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6 Proposed Attorneys for Western Asbestos
Settlement Trust and the Inchoate Trust
7

8 **UNITED STATES BANKRUPTCY COURT**
9 **NORTHERN DISTRICT OF CALIFORNIA**
10 **OAKLAND DIVISION**

11 In re:
12 WESTERN ASBESTOS COMPANY,
13 WESTERN MACARTHUR CO., and
14 MACARTHUR CO.,
15 Debtors.

Case No. 02-46284-T thru 02-46286-T
Jointly Administered under 02-46284-T

Chapter 11

**FIRST ANNUAL REPORT AND
ACCOUNTING OF WESTERN
ASBESTOS SETTLEMENT TRUST**

Date: May 16, 2005
Time: 2:00 p.m.
Place: 1300 Clay Street, Room 300
Oakland, CA 94604

16 Western Asbestos Settlement Trust by and through its counsel, Janet L. Chubb, Esq., of
17 Jones Vargas, hereby files its First Annual Report and Accounting, which is attached.
18

19 DATED this 22nd day of April, 2005.
20

21 JONES VARGAS
22

23 By: //s// Janet L. Chubb
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Western Asbestos Settlement Trust

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**FIRST ANNUAL REPORT AND ACCOUNTING
OF WESTERN ASBESTOS SETTLEMENT TRUST**

The Trustees of the Western Asbestos Settlement Trust (“Trust”) hereby submit this First Annual Report and Accounting (“Annual Report”) covering Trust activities occurring during the period from commencement of the Trust on April 22, 2004 to and including December 31, 2004 (“Accounting Period”). The Annual Report also covers certain activities of the Trust, specified below, that took place outside the Accounting Period. This Report and Accounting is submitted to the U.S. Bankruptcy Court for the Northern District of California, Oakland Division, *In Re Western Asbestos Company, Western MacArthur Co., and MacArthur Co.*, Case no. 02-46284-T through 02-46286-T, Jointly Administered Under No. 02-46284 T, in accordance with the Second Amended Joint Plan of Reorganization (“Plan”),¹ and pursuant to the laws of the state of Nevada, where the Trust is organized and where it resides. The factual statements in this Annual Report are supported by the Declaration of Sara Beth Brown in Support of Motion to Approve and Settle Western Asbestos Settlement Trust’s Annual Report and Accounting, Audited Financial Statements, and Claim Report; and to Approve Resolution Regarding the FAIR Act (“Brown Declaration”).

This Annual Report respectfully shows:

1. Effective Date: In compliance with Sections 4.1 and 7.2 of the Plan, and the Glossary of Terms for the Plan Documents, the Effective Date of the Trust is April 22, 2004.
2. Appointment of Trustees: In its February 2, 2004 Order Approving Futures Representative’s Motion for Approval of Appointment of Trustees for the Western Asbestos Settlement Trust, this Court approved the appointment of SANDRA R. HERNANDEZ, M.D., JOHN LUIKART and STEPHEN M. SNYDER as Trustees of the Trust, who have acted in that capacity since that time. Stephen M. Snyder was Interim Managing Trustee between the Effective

¹ The Annual Report is filed in compliance with the following Plan documents: Court’s January 23, 2004 Order Confirming Second Amended Joint Plan of Reorganization and Granting Related Relief (“Order Confirming the Plan”), Western Asbestos Settlement Trust Agreement and the Fourth Amendment to and Complete Restatement of the Western Asbestos Settlement Trust Agreement (“Trust Agreement”), Western Asbestos Settlement Trust Bylaws (“Trust Bylaws”), Case Valuation Matrix (“Matrix), Trust Distribution Procedures (“TDP”) and other controlling documents approved by this Court. The Appendix includes the above-referenced sections of the Plan documents and all Court Orders referenced herein.

1 Date and September 10, 2004, at which time he was unanimously elected by the Trustees to serve
2 as Managing Trustee.

3 3. Tax Obligations: Section 2.2(b) of the Trust Agreement requires the Trustees to
4 file income tax and other returns and statements in a timely manner, and comply with all
5 withholding obligations as legally required, including fulfilling requirements to maintain its status
6 as a Qualified Settlement Fund. The Trust has complied with state and federal tax obligations on a
7 quarterly basis since April 22, 2004, based upon the advice of the Trust's certified public
8 accountants, Sitkoff /O'Neil Accountancy Corporation. The federal tax return for 2004 will be
9 filed on or before September 15, 2005. Because Nevada has no state income tax, the Trust, which
10 resides in Nevada, is not obligated to pay state income taxes.

11 4. Annual Report: Section 2.2 (c)(i) of the Trust Agreement provides in pertinent
12 part:

13 The Trustees shall cause to be prepared and filed under seal with the Bankruptcy
14 Court . . . an annual report containing financial statements of the Trust (including,
15 without limitation, a statement of the net claimants' equity of the Trust as of the
16 end of such fiscal year and a statement of changes in net claimants' equity for such
17 fiscal year) audited by a firm of independent certified public accountants selected
18 by the Trustees and accompanied by an opinion of such firm as to the fairness of
19 the financial statements' presentation of the equity presently available to current
20 and future claimants and as to the conformity of the financial statements with
21 accounting principals generally accepted in the United States, except for the
22 special-purpose accounting methods set forth [in this Amendment].²

19 The Trust is required by the Internal Revenue Code to conduct business on a calendar-year basis.
20 Therefore, all reports attached to this pleading cover the period between the Trust's Effective
21 Date, April 22, 2004, and fiscal year end, December 31, 2004 ("Accounting Period").
22

23 ² As explained in more detail in the Fourth Amendment and Restatement and in "Notes to
24 Financial Statements", A.2, the Trust's financial statements are prepared using special-purpose
25 accounting methods that depart from Generally Accepted Accounting Principals (GAAP) in
26 certain instances, in order to better disclose the amount and changes in net claimants' equity.
27 After discussions with the Trust's accountants and legal counsel in March 2005, the Trustees
28 and the Approving Entities amended the Trust Agreement to employ specialized accounting
principles in certain instances due to the "special purpose" nature of the Trust. The Fourth
Amendment and Restatement also reflects a decision by the TAC, Futures Representative and
Trustees to remove the requirement that the Annual Report be filed under seal, thus allowing it
to be noticed publicly. It additionally provides the Trustees shall file materials under seal which
they determine should remain confidential, and that these are made available to the TAC and the
Futures Representative. The Fourth Amendment and Restatement is attached to the Appendix.

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1 5. Financial Report: In accordance with the requirements of Section 2.2(c)(i) of the
2 Trust Agreement, the Trust has caused its accounts to be audited by independent Certified Public
3 Accountants. The Trust’s audited financial statements are attached as Exhibit “A”. These include
4 a Statement of Net Claimants’ Equity, a Statement of Changes in Net Claimants’ Equity, a
5 Statement of Cash Flows and explanatory Notes. The Statement of Net Claimants’ Equity reflects
6 total assets of the Trust (at market value and on an accrual basis, as of December 31, 2004) that
7 were available to pay claims and operate the Trust. The Net Claimants’ Equity is equivalent to
8 Retained Earnings on a corporate balance sheet. The Statement of Changes in Net Claimants’
9 Equity reflects, on an accrual basis, the initial funding of the Trust, investment income received
10 and accrued, and unrealized gains less disbursements that the Trust paid or accrued during the
11 Accounting Period. The Statement of Cash Flows reflects the actual monies received and
12 expended by the Trust on a cash basis during the Accounting Period.

13 6. Claim Report: Section 2.2(c)(ii) of the Trust Agreement provides that along with
14 the financial statements, the Trust shall file with the Court a report containing a summary
15 regarding the number and type of claims disposed of during the period covered by the financial
16 statements (“Western Asbestos Settlement Trust Claim Report As Of December 31, 2004” or
17 “Claim Report”) attached as Exhibit “B”. The Claim Report demonstrates that the first
18 unliquidated claim (“Trust Claim”) was submitted to the Trust in August 2004, and that by
19 December 31, 2004, the Trust had received 1,475 Trust Claims. Of the Trust Claims that have met
20 the requirements of the Matrix, the Trust has paid and closed 72, and made settlement offers on an
21 additional 111, through December 31, 2004.

22 In addition to processing the Trust Claims, the Trust has paid pre-petition Default,
23 Settlement and Matrix claims (hereafter “Pre-Petition Liquidated Claims”). See this Court’s
24 February 3, 2004 Memorandum of Decision After Confirmation Hearing. Section 5.4 of the TDP
25 provides that within ninety days from the Effective Date, the Trust shall pay Pre-Petition
26 Liquidated Claims “as is possible”. The Managing Trustee and the Trust’s counsel, Jones Vargas
27 Law Firm, reviewed and processed for payment approximately 5,448 Pre-Petition Liquidated
28 Claims in the month following the Effective Date. Of these claims, 5,393 were paid during the

1 Accounting Period in the amount of \$646,295,687. The vast majority of the Pre-Petition
2 Liquidated claims were paid by June 6, 2004, only six weeks after the Trusts' inception.

3 7. Biannual Review: Section 5.7(b) of the TDP requires that the Trust shall review
4 biannually (or more frequently at the request of the TAC or the Futures Representatives) a review
5 of filed claims, paid claims, average payments and disallowed claims, sufficient to allow an
6 estimation of the adequacy of the Trust fund to compensate claimants as compared to the current
7 claims forecast. In October 2004 and April 2005, the Trust prepared a biannual report in
8 compliance with this provision and shared and discussed it with the TAC and Futures
9 Representatives.

10 8. Trustees' Meetings: Article II, Section 4 of the Trust Bylaws provides that the
11 Trustees shall meet in Nevada, or a state other than California, at least once per quarter as soon as
12 practicable after the Effective Date, and on the anniversary of the Effective Date. The Trustees
13 held nine meetings over ten days during the Accounting Period (on April 26th, April 29th, May
14 3d, June 9-10th, July 27th, September 10th, October 12th, November 12th and December 13th of
15 2004) and three meetings over five days after the Accounting Period (on February 28, March 22d,
16 March 23d, April 21st and April 22d). All meetings were held outside of California.

17 9. Public Inspection: In compliance with Sections 2.2(c)(ii) and 2.2(c)(iii) of the
18 Trust Agreement, the Claim Report has been sent to the Approving Entities and the Office of the
19 United States Trustee with responsibility for the Northern District of California, and has been
20 made available for inspection by the public in accordance with procedures established by this

21 Court. 10. Claims Processing Procedures: Section 5.3(b) of the TDP provides that six months
22 after the establishment of the Trust (October 22, 2004), the Trustees, with the consent of the
23 Approving Entities, shall adopt procedures for reviewing and liquidating all Trust Claims, which
24 shall include deadlines for processing such claims. The Trust adopted timelines and developed
25 written procedures for the processing of Trust Claims which were approved by the Trustees and
26 the Approving Entities on July 22 and July 27, 2004, well before the October 22, 2004 deadline.
27 This allowed claims to be submitted to the Trust by August 2004.

28

1 11. Budget and Cash Flow Projections: Section 2.2(d) of the Trust Agreement requires
2 the Trustees to cause to be prepared a budget and cash flow projections prior to the
3 commencement of each fiscal year covering such fiscal year and the succeeding four fiscal years.
4 The Trustees approved the 2005 budget and the required four-year budget and cash flow
5 projections on December 13, 2004. Pursuant to the Trust Agreement these were provided to the
6 Approving Entities and the Debtors. The budget for operating expenses in 2005 (net of claimant
7 payments which are budgeted for \$72,000,000, and net of tax payments which are budgeted for
8 \$4,200,000) is \$7,237,250.

9 12. Custodial Accounts: The Trust established a custody relationship and opened
10 accounts with Wells Fargo Bank, N.A., to act as custodian for the Trustees in connection with
11 Trust investments.

12 13. Reimbursement of USF&G: Section 2.4 of the Trust Agreement provides that the
13 Trust shall reimburse USF&G for certain amounts specified in Section 3.2(c) of the USF&G
14 Settlement Agreement.³ The Trust has estimated funds due to USF&G and deposited these in a
15 Wells Fargo account earning the required interest, as required by the USF&G Settlement
16 Agreement and Section 2.4 of the Trust Agreement. The Trust has not yet paid USF&G because
17 USF&G has not yet submitted a bill. To avoid further accounting difficulties, the Trustees may
18 seek an order from this Court that USF&G submit a statement to the Trust of the total amount to
19 be reimbursed, and supporting documentation on or before June 30, 2005.

20 14. Indemnification Funds: The Trust opened a separate account with Wells Fargo
21 entitled "Claims Defense Fund for Ordway and Milwaukee, Van Packer, and Mac Arthur and
22
23

24 ³ Section 3.2(c) of the June 3, 2002 USF&G Settlement Agreement states: All amounts advanced
25 (1) under Section 3.2(a)(i) through (iii) [for fees incurred by (i) Debtors in defending asbestos
26 claims, (ii) the Futures Representative in connection with the Chapter 11 Cases, and (iii)
27 Asbestos Plaintiffs' Counsel in seeking Plan Approval] or (2) for fees and expenses of the
28 USF&G Parties that were requested to be performed by the Asbestos Plaintiffs' Counsel, shall
be reimbursed to the USF&G Parties by the 524(g) Trust, with interest at the 30-day T bill rate
accrued from the date of payment by the USF&G Parties, within (15) fifteen days following the
524(g) Trust's recovery from any of the Other Insurers of any amounts, whether by judgment,
settlement or otherwise, but in no event shall such fees exceed the amounts recovered by the
Trust.

1 Western Mac Arthur”. This account holds \$15.5 million in cash and securities for the following
2 indemnification obligations:

3 a. Property Damage Claims Defense Fund: Section 2.5 of the Trust
4 Agreement provides that “for a period of ten years following ‘substantial consummation’ of the
5 Plan, the Trustees shall make available to Western Mac Arthur and Mac Arthur funds in an
6 amount not to exceed \$5,000,000” aggregate for defense of claims potentially covered by the
7 insurance policies USF&G issued to Western Asbestos, described in the form of “Stipulation and
8 Order Re: Determination of Certain Issues and Stay of Trial Against USF&G”, entered in
9 *Western Mac Arthur Co., et al. v. USF&G, et al.*, Case No. 828101-2, Alameda Superior Court.

10 b. Pursuant to section V.5.1(a) of the Hartford Settlement Agreement and
11 ancillary agreements, the Trust set aside \$10,000,000 plus after-tax earnings for the purpose of
12 providing a limited indemnity to Milwaukee Insulation Company and John G. Ordway, Jr., in
13 exchange for their release of Hartford in connection with Mac Arthur’s insurance settlements.

14 c. Pursuant to section V.5.1(a) of the Hartford Settlement Agreement and
15 ancillary agreements, the Trust set aside \$500,000 to indemnify Van Packer in exchange for its
16 release given in connection with Mac Arthur’s insurance settlements.

17 15. Johns-Manville Litigation Fund: Section 2.6 of the Trust Agreement provides that
18 Western Mac Arthur must pay \$10,000,000 plus interest to the Johns-Manville Trust as described
19 in the Disclosure Statement, under the terms of the Johns-Manville Plan of Reorganization. On
20 July 27, 2004 the Trustees approved payment to the Johns-Manville Trust of \$12,411,252 pursuant
21 to the provisions in the Disclosure Statement and the Johns-Manville Plan.

22 16. Self-Insured Retention: The Trust initially purchased Director and Officer
23 Liability insurance pursuant to Section 4.6(e) of the Trust Agreement. However, it soon became
24 clear that available policies that offered appropriate protection to the Trustees, Approving Entities,
25 the Debtors and their respective agents, were excessively expensive. Therefore, on September 10,
26 2004, at the recommendation of Woodruff, Sawyer, an independent insurance consulting and
27 brokerage company, the Trustees approved the creation of a self-insurance fund to provide
28 liability coverage for the Trustees, the Futures Representative and members of the Trust Advisory

1 Committee and their agents. Pursuant to the resulting Indemnity Agreement, dated September 10,
2 2004, by and among the Trust, the Trustees, the Futures Representative and the TAC, the Trustees
3 created a custodial account with Wells Fargo entitled “The Indemnity Fund” to provide for the
4 expenses, costs and fees (including attorneys’ fees and costs) associated with defending any
5 judicial, administrative, or arbitrative action, suit or proceeding. The Trustees agreed that the
6 \$40,000,000 in the Indemnity Fund could be reduced after the expiration of three years upon
7 notice, as approved by the Bankruptcy Court, to affected parties. The Trustees also voted to
8 terminate the existing insurance policies and obtain a refund of unearned premiums.

9 17. Priority Lien Funds: Paragraphs 4.5 through 4.8 of the Trust Agreement, as
10 amended, provide in pertinent part that the Trustees, and the Approving Entities and their agents
11 are granted a first priority lien to hold cash and securities sufficient to pay the anticipated
12 compensation and expenses of such parties. The parties who hold a security interest in these funds
13 include the Trustees, the TAC, the Futures Representative and their agents, professionals and
14 representatives (“Secured Parties”). In order to further perfect and acknowledge such priority
15 security interest for the benefit of Secured Parties, the Trust, without waiving or eliminating the
16 security interest rights in any other assets of the Trust by the Secured Parties or anyone else, has
17 established the following three segregated bank accounts which reflect such security interests in
18 favor of the Secured Parties:

19 (a) Indemnity Fund/Self-Insured Retention: A \$40,000,000 Indemnity Fund
20 established at Wells Fargo, as described in paragraph 16, *supra*;

21 (b) Special Budget Fund: A Special Budget fund in the amount of \$36,625,818
22 established at Wells Fargo to cover the expenses set forth in the Special Budget in the event the
23 FAIR Act passes (attached as Exhibit G to Brown Declaration, filed concurrently herewith); and

24 (c) First Priority Lien Fund: The First Priority Lien Fund established by the
25 Trustees at Wells Fargo to pay anticipated compensation and expenses of the Trustees during the
26 first two years of Trust operations.

27 18. Amendments to The Trust Agreement: The Trustees approved two amendments to
28 the Trust Agreement during the Accounting Period: (1) First Amendment to the WAST Trust

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1 Agreement, dated April 29, 2004, provides per diem compensation to the Trustees of \$2,000 per
2 day and \$1,000 for a half day, plus reasonable reimbursement of expenses. The per diem
3 compensation had been offered to the Trustees, as inducements to serve, at the time they were
4 recruited for their positions but was not included in the original Trust Agreement.

5 (2) Second Amendment to and Complete Restatement of Western Asbestos Settlement
6 Trust Agreement, approved December 13, 2004, revised the Trust Agreement in two ways: (a)
7 The Trust Agreement was amended to allow the Trust to invest up to 25% of its assets in stock or
8 convertible securities managed in diversified portfolios of equities that are publicly traded on a
9 major United States exchange. Previously, the Trust Agreement limited the Trust's stock and
10 securities investments to "A"-rated stocks. A change was deemed prudent based on the advice of
11 Callan and Associates, hired by the Trust to assist the Trustees in the selection of investment
12 managers and in developing an investment policy. Prior to the change, the Trust was unable to
13 invest in all securities which were part of the S & P 500; (b) The Trust Agreement was amended
14 to provide per diem compensation of \$2,000 per day (or a pro-rated portion thereof) and
15 reasonable reimbursement of expenses to members of the TAC or their representatives for
16 attending Trustees' meetings, traveling on an official trip of the Trustees, or performing any other
17 "TAC Trust task".

18 19. Statute of Limitations: On December 13, 2004, the Trustees approved a resolution
19 regarding the tolling of the statute of limitations entitled "Trust Resolution Re: Tolling the Statute
20 of Limitations for Certain Claims Through and Including April 22, 2005". The Resolution
21 extends the statute of limitations tolling period from the Petition Date to one year after the
22 Effective Date. The Trust was not in an immediate position, beginning on the Effective Date, to
23 receive and process claims. Because the Trust system was first available to receive claims on
24 August 16, 2004, it was deemed prudent and fair to extend the tolling period. The extension
25 permitted the Trust to further publicize its existence and disseminate its claim forms and
26 guidelines to the public, thereby providing better notice to potential claimants who may otherwise
27 have been unfairly barred by the statute.

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1 20. On-going Litigation: The Trust has filed two unrelated lawsuits during the
2 Accounting Period: (1) *Stephen Snyder, Sandra Hernandez and John Luikart in Their Capacity*
3 *as Trustees of the Western Asbestos Settlement Trust v. The Bank of New York Company, et al.*,
4 Alameda Sup. Ct., November 9, 2004, Case No. BG04184438, and removed by Defendant Bank
5 of New York on Dec. 9, 2004 to U.S. Dist. Ct., N.D.Cal. (Oakland Division), Case No. 04-04372,
6 under jointly administered Case No. 02-46284T. The complaint alleges that the Bank of New
7 York unlawfully charged excessive fees when acting in a fiduciary capacity as the escrow holder
8 of settlement funds before the establishment of the Trust. Also, as part of its fiduciary obligation,
9 Bank of New York was required to send an invoice to USF&G for payment of the fees but instead
10 improperly deducted those fees from the escrow accounts. The Trustees retained Pinnacle Group
11 to represent them in the *Bank of New York* case based on a contingency fee agreement in which
12 the stated fee, as a percentage of any recovery, escalates over time. The percentage fee is now
13 thirty percent.

14 (2) *Western Asbestos Settlement Trust, et al. v. Zurich-American Insurance*
15 *Co., et al.*, San Francisco Sup.Ct., Case No. CGC04-436181, November 9, 2004, is an insurance
16 coverage action against various insurers for recovery under numerous primary and excess policies
17 issued to the Debtors starting in 1946. The Trustees retained Morgan, Lewis & Bockius, LLP to
18 represent the Trust in the *Zurich* litigation pursuant to an hourly fee arrangement, capped monthly,
19 in addition to a contingency payment based on the amount of the final award.

20 21. Trustee Compensation: Section 4.5(c) of the Trust Agreement requires the Trust to
21 report the amounts paid to the Trustees for per annum compensation and expenses. Pursuant to
22 section 4.5(a) of the amended Trust Agreement, the Trustees receive \$50,000 per annum, payable
23 on the Effective Date, plus \$2,000 per eight-hour day for working on Trust business or attending
24 Trustees' meetings. This amount is pro-rated for any work less than eight hours. On September
25 10, 2004, in accordance with Section 4.5(a) of the Trust Agreement, the Managing Trustee's
26 compensation was set at \$3,200 per eight-hour day by the other Trustees and the Approving
27 Entities. The Trust does not compensate Trustees for work in excess of eight hours in one day.
28

1 22. Fees for Plaintiffs’ Firms: In the process of entering the Confirmation Order, the
2 Bankruptcy Court entered Order Regarding Fees Paid to Certain Law Firms, on January 26, 2004
3 (“Fee Order”), requiring three firms to pay to the Trust a total of \$12.3 million in legal fees
4 previously paid to such firms by USF&G. The three firms were Brayton and Purcell, Kazan,
5 McLain, et al. and the Wartnick Law Firm (hereafter “Plaintiffs’ Firms”). On the Effective Date,
6 the Plaintiffs’ Firms paid such amounts to the Trust, but appealed the Fee Order to the Federal
7 District Court. The Trust put the \$12.3 million in a segregated account pending the appeal. The
8 Fee Order was reversed by District Court Order on July 14, 2004. Pursuant to the Court’s Order
9 of July 14, 2004, the Trustees approved payment on July 27, 2004 of the \$12.3 million in fees to
10 Plaintiffs’ Counsel.

11 23. Fees for Special Counsel: Pursuant to this Court’s July 13, 2004 Order of Final
12 Allowance of Contingent Bonus Fees to Debtors’ Special Counsel, the Trust paid fees totaling
13 \$35,542,397 to Brobeck, Phleger and Harrison, Faricy and Roen, Miller, Starr and Regalia and
14 Morgan, Lewis & Bockius law firms.

15 24. Final Fee Applications: In compliance with this Court’s August 2, 2004 Order
16 Modifying Requirements of Guidelines in Connection with Final Fee Applications, the Trust
17 reviewed all legal bills for work completed in the bankruptcy cases between November 22, 2002
18 and April 22, 2004. As a result of this review, the Trust entered into numerous agreements with
19 bankruptcy counsel for reimbursement of improperly billed fees or expenses. Subject to Fee
20 Applicants’ agreements with the Trust, the Court approved all Final Fee Applications in December
21 2004 and January 2005 except for the application of Baron and Budd which was decided outside
22 the Accounting Period.

23 25. Western Asbestos Claims Fund: Section L, paragraphs 50 and 51, of the Order
24 Confirming the Plan, provides that the Trustees shall maintain all proceeds from Debtors’
25 settlement with General Accident in a segregated account to pay individuals’ bodily injury claims
26 that resulted exclusively from exposure to Western Asbestos’ products. The Trust therefore
27 established the Western Asbestos Settlement Fund Custody Account for funds to be paid to
28 Western-only claimants who met the requirements specified in the Plan, this Court’s Orders, the

1 General Accident Settlement Agreement, the Western Group Settlement Trust and the May 3,
2 2004 Stipulation and Order from this Court. The Trust's payment obligation to Western-only
3 claimants was discharged before July 27, 2004. At that time, the Trust closed the Western
4 Asbestos Claims Custody Account and transferred remaining funds to the Western Asbestos
5 Settlement Fund Custody Account.

6 26. Significant Vendors: Although the Trust has many vendors, the most significant of
7 these during the Accounting Period received over \$100,000 for services rendered. These are:

8 (1) Jones, Vargas: Legal counsel responsible for the legal administration of the Trust
9 and bankruptcy matters.

10 (2) Analysis Research Planning Corporation ("ARPC"): Consulting firm hired to help
11 the Trust to develop a claims manual and claims processing procedures. Also hired to create a
12 system to process claims after it was discovered that no existing vendor would be able to meet the
13 requirements of the Matrix and TDP in a timely manner. Also offer ongoing advice concerning
14 improvements to the system.

15 (3) Sierra Computers: Local firm that provides the Trust with technical support and
16 assistance. Worked closely with ARPC to develop the Trust's Case Processing System.

17 (4) 100 W. Liberty LP: Landlord for the Trust office who was prepaid for eighteen
18 months rent, commencing in August 2004.

19 (5) Faricy & Roen PA: Legal counsel to Debtors Mac Arthur and Western Mac
20 Arthur. (6) Fergus, a Law Firm: Counsel to Judge Renfrew, Futures Representative.

21 (7) Morgan, Lewis: Counsel to Debtors and now counsel to the Trust in the *Zurich*
22 litigation described in paragraph 18 above.

23 (8) Orrick: Counsel to the Trust relating to bankruptcy and tax matters.

24 (9) Prindle, Decker & Amaro: Asbestos plaintiffs' law firm that provided the Trust
25 with temporary paralegal staff and training for the expeditious processing of claims soon after the
26 Trust started operations.

27 (10) Sheppard, Mullin, Richter & Hampton LLP: Legal counsel to the TAC.

28 (11) Stutman, Treister & Glatt PC: Legal counsel to the Trust on bankruptcy matters.

1 No vendor was paid more than \$430,000.

2 27. Payment Percentage: Section 4.2 of the TDP provides that, commencing on the
3 first day of January, the Trustees shall reconsider the Payment Percentage to assure that it is based
4 on accurate current information and may, after such reconsideration, change the Payment
5 Percentage if necessary with the consent of the TAC and the Futures Representative. In its April
6 14, 2004 Order Under Fed.R.Bankr.P. 9019 Approving Compromises with Settling Insurers, this
7 Court approved a payment percentage to Western Asbestos claimants of 31.5 percent. At the
8 December 13, 2004 Trustees' Meeting, the Trustees, TAC and counsel to the Future's
9 Representative considered the advisability of changing the payment percentage based upon then-
10 available past and future claim and financial data. It was decided at that time that the parties did
11 not have sufficient data, based on the short duration of the Trust's operation, to make changes to
12 the payment percentage. However, in accordance with Section 4.2 of the TDP, the Trustees shall
13 reconsider the Payment Percentage within three years of January 1, 2005, or at any time if
14 requested to do so by the TAC or the Futures Representative.

15 28. Trust Investment Management: Article 3 of the Trust Agreement authorizes the
16 Trust to administer the investment of funds in the manner in which individuals of ordinary
17 prudence, discretion and judgment would act in the management of their own affairs, subject to
18 certain limitations. The Trust hired Callan & Associates on August 20, 2004 to assist it in
19 developing an investment policy and selecting investment managers. Throughout the fall of 2004,
20 the Trustees and Futures Representative carefully reviewed investment portfolios and interviewed
21 numerous investment management candidates. After thorough analysis and lengthy discussion,
22 the Trustees hired Standish Mellon Asset Management Company, LLC and BlackRock Financial
23 Management, Inc. to act as two of the Trust's investment managers.

24 29. Fairness in Asbestos Injury Resolution ("FAIR Act"): On April 22, 2005 the
25 Trustees passed the "Western Asbestos Settlement Trust's Resolution Regarding the FAIR Act".
26 After consulting with legal counsel, the Trustees passed the Resolution based on their belief that
27 the FAIR Act, as proposed, is unconstitutional and would cause them to breach their duties to the
28 Trust's beneficiaries, many of whom stand to receive significantly less or no payment if the Act

1 passes. In brief, the Resolution provides for the set aside of Trust assets, in the custody of this
2 Court, if necessary, to fund a judicial challenge to the Act based on constitutional grounds, and to
3 maintain limited Trust operations during the duration of the court challenge. The set aside is
4 necessary because if passed, the FAIR Act would force the Trust to shut down operations and
5 transfer all assets to a national asbestos fund within six months of its passage. The set aside of
6 funds will enable the Trust to continue to operate on a limited basis so that if and when the Act is
7 overturned, the Trust will be able to begin paying claims with minimal interruption and expense.
8 The Resolution is attached as Exhibit "A" to Brown Declaration.

9 In conclusion, the Annual Report and attached exhibits demonstrate that the Trust
10 acted prudently and expeditiously in executing its legal obligations during the Accounting Period.
11 The Trust conscientiously worked to establish equitable claims procedures and processed Trust
12 Claims with due diligence soon after the Effective Date. Moreover, the Trust worked assiduously
13 with its accountants and financial advisors to preserve and grow Trust assets in order to fulfill the
14 purpose of the Trust--paying valid asbestos claims. Finally, in discharging their fiduciary duties
15 to the Trust beneficiaries, the Trustees have made a concerted effort to address the special
16 challenges that would arise in the event the FAIR Act passes. In so doing, the Trust carefully
17 complied with all Plan documents and the mandates of this Court.

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