

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

THE BENNETT FUNDING GROUP, INC.

Debtors

CASE NO. 96-61376

Chapter 11

Substantively Consolidated

APPEARANCES:

SIMPSON THACHER & BARTLETT

Attorneys for § 1104 Trustee

425 Lexington Avenue

New York, New York 10017-3954

WILLIAM T. RUSSELL, ESQ.

KATHRINE A. MC LENDON, ESQ.

MICHELLE B. CHERANDE, ESQ.

Of Counsel

WASSERMAN, JURISTA & STOLZ

Attorneys for Committee of Unsecured Creditors

225 Millburn Avenue

Millburn, NJ 07401

HARRY GUTFLEISH, ESQ.

Of Counsel

COSTIGAN & COMPANY, P.C.

Attorneys for Ades and Berg Investors

305 Broadway, 7th Floor

New York, NY 10007

WILLIAM F. COSTIGAN, ESQ.

Of Counsel

KIRBY McINERNEY & SQUIRE, LLP

Attorneys for Class Action Plaintiffs

830 Third Avenue, 10th Floor

New York, NY 10022

RANDALL K. BERGER, ESQ.

Of Counsel

RICHARD L. STONE

Of Counsel

Hon. Stephen D. Gerling, Chief U.S. Bankruptcy Judge

**MEMORANDUM-DECISION, FINDINGS OF FACT,
CONCLUSIONS OF LAW AND ORDER**

Presently before the Court is the final portion of a motion, filed by Richard C.

Breeden, chapter 11 trustee (the "Trustee") of The Bennett Funding Group, Inc. ("BFG") and

other substantively consolidated debtors¹ (together with BFG, the “Debtors” or the “Estate”), on March 13, 2003, seeking, *inter alia*, the Court’s approval of the Trustee’s plan to ratably allocate to unsecured creditors of the Estate the proceeds of a settlement (the “Settlement”) executed by the Trustee; Sphere Drake Insurance plc and Sphere Drake Underwriting Management (Bermuda) (collectively, “Sphere Drake”); Triangle Insurance Management, Ltd.; Janice Witkowski; Lloyd Thompson, Ltd., currently known as JLT Risk Solutions, Ltd.; Sherwood Insurance Services, Inc.; Ivan Small; certain purchasers and investors in BFG securities (the “Sphere Drake Class”); Dollar Capital Corp. and its bankruptcy estate (“Dollar”); Charles Forman, as chapter 11 trustee for Halpert and Co. (“Halpert”); and the Official Receiver of Bermuda, on behalf of Capital Insurance, Ltd. The Ades and Berg investor groups (“Ades and Berg”) filed an objection on March 26, 2003. The Sphere Drake Class also filed an objection on April 9, 2003, which received the joint support of Dollar and Halpert in a statement filed on April 25, 2003.

The Court heard oral argument on March 27, 2003 during its regular motion term in Utica, New York. Further argument was heard on May 29, 2003 during the Court’s regular motion term in Utica. The matter was submitted on June 26, 2003.

In a letter dated February 13, 2004, the Court requested the Trustee to supplement the record with various data pertaining to this matter. The Trustee responded to the Court’s request on March 31, 2004.

¹ On March 29, 1996, BFG, along with Bennett Receivables Corp., Bennett Receivables Corp. II, and Bennett Management and Development Corp., filed voluntary petitions pursuant to chapter 11 of the Bankruptcy Code, 11 U.S.C. §§ 101-1330 (“Code”). On April 19, 1996, American Marine International, Ltd. and Resort Service Co., Inc. filed voluntary petitions pursuant to chapter 11 of the Code and on April 25, 1996, an involuntary case was commenced against Aloha Capital Co. On April 26, 1996, The Processing Center (“TPC”) also filed a chapter 11 petition. By Order dated July 25, 1997, the Court substantively consolidated the Debtors’ estates.

JURISDICTIONAL STATEMENT

The Court has jurisdiction over the subject matter and parties of this contested matter pursuant to 28 U.S.C. §§ 1334, 157(a), (b)(1), and (b)(2)(A) and (O).

FACTS

For an account of the procedural and factual background of this thread of the BFG case, the Court refers readers to its opinions dated May 22, 2003 and February 9, 2004 and to the following decisions: *Breeden v. Sphere Drake Ins. plc (In re Bennett Funding Group, Inc.)*, 270 B.R. 126 (S.D.N.Y. 2001), *aff'd sub nom. Breeden v. Ades Investor Group (In re Bennett Funding Group, Inc.)*, 60 Fed. Appx. 863 (2d Cir. 2003); *Breeden v. Sphere Drake Ins. plc (In re Bennett Funding Group, Inc.)*, 258 B.R. 67 (Bankr. N.D.N.Y. 2000); *Breeden v. Sphere Drake Ins. plc (In re Bennett Funding Group, Inc.)*, No. 97-70049, 2000 Bankr. Lexis 1693 (Bankr. N.D.N.Y. Mar. 3, 2000); *Breeden v. Sphere Drake Ins. plc (In re Bennett Funding Group, Inc.)*, No. 97-70049, 1999 Bankr. Lexis 1857 (Bankr. N.D.N.Y. Aug. 6, 1999).

I. The Settlement

The Settlement resolved the tort and contract claims brought by the Trustee and the Sphere Drake Class against, *inter alia*, Sphere Drake.² The District Court approved the

² The Trustee's claims were originally filed in this Court as part of an adversary proceeding that commenced on February 24, 1997. On June 20, 2000, the Court recommended that the reference be withdrawn with respect to the adversary proceeding. The reference was withdrawn soon thereafter and the proceeding was transferred to the United States District Court for the Southern District of New York ("District Court"), to be administered in conjunction with a securities class action brought by the Sphere Drake Class and styled *Becker v. Sphere Drake*

Settlement on June 5, 2003, and remanded to this Court jurisdiction over the allocation of the proceeds of the Settlement and over Ades and Berg's counterclaim seeking a constructive trust. *Becker v. Sphere Drake Ins. plc (In re Bennett Funding Group, Inc. Sec. Litig.)*, No. 97 Civ. 9485 (JES) (S.D.N.Y. June 5, 2003).

The Settlement requires Sphere Drake to pay \$27,500,000 in exchange for the release of the Trustee's and the Sphere Drake Class's claims against Sphere Drake. Stipulation and Agreement of Settlement (the "Stipulation") § VII *in* Trustee's Mot., filed June 13, 2003 (the "9019 Motion"), at Ex. 1. The Trustee proposed that the Settlement be ratably allocated to all general unsecured creditors. 9019 Motion ¶ 21.

II. The Generali settlement

The Court in an Order dated April 9, 1999 approved a settlement between the Trustee and Assicurazioni Generali S.p.A., Generali U.S. Branch, and Generali Underwriters, Inc. (collectively, "Generali"). *In re Bennett Funding Group, Inc.*, No. 96-61376, 1999 Bankr. Lexis 1860, at *44 (Bankr. N.D.N.Y. Apr. 9, 1999). Generali agreed to pay the Trustee \$125 million in exchange for the release of the claims of the Trustee and a class of purchasers of Generali insured BFG investments (the "Generali Class"). *Id.* at *13-14. The Generali settlement carved out a pool of \$15.9 million that was proportionally and exclusively distributed to the Generali Class. *See* Trustee's Mot., filed Dec. 23, 1998 ("Generali 9019 Mot."), ¶ 15. The remaining funds were ratably distributed to all BFG unsecured creditors. *See id.* ¶ 21. The Trustee in his motion to approve the Generali settlement proposed that either the special pool allocation or a fully ratable allocation would be fair and reasonable. *See id.* ¶ 5.

The Generali settlement was the only settlement in the case that featured a special pool plan of allocation. Based on a review of reports filed by the fee auditor in the case, Stuart Maue Mitchell & James, Ltd., the Trustee spent an estimated \$291,870 over one and a half years performing services pertaining to the allocation of the Generali settlement proceeds.

ARGUMENTS

The Trustee argues in favor of ratably allocating the Settlement proceeds among all unsecured creditors because a special pool plan of allocation, as in Generali, is not justifiable in light of the smaller size of the Settlement and the time and expense required to administer such a special pool allocation. The Trustee supports his position with the affirmance of the United States Court of Appeals for the Second Circuit (the “Second Circuit”) of a decision by the District Court that held that Ades and Berg have no standing to individually sue Sphere Drake on a contract theory of liability, which the Trustee contends weakens the claims of the Sphere Drake Class as well. The Trustee also compares the Settlement with all prior settlements reached in the case save Generali in which the proceeds were ratably allocated. At oral argument, the Official Committee of Unsecured Creditors (the “Committee”) supported the Trustee’s position and added that all creditors should share equally in the Settlement proceeds because the proceeds are essentially assets that have accrued solely to the Estate.

The Sphere Drake Class objects to a ratable allocation because the extra time and expense required to administer a special pool plan of allocation does not outweigh the injustice to the Sphere Drake Class should such a plan of allocation be denied in this case. The Sphere Drake Class contends that it is entitled to a greater distribution than other creditors because its

members received certificates and other documentation from BFG that created the impression that Sphere Drake insured their investments. Dollar and Halpert join in the Sphere Drake Class's objection.

Ades and Berg also object to a pro rata allocation and support a targeted allocation on the ground that, because the loss payee on the Sphere Drake policy acts on behalf of purchasers of Sphere Drake-insured investments, all or at least a substantial portion of the Settlement proceeds should flow to those investors. Ades and Berg further propose that, before ruling upon the plan of allocation, the Court should adjudicate their counterclaim for a constructive trust and, in the event that they prevail on their constructive trust counterclaim, order that the Settlement proceeds be distributed solely to them.

Alternatively, should the Court approve the Trustee's plan of allocation, Ades and Berg object to the amount to be deducted from the Settlement proceeds to compensate counsel for the Sphere Drake Class. Counsel for the Sphere Drake Class counters that the Court should dismiss this argument on the ground that the District Court is the proper forum in which to litigate disputes concerning their compensation.

DISCUSSION

I. Allocation of the Settlement proceeds

As a continuation of the Settlement approval process commenced by the District Court, the approval of the plan of allocation is governed by the standard for approving

settlements, *i.e.*, whether the plan of allocation is fair, reasonable, and in the best interests of the Estate. *See In re Enron, Inc.*, No. 02 Civ. 8489 (AKH), 2003 WL 230838, at *2 (S.D.N.Y. Jan. 31, 2003). Factors relevant to this analysis include the likelihood of success in the underlying litigation; the complexity, expense, inconvenience, and delay presented by the litigation; and the interests of the creditors. *Nellis v. Shugrue*, 165 B.R. 115, 122 (S.D.N.Y. 1994).

The Trustee proposes to ratably allocate the Settlement to all general unsecured creditors. In recommending a pro rata plan of allocation, the Trustee relies on his experience administering the settlement with Generali earlier in this case. In that settlement, \$15.9 million of a \$125 million settlement was distributed exclusively to purchasers of Generali-insured investments. The Trustee contends that administering the Generali settlement was a time-consuming and expensive process, requiring the provision of notice to several thousand creditors, analyzing proofs of claim, objecting to deficient claims, and sometimes litigating with claimants. The Sphere Drake Class, with the support of Dollar and Halpert, objects to the proposed pro rata allocation, contending that the burdens of time and expense that attend the administration of a special pool allocation do not outweigh the injustice that a pro rata distribution would wreak on the Sphere Drake Class. Specifically, the Sphere Drake Class argues that its exclusive entitlement to the Settlement proceeds arises from the certificates of insurance and other documentation that accompanied its members' investments, which created the impression—deceptively advanced by BFG to attract investors—that Sphere Drake would insure those investments.

The Court's assessment of the administration of the Generali settlement reveals that the Trustee spent nearly \$300,000 and over one and a half years allocating that settlement. Even though there are fewer potential special pool allocation claimants in the Settlement as

compared to the Generali settlement, it can be conservatively assumed that roughly the same amount of time and money will be spent administering the Settlement on account of the reduction of the Trustee's staff. The economic cost of allocating the Generali settlement represented .25 percent of the total settlement amount, whereas that same expense in the Sphere Drake settlement would equal slightly over 1 percent of the total settlement amount. The Sphere Drake cost ratio, though larger than the Generali ratio, still represents a *de minimis* portion of the total proceeds and does not alone justify a ratable allocation among all unsecured creditors.

Of greater import for this analysis is the amount of time necessary to administer a special pool plan of allocation. The Court assumes for purposes of this analysis that allocating a special pool would take a year and a half, which does not include the additional time that may be necessary to actually consummate the Settlement. The Court also notes the Trustee's current reduced staff relative to the number of staff that administered the Generali settlement, a factor that would further limit the Trustee's ability to efficiently administer a special pool allocation. However, the Court also recognizes that the interests of the Sphere Drake Class and Ades and Berg are no different than those of the Generali Class. Indeed, the achievement of the Settlement is wholly due to the collaborative efforts of the Sphere Drake Class, Ades and Berg, and the Trustee; such contributions on their part cannot be simply cast aside. Thus, the Court does not find the temporal burden on the Trustee a sufficiently compelling basis to apply a lesser standard of treatment to the Sphere Drake Class and Ades and Berg than was provided to the Generali Class.

The Trustee also distinguishes the Settlement from the Generali settlement by calling attention to the Second Circuit's affirmance of the District Court's conclusion that Ades and Berg, because they are not listed as loss payees on the Sphere Drake policies, do not have

standing to individually sue Sphere Drake. *In re Bennett Funding Group, Inc.*, 60 Fed. Appx. 863, 865 (2d Cir. 2003), *aff'g Breeden v. Sphere Drake Ins. plc (In re Bennett Funding Group, Inc. Sec. Litig.)*, 270 B.R. 126, 130 (S.D.N.Y. 2001). The Trustee characterizes that decision as not wholly dispositive of whether the plan of allocation is fair and reasonable but still contends it is a strong factor to be weighted in favor of approving the ratable allocation. Indeed, the Second Circuit's ruling struck a fatal blow to the contract claims that Ades and Berg and the Sphere Drake Class had against Sphere Drake. In contrast, the Trustee, as representative of the loss payee on the Sphere Drake policy, settled a relatively strong contract claim. However, the Second Circuit decision did not rule on Ades and Berg's or the Sphere Drake Class's ability to sue Sphere Drake on tort theories of liability. Even though the Settlement requires the Sphere Drake Class and Ades and Berg to release tort claims that were far from certain, it appears unfair not to recognize the relinquishment of their rights to sue Sphere Drake. Furthermore, the Sphere Drake Class's and Ades and Berg's tort rights are not impaired by unfavorable precedent and thus should be afforded the same treatment as the Generali Class received in the Generali settlement.

Militating in favor of a ratable allocation are the interests of the unsecured creditors in this case who are not members of the Sphere Drake Class or the Ades and Berg groups. It must not be forgotten that these creditors have also been injured by BFG's deception insofar as BFG, in furtherance of its alleged fraud, diverted funds that could have been used to pay such unsecured creditors that are not participating in the Settlement. The Court does not deem the injuries resulting from such diversionary tactics insignificant. However, that does not inevitably lead to the conclusion that all of the proceeds of the Settlement should be allocated to the general unsecured creditors.

Thus, the question is who should get how much. Ades and Berg incorrectly

contend that only the purchasers of Sphere Drake-insured investments should receive the proceeds based on the loss payee's contract claim against Sphere Drake. Because the Trustee represents TPC, the actual loss payee on the Sphere Drake policy, the proceeds of that claim would inure entirely to the Estate and thus to all unsecured creditors. Conversely, all general unsecured creditors have borne the substantial cost of litigating and settling TPC's claim. Their interests cannot be entirely ignored while the Sphere Drake Class and Ades and Berg reap all the benefits of the Settlement. Therefore, given the nature of general injury attending all creditors and the specific injuries suffered by the Sphere Drake Class and Ades and Berg, the Court finds that the most equitable outcome, which serves the various interests at play in the Settlement, would be to allocate the Settlement in the same fashion as the Generali settlement, apportioning a segment of the proceeds to a special pool to be allocated to the Sphere Drake Class and Ades and Berg. While the Sphere Drake Class and Ades and Berg will receive a greater proportional share of the Settlement than the general unsecured creditors, the Court notes that a special pool allocation does not overlook the general unsecured creditors' interests; indeed, they will collectively receive the greatest portion of the Settlement proceeds.

The Generali special pool was \$15.9 million, or the amount equal to the maximum lease payment shortfall. Generali 9019 Mot. ¶ 15. The special pool in this case will reflect the maximum lease payment shortfall reduced, however, by the degree of litigation risk attending the claims of the Sphere Drake Class and Ades and Berg. *See id.* ¶¶ 15, 24. The Court will use \$9,393,340, the amount alleged by Sphere Drake to be the maximum lease payment shortfall, as a base figure. *See* Letter from Kathrine A. McLendon, Esq. to the Court, dated Mar. 31, 2004, at Ex. C. That figure will be reduced by a litigation risk factor of 50% to account for the precedential obstacle posed to the contract claims of Sphere Drake Class and Ades and Berg and

the high temporal and monetary costs of pursuing their tort claims as well as their inherent complexity. After accounting for this reduction, the Court arrives at a special pool figure of \$4,696,670. The special pool will be distributed in the same manner as the Generali settlement and to a similarly broad class of investors. *See* Generali 9019 Mot. ¶ 19. However, the Court provides the Trustee wide latitude in seeking the most efficient and expeditious method of administering the Settlement and encourages him to draw upon his experience distributing the Generali settlement. The Court further notes that this plan of allocation will not disturb the Settlement's terms regarding payment of attorney's fees and costs.

Accordingly, the Court finds that the allocation, as modified above, is fair, reasonable, and in the best interest of the Estate.

II. Ades and Berg's constructive trust counterclaim

Additionally, Ades and Berg argue that the allocation of the Settlement should not be approved at all until the Court adjudicates their counterclaim against the Trustee seeking to impose a constructive trust over the Settlement proceeds in their favor. The Court disagrees. The Court may approve the plan allocation before adjudicating the constructive trust counterclaim. Disbursement of the Settlement proceeds must still await the establishment of all of the conditions to consummation. Nonetheless, in order to protect Ades and Berg's interests, the Court directs the Trustee not to distribute the Settlement proceeds until the counterclaim is finally adjudicated.

In that regard, the Court notes that on February 27, 2004, the Trustee filed a Reply to Ades and Berg's renewal of their counterclaim. The Court will schedule a pretrial conference pertaining to this matter.

III. Compensation of counsel for the Sphere Drake Class

Lastly, the Court also dismisses Ades and Berg's argument that the Court should not approve an award of fees to counsel for the Sphere Drake Class because their services did not benefit their clients. Ades and Berg, as counsel for the Sphere Drake Class have astutely pointed out, have petitioned the wrong court. The District Court in an Order dated June 5, 2003 clearly indicated that it would maintain jurisdiction over the disbursement of compensation to counsel for the Sphere Drake Class. *Becker v. Sphere Drake Ins. plc (In re Bennett Funding Group, Inc. Sec. Litig.)*, No. 97 Civ. 9485 (JES), at ¶ 11 (S.D.N.Y. June 5, 2003).

Based on the foregoing, it is hereby

ORDERED that the Trustee's motion to allocate the proceeds of the Settlement is granted in accordance with the Court's directions as set forth herein; and it is further

ORDERED that with regard to Ades and Berg's renewed counterclaim the parties are directed to appear before this Court in Utica, New York on April 29, 2004 at 2:00 p.m. for a scheduling conference.

Dated at Utica, New York

this 12th day of April 2004

STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge