

THE STATE OF TEXAS	§	IN THE DISTRICT COURT OF
	§	
v.	§	
	§	
MEMORIAL SERVICE LIFE	§	TRAVIS COUNTY, TEXAS
INSURANCE COMPANY, LINCOLN	§	
MEMORIAL LIFE INSURANCE	§	
COMPANY, AND NATIONAL	§	
PREARRANGED SERVICES, INC.	§	250 TH JUDICIAL DISTRICT

REPLY BRIEF IN SUPPORT OF MOTION TO LIFT STAY

I. INTRODUCTION¹

1. In an attempt to exercise control over assets which are not property of the Lincoln’s estate, the Special Deputy Receiver (“SDR”) makes a series of false legal and factual contentions. First and foremost among them is the claim that Northstar filed its Motion to Lift the Stay in order to pursue property of the estate. On the contrary, Lincoln’s property interest in the Reinsurance Agreement and the related collateral terminated before this insolvency proceeding commenced and, therefore, the Liquidation Order does not apply to this property. Given that Northstar is not making a claim against the estate, Northstar is not seeking preferential treatment as a creditor. Rather, Northstar seeks only to resolve a dispute concerning whether the Reinsurance Agreement and related collateral posted by Northstar thereunder constitute assets of the estate.

2. The SDR also asserts, without legal basis, that the stay cannot be lifted simply because the SDR disputes that the Agreement was terminated. The SDR’s assertions in this regard are plainly incorrect. Indeed, in arguing that its mere assertion of a claim that the collateral posted by Northstar to secure its obligations under the Agreement is “property of the estate” prevents this Court from lifting the stay in order to determine the Termination Issue, the

¹ Unless otherwise specified, defined terms herein are used as defined in Northstar’s previously-filed Motion to Lift Stay.

SDR, in effect, asks this Court to proceed as though the SDR has prevailed on the Termination Issue – without permitting Northstar the opportunity to present its case to any tribunal. Without lifting the stay in order to allow the arbitration panel to determine whether the Agreement was properly terminated as of May 2, 2008, however, the threshold question whether the collateral posted under that Agreement constitutes “property of the estate” to which the stay even applies cannot be resolved. In permitting actions against property in which the insolvent insurer has no equity interest, sec. 443.008(h)(2) of the Receivership Act recognizes that the mere assertion of a claim that the estate has an interest in particular property does not automatically transform that property into “property of the estate.” Thus, lifting the stay in order to determine that threshold issue is both appropriate and warranted.

3. Equally spurious is the SDR’s contention that the Permanent Injunction entered by this Court prohibits Northstar from pursuing a resolution of the termination dispute. This argument is contrary to Northstar’s contractual rights, the Receivership Act and the express terms of the Liquidation Order. The Receivership Act and the Liquidation Order are designed to protect the property of the Lincoln estate – not to ensnare assets in which the estate had no interest at the time the insolvency proceeding commenced. The SDR asks the Court to disregard the numerous bankruptcy cases Northstar cited as authority for lifting the stay in these circumstances, without explaining why these cases are not analogous and without citing any cases to the contrary. Clearly, federal bankruptcy law addresses the same issues as does the Receivership Act regarding the appropriate balance to strike between protection of the insolvent entity, protection of parties who had contractual relationships with the insolvent entity that had terminated prior to the insolvency, and protection of any third parties with any interest in those contractual relationships. Thus, federal bankruptcy law provides persuasive authority for construing provisions of the Receivership Act that have not yet been construed by any reported Texas decision. Finally, the Permanent Injunction itself contemplates that actions against

Lincoln can proceed as allowed by the Receivership Act – and the Receivership Act allows Northstar’s action to go forward.

4. Further, any dispute concerning the termination of the Agreement should be resolved by arbitration, in accordance with Northstar’s contractual rights and Section 443.005 of the Receivership Act. Even if the Court were to reject arbitration, however, the Court still should conduct an evidentiary hearing on whether the Agreement is property of the estate. Although the SDR attempts to argue that there are complex factual disputes about the termination of the Agreement, the reality is that there are only a handful of facts salient to Northstar’s exercise of its contractual termination rights: (1) that according to Lincoln’s own calculation, Lincoln owed \$846,000 to Northstar as of January 31, 2008; (2) that Lincoln failed to pay that amount; (3) that, sixty days following the end of the January accounting period, Northstar properly provided Lincoln with a thirty-day notice of termination under the Agreement; (4) that said termination relieves Northstar of any further liability under the Agreement; and (5) that Lincoln made no attempt to cure the default or make any subsequent payments. Tellingly, the SDR has not denied any of these facts. The SDR also has not denied that if the Agreement has been properly terminated, Lincoln’s right to the collateral has also necessarily terminated, given that Northstar would have no further obligations under the Agreement requiring security. Indeed, the SDR apparently does recognize that Lincoln cannot draw on the trust assets or the LOC unless it has a right to do so under the Reinsurance Agreement. (Exh. D to SDR Response.) In addition to the restraining order entered by the Court, prior to the entry of the insolvency stay, the arbitration panel also enjoined Lincoln from drawing on the collateral.

5. Moreover, the SDR does not point to any evidence of the supposedly complex factual disputes that would preclude resolution of the Termination Issue. The SDR specifically claims that Northstar repudiated the contract and/or that Lincoln’s failure to pay amounts due to

Northstar resulted from an error or omission that Northstar somehow induced Lincoln to make. To the contrary, the evidence demonstrates that Northstar has always complied with its contractual obligations under the Agreement, even after it demanded arbitration. Similarly, no evidence supports the claim that Lincoln's failure to pay was the result of any actual error, mistake, or misunderstanding by Lincoln that the TDI's Supervisory Order somehow prevented payment. Further, the SDR's suggestion that Northstar somehow tricked Lincoln into this default by failing to raise the issue with the Arbitration Panel on April 28, 2008 – twenty-six days after Lincoln's right to cure had expired – is absurd on its face. In fact, Northstar discussed with Lincoln its failure to make any payments for January, February or March on the day of the organizational meeting for the arbitration.

6. Finally, the SDR's conclusory statements of burden are not supported by the facts. On the contrary, as will be discussed below, Northstar will suffer significant hardship if the stay is not lifted.

7. For all of these reasons, Northstar's motion to lift the stay should be granted.

II. ARGUMENT

A. **The Stay Should Be Lifted in order to Determine whether the Collateral Posted to Secure Northstar's Obligations under the Reinsurance Agreement Constitutes Property of the Estate.**

8. The lynchpin for the SDR's argument that the stay should not be lifted is Paragraph 5.1 of the Permanent Injunction entered on September 22, 2008 which provides:

An automatic stay is in effect with respect to actions against Defendants or their property as provided by TEX. INS. CODE § 443.008(c). In accordance with TEX. INS. CODE § 443.008(f), such stay of actions against Defendants is in effect for the duration of this proceeding, and the stay of actions against Defendants' property is in effect for as long as the property belongs to the receivership estate.

9. The SDR attempts to sidestep the fact that, as a condition precedent to the continued stay of actions against the property of the estate, *the property at issue must belong to the estate*. Indeed, Paragraph 5.1 of the Permanent Injunction, cited above, specifically

recognizes that stay applies for only so long as “the property belongs to the receivership estate.” Moreover, Texas Insurance Code § 443.008(h)(2) permits the pursuit of “acts against property” if the insolvent insurer does not have equity in the property, and the property is not necessary to an effective rehabilitation plan. Northstar and the SDR dispute the threshold question of whether or not the collateral that Northstar posted under the Agreement constitutes property of the estate to which the stay applies.

10. The SDR also ignores the express language of Paragraph 4.7 of the Permanent Injunction, which provides that the stay applies to “prosecuting any . . . arbitration . . . against Defendants, Defendants’ Property or any part thereof, or the Liquidator; *except as permitted by TEX. INS. CODE Chapter 443.*” (Emphasis added.) As explained at length in Northstar’s Motion to Lift Stay and herein, §§ 443.008(h)(1) and (2) of the Receivership Act provide two independent bases for lifting the stay to permit Northstar’s arbitration against Lincoln to proceed with respect to the Termination Issue. Accordingly, the Permanent Injunction expressly permits lifting the stay under the precise circumstances presented by Northstar’s Motion.

11. The SDR’s position is apparently that the collateral for the Agreement constitutes property of the estate because “the books and records of the receivership estate establish that the trust account is ‘property of the estate’ . . .”² (SDR Response, p. 1.) Of course, the fact that the collateral is on the books and records of the receivership estate establishes nothing more than that the estate’s position is that the collateral constitutes property of the estate. Simply saying it doesn’t make it so, however – nor does the conclusory, self-serving affidavit submitted by the SDR somehow establish that the estate owns the collateral. The SDR attempts to rely on § 443.004(20) to assert that the collateral constitutes “property of the estate” because such property includes “entitlements that . . . existed prior to the entry of an order of rehabilitation or liquidation.” (SDR Response, ¶ 4.5.) Any entitlement that Lincoln may have had to the

² Northstar notes that the collateral at issue includes a letter of credit (“LOC”) as well as a trust account.

collateral supporting Northstar's obligations under the Reinsurance Agreement *ceased* prior to the entry of both the order of rehabilitation and the order of liquidation in this case, however. Accordingly, the estate has no entitlement to that property.

12. The SDR argues against lifting the stay because “[t]here is no ruling, whether final or interlocutory, granting Northstar ownership of the trust funds.” (SDR Response, ¶ 6.2.) This is not a situation, however, where Northstar was required to obtain a court ruling transferring ownership of the collateral to Northstar as, for example, one might be required to do in a foreclosure situation. Rather, once Northstar had validly terminated the Agreement and had no further obligation thereunder, Northstar was entitled to the return of its collateral by operation of the Agreement.

13. As explained at length in Northstar's Motion to Lift Stay, Lincoln's rights in the collateral were extinguished upon the valid termination of the Agreement for nonpayment of sums owed to Northstar. In short, as of April 2, 2008, Lincoln had failed to pay Northstar over \$846,000 that Lincoln owed to Northstar as of January 31, 2008. (Exhibit C to Motion to Lift Stay; Tweedie Aff., attached as Exh. 1 hereto, ¶¶ 5-6; January Account Statement, attached as Exh. 2.) In light of the fact that this amount was calculated by Lincoln and set forth in its January statement of account to Northstar, there can be no dispute that Lincoln owes Northstar at least this amount. (Exh. C to Motion to Lift Stay; Exh. 1, ¶ 5; Exh. 2.) Accordingly, on April 2, 2008, Northstar exercised its right under Article VII of the Agreement to send Lincoln a 30-day written notice of termination. (Exhibit B to Motion to Lift Stay; Exh. 1, ¶ 6.) On May 2, 2008, the Agreement terminated pursuant to the terms of Article VII. (Exh. A to Motion to Lift Stay.) Given that termination, the Lincoln estate has no “equity” in the Agreement. In addition, the Agreement is not necessary to an effective rehabilitation plan because Lincoln is in liquidation, not rehabilitation. Thus, § 443.008(h)(2) of the Texas Insurance provides a clear basis for permitting Northstar's action against Lincoln to go forward.

14. The SDR next argues that Northstar has not established “cause” sufficient to lift the stay pursuant to § 443.008(i) because “cause” is restricted to the single set of circumstances outlined in that provision. (SDR Response, ¶ 4.4.) In so arguing, the SDR ignores the plain language of § 443.008(i), which provides, in pertinent part, that:

“cause” *includes* the receiver canceling a policy, surety bond, or surety undertaking if the creditor is entitled, by contract or by law, to require the insured or the principal to have a policy, surety bond, or surety undertaking and the insured or the principal fails to obtain a replacement policy, surety bond, or surety undertaking . . .

§443.008(i)(emphasis added). Pursuant to § 311.005 of the Texas government code, “‘includes’ and ‘including’ are terms of enlargement and not of limitation or exclusive enumeration, and use of the terms does not create a presumption that components not expressed are excluded.” TEX. GOV. CODE, §311.005(13). In accordance with this statutory definition, Texas courts have repeatedly construed the word “include” to signify a non-exclusive list. *E.g., State v. Vasilas*, 187 S.W.3d 486, 488-92 (Tex. Crim. App. 2006); *H.G. Sledge, Inc. v. Prospective Inv. & Trading Co., Ltd.*, 36 S.W.3d 597, 603 (Tex. App. – Austin 2000, pet. denied); *Wilburn v. State*, 824 S.W.2d 755, 762 (Tex. App. – Austin 1992, no writ). Thus, the SDR’s contention that “cause” only exists under one limited set of circumstances contravenes the explicit pronouncements of both the Texas legislature and the Texas courts regarding the meaning of the word “includes” and, therefore, must be rejected.

15. The SDR further contends that federal bankruptcy law does not provide persuasive authority for interpreting the meaning of “cause” under the Receivership Act. Specifically, the SDR argues that because Northstar has not argued that § 443.008(i) is ambiguous, it is inappropriate to look to federal bankruptcy law in order to interpret “cause.” This argument flows from the same flawed premise that leads to the SDR’s overly-restrictive view of “cause,” discussed in Paragraph 12 above. Northstar need not argue that the statute is ambiguous – to the contrary, the plain meaning of the statute is that “cause” encompasses both

the specific set of circumstances set forth in the Receivership Act *and* other sets of circumstances.

16. Moreover, federal bankruptcy law provides perhaps the closest analogy to the Receivership Act and, therefore, case law arising under federal bankruptcy law provides persuasive authority for determining when “cause” to lift the insolvency stay exists. Indeed, various federal courts have stated that the Bankruptcy Code and case law interpreting the Bankruptcy Code can be persuasive authority when analyzing an analogous provision under state law. *See, e.g., In re AFI Holding, Inc.*, 525 F.3d 700, 703 (9th Cir. 2008) (“Where state statutes are similar to the Bankruptcy Code, cases analyzing the Bankruptcy Code provisions are persuasive authority.”); *Badalament, Inc. v. Mel-O-Ripe Banana Brands, Ltd.*, 265 B.R. 732, 738 (E.D. Mich. 2001) (applying the same analysis in interpreting whether Canadian bankruptcy provisions require proceedings to be stayed for a non-bankruptcy co-defendant as the court would use in interpreting the analogous provisions in the Bankruptcy Code). Thus, Northstar has properly referred to federal bankruptcy law for guidance as to the appropriate circumstances under which the stay should be lifted. Those circumstances include situations in which the court must resolve whether the property at issue even comprises part of the insolvent estate – precisely the issue that Northstar seeks to have resolved by lifting the stay to proceed with arbitration of the Termination Issue. *See In re White*, 851 F.2d 170, 174 (6th Cir. 1988) (upholding trial court’s decision to lift bankruptcy stay to allow divorce proceeding to conclude because, “until [the domestic relations court] makes a specific determination of the property rights as between the Debtor and his spouse, what is property of the Debtor’s estate in this cause is unclear, and the reorganization of Debtor’s business cannot proceed in an orderly fashion.”); *In re Paro*, 362 B.R. 419, 427 (Bankr. E.D. Ark. 2007) (lifting stay in order to allow state court to determine whether debtor or third-party had title to certain real estate); *see also In re Stockwell*, 262 B.R. 275, 283

(Bankr. D. Vt. 2001) (retroactively lifting stay to allow foreclosure action pending at the time of bankruptcy to proceed).

17. The SDR claims that “[l]ifting the stay for Northstar would appear to mandate lifting the stay for any reinsurer or other alleged creditor. Northstar makes no effort to distinguish its efforts to seize estate property from any other claimant.” (SDR Response, ¶ 6.7.) As an initial matter, Northstar obviously disagrees that the collateral at issue constitutes “estate property.” Moreover, the SDR’s complaint in this regard is all sound and no substance. All Northstar must demonstrate is that, under the facts pertaining to its own dispute with Lincoln, Northstar is entitled to have the stay lifted to resolve whether the property at issue constitutes property of the estate. And, as discussed in Northstar’s Motion to Lift Stay and herein, Northstar has demonstrated its entitlement to a hearing on that issue. Further, nothing in the material that the SDR has submitted in relation to the two other reinsurance disputes in which Lincoln is engaged suggests that anyone has contended that the reinsurance contracts at issue in those disputes have been terminated or are not property of the estate. Thus, in distinction to the dispute between Northstar and Lincoln, the other reinsurance disputes referenced by the SDR do not implicate the threshold issue of whether the reinsurance contracts, and the collateral relating thereto, constitute “property of the estate” to which the stay applies.

18. Indeed, the fact that the Termination Issue happened to be in front of the arbitration panel at the time that the stay became effective is mere coincidence – and an apparent stroke of luck for Lincoln to the extent that the stay has delayed the resolution of the Termination Issue. Pursuant to §443.008(e)(7) of the Texas Insurance Code, the stay does not apply to “enforcement of rights against single beneficiary trusts established pursuant to and in compliance with laws relating to credit for reinsurance.” The Termination Issue involves the enforcement of Northstar’s right to terminate the trust which was established for the sole benefit of Lincoln in order to permit Lincoln to take credit for the reinsurance provided by Northstar and thus falls

within the exception to the stay set forth in § 443.008(e)(7). Accordingly, Northstar could have pursued resolution of the Termination Issue before this Court, forcing the SDR to bear the burden of demonstrating to the Court why this issue should *not* be resolved at this time.

19. Finally, Northstar will suffer undue hardship if the stay is not lifted in order to determine the threshold issue whether the collateral originally posted under the Reinsurance Agreement even constitutes property of the estate to which the stay is applicable. Indeed, with continued losses and no means of writing new business, Northstar will be forced to wind up its affairs as an ongoing business unless the stay is lifted and the collateral supporting the Agreement is released. (Exh. 1, ¶ 10.) Northstar is a relatively small offshore reinsurer that is allowed by United States insurance regulators to reinsure companies in the United States as long as it places security in the United States for its reinsurance obligations. (*Id.*) With respect to its Agreement with Lincoln, Northstar complied with this requirement by placing \$9.6 million trust assets in a trust located in the United States and by procuring a letter of credit in the amount of \$28.5 million issued by a United States bank. (*Id.*) The Liquidation Order presently ties up these \$38 million in assets even though Northstar has terminated the Agreement. (*Id.*) Further, Agreement comprises a significant part of Northstar's business, with the assets which Northstar has committed as security for the Lincoln treaty obligations representing 12.8% of all regulatory capital which Northstar has committed as security for all of its treaty obligations. (*Id.*) As a practical matter, Dresdner Bank, N.A., the bank that issued the letter of credit for the Agreement, is unwilling to issue any further letters of credit to support any new business for Northstar because of the present unresolved issues concerning the letter of credit on the Lincoln treaty. (*Id.*) Before Lincoln's default, the Agreement with Lincoln was providing 30% of Northstar's revenues. (*Id.*) Because Northstar's revenues have dropped 30% as a result of Lincoln's default, Northstar will have to reduce its staff. (*Id.*) Notwithstanding any reduction in staff, Northstar's expenses will continue to exceed its revenues, and Northstar will continue to sustain

operating losses unless it can find a new revenue source from new business. (*Id.*) However, since it is unable to obtain any further letters of credit as long as the stay is in effect with respect to the LOC for the Lincoln treaty, Northstar cannot contract for any new business to replace the existing Lincoln treaty. (*Id.*) Resolution of the Termination Issue is therefore paramount to Northstar.

B. Northstar’s Dispute with Lincoln Does Not Involve a “Claim Against the Estate.”

20. Building upon the flawed premise that the collateral at issue constitutes “property of the estate” merely because the SDR says so, the SDR further contends that “Northstar needs to file its proof of claim like any creditor of this estate” so that Northstar can “be treated equally with all the other creditors of the estate.” (SDR Response, ¶ 7.1.) As discussed in detail above, these assertions simply assume the threshold issue that Northstar seeks to resolve – whether the collateral at issue constitutes property of the estate. Moreover, the Receivership Act makes clear that a “claim” refers to an action for monetary amounts owed. *See* Texas Insurance Code, Sec. 443.252. With respect to the Termination Issue, Northstar does not seek amounts owed to it by Lincoln. All Northstar seeks is a determination that the Reinsurance Agreement has been properly terminated, that Northstar bears no further liability under the Agreement and that, in the absence of such liability, Northstar has no further security obligations under the Agreement, such that the amounts that Northstar previously posted as security may be released to Northstar. Northstar does not seek payment of past due amounts owed to it by Lincoln. Accordingly, Northstar’s dispute with Lincoln over the Termination Issue does not involve a “claim” against the estate in accordance with the meaning of that term under the Receivership Act, and the SDR’s assertion that Northstar can be lumped in with “other creditors” is simply incorrect.

C. Northstar Has Not Repudiated the Reinsurance Agreement.

21. The SDR argues that Northstar's termination of the Agreement was not valid because Northstar repudiated the Agreement "by February 2, 2008 before the January accounting was even due" by "admit[ting] that it intended to rescind the Agreement *ab initio*." According to the SDR, Northstar's "admission" somehow constituted a repudiation of the Agreement that relieved Lincoln of any of its obligations thereunder. The SDR's argument in this regard is incorrect both as a matter of fact and as a matter of law.

22. Indeed, the SDR offers no evidence for its assertion that Northstar had indicated its intent to seek rescission of the Agreement as of February 2, 2008, nor has Northstar identified any document in which it stated that intent prior to April 21, 2008, when Northstar filed its statement of issues with the arbitration panel. Moreover, the mere fact that Northstar sought relief in the form of rescission of the Agreement does not mean that Northstar "repudiated" the Agreement. Under Texas law, "[t]o repudiate a contract, the repudiating party must positively, unequivocally, and unconditionally refuse to perform the contract prior to the time fixed for performance." *Munoz v. Witt*, 2008 WL 3971683 at *4 (Tex. App.-Waco Aug. 27, 2008); *Walker v. Satchell*, 1988 WL 40476 at * 4 (Tex. App.-Hous. Apr. 28, 1988); *Cooper v. Wildman*, 528 S.W.2d 80, 86 (Tex. App.- Corp. Christi 1975) Far from meeting this standard, Northstar has fully complied with its obligations under the Agreement since it demanded arbitration in November 2007. (Tweedie Aff., ¶ 9.) In fact, as of the end of December 2007, pursuant to Northstar's obligations under Article IV of the Agreement, Northstar increased the amount of the LOC posted as partial security for its obligations under the Agreement from \$25 million to \$28 million in order to ensure that the LOC, along with the trust account that Northstar had established, would equal the full amount of statutory reserves reported by Lincoln. (*Id.*) In other words, Northstar remains in compliance with its obligations under the Agreement – and Northstar will continue to remain in compliance with its obligations under the Agreement until

Northstar's dispute with Lincoln is fully resolved, whether by a finding in Northstar's favor on the Termination Issue or otherwise.

23. The SDR appears to believe that a mere assertion of a right to rescind constitutes "repudiation" of the Agreement. As discussed above, this belief is incorrect as a matter of law. Moreover, none of the cases cited by the SDR for this proposition is apposite. In *Ridge Oil Co. v. Guinn Investments, Inc.*, 148 S.W.3d 143, 157 (Tex. 2004) for example, Guinn alleged that the repudiating party, Ridge, had *ceased complying* with its obligations under an oil and gas lease, and that in doing so, Ridge had prevented Guinn from complying as well. *Id.* at 149. As noted above, Northstar has remained in compliance with its obligations under the Agreement, and nothing prevented Lincoln from doing the same. Further, the defendant in *Ridge* faced *prospective* losses if it continued to perform following repudiation of the contract at issue. Even if one were to accept the SDR's contention that Northstar repudiated the Agreement – which Northstar vehemently denies – Lincoln already owed past due payments to Northstar at that time; compliance with those past due payment obligations did not put Lincoln at risk of wrongfully losing money.

24. The SDR's citation to *McNair v. City of Cedar Park*, 993 F.2d 1217, 1221 (5th Cir. 1993), is also inapt. The SDR cites dicta from a footnote in which the Court stated that the plaintiff's repudiation of a contract precluded the plaintiff from recovering damages for a breach of the contract by the defendant. In contrast, as explained above, Northstar has never unequivocally refused to perform its contractual obligations, but, rather, has continued to perform its obligations under the Agreement. Thus, Northstar has never repudiated the Agreement, and the SDR has no basis for its claim that its performance under the Agreement was excused due to any repudiation by Northstar.

D. The SDR Cannot Demonstrate that Lincoln's Default under the Reinsurance Agreement Resulted from an Error or Omission.

25. In Paragraphs 3.4 and 3.5 of its Response, the SDR claims that the panel would have ground to conclude that Lincoln's failure to pay amounts to Northstar when due was "unintentional" or "caused by misunderstanding or oversight," such that the parties should "adjust the situation to what it would have been had the misunderstanding or oversight not occurred," as contemplated by Paragraph 11 of Article I of the Agreement. The SDR also claims that the fact that the parties were engaged in an arbitration gave rise to a "legitimate 'misunderstanding'" about whether Lincoln was bound to meet its payment obligations "under the time frames imposed by the Agreement that Northstar was alleging was no longer in operation." The SDR, however, offers no evidence in support of this bald assertion. To the contrary, had Lincoln actually believed as of February 2, 2008 that the Agreement was "no longer in operation" such that Lincoln could ignore its obligations thereunder, Lincoln would not have provided Northstar with the February Accounting Statement – which Lincoln did on March 13, 2008. (February Account Statement, attached as Exh. 3.)

26. Further, as discussed above, as of April 2, 2008 – the absolute deadline for payment from Lincoln of amounts due as of January 31, 2008 – Northstar had never alleged that the Agreement "was no longer in operation." The mere fact that Northstar sought rescission as a remedy for Lincoln's fraud and breach of contract does *not* equate to an allegation that the Agreement was no longer in operation. Northstar always recognized that, because of the dispute over the termination, unless and until the tribunal deciding the parties' dispute ruled that the Agreement was no longer in effect, the parties were bound by their obligations thereunder. Thus, as discussed above, Northstar continued to comply with its own contractual obligations, including posting an additional \$2.6 million in collateral after it had demanded arbitration. Lincoln bore that same responsibility to meet its contractual obligations unless and until it had reason not to do so – particularly given Lincoln's position that Northstar's termination of the Agreement is invalid and the Agreement remains in full force and effect.

27. The SDR next argues that because Article VI, ¶ 8 of the Agreement expressly contemplates that payments might be delayed for “multiple accounting periods,” Northstar’s termination of the Agreement must somehow be invalid. The SDR’s conclusion does not follow from its premise. The termination provision set forth in Article VII, Paragraph 3 of the Agreement clearly provides that Northstar *may* terminate the Agreement due to a failure by Lincoln to pay amounts due within sixty days of the end of an accounting period. In other words, termination due to nonpayment by Lincoln was *at Northstar’s option*. There are myriad business reasons why Northstar might have decided *not* to terminate the Agreement despite Lincoln’s failure to pay, and there are myriad business reasons why Northstar might have permitted such a default to span multiple accounting periods. If Northstar had chosen that route, then the “Delayed Payment Rate” contemplated by Article VI, ¶¶ 7 and 8 would apply. Northstar did not choose that route, however. Instead, Northstar decided to terminate the Agreement upon the first default by Lincoln – as Northstar was well within its rights to do.

28. The SDR further argues that because there was a general errors and omissions clause in the Agreement, Lincoln’s failure to pay was excusable, and Northstar’s termination of the Agreement was invalid. (SDR Response, ¶ 3.6.) As with the “legitimate misunderstanding” provision referenced above, the SDR offers no facts that would suggest that Lincoln’s failure to pay the amounts due Northstar resulted from an “inadvertent . . . error or omission” such that Lincoln should be permitted to rectify its failure to pay.

29. Finally, the SDR attempts to argue that Northstar somehow duped Lincoln into failing to pay amounts due to Northstar under the Agreement. To that end, the SDR complains of Northstar’s statements during the organizational meeting on April 28, 2008, the SDR fails to mention that on April 2, 2008 – almost four weeks *prior to* the organizational meeting – Northstar sent Lincoln the termination notice required by Article VII of the Agreement. (Termination Notice, Exh. 4.) That termination notice explicitly stated that Northstar was

“terminating the Agreement pursuant to Article VII paragraph 3 of the Agreement on account of [Lincoln’s] failure to pay amounts due for the January 2008 accounting period within sixty (60) days after the end of said accounting period.” (*Id.*) Further, when it forwarded the termination notice, Northstar went above and beyond its obligations under the Agreement by addressing the termination notice not only to the parties identified in the notice provision of the Agreement, but also to additional individuals with whom Northstar had been discussing its overall dispute with Lincoln including Katherine Scannell, Lincoln’s general counsel.

30. Finally, during a meeting between the parties on the same day as and immediately following the organizational meeting, Northstar explicitly advised Lincoln’s attorney, Doug Schmidt, that Lincoln had failed to make any payments to Northstar for January, February or March.

31. Thus, the SDR’s claims that Northstar somehow failed to notify Lincoln of its default under the Agreement ring exceedingly hollow. To the contrary, Northstar went above and beyond its contractual notice obligations in providing the termination notice, and explicitly informed Lincoln of its continued default on the day of the organizational meeting. The SDR has provided no evidence even suggesting that Lincoln’s default was somehow inadvertent or unintentional. Indeed, in light of the fact that Northstar and Lincoln were engaged in a dispute beginning in November 2007, with arbitration-related matters being discussed up and until Lincoln’s insolvency was announced, it is much more likely Lincoln was focused on its Reinsurance Agreement with Northstar, and affirmatively chose, for whatever reason, not to comply with its obligations thereunder.

E. Northstar Has Provided Clear and Convincing Evidence in Favor of Lifting the Stay.

32. The SDR further contends that Northstar cannot establish its entitlement to lift the stay by “clear and convincing evidence,” as required by § 443.008(j) of the Receivership Act

(SDR Response, ¶ 4.6.) The SDR is incorrect. “‘Clear and convincing’ means the measure or degree of proof that will produce in the mind of the trier of fact a firm belief or conviction as to the truth of the allegations sought to be established.” Tex. Civ. Prac. & Rem. Code § 41.001(2) (Vernon Supp. 2007). While this particular burden is higher than the “preponderance of the evidence” standard, “there is no requirement that the evidence be unequivocal or undisputed.” *State v. Addington*, 588 S.W.2d 569, 570 (Tex. 1979); *State ex. rel. T.H.*, 194 S.W.3d 82, 85 (Tex. App.- El Paso 2006). The Termination Issue involves a very simple inquiry – whether Northstar’s termination of its Reinsurance Agreement with Lincoln met the contractual requirements for termination. Northstar has provided sufficient evidence to this Court that Northstar did indeed meet the contractual requirements for termination: (1) as of January 31, 2008, by Lincoln’s own calculation, Lincoln owed Northstar \$846,000; (Exh. 1, ¶ 5); (2) Lincoln failed to pay that \$846,000 by April 2, 2008, sixty days after the end of the accounting period for which the funds were due; (*Id.*, ¶ 6); (3) on April 2, 2008, sixty days after the funds were due, Northstar provided Lincoln with the contractually-required notice of termination (*Id.*) and (4) by its express terms, the Agreement then terminated as of May 2, 2008 (Exh. A to Northstar’s Motion to Lift Stay, Art. VI, Art. VII, ¶ 4). Those simple facts in and of themselves suffice to provide a firm belief or conviction of the truth of Northstar’s allegation that Northstar validly terminated the Agreement. The fact that the SDR may dispute the effect of the termination notice by raising defenses does not change the fact that Northstar has met its burden.

33. In making its argument regarding the need to provide “clear and convincing evidence,” the SDR misleadingly cites the dissent in *Columbia Medical Center of Las Colinas, Inc. v. Hogue*, No. 04-0575, 2008 WL 3991190 at *21-22 (Tex. Aug. 29, 2008), a medical malpractice case. The SDR. *See id.* at *21-22 (“Because the Court fails [to find that clear and convincing evidence did not support a finding of gross negligence], I dissent.”). The actual holding of *Hogue* was that the evidence *was* sufficient to support a “firm belief or conviction”

that the hospital was grossly negligent. *Id.* at *1, *12. Further, *Hogue* involves the application of the clear and convincing evidence standard to a medical malpractice action of gross negligence, an action that necessarily requires a more intensive factual inquiry than the straightforward factual inquiry necessary to determine whether Northstar's termination of its Reinsurance Agreement with Lincoln complied with the contractual requirements therefore, discussed above.

34. The affidavit supplied by the SDR does not somehow negate the fact that Northstar has provided "clear and convincing evidence" of the truth of its allegations. As noted above, evidence need not be undisputed in order to be clear and convincing. Moreover, it is questionable whether the affidavit filed by the SDR even meets the applicable standards for an affidavit under Texas law. Texas Rules of Civil Procedure require affidavits in a summary judgment context to "be made on personal knowledge" setting forth "such facts as would be admissible in evidence" and showing "affirmatively that the affiant is competent to testify to the matters stated therein." Tex. R. Civ. P. 166a(f). The SDR has no personal knowledge of the factual issues giving rise to the termination. In fact, the SDR did not become involved until Lincoln was placed into rehabilitation on May 13, 2008. All of the events that resulted in the termination of the Agreement took place well before that date, with the thirty-day notice of termination being sent to Lincoln on April 2, 2008.

35. Furthermore, the SDR's affidavit contains nothing more than the conclusory, self-serving statement that the SDR "read the attached Response and the statements contained therein are true and correct." (SDR Response, Exh. C.) Both state and federal courts in Texas have held that conclusory allegations contained in affidavits are insufficient to avoid summary judgment. *Dimon v. Trendmaker, Inc.*, No. 14-96-01081-CV, at *6 (Tex. Ct. App. 1998) (stating that "[i]t is well settled that conclusory statements in an affidavit unsupported by facts are insufficient to support or defeat summary judgment" but ultimately finding that the affidavit in question sufficiently raised a question of fact); *Travelers Ins. Co. v. Liljeberg Enterprises, Inc.*, 7

F.3d 1203, 1207 (5th Cir. 1993) (stating that in opposing summary judgment, a party must produce affidavits that set out specific facts showing a trial issue); *In re Absolute Resource Corp.*, 76 F. Supp. 2d 723, 732 n. 5 (N.D. Tex. 1999) (same); *Martinez v. Lenno Int'l, Inc.*, No. CIV. A. 3:96-CV-0702, 1997 WL 209306, at *6 (N.D. Tex. Apr. 18, 1997) (same); *Tanner v. Academy Tankers Inc.*, 898 F. Supp. 421, 426 (E.D. Tex. 1995) (“A nonmovant’s conclusory allegations supported by a conclusory affidavit are insufficient to avoid summary judgment.”).

36. Thus, the affidavit filed by the SDR does not overcome the clear and convincing evidence of termination that has been proffered by Northstar in support of its Motion to Lift Stay.


III. CONCLUSION

37. For all of the foregoing reasons, this Court should grant Northstar’s Motion to Lift Stay for the purpose of arbitrating the Termination Issue.

Dated: November 17, 2008

Respectfully submitted,

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REINSURANCE IRELAND LIMITED**



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I hereby certify that a true and correct copy of the foregoing has been served via electronic transmission in accordance with the Texas Rules of Civil Procedure on this the 17th day of November, 2008, to the following counsel:

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THE STATE OF TEXAS	§	IN THE DISTRICT COURT OF
	§	
v.	§	
	§	
MEMORIAL SERVICE LIFE	§	TRAVIS COUNTY, TEXAS
INSURANCE COMPANY, LINCOLN	§	
MEMORIAL LIFE INSURANCE	§	
COMPANY, AND NATIONAL	§	
PREARRANGED SERVICES, INC.	§	250 TH JUDICIAL DISTRICT

ORDER GRANTING NORTHSTAR REINSURANCE IRELAND LIMITED'S MOTION TO LIFT STAY

On the undersigned day, the Court considered the Motion to Lift Stay filed by Northstar Reinsurance Ireland Limited (“Northstar”), the Response in Opposition to Motion to Lift Stay by Northstar Reinsurance Ireland Limited, filed by Donna Garrett, Special Deputy Receiver of Memorial Service Life Insurance Company, Lincoln Memorial Life Insurance Company (“Lincoln”) and National Prearranged Services, Inc, and the Reply in Support of Motion to Lift Stay filed by Northstar. Having considered the foregoing documents and the recommendation of the Special Master appointed in this proceeding, the Court finds that the Motion to Lift stay should be granted for the purpose of allowing the underlying arbitration panel to decide whether the Reinsurance Agreement between Northstar and Lincoln has terminated and whether the letter of credit and trust account posted by Northstar thereunder should be released.

IT IS THEREFORE ORDERED, ADJUDGED, and DECREED that Northstar Reinsurance Ireland Limited’s Motion to Lift Stay is GRANTED.

SO ORDERED this ___ day of _____, 2009.

JUDGE PRESIDING