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7 Western Asbestos Settlement Trust

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

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

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

Chapter 11

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

Date: May 19, 2008
Time: 11:00 a.m.
Place: 1300 Clay Street, Room 201
Oakland, CA 94604

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18 Western Asbestos Settlement Trust by and through its counsel, Janet L. Chubb, Esq., of
19 Jones Vargas, herewith files its Fourth Annual Report and Accounting.

20 Respectfully submitted this 25th day of April, 2008.

21 JONES VARGAS

22
23 By: /s/ Janet L. Chubb
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1 **FOURTH ANNUAL REPORT AND ACCOUNTING**
2 **OF WESTERN ASBESTOS SETTLEMENT TRUST**

3 The Trustees of the Western Asbestos Settlement Trust (“Trust”) hereby submit this Fourth
4 Annual Report and Accounting (“Annual Report”) covering Trust activities occurring from
5 January 1, 2007, to and including December 31, 2007 (“Accounting Period”) and certain activities
6 of the Trust, specified below, that took place outside the Accounting Period. This Annual Report
7 is submitted to the U.S. Bankruptcy Court for the Northern District of California, Oakland
8 Division, *In Re Western Asbestos Company*, Case no. 02-46284-T, in accordance with the Second
9 Amended Joint Plan of Reorganization (“Plan”); the Court’s January 27, 2004, Order Confirming
10 Second Amended Joint Plan of Reorganization and Granting Related Relief (“Order Confirming
11 the Plan”); Sixth Amendment to and Complete Restatement of Western Asbestos Settlement Trust
12 Agreement (“Trust Agreement”); First Amendment to and Complete Restatement of Western
13 Asbestos Settlement Trust Bylaws (“Trust Bylaws”); Case Valuation Matrix (“Matrix”); First
14 Amendment to and Complete Restatement of the Western Asbestos Company/ Western Mac
15 Arthur Co./Mac Arthur Co. Asbestos Personal Injury Settlement Trust Distribution Procedures
16 (“TDP”); other controlling documents approved by this Court¹ and pursuant to the laws of the
17 State of Nevada, where the Trust is organized and where it resides. The factual statements in this
18 Annual Report are supported by the Declaration of Sara Beth Brown, Executive Director, in
19 Support of Motion to Approve and Settle Western Asbestos Settlement Trust’s Fourth Annual
20 Report, the Audited Financial Statements, and the Claim Report, as described in paragraphs 5 and
21 6, *infra*. Capitalized terms not defined herein are as defined in the Glossary of Terms for the Plan
22 Documents.

23 1. Effective Date: In compliance with Sections 4.1 and 7.2 of the Plan, and the
24 Glossary of Terms for the Plan Documents, the Effective Date of the Trust is April 22, 2004.

25 2. Appointment of Trustees: In its February 2, 2004, Order Approving Futures
26 Representative’s Motion for Approval of Appointment of Trustees for the Western Asbestos
27 Settlement Trust, this Court approved the appointment of SANDRA R. HERNANDEZ, M.D.,
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¹ The Appendix includes all sections of the Plan Documents, Court Orders, and Agreements referenced herein.

1 JOHN LUIKART and STEPHEN M. SNYDER as Trustees of the Trust, who have acted in that
2 capacity since that time. Elected in 2004 by the other two Trustees, Stephen M. Snyder has
3 continued to serve as Managing Trustee throughout 2007.

4 3. Tax Obligations: Section 2.2(b) of the Trust Agreement requires the Trustees to
5 file income tax and other returns and statements in a timely manner, and comply with all
6 withholding obligations as legally required, including fulfilling requirements to maintain its status
7 as a Qualified Settlement Fund. The Trust has complied with its tax obligations on a quarterly
8 basis based upon the advice of Sitkoff/O'Neil Accountancy Corporation, the certified public
9 accountants retained by the Trust to prepare its annual tax returns. The 2007 federal tax return
10 must be filed on or before September 15, 2008. The Trust resides in Nevada and Nevada has no
11 state income tax. Although the Trust is not subject to tax in California, the Trustees will file a tax
12 return in California, attaching a copy of the Trust's federal tax return but showing no California
13 taxable income or state tax liability.

14 Based on the opinion of tax counsel and relevant authorities, the Trust allocated a
15 portion of each of the 2004, 2006 and 2007 partial payments it made on Pre-Petition Liquidated
16 Default Claims between the judgment amount, which is excluded from income as damages on
17 account of personal physical injury, and interest, which the Trust reported on a Form 1099. In
18 December of 2007, the Trust learned that there may be authority for allocating partial payments
19 entirely to the nontaxable judgment, and none to interest, until the amount of the judgment has
20 been paid in full. The Trust is therefore seeking a ruling from the Internal Revenue Service to
21 confirm that nontaxable treatment of the partial payments, as discussed in paragraph 21. b., *infra*.

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

23 The Trustees shall cause to be prepared and filed with the Bankruptcy Court, as
24 soon as available, and in any event within 120 days following the end of each fiscal
25 year, an annual report containing financial statements of the Trust (including,
26 without limitation, a statement of the net claimants' equity of the Trust as of the
27 end of such fiscal year and a statement of changes in net claimants' equity for such
28 fiscal year) audited by a firm of independent certified public accountants selected
by the Trustees and accompanied by an opinion of such firm as to the fairness of
the financial statements' presentation of the equity presently available to current
and future claimants and as to the conformity of the financial statements with
accounting principles generally accepted in the United States, except for the
special-purpose accounting methods set forth.

1 The special-purpose accounting methods were adopted by the Trustees with the approval of the
2 TAC and the Futures Representative in the Third Amendment to and Complete Restatement of the
3 Western Asbestos Settlement Trust Agreement, dated February 28, 2005. The Trust's financial
4 statements are prepared using special-purpose accounting methods that depart from Generally
5 Accepted Accounting Principles (GAAP) in certain instances in order to better disclose the
6 amount and changes in net claimants' equity.

7 The Trust is required by the Internal Revenue Code to account for and report on its
8 activities for tax purposes on a calendar-year basis. Therefore, except where otherwise stated, all
9 reports attached to this Annual Report cover the Accounting Period.

10 5. Financial Report: In accordance with the requirements of Section 2.2(c)(i) of the
11 Trust Agreement, the Trust has caused its accounts to be audited by Grant Thornton LLP, the
12 independent certified public accountants retained by the Trust to perform the annual audit of its
13 financial statements. The Trust's audited financial statements ("Audited Financial Statements")
14 are attached hereto as Exhibit "A". These include a Statement of Net Claimants' Equity, a
15 Statement of Changes in Net Claimants' Equity, a Statement of Cash Flows and explanatory
16 Notes. The Statement of Net Claimants' Equity, which is the equivalent of a corporate balance
17 sheet, reflects total assets of the Trust at market value and on the other comprehensive basis of
18 accounting adopted by the Trust. These Audited Financial Statements show, among other things,
19 that as of December 31, 2007, total Trust assets were \$1,033,627,574, total liabilities were
20 \$53,357,112, and Net Claimants' Equity was \$980,270,462.

21 6. Claim Report: Section 2.2(c)(ii) of the Trust Agreement provides that along with
22 the Audited Financial Statements, the Trust shall file with the Court a report containing a
23 summary regarding the number and type of claims disposed of during the period covered by the
24 financial statements. The Western Asbestos Settlement Trust Claim Report As Of December 31,
25 2007 ("Claim Report"), is attached hereto as Exhibit "B". During the Accounting Period, the
26 Trust received 933 claims, paid and closed 917 claims, and made settlement offers on an
27 additional 218 claims. Since the Trust received its first Trust claim² on August 27, 2004, the Trust

28 _____
² A claim submitted to the Trust after the Effective Date.

1 has received 5,909 claims, paid and closed 3,525 claims, and 975 claims have been withdrawn.

2 Section 5.4 of the TDP provides that the Trust shall pay Pre-Petition Default,
3 Settlement, and Matrix Claims (hereafter “Pre-Petition Liquidated Claims”)³ “[as] soon as
4 practicable after the Effective Date”. The vast majority of these claims were paid in 2004, and by
5 December 2005, the Trust had paid 99% of all Pre-Petition Liquidated Claims. During the
6 Accounting Period, the Trust paid two (2) Pre-Petition Liquidated Claims in the total amount of
7 \$5,182.86. That amount was paid in trust to the representative law firms after appropriate releases
8 from the respective claimants were received by the Trust. The Trust has not yet received proper
9 release documents for 37 remaining unpaid Pre-Petition Liquidated Claims in the total amount of
10 \$645,762.67.

11 7. Trustees’ Meetings: Article II, Section 4 of the Trust Bylaws provides that the
12 Trustees shall meet in Nevada, or a state other than California, at least once per quarter as soon as
13 practicable after the Effective Date, and on or about the anniversary of the Effective Date. The
14 Trustees held five (5) meetings during the Accounting Period (February 22, 2007, April 19, 2007,
15 July 24, 2007, September 20, 2007, and November 15, 2007). All meetings were held at the Trust
16 headquarters in Reno, Nevada.

17 8. Public Inspection: In compliance with Section 2.2(c) of the Trust Agreement, the
18 Annual Report, including the Audited Financial Statements and Claim Report, has been sent to the
19 Approving Entities and the Office of the United States Trustee with responsibility for the Northern
20 District of California, and has been made available for inspection by the public in accordance with
21 procedures established by this Court.

22 9. Budget and Cash Flow Projections: Section 2.2(d) of the Trust Agreement requires
23 the Trustees to cause to be prepared a budget and cash flow projections prior to the
24 commencement of each fiscal year covering such fiscal year and the succeeding four fiscal years.
25 The Trustees approved the 2008 budget and the required four-year budget and cash flow
26 projections on November 15, 2007. Pursuant to the Trust Agreement, these were provided to the
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³ See this Court’s February 3, 2004 Memorandum of Decision after Confirmation Hearing.

1 Approving Entities. The budget for operating expenses in 2008 is \$3,751,965.⁴

2 10. Maximum Annual Payment: Section 2.4 of the TDP requires that the Trust
3 calculate an annual payment limit for claims based upon a model of the amount of cash flow
4 anticipated to be necessary over the entire life of the Trust to ensure that funds will be available to
5 treat all present and future claimants as similarly as possible. At the November 15, 2007, meeting,
6 the Maximum Annual Payment for 2008 was set at \$62,530,350, plus the amount of \$40,359,650
7 of excess funds carried over from prior years, which Section 2.5 of the TDP requires to be rolled
8 over and remain dedicated to the respective Disease Category in the Jurisdiction to which they
9 were originally allocated.

10 11. Custodial Accounts: Wells Fargo Bank, N.A., continues to act as custodian for the
11 Trust.

12 12. Set Aside Fund: The Trust continues to maintain a separate account with Wells
13 Fargo Bank, N.A. entitled "Claims Defense Fund for Ordway and Milwaukee, Van Packer, and
14 Mac Arthur and Western Mac Arthur" as required by the Trust Documents. This account holds
15 the legally required amount in cash and securities for certain indemnification obligations. No
16 claims were made against any of these indemnity funds during the Accounting Period.

17 13. Indemnity Fund: Section 4.6 of the Trust Agreement provides that the Trust shall
18 indemnify the Trustees, the Trust's officers and employees, the Futures Representative, the TAC
19 and each of their respective agents. The Trustees, the Futures Representative, the TAC and their
20 respective agents have a first priority lien upon the Trust's assets to secure the payment of any
21 amounts payable to them pursuant to Section 4.6.

22 In 2004, the Trust established an indemnity fund in the amount of \$40,000,000, as
23 described in the Trust's Third Annual Report and Accounting. All interest earned by the fund is
24 returned to the Trust quarterly. During the accounting period, no claims were made against the
25 fund and no money was paid from the fund.

26 14. Special Budget Fund: A Special Budget fund was approved in this Court's May
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28 ⁴ This figure is net of claimant payments which are budgeted for \$102,890,000, net of income tax payments which are budgeted for \$5,000,000, and after taking into consideration the J.T. Thorpe facility sharing payment of \$252,000

1 18, 2005, Order to Approve and Settle Western Asbestos Settlement Trust’s Annual Report and
2 Accounting, Audited Financial Statements, and Claim Report; and to Approve Resolution
3 Regarding the FAIR Act (“May 18, 2005, Order”) in the event federal tort reform legislation that
4 would seek to confiscate Trust accounts such as the FAIR Act (S.B. 852) passes. The Special
5 Budget Fund was established to permit the Trust to continue to operate on a limited basis so that if
6 and when the Act is overturned, the Trust will be able to begin paying claims with minimal
7 interruption and expense. In keeping with the May 18, 2005, Order, the Managing Trustee is in
8 charge of administering and reporting on the Special Budget Fund. All interest earned by the fund
9 is returned to the Trust quarterly. In accordance with the May 18, 2005, Order, the Managing
10 Trustee has reported regarding the disposition and status of these monies at each regular meeting
11 in 2007 to determine whether to increase or decrease the amount in this Special Budget Fund. No
12 changes were recommended to adjust the amount during the Accounting Period. As of December
13 31, 2007, the Special Budget Fund contained \$37,715,912.16.

14 15. Settlement Fund Control Account and Control Agreements: Section 4.7 of the
15 Trust Agreement grants to the Trustees, the Futures Representative and the TAC, a security
16 interest in all of the assets of the Trust to secure the indemnification obligations of the Trust to
17 such parties. The Trustees, the TAC, the Futures Representative and their agents have a security
18 interest in the assets of the Trust, including, but not limited to, the five Wells Fargo Bank, N.A.
19 sub-accounts, including the Set Aside Fund, Indemnity Fund, Operating Account, Special Budget
20 Fund and Settlement Fund Account (“Specific Funds”). The Trust has entered into five separate
21 Control Agreements with respect to the Specific Funds, as described in the Trust’s Third Annual
22 Report and Accounting. There has been no change in these Control Agreements during the
23 Accounting Period.

24 16. Resolution Regarding Payment Percentage: Section 4.2 of the TDP provides that,
25 commencing on the first day of January, after the Plan has been confirmed and no less frequently
26 than once every three years thereafter, the Trustees shall reconsider the Payment Percentage to
27 assure that it is based on accurate current information and may, after such reconsideration, change
28 the Payment Percentage if necessary with the consent of the TAC and the Futures Representative.

1 In its April 14, 2004, Order Under Fed.R.Bankr.P. 9019 Approving Compromises with Settling
2 Insurers, this Court approved a Payment Percentage to the Trust's claimants of 31.5%. The
3 Payment Percentage was increased to 34.2% effective January 1, 2006, as described in the Trust's
4 Third Annual Report and Accounting. At the February 22, 2007, meeting, the TAC requested a
5 review of the Payment Percentage and claims projections and the Trustees and Approving Entities
6 agreed to employ Dr. Thomas Vasquez of Analysis Research Planning Corporation to utilize the
7 previous research and analyze new data to determine if the claims projections made at the
8 commencement of the Trust should be revised. Dr. Vasquez was requested to update the forecast
9 as necessary and to determine if the Payment Percentage should be adjusted. Dr. Vasquez
10 submitted his report dated July 1, 2007, to the parties and based upon his conclusions, the
11 Payment Percentage was increased to 40% at the July 24, 2007, meeting.

12 17. Resolution Regarding Inflation Adjustment: The original Payment Percentage
13 approved by this Court was based upon projections of future claims payments adjusted annually
14 for inflation. Beginning in 2006, all claims payments made during a calendar year include a cost
15 of living adjustment for inflation based upon the Federal Bureau of Labor Statistics' *Consumer*
16 *Price Index for Urban Wage Earners and Clerical Workers* (CPI-W) announced in January each
17 year, as described in the Trust's Third Annual Report and Accounting. Consequently, as of
18 January 1, 2007, all claims payments made during the calendar year were increased by 6.09% to
19 account for inflation in 2005 and 2006. At the November 15, 2007, meeting, the CPI-W to be
20 published in January 2008, was approved for use by the Trust in making the 2008 cost of living
21 adjustment for claims payments. Thus, all claims payments made during the 2008 calendar year
22 are increased by 10.65% to account for inflation in 2005, 2006, and 2007.
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25 18. Amendments to the Trust Documents: During the Accounting Period, certain of
26 the Trust documents were revised and placed on the Trust's website as follows:

27 a. As previously set forth in the Trust's Third Annual Report and Accounting: on
28 February 22, 2007, the following significant changes were made to the Trust Agreement:

1 Paragraphs 2.2(c) (i) 6 and 7 of the Trust Agreement were amended to restate financial reporting
2 of interest and dividend income on available-for-sale securities on a net realized and unrealized
3 gains and losses basis; Paragraph 2.2(d) was amended to remove the requirement that the budgets
4 be sent to the Debtors; Paragraph 4.5(a), 4.6(b) and (d) and 5.5(a) were amended to reflect the
5 current compensation of the Trustees, TAC and Futures Representative.

6 b. On September 20, 2007, the following significant changes were made to the
7 Trust Agreement: Paragraph 4.3(a) was revised to allow the Approving Entities to apply to the
8 Bankruptcy Court to fill the vacancy of one (1) Trustee position should the need arise; Paragraph
9 4.5(a) was revised to reflect the current hourly compensation of the Managing Trustee, which was
10 reviewed and increased to \$550 by the Futures Representative and TAC, with the consent of the
11 non-managing Trustees, on July 24, 2007; and Paragraph 4.6, "Compensation and Expenses of
12 TAC Members" was removed from Article 4, "Trustees" and added as Paragraph 6.5 to Article 6,
13 "Trust Advisory Committee", and the paragraphs under Articles 4 and 6 were renumbered
14 accordingly.

15 c. On September 20, 2007, a previously approved revision to Section 4 of the
16 Trust Bylaws concerning the annual meeting requirement. The amendment allows the annual
17 meetings to be held "on or about" the anniversary of the Effective Date.

18 d. On September 20, 2007, the Trust Facilities and Services Sharing Agreement
19 entered into with the J.T. Thorpe Settlement Trust was amended as follows: revisions were made
20 throughout the document to provide for the addition of two (2) Trustees of the J.T. Thorpe
21 Settlement Trust; and Paragraph 4.2 was revised to change the measuring period for the Annual
22 Reconciliation to be on a calendar year basis and to specify the time period of July 1, 2007, to and
23 including December 31, 2008, for the next reconciliation.

24 19. Arbitration Procedures: The current Trust Arbitration Procedures and forms
25 enacted pursuant to Section 5.9(a)-(c) of the TDP were reviewed by the Trust and revisions were
26 approved at the September 20, 2007, meeting. Additional updated procedures and forms were
27 approved on November 15, 2007. Claims Resolution Management Corporation ("CRMC") of
28 Falls Church, Virginia, was retained by the Trust to assist in the administration of claims that

1 proceed through arbitration. CRMC provides arbitration management services and arbitrators to
2 other similar asbestos bankruptcy trusts.

3 20. Fraud Audit: Trust Claims Audit procedures were approved at the February 2,
4 2006, meeting and the Claims Processing and Internal Controls Audit was conducted by Mr.
5 David Maxam in 2006 as described in the Trust's Third Annual Report and Accounting. One of
6 Mr. Maxam's recommendations was that the Trust should conduct an internal claims processing
7 audit in 2007. Such an audit was conducted in July of 2007, by the Trust's outside claims
8 consultant, Mr. Charles LaGrave. Mr. LaGrave's findings were reported at the September 20,
9 2007, meeting and indicated that the Trust was in compliance with the established claims
10 processing practices.

11 Financial Investigative Services, Inc. (FIS) was retained by the Trust to conduct the
12 remaining two phases of the audit which include: (1) a random sample of paid claims to verify
13 that they were valid claims and that the claimants had received the appropriate amounts from their
14 attorney representatives; and (2) a random sample of in-process claims to confirm that the
15 supporting medical documents provided are based upon actual tests, x-rays, examinations, etc. and
16 that the reviewing doctor's diagnosis is reasonable. The findings of the first phase will be
17 completed and reported by the end of the third quarter 2008 and it is anticipated that the findings
18 of the second phase will be completed and reported by the end of 2008.

19 21. Claims and Legal Disputes: The Trust has been involved in three (3) legal disputes
20 during the Accounting Period:

21 a. *Western Asbestos Settlement Trust, et al. v. Zurich-American Insurance Co., et*
22 *al.*, San Francisco Sup.Ct., Case No. CGC04-436181, November 9, 2004: This is an insurance
23 coverage action against various insurers for recovery under numerous primary and excess policies
24 issued to the Debtors starting in 1946. The Trustees retained Morgan Lewis & Bockius LLP to
25 represent the Trust in the *Zurich* litigation pursuant to an hourly fee arrangement, capped monthly,
26 in addition to a contingency payment based on the amount of the final award. The Trust reports
27 on the amounts paid and accrued to the law firm at each Trustees' meeting.

28 b. On April 27, 2007, Patricia Grizzle, Successor-in-Interest of the Estate of Jessy

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1 Grizzle, Deceased, filed a Motion for Order *Nunc Pro Tunc*, Clarification of Second Amended
2 Joint Plan of Reorganization, in this Bankruptcy Court proceeding. Ms. Grizzle's Motion asserted
3 that the portion of default judgment interest paid by the Trust should be reclassified as principal
4 and not be reported to the Internal Revenue Service as interest income until after the amount of the
5 default judgment has been paid in full. A hearing on said Motion was conducted on November 26,
6 2007. The Motion was denied without prejudice and the Order Denying Patricia Grizzle's Motion
7 for Order *Nunc Pro Tunc*, Clarification of Second Amended Joint Plan of Reorganization Without
8 Prejudice was filed on December 17, 2007. Since that time, the Trust learned that there may be
9 authority for allocating partial payments entirely to the nontaxable judgment, and none to default
10 judgment interest, until the amount of the default judgment has been paid in full. The Trust is
11 therefore seeking a ruling from the Internal Revenue Service to confirm that nontaxable treatment
12 of the partial payments. Based on this authority, the Trust notified the holders of Pre-Petition
13 Liquidated Default Claims of the possibility to claim a refund of any federal, state, and local
14 income taxes that they paid with respect to the interest reported by the Trust on Forms 1099 in
15 2004 and 2006. A copy of the Memorandum sent to the Trust's beneficiaries is included in the
16 Appendix filed herewith.

17 c. By letter dated March 6, 2007, the Hartford Accident and Indemnity Company
18 ("Hartford") notified the Trust of Hartford's intention to conduct an audit of all claims submitted
19 to the Trust. Hartford's rights to audit Trust claims information, and the Trust's obligations to
20 accommodate these rights, are spelled out in the original settlement agreement between Hartford
21 and the Debtors (i.e., Mac Arthur Company, Western Mac Arthur Company and Western
22 Asbestos Company) that was approved as a part of the January 27, 2004 Plan Confirmation
23 Order. The Trust determined that, even though this request for claims information is not being
24 made by subpoena, because of the existence of this Court's approval any individual claim
25 information it provides to Hartford should be provided under guidelines of the Trust's Third Party
26 Disclosure Policy in order to provide claimants an opportunity to address any objections to this
27 Court. The Trust provided notice of Hartford's intent to audit through a general notification e-mail
28 to Plaintiffs' attorneys and by posting the general notification on the Trust's website. Since that

1 time, the Trust Advisory Committee and the Futures Representative filed an adversary proceeding
2 in this Bankruptcy Court proceeding seeking declaratory and injunctive relief to limit the scope of
3 Hartford's audit and its use of information received in the course of the audit, including personal
4 claims information. The Trust has intervened in the action. Hartford opposes restrictions on the
5 scope of its review and on its ability to use the information it obtains. Hartford counterclaimed
6 seeking "an order granting specific performance of Hartford's audit right under the Settlement
7 Agreement, requiring the Trust to grant Hartford complete access to review and/or audit the Trust
8 and Trust documents, including allowing Hartford to copy Trust documents." A hearing was held
9 before this Court on March 31, 2008, and the parties' oral arguments were taken under
10 submission. On April 11, 2008, this Court entered an order permitting Hartford to obtain copies
11 of any Trust documents to the extent necessary to perform the audit subject to a protective order;
12 thereby granting the injunctive relief sought by the Trust Advisory Committee and Futures
13 Representative and further, that the injunction should mirror the limitations set forth in the
14 stipulated protective orders executed during the active phase of the Bankruptcy proceedings.

15 22. Reimbursement of USF&G: Section 2.4 of the Trust Agreement provides that the
16 Trust shall reimburse USF&G for certain amounts specified in Section 3.2(c) of the USF&G
17 Settlement Agreement.⁵ The Trust has estimated funds due to USF&G and deposited these in an
18 interest bearing account with Wells Fargo Bank. The Trust calculates the 30 day T-Bill interest
19 rate monthly as required by the USF&G Settlement Agreement and Section 2.4 of the Trust
20 Agreement. Each year the Trust has continued to calculate the interest owed, less the cost of
21 investing the funds and the taxes paid on the funds. The Trust has not yet paid USF&G because
22 USF&G has not responded and not submitted an invoice detailing the amount due. The Trust
23 made numerous requests for USF&G to provide an invoice, with no response. The Trust has also
24 presented USF&G with its own calculation reflecting the amount due in March, 2006, (Exhibit
25

26 ⁵ Section 3.2(c) of the June 3, 2002 USF&G Settlement Agreement states: All amounts advanced (1) under Section
27 3.2(a)(i) through (iii) [for fees incurred by (i) Debtors in defending asbestos claims, (ii) the Futures Representative
28 in connection with the Chapter 11 Cases, and (iii) Asbestos Plaintiffs' Counsel in seeking Plan Approval] or (2) for
fees and expenses of the 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 “C”) and despite several follow up communications, including correspondence and telephone
2 calls; USF&G has failed to respond. As a result of USF&G’s disregard of the Trust’s many
3 attempts to satisfy its obligation, the Trust has had to continue to use its staff time, and to pay for
4 additional audit time, accounting time and investment management fees.

5 The Trust has an obligation to pay claimants and properly calculate future amounts which
6 may be owed. The uncertainty created by USF&G’s failure to respond, makes the task more
7 difficult and requires the Trust to expend funds that should be reserved for payments to claimants.
8 Thus, the Trust intends to cease accruing interest on the estimated funds due as of December 31,
9 2007, in the amount of \$27,434,206.00 as set forth in Exhibit “D” on June 30, 2008. The Trust
10 has specifically provided USF&G with notice by mailing copies of this Annual Report, the
11 motion, declaration in support of the motion, and proposed order via certified mail, return receipt
12 requested, to counsel for USF&G and to USF&G directly.

13 23. Notifications to Beneficiaries: During the Accounting Period, the following
14 notifications were placed on the Trust’s website and forwarded to all interested parties via
15 electronic mail on or about the date of the website posting:

16 a. Notice of an amendment to Section VII d of the Case Valuation Matrix
17 regarding minimum exposure requirements and pro-rata awards; blended exposure rates; and
18 allocation of exposure time at multiple sites (posted on March 14, 2007).

19 b. Notice of claims audit request by Hartford Accident and Indemnity Company
20 (posted on May 10, 2007).

21 c. Notice of increase in Payment Percentage (posted on August 6, 2007).

22 d. Notice of modified Prima Facie notification process (posted on October 31,
23 2007).

24 e. Notices regarding updates to the ship and job site lists and updated claim form
25 (posted on March 14, 2007, May 10, 2007, August 7, 2007, and December 17, 2007).

26 24. Trustees’ Compensation: Section 4.5(c) of the Trust Agreement requires the Trust
27 to report the amounts paid to the Trustees for compensation and expenses. During the Accounting
28 Period, the Trustees each received an annual payment in the amount \$65,000, plus a retroactive

1 payment in the amount of \$3,750.⁶ The total paid to all Trustees for hourly compensation was
2 \$258,036 and \$10,013 was the total amount of expenses incurred by all Trustees.

3 25. Filing Fee: Pursuant to Section 6.4 of the TDP, there were no recommended
4 changes to the current amount of the filing fee during the Accounting Period.

5 26. J.T. Thorpe Settlement Trust Administration: On June 29, 2006, the Trust entered
6 into the Trust Facilities and Services Sharing Agreement with the J.T. Thorpe Settlement Trust
7 (the "J.T. Thorpe Trust") as described in the Trust's Third Annual Report and Accounting. The
8 agreement provides:

9 i) for the J.T. Thorpe Trust to pay all of its own start up costs and a monthly
10 amount, subject to the annual adjustment described in iii), of \$21,000 to the Trust for processing
11 and its share of fixed costs ("Advance Payments") as well as the hiring of the Trust Executive
12 Director as its Executive Director;

13 ii) for the sharing of the Trust employees other than the Executive Director; and

14 iii) for an annual accounting to identify and adjust costs as shared to insure that
15 each trust is paying its proportionate share of the expenses.

16 On July 24, 2007, the Trust provided a written reconciliation of the costs incurred
17 by the J.T. Thorpe Trust. The reconciliation demonstrated that the Annual Services Cost was in
18 excess of the total amount of the Advance Payments. That excess amount, including interest,
19 totaled \$46,308 and was paid by the J.T. Thorpe Trust on July 24, 2007. At that time, it was
20 approved that the amount of the Advance Payments shall remain at \$21,000 per month.

21 27. Significant Vendors: Although the Trust has many vendors, those who were paid
22 more than \$100,000 during the Accounting Period are listed below:

23 a. Analysis Research Planning Corporation ("ARPC"): Consulting firm hired to
24 help the Trust develop a claims manual, claims processing procedures, create a system to process
25 claims, provide program updates and improvements to the claims processing system and provide
26
27

28 ⁶ As described in the Trust's Third Annual Report and Accounting, the Trustees' annual payment was increased from
\$50,000 to \$65,000, effective January 1, 2007. The retroactive payment was for the period of January 1, 2007,
through and including March 31, 2007.

1 monthly maintenance. Dr. Vasquez of ARPC also acts as the expert professional with whom the
2 Trustees and Approving Entities consult.

3 b. BlackRock Financial Management: One of five investment managers for the
4 Trust.

5 c. Dwight Asset Management Company: One of five investment managers for the
6 Trust.

7 d. Eagle Capital Management, LLC: One of five investment managers for the
8 Trust.

9 e. Fergus, a Law Firm: Counsel to The Honorable Charles Renfrew, Futures
10 Representative.

11 f. Jones Vargas: Law firm that acts as Nevada counsel responsible for the legal
12 administration of the Trust and bankruptcy matters.

13 g. Morgan Lewis & Bockius LLP: Counsel to Debtors, counsel to the Trust in the
14 *Zurich* and *Hartford* matters described in paragraph 21, *supra*.

15 h. Sheppard, Mullin, Richter & Hampton LLP: Legal counsel to the TAC.

16 i. Standish Mellon Asset Management Company: One of five investment
17 managers for the Trust.

18 j. State Street Global Advisors: One of five investment managers for the Trust.

19 28. Trust Investment Management: Article 3 of the Trust Agreement authorizes the
20 Trust to administer the investment of funds in the manner in which individuals of ordinary
21 prudence, discretion and judgment would act in the management of their own affairs, subject to
22 certain limitations. Callan & Associates continued to assist the Trust during the Accounting
23 Period as its manager of investment managers. BlackRock Financial Management, Inc., Dwight
24 Asset Management Company, Eagle Capital Management, LLC, Standish Mellon Asset
25 Management Company, LLC, and State Street Global Advisors have continued to act as
26 investment managers to the Trust. The Trust closely monitors any market volatility with its
27 investment advisors and continues to be in compliance with its Investment Policy Statement.

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The Trustees submit that the Annual Report and attached exhibits demonstrate the Trust acted prudently and expeditiously in executing its legal obligations during the Accounting Period. The Trust conscientiously worked to execute equitable claims procedures and process Trust Claims with due diligence during the Accounting Period. Moreover, the Trust worked with its accountants and financial advisors to preserve and grow Trust assets in order to fulfill the purpose of the Trust--paying valid asbestos claims. In so doing, the Trust carefully complied with all Plan documents and the mandates of this Court.