UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

In re: Chapter 7 Case

SRC Holdings Corporation, BKY Case Nos. 02-40284 to 02-40286
f/k/a Miller & Schroeder, Inc.
and its subsidiaries, Jointly Administered

Debtor.

Brian F. Leonard, Trustee, ADV Case No. 03-4284

Plaintiff,

v.

Executive Risk Indemnity, Inc.

Defendant.

The Marshall Group, Inc., Jerome A. Tabolich, James E. Iverson, Edward J. Hentges, Kenneth R. Larsen, Steven W. Erickson, Paul R. Ekholm, and Mary Jo Brenden,

Intervenors.

NOTICE OF HEARING AND MOTION FOR PARTIAL SUMMARY JUDGMENT

To: Entities Specified in Local Rule 9013-3

1. Brian F. Leonard, Trustee, and Plaintiff herein (**"Plaintiff"**), by and through his undersigned attorneys, moves the Court for the relief requested below and gives notice of hearing.

2. The Court will hold a hearing on this motion at 10:30 a.m. on December 16, 2004,

before the Honorable Nancy C. Dreher, in Courtroom 7, U.S. Courthouse, 300 South Fourth Street, Minneapolis, Minnesota.

3. Any response to this Motion must be filed and delivered no later than November 12, 2004 which is thirty-four (34) days before the time and date set for the hearing, or mailed and filed by November 9, 2004 which is thirty-seven (37) days prior to the hearing. **UNLESS A RESPONSE OPPOSING THE MOTION IS TIMELY FILED, THE COURT MAY GRANT THE MOTION WITHOUT A HEARING.**

4. This Court has jurisdiction over this Motion pursuant to 28 U.S.C. §§ 157 and 1334, Fed. R. Bankr. P. 5005 and Local Rule 1070-1. This proceeding is a core proceeding. The complaint commencing this adversary proceeding was filed on October 1, 2003. The case is now pending in this court.

5. This Motion arises under Bankruptcy Rule 7056 and Local Rule 9013. This Motion is filed under Bankruptcy Rule 9014 and Local Rules 7007-1, 9006-1, 9013-1, 9013-2 and 9017-1. Movant requests an order granting Plaintiff's partial summary judgment on all Counts in this matter.

6. This Motion is based upon the attached Memorandum of Law in Support of Motion for Summary Judgment, Affidavit of Thomas C. Atmore, and upon the files, records and proceedings herein, as well as the arguments of counsel.

WHEREFORE, Plaintiff requests that the Court enter an Order as follows:

1. Granting Plaintiff partial summary judgment declaring that the subject insurance policy provides coverage for the indemnifying claims; and
2. For such other relief as is just and equitable.

LEONARD, O'BRIEN
SPENCER, GALE & SAYRE, LTD.

Dated: October 29, 2004

By /e/ Thomas C. Atmore

Thomas C. Atmore, #191954
Matthew R. Burton, #210018
Attorneys for Plaintiff
100 South Fifth Street
Suite 2500
Minneapolis, Minnesota 55402
(612) 332-1030

@PFDesktop\::ODMA/GRPWISE/GWDSTP.GWPOSTP.STPLIB1:313744.1

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ADV Case No. 03-4284

PLAINTIFF'S MEMORANDUM IN SUPPORT OF MOTION FOR PARTIAL SUMMARY JUDGMENT

The Marshall Group, Inc., Jerome A. Tabolich, James E. Iverson, Edward J. Hentges, Kenneth R. Larsen, Steven W. Erickson, Paul R. Ekholm, and Mary Jo Brenden,

Intervenors.

INTRODUCTION

The Heritage Bond claims made against Miller & Schroeder and its officers and directors fall squarely within the coverage afforded by the policy and, in particular, Endorsement No. 9.

Plaintiff is entitled to summary judgment on his request that the Court declare that the policy

provides coverage for the Heritage Bond claims.[1]

When this case began, Executive Risk Indemnity, Inc. ("Executive Risk") responded to the Complaint by filing a motion to dismiss on the grounds that the "Securities Exclusion" precluded coverage. At the hearing on the motion, the Court asked counsel for each side to discuss the underlying insurance policy in its entirety and explain whether coverage would or would not be available for the Heritage Bond claims. Executive Risk chose to focus on the "Securities Exclusion" and did not fully address the other endorsement at issue, Endorsement No. 9 the "General E&O Exclusion (with Management Carveback)." Now, after extensive discovery has been conducted and the depositions of Executive Risk'S claims examiners have been taken, the reason why Executive Risk avoided Endorsement No. 9 and sought to focus attention on the Securities Exclusion has become clear. Executive Risk's position on Endorsement No. 9, and its interaction with the Securities Exclusion, has changed over time. It was not until Executive Risk realized that it would be faced with paying out the entire limit of the policy that it decided that Endorsement No. 9, and its management carveback, could never provide coverage. Executive Risk's interpretation of Endorsement No. 9, however, defies logic and is contrary to the plain language of the endorsement. Executive Risk's internal communications, as opposed to its current position, moreover, establish that the intent of the

[1] The purpose of the present motion is to establish that there is coverage for the claims. The next step, allocation of that coverage, is an issue that remains for resolution once coverage is established.

carveback was to provide coverage for claims like those made the Heritage Bond bondholders.[2]

FACTUAL BACKGROUND

The facts are undisputed, but a detailed recitation is necessary to an understanding of the insurance policy at issue and why it provides coverage.

A. MI Acquisition Corp. Purchases the Policy in 1997

In 1997, MI Acquisition Corporation, headed by James Dlugosch, purchased the stock of Miller & Schroeder, Inc. and took over the company and its subsidiaries. Ex. A (Deposition of James F. Dlugosch) to Affidavit of Thomas C. Atmore at 19-20.[3] Mr. Dlugosch and the other directors considered it important to have insurance protection for the officers and directors of the company. *Id*. at 36-37. The purpose in obtaining the insurance was to protect the officers and directors from suits by customers. *Id*. at 37. MI Acquisition used The Hays Group, a retail insurance broker; The Hays Group worked through a wholesale broker, ARC Excess and Surplus ("ARC"); and one of ARC's principals, Richard Fierstein, contacted Executive Risk. Ex. B (Deposition of Richard Fierstein) at 22-24, 28-31. ARC was Executive Risk's agent. *Id*. at 24.

Michael Watts, the Executive Risk underwriter, worked with Mr. Fierstein in negotiating

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[2] Both sets of intervenors have also moved for summary judgment on the issue of coverage. Although the parties' interests may diverge after coverage is declared and the focus turns to the allocation of the limited coverage, Plaintiff joins in and adopts the arguments of the Intervenors regarding coverage.

[3] With two exceptions, all exhibits are attachments to the Atmore Affidavit. Reference will only be made to the exhibit letter, the deponent or deposition exhibit (if applicable), and the page(s) of the exhibit, rather than repeatedly reciting that the exhibits are attached to the affidavit. The exceptions will be clearly identified.

the terms of the D&O policy. Neither Mr. Watts nor Mr. Fierstein could recall any details of the transaction. *Id*. at 31; Ex. C (Deposition of Michael Watts) at 36.

Executive Risk, after receiving an application and other information via The Hays Group and ARC, submitted a proposal to ARC. Ex. D (Watts Dep. Ex. 5). Executive Risk's D&O policy was called The POWER. Ex. E (Watts Dep. Ex. 1). According to Mr. Fierstein, a D&O policy like The POWER was intended to cover a variety of claims, including customer lawsuits. Ex. B (Fierstein Dep.) at 8. There were a number of standard endorsements to the policy, including the securities exclusion and the general E&O exclusion. Ex. C (Watts Dep.) at 21-22. The securities exclusion was intended to preclude claims made against the insureds arising out of sales of the insured company's stock. In fact, Mr. Fierstein testified that the understanding in the insurance industry is that a "Securities Exclusion" is designed to exclude coverage for claims arising from an insured's Initial Public Offering. Ex. B (Fierstein Dep.) at 42-43. The general E&O exclusion, meanwhile, was intended to preclude coverage for errors and omissions type liability, but, of course, in the present case the endorsement included a "management carveback."

There was limited negotiation of the terms and scope of the endorsements. First, the parties added an endorsement that allowed coverage for any claims that might arise out of a specific private placement of Miller & Schroeder stock in May of 1997. Ex. E (Watts Dep. Ex. 1). Second, as to the E&O exclusion, the parties changed it from a general, broad exclusion to one that listed the specific services that were subject to the exclusion and also included the "management carveback," bringing back into coverage claims against an insured based upon the alleged failure to supervise any subsidiary, group or division. Ex. F (Watts Dep. Ex. 7).

Executive Risk agreed to bind coverage and then issued a policy. *Id*., and Ex. G (Watts Dep. Ex.11).

The 1997 policy was effective from July 1997 to July 2000, when it was renewed, without substantive change, for another three years. Ex. H. In 1999, however, Executive Risk was purchased by Chubb Insurance Group. Ex. C (Watts Dep.) at 57-58. Mr. Watts left the company. *Id*.

Mr. Dlugosch and Tom Nelson, the two people involved in obtaining the policy on behalf of MI Acquisition Corp., both testified that they understood the policy, and in particular the "management carveback," to provide coverage for claims like those made by the Heritage Bondholders. Ex. A (Dlugosch Dep.) at 47-48 and Ex. I (Deposition of Tom Nelson) at 57.

B. <u>The Policy</u>[4]

The renewed POWER "Directors and Officers Liability Insurance Policy" (the "Policy") was in effect from July 31, 2000 to July 31, 2003. Ex. H at p. 1. The "Parent Corporation" listed on the Declarations is "Miller & Schroeder, Inc." *Id*. Miller & Schroeder, Inc. paid for coverage for claims made against officers and directors and for claims made against the insured companies (the latter is referred to as "Insuring Agreement (B)(2)"). *Id*. *See also* Section I of the Policy. *Id*. at p. 3. The liability limit is $5,000,000, inclusive of defense costs, and there are retentions of $50,000 for Company indemnification and $100,000 for claims directly against the Company. *Id*. at p. 1. The Policy is a "claims made" Policy, meaning that it provides coverage if the claim is first made during the Policy period. *Id*.

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[4] This section is taken virtually verbatim from Plaintiff's Response to Executive Risk's Motion to Dismiss.

The "Insuring Agreement" provides, in relevant part:

> (B) The Underwriter will pay on behalf of the **Company**:
>
> > (1) **Loss** from **Claims** first made against the **Insured Persons** during the **Policy Period** for **Wrongful Acts**,...if the **Company** pays such **Loss** to or on behalf of the **Insured Persons** as indemnification; and
> >
> > (2) (OPTIONAL COVERAGE) if it is stated in the Declarations that coverage has been made available under this INSURING AGREEMENT (B)(2), **Loss** from **Claims** first made against the **Company** during the **Policy Period** for **Wrongful Acts**,...
>
> (C) As a part of and subject to the limit of liability stated in ITEM 3 of the Declarations, <u>the Underwriter will have the right and duty to defend any **Claim** as described in INSURING AGREEMENTS (A) and (B)(1)(and, if it is stated in the Declarations that coverage has been made available thereunder, INSURING AGREEMENT (B)(2)), even if such **Claim** is groundless, false or fraudulent.</u>

Id. at ¶ I, p. 3 (bold in original; underline supplied). Executive Risk, then, agreed to both pay any covered loss and defend its insureds against any covered claims.

The terms in bold above are defined terms in the Policy. The "**Company**" is defined as Miller & Schroeder, Inc. and its subsidiaries. *Id*. at II(C), p. 4 "**Insured**" means the **Company** and any "**Insured Person**." *Id*. at II(F), p. 4. An **Insured Person** is, for purposes of the subject claims, "any past, present or future director or officer of the **Company**..." *Id*. at II(G)(1), p. 4.

"**Loss**" is defined as any defense expenses and any "damages, judgments, settlements or other amounts" that the insured has to pay as a result of a **Claim**. *Id*. at II(H), p. 5. A "**Wrongful Act**" is, for our purposes, defined as "any actual or alleged act, error, omission, misstatement, misleading statement or breach of duty by an **Insured Person** in his or her capacity as a director or officer of the **Company**...." <u>and</u> "any matter asserted against an **Insured Person** solely by reason of his or her status as a director or officer of the **Company**..." *Id*. at

II(M)(2) and (3), p. 5.

The "Securities Exclusion" attempts to exclude from coverage any claims brought under Federal and State securities laws and any common law relating to the "offer, sale or purchase of securities." *Id*. The exclusion carefully lists the "Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, any other federal law, rule or regulation with respect to the regulation of securities, any rules or regulations of the United States Securities and Exchange Commission...." *Id*. at ¶(1). Note that the rules and regulations of the National Association of Securities Dealers are **not** listed, nor are the rules of the Municipal Securities Regulation Board.

The "Securities Exclusion" is modified by "Endorsement No. 6 Limited Securities Coverage Endorsement" which allows coverage for any claims arising out of the "offering, sale or purchase" made in a "Private Placement" of stock that occurred on May 20, 1997. *Id*. at p. 21.

The final "endorsement" of relevance to the present case is "Endorsement No. 9 General E & O Exclusion (with Management Carveback)." *Id*. at p. 25. This exclusion provides that there is no coverage for claims against an insured based on the "actual or alleged rendering or failure to render" certain listed services. *Id*. at ¶(1). The services listed are: "Investment Banking Services, Securities Broker/Dealer Services, Securities Underwriting." *Id*. The exclusion is limited by a "management carveback," that provides coverage for claims arising out of the listed services made against "an Insured to the extent such Claim is for a Wrongful Act by Insured Person in connection with the management or supervision of any division, Subsidiary or group of the Parent Corporation offering any of the aforementioned services." *Id*. at ¶(2).

C. <u>The Heritage Bonds</u>

The present dispute arises out of Executive Risk's refusal to provide a defense, provide coverage, or reimburse defense costs incurred by Miller & Schroeder in defending what has come to be known as the "Heritage Bond Litigation."

The Solano Beach office of Miller & Schroeder Financial, Inc. underwrote and sold $140,000,000 worth of bonds, all of which were defaulted upon. Miller & Schroeder customers lost anywhere from thousands to millions of dollars and initiated suits and arbitration proceedings naming the Miller & Schroeder entities, the employees who handled the bond sales, and the various officers and directors of Miller & Schroeder.

The majority of the claims were asserted in NASD arbitration proceedings. *See e.g.*, Exs. 4 and 5 to the Affidavit of John M. Anderson dated November 14, 2003 and on file herein. Miller & Schroeder, Inc. and/or Miller & Schroeder Financial, Inc. were named in virtually every arbitration, as were a variety of officers and directors, whether or not they had any direct participation in the bond sales. *Id*. They were also named because they served on the Credit Committee that had a supervisory role over the underwriter selling the bonds. Ex. I (Nelson Dep.) at 38-40, 63.

The NASD arbitrations involve claims that Miller & Schroeder violated NASD rules, including the rule requiring that Miller & Schroeder properly supervise its brokers. *See e.g.*, Ex. J. The NASD rules also provide that investments recommended to customers must be suitable for that customer and his or her goals and circumstances. *Rule 2310 of NASD Rules*. The Heritage Bond customers routinely alleged that the bond investments, because they were speculative and high risk, were not suitable. *See e.g.*, Ex. J. The claimants in arbitration also alleged that Miller & Schroeder violated Municipal Securities Regulation Board rules. *See e.g.*,

Ex. K; and Ex. 4 to Anderson Affidavit at p. 20.

The lawsuits remain pending. Some arbitrations have reached resolution and in each one that has, the result has been an award in favor of the claimants and the arbitrators have, among other things, concluded that Miller & Schroeder failed to supervise its brokers. *See e.g.,* Ex. J. Most of the bondholders have also made claims in the bankruptcy estate. *See* e.g., Ex. K-1.

It appears that Miller & Schroeder, prior to filing for bankruptcy, incurred and paid in legal fees of approximately $735,658.65 defending the various actions and became liable for millions in dollars in damages. Ex. L; *see also* Atmore Aff. at ¶11. Executive Risk has not provided a defense to any of the claims and has not paid any of the awards. The former Miller & Schroeder entities were driven into bankruptcy as a result of the mounting fees and exposure to liability.

Executive Risk has repeatedly admitted that the Heritage Bond claims are "claims" under the Policy. *See e.g.,* Ex. M. The sole basis for denial of coverage has been the two exclusions at issue. Ex. N (Deposition of Joel Townsend) at 45.

D. <u>Executive Risk's Claims Handling and Interpretations of the Policy</u>

It does not appear that there were any claims made under the Policy prior to the 2000 renewal. After the renewal, however, claims were made under the policy that gave Executive Risk, now owned by Chubb, an opportunity to address the securities exclusion and the management carveback. Several claims examiners were involved in addressing the coverage issues.

1. <u>Cheryl O'Malley</u>

In late 2001, a claim was made against Miller & Schroeder arising out of a sale of participations in a casino loan and Miller & Schroeder tendered the claims to Executive Risk for defense and coverage. Ex. O (Deposition of Cheryl O'Malley) at 9-10; *see also* Ex. P (O'Malley Dep. Exs. 1-9). Claims were made in the underlying case against two officers of Miller & Schroeder who had no involvement in the transaction, but who had supposedly failed to supervise the involved employees. *Id*. The claim was assigned to Cheryl O'Malley, a claims examiner in Chubbs' Pittsburgh office. Ex. O (O'Malley Dep.) at 5-6.[5] Ms. O'Malley, a lawyer, discussed the policy language with broker and, when the broker raised the issue of the management carveback and its application to the claims against the officers, Ms. O'Malley struggled with its language. Ex. P at 1-2. Initially, she determined that the claim did not invoke coverage because the officer had some involvement in the underlying transaction. *Id.* at 2. She then decided that she needed to discuss the intent of the carveback with an underwriter. *Id.* at 1. (Note, this was <u>not</u> the underwriter involved in issuing the initial policy.)

The Chubb underwriter responded by indicating that the intent of the carveback was to cover only "vicarious liability" situations. *Id*. Ms. O'Malley then concluded that Executive Risk might have to defend the case with a "reservation of rights." *Id*.

At about this same time, however, the Heritage Bond claims were coming into Executive Risk. Executive Risk soon realized that there were going to be a significant number of these claims. It was decided that all claims would be assigned to Carrie Campi, a claims examiner in

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[5] Ms. O'Malley had no independent memory of her claims handling. Ex. O at 11, 21-23, 25-30, 47. Her contemporaneous notes and letters provide the only evidence of her thought process and claims handling. Ex. P (O'Malley Dep. Exs. 1-9).

Simsbury, CT. *Id*. at 3. Joel Townsend, claims counsel for Chubb, became involved. Ms. Campi and Mr. Townsend had a conference call with Ms. O'Malley in January 2002.[6] None of the participants could recall the conversation, but Ms. O'Malley made a record in her claims notes:

> Conference call with Carrie Campi and Joel Townsend in late Dec to discuss Miller & Schroeder E&O Exclusion; all new claims will go to Carrie in Simsbury. Joel explained that E&O exclusion not intended to carve back E&O for supervisors; **doesn't make sense**.

Id. (emphasis added). *See also* Ex. Q (Deposition of Carrie Campi) at 51-52.

Ms. O'Malley then contacted the broker and told him that a denial of coverage letter would be coming soon. Ex. P at 3. She had the letter reviewed by Mr. Townsend before it was sent. *Id.* The letter was sent a few days later. *Id*. In discussing Endorsement No. 9, Ms. O'Malley first noted that she believed the allegations in the underlying complaint indicated that the subject officer was directly involved in the underlying transaction. She then wrote:

> For the exception to the General E&O exclusion to apply, a Claim must involve allegations of a Wrongful Act *in connection with the management or supervision of* a division, subsidiary of group. The purpose of the exception is clear from this language - a claim against an insured director or officer for breach of duty owed as a manager/supervisor - ...would not be excluded **simply by virtue of the fact that the unit engages in investment banking transactions**.

Id. at p. 8 (italics in original; bold added). In short, Ms. O'Malley believed that the exclusion, as indicated to her by the underwriter, would allow coverage for "vicarious liability" situations. (The coverage is actually broader than that (*See* definition of "Wrongful Act" in the policy).

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[6] By this time, as Executive Risk knew, the former Miller & Schroeder entities were seeking bankruptcy protection.

Before they were consolidated with Ms. Campi, a Heritage Bond claim was assigned to one of the "technical supervisors" at Chubb. Technical Supervisors have more experience than claims examiners. Ex. O (O'Malley Dep.) at 41. The Supervisor wrote a memorandum to the file that includes a discussion of Endorsement No. 9 (referred to as 11) and its application to a claim of "failure to supervise" under the NASD rules. She provided the memo to Ms. O'Malley. Ex. P at 19. The memo is important because it indicates how Executive Risk/Chubb interpreted the securities exclusion and management carveback together and because of how Executive Risk, at that time, interpreted the management carveback. The memo concludes:

> Endorsement No. [9] deals with the management or supervision of a specific division or part of the parent corporation and not employee supervision. Thus, the carveback...is not applicable to this matter and the exclusion for securities claims...serves to exclude this matter.

Id. at 22. Executive Risk, then, recognized that the management carveback would override the securities exclusion.[7] It was only because Executive Risk, incorrectly, decided that the supervision claim was employee specific that it then concluded that securities exclusion would preclude coverage.

2. <u>Carrie Campi</u>

As noted above, the Heritage Bond claims were eventually centralized with Ms. Campi. Her deposition testimony needs to be reviewed in some detail.[8]

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[7] Note that even on this point, Executive Risk is incorrect. As Mr. Fierstein noted, the "Securities Exclusion" is intended to preclude coverage for the insured's sale of the insured's stock. It was not intended as a blanket exclusion for all of Miller Schroeder's activities.

[8] It should also be noted that on October 28, 2004, one day before this memorandum was due and over a month after Ms. Campi's deposition, Executive

Ms. Campi, like Ms. O'Malley and Mr. Townsend, is a lawyer. Ex. Q at p. 7. Ms. Campi started with Chubb in August of 2000. *Id*. In handling the Heritage Bond claims and the subject policy, she indicated that she would review the claim, review the policy, and determine if the claim was, in fact, a claim. *Id*. at 14. She would then look for any exclusions and discuss the claim with her supervisor. *Id*. She may also consult with the underwriter, but she noted that in this case, he was no longer with the company. *Id*. at 17. She noted that it was somewhat unique to see the subject policy with a "financial institution" as the insured, as opposed to a "small family run private business[]." *Id.* at 19 and 22.

In discussing the E&O exclusion, she agreed that in the absence of the exclusion, coverage might be available for E&O claims under the other language of the Policy. *Id*. at 26-27. In discussing the definition of Wrongful Act, she agreed that the officers and directors, as such, could have coverage for E&O claims. *Id*. at 28. She also agreed that the "management carveback" limits the exclusion in Endorsement No. 9. *Id*. at 30-31.

She then explained the reasoning behind Executive Risk's denial of coverage under Endorsement No. 9, by indicating that the allegations did not involve the management or supervision of a division, subsidiary or group, but instead involved the "management of individuals and specific activities. The sale of Heritage Bonds." *Id*. at 33. Ms. Campi said that the carveback might provide coverage for "A shareholders' suit." *Id*. at 36. As long as a customer claim involved a "particular transaction" she did not believe the carveback would

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Risk produced one hundred and thirty pages of new documents, the last of which is a four page document containing Ms. Campi's initial claims handling notes. Ex. R. These notes contradict Ms. Campi's deposition testimony and clearly show that she, like Ms. O'Malley, thought the management carveback would provide coverage.

allow for coverage. *Id*. at 37.

In discussing the fact that the definition of Wrongful Act contains "errors, omissions," Ms. Campi first said that she thought that language was different from "errors and omissions," but then agreed that "It could be the same." *Id*. at 54-55. She also ultimately agreed that "how people interpret [Endorsement No. 9] can be different." *Id*. at 55. She refused to say whether Plaintiff's interpretation of Endorsement No. 9 was or was not reasonable, saying she never considered the question. *Id*. at 57-58.

Ms. Campi then discussed in more detail her current notion of why the carveback would not apply in the Heritage Bond situation. Unlike Ms. O'Malley, Ms. Campi's focus was on the transaction. She concluded that even though there "may have been five different people selling the bonds to different people but only one person was doing the one transaction with whoever they sold the bonds to." *Id*. at 56. She concluded that if the claim involved a "specific sale" there was no coverage, even if the officer or director played no role in the transaction. *Id*. at 59. When pressed as to how that position was consistent with the definition of Wrongful Act, she stated that now the issue was whether the officer or director was "responsible for the liability occurring from whatever wrongful act that occurred with regard to the sales." *Id*. at 60-63. In the end, she could not explain what she meant or whether the officer had to be involved or responsible for the sale. *Id.* at 63-65.

As noted above, Ms. Campi's initial claims handling notes were not produced until long after her deposition. Her comments in those notes are in stark contrast to her deposition testimony and, perhaps, explain why Ms. Campi had difficulty explaining her position at her deposition.

In November 2001, before all the claims were consolidated and before Joel Townsend got involved, the Spanglor Heritage Bond claim was assigned to Ms. Campi. Ex. R. Ms. Campi noted that Mr. Dlugosch was named in the demand for arbitration because he was "M&S CEO and a control person." *Id*. at 1. Ms. Campi then noted:

> Coverage Issues:
>
> The E&O exclusion precludes coverage for Hill and M&S. There is a management carveback that would at least possibly trigger the duty to defend for Dlugosch.

Id. Ms. Campi later spoke with Ken Larson from Miller & Schroeder, telling him Executive Risk would be appointing counsel for Mr. Dlugosch. *Id*.

Ms. Campi, a few days later, realized that there would be more of these claims and that "this account could hit fairly hard." *Id*. at 2. She notified the Chicago office and also sent an email to all other claims examiners. *Id*.

Still later, she comments on the "broad form securities exclusion" and notes that she is "calling the underwriters to discuss the intent between the securities exclusion and the E&O exclusion with a management carveback." *Id*. Ms. Campi discusses the claims with another claims examiner, and notes that the securities exclusion "might be inconsistent with the management carveback..." *Id*.

Soon, though, Ms. Campi has discussed the claims with Joel Townsend, who tells her that all claims are excluded, regardless of any supervision claims. *Id*. (In an email, Ms. Campi notes that Mr. Townsend said "...the intention behind the E&O endorsement carveback was to allow claims for mismanagement as made by shareholders not clients." Ex. S at 2). A conference call is held and it is agreed that Ms. Campi will handle all the claims and that all the

claims will be denied. *Id*.

3. <u>Joel Townsend</u>

Mr. Townsend also testified as to his interpretation of Endorsement No. 9. Mr. Townsend is claims counsel and supervises the claims examiners. He decided that the claims examiners were wrong and that the management carveback did not provide coverage. Mr. Townsend thought that Endorsement No. 9 was clear "on its face." Ex. N at 35, 44. He agreed, though, that absent the E&O exclusion, "others" might conclude that the policy provides some E&O coverage. *Id*. at 38-39, 42. He also agreed that the purpose of the carveback was to limit the exclusion. *Id*. at 46. His conclusion, though, was that the carveback did not bring back into coverage any claims that may be covered under the exclusion in paragraph 1, but instead that the carveback, despite that it lacks any such limiting language, served only to allow coverage for shareholder suits and breach of fiduciary duty claims. *Id*. at 51-52. In other words, unlike Ms. O'Malley and Ms. Campi, Mr. Townsend's focus was on the nature of the activity. If the underlying activity involved one of the three services listed in the exclusion, the carveback did nothing to limit the exclusion. Mr. Townsend, though, did not have an understanding of the specific claims alleged in the Heritage Bond arbitrations and suits. *Id*. at 50-51, 64-65.

Mr. Townsend, however, agreed that if the basis for the claim against the officer or director was simply that they were an officer and director, paragraph 1 of the E&O exclusion would not prevent coverage and there would be no need to look at the carveback. *Id*. at 54-55.

4. <u>Sherri McKelvey</u>

Sherri McKelvey took over the Heritage Bond claims handling from Ms. Campi. Ms.

McKelvey, also a lawyer, started with Chubb in October 2002. Ex. T (Deposition of Sherri McKelvey) at 6, 9. She did not review all of the complaints. *Id*. at 37. Ms. McKelvey concluded, under the guidance of Mr. Townsend, that any and all "E&O claims" are excluded by Endorsement No. 9, regardless of the management carveback. *Id*. at 53. (This appears to be Executive Risk's current position, being advanced in defense of this case). Ms. McKelvey, who started at Chubb five years after Endorsement No. 9 was negotiated and written and who did not talk to the involved underwriter, or any underwriter, then opined as to what Executive Risk intended to do in Endorsement No. 9. *Id*. at 54, and 107-108. She testified, though, that she had no basis for her statement as to the intent behind the Endorsement. *Id*. at 109.

Ms. McKelvey, like Mr. Townsend, also concluded that the carveback essentially had nothing to do with the exclusion. *Id*. at 55, 64. Ms. McKelvey explained that the failure to supervise claims like those made in the Heritage Bond cases were not covered because "it's not with respect to the management of the company, it's the management of those securities." *Id*. at 59-61.

Ms. McKelvey's position led her to admit that in the Heritage Bond cases "there are certainly allegations for management of the group." *Id*. at 67-68. She also agreed that the officers and directors were not alleged to have individually sold the securities. *Id*. at 68. For Ms.

McKelvey, though, that fact did not matter, as the claims involved the listed services and "improper securities." *Id*. at 67-68.

Despite that she had earlier testified that Endorsement No. 9 does not cover errors and omissions claims, Ms. McKelvey, when presented with the definition of Wrongful Act and its

inclusion of "errors, omissions", decided that some "errors" would be covered. *Id*. at 102. She could not remember reading the definition or other parts of the Policy. *Id*. at 104-106.

ARGUMENT

The Policy provides coverage for the Heritage Bond claims made against the Miller & Schroeder entities and the officers and directors for failure to supervise the Solano Beach office and the Sales Division of the Company. Executive Risk was obligated to provide a defense and to pay any resulting awards or judgments.

Neither of the two exclusions eliminate coverage. The "Securities Exclusion" does not defeat coverage. A complete reading of the Policy, the claims handling notes, and Mr. Fierstein's testimony all lead to the conclusion that the exclusion is intended to exclude only claims based on sales of stock by the company and its officers and directors, and not the brokering of securities. As the Executive Risk claims examiners realized, moreover, there is conflict between the securities exclusion and the management carveback. Endorsement No. 9, meanwhile, far from precluding coverage, expressly preserves coverage for the Heritage Bond claims.

I. STANDARD FOR SUMMARY JUDGMENT

Bankruptcy Rule 7056 provides that Rule 56 of the Federal Rules of Civil Procedure applies in adversary proceedings in bankruptcy cases. Rule 56 states:

> That judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.

Summary judgment plays a very important role in the judicial proceedings by allowing the judge to "pierce the pleadings and to assess the proof in order to see whether there is a genuine need for trial." Fed. R. Civ. P. 56, Advisory Committee note. Summary judgment is properly regarded not as a disfavored procedural shortcut, but rather as an integral part of the federal rules as a whole, which are designed "to secure the just, speedy and inexpensive determination of every action." *Celotex Corp. v. Catrett*, 477 U.S. 317, 327 (1986).

The initial burden is on the party seeking summary judgment. To that end, the movant discharges its burden by showing that the record does not contain a triable issue and by identifying that part of the record which supports the moving party's assertion. *Id.*, 477 U.S. at 323; *City of Mt. Pleasant, IA v. Assoc. Electric Co-op, Inc.* 838 F.2d 268, 273 (8th Cir. 1988). Once the movant has made its showing, the burden of production shifts to the non-moving party. The non-moving party must present specific, significant and probative evidence supporting its case, *Johnson v. Enron Corp.*, 906 F.2d 1234, 1237 (8th Cir. 1990), which is sufficient enough "to require a judge to resolve the parties' different versions of the truth at trial." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 249 (1986) (quoting *First National Bank of Arizona v. Cities Service Co.*, 391 U.S. 253, 288-89 (1968)).

II. APPLICABLE RULES FOR CONSTRUING THE POLICY

It is "settled law in Minnesota" that the Policy must be construed as a whole and any doubts about the meaning of its language resolved in favor of the insured. *Sphere Drake Ins. PLC v. Trisko,* 24 F.Supp.2d 985, 991 (D. Minn. 1998); *See also Watson v. United Services Automobile Association,* 566 N.W.2d 683,692 (Minn. 1997); *Henning Nelson Constr. Co. v. Firemans' Fund Amer. Life Ins. Co.,* 383 N.W.2d 645,652 (Minn. 1986); *Canadian Universal*

Ins. Co., Ltd. v. Fire Watch, Inc., 258 N.W.2d 570, 572 (Minn. 1977). Any ambiguity is construed against the insurer. *Sphere Drake,* supra at 991. *See also American Commerce Ins. Brokers, Inc. v. Minnesota Mut. Fire and Cas. Co.,* 551 N.W.2d 224, 227 (Minn. 1996). Exclusions, in particular, are strictly construed against the insurer and when a claim is arguably within the policy's coverage, the insurer must prove that the exclusion applies. *Sphere Drake,* supra at 992 *citing Columbia Heights Motors, Inc. v. Allstate Ins. Co.,* 275 N.W. 2d 32, 35 (Minn. 1979); *Caledonia Community Hosp. v. St. Paul Fire & Marine Ins. Co.,* 307 Minn. 352, 354, 239 N.W.2d 768, 770 (Minn. 1976).

Where, as here, the policy includes a duty to defend, the insurer also has the obligation to establish that no claim even arguably fits within the coverage provided by the policy, because the duty to defend is broader than the duty to indemnify. *Meadowbrook, Inc., et. al. v. Tower Insurance Company, Inc.*, 559 N.W.2d 411, 415 (Minn. 1997). If any one of multiple claims involves coverage, the insurer must defend the entire case. *See Brown v. State Auto. & Cas. Underwriters,* 293 N.W.2d 822 (Minn.1980). *See also, U.S. Fidelity and Guaranty Co. v. Louis A. Roser Co., Inc.,* 585 F.2d 932 (8th Cir. 1978). As the Court suggested in *Piper Jaffray Companies, Inc.*, when the task involves determining and giving effect to the parties' intent, the Court must look to both the circumstances surrounding the purchase of the Policy and any subsequent interpretations of the Policy by the parties. *Id*. at 1154.

III. THE POLICY PROVIDES COVERAGE FOR THE HERITAGE BOND CLAIMS.

The Policy provides coverage for the Heritage Bond claims. Executive Risk agrees that the Heritage Bond claims are "Claims" under the policy and also agrees that the Miller & Schroeder entities and the officers and directors are "Insureds." The focus, then, is the

"Management Carveback." It is Executive Risk's burden to prove that an exclusion applies and, regarding the duty to defend, to prove that no claims are even arguably covered. Executive Risk cannot make the required showing.

An understanding of the carveback begins with the definition of "Wrongful Act." As noted above, the definition of Wrongful Act includes:

> (2) any other actual or alleged act, error, omission, misstatement, misleading statement or breach of duty by an Insured Person in his capacity as a director or officer of the Company;
>
> (3) any matter asserted against an Insured Person solely by reason of his or her status as a director or officer of the Company;...

Ex. H at 5. An officer or director, then, that commits an error or omission or breach of duty commits a Wrongful Act. If a claim is made against an officer or director solely because he or she is an officer or director, that officer or director has also committed a Wrongful Act. The Policy provides coverage for losses arising out of Wrongful Acts.

The first paragraph of Endorsement No. 9, takes out of coverage a Wrongful Act as defined in paragraph (2) above, as the endorsement excludes claims involving the actual or alleged rendering of the listed services, to the extent that the officer or director has actually or allegedly rendered those services. The carveback, however, leaves in coverage a Wrongful Act as defined in paragraph (3) above, if the "...Wrongful Act [is] by an Insured Person in connection with the management or supervision of any division, Subsidiary or group of the Parent Corporation offering any..." of the listed services.

The language of Endorsement No. 9, then, allows for coverage if the insured is not involved in the actual or alleged rendering of the listed services or if the claim alleges errors, omissions, or breach of duty in managing or supervising a division, subsidiary or group. In other

words, the Policy contemplates coverage for claims against officers and directors arising out of their status as officers or directors or if they commit an error or omission or breach of duty in the exercise of their responsibilities as an officer or director. The Heritage Bond claims made against the company and the officers and directors fit squarely within the coverage provided.

The Heritage Bonds were underwritten and sold by Miller & Schroeder Financial, a subsidiary of Miller & Schroeder. *See* Ex. K. The vast majority of the sales were made through brokers in the Solano Beach, CA sales office. As Ms. McKelvey admitted, the allegations against the officers and directors relate to the management or supervision of a group. The allegations against the officers and directors, moreover, are either for "control person" liability or relate to the alleged failure to implement a system of supervision. The control person liability is based on the status of the officer or director and, thus, the claim is a covered claim under the Policy. The failure to supervise claims are based on the status of the officer or director and/or on the fact that the officer or director was a member of the Credit Committee.

As noted by Mr. Dlugosch and Mr. Nelson, it was the intent of the parties to cover Heritage Bond type claims. That such coverage would be provided was critical, according to Mr. Dlugosch, in MI Acquisitions' decision to purchase the policy. Neither the Executive Risk underwriter, Mr. Watts, nor the wholesale broker, Mr. Fierstein, had any recollection regarding the issuance of the policy. Subsequent interpretations of the policy by Executive Risk, as detailed above in the discussion of the claims handling by Chubb personnel, makes clear that the Chubb claims examiners, all of whom were lawyers, read the carveback as allowing coverage. It was not until Chubb realized that the policy might be "hit fairly hard" and Mr. Townsend became involved that Executive Risk decided the carveback provided no coverage. Prior to that,

Ms. O'Malley and Ms. Campi and other claims examiners were prepared to provide a defense to Mr. Dlugosch and to agree that the carveback allowed coverage.

The evidence shown in the claims handling notes, moreover, establishes not only that there should be coverage, but that the insureds (Miller & Schroeder and its officers and directors) had every reasonable expectation of coverage. *See Josten, Inc. v. Northland Ins. Co.*, 527 N.W.2d 116 (Minn. Ct. App. 1995) (Doctrine reasonable expectations protects insureds objectively reasonable expectations). While Ms. Campi refused to say whether she thought the insureds' interpretation was reasonable, her claims handling shows that she had the same interpretation.

These claims are covered by the Policy. Executive Risk had a duty to defend the claims and to cover any loss arising from the claims.

IV. THE EXCLUSIONS DO NOT DEFEAT COVERAGE

Executive Risk cannot meet its burden or proving that the two exclusions it has raised in denying coverage actually defeat coverage.

A. <u>The Securities Exclusion Does not Defeat Coverage</u>

Endorsement No. 3, the "Securities Exclusion" does not, for several reasons, defeat coverage. First, in the context of the entire Policy, the exclusion must be read as only excluding from coverage claims made against insureds relating to sales of company stock. Second, the exclusion does not mention NASD claims (or Municipal Securities Regulation Board claims) and, therefore, such claims are not excluded. Third, the exclusion is contradicted, and rendered ambiguous, by other language in the Policy.

The application of the Securities Exclusion was fully briefed and argued in the context of

Executive Risk's prior motion to dismiss. The detailed arguments set forth in Plaintiff's prior memorandum opposing that motion and the arguments made at the hearing on that motion will not be repeated here (but are incorporated herein by reference). Several facts brought to light during discovery, however, should be highlighted.

First, Mr. Fierstein, from ARC, confirmed during his deposition that Plaintiff's interpretation of the intent of the Securities Exclusion was correct. The purpose of the exclusion is to preclude coverage for claims arising from the sale of company stock. *See Quinlivan v. EMCASCO Ins. Co.*, 414 N.W.2d 494, 497 (Minn.Ct. App. 1987), citing *Taylor v. Security Mutual Fire Insurance Co.,* 88 Minn. 231, 92 N.W. 952 (1903) (Court can look to insurance industry trade usage in determining the meaning of policy language).

Second, the claims handling notes quoted above, and in particular Ms. Campi's claim handling notes, make clear that even Executive Risk recognized inconsistency between the Securities Exclusion and the management carveback. The problem arises from the fact that Miller & Schroeder was in the securities business. To exclude all claims that implicate securities law violations simply does not make sense.

B. <u>The E&O Exclusion Does Not Defeat Coverage</u>

Endorsement No. 9 cannot defeat coverage. To the contrary, as discussed above, the management carveback allows coverage for the Heritage Bond claims. Executive Risk's position, as expressed by Mr. Townsend, contradicts the language of the endorsement and is inconsistent with other language in the Policy.

Mr. Townsend's position is, essentially, that the carveback does not allow coverage for

claims that arise out the provision of listed services, but instead only allows claims wholly unrelated to the listed services. In fact, Mr. Townsend insists that the only claims allowed in by the carveback would be shareholder claims and employment claims. Mr. Townsend is incorrect for several reasons.

First, there is no such limitation of the carveback on the face of the endorsement. Had Executive Risk wanted to so limit the carveback, it could have easily included language to the effect that only shareholder claims and employment claims would result in coverage.

Second, Mr. Townsend's interpretation is contrary to everyone else's reading of the endorsement. Each Chubb claims examiner reading the policy before speaking to Mr. Townsend believed it allowed, to some extent, coverage and that it was not limited as Mr. Townsend suggests.

Third, employment claims are addressed, extensively, elsewhere in the policy as are shareholder claims. Ex. H at 3-6. Not only would Mr. Townsend's interpretation render the carveback redundant, but, again, had Executive Risk wanted to limit the carveback it could have easily included a reference to the sections of the policy dealing with employment claims and shareholder suits and could have used the defined terms found in those sections of the policy.[9]

CONCLUSION

The claims made by the Heritage Bond bondholders invoke the promise of coverage given in paragraph I(B), quoted above, and the promise of coverage given in the "management carveback" under Endorsement No. 9 and come within the definition of "Wrongful Act" found in

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[9] For example, Endorsement No. 8 refers specifically to the term "Employment Practices Wrongful Act" and includes it in the definition of "Wrongful Act" for the purposes of that endorsement.

paragraph II(M)(2) and (3) of the Policy. The claims arise directly out of the business of Miller & Schroeder and out of the rendering of the services listed in Endorsement No. 9, and are the reason that Miller & Schroeder needed the policy it purchased.

For the reasons set forth above, the Trustee respectfully requests that the Court deny the Defendants motion in its entirety.

LEONARD, O'BRIEN
SPENCER, GALE & SAYRE, LTD.

Dated: October 29, 2004

By /e/ Thomas C. Atmore

Thomas C. Atmore, #191954
Matthew R. Burton, #210018
Attorneys for Plaintiff
55 East Fifth Street
Suite 800
St. Paul, Minnesota 55101
(651) 227-9505

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UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

In re: Chapter 7 Case

SRC Holdings Corporation, BKY Case Nos. 02-40284 to 02-40286
f/k/a Miller & Schroeder, Inc.
and its subsidiaries, Jointly Administered

Debtor.

Brian F. Leonard, Trustee, ADV Case No. 03-4284

Plaintiff,

v.

Executive Risk Indemnity, Inc.

Defendant.

The Marshall Group, Inc., Jerome A. Tabolich, James E. Iverson, Edward J. Hentges, Kenneth R. Larsen, Steven W. Erickson, Paul R. Ekholm, and Mary Jo Brenden,

Intervenors.

AFFIDAVIT OF THOMAS C. ATMORE IN SUPPORT OF A PARTIAL SUMMARY JUDGMENT MOTION

Thomas C. Atmore, under penalties of perjury states as follows:

1. I am a shareholder at Leonard, O'Brien, Spencer, Gale & Sayre, Ltd., counsel for Plaintiff in the above-captioned matter and have personal knowledge of the facts stated herein.

2. Attached hereto as Exhibit A is a true and correct copy of selected pages from the Deposition of James F. Dlugosch..

3. Attached hereto as Exhibit B is a true and correct copy of selected pages from the Deposition of Richard Fierstein.

4. Attached hereto as Exhibits C, D, E, F, G are true and correct copies of selected pages from the Deposition of Michael Watts and select exhibits thereto.

5. Attached hereto as Exhibit H is a true and correct copy of the POWER Policy for policy period 2000-2003.

6. Attached hereto as Exhibit I is a true and correct copy of selected pages from the Deposition of Tom Nelson.

7. Attached hereto as Exhibit J is a true and correct copy of the *Second Amended Statement of Claim* in *Onderwyzer, et al. v. Miller & Schroeder Financial, Inc., et al.*

8. Attached hereto as Exhibit J1 is a true and correct copy of an NASD Award in *In re: Lundquist Family Trust*.

9. Attached hereto as Exhibit K is a true and correct copy *Statement of Claim* in *Edge v. Miller & Schroeder Financial, Inc.*

10. Attached hereto as Exhibit K1 is a true and correct copy the Baker Living Trust Proof

of Claim.

11. Attached hereto as Exhibit L is a true and correct copy the summary of the invoices from the Arthur, Chapman and Faegre & Benson law firms for defense of Heritage Bond claims (invoices voluminous and not attached).

12. Attached hereto as Exhibit M is a true and correct copy letter dated May 12, 2003 from Sherri McKelvey to Thomas C. Atmore.

13. Attached hereto as Exhibit N is a true and correct copy of selected pages from the Deposition of Joel Townsend.

14. Attached hereto as Exhibits O and P are true and correct copies of selected pages from the Deposition of Cheryl O'Malley and exhibits thereto.

15. Attached hereto as Exhibit Q, R, and S are true and correct copies of selected pages from the Deposition of Carrie Campi and select exhibits thereto.

16. Attached hereto as Exhibit T is a true and correct copy of selected pages from the Deposition of Sherri McKelvey.

Signed under penalties of perjury.

Dated: October 29, 2004 By /e/ Thomas C. Atmore

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EXHIBIT A

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Q Were you ever involved in decisions concerning insurance coverage for Dain Bosworth?
A No.
Q Do you know whether Dain Bosworth had D&O insurance?
A I don't know firsthand; I, I believe that they did, but I do not know for certain.
Q Do you know whether they had E&O insurance?
A No, they did not.
Q And how do you know that?
A Serving on the management committee, I became aware that they -- I, I was not -- to put it differently, I'm not aware that they had it. That's probably more accurately stated. It never came to our attention on the management committee.
Q So there was never any discussion about whether or not they had E&O insurance?
A That's correct.
Q After you left Dain Bosworth, where did you go?
A Miller & Schroeder.
Q Why did you leave Dain Bosworth?
A Just overall change in the management of the company.
Q And in 1990 you went to Miller & Schroeder?
A 1991 I went to Miller & Schroeder.
Q In 1991 was Miller & Schroeder a privately held company?

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A Yes.
Q What was your position at Miller & Schroeder in 1991?
A I was executive vice president.
Q How long were you in that position?
A Until 1997.
Q What were your responsibilities at Miller & Schroeder as executive vice president from 1991 to 1997?
A Business development, budgeting, personnel review and compensation.
Q In the position of executive vice president at Miller & Schroeder, did you have responsibility for insurance policies?
A No.
Q Did you participate in discussions about insurance policies?
A No.
Q Do you know whether between 1991 and 1997 Miller & Schroeder had D&O insurance?
A To the best of my knowledge, they did not.
Q Do you know whether they had E&O insurance during that period?
A To the best of my knowledge, they did not.
Q Do you know why they didn't have those policies?
A No.
Q Then in 1997, I gather you had a new position at

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Miller & Schroeder.
A That's correct.
Q What was the new position?
A I was president and CEO and chairman of the board.
Q Do you recall when in 1997 you got that position?
A June 30. It might be more accurate July 1.
Q Am I correct there was some kind of a private placement done at that point in time?
A That's correct.
Q Could you just explain to me generally what was the transaction in 1997 of the organization of Miller & Schroeder, what happened?
A I, I put together an investment group that acquired the stock of Miller & Schroeder with a combination of equity and debt.
Q So you bought out the prior owners?
A That's correct.
Q Who were the prior owners, a group of individuals?
A Primarily, it was Roger Wikner W-I-K-N-E-R.
Q This was a private individual?
A Yes. And Jim Iverson, I-V-E-R-S-O-N. A third partner who had 1 percent interest was Steve Erickson.
Q So from July 1997 or June 30th at this time, how much of an ownership interest did you have in Miller &

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Schroeder?
A I had about a 19 percent ownership interest.
Q And I guess the owner was actually, to be precise, it was what, MI Acquisition Corporation doing business as Miller & Schroeder?
A That's correct.
Q And after 1997, July 1997, did Miller & Schroeder continue in the same lines of business?
A Generally, yes.
Q What were those lines of business?
A Underwriting and distributing municipal bonds. Originate and selling commercial real estate loans and trading municipal and corporate bonds and governments.
Q Any other lines of business?
A Pardon?
Q Any other lines of business?
A No.
Q And you, when I asked the question, said generally stayed in the lines of business.
Was there any difference?
A Only in emphasis.
Q What was the change in emphasis?
A The growth area of the firm was in the commercial real estate business and in financing the gaming

A Yes, I did look at it; I did read it.

(Dlugosch Deposition Exhibit 4 was marked for identification.)

BY MR. TOPOL:

Q I've handed you what I've marked as Exhibit Number 4, which is the 1997 policy. I'll represent that to you.

Take a look through it and see if you agree that that's the 1997 policy issued to MI Acquisition Corp.

A I believe this is it, yes.

Q You say you recall reading it. Do you recall whether you read it in 1997 at the time it was issued?

A Yes, I did.

Q Do you recall whether you read the policy before it issued?

A I don't recall.

Q Do you recall about how long you spent reading it?

A No, I don't.

Q Do you have expertise in D&O insurance?

A No, I do not.

Q Had you read any D&O policies before this policy was issued in 1997?

A No.

Q This was the first D&O policy you ever read?

A Yes.

(Dlugosch Deposition Exhibit 5 was marked for identification.)

BY MR. TOPOL:

Q I hand you what's marked Exhibit Number 5, Hays 002004. The document at the top says, "Miller & Schroeder Agenda 10-22-97."

I ask you, do you recall whether you've seen this document before?

A No, I have not.

Q Do you know whether you might have seen it in 1997?

A I don't believe I did.

Q If there were a meeting in October of 1997 to talk about Miller & Schroeder's insurance coverage, would you have attended that meeting?

A Not necessarily.

Q Do you know who would have attended?

A Chief financial officer, accounting department. Probably, probably counsel but I'm not certain.

Q You see under Item Number 4 there's some diamonds and the second diamond says, "E&O coverage option"? Do you see that?

A Yes.

Q Do you know whether in October 1997 Miller & Schroeder had E&O coverage?

A I believe we did at that time, yes.

Q And do you know who issued the coverage?

A I believe that -- when I say I believe that we did, obtaining the E&O coverage was an important issue for myself and for the directors. And I would have -- I thought it was in place before October 22nd of '97. That's why I say I believe it was, but this is -- the only E&O coverage that the firm got was through the Hays Group. And so if this says that it was not in place at that time, then I presume it was not in place.

Q Why was E&O coverage important?

A Well, it was important because we did not want to have the directors -- I'm sorry, E&O coverage. I, I'm going to back up -- back off.

Q You were referencing D&O before?

A I was, I was thinking of D&O coverage.

Q Okay.

A So I'll -- why don't you --

Q Why don't we start the line again.

A Start the line again.

Q Okay. So in July of '97 there was D&O coverage, correct?

A That's what I recall. I mean, that's what I intended was to have D&O coverage in place.

Q And that's what Exhibit Number 4 is, it's your

understanding.

A Yes. And so we did not have E&O coverage, and I do not believe we had it prior to that time, and I do not believe we had it after, but I can't say that for certain.

Q Why was D&O, officers and directors, coverage important?

A Because it was critical for us to have protection of our directors and our officers for acts that were not -- that they weren't directly responsible for.

Several of the directors had wanted to make certain that we had D&O coverage. And I can't recall which of them, but one of them was in the insurance industry for all his life, so he probably was the one that -- and it was important to me to have insurance covering the potential exposures of directors and officers to claims by customers and others for, for perceived wrongdoings of the company.

Q Did the company consider getting E&O coverage?

A I don't recall any discussion about getting E&O coverage.

Q And is it your understanding that D&O coverage provides insurance for suits by customers?

A It would provide coverage for suits against directors and officers but not against the company or the

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1 salespeople.
2 Q It would provide coverage to directors and officers
3 in all circumstances or just if they, as you framed
4 it, had no responsibility?
5 A It would protect them if they were not directly
6 responsible for the perceived transgression.
7 Q And what do you mean by "not directly responsible"?
8 A That they were not the party who was engaged in the
9 action that brought about the complaint.
10 Q And did you have an understanding as to whether the
11 1997 policy that's Exhibit 4 provided coverage for
12 the directors and officers for customer suits?
13 A It was my understanding that it did, and that was the
14 purpose for obtaining the policy.
15 Q And what's the basis of that understanding?
16 A It was, it was what we requested and, and believed
17 that we had received.
18 Q When you say "we had requested," who is "we"?
19 A I don't recall who all was involved. At the time we
20 were putting the acquisition together, the, the
21 principal parties that were engaged were John Clarey
22 and myself, my son, Jamie, and Paul Tietz at Briggs
23 and Morgan along with Brian Wenger and Laurie Ketola.
24 Q You mentioned there was a director with significant
25 insurance experience.

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1 Do you know who that person was?
2 A Yeah, Bill Sexton.
3 Q Do you know where he worked at the time?
4 A He was retired.
5 Q And you say "we had requested."
6 Do you know who this was request was conveyed
7 to?
8 A To the best of my recollection, it was conveyed to
9 one of the principals of The Hays Group. And I'm not
10 sure if his name appears anywhere in these documents,
11 I don't believe it does. So I'm not remembering his
12 name.
13 Q But not to Mary Marshall, somebody else?
14 A No, not to Mary Marshall.
15 Q Was it conveyed in writing, do you know?
16 A Not by myself. It could have been by counsel but it
17 was not by me.
18 Q Did you ever get a written opinion from the lawyers
19 as to what coverage was provided by the 1997 policy?
20 A Not to my recollection.
21 Q Did you ever ask for a written opinion?
22 A No.
23 Q Did you ever ask for a written opinion from The
24 Marshall Group as to what coverage was afforded by
25 the D&O policy?

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1 A I'm sorry.
2 Q For what coverage, what the extent of coverage was?
3 A Who is The Marshall Group?
4 Q I'm sorry, strike that, you're right. From The Hays
5 Group. Did you ever ask The Hays Group for a written
6 opinion as to what coverage is available, and in
7 particular whether there was coverage for customer
8 suits?
9 A No, I don't recall requesting that.
10 Q Did you ever take any notes documenting information
11 about whether the 1997 policy would provide coverage
12 for customer suits by customers?
13 A I can't recall whether I did or not.
14 Q Do you know whether anybody else ever documented this
15 understanding?
16 A I don't know.
17 Q Do you recall discussions about the -- we talked
18 earlier about SIPC insurance coverage.
19 A Yes.
20 Q Who would you have had discussions with about that
21 coverage?
22 A With our sales manager, with salespeople, with the
23 chief financial officer. And probably the other
24 members of our management committee.
25 Q Would you have discussed that with the law firm,

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1 Briggs and -- what did you call it, Briggs and --
2 A Briggs and Morgan?
3 Q Yes.
4 A No, I don't recall it, and I don't believe I did.
5 Q Would you have discussed it with The Hays Group?
6 A I would have -- I wouldn't have directly discussed it
7 with them, no.
8 Q You would have directed somebody else --
9 A Yes.
10 Q -- to talk to them about the coverage?
11 A Yes.
12 Q Did Miller & Schroeder have general liability
13 insurance coverage, or commercial liability?
14 A Not that I recall. I don't know one way or the other
15 whether we had commercial liability coverage.
16 Q Do you know whether you had workers' compensation
17 coverage?
18 A Yes, we did.
19 Q Were you involved in those decisions?
20 A No.
21 Q So how do you know that they had workers'
22 compensation insurance?
23 A I, I know that we had workers' compensation claims
24 that were filed, and I'm making an assumption that we
25 had workers' comp insurance coverage.

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Q Do you know whether there was any negotiation about which of these -- about what specific types of business would be included here?
A I don't recall any negotiation of that issue.
Q Do you recall whether Miller & Schroeder requested any changes to this endorsement?
A No, I don't recall that we did.
Q Do you recall whether this endorsement ever had a different form to it?
A Not that I recall.
Q Do you recall whether there was any language or communications concerning the form of the endorsement?
A Do I --
Q Do you recall whether there were any communications concerning the content of this endorsement?
Let me rephrase that. Do you recall whether there were any communications you ever saw between any parties discussing changes in the language of this endorsement?
A No, I don't recall any.
Q If there were, would you have seen those communications?
A Yes, I would have.
Q And why do you think you would have seen those

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communications.
A It's part of my responsibility as CEO, and I was concerned about -- yeah, I think it was well known that I was concerned about this aspect of the exposures.
Q So your recollection today is that you had discussions clarifying that there would be coverage for directors and officers for suits by customers --
A Regarding --
Q -- correct?
A Yes.
Q But you don't recall that there were ever any communications about the language of this endorsement.
A No, I don't recall that.
Q Did you do anything before this deposition to refresh your recollection as to your testimony that there were --
A No.
Q -- that there was coverage for this endorsement?
A No, I did not.
Q I'm handing you what is Endorsement Number 3 called "Securities Exclusion," SRC1540. I ask you to take a look at that.
Do you recall whether you looked at the

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securities exclusion before?
A Yes, I did.
Q Do you recall whether you looked at this exclusion in 1997?
A Yes, I did.
Q Why did you look at it in 1997?
A I reviewed the whole policy in 1997, including endorsements, and wanted to ensure that that endorsement was not going to exclude coverage for directors and officers for the items in the Endorsement Number 9.
Q And were you -- did you reach a conclusion as to whether or not it would?
A Yes, I concluded that it would cover.
Q And how did you reach that conclusion?
A Discussions with counsel, and I'm not -- I don't recall whether I had direct discussions with The Hays Group on it or not, but I was given assurance that it was.
Q Did you ask for an explanation for why or just their assurance?
A Just the assurance.
Q Did you ask them to document the assurance?
A No.
Q Do you have an understanding as to why, you know,

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from conversations from with them or any other reason, why endorsement Number 3 wouldn't not apply to directors and officers?
A The discussion was that Endorsement Number 9 was a clarification to ensure that Endorsement Number 3 was not going to be, would not expose the directors and officers to claims.
Q Can you turn ahead to Endorsement Number 9?
When you say a clarification of Endorsement Number 9, are you referring to a specific part of Endorsement Number 9?
A The, the concern that I had -- the assurance that I was looking for was that Paragraph 2 in Number 9 did, in fact, give us assurance that the directors and officers would be covered from claims arising from these actions.
Q And Paragraph 2 starts out by making a reference to Paragraph Number 1, correct? It says, "Paragraph (1) above is not intended however, nor shall be it construed," dot, dot, dot, is that correct?
A That's correct.
Q It doesn't make any reference to Endorsement Number 3, does it?
A No, it doesn't.
Q So why did you think this provision in Endorsement

EXHIBIT B

Page 6

A. Tarkio, Missouri. I don't believe it is any longer in existence.
Q. What was your degree in?
A. I had a bachelor of arts in business.
Q. Do you have any postgraduate education?
A. None.
Q. After you graduated from Tarkio College in 1970 where did you go to work?
A. I went to work for a firm called Wohlreich and Anderson.
Q. What did you do for Wohlreich and Anderson?
A. In their back office. They were in wholesale brokerage located on John Street in Manhattan.
Q. The firm Wohlreich was a wholesale --
A. Insurance brokerage.
Q. What is a wholesale insurance brokerage?
A. A wholesaler broker is an intermediary between a retail broker and the insurance company. Normally, they bring an

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expertise to a specific type of coverage which the retail broker might not have. And/or bringing a premium volume, that being strengthening the marketplace, in a class of business that the retail broker may not do as much business in. Do I make sense to you?
Q. Yes. What kind of insurance were you a wholesale broker for?
A. In Wohlreich & Anderson?
Q. Yes.
A. I was in the back office, I was in administration. I just got out of college and I had no real involvement in placing insurance.
Q. How long did you work at Wohlreich?
A. About a year and a half.
Q. Where did you go to work there?
A. AIG.
Q. That was around 1971, '72?
A. '71, '72.
Q. How long were you at AIG?
A. For about two and a half years.
Q. AIG is a a large insurance company?
A. Number one and number two right, in the world right now.
Q. What did you do for AIG?

Page 8

A. Worked in their directors & officers liability area. Which included at the time -- well D & O was a very small product at that point so we did D & O, umbrella and E & O coverage.
Q. Can you for the record explain what D & O and what E & O insurance is?
A. D & O is directors and officers liability. Insuring corporate directors and officers of corporation and/or eleemosynary corporations against shareholder suits, employment-related suits, customer suits, governmental actions alleging, normally, breach of fiduciary duty.
Q. What are E & O?
A. Errors and omissions coverage, normally is utilized by a specific profession covering that individual or company in their, in the services they are providing to customers. It would cover them for misstatements, not mismanagement but misstatements, errors or omissions that they may commit in their or alleged errors and omissions they may commit in their capacity as lawyer, accountant, investment banker, et cetera.
Q. For a policy issued to a securities

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broker/dealer what would this E & O cover?
A. Again I did not underwrite security broker-dealers, it normally covers from my recollection, it would cover a security broker/dealer for, again, breach of their duty in their capacity as a broker. Could be anything. It's what is alleged in the specific complaint. In other words, there is no -- I don't know what else to say.
Q. But AIG, at AIG you were working on D & O?
A. Yes. We did some E & O but primarily lawyers, professional, employment agents and brokers. Not financial related E & O products.
Q. Where did you go to work after AIG?
A. For the Home Insurance Company.
Q. That would have been around what year?
A. '70, '71. About '72 to '73. I worked there about four and a half years.
Q. So until around '76, '77?
A. Correct.
Q. What did you do for the Home Insurance Company?

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1 Q. What was ARC's line of business?
2 A. Wholesale broker in the area of D &
3 O and professional liability. Our biggest product
4 was D & O liability by far. And still is. Still
5 is an ongoing firm. 85 percent of the firm at the
6 time that I left, about 85 percent of the product
7 was D & O.
8 Q. When did you leave?
9 A. Little over two and a half years
10 ago.
11 Q. Retire?
12 A. Retired.
13 Q. You mentioned you said D & O
14 primarily but some professional liability?
15 A. Correct.
16 Q. What do you mean by the term
17 professional liability?
18 A. Could be lawyers professional, could
19 be financial related errors & omissions coverage,
20 pension trust liability, as a firm we brokered
21 bonds. I'm not saying I did these things
22 specifically but these are things our firm did, et
23 cetera.
24 Q. Did you have a position while you
25 were at ARC?

Page 23

1 A. I was a partner. It was myself, and
2 I said to you before two other individuals. The
3 acronym stands for Al, Richie, Chris. Al
4 Salvatico and Chris Cavallaro, thus the acronym
5 ARC. A third, a third, a third partners.
6 Q. ARC did wholesale brokering but not
7 retail brokering?
8 A. Correct.
9 Q. You mentioned some of the
10 professional liability products. Did you work on
11 any of those products?
12 A. Very little. I was more in the D &
13 O area than I was in the E & O area. Did not do
14 any securities broker/dealer placements at all. I
15 didn't feel comfortable because I didn't have a
16 background in that area. My area of expertise was
17 D & O liability. Not E & O.
18 Q. Did you do D & O policies to
19 financial institutions?
20 A. Did I -- yes, I did.
21 Q. Do you know if you handled D & O
22 policies to securities broker-dealers?
23 A. If I did, you know, talking about
24 one right now but none of the meaningful ones
25 stick in my mind. I was not involved with the

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1 major firms, I might have handled one or two over
2 the years but I didn't think of them specifically
3 as financial institutions because again, you know
4 I was looking at the D & O exposure, not the E & O
5 exposure.
6 Q. Is a wholesale broker an agent for
7 anybody?
8 A. I think technically we were an agent
9 for several companies but that was a requirement.
10 In other words, certain companies let you broker
11 to them. You have an account with them and you
12 deal with them on an account current basis but
13 from a technical perspective I think some
14 companies required you to be an agent.
15 Q. "Companies", you mean insurance
16 companies?
17 A. Insurance companies, in order to
18 deal with them. But we didn't have the
19 underwriting authority for the company that we
20 were an agent for. In other words, there is a
21 distinction between an agent that you might go for
22 your homeowner's insurance where he has authority
23 potentially to quote you a homeowner's policy. We
24 didn't have that authority. So we were not an
25 agent as you think of an agent. We had to submit

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1 each account to the company for quoting purposes.
2 Quotation purposes.
3 Q. When you were brokering D & O
4 policies did you work with a single insurance
5 company or various policies?
6 A. Various companies.
7 Q. So if a company wanted a D & O
8 policy, how would you decide, a policy holder is
9 interested in getting D & O coverage, how would
10 you decide which company to go to?
11 A. I would submit it to all of the
12 markets that we at that time placed coverage with
13 and make a submission to them, looking for them to
14 quote the account.
15 Q. By "markets" you mean insurance
16 companies?
17 A. Correct. And as the quotes came
18 back and the declinations, because invariably some
19 accounts would not be everybody's cup of tea, as
20 the quotes came back we would put them together
21 and send the quotes on to the retail broker along
22 with the declinations and then the retail broker
23 with us we would make a recommendation potentially
24 to the client. There are some accounts where the
25 retail broker didn't want us to make

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1 recommendations at all. They would make the
2 recommendations. What we were was a marketing arm
3 for them. They would make the decision with the
4 client. And the client would come back, I guess
5 eventually to the retail broker and make the
6 decision as to which insurance company they wished
7 to purchase the coverage through.
8 Q. If you made a recommendation what
9 criteria would you look at?
10 A. Would you clarify.
11 Q. If you brought back seven or eight
12 quotes how would you decide?
13 A. Premium, it could be deductible.
14 And terms and conditions of the quotation. Each
15 insurance company may not view the same account in
16 the same way and it is one company could put on a
17 specific restriction that another company might
18 not put on. And you would review the quotes and
19 then if we were to make a recommendation, it would
20 be based on the terms and conditions and the
21 premiums and the deductible provided by the
22 various insurance companies.
23 Q. Where did the fee to ARC come from
24 for doing this brokering?
25 A. Commission. It was a commission

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1 that was paid by the insurance company that was
2 split between ARC and the retail broker.
3 Q. Was it a set percentage, the
4 commission?
5 A. No, negotiated. Set commission from
6 who? From the company or from --
7 Q. From the insurance company. Sort of
8 standard in the industry?
9 A. It fluctuates.
10 Q. Do you mean over time or by company
11 or both?
12 A. By company certainly. And by --
13 over time. There were certain times in the
14 marketplace where commissions may be higher and
15 then commission cost be lower.
16 Q. You mentioned a few minutes ago that
17 you dealt with a number of markets or insurance
18 companies while you were at ARC. Do you recall
19 what some of them are?
20 A. We worked with AIG, Chubb, Executive
21 Risk when they were two different companies, X/L,
22 Reliance Insurance Company when they were in
23 existence, Home Insurance Company, Great American,
24 Hartford. CNA and a variety of other companies.
25 Probably about 20 companies in total.

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1 Q. Did you deal with one retail broker
2 or a variety of retail brokers?
3 A. Variety.
4 Q. Do you recall about how many?
5 A. Hundreds.
6 Q. Did you deal with the Hays Group?
7 A. Yes.
8 Q. What type of retail brokering did
9 the Hays Group do?
10 A. They were a standard retail broker.
11 I don't understand what you mean.
12 Q. Just D & O or --
13 A. They were a full service brokerage,
14 to my knowledge.
15 MR. TOPOL: Could you mark this as
16 Exhibit 1 and give it to the witness,
17 please.
18 (July 29, 1997 letter from Richard
19 Fierstein to Michael Watts marked Exhibit
20 1 for identification, as of this date.)
21 Q. Before you look at Exhibit 1, Mr.
22 Fierstein, did you -- you didn't bring any
23 documents with you today?
24 A. No, I did not.
25 Q. You don't have in your possession

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1 any documents relating to Miller & Schroeder?
2 A. Do not.
3 Q. All right.
4 MR. TOPOL: For the record, Exhibit
5 1 bears the Bates label ERII 6519. It is
6 a June -- July 29, 1997 letter from
7 Richard Fierstein to Mr. Michael Watts.
8 Q. Do you recall seeing this letter
9 before?
10 A. No.
11 Q. Is that the ARC letterhead on top?
12 A. Yes, it is.
13 Q. The signature down below, does that
14 look to be your signature?
15 A. Probably not. In other words, my
16 secretary would sign these letters. I don't
17 specifically -- this is not my signature.
18 Q. It is not your signature. Was it
19 your practice to have your secretary would often
20 sign letters for you?
21 A. Yes.
22 Q. From reading this letter can you
23 tell what it is?
24 A. What do you mean -- this is a letter
25 -- what is this letter?

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1 Q. What is this letter?
2 A. A letter that I sent to Mike Watts
3 looking for a quotation for MI Acquisition, D & O
4 liability because that is the reference on the top
5 of the letter and I probably, what I did, in the
6 third paragraph, I don't know I did this but I did
7 this on several occasions, paraphrased part of a
8 letter that I received from my retail broker.
9 Q. O.K.
10 A. In other words, this paragraph here,
11 "I would appreciate, we would appreciate your
12 comments on the concerns of Paul Tietz, board
13 member. Paul is an attorney with Briggs & Morgan
14 and wants to insulate Briggs & Morgan from
15 professional liability claims from his board
16 affiliation with Miller & Schroeder. Your
17 thoughts on claim situations. Need your interest
18 in quoting. Limits of 1, 3 and 5 million as soon
19 as possible." This might have been a paraphrase
20 from the Hays Group letter, I assume that was the
21 broker --
22 Q. Who was Mr. Michael Watts?
23 A. Mike was an underwriter at Executive
24 Risk.
25 Q. Did you deal with Mike a lot?

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1 A. I used to when I was a broker, yes,
2 I did.
3 Q. What was your understanding of what
4 he did at Executive Risk Management?
5 A. Michael grew up through the ranks, I
6 don't really know where he was in 1997. I don't
7 know where he was in his growth.
8 Q. Right.
9 A. Mike was an underwriter that I dealt
10 with at Executive Risk to secure quotes for
11 directors & officers liability so he was the
12 individual I sent this account to looking for
13 quotations when I went to market on this account.
14 Q. Do you know whether you would have
15 spoken with Michael by phone?
16 A. I have absolutely no recollection.
17 Q. Sitting here today, do you have any
18 recollection of working on the policy for Miller &
19 Schroeder?
20 A. Absolutely none.
21 Q. Is there anything you think would
22 refresh your recollection?
23 A. It's seven years. From 1997 to
24 today. I don't remember who I played golf with
25 last week. I don't know how I would remember --

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1 there are certain accounts that always will stick
2 in my mind but Miller & Schroeder was not a large
3 enough account that I would have had, that I would
4 remember them. I might add that I don't remember
5 having any relationship with Miller & Schroeder on
6 a direct basis. There were certain clients that I
7 did have. The retail broker had me deal with the
8 client with the retail broker in concert. I do
9 not remember ever speaking with anybody at Miller
10 & Schroeder.
11 Q. You don't recall speaking with Mr.
12 Tietz?
13 A. Never.
14 MR. TOPOL: Mark this as Exhibit 2.
15 (Document Bates stamped ERII 6579
16 marked Exhibit 2 for identification, as of
17 this date.)
18 Q. Can you take a look, Mr. Fierstein,
19 at Exhibit 2 which is marked ERII 6579. You will
20 see on that document are identified some names of
21 directors, starting with James F. Dlugosch. Any
22 of those names ring a bell?
23 A. None.
24 Q. You don't recall ever speaking with
25 them?

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1 A. Never.
2 Q. Do you ever recall speaking with Tom
3 Nelson?
4 A. No.
5 Q. Ken Larson?
6 A. No.
7 MR. TOPOL: Mark this as 3, please.
8 (Document bearing Bates number ERII
9 6479 marked Exhibit 3 for identification,
10 as of this date.)
11 Q. Take a look, Mr. Fierstein, at
12 Exhibit number 3. Bears Bates number ERII 6479?
13 A. Uh-huh. Yes.
14 Q. Can you identify what this document
15 is.
16 A. It's apparently the cover sheet for
17 a binder. I'm sorry. For a quotation. Not for a
18 binder.
19 Q. That is from what, the bottom
20 reference where it says enclosed directors &
21 officers liabilities --
22 A. Right on the top it says MI
23 Acquisition Corporation insurance proposal which
24 would obviously be Executive Risk's proposal to
25 provide a quotation.

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1 document speaks for itself.
2 MR. ATMORE: Same objection.
3 Q. You can answer the question?
4 A. I hear them. I think the exclusion
5 speaks for itself.
6 Q. What do you think it says?
7 MR. KOLBO: Same objection.
8 MR. ATMORE: Same objection.
9 A. I think it speaks for itself. I
10 mean, I don't know what to say to you. It's an
11 SEC exclusion. It refers to the terminology in
12 the market, it says securities exclusion. Right
13 on the top it says that.
14 Q. Do you know why securities exclusion
15 would go in a D & O policy?
16 MR. ATMORE: Same objection.
17 A. It would -- this wording or wording
18 -- I don't know. Let me just, give me have a
19 second.
20 Q. Sure.
21 (Pause)
22 A. There is an SEC exclusion on most
23 forms. Actually on all private forms. I'm not
24 saying that this is the specific reason why this
25 exclusion is on this form. In that, but there are

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1 wordings on most forms in the private company
2 arena to eliminate coverage for an IPO. Restrict
3 coverage, any private company can go public during
4 a policy period.
5 Q. Right?
6 A. There is no, normally the carrier
7 puts on an exclusion or restriction, do you
8 understand? To eliminate or protect them, give
9 them the right to re-underwrite to cover the
10 exposure if they were to go public. Now this is a
11 broad form SEC exclusion which would serve that
12 purpose. It might serve other purposes but it
13 would certainly serve that purpose.
14 Q. When you say could serve other
15 purposes what other purposes could it serve?
16 MR. KOLBO: Object to foundation.
17 A. What else could it do?
18 Q. Right, --
19 A. Well, it is what it says. It is an
20 SEC exclusion so depending on the claim, you know,
21 I don't know what else to say to you. It is an
22 SEC exclusion. So depending on -- I have nothing
23 else to say.
24 Q. It means what the language says it
25 means?

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1 A. Exactly.
2 Q. Okay. Take a look at what is SRC
3 1547 which is endorsement number 9. Called
4 "General E & O exclusion with management carve
5 back."
6 A. Okay.
7 Q. Have you seen this type of exclusion
8 before?
9 A. Yes, I have.
10 Q. Estimate how many times.
11 A. At least 50. In this form or other
12 forms.
13 Q. By forms you mean --
14 A. Other carriers, other companies.
15 Q. Do you have an understanding as to
16 why this exclusion would be included in a D & O
17 policy?
18 MR. KOLBO: Object to the
19 foundation.
20 MR. ATMORE: Same objection.
21 A. Why it's there?
22 Q. Correct.
23 A. Well, it prevents a D & O --
24 paragraph 1 is a, speaks for itself, it's an E & O
25 exclusion. Even though it -- it excludes them,

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1 just what it says, it excludes claims for specific
2 services.
3 Q. I'll tell you, Miller & Schroeder,
4 to make this more concrete, they did securities
5 underwriting.
6 A. Okay.
7 Q. Is it your understanding paragraph
8 would exclude coverage for underwriting
9 services?
10 A. It would not provide coverage for
11 their specific professional service on an E & O
12 basis.
13 Q. Are there products out there that
14 would provide coverage for those services?
15 A. Yes, there are.
16 Q. What times of products are there?
17 A. Securities broker/dealer policy.
18 Q. Were those policies --
19 A. Or investment counselors policy.
20 I'm not -- I don't remember specifically what
21 Miller & Schroeder did but there were several
22 policies policies that were available in the
23 market. As to whether -- as to whether Miller &
24 Schroeder could have afforded to buy the policy or
25 could they have handled the retention, there are a

EXHIBIT C

1 Q. And what kind of decisions would you have to
2 make? Once you've learned about the company, do you
3 have to make certain decisions about what endorsements
4 are going to issue?
5 First of all, you have to make a decision
6 I suppose as to whether it's going to be the Power or
7 some other D and O policy, right, or the public
8 policy?
9 A. Correct.
10 Q. But beyond that do you have to make some
11 decisions about what, if any, particular endorsements
12 are going to be attached or are the endorsements
13 generally --
14 A. They were standard.
15 Q. Standard endorsements?
16 A. Yes.
17 Q. How often would it be or would it ever be
18 the case that you'd look at a particular application
19 and decide that some special endorsement or additional
20 endorsement that wasn't standard should be part of
21 that application or part of that policy?
22 A. I'm sure it happened but I do not recall.
23 Q. Were the endorsements for the Power and for
24 the public placement D and O policies, were they
25 identical in the standard sense when they were issued

1 as a standard policy?
2 A. There were standard endorsements for each
3 policy.
4 Q. But were they different standard
5 endorsements between the two policies?
6 A. I'm assuming they would be since one was for
7 private business and the other is for public business.
8 Q. Do you remember what the differences were in
9 those endorsements?
10 A. No.
11 Q. It's been awhile?
12 A. Yeah.
13 MR. KOLBO: Mark that, please.
14 (Intervenor Exhibit No. 1,
15 Offered and marked.)
16 Q. (By Mr. Kolbo) Showing you what's been
17 marked as Exhibit No. 1.
18 Would you take a look at that and tell me
19 whether you've seen it before?
20 A. Do I recall seeing it? No. But it just
21 looks like some type of quote sheet.
22 Q. Is this a form that would have been
23 completed by Executive Risk, do you know?
24 A. I believe so.
25 Q. Is this your handwriting?

1 policy, was it standard for the Power policy that was
2 issued to have a general E and O exclusion with a
3 management carveback?
4 A. Yes.
5 Q. Was that also standard with respect to the
6 public D and O policy that was issued?
7 A. Could be. Yeah.
8 Q. Do you have a recollection of that?
9 A. Not specific, no.
10 Q. Do you recall any discussions with Mr.
11 Fierstein about what should be the scope of any
12 general E and O exclusion and whether there should be
13 a management carveback?
14 A. No, I do not.
15 Q. Did you have -- do you recall any
16 discussions at all with anybody other than Mr.
17 Fierstein?
18 And maybe you don't recall those
19 conversations either but I'm trying to find out if you
20 recall speaking with anybody associated with the
21 insured, Miller and Schroeder in connection with this
22 application in 1997?
23 A. No. Sorry.
24 MR. KOLBO: Mark this please, six.
25

1 particular claim, lawsuit or application?
2 A. No, sir.
3 MR. KOBOL: Let's take a short break.
4 A recess was taken.)
5 MR. KOLBO: I don't have any more
6 questions. Mr. Atmore may. He represents another
7 party in this case.
8 MR. ATMORE: Yes, I do have some
9 questions. They'll be random because I'm just picking
10 out things when you were talking with Mr. Kolbo.
11 CROSS EXAMINATION BY MR. ATMORE
12 Q. First of all, let me start here. You left
13 Executive Risk in 1999, correct?
14 A. Correct.
15 Q. And you started in 1994. When in 1994 did
16 you start, do you remember?
17 A. July.
18 Q. When did you leave?
19 A. July of 1999.
20 Q. Why did you leave?
21 A. Went on to a better opportunity.
22 Q. Now, at the time you started with Executive
23 Risk, did Chubb have an ownership interest in
24 Executive Risk?
25 A. No.

1 Q. When did the Chubb Group --
2 A. The Chubb Group announced their acquisition
3 in February of 1999. The deal was closed in July of
4 1999.
5 Q. That's the same time you moved on to
6 Executive Liability, correct?
7 A. Correct.
8 Q. As an underwriter did you play any role in
9 writing the contract form or the endorsements?
10 A. None whatsoever.
11 Q. I think you testified that you would have
12 had no involvement in the issue of what claims would
13 be covered after the policies issue, correct?
14 A. That's correct.
15 Q. Would the claims people ever look to
16 underwriting for information on how to interpret the
17 contract?
18 A. No. Claims would look at to make sure the
19 contract was issued properly. Their interpretation
20 would be what drove it.
21 Q. Their interpretation being?
22 A. Their interpretation of the contract.
23 Q. Claims' interpretation?
24 A. Claims.
25 Q. Now, you met with Ms. Schwarz for 45 minutes

EXHIBIT D

Executive Risk

Binder

July 31, 1997

5 mil 0/50/100 $110,000
7/31/97 - 7/31/2000
3 Year Policy Period - Single Aggr

Richard A. Fierstein
ARC Excess & Surplus, Inc. Mineola
300 Old Country Road
Garden Level
Mineola, NY 11501-4192

RE: MI ACQUISITION CORPORATION INSURANCE PROPOSAL

21.5%

Dear Richard:

Thank you for the opportunity to offer an insurance proposal for MI Acquisition Corporation. Executive Risk is proud of its ability to customize an insurance program for each account's needs. If there are any additional requirements not addressed in the enclosed proposal, please call to discuss.

Executive Risk offers D&O for financial institutions, diversified financial institutions and community banks, healthcare institutions, non-profit organizations, large commercial risks and The Power℠ for private risks. We also provide professional liability insurance for employed lawyers, specialized insurance agents and brokers, mortgage brokers, title agents, as well as miscellaneous professional liability insurance programs. Other insurance programs include: fiduciary liability and crime insurance, Form24Plus™ expanded bond coverage for community banks, general partners liability, managed care E&O and D&O, Systems Rx℠: a medical technology management program, employment practices liability for law firms, and employment practices liability for financial institutions and mid- to large-sized commercial entities.

We look forward to discussing this proposal with you.

Sincerely,

Michael J. Watts
Senior Underwriter

Encl: Directors & Officers Liability Including EPL Proposal

EXHIBIT
Watts 5
8/4/04

Executive Risk
Management Associates

82 Hopmeadow Street
Post Office Box 2002
Simsbury, Connecticut 06070-7683

860.408.2000
Fax: 860.408.2002
Email: info@execrisk.com
Web Site: http://www.execrisk.com

Executive Risk

July 31, 1997

Quotation Worksheet

Account: MI Acquisition Corporation
Account Number: 182537
Producer: ARC Excess & Surplus, Inc. Mineola
Mineola, NY

Directors & Officers Liability Including EPL on Executive Risk Indemnity Inc. Form C22163 (3/1996 ed.)

NO.	LIMIT OF LIABILITY (inclusive of def. expenses)	RETENTIONS (A) each Insured Person, each claim	RETENTIONS (B) each claim by the Company	ANNUAL PREMIUM
1.	$1,000,000	$0	$50,000	$17,393

Insured percentage(A): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.
Insured percentage(B1): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

Entity Coverage (B)(2) Retention: $50,000

Insured percentage(B2): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

2.	$1,000,000	$0	$100,000	$17,393

Insured percentage(A): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.
Insured percentage(B1): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

Entity Coverage (B)(2) Retention: $100,000 **(private placement)**

Insured percentage(B2): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

3.	$2,000,000	$0	$50,000	$28,250

Insured percentage(A): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.
Insured percentage(B1): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

Entity Coverage (B)(2) Retention: $50,000

Insured percentage(B2): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

4. $2,000,000 $0 $100,000 $28,250

Insured percentage(A): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.
Insured percentage(B1): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

Entity Coverage (B)(2) Retention: $100,000 **(private placement)**

Insured percentage(B2): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

5. $3,000,000 $0 $50,000 $37,250

Insured percentage(A): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.
Insured percentage(B1): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

Entity Coverage (B)(2) Retention: $50,000

Insured percentage(B2): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

6. $3,000,000 $0 $100,000 $37,250

Insured percentage(A): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.
Insured percentage(B1): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

Entity Coverage (B)(2) Retention: $100,000 **(private placement)**

Insured percentage(B2): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

7. $5,000,000 $0 $50,000 $45,750

Insured percentage(A): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.
Insured percentage(B1): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

Entity Coverage (B)(2) Retention: $50,000

Insured percentage(B2): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

3yr Single Aggr

8.	$5,000,000	$0	$100,000	$ 110,000 ~~$45,750~~

Insured percentage(A): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.
Insured percentage(B1): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

Entity Coverage (B)(2) Retention: $100,000 **(private placement)**

Insured percentage(B2): 100% of Loss in excess of the Retention; the remaining 0% of Loss shall be uninsured.

7/31/97 → 7/31/~~97~~ 2000

DISCOVERY PERIOD:

A one year discovery period is available for 75% of the total annual premium.

ENDORSEMENTS (The titles and headings are for convenience only. Please refer to the policy and endorsements for a description of coverage): 3-year Deal

Applicable to Quote Number: 1, 2, 3, 4, 5, 6, 7, 8

D21237 C23115	MINNESOTA AMENDATORY ENDORSEMENT
modified ~~D21371A~~	GENERAL E+O EXCLUSION (WITH MANAGEMENT CARVEBACK) → schedule
✓D22309	SECURITIES EXCLUSION - BROAD FORM
✓D22529	EXCLUDES CLAIMS BASED ON MALFUNCTION, DEFECT IN ANY PRODUCT (ENTITY ONLY)
✓D22560	INTELLECTUAL PROPERTY EXCLUSION (ENTITY COVERAGE ONLY)
✓D23005	LIMITED SECURITIES ENDORSEMENT
✓D23091	PROVIDES DEFENSE EXPENSES FOR CLAIMS SEEKING NON-MONETARY RELIEF
✓D23299	2XODL FOR NOT FOR PROFIT FOR DIRECTORS AND OFFICERS
T-99a	Inverted Warranty

CONTINGENCIES (Prior to binding, this proposal is subject to the underwriter's receipt and satisfactory review of the following):

T-99b Letter Clarifying ERII's intent with regards to coverage for ATTY

1. Completed Application Signed and Dated by the President or CEO
2. D&O Breakout
3. Investor Base? Fully subscribed?
4. Any changes with regards to their financing arrangements ?

Paul Tietz/ Board Member

ERII 006482

4

OTHER:
The policy will show a retroactive date as: Policy Inception

Quotation Expiration: 30 Days

Commission: ~~10.5%~~ 21.5%

Premium Due: within 30 Days of policy effective date

Notes:

EXHIBIT E

Acct # 102 ... Miller + Schroeder

INFORMATION NEEDED TO QUOTE/ BIND

Circle One: Aetna ERII New Old ERSIC New Old

Product: FBL GPL EPL D&O FLIP FIE&O Crime DILP

Submission Type: New Business Run-Off New Business Renewal Business

Total Assets : 55 mil ~~C 2120~~ → Power?

QPC Rating : 1A

Company Type: Public Private

Subject To:
- D&O Breakout
- Investor Base? Fully Subscribed
- Any ~~Financing~~ Changes with regards to their Financing Arrangement

Limit: 1, 2, 3, 5

EXCESS:

Underlying Limits:

Underlying Primary Carrier :

Deductibles: ~~[illegible]~~ 50K EPLI 100K Private Placement 0/50/50 100 Private Placement

Premium: 17,393 + ~~[illegible]~~ 28,250 + 37,250 + 45,750

Commission % : 16.5

Endorsements: Please make sure they reference the correct policy.
- D23299 - 2xs ODL
- D21371A - E&O w/curveback
- D22529 - X Sir
- D22560 - Int Prop Ex
- D22309 - SEC EX
- D23005 - Caribbean

3 yr prepaid 1.05 for

Quote Expiration Date : 30 days- Please state if otherwise.

Payment Due : 15 30 days.

Discovery : 1 yr at 75 % 2 yrs at 150%

Retro Date : Incorporation Policy Inception or Date / /

Endorsments Printed : Y N

Application : Y we need N

Policy Period: 8/1/97 - 8/1/98

ELP Coverage: Price per Attorney $_____

Risk Manager:

1 mil at 20K
3 mil at 39
5 mil at 50

P Print

Power Form 50 100

Please submit this sheet with Status Change/ Binder Form.

MN

EXHIBIT
2 ATS 1
8/14/04

ERII 006484

7

EXHIBIT F

EXHIBIT
WATTS 7
9/14/04

MT

ARC EXCESS & SURPLUS, LLC
300 OLD COUNTRY ROAD
MINEOLA, NEW YORK 11501
FAX: (516) 747-3633

COMPANY: Executive Risk
CITY & STATE: Simsbury, CT
ATTENTION: Mike Watts
TELECOPIER NO: #12

TOTAL NUMBER OF PAGES 1 (INCLUDING THIS COVER PAGE)

FROM: Richard A. Fierstein **DATE:** 8/1/97

Re: MI ACQUISITION CORPORATION D/B/A MILLER & SCHROEDER
Directors and Officers Liability
Policy #:
Policy Term: July 31, 1997 to July 31, 2000
Executive Risk Indemnity

This is to confirm you have bound the captioned account on behalf of Executive Risk Indemnity effective July 31, 1997 to July 31, 2000 at a $5,000,000 limit excess of a $0/$50,000 retention except for Private Placement Claims which have a $0/$100,000 retention for a three year prepaid premium of $110,000 per the terms and conditions of Options #7/#8 of your 7/31/97 quote letter except Executive Risk has agreed to delete the General E&O Exclusion with Management Carveout and replace it with a Specific E&O Exclusion with Management Carveout relating to the Security Broker, Dealer Investment Banking and Underwriting of Securities Activities.

Also, Executive Risk has agreed to provide a letter of Intent regarding coverage for Mr. Paul Tietz while acting in the capacity of Director of MI Acquisition Corporation/Miller & Schroeder.

Coverage is bound subject to receipt of the information noted in the quote letter. Also, please note, coverage is bound subject to a reverse warranty until Executive Risk received the aforementioned subjectivities and is satisfied.

Please advise your assigned policy number as soon as possible.

Thanks for your help.

IF YOU HAVE NOT RECEIVED ALL OF THE PAGES INDICATED ABOVE, PLEASE CALL US BACK AS SOON AS POSSIBLE AT (516) 747-4100.

RECEIVED TIME AUG. 1. 10:57AM PRINT TIME AUG. 1. 10:58AM

ARC EXCESS & SURPLUS, LLC.
300 OLD COUNTRY ROAD
MINEOLA, NEW YORK 11501

FAX #: (516) 747-3633

TELECOMMUNICATIONS COVER PAGE

PLEASE DELIVER THE FOLLOWING PAGE(S) TO:

COMPANY: ERMA
ATTENTION: Michael Watts
CITY & STATE: Simsbury, CT
FAX NO: 12

TOTAL NUMBER OF PAGE(S) 1 (INCLUDING THIS COVER PAGE)

FROM: *RICHARD A. FIERSTEIN (EXT. 117) /hed* DATE: *9/4/97*

RE: MI ACQUISITION CORPORATION
Directors and Officers Liability
Policy #: 751-075440-97

When issuing the caption policy, please add MI Acquisition Corporation as a named insured. This is the name of the company that was used as the vehicle for the stock ownership change. Please call if you have any questions or require additional information.

IF YOU HAVE NOT RECEIVED ALL OF THE PAGES INDICATED ABOVE, PLEASE CALL US BACK AS SOON AS POSSIBLE AT (516) 747-4100.

EXHIBIT G

Executive Risk Indemnity Inc.
Home Office
32 Loockerman Square, Suite L100
Dover, Delaware 19901

Administrative Offices/Mailing Address:
82 Hopmeadow Street
Simsbury, Connecticut 06070-7683

DECLARATIONS

THE POWER℠

POLICY NUMBER
751-075440-97

DIRECTORS AND OFFICERS LIABILITY INSURANCE POLICY INCLUDING EMPLOYMENT PRACTICES LIABILITY COVERAGE

NOTICE: THIS IS A CLAIMS MADE POLICY WHICH APPLIES ONLY TO "CLAIMS" FIRST MADE DURING THE "POLICY PERIOD", OR, IF PURCHASED, THE DISCOVERY PERIOD. THE LIMIT OF LIABILITY AVAILABLE TO PAY DAMAGES OR SETTLEMENTS WILL BE REDUCED BY THE PAYMENT OF "DEFENSE EXPENSES", AND "DEFENSE EXPENSES" WILL BE APPLIED AGAINST THE RETENTION. THE COVERAGE AFFORDED UNDER THIS POLICY DIFFERS IN SOME RESPECTS FROM THAT AFFORDED UNDER OTHER POLICIES. PLEASE READ THE ENTIRE POLICY CAREFULLY.

OPTIONAL COVERAGE UNDER INSURING AGREEMENT (B)(2) IS X IS NOT _ AVAILABLE UNDER THIS POLICY.

ITEM 1. **PARENT CORPORATION** –NAME AND PRINCIPAL ADDRESS: MI Acquisition Corporation dba Miller & Schroeder, Inc. 2400 IDS Center Minneapolis, MN 55402	ITEM 2. **POLICY PERIOD:** (a) Inception Date: July 31, 1997 (b) Expiration Date: July 31, 2000 at 12:01 a.m. both dates at the Principal Address in ITEM 1.

ITEM 3. **LIMIT OF LIABILITY** (inclusive of **Defense Expenses**):
$ 5,000,000.00 maximum aggregate limit of liability for all **Claims**.

ITEM 4. **PREMIUM:**
$110,000.00 total prepaid premium.

ITEM 5. **RETENTIONS:**

(a)	$0.00	each **Insured Person** each **Claim**, but only for **Loss** as to which indemnification by the **Company** is not legally permissible or is not made solely by reason of the **Company's** financial insolvency.
(b)	$50,000.00	each **Claim**, for **Loss** as to which indemnification by the **Company** is legally permissible.
(c)	$100,000.00	each **Claim** under Insuring Agreement (B)(2), if applicable.

ITEM 6. **LENGTH OF DISCOVERY PERIOD:** one year	ITEM 7. **ADDITIONAL PREMIUM FOR DISCOVERY PERIOD:** $36,648.00

ITEM 8. **NOTICE UNDER CONDITIONS (G)(1) AND (G)(2) MUST BE ADDRESSED TO:**
Vice President of Claims
Executive Risk Management Associates
P. O. Box 2002
Simsbury, CT 06070-7683

ITEM 9. **ENDORSEMENTS ATTACHED AT ISSUANCE:**

C23115	D23091
D22229	D23299
D22309	D25090
D22529	
D22560	
D23005	

These Declarations, the signed and completed Application and the Policy, with endorsements, will constitute the entire agreement between the Underwriter, the Company and the Insured Persons.

EXECUTIVE RISK INDEMNITY INC. by (Attorney-in-Fact): 09/17/97

Form C22164 (306ed.)

Catalog No. Scd-I

EXHIBIT
WATTS 11
9/14/04

ENDORSEMENT NO. 1
MINNESOTA AMENDATORY ENDORSEMENT

This Endorsement, effective at 12:01 a.m. on July 31, 1997, forms part of

Policy No. 751-075440-97
Issued to MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by Executive Risk Indemnity Inc.

In consideration of the premium charged:

1. THIS POLICY PROVIDES COVERAGE ON A CLAIMS-MADE BASIS.

   This means that only Claims actually made during the Policy Period are covered unless coverage for a Discovery Period is purchased. If a Discovery Period is not made available to the Insureds, the Insureds risk having gaps in coverage when switching from one insurer to another. Moreover, even if such a Discovery Period is made available to the Insureds, the Insureds may still be personally liable for claims reported after the Discovery Period expires.

   Claims-made policies do not provide coverage for Wrongful Acts committed before a fixed retroactive date.

   Rates for claims-made policies are discounted in the early years of a policy, but increase steadily over time.

2. Section IV. CONDITIONS (A) Limit of Liability is amended by adding the following thereto:

   "(3) If a judgment is entered against the Insured Persons the principal amount of which is within the applicable policy limits, the Underwriter will be responsible for the Insured Person's share of the costs, disbursements, and prejudgment interest, as determined under Section 549.09 of Minnesota's insurance law, included in such judgment, even if the total amount exceeds the applicable policy limits."

3. Section III. Exclusions (C) is deleted in its entirety and replaced with the following:

   "(C) fines, taxes or penalties, punitive or exemplary damages, the multiplied portion of any multiplied damage award, or matters which are uninsurable under the law pursuant to which this Policy will be construed."

4. The COOPERATION, SUBROGATION section of Section IV. CONDITIONS of this Policy will be deemed to have been amended to provide that:

   (a) The Underwriter and its reinsurers may not proceed against the Insured Persons in a subrogation action if the Loss that could give rise to such action was caused by the nonintentional acts of the Insured Persons, and

   (b) The Underwriter and its reinsurers may not subrogate themselves to the rights of the Insured Persons to proceed against another person if that other person is also insured by the Underwriter for the same Loss, except that this subparagraph (b) will apply only if the Loss was caused by the nonintentional acts of the person against whom subrogation is sought.

5. The DISCOVERY PEF D section of Section IV. CONDITIONS of t Policy is amended to allow the Parent Corporation to purchase the Discovery Period in accorda... e with the provisions of such section if the Parent Corporation cancels the Policy.

6. Paragraph (1) of the CANCELLATION section of Section IV. CONDITIONS of this Policy is deleted in its entirety and replaced by the following:

   "(1) The Underwriter may cancel this Policy only for failure to pay a premium when due, and only by delivering or mailing by first class mail to the entity named in ITEM 1 of the Declarations at its last known address, not less than ten (10) days before the effective date of cancellation, written notice stating the amount of premium due, the date on which such premium is due and the effect of non-payment by the due date; provided, that no cancellation for non-payment of premium of the amount due will be effective if payment is made before the effective date of cancellation set forth in the notice."

7. Paragraph (3) of Section IV. CONDITIONS (J) CANCELLATION; NO OBLIGATION TO RENEW is deleted in its entirety and replaced by the following:

   "(3) The Underwriter will not be required to renew this Policy upon its expiration. The Underwriter may non-renew this Policy only by delivering or mailing by first class mail to the entity named in ITEM 1 of the Declarations at its last known address, not less than sixty (60) days before the Expiration Date set forth in ITEM 2(b) of the Declarations, written notice of its intention to non-renew. If the Underwriter does not mail or deliver such notice at least sixty (60) days before the Expiration Date set forth in ITEM 2(b) of the Declarations, the coverage afforded under this Policy shall continue in force with no change in its terms, conditions and limitations for sixty (60) days after the entity named in ITEM 1 of the Declarations receives such notice. The foregoing will not apply, however, if the entity named in ITEM 1 of the Declarations has insured elsewhere, has accepted replacement coverage, or has requested or agreed to non-renewal."

8. The last sentence of Section IV. CONDITIONS (K) REPRESENTATIONS; SEVERABILITY is deleted in its entirety.

9. The Policy will be deemed to have been amended as necessary to effect the purposes of this endorsement.

All other terms, conditions and limitations of this Policy shall remain unchanged.

_____
Authorized Representative

ENDORSEMENT NO. 2
AMEND DEFINITION OF PARENT CORPORATION

This Endorsement, effective at 12:01 a.m. on July 31, 1997, forms part of

Policy No. 751-075440-97
Issued to MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by Executive Risk Indemnity Inc.

In consideration of the premium charged, the definition of "Parent Corporation" contained in Section II Definitions is amended to include MI Acquisition Corporation.

All other terms, conditions and limitations of this Policy shall remain unchanged.

Authorized Representative

4

ENDORSEMENT NO. 3
SECURITIES EXCLUSION

This Endorsement, effective at 12:01 a.m. on July 31, 1997, forms part of

Policy No.	751-075440-97
Issued to	MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, this Policy does not apply to any Claim based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged violation of:

(1) the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, any other federal law, rule or regulation with respect to the regulation of securities, any rules or regulations of the United States Securities and Exchange Commission, or any amendment of such laws, rules or regulations; or

(2) any state securities or "Blue Sky" laws or rules or regulations or any amendment of such laws, rules or regulations; or

(3) any provision of the common law imposing liability in connection with the offer, sale or purchase of securities.

All other terms, conditions and limitations of this Policy shall remain unchanged.

_____
Authorized Representative

ENDORSEMENT NO. 4
PRODUCT EXCLUSION

This Endorsement, effective at 12:01 a.m. on July 31, 1997, forms part of

Policy No.	751-075440-97
Issued to	MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, this Policy does not apply to any Claim against the Company based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged malfunction of any product or failure of any product to perform in any manner as a result of any defect, deficiency or inadequacy in the design or manufacture of such product. This exclusion applies only to the coverage available to the Company under Insuring Agreement B(2).

All other terms, conditions and limitations of this Policy shall remain unchanged.

Authorized Representative

ENDORSEMENT NO. 5
INTELLECTUAL PROPERTY EXCLUSION

This Endorsement, effective at 12:01 a.m. on July 31, 1997, forms part of

Policy No.	751-075440-97
Issued to	MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, this Policy does not apply to any Claim against the Company based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged infringement of any patent, copyright, trademark or service mark, including any actual or alleged violation of any law or statute, or rule or regulation promulgated thereunder or of any provision of the common law imposing liability in connection therewith. This exclusion applies only to the coverage available to the Company under Insuring Agreement B(2).

All other terms, conditions and limitations of this Policy shall remain unchanged.

Authorized Representative

ENDORSEMENT NO. 6
LIMITED SECURITIES COVERAGE ENDORSEMENT

This Endorsement, effective at 12:01 a.m. on July 31, 1997, forms part of

Policy No. 751-075440-97
Issued to MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by Executive Risk Indemnity Inc.

In consideration of the premium charged, Endorsement No. 3 will not apply to any Claim made against an Insured Person arising out of the offering, sale or purchase of Common Stock as described more fully in the Private Placement dated as of May 20, 1997.

All other terms, conditions and limitations of this Policy shall remain unchanged.

Authorized Representative

ENDORSEMENT NO. 7
AMEND EXCLUSION (A)(2)

This Endorsement, effective at 12:01 a.m. on July 31, 1997, forms part of

Policy No.	751-075440-97
Issued to	MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, Section III Exclusions (A)(2) is amended to read in its entirety as follows:

"(2) as a result of any portion of a Claim seeking relief or redress in any form other than money damages; or"

All other terms, conditions and limitations of this Policy shall remain unchanged.

Authorized Representative

ENDORSEMENT NO. 8
OUTSIDE DIRECTORSHIP LIABILITY ENDORSEMENT

This Endorsement, effective at 12:01 a.m. on July 31, 1997, forms part of

Policy No. 751-075440-97
Issued to MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by Executive Risk Indemnity Inc.

In consideration of the premium charged:

(1) The term "Wrongful Act" will also mean any Employment Practices Wrongful Act or other actual or alleged act, error, omission, misstatement, misleading statement or breach of duty by an Insured Person in his or her capacity as a director, officer, trustee, regent or governor of a not-for-profit organization or corporation, and DEFINITION (M) is amended accordingly.

(2) EXCLUSION (D)(4) will not apply to Claims against Insured Persons for Wrongful Acts in their capacities as directors, officers, trustees, regents or governors of not-for-profit organizations or corporations when their service as such is with the consent the Company.

(3) All Loss payable under this Policy in respect of Claims against the Insured Persons for Wrongful Acts in their capacities as directors, officers, trustees, regents or governors of not-for-profit organizations or corporations will be specifically excess of and will not contribute with:

(a) any indemnification from any such not-for-profit organization or corporation available to an Insured Person by reason of his or her service as a director, officer, trustee, regent or governor thereof; and

(b) any insurance of any such not-for-profit organization or corporation available to an Insured Person by reason of his or her service as a director, officer, trustee, regent or governor thereof, except that if the Underwriter shall have issued any such policy or policies of insurance to the not-for-profit corporation and a Claim gives rise to coverage both under this Policy by reason of this endorsement and under such other policy or policies, then the Underwriter's maximum aggregate limit of liability under all such policies, including this Policy, for all Loss, including Defense Expenses, in respect of such Claim will not exceed the largest single available limit of liability under any of such policies. Nothing in this subparagraph (4)(b) is intended, nor shall it be construed, to obligate or require the Underwriter to pay any Loss, including Defense Expenses, under this Policy in respect of any such Claim in any amount exceeding the available Limit of Liability as set forth in ITEM 3 of the Declarations.

All other terms, conditions and limitations of this Policy shall remain unchanged.

Authorized Representative

ENDORSEMENT NO. 9
GENERAL E & O EXCLUSION (WITH MANAGEMENT CARVEBACK)

This Endorsement, effective at 12:01 a.m. on July 31, 1997, forms part of

Policy No.	751-075440-97
Issued to	MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged:

(1) No coverage will be available under the Policy for Loss including Defense Expenses for any Claim made against any Insured based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving an Insured's actual or alleged rendering or failure to render the following services:

Investment Banking Services
Security Broker/Dealer Services
Securities Underwriting

(2) Paragraph (1) above is not intended, however, nor shall it be construed, to apply to Loss, including Defense Expenses, in connection with any Claim against an Insured to the extent that such Claim is for a Wrongful Act by Insured Person in connection with the management or supervision of any division, Subsidiary or group of the Parent Corporation offering any of the aforementioned services.

All other terms, conditions and limitations of this Policy shall remain unchanged.

Authorized Representative

D25090 (9/97)

ENDORSEMENT NO. 10
AMEND PARENT CORPORATION NAME ENDORSEMENT

This Endorsement, effective at 12:01 a.m. on November 16, 1998, forms part of

Policy No.	751-075440-97
Issued to	MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, the name of the Parent Corporation set forth in Item 1 of the Declarations is amended to read as follows:

MI Acquisition Corporation
P.O. Box 789
Minneapolis, MN 55440-0789

All other terms, conditions and limitations of this Policy shall remain unchanged.

Authorized Representative

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EXHIBIT H

Executive Risk Indemnity Inc.
Home Office
32 Loockerman Square, Suite L100
Dover, Delaware 19901

Administrative Offices/Mailing Address:
82 Hopmeadow Street
Simsbury, Connecticut 06070-7683

DECLARATIONS

THE POWER SM

POLICY NUMBER
8166-6027

DIRECTORS AND OFFICERS LIABILITY INSURANCE POLICY INCLUDING EMPLOYMENT PRACTICES LIABILITY COVERAGE

NOTICE: THIS IS A CLAIMS MADE POLICY WHICH APPLIES ONLY TO "CLAIMS" FIRST MADE DURING THE "POLICY PERIOD", OR, IF PURCHASED, THE DISCOVERY PERIOD. THE LIMIT OF LIABILITY AVAILABLE TO PAY DAMAGES OR SETTLEMENTS WILL BE REDUCED BY THE PAYMENT OF "DEFENSE EXPENSES", AND "DEFENSE EXPENSES" WILL BE APPLIED AGAINST THE RETENTION. THE COVERAGE AFFORDED UNDER THIS POLICY DIFFERS IN SOME RESPECTS FROM THAT AFFORDED UNDER OTHER POLICIES. PLEASE READ THE ENTIRE POLICY CAREFULLY.

OPTIONAL COVERAGE UNDER INSURING AGREEMENT (B)(2) IS X IS NOT _ AVAILABLE UNDER THIS POLICY.

ITEM 1. **PARENT CORPORATION** –NAME AND PRINCIPAL ADDRESS: Miller and Schroeder, Inc. PO Box 789 Minneapolis, MN 55440-0789	ITEM 2. **POLICY PERIOD:** (a) Inception Date: July 31, 2000 (b) Expiration Date: July 31, 2003 at 12:01 a.m. both dates at the Principal Address in ITEM 1.
ITEM 3. **LIMIT OF LIABILITY** (inclusive of **Defense Expenses**): $5,000,000.00 maximum aggregate limit of liability for all **Claims**.	
ITEM 4. **PREMIUM:** $82,500.00 total prepaid premium.	
ITEM 5. **RETENTIONS:** (a) $0.00 each **Insured Person** each **Claim**, but only for **Loss** as to which indemnification by the **Company** is not legally permissible or is not made solely by reason of the **Company's** financial insolvency. (b) $50,000.00 each **Claim**, for **Loss** as to which indemnification by the **Company** is legally permissible. (c) $100,000.00 each **Claim** under Insuring Agreement (B)(2), if applicable.	
ITEM 6. **LENGTH OF DISCOVERY PERIOD:** one year	ITEM 7. **ADDITIONAL PREMIUM FOR DISCOVERY PERIOD:** $61,875.00
ITEM 8. **NOTICE UNDER CONDITIONS (G)(1) AND (G)(2) MUST BE ADDRESSED TO:** Vice President of Claims Executive Risk Management Associates P. O. Box 2002 Simsbury, CT 06070-7683	
ITEM 9. **ENDORSEMENTS ATTACHED AT ISSUANCE:** C23115 D23091 C30302 D23299 D22309 D25090 D22529 D22560 D23005	

These Declarations, the signed and completed Application and the Policy, with endorsements, will constitute the entire agreement between the Underwriter, the Company and the Insured Persons.

EXECUTIVE RISK INDEMNITY INC. by (Attorney-in-Fact):
09/18/00

*The Power*SM

Directors and Officers Liability Insurance Policy
Including Employment Practices Liability Coverage

Executive Risk Indemnity Inc.
Home Office:
32 Loockerman Square, Suite L100
Dover, Delaware 19901

Administrative Offices/Mailing Address:
82 Hopmeadow Street
Simsbury, Connecticut 06070-7683

THIS IS A CLAIMS MADE POLICY WITH
DEFENSE EXPENSES INCLUDED IN THE LIMIT OF LIABILITY.
PLEASE READ THE ENTIRE POLICY CAREFULLY.

EXECUTIVE RISK INDEMNITY INC.

THE POWER℠

DIRECTORS AND OFFICERS LIABILITY INSURANCE POLICY INCLUDING EMPLOYMENT PRACTICES LIABILITY COVERAGE

Executive Risk Indemnity Inc. (the "Underwriter"), the Insured Persons and the Company, subject to all of the terms, conditions and limitations of and any endorsements to this Policy, agree as follows:

I. INSURING AGREEMENTS

(A) The Underwriter will pay on behalf of the **Insured Persons Loss** from **Claims** first made against them during the **Policy Period** for **Wrongful Acts**, including **Employment Practices Wrongful Acts**, unless the **Company** pays such **Loss** to or on behalf of the **Insured Persons** as indemnification.

(B) The Underwriter will pay on behalf of the **Company**:

(1) **Loss** from **Claims** first made against the **Insured Persons** during the **Policy Period** for **Wrongful Acts**, including **Employment Practices Wrongful Acts**, if the **Company** pays such **Loss** to or on behalf of the **Insured Persons** as indemnification; and

(2) (OPTIONAL COVERAGE) if it is stated in the Declarations that coverage has been made available under this INSURING AGREEMENT (B)(2), **Loss** from **Claims** first made against the **Company** during the **Policy Period** for **Wrongful Acts**, including **Employment Practices Wrongful Acts**.

(C) As part of and subject to the limit of liability stated in ITEM 3 of the Declarations, the Underwriter will have the right and duty to defend any **Claim** as described in INSURING AGREEMENTS (A) and (B)(1) (and, if it is stated in the Declarations that coverage has been made available thereunder, INSURING AGREEMENT (B)(2)), even if such **Claim** is groundless, false or fraudulent.

II. DEFINITIONS

(A) "**Application**" means the application attached to and forming part of this Policy, including any materials submitted in connection therewith, all of which are on file with the Underwriter and are a part of the Policy, as if physically attached.

(B) "**Claim**" means written notice received by an **Insured** that any person or entity intends to hold any **Insured** responsible for a **Wrongful Act**. A **Claim** will be deemed to have been made when such written notice is first received by any **Insured**.

(C) "**Company**" means the **Parent Corporation** and any **Subsidiary** created or acquired on or before the Inception Date in ITEM 2(a) of the Declarations or, subject to CONDITION (H), during the **Policy Period**.

(D) "**Defense Expenses**" means reasonable legal fees and expenses incurred by or on behalf of the **Insured Persons** (or, if coverage has been made available under INSURING AGREEMENT (B)(2), the **Company**) in the defense or appeal of a **Claim**, subject to the Underwriter's right and duty to defend as set forth in INSURING AGREEMENT (C); provided, that **Defense Expenses** will not include the **Company's** overhead expenses or any salaries, wages, fees or benefits of its directors, officers or employees.

(E) "**Employment Practices Wrongful Act**" means any actual or alleged:

(1) wrongful termination of the employment of, or demotion of or failure or refusal to hire or promote, any person;

(2) discrimination or sexual harassment adversely affecting any employee of, or applicant for employment with, the **Company**; or

(3) retaliatory treatment against an employee of the **Company** on account of such employee's exercise or attempted exercise of his or her rights under law.

(F) "**Insured**" means the **Company** and any **Insured Person**.

(G) "**Insured Person**" means:

(1) any past, present or future director or officer of the **Company**; and

(2) any past, present or future employee of the **Company**; provided, that employees, unlike directors and officers, will be **Insured Persons** only if and to the extent that **Claims** are made against them for **Employment Practices Wrongful Acts**.

In the event of the death, incapacity or bankruptcy of an **Insured Person**, any **Claim** against the estate, heirs, legal representatives or assigns of such **Insured Person** for a **Wrongful Act** of such **Insured Person** will be deemed to be a **Claim** against such **Insured Person**.

(H) **"Loss"** means **Defense Expenses** and damages, judgments, settlements or other amounts that an **Insured Person** (or, if coverage has been made available under INSURING AGREEMENT (B)(2), the **Company**) is obligated to pay as a result of a **Claim**.

(I) **"Parent Corporation"** means the entity named in ITEM 1 of the Declarations.

(J) **"Policy Period"** means the period from the Inception Date to the Expiration Date in ITEM 2 of the Declarations or to any earlier cancelation date.

(K) **"Related Claims"** means all **Claims** for **Wrongful Acts** based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving the same or related facts, circumstances, situations, transactions or events or the same or related series of facts, circumstances, situations, transactions or events.

(L) **"Subsidiary"** means any entity during any time in which the **Parent Corporation** owns or controls, directly or through one or more **Subsidiaries**, the right to elect or appoint more than fifty percent (50%) of such entity's directors or trustees.

(M) **"Wrongful Act"** means:

(1) any **Employment Practices Wrongful Act** by an **Insured Person** in his or her capacity as a director, officer or employee of the **Company**;

(2) any other actual or alleged act, error, omission, misstatement, misleading statement or breach of duty by an **Insured Person** in his or her capacity as a director or officer of the **Company**;

(3) any matter asserted against an **Insured Person** solely by reason of his or her status as a director or officer of the **Company**; and

(4) any **Employment Practices Wrongful Act** by the **Company** or any other actual or alleged error, omission, misstatement, misleading statement or breach of duty by the **Company**; provided, that this DEFINITION (M)(4) will only apply if it is stated in the Declarations that coverage has been made available under INSURING AGREEMENT (B)(2).

III. EXCLUSIONS

This Policy does not apply to:

(A) **Loss**, other than **Defense Expenses,** which an **Insured** is obligated to pay:

(1) as a result of a **Claim** brought about or contributed to in fact by any dishonest or fraudulent act or omission or any willful violation of any statute, rule or law by any **Insured**, or by the gaining by any **Insured** of any profit, remuneration or advantage to which such **Insured** is not legally entitled; provided, that for the purposes of determining the applicability of this EXCLUSION (A)(1), no **Wrongful Act** of any **Insured Person** will be imputed to any other **Insured Person**; and further, provided, that each **Insured** agrees that, if it is finally established that the Underwriter has no liability to an **Insured** for **Loss** as a result of a **Claim** by reason of this EXCLUSION (A)(1), such **Insured** will repay the Underwriter upon demand all **Defense Expenses** paid on behalf of such **Insured** in connection with such **Claim**;

(2) as a result of any portion of a **Claim** for an **Employment Practices Wrongful Act** seeking relief or redress in any form other than money damages; or

(3) by operation of the Fair Labor Standards Act, the National Labor Relations Act, the Worker Adjustment and Retraining Notification Act, the Consolidated Omnibus Budget Reconciliation Act of 1985, the Occupational Safety and Health Act, any workers' compensation, unemployment insurance, social security, or disability benefits law, other similar provisions of any federal, state or local statutory or common law or any rules or regulations promulgated under any of the foregoing;

(B) any salary, wages or other employment-related benefits which the **Company** is obligated to pay to any employee under a written contract either to commence or continue employment or to make any payment in the event of a termination of employment;

(C) fines, taxes or penalties, punitive or exemplary damages, the multiplied portion of any multiplied damage award, or matters which are uninsurable under the law pursuant to which this Policy will be construed; provided, that if applicable law so permits, this EXCLUSION (C) will not apply to punitive or exemplary damages or to the multiplied portion of a multiple damage award in any amount not exceeding $25,000 in connection with any **Claim**, such amount to be part of, and not in addition to, the limit of liability set forth in ITEM 3 of the Declarations;

(D) any **Claim** based upon, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving:

(1) any actual or alleged bodily injury, sickness, mental anguish, emotional distress, disease or death of any person, damage to or destruction of any

tangible property including loss of use thereof, libel, slander, oral or written publication of defamatory or disparaging material, invasion of privacy, wrongful entry, eviction, false arrest, false imprisonment, malicious prosecution, malicious use or abuse of process, assault, battery or loss of consortium; provided, that this EXCLUSION (D)(1) will not apply to allegations of mental anguish, emotional distress or libel, slander or oral or written publication of defamatory or disparaging material if and only to the extent that such allegations are made as part of a **Claim** for an **Employment Practices Wrongful Act**;

(2) any actual, alleged or threatened exposure to, or generation, storage, transportation, discharge, emission, release, dispersal, escape, treatment, removal or disposal of, any smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gases, waste materials (including materials which are intended to be or have been recycled, reconditioned or reclaimed) or other irritants, pollutants or contaminants, or any regulation, order, direction or request to test for, monitor, clean up, remove, contain, treat, detoxify or neutralize any of the foregoing, or any action taken in contemplation or anticipation of any such regulation, order, direction or request, including but not limited to any such **Claim** alleging damage to the **Company** or to its shareholders;

(3) any fact, circumstance, situation, transaction, event or **Wrongful Act**:

(a) underlying or alleged in any prior and/or pending litigation or administrative or regulatory proceeding of which any **Insured** had received written notice before the Inception Date in ITEM 2(a) of the Declarations; or

(b) which, before the Inception Date in ITEM 2(a) of the Declarations, was the subject of any notice given by or on behalf of any **Insured** under any other policy of insurance; or

(4) the service by any **Insured Person** as a director, officer or employee of any entity other than the **Company**, even if directed or requested by the **Company** to serve as a director, officer or employee of such other entity;

(E) any **Claim** by or on behalf of, or in the name or right of, the **Company** or any **Insured Person**, except that this EXCLUSION (E) will not apply to:

(1) any derivative action by a security holder of the **Company** on behalf of, or in the name or right of, the **Company**, if such action is brought and maintained independently of, and without the solicitation, assistance, participation or intervention of, the **Company** or any **Insured Person**;

(2) any **Claim** in the form of a crossclaim, third party claim or other claim for contribution or indemnity by an **Insured Person** which is part of or results directly from a **Claim** which is not otherwise excluded by the terms of this Policy; or

(3) any **Claim** for an **Employment Practices Wrongful Act**;

(F) any **Claim** for any actual or alleged violation of the Employee Retirement Income Security Act of 1974 or any regulations promulgated thereunder, or of any similar provisions of federal, state or local law or regulation;

(G) any **Claim** against any **Subsidiary** or other entity acquired by the **Company**, whether by merger, consolidation or otherwise, or against any **Insured Person** of such **Subsidiary** or other entity in his or her capacity as such for any **Wrongful Act**, including any **Employment Practices Wrongful Act**, committed during any time in which such entity is not a **Subsidiary** or at any time before the **Company's** acquisition of such entity; or

(H) any **Claim** arising out of any actual or alleged liability of the **Company** under any express contract or agreement. For the purposes of this EXCLUSION (H), an "express contract or agreement" is an actual agreement among the contracting parties, the terms of which are openly stated in distinct or explicit language, either orally or in writing, at the time of its making. This EXCLUSION (H) will apply only to the coverage available to the **Company** under INSURING AGREEMENT (B)(2) if it is stated in the Declarations that coverage has been made available thereunder, and this EXCLUSION (H) will not apply to **Claims** for liability resulting from **Employment Practices Wrongful Acts** if such liability would have attached to the **Company** in the absence of the express contract or agreement in question.

IV. CONDITIONS

(A) **Limit of Liability:**

(1) The amount stated in ITEM 3 of the Declarations will be the maximum aggregate limit of liability of the Underwriter under this Policy for all **Loss**, including **Defense Expenses**, from all **Claims** for which this Policy provides coverage, regardless of the time of payment by the Underwriter, and regardless of whether such **Claims** are made during the **Policy Period** or during the Discovery Period.

(2) **Defense Expenses** are part of and not in addition to the Underwriter's limit of liability, and payment of **Defense Expenses** by the Underwriter will reduce its limit of liability.

(B) **Application of Retention; Presumption of Indemnification:**

(1) The obligation of the Underwriter to pay **Loss**, including **Defense Expenses**, will only be in excess of the applicable retention. The Underwriter will have no obligation whatsoever, either to the **Insureds** or to any other person or entity, to pay all or any portion of any retention amount on behalf of any **Insured**, although the Underwriter will, at its sole discretion, have the right and option to do so, in which event the **Insureds** agree to repay the Underwriter any amounts so paid.

(2) The certificate of incorporation or articles of association, bylaws and resolutions of the **Parent Corporation** and each **Subsidiary** will be deemed to have been adopted or amended to provide indemnification to the **Insured Persons** to the fullest extent permitted by law.

(3) The retention set forth in ITEM 5(b) of the Declarations will apply to any **Loss** incurred by or on behalf of the **Insured Persons** as to which indemnification by the **Company** is legally permissible, whether or not actual indemnification is made, unless such indemnification is not made by the **Company** solely by reason of its financial insolvency.

(4) If different retentions are applicable to different parts of any **Claim**, the applicable retentions will be applied separately to each part of such **Claim**, but the sum of such retentions will not exceed the largest applicable retention as set forth in ITEM 5 of the Declarations.

(C) **Defense and Settlement of Claims**:

(1) No **Insured** may incur any **Defense Expenses** or admit liability for or settle any **Claim** without the Underwriter's written consent. The Underwriter will have the right to make investigations and conduct negotiations and, with the consent of the **Insureds**, to enter into such settlement of any **Claim** as the Underwriter deems appropriate. If the **Insureds** refuse to consent to a settlement acceptable to the claimant in accordance with the Underwriter's recommendation:

(a) the **Insureds** will thereafter be responsible for negotiating and defending such **Claim** at their own expense independently of the Underwriter; and

(b) subject to the Underwriter's maximum aggregate limit of liability as set forth in ITEM 3 of the Declarations, the Underwriter's liability in respect of any such **Claim** will not exceed the amount for which such **Claim** could have been settled by the Underwriter plus **Defense Expenses** up to the date the **Insureds** refused to settle such **Claim**.

(2) The Underwriter will have no obligation to pay **Loss** or **Defense Expenses** or to defend or continue to defend any **Claim** after the Underwriter's maximum aggregate limit of liability, as set forth in ITEM 3 of the Declarations, has been exhausted by the payment of **Loss** or **Defense**

Expenses, or both. If the Underwriter's limit of liability is exhausted by the payment of **Loss**, including **Defense Expenses**, the premium will be fully earned.

(D) **Other Insurance; Other Indemnification:**

All **Loss** payable under this Policy will be specifically excess of and will not contribute with (1) other existing insurance, including but not limited to any other insurance under which there is a duty to defend, unless such other insurance is specifically in excess of this Policy, and (2) indemnification to which an **Insured** is entitled from any entity other than the **Company**. This Policy will not be subject to the terms of any other insurance.

(E) **Cooperation; Subrogation:**

In the event of a **Claim**, the **Insureds** will provide the Underwriter with all information, assistance and cooperation that the Underwriter reasonably requests, and will do nothing that may prejudice the Underwriter's position or potential or actual rights of recovery. At the Underwriter's request, the **Insureds** will assist in the conduct of actions, suits or proceedings, including but not limited to attending hearings, trials and depositions, securing and giving evidence and obtaining the attendance of witnesses, and will also assist in making settlements. In the event of payment, the Underwriter will be subrogated to the extent of any payment to all of the rights of recovery of the **Insureds**. The **Insureds** will execute all papers and do everything necessary to secure such rights, including the execution of any documents necessary to enable the Underwriter effectively to bring suit in their name. The obligations of the **Insureds** under this CONDITION (E) will survive the Policy.

(F) **Discovery Period:**

If either the Underwriter or the **Parent Corporation** refuses or declines to renew this Policy for any reason and, within thirty (30) days of the end of the **Policy Period**; the **Parent Corporation** elects to purchase the Discovery Period set forth in ITEM 6 of the Declarations by paying the additional premium set forth in ITEM 7 of the Declarations, then the coverage otherwise afforded by this Policy will be extended to apply to **Loss** from **Claims** first made during the Discovery Period, but only if such **Claims** are for **Wrongful Acts** committed before the end of the **Policy Period** or the date of any conversion of coverage under CONDITION (I), whichever is earlier.

(G) **Notice; Timing and Interrelationship of Claims:**

(1) As a condition precedent to any right to payment in respect of any **Claim**, including any **Claim** for a **Wrongful Act** of which notice was previously given under CONDITION (G)(2), the **Insureds** must give the Underwriter written notice of such **Claim**, with full details, as soon as practicable after

it is first made.

(2) If, during the **Policy Period**, the **Insureds** first become aware of a **Wrongful Act** which may subsequently give rise to a **Claim** and, as soon as practicable thereafter but before the expiration or cancelation of the Policy:

(a) give the Underwriter written notice of such **Wrongful Act**, including a description of the **Wrongful Act** in question, the identities of the potential claimants, the consequences which have resulted or may result from such **Wrongful Act**, the damages which may result from such **Wrongful Act** and the circumstances by which the **Insureds** first became aware of such **Wrongful Act**, and

(b) request coverage under this Policy for any subsequently resulting **Claim** for such **Wrongful Act**;

then the Underwriter will treat any such subsequently resulting **Claim** as if it had been first made during the **Policy Period**.

(3) All notices under CONDITIONS (G)(1) and (2) must be sent by certified mail to the address set forth in ITEM 8 of the Declarations.

(4) All **Related Claims** will be treated as a single **Claim** made when the earliest of such **Related Claims** was first made, or when the earliest of such **Related Claims** is treated as having been made in accordance with CONDITION (G)(2), whichever is earlier.

(H) **Adjustments**:

If, during the **Policy Period**, any of the following events occurs:

(1) the **Company** acquires any assets, acquires a **Subsidiary** or acquires any entity by merger and, at the time of such transaction, the assets so acquired or the assets of the entity so acquired exceed twenty-five percent (25%) of the total assets of the **Company** as reflected in the **Company's** most recent audited consolidated financial statements; or

(2) the **Company** assumes any liabilities and, at the time of such assumption, the liabilities so assumed exceed twenty-five percent (25%) of the total liabilities of the **Company** as reflected in the **Company's** most recent audited consolidated financial statements;

there will be no coverage under this Policy for any **Claim** for **Wrongful Acts** arising out of or in any way relating to the entity, assets or liabilities acquired, assumed or merged with, unless the Underwriter receives from the **Company** full details of such transaction or event and the Underwriter, at its sole discretion, agrees by written endorsement to provide such coverage upon such terms, conditions and limitations as it may require.

(I) **Conversion of Coverage Under Certain Circumstances:**

If, during the **Policy Period**, any of the following events occurs:

(1) the acquisition of the **Parent Corporation**, or of all or substantially all of its assets, by another entity, or the merger or consolidation of the **Parent Corporation** into or with another entity such that the **Parent Corporation** is not the surviving entity;

(2) the appointment of a receiver, conservator, trustee, liquidator or rehabilitator, or any similar official, for or with respect to the **Parent Corporation**; or

(3) the obtaining by any person, entity or affiliated group of persons or entities of the right to elect, appoint or designate at least fifty percent (50%) of the directors of the **Parent Corporation**;

coverage under this Policy will continue in full force and effect with respect to **Claims** for **Wrongful Acts** committed before such event, but coverage will cease with respect to **Claims** for **Wrongful Acts** committed after such event. After any such event, the Policy may not be canceled, regardless of CONDITION (J)(2), and the entire premium for the Policy will be deemed fully earned.

(J) **Cancelation; No Obligation to Renew:**

(1) The Underwriter may not cancel this Policy except for failure to pay a premium when due, in which case fifteen (15) days' written notice will be given.

(2) The **Parent Corporation** may cancel this Policy by mailing to the Underwriter written notice stating when, not later than the Expiration Date set forth in ITEM 2(b) of the Declarations, such cancelation will be effective. In such event, the earned premium will be computed in accordance with the customary short rate table and procedure. Premium adjustment may be made either at the time cancelation by the **Parent Corporation** is effective or as soon as practicable thereafter, but payment or tender by the Underwriter of unearned premium is not a condition of cancelation by the **Parent Corporation.**

(3) The Underwriter will not be required to renew this Policy upon its expiration. If the Underwriter elects not to renew this Policy, the Underwriter will deliver or mail to the **Parent Corporation** written notice to that effect at least sixty (60) days before the Expiration Date set forth in ITEM 2(b) of the Declarations.

(K) **Representations; Severability:**

The **Insureds** represent that the particulars and statements contained in the

Application are true, accurate and complete, and agree that this Policy is issued in reliance on the truth of that representation, and that such particulars and statements, which are deemed to be incorporated into and to constitute a part of this Policy, are the basis of this Policy. No knowledge or information possessed by any **Insured** will be imputed to any other **Insured**, except for material facts or information known to the person or persons who signed the **Application**. In the event of any material untruth, misrepresentation or omission in connection with any of the particulars or statements in the **Application**, this Policy will be void with respect to any **Insured** who knew of such untruth, misrepresentation or omission or to whom such knowledge is imputed.

(L) **No Action Against the Underwriter**:

(1) No action may be taken against the Underwriter unless, as conditions precedent thereto, there has been full compliance with all of the terms of this Policy and the amount of the **Insureds'** obligation to pay has been finally determined either by judgment against the **Insureds** after adjudicatory proceedings, or by written agreement of the **Insureds**, the claimant and the Underwriter.

(2) No person or entity will have any right under this Policy to join the Underwriter as a party to any **Claim** to determine the liability of any **Insured**; nor may the Underwriter be impleaded by an **Insured** or his, her or its legal representative in any such **Claim**. The Underwriter will not be relieved of any of its obligations under the Policy by the bankruptcy or insolvency of any of the **Insureds** or their estates.

(M) **Authorization and Notices**:

The **Insureds** agree that the **Parent Corporation** will act on their behalf with respect to receiving any notices and return premiums from the Underwriter.

(N) **Changes**:

Notice to any agent or knowledge possessed by any agent or other person acting on behalf of the Underwriter will not effect a waiver or change in any part of this Policy or estop the Underwriter from asserting any right under the terms, conditions and limitations of this Policy. The terms, conditions and limitations of this Policy can be waived or changed only by written endorsement.

(O) **Assignment**:

No assignment of interest under this Policy will bind the Underwriter without its consent.

(P) **Entire Agreement**:

The **Insureds** agree that this Policy, including the **Application** and any endorsements, constitutes the entire agreement between them and the Underwriter or any of its agents relating to this insurance.

(Q) **Headings**:

The descriptions in the headings and sub-headings of this Policy are solely for convenience, and form no part of the terms and conditions of coverage.

In witness whereof the Underwriter has caused this Policy to be executed on the Declarations Page.

Secretary

Co-Chairman

ENDORSEMENT NO. 1
MINNESOTA AMENDATORY ENDORSEMENT

This Endorsement, effective at 12:01 a.m. on July 31, 2000, forms part of

Policy No.	8166-6027
Issued to	Miller and Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged:

1. THIS POLICY PROVIDES COVERAGE ON A CLAIMS-MADE BASIS.

   This means that only Claims actually made during the Policy Period are covered unless coverage for a Discovery Period is purchased. If a Discovery Period is not made available to the Insureds, the Insureds risk having gaps in coverage when switching from one insurer to another. Moreover, even if such a Discovery Period is made available to the Insureds, the Insureds may still be personally liable for claims reported after the Discovery Period expires.

   Claims-made policies do not provide coverage for Wrongful Acts committed before a fixed retroactive date.

   Rates for claims-made policies are discounted in the early years of a policy, but increase steadily over time.

2. Section IV. CONDITIONS (A) Limit of Liability is amended by adding the following thereto:

   "(3) If a judgment is entered against the Insured Persons the principal amount of which is within the applicable policy limits, the Underwriter will be responsible for the Insured Person's share of the costs, disbursements, and prejudgment interest, as determined under Section 549.09 of Minnesota's insurance law, included in such judgment, even if the total amount exceeds the applicable policy limits."

3. Section III. Exclusions (C) is deleted in its entirety and replaced with the following:

   "(C) fines, taxes or penalties, punitive or exemplary damages, the multiplied portion of any multiplied damage award, or matters which are uninsurable under the law pursuant to which this Policy will be construed."

4. The COOPERATION, SUBROGATION section of Section IV. CONDITIONS of this Policy will be deemed to have been amended to provide that:

   (a) The Underwriter and its reinsurers may not proceed against the Insured Persons in a subrogation action if the Loss that could give rise to such action was caused by the nonintentional acts of the Insured Persons, and

   (b) The Underwriter and its reinsurers may not subrogate themselves to the rights of the Insured Persons to proceed against another person if that other person is also insured by the Underwriter for the same Loss, except that this subparagraph (b) will apply only if the Loss was caused by the nonintentional acts of the person against whom subrogation is sought.

5. The DISCOVERY PERIOD section of Section IV. CONDITIONS of this Policy is amended to allow the Parent Corporation to purchase the Discovery Period in accordance with the provisions of such section if the Parent Corporation cancels the Policy.

6. Paragraph (1) of the CANCELLATION section of Section IV. CONDITIONS of this Policy is deleted in its entirety and replaced by the following:

"(1) The Underwriter may cancel this Policy only for failure to pay a premium when due, and only by delivering or mailing by first class mail to the entity named in ITEM 1 of the Declarations at its last known address, not less than ten (10) days before the effective date of cancellation, written notice stating the amount of premium due, the date on which such premium is due and the effect of non-payment by the due date; provided, that no cancellation for non-payment of premium of the amount due will be effective if payment is made before the effective date of cancellation set forth in the notice."

7. Paragraph (3) of Section IV. CONDITIONS (J) CANCELLATION; NO OBLIGATION TO RENEW is deleted in its entirety and replaced by the following:

"(3) The Underwriter will not be required to renew this Policy upon its expiration. The Underwriter may non-renew this Policy only by delivering or mailing by first class mail to the entity named in ITEM 1 of the Declarations at its last known address, not less than sixty (60) days before the Expiration Date set forth in ITEM 2(b) of the Declarations, written notice of its intention to non-renew. If the Underwriter does not mail or deliver such notice at least sixty (60) days before the Expiration Date set forth in ITEM 2(b) of the Declarations, the coverage afforded under this Policy shall continue in force with no change in its terms, conditions and limitations for sixty (60) days after the entity named in ITEM 1 of the Declarations receives such notice. The foregoing will not apply, however, if the entity named in ITEM 1 of the Declarations has insured elsewhere, has accepted replacement coverage, or has requested or agreed to non-renewal."

8. The last sentence of Section IV. CONDITIONS (K) REPRESENTATIONS; SEVERABILITY is deleted in its entirety.

9. The Policy will be deemed to have been amended as necessary to effect the purposes of this endorsement.

All other terms, conditions and limitations of this Policy shall remain unchanged.

John P Kearney

Authorized Representative

ENDORSEMENT NO. 2
Notice of Loss Control Services

RE: Directors and Officers Liability

As a valued policyholder, we want to let you know that we have loss prevention information available to you.

Available to you are copies of a Directors and Officers Liability Loss Prevention booklet written by Dan A. Bailey, a partner in the law firm of Arter & Hadden as well as Employment Practices Liability Loss Prevention booklet. These booklets discuss general principles governing D&O and EPL liability and the potential exposures insureds face in these areas in performing their everyday business activities. It also contains information that may be helpful to you in your loss prevention efforts. You may obtain copies by contacting your agent or your local Chubb Executive Risk underwriter.

As the booklets note, it is important that you consult competent counsel to design and implement your loss control programs.

If you have any questions, please call 800-432-8168 and press 3 to reach our Marketing Department to obtain additional materials.

ENDORSEMENT NO. 3
SECURITIES EXCLUSION

This Endorsement, effective at 12:01 a.m. on July 31, 2000, forms part of

Policy No.	8166-6027
Issued to	Miller and Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, this Policy does not apply to any Claim based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged violation of:

(1) the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, any other federal law, rule or regulation with respect to the regulation of securities, any rules or regulations of the United States Securities and Exchange Commission, or any amendment of such laws, rules or regulations; or

(2) any state securities or "Blue Sky" laws or rules or regulations or any amendment of such laws, rules or regulations; or

(3) any provision of the common law imposing liability in connection with the offer, sale or purchase of securities.

All other terms, conditions and limitations of this Policy shall remain unchanged.

John P Kearney

Authorized Representative

ENDORSEMENT NO. 4
PRODUCT EXCLUSION

This Endorsement, effective at 12:01 a.m. on July 31, 2000, forms part of

Policy No.	8166-6027
Issued to	Miller and Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, this Policy does not apply to any Claim against the Company based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged malfunction of any product or failure of any product to perform in any manner as a result of any defect, deficiency or inadequacy in the design or manufacture of such product. This exclusion applies only to the coverage available to the Company under Insuring Agreement B(2).

All other terms, conditions and limitations of this Policy shall remain unchanged.

John P Kearney

Authorized Representative

ENDORSEMENT NO. 5
INTELLECTUAL PROPERTY EXCLUSION

This Endorsement, effective at 12:01 a.m. on July 31, 2000, forms part of

Policy No.	8166-6027
Issued to	Miller and Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, this Policy does not apply to any Claim against the Company based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged infringement of any patent, copyright, trademark or service mark, including any actual or alleged violation of any law or statute, or rule or regulation promulgated thereunder or of any provision of the common law imposing liability in connection therewith. This exclusion applies only to the coverage available to the Company under Insuring Agreement B(2).

All other terms, conditions and limitations of this Policy shall remain unchanged.

John P Kearney

Authorized Representative

ENDORSEMENT NO. 6
LIMITED SECURITIES COVERAGE ENDORSEMENT

This Endorsement, effective at 12:01 a.m. on July 31, 2000, forms part of

Policy No.	8166-6027
Issued to	Miller and Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, Endorsement No. 3 will not apply to any Claim made against an Insured Person arising out of the offering, sale or purchase of Common Stock as described more fully in the Private Placement dated as of May 20, 1997.

All other terms, conditions and limitations of this Policy shall remain unchanged.

John P Kearney

Authorized Representative

ENDORSEMENT NO. 7
AMEND EXCLUSION (A)(2)

This Endorsement, effective at 12:01 a.m. on July 31, 2000, forms part of

Policy No.	8166-6027
Issued to	Miller and Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, Section III Exclusions (A)(2) is amended to read in its entirety as follows:

"(2) as a result of any portion of a Claim seeking relief or redress in any form other than money damages; or"

All other terms, conditions and limitations of this Policy shall remain unchanged.

John P Kearney

Authorized Representative

ENDORSEMENT NO. 8
OUTSIDE DIRECTORSHIP LIABILITY ENDORSEMENT

This Endorsement, effective at 12:01 a.m. on July 31, 2000, forms part of

Policy No. 8166-6027
Issued to Miller and Schroeder, Inc.
Issued by Executive Risk Indemnity Inc.

In consideration of the premium charged:

(1) The term "Wrongful Act" will also mean any Employment Practices Wrongful Act or other actual or alleged act, error, omission, misstatement, misleading statement or breach of duty by an Insured Person in his or her capacity as a director, officer, trustee, regent or governor of a not-for-profit organization or corporation, and DEFINITION (M) is amended accordingly.

(2) EXCLUSION (D)(4) will not apply to Claims against Insured Persons for Wrongful Acts in their capacities as directors, officers, trustees, regents or governors of not-for-profit organizations or corporations when their service as such is with the consent the Company.

(3) All Loss payable under this Policy in respect of Claims against the Insured Persons for Wrongful Acts in their capacities as directors, officers, trustees, regents or governors of not-for-profit organizations or corporations will be specifically excess of and will not contribute with:

(a) any indemnification from any such not-for-profit organization or corporation available to an Insured Person by reason of his or her service as a director, officer, trustee, regent or governor thereof; and

(b) any insurance of any such not-for-profit organization or corporation available to an Insured Person by reason of his or her service as a director, officer, trustee, regent or governor thereof, except that if the Underwriter shall have issued any such policy or policies of insurance to the not-for-profit corporation and a Claim gives rise to coverage both under this Policy by reason of this endorsement and under such other policy or policies, then the Underwriter's maximum aggregate limit of liability under all such policies, including this Policy, for all Loss, including Defense Expenses, in respect of such Claim will not exceed the largest single available limit of liability under any of such policies. Nothing in this subparagraph (4)(b) is intended, nor shall it be construed, to obligate or require the Underwriter to pay any Loss, including Defense Expenses, under this Policy in respect of any such Claim in any amount exceeding the available Limit of Liability as set forth in ITEM 3 of the Declarations.

All other terms, conditions and limitations of this Policy shall remain unchanged.

John P Kearney

Authorized Representative

ENDORSEMENT NO. 9
GENERAL E & O EXCLUSION (WITH MANAGEMENT CARVEBACK)

This Endorsement, effective at 12:01 a.m. on July 31, 2000, forms part of

Policy No.	8166-6027
Issued to	Miller and Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged:

(1) No coverage will be available under the Policy for Loss including Defense Expenses for any Claim made against any Insured based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving an Insured's actual or alleged rendering or failure to render the following services:

Investment Banking Services
Security Broker/Dealer Services
Securities Underwriting

(2) Paragraph (1) above is not intended, however, nor shall it be construed, to apply to Loss, including Defense Expenses, in connection with any Claim against an Insured to the extent that such Claim is for a Wrongful Act by Insured Person in connection with the management or supervision of any division, Subsidiary or group of the Parent Corporation offering any of the aforementioned services.

All other terms, conditions and limitations of this Policy shall remain unchanged.

John P Kearney

Authorized Representative

D25090 (9/97)

EXHIBIT I

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1 Q. Is it form B dash D?
2 A. Yes.
3 Q. While you were employed at Miller & Schroeder,
4 what involvement did you have with Heritage bonds in
5 terms of underwriting or sales or interaction with
6 customers?
7 A. I would have been on the Credit Committee. I was
8 on the Credit Committee.
9 Q. What did the Credit Committee do?
10 A. Any new issuance of those bonds or any of the new
11 issues that the company did had to be approved by the
12 Credit Committee. So the public finance banker would
13 present a package of information to the Credit Committee
14 in advance to review. That would have included
15 financials and a description of the financing. We would
16 have met to ask questions, had discussions, and the
17 financing would have been approved or not approved based
18 on that.
19 Q. Would you have been on the Credit Committee the
20 entire time you were at Miller & Schroeder?
21 A. Virtually all of the time. I can't recall if I
22 joined immediately on employment or I think I got added
23 on like three months after I started work so shortly
24 after I started.
25 Q. Were the bonds sold out of all your offices? Or

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1 in other words, the Minneapolis office sells all the
2 Heritage bonds. You mentioned there were four offices
3 of Miller & Schroeder. Were they all selling Heritage
4 bonds?
5 A. All the offices were eligible to sell them or
6 could sell them, our salespeople. I mentioned, in
7 different offices like Seattle as an example, but there
8 were no salespeople in Seattle. They were bankers. So
9 the salespeople were in Solana Beach and Minneapolis.
10 Q. Did you work on sales of Heritage bonds?
11 A. I did not work on sales, no.
12 Q. Other than being on the Credit Committee, what
13 other work did you do in connection with the Heritage
14 bonds?
15 A. I can't recall anything specifically that I did
16 with Heritage bonds. I don't mean to -- not be
17 uncooperative, but as far as working on the Heritage
18 bonds, I did nothing regarding the underwriting or
19 structuring of the bonds on the banking side. I did
20 nothing regarding the sales or trading of the bonds on
21 the distribution side.
22 In my general role as an officer of the company, I
23 would have been very aware of the Heritage bonds. I
24 would have worked with them. If they were in inventory,
25 I would have taken capital haircuts on them or account

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1 for them but really wasn't involved in the business with
2 them.
3 (Whereupon, a brief recess was taken.)
4 (Whereupon, Deposition Exhibit No. 4 was marked for
5 identification.)
6 Q. (By Mr. Topol) Mr. Nelson, when you joined Miller
7 & Schroeder October '98--
8 A. '97.
9 Q. I'm sorry, '97, correct, October '97, the company
10 already had insurance policies in place?
11 A. Yes.
12 Q. Let me hand you what's been marked as Nelson
13 Exhibit 4. Take a look at that.
14 Do you know whether Nelson Exhibit 4 was the D&O
15 policy that the company had in place?
16 A. I understood it was, yes.
17 Q. While you were CFO of Miller & Schroeder, how many
18 hours would you say you spent dealing with insurance
19 coverage?
20 A. Four or less.
21 Q. Four or less hours?
22 A. (Witness indicates yes.)
23 Q. Who else at Miller & Schroeder during the time you
24 were there would have dealt with purchasing insurance
25 policies?

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1 A. Ken Larsen.
2 Q. Anyone else?
3 A. Not that I recall, no.
4 Q. When you made decisions about insurance policies,
5 would you have to have those approved by the board of
6 the company?
7 A. No, not that I recall, not while I was there.
8 Q. While you were there, you didn't go to the board
9 for approval?
10 A. No.
11 Q. Did you have to have your decisions about
12 insurance policies approved by Mr. Dlugash?
13 A. No, not that I recall.
14 I would like to add to that answer if you don't
15 mind--
16 Q. Please.
17 A. --just in case it's not communicating.
18 But to the extent that we considered it a routine
19 renew of the same coverages, we did not see a need to go
20 for approval and did not go for approval. If there was
21 a situation as far as a change, a significant increase
22 in premium and a new coverage that we were seeking, then
23 we would communicate and seek its approval. But I don't
24 recall that there were any significant issues like that
25 that we ever went to them on.

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1 I'm just making objections for the record.
2 Q. (By Mr. Topol) You can go ahead and answer.
3 A. I'm sorry, I'm not sure if I understood the
4 question.
5 Q. Let me rephrase it. Did you have an understanding
6 in 1990 as to whether the D&O policy issued by Executive
7 Risk provided coverage for securities broker/dealer
8 services?
9 MR. KOLBO: Same objection.
10 THE WITNESS: I can't say that I had a good
11 understanding of the protection that it provided. I
12 don't know.
13 Q. (By Mr. Topol) Did you at any time look into the
14 question of whether the company -- strike that.
15 Did you at any time look into the question of
16 whether Miller & Schroeder had insurance coverage for
17 securities broker/dealer services?
18 A. I did not.
19 Q. You didn't look into the question of whether
20 Miller & Schroeder had coverage for investment banking
21 services?
22 A. I did not.
23 Q. I believe you testified earlier that when you were
24 at E.W. Blanch, they had E&O coverage; is that correct?
25 A. Yes, they would.

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1 Q. Did Miller & Schroeder have E&O coverage?
2 A. No, we did not.
3 Q. Do you know why?
4 A. I don't. I worked at three security
5 broker/dealers in my career and none of those three have
6 had or purchased E&O coverage.
7 Q. Any point when you were at Miller & Schroeder, did
8 you look into purchasing E&O coverage?
9 A. No.
10 Q. Did you instruct Mr. Larsen to look into
11 purchasing E&O coverage?
12 A. Not that I recall.
13 Q. Do you know whether anybody at Miller & Schroeder
14 looked into purchasing E&O coverage?
15 A. Not that I'm aware of.
16 Q. Did you have any discussions while you were at
17 Miller & Schroeder about purchasing E&O coverage?
18 A. I don't remember.
19 MR. ATMORE: Just to clarify, you're talking
20 about a separate E&O policy, is that what your question
21 is?
22 MR. TOPOL: Correct, an additional policy
23 beyond.
24 THE WITNESS: I don't remember. They may have
25 raised it in their role as our agent and I might have --

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1 I might have dismissed it as something to not look into.
2 I don't recall. I have carried with my experience a
3 belief that broker/dealers generally do not buy that
4 policy or I haven't commonly seen it so I haven't spent
5 any time pursuing it.
6 Q. (By Mr. Topol) What's the basis for your belief?
7 A. I think I started at Dougherty Dawkins and I think
8 we had hired attorneys to look into E&O for brokers, and
9 I think we had done some survey of firms in our area to
10 see if anybody had it. And it seemed like the majority
11 of the broker/dealers did not purchase the coverage.
12 And upon our -- upon our counsel's giving us advice on
13 the E&O policy language, it sounded to us that the
14 exclusions basically didn't really provide any coverage
15 and we would pay a lot of premium for essentially no
16 coverage. But that's my general understanding from when
17 we looked at it in the '80s.
18 Q. The exclusions in the E&O policies?
19 A. Correct.
20 Q. And the premiums were expensive for E&O policies?
21 A. Correct.
22 Q. Do you know whether they were higher than the
23 premiums for D&O policies?
24 A. I don't recall. I thought they were.
25 Q. Do you recall having any discussions with the Hays

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1 Group about whether Miller & Schroeder should purchase
2 an additional policy?
3 A. No, I did not. I did not have any conversations
4 with the Hays Group.
5 Q. You testified I think a few minutes earlier that
6 you understood there was a dispute about the meaning of
7 -- that the subject of the litigation about the meaning
8 of the policy?
9 A. Yes.
10 Q. Do you have an understanding as to who is correct
11 in that dispute?
12 MR. KOLBO: Object to the foundation.
13 THE WITNESS: I don't know. I'm biased. I'm a
14 director and officer that has been damaged and I'm
15 frustrated to hear that there is no coverage. And I
16 would read this and, you know, clearly believe in my
17 corporate management role as president and CFO that item
18 No. 2 listed here would have protected me.
19 Q. (By Mr. Topol) What's the basis for that
20 understanding?
21 A. I simply thought I was an employee doing a job
22 that happened to be functioning as a CFO with corporate
23 administrative duties as a security broker/dealer
24 business, no different than I was a retail store or
25 anywhere else and would have been frustrated thinking

1 E-K-H-O-L-M, a public finance banker out of Minneapolis.
2 He was also on the Credit Committee and was also
3 involved or knowledgeable relative to the structure of
4 the finances, so Vic probably would have led the
5 discussion with Jim and Paul part of the team.
6 Q. And the Solana Beach office was a sales office?
7 A. Solana Beach was both sales and banking.
8 Q. And you, in contrast, were on the business side of
9 the company, correct?
10 A. Corporate side.
11 Q. Corporate side. Okay.
12 You were referring to Endorsement No. 9 from the
13 2000 renewal. Do you recall back in '97 whether there
14 were any discussions with what was going to go into that
15 Endorsement No. 9?
16 A. I don't recall any. I started in October and I
17 think the policy was done in July so--
18 Q. So the first policy came after you -- it came
19 prior to you starting?
20 A. Correct.
21 Q. Okay. And then this policy was largely handled by
22 Mr. Larsen, is that right, this renewal in 2000?
23 A. Yes. And I was involved with the fax that was No.
24 7. Like I say, based on that review of that fax and
25 recommendation from our agent, I viewed it as a routine

1 renewal and didn't spend any other substantive time on
2 it.
3 Q. Aside from the Credit Committee, did you have any
4 other supervisory roles over the Solana Beach office?
5 A. When I became president, I guess their sales and
6 trading operations would have reported up to the people
7 in charge of sales and trading in Minneapolis that
8 reported up to me.
9 Q. Prior to you becoming president, who did they
10 report to?
11 A. Those same functions would have reported directly
12 to Jim Dlugash.
13 MR. ATMORE: That's all I have.
14 MR. TOPOL: Nothing further.
15 (Off the record briefly.)
16 MR. TOPOL: The question was do you want to
17 read and sign. You have the opportunity to look at the
18 transcript and to note any edit changes or correct names
19 spelled wrong or anything else you think needs to be
20 corrected or you can waive the right to review it. It's
21 just when it becomes final, with an opportunity for you
22 to read it and make any corrections.
23 THE WITNESS: Sure, I'll review it.
24 (Whereupon, the foregoing deposition was concluded
25 at 10:59 a.m.)

1 PLEASE MAKE ALL CHANGES OR CORRECTIONS ON THIS SHEET,
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2 REPORTER'S INSERTION INTO THE ORIGINAL DEPOSITION. DO
NOT MAKE ANY MARKS ON THE ORIGINAL DEPOSITION. SIGN
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OF THIS DISTRICT.
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SIGNATURE HERE AND ON FOLLOWING
PAGE
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23 _____
NOTARY PUBLIC FOR STATE OF ___
24
RESIDING AT _____
25 MY COMMISSION EXPIRES _____

1
2 DEPONENT'S CERTIFICATE
3
4 I, TOM NELSON, the deponent in the foregoing
5 deposition, DO HEREBY CERTIFY that I have read the
6 foregoing -63- pages of typewritten material, and that
7 the same is, with any changes thereon shown on the
8 preceding page, a full, true and correct transcript of
9 my oral deposition given at the time and place
10 hereinbefore mentioned.
11
12
13
_____
14 TOM NELSON
15
16 SUBSCRIBED AND SWORN to before me this _____
day of _____, 2004.
17
18
_____
19 NOTARY PUBLIC FOR STATE OF

20
RESIDING AT _____
21 MY COMMISSION EXPIRES _____
22
23
24
25

EXHIBIT J

RONALD A. MARRON
MARRON & WILSON, LLP
1475 6TH Avenue, 3rd Floor
San Diego, CA 92101
Telephone: (619) 696-9006
Facsimile: (619) 696-0983

Attorneys for Claimants
STEVEN ONDERWYZER, et.al.

BEFORE THE ARBITRATION PANEL OF THE
NATIONAL ASSOCIATION OF SECURITIES DEALERS

STEVEN ONDERWYZER, TRUSTEE, CLAIRE ONDERWYZER TR, UAD 8/14/78; CLAIRE ONDERWYZER LIVING TR, UAD 7/17/95; STEVEN J. ONDERWYZER LIVING TR, UAD 7/17/95; ONDERWYZER TRUST #1, UAD 7/14/89; ONDERWYZER TRUST #2, UAD 7/14/89, STEVEN ONDERWYZER Claimants, vs. MILLER & SCHROEDER FINANCIAL, INC., a Minnesota corporation; MARSHALL, MILLER & SCHROEDER, INC.; JAMES DLUGOSCH, JAMES IVERSON, JOHN CLAREY, ROGER WICKNER, NANCY MELDON, VICTOR DHOOGE, TIMOTHY JONES, M.M.& S. FINANCIAL, INC., JEROME A. TABOLICH, EDWARD J. HENTGES, KENNETH R. LARSEN, STEVEN W. ERICKSON, PAUL R. EKHOLM, KENNETH HALLORAN, KENNETH DAWKINS, TOM S. NELSON, MARY JO BRENDEN, DANIEL DILL, Respondents.	Case No. 01-05301 **SECOND AMENDED STATEMENT OF CLAIM**

SRC1353

I.

INTRODUCTION

1. Miller and Schroeder Financial, Inc., ("Miller") was bought out in late 1996/early 1997 by its now CEO, Mr. James Dlugosch. Specifically, Mr. Dlugosch bought out the two former owners of Miller, Mr. James Iverson and Mr. Roger Wickner for about $17 million. On information and belief, the buy-out was financed from Miller's underwriting of bond deals, including Heritage Healthcare Bonds issued and sold throughout the country. The essence of these deals was that each of the parties involved would collect substantial fees for their participation passing the cost to the investors. These fees included underwriting fees for Miller, management fees for Mr. Kasirer, and architectural fees for Mr. Bertolini.

2. Due to the fact that the substantial fees were lining the pockets of the participants, certain disclosures and duties were overlooked and/or purposely not made, and Miller and its executives failed to properly perform the underwriting duties and subsequent disclosures mandated therefrom. Further, in order to "push" these shady deals, Miller enlisted the help of its army of brokers and made it known that Miller must sell these issues to rid their inventory of them. Of these brokers, Mr. Timothy Jones was the broker of Mr. Onderwyzer and sold Mr. Onderwyzer these bonds under the representations that they were safe, income producing municipal bonds. Mr. Onderwyzer has been retired for 13 years and placed his trust and confidence in Mr. Jones who represented he was an expert in these investments, that they were safe, income producing investments, and there was no risk of loss to the principal.

3. Eventually all of these bond deals collapsed, but only after Mr. Iverson and Mr. Wickner were paid, Mr. Dlugosch retained control of Miller, and the other parties collected their fees. Mr. Onderwyzer, along with many other bondholders including the Heartland Funds, were left holding the bag. Mr. Onderwyzer lost approximately $1.5 million of his retirement money.

4. Several indications of Miller's credibility in the bond business have recently arisen. Notably, Miller, one of its executive vice-presidents, and Miller's bond lawyer John Larsen recently

agreed to pay a total of $400,000 to settle allegations made by San Bernadino County, California, and several authorities, that they bribed county officials to obtain municipal bond business. In addition, there have been a litany of arbitration claims and civil actions filed (including a suit seeking class action status) against Miller making the same allegations as contained herein.

II.

PARTIES

5. Claimant, STEVEN J. ONDERWYZER, is and was during the relevant time period, the trustee of the CLAIRE ONDERWYZER TRUST (UAD 8/14/78), the CLAIRE ONDERWYZER LIVING TRUST (UAD 7/17/95), the STEVEN J. ONDERWYZER LIVING TRUST (UAD 7/17/95), the ONDERWYZER TRUST #1 (UAD 7/14/89), and the ONDERWYZER TRUST #2 (UAD 7/14/89)[collectively referred to herein as "the Trusts"]. Mr. Onderwyzer is a resident of California residing at 1 Jib St. Unit 301A, Marina Del Ray, California, 90292.

6. Respondent MILLER & SCHROEDER FINANCIAL, INC. (hereinafter "Miller") is Minnesota corporation with its principal place of business located at 150 South Fifth Street, Suite 3000, Minneapolis, Minnesota 55402. Miller is qualified to do business in California and is a licensed broker-dealer under the laws of California and the United States. Miller is a member of the National Association of Securities Dealers; Miller transacts business in the municipal securities market and is governed by the rules of the NASD, the Municipal Securities Rulemaking Board, the Securities and Exchange Commission, and federal and state securities laws. During the relevant time period, Miller maintained a branch office location in Solana Beach, California, from which it offered and sold securities (particularly, bond investments) to the public. The Solana Beach office has recently been closed due to Miller's exodus from the retail securities market.

7. Respondent MARSHALL, MILLER & SCHROEDER, INC. ("Marshall") is believed to have purchased Respondent MILLER & SCHROEDER FINANCIAL, INC. The

Minneapolis Secretary of State records shows that Marshall was formed on April 5, 2001. Current NASD records do not show a change in licensing or business structure.

8. Respondent James F. Dlugosch is Miller's Chief Executive Officer and Chair of the Board of Directors. On information and belief, Mr. Dlugosch and Mssrs. Iverson and Wickner organized the buy-out, which was to be financed through underwriting fees received from the Heritage bonds and other speculative bonds.

9. Respondent James Iverson was a former Director, Vice President, and controlling shareholder of Miller and Schroeder Financial, Inc. and now is employed by Miller. On information and belief, Mr. Iverson received buy-out payments for his interests in Miller & Schroeder Financial, Inc. based on proceeds from underwriting of the Heritage bonds.

10. Respondent Roger James Wickner was a President, Director, of Miller & Schroeder Financial, Inc., and was the former part-owner of Miller & Schroeder Financial, Inc.. On information and belief, Mr. Wickner received buy-out payments for his interests in Miller & Schroeder Financial, Inc. based on proceeds from underwriting of the Heritage bonds.

11. Respondent Victor Dhooge was on information and belief the President (or held such title and responsibilities as would be commensurate with the title of President) of the Underwriting Department and organized, cooridinated, and performed or managed the performance of all Miller's due diligence responsibilities relating to Miller's underwriting of bonds, which are the subject of this complaint.

12. Respondent Nancy Meldon was on information and belief the Chief Compliance Officer at Miller. Ms. Meldon was responsible for review, inspection, and approval of certain aspects of Miller's due diligence responsibilities and supervisory responsibilities over customer accounts including the accounts at issue.

13. Respondent John Clarey was an Owner of Miller and also had responsibilities for customer service and complaints. Mr. Clarey was a member of Miller's Credit Committee, which had oversight and approval powers and duties over all of Miller's underwriting ventures including the ones which are the subject of this complaint.

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14. Respondent Timothy Jones was a senior vice president and Mr. Onderwyzer's account executive at Miller's Solana Beach California office, which has since closed due to Miller's exodus from the retail securities market.

15. Respondent MM&S Financial. Inc. holds itself out to the public as a regulated entity composed of securities professionals specializing in municipal bonds. Beginning in 2000, Miller & Schroeder Financial, Inc. began divesting portions of its business and businesses to various individuals and entities, including respondent MM&S Financial, Inc. Respondent MM&S Financial, Inc. is conducting business from its Solana Beach, California location as the successor to Miller & Schroeder Financial, Inc.

16. Any and all references herein to Respondent MM&S Financial, Inc. shall be as successor to Miller & Schroeder Financial, Inc.

17. Any and all references herein to Miller & Schroeder Financial, Inc. shall be as predecessor to respondent MM&S Financial, Inc.

18. Claimants allege that Respondents, James E. Iverson, Jerome A Tabolich, Edward J. Hentges, Kenneth R. Larsen, Steven W. Erickson, Paul R. Ekholm, James F. Dlugosch, Kenneth Halloran, Kenneth E. Dawkins, Tom S. Nelson, John M. Clarey ,Victor Dhoogie, Mary Jo Brenden, Daniel Dill are and were at all relevant times, officers, underwriters, directors, members of the credit committee, and supervisors at Miller & Schroeder Financial, Inc. Miller & Schroeder Financial, Inc. filed bankruptcy on or about January 21, 2002. Claimants believes that these named individuals are members of the NASD and/or the Municipal Bond Securities group giving the NASD jurisdiction in this case.

19. Respondent Iverson, Clarey, Tabolich, Hentges, Larsen, Erickson, Ekholm, Dlugosch, Halloran, Dawkins, Nelson, Dhoogie, Brenden, and Dill were at all relevant times herein key officers, underwriters, directors, members of the credit committee, and supervisors of Miller & Schroeder Financial, Inc. predecessor to Respondent herein, MM&S Financial, Inc.and its associated entities with responsibility for the due diligence for the Heritage Health Care Bonds and other investments

including Boston Chicken, Jackson County Bonds, Service Merchandise Bonds, Globalstar Bonds, Beech Grove Bonds, Housing Authority of City of Tupelo Bonds, Dakota Colorado Bonds, Tillman Co. Bonds and others which were sold to the public including the claimants, causing the substantial losses to the claimants because of the action of the 'CONTROL PERSONS" and Miller & Schroeder Financial, Inc. predecessor to third party respondent herein, MM&S Financial, Inc. At all times during the actions alleged herein, control person respondents were agents and coconspirators of each other in the activities alleged.

ALTER EGO ALLEGATIONS

20. There exists, and at all times herein mentioned there existed, a unity of interest and ownership between all respondents, and each of them, and all the other remaining respondents, and each; of them, such that any individuality and separateness between all respondents, and each of them and the respondent corporate entities, has ceased to exist, and all the respondents corporate entities are the alter egos of respondents, and each of them, in that claimants allege that each of the individual third respondents used the assets of the respondent corporate entities to cause the losses to claimants alleged herein.

21. Adherence to the fiction of the separate existence of any respondent corporate entity as an entity distinct from any of the other respondents, individual or corporate, would permit an abuse of the corporate privilege and would promote injustice in that such asserting respondents, and each of them, would be shielded from their proper and lawful obligations, and would allow the perpetration of acts of bad faith and malfeasance without financial liability.

III.

FACTUAL ALLEGATIONS

22. Miller held itself out as an experienced underwriter of fixed income securities.

23. Jones and Miller at all material times were governed by state and federal securities laws, the rules and regulations of the NASD, the Securities and Exchange Commission, the Municipal Securities Rulemaking Board, and the California Department of Corporations.

24. Mr. Onderwyzer has been retired for 13 years and pays for his family's living expenses exclusively from the interest income of their investments. At all relevant times, Mr. Jones was aware and knew that Mr. Onderwyzer depended on such income for his support and the support of his sister who is mentally ill with schizophrenia.

25. Sometime in 1997, Mr. Onderwyzer saw a television advertisement or an advertisement in the Los Angeles Times newspaper regarding municipal bonds and Miller & Schroeder. Interested in gaining access to safe municipal bond investments, Mr. Onderwyzer called Miller and was referred to Mr. Jones. After several discussions over the course of a few months, Jones gained Mr. Onderwyzer's trust and confidence. Mr. Onderwyzer expressed his goals of investing for safety of principal and income. Jones and Miller represented that they were very experienced in tax-free municipal bond offerings as well as other bond offerings and agreed they would recommend bond investments commensurate with Mr. Onderwyzer's expressed goals.

26. In stark disregard for Mr. Onderwyzer's requests for safe municipal bond investments, Miller and Jones recommended and sold to Mr. Onderwyzer many bonds outside of these stated objectives. Jones recommended several bonds underwritten by Miller and represented these bonds to be safe, income producing investments.

27. Over the course of their relationship, Jones persuaded Mr. Onderwyzer to invest in "Heritage"[1] industrial revenue bonds and several other bond offerings promoted by Miller. Eventually, most of these investments would either default, enter bankruptcy, or the underlying value become worthless. Mr. Onderwyzer's losses from the Heritage bond investments with Miller totaled $1.5 million.

28. At all relevant times surrounding Mr. Onderwyzer's bond purchases, Jones and Miller represented that the bonds were low-risk in character. On several occasions, Jones, in order to assure Mr. Onderwyzer of the Heritage bonds' risk level, represented the investments were safe. Jones further represented on many occasions before and after the sales of the bonds to Mr. Onderwyzer that he and other executives at Miller had personally inspected the facilities and that the Heritage entities

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[1] The Heritage bonds include all bonds offered through the various Heritage entities in various states.

were completing their stated objectives according to plan and there were "no problems" with the projects. Moreover, Jones stated that the hospitals were 90% occupied (and/or there was a waiting list to get in) and all bonds had debt service ratios of at least 1.5 times that needed.

29. At all material times, Miller, First Wall Street, Pumar and Jones knew or should have known that the bonds were unrated, or of questionable viability, and that, if rated, such rating would have been such as to indicate that the ability of Heritage to meet their obligations in connection with the debentures was subject to substantial doubt in light of its financial condition at the time of the offering and their then recent financial history. Thereby meaning that the bonds were in fact not "safe" and were extremely risky.

30. Further, Miller and Jones knew or should have known, due to their underwriting research and position as financial advisor to Heritage, that the financial condition of Heritage was such that the projects were not feasible from inception due to several factors including but not limited to: 1) the "soft costs" (fees to consummate the deals) of the projects were too high on a percentage basis, 2) revenues to be derived from the facilities were unreasonably overstated, 3) the appraisal values of the land and facilities were overstated, and 4) the costs and expenses for operating long-term health care facilities were unreasonably underestimated.

31. In connection with the sales of the debentures and with the intent of inducing Mr. Onderwyzer to purchase the debentures, Miller and Jones failed to disclose material negative and adverse facts, which facts were known to Miller and Jones or would have been known to them in the exercise of reasonable care, including but not limited to the following:

a. The audited financial statements were outdated.

b. The issuers were highly leveraged.

c. The issuer's financial condition was such that it was unlikely to be able to service the debentures in accordance with the terms thereof.

d. From 1997 through the date of Claimant's purchases, the issuers earnings were either insufficient or barely sufficient to cover its then fixed charges.

e. The issuer's cash flows were negative or close thereto from their inception through the offering of the bonds.

SRC1360

f. The issuers customarily borrowed additional amounts to pay existing obligations.

g. Miller was compensated a high percentage of the principle amount of the securities offered.

h. Total expenses of the offering were an excessive percentage of the principle amounts offered.

i. A substantial portion of the earnings from the Heritage bonds was required to be paid to certain entities in which Heritage or their insiders had partial interests.

j. Heritage was insolvent at all relevant times herein.

k. There was significant commingling of funds among the different Heritage projects such that the Heritage combined offerings violated the applicable Bond documents and thus was misrepresented in the various prospectuses provided to the bondholders

32. The misrepresentations and omissions of material facts related to the sales of the debentures by Miller and Jones violated state and federal laws regulating underwriters, the rules, regulations, standards of conduct imposed on licensed brokers and agents by the SEC, the California Department of Corporations, the Municipal Securities Rulemaking Board and the NASD.

33. Said misrepresentations and omissions of material facts were made negligently and/or purposefully and with intent in order to accomplish the sale of the debentures to Mr. Onderwyzer.

34. The purchases by Mr. Onderwyzer were made in reliance upon and/or assuming the absence of any material negative information about the issuer of the debentures. Mr. Onderwyzer's reliance on his broker was justified in that Mr. Onderwyzer is retired and relied on the statements of his broker due to the trust and confidence relinquished to Mr. Jones by way of his fiduciary relationship with Mr. Onderwyzer.

35. Not until after Mr. Onderwyzer's purchase of the debentures, which determination was based on the oral representations of Jones (no other information having been provided to Mr. Onderwyzer when the decision to purchase was made), which representations were misleading because they did not include any material adverse or negative information about the Heritage entities, did Miller furnish to Mr. Onderwyzer a prospectus that described such debentures.

36. Even though a prospectus was eventually provided, the Appraisal reports purporting to provide the basis for land and facilities valuations were not included in any prospectus.

BACKGROUND INFORMATION ON MILLER & SCHROEDER, INC.

37. On information and belief, Mr. James Iverson and Mr. Roger Wickner were the owners of Miller until sometime in early 1997. Mr. James Dulugosh arranged to buy out Iverson and Wickner and finance the buy-out with income from the underwriting of speculative municipal bonds.

38. On information and belief, the buy-out contract's terms included payments over a three-year period totaling $17 million dollars. Concurrently, Miller began underwriting a large amount of speculative municipal bond deals. These deals were commonly negotiated bids, as opposed to competitively bid deals where other underwriters bid for the deal. On information and belief, these deals included the Heritage bonds and essentially allowed Miller to set its underwriting fee at a very large percentage—amounting to about 5% in underwriting fees as opposed to the industry standard of 1-2%.

39. In fact, Miller has underwritten over 80 municipal bond deals that have defaulted or gone into bankruptcy in the past several years. Miller has reaped untold millions of dollars in fees for organizing these deals all under the radar of the SEC and other regulatory agencies.

FIRST CLAIM

BREACH OF FIDUCIARY DUTY AND BREACH OF THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING

40. Claimant repeats and incorporates all preceding relevant paragraphs.

41. At all times herein mentioned, there existed between Respondents and Claimant a fiduciary relationship which arose from the Respondents serving as the agent in executing transactions for Claimant. This fiduciary duty mandates honesty, fair dealing and a duty to inform clients of material information regarding their relationship and exercise reasonable care in handling Claimant's Account. Gaining the trust and confidence of Claimant, Respondents owed to Claimant the highest standard of care, loyalty and fiduciary duty.

42. Respondents breached their fiduciary duty to Claimant by:

a. Failure to adequately disclose the true risks and facts associated with the various bond sales to Claimant;

b. Materially misrepresenting and/or omitting to disclose the true risks and facts associated with the various bond sales to Claimant;

c. Failing to implement a system of supervision and/or failing to supervise its employees and agents as set forth hereinafter:

d. Placing Respondents' own interests ahead of it customer's interests.

43. As a result of the aforementioned acts of Respondents, Claimant was actually and proximately harmed by the purchases of the various bonds sold and underwritten by Miller. Further, the aforementioned acts of Respondents were willful, wanton, malicious, and oppressive and justify an award of exemplary and punitive damages in an amount to be proven at trial.

SECOND CLAIM

PROFESSIONAL NEGLIGENCE: VIOLATION OF NASD AND NYSE CONDUCT RULES

44. Claimant repeats and incorporates all previous relevant paragraphs.

NASD RULE 2110 – "STANDARDS OF CONDUCT"

45. The conduct of Miller constituted a willful and/or intentional violation of NASD Conduct Rule 2110 in that it had the responsibility to observe high standards of commercial honor and just and equitable principles of trade; and engaged in acts practices and course of business which operated as a breach of such responsibilities.

2210 – "COMMUNICATIONS WITH THE PUBLIC"

46. The conduct of Miller constituted a willful and/or intentional violation of NASD Conduct Rule 2210 in that it had the responsibility to insure that its advertisements and correspondence with the public and customers were based on principles of fair dealing and good faith and did not omit any

material fact; and engaged in acts practices and courses of business which operated as a breach of such responsibilities.

3010 – "SUPERVISION"

47. The conduct of Miller constituted a willful and/or intentional violation of NASD Conduct Rule 3010 in that it had the responsibility to establish a system to supervise it agents and employees in each of its offices, departments and/or business activities, which was reasonably designed to achieve compliance with all applicable securities laws and regulations and with the rules of the NASD; and engaged in acts practices and courses of business which operated as a breach of such responsibilities.

IM – 2310 – 2 – "FAIR DEALING WITH CUSTOMERS"

48. The conduct of Miller constituted a willful and/or intentional violation of NASD Conduct Rule 2310 in that it had the responsibility to deal fairly in all interactions with customers; and engaged in acts practices and courses of business which operated as a breach of such responsibilities.

THIRD CLAIM

VIOLATION OF SECTIONS 10 (B) AND 20 OF THE SECURITIES EXCHANGE ACT OF 1934 AND RULE 10B-5 OF THE SECURITIES EXCHANGED COMMISSION

49. Claimant repeats and incorporates all previous relevant paragraphs.

50. Respondents are liable as controlling persons for the damages herein alleged under Section 20 of the Securities Exchange Act of 1934 and under the doctrine of *respondent superior.*

FRAUD, DECEIT, AND OMISSION OF MATERIAL FACT

Respondents engaged in an unlawful course of conduct, pursuant to which they knowingly and/or recklessly made representations with no reasonable basis in fact and which acted as a fraud upon Claimant. Respondents made various untrue statements of material facts and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, no misleading to Claimant.

SRC1364

51. Respondents further engaged in an unlawful course of conduct specifically prohibited by the SEC as a violation of Rule 10b-5 in that they induced purchases of the various bonds without disclosure of all material adverse and negative facts which Respondent knew and was aware of and further misrepresented material facts concerning the various bond investments.

52. Claimant relied on Respondent's material misrepresentations and/or non-disclosure to his detriment. As a result of the aforementioned acts of Respondents, Claimant was actually and proximately harmed by the substantial decline of the value of his investments. Further, the aforementioned acts of Respondents were willful, wanton, malicious, and oppressive and justify an award of exemplary and punitive damages in an amount to be proven at trial.

FOURTH CLAIM

CONSTRUCTIVE FRAUD

53. Claimant repeats and incorporates all previous relevant paragraphs.

54. As set forth above, a fiduciary relationship arose from the Respondents serving as advisors and brokers for Claimant and from the contracts executed by the parties. The fiduciary duty mandates honesty, fair dealing, a duty to exercise reasonable care in handling customer accounts, and the obligation to accurately disclose known material facts.

55. Respondents made material misrepresentations with regard to the nature and extent of the risks and material facts relevant to the various bond investments. Respondents had knowledge of the falsity and/or lacked reasonable grounds to believe in its truth and/or suppressed the truth which amounted to a breach of duty or intentional deception on behalf of the Respondents.

56. Respondents did these acts with the intent to induce reliance and trust by Claimant in Respondents and to placate Claimant. Claimant did in fact place his confidence in Respondents' false representations and material omissions.

57. As a result of the aforementioned acts of Respondents, Claimant was actually and proximately harmed by the substantial decline in the value of the various bond investments. Further,

the aforementioned acts of Respondents were willful, wanton, malicious, and oppressive and justify an award of exemplary and punitive damages in an amount to be proven at trial.

FIFTH CLAIM

NEGLIGENT MISREPRESENTATION

58. Claimant repeats and incorporates all previous relevant paragraphs.

59. Miller and Jones had and have a continuing duty to inform Claimant truthfully, accurately and fully about the characteristics and risks of the various bond investments.

60. Miller and Jones acted negligently and/or recklessly, in making various untrue statements of material fact and/or omitting to state material facts about the characteristics and risks of the various bond investments, as previously set forth herein, through oral and written communications, in order to induce Claimant to purchase said investments.

61. At the time these misrepresentations, misleading statements, and omissions were made, Claimant was ignorant of their falsity. Claimant justifiably relied, to his detriment, upon the superior knowledge and expertise of Miller and Jones, and on the misrepresentations, misleading statements, and omissions of Miller and Jones. Had Claimant been aware of the true facts, he would not have purchased said investments from Miller and Jones.

62. Further, Miller owed to Claimant a duty to disclose accurately, completely and fully all material facts that it knew or should have known and that were relevant to a decision to purchase the debentures.

63. Miller failed to exercise that degree of diligence and due care that Claimant was entitled to expect of Miller.

64. Miller owed to Claimant a duty of disclosure by virtue of its function as the underwriter of the debentures.

65. Miller failed to exercise due care and failed to satisfy its duty of disclosure in connection with the sales of the debentures to Claimant by misrepresenting and omitting material facts with

respect to the debentures. Miller knew, or in the exercise of reasonable care would have known, of those material facts and misrepresentations.

66. In connection with his decision to purchase the debentures, Claimant reasonably and detrimentally, relied on Miller's failure to disclose material negative and adverse information about the issuer of said debentures.

67. In connection with his reliance on Miller's failure to disclose material negative and adverse information about the issuer of said debentures and the assumed absence of such information Claimant exercised due care.

68. As a result, and in proximate consequence, of Miller and Jones's negligent failure to disclose material negative and adverse information to Claimant at the time he decided to purchase the debentures, Claimant has been damaged and is entitled to recover damages from Miller in an amount to be proven at trial.

SIXTH CLAIM

VIOLATIONS OF BUSINESS AND PROFESSIONS CODE SECTION 17200 et. seq., "UNFAIR TRADE PRACTICES ACT"

69. Claimant repeats and incorporates all previous relevant paragraphs.

70. The Unfair Trade Practices act defines unfair competition to include "any unfair, unlawful, or fraudulent" business act or practice. (Cal. Bus. & Prof. Code§17200) Unfair competition also includes "unfair, deceptive, untrue, or misleading advertising." The Act also provides for injunctive relief and restitution for violations.

71. Miller committed acts of unfair competition, as defined by Business & Professions Code Section 17200, by falsely and inaccurately making representations regarding the quality, risks, and economic viability of the various bond investments, when, in fact, Miller knew of material adverse and negative facts surrounding such bond investments. As a result, Claimant sustained substantial losses in his account.

SRC1367

72. Miller's failure to inform Claimant of the true quality, risks, and economic viability of the various bond investments was contrary to the representations it made in its advertisements, communications, and correspondence with Claimant and therefore violated Business & Professions Code §17200.

73. Pursuant to Business & Professions Code §17200 *et. seq.*, Claimant is entitled to enjoin Miller's wrongful practices and to obtain compensation for the losses they incurred by reason of Miller's unlawful, unfair and/or deceptive practices. As a direct and proximate result of the acts and practices alleged above Claimant is entitled to monetary losses suffered as a result of Miller's actions and disgorgement of Miller's ill-gotten gains in order to accomplish complete justice between the parties.

SEVENTH CLAIM

VIOLATION OF CONSUMER LEGAL REMEDIES ACT CALIFORNIA CIVIL CODE SECTION 1750 et. seq. AND CIVIL CODE SECTIONS 1709, 1710 FALSE ADVERTISING/ NEGLIGENT OR INTENTIONAL MISREPRESENTATION OF FACT

74. Claimant repeats and incorporates all previous relevant paragraphs.

75. The conduct of Miller constituted a violations of Section 1770, 1709, 1710 of the California Civil code, which prohibit unlawful advertising practices by representing that its bond offerings had characteristics and/or benefits which it did not have, namely (without limitation) that they were low-risk municipal bonds, that the financial circumstances surrounding the bonds were accurately represented, and that the bonds were guaranteed by Medicare, amongst other misrepresentations included in the preceding paragraphs.

76. Miller knew, or by the exercise of reasonable care should have known the various representations were false and/or misleading and that the statements Miller and its salespeople made in order to sell the bonds were inaccurate.

SRC1368

77. California Civil Code Section 1709 provides: "One who willfully deceives another with intent to induce him to alter his position to his injury or risk is liable for any damages which he thereby suffers."

78. California Civil Code Section 1710 provides: "A deceit, within the meaning of the last section, is either:

A. The suggestion, as a fact, of that which is not true, by one who does not believe it to be true;

B. The assertion, as a fact, of that which is not true, by one who has no reasonable ground for believing it to be true;

C. The suppression of a fact, by one who is bound to disclose it, or who gives information of other facts which are likely to mislead for want of communication of that fact; or

D. A promise made without any intention of performing it."

79. As a result of Respondents actions, Claimant suffered damages in an amount according to proof at the arbitration of this matter.

EIGHTH CLAIM

VIOLATION OF CALIFORNIA CORPORATIONS CODE SECTIONS 25401 et. seq. & 25501 et. seq.

80. Claimant repeats and incorporates all previous relevant paragraphs.

81. Respondents engaged in an unlawful course of conduct, pursuant to which they knowingly and/or recklessly made representations with no reasonable basis in fact and which acted as a fraud upon Claimant. Respondents made various untrue statements of material facts and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading to Claimant.

82. Claimant relied on Respondent's material misrepresentations and/or non-disclosures to their detriment. As a result of the aforementioned acts of Respondents, Claimant was actually and proximately harmed by substantial decline in the various bond investments offered by miller and Jones. Further, the aforementioned acts of Respondents were willful, wanton, malicious, and oppressive and justify an award of exemplary and punitive damages in an amount to be proven at trial.

NINTH CLAIM

NEGLIGENCE

83. Claimant repeats and incorporates all previous relevant paragraphs.

84. By underwriting the debentures, Miller implicitly represented that it had determined that such debentures were meritorious investments and that it had conducted its due diligence in accordance with the standards of the industry. Miller was obliged to disclose all material facts that it knew and that were reasonably ascertainable.

85. Miller was obliged not to underwrite, and not to offer or recommend to investors such as Claimant, securities that it had not affirmatively determined to be meritorious investments.

86. Miller was obligated to investigate the merits of a security such as the debentures before underwriting them and offering them to investors such as Claimant to determine whether such security was a meritorious investment.

87. By underwriting the debentures, Miller owed to Claimant a duty of due care and due diligence to investigate the merits of the debenture offering and to determine that there was a substantial likelihood that the various bond investments would be able to meet their obligations in accordance with the terms of such debentures.

88. By carelessly and negligently failing to affirmatively determine that there was a substantial likelihood that the various bond investments would be able to meet their obligations under the debentures, Miller failed to exercise its duty of due care and due diligence in connection with its underwriting of the debentures.

89. If Miller had properly carried out its due diligence responsibilities, it would be determined that the various bond investments were unlikely to be able to meet their obligations in accordance with the terms of such debentures.

90. In determining whether to purchase the debentures, Claimant was induced by, and reasonably relied upon Miller to properly perform its duties of due care and due diligence in underwriting said debentures.

91. But for Miller's negligence, Claimant would not have suffered substantial losses on his purchase of the debentures, and such losses were the proximate or foreseeable consequence of Miller's negligence.

92. In view of the absence of any material negative or adverse information about the issuer of the debentures at the time that the decision was made to purchase the debentures and in reliance on Miller's implicit representations, by underwriting the debentures, that such debentures were a meritorious investment, Claimant exercised due care.

93. As a result of Miller's careless and negligent underwriting of the debentures, Claimant has been damaged and is entitled to recover damages from Miller in an amount to be proven at trial.

TENTH CLAIM

VIOLATION OF §12 (2) OF THE SECURITIES ACT OF 1933

94. Claimant repeats and incorporates all previous relevant paragraphs.

95. Miller offered and sold a security, namely the debentures, by means of a prospectus and oral communications. This prospectus and oral communications contained untrue statements of material facts and omitted to state material facts necessary in order to make the statements and omissions Respondents knew, or in the exercise of reasonable care Respondents would have known, were false or were material facts which were required to be disclosed to avoid the representations which were made from being misleading.

96. Claimant did not know that the representations made to them by Miller regarding the matters described above were untrue and did not know the material facts that were not disclosed.

97. As a result of the matters set forth herein, pursuant to §12 (2) of the Securities Act, Claimant is entitled to rescind his purchases of the debentures and is entitled to interest on the amount paid for the debentures.

98. Miller is liable to Claimant pursuant to §12 (2) of the Securities Act.

99. Claimant did not know, and could not have known, of the facts upon which he has brought this claim sooner than one year before the date hereof. This claim is brought within three years from the date upon which the debentures were offered to the public.

ELEVENTH CLAIM

PROFESSIONAL NEGLIGENCE: VIOLATIONS OF MUNICIPAL SECURITIES RULEMAKING BOARD RULES

100. Claimant repeats and incorporates all previous relevant paragraphs.

101. Miller and Jones did not deal fairly with Mr. Onderwyzer who purchased the bonds.

102. For the reasons stated above, Respondents Miller and Jones, directly or indirectly, by use of the means or instrumentalities of interstate commerce, or of the mails, effected transactions in, or induced or attempted to induce the purchase or sale of municipal securities in contravention of Rule G-17 of the Municipal Securities Regulation Board.

103. By reasons of the foregoing transactions, acts, practices and courses of conduct, Respondents Miller and Jones violated Rule G-17 of the MSRB.

PRAYER

WHEREFORE, Claimant prays for damages in law and/or in equity and recovery against Respondents, and each of them, jointly and severally. The objective of this award is to make Claimant whole. That is, after attorneys' fees and costs are deducted from the award, Claimant should be left with 100% of his out-of-pocket losses. He is also entitled to receive imputed interest on his loss at the

legal rate from the first date of his loss. The appropriate "make-whole" amount for the Claimant is as follows:

1. For the decline in the value of his investments and the opportunity cost associated with said investments in the approximate sum of $2,000,000.

2. Pre-award and post-award interest of Ten percent (10%) from the date of the original investment as allowed by law in an amount to be proven at trial;

3. For costs of arbitration and expenses including reasonable attorneys' fees and the cost of expert witnesses, and any other costs deemed reasonable and just, in an amount to be proven at trial;

4. Damages pursuant to California Civil Code Sections 3294 and 3333;

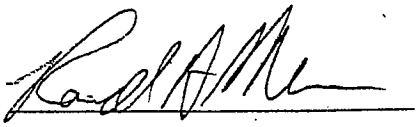
5. For such exemplary damages as to make an example of Respondents and to punish their conduct; and

6. For such further relief as the Court deems to be just and equitable.

RESPECTFULLY SUBMITTED:

October 1, 2001

MARRON & WILSON, LLP



Ronald A. Marron, Esq.
L. Michael Wilson, Esq.
Attorneys for Claimants

EXHIBIT J-1

AWARD

NASD Dispute Resolution, Inc.

In the Matter of the Arbitration Between:

Robert H. Lundquist, Individually and as Trustee of the Lundquist Family Trust UAD 12/09/83, Claimants v. Miller & Schroeder Financial, Inc., Respondent

Case Number: 00-04006 Hearing Site: Los Angeles, California

REPRESENTATION OF PARTIES

For Claimants:

Brad L. Milove, Esq.
W. Richard Sintek, Esq.
Miller, Milove & Kob
San Diego, California

Kathleen G. Smith, Esq.
Law Office of Kathleen G.
Manhattan Beach, California

For Miller & Schroeder Financial, Inc. (and for Mark Augusta until replaced by Steven M. Green, Esq. after the Hearings):

Lindsay G. Arthur, Jr., Esq.
Michael G. Brennan, Esq.
Arthur, Chapman, Kettering, Smetak, Pikala, P.A.
Minneapolis, Minnesota

Henry H. Rossbacher, Esq.
Rossbacher & Associates
Los Angeles, California

For Respondent Mark Augusta (following the conclusion of the Hearings):

Steven M. Green, Esq.
Law Office of Steven M. Green
San Diego, California

CASE INFORMATION

Statement of Claim filed: September 12, 2000

Claimants' Uniform Submission Agreement signed: September 8, 2000

Joint Statement of Answer filed by Miller & Schroeder Financial, Inc. and Mark Augusta: November 14, 2000

Miller & Schroeder Financial, Inc. and Mark Augusta's Joint Uniform Submission Agreement signed: November 3, 2000

CASE SUMMARY

Claimants alleged unsuitability, failure to supervise, misrepresentation, negligence, and breach of fiduciary duty. The allegations arose out of the purchase and/or sale of investments in Heritage bonds, Globalstar Telecommunications notes, Boston Chicken bonds, Brazos Sportswear bonds and City of Lancaster assessment bonds.

Miller & Schroeder Financial, Inc. and Mark Augusta denied the allegations of wrongdoing set forth in the Claimants' Statement of Claim.

RELIEF REQUESTED

Claimants requested compensatory damages of $230,000.00, bond interest, punitive damages, and unspecified damages for lost opportunity. Claimants also requested interest, and sought reimbursement for attorneys' fees and arbitration costs.

Miller & Schroeder Financial, Inc and Mark Augusta requested dismissal of Claimants' Statement of Claim in its entirety, and sought reimbursement for arbitration costs and attorneys' fees.

OTHER ISSUES CONSIDERED AND DECIDED

Upon notice of an arbitrator recusal, the parties conferred and on October 22, 2001 gave notice to NASD Dispute Resolution, Inc. that they stipulated to proceed with a two-member Panel.

At the close of the evidentiary hearing, the Panel agreed with counsel that the record would remain open for a period of time.

The Panel ordered post-hearing submissions and thereafter convened to deliberate on the remaining issues.

On February 14, 2002, the Panel was notified by NASD Dispute Resolution, Inc. that Miller & Schroeder Financial, Inc. had filed a Chapter 7 bankruptcy proceeding in the U.S. Bankruptcy Court. As a result of such filing (Case No. 02-40286-NCD, filed in on January 22, 2002, in Minneapolis, MN), all proceedings against such Respondent were stayed. Consequently, the Findings, Disposition of Pending Motions, Rulings and Award dated March 6, 2002 were issued only against Respondent Mark Augusta. On May 13, 2002, the Panel was notified by NASD Dispute Resolution, Inc. that the law firm of Arthur, Chapman et al. no longer represents Miller & Schroeder Financial, Inc., and on that same date the Panel was also notified by NASD Dispute Resolution, Inc. that on March 28, 2002 the Bankruptcy Court issued an "Order Granting Motion For Relief From Stay," stating in relevant part as follows:

> "NOW, THEREFORE, IT IS HEREBY ORDERED that the automatic stay of 11 U.S.C. § 362 is immediately terminated as to Robert Lundquist, individually and as Trustee of the Lundquist Family Trust U/A 12/09/83, and he is authorized to request the issuance of an arbitration award from the National Association of Securities Dealers, Inc. ("NASD") in connection with *In the Matter of the Arbitration Between Robert Lundquist, Individually and as Trustee of the Lundquist Family Trust U/A 12/09/83 v. Miller & Schroeder Financial, Inc. and Mark Augusta*, NASD Case Number 00-04006 with respect to the above-named Debtor, and seek confirmation of said award as a judgment in any appropriate state court or United States District Court. Such relief is specifically limited to exclude any action by Movant to seek collection of any judgment against assets of the Debtor, but does not limit Movant's right to seek collection of any judgment against Mark Augusta or any insurer of the Debtor or Mark Augusta. Notwithstanding Fed R. Bankr. P. 4001 (a)(3), this order is effective immediately."

Hence, in accordance with and consistent with the Order of the Bankruptcy Court, the Findings, Disposition of Pending Motions, Rulings and Award contained herein are now issued only against Respondent Miller & Schroeder Financial, Inc.

The parties agreed that the Award in this matter may be executed in counterpart copies or that a handwritten, signed Award may be entered.

AWARD

After considering the pleadings, testimony, and evidence presented at the hearing, and the post-hearing submissions, the Panel decided in full and final resolution of the issues submitted for determination against Respondent Miller & Schroeder Financial, Inc. only as follows:

This arbitration proceeding was [illegible] ("Claimant" or "Lundquist") [illegible] who became a widower upon the death of his wife in December of 1994 (some years after he had retired and they had moved from San Marino, CA to Joshua Tree, CA).

Claimant first opened an account with Miller & Schroeder Financial, Inc. ("M&SF") in 1990 – approximately seven years after his wife was diagnosed with Alzheimer's Disease. Respondent Mark Augusta ("Augusta") was the broker assigned by M&SF to Lundquist, 'by the luck of the draw', when Lundquist opened his initial account with M&SF, and Augusta thereafter remained Claimant's only broker at M&SF.

Lundquist had three accounts with M&SF, one of which was in his name as Trustee of the Family Trust established for him and his wife after she had become ill with Alzheimer's and another one of which was Claimant's IRA. The only investment objectives that were ever stated for any of Lundquist's accounts with M&SF were Income and Safety of Principal.

Over an extended period of time, beginning approximately in December 1996 and ending in March 1999, M&SF and Augusta solicited and recommended to Lundquist that he purchase for one or more of his accounts those certain securities (sometimes hereinafter referred to as "the securities") which are the subject of this arbitration proceeding, namely:

1) original issues of a number of unrated health care facility bonds that were underwritten and offered for sale by M&SF and that (with one exception) were exempt from federal income tax;
2) several other below-investment-grade debt securities of publicly held companies which were not 'new' issues and which were available for purchase in the general securities market place.

None of the health care facility bonds were required to be registered under the Securities Act of 1933. However, Official Statements were prepared by the issuers for each of the bond offerings, in collaboration with M&SF as the underwriter of the offerings. Lundquist testified that Augusta knew of his wife's battle with Alzheimer's, and Lundquist further testified that the health care bonds in question had a special appeal for him because the facilities to which the bond proceeds were to be applied would be used at least in part to accommodate persons suffering from Alzheimer's. Lundquist also testified that, had he been informed of all the risks that accompanied the securities referred to in (a) and (b) above, he would never have invested in them since safety of principal was an essential investment objective for him as a retired senior citizen whose financial resources were limited and whose employment earning power was essentially ended.

Claimant presented evidence to show that: 1) the health care facility bonds were secured solely by the prospective revenues to be generated from the operation of the facilities, and the real property value of the facilities themselves; 2) that there were material misstatements and omissions in the Official Statements for the original issues of the health care facility bonds; and 3) that M&SF and

Augusta misled him with respect to the other securities at issue in this proceeding (which were already outstanding and which were sold to him without the necessity of any current prospectus or Official Statement).

Lundquist further claimed that M&SF and Augusta knew or, in the exercise of due diligence and the discharge of their fiduciary obligations to him should have known, of these misstatements and omissions, so that they could and should have been fully disclosed to him (as a prospective investor) before any final investment decisions were made by him. The following are among the undisclosed problems cited by Claimant (which Claimant contended Respondents knew or should have known of) with respect to the health care facility bonds:

1) The real property collateral securing the bonds had deed restrictions prohibiting future use of that property for general hospital or any other similar purpose that could compete with the business of the former owners of the property;

2) The proceeds of each separate bond issue were supposed to be kept separate, but no public disclosure was ever made that in some instances the proceeds were co-mingled and applied to facilities different from the ones for which the Official Statement had indicated they were intended;

3) Construction delays and cost over-runs that had occurred in earlier projects under the same management as subsequent projects were not disclosed in the Official Statements for the subsequent projects;

4) M&SF made an undisclosed loan of a substantial sum of money to Health Care Holdings (an entity that had contracted with the issuers to manage the various different health care facilities) to assist Health Care on a short term basis in meeting its management obligations;

5) Certain materially negative information that was publicly available about the principal (i.e. Robert Kasirer) of Health Care Holdings and/or about certain entities controlled by Kasirer or in which he actively participated was not disclosed to Claimant, e.g.(a) accusations of bond fraud in 1990, (b) recorded tax and other liens, (c) recorded judgments, and (d) an IRS investigation.

Approximately ten months after the September 2000 date when Lundquist began this Arbitration Proceeding, M&SF entered into an Asset Purchase Agreement dated July 26, 2001 (the "APA") pursuant to which it sold certain of its assets on August 31, 2001 (the 'closing date") and the buyers named therein (the "Buyers") acquired those assets and assumed certain liabilities (but not the liabilities that are at issue in this proceeding) in exchange for consideration that was stated by Respondent's counsel in their October 22, 2001 letter to the NASD to be (a) $1,600,00 in cash and (b) the assumption of approximately $13,000,000 in liabilities.

However, the consideration figures given in Counsel's October 22, 2001 letter are not consistent with the express language in Article 3 of the APA (entitled "Purchase Price") which provides for "contingent" cash payments up to a cumulative maximum of $1,600,000, to be calculated and paid on a fiscal year basis as provided in Section 3.2 of the APA. Section 3.2 of the APA also provides for an annual limitation on the amount of any contingent payment made pursuant to Section 3.1(b). Additionally, under Section 3.1 of the APA there is also a possibility of further cash consideration, depending on whether the business that was being acquired by the Buyers experienced a profit or a loss during the period from May 1, 2001 through the August 31, 2001 closing date. Compounding the uncertainty as to what consideration was actually received, or to be received, by M&SF under the APA, John Clarey, an Executive Vice President of M&SF prior to his retirement on May 31, 2001, testified at the Hearing on the morning of October 30th that M&SF had received $1,000,000 cash from the Buyers under the APA when the APA was 'closed' on August 31, 2001.

In short, on the basis of the documentary evidence that was introduced, the testimony that was heard and the correspondence of counsel that was reviewed, it is not possible for the Panel to determine what was the total consideration that was received, or what is the contingent future consideration (if any) that may be received, by M&SF from the consummation of the APA.

Claimant asked the Panel to find that the consummation of the APA was:

(a) a fraudulent conveyance, and/or
(b) that the Buyers named in the APA were the alter ego of M&SF, and/or
(c) that the Buyers named in the APA were the successors-in-interest to M&SF, and/or
(d) that the corporate veil shielding the Buyers named in the APA should be 'pierced',

all with the goal of finding some liability from those Buyers to Claimant as well.

In addition, Claimant asked the Panel to find that certain other pre-Hearing transfers of assets by M&SF to various other persons and/or entities (none of whom were parties to this arbitration proceeding) were improper and should be set aside or otherwise challenged.

After the Hearings were concluded on November 2, 2001, but before the record was closed, the following occurred:

1) The Panel found that Claimant had presented sufficient convincing evidence to justify the award of exemplary damages, and ordered the production of certain documents; the Panel's order was duly complied with;

2) Respondents filed a Motion to Dismiss the Proceeding on the grounds that Claimant's counsel made materially false and misleading statements and representations regarding M&SF's knowledge of private causes of action, tax liens, judgments and IRS investigations of Robert Kasirer (the principal of Healthcare Holdings, Inc., which, as previously noted, was the operator of the health care facilities that were to have been financed by the proceeds of the health care bonds at issue in this proceeding) -- and led the Panel to believe that the information concerning those matters had been derived by Claimant's counsel from their review of M&SF's due diligence files when in fact there was no such information contained in any of those due diligence files of M&SF;

Claimant's counsel responded by stating that they had made no such representation, that the information was obtained by them from other, publicly-accessible sources and that in any event, if it was not in M&SF's due diligence files and was not in fact known by them (notwithstanding that Mr. Kasirer testified during the Hearing that he'd known Mr. Iverson [M&SF's President] for many years and had been fully interviewed by Mr. Iverson as a part of M&SF's due diligence investigation of him), it should have been known by them if they had exercised proper due diligence and discharged their fiduciary obligations to Claimant. However, in their "Opposition to Respondents' Motion to Dismiss" Claimant's counsel voluntarily withdrew their 10b-5 claim [and their Lancaster assessment bond claim for $6,225], stating that they had done so in order to "...alleviate any burden on Claimants and any reviewing Court when Respondents attack...the Award."

3) The Panel received a copy of Claimant's November 6, 2001 letter moving for an Order striking Respondents' 'Confidentiality Designation' of all documents and transcribed proceedings in this matter, except proprietary documents such as Respondent's Supervisory Manuals. The Panel received no response from Respondents to the Motion contained in Claimant's November 6th letter (nor did it ever receive a copy of Respondents' 'Confidentiality Designation').

4) The Panel received a written request from Claimant's counsel that it find that "...officers, directors and control persons of M&SF participated in the unlawful [sic] activity..." but that it not render an Award against any such persons who were not named as Respondents in the Statement of Claim.

FINDINGS AS TO RESPONDENT MILLER & SCHROEDER FINANCIAL, INC. ONLY

A. Miller & Schroeder Financial, Inc.:

1) underwrote, offered and sold unsuitable securities to Claimant;

2) misrepresented the securities that were sold to Claimant;

3) failed to exercise the requisite due diligence in its capacity as underwriter of the health care facility bonds that were sold to Claimant;

4) failed to supervise its broker, Mark Augusta, in the sale to Claimant of all those securities which are the subject of this proceeding;

5) breached its fiduciary duty with respect to the sale to Claimant of all those securities which are the subject of this proceeding;

6) acted recklessly and committed both constructive and actual fraud in its underwriting, soliciting, offering and sale to Claimant of all those securities which are the subject of this proceeding; and

7) acted deceitfully in its soliciting, offering and sale to Claimant of all those securities which are the subject of this proceeding.

B. Claimant's age was known to Respondent Miller & Schroeder Financial, Inc., and Claimant was at all relevant times a senior citizen within the meaning of California Civil Code § 1761 (f) and an "elder" under California Welfare & Institutions Code § 15610.27.

C. The conduct of Respondent Miller & Schroeder Financial, Inc. in recommending, soliciting, offering and selling to Claimant all the securities which are the subject of this proceeding was reckless and deceitful, and constituted actionable "abuse" within the meaning and scope of Sections 15610.30 and 15657 of the California Welfare and Institutions Code.

D. As to all other persons or entities that were not named as Respondents in Claimant's September 2000 Statement of Claim, that were not parties to any agreement to arbitrate any disputes with Claimant, that did not enter appearances in this proceeding and that were not represented in propria persona or by counsel in this proceeding, the Panel declines to make any findings; provided, however, that nothing contained in this Award is intended to, nor shall it be deemed to, foreclose any rights of Claimant to proceed against any or all of such other persons or entities in another proceeding in this forum or in any other available forum or court.

DISPOSITION OF PENDING MOTIONS AS TO RESPONDENT MILLER & SCHROEDER FINANCIAL, INC. ONLY

In its deliberations, the Panel has accepted as fact that none of the Exhibits attached to Respondents' November 16, 2001 Motion to Dismiss the Proceeding were in Miller & Schroeder Financial, Inc.'s due diligence files, and has further assumed that Respondents had no actual knowledge of any of those specific documents or, except as and to the extent that there was any contrary testimony (from

Robert Kasirer, James Iverson or any other witnesses), of the substantive contents of any of those documents. Accordingly, after due consideration, the Panel denies Respondent Miller & Schroeder Financial, Inc.'s Motion to Dismiss the Proceeding.

After due consideration, the November 6, 2001 Motion of Claimant for an Order Striking Respondent Miller & Schroeder Financial, Inc.'s 'Confidentiality Designation' is granted insofar as it relates to Respondent Miller & Schroeder Financial, Inc. only, except with respect to the following:

1) proprietary documents such as Miller & Schroeder Financial, Inc.'s Supervisory Manuals;

2) all documents produced by Respondent Miller & Schroeder Financial, Inc. in response to the Panel's November 6, 2001 letter requesting such documents.

RULINGS

A. Firstly, Claimant is awarded the following amounts against Respondent Miller & Schroeder Financial, Inc.:

1) $3,500,000.00 exemplary damages; and
2) $29,140.00 costs.

B. Secondly, Claimant is also awarded the following amounts against Respondent Miller & Schroeder Financial, Inc.:

1) $243,125.00 compensatory damages; and
2) $240,000.00 attorneys' fees (see paragraph C, below).

To the extent that Claimant recovers all or any part of said $243,125.00 in compensatory damages and/or $240,000.00 in attorneys' fees from Mark Augusta pursuant to the March 6, 2002 Award issued against Mark Augusta, the total amount of the category B awards referred to above shall be correspondingly reduced, so that in any case the total amount of such category B awards recovered by Claimant from Mark Augusta and Miller & Schroeder Financial, Inc. shall not in the aggregate exceed $243,125.00 for compensatory damages and $240,000.00 for attorneys' fees, respectively.

C. Thirdly, fees shall be assessed as set forth below.

All other relief requested and not expressly granted is denied.

FEES

Pursuant to the NASD Code of Arbitration Procedure, the following fees are assessed:

Filing Fees

NASD Dispute Resolution, Inc. received or will collect the non-refundable filing fees for each claim as follows:

Initial claim filing fee	= $ 300.00

Member Fees

Member fees are assessed to each member firm that is either a party in the matter or an employer of a respondent associated person at the time of the events which gave rise to the dispute, claim, or controversy. Accordingly, the member firm Miller & Schroeder Financial, Inc. is a party and the following fees are assessed:

Member Surcharge	= $ 1,500.00
Pre-Hearing Process Fee	= $ 600.00
Hearing Process Fee	= $ 2,500.00
Total Member Fees	**= $ 4,600.00**

Forum Fees and Assessments

The Panel assessed a forum fee for each pre-hearing conference or hearing session conducted. A pre-hearing conference and hearing session is any meeting between the parties and the Chair or Panel. The following fees are assessed:

1 Pre-hearing conference session with the Panel @ $1,125.00/session			= $1,125.00
Pre-hearing conference:	August 28, 2001	1 session	
7 Hearing sessions @ $1,125.00/session			= $7,875.00
Hearings:	October 29, 2001	2 sessions	
	October 30, 2001	2 sessions	
	October 31, 2001	2 sessions	
	November 1, 2001	1 session	
Total Forum Fees			**= $9,000.00**

The Panel assessed $ 9,000.00 of the forum fees to Respondent Miller & Schroeder Financial, Inc. To the extent that the NASD recovers all or any part of said $9,000.00 in forum fees from Mark Augusta pursuant to the March 6, 2002 Award issued against Mark Augusta, the total amount of

forum fees shall be correspondingly reduced, so that in any case the total amount of such forum fees recovered by the NASD from Mark Augusta and Miller & Schroeder Financial, Inc. shall not in the aggregate exceed $9,000.00.

Administrative Costs

Administrative costs are expenses incurred because a party requested additional services beyond the normal administrative services. These additional services include, but are not limited to, additional copies of Awards, copies of audio transcripts, retrieval of documents from archives, interpreters, security, and other requests.

Claimants requested 143 photocopies @ $ .50	= $ 71.50
Miller & Schroeder Financial, Inc. requested past Awards	= $ 70.00
Miller & Schroeder Financial, Inc. requested 651 photocopies @ $0.50	= $ 325.50

Fee Summary

Claimants are charged with the following fees and costs:

Initial Filing Fee	= $ 300.00
Administrative Costs	= $ 71.50
Total Fees	= $ 371.50
Less Payments	= $(1,425.00)
Refund Due Claimant	**= $(1,053.50)**

Respondent Miller & Schroeder Financial, Inc. is charged with the following fees and costs:

Member Fees	= $ 4,600.00
Forum Fees	= $ 9,000.00
Administrative Costs	= $ 395.50
Total Fees	= $13,995.50
Less Payments	=($ 4,600.00)
Balance Due NASD Dispute Resolution, Inc.	**= $ 9,395.50**

All balances are payable to NASD Dispute Resolution, Inc. and are due upon receipt of the Award pursuant to Rule 10330(g) of the Code

ARBITRATION PANEL

Alan Stamm, Esq. — *Chair, Public Arbitrator*
Allan D. Stampa — *Non-Public Arbitrator*

Concurring Arbitrators' Signatures

Alan Stamm, Esq.
Chair, Public Arbitrator

Signature Date

Allan D. Stampa
Non-Public Arbitrator

May 30, 2002
Signature Date

6/11/02
Date of Service

ARBITRATION PANEL

Alan Stamm, Esq. — *Chair, Public Arbitrator*
Allan D. Stampa — *Non-Public Arbitrator*

Concurring Arbitrators' Signatures

Alan Stamm

Alan Stamm, Esq.
Chair, Public Arbitrator

May 31, 2002
Signature Date

Allan D. Stampa
Non-Public Arbitrator

Signature Date

6/11/02
Date of Service

EXHIBIT K

Franklin Geerdes, Esq. State Bar No. 38566
Mary E. Geerdes, Esq. State Bar No. 174992
GEERDES & GEERDES
328 West Third Ave
Escondido, CA 92025
(760) 420-6560

Attorney for Claimant,
Chloe Kerns Edge TRS/Chloe Edge TR

NATIONAL ASSOCIATION OF SECURITIES DEALERS
NASD REGULATION - ARBITRATION TRIBUNAL

Chloe Kerns Edge TRS/Chloe Edge TR	NASDR ARBITRATION
Claimant,	Case No.: ___ ___ ___ _____
vs.	
Miller & Schroeder Financial, Inc., and Scott Penwarden	
	STATEMENT OF CLAIM
Respondents.	

Jurisdiction, Venue and Parties

Jurisdiction: The National Association of Securities Dealers/NASD Regulation, Inc. (NASDR) has jurisdiction under the Code of Arbitration Procedure (required submission) as each of the named Respondents was at all relevant times a member or a registered representative of or person associated with a member and bound to submit customer disputes to arbitration, regardless of the existence or nonexistence of a contractual arbitration agreement with a customer.

Venue: San Diego County California is a proper venue because the Claimant resides in County of San Diego, City of San Diego, and offices of the Respondents at which the subject transactions were conducted are were located in the County of San Diego, City of Carlsbad.

Claimant: The claimant Chloe Kerns Edge TRS/Chloe Edge TR

Respondents: The respondents are Miller & Schroeder Financial, Inc., and Scott Penwarden, its employee / representative. The main office address of MILLER & SCHROEDER FINANCIAL, INC., 150 South Fifth Street, Suite 3000, Minneapolis, Mn 55402-4200 P.O. Box 789, Minneapolis, Mn 55440-0789. The address of the local office at which the customer's account was held was MILLER & SCHROEDER FINANCIAL, INC. 505 Lomas Santa Fe Drive, Ste. 100, P.O. Box 946, Solana Beach, CA 92075-0946.

BACKGROUND FACTS

Re: Claimant, Chloe Kerns Edge TRS/Chloe Edge TR;
Account numbers # RI 2762712; # 38008892; # 38020178.

1. The underlying facts supporting the claim are without limitation as follows: In 1992, the customer opened an account with Miller & Schroeder through its representative, Mr. Scott Penwarden, to whom she had been referred by a retired Navy Captain who was a friend of her father who is also her father in law

2. The customer held the belief that tax free municipal bonds were safe as to yield and principal. That belief was based on the fact that her father held tax free municipal bearer bonds when he died and she thought him to be conservative in his investments.

3. The customer expressed [in several long initial conferences] to Mr. Penwarden that she knew nothing about bonds, and that she wanted safety of principal and that she thought that bonds were safe only because her father held them but needed Mr. Penwarden's expertise and knowledge relating to safety. Indeed her father held old bearer bonds subject to surrender to a bank at face value, bonds which may no longer frequent the market place.

4. The customer explained to Mr. Penwarden that she wanted to place one million dollars into safe investments, that she had inherited other money that she might invest in other things but wanted this account to be safe as to yield and principal, her safety net if everything else failed.

5. Mr. Penwarden asserted to the customer and her husband that Miller & Schroeder had not

experienced a bond default in sixty-five years and that the bonds selected for her would be of good and safe quality. Upon being pressed about the safety, Mr. Penwarden said that Miller & Schroeder had not had a bad bond in sixty-five years. Mr. Penwarden allowed as how there may have been a minor default but that Miller & Schroeder always made it good, and that times change but that the bonds purchased for her would be safe.

6. Thereafter the customer transferred cash and securities to Miller & Schroeder. The securities transferred included old bearer bonds from her father's estate to create a principal account of approximately one million dollars.

7. As bonds later were later paid off, Mr. Penwarden of Miller & Schroeder used the funds to purchase non rated [tax free] Municipal Bonds. The bonds so purchased were generally carried in the account at their purchase value instead of their true market value.

8. In February 1996, the customer's account(s) at Miller and Schroeder was worth $1,135,000 (document number 000158, appended), according to reports from Miller & Schroeder and its representative.

9. The customer believed, based on her trust in Mr. Penwarden, Miller & Schroeder, and the monthly statements, and Mr. Penwarden's repeated assurances, that her principal was safe and intact. Around late 2000, Mr. Penwarden called the customer to say that she should not be shocked when she got her new statement, that there was a change in reporting practice in the monthly statements. She was, however, greatly shocked to learn the true value of her account was substantially less than the purchase price or face value of the bonds, and that the true value of her account was substantially less than one million dollars.

10. At that time, Mr. Penwarden transferred to Paine Webber but the claimant did not sign transfer documents to Paine Webber, and instead transferred her accounts to Prudential Securities Incorporated where some of the [junk] bonds were sold off. The value of the account(s) as disclosed on the monthly statement of Prudential Securities for February 1, 2001 through February 28, 2001, was $608,824 (documents numbers 000984 - 000990, appended). The difference is $526,176, less withdrawals of principal in the amount of $78,600.00, showing a loss of principal in the amount of $447,576.00.

11. A part of the loss was fixed upon the sale of certain of the bonds by Prudential at market value. However, none of the loss would have occurred if the customer had been told the truth

at the very beginning of the account. The customer would not have invested in non rated tax free municipal bonds had she known that those bonds were not safe as to principal or yield, and that the true market value of the bonds dropped substantially as soon as the bonds were purchased for her. and that the purchase of the bonds would in truth and in fact not operate to maintain a true account value of at least one million dollars.

12. Neither Miller & Schroeder nor Mr. Penwarden ever disclosed to the customer that the value of the bonds was not equal to the purchase price or their face value, nor was it ever explained to the customer that non rated tax free municipals were valued at substantially less than their purchase price or face value immediately after the bonds were purchased for her, nor that the purchase of such bonds would fail to provide or maintain a true account value of at least one million dollars.

13. Neither Miller & Schroeder nor its representative explained to the customer the difference between rated bonds. rated insured bonds and non rated bonds, and that the latter were not safe as to yield or principal value. The customer repeatedly told the representative that her account (s) with Miller & Schroeder had to be safe and that the bonds purchased had to be safe. The customer was given repeated assurances of complete safety, assurances that were given at the beginning of the account and repeated at various times as late as the year 2000. In the case of Hesperia bonds, the representative said that he had made a personal inspection of the property underlying the bond and that it was in good condition and that the bond was safe. Default information received later disclosed that the property underlying the bonds was the subject of substantial deferred maintenance and in serious disrepair.

14. The customer was unsophisticated in securities generally and bonds in particular. That fact was known to Mr. Penwarden. She repeatedly informed the representative that she was unable to comprehend the monthly statements or the prospectuses received. Mr. Penwarden provided the customer with his own reports/schedules about the income to be expected from each of the bonds.

15. When several of the bonds defaulted, Mr. Penwarden told the customer that the defaults were only technical. that she would be paid and that her bonds were safe.

16. About the time [late 2000] that the monthly statements began showing true value rather than being carried at purchase price, Mr. Penwarden moved to a different broker as shown above. Among other things. Mr. Penwarden told this customer that he had not been satisfied

with the quality of bonds that Miller & Schroeder had been offering to its customers. He did not reveal that dissatisfaction while purchasing the bonds for the customer.

17. In the case of Globalstar, the only non municipal bond purchase, Mr. Penwarden strongly sold it to the customer on the basis that it was safe and suitable to her investment objective of safety in the account, and that he had purchased a "sizable amount" for himself and his wife.

18. The losses in the value of the account were caused by misrepresentations to the customer, breach of fiduciary duty, negligence and unsuitability as to the express needs and objectives of the customer and a failure of supervision by Miller & Schroeder. The claimant further says that Mr. Penwarden and Miller & Schroeder failed to comply with Municipal Securities Rule-making Board (MSRB) suitability and disclosure rules. The customer would not have followed the recommendations of Mr. Penwarden in the purchase of the bonds were it not for the misrepresentations and omissions of Mr. Penwarden the breach of duties set forth in this Statement of Claim.

Common Law Fraud/Misrepresentation

19. The claimant here incorporates the facts and allegations of fact set forth in paragraphs 1 through 18.

20. The courts have held that fraud may include (1) misrepresentation(false representation, false promise, or nondisclosure), (2) knowledge of falsity or reckless disregard for the truth or falsity (scienter), (3) intent to induce reliance, (4) the plaintiff's justifiable reliance on the misrepresentation, and (5) damage resulting from that reliance. However, the courts also instruct that the concept of fraud includes anything that is intended to deceive, including all statements, acts, concealments, and omissions involving a breach of legal or equitable duty, trust or confidence that results in injury to one who justifiably relies thereon. Ach v. Finkelstein (1968) 264 Cal. App. 2d 667, 674, 70 Cal. Rptr. 472. More particularly, a fraudulent misrepresentation is one made with the knowledge that it is or may be untrue, and with the intention that the person to whom it is made act in reliance on it. "But fraud occurs in so many situations that it is difficult to define, and each case must be considered on its own facts" Estate of Arbuckle (1950) 98 Cal. App. 2d 562, 568, 220 P.2d 950.

21. The claimant says that the statements, representations and assurances reported above

were made by Mr. Pen)rden with knowledge of falsity or reckless disregard for the truth or falsity, were made intent to induce reliance on the part of the claimant, and the claimant justifiably relied thereon, and damage resulted from that reliance as set forth in this Statement of Claim.

Fraud/Breach of Fiduciary Duty

22. The claimant here incorporates the facts and allegations of fact set forth in paragraphs 1 through 21.

23. The claimant alleges that a fiduciary relationship existed between the claimant and Mr. Penwarden and Miller & Schroeder. Mr. Penwarden at all times knew that the claimant was unsophisticated in securities matters and, especially, bonds. Moreover, Mr. Penwarden knew that he was in a superior position of knowledge and that the claimant relied upon him for information and recommendations concerning bond investments. Additionally, the fiduciary relationship is also predicated upon the relationship of customer and broker.

> A securities broker acts as an agent for his customers. Under the common law, any agent by virtue of his relationship to his principal is considered a fiduciary with respect to all matters within the scope of the agency. A broker is generally regarded by the courts as a fiduciary.
>
> A fiduciary, in turn, is subject to duties that "go beyond mere fairness and honesty; the oblige him to act to further the beneficiary's interests. A fiduciary owes his principal an obligation of diligent and faithful service similar to that of a trustee. In the famous words of Judge Benjamin Cardozo: "Many form of conduct permissible in the workaday world for those acting at arm's length, are forbidden to those bound by fiduciary duties. A trustee is held to something stricter than the morals of the market place. ... ."

24. The claimant and the respondents were in a fiduciary relationship with the respondents, owing the highest degree of care, good faith and honesty toward the claimant on the basis of the facts of that relationship and on the basis of their relationship as broker and his customer.

25. The respondents breached their duties when respondent Mr. Penwarden sought to gain the confidence of the claimant by misrepresenting that the company had no bond defaults in

65 years. Moreover, the breaches of duty included without limitation:

Failing to inform the claimant about the nature of bonds being offered by Miller & Schroder, that is, that the bonds were nonrated and that safety could only be achieved with highly-rated bonds or bonds that could be insured;

Assuring the customer that the bonds offered were safe;

Recommending the non rated Municipal Bonds as suitable to the customer's expressed objective of safety of principal;

Failing to inform the customer that the market value of the non rated bonds would generally be substantially less than the purchased price or face value immediately after purchase;

Strongly recommending Globalstar Bonds as suitable to the customer's expressed objective of safety of principal;

Failure to comply with MSRB Rule G-17 concerning the Conduct of Municipal Securities Activities. Rule G-17, the MSRB's fair dealing rule, encompasses two general principles. First, the rule imposes a duty on dealers not to engage in deceptive, dishonest, or unfair practices. This first prong of rule G-17 is essentially an antifraud prohibition. Second, the rule imposes a duty to deal fairly. It is under this second prong of rule G-17 that the MSRB has interpreted the rule to create affirmative disclosure obligations for dealers. These obligations require that a dealer disclose, at or before the sale of municipal securities to a customer, all material facts. Neither the SEC nor the MSRB has provided dealers with a checklist of material facts.

> **However, the standard set forth in TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976), is that a fact is material if there is a substantial likelihood that its disclosure would have been considered significant by a reasonable investor.**

In this case, the customer should have been fully informed of the nature of nonrated municipal bonds verus rated bonds and rated and insured bonds, the latter generally costing about one half percent of the purchase price, more or less. The information

would have been considered significant by this customer who sought safety and preservation of principal.

26. As a result of a breach of fiduciary duties by respondent Penwarden, the claimant suffered the losses and damage as described in this claim.

Negligence

27. The claimant here incorporates the facts and allegations of fact set forth in paragraphs 1 through 26.

28. Additionally, the acts and omissions of Respondent Penwarden were negligent, it being foreseeable that recommending the bonds as herein alleged would result in investments that were not within the customer's stated objectives and that the customer would be "shocked" when she learned the truth about the nature and market value of the bonds that were recommended for purchase, and that the customer would be moved to sell bonds that were worth less than their purchase price or face value or currently in default or in danger of default or in danger of further loss in value.

29. As a result of said negligence, the claimant accepted the recommendations of Respondent Penwarden and suffered loss in the value of the account as described in this claim.

Unsuitability per MSRB G-17

30. The claimant here incorporates the facts and allegations of fact set forth in paragraphs 1 through 29.

31. The claimant alleges that the recommendations made by Mr. Penwarden were also unsuitable under the Rule G-17. The text relating to Rule G-17under Breach of Fiduciary Duty above is here repeated:

32. Failure to comply with MSRB Rule G-17 concerning the Conduct of Municipal Securities Activities. Rule G-17, the MSRB's fair dealing rule, encompasses two general principles. First, the rule imposes a duty on dealers not to engage in deceptive, dishonest, or unfair practices. This first prong of rule G-17 is essentially an antifraud prohibition. Second, the rule imposes a duty to deal fairly. It is under this second prong of rule G-17 that

the MSRB has interpreted the rule to create affirmative disclosure obligations for dealers. These obligations require that a dealer disclose, at or before the sale of municipal securities to a customer, all material facts. Neither the SEC nor the MSRB has provided dealers with a checklist of material facts.

> **However, the standard set forth in TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976), is that a fact is material if there is a substantial likelihood that its disclosure would have been considered significant by a reasonable investor.**

33. In this case, compliance with the standard set forth in TSC Industries, Inc. created a duty to fully inform this customer of the nature of nonrated municipal bonds verus rated bonds and rated and insured bonds, the latter generally costing about one half percent of the purchase price, more or less. The information would have been considered significant by this customer who sought safety and preservation of principal.

34. The claimant would not have purchased the non rated municipal securities if the claimant had been informed of the nature of the non rated municipal securities and had been informed of the nature of rated and/or rated and insured Municipal Bonds.

35. As a result of the alleged non-compliance with the Rule, the claimant suffered damages as set forth in this Statement of Claim.

<u>Miller & Schroeder Failure to Supervise/Breach of Fiduciary Duty</u>

36. The claimant here incorporates the facts and allegations of fact set forth in paragraphs 1 through 35.

37. The claimant asserts that as the employer broker of Mr. Penwarden, and as a fiduciary of the claimant, Miller & Schroeder was under a duty to adequately supervise the activities of Mr. Penwarden. More specifically, the claimant asserts that as a fiduciary and to comply with MSRB Rule G-17 as set forth herein, Miller & Schroeder owed a duty in insure that its employee, Mr. Penwarden, provided full and complete information to this customer of the nature of nonrated municipal bonds verus rated bonds and rated and insured bonds, the latter generally costing about one half percent of the purchase price, more or less.

38. The claimant is informed and believed that Miller & Schroeder did not so supervise its employee, Mr. Penwarden, nor set in place any means to assure compliance with its duty as

herein alleged.

39. As a result of said lack of supervision, the claimant suffered damages as set forth in this Statement of Claim.

Miller & Schroder - Respondeat Superior and Agency law

40. The claimant further alleges that Miller & Schroder is legally responsible and liable for the acts and omissions of Mr. Penwarden based on the Doctrine of Respondeat Superior and on the Law of Agency

Exemplary and Punitive Damages

44. The claimant here incorporates the facts and allegations of fact set forth in paragraphs 1 through 40.

45. The claimant asserts that the Fraud, Breaches of Fiduciary Duties by the respondents in this case, as alleged herein, demonstrate that the conduct, actions, and omissions, as hereinbefore described were willful, intentional, and in any case done in a willful and conscious disregard of the rights of the claimant and with oppression, fraud and malice, and amounted to despicable conduct within the meaning of California Civil Code Section 3924 (c), entitling the claimant to punitive damages in an amount deemed appropriate by the Arbitrators, not to the amount of $447,576.00.

The claimant seeks an award as follows:

The claimant seeks an award as follows:

1. The sum of $447,576.00 [reference paragraph 10 above] or according to proof at Arbitration:
2. A reasonable rate of return on the sum of $447,576.00, from after the date of February 1, 2001 [reference paragraph 10 above] to the date of an award herein.
3. Interest on any award in favor of the claimant in an amount authorized by law until the award is paid.
4. Exemplary and Punitive Damages as the arbitrators may deem appropriate, not to exceed $50,000.00.
5. Such other relief as the arbitrators may deem appropriate.

Documents referred to in this statement of claim are incorporated, attached and number stamped. The number stamps generally appear at the upper right hand portion of the document subject to noninterference with the location of text. The numbers of the documents are: documents 000158 and 000984-000990 .

DATED: 6/6/01

Chloe Kerns Edge

Chloe Kerns Edge TRS/Chloe Edge TR

DATED: 6-6-01

Franklin Geerdes, Esq.
Mary E. Geerdes, Esq.
GEERDES & GEERDES
Attorneys for Claimant

EXHIBIT K-1

B10 (Official Form 10) (4/98)

UNITED STATES BANKRUPTCY COURT DISTRICT OF MINNESOTA		PROOF OF CLAIM
Name of Debtor: SRC HOLDING CORPORATION	Case Number: 02-40284	RECEIVED 2002 MAY -6 PM 1:56 U.S. BANKRUPTCY COURT
NOTE: This form should not be used to make a claim for administrative expense arising after the commencement of the case. A "request" for payment of an administrative expense may be filed pursuant to 11 U.S.C. § 503.		
Name of Creditor: (The person or entity to whom the debtor owes money or property BAKER LIVING TRUST UAD 3-5-86 Name and address where notices should be sent: BAKER LIVING TRUST UAD 3-5-86 C/O JOHN R STOEBNER, ESQ. LAPP, LIBRA, THOMSON, STOEBNER & PUSCH, CHARTERED 120 SOUTH SIXTH STREET, SUITE 2500 MINNEAPOLIS, MN 55402 Telephone number: 612-338-5815	☐ Check box if you are aware that anyone else has filed a proof of claim relating to your claim. Attach copy of statement giving particulars. ☐ Check box if you have never received any notices from the bankruptcy court in this case. ■ Check box if the address differs from the address on the envelope sent to you by the court.	THIS SPACE IS FOR COURT USE ONLY 5
Account or other number by which creditor identifies debtor:	Check here if this claim: ☐ replaces ☐ amends a previously filed court claim dated: _____	

1. Basis for Claim:
☐ Goods sold
☐ Services performed
☐ Money loaned
☐ Personal injury/wrongful death
☐ Taxes
■ Other BOND INVESTMENTS

☐ Retiree benefits as defined in 11 U.S.C. § 1114 (a)
☐ Wages, salaries, and compensation (Fill out below)
Your SS# _____
Unpaid compensation for services performed
from _____ (date) to _____ (date)

2. Date debt was incurred: 1994 THROUGH 1999

3. If court judgment, date obtained:

4. Total amount of Claim at Time Case Filed: $ 616,876.00 .

If all or part of your claim is secured or entitled to priority, also complete Item 5 or 6 below.
☐ Check this box if claim includes interest or other charges in addition to the principal amount of the claim. Attach itemized statement of all interest or additional charges.

5. Secured Claim
☐ Check this box if your claim is secured by collateral (including a right of setoff).
Brief Description of Collateral:
☐ Real Estate ☐ Motor Vehicle
☐ Other _____

Value of Collateral: $_____

Amount of arrearage and other charges at time case filed included in secured claim, if any:
$_____

6. Unsecured Priority Claim
☐ Check this box if you have an unsecured priority claim
Amount entitled to priority claim $_____
Specify the priority of the claim:
☐ Wages, salaries, or commissions (up to $4,300*), earned within 90 days before filing of the bankruptcy petition or cessation of the debtor's business, whichever is earlier — 11 U.S.C. § 507 (a)(3)
☐ Contributions to an employee benefit plan — 11 U.S.C. § 507 (a)(4)
☐ Up to $1,950* of deposits toward purchase, lease, or rental of property or services for personal, family, or household use — 11 U.S.C. § 507 (a)(6)
☐ Alimony, maintenance, or support owed to a spouse, former spouse, or child — 11 U.S.C. § 507 (a)(7)
☐ Taxes or other penalties of governmental units — 11 U.S.C. § 507 (a)(8)
☐ Other — Specify applicable paragraph of 11 U.S.C. § 507 (a)
_____

**Amounts are subject to adjustment on 4/1/98 and every 3 years thereafter with respect to cases commenced on or after the date of adjustment.*

7. **Credits:** The amount of all payments on this claim has been credited and deducted for the purpose of making this proof of claim.
8. **Supporting Documents:** *Attach copies of supporting documents*, such as promissory notes, purchase orders, invoices, itemized statements of running accounts, contracts, court judgments, mortgages, security agreements, and evidence of perfection of lien. DO NOT SEND ORIGINAL DOCUMENTS. If the documents are not available, explain. If the documents are voluminous, attach a summary.
9. **Date-Stamped Copy:** To receive an acknowledgment of the filing of your claim, enclosed a stamped, self-addressed envelope and copy of this proof of claim.

SEND CLAIMS TO:
U.S. Bankruptcy Court
301 U.S. Courthouse
300 South Fourth Street
Minneapolis, MN 55415

Date	Sign and print the name and title, if any, of the creditor or other person authorized to file this claim (attach copy of power of attorney, if any):
May 6, 2002	John R. Stoebner, Attorney for Baker Living Trust UAD 3-5-86

Penalty for presenting fraudulent claims: Fine of up to $500,000 or imprisonment for up to 5 years, or both. 18 U.S.C. §§ 152 and 3571.

For CHAPTER 7, 11 or 12 CASES filed on or after April 1, 1998

	A	B	C	D	E	F	G	H	I	J	K	L	M	N	O
1	4/15/15	3/16/09				BONDS ONLY-UPDATED 4-15-02									
2	Age of Charles Baker	AGE OF FRAN BAKER	BAKER'S ID NUM	AGENTS	PURCHASED OR EVENT DATE	TRANSACTIONS FROM MILLER AND SCHROEDER INC. AND THE SPELMAN CO.	PAR VALUE	ACQ. PRICE	SALE PRICE	DATE OF SALE	PROFIT/ LOSS OF BONDS	RATE	STATED MATURITY DATE	CUSPID-	comments
3	79	85	7B29	JONES	11/12/93	CEDAR CITY CORP- UTAH- IND DEVEL REV BDS (DCI INC PROJ) SER 1993	$10 000	$10 031	$7 740	5/31/01	($2,291)	8 000%	12/1/23	150056AK1	R-195
4	75	85	7B27 B.7b30 7b32	JONES	5/23/94	CITY OF INDIANAPOLIS-IN ,MULTI FAM HSG REV BD (SUNRISE APTS PROJ)-SERIES-C [illegible] bonds	$45,000	$44,454	$10 108	6/1/01	($34 346)	9 000%	6/1/19	455284AE9	C-154
5	75	85	7B30	JONES	2/21/94	CITY OF INDIANAPOLIS-M ULTI FAM HSG REV.BDS (SUNRISE APT PROJ (SERIES-C-)	see 7b27b		see below	6/1/01		9 000%	6/1/19	455284AE9	C-129
6	75	85	7B32	JONES	7/11/94	CITY OF INDIANAPOLIS-SUNRISE APT-SERIES-C-219	see7b27b		see above	6/1/01		9 000%	6/1/19	455284AE9	C-219
7	79	86	7B34	JONES	9/24/94	SOUTH EAST TEXAS HOUSING FINANCE CORP MULTI FAM HSG REV GARDLAND OAKS APT PROJ	$10 000	$10 016	$1	9/7/00	($10 015)	8 500%	8/1/24	841514 CG5	R0120
8	82	88	7B44	JONES	10/19/96	CITY OF INDIANAPOLIS ECON DEVEL REV BD (WILLOWBROOK APTS PROJ)JUNIOR SUBOR SER -1996D	$20 800	$20 800	$719	5/24/01	($20 081)	9 000%	7/1/26	455261 RRO	D-89
9	82	88	7B45	JONES	3/12/97	DANSFORTH HEALTH Fac Corp Rev Bd.(Sam Houston Long Term Care Fac Houston Tex)1997SER A	$20,000	$20,073	$2,269	5/30/01	($17,804)	8.250%	3/1/27	236141BH9	R0149
10	83	89	7B53	JONES	12/18/97	CITY OF FONTANA- CMNTY FAC DIST 90-3(EMPIRE CENTER)-SPEC.TX BOND SER A	$20,000	$19,891	$10,200	5/18/01	($9,791)	8.500%	4/1/21	344630EY0	#3148
11	83	89	7B55	JONES	7/8/98	DANFORTH HEALTH FAC CORP.REV BD (HERITAGE DUVAL GARDENS-AUSTIN TEX)1998 SRS -A	$20,000	$20,061	$1,022	5/29/01	($19,039)	7.375%	7/1/28	236141CF2	R0073
12	83	90	7B56	JONES	9/9/98	DESERT HOT SPRINGS PUBL FIN.AUTH.(HEALTH CARE REFUNDING.IMPT CERT OF PART -HERITAGE HOSP PROJ)1998 SERIES A	$20,000	$20 508	$1,338	5/31/01	($19,170)	6 500%	8/1/28	25041LAV3	R28-96
13	84	90	7B58	JONES	10/14/98	CITY OF CHICAGO-ILL HLTH. FACS REV BDS (HERITAGE CARE OF CHICAGO INC)1998 SERIES A	$10,000	$10,531	$559	5/29/01	($9,972)	7.625%	7/1/28	16753AAQ5	R0196
14	84	90	7B60B	JONES	12/16/98	ILLINOIS DEVEL FIN AUTH -MULTI FAM MTG REV BDS (SPRING GROVE APTS PRJ)SUBOR SER1998C	$35,000	$35,155	$11 487	5/18/01	($23,668)	8.000%	1/1/29	451915BG6	C29
15	84	90	7B61	JONES	3/4/99	INDUST.DEVEL AUTH- COUNTY OF JACKSON ,STATE OF MO - MULTI FAM HSG REV BDS (SANTA FE VLG APTS PROJ) SENIOR SER 1999A	$20,000	$20,128	$5,684	5/18/01	($14 444)	7 000%	7/1/29	467369AS3	R35
16	84	90	7B62	JONES	4/15/99	TARRANT COUNTY HEALTH FAC.DEV CORP REV BD (HERITAGE VALLEYGARDENS BROWNSVILLE TX) 1996 BRNSVLLE SER A	$25,000	$25,161	$1,150	5/30/01	($24,011)	7.750%	3/1/29	87638LFY1	RC108
17															
18	83	89	7B51	JONES	12/17/97	CITY OF BEECH GROVE ECONOMIC DEV REV DIPLOMAT SOUTH APTS PROJ	$25 000	$25,017	$2,500	estimated value	($22 517)	8 000%	1/1/28	076698-DG1	
19	79	85	7B31	JONES	3/29/94	INDUST DEV BD- CNTY OF HAMILTON TENN- MULTI FAM HSG REV (WATERFORD PL APTS)-SUBOR SER 1994 C-1	$10,000	$10,185	$5,000	estimated value	($5 185)	9 000%	2/1/14	407339AP5	RC-1-0036
20	82	88	7B46 and 7b60	JONES	5/7/97	TARRANT CNTY HEALTH FAC DEV CORP REC BD (ST JOSEPH L T CARE FAC FT WORTH TEX -SRS 1997A	$30,000	$30,661	$3,600	estimated value	($27 061)	8.500%	5/1/27	87636LBN9	R27-123
21	82	89	7B49	JONES	9/10/97	SHELBY CNTY TENN-HEALTH EDUC -HOUSING FAC BRD REV MULTI HSG JR SUB CORNERS SER 96C	$20 000	$20 582	$16,000	estimated value	($4,582)	8 000%	1/1/27	821697-PL7	R0037
22	83	89	7B50	JONES	10/22/97	CITY OF BEECH GROVE-INDIANA - ECON DEV REV BD (BEECH GROVE VILLAGE APTS PROJ)SENIOR SER 1997A	$20 000	$19 619	$6,000	estimated value	($13 619)	7 000%	1/1/28	076698-CB3	A185
23	83	89	7B52	JONES	12/15/97	CITY OF MEXICO BEACH PUBL SERV FAC REV BD MULTI-JURIS N P SERIES 1997-HERITAGE HOUSE OF SARASOTA-FLA PROJ)1997 SER -A	$29,000	$20,089	$5,000	estimated value	($15 089)	8 000%	12/1/27	59283TAQ3	R27-41
24	83	90	7B57	JONES	5/18/98	OKA COUNTY FIN AUTH MULTI FAM HSG (OKA CTY/MIDWEST CTY APTS POOL)SUBORD SER 1998C	$20,000	$20 102	$2,000	estimated value	($18 102)	8 000%	7/1/28	678902-CV7	R22
25	84	90	7B60	JONES	10/1/98	TARRANT CNTY HEALTH FAC DEV CORP REV BD (ST JOSEPH L T CAREFAC FT WORTH TEX)SRS1997A		see 7b46	see 7b46	estimated value		8 500%	5/1/27	87636LBN9	R27-363
26	84	90	7B59	JONES	10/16/98	TULSA CNTY STATE OF OK INDUST AUTH MULTI FAM HSG REV (SHADYBROOK APTS PROJ)SERIES 1998A	$20 000	$20 068	$14,000	est value	($6 068)	6 375%	7/1/28	899522 CE4	R16
27						TOTALS		$423 252	$106 377		($316 876)				

EXHIBIT L

ARTHUR, CHAPMAN, KETTERING, SMETAK & PIKALA. P.A.

Invoice No.	Invoice Date	Fees	Expenses	CLA
111022	9/30/2001	623.50	23.26	Chloe Kerns
111118	10/31/2001	2442.50	14.60	Chloe Kerns
111840	11/30/2001	746.00	48.00	Chloe Kerns
112355	12/31/2001	95.00	11.00	Chloe Kerns
112363	12/31/2001	0.00	10.20	Gerald F. Johansen
110289	8/31/2001	2864.00	35.60	FNB of the No.
111023	9/30/2001	11756.00	205.20	FNB of the No.
111115	10/31/2001	627.00	92.00	FNB of the No.
111841	11/30/2001	711.00	78.84	FNB of the No.
112356	12/31/2001	152.00	98.20	FNB of the No.
111116	10/31/2001	1188.00	762.84	Baker Living Trust
111842	11/30/2001	12.00	.46	Baker Living Trust
111117	10/31/2001	1956.00	442.48	Ralph E. Woodhouse
112362	12/31/2001	37.50	13.60	Steven Onderwyzer
112361	12/31/2001	0.00	16.80	Phillip J. Salley
112358	12/31/2001	2851.00	44.32	Frank T. Spangler
110287	8/31/2001	9698.25	60.86	Base File
111020	9/30/2001	5470.25	211.63	Base File
111113	10/31/2001	1444.75	32.39	Base File
111838	11/30/2001	3993.50	182.22	Base File
112353	12/31/2001	662.50	536.89	Base File
110288	8/31/2001	213.25	0.00	James D. Moreland
111021	9/30/2001	2423.00	141.04	James D. Moreland
111114	10/31/2001	1031.00	63.86	James D. Moreland
111839	11/30/2001	2064.00	139.32	James D. Moreland

112349	12/31/2001	38.00	3.20	James D. Moreland
110283	8/31/2001	100.00	4.69	Frederick Fink
111017	9/30/2001	946.00	8.20	Frederick Fink
111107	10/31/2001	169.00	1.00	Frederick Fink
111833	11/30/2001	0.00	4.36	Frederick Fink
112348	12/31/2001	0.00	645.05	Frederick Fink
110286	8/31/2001	1123.25	8.49	John Kocourek
111019	9/30/2001	3722.75	39.10	John Kocourek
111112	10/31/2001	16575.75	318.09	John Kocourek
111837	11/30/2001	745.00	2251.00	John Kocourek
112352	12/31/2001	0.00	40.77	John Kocourek
111111	10/31/2001	199.00	6.20	George McCauley
112351	12/31/2001	38.00	1.40	George McCauley
110285	8/31/2001	418.00	2.86	Fleshman Family Trust
111110	10/31/2001	19.00	.92	Fleshman Family Trust
111836	11/30/2001	0.00	1.20	Fleshman Family Trust
112350	12/31/2001	114.00	8.00	Fleshman Family Trust
111109	10/31/2001	43.00	47.48	English Irrevocable Trust
111835	11/30/2001	589.00	5.70	English Irrevocable Trust
111016	9/30/2001	925.00	8.16	John D. Behnke
111105	10/31/2001	2091.00	42.88	John D. Behnke
111831	11/30/2001	5049.50	1154.83	John D. Behnke
112346	12/31/2001	120.00	724.43	John D. Behnke
111106	10/31/2001	1245.00	332.54	Billy Lenser
111832	11/30/2001	0.00	21.95	Billy Lenser
112347	12/31/2001	0.00	246.93	Billy Lenser
110284	8/31/2001	407.50	0.00	Erwin J. Shustak
111018	9/30/2001	816.00	106.40	Erwin J. Shustak

111108	10/31/2001	336.00	24.60	Erwin J. Shustak
110280	8/31/2001	1315.50	0.00	Robert Lundquist
111012	9/30/2001	4536.75	116.45	Robert Lundquist
111101	10/31/2001	46006.00	1369.05	Robert Lundquist
111827	11/30/2001	6063.00	7597.02	Robert Lundquist
112344	12/31/2001	0.00	841.98	Robert Lundquist
111834	11/30/2001	76.00	1.80	Erwin Shustak
111100	10/31/2001	3644.00	4517.96	John Rohner
111826	11/30/2001	1182.50	643.90	John Rohner
112343	12/31/2001	38.00	55.18	John Rohner
110281	8/31/2001	294.50	7.52	Gold Family Trust
111014	9/30/2001	2815.75	53.50	Gold Family Trust
111103	10/31/2001	985.50	30.84	Gold Family Trust
111829	11/30/2001	2925.00	68.92	Gold Family Trust
112345	12/31/2001	0.00	27.11	Gold Family Trust
111015	9/30/2001	363.00	26.28	Sherman Peterson
111104	10/31/2001	76.00	7.04	Sherman Peterson
111830	11/30/2001	0.00	15.79	Sherman Peterson
110282	8/31/2001	330.50	21.69	John D. Behnke
111013	9/30/2001	407.50	.92	James McElfish
111102	10/31/2002	769.00	3.58	James McElfish
111828	11/30/2001	95.00	2.00	James McElfish
110279	8/31/2001	17396.50	723.57	John Rohner
111011	9/30/2001	39447.50	3956.26	John Rohner
TOTAL		**217,655.55**	**58,805.40**	

FAEGRE & BENSON

INVOICE NO.	INVOICE DATE	FEES	EXPENSES
599862	July 21, 1999	$607.50	$0.00
603605	September 1, 1999	22,572.50	1,011.15
606762	September 22, 1999	41,368.75	2,244.82
609111	October 18, 1999	8,592.50	2,033.59
612682	November 17, 1999	2,082.50	90.50
616395	December 13, 1999	7,655.00	20.27
620845	January 20, 2000	3,905.00	8.04
624502	February 23, 2000	2,363.75	1.40
627668	March 21, 2000	6,042.50	0.00
631857	April 25, 2000	12,966.25	777.29
635981	May 30, 2000	4,348.75	64.97
638375	June 21, 2000	3,746.25	193.70
642632	July 26, 2000	823.75	7.84
645254	August 22, 2000	2,280.00	7.90
648538	September 20, 2000	5,032.50	39.20
653750	October 25, 2000	10,262.50	331.58
657055	November 21, 2000	28,405.00	2,618.55
660893	December 19, 2000	20,530.75	814.97
664186	January 18, 2001	3,996.25	503.50
668901	February 23, 2001	2,092.50	259.44
672215	March 22, 2001	2,218.75	470.40
676276	April 24, 2001	2,242.50	982.69
680947	May 29, 2001	7,220.00	742.48
684814	June 27, 2001	9,591.25	227.43
688257	July 26, 2001	3,186.25	787.30

INVOICE NO.	INVOICE DATE	FEES	EXPENSES
693327	August 29, 2001	$3,908.75	$11.19
703157	November 16, 2001	75.00	0.00
707152	December 14, 2001	225.00	0.00
656875	November 21, 2000	2,062.50	0.00
660930	December 19, 2000	8,920.00	1,884.17
664386	January 19, 2001	7,507.50	671.99
668903	February 23, 2001	11,046.25	310.37
672047	March 21, 2001	2,987.50	153.94
676278	April 24, 2001	3,177.50	143.42
680948	May 29, 2001	587.50	1.88
684815	June 27, 2001	987.50	0.84
688259	July 26, 2001	680.00	338.79
693328	August 29, 2001	206.25	9.87
703158	November 16, 2001	450.00	0.00
707153	December 14, 2001	412.50	0.00
660929	December 19, 2000	56.25	0.00
664127	January 18, 2001	75.00	0.00
676279	April 24, 2001	68.75	0.00
680949	May 29, 2001	131.25	32.10
684813	June 27, 2001	5,135.00	287.62
688261	July 26, 2001	1,945.00	1,928.41
691443	August 20, 2001	401.25	77.50
693329	August 29, 2001	97.50	6.78
660928	December 19, 2000	1,737.50	204.15
664138	January 18, 2001	3,783.75	2,547.91
668924	February 23, 2001	1,985.00	417.76
672042	March 21, 2001	4,337.50	561.16

INVOICE NO.	INVOICE DATE	FEES	EXPENSES
676280	April 24, 2001	$3,688.75	$115.19
680950	May 29, 2001	3,037.50	218.86
684811	June 27, 2001	1,987.50	361.07
688262	July 26, 2001	2,622.50	32.18
691445	August 20, 2001	975.00	17.97
693330	August 29, 2001	0.00	7.57
660927	December 19, 2000	56.25	0.00
660926	December 19, 2000	753.75	0.00
664142	January 18, 2001	56.25	0.00
676281	April 24, 2001	75.00	0.00
660924	December 19, 2000	786.25	6.75
664145	January 18, 2001	2,996.25	417.32
668926	February 23, 2001	1,875.00	256.82
672040	March 21, 2001	5,696.25	352.77
676283	April 24, 2001	333.75	19.95
680952	May 29, 2001	165.00	3.23
691447	August 20, 2001	82.50	13.04
693331	August 29, 2001	82.50	11.02
700110	October 24, 2001	75.00	0.00
660923	December 19, 2000	93.75	0.00
668927	February 23, 2001	3.90	0.00
680705	May 24, 2001	465.00	55.16
684809	June 27, 2001	1,100.00	2.79
688263	July 26, 2001	1,347.50	2.79
664148	January 18, 2001	726.25	0.00
668931	February 23, 2001	7,636.25	1,919.98
672032	March 21, 2001	4,792.50	446.19

INVOICE NO.	INVOICE DATE	FEES	EXPENSES
676285	April 24, 2001	$230.00	$41.88
680953	May 29, 2001	517.50	113.85
684807	June 27, 2001	402.50	1.80
688267	July 26, 2001	3,538.75	25.73
691450	August 20, 2001	747.50	45.93
693333	August 29, 2001	625.00	26.13
664150	January 18, 2001	1,102.50	1.35
668930	February 23, 2001	6,185.00	777.30
672031	March 21, 2001	990.00	400.58
676286	April 24, 2001	1,946.25	357.48
680954	May 29, 2001	2,461.25	106.89
684806	June 27, 2001	3,383.75	153.63
688269	July 26, 2001	2,578.75	739.46
691451	August 20, 2001	715.00	914.86
693334	August 29, 2001	422.50	5.05
668928	February 23, 2001	7,038.75	771.24
672041	March 21, 2001	345.00	66.45
676287	April 24, 2001	4,120.00	1,010.44
680955	May 29, 2001	37.15	0.00
684805	June 27, 2001	370.00	117.26
688272	July 26, 2001	15.11	0.00
693335	August 29, 2001	57.50	47.80
668902	February 23, 2001	937.50	100.80
672045	March 21, 2001	3,156.25	1,125.95
676288	April 24, 2001	1,300.00	385.51
680957	May 29, 2001	2,392.50	182.94
684804	June 27, 2001	206.25	20.29

INVOICE NO.	INVOICE DATE	FEES	EXPENSES
688275	July 26, 2001	$1,400.00	$15.41
691453	August 20, 2001	1,280.00	20.55
693337	August 29, 2001	453.75	38.53
672048	March 21, 2001	93.75	0.00
676290	April 24, 2001	2,550.00	1,056.59
680959	May 29, 2001	1,087.50	300.11
684802	June 27, 2001	2,578.75	140.95
688278	July 26, 2001	2,203.75	127.79
691455	August 20, 2001	206.25	7.70
693338	August 29, 2001	82.50	4.53
672049	March 21, 2001	56.25	0.00
676291	April 24, 2001	4,772.50	774.22
680960	May 29, 2001	2,451.25	665.68
684800	June 27, 2001	5,161.25	1,162.68
688279	July 26, 2001	870.00	60.90
693339	August 29, 2001	0.00	2.75
680942	May 29, 2001	268.75	0.00
684799	June 27, 2001	3,120.00	65.01
688281	July 26, 2001	2,892.50	421.51
691456	August 20, 2001	245.00	43.13
693340	August 29, 2001	0.00	5.85
688282	July 26, 2001	0.00	2.61
680943	May 29, 2001	1,596.25	100.00
684797	June 27, 2001	2,165.00	922.11
688284	July 26, 2001	2,527.50	192.21
691458	August 20, 2001	32.50	0.00
693341	August 29, 2001	0.00	4.83

INVOICE NO.	INVOICE DATE	FEES	EXPENSES
680944	May 29, 2001	$125.00	$0.00
684796	June 27, 2001	6,222.50	9.26
688285	July 26, 2001	4,081.25	1,806.17
691460	August 20, 2001	236.25	1,308.63
693342	August 29, 2001	94.02	0.00
680945	May 29, 2001	443.75	0.00
684795	June 27, 2001	412.50	0.00
688286	July 26, 2001	144.45	0.00
	TOTAL:	$414,307.88	$44,889.82

EXHIBIT M

CHUBB

Chubb Group of Insurance Companies
82 Hopmeadow Street
P.O. Box 2002
Simsbury, CT 06070-7683
Phone: 860.408.2000 • Fax: 860.408.2002
www.chubb.com

May 12, 2003

Direct Dial: (860) 408-2574
Fax: (860) 408-2464
E-mail: smckelvey@chubb.com

Thomas C. Atmore
Leonard, O'Brien, Wilford, Spencer & Gale
55 East Fifth Street
Suite 800
St. Paul, MN 55101-1718

RE:	INSURED:	Miller and Schroeder, Inc.
	POLICY NO:	81666027
	CLAIM NO:	59159
	SUBJECT:	Hermann v. Miller & Schroeder Financial, Inc., et al.

Dear Mr. Atmore:

This letter is in response to our recent correspondence, including your letter dated April 29, 2003, and our telephone conversation of May 5, 2003, wherein you requested a coverage position relative to the entity Miller & Schroeder Financial, Inc. ("MSF") in the Heritage Bond matters.

You note a number of claims, both lawsuits and arbitrations, in your letter, including: Herrmann, Kellar, Onderwyzer, Cates, Moreland, Johansen, Baker Living Trust, Spangler, Formica, Timmerman, Salley, McGuire, and Hyde. We do not have copies of all these actions, but as you noted in our discussion, the claims alleged are similar in each case. Accordingly, we will address the claims set forth in the Herrmann lawsuit and the Timmerman NASD matters, which are representative of the other claims you have referenced, and copies of which we have in our possession. If any of the bankruptcy claims differ materially from the Herrmann or Timmerman claims, we urge you to submit those claims for analysis.

In both these claims, the claimants allege that MSF schemed to defraud investors by selling them bonds of questionable viability. Claimants further allege that MSF failed to disclose material negative and adverse facts. Further, as alleged in the Timmerman claim, following the collapse of the bond sales, claimants allege that MFS fraudulently conveyed its assets to Marshall, Miller & Schroeder ("MM&S") to avoid attachment under pending claims with regard to these bond offerings. The causes of action against MSF all stem from, or are related to, the allegedly unduly risky sale of the bonds.

ERII issued a Directors and Officers Liability Insurance Policy, Policy Number 8166-6027 to Miller and Schroeder, Inc. ("M&S" or the "Company") effective from July 31, 2000 to July 31, 2003 (the "Policy"). The Policy has a $5 million maximum aggregate limit of liability, inclusive of Defense Expenses, and a $50,000 per-claim retention for Insured Persons as to which indemnification by M&S is legally permissible and $100,000 for the Company.

Subject to all Policy terms and conditions, the Policy provides coverage for Loss from Claims first made against the Company during the Policy Period for Wrongful Acts. Under Section II(F) of the Policy, an Insured includes the Company. The Company is defined in Section II(C) as the Parent Corporation (M&S), and any Subsidiary created on or before the inception of the Policy. It is our understanding that MSF is a subsidiary of M&S, and, consequently, would fit this latter definition, and be an Insured under the Policy. ERII reserves its rights to deny coverage to MSF if we determine MSF is not a Subsidiary of M&S. Section II(B) defines a Claim as "*written notice received by an **Insured** that any person or entity intends to hold any **Insured** responsible for a **Wrongful Act**. A **Claim** will be deemed to have been made when such written notice is first received by any Insured.*" Section II(M) defines Wrongful Act in pertinent part as *"(4) any . . . actual or alleged error, omission, misstatement misleading statement or breach of duty by the Company."*

These matters appear to constitute Claims as each is written notice that the claimant intends to hold the Company responsible for breaches of duty allegedly committed by the Company. Although these matters constitute Claims, they are excluded from coverage pursuant to the following policy provisions.

The facts alleged in the underlying claims assert that the MSF and its representatives misrepresented the nature of the securities sold and that the securities recommended and sold by MSF were of questionable viability and not financially feasible. Thus, the claimants' allegations solely arise out of the offer or sale of securities. Endorsement No. 3 of the Policy provides that *"this Policy does not apply to any Claim based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged violation of:*

(1) the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, any other federal law, rule or regulation with respect to the

regulation of securities, any rules or regulations of the United States Securities and Exchange Commission, or any amendment of such laws, rules or regulations; or

(2) any state securities or "Blue Sky" laws or rules or regulations or any amendment of such laws, rules or regulations; or

(3) any provision of the common law imposing liability in connection with the offer, sale or purchase of securities.

All of the claimants' allegations arise out of the offer, sale or purchase of securities. As such, Endorsement No. 3 precludes coverage for these matters.

These matters also are excluded pursuant to the General E&O Exclusion found in Endorsement No. 9 of the Policy, which provides that

(1) No coverage will be available under the Policy for Loss including Defense Expenses for any Claim made against any Insured based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving an Insured's actual or alleged rendering or failure to render the following services:

Investment Banking Services
Security Broker/Dealer Services
Securities Underwriting

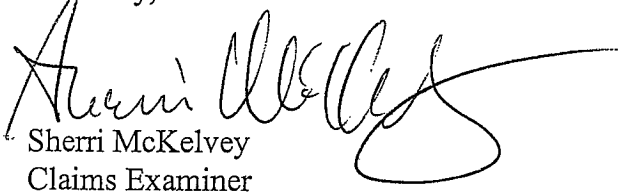
(2) Paragraph (1) above is not intended, however, nor shall it be construed, to apply to Loss, including Defense Expenses, in connection with any Claim against an Insured to the extent that such Claim is for a Wrongful Act by Insured Person in connection with the management or supervision of any division, Subsidiary or group of the Parent Corporation offering any of the aforementioned services.

The allegations in the Claims are based on and involve the rendering or failure to render Security Broker/Dealer Services, Investment Banking Services, and/or Securities Underwriting. Thus Endorsement No. 9 applies to preclude coverage for these matters.

As ERII is denying coverage for these matters for the foregoing reasons, we will not be addressing all of the Policy provisions that may apply to limit or preclude coverage. However, ERII expressly reserves its right under all Policy terms and conditions as well as any applicable law including Sections III(A)(1) fraud and dishonesty exclusion, III(C) punitive damages exclusion, III(D)(3) prior and pending litigation exclusion, and III(H) Company contract liability exclusion. Please refer to the Policy form for the complete terms of these provisions.

Please do not hesitate to contact me if you have any questions or any additional information of which we should be aware.

Sincerely,



Sherri McKelvey
Claims Examiner

cc Bryan Huft
Claims Analyst
Hays Companies
ID Center, Suite 1650
80 South 8th Street
Minneapolis, MN 55402

EXHIBIT N

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1 A. I don't have the specifics.
2 Q. Have you been involved in the past in making
3 the decision to deny a claim based on the securities
4 exclusion, the form that's involved here?
5 A. Again involved in the decision, involved at
6 some point in a claim that involved -- that had a
7 denial based on the securities exclusion, again I
8 don't have specific recollection but I suspect that I
9 have been.
10 Q. Your experiences with -- involved with the
11 general E and O exclusion don't include, as far as you
12 can recall anyway, experience as a private litigant or
13 at Chubb or Executive Risk being involved in courtroom
14 litigation or court litigation in some respect to this
15 endorsement, does it?
16 A. That's correct.
17 Q. Is the same true with respect to the
18 securities exclusion?
19 A. Yes.
20 Q. So your knowledge -- is your knowledge at
21 all with respect to these two exclusions based on what
22 you understand to be how courts have interpreted these
23 two exclusions?
24 A. No, it's not. My understanding of the
25 exclusions is what I understand the exclusions to do

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1 and what I know from my experience both as a lawyer
2 and as an underwriting manager what they're intended
3 to do.
4 I'm not aware and it isn't -- the basis
5 of it isn't based on my understanding of case law
6 interpreting it, it's based on our understanding of
7 how they apply and why they're in this policy.
8 Q. I'm just trying to get where does that
9 understanding come from? Is it from oral
10 conversations with other underwriters?
11 A. It's from understanding the risks that
12 you're insuring under a particular form and why you
13 would want to have a particular type of exclusion.
14 For example, an E and O exclusion in a D
15 and O policy written to a broker dealer firm because
16 you're intending to cover D and O exposures and not E
17 and O exposures.
18 Q. If you wanted to go -- if you were
19 interested in finding written documents that are the
20 product of Chubb or Executive Risk that explain what
21 was intended to be covered by the D and O and excluded
22 by the general E and O exclusion with management
23 carveback, is there some document you could look for
24 other than the endorsement itself that would explain
25 that to you?

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1 A. The endorsement itself speaks pretty plainly
2 to it.
3 Q. I'm just wondering would there be -- if
4 someone wanted, yourself or someone else wanted to go
5 and find some documents where Chubb or Executive Risk
6 explained other than the endorsement itself what it's
7 intended to cover or exclude, are there such
8 documents.
9 A. I don't think -- what you're asking for, I
10 don't think -- I think the answer to that is no.
11 There isn't a document that explains what an
12 endorsement that on its face quite clearly says what
13 it excludes, there isn't a document somewhere else
14 that says this is what that endorsement excludes.
15 It's right here in the document
16 Q. I'm not asking quite that specifically. I'm
17 just asking is there some document you could go to as
18 a Chubb employee, Executive Risk employee that would
19 shed some light other than the endorsement itself on
20 what is meant by this endorsement?
21 A. Some document -- I'm sorry.
22 Q. Are you aware of any documents that as a
23 claims counsel, you could go to and that would from
24 Chubb's perspective or Executive Risk's shed any light
25 on how endorsement No. 9 is to be interpreted other

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1 than looking at the endorsement itself?
2 A. No. I'm not aware -- there is not to my
3 knowledge some other document that I would go to that
4 is an interpretive document for this endorsement.
5 Q. And I think you said your understanding is
6 based on what you understand to be the plain meaning
7 of the endorsement No. 9 itself, true?
8 MR. TOPOL: Objection.
9 THE WITNESS: Yes.
10 Q. (By Mr. Kolbo) Same with endorsement No. 3,
11 the securities exclusion?
12 A. That's correct.
13 Q. Let me ask you about the relationship
14 between a directors' and officers' liability policy
15 and the errors and omissions policy.
16 Would you agree that the coverage
17 provided by a directors' and officers' liability
18 policy can overlap with the coverage provided by an
19 errors and omissions policy?
20 A. I'm sorry, can you read that back?
21 (Reporter read back as requested.)
22 THE WITNESS: Not really. As I think I
23 indicated before there are policies that are written,
24 that Chubb has written, that Executive Risk had
25 written before it was acquired by Chubb that are

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1 blended policies that -- so they are a policy but they
2 contain separate components, one for directors and
3 officers and one for errors and omissions or
4 professional services.
5 To that extent if you have a blended
6 policy that contains both of those coverages, yes, you
7 know, you could have a single policy that provides
8 coverage for both of them.
9 But a directors' and officers' policy
10 doesn't provide coverage for professional services, E
11 and O, and an E and O policy doesn't provide coverage
12 for directors' and officers' liability as a D and O
13 policy is understood.
14 Q. Well, first of all let me back up a little
15 bit.
16 Is it my understanding, we've had
17 testimony to this, is it my understanding that your
18 position is that the claims being asserted against the
19 insureds in this case, the Miller and Schroeder case
20 are claims that would implicate an errors and
21 omissions policy but not a directors' and officers'
22 liability policy?
23 A. Claims that potentially could implicate an
24 errors and omissions policy. The nature of the claims
25 are the type of claims that you would expect to see

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1 under a professional liability policy.
2 Now they might not be covered under the
3 policy but that's the type of risk at issue.
4 Q. Am I correct that the only errors and
5 omissions exclusion in the policy issued here is
6 contained in endorsement No. 9 of the policy?
7 A. I don't know. I'd have to go back through
8 the entire policy to figure that out. I know that
9 endorsement No. 9 certainly is an errors and omissions
10 exclusion.
11 I don't know if there are other
12 exclusions in here that might also serve to exclude
13 something, for example, there is the dishonesty
14 exclusion in here.
15 Q. That's not specifically to errors and
16 omissions?
17 A. You're asking me is the only exclusion here
18 that is specific to professional services with the
19 focus being on professional services, that is
20 endorsement No. 9.
21 Q. And if that's -- assuming that's the case
22 and I think it's the case, in the absence of
23 endorsement No. 9, the policy could provide coverage
24 for errors and omissions, claims based on errors and
25 omissions, correct?

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1 A. It's not intended to, no. I think that you
2 would have to -- you'd have to take a look at the
3 insuring clause and the relevant definitions of the
4 different terms to see what is and isn't covered.
5 I think absent that exclusion you
6 certainly would leave yourself more open to arguments
7 by others that it would. Or others would try and read
8 it that way. So I think the E and O exclusion makes
9 it clear that it's not intended to provide coverage
10 for this?
11 Q. Let me back up a little bit. One of the
12 first decisions that a claim examiners has to make
13 when a policy -- when a claim is presented is to
14 determine whether or not what's been alleged is in
15 fact a claim under the policy, correct?
16 A. Correct.
17 Q. Were you involved at all in making the
18 decision for Chubb, Executive Risk as to whether or
19 not the allegations that were presented in this case,
20 any of them, I know there is a series of cases,
21 whether any of them constituted a claim under the
22 policy?
23 A. Was I involved in the decision -- no, other
24 than -- I mean I assume that -- as I recall there was
25 a coverage letter that was going out that would

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1 involve a whole variety of issues.
2 And I most certainly reviewed the entire
3 coverage letter. And there may have been some
4 statement in the coverage letter that the claims
5 themselves -- that the allegations or whatever
6 constituted a claim under the policy.
7 Q. Did you agree with that assessment that the
8 allegations did constitute a claim under the policy?
9 MR. TOPOL: Objection.
10 THE WITNESS: I'd have to take a look
11 at the assessment that you're talking about.
12 Q. (By Mr. Kolbo) Let me show you Exhibit 9,
13 for example, and I don't have a copy in front of me
14 but it's the second page, its Bates No. 003004 and
15 it's the third paragraph on the bottom. Starts with
16 this matter.
17 If you could read that?
18 A. The paragraph to which you're referring,
19 this matter appears to constitute a claim as it is
20 written notice that the trustee intends to hold an
21 insured person responsible for breaches of duty
22 allegedly committed in his capacity as an insured
23 person.
24 However, although this matter constitutes
25 a claim it is precluded from coverage pursuant to the

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1 following policy provisions. I don't have any problem
2 with that.
3 Q. But you would agree that that letter and I
4 think I can represent there are a series of letters
5 like that for different claims, that letter represents
6 the position of the Chubb that this matter does
7 constitute a claim, correct?
8 A. Appears to constitute a claim. Keep in mind
9 that that's -- I think there is a presumption that it
10 appears to constitute a claim, but we're telling you
11 that there is an exclusion that applies.
12 So even if it is, keep in mind that
13 ultimately if you get into coverage litigation, it's
14 the burden of the insured to establish that something
15 is within the coverage.
16 This letter simply says, all right, it
17 appears that there may be facially based on what we
18 have, this might be something that you could argue
19 fits within the insuring clause. Even if it does,
20 you've got these exclusions that are going to apply to
21 kick it out.
22 Q. Well, yes but the first determination is
23 whether or not a claim has been alleged, correct? And
24 Chubb's position is not set forth there, that it could
25 be argued that it is. Chubb's position is first of

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1 all, it appears and later on in the sentence says it
2 is a claim, correct?
3 A. I read the language. It says what it says.
4 Says it appears to constitute a claim dot dot dot dot
5 as it is written notice -- it does say although this
6 matter constitutes a claim it is excluded from
7 coverage pursuant to the policy provisions. That's
8 what the language says.
9 Q. But if it's true that the matters alleged
10 here constitute a claim, wouldn't you agree with me
11 that the allegations to the extent that they're the
12 kind of allegations that would be also a claim under
13 an errors and omissions policy are also allegations
14 that would constitute a claim under a directors' and
15 officers' liability policy?
16 A. Repeat that again. He's asking me if I
17 agree to something. So let me hear what it was.
18 (Reporter read back as requested.)
19 THE WITNESS: No, I wouldn't agree with
20 it. I would say that it could be. It certainly could
21 be argued that allegations of a certain type give rise
22 to coverage under a directors -- and even though
23 they're E and O claims give rise to coverage under the
24 directors' and officers' liability insurance policy.
25 But what I'll tell you is it is not the

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1 intent. An E and O claim is not necessarily asserted
2 against a director in an insured capacity which is the
3 focus of the D and O claim but, you know, it could be
4 argued.
5 It's sort of -- in this particular case I
6 think there wasn't -- there is not really a point in
7 saying even if you could say that the allegations at
8 issue in the Miller and Schroeder litigation fell
9 within the definition of claim, it's still excluded.
10 That's why you have the E and O exclusion
11 in there, to make it absolutely certain belts and
12 suspenders that there is not coverage for E and O
13 claims.
14 Q. Right. But if one first concludes that a
15 matter is covered as a claim, then it becomes critical
16 to ascertain, does it not, whether that claim is
17 excluded somewhere in the policy?
18 A. It is correct as a general matter that if
19 you determine that something falls within the scope of
20 coverage is a -- that based on the allegations is a
21 potentially covered claim, one of the next steps you
22 would take would be to determine whether or not an
23 exclusion applies to exclude coverage for that.
24 Q. Assuming that the claim is covered here, the
25 only exclusion that you're aware of in the policy that

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1 would relate to the exclusion for errors and omissions
2 would be endorsement No. 9, correct?
3 A. The only -- no, that's not correct.
4 Q. What other exclusions?
5 A. For example, the securities exclusion. I
6 mean, if what you're saying is the only exclusion that
7 is specifically geared at saying claims for these type
8 of services are covered, that's endorsement No. 9.
9 It says what it says. Which is claims
10 based on arising out of the rendering or failure to
11 render the following types of services are excluded.
12 That says what it says. It is there to
13 make it clear that this policy doesn't cover those
14 type of claims.
15 But there are other exclusions and other
16 endorsements in here that contain exclusions that
17 could equally apply to a professional services claim
18 but they are not specifically characterized as a
19 professional services exclusion.
20 Q. Other than the securities exclusion, what
21 other exclusions would you look to?
22 A. Like I say, the dishonesty exclusion in a
23 given case could be something that would kick out
24 coverage for acts that are dishonest or fraudulent
25 acts that are alleged or established again depending

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1 upon what your exclusion requires, that could be a
2 professional services type exclusion or could be
3 invoked with respect to a professional service type
4 claim, as it could be with respect to a D and O claim.
5 Q. Is Chubb Executive Risk taking the position
6 in this case as far as you know that the dishonesty
7 fraud clause excludes coverage in this case?
8 A. No, not to my knowledge. You asked me for
9 an example.
10 Q. Do you know of any -- are you aware of any
11 clause in the policy other than the securities and the
12 general E and O exclusion on which Chubb is relying
13 rather than simply reserving their rights but actually
14 relying to deny coverage in this case?
15 A. No. It's my understanding that Chubb has
16 reserved its rights but that the two exclusions on
17 which it's relying in this case are the exclusion
18 contained in endorsement No. 3 which is the securities
19 exclusion and the exclusion contained in endorsement
20 No. 9 which is the general E and O exclusion with the
21 management carveback.
22 MR. TOPOL: Could we take a break?
23 MR. KOLBO: Sure.
24 (A recess was taken.)
25 MR. KOLBO: Back on the record.

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1 Q. (By Mr. Kolbo) If I can return your
2 attention to endorsement No. 9 and ask you a few more
3 questions about that.
4 I think your earlier testimony was that
5 there are some E and O exclusions endorsements that do
6 not contain the management carveback and others like
7 this one that contain a management carveback, is that
8 true?
9 A. That's -- I'm sure that's correct.
10 Q. Am I correct in understanding that an E and
11 O exclusion without a management carveback is a
12 broader exclusion than an E and O exclusion with a
13 management carveback?
14 A. That's also correct.
15 Q. The purpose of a carveback is to bring back
16 into coverage something that's otherwise excluded by
17 the exclusion? Is that a fair statement?
18 A. I would say that the purpose of a carveback
19 would be to limit the scope of the exclusion.
20 Q. Okay. I'll take that. In this case am I
21 correct that paragraph No. 1 including the three
22 services that are identified there, that's what
23 constitutes the exclusion, the basic exclusion in
24 endorsement No. 9; is that correct?
25 A. The basic exclusion is contained in subpart

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1 1 of that endorsement.
2 Q. Subpart 2 is what contains the management
3 carveback, correct?
4 A. That's correct. That's the limitation on
5 the scope of the exclusion in subpart 1.
6 Q. All right. In subpart 1, is it your
7 understanding under the language of this exclusion
8 subpart 1, that claims against an officer and director
9 would be excluded if they were say employment related
10 claims against an officer and director who happened to
11 run a securities underwriting firm?
12 A. I'm sorry, could you repeat that again?
13 Q. Assume -- I'm just trying to find out the
14 scope of subparagraph No. 1.
15 And assume a claim was made against an
16 officer and director not for actually rendering or
17 failing to render any of the services listed there,
18 but they're employment related claims against an
19 officer and director of a company that provides to
20 others those types of services, would that be excluded
21 under this subparagraph 1?
22 A. I'm sorry, I lost track of your question
23 again. Could you read it back?
24 (Reporter read back as requested.)
25 THE WITNESS: I can't answer that.

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1 It's sort of so general and actually hypothetical as
2 well. I mean could it possibly be excluded by it? I
3 don't even know. You'd have to have a specific claim.
4 Generally speaking you would have to
5 focus on the language which says was -- the particular
6 claim that you're hypothesizing, is it a claim made
7 against an insured based on arising out of, directly
8 or indirectly resulting from in consequence of or in
9 any way involving the actual alleged rendering or
10 failure to render the following, those services.
11 And if it wasn't, if it was an employment
12 related claim that didn't -- wasn't based on, arising
13 out of or directly or indirectly resulting from or in
14 consequence of or involving the rendering of those
15 services, then no, it wouldn't fall -- it wouldn't be
16 excluded.
17 If it was, then yes, it potentially could
18 be. But it's so hypothetical, I don't see that an
19 employment, that you're sort of describing as an
20 employment action I guess, generally isn't an action
21 that involves the rendering, the actual or alleged
22 rendering or failure to render a service.
23 Q. Well, we would agree the exclusion is tied
24 to the rendering or failure to render specified
25 services by the insured, correct?

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1 A. Right.
2 Q. Now, let me then ask you about paragraph --
3 subpart No. 2, the management carveback.
4 Would I be correct in understanding if a
5 claim is made against an insured in connection with
6 the management or supervision by that insured of any
7 division, subsidiary or group of the parent offering
8 any of the services identified in paragraph No. 1,
9 that's what's carved back under coverage here?
10 A. To the extent that such claim is for a
11 wrongful act by an insured person in connection with
12 the management or supervision of any division,
13 subsidiary or group of the parent corporation.
14 Q. Which is the same to say if there is a
15 claim, correct, because a claim assumes a wrongful
16 act?
17 A. Well, no. The words say what the words say.
18 It's to the extent it is a claim against an insured
19 person -- I mean, a claim is for a wrongful act by an
20 insured person in connection with the management or
21 supervision of the division -- supervision of any
22 division, subsidiary or group of the parent
23 corporation.
24 Q. Is it your understanding that any claims
25 against insureds in this case are being made based on

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1 their management or supervision of employees within
2 any subsidiary or group or division of Miller and
3 Schroeder?
4 A. Is it my understanding that any of the
5 claims at issue in this litigation are made based on
6 their management or supervision of a division,
7 subsidiary or group of Miller and Schroeder? No, it
8 is not.
9 Q. Is it your understanding that some claims
10 are made based on the management or supervision
11 liability of the officers and directors?
12 A. I don't know what you mean by management or
13 supervision liability of the officers.
14 Q. Are you familiar with any allegations and
15 any of the statements of claim or any of the
16 complaints that allege that the officers and directors
17 are liable to the claimants because of their improper
18 management supervision of the employees at Miller and
19 Schroeder?
20 A. Specifically no. Generally I am familiar
21 that there are claims against officers and directors
22 that relate to the sales of securities by people for
23 whom they were responsible.
24 Q. Is it your understanding that the officers
25 and directors are themselves alleged to have been

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1 involved in the issuance of securities?
2 A. I don't have an understanding one way or the
3 other.
4 Q. What's the basis for your -- what's the
5 basis for your understanding that Chubb has denied
6 liability in this case on the basis of the E and O
7 exclusion with the management carveback? What's the
8 basis for your understanding?
9 A. What's the basis for my understanding that
10 Chubb has denied based on this endorsement No. 9?
11 Q. Yeah.
12 A. My understanding is that I've had a number
13 of discussions with the claims personnel involved in
14 the case, who, you know, came to me, approached me
15 initially and at other times during the course of
16 their handling of the claim, to run their views of
17 coverage by me and to get my views on it and make sure
18 that they weren't missing anything and that my views
19 were consistent with theirs.
20 Q. What would be an example of the kind of
21 claim that is being carved back into coverage under
22 subparagraph 2 in your opinion?
23 A. Hypothetically speaking?
24 Q. Yes.
25 A. Subparagraph 2 really the intent of this

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1 management carveback is really to get at sort of the
2 -- the true director and officer exposure.
3 Shareholder, derivative type claim or an actual owner
4 of the company type claim against management alleging
5 sort of basic mismanagement, breach of fiduciary duty,
6 that type of claim.
7 And the purpose of it is to make sure
8 that if -- that you would not read one so broadly as
9 to say well, because the entire business involves
10 these sort of services, we carve it out.
11 Because the entire business involves
12 these sort of services that any sort of shareholder
13 derivative type action, fiduciary duty type claim
14 would be excluded by virtue of the fact that the
15 company is involved in rendering services.
16 Q. You would agree, would you not, that
17 paragraph -- subparagraph No. 1 does not exclude
18 coverage simply for being in the business of
19 securities underwriting or the other services listed,
20 correct?
21 A. It is not -- I would agree that paragraph
22 No. 1 is not intended to operate as an exclusion, that
23 excludes any claims simply because the company is
24 involved in the business of writing -- a securities
25 brokerage.

1 Q. And that's clear from the face, from the
2 language of subparagraph No. 1, correct?
3 A. Is that clear from the face of No. 1? I
4 think that it's -- I think it depends upon the
5 particular claim that you get in, that you could get
6 in the type of claim that someone could take a look at
7 it and say it is based on, arises out of, directly or
8 indirectly resulting from or in consequence of or in
9 any way involves the rendering of professional
10 services. It's a very broad exclusion.
11 Q. Is it your opinion that the exclusion is
12 ambiguous?
13 A. No.
14 Q. It's clear?
15 A. I think it's clear. I think it's also very
16 clearly very broad.
17 Q. Is it your -- we're talking just about
18 paragraph No. 1, subparagraph No. 1. Your opinion is
19 that language is clear and unambiguous, correct?
20 A. My view is that language is clear and
21 unambiguous.
22 Q. And it clearly and unambiguously does not
23 apply to exclude coverage for an officer and director
24 and merely because they happen to work for a company
25 that provides securities underwriting and other

1 services, correct?
2 A. Not merely because but again based on the
3 allegations that could be in a particular claim, it
4 could be read to exclude coverage for that.
5 Q. It could?
6 A. Yes. Depending on the specific allegations
7 of a particular claim.
8 Q. Why do the allegations of a complaint
9 determine what is meant by Paragraph 1? Either it
10 means something or it doesn't?
11 A. I'm sorry, I'll let you finish your
12 question.
13 Q. How is the meaning of subparagraph 1
14 determined by the allegations in a particular
15 complaint?
16 A. The meaning of -- it is not. The meaning of
17 subparagraph 1 is not in any way governed by the
18 allegations of the complaint.
19 The allegations of the complaint are what
20 are critical in determining whether or not
21 subparagraph 1 applies or potentially applies.
22 Q. All right. If the allegations of a
23 complaint are that an officer and director is liable
24 purely because of their status of being an officer and
25 director of a securities underwriting firm, that's not

1 excluded under the terms of Paragraph 1, is it?
2 A. If that's the entire allegations of the
3 complaint, it is not excluded under paragraph 1.
4 Q. One doesn't need Paragraph 2 to reach that
5 conclusion, does it?
6 A. For a claim against a director or officer
7 that says the only reason this claim is against you is
8 because you were a director or an officer of the
9 company, you would not need Paragraph 2 to conclude
10 that Paragraph 1 doesn't exclude that specific claim?
11 Q. Okay. Now, you mentioned earlier something
12 about shareholder derivative suits.
13 You would agree with me that Paragraph
14 No. 2 says nothing about shareholder derivative suits,
15 correct? It does not limit the carveback, the
16 shareholder derivative suit?
17 A. I will -- subpart 2 of this exclusion does
18 not specifically limit itself to shareholder
19 derivative suits.
20 You asked me for an example of a type of
21 claim that subpart 2 is intended to get at and I gave
22 you an example.
23 Q. And subpart 2 does not exclude claims by
24 customers, does it, against officers and directors?
25 Customers of a company that -- for whom the officers

1 and directors --
2 A. Your question is does it -- it could
3 conceivably or it might not. Again it depends upon
4 the particular claim and how you would apply each part
5 of the exclusion in the context of a particular claim.
6 Q. But you would agree with me that the mere
7 fact that a claim is by a customer against the officer
8 and director, that by itself does not give you enough
9 information to ascertain that the carveback did not
10 apply?
11 A. The mere fact that a claim is by a customer
12 does not in and of itself. You would need to know
13 more about the claim to know whether or not the
14 carveback would apply.
15 Q. Have you been involved with in your
16 employment at Chubb, Executive Risk involved in
17 writing management carvebacks that differ from this
18 one?
19 A. I'm sure I have. But I don't specifically
20 recall.
21 Q. Are you aware of the existence of carvebacks
22 that are either narrower or broader than the carveback
23 that you have in front of you here?
24 A. Generally speaking I am aware of the
25 existence of carvebacks that are different.

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1 consequence of or in any way involving the actual or
2 alleged rendering or failure to render only those
3 services.
4 So there is a limitation on the exclusion
5 in that. As compared to an endorsement that would say
6 any services of any nature whatsoever. That's all you
7 can say about that endorsement and the effect of
8 manuscripting, you know, limiting the scope of that
9 exclusion.
10 The fact that another exclusion applies
11 independently is completely independent of whatever
12 was done in manuscripting this endorsement.
13 Q. The services that are identified under
14 paragraph No. 1, do you have an opinion as to whether
15 those -- the exclusion putting aside paragraph No. 2,
16 the exclusion in subpart No. 1 do you have an opinion
17 as to whether or not that exclusion is -- excludes
18 anything that's not already excluded by endorsement
19 No. 3, the securities exclusion?
20 A. Do I have an opinion as to whether or not
21 anything excluded in No. 1 isn't already excluded by
22 the securities exclusion?
23 Q. Right.
24 A. I don't know if I have an opinion as to it.
25 I know that they're two completely separate exclusions

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1 that come at two different issues.
2 One of which is an exclusion that says we
3 don't want to cover claims, essentially E and O
4 claims. Any claims that arise out of your rendering
5 of these type of services; investment banking
6 services, securities broker dealer focuses on the
7 nature of the conduct at issue in the claim.
8 The securities exclusion focuses on the
9 nature of the claim. There is a particular type of
10 exposure we also don't want to cover. There may be
11 significant overlap between those two but they're both
12 serious concerns dealing with a broker dealer firm
13 that we had exclusions for.
14 And the fact that there may be overlap
15 between the two exclusions and may in fact be
16 significant overlap between the two exclusions only
17 reflects good underwriting which is they wanted to
18 make it clear from both angles, both from an exposure
19 angle that all securities type claims, claims arising
20 out of violations of any law in connection with the
21 offer or sale of securities is excluded and they also
22 wanted to make sure that E and O coverage,
23 professional liability, professional services claims
24 weren't covered.
25 And if those two overlap, then you have

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1 two exclusions that apply.
2 Q. You don't have an opinion as to whether one
3 is broader than the other with respect to securities?
4 A. They're different. I don't. They each --
5 you know, you have to deal with each claim as it comes
6 in. You can't talk in the abstract about it. You
7 look at a claim when it comes in and evaluate whether
8 one or more exclusions apply. In this case we
9 evaluated and concluded that both endorsement No. 3
10 and endorsement No. 9 apply.
11 MR. KOLBO: I'm going to pass over to
12 Tom.
13 CROSS EXAMINATION BY MR. ATMORE
14 Q. One of the examples you gave as to what
15 Paragraph 2 of endorsement No. 9 might apply to; in
16 other words, what it might allow and set back into
17 coverage was an owner versus management type lawsuit.
18 Do you remember saying that?
19 A. I said what I said. I agree that one of the
20 things that it might apply to would be a shareholder
21 claim and a shareholder is an owner of the company,
22 right, against the management.
23 Q. Are you aware of whether there was any
24 distinction in -- when this policy was originated in
25 2000 and renewed in 2003 between management and

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1 ownership at Miller and Schroeder or any of its
2 subsidiaries; in other words, was there an owner who
3 was not a manager?
4 A. Am I -- I don't know the answer to that
5 question.
6 Q. Let me ask this. When you -- I think you
7 said you reviewed Carrie Campi's letter and initial --
8 or rather initial determination, that there would not
9 be coverage.
10 When you did so did you review the
11 underlying complaint that formed the basis of the
12 claim?
13 A. I don't specifically recall right now. I
14 may have. I may not have. Sometimes I would rely on
15 the claims examiner to advise me of the nature of the
16 claim and the elements of it.
17 Sometimes they would provide me with
18 copies of the complaint and I would review those. I
19 just don't recall in this case which I did.
20 Q. Other than the time you reviewed her initial
21 determination, have you gotten back into this case and
22 reviewed other claims?
23 There is more than one denial letter.
24 Were you only involved in the one or have you been
25 involved in more than one?

A. No. I have been involved sequentially throughout the progress of the claim.
Q. Okay. Do you remember ever looking at any of the NASD arbitrations, petitions?
A. I don't specifically recall.
Q. How about the California class action lawsuit complaint? Did you review that?
A. Again, no specific recollection.
Q. When Mr. Kolbo asked you whether you had talked to anyone other than your counsel, you knew he was referring to doctor -- I just gave you --
MR. TOPOL: I don't know where I got that degree.
MR. ATMORE: JD, all right.
Q. (By Mr. Atmore) Other than Mr. Topol?
A. Right.
Q. We're all lawyers in this case, that's why I'm asking.
A. The only person I spoke to in preparation for this deposition was David.
Q. Did you ever try to contact Michael Watts and ask him what was the intent of the parties when they first -- when this policy was first issued in 2000?
A. No. Once again because I was familiar with

both endorsements, the securities exclusion and the general E and O exclusion, it wasn't necessary to contact Mike.
MR. ATMORE: That's all I have.
MR. KOLBO: Done. Thanks very much. I appreciate it.
MR. TOPOL: We'll want to review and sign, please.
(Deposition concluded at 2:40 p.m.)

CERTIFICATE

I hereby certify that I am a Notary Public, in and for the State of Connecticut, duly commissioned and qualified to administer oaths.

I further certify that the deponent named in the foregoing deposition was by me duly sworn, and thereupon testified as appeared in the foregoing deposition; that said deposition was taken by me stenographically in the presence of counsel and reduced to typewriting under my direction, and the foregoing is a true and accurate transcript of the testimony.

I further certify that I am neither of counsel nor attorney to either of the parties to said suit, nor am I an employee of either party to said suit, nor of either counsel in said suit, nor am I interested in the outcome of said cause.

Witness my hand and seal as Notary Public this 30th day of September, 2004.

_____
Barbara L. Murphy, LSR
Notary Public

My Commission Expires:
June 30, 2007

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF MINNESOTA
CHAPTER 7 CASE
BKY CASE NO. 02-40284 TO 02-40286
JOINTLY ADMINISTERED

IN RE:
SRC HOLDING CORP. F/K/A MILLER & SCHROEDER, INC., AND ITS SUBSIDIARIES
Debtor

BRIAN F. LEONARD, TRUSTEE ADV CASE NO. 03-4284
Plaintiff NON-CORE PROCEEDING
Vs.
EXECUTIVE RISK INDEMNITY, INC.
Defendant

THE MARSHALL GROUP, INC., JEROME A. TABOLICH, JAMES E. IVERSON, EDWARD J. HENTGES, KENNETH R. LARSEN, STEVEN W. ERICKSON, PAUL R. EKHOLM AND MARY JO BRENDEN
Intervenors

I hereby certify that I have read the foregoing transcript of my deposition given at the time and place aforesaid, consisting of Pages 1 to 66, inclusive, and I do again subscribe and make oath that the same is a true, correct and complete transcript of my deposition so given as aforesaid, and includes changes, if any, so made by me on the attached errata sheet(s).

_____
JOEL TOWNSEND

Subscribed and sworn to before me
this ___ day of _____, 2004.

_____
NOTARY PUBLIC

EXHIBIT O

1 set.
2 Q. Would you state your name for the record, please.
3 A. My name is Cheryl Ng O'Malley.
4 Q. You understand you're under oath today?
5 A. I do.
6 Q. You're a claims examiner for the Chubb Group; is
7 that correct?
8 A. That's correct.
9 Q. Is that a particular company within the Chubb
10 Group or just generally the Chubb group?
11 A. I work for the northern claims office of the
12 Chubb Group of Insurance Companies.
13 Q. You can hear me all right through the telephone
14 connection?
15 A. Yes.
16 Q. I can hear you.
17 MR. ATMORE: Can everybody else hear?
18 MR. KOLBO: I can hear.
19 Q. How long have you been a claims examiner for
20 Chubb, Ms. O'Malley.
21 A. I began in December of 2000.
22 Q. You began as a claims examiner? That was your
23 title?
24 A. Yes, specialty claims examiner.
25 Q. Is that your title today, specialty claims

1 examiner?
2 A. I became a senior claims examiner, and at the
3 present I am working just part time on a
4 temporary basis as a specialty claims examiner.
5 Q. What's the reason for the change in status?
6 A. I have young children at home.
7 Q. When did you change from being a specialty claims
8 examiner to a senior claims examiner?
9 A. I believe it was in late 2002, but I don't know.
10 I don't recall exactly.
11 Q. When did you go to part time?
12 A. It would have been January 2003.
13 Q. Prior to becoming a claims examiner, did you have
14 other jobs at Chubb, or did you work somewhere
15 else, or what did you do?
16 A. Prior to working at Chubb, I worked for Equitable
17 Resources in their Equitable Gas Company division
18 as in-house counsel.
19 Q. What does that company do?
20 A. They are a natural gas utility.
21 Q. Did you do anything that might be related to
22 insurance for them?
23 A. I did claims review, claims against the company.
24 I helped with various litigation and customer
25 relations.

1 Q. How about when you were in private practice, what
2 was your area of practice?
3 A. I was doing various civil litigation, but it was
4 not directly insurance law. We obviously dealt
5 with insurance companies, but I was not
6 practicing insurance law per se.
7 Q. I want to turn to some of the specifics of the
8 case we're involved in today. I understand that
9 you worked on several Miller & Schroeder related
10 claims when you were a claims examiner for Chubb.
11 MR. TOPOL: Objection.
12 Q. Is that correct? Do you know what I mean by
13 Miller & Schroeder?
14 A. I do know of the insured Miller & Schroeder, and
15 I believe I may have been involved in a couple
16 cases.
17 Q. The first one I want to talk to you about is a
18 claim made under the policy relating to a lawsuit
19 by Bremer Bank in 2001. Do you have a memory of
20 that?
21 A. I don't really recall the case in particular.
22 Q. Why don't we have marked and shown to the witness
23 what was Campi Exhibit No. 3.
24 - - - -
25 (O'Malley Deposition Exhibit 1

1 was marked for identification.)
2 - - - -
3 A. I have the exhibit.
4 Q. It's a four-page exhibit with Bates numbers ERII
5 007103 to 007106; is that right?
6 A. Yes.
7 Q. If you turn to the second page of the exhibit, at
8 the very bottom box dated 10/12/01, it refers to
9 Claimant Bremer Business Corporation. Do you see
10 that?
11 A. Yes.
12 Q. Can you tell me, are these your notes handling
13 that claim?
14 A. That 10/12/01 does not appear to be my note.
15 That would typically be a customer service
16 assistant entering a note to open a claim.
17 Q. Do you recall that you were the claims examiner
18 on this claim, however?
19 A. It does appear that I was.
20 Q. How is it that it came to be assigned to you, do
21 you know?
22 A. In typical fashion, the claim would come in to a
23 division and would be assigned by one of the
24 supervisors.
25 Q. What division were you in at the time?

1 A. The northern specialty claims division.
2 Q. Do you know why this claim would have ended up in
3 the northern specialty claims division?
4 A. It would have been based on where the litigation
5 or claim was made. We have a certain territory.
6 Q. When I use the term "Heritage bond claims," do
7 you know what I'm talking about?
8 A. I do not.
9 Q. Do you recall working on any claims under the
10 Miller & Schroeder policy at issue that related
11 to customers' complaints as to losses on Heritage
12 bonds issued by Miller & Schroeder?
13 A. No, I do not.
14 MR. ATMORE: Do you have McKelvey
15 Exhibit 1?
16 MR. TOPOL: Yes.
17 MR. ATMORE: Have that marked.
18 - - - -
19 (O'Malley Deposition Exhibit 2
20 was marked for identification.)
21 - - - -
22 A. I have a copy of the exhibit.
23 Q. Do you recognize what that is?
24 A. I have not seen this.
25 Q. It says "Claims Summary" up at the top. Is any

1 bottom.
2 Q. They go in reverse chronologic order.
3 A. Correct.
4 MR. TOPOL: You mean the one that says
5 "called INSD contact"?
6 MR. ATMORE: Right.
7 Q. You testified before that the first 10/15/01,
8 that acknowledgement letter is from
9 administrative staff; correct?
10 A. Correct.
11 Q. My question is: The next 10/15/01, is that where
12 your notes start?
13 A. I'm assuming that it is. I don't recall the
14 note, but yes, it would typically be my notes
15 from then on.
16 Q. Do you recall having discussions with Bryan Huff
17 at the Hayes Group regarding this claim?
18 A. I don't have any recollections of the calls or
19 talks or discussions.
20 Q. So other than what might be in your notes here,
21 you don't have an independent recollection of any
22 discussion?
23 A. Correct.
24 Q. Have you had a chance to look over these notes,
25 by the way?

1 A. Sitting here, I have looked at the document just
2 briefly.
3 Q. There's an entry on 10/31/01 that begins,
4 "Returned Bryan Huff's call." Do you see that?
5 A. I do see that.
6 Q. It says that you "advised that I have reviewed
7 allegations against the officer per the" -- what
8 is that M?
9 A. Motion.
10 Q. -- "motion to amend complaint"?
11 A. Correct.
12 Q. "And the allegations relating to investment
13 banking services, which are excluded from
14 coverage" -- is that what "cvg" means?
15 A. That's correct.
16 Q. -- "under the policy." Do you remember why they
17 were excluded?
18 A. I don't recall in particular other than what's
19 written here in this note; that they must have
20 been -- they must have involved some matter that
21 was excluded under the policy.
22 Q. Now, the next block quote or block note doesn't
23 appear to have a date on it. We go in
24 chronological order. Do you know if it's a
25 carryover from 11/1/01, or is it a different

1 note?
2 A. I would believe it's a carryover from
3 11/1/01 because the system automatically dates
4 entries.
5 Q. So you believe the entirety of the 11/1/01 note
6 starts at the bottom of the first page of this
7 exhibit and continues on the second page?
8 A. I don't know for sure, but I would assume so.
9 Q. Let's go to that first page then, the
10 11/1/01 note.
11 A. Okay.
12 Q. You say that "Broker has raised a dispute on
13 meaning and INTENT," and intent is all caps,
14 "between the 'Management Carveback' found in the
15 E & O exclusion in the above policy. Left voice
16 mail message and e-mail with underwriter Keith
17 Doan for understanding of intent." Do you see
18 that?
19 A. Yes.
20 Q. What were you doing there?
21 A. I'm assuming that -- I really don't recall, but
22 I'm assuming I was doing what the note said, that
23 I had talked to the broker, and he raised some
24 issue that I followed up with with underwriting.
25 Q. Do you know why you would have followed up with

1 A. I see.
2 Q. I assume that had you spoken with an underwriter
3 before that, you would have made an entry in the
4 note?
5 A. I would assume, but I don't recall.
6 Q. The last paragraph of the note entry which ends
7 on page two starts "I disagree." Do you see
8 that?
9 A. I do see that.
10 Q. Then you state, "I disagree and believe that
11 there's no coverage because the allegation
12 against the officers pertain to wrongful act that
13 they committed (in the area of investment banking
14 services) and not just their failure to
15 supervise/recognize wrongful act committed by
16 their employees/division." Do you see that?
17 A. I see that.
18 Q. That statement is your understanding of the
19 carveback and what it means; is that fair?
20 A. I'm assuming that if I wrote it there, that it
21 was my understanding of some position in this
22 matter.
23 Q. Does the fact that this is in the note mean that
24 you related that position to Mr. Huff at the
25 Hayes Group?

1 A. I don't recall exactly what we talked about, but
2 I would typically explain my understanding once I
3 had the complaint and the policy in front of me.
4 At some point I must have issued a coverage
5 opinion.
6 Q. You don't recall whether this was part of your
7 discussion with Mr. Huff?
8 A. No. I don't recall any conversation. I'm sorry.
9 Q. After reading this, do you have an idea of what
10 you were trying to tell him about the policy?
11 A. Can you ask that question again, please?
12 Q. Yes. I understand you don't have a particular
13 memory of the discussion. Basically what I'm
14 asking is after reading this, does that refresh
15 your memory of anything you may have discussed
16 with him about the policy and the carveback?
17 A. It doesn't really refresh my memory as to what I
18 might have said to him. I'm sorry.
19 Q. In reading this last paragraph, does it refresh
20 your memory as to what you may have believed the
21 purpose of the carveback was? In other words,
22 can you expound on this beyond what you've just
23 written here?
24 A. No, I can't.
25 Q. The next entry, we go to the first page,

1 11/05/01. Do you see that one?
2 A. I do.
3 Q. It says you "spoke to underwriter regarding
4 intent of carveback." Do you see that?
5 A. Yes.
6 Q. Then there's a name under there, Blair McCloud,
7 underwriter. Does that mean that's who you spoke
8 with?
9 A. I don't recall a conversation or the
10 conversation, but I assume if I put the name down
11 there, that that was the person I spoke with.
12 Q. You write, "He advised that coverages for
13 vicarious liability situations only. No coverage
14 intended where claim alleges wrongful acts by D &
15 O in area of investment banking." Do you see
16 that?
17 A. I see that.
18 Q. Independent of these notes, do you have any
19 recollection of your discussion with the
20 underwriter?
21 A. I'm sorry. I do not.
22 Q. Independent of these notes, do you have any
23 memory as to what your understanding was after
24 this discussion?
25 A. No, I do not.

1 Q. Of the carveback?
2 A. I don't recall.
3 Q. Now, the next set of entries don't have lines
4 between them, but they do have different dates.
5 The first one I want to talk about is 11/07/01.
6 A. Okay.
7 Q. It starts, "Yesterday I received a second amended
8 complaint on this claim." And it goes on to say,
9 "The amended complaint appears to add fraudulent
10 inducement allegations against Steven Erickson
11 (senior VP of the Insured's Gaming Finance
12 Department) for false representations made by
13 employees supervised by him."
14 It goes on to say, "We may have to
15 issue a reservation of rights with regard to that
16 single allegation; however, the remainder of the
17 claim is still excluded based upon the exclusion
18 of claims arising out of investment banking
19 services." Do you see that?
20 A. I see that.
21 Q. When you say, "We may have to issue a reservation
22 of rights with regard to that single allegation,"
23 what are you saying there? What are you
24 intending to say?
25 A. I don't recall specifically about this incident,

1 but what reservations of rights would mean would
2 be possible acceptance of coverage on the one
3 issue.
4 Q. So acceptance of coverage on one issue and then a
5 defense of that claim with that intent, is that
6 what you're trying to convey there?
7 MR. TOPOL: Objection.
8 A. I really don't know what I was -- I don't recall
9 the policy. I don't recall the complaint, the
10 situation. I mean there are various ways of
11 accepting coverage, issuing reservations of
12 rights. It depends on the policy.
13 Q. The next paragraph under that note says, "Note
14 that I discussed my position with Bryan Huff of
15 the Hayes Group, and he still believes the entire
16 claim against both officers are covered (pursuant
17 to the management carveback) merely because they
18 were supervisors. He advises that he will push
19 back on any reservation of rights we take on this
20 claim." Do you see that?
21 A. Yes.
22 Q. First of all, does that mean that you told him
23 that you may have to issue a reservation of
24 rights regarding the Erickson allegation
25 discussed above?

1 A. I mean I don't recall what conversation I had
2 with him, but I mean I think the note -- I don't
3 have anything, any recollection other than what's
4 written in this note unfortunately.
5 Q. What does it mean to push back? You say that "he
6 will bash back."
7 A. To disagree.
8 Q. The next entry is 11/16/01. It begins, "Received
9 actual second amended complaint filed by claimant
10 against Erickson and Frank." Do you see that?
11 A. I see that.
12 Q. The last line of that entry says, "Discussed
13 issues with counsel regarding coverage for Frank;
14 possible coverage for Erickson. Will further
15 review with supervisor." Who are you referring
16 to when you say counsel?
17 A. To be honest, I don't know. I mean I would
18 assume the way it was written, I was talking
19 about insured counsel, but I don't know, to be
20 honest. I don't recall.
21 Q. It says, "Possible coverage for Erickson. Will
22 review further with supervisor." Do you recall
23 reviewing the issue with your supervisor?
24 A. I don't recall doing that.
25 Q. The last entry is 11/30/01. It begins,

1 A. Sandy Stankovic.
2 Q. Who is she?
3 A. I don't know her exact position, but she's like a
4 technical assistant. She assists the claims
5 adjusters.
6 Q. Did she work for you?
7 A. She worked for the entire northern claims
8 division.
9 Q. So she notes she "spoke with Ken Larsen advising
10 him that Maggie Klimczyk" -- is that how you
11 pronounce that?
12 A. Correct.
13 Q. -- "is the adjuster."
14 A. That is what the note says.
15 Q. Who is Maggie Klimczyk?
16 A. Maggie Klimczyk is a technical supervisor with
17 the northern claims division.
18 Q. At the time, was that her title?
19 A. I don't know if it was her exact title, but that
20 was her general position.
21 Q. What does a technical supervisor do?
22 A. She is a specialty claims examiner with expertise
23 or who has been there for a long time. It's a
24 higher level position for an examiner.
25 Q. Higher than what you were at the time; is that

1 - - - -

2 MR. TOPOL: That's marked as 9.

3 Q. I'm showing you or you're being shown Exhibit 9

4 to your deposition. These are handwritten notes

5 dated 12/6/01, Bates range ERII 02601 through

6 2604. Is this your handwriting?

7 A. This is not my handwriting.

8 Q. Do you recognize it as Maggie Klimczyk's

9 handwriting?

10 A. I don't recognize this handwriting.

11 Q. Have you ever seen these notes before?

12 A. No, I have not.

13 Q. If a claims examiner took handwritten notes of a

14 meeting or discussion or an analysis of a file,

15 would those notes be put into the claims file?

16 A. Yes.

17 Q. Just so the record is clear, you have no

18 independent recollection of how you may have

19 interpreted the E & O exclusion with management

20 carveback at the time you were handling these

21 claims other than what's in your notes and

22 letters we've looked at today; is that right?

23 A. That is correct. I do not have an independent

24 recollection.

25 MR. ATMORE: That's all I have.

EXHIBIT P

EXHIBIT
Cmmpr 3
9/23/04

PENGAD 800-631-69

EXHIBIT
1
O'Malley

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11/30/01	Discussed with Brian Huff at Hayes Group that I drafted declination, based upon exclusion that we earlier discussed. Also advised that letter is being reviewed by Spvr and will be sent next week. He will review letter and respond. I further advised that I talked to Atty Lindsey Arthur (on First Bank of North claim), and he advised of 2 new D&O claims, Behnke & Moreland. These claims have yet to be assigned to a Chubb examiner, but I advised Brian since claims did not originate with Hayes Group.
11/16/01	Received actual second amended complaint filed by Claimants against Erickson and Frank. It appears that 2 motions to amend complaint were filed by Claimant. One (re: erickson and frank) was granted; the other was denied. Atty's have moved to dismiss complaint against erickson and frank. Discussed issues with counsel, regarding coverage for frank; possible cvg for ericksor will review further with Spvr.
11/07/01	Yesterday I received a Second Amended Complaint on this Claim. The amended complaint appears to add fraudulent inducement allegations against Steven Erickson (Sr. VP of the Insured's Gaming Finance Dept) for false representations made by employees supervised by him. (We are reviewing further; allegations are very poorly drafted & vague regarding employee-involvement). We may have to issue a reservation of rights with regard to that single allegation; however the remainder of the claim is still excluded based upon the Exclusion for claims arising out of Investment Banking services. Note that I discussed my position with Bryan Huft of the Hayes Group. And he still believes the entire claim against both officers are covered (pursuant to the management carveback) merely because they were supervisors. He advises that he will push back on any reservations of rights that we take on this Claim. I advised Keith Doan & Blair McCloud. Keith requested updates if situation changes.
11/05/01	Spoke to UW regarding intent of carveback. He advised that cvg is for vicarious liability situations only. No cvg intended where claim alleges wrongful acts by D&O in area of investment banking. Blair McCloud Underwriter Chubb DFI Bmccloud@Chubb.com 312/454-4275
11/1/01	Broker has raised dispute on meaning and INTENT behind the "Management Carveback" found in the E&O exclusion in the above policy. Left vm message and email with UW Keith Doan for understanding of intent.

	Advised Broker that the Claimant (Bremer Business Finance Corp) alleges tha 2 officers of the Insured fraudulently induced Bremer to fund a $2M participation in a loan made by the Insured on a gambling casino development. Such activities fit within Investment Banking Services. Broke requested definition; none in policy. I requested actual copy of Amended Complaint, if any filed yet. What was submitted was memorandum in support of m/file amended complaint. A "General E&O Exclusion (with Management Carveback)" is endorsed onto the Policy (The Policy is Chubb-ER's *The Power* D&O Liability Insurance Policy). I believe there is NO coverage for the Claim, based upon the E&O exclusion, however, the Broker (Bryan Huff from Hayes Group) argues there should be coverage based upon the carve-back in Paragraph 2 of the Exclusion. The Exclusion carves-back Claims in connection with the management or supervision of any division, subsidiary or group of the Parent Corporation offering any of the excluded services. The Broker interprets this carve-back to mean that the Policy provides coverage for the Officers in this case, because simply because they were the Senior VP and Managing Director in charge of the division that performed the investment banking services. I disagree, and believe that there is no coverage, because the allegations against the Officers pertain to Wrongful Act that they committed (in the area of investment banking services), and not just their failure to supervise/recognize Wrongful Acts committed by their employees/division.
10/31/01	Returned Bryan Huff's call, and advised that I have reviewed allegations against the Officer, per the m/amend complaint. And the allegations relate to investment banking services, which are excluded from cvg under the policy.
10/30/01	Bryan Huff at Hayes called to ask whether defense costs will be covered. The Insd has retained counsel to prepare m/dismiss officers from case.
10/29/01	Broker, Bryan Huff at Hayes Group called. Returned his call & left message.
10/15/01	Called Insd contact, Ken Larson and discussed case. Original action agains Insd filed on 12-26-00; therefore, prior and pending exclusion applies. Insd submitted info that D/O to be added pending decision on m/amend file i Sept 01. Claimant alleges investment banking functions which are excluded under policy. M/Amend may have been granted; Brian Palmer at Dorsey and Whitney is counsel. 612-340-2797. Advised Insd of coverage issues.
10/15/01	SENT ACK LTR - DAB
10/12/01	24 hr. contact/ss - Left voicemail message for Ken Larson advising him that Cheryl O'Malley is the adjuster. Claimant: Bremer Business Finance Corporation Ken Larson Miller & Schroeder, Inc. 150 South 5th Street Suite 3000 Minneapolis, MN 55402 Phone - 612/376-1310 Fax – 612/692-5192

	Agent: Bryan Huft The Hays Group, Inc. 80 South 8th Street Suite 1650 Minneapolis, MN 55402 Phone - 612/373-9454 Fax - 612/373-7270
10/11/01	FAXED & MAILED NEW CLAIM TO PITTSBURGH. APPS. WILL BE SENT AT A LATER DATE. RB

10/16/01- MAILING APPLICATIONS AND SUMMARY SHEET TO PITTSBURGH. RB

***Investigation**
01/25/2002: CNO Conference call with Carrie Campi and Joel Townsend in late Dec to discuss Miller & Schroeder E&O exclusion; all new claims will go to Carrie in Simsbury. Joel explained that E&O exclusion not intended to carve back E&O for supervisors; doesn't make sense.

Spoke with Bryan Huff at Hayes Group on 1/17. Advised that we are addressing his request for reconsideraiton, with assistance from Joel Townsend in Simsbury. Sent Joel a draft response for comments.

Bryan Huff called again today, 1/25, requesting status of review.

***Coverage**
02/26/2002: DB2 COVERAGE LETTER SENT - FILED IN ATTACHED DOCUMENTS

***Investigation**
08/22/2002: CNO Rec'd letter from Brian Palmer at Dorsey & Whitney requesting that Chubb reevaluate its cvg position re: Mr. Erickson, given that recent ruling that dismissed Erickson from case, and the findings that Erickson had no direct contact with the Claimants. Insd argues that this proves that Insd-Erickson was acting in managerial capacity only, and cvg should be extended to him based upon carve back.

will review with Spvr.

***Administrative**
02/10/2003: KPE Memo to File.

***Administrative**

02/12/2003: KPE Attorney Correspondence sent.

***Diary Review**
02/27/2003: MMK

Note that coverage challenge was reviewed and responded to on 2/7/03. Chubb's coverage position was not changed.

WIll rediary 45 dyas and review file for closure.

MMK

***Status**
05/07/2003: MMK Based upon info to date, file can be closed.

MMK

EXHIBIT
2
O'Malley
PENGAD 800-631-6989

EXHIBIT
SM 1
9/23/08

Claims Summary

	Plaintiff	Description of Loss	Claim Status	
	Behnke	Tabolich, Iverson, Augusta - NASD	Settled per Cari Campi	Cheryl's
mms	Hyde Family Trust	Dlugosche, Jones - NASD	OPEN	mine
mms	Kellar	Rolblecki,successor	OPEN	mine
mms	Herrmann (heritage)	Iverson, Clarye, Tabolich, Hentges, Larsen, Erickson, Eckholm, Dlugosch, Augusta, Talley, Reeves (Diaz), Wagner, Osgood, Stokes, Penwarden, Jones	OPEN	mine
	Cates	Dlugsoch, Flynn - NASD	OPEN	mine
	McGuire	Dlugsoch, Clarey, Talley, Holtzclaw	OPEN	mine
	Moreland	Webb, Wikner, Dlugosch, Hentges, Mehlaff, McKeand, Nelson, Clarey, Iverson, Erickson - NASD	OPEN	mine
	Johansen	Kallstrom, Frank - NASD	OPEN	mine
	Formica	Hill, Larsen, Clarey, Reinhart - NASD	OPEN	mine
mms	Bremer	Erickson, Frank – loan underwriting NIGC	OPEN	Cheryl's

Company	LOB	Sev	Ar	No	St	Ty	In	Claim No	Pc	Claimant	Claim Handl	Product	
ERII	D&O	03	5	5			Mi	0031	7	San Bernardino County	Carrie I	D&OEPL	
ERII	D&O	03	7	8			Mi	0016[illegible]	7	Patrick Stanchfield	Richard	D&OEPL	
ERII	D&O	03	6	7			Mi	0016205	7	Robert MacAdam	Brooke A.	D&OEPL	
ERII	D&O	03	1	2			Mi	0048025	1	Mark Augusta	Carrie L	D&OEPL	
ERII	D&O	03	1	1			Mi	0047533	1	Kenneth Kellar	Carrie L	D&OEPL	~~[illegible]~~
ERII	D&O	03	2	1			Mi	0047204	1	Baker Living Trust	Carrie L	D&OEPL	NYSE, NASD CA
ERII	D&O	03	1	1			Mi	0047203	1	M.B. Timmerman	Carrie L	D&OEPL	~~[illegible]~~ ~~[illegible]~~
ERII	D&O	03	2	1			Mi	0047201	1	Patrick W. McGuire	Carrie L	D&OEPL	CA, NASD
ERII	D&O	03	2	1			Mi	0047200	1	Leroy R. Cates	Carrie L	D&OEPL	CA
ERII	D&O	03	7	1			Mi	0047199	1	Gerald F. Johansen	Carrie L	D&OEPL	MN
ERII	D&O	03	1	1			Mi	0047198	1	Will Thomas Hyde	Carrie L	D&OEPL	CA
ERII	D&O	03	2	1			Mi	0047197	1	Joseph Formica	Carrie L	D&OEPL	CA
ERII	D&O	03	0	1			Mi	0047196	1	Phillip J. Salley	Carrie L	D&OEPL	NYSE, NASD, CA
ERII	D&O	03	0	1			Mi	0047195	1	Steven Onderwyzer	Carrie L	D&OEPL	
ERII	D&O	02	1	2			Mi	0046559	1	Lewis G. Herrmann	Carrie L	D&OEPL	
ERII	D&O	03	9	1			Mi	0046121	1	Frank T. Spanglor and	Carrie L	D&OEPL	CA
ERII	D&O	03	6	1			Mi	0045979	1	Moreland, James	Carrie L	D&OEPL	
ERII	D&O	04	9	1			Mi	0045978	1	Behnke, John	Ruthanne	D&OEPL	
ERII	D&O	05	9	0			Mi	0044840	1	Bremer Business Financ	Cheryl N	D&OEPL	
ERII	D&O	04	7	7			Mi	0042432	1	First National Bank of	Cheryl N	D&OEPL	
ERII	D&O	02	8	9			Mi	0034574	1	Helen J. Dixon	Marnie M.	D&OEPL	

6

CHUBB GROUP OF INSURANCE COMPANIES

Fifth Avenue Place, 120 Fifth Avenue, Pittsburgh, PA 15222-3008
Phone: (412) 391-6585 • Facsimile (412) 456-8009

February 25, 2002

Bryan Huff
The Hayes Group, Inc.
IDS Center, Suite 1650
80 South 8th Street
Minneapolis, MN 55402

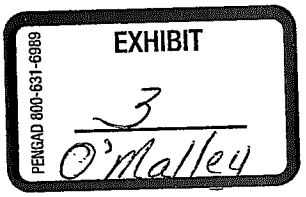
RE: INSURED: Miller and Schroeder, Inc.
POLICY NO: 8166-6027
CLAIM NO: 44840
SUBJECT: Bremer Business Finance Corporation v. Miller & Schroeder Investments Corporation

Dear Mr. Huff:

On behalf of Chubb Executive Risk ("Chubb"), this letter will acknowledge receipt of your request for reconsideration of Chubb's coverage position regarding the above-referenced matter against Miller & Schroeder Investments Corporation ("M&S"), Steven W. Erickson, and Michael J. Frank.

The above matter involves a lawsuit by Bremer Business Finance Corporation ("Bremer") against M&S and Messrs. Erickson and Frank, in the District Court, Second Judicial District of the County of Ramsey, State of Minnesota. In the lawsuit, Bremer alleges that the defendants are liable for misrepresentation and fraud in the inducement in connection with a specific transaction – namely, M&S's sale to Bremer of a $2 million participation in a loan M&S had made to President R.C.- St. Regis Management Company. Bremer alleges that in connection with the sale of the loan participation, the defendants falsely represented that a contract and a pledge agreement necessary to the performance of the loan had been ratified by the necessary regulatory authorities, when in fact they had not. As a result, prospects for repayment of the loan were materially impaired, a fact that allegedly was not disclosed to Bremer when M&S sold the participation to it. Soon after Bremer funded its participation, President R.C. – St. Regis defaulted on the loan, and litigation regarding various parties' obligations ensued. In the above action, Bremer seeks rescission of its participation in the loan, and an award of $2 million (the consideration paid for its participation) together with interest, costs and disbursements.

By letter dated December 13, 2001, I advised you that no coverage would be available for this matter under the Directors and Officers Liability coverage, Policy No. 8166-6027 ("the Policy"), issued to Miller & Schroeder by Chubb. Specifically, coverage was denied pursuant to a broad E&O exclusion in the Policy (the "General E&O Exclusion") that provides that:



1. No coverage will be available under the Policy for **Loss** including Defense Expenses for any **Claim** made against any **Insured** based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving an **Insured's** actual or alleged rendering or failure to render the following services:

   Investment Banking Services
   Security Broker/Dealer Services
   Securities Underwriting

2. Paragraph (1) above is not intended, however, nor shall it be construed to apply to **Loss**, including Defense Expenses, in connection with any **Claim** against an **Insured** to the extent that such **Claim** is for a **Wrongful Act** by **Insured Person** in connection with the management or supervision of any division, subsidiary or group of the Parent Corporation offering any of the aforementioned services.

In your letter dated December 28, 2001, you conceded that this matter involves allegations of **Wrongful Acts** based on and arising out of the defendants' actual or alleged rendering of investment banking services. Thus, there is no dispute that this matter triggers the first paragraph of the General E&O Exclusion. You argued, however, that with respect to Mr. Erickson, a Senior Vice President of M&S, the exception contained in paragraph 2 of the General E&O exclusion should apply, and that Chubb erred in concluding otherwise. In particular, you assert that Mr. Erickson "was acting in an Insured capacity, as supervisor and administrator of the Gaming Finance Division, and that it was in this capacity, only, that he was included in the complaint." (Emphasis omitted.) You then cited isolated statements in a legal memorandum and a proposed complaint in the matter that refer to Mr. Erickson's supervisory role with respect to the loan participation offering to support your argument that the exception for management or supervisory claims should apply here, so that Mr. Erickson would be entitled to coverage for his defense in this case.

We have carefully considered your arguments and have again reviewed the provisions of the Policy in light of the allegations set forth in the Complaint. Unfortunately, Chubb must respectfully reaffirm its declination of coverage under the Policy based upon the General E&O Exclusion. As an initial matter, the Complaint does not support your assertion that Mr. Erickson was only named as a defendant because he was the supervisor and administrator of the Gaming Finance Division of M&S. To the contrary, the **Wrongful Acts** alleged against Mr. Erickson, as with the other defendants, are for his direct involvement in a specific investment banking transaction, not for liability in connection with his management or supervision of a particular M&S division, subsidiary or group. For the exception to the General E&O exclusion to apply, a **Claim** must involve allegations of a **Wrongful Act** *in connection with the management or supervision of* a division, subsidiary or group. The purpose of the exception is clear from this language – a claim against an insured director or officer for breach of duty owed as a manager/supervisor – for example, a shareholder claim alleging mismanagement of a unit --

would not be excluded simply by virtue of the fact that the unit engages in investment banking transactions. By the same token, however, the mere fact that Mr. Erickson is identified in a claim as a person with management or supervisory responsibilities does not convert an E&O claim against him into one alleging **Wrongful Acts** in connection with his management or supervisory responsibilities. Indeed, our review of the pleadings provided to us confirms that Mr. Erickson's alleged liability arises out of his direct involvement in the transactions at issue (and alleged misrepresentations and inducements in connection therewith), not out of any alleged improper management or supervision of M&S. Accordingly, Chubb reaffirms its decision to **decline** coverage, as initially stated in my December 13 letter.

Chubb does, however, accept the submitted materials as notice of a potential claim pursuant to the Notice provisions of the Policy. Please submit for our review any further information which you might now have or may obtain in the future that you believe may bear upon the question of insurance coverage in this matter. If a covered **Claim** related to the above set of facts and circumstances should arise in the future, upon written notice of such **Claim**, coverage will be examined during the applicable **Policy Period** and its corresponding Limits of Liability.

The foregoing statements of Chubb's position as to coverage for this matter are premised upon the allegations in the Complaint as presently filed and are by necessity subject to change as additional allegations and facts are developed through the course of discovery and further pleadings. Chubb expressly reserves all rights under the Policy and available at law to deny coverage and/or rescind the policy on additional and alternative bases as other terms, conditions, exclusions, endorsements and provisions of the Policy, including representations, statements, declarations and omissions in connection with the application therefor, are found to be applicable.

Please do not hesitate to contact me at (412) 456-8879 or at my e-mail address *comalley@chubb.com*, if you wish to further discuss this matter.

Very truly yours,
Chubb Specialty Insurance

Cheryl O'Malley

Cheryl N O'Malley, Esq.
Specialty Claim Examiner

CNO/dab.Cov Ltr

cc: Brian Palmer
Dorsey & Whitney LLP
50 South Sixth Street, Suite 1500
Minneapolis, MN 55402-1498

Ken Larsen
Vice President and Controller
Miller and Schroeder, Inc.
150 South 5th St.,,Suite 3000
Minneapolis, MN 55402

bcc: Christine Fear
EPP – Simsbury
Fax – 860-408-2016

Chubb Group of Insurance Companies

send copies to Carie Campi + Jodi Townsend

September 18, 2001

Ken Larsen
Vice President and Controller
Miller and Schroeder, Inc.
150 South 5th Street
Suite 3000
Minneapolis, MN 55402

RE: INSURED: Miller and Schroeder, Inc
POLICY NO: 8166-6027
CLAIM NO: 42432
SUBJECT: First National Bank of the North, et al. v. Miller & Schroeder Financial, Inc., et al.

Dear Mr. Larsen:

On behalf of Chubb Executive Risk ("Chubb"), this letter will again acknowledge receipt of the complaint filed by First National Bank of the North, et al. against Miller and Schroeder Financial, Inc., Miller and Schroeder, Inc., MI Acquisition Corporation, and John Does 1-20 (allegedly officers, directors or employees of Miller and Schroeder, Inc.). The Complaint is filed in the District Court, Fourth Judicial District of the County of Hennepin, State of Minnesota, at Court File No. 00-15958 ("Complaint"), and alleges:

Count I – negligence in the underwriting of the United Homes, Inc. debentures;

Count II – negligent misrepresentation of material facts with respect to the UHI debentures;

Count III – violation of the Minnesota Securities Act with respect to participation in misrepresentations in the sale of the UHI debentures;

Count IV – violation of the Minnesota Securities Act with respect to the "use of manipulative, deceptive and other fraudulent devices and contrivances";

Count V – violation of the Minnesota Consumer Fraud Act in connection with the sale of the UHI debentures and failure to disclose material negative and adverse information about the UHI;

ERII 001809

12

Count VI and VII– violations of the Securities Act of 1933 for defendants' offer and sale of the UHI debentures by means of a prospectus and oral communications that contained untrue statements or omissions of material facts;

Count VIII – common law fraud based upon a scheme to deceive and defraud plaintiffs into investing in the UHI debentures;
Plaintiffs seek class certification, an award of compensatory damages, interest, costs and expenses, including attorney's fees.

We have reviewed the provisions of the Directors and Officers Liability Insurance coverage under Chubb Executive Risk Policy No. 8166-6027 in light of the allegations set forth in the Complaint, and in the context of this litigation as presently submitted, coverage is respectfully **declined** under the Policy.

It appears that the applicable Policy Period is July 1, 2000 to July 1, 2001 and provides limits of $5,000,000 for each **Loss**, each **Policy Period**. These limits are subject to deductible Amount of $50,000 for each **Claim** under Insuring Clause B(1), or $100,000 for each **Claim** under Insuring Clause B(2).

Coverage is declined under the Policy for the following reasons. There is no coverage under Insuring Clauses (A) or (B)(1) of the Policy, given that no Insured Person (director and/or officer of the **Insured Organization**) has been specifically named or served as a **Defendant** in the litigation. Under the Complaint, no **Claim** has been asserted against any **Insured Person** under the Policy for which coverage should be granted under Insuring Clause (A), or for which the **Insured Organization** must provide indemnification to trigger coverage under Insuring Clause (B)(1).

Furthermore, there is no coverage available under Insuring Clauses A, B(1) or B(2) of the Policy, given the Securities Exclusion under Policy Endorsement No. 3, which provides:

> ...[the] Policy does not apply to any Claim based on, arising out of directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged violation of:
>
> (1) the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, any other federal law, rule or regulation with respect to the regulation of securities, any rules of regulations of the United States Securities and Exchange Commission, or any amendment of such laws, rules or regulations; or
>
> (2) any state securities or "Blue Sky" laws or rules or regulations or any amendment of such laws rules or regulations; or

(3) any provision of the common law imposing liability in connection with the offer, sale or purchase of securities.

Chubb Executive Risk does, however, accept the submitted materials as notice of a potential claim pursuant to the Reporting and Notice provisions of the Policy. Please submit for our review any further information which you might now have or may obtain in the future that you believe may bear upon the question of insurance coverage in this matter. If a covered **Claim** related to the above set of facts and circumstances should arise in the future, upon written notice of such **Claim**, coverage will be examined during the applicable **Policy Period** and its corresponding Limits of Liability. [Note however that if Miller and Schroeder, Inc., or any other **Insured** under this Policy, received this **Claim** prior to July 1, 2000, then the above referenced policy period will not apply.]

The foregoing statements of Chubb Executive Risk's position as to coverage for this matter are premised upon the allegations in the Complaint and presently known facts and are by necessity subject to change as additional allegations and facts are developed through the course of discovery and further pleading.

Chubb Executive Risk expressly reserves all rights under the policy and available at law to deny coverage and/or rescind the policy on additional and alternative bases as other terms, conditions, exclusions, endorsements and provisions of the Policy, including representations, statements, declarations and omissions in connection with the application therefore, are found to be applicable.

Please do not hesitate to contact me at (412) 456-8879 or at my e-mail address, *comalley@chubb.com*, if you wish to further discuss this matter.

Very truly yours,

Cheryl N. O'Malley, Esq.
Examiner

CNO/dab.Cov

cc: Erin Dooley
The Hays Group, Inc.
IDS Center, Suite 1650
80 South 8th Street
Minneapolis, MN 55402

Chubb Group of Insurance Companies
Chubb Specialty Insurance
120 Fifth Avenue
Fifth Avenue Place
Pittsburgh, PA 15222-3008
Phone: 412 456 8879 • Fax: 412.456.8009

January 22, 2002

Ken Larsen
Vice President and Controller
Miller and Schroeder, Inc.
150 South 5th Street
Suite 3000
Minneapolis, MN 55402

RE:	INSURED:	Miller and Schroeder, Inc.
	POLICY NO:	8166-6027
	CLAIM NO:	42432
	SUBJECT:	First National Bank of the North, et al. v. Miller & Schroeder Financial, Inc., et al.

Dear Mr. Larsen:

On behalf of Chubb Executive Risk ("Chubb"), this letter will serve to update Chubb's coverage opinion from September 18, 2001 following our amended complaint filed by First National Bank of the North, et al. against Miller and Schroeder Financial, Inc., Miller and Schroeder, Inc., MI Acquisition Corporation, and officers, directors or employees of Miller and Schroeder, Inc. including James A. Arias, John Clarey, Kenneth Dawkins, James Dlugosh, Theodore Glasrud and Thomas Nelson. The Complaint is filed in the District Court, Fourth Judicial District of the County of Hennepin, State of Minnesota, at Court File No. 00-15958 ("Complaint"), and alleges:

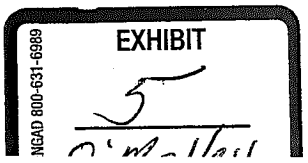
Count I – negligence in the underwriting of the United Homes, Inc. debentures;

Count II – negligent misrepresentation of material facts with respect to the UHI debentures;

Count III – violation of the Minnesota Securities Act with respect to participation in misrepresentations in the sale of the UHI debentures;

Count IV – violation of the Minnesota Securities Act with respect to the "use of manipulative, deceptive and other fraudulent devices and contrivances";

Count V – violation of the Minnesota Consumer Fraud Act in connection with the sale of the UHI debentures and failure to disclose material negative and adverse information about the UHI;



15

Count VI and VII– violations of the Securities Act of 1933 for defendants' offer and sale of the UHI debentures by means of a prospectus and oral communications that contained untrue statements or omissions of material facts;

Count VIII – common law fraud based upon a scheme to deceive and defraud plaintiffs into investing in the UHI debentures; Plaintiffs seek class certification, an award of compensatory damages, interest, costs and expenses, including attorneys fees.

Count IX – violation of the Uniform Fraudulent Transfer Act for advances by MSF to MSI.

We have reviewed the provisions of the Directors and Officers Liability Insurance coverage under Chubb Executive Risk Policy No. 8166-6027 in light of the allegations set forth in the Amended Complaint, and in the context of this litigation as presently submitted, coverage is respectfully declined under the Policy.

The applicable **Policy Period** is July 1, 2000 to July 1, 2001 and provides limits of $5,000,000 for each **Loss**, each **Policy Period**. These limits are subject to deductible Amount of $50,000 for each **Claim** under Insuring Clause B(1), or $100,000 for each **Claim** under Insuring Clause B(2).

Coverage is declined under the Policy for the following reasons. There is no coverage available under Insuring Clauses A, B(1) or B(2) of the Policy, based upon the Securities Exclusion under Policy Endorsement No. 3, which provides:

> ...[the] Policy does not apply to any Claim based on, arising out of directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged violation of:
>
> (1) the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, any other federal law, rule or regulation with respect to the regulation of securities, any rules of regulations of the United States Securities and Exchange Commission, or any amendment of such laws, rules or regulations; or
>
> (2) any state securities or "Blue Sky" laws or rules or regulations or any amendment of such laws rules or regulations; or
>
> (3) any provision of the common law imposing liability in connection with the offer, sale or purchase of securities.

Chubb Executive Risk does, however, accept the submitted materials as notice of a potential claim pursuant to the Reporting and Notice provisions of the Policy. Please submit for our review any further information which you might now have or may obtain in the future that you

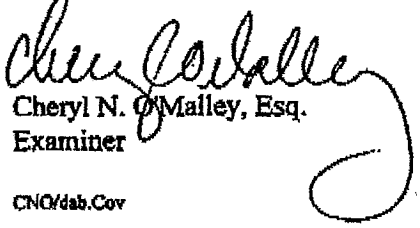
believe may bear upon the question of insurance coverage in this matter. If a covered **Claim** related to the above set of facts and circumstances should arise in the future, upon written notice of such **Claim**, coverage will be examined during the applicable **Policy Period** and its corresponding Limits of Liability. [Note however that if Miller and Schroeder, Inc., or any other **Insured** under this Policy, received this **Claim** prior to July 1, 2000, then the above referenced policy period will not apply.]

The foregoing statements of Chubb Executive Risk's position as to coverage for this matter are premised upon the allegations in the Complaint and presently known facts and are by necessity subject to change as additional allegations and facts are developed through the course of discovery and further pleading.

Chubb Executive Risk expressly reserves all rights under the policy and available at law to deny coverage and/or rescind the policy on additional and alternative bases as other terms, conditions, exclusions, endorsements and provisions of the Policy, including representations, statements, declarations and omissions in connection with the application therefore, are found to be applicable.

Please do not hesitate to contact me at (412) 456-8879 or at my e-mail address, *comalley@chubb.com*, if you wish to further discuss this matter.

Very truly yours,



Cheryl N. O'Malley, Esq.
Examiner

CNO/dab.Cov

cc: Erin Dooley
The Hays Group, Inc.
IDS Center, Suite 1650
80 South 8th Street
Minneapolis, MN 55402

Lindsey Arthur, Esq.
500 Young Quinlan Building
81 South Ninth Street
Minneapolis, MN 55402

Proprietary & Confidential. For Internal Use Only.

11/29/01	24 hr contact/ss - Spoke with Ken Larson advising him that Maggie Klimczyk is the adjuster. Claimant: James Moreland Ken Larson Miller & Schroeder, Inc. 150 South 5th Street Suite 3000 Minneapolis, MN 55402 Phone - 612/376-1310 Fax – 612/376-1321 Agent: Marsh USA, Inc. 500 West Monroe Street 21st Floor Chicago, IL 60661 Phone - 312/627-6702 Fax - 312/627-6939

PENGAD 800-631-6989
EXHIBIT
6
O'Malley

MEMORANDUM

TO: File

FROM: Maggie Klimczyk

DATE: December 10, 2001

SUBJECT: Insured: Miller and Schroeder
Claimant: James Moreland
Policy No.: ER - 8166-60-27
Claim No.: 45979

Received new matter on 11/26. Reviewed on 12/6 with respect to coverage.

This matter was filed on August 10, 2001. Received by letter from Lindsay G. Arthur of Arthur Chapman Kettering Smetak & Pikala of Minneapolis. With respect to the Moreland matter, Mr. Arthur indicates that he is specifically tendering on behalf of Mr. Iverson. He states on page two of his letter that it is apparent that this policy, together with attached Endorsement 9, provides coverage for Mr. Iverson for the claims of inadequate management and supervision that have been made against him.

Reviewed the proceeding file. This is an arbitration proceeding before NASD. Answered questions in Chicago. The claimants are James D. Moreland, Doris N. Moreland and Donald Moreland. James and Doris are husband and wife. Donald is their son. All had accounts with Miller and Schroeder. Allegations state that in or about 1996, respondent Margaret Webb started to call with investment recommendations. States that Webb was an employee and authorized agent of Miller, acting in the capacity of account executive and sales representative. Webb was the sales representative who handled the claimant's account during the relevant period. Other defendants in the action are Roger James Wikner, President, Director, shareholder and control person for Miller; James Francis Dlugosch, President, Director and control person of Miller; Edward Joel Hentges, officer and control person of Miller; Bradley Rae Mehlaff, officer and control person of Miller; Judith Marie McKeand, officer and control person of Miller; Thomas Steven Nelson, Senior Vice President and control person of Miller; John Clarey, officer and control person of Miller; James Edward Iverson, Director and control person of Miller; Steven Wesley Erickson, officer, Senior Vice President and control person of Miller.

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EXHIBIT
7
O'Malley
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The Complaint alleges the following causes of action: Count I Section 10(b) and 10b-5; Count II – Fraud; Count III – Negligence; Count IV – Negligence and Breach of Fiduciary Duty (failure to supervise); Count V – Violations of Section 15(b)(4)(E). Plaintiffs seek compensatory damages of approximately $161,528.23 plus $300,000 in punitive damages. Briefly, the allegations are that the claimants were retired and wanted conservative investments. Allegedly as part of the fraudulent scheme, the respondents recommended the poorest quality/highest risk securities which resulted in their loss. Specifically, with respect to the negligence and breach of fiduciary duty (Failure to Supervise Count), the allegation is that the respondents were liable for their own negligence and have breached their duties in failing to adequately supervise persons in connection with the claimants' accounts. Further, it is alleged the respondents did not maintain a reasonably adequate system of supervision and control or did not enforce such system with a reasonable diligence.

On October 1, 2001, an answer was filed on behalf of all respondents. This answer noted that on July 10, 2001, NASD determined that a previous claim by Doris Moreland against Miller and Schroeder and Webb was unsupported by the evidence and that the basis of this claim was the same. As such, the basis that the claim is the same is the matter now brought by the Morelands in this proceeding and this proceeding should be dismissed. The answer also goes through the transactions at issue and states that the claimants were financially sophisticated and, in fact, made their own investment decisions after information was provided to them.

Reviewed the Policy. The policy period is July 31, 2000 to July 31, 2003. Endorsement No. 4 of the Policy states that in consideration of the premium charged, this Policy does not apply to any Claim based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged violation of:

(1) the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, any other federal law, rule or regulation with respect to the regulation of securities, any rules or regulations of the United States Securities and Exchange Commission, or any amendment of such laws, rules or regulations: or

(2) any state securities or "Blue Sky" laws or rules or regulations or any amendment of such laws, rules or regulations; or

(3) any provision of the common law imposing liability in connection with the offer, sale or purchase of securities.

Endorsement 9 which is referred to in the letter from counsel is an endorsement for Outside Directorship Liability and is not applicable to this matter.

Endorsement 11 is a General E & O Exclusion (With Management Carveback). This Endorsement states that in consideration of the premium charged:

(1) No coverage will be available under the Policy for Loss including Defense Expenses for any Claim made against any Insured based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving an Insured's actual or alleged rendering or failure to render the following services:

Investment Banking Services
Security Broker/Dealer Services
Securities Underwriting

(2) Paragraph (1) above is not intended, however, nor shall it be construed, to apply to Loss, including Defense Expenses, in connection with any Claim against an Insured to the extent that such Claim is for a Wrongful Act by Insured Person in connection with the management or supervision of any division, Subsidiary or group of the Parent Corporation offering any of the aforementioned services.

The Policy provides limits of $5,000,000 with deductible amounts of $50,000 for each claim arising under Insuring Clause B(1) or $100,000 for each claim under Insuring Clause B(2). From a review of the information to date, the 10(b)/10b-5 claim is against all respondents and alleges various misrepresentations and omissions as well as a violation of the Illinois Securities Law of 1953 with respect to the investments question. The fraud count is against all respondents and alleges that the respondents made misrepresentations and omissions of material facts to the claimants to induce them, to their financial detriment, to enter into the transactions in question. The negligence count alleges that the respondents had a duty to act in the best interest of their clients and not of themselves and breached this duty. The negligence and breach of fiduciary duty (failure to supervise) count alleges that the respondents were liable for failing to supervise the respondents and not maintaining an adequate system of supervision or control.

December 11, 2001
Miller and Schroeder
Page 4

Endorsement No. 11 deals with the management or supervision of a specific division or part of the parent corporation, and not employee supervision. Thus, the carveback under Endorsement 11 is not applicable to this matter and the exclusion for securities claims with respect to Endorsement 4 serves to exclude this matter. Dictated coverage letter with respect to this and called counsel to inform them of coverage denial. Counsel was not in Left message for him to return my call.

MMK/ke.ER

PS * Answer to the complaint notes a prior NASD filing by Mrs. Marchand against Miller + Schroeder + [illegible]. Marriage [illegible] - Related?

Atty claimed so in Answer; but stated [illegible] when I inquired about [illegible]. Should request further info → pending + pending exclusion may apply.

Cheryl

ERII 002599

22

ENDORSEMENT NO. 3
SECURITIES EXCLUSION

This Endorsement, effective at 12:01 a.m. on July 31, 1997, forms part of

Policy No.	751-075440-97
Issued to	MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by	Executive Risk Indemnity Inc.

In consideration of the premium charged, this Policy does not apply to any Claim based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving any actual or alleged violation of:

(1) the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, any other federal law, rule or regulation with respect to the regulation of securities, any rules or regulations of the United States Securities and Exchange Commission, or any amendment of such laws, rules or regulations; or

(2) any state securities or "Blue Sky" laws or rules or regulations or any amendment of such laws, rules or regulations; or

(3) any provision of the common law imposing liability in connection with the offer, sale or purchase of securities.

All other terms, conditions and limitations of this Policy shall remain unchanged.

_____
Authorized Representative

ERII 006644

23

ENDORSEMENT NO. 9
GENERAL E & O EXCLUSION (WITH MANAGEMENT CARVEBACK)

This Endorsement, effective at 12:01 a.m. or July 31, 1997, forms part of

Policy No. 751-075440-97
Issued to MI Acquisition Corporation dba Miller & Schroeder, Inc.
Issued by Executive Risk Indemnity Inc.

In consideration of the premium charged:

(1) No coverage will be available under the Policy for Loss including Defense Expenses for any Claim made against any Insured based on, arising out of, directly or indirectly resulting from, in consequence of, or in any way involving an Insured's actual or alleged rendering or failure to render the following services:

Investment Banking Services
Security Broker/Dealer Services
Securities Underwriting

(2) Paragraph (1) above is not intended, however, nor shall it be construed, to apply to Loss, including Defense Expenses, in connection with any Claim against an Insured to the extent that such Claim is for a Wrongful Act by Insured Person in connection with the management or supervision of any division, Subsidiary or group of the Parent Corporation offering any of the aforementioned services.

All other terms, conditions and limitations of this Policy shall remain unchanged.

Authorized Representative

D25090 (9/97)

ERII 006651

24

12/6/01

Miller & Schroeder
Moreland Malter

- Files 8/10/01

- on b/h of Iversen tendering def to Webb
- states ends 9 provides coverage for Iversen for claims of inadequate management and supervision.

ARBITRATION PROCEEDING
hearing requested in Chicago

π's James & Doris Moreland - h&w customers of Miller & Schroeder

Donald - son who maintains acct. investment experience. highly conservative. many yrs ago purchased bonds for Miller

'94 Δ Webb starts to call w/ investors
Δ's - Miller - broker dealer & member of NASD.

ERII 002601

Webb - employee / sales rep
Wikner - Pres / Dir / Sh / control person for Miller
Dlugosch - " "
Hentges - officer & control person of Miller
Mehlaff - officer & control person of Miller
McKeand - " "
[illegible]

EXHIBIT
9
O'Malley

NGAD 800-631-6989

25

Clary – officer & control person of Miller
Iversen – Director & control person of Miller
Ericson – officer / Sr VP / control person of Miller
Claim – Violations of 10(b) / 10(b-5)
ILL Sec Law
ILL Deceptive Trade Practices Act
Common law fraud
br of Fid duty
Aid & violations of Sec 15(b)(4)(E)
20(a)
Negligence / Failure to supervise
respondeat superior

Client relations. Wanted conservative investments as part of fraudulent scheme, Respondents recommended the poorest quality / highest risk securities.

Bonos in accts – total loss – $33,339.72

Respondents received substantial remuneration.
Total Loss – 161,528.23
also seek 300K in punitive damages.
para 21 – Miller failed to adequately supervise employees.
para 34 – Negligence & Br of Fid duty – (Failure to Supervise).

Filed?

Answer —

7/10/2001 NASD determined that a previous claim by Doris Moreland against Miller & Schroeder & Webb was unsupported by the evidence.
— basis of claim the same.

When was this matter filed?

A's — aware of risks
client made decision on purchase after being sent info & reviewing it.

Requirements very involved in direct supervision of Webb.

Filed 10/1/2001 by Arthur, Chapman Kettering Smith & Pickett.

Policy: Insured: Miller & Schroeder
7/31/2000 – 7/31/2003
D&O policy
Limit — 5M. 0/50/100K retention
END #1 — punitive damage excl.
END #4 — Sec exclusion

ERII 002603

END #9 —
o/s D end. ?

END # 11 — Management carveback for E&O exclusion.
— for management / supervising of a division. Limited exception not applicable to supervision of employee.

END #4 —
* exclusion from claims based upon arising out of securities violations.

— entire copy of policy?
other claims?

81666027 —

EXHIBIT Q

1 A. Yes.
2 Q. Prior to that how -- what was your position?
3 A. I was a claims examiner.
4 Q. In a particular unit?
5 A. In the D and O unit.
6 Q. How long were you in that position?
7 A. From my start date, August 14, 2000.
8 Q. Had you worked for an insurance company
9 prior to working for Chubb?
10 A. No.
11 Q. What is your -- let me just sort of start
12 and get a rough chronology.
13 When did you -- did you graduate from
14 college?
15 A. Yes.
16 Q. Where did you attend?
17 A. I went to the University of Kansas.
18 Q. Obtain a BA?
19 A. BS in business administration.
20 Q. What year was that?
21 A. 1988.
22 Q. Any formal education beyond that?
23 A. Yes. I have a law degree.
24 Q. Where did you obtain that?
25 A. Rutgers University.

1 policy you didn't have any written materials supplied
2 by Chubb that -- with respect to the policy
3 generally --
4 A. No.
5 Q. -- that explained or helped to explain the
6 terms of coverage or endorsements?
7 A. No.
8 Q. How would you go about then, let's say
9 you're a brand new claims examiner in 2000, you get a
10 claim in, a D and O claim, you're asked to render a
11 coverage opinion on it.
12 I'm just asking generally now. What was
13 your process for going about determining whether there
14 was coverage for a claim that's been submitted to you?
15 A. I would review the claim, I would review the
16 policy, I would review the policy provisions and
17 determine if it was a claim.
18 And if it was a claim, if any exclusions
19 applied to preclude coverage and I would discuss it
20 with my supervisor.
21 Q. Do you undertake any -- I'm just assuming
22 this, but Chubb is an insurance company that gets lots
23 of claims presented every day.
24 And I would think some of them may
25 present sort of garden variety issues that the company

1 A. No.
2 Q. Did you consult with anybody in the
3 Underwriting Department in making any decisions on
4 coverage with respect to the Heritage Bond claims?
5 A. No.
6 Q. Is that something you would do from time to
7 time in other areas?
8 A. Yes.
9 Q. What would be the circumstances where you
10 might consult somebody in underwriting?
11 A. From my understanding -- I would have
12 consulted with someone in underwriting had the
13 underwriter been at the company but he was not.
14 Q. Had the underwriter that issued the Miller
15 and Schroeder policy been still at the company, you
16 would have consulted him?
17 A. I possibly would have.
18 Q. About what kind of things?
19 A. To determine -- well, actually if I can step
20 back.
21 Q. Sure.
22 A. Thinking back the way that we went through
23 this, if I were to talk to an underwriter, it would be
24 to clarify any -- the endorsements or that type of
25 thing.

1 Q. Do you remember, I know it's been awhile
2 now, but do you remember having any questions about
3 the claim that you wanted to get answered from an
4 underwriter?
5 A. I went to speak with Joel Townsend.
6 Q. What questions did you have for him?
7 A. This policy -- as you can tell, I was fairly
8 new to the company. This policy was somewhat
9 unfamiliar to me.
10 Q. The policy itself was?
11 A. Yes, the policy form. So I wanted to
12 discuss the coverage with Joel Townsend.
13 Q. When you say this policy form was -- did you
14 say unusual to you?
15 A. I had not seen it on a financial institution
16 previously.
17 Q. Okay. You had not seen a --
18 A. The Power.
19 Q. The Power on a financial --
20 A. With a financial institution.
21 Q. Had you seen the Power before?
22 A. Yes.
23 Q. What types of claims had you seen it with?
24 A. Typically small family run private
25 businesses.

1 A. I went to Joel because of his expertise in
2 the financial -- he deals with the financial industry.
3 So that's -- I mean it didn't surprise
4 me. Nothing surprised me.
5 Q. You used the word "unusual". There was
6 something unusual about this?
7 A. It was a financial institution on a Power.
8 That's unusual.
9 Q. Is there something you would -- was it more
10 common to expect a financial institution to be covered
11 by some other type of D and O policy?
12 A. There are policies written for financial
13 institutions. I don't know what the policy forms are.
14 Q. Are you talking about D and O policies?
15 A. Um-hm.
16 Q. That's a yes?
17 A. Yes, sorry. Can I clarify that? I'm not
18 sure if at that time they were being written. I know
19 they are now.
20 Q. You're not sure of what was being written?
21 A. The D and O forms for financial
22 institutions. This was a policy written quite awhile
23 ago. At that time they may not have been -- I don't
24 know.
25 Q. It just suggests to me if you thought it was

1 endorsement No. 9 to the Miller and Schroeder policy.
2 That is the general E and O exclusion
3 with management carveback, correct?
4 A. That's correct.
5 Q. You made a determination that in this case
6 that was at least one ground for denying coverage to
7 the insureds?
8 A. That's correct.
9 Q. This exclusion?
10 A. That's correct.
11 Q. I want to ask you about some of your
12 opinions with respect to that endorsement.
13 First of all, would you agree with me
14 that in the absence of an E and O exclusion the Power
15 D and O policy can provide coverage for some types of
16 E and O claims?
17 MR. TOPOL: Objection.
18 THE WITNESS: I would -- it's very
19 difficult for me to answer that without seeing a claim
20 put in front of me.
21 Q. (By Mr. Kolbo) Isn't the reason for -- the
22 reason for an endorsement that's an exclusion, I
23 presume is to exclude something that would otherwise
24 potentially be covered under the policy, correct?
25 A. That's a reasonable understanding of it.

1 Q. If the Power policy itself minus the
2 endorsements already excluded E and O coverage, than
3 endorsement 9 would be rather superfluous, wouldn't
4 it?
5 A. From a general standpoint. I guess that's a
6 reasonable statement.
7 Q. Is it your experience that there can
8 sometimes, as a claims examiner or supervisor, that
9 there can be overlapping coverages let's say between a
10 D and O policy and E and O policy?
11 A. Typically not.
12 Q. Have you seen that?
13 A. No.
14 Q. Never seen that?
15 A. No.
16 Q. You're familiar I take it with -- we can
17 take a look at it here with the definitions of a
18 wrongful act under the D and O policy, the Power?
19 A. Um-hm.
20 Q. I think it's under Page 3 of the policy if
21 you want to just turn to that quickly.
22 Paragraph 3 or Page 3 under paragraph M
23 there is some definitions of wrongful act.
24 A. Yes.
25 Q. And there is a variety of them but among

1 them is M2 which is any other actual or alleged act,
2 error, omission, misstatement, misleading statement or
3 breach of duty by an insured person in his or her
4 capacity as a director or officer of the company.
5 Would you agree with me that that
6 paragraph could at least by its own terms contemplate
7 coverage for error and omission type claims?
8 A. Only in their role as director and officer.
9 Q. Right. Well, this is a D and O policy,
10 right?
11 A. Right.
12 Q. But it contemplates coverage for errors and
13 omissions alleged against an insured person in his or
14 her capacity as director or officer of the company?
15 A. The terminology error and omissions
16 insurance to me is a word of art. Tends to mean a
17 professional service. So the word error and omission
18 in this particular definition of wrongful act does not
19 mean the same thing to me as an E and O policy for E
20 and O coverage.
21 Q. Term of art by the Chubb?
22 A. No. I think in general error and omission
23 coverage is professional services of some sort.
24 Q. Let me then ask you with respect to the
25 endorsement No. 9 itself. Paragraph 1 of the

1 security broker --
2 A. I don't remember.
3 Q. Would in your judgment if a claim had been
4 made against Miller and Schroeder or one of its
5 officers and directors I should state for say an
6 employment law claim, one of the officers or directors
7 is sued for a employment law claim, would that be
8 excluded by paragraph 1?
9 A. No.
10 Q. What exclusion -- what paragraph 1 excludes
11 is if an officer and director is sued or claim is made
12 against it for the actual or alleged rendering or
13 failure to render any of these listed services, that
14 would be excluded by paragraph 1?
15 MR. TOPOL: Objection. That's an
16 incomplete read based on -- there is a lot of
17 prefatory language that matters here.
18 Q. (By Mr. Kolbo) Let's just skip to paragraph
19 2. Paragraph 2 is -- that contains what's called at
20 the top of the endorsement the management carveback,
21 right.
22 A. Yes.
23 Q. And is it fair to say that a management
24 carveback or is it fair to say that a carveback is a
25 carveback of coverage that has otherwise been

1 excluded?
2 A. It limits the exclusion.
3 Q. So in the absence of the carveback, the
4 exclusion would be broader?
5 A. Yes.
6 Q. And in this case the carveback is for claims
7 for a wrongful act by an insured person in connection
8 with the management or supervision of any division,
9 subsidiary or group of the parent corporation offering
10 any of the aforementioned services, correct?
11 A. Correct.
12 Q. So if an officer or director is sued or a
13 claim is made against it in connection with the
14 management or supervision of any division, subsidiary
15 or group of the parent offering securities
16 underwriting, securities broker dealer services,
17 investment banking services that would be covered
18 pursuant to the carveback, correct?
19 MR. TOPOL: Objection.
20 THE WITNESS: I guess I have a hard
21 time -- I mean you're basically reading back the
22 endorsement to me and the exclusion. The exclusion
23 says what it says. I can't disagree that it doesn't
24 say what it says. How you interpret that can be
25 different.

1 trying to make it difficult.
2 You made a conclusion -- first of all,
3 you examined endorsement No. 9 to determine whether it
4 applied in this case?
5 A. Right.
6 Q. The Heritage case?
7 A. Um-hm.
8 Q. And you made a determination, I take it,
9 according to your letters that the management
10 carveback position did not carve back coverage for any
11 of the allegations made against the officers and
12 directors in this case; is that correct?
13 A. Yes.
14 Q. What was the reasoning you employed to
15 determine that the carveback did not apply?
16 A. Because the allegations were not against the
17 insured persons in connection with the management or
18 supervision of a division, subsidiary, group.
19 It was as a result of the management of
20 individuals and specific activities. The sale of
21 Heritage Bonds.
22 Q. Would you agree with me that the allegations
23 of the -- a number of the statements and complaints,
24 statements of claim and complaints, did include
25 allegations of management and/or supervisory liability

1 me.
2 Managing a group means managing the
3 business activities, the management of the daily --
4 the facilities, the whole management of the group or
5 subsidiary or division. Management of individuals and
6 the individual activities that those people partake in
7 is different.
8 Q. Can you give me an idea what kind of claim
9 in your judgment would be contemplated to be within
10 the management carveback for the management or
11 supervision of a division, subsidiary or a group?
12 MR. TOPOL: Objection.
13 THE WITNESS: Again you're asking for
14 me to hypothesize on a potential claim?
15 Q. (By Mr. Kolbo) I'm just trying to find out
16 from a claims perspective what -- you've concluded
17 what's not covered in this case and you've
18 distinguished it from another situation.
19 So I'm trying to find out what you would
20 give me as an example of the type of thing that would
21 be covered?
22 A. A shareholders' suit.
23 Q. Now you would agree with me the language of
24 the endorsement itself doesn't require that it be a
25 shareholder suit to be covered under the carveback?

1 A. Could be an employment claim as well.
2 Q. Could it also be a customer claim?
3 MR. TOPOL: Objection.
4 THE WITNESS: If it's in relation to a
5 particular transaction, no, I don't believe it could.
6 Q. (By Mr. Kolbo) And your opinion for that
7 is -- you would agree with me that the paragraph
8 doesn't say anything about excluding management or
9 supervision that may have something to do with
10 individual transactions, does it?
11 A. This is a D and O policy. It's not an E and
12 O policy. And an E and O policy is one that would
13 provide insurance for professional services.
14 The individual transactions that this
15 company provided were professional services. And I
16 did not -- I read this particular endorsement to carve
17 back or carve away the exclusion for traditional D and
18 O claims.
19 Q. But you say it's not an E and O policy but
20 it's a carveback to coverage under an E and O
21 exclusion, correct?
22 A. Management carveback.
23 Q. Well, in your judgment can a -- is it
24 conceivable for a customer to sue, make claim against
25 an officer and director for the management or

1 I don't know enough about the
2 securities laws or securities underwriting to that
3 type of business but there may be a claim that may be
4 excluded under endorsement No. 9 subsection 1 that's
5 not excluded by endorsement No. 3. There very well
6 could be.
7 Q. (By Mr. Kolbo) You didn't make any
8 determinations about that in considering coverage?
9 A. No.
10 MR. KOLBO: I think I'm going to pass
11 to Tom and look for these notes.
12 MR. ATMORE: Thanks.
13 CROSS EXAMINATION BY MR. ATMORE
14 Q. Let's look at Exhibit No. 3 on Page 3. The
15 entry for January 25, 2002.
16 A. Sure.
17 Q. Do you remember this conference call?
18 A. I vaguely or I remember being on a
19 conference call with Joel and Cheryl. I don't know if
20 it's this one.
21 Q. She says in the last line, Joel explained
22 that E and O exclusion not intended to carve back E
23 and O for supervisors semicolon doesn't make sense.
24 Do you remember discussion by her that it
25 didn't make sense.

1 A. I don't recall.
2 Q. You talked about remembering that you were
3 looking for Michael Watts or trying to find out if he
4 still worked for the company, right?
5 MR. TOPOL: Objection.
6 THE WITNESS: I remember that I knew
7 that he didn't work for the company. I don't remember
8 exactly how we got --
9 Q. (By Mr. Atmore) I think you said that you
10 were looking for him, trying to contact him. Am I
11 wrong about that?
12 A. No. That's what I was saying. I don't
13 remember how I found out that he wasn't there. I just
14 know I found out that he wasn't there.
15 Q. So you may or may not have been looking for
16 him but in any event, you found out he wasn't working
17 there anymore?
18 A. Yes.
19 Q. And then you said that you wanted to discuss
20 the policy with Joel Townsend, right?
21 A. Yes.
22 Q. Was that because you weren't sure how the
23 language should apply in the case you were reviewing?
24 A. Joel has particular expertise in financial
25 institutions and underwriting of the errors and

1 question?
2 A. The reason that I went to Joel was not
3 because I was uncertain. The reason that I went to
4 Joel was because of the potential severity of the
5 claim and I wanted to make sure that my coverage
6 decision was correct.
7 Q. Now, the designation in endorsement No. 9, E
8 and O E stands for errors and O stands for omissions,
9 correct?
10 A. Correct.
11 Q. And I think you said that to you E and O
12 means professional coverage. It refers to a type of
13 coverage.
14 Is that what you were saying?
15 A. Yes. For professional services.
16 Q. And then your testimony is that the words
17 errors and omissions in the wrongful act definition
18 means something else.
19 Is that what you're saying?
20 A. I believe that it's not limited to the
21 traditional view of E and O insurance being insurance
22 for professional services rendered.
23 Q. What's not limited to?
24 A. The term error and omission.
25 Q. It's broader than E and O?

1 A. I guess in answering that question it's
2 different.
3 Q. How is it different?
4 A. It could be the same.
5 Q. I think several times during your testimony
6 you referred to endorsement No. 9 and said how you
7 interpret that can be different, how people interpret
8 that can be different.
9 Do you remember testifying to that?
10 A. Yes.
11 Q. And I think you also said that the carveback
12 would not bring these, the underlying Heritage Bond
13 claims back into coverage because the supervision of
14 the individuals and the transaction itself related to
15 a specific bond issuance; is that right? Am I
16 understanding you correctly?
17 A. Could you say that again?
18 Q. The carveback doesn't bring coverage back in
19 I think you said was because the supervision at issue
20 here is of individuals and also in relation to a
21 specific bond sale, the Heritage Bonds, correct?
22 A. Correct.
23 Q. And so the basis for the denial is that you
24 believed that in these cases the supervision or
25 management was of an individual and/or only related to

1 the bond issues, correct?
2 A. Related to the bond issue.
3 Q. So how about the individual part?
4 A. The individual --
5 Q. Let's break it down. Let's suppose the
6 individual had sold more than Heritage Bonds, sold
7 Heritage Bonds and USA bonds and E bonds, whatever it
8 might be.
9 Would the carveback still not apply
10 because it's an individual?
11 A. With regard to the sale of those securities,
12 yes.
13 Q. So then is it fair to say that the basis for
14 the denial was that it was your belief that it was a
15 single person that was being supervised?
16 A. No.
17 Q. It's both?
18 A. Yes. It's both -- the sales were performed
19 by individuals meaning five people didn't sell a bond
20 to one person.
21 There may have been five different people
22 selling the bonds to different people but only one
23 person was doing the one transaction with whoever they
24 sold the bonds to.
25 So it is with regard to the bond

1 transactions and they were supervising the individuals
2 that were transacting those bond issues.
3 Q. Was it more than one individual?
4 A. I don't remember, to be honest with you.
5 Q. So then the real basis is that it was a
6 single type of bond, it was a Heritage Bond; is that
7 right?
8 A. It's with regard to a transaction selling
9 the Heritage Bonds.
10 Q. And you're aware that those transactions
11 occurred over time, different bond sales?
12 A. Yes. I haven't reviewed the complaint and I
13 don't remember the particular allegations from that.
14 Q. Is it your belief that the insured's
15 interpretation as expressed through the Hayes Group
16 and in this lawsuit is a completely unreasonable
17 interpretation as regards to this endorsement 9?
18 A. I would have no opinion as to regards to
19 their -- you mean -- I think that our position is the
20 correct position.
21 Q. Do you think that theirs is unreasonable?
22 MR. TOPOL: Objection.
23 THE WITNESS: I wouldn't fathom a guess
24 as to whether or not theirs is unreasonable.
25 Q. (By Mr. Atmore) So you can't say one way or

1 another; is that right?
2 A. I've never --
3 MR. TOPOL: Objection.
4 THE WITNESS: -- considered it. It's
5 not something I --
6 Q. (By Mr. Atmore) You didn't consider the
7 insured's interpretation?
8 A. No. I considered their interpretation and
9 determined whether or not our position was correct and
10 that was the determination that I came up with.
11 Whether or not it was reasonable or not was not
12 something I considered.
13 Q. And I think you said that in terms of
14 endorsement No. 9 and examples of things that might be
15 covered with the carveback would be a shareholder
16 derivative suit, correct?
17 A. I said a shareholder suit. It could be
18 derivative or direct.
19 Q. And an employment suit?
20 A. Sure.
21 Q. When you made your coverage determination,
22 did you look at other parts of the policy to see
23 whether shareholder suits might be covered elsewhere?
24 A. I don't think I understand the question.
25 Q. Did you read the whole policy when you made

1 the coverage determination?
2 A. Yes, I did.
3 Q. In doing so did you look -- do you remember
4 seeing whether or not shareholder suits are discussed
5 or covered elsewhere in the policy?
6 A. I don't recall.
7 Q. How about employment related suits?
8 A. I don't recall.
9 Q. Going back to your interpretation of
10 endorsement No. 9 and the issue of whether the claim
11 involves the sale of a particular security.
12 Is your interpretation true or do you
13 believe that there is no coverage even if the company
14 or the director or officer sued played no active role
15 in the sale of that security?
16 A. If the allegations are based upon a specific
17 sale, there is no coverage.
18 Q. Whether or not the officer, director or the
19 company sued -- you understand there is company
20 coverage in this policy, right? Entity coverage, do
21 you understand that?
22 A. There may be coverage under other certain
23 circumstances.
24 Q. Well, entity coverage is something that's
25 checked under the declarations page, do you understand

1 that?
2 A. I'll review it to make sure.
3 Q. Coverage B2?
4 A. Yes.
5 Q. So going back to the question. As long as a
6 specific security sale is involved in the underlying
7 claim, it doesn't matter whether or not the company
8 sued, there is still going to be no coverage, right?
9 A. For?
10 Q. For the claim?
11 A. Yes.
12 Q. And even if a director or officer is sued
13 solely because they are a director and officer and not
14 because of any role they may have played in the sale
15 of the security, there is still no coverage under your
16 interpretation, correct?
17 A. For specific bond transactions, correct.
18 Q. Okay. Let's look at the definition of
19 wrongful act. Paragraph 1, insuring agreements and
20 sub M is on Page 3 of mine. I don't know what page
21 you have.
22 Paragraph 3 says that wrongful act means
23 any matter asserted against an insured person solely
24 by reason of his or her status as director or officer
25 of the company.

1 Do you see that?
2 A. In subsection 1? Oh, down here.
3 Q. M3?
4 A. Yes.
5 Q. How is that consistent with your
6 interpretation that there doesn't need to be any
7 involvement by the director or officer in the
8 underlying transaction that's the subject of the suit?
9 A. I'm sorry, I don't understand what you're
10 asking.
11 Q. Well, this says a wrongful act means any
12 matter asserted against an insured person solely by
13 reason of his or her status as a director or officer
14 of the company, right?
15 A. Right.
16 Q. So a wrongful act is whether or not they had
17 anything to do with the underlying transaction, right?
18 A. Right.
19 Q. Solely by reason of his or her status?
20 A. Yes.
21 Q. How is it consistent -- how is that
22 definition consistent with your interpretation that
23 the officer or director needs to have no involvement
24 for the carveback -- under the carveback?
25 A. I guess I misunderstood you before because I

1 think you were asserting a hypothetical that's not
2 this particular case.
3 Q. No, I'm not.
4 A. Because the ones that I remember reviewing
5 and my basis for the coverage decision, was that they
6 allegedly were responsible for the bond sale and
7 transactions in their capacity as a director or
8 officer.
9 Q. All right. So clarify your testimony for me
10 then.
11 If the allegations are that the
12 particular officer or director is not involved, does
13 the carveback provide coverage or not?
14 MR. TOPOL: Objection.
15 THE WITNESS: Not involved. I don't --
16 that word involved is not -- responsible for is the
17 word I would use.
18 Q. (By Mr. Atmore) Responsible for meaning
19 what?
20 A. Responsible for the bond sale.
21 Q. Okay. So you're interpretation is that the
22 carveback will not provide coverage if the officer or
23 director who is sued is responsible for the bond
24 sales?
25 A. Responsible for the liability occurring from

1 whatever wrongful act that occurred with regard to the
2 sales.
3 Q. Responsible -- let me see if I understand
4 that.
5 Responsible for the liability that
6 occurred as a result of the underlying sales?
7 A. Yes.
8 Q. What do you mean by responsible for the
9 liability that is incurred?
10 A. Liable. That they could be held liable for
11 -- I don't remember what the actual causes of action
12 were. I can explain to you what I think paragraph 3
13 means.
14 Q. Well, I want -- first I want to go with what
15 you already testified to and see if I understand it.
16 And that is that if they're responsible
17 for the liability of the underlying sales, the
18 question I have is what would the basis of liability
19 have to be for them to be responsible?
20 A. Again, I don't remember what the causes of
21 action were.
22 Q. Are you using the word responsible for
23 different from the idea of involvement in the sale?
24 A. Again, I don't remember what the causes of
25 action are.

1 Q. I'm just asking you about your testimony
2 that you've already given. You need to understand the
3 underlying causes of action?
4 A. Involvement -- the definition of those
5 particular words.
6 Q. Which words?
7 A. Involvement and responsible.
8 Q. Um-hm. Are they in the policy, by the way?
9 A. Not that I recall.
10 Q. So when you say the definition you mean --
11 A. It could be. I mean just a general -- your
12 definition, my definition, whoever, I can't answer
13 that question.
14 It depends on the situation that's put in
15 front of me. The difference between the two words if
16 you're trying to figure out what my definition is
17 between the two of them, I can't answer that question.
18 Q. Okay. But your understanding was that every
19 claim you looked at the directors and officers sued
20 had some involvement in the sales; is that --
21 A. A potential for liability for. How is that?
22 Q. I'm not very good with -- what does that
23 mean? What does that mean to you?
24 A. That they could be held responsible at the
25 end of the day for the bond sales for any act, error,

1 problem with regard to the specific transactions that
2 have been the subject of this litigation.
3 Q. And that would be regardless of whether they
4 had any involvement in those transactions; is that
5 right? Is that your testimony?
6 A. I don't like using that word. I'm not
7 comfortable with that statement.
8 Q. The word involvement?
9 A. Regardless of their involvement. I don't
10 know if it requires them to be involved to be
11 responsible. I'm not comfortable with answering yes
12 or no to that question.
13 MR. ATMORE: That's all I have.
14 REDIRECT EXAMINATION BY MR. KOLBO
15 Q. I want to follow-up. There is a marked
16 exhibit. I want to ask you about Exhibit 2.
17 A. My Exhibit No. 2?
18 Q. No. This is from the earlier deposition,
19 Ms. McKelvey. Take a look at this document and see if
20 this is your claim notes?
21 MR. ATMORE: What is it, two?
22 MR. KOLBO: From the earlier
23 deposition.
24 Q. (By Mr. Kolbo) Do you recognize it as such?
25 A. Yes.

EXHIBIT R

#46121

11/30/01: Attempted to make 24 hour contact. Left vm with Broker to get Insured contact.

Later: T/C with Bryan Huft, the broker. The contact is Ken Larson at 612-376-1310. Left vm with Mr. Larson.

Insured: Miller & Schroeder Inc.
Claimant: Mr. and Mrs. Spanglor
Claim #: 46121

Policy Information:
Old Power # 8166-6027
LOL: $5M
Ret: $50K for individuals and $100K for the Company
Pertinent Endorsements: No 9, General E&O Exclusion with Management Carveback; No. 1, Minnesota Amendatory Endorsement, Excluding punitive damages.

NASD Arbitration to be venued in San Diego, CA

Loss Description: Unsuitability of investment.

Facts: Frank and Joanne Spanglor invested money through Miller & Schroeder. They complain that Jeffrey Hill was a financial consultant for the Spanglors and an employee of M&S. James Dlugosch is named as the M&S CEO and a control person. The Spanglor's allege that Hill, Dlugosch and M&S are responsible for them investing in a bond that was unsuitable for their investment needs. The allegations are fraud, negligence, fraudulent misrepresentation and omission and breach of fiduciary duty. The Spanglors have brought an NASD arbitration claim against the defendants. The plaintiffs are seeking compensatory damages in the amount of $50,000, punitives, interest, costs and attorney's fees.

Coverage issues:
The E&O exclusion precludes coverage for Hill and M&S. There is a management carveback that would at least possibly trigger the duty to defend for Dlugosch.

The broadform securities exclusion appears to be at issue.

Fraud
Punitive damages
Capacity issue with regard to the management or supervision of Mr. Spanglor.

Duty to Defend: The broker indicated that M&S has typically used Dorsey & Whitney as counsel in Milwuakee. They are not on panel counsel. We do not have any NASD attorney's in Milwaukee. We have one in Chicago with Seyfarth Shaw. If we consent to use the same attorney for all defendants, we should allocate defense expenses. CLC

12/6/01: Left vm with Ken Larson again. CLC

Later: T/C with Ken Larson. Explained our coverage position. They are preparing to file bankruptcy in the next few weeks and have not been defending anything. He said that I need to speak with David Reinhardt at 612-376-1354, one of the principles in the Insured regarding the status. He is going to call him and he said that either David or Ken will call me back today. I stated that we would be appointing defense counsel for Mr. Dlugosch. Got a recommendation from Mai of Steven Wasserman of Sedgwick Detert Moran and Arnold. CLC

12/10/01: Left vm with David Reinhardt. CLC

12/11/01: Dave called and left vm. I left another vm. CLC

12/12/01: Left vm with Dave again. CLC

12/17/01: Called Dave again and the phone rang continuously. Left vm with Ken Larson. CLC

12/18/01: Left vm with Dave again. Called Brian Huft and told him that I was having a problem getting a hold of the Insured and need the contact information for Dlugosch. He will get back with me tomorrow. CLC

12/19/01: Left vm with Dave again. T/C with Dave. The attorney on the matter is Linzie Arthur 612-339-3500. He is going to email him that I am going to call. There are several claims that have recently been submitted. Dave is going to send me a matrix outlining the outstanding claims. Called Keith Doan in Chicago Bkrg to let him know that this account could hit fairly hard. Sent email to all of the other claims examiners to discuss the nature of the other claims. CLC

The following notes have been made in the anticipation of potential litigation.

Later: It has been brought to my attention that there is a broad form securities endorsement that appears to preclude coverage for this matter. I am calling the underwriters to discuss intent between the securities exclusion and the E&O exclusion with a management carveback. CLC

12/27/01: T/C with Greg Barabas about the potentially inconsistant endorsements. He stated that I should talk with Cabot Wigger in the Chicago office. Sent him the information. HE will be out until 1/7/02/ Called Kevin Pyne in the Chicago Retail office and left vm. Keith Doan is the DFI Practice Leader. Allison Rose from the Western Zone appears to have a related Heritage Bond case. She has taken the position that the Securities exclusion precludes coverage. However it appears that it might be inconsistent with the management carveback in the E&O Exclusion. Greg also suggested that I get Joel Townsend involved in this matter. Sent email to discuss with Joel. Sent letter to the Insured stating that we are continuing to investigate our coverage position. CLC

1/2/02: T/C with Joel Townsend. After the discussion with Joel, it appears that this matter should be excluded. The E&O exclusion would apply. There is no allegation of a failure to supervise that would bring the E&O carveback into play. The general securities exclusion would appear to apply to disclaim any coverage even if there were a failure to supervise allegation.

Will try to set up conference call to discuss with all of the claims examiners throughout the country. CLC

1/4/01: Attended a conference call with Joel Townsend, Dannielle Francis, Allison Rose and Cheryl O'Malley. Agreed that I would handle all of the claims so that there is coordination. Agreed also that these matters should be denied. CLC

1/14/01: T/C with Ken Larsen at the Insured and explained the coverage position. He seemed to understand it. I sent the following email to confirm receipt of a bunch of similar claims.

Mr. Huft, Mr. Larsen and Mr. Arthur,

I have received several of the actions filed recently against Miller & Schroeder and wanted to acknowledge the receipt of them in a consolidated fashion. We understand that these matters have been submitted for coverage under Executive Risk Indemnity Inc. ("ERII") policy #8166-6027 (the "Policy"). This email is not intended to indicate that there is coverage for any of the following matters under the Policy. ERII expressly reserves all rights under the Policy terms and conditions as well as any applicable law. We are currently conducting an investigation with regard to coverage, but expect to deliver coverage letters as soon as possible.

I have the following matters assigned to my attention:

Hermann, et al v. Miller & Schroeder Financial Inc., et al - NASD Arbitration Reference No. 46559
Hermann, et al v. Miller & Schroeder Financial Inc., et al - Class Action CA state court 46559
Spanglor, et al v. Miller & Schroeder Financial Inc., et al - NASD Arbitration 46121
Moreland v. Miller & Schroeder Financial Inc., et al 45979
Onderwyzer et al v. Miller & Schroeder Financial Inc., et al - NASD Arbitration 47195
Salley et al v. Miller & Schroeder Financial Inc., et al - NASD Arbitration 47196
Formica et al v. Miller & Schroeder Financial Inc., et al - NASD Arbitration 47197
Hyde et al v. Miller & Schroeder Financial Inc., et al - NASD Arbitration 47198
Johansen et al v. Miller & Schroeder Financial Inc., et al - NASD Arbitration 47199
Cates et al v. Miller & Schroeder Financial Inc., et al - NASD Arbitration 47200
McGuire, et al v. Miller & Schroeder Financial Inc., et al - NASD Arbitration 47201
Timmerman et al v. Miller & Schroeder Financial Inc., et al - NASD Arbitration 47203
Baker Living Trust et al v. Miller & Schroeder Financial Inc. et al - NASD Arbitration 47204

We have two other actions open in our system. We understand that the Behnke matter, Reference No. 45978, which is assigned to Ruthann Rozenek, settled below the retention on the Policy. The other matter, Bremer Business Finance Corp., Reference No. 44840, is continuing to be handled by Cheryl O'malley in our Pittsburgh office.

If you have any questions, please feel free to contact me.

Carrie L. Campi, Esq.
Claims Examiner
Chubb Specialty Insurance
82 Hopmeadow St.
Simsbury, CT 06070
Direct dial (860)408-2733
Fax (860) 408-2851

Email ccampi@chubb.com

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***Investigation**

02/08/2002: CLC Drafted coverage letter for Moreland action, another claim against Miller & Schroeder with similar allegations. Joel Townsend reviewed letter denying coverage. Told broker, Bryan Huft of our coverage position. Ken Larsen is no longer with M&S, he is now with Marshall Miller and Schroeder (MM&S). KEn said that Dave Reinhardt is the only one still affiliated with M&S, which is now in bankruptcy proceedings, Chapter 7. No trustee has been appointed as yet.

Sent denial letter. Calendaring ahead for closure.

***Settlement/Resolution**

08/15/2002: CLC Closing claim as denial has not been further disputed.

***Administrative**

06/14/2004: DBS Returned file to archives.

EXHIBIT S

LMTCB

RR

12/19/01

Rcv'd return t/c from Rich Gluck confirming $15k settlement on behalf of Miller & Schroeder. Requested copies of the settlement docs be faxed.

RR

1/2/02

Ruthanne Rozenek

01/02/02 03:33 PM

To: Carrie L Campi/ChubbMail@ChubbMail
cc: Allison Rose/ChubbMail@ChubbMail, Cheryl N O'malley/Chub
Margaret M Klimczyk/ChubbMail@ChubbMail
Subject: Re: Miller

Carrie:

As my claim didn't involve Heritage Bonds and has been resolved by the insured within their deductible I won't participate in any further conference calls.

Ruthanne

Carrie L Campi

12/28/01 12:39 PM

To: Allison Rose/ChubbMail@ChubbMail
cc: Cheryl N O'malley/ChubbMail@ChubbMail, Margaret M Klimczyk/ChubbM
Ruthanne Rozenek/ChubbMail@ChubbMail
Subject: Re: Miller

I spoke with Joel Townsend today about the Miller & Schroeder matters relating to the Heritage Bonds. He stated that the intention behind the E&O endorsement carveback was to allow claims for mismanagement as made by shareholders not clients. He feels comfortable denying the actions under the two endorsements. He said that it is not his call as to whether we consolidate the claims in one location or not, but thought that we should have similar coverage letters. Hopefully we can set up a conference call when everyone returns from the holiday.

Happy New Year

Carrie L. Campi
Claims Examiner

EXHIBIT T

1 like that.
2 Does that sound agreeable?
3 A. That's fine.
4 Q. And if I ask a question that you don't
5 understand, if I don't state it clearly or for
6 whatever reason you don't understand my question,
7 would you let me know so I can try to rephrase it so
8 we can make sure we're communicating on the same wave
9 length?
10 A. Yes.
11 Q. And lastly, you do understand that you're
12 testifying here today under oath and you have the same
13 obligations to tell the truth as if you were
14 testifying in a courtroom?
15 A. I understand.
16 Q. What is your position, your current
17 position?
18 A. Claims examiner.
19 Q. You're employed by Executive Risk?
20 A. Chubb Insurance.
21 Q. Chubb Insurance. Okay. Chubb Insurance
22 owns Executive Risk? What's the relationship as far
23 as you know?
24 A. It's Chubb Group of insurance companies. As
25 I understand it Chubb acquired Executive Risk a few

1 Hartford, Connecticut.
2 Q. So you're a lawyer?
3 A. Yes.
4 Q. How long were you employed by that firm?
5 A. Probably all total three years.
6 Q. What years are those approximately?
7 A. '92 to '94 and then again in '95, '96.
8 Q. Same firm both times?
9 A. Well, let me just start at the beginning. I
10 graduated from law school in '91. Went to work for a
11 law firm in town, Murtha Cullina. Worked for them
12 from '92 to '94.
13 Left them and went to Reid and Riege,
14 another law firm in town, in Hartford. I worked for
15 them for two years and then took some time off and
16 then went back to work for Murtha for a six or
17 eight-month period.
18 Then I went back to school for sport
19 management and got my Master's which led to the
20 University of Hartford job.
21 Q. Where did you get your Master's?
22 A. University of Massachusetts.
23 Q. Did you say where you got your JD from?
24 A. I did not. Got it from the University of
25 Connecticut.

1 well, let me strike that.
2 I think you mentioned you play some
3 independent role even if you've taken on a
4 reassignment of a claim that somebody else originally
5 examined, you'll provide some independent review of
6 those claims; is that correct?
7 A. Yes.
8 Q. Can you tell me what -- in a general
9 fashion, what you recall doing with respect to your
10 examination of the claims that were transferred from
11 Carrie Campi to you?
12 A. I would have reviewed all the contents of
13 the file. And I would have reviewed the -- I don't
14 recall reviewing all of the complaints because there
15 were a number of them.
16 And in talking to her she said that they
17 were -- I believe she informed me that they were
18 pretty much all similar.
19 But I was transferred all the complaints
20 that had been filed, looked through those, looked at
21 the coverage letter, looked at the policy. Didn't see
22 anything she had done wrong. And then when new
23 submissions came in, then, of course, you have the
24 role of reviewing those as well.
25 MR. KOLBO: Mark this one, please.

1 THE WITNESS: I think that's a broad
2 reading that's not accurate.
3 Q. (By Mr. Kolbo) In what respect?
4 A. I don't think it covers -- the idea is to
5 exclude coverage for E and O claims. And if a -- if
6 there is an E and O claim, just because you happen to
7 be a manager of a division I don't think that that
8 necessarily extends coverage.
9 Q. No but if the claim is in connection with
10 the management or supervision of a division providing
11 the services specifically identified above, isn't that
12 precisely what coverage is intended to be provided for
13 here?
14 A. No.
15 Q. Well, the carveback does apply, does it not,
16 that there is going to be some coverage for some types
17 of E and O claims?
18 MR. TOPOL: Objection.
19 THE WITNESS: No.
20 Q. (By Mr. Kolbo) How is it a carveback if
21 it's not creating some coverage for some types of E
22 and O claims putting aside what those are, how can it
23 be a carveback?
24 A. It's a carveback for management under D and
25 O activities. It doesn't provide E and O coverage.

1 The idea of this endorsement is to exclude E and O
2 coverage but because it's an investment brokerage
3 house, anything they do could conceivably be excluded
4 under E and O. We wanted to make it very clear that if
5 you're sued in your D and O capacity for a management
6 type activity unrelated to the E and O things, such as
7 employment practices or something along those lines,
8 then that's where there is intended coverage.
9 Q. Well, how about if a director or officer is
10 sued in his capacity, purely in his capacity as a
11 director and officer for matters relating to the
12 rendering or the failure to render of securities
13 broker dealer services, is that not covered by the
14 carveback?
15 MR. TOPOL: Objection.
16 THE WITNESS: No, I don't think it is.
17 Q. (By Mr. Kolbo) And the reason is?
18 A. Because this carveback does not provide E
19 and O coverage. This is an E and O exclusion and if
20 the entity is providing investment banking services
21 and that's the basis for the claim and why he's being
22 sued, then no, there is no coverage.
23 Q. Even though there is a carveback in the
24 policy?
25 A. I don't believe you're reading the carveback

1 correctly.
2 Q. Well, we agree there is a carveback?
3 A. Yes, there is.
4 Q. There is a carveback for -- you disagree
5 with my suggestion that the carveback carves back in
6 coverage for certain types of E and O claims?
7 A. It carves back coverage for management type
8 claims but not for E and O claims. This is an E and O
9 exclusion.
10 Q. I guess what I'd like to find out is how are
11 you defining the difference between a management type
12 claim and an E and O claim?
13 A. If you are sued -- if you -- one of the
14 defense was an insured person had been sued as an
15 insured person for cooking the books or maybe some
16 employment type thing where they are acting as a
17 director and officer, that would be covered.
18 But if there is a sale of securities and
19 that's the basis of the claim or an underwriting of
20 securities and that's the basis of the claim, then I
21 don't believe that as a manager that they're covered.
22 Q. All right. Just so I can be clear. Is it
23 your position -- and the reason that you say that
24 provisions -- that coverage relating to security
25 services are excluded is because of paragraph 1?

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1 allegations arising out of the underwriting of
2 securities? Is that something that is contemplated?
3 MR. TOPOL: Objection.
4 THE WITNESS: Can they be sued for
5 that?
6 Q. (By Mr. Kolbo) Yes.
7 A. Yes.
8 Q. It's your position that that kind of suit
9 would be not covered because of endorsement No. 9?
10 A. It definitely could be excluded by
11 endorsement No. 9.
12 Q. In your opinion, does it matter whether the
13 officer or director is directly engaged in the
14 underwriting of services for which he's sued?
15 Does that make a difference whether
16 endorsement No. 9 applies or not?
17 A. No.
18 Q. If an officer and director is sued in his
19 capacity as an officer and director for failure to
20 properly manage and supervise an office in connection
21 with that office's issuing of securities services,
22 does that type of an allegation -- is that allegation
23 of the kind that would be brought within coverage by
24 the carveback?
25 A. No.

1 MR. TOPOL: Objection.
2 Q. (By Mr. Kolbo) And the reason is what?
3 A. They're being sued in their capacity as an
4 insured person regarding the underwriting of
5 securities which is an excluded provision. And
6 because it's -- it's not with respect to the
7 management of the company, it's the management of
8 those securities.
9 Q. But let me ask you this. If the claim is
10 that the officers and directors failed to properly
11 manage and supervise an office or group or division of
12 the company in the issuance -- by that office or
13 division or group of the company in the issuance of
14 securities, why would that not be contemplated and
15 within the coverage of the management carveback.
16 MR. TOPOL: Objection.
17 THE WITNESS: Because that's an E and O
18 type issue where you're issuing securities and that
19 all ties with the issuing of securities. If this
20 was -- you mismanaged the office and discriminated
21 against employees, then that's the sort of claim that
22 would be covered.
23 Q. (By Mr. Kolbo) Where does it draw that
24 distinction in paragraph 2 between say an employment
25 related claim against a director and officer and a

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1 claim for the management or supervision of an office
2 in the issuance of the securities, what language are
3 you relying upon in paragraph No. 2?
4 A. I'm relying upon the wording of the entire
5 paragraph. Is there a specific provision that says
6 employment claims are covered and securities types are
7 not? No, it doesn't specifically say that in there.
8 But based upon paragraph 1 which excludes
9 coverage for these sorts of activities and paragraph 2
10 saying okay, but we're going to go ahead and cover you
11 for the management of the division, not the management
12 of the sale of securities.
13 Q. Paragraph No. 1, the exclusion with respect
14 to E and O activities is limited to the services
15 identified there, correct? Those three line items;
16 investment banking services, security broker dealer
17 services, securities underwriting services, correct?
18 A. I'm sorry, it's limited to the --
19 Q. The exclusion in paragraph No. 1 does not
20 even purport to exclude E and O coverage for claims
21 other than those services specifically identified in
22 paragraph 1, correct?
23 A. Correct. It enumerates certain services,
24 yes.
25 Q. So paragraph -- there would be no point in

1 general the question you're asking, it is correct it
2 would not normally be -- employment claims would not
3 normally be excluded by paragraph 1. I don't want to
4 make a blanket statement because there is always an
5 exception out there but in general you're correct.
6 Q. I understand that. So there would be no
7 point in a carveback, for example, carving back in
8 coverage for employment related claims against
9 directors and officers because paragraph 1 doesn't as
10 a general proposition exclude those claims, correct?
11 A. Generally speaking, no.
12 Q. So the only point of the carveback it seems
13 to me, if it had a point, is to carve back into
14 coverage those things that are excluded by paragraph
15 No. 1?
16 A. I disagree.
17 Q. What other purpose would it have?
18 A. To re -- well, I think I've stated this but
19 it's -- my reading of this endorsement is that the
20 purpose is to make clear that we're still going to
21 cover management for the supervision of the division,
22 subsidiary or group that offers those services.
23 And it could be -- could come up that
24 you'd automatically exclude claims just by virtue of
25 the fact that they offer those services.

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1 to draw there?
2 Is it your suggestion that the officers
3 and directors of Miller and Schroeder are not being
4 sued for how they managed or supervised any office or
5 group or division of the company?
6 A. Well, I don't think that that's exactly
7 right given that there are certainly allegations for
8 management of the group.
9 The issue here is more that all of these
10 allegations are tied to one of these three services.
11 And so while we're saying, as I think I said earlier,
12 that there is -- they're not being sued for how they
13 managed the company meaning that no one was cooking
14 the books or anything like that, they were being sued
15 because of the impropriety of these securities and
16 that is specifically what's being excluded by
17 endorsement No. 9.
18 Q. So that ties back to what we were talking
19 about earlier.
20 Your conclusion was as long as these
21 officers and directors were being sued for anything
22 arising out of the three services that are identified
23 in endorsement No. 9, coverage is excluded regardless
24 of the management carveback?
25 MR. TOPOL: Objection.

1 THE WITNESS: If -- that was the basis
2 in this case. Those were the allegations. Yes, that
3 fell squarely within the services that were -- the
4 rendering or failure to render those services. So it
5 fell squarely within that.
6 It wasn't overall management of the
7 company like an employment type claim or something
8 like that.
9 It was -- you had improper securities
10 and so that's not what the carveback was designed to
11 cover.
12 Q. (By Mr. Kolbo) Your coverage wasn't based
13 on any understanding or premise that the officers and
14 directors were themselves being sued for their direct
15 issuance of the securities, for example?
16 A. I don't recall all the allegations of the
17 complaint. But I don't believe that the directors or
18 officers were ever alleged to have individually sold
19 the securities. That was not the analysis.
20 Q. Your understanding that allegations against
21 the officers and directors were that they had some
22 management or supervisory responsibilities for those
23 individuals who did issue the securities at issue?
24 MR. TOPOL: Objection.
25 THE WITNESS: Correct.

1 subparagraph 2 as not to refer to E and O type
2 situations when the definition of wrongful act
3 includes the words error, omission? What's your
4 reasoning?
5 A. Because the policy is designed to give D and
6 O coverage and it does cover an error or an omission
7 in a D and O capacity.
8 It's not designed to include coverage for
9 claims -- excuse me, resulting from regular -- what
10 would generally be covered under an E and O policy.
11 Just because we have an errors and
12 omission exclusion, that doesn't mean that we exclude
13 all errors. An individual can make an error in his
14 capacity as a manager of the company, in his D and O
15 capacity, you know, erroneously instituting an
16 employment policy that discriminates against people.
17 We would cover that. That would be an
18 error but we would cover it.
19 Q. So employment practices is included in the
20 definition of wrongful act?
21 A. Yeah.
22 Q. Can you turn to the prior page, subparagraph
23 E. Refers and defines employment practice as wrongful
24 act. Do you see that?
25 A. Yes.

1 Q. What was your analysis?
2 A. Well, the analysis was that a wrongful act
3 had occurred and that this matter constituted a claim
4 but that it was excluded from coverage by exclusions
5 -- endorsements 3 and 9.
6 Q. Specifically did you consider the definition
7 in M3? Do you remember considering that definition
8 when considering whether or not sub 2 applied under
9 endorsement No. 9?
10 A. I don't recall.
11 Q. And in considering whether endorsement No. 9
12 and the carveback applied, I think you said in some
13 letters that -- and you said today in your testimony
14 that one of the things that might cover or might allow
15 coverage for would be a shareholder derivative suit
16 against an officer or director related to necessarily
17 the sale of a particular security?
18 A. That might be, yes.
19 Q. Could you turn to Page 6 of the policy?
20 Actually we have started at four. This is section 3
21 exclusions.
22 Do you see that up at the top of Page 4?
23 A. Yes.
24 Q. Then turning to Page 6 we get to
25 subparagraph E under section 3?

1 A. E3.
2 Q. Subparagraph E under section 3, so 3E is the
3 way it would be read.
4 A. Right. 3E3 is on Page 6. Is that what
5 you're looking at?
6 Q. No. I'm looking at 3E, sub 3 of E. Just 3E.
7 MR. TOPOL: I think you're on different
8 pages but your exclusion 3E.
9 Q. (By Mr. Atmore) And the copy you have might
10 be on a different page. Okay.
11 And this E says any claim -- first of
12 all, on what is my Page 4 it begins, this policy does
13 not apply to and E says, any claim by or on behalf of
14 or in the name or right of, the company or any insured
15 person except that this exclusion E will not apply to
16 and then sub 1 is any derivative action by a security
17 holder of the company on behalf of or in name or right
18 of the company if such action is brought independently
19 of and without the solicitation, assistance,
20 participation or intervention of the company or any
21 insured person.
22 Do you see that?
23 A. Yes.
24 Q. In considering whether endorsement No. 9 and
25 the carveback applied, do you remember reading this

1 exclusion E and the exception to the exclusion?
2 A. I'm sure I read all the exclusions.
3 Q. Do you remember specifically reading this
4 one?
5 A. Do I remember reading it?
6 Q. Yes.
7 A. Not other than a general recollection.
8 Q. Okay. Do you know what state law governs
9 this policy?
10 A. No, I do not.
11 Q. In making the coverage decisions that you
12 made in this case, did you refer to any law?
13 A. In making the coverage determinations?
14 Q. Yes.
15 A. No. But I did refer to certain cases in one
16 of my letters.
17 Q. Do you know if those cases are Minnesota
18 cases?
19 A. I don't recall. I could look back. I don't
20 recall.
21 Q. I think you said earlier that your
22 supervisor might review your coverage letters?
23 A. Yes.
24 Q. By coverage letter you mean coverage or
25 denial or the opinion on coverage, right?

1 A. Correct.
2 Q. But I think you also said that Joel Townsend
3 was not your supervisor?
4 A. Correct.
5 Q. Why is he reviewing your letters?
6 A. Because he had worked with Carrie on this
7 matter. And he was familiar with the issues and
8 because she had already gone to him, then it would
9 make sense for me to approach him about these issues
10 again.
11 Q. Who is your supervisor?
12 A. Richard Falcigno.
13 Q. I think earlier you testified as to the
14 intent of endorsement No. 9 and the carveback.
15 And I think you referenced that you might
16 discuss with the underwriter what the intent was,
17 right?
18 A. I might, yes.
19 Q. And it's true that the underwriter who was
20 involved in creating endorsement No. 9 did not work at
21 Executive Risk or the Chubb Group after -- even before
22 you took over handling the file, correct?
23 A. I don't -- that's my understanding, yes.
24 Q. So did you ever contact the underwriter who
25 was involved to discuss the intent of endorsement

1 No. 9?
2 A. No, I did not.
3 Q. Did you contact any underwriter to discuss
4 the intent of endorsement No. 9?
5 A. I did not.
6 Q. And I think you stated earlier in your
7 testimony that the intention behind sub 2 of
8 endorsement No. 9 was to make it very clear that there
9 isn't E and O coverage but there is carveback for
10 claims that don't arise out of the services listed?
11 Was that your testimony?
12 MR. TOPOL: Can you read back the
13 question, please.
14 (Reporter read back as requested.)
15 MR. TOPOL: Objection.
16 THE WITNESS: I believe that the
17 interpretation that's been put on this and our reading
18 of it is that there is no E and O coverage but there
19 are other -- there is coverage for other D and O
20 actions by companies that are in these -- that provide
21 these businesses, yes.
22 Q. (By Mr. Atmore) My question was intended to
23 highlight the word "intent". And I believe you said
24 before that this was -- you referred to the intent of
25 this endorsement No. 9.

1 My question is what is the basis for you
2 knowing what the intent was?
3 A. I don't have a basis. I think I said, I
4 believe the intent was, but other than reading the
5 language of it and talking to Joel and Carrie, that
6 was -- we went on the language.
7 We did not consult the underwriter to
8 determine the intent.
9 Q. Will you look at Exhibit 4, please, and
10 Page 3 and the last full paragraph on Page 3.
11 And I think you said before that it was
12 not -- you were not denying coverage based on, and I
13 think reference was made to Exhibit 5 where you were
14 talking about whether or not Miller and Schroeder
15 decided not to buy E and O coverage, that you weren't
16 intending to deny coverage solely on the basis that
17 they didn't purchase E and O coverage, correct?
18 A. Correct.
19 Q. You state in this last -- last sentence of
20 this paragraph had Miller and Schroeder wished to
21 obtain E and O coverage for this type of action,
22 Miller and Schroeder could have sought such coverage.
23 However, Miller and Schroeder chose not to and cannot
24 now claim E and O coverage under its D and O policy.
25 So just to clarify, is it your testimony

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

In re:

SRC Holdings Corporation,
f/k/a Miller & Schroeder, Inc.
and its subsidiaries

Debtor.

Chapter 7 Case

BKY Case Nos. 02-40284 to 02-40286

Jointly Administered

Brian F. Leonard, Trustee,

Plaintiff,

v.

Executive Risk Indemnity, Inc.

Defendant.

ADV Case No. 03-4284

The Marshall Group, Inc., Jerome A. Tabolich, James E. Iverson, Edward J. Hentges, Kenneth R. Larsen, Steven W. Erickson, Paul R. Ekholm, and Mary Jo Brenden,

Intervenors.

UNSWORN CERTIFICATE OF SERVICE

I, Lynn Fischer, declare under penalty of perjury that on the 29th day of October, 2004, I mailed and faxed a copy of the annexed ***Notice of Motion and Motion; Plaintiff's Memorandum in Support of Motion for Partial Summary Judgment; Affidavit of Thoams C. Atmore in Support of a Partial Summary Judgment Motion;*** **and** ***Order*** on

VIA FACSIMILE (202-719-7049)
AND U.S. MAIL

David H. Topol, Esq.
Wiley, Rein & Fielding, LLP
1775 K Street NW
Washington, DC 20006

VIA FACSIMILE (651-297-6226)
AND U.S. MAIL

Klay C. Ahrens, Esq.
Johnson, Provo-Petersen, LLP
332 Minnesota Street
Suite W-975
St. Paul, MN 55101

VIA FACSIMILE (612-642-8327)
AND U.S. MAIL

Kirk O. Kolbo, Esq.
Maslon Edelman Borman & Brand, LLP
3300 Wells Fargo Center
90 South 7th Street
Minneapolis, MN 55402

by mailing and faxing to all parties copies thereof, enclosed in an envelope, postage prepaid, and by depositing the same in the post office at Minneapolis, Minnesota, directed to said parties at the last known addresses of said parties.

Dated: October 29, 2004

Lynn Fischer

Lynn Fischer
100 South Fifth Street, Suite 2500
Minneapolis, MN 55402
(612) 332-1030

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UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

In re: Chapter 7 Case

SRC Holdings Corporation, BKY Case Nos. 02-40284 to 02-40286
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Intervenors.

ORDER

The above-captioned matter came before the Honorable Nancy C. Dreher, Judge of the United States District Court for the District of Minnesota on December 16, 2004. Thomas C. Atmore, Esq, appeared on behalf of Plaintiff Brian F. Leonard, as Trustee. Other appearances were noted on the record.

Based upon the files and records filed in this matter, the arguments of counsel, and after due consideration of the same,

IT IS ORDERED:

1. Plaintiff's motion for partial summary judgment is hereby granted.

LET JUDGMENT BE ENTERED ACCORDINGLY.

BY THE COURT:

Dated: _____, 2004

_____
The Honorable Nancy C. Dreher
United States Bankruptcy Judge

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