EXHIBIT 16

In the Matter of:

PHH Corporation, et al.

March 12, 2014
Michael Cascio

Condensed Transcript with Word Index

For The Record, Inc.
(301) 870-8025 - www.ftrinc.net - (800) 921-5555

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BY MR. VAZIRE:
Q. Do you recognize this amendment?
A. I do.
Q. What is it?
A. I'd have to read it because I don't recall exactly what it says, but it -- it's not -- it doesn't address the issue we were just discussing.
Q. Okay. But it's the tenth amendment to the UGI-Atrium contract; do you agree?
A. Correct.
Q. And you said it does not address the issue we were talking about?
A. As I quick read, I didn't see it. I didn't see a reference to that.
Q. Okay. Did Genworth benefit from Atrium's or PHH's expertise through the amendments to that agreement?
A. I don't remember those amendments, so I don't know.
Q. Okay.
A. Yeah.
MR. VAZIRE: Let's mark this as the next exhibit.
(Enforcement Deposition Exhibit Number 10, Reinsurance Agreement between General Electric Mortgage Insurance Corporation and Atrium Insurance Corporation, was marked for identification.)

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BY MR. VAZIRE:
Q. Do you recognize this document?
A. I recognize the cover page.
(Pause in the proceedings.)
I do, yes.
Q. What is it?
A. Exhibit Number 10 is the reinsurance agreement, dated October 9, 2000, of General Electric Mortgage Insurance Corporation.
Q. Is that Genworth?
A. Genworth, yes. I think we both were referring to it as Genworth, the Genworth contract.
Q. Okay.
A. And Atrium as the reinsurer.
Q. And no amendments are attached to this document; is that right?
A. That is correct.
Q. Okay.
This will be the next exhibit.
(Enforcement Deposition Exhibit Number 11, First Amendment to Reinsurance Agreement between General Electric Mortgage Insurance Corporation and Atrium Insurance Corporation, was marked for identification.)
BY MR. VAZIRE:
Q. Do you recognize this document?

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A. Yes. I have seen this before.
Q. Does it contain any provision that demonstrates Genworth using Atrium's expertise?
(Pause in the proceedings.)
Protective Order
[redacted]
exhibit.
(Enforcement Deposition Exhibit Number 12, Second Amendment to Reinsurance Agreement between

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General Electric Mortgage Insurance Corporation and Atrium Insurance Corporation, was marked for identification.)
BY MR. VAZIRE:
Q. Do you recognize this document?
A. Well, it doesn't say "second amendment." That would help. Is this the second amendment?
Q. You're right, it doesn't.
If you look at the Bates number in the bottom right that says "CONFIDENTIAL PHH BOGANSKY CFPB 019896," if you look at the updated Attachment B I gave you earlier -- and I'm sorry. I don't know what exhibit number that was. Maybe 2 -- no. It was 4. I'm sorry. It was 4.
A. 1, 2, 3 -- oh, there it is, 4.
Q. If you look at item 3, it says "the second amendment" and then it gives a Bates number?
A. Oh, they match. Yes. Okay.
Q. So this is the second amendment; right?
A. Perfect.
Protective Order
[redacted]
MR. VAZIRE: Let's mark this as the next exhibit.

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(Enforcement Deposition Exhibit Number 13, Third Amendment to Reinsurance Agreement between General Electric Mortgage Insurance Corporation and Atrium Insurance Corporation, was marked for identification.)

BY MR. VAZIRE:

Q. Do you recognize this document?

A. Yes.

Q. What is it?

A. This is the third amendment to the reinsurance agreement between Atrium and Genworth.

Protective Order

[redacted]

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Protective Order

[redacted]

the next exhibit number.

(Enforcement Deposition Exhibit Number 14, Fourth Amendment to Reinsurance Agreement between General Electric Mortgage Insurance Corporation and Atrium Insurance Corporation, was marked for identification.)

BY MR. VAZIRE:

Q. Do you recognize this document?

A. I do.

Q. What is it?

A. This is the fourth amendment to the reinsurance

Protective Order

[redacted]

MR. VAZIRE: This will be the next exhibit.

(Enforcement Deposition Exhibit Number 15, Fifth Amendment to Reinsurance Agreement between

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General Electric Mortgage Insurance Corporation and Atrium Insurance Corporation, was marked for identification.)

BY MR. VAZIRE:

Q. Do you recognize this document?

A. I do.

Q. What is it?

A. This is the fifth amendment to reinsurance between Genworth and Atrium.

Protective Order

[redacted]

Q. Did UGI or Genworth ever put out a request for proposal requesting Atrium's expertise?

(Telephone interruption.)

A. I apologize for that. I thought it was off. I'm sorry.

Q. That's okay. I'll just ask the question again.

A. Sorry.

Q. Did UGI or Genworth ever put out a request for proposal requesting Atrium's expertise?

MR. SOUDERS: Object to the form of the question.

THE WITNESS: Not that I'm aware of.

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BY MR. VAZIRE:

Q. Can an insurance company obtain a reinsurer's expertise even if the reinsurance arrangement does not involve risk transfer?

A. Theoretically, yes.

Q. Let's move on to paragraph D, which starts at the bottom of page 3 of your report.

You already explained what a 4/10/40 structure is; right?

A. Yes.

Q. And that's the same thing as what you discuss in the first few sentences or in the first sentence at least here at the bottom of page 3 with the 10 percent XS 4 percent for 40 percent?

A. Yes.

Q. Okay. Does -- I'm going to refer to this, as you did before, as a 4/10/40 structure if that's okay with you?

A. Yes.

Q. Okay. Does a 4/10/40 structure always involve risk transfer?

MR. SOUDERS: Object to the form of the question.

THE WITNESS: It is certainly possible for there to be a reinsurance between two entities which

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portfolio, so I just wanted to be clear that that's what we're talking about. It's those loans that are only for where the LTVs are not equal to 80 percent. They're higher than 80 percent.
I think we're on the same page.
Q. Okay. But I just want to make sure that we're clear about what we mean by a lot loss of 10 percent or a loss of 14 percent. You said that the ground-up losses had to reach 14 percent.
A. Correct.
Q. And 14 percent is -- means that the losses are or amount to 14 percent of the size of the total book of reinsurance; is that --
A. The total book. It's the total book, yes, yes, yes. We could get better wording if we want it right from here, but it's probably not necessary for our purposes (indicating).
Q. I'm sorry?
A. From the contract wording, if we wanted to get real exact wording when we talk about the 4, the 10 and the 14 --
Q. As long as the --
A. I think we're on the same page.
Q. -- the statements are clear that we're talking about what the 10 percent refers to, then I'm

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satisfied.
A. Okay.
Q. Okay. So again, that statement starts with "when the reinsurer suffers a full limit loss of 10 percent"; right?
A. Correct.
Q. How likely is that to occur at the time of the inception of the book?
A. What's the probability in book year one?
I don't know that probability. I think it's higher than 10 percent.
Q. There's -- so in your opinion, there's a more than 10 percent chance that the losses will be more than 14 percent of the aggregate risk?
A. In book year one. Yes.
Q. In any given book year.
A. In any given book year, yes.
Q. And what is that opinion based on?
A. When you do a priori projections, you're really not supposed to, to be fair, use the benefit of hindsight or actual loss experience.
That said, there are roughly nine book years between UGI -- and we could go back and check the Milliman report to make sure it's accurate, but nine is right within one -- nine book years where there was

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projected to be a full limit loss, and a full limit loss I'm defining as a ground-up loss of 14 percent or more, for between seven and nine, say, book years and the total number of book years, you know, roughly 15 for UGC and say 8 to 10, say 25 just to do round numbers.
So if you have roughly -- even let's take the lower number -- seven full limit book year losses per -- out of 25, seven out of -- that's a 28 percent chance of the thing being hit, based on actual experience.
And again, I really want to caveat the fact that you really can't say -- you can't -- you can't say because we experienced 28 percent that that's the right number. That would be -- any actuary would tell you that's not correct.
Q. Okay.
A. But it's what we observed.
Q. So what was the probability at the beginning, before the benefit of hindsight existed, that a full limit loss would be experienced on a book year?
A. I would sit here today and say it's well north. The fact that we saw 28 percent with actual history, roughly, well north of 10 percent. I can't believe -- when you go from 28 down to 10, that's almost a third, a third to bring it down. I would have a hard time saying it's less than 10 percent being --

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Q. For -- are you talking about a book that would be written today?
A. Any book year.
Q. Any book year.
So even in 1997, the a priori likelihood of a full limit loss was more than 10 percent?
A. I would say that, yes.
Protective Order
[redacted]
Q. Okay.
A. Per Milliman. I'm relying on Milliman here. I actually didn't do the numbers. I'm reading the reports.
Q. What if the aggregate losses -- actually, let me step back. Let me go back to the report.
You say that when the aggregate -- when there's a full limit loss, then the total loss in the aggregate needs to be 25 percent for the loss ratios to be

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you would have 4 percent in one and .02 percent in the other, there's just -- when you start dividing, there's too much variability or error that would enter into that.

So it works well as long as you have decent amount of numbers in there, but if the number gets to be less than 1 percent, your proportions will be skewed because of the truncation of the numbers.

But that's something your consulting actuary can easily do also.

Q. Okay.

A. Okay? I apologize for the longevity of that, of that answer.

Q. No. Thank you.

Moving on to subparagraph (c) on page 5, you say, in the second sentence, "I also believe, based on the above, that Atrium was in a more tenuous position than UGI or Genworth."

When you say "based on the above," are you referring to the need for the aggregate loss to be 25 percent in order for the loss ratios to be equivalent?

A. That's -- that's what that's referring to. That's correct.

Q. Okay. What do you mean, Atrium was in a more

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tenuous position than UGI and Genworth?

A. Meaning that they were -- they were suffering -- they were suffering more severe losses virtually every time things went badly.

Q. And how do you know that?

A. Again, from -- from what I have here (indicating). I'll put together a better exhibit that actually lays it out nicely.

Q. Okay. So again, this would be hindsight then.

A. Absolutely. And I think that's important. Right. I'm looking -- I'm looking back. I'm just looking at actually what developed, and that's -- and that's important, and that's a good clarification.

Q. Okay. And that statement is based on the fact that the actual experience showed that in some book years there were full limit losses to Atrium.

A. Correct. It was -- it was very -- it depends upon how you distribute IBNR by book year, but it virtually never happened that it blew through

Protective Order

[redacted]

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Protective Order

[redacted]

Q. The next sentence says, "The actual ultimate loss ratios for all book years illustrate this point emphatically, as the Atrium estimated ultimate loss ratio is significantly higher than the ceding company's retained loss ratio."

What does that mean?

A. I lost you. I'm sorry.

Q. I'm just reading from --

A. Yeah. Where on the page are you? Page 5?

Q. Yeah, still page 5.

A. Paragraph (c).

Q. Paragraph (c).

A. Okay. What that means is if you -- again, you have to do a lot of math from the reports. But if you were to look at the -- in the aggregate, which probably isn't the right way -- I'll be right up front with

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Q. So you say, "The various issues related to any trust agreement include," and then there's a list A through J.
Does that mean that the things that are listed as A through J are the only things relevant to a trust agreement?
MR. SOUDERS: Objection to the form.
MR. VAZIRE: I'll just note that the witness used the word "things," so I'm just repeating your word.
MR. SOUDERS: Well, let me just say for the record, it speaks for itself. The issues related include, for example, so let's just make sure we're clear on the record.
MR. VAZIRE: Okay. And I'm asking if there's anything else.
MR. SOUDERS: Let me finish my objection. Okay? If you're going to read it, you're going to read the whole thing.
Thank you.
THE WITNESS: The list here, you know, there may are other items. Sitting here at this time of the day, I can't think of other items to be considered.
The -- the big -- the big items for a trust, as I stated earlier, would be the amount, which would

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cover at a minimum the unearned premium and the unpaid losses, and the quality of those assets has to be in conformity to something called a 114 trust, which essentially refers to a New York statute numbered 114. It really just talks about the quality of the assets that make it, you know, a viable trust per state insurance law.
BY MR. VAZIRE:
Q. How do you know that the provisions contained in the trust agreements are standard provisions?
A. I've done quite a few trusts. You know, in my time as a Bermuda reinsurer, we -- because we were not admitted as a -- so trusts and letter of credits were really just a way of business, so I -- I've done literally hundreds of these, so I'm fairly familiar with trust arrangements.
Q. Okay. Are the provisions of the reinsurance agreement standard provisions?
MR. SOUDERS: Objection to the form.
THE WITNESS: As related to the trust are you referring to or just in general?
BY MR. VAZIRE:
Q. So now I'm talking about the reinsurance agreements, not the trust agreements.
A. Okay. I'm sorry.

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Q. Are the provisions of the reinsurance agreements standard provisions?
A. You have to be a little careful when you start to use the word like a standard provision. There was -- as I read the reinsurance agreements, there -- I didn't see anything in there that gave me reason to pause as something that I thought was out of the ordinary.
Q. Did Atrium comply with all of the provisions of the UGI reinsurance agreement?
A. I don't know that.
Q. Did Atrium comply with all the provisions of the UGI trust agreement?
A. I don't know.
Q. And did Atrium comply with all the provisions of the Genworth reinsurance agreement?
A. I don't know.
Q. Did Atrium comply with all the provisions of the Genworth trust agreement?
A. I don't know.
I will say that I've seen no evidence to suggest that there was noncompliance on any of those questions. That's not answering your question specifically, though.
Q. Moving on to paragraph 8, what do you mean by

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"The premiums received by the reinsurer for that policy year become the funds or assets of the reinsurer"?
A. What I mean is, when an insurer wants to provide protection for an exposure that they've assumed and at least a portion of that exposure is transferred to the reinsurer in exchange for a reinsurance premium, those premiums are not notionally the money of the insurer anymore because they purchased a product. That's what I mean by that.
Q. Okay. And is that statement true of Atrium?
A. Meaning?
Q. Meaning, are the premiums received by Atrium for that policy year the funds or assets of Atrium?
A. They are. You have to be a little careful because some of the premiums would be unearned, so an unearned premium wouldn't be an asset. It would only be an asset of them when it becomes earned. But generally, yes. I'm nitpicking a little bit.
Protective Order
[redacted]

Q. Were the premiums that had to be earmarked into trusts the funds or assets of Atrium?
A. I don't know how to -- I don't know.
Q. Why don't you know?
MR. SOUDERS: Objection to the form.
THE WITNESS: I just -- I don't know who -- if, you know, when something is in a trust, does it prolong to the insured or the insurer or the reinsurer? That's not a question I've ever contemplated.
BY MR. VAZIRE:
Q. Do the premiums that are in the trust qualify under the statement in paragraph 8 that the premiums received by the reinsurer become the funds or assets of the reinsurer?
MR. SOUDERS: Objection. Asked and answered.
THE WITNESS: Sorry. Which sentence in paragraph 8 are you referring to?
MR. VAZIRE: The second one.
MR. SOUDERS: (Counsel indicating.)
THE WITNESS: For that policy year become the funds or assets of the reinsurer. When earned. When earned. When earned.
BY MR. VAZIRE:
Q. Okay. Even if they had to be earmarked in the trust.

A. Yeah, there, I'm not sure.
Q. If Atrium and UGI had decided to end their arrangement after the first book year and put it into runoff, when would Atrium have stopped being liable for any claims?
A. I think that would depend upon the arrangement the two of them came to.
Are you asking if it just went to fruition?
Q. Yes.
A. Then close to ten years.
Q. Okay. And what would have happened to the funds in the trust at the end of that time?
A. I think that would be a function of what the experience was over that period of time.
Q. Whatever was left at the end of that period, what would have happened to those --
A. So it was completely done?
Without going back and reading the trust, I would have -- I would have expected that the reinsurer could retain that, those monies.
Q. At that time, would those be the funds or assets of Atrium?
A. Yes.
Q. What about the contingency reserve? What would happen to that at the end of the ten years?

A. I'd have to go back and look at the contract. I don't know.
I would have said there's probably no contingency reserve relative to the hypothetical we just talked about.
Q. Why not?
A. I thought we had said at the end of ten years everything was settled. Is that not -- wasn't that the hypothetical?
Q. The hypothetical was just that they only did one year of business, and I'm asking you what would happen at the end.
A. At the end of ten years, it should be completely run off. I didn't see any evidence in anything that I read that would suggest that the runoff period was longer than ten years, so in that case, there should be no liability at all.
Q. And what would happen to the funds in the contingency reserve at the end of ten years?
A. Well, the contingency reserve I would have thought as time went on would have -- when you set up a contingency reserve, it's a -- it's a function of the underlying liabilities, so as time goes on, as the contract runs off, the potential liabilities are also declining, so the contingency reserve at the end of ten

years probably wouldn't -- it would probably be zero I would guess. I don't see a reason why there would be a contingency reserve at that point.
Q. What is a contingency reserve?
A. What it is, it's an amount of money set aside. It acts as a smoothing mechanism, but it's essentially there as a buffer in the event, you know, the loss experience develops as such that is a little worse than expected.
Q. And what is it?
A. It's a pot of money.
Q. How does one compute what goes into that pot?
A. It's formulamatic, but I couldn't tell you the formula.
Q. In the last sentence, at the top of page 8, what do you mean by "cross-collateralization structure"?
A. What I'm referring to there is that there is money available for -- let me back up.
Each book year, as it runs off, the monies response -- the monies available in earlier book years could be used to pay for losses in later book years.
So the cross-collateralization, I'm just referring to that the monies with -- can be intermingled between book years.
Q. How do you know when cross-collateralization has

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happened?
A. I think all you would know is, because each -- each book year is accounted for separately, so you know what the premiums are for a particular book year, so to the extent that losses are paid in excess of the premium received for that book year, I think by definition

Protective Order

[redacted]

Q. Are you familiar with the letter from Nicolas Retsinas to the general counsel of Countrywide Funding Corporation dated August 6, 1997?
A. I am.
Q. Okay. And what is the basis for your professional opinion that the Atrium agreements met the requirements of the HUD letter regarding risk transfer?
A. Because I do believe that there was -- that there was true -- that there was two benefits and real business justifications for entering into a reinsurance of that 10 percent layer.

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Q. Those are the business justifications that we talked about earlier, namely, surplus release, catastrophic exposure, use of the reinsurer's expertise, risk sharing or transfer, and smoothing?
A. Smoothing, right. We probably didn't get into a whole lot of why that's important, you know, you know, rating agencies.
Q. You're talking about smoothing?
A. Right.
You know, accountability to shareholders, but -- but yeah, those are the reasons.
Q. Are there any of the other requirements of the HUD letter other than the business justifications that you considered?
A. I considered the whole letter in its entirety.
Q. Okay. So what are the other requirements of the letter other than business justifications?
A. I don't recall.
Q. In paragraph 10 you refer to the analysis of excess-of-loss reports.
What is an analysis of excess-of-loss report?
A. Those were the Milliman reports that were, you know, performed, you know, on a periodic basis, and those are the reports that I have listed at the back of my report as those that I reviewed.

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Q. Okay. Which items on the list at the back of the report are analysis of excess-of-loss reports?
A. Well, I would have said certainly items 11 through 13. And I'm hedging a little with number 5. I'd have to go back and make sure that that also -- I would assume it did, but I would have to go back and make sure.
Q. Okay. Is there any other analysis of excess-of-loss report on this list?
A. By Milliman, I don't believe so.
Q. Okay. So 11 through 13 and possibly 5?
A. 5, yes.
Q. Okay. And what are analysis of excess-of-loss reports about?
A. What Milliman was doing in each of their reports is they were -- they were looking at the exposure to Atrium on a book year basis, and they would look at their exposure both on a paid and incurred, which is a paid plus reported, loss basis, as well as an ultimate basis, paid plus incurred plus IBNR basis.
That was the crux of the reports, you know, looking at the loss experience by year.
Q. And what did they say about the loss experience, if anything?
A. I really focused on the exhibits. I don't

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know what that percentage is? No. It's probably 99.9-something. I know what the statement means, but I don't know what the number is.
Q. But you know what 99.9 percent means.
A. Sure.
Q. Okay.
A. But I made that up.
Q. Does anything in the HUD letter indicate how a reasonable probability should be interpreted?
A. Nothing in the HUD letter discusses numeric percentages.
Q. Does anything in the HUD letter discuss the term "reasonable probability"?
A. I'd have to go back and check, but usually when people talk about reasonable probability, they're talking about it being not remote.
Q. Okay. Let's move on to paragraph 11.
You say that "The Atrium agreements clearly state that the reinsurer will continue to be liable, notwithstanding any termination."
That's near the bottom of page 8?
A. Yes.
Q. Okay. How do you know that?
A. That's what the contract says.
Q. Okay. What is your qualification to opine on

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what the contract means?
A. I've probably written north of a hundred reinsurance contracts from scratch over the history, so I'm pretty good at contract wording. I've also been held out as an expert on reinsurance contract wording, so I'm okay.
Q. Okay. So you have provided expert testimony on the meaning of contract provisions?
A. On contract -- yes. Absolutely.
Q. In what matters?
A. We -- there was -- there was one matter where the contract was a little vague as to whether the contract was covering losses paid by the -- was the reinsurer going to indemnify the insured on paid -- on a paid basis or on a -- or an incurred basis. That was a very sticky one because normally reinsurers are responsible virtually always on an ultimate or an incurred basis.
Q. What was the name of that case?
A. I don't recall.
Q. When was it?
A. It was certainly about five years ago.
Q. And in what court?
A. I don't recall.
Q. Was it an arbitration?

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A. Yes.
Q. What party retained you?
A. I don't -- I don't recall.
Q. Were there any other cases in which you were retained to interpret a contract?
A. Often -- oftentimes the cases hinge on contract wording, so it's not -- it may have not been the only issue discussed, but it was -- you know, it was part of the case involved, so it's something that does come up more often than not.
Q. Okay. But in what cases were you retained to provide an expert opinion on the meaning of a contract?
A. On strictly contract wording, I think it was only that one time.

Protective Order

[redacted]

in time, because if you just talk generally --
Q. Okay. In 2000, what assets were available to pay UGI's --
A. I'd have to look. Normally what would happen is, you know, in 2000, for UGI, they would have been on risk for, you know, three, four years, so they would have -- they would have had -- they would have had the benefit of some -- of some cash flow that would have -- that would have accrued to them over the first few years of the contract.
Q. What is that cash flow?
A. That was the cross-collateralization that we spoke about earlier.
Q. So that was all inside of the trust established for the UGI arrangement?
A. The trust -- you've got to remember, the trust is there to make sure that the unearned premium is satisfied, the -- that any reasonable estimate of

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unpaid losses are satisfied, so that should pretty much cover whatever, whatever becomes due.

Q. What other assets outside of the trust were available to pay claims to UGI?

A. On their balance sheet?

Q. Anywhere.

A. Anywhere? Well, they have a parent company.

Q. And who is that?

A. PHH.

Q. Okay. So PHH was liable for Atrium's claims -- for UGI's claims to Atrium?

A. I would -- I would sit here today and say, in the event that Atrium -- and we're very hypothetical here, by the way, because any time claims were presented to them -- and they paid at least seven to nine full -- or they paid many full limit losses, so they, in my mind, had a very demonstrated track record of paying all their claims when they became due.

Q. Okay. But I just want to be clear. I'm not asking a hypothetical. I'm asking about the meaning of the contract, the interpretation of the contract.

A. Right.

Q. Was PHH liable for any claims by UGI under the contract?

A. In the event Atrium was unable to satisfy

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claims -- and I think that's very hypothetical because that never happened -- but in the event, the way the contract -- the way the contract reads, Atrium -- Atrium had to come up with the money to pay all their claims.

Q. But was PHH legally obligated under the contract?

A. No. There's no mention of PHH in the contract.

Q. So what is the relevance of Atrium's parent?

A. Oftentimes parents support their subs.

Q. You mean that PHH could choose to provide Atrium with capital; is that right?

A. Yes.

Q. Okay. Did PHH have any obligation under the UGI contract to do that?

Protective Order

[redacted]

Q. So in 2000, what assets did Atrium have that it could use to satisfy claims to UGI, other than the trust?

MR. SOUDERS: Objection. Asked and answered.

THE WITNESS: I think we've discussed the monies that they had received over time.

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BY MR. VAZIRE:

Q. Those were in the trust. I'm asking for monies beyond that.

A. I'm not aware of any monies beyond the trust

Protective Order

[redacted]

your belief that if this issue were to be put before an arbitration panel, the panel would award the ceding company an amount equal to the unpaid liabilities?

A. I guess being in front of many arbitration panels, they're usually not happy if people do not fulfill their financial obligations.

Q. Is there any other basis?

A. No.

Could I take a one-minute break just to run out?

MR. VAZIRE: Sure.

THE WITNESS: Are you sure? I'll just be one minute.

(Recess)

BY MR. VAZIRE:

Q. What was Atrium's reinsurance later for the UGI 1997 book year?

A. I would have thought it was the same layer,

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10 excess of 4.

Q. What was the dollar amount of that coverage?

A. I don't know.

Q. When did the funds in the UGI trust become sufficient to pay that full reinsurance layer?

A. I don't know.

Q. Was the -- did the fund have enough in it by the end of 1997 to cover the full reinsurance layer at that time?

A. The full layer -- I don't know. I would have thought at the end of the first year you're also relying on capital.

Q. Yeah. Including capital, including everything that's in the trust fund.

A. Would it fund the entire first year.

I don't know.

Q. What about by the end of 1998?

A. I don't know.

Q. What about by the end of 1999?

A. Yeah. I don't know the numbers.

Q. Is there some time, some year where you know that definitely by that year there was enough in the fund to cover --

A. A full --

Q. -- the full limit on the 1997 book year?

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A. I don't know that date.
Q. Okay. But is there a date where at which point you know for sure yes, definitely by that date there was enough in the fund?
A. No.
Protective Order
[redacted]
Q. And what was the dollar amount of that layer?
A. I don't know.
Q. And when did the funds in the Genworth trust become sufficient to cover that full layer?
A. In the first year?
Q. Yes.
A. I don't know.
Q. What is the Financial Accounting Standard Board?
A. It's the policymaking group for CPAs in the United States.
Q. And CPAs are certified public accountants?
A. Yes.
Q. Are you a member of that group?
A. No. I'm not an accountant.
Q. What is -- is it "FASB" or "FASB"?
A. I say "FASB." Most people say "FASB," but some people say "FAS."

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Q. What is FASB 113?
A. FASB 113 was -- it is basically held out in the industry for GAAP financial statements as the document which discusses in great detail the requirements and criteria for risk transfer for reinsurance contracts.
Q. So it's an accounting standard?
A. Yes. For U.S. GAAP.
Q. What do you mean by the word "applicability" in the second sentence of paragraph 12?
A. Right. I'm not sure -- I'm not sure FASB 113 necessarily -- I'm not sure, is the right answer. I'm not sure it applies to mortgage insurance.
Q. Does it apply to mortgage reinsurance?
A. Reinsurance. Sorry. I'm not sure.
And the reason why I'm not sure is the task force was divided on this question because FASB 113 is written to pertain to all -- to all lines of business that are covered by FASB 60. And FASB 60 specifically excludes mortgage insurance.
So when I first came on this case, I was a little surprised that everybody seemed to be using FASB 113, not that it's necessarily wrong, but I would have thought there would have been some discussion surrounding 113, arguments pro and con, before everybody accepted it as the standard.

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Q. Who are you referring to when you say "everybody"?
A. It just seemed like every -- you know, Milliman talks about FASB 113. I believe -- anything I seem to read about, you know, the precursor to this case and now, everybody seems to quote 113 as the gospel. And again, I'm not saying it does not apply, but it just seemed to me that a discussion where all sides agreed that that was applicable might have been healthy.
Q. Who other than Milliman have you seen discuss FASB 113?
A. Your expert.
Q. Okay. Who else?
A. In relation to this case?
Nobody else bounces to mind, right.
Q. When you say that it applies, applies for which purpose?
A. As the standard for whether or not a reinsurance contract constitutes sufficient risk.
Q. For what purpose?
A. For MI reinsurance.
Q. But for an accounting purpose?
A. For an accounting purpose -- well, yeah, for an accounting purpose.
Q. And specifically for what accounting purpose?

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A. FASB pertains to statutory -- sorry -- to U.S. GAAP financial statements.
Q. I guess, what does a company get from having reinsurance that qualifies for FASB 113?
A. It really just enables them to take credit for reinsurance and to report their losses on both a gross and net of reinsurance basis.
Q. By "take credit," this is the same thing as a statutory credit that you spoke about earlier or is it something else?
A. No. It's very -- yeah. Statutory credit would be for the statutory statements, and U.S. GAAP would be -- or the 113 would be for U.S. GAAP statements.
Q. Okay. Great.
At the very end of paragraph 12, what are the other means of evaluating risk transfer other than FASB 113?
A. That's a great question.
The actual -- both the Casualty Actuarial Society and the American Academy of Actuaries has some, you know, pretty good papers on assessing risk transfer.
Q. And those are different from the FASB 113 way of assessing risk transfer?
A. Yes. Yeah.

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Q. How so?
A. They -- FASB -- FASB, rightly or wrongly, is burdened with this whole 1010 argument. And what the actuaries would say is, if you're on, for example -- and the 10/10 argument, 10 percent pertains to both probability of loss and 10 percent of the quantum of loss where the 10 percent is measured as a percentage of premium.
What the actuaries are quick to point out is that there's many property cat contracts that clearly have less than a 10 percent probability of loss but are self-evident to be risk bearing, such as a very high layer, you know, cat cover for, say, California earthquake, which would have run clean for the last twenty years, but clearly risk has been transferred and assumed by the cat writers, so that would violate the 10 percent probability law.
And likewise, if you're reinsuring a very stable book of, say, automobile liability, if you're expected to be able to lose 10 percent of your premium, but the most that this book -- let's say a State Farm book of auto business -- the most that's ever going to move is 2, 3, 4, 5 percent at most a year, so you're not going to be able to lose 10 percent of your premium, so in that -- so what the actuaries are arguing is that

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that is probably not the best way to look at risk transfer.
Q. By "loss" again you mean claims payments above premiums?
A. Correct. Yes.
From the perspective of the reinsurer always, too. We're always talking about reinsurance. We're not concerned about the insurance company.
Q. Right.
A. They get a free pass.
Q. So what does FASB 113 have to do with the 10/10 test?
A. FASB -- FASB has a -- paragraph 9 in FASB actually has subparagraphs, a part A paragraph and a part B paragraph. And the part A paragraph I believe talks about the frequency of loss to the reinsurer or the probability of loss to the reinsurer not being remote, and somehow that not being remote has evolved into 10 percent.
And paragraph 9-B of FASB talks about the quantum of loss and, again, loss being the amount over and above, you know, the amount of premium that the reinsurer receives, that that has -- I'm trying to remember the exact words that they use. I don't recall, but it's evolved again into 10 percent of the premium,

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of the ceded premium to the reinsurer.
So that's how FASB has kind of morphed into this 10/10 rule.
Q. Did you use any means other than that rule to evaluate risk transfer in connection with this report?
A. No.
Q. Did you use the FASB 113 10/10 rule to evaluate risk transfer in connection with this report?
A. That's the one I felt like I was -- I inherited, so that's what I was using.
Q. Okay. And how did you use it?
A. Well, again, you want to be able to satisfy both the probability of loss and the quantum of loss.
And I think we touched upon this a little

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FASB 113 requirement.
Q. And can that requirement be applied retrospectively the way you just did?
A. Those are supposed to be -- no. It's a prospective test.
Q. Okay. So did you evaluate risk transfer from a prospective perspective?
A. Not in 1997.
Q. Okay.
A. I --
Q. Is it possible to evaluate risk transfer for an arrangement that was entered into in the past using the 10/10 test?
A. Yeah. It is -- you know, unfortunately, you know, humans or people being people, you are always -- rightly or wrongly, you are always swayed by what you've observed.
Can we go back and sit ourselves, you know, at a desk in 1997 and say what were the true a priori, you know, probabilities and loss distributions? I'm not sure. I'm not sure.
Q. What information would have to have been used in 1997 in order to evaluate risk transfer under the 10/10 test?
A. The information that would be used would be a

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would be, if you go three years loss-free, you're ecstatic. Three to five years would be great.
Q. Okay.
A. Yeah.
Q. And was this the case with the Atrium arrangements?
A. Yeah. They didn't -- I don't remember the first year where there was, you know, real loss activity for UGIC, but it was -- it was pushing ten

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Q. Okay. The first sentence of paragraph 16 reads, "FASB 113 does not require a reinsurer to assume risks where it ultimately believes that it will suffer an economic loss."
What does that mean?
A. I think to the non-insurance or reinsurance practitioner, risk -- risk sometimes means certainty of loss. The way the insurance and reinsurance mechanisms work is the buyer or the cedant of the exposure -- the loss needs to be fortuitous from the perspective of that ceding the loss, so in the case of the insured, whether

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the insured defaults or not on her loan, it needs to be fortuitous from their perspective.
For the reinsurer, the reinsurer, whether or not it experienced a loss, it also needs to be fortuitous from their perspective to write a piece of business that you're virtually certain is going to be a loser. That's -- that's not what FASB was talking about.
Q. In the third sentence, you refer to what you call "the usual risk transfer criteria."
What are those?
A. That's the 10/10 I'm talking about.
Q. Okay. In the sentence after that, you refer to "the following example."
What is that example?
A. The one in paragraph 17.
Q. Okay. What is the example in paragraph 17?
A. Let me see. I think what I'm referring to there are the high -- if you see above there, I'm referring to the, you know, cat- -- excess of loss catastrophe, and then here I'm talking about catastrophe covers that are -- you know, that are sold now even by the investment banks, you know, the one-in-100-year event, the one-in-250-year event, the one-in-500-year event.
Those covers are clearly risk bearing but yet

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would fail the 113 test miserably.
Q. Okay. So going back to paragraph 16, you say, "The charges brought against PHH, et al., also imply that an XOL catastrophe reinsurer needs to satisfy the usual risk transfer criteria," which you've said is a reference to FASB 113.
Then you say, "Nothing can be further from the truth," so I assume you're saying that an XOL catastrophe reinsured does not need to satisfy FASB 113?
A. That's my view, although I feel like I'm being held to the standard, so I defend it by the 10/10, but again I keep going back to, I'm not sure it's been -- it's been demonstrated that that's -- that's the standard that should be -- that should be held.
Q. Okay. And your view that XOL catastrophe reinsurance does not need to be held to the standard of FASB 113 is demonstrated by the example in paragraph 17; is that right?
A. Right. When I talk about the 100, 250 and 500-year covers.
Q. How does that demonstrate that catastrophe reinsurance does not need to satisfy FASB 113?
A. Well, there is zero argument in the industry that those types of reinsurances are risk bearing,

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they're extremely risky, but yet they're nowhere remotely close to having a 10 percent probability of being a loser.
Q. Okay. Does the Atrium reinsurance qualify as a this type of reinsurance in paragraph 17?
A. It's not a one in 100, one in 250 or one in 500 by any stretch, but it is an excess of loss cat cover.
Q. But it's not the type that you talk about in paragraph 17.
A. No. No.
Q. Okay. So then --
A. I'm -- sorry. I didn't mean to interrupt you.
Q. No. Go ahead.
A. I'm basically saying that FASB 113 should not be strictly supplied in all instances, is just the point I'm making there.
Q. But that point doesn't show that it should not be applied to the Atrium arrangements.
MR. SOUDERS: Objection to the form.
Go ahead. Answer if you can.
THE WITNESS: I am still -- I still try to say that despite in my own mind the applicability of 113 to the Atrium arrangements, even being held to this higher standard, I still feel it passes muster.