen Re which therefore had actual knowledge that Patterson and Hudgins had not accounted for or disclosed the Gen Re Loans.

113. "The ROA 2001 accident year stop loss cover," structured as purported

reinsurance with a $706,667 premium and a limit of $2 million, was, in fact, a reimbursement by ROA of Gen Re's "hits" on the finite covers on the DIR and ANLIR books of FVR's pass-through business, and was not intended to transfer to Gen Re any substantial insurance risk of net loss to itself. Pursuant to VA. CODE ANN. § 38.2-1316.6, the "ROA 2001 accident stop loss cover" is deemed, *prima facie*, to have been arranged for the purpose principally of deception or financial statement distortion.

114. Part of the motivation of the Management Defendants, Director and Officer Defendants and Conspiracy Defendants was to help ensure that the due diligence process in which MHP (Missouri Hospital Plan) was fully engaged in the 1998 and 1999 time frame was not interrupted by the full disclosure of DIR's deteriorating financial condition. MHP's participation and investment in ROA yielded millions of dollars.

115. Patterson and Hudgins made false statements on ROA's Annual Statements for 1998, 1999, 2000, and 2001, asserting that ROA had no material contingent liabilities even though ROA had contingent liabilities to reimburse Gen Re for the sham reinsurance. These false statements were material by Patterson and Hudgins and which ultimately led to injury to the RRGs and their policyholders.

C. RRGs' Reliance on Gen Re Loans to FVR Misrepresented as Reinsurance

116. RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage relied to the detriment of their Companies and their policyholders on the misrepresentations made by the Conspiracy Defendants. The Management Defendants as described herein falsified financial reports to RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-

fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage with the intent that RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage would rely on the misrepresentations. Similarly, the Management Defendants, Director and Officer Defendants and Conspiracy Defendants executed sham reinsurance contracts with the full knowledge and intent that the "non-contractual" understandings entered into with the Management Defendants would be secreted from RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. The Management Defendants, upon information and belief, actively discussed with Defendants Gen Re, Reindel, Kellog, Seeger and Migel the misleading nature of the "reinsurance contracts." The Management Defendants, Director and Officer Defendants and Conspiracy Defendants knew that the "reinsurance contracts" were executed for the purpose of deceiving RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage

117. The $2 million "reinsurance contract" with Gen Re that should have been properly characterized as a loan in 1998 was misrepresented to RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage occurring in 1998 and 1999. The $6 million "reinsurance contract" with Gen Re that should have been properly characterized as a loan in 1999 was misrepresented to RRG

policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coveragein each and every quarterly board meeting occurring in 1999 and 2000. The Gen Re "reinsurance contracts" were delivered to RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage and/or referenced in financial documents presented to RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage.

118. The financial documents were prepared and presented to the Boards of Directors of the RRGs by the Management Defendants. The "reinsurance contract" itself was a fraudulent misrepresentation by Gen Re made to RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage with the intent of Gen Re that RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage should rely on them.

119. RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage in reliance on the misrepresentations and suppressions by the Conspiracy Defendants of the "loan scheme," refrained from taking affirmative steps to minimize or eliminate damage to the RRGs and its

policyholders. Had it been apprised of the true facts, RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage would have taken several steps. The failure of RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage to take these steps in 1998, 1999 and 2000 resulted in damage to the Companies and their policyholders. The following actions would have been taken but for the deceit practiced upon them by the Conspiracy Defendants.

a. Each RRG would have conducted an investigation of the circumstances surrounding the fraudulent transaction, identified the culpable parties (identified in this Amended Complaint as the Management Defendants) and replaced them.

b. Each RRG would have conducted an audit of the reserves and all monies held by FVR.

c. Each RRG would have ensured that all monies held by FVR for the benefit of each RRG would be unaffected by losses experienced by the other RRGs.

d. Each RRG would have informed the Tennessee and Virginia regulators of the impropriety of the transaction.

e. Each RRG would have ceased writing any new business.

f. Each RRG would have sought to procure reinsurance for its direct book of business without respect to arrangements that may have existed for other RRGs.

120. The failure to take these steps directly resulted in damage toRRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. Had RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage taken these steps (or any one of them) the fraud practiced by the Conspiracy Defendants would have been interrupted much earlier than it was and it is the contention of the Receiver that DIR, ANLIR and TRA could have been saved and many millions of dollars in losses prevented for the Companies and their policyholders. The calculation of the damage to DIR, ANLIR and TRA and their policyholders is ongoing in their receivership estates. Once the damage calculations are finalized the same will be added by amendment.

D. $10 Million Fraudulently Transferred from ROA to FVR Trusts

121. DIR's losses continued to mount throughout the 1990's, and as a result, DIR's trust account with FVR fell into a $12 million deficit. This deficit presented problems for all Defendants who knew or should have known of the Trust deficit. No Defendant who knew or should have known could afford for the continuing Trust deficit to be discovered, otherwise their fraudulent and incestuous relationship would have been uncovered by the insurance regulators and by the Board Members of the RRGs and ROA. As such, the Defendants including the Management Defendants and Gen Re continued their fraudulent schemes to artificially inflate the surplus of DIR held by FVR.

122. In order to disguise the $12 million deficit, DIR sent FVR a $2 million

letter of credit, and in addition, TRA sent FVR a $10 million letter of credit. These letters of credit raised questions from TDCI regulator Kathy Fussell because the instrument was in the form of a letter of credit rather than a premium. Following her inquiry with the Defendant Crews, Fussell was told to disregard the letters of credit because the deal had been unwound. Upon information and belief, this response to Fussell came as a result of contact between Crews and Gen Re.

123. Following the failure of the letter of credit scheme, Gen Re continued to pressure ROA to fill the hole the $12 million deficit had created in order to limit Gen Re's exposure under its reinsurance agreements. As a result, Patterson, Crews, and Hudgins conspired to make a disguised transfer of $10 million from ROA to the FVR Bermuda Trusts.

124. Among the aforementioned agenda items for the December 4, 2000, meeting at Gen Re's headquarters was "Funding for Trust Agreement." On information and belief, Patterson, Crews, and Hudgins conspired to make a disguised transfer of $10 million from ROA to the FVR Bermuda Trusts (assisted by the complicity of Witkowski and Atlantic Security, and the complicity, reckless disregard, or negligence of PwC). If such payment had not been disguised, the Companies, their policyholders and creditors, A.M. Best, and regulators likely would have discovered the schemes employing undisclosed rebates and deceptive reinsurance.

125. On December 28, 2000, Patterson and Hudgins transferred $10 million to be incorrectly and misleadingly accounted for as prepayment of reinsurance premiums to Gen Re, included in ROA's 2000 annual statement (filed under oath) among "Premiums Due from Reinsurance Companies," thereby inflating ROA's surplus to policyholders by $10 million. On information and belief, Patterson, Crews, and Hudgins also caused ROA's 2000 annual statement

to omit a $1.3 million reinsurance liability to Gen Re, thereby overstating surplus to policyholders by that additional amount.

126. Even after the December 28, 2000, fraudulent transfer of $10 million, the FVR Bermuda Trusts were underfunded. In a February 21, 2001, correspondence to Crews (copied to Hudgins), Patterson stated:

> Bill, I have already gotten an email from Vicki [Seeger, of Gen Re] saying we are $10 - $14M short in the trust funds for FVR. I haven't responded yet as I'm still churning on the presentation for [A.M.] Best. We still need to brainstorm on the FVR situation. Between Surplus Notes at FVR and DIR's results, we continue to be cash challenged. Nothing to do right now but Vicki is hot on this case before [Gen Re's] Steve Barbor [sic] gets involved.

127. While auditing ROA's statutory financial statements for the year ending December 31, 2000, PwC detected ROA's improper treatment of the $10 million "prepaid premiums" as an asset. In a March 26, 2001, communication, Patterson enlisted the assistance of Crews in dealing with PwC:

> Bill, I may need some help with the PwC auditors. I hear that they are making threats about nonadmitting the $10M we sent to [Gen Re] before year end. There was a meeting today and I'm not sure what was resolved but Fri is our deadline and I may need some "opining" from you, if possible.

> In response to the questions, ROA officers arranged a meeting to brainstorm about what position they would take. An email from Ken Patterson to Bill Crews states, "We [ROA officers] need to brainstorm with you on this as well. Once we take a position, I think it will be irreversible and if they want to – they can probably support that it's nonadmitted."

Furthermore, in an appropriately devious joke, Patterson inquires of Crews, "Are your 'cannons [sic] of ethics' loaded?" Id

128. On information and belief, the result of the "brainstorming" by Crews, Patterson, and Hudgins represented an attempt to enlist the aid of Gen Re to support the fraudulent characterization by Patterson, Crews, and Hudgins of the $10 million "asset."

129. On or about April 2, 2001, Patterson asked Seeger to influence PwC on this issue, by fraudulently confirming in writing that the $10 million was a prepayment of premiums to Gen Re:

> Will you please, by signing below where indicated, confirm that the $10 Million transfer to [Gen Re] in late December <u>was explained to you as</u> a prepayment that ROA made to the fund for premiums expected to normally have been remitted during the first quarter of 2001?

(Emphasis added).

130. Undoubtedly, Defendant Gen Re understood the purpose behind the improper accounting and an email from Gen Re's Wixtead stated:

> Once again they are showing the $10M deposit made directly to the trust account at 12/31/00 as a premium advance...This allows them to show the bottom line figure for the 9/30/01 account as zero funds due.

So although Gen Re had knowledge of the improper transfer and accounting they allowed the fraud to be perpetuated, and worse, ignored auditors' requests of confirmation of the transfer.

131. On information and belief, Patterson, Crews, and Hudgins also attempted to enlist the aid of Wachovia (through Richard Hazelgrove) in influencing PwC on this issue.

132. On information and belief, PwC succumbed to the efforts of the Conspiracy Defendants (including at least Patterson, Hudgins, and Crews), failing to require ROA to non-admit the $10 million "prepaid premiums," even though PwC knew, or should have known, that this was a false entry. PwC only described the $10 million "prepaid premiums" as an "unusual transaction." PwC's failure to require ROA to non-admit the $10 million "prepaid

premiums" constituted intentional, reckless, or negligent dereliction of its duty as an independent auditor and resulted in a material misstatement of ROA's financial condition.

133. On May 8, 2001, a senior analyst of the [Virginia] Bureau [of Insurance], after completing a review of ROA's 2000 annual statement, questioned Patterson regarding the large increase in "premiums due from reinsurance companies." The analyst requested that Patterson provide details and explain the reason for the increase.

134. On May 21 and 22, 2001, Hudgins e-mailed Witkowski and ASL regarding the fraudulent $10 million transfer from ROA to the FVR Bermuda Trusts. Hudgins wrote: "we want them [(*i.e., regulators*)] to think . . . it is an advance premium."

135. On June 6, 2001, Hudgins, with the knowledge of Patterson, replied to the Bureau's analyst by letter including the following false statement:

> This increase related to reinsurance premiums due early in the first quarter of 2001, and sent to the reinsurer within the last few days of 2000. Since Reciprocal of America had a favorable cash position at year end, it was a business decision to make this payment. The remainder of the balance was miscellaneous recoverables due from the reinsurer, General Reinsurance Corporation, an A++ A.M. Best rated reinsurer.

136. As a result of the overstatement of ROA's Surplus to policyholders, the RRGs' 2000 Annual Statements filed with TDCI also fraudulently overstated Surplus to Policyholders.

137. The fraudulent $10 million transfer did not account for the entire $12 million deficit in DIR's trust account with FVR. As a result, the Conspiracy Defendants including the Management Defendants and Gen Re engaged in arbitrary reserve write-downs in the amount of $2 million. These write downs were fraudulent and were relied upon by RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-

fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage to their detriment.

E. RRGs' Reliance on the Fraudulent $10 Million Transfer from ROA to FVR Trusts

138. RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage relied to their detriment on the misrepresentations made by the Conspiracy Defendants. Upon information and belief, the Management Defendants, Director and Officer Defendants and Conspiracy Defendants actively suppressed the true nature of the $10 million transfer from RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. The Management Defendants, Director and Officer Defendants and Conspiracy Defendants knew that the "$10 million transfer" was completed for the purpose of deceiving RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage.

139. The true nature of the $10 million fraudulent transfer from ROA to FVR Trusts was fraudulently characterized as a pre-paid insurance premium to RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. Specifically, in all board meetings during this time frame the $10 million transfer was presented to RRG policyholders – claimants – subscribers, TRG (as manager of the

RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage as a pre-paid insurance premium.

140. The documents surrounding the fraudulent transfer were prepared and presented to the Board of Directors of the RRGs by the Management Defendants.

141. The Board of Directors of the RRGs, in reliance on the misrepresentations and suppressions by the Management Defendants, Director and Officer Defendants and Conspiracy Defendants of the $10 million transfer that was fraudulently characterized as a pre-paid insurance premium, refrained from taking affirmative steps to minimize or eliminate damage to the RRGs and its policyholders. Had the RRGs been apprised of the true facts, the Board of Directors of the RRGs would have taken several steps. The failure of the RRGs Board of Directors to take these steps in 1999 and 2000 resulted in damage to their Companies and their policyholders. The following actions would have been taken but for the deceit practiced by the Conspiracy Defendants.

a. Each RRG would have conducted an investigation of the circumstances surrounding the fraudulent transaction, identified the culpable parties (identified in this Amended Complaint as the Management Defendants) and replaced them.

b. Each RRG would have conducted an audit of the reserves and all monies held by FVR.

c. Each RRG would have ensured that all monies held by FVR for the benefit of each RRG would be unaffected by losses experienced by the other RRGs.

d. Each RRG would have informed the Tennessee and Virginia regulators of the impropriety of the transaction.

e. Each RRG would have ceased writing any new business.

f. Each RRG would have sought to procure reinsurance for its direct book of business without respect to arrangements that may have existed for other RRGs.

142. The failure of RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage to take, these steps directly resulted in damage to the RRGs and their policyholders. Had RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage taken these steps (or any one of them) the fraud practiced by the Conspiracy Defendants would have been interrupted much earlier than it was and it is the contention of the Receiver that DIR, ANLIR and TRA could have been saved and many millions of dollars in losses prevented for their Companies and their policyholders. The calculation of the damage to DIR, ANLIR and TRA and their policyholders is ongoing in their receivership estates. Once the damage calculations are finalized the same will be added by amendment.

F. ROA Employed Sham Commutations

143. In yet another scheme, ROA employed sham commutations to transfer funds between the RRGs without Board notification and, more importantly, without Board approval. In particular, on April 1, 2001, The Reciprocal Alliance (TRA) and FVR executed a commutation that transferred $5M in liabilities owed by FVR to TRA without any consideration. This "commutation" forced TRA to accept $5 million in liabilities which were owed by FVR without due consideration and resulted in a loss of surplus at TRA in an amount in excess of $5

million. However, upon information and belief, mention to the TRA Board of this assumption of $5 million in liabilities did not occur until months after the Commutation Agreement had been executed. Outraged TRA Board members challenged the validity of the transfer but were told that nothing could be done as the commutation was completed. Kenneth Patterson and Bill Crews said that the commutation could not be reversed. This sham "commutation" further evidences the intent that the ROA family of companies absorb any risk of loss under the Pass Through Arrangement and that Gen Re be completely insulated from actual loss under the Pass Through Arrangement per the terms of the "handshake" side deal.

G. False Recording of "Assets" on ROA's Financial Statements

144. The Management Defendants had a regular practice of re-characterizing liabilities as "assets" whenever needed to fraudulently boost surplus to policyholders shortly before filing quarterly or annual statements. The purpose of these fraudulent characterizations was to enable the Management Defendants to report ROA's, DIR's, ANLIR's, and TRA's Surplus to Policyholders as being above the RBC percentage calculated as 200% of Authorized Control Level ("ACL," which is half of the RBC), thereby avoiding enhanced regulatory scrutiny.[4]

145. These false entries were material and ultimately led to injury to the RRGs and their policyholders.

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[4] Risk Based Capital ("RBC") is the result of a method that attempts to determine the surplus required to support the business written by an insurance company, given the characteristics of the insurance company's assets. A complex calculation produces an estimate of the required capital. The Authorized Control Level ("ACL") is equal to one-half of this capital or surplus requirement. Actions by the domiciliary insurance department are predicated on the ratio of actual surplus to ACL. If the ratio is above 200%, no action is contemplated. A ratio between 150% and 200% is "company action level," at which the company is required to take corrective action. If the ratio is between 100% and 150%, regulatory action is authorized. If the ratio is less than 100%, regulatory intervention is required.

H. Arbitrary Reserves Write-Downs

146. The arbitrary write-down of reserves was a covert, yet brazen scheme falsifying the claim reserve numbers of ROA so as to minimize the required regulatory reserves that ROA and its sister companies would be mandated to possess. The Management Defendants caused DIR and ROA to engage in arbitrary and improper reserve write-downs for loss and loss adjustment expenses, which resulted in the financial statements for DIR and ROA showing artificially high Surplus to Policyholders that in turn overstated the Risk Based Capital ("RBC") percentages. These artificially high RBC percentages had the effect of concealing from the regulators the true financial condition of DIR and ROA. If the regulators had known the true condition of DIR and ROA, the regulators would not have allowed DIR and ROA to continue to operate. If the Virginia insurance regulators had not permitted ROA to continue to operate, the Tennessee insurance regulators would in addition not have permitted ANLIR, DIR and TRA to continue to operate.

147. The reserve write-downs occurred on several occasions shortly before quarterly and annual financial statements were due to be filed, and were backdated so that the statements for periods already ended would report Total Adjusted Capital in excess of 200% of ACL, the level below which company action would have been required. The Management Defendants and the Director and Officer Defendants would instruct claims personnel to reduce large case reserves without any reasonable basis for doing so and without regard to claims case reserving policies. Legitimate claim reserve write-downs include an involved analysis of liability, damages, mitigating factors and settlement options; however ROA's analysis and the criteria for claims slashing wrongfully centered upon the amount of money by which ROA had to reduce reserves so as to escape regulatory scrutiny.

148. ROA did no substantive analysis of the claims they slashed. Instead, the amount of the reserve write-downs was outcome-driven by the amount needed to keep Total Adjusted Capital in excess of 200%. In April 1995, January 1998, December 1998, December 1999, and October 2000, Patterson, Crews, and Kelley directed claims personnel to reduce DIR claims, and in each instance to backdate the reductions for purposes of upcoming DIR Quarterly and Annual Financial Statements to be filed with the TDCI and, because of the reinsurance relationship, for purposes of ROA's Quarterly and Annual Financial Statements to be filed with the Virginia SCC. The total amount of these reserve write-downs was in excess of $6.5 million. The reserves write-downs were made without examination of the claims filed by claims adjusters pursuant to established claims review policies and there was therefore no legitimate basis for the claims reserves write-downs. As a result of the reserves write-downs, ROA's Surplus to Policyholders was fraudulently overstated by approximately $2.3 million in the March 1995 Quarterly Statement, $2 million in the 1997 Annual Statement, and $300,000 in the 1998 Annual Statement, and $1 million in the September 2000 Quarterly Statement. DIR's Surplus to Policyholders was similarly overstated in the corresponding Quarterly and Annual Statements filed with the TDCI.

149. On an even grander scale, in November 2000, January 2001, and November 2001, Patterson, Crews, and Hudgins directed claims personnel to reduce ROA claims, and in each instance to backdate the reductions for purposes of upcoming Quarterly and Annual Financial Statements to be filed with the Virginia SCC. The total amount of these reserves write-downs was in excess of $30 million. The reserves write-downs were made without examination of the claims files by claims adjusters pursuant to established claims review policies and therefore lacked any legitimate basis for reserves write-downs.

150. Tellingly, employees who had been instructed by ROA officials to write-down the claims recognized the superficiality of the write-down criteria and documented their orders to seemingly ensure themselves protection from the suspicious reserve slashing they were commanded to perform. One such memorandum thoroughly chronicled the date, time, individuals and instructions given to him. He also set out the superficial criteria upon which he was supposed to base the reserve reductions:

> The criteria for selecting cases [for write-downs] was: 1. Any cases that were created in the first nine months of 2001 with indemnity reserves greater than $50,000; 2. Cases that had reserve increases of $50,000 or more during that same nine month period.

151. In this particular instance, the orders from top ROA officers resulted in an aggregate reserve slashing of nearly $19 million in November of 2001. In another illustration of the arbitrary and extreme reductions that ROA officers ordered, a newly appointed ROA employee wrote a revealing email questioning Bill Crews about such write-downs. In the email he questions:

> Bill, today at my roundtable discussion a claim came up…[T]he claim currently carries a $1.00 case estimate on the claim file set up for the primary policy and a $2.1M case estimate on the excess policy claim file. According to the claims handler this file had a $1.5M case estimate on it that was reduced to $1.00 by "executive management". Further investigation reveals that numerous cases received similar adjustments to their case estimates. Given your role as general counsel I would appreciate your thoughts on this.

151. As a result of the arbitrary reserves write-downs, ROA's Surplus to Policyholders was fraudulently overstated by approximately $5.4 million in the September 2000 Quarterly Statement, $5.8 million in the 2000 Annual Statement, and $25.8 million in the September 2001 Quarterly Statement.

153. In addition to the effect of the write-down of DIR reserves on ROA, the write-down also impacted the RBC calculation for DIR. The acknowledged $2.1 million write-down for 2001 was sufficient to put the ratio of policyholder surplus to ACL above 200%, and keep DIR from immediate regulatory scrutiny. ANLIR and TRA each reported reserves write-downs in their 2001 annual statements. The write-down of reserves also impacted the RBC calculation for ANLIR. The acknowledged $330,000 write-down for 2001 was sufficient to put the ratio of policyholder surplus to ACL above 200% and keep ANLIR from immediate regulatory scrutiny. The reserve write-down for TRA in 2001 was $5 million. While this write-down was substantial and translated into a significant impact on policyholder surplus, the surplus of TRA would have been above the 200% of ACL level even without the write-down.

154. Intentionally seeking to conceal their fraudulent actions, the Management Defendants did not share analysis of RRG loss reserves with RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. The following is the text of a May 29, 1997 Memorandum from Kenneth Patterson to William F. Jacobs, Jr., Judy A. Kelly, Robert E. McMillion, Jr. and Bill Crews:

> Just for you <u>confidential</u> info. only, please see a nice summary Vince [Franz] put together on where we are with reserves by company. The select column is where E&Y thinks the perfect point is; however, as long as we are between the low and high ends we are OK.
>
> My personal preference is ***not to share with the Boards much of this info*** since the last time we did (FVR) it came back to haunt us. (Emphasis Added).

H. Reliance by RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage on the Fraudulent and Arbitrary Write-down of Reserves

155. The Management Defendants, Director and Officer Defendants and Conspiracy Defendants, as described in paragraphs 155 through 161 of this Complaint intentionally suppressed from RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage that the surplus of DIR was overstated as a result of the arbitrary write-down of reserves as described herein. This overstatement of surplus occurring in 1995, 1997, 1998, 1999, 2000 and 2001 was withheld from RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. The Management Defendants, Director and Officer Defendants and Conspiracy Defendants made misrepresentations and/or suppressed these material matters from the Boards of Directors of the RRGs during all board meetings occurring in 1995, 1997, 1998, 1999, 2000 and 2001. Moreover, the Management Defendants misrepresented the surplus of DIR in financial reports, including quarterly and annual reports, to RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. The Defendants, Milliman and Sanders, were aware of the improper and arbitrary write-down of reserves as described herein and were under a duty to report the same to RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage but failed to do so. The intent of the Management Defendants, Director and Officer Defendants and Conspiracy Defendants to defraud RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each

RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage was formulated to prevent action harmful to their fraudulent scheme from being undertaken by RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage.

156. RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage, in reliance on the misrepresentations and suppressions by the Management Defendants, Director and Officer Defendants, Conspiracy Defendants and Milliman Defendants of the fraudulent and improper write-down of the reserves of DIR, refrained from taking affirmative steps to minimize or eliminate damage to the RRGs and its policyholders. Had they been apprised of the true facts, RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage would have taken steps. The failure of the RRGs Boards of Directors to take these steps in 1995, 1997, 1998, 1999, 2000 and 2001 resulted in damage to the Companies and their policyholders. The following actions would have been taken by RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage but for the deceit practiced upon it by the Management Defendants, Director and Officer Defendants, Conspiracy Defendants and Milliman Defendants:

a. Each RRG would have conducted an investigation of the circumstances surrounding the fraudulent transaction, identified the culpable parties (identified in this Amended Complaint as the Management Defendants) and replaced them.

b. Each RRG would have conducted an audit of the reserves and all monies held by FVR.

c. Each RRG would have ensured that all monies held by FVR for the benefit of each RRG would be unaffected by losses experienced by the other RRGs.

d. Each RRG would have informed the Tennessee and Virginia regulators of the impropriety of the transaction.

e. Each RRG would have ceased writing any new business.

f. Each RRG would have sought to procure reinsurance for its direct book of business without respect to arrangements that may have existed for other RRGs.

157. The failure of RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage to take these steps directly resulted in damage to the RRGs and their policyholders. Had RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage taken these steps (or any one of them) the fraud practiced by the Conspiracy Defendants would have been interrupted much earlier than it was and it is the contention of the Receiver that DIR, ANLIR and TRA could have been saved and many millions of dollars in losses prevented for the Companies and their policyholders. The Milliman Defendants conducted claims studies for the RRGs. Their study of initial reserves, adjustor authority levels to change reserves, claim settlement practices, etc. was not disclosed in any of the RRG reserve

reports, even though the Milliman Defendants had concern about these areas. The Milliman Defendants discovered that inaccurate underlying factors such as, the artificial suppression of case reserves, the change in philosophy on litigating claims and the conscious slowdown of settlements were occurring at the RRGs. These factors, known to the Milliman Defendants as professional actuaries, had the effect of biasing estimates of ultimate losses and allocated loss adjustment expense projections. The Milliman Defendants also knew that ROA personnel were pressured every year after 1999, by the Management Defendants to push reserves for ROA, and therefore the RRGs, to a bear minimum or at times below acceptable minimums. The calculation of the damage to DIR, ANLIR and TRA and their policyholders is ongoing in their receivership estates. Once the damage calculations are finalized the same will be added by amendment.

VII. SIDE LETTER AGREEMENTS

A. The 2000 Unreported Side Letter Agreement

158. On information and belief, early in the year 2000, the Management Defendants, Director and Officer Defendants and Conspiracy Defendants became aware that premiums charged under DIR policies in prior years had been inadequate, and/or that losses being experienced were more severe than had been predicted. Gen Re became concerned that the FVR Bermuda Trusts were inadequately funded to cover FVR's obligations to Gen Re under the Gen Re-FVR Retrocession Agreements, and that the extent of Gen Re's insurance risk of net loss was greatly increased. These Defendants conspired, through the use of a fraudulent and unreported side agreement, to limit or eliminate Gen Re's reinsurance risk of loss, while maintaining the illusion that Gen Re continued to bear a substantial insurance risk of net loss under the Gen Re/ROA reinsurance treaties.

159. Reindel, on behalf of Gen Re, therefore proposed a scheme involving an aggregate cap that would limit Gen Re's reinsurance risk of loss under the Gen Re/ROA reinsurance treaties. On information and belief, this scheme was intended to allow ROA to continue claiming a credit for its reinsurance with Gen Re, undiminished by the effect of the cap, which would not be disclosed to regulators.

160. A cap on Gen Re's obligations to ROA had the potential and did in fact diminish the surplus of ROA, which diminished the security for the reinsurance available to the RRGs. It thereby effectively destroyed the reinsurance available to the RRGs, since the RRGs reinsurance with ROA had been passed-through to Gen Re.

161. On information and belief, the Management Defendants, Director and Officer Defendants and Conspiracy Defendants hoped that they could yet avoid discovery of the deteriorating financial condition of ROA, and therefore of each of the RRGs, by evading the enhanced regulatory monitoring that would be triggered if ROA's RBC or the RBC of any RRG fell to a level low enough to require regulatory intervention. In the absence of the fraud practiced upon the RRGs by these repeated misrepresentations and suppressions, the RBC of DIR would have fallen to a level low enough to require both regulatory intervention and immediate action by RRG policyholders -- claimants -- subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. The Report of the Inter-Organizational Structure Committee of the Board of Directors of Reciprocal of America found that "ROA's RBC ratio is adversely impacted by the reinsurance obligations it has with DIR, ANLIR and the Alliance, whereby premiums are ceded to FVR and General Reinsurance Corporation."

162. On information and belief, by letter dated November 16, 2000, Seeger sent what she referred to as "a finalized side-letter agreement" (the "2000 Unreported Side Agreement") from Gen Re's offices to Patterson. This communication was copied to Gen Re's Migel and Kellogg. This communication proves the fraudulent nature of the written reinsurance agreement that the Management Defendants, Director and Officer Defendants and Conspiracy Defendants executed and delivered to RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. The intent of these Defendants was that RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage would rely on the written agreements with no knowledge of the 2000 Unreported Side Agreement.

163. The 2000 Unreported Side Agreement was dated as of November 11, 2000. On information and belief, Gen Re executed the Agreement on December 15, 2000. On December 28, 2000, Patterson and Hudgins, on behalf of ROA, executed the Agreement.

164. Seeger knew as early as 1997 that unreported side agreements were illegal under Virginia law, having received a January 10, 1997, email from a Gen Re employee quoting the relevant statute. Seeger forwarded the email by facsimile to Hudgins on January 28, 1997.

165. Pursuant to the 2000 Unreported Side Agreement, Gen Re's liability for payments made by ROA at and after 12:01 a.m., January 1, 2000, for Net Loss and Adjustment Expense under all Subject Reinsurance Agreements combined, purported to be limited to the sum of $140 million plus 100% of the reinsurance premium ceded by ROA, net of commission, for

calendar year 2000 under Agreements of Reinsurance No. A456 and No. A481 (the "$140 Million Cap").

166. For purposes of the 2000 Unreported Side Agreement, the Subject Reinsurance Agreements included reinsurance agreements between ROA and Gen Re for business written by ROA, and also reinsurance agreements between ROA and Gen Re for business written by the RRGs and assumed by ROA under reinsurance agreements with the RRGs.[5]

167. On information and belief, neither ROA nor any of the RRGs received any consideration for agreeing to the $140 Million Cap, *nor were the independent Directors of the RRGs privy to the arrangement.*

168. In ROA's Annual Statement for the Year 2000, which was filed with TDCI on or about March 2001, and relied upon by the Tennessee and Virginia regulators, Patterson and Hudgins (on information and belief with the knowledge and complicity of Gen Re, Crews & Hancock, Crews, and Kelley) answered falsely under oath "No" to the following general interrogatories:

> 15.(a) Has this company reinsured any risk with any other company under a quota share reinsurance contract which includes a provision which would limit the reinsurer's losses below the stated quota share percentage (e.g., a deductible, a loss ratio corridor, a loss ratio cap, an aggregate limit or any similar provision?)
>
> 16.(a) Has this company reinsured any risk with any other company and agreed to release such company from liability, in

[5] The applicable agreements were stated as Agreements of Reinsurance No. A238 between ROA and Gen Re; No. A273 between ROA and Gen Re (applying to business assumed by ROA from DIR under Agreement No. A 1993 between ROA and DIR); No. A289 between ROA and Gen Re (applying to business assumed by ROA from ANLIR under Agreement No. B 1993 between ROA and ANLIR); No. A442 between ROA and Gen Re (applying to business assumed by ROA from TRA under Agreement No. A1995 between ROA and TRA); No. A456 between ROA and Gen Re; and No. A481 between ROA and Gen Re.

> whole or in part, from any loss that may occur on the risk, or portion thereof, reinsured?

169. Patterson made similar misrepresentations in ROA's subsequent quarterly financial statement and in ROA's 2001 Annual Statement (and amended 2001 Annual Statement). These statements were delivered by the Management Defendants to the RRGs and relied upon by RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage.

170. These false statements were material and were intended to deceive.

171. On information and belief, contemporaneously with their being filed, the Management Defendants mailed a copy of the 2000 Annual Statements of ROA and each of the RRGs to Defendant Gen Re. Defendants Reindel, Seeger, and Kellogg therefore had actual knowledge that the Management Defendants had not reported the 2000 Unreported Side Agreement.

172. The 2000 Unreported Side Agreement, like the other schemes and arrangements evidences the pattern of racketeering activity engaged in by the Defendants for the purpose of evading regulatory scrutiny in furtherance of maximizing benefits to themselves, which ultimately led to injury to the RRGs and their policyholders.

B. RRGs' Reliance on the Fraudulent Scheme Involving the 2000 Unreported Side Agreement

173. The RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage relied to the detriment of

their Company and their policyholders on the misrepresentations made by the Management Defendants, Director and Officer Defendants and Conspiracy Defendants and Milliman Defendants. The Management Defendants as described herein falsified financial reports presented to RRGs and relied upon by RRG policyholders -- claimants -- subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage with the intent that RRGs and relied upon by RRG policyholders -- claimants -- subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage would rely on the misrepresentations. Similarly, the Management Defendants, Director and Officer Defendants, and Conspiracy Defendants executed sham reinsurance contracts with the full knowledge and intent that the 2000 Unreported Side Agreement would be secreted from RRGs and relied upon by RRG policyholders -- claimants -- subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. The Management Defendants, Director and Officer Defendants, Conspiracy Defendants and Milliman Defendants, upon information and belief, actively discussed among themselves the misleading nature of the 2000 Unreported Side Agreement to the reinsurance contract reported in the financials of ROA and each of the RRGs. The Management Defendants, Director and Officer Defendants, Conspiracy Defendants and Milliman Defendants knew that the reinsurance contracts, with the 2000 Unreported Side Agreement, was executed for the purpose of deceiving RRGs and relied upon by RRG policyholders -- claimants -- subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage.

174. To the contrary, this information was withheld from RRGs and relied upon by RRG policyholders -- claimants -- subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage at the board meetings and in the financial reports of the RRGs and ROA. Indeed, the delivery of the written reinsurance agreement between ROA and Gen Re to RRGs and relied upon by RRG policyholders -- claimants -- subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage amounted to a fraudulent misrepresentation by the Management Defendants, Director and Officer Defendants, Conspiracy Defendants and Milliman Defendants to RRGs and relied upon by RRG policyholders -- claimants -- subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage. It was the intent and purpose of the Management Defendants, Director and Officer Defendants and Conspiracy Defendants to induce and obtain the reliance of RRGs and relied upon by RRG policyholders -- claimants -- subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage upon the written reinsurance agreement without disclosure of the 2000 Unreported Side Agreement. The Milliman Defendants became aware of the 2000 Side Letter on February 20, 2002. Despite knowledge that the Management Defendants had intentionally withheld the disclosure of the 2000 Cap

Letter, the Milliman Defendants allowed their actuarial report of ROA and the RRGs for the year 2000 to be disseminated to regulators even though it was false.

175. RRG policyholders – claimants – subscribers, TRG (as manager of the RRGs), each RRG attorney-in-fact, state insurance regulators, official insurance rating services and entities to whom the RRGs marketed insurance coverage, in reliance on the misrepresentations and suppressions by the Management Defendants, Director and Officer Defendants, Conspiracy Defendants and Milliman Defendants of the scheme involving the 2000 Unreported Side Agreement refrained from taking affirmative steps to minimize or eliminate damage to the RRGs, and their policyholders. Had it been apprised of the true facts, the RRGs would have taken several steps. The failure of the RRGs to take these steps in 2000 resulted in damage to the Companies, and their policyholders. The following actions would have been taken but for the deceit practiced by the Defendants:

a. Each RRG would have conducted an investigation of the circumstances surrounding the fraudulent transaction, identified the culpable parties (identified in this Amended Complaint as the Management Defendants) and replaced them.

b. Each RRG would have conducted an audit of the reserves and all monies held by FVR.

c. Each RRG would have ensured that all monies held by FVR for the benefit of each RRG would be unaffected by losses experienced by the other RRGs.

d. Each RRG would have informed the Tennessee and Virginia regulators of the impropriety of the transaction.

e. Each RRG would have ceased writing any new business.

f. Each RRG would have sought to procure reinsurance for its direct book of business without respect to arrangements that may have existed for other RRGs.

176. The failure of the RRGs to take these steps directly resulted in damage to the RRGs and their policyholders. Had the RRGs taken these steps (or any one of them) the fraud practiced by the Conspiracy Defendants would have been interrupted much earlier than it was and it is the contention of the Receiver that DIR, ANLIR and TRA could have been saved and many millions of dollars in losses prevented for the Companies and their policyholders. The calculation of the damage to DIR, ANLIR and TRA and their policyholders is ongoing in their receivership estates.

C. The 2002 Unreported Side Letter Agreement

177. On information and belief, in furtherance of their continuing conspiracy, in May of 2001, the Conspiracy Defendants discussed limiting further, through a new fraudulent and unreported side agreement, Gen Re's reinsurance risk of loss under the Gen Re/ROA reinsurance treaties.

178. In October 2001, Seeger, Migel, and Kellogg began proposing various drafts of a side agreement to replace the 2000 Unreported Side Agreement.

179. By January 4, 2002, Patterson distributed to Kelley, Hudgins, and Crews the final draft of a reinsurance "white paper" that had been sent on January 3, 2002, to members of ROA's Executive Committee. As reflected in the "white paper," the Conspiracy Defendants became increasingly concerned that premiums charged for the physician book of business starting in about 1997 were even more inadequate, and/or that losses being experienced were even more severe, than they had feared in 1999, resulting in FVR having "a minimum amount of surplus." Based on this new information, Gen Re proposed a new fraudulent scheme pursuant to

which ROA would enter into several related agreements as part of a step transaction with Gen Re and FVR in and after March of 2002, effective retroactively as of December 31, 2001, or January 1, 2002, depending on the agreement. Collectively, the agreements comprising the step transaction were referred to as the "Loss Portfolio Transfer."

180. Pursuant to the Loss Portfolio Transfer, FVR commuted to Gen Re all of FVR's liabilities and obligations under the Gen Re-FVR Retrocession Agreements. In exchange for the commutation of liabilities and obligations under the Gen Re-FVR Retrocession Agreements, FVR paid Gen Re a commutation payment of $112,998,000 from the FVR Bermuda Trusts, which was intended to cover Gen Re's potential liability for the commuted risk, attributable to the pre-2002 claims. Gen Re agreed to release to FVR's control another $11 million of assets that had been in the FVR Bermuda Trusts (the "Pre-2002 Trust Balance").

181. As part of the Loss Portfolio Transfer, Gen Re ceased accepting reinsurance from ROA, including the pass-through reinsurance from the RRGs, for the primary layers that it had previously accepted and ceded to FVR. ROA and Gen Re executed Reinsurance Agreement A593, effective December 31, 2001, whereby Gen Re agreed to reinsure ROA for claims made by insureds of DIR, ANLIR, or TRA in 2002 through 2005, if the occurrence giving rise to the claim took place on or before December 31, 2001 (the "Gen Re Tail"). The following executive summary of a different proposed agreement between ROA, Gen Re, ANLIR, DIR and TRA set out the changes effective December 31, 2002 as follows:

> ROA, FVR and [Gen Re] entered into a transaction to change the existing reinsurance relationship among the three parties. The transaction consisted of the following components:
>
> - [Gen Re] terminated the reinsurance and retrocession agreements applicable to the primary layers of ANLIR, DIR and TRA business reinsured by ROA so that such business would no longer pass through [Gen Re] to FVR.

- [Gen Re] and ROA entered into a tail cover (Reinsurance Agreement A593) whereby [Gen Re] agreed to reinsure incidents occurring on or before December 31, 2001 which are reported on policies issued by ANLIR, DIR or TRA between January 1, 2002 and December 31, 2005

- [Gen Re] assumed liability for all outstanding losses under the existing [Gen Re]-FVR retrocession agreements in exchange for a cash commutation payment from FVR of approximately $113 million dollars.

- [Gen Re] and ROA signed an Aggregate Cap Letter to cap [Gen Re's] liability at $135 million dollars for losses on ANLIR, DIR, and TRA business previously ceded to [Gen Re] and FVR from ROA.

  The transaction described above did not affect the "true" reinsurance provided by [Gen Re] on the secondary layers of ANLIR, DIR and TRA business. Such business continue[d] to be reinsured by [Gen Re] pursuant to the terms of Reinsurance Agreement A443 between ROA and [Gen Re].

182. On information and belief, on January 11, 2002, Seeger confirmed with Patterson the terms of the tentative second side agreement among the Conspiracy Defendants regarding the replacement of the 2000 Unreported Side Agreement. This letter was copied to Migel, Reindel, and Crews.

183. On information and belief, on January 24, 2002, ROA's Senior Vice President Actuarial informed Milliman's Pete Wick and Robert L. Sanders that a "unique loss ratio cap of 130% or greater" would be put in place. This communication was copied to Hudgins and Patterson.

184. On February 19, 2002, Sanders acknowledged to Patterson that Bland had briefed Sanders on the effects of the Loss Portfolio Transfer, and had informed Sanders of the 2000 Unreported Side Agreement and the proposed new side agreement (the "2002 Unreported Side Agreement"). Sanders' asked Patterson for copies of the side agreements, which Bland provided to Sanders dated February 20, 2002.

185. On February 27, 2002, Defendant Sanders issued his statement of Actuarial Opinion for ROA, for the year ended December 31, 2001. At page 3, paragraph 5, Sanders represented:

> My opinion on the loss and loss adjustment expense reserves net of ceded reinsurance assumes that all ceded reinsurance is valid and collectible. The Company has represented to me that it knows of no uncollectible reinsurance cessions. I am not aware of any reinsurance that the Company treated as collectible but should have treated as uncollectible. This does not imply an opinion on the financial conditions of the Company's reinsurers. I have not anticipated any contingent liabilities that could arise if the reinsurers do not meet their obligations to the Company as reflected in the date and other information provided to me.

186. On page 4 of the opinion, Sanders discussed various risk factors, including: "If the Company's reinsurance protection does not respond to adverse reserve deviation, such deviation could materially affect the Company's surplus." He did not mention, however, the proposed 2002 Unreported Side Agreement or its $135 million aggregate cap, of which he had actual knowledge. Defendant Sanders did not, in evaluating net reserves, address the impact of the proposed 2002 Unreported Side Agreement or its $135 million aggregate cap on the ceded reinsurance.

187. Although the 2002 Unreported Side Agreement had not been finalized as of the date of the Statement of Actuarial Opinion signed by Sanders, he had knowledge of its impending implementation. More importantly, Sanders did not mention the 2000 Unreported Side Agreement and its $140 million cap and attendant impact on reserves as of December 31, 2001. This Agreement was in effect and was known to Sanders and Milliman. Since the 2000 Unreported Side Agreement made material changes to existing reinsurance contracts, Sanders and Milliman should have questioned the accounting treatment of the affected reinsurance contracts. Statement of Statutory Accounting Practices 62 ("SSAP 62," which is a statutory

implementation of Financial Accounting Standards 113 ("FAS 113")) requires that reinsurance contracts that undergo material changes be treated as deposit accounting, not the more favorable reinsurance accounting. The implementation of a cap on a contract would be such a material change.

188. Despite knowledge of the 2002 Unreported Side Agreement and its $135 million aggregate cap, Defendants Milliman and Sanders never disclosed these as a material change in the assumptions previously employed by them in providing an opinion on the adequacy of reserves of ROA or the RRGs. Nor did Milliman or Sanders ever determine, or disclose, the additional amount of reserves that would be necessary as a consequence of the 2002 Unreported Side Agreement and its $135 million aggregate cap. The failure of Milliman and Sanders to disclose this information led to major problems for ROA and the RRGs. The following is a portion of the text from a December 16, 2002 e-mail from Sanders to TRG Executive Vice President Thomas K. Smith that discusses the exposure that the aggregate cap placed on ROA:

> [W]e will be completing our analysis this week on ROA's exposure to the LPT aggregate cap of $135 million, but based on Vince's [Franz] e-mail of December13, we should quickly begin discussing ways to dampen what may be significant reserve adjustments to ROA in the fourth quarter.
> At least two thoughts come to mind:
> (1) Discounting ROA's Loss Reserves: We had discussions with Craig about approaching the Virginia Bureau to receive permission for ROA to begin discounting its loss reserves for statutory financial reporting. The time has come to raise this issue with the Bureau. If they are not receptive to allowing discounting for ROA's reserves related to its core hospital business, perhaps they can be persuaded that, given the nature of the exposure from the LPT aggregate cap (where ROA will not make its first payment until after Gen Re has first paid its $135 million), a special case can be made for that promotion of ROA's reserves related to the aggregate cap; and/or
> (2) Revising the terms of the LPT: Another approach would be to renegotiate the terms of the LPT with Gen Re. Perhaps Gen Re would be willing to increase the aggregate by $25 to $50 million (which would bring the cap to $160 or $185 million, respectively). Gen Re would expect a payment for this

additional coverage, and depending on the negotiations, the payments would be roughly equivalent to the discounted value of the additional coverage provided by Gen Re. Most likely, the payments will need to be made by FVR (Crews & Hancock can confirm this), which may place a constraint as to how much additional coverage can be purchased.

This would appear to be a significant disclosure item (related to the subordinated convertible note offering being prepared by ROA) that we should try to resolve as quickly as possible (emphasis added).

189. On information and belief, on March 6, 2002, Migel sent a draft of the 2002 Unreported Side Agreement to Patterson.

190. On information and belief, on or about April 2, 2002, Hudgins and Reindel provided PwC with a list of the Agreements of Reinsurance between ROA and Gen Re, which list mentioned reinsurance agreements entered into, terminated, or commuted effective December 31, 2001, as part of the Loss Portfolio Transfer that was an integral part of the 2002 Unreported Side Agreement, but the list did not mention the 2002 Unreported Side Agreement or its $135 million aggregate cap.

191. The Loss Portfolio Transfer, which was effective as of January 1, 2002, was part of the 2002 Unreported Side Agreement. Pursuant to the Agreement, Gen Re's liability for payments made by ROA, including payments on account of RRG claims, was further limited. Payments for claims incurred, at and after 12:01 a.m., January 1, 2002, purported to be limited to an aggregate cap of $135,000,000. On March 27, 2002, Patterson executed the 2002 Unreported Side Agreement. On April 11, 2002, Gen Re executed the 2002 Unreported Side Agreement.

192. On information and belief, Kelley and Hudgins had knowledge of, and conspired with, Patterson, Crews, and Crews & Hancock with respect to the execution of the 2002 Unreported Side Agreement. Before their issuance of a year-end 2001 actuarial report, the Milliman Defendants were aware of the details of the Loss Portfolio Transfer and the execution of the Loss Portfolio Transfer itself. Despite their concerns and knowledge, the Milliman

Defendants provided a "clean" actuarial statement of opinion on company reserves as of December 31, 2001 (the Loss Portfolio Transfer was drawn up as a 2001 event for FVR and a 2002 event for ROA).

193. The reinsurance agreements that were the subject of the 2002 Unreported Side Agreement included reinsurance agreements between ROA and Gen Re for business written by ROA, and also reinsurance agreements between ROA and Gen Re for business written by the RRGs and assumed by ROA under reinsurance agreements with the RRGs.[6]

194. On information and belief, by April 30, 2002, PwC had knowledge and copies of the 2002 Unreported Side Agreement (and, therefore, of the 2000 Unreported Side Agreement) and the $135 million aggregate cap. However, PwC's audit report and opinion on ROA's amended statutory basis financial statements for the years ended December 31, 2001, and 2000, dated September 25, 2002, did not mention or account for the 2002 Unreported Side Agreement or its $135 million aggregate cap, although it mentioned the components of the Loss Portfolio Transfer that the Management Defendants had reported to the Commission.

194. PwC's audit report and opinion on ROA's amended statutory basis financial statements did not opine as to whether the reinsurance accounting treatment of the contracts affected by the Loss Portfolio Transfer was proper. As mentioned earlier, SSAP 62 requires that material changes to reinsurance agreements be accounted for under deposit accounting rules rather than the more favorable reinsurance accounting treatments.

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[6] The listed agreements were Agreements of Reinsurance No. A238 between ROA and Gen Re, No. A273 between ROA and Gen Re (applying to business assumed by ROA from DIR under Agreement No. A 1993 between ROA and DIR), No. A289 between ROA and Gen Re (applying to business assumed by ROA from ANLIR under Agreement No. B 1993 between ROA and ANLIR), No. A442 between ROA and Gen Re (applying to business assumed by ROA from TRA under Agreement No. A 1995 between ROA and TRA), No. A456 between ROA and Gen Re, and No. A593 between ROA and Gen Re.

195. The 2002 Unreported Side Agreement and the $135 million cap applied to claims that had occurred by December 31, 2001, and were reported as of that date, as well as to claims on policies in-force on December 31, 2001. This was known as the Gen Re Tail coverage. Two sets of claims are not included in this Gen Re Tail coverage: claims that occur after December 31, 2001, on policies in-force as of December 31, 2001; and new and renewal policies written on or after December 31, 2001, with claims that occurred prior to December 31, 2001, reported after that date.

196. In July 2002, ROA and FVR entered into an agreement that provided purported reinsurance for these claims. As part of the entire Loss Portfolio Transfer process, ROA and FVR executed Agreement of Retrocession No. 2002-1 ("Retrocession Agreement No. 2002-1"), which was effective retroactively to January 1, 2002, pursuant to which FVR reinsured ROA for new and renewal policies written or reinsured by ROA which became effective after 11:59 p.m., December 31, 2001, with respect to:

> (1) claims and losses resulting from Occurrences taking place at and after [11:59 p.m., December 31, 2001]; and
>
> (2) claims first made at and after [11:59 p.m., December 31, 2001] under coverage's written on a claims-made basis but only to the extent such claims are not otherwise reinsured under the terms of Agreement of Reinsurance No. A593 between ROA and General Reinsurance Corporation [(i.e., the Gen Re Tail)]

197. Retrocession Agreement No. 2002-1 obligated ROA to pay FVR 100% of the reinsurance premium allocated to the limits reinsured thereunder, net of commission, under "ROA's reinsurance agreements A1993 with DIR, B1993 with ANLIR, and A1995 with TRA." Retrocession Agreement No. 2002-1 obligated FVR to pay ROA 100% of that portion of Net Loss sustained by ROA that were not payable by Gen Re pursuant to Gen Re's reinsurance agreements with ROA. Retrocession Agreement No. 2002-1 would include amounts not payable

as the result of the $135 million aggregate cap, as well as claims occurring after December 31, 2001, on the then in-force policies.

198. On a date in 2002 contemporaneous with, or subsequent to execution of, Retrocession Agreement No. 2002-1, Patterson (ostensibly on behalf of ROA), FVR, and Wachovia executed a trust agreement, to secure the performance of FVR's obligations to ROA and the RRGs pursuant to Retrocession Agreement No. 2002-1 (the "Wachovia-FVR Trust Agreement").

199. The initial funding of the trust created by the Wachovia-FVR Trust Agreement (the "Wachovia-FVR Trust") was made on July 11, 2002, in the amount of $6,140,578.20, which, on information and belief, consisted of part of the Pre-2002 Trust Balance of $11 million.

200. The Wachovia-FVR Trust was executed for the purpose of obtaining for ROA the benefit of reinsurance accounting. A reinsurance agreement with a non-admitted, alien (i.e. Bermuda) reinsurer does not qualify for the beneficial reinsurance accounting treatment unless there is a trust fund running to the benefit of the ceding company, funds are withheld by the ceding company to cover the reinsured portion of the risk, or a letter of credit is posted by the reinsurer. The amount of the credit against current liabilities is limited to the amount of the trust, the amount of funds withheld by the insurer, or the face value of the letter of credit.

201. Reinsurance accounting would permit ROA to reduce certain claims liabilities for reinsurance in the form of a reduction from liability for reinsurance ceded to FVR in an amount not exceeding the maximum of (1) the liabilities carried by ROA (including liabilities for reinsurance obligations to the RRGs) and covered under the reinsurance agreement, or (2) the amount of funds held in the Wachovia-FVR Trust.

202. The Wachovia-FVR Trust existed as security for ROA's obligations to the RRGs, which liabilities passed to FVR under Retrocession Agreement No. 2002-1.

203. Any credit for reinsurance obtained by ROA under Virginia law enabled ROA to maintain sufficient surplus to continue to be an admitted reinsurer with respect to the RRGs under Tennessee law.

204. On information and belief, the Wachovia-FVR Trust was always capitalized inadequately to fund FVR's disclosed and undisclosed obligations to ROA, and Defendants Patterson, Hudgins, Crews, Kelley and Gen Re had knowledge that the Wachovia-FVR Trust was inadequately capitalized.

205. At the time the 2002 Unreported Side Agreement was executed, the Conspiracy Defendants knew, or should have known, that ROA's Net Loss and Adjustment Expense under all Subject Reinsurance Agreements would far exceed the $135 million aggregate cap on Gen Re's liability as ROA's reinsurer.

206. No later than June of 2002, Defendant Milliman had knowledge that the aggregate liabilities under the publicly disclosed ROA-Gen Re reinsurance treaties exceeded the $135 million aggregate cap on Gen Re's liability established by the 2002 Unreported Side Agreement.

207. ROA's Net Loss and Adjustment Expenses under the business subject to the Loss Portfolio Transfer between Gen Re and FVR alone were already anticipated in March 2002 to be on the order of at least $165 million. Therefore, even without considering the other Subject Reinsurance Agreements, ROA's reported insurance recoverable from Gen Re would likely be impaired by at least $30 million, and ROA's March 2002 Quarterly Statement overstated ROA's surplus to policyholders by at least $30 million.

208. If the full impact of the Loss Portfolio Transfer had been recognized by ROA in its quarterly financial statements filed with the SCC, the resulting decrease in policyholder surplus would have indicated that the SCC act sooner to take regulatory action regarding ROA. Therefore, this overstatement of credit for reinsurance and the concomitant overstatement of ROA policyholder surplus translated into overstatements on the RRGs' March, June, and September 2002 Quarterly Statements filed with the TDCI and signed by and attested to by certain of the Management Defendants.

209. Under Virginia law, the SCC's prior written approval of the 2002 Unreported Side Agreement was required if, as of the date the 2002 Unreported Side Agreement was executed, the resulting change in ROA's liabilities was anticipated to equal or exceed 50% of ROA's surplus to policyholders as of the immediately preceding December 31.

210 Disclosure of the 2002 Unreported Side Agreement to the TDCI would have prompted immediate regulatory investigation.

211. As of December 31, 2001, as reported in ROA's 2001 Annual Statement, signed February 27, 2002, 50% of ROA's reported surplus to policyholders equaled $41,118,168.50. However, as discussed above, ROA's reported surplus to policyholders as of December 31, 2001, was inflated by at least $22.9 million (as a result of $2.5 million in false assets and $20.4 million of arbitrary reserves write-downs). Fifty percent of ROA's reported surplus to policyholders as of December 31, 2001, did not exceed $30 million (*i.e.*, $41.1 million less 50% of the $22.9 million surplus to policyholders inflation). In fact, as reported in ROA's Amended 2001 Annual Statement, signed September 6, 2002 (after the Virginia SCC required ROA to re-file its annual statement due to irregularities), 50% of ROA's reported surplus to policyholders as of December 31, 2001, equaled $18,789,402.50.