

Judge Berman
UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

ECF CASE

-----X
Gregory V. Serio, Superintendent of Insurance
of the State of New York, as Rehabilitator of
FRONTIER INSURANCE COMPANY, and as
Assignee of PLATINUM INDEMNITY, LTD.,

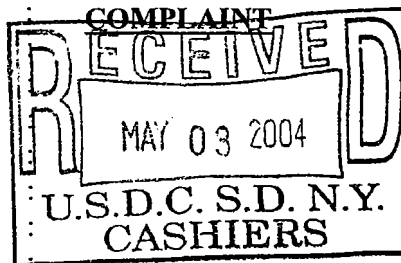
04 CV Civil Action No. 3361

Plaintiff,

-against-

DWIGHT HALVORSON INSURANCE
SERVICES, INC d/b/a/ F.S.I.M. INSURANCE
SERVICES and FOOD SERVICE INSURANCE
MANAGERS, INC.,

Defendants.
-----X



Plaintiff Gregory V. Serio, Superintendent of Insurance of the State of New York,
as Rehabilitator of Frontier Insurance Company ("FIC") and as the Assignee of Platinum
Indemnity, Ltd., by and through the undersigned attorneys, as and for his Complaint against
defendants Dwight Halvorson Insurance Services, Inc. d/b/a F.S.I.M. Insurance Services
("DHIS") and Food Service Insurance Managers, Inc. ("FSIM"), hereby alleges as follows:

NATURE OF THE ACTION

1. This action arises out of a workers' compensation insurance program that the defendants developed for and marketed to the food services industry.
2. FIC provided insurance coverage under this program and, in return, was entitled to receive from DHIS certain payments pursuant to the terms of the controlling agency agreement.
3. FIC fully performed its obligations to DHIS by, among other things, not only issuing the insurance policies in question but also paying out millions of dollars on workers'

compensation claims made on those policies.

4. DHIS, however, has breached its contractual and fiduciary obligations to FIC by collecting premiums from insureds but failing to forward the payments due and owing to FIC.

5. Subsequent to the termination of its relationship with the insurance program at issue, FIC confirmed that DHIS improperly has withheld millions of dollars in payments due to it under the program. FIC brings this action to recover these payments from DHIS.

6. In addition, pursuant to a binding and court-authorized assignment of certain claims belonging to the offshore reinsurer involved in the insurance program giving rise to this litigation, FIC brings this action to recover several million dollars due from FSIM to the reinsurer under certain agreements between those parties.

JURISDICTION AND VENUE

7. The Court has subject matter jurisdiction over this action pursuant to 28 U.S.C. § 1332(a) because the matter in controversy is in excess of \$75,000.00, exclusive of interest and costs, and is between citizens of different states.

8. This district is a proper venue pursuant to 28 U.S.C. § 1391(a)(1)(2) because a substantial part of the events and/or omissions giving rise to this action occurred within this district.

THE PARTIES

Frontier Insurance Company

9. FIC at all relevant times was and is an insurance company organized and existing under the laws of the State of New York and maintaining its principal place of business in Rock Hill, New York.

10. On or about August 24, 2001, the Superintendent of Insurance of the State of New

York (“Superintendent”) initiated proceedings in the Supreme Court of the State of New York, New York County, seeking an order placing FIC into rehabilitation pursuant to Article 74 of the New York Insurance Law.

11. On or about August 27, 2001, the Court appointed the Superintendent as temporary receiver of FIC.

12. The Court entered an Order of Rehabilitation with respect to FIC on or about October 15, 2001. Therein, the Court appointed the Superintendent as Rehabilitator of FIC, declared FIC insolvent and found that “[i]t is in the best interest of Frontier’s policyholders, creditors and the general public that the Superintendent be directed to take possession of Frontier’s property and to rehabilitate its business and affairs[.]”

13. The Order of Rehabilitation expressly authorizes the Superintendent to:

[T]ake possession of [FIC’s] property, conduct its business . . . take such steps toward the removal of the causes and conditions which made [the rehabilitation] proceeding necessary as he shall deem wise and expedient, and deal with the property and business of [FIC] in its name or in the name of the Superintendent as Rehabilitator.

14. As Rehabilitator, the Superintendent also is authorized and empowered to commence litigation and pursue the recovery of damages on FIC’s behalf, as well as for the benefit and protection of its policyholders, insureds and creditors. It is in this capacity that the Superintendent brings this action.

The Defendants

15. DHIS at all relevant times was and is a corporate entity organized and existing under the laws of the State of California.

16. At all times relevant to this litigation, DHIS was an insurance agency specializing in providing insurance and risk management services to clients in the food services industry.

17. FSIM at all relevant times was and is a corporate entity organized and existing under the laws of the State of California.

18. At all relevant times, FSIM was engaged in the business of securing workers' compensation insurance coverage for insureds in the agribusiness and food-related industries.

19. Both DHIS and FSIM maintain their principal places of business at 3300 Douglas Boulevard, Roseville, California.

FACTUAL BACKGROUND

The FSIM Program

20. DHIS was formed in or about 1987 as an insurance agency specializing in providing risk management services to businesses in the food services industry in and around California's Sacramento Valley.

21. DHIS grew to become a regional leader in that segment of the insurance industry, servicing growers, shippers, packers, distributors and processors of food products in Northern California.

22. In or about 1997, DHIS's president, Dwight J. Halvorson, formed FSIM as part of a comprehensive workers' compensation insurance program specifically designed for and marketed to the agribusiness and food-related industries (the "FSIM Program").

23. At all relevant times, FSIM was a risk-bearing managing general agency providing workers' compensation coverage to its clients through an offshore rent-a-captive insurance facility.

24. A captive insurance company is an insurance company owned and controlled by the insureds themselves. Its primary purpose is to insure the risks of those owners.

25. Captive insurance programs provide an alternative source of coverage to insureds

for whom the conventional approach of purchasing policies from an established insurance carrier may be unavailable or prohibitively expensive.

26. For a variety of regulatory and financial reasons, captive insurers typically are domiciled in offshore jurisdictions such as Bermuda, the Cayman Islands, Barbados and the British Virgin Islands.

27. These offshore captives typically are not licensed to actually issue insurance policies within the United States. As a result, they typically act solely as reinsurers and partner with a fronting insurer that is licensed to issue policies in the United States to the insureds. The fronting carrier issues those policies and then transfers a significant portion of the risk back to the offshore captive pursuant to a reinsurance agreement.

28. One variation of the captive insurance program approach -- and the alternative the defendants in this action utilized -- is to structure the program around a rent-a-captive.

29. The rent-a-captive is designed to accommodate insureds who either are unable or unwilling to assume the higher costs of establishing their own captive, a process which can require substantial upfront costs and capital investment.

30. A rent-a-captive facility involves a captive formed by one or more sponsors who then "rent" the captive's capital, surplus, services and expertise to various insureds or groups of insureds.

31. The insured or insureds who use the rent-a-captive typically purchase non-voting preferred shares in the captive, pay a fee and post some form of collateral to shield the captive reinsurer from any underwriting losses that may arise.

32. In the typical rent-a-captive facility, separate rent-a-captive accounts are established within the overall captive infrastructure for each distinct set of insureds. Premiums

collected on policies issued under a particular program are credited to the appropriate rent-a-captive account and loss payments made in connection with those losses are debited from the appropriate account.

33. Platinum Indemnity, Ltd. (“Platinum Indemnity”) served as the rent-a-captive around which the defendants structured the FSIM Program.

34. At all relevant times, Platinum Indemnity was a corporate entity organized and existing under the laws of the Islands of Bermuda and maintained its principal place of business at Windsor Place, 18 Queen Street, Hamilton, Bermuda.

**FIC Is Enlisted as the FSIM
Program’s “Fronting” Insurer**

35. In or about 1997, Halvorson, DHIS’s president, approached FIC to determine if FIC would be interested in serving as the fronting carrier for the FSIM program.

36. During its negotiations with DHIS, FIC emphasized that it would consider Halvorson’s proposed program only if it received assurance that, whether through reinsurance or otherwise, FIC as the fronting insurer would be exposed to virtually no risk on the underlying policies.

37. Halvorson acknowledged this demand and assured FIC that the FSIM Program would be structured in such a way that FIC would face minimal exposure on the underlying policies.

38. FIC and DHIS ultimately entered into a Limited Agency Agreement (the “Agency Agreement”) dated effective January 1, 1998.

39. Under the Agency Agreement, FIC appointed DHIS as its agent and authorized it to quote, bind and decline workers’ compensation insurance coverage for agricultural operations,

including farms and vineyards, as well as produce packing and handling operations.

40. The Agency Agreement provided that DHIS, “as a trustee for” FIC, was authorized to receive premiums and fees, pay return premiums, pay adjustments and retain and pay commissions out of the premiums collected through the FSIM program.

41. The Agency Agreement further provided for DHIS to accept and maintain all premiums and other funds it collected under the FSIM program “in the capacity of a fiduciary and trustee” for FIC.

42. Pursuant to the Agency Agreement, within fifteen days of the end of each month, DHIS was required to provide FIC with an “Account Current.” This monthly Account Current was an itemized statement of all premiums written, as well as any premium adjustments, made within the month in question.

43. Pursuant to the Agency Agreement, each Account Current forwarded to FIC was to reflect DHIS’s customer numbers for each insured; FIC policy numbers for each policy; gross premiums to be paid; the percentage of commission to be retained -- and most significantly for purposes of this dispute -- the net premium payment to be remitted to FIC.

44. Under the Agency Agreement, within forty-five days following the end of each month, DHIS was obligated to pay to FIC the balance due as reflected on the Account Current relating to that month.

45. Pursuant to the Agency Agreement, DHIS was obligated to make these payments to FIC regardless of whether the premiums in question actually were paid by the insured or subproducer. Therein, the parties expressly agreed that DHIS “assumes the credit risk should it bind insurance without receiving premium.”

46. Pursuant to the terms of the Agency Agreement, upon termination, all premiums

in DHIS's possession as of that time, as well as those DHIS was obligated to collect, became immediately due and owing to FIC.

47. As compensation for its services, FIC agreed to allow DHIS a gross commission of 12 percent of all gross premium collected on policies underwritten or delivered by DHIS through the program.

48. Subsequently, the Agency Agreement was amended effective January 1, 1999 to allow DHIS a 15.65 percent commission.

49. In the Agency Agreement, FIC and DHIS specifically agreed that "the courts of New York shall have exclusive jurisdiction to resolve" any dispute arising between the parties. Further, FIC and DHIS agreed that any such dispute would be resolved under New York law.

The Subscription and Shareholders Agreement

50. On or about January 16, 1998, FSIM and Platinum Indemnity entered into a Subscription and Shareholders Agreement.

51. Therein, as part of its rent-a-captive arrangement with Platinum Indemnity, FSIM agreed to purchase a non-voting redeemable preferred share in the captive for \$125,000.00.

52. Among the rights and obligations reflected in the Subscription and Shareholder's Agreement is FSIM's obligation to pay to Platinum Indemnity all amounts necessary to remedy any "Negative Balance" in its account.

53. In essence, a Negative Balance would arise under the terms of the Subscription and Shareholders Agreement if the losses Platinum Indemnity was compelled to reinsure under the FSIM Program outstripped the level of premium dollars flowing from DHIS to FIC and, ultimately, into FSIM's rent-a-captive account at Platinum Indemnity.

The Promissory Note

54. On or about November 8, 2000, FSIM executed and delivered to Platinum Indemnity a promissory note ("Note") obligating itself to pay to Platinum Indemnity the amount of \$469,515.00, plus interest. A copy of the Note is attached hereto as Exhibit A.

55. The Note was executed as a means of securing FSIM's performance of its financial obligations to Platinum Indemnity under the Subscription and Shareholders Agreement.

56. Pursuant to the terms of the Note, FSIM was obligated to pay the \$469,515.00 in monthly installments of \$21,000.00, commencing in or about August 15, 2000.

57. The Note provides that the "balance of principal and any outstanding interest as well as any other sum remaining unpaid on this Note shall be paid in full no later than August 15, 2002."

58. The Note further provides that FSIM would be in default thereunder if, among other things, FSIM "fails to pay any principle or interest on this Note when it becomes due and payable, or Debtor fails to pay any other cost, fee, expense or other amount owing to [Platinum Indemnity] under the Note[.]"

59. The Note expressly authorized Platinum Indemnity to assign its rights thereunder to any third party with or without FSIM's consent.

**DHIS's Failure to Make Payments Due
To FIC Under the Agency Agreement**

60. On or about November 10, 1999, FIC placed DHIS on notice of its intention to terminate the Agency Agreement.

61. The Agency Agreement, in fact, was terminated effective January 1, 2000.

62. The Agency Agreement was terminated due, in part, to DHIS non-compliance with the FSIM Program's underwriting guidelines and other provisions of said agreement.

