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Vermont Superior Court
Washington Unit
21-CV-00406

STATE OF VERMONT
WASHINGTON COUNTY, SS

COMMISSIONER OF THE DEPARTMENT OF FINANCIAL REGULATION PLAINTIFF, v. HOSPITALITY RISK RETENTION GROUP, INC., RESPONDENT.	SUPERIOR COURT DOCKET NO. 21-CV-0406

MOTION FOR AN ORDER APPROVING THE FIRST CLAIM REPORT AND AUTHORIZING INTERIM DISTRIBUTIONS ON ALLOWED PRIORITY CLASS 3 CLAIMS

Michael S. Pieciak, Commissioner of the Vermont Department of Financial Regulation (“Commissioner”) in his capacity as Liquidator (“Liquidator”) of Hospitality Risk Retention Group, Inc. (“Hospitality” or the “Company”), hereby submits this Motion for an Order Approving the First Claim Report and Authorizing Interim Distributions on Allowed Priority Class 3 Claims (“Motion”) requesting that the Court enter an order approving the First Claim Report and authorizing a 10% distribution on allowed priority class 3.

1. On March 1, 2021, the Commissioner filed an Assented-To Petition for Order of Liquidation for Hospitality (“Petition”). The Petition noted Hospitality’s insolvency, proposed a Plan of Liquidation, and reported that management had assented to entry of an order of liquidation. The Court approved the Plan of Liquidation pursuant to the Order of Liquidation entered on April 8, 2021. The Plan of Liquidation requires that the Liquidator “monitor Hospitality’s financial condition, and as circumstances warrant, petition the Court to establish a

distribution percentage for making interim payments on finally determined claims in priority class 3." See id., at ¶ 2.e.

2. The Liquidator believes that Hospitality's financial condition and the circumstances of the proceeding warrant an interim distribution on allowed priority class 3 claims. The Liquidator therefore requests that a 10% distribution percentage be established for priority class 3 and that he be authorized to make an interim distribution at that rate on allowed priority class 3 claims.

Background

3. Hospitality was organized to provide commercial automobile liability insurance to franchisees of Domino's Pizza, Inc. ("Domino's"). Ultimately, it was determined that liability coverage afforded by a risk retention group did not satisfy the insurance requirements established by Domino's. The Company accordingly ceased writing business and by March 31, 2019 had no in-force business and entered run-off. The Company afforded coverage with relatively high limits (up to $5 million per incident) and presently has no reinsurance for covered losses. Following review of loss reserve reports from the Company's consulting actuaries that were calculated as of December 31, 2020, the Commissioner determined that Hospitality was insolvent and filed the Petition. See Liquidator's Second Status Report, Annual Accounting, and First Report of Claims, ¶ 12. (hereinafter, "Second Status Report, ¶ __").

4. When the Court entered the Order of Liquidation, the Liquidator sent notice of the proceeding and instructions for filing proofs of claim ("POCs") to those individuals and entities suspected to be creditors of the Company or otherwise entitled to receive such notice. The notice advised that the Liquidator had established a claim filing deadline of October 8, 2021 (six months from entry of the Order of Liquidation). See Second Status Report, ¶¶ 1 and 2.

5. As of March 31, 2022, the Liquidator had received and acknowledged a total of 31 completed POCs. These POCs present 63 claims relating to 32 separate incidents. (A POC form may present a single claim or include a schedule of multiple claims and a single auto accident may give rise to claims by multiple individuals and entities including insureds, third-party claimants, other carriers, vendors, etc…). The Liquidator has reviewed these claims and made preliminary judgments as to the priority class in which they are likely to fall. On this basis, it appears that there may be 47 claims asserting obligations with the potential of falling in priority class 3 and 12 claims with the potential of falling in priority class 6. See 8 V.S.A. § 7081 (defining priority classes). See Second Status Report, ¶¶ 5-9.

Interim Distribution Analysis

6. Hospitality's insolvency has imposed a significant economic burden on its Class 3 creditors due to the fact that a defense of claims is no longer being afforded and the insureds must pay amounts in the first instance to resolve claims against them that would otherwise have been funded by Hospitality. This burden can be reduced if the Liquidator is able to accelerate the disbursement of funds through the mechanism of an interim distribution. Accordingly, the Plan of Liquidation requires that the Liquidator monitor Hospitality's financial condition, and as circumstances warrant, petition the Court to establish a distribution percentage for making interim payments on finally determined claims in priority class 3. Id., ¶ 2.e; see Second Status Report, ¶ 13.

7. An interim distribution may be ordered if it can be accomplished "in a manner that will assure the proper recognition of priorities and a reasonable balance between the expeditious completion of the liquidation and the protection of unliquidated and undetermined claims." 8 V.S.A. § 7083; see 8 V.S.A. § 7081 (with regard to priorities, "[e]very claim in each

class shall be paid in full or adequate funds retained for such payment before the members of the next class receive any payment."). The analytical steps in considering the possibility of an interim distribution on allowed priority class 3 claims are therefore to ascertain the assets of the insolvent insurer, reserve funds for the payment of claims falling in higher priority classes, and establish a distribution percentage that reasonably balances the interest of creditors with allowed claims and the interests of creditors with unliquidated/undetermined claims.

8. *Estate Assets*. In analyzing whether the Liquidator may distribute estate assets to creditors it is necessary to ascertain the value of all estate assets. In this proceeding, that process is straightforward since the Company has no in-force reinsurance or material receivables. The only significant estate assets, therefore, are cash and invested assets. As of March 31, 2022, these totaled $3,849,319. See Exhibit A to the Second Status Report (Simplified Balance Sheet as of March 31, 2022).

9. *Claims in Higher Priority Classes.* By statute, the "costs and expenses of administration" fall in priority class 1. See 8 V.S.A. § 7081(1). The Liquidator estimates that a $500,000 reserve should be sufficient for administrative expense in this proceeding and has therefore established a $500,000 reserve.[1] Risk retention groups such as Hospitality are prohibited by federal statute from participating in the guaranty fund system so priority class 2 – the administrative expenses of guaranty associations – will be empty in this proceeding. See 8 V.S.A. § 7081(2); see also 15 U.S.C.A. § 3902(a) (risk retention groups excluded from guaranty fund system) and 8 V.S.A. § 6054(a) (conforming to federal law). The Liquidator

[1] Because of the statutory mandate to "assure the proper recognition of priorities", this $500,000 reserve is intended to be conservative. See 8 V.S.A. § 7083. Any funds not needed for the payment of administrative expense will be released at the close of the proceeding and become available to pay claims falling in priority class 3.

therefore projects that the Hospitality estate has $3.35 million available to pay claims falling in priority class 3. See Second Status Report, ¶ 14.

10. *Claims Falling in Priority Class 3.* The liquidation statutes require that, where there are insufficient funds to ensure that all claims within a priority class are paid in full, the Liquidator balance the interests of creditors with allowed claims (who benefit from accelerated distribution) and the interest of creditors with unliquidated/undetermined claims (who benefit from the reservation of assets to satisfy their claims). See 8 V.S.A. § 7083; see also 8 V.S.A. § 7081 (prohibiting the establishment of subclasses). This can be done by establishing a conservative interim distribution percentage that ensures the estate will retain sufficient assets to make equal distribution to all creditors with priority class 3 claims as their claims are determined and allowed. It is therefore necessary to estimate the likely total value of claims falling in priority class 3:

a. Allowed Claims. The Liquidator is charged with reviewing all claims filed in the liquidation, making such investigation as he deems necessary, and issuing a determination as to whether the claim should be denied or approved. For approved claims, the determination will also identify an amount and priority classification. "Within 60 days from the mailing of the notice [of determination], the claimant may file objections with the liquidator" and "[i]f no such filing is made the claimant may not further object to the determination." 8 V.S.A. § 7078(a). After the 60-day period has run (or been waived) the claim is deemed to be "finally determined" and the Liquidator will report it to the Court with his recommendations. See 8 V.S.A. § 7082(a). The Court may then approve, disapprove, or modify the Liquidator's report. 8 V.S.A. § 7082(b). The Liquidator has now issued 7 notices that have become "finally determined". The

Liquidator has filed a report recommending the priority class and amount in which such claims should be allowed. If the Court approves that report, there will be 7 allowed priority class 3 claims totaling $9,560,001. See Second Status Report, ¶¶ 11 and 15; Exhibit B to the Second Status Report (Liquidator's First Report of Claims).

b. Open Claims. In addition to the 7 "finally determined" claims, there are 40 priority class 3 claims that have not yet been determined. For some of these claims, the Liquidator has high confidence regarding their ultimate value because the underlying liabilities have been settled or adjudicated. Accordingly, while these claims remain "open", all that remains to be determined are defense expenses or matters that will not have large impacts on total claim value. For other claims, however, there is significant uncertainty as to the insured's liability, the amount of damages, or the existence of coverage. Given the high policy coverage limits applicable to certain of these claims ($1.5 million to $5 million per occurrence), this means that there could be a wide range of potential outcomes. The Liquidator has therefore evaluated the value of "open claims" falling in priority class 3 in two ways. First, the Liquidator has reviewed the available claim/coverage information and estimated the most likely value in which the claim might be allowed. Viewed on this "best estimate" basis, the Liquidator projects that the ultimate value of the "open" priority class 3 claims may total $5.24 million. Second, the Liquidator has evaluated the "open" claims in terms of a "pessimistic scenario" which reflects the adverse end of the expected range of values for each claim. Viewed on this "pessimistic scenario" basis, the Liquidator projects the ultimate value of the "open" priority class 3 claims may total $16.94 million. See Second Status Report, ¶ 15.

c. Total for Priority Class 3. In balancing the interests of creditors with allowed claims and the interest of creditors with unliquidated/undetermined claims, the Liquidator believes it will be appropriate to use conservative estimates of claim values. Specifically, the risks associated with using a conservative estimate is moderate (e.g. in retrospect, it will be apparent that the interim distribution could have been larger such that funds could have been distributed more quickly) while the risks associated with using a more optimistic estimate are very significant (e.g. there will be insufficient funds to make equal distributions to all creditors with allowed priority class 3 claims and it might be necessary to institute claw-back proceedings seeking recovery of excess funds from some creditors). The Liquidator therefore propose to use the "pessimistic scenario" estimate of "open claims" to calculate that the ultimate value of claims in priority class 3 will be \$26.5 million.[2] See Second Status Report, ¶ 16.

Using a \$26.5 million estimate for the value of claims falling in priority class 3 suggests that estate assets will be sufficient to permit a 12.6% distribution at the close of the proceeding.[3] Using these figures and providing a cushion against adverse development, the Liquidator has concluded that Hospitality's financial condition and the circumstances of the proceeding warrant establishment of a 10% interim distribution on allowed priority class 3 claims. See Second Status Report, ¶ 17.

11. The Liquidator has reviewed and approved the claims in the amount and priority class set forth on Exhibit B to the Liquidator's Second Status Report, Annual Accounting, and

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[2] Claims for which the Liquidator has recommended allowance (\$9.56 million) plus the \$16.94 million value of "open" claims under the "pessimistic scenario" equals \$26.5 million.

[3] In contrast, using the Liquidator's "best estimate" of open claim values (\$5.24 million) would suggest \$14.8 million in priority class 3 claims and an ultimate distribution of 22.7%.

First Report of Claims and requests that the Court issue and order approving those determinations. See, Second Status Report, ¶ 11 and Exhibit B.

WHEREFORE, the Liquidator requests that the Court enter an order:

(a) Granting this Motion for an Order Approving the First Claim Report and Authorizing Interim Distributions on Allowed Priority Class 3;

(b) Approving the claim determinations set forth on Exhibit B of the Liquidator's Second Status Report, Annual Accounting, and First Report of Claims;

(c) Establishing a 10% interim distribution rate on allowed priority class 3 claims;

(d) Authorizing the Liquidator to make an interim distribution at the 10% rate on all allowed priority class 3 claims; and,

(e) Granting such other and further relief as justice may require.

Dated in Montpelier, Vermont, this 19th day of April, 2022.

MICHAEL S. PIECIAK, COMMISSIONER
DEPARTMENT OF FINANCIAL REGULATION
AS LIQUIDATOR OF HOSPITALITY RISK
RETENTION GROUP, INC.

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