IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re: **VESTTOO LTD., *et al*.,** **Debtors.**[1]	**Chapter 11** **Case No. 23-11160 (MFW)** **(Jointly Administered)**
CHAUCER INSURANCE CO. DAC and CHAUCER SYNDICATES LTD., as managing agent for LLOYD'S SYNDICATE 1084, **Plaintiffs,** **v.** **VESTOO BAY XXIV, LIMITED PARTNERSHIP, WHITE ROCK INSURANCE (SAC) LTD. IN RESPECT OF SEGREGATED ACCOUNT T108-CHAUCER AND CHARLES THRESH AND MICHAEL MORRISON AS JOINT PROVISIONAL LIQUIDATORS OF WHITE ROCK INSURANCE (SAC) LTD.,** **Defendants.**	**Adv. Proc. No. 24-50010 (MFW)**

CHAUCER INSURANCE COMPANY DAC'S AND CHAUCER SYNDICATES LIMITED'S, AS MANAGING AGENT OF LLOYD'S SYNDICATE 1084, AMENDED MEMORANDUM OF LAW IN SUPPORT OF THEIR MOTION FOR A TEMPORARY RESTRAINING ORDER AND PRELIMINARY INJUNCTION

Chaucer Insurance Company DAC and Chaucer Syndicates Limited, as managing agent of Lloyd's Syndicate 1084 (collectively, "**Chaucer**" or "**Plaintiffs**"), by and through their undersigned counsel, respectfully submit this amended memorandum of law (this "**Amended Memorandum**") in support of their Motion for a Temporary Restraining Order and Preliminary

[1] Due to the large number of debtor entities in these chapter 11 cases, a complete list of the Debtors and the last four digits of their federal tax identification numbers is not provided herein. A complete list of such information may be obtained on the website of the Debtors' claims and noticing agent at https://dm.epiq11.com/vesttoo.

Injunction (the "**Motion**") filed concurrently herewith against the above-captioned defendants (collectively, the "**Defendants**"). In support of this Amended Memorandum and the Motion, Chaucer submits the *Amended Declaration of Andrew Ritter in Support of Chaucer Insurance Company DAC's and Chaucer Syndicates Limited's, as Managing Agent of Lloyd's Syndicate 1084, Memorandum of Law in Support of their Motion for a Temporary Restraining Order and Preliminary Injunction* (the "**Amended Ritter Declaration**").

PRELIMINARY STATEMENT[2]

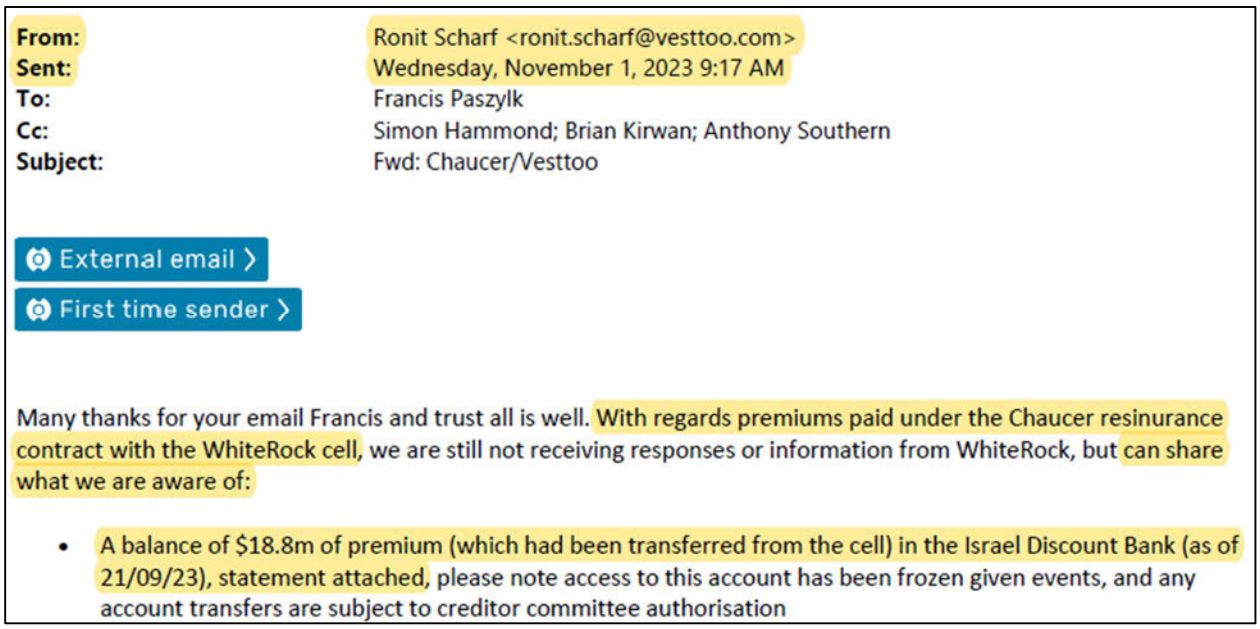
1. As alleged in their Complaint, Plaintiffs are the victims of a fraud perpetrated by the Bay XXIV Debtor. Pursuant to the fraud, the Bay XXIV Debtor wrongfully received approximately $18.8 million from Plaintiffs by delivering two phony "letters of credit" that were purportedly for Plaintiffs' sole benefit. The Bay XXIV Debtor received this money in early 2023 directly from the Chaucer Cell, a Segregated Cell created solely for the purposes of holding Plaintiffs' ceded premiums. Plaintiffs are the only ones who ever contributed money to the Chaucer Cell.

2. Together with the Chaucer Cell, the Bay XXIV Debtor was created for the sole purpose of doing business with Plaintiffs. No other cedent ever did business with the Bay XXIV Debtor or the Chaucer Cell, and the Bay XXIV Debtor never provided any letters of credit (phony or legitimate) for the benefit of any other cedent. At all times, the Bay XXIV Debtor's only known asset has been the approximately $18.8 million in Traceable Premiums it received from Plaintiffs. Today, these funds are held in a segregated account at Israel Discount Bank in the name of the Bay XXIV Debtor.[3]

[2] Capitalized terms used in this Preliminary Statement but not yet defined have the meanings ascribed to such terms in the remainder of this Amended Memorandum.

[3] Notably, in Plaintiffs Proofs of Claim filed against the Bay XXIV Debtor, Claim Nos. 50821 and 50823 (the "**Chaucer Bay XXIV POCs**"), Plaintiffs expressly reserved the right to assert claims against property in the Bay

3. The Debtors have known for some time that the funds held in this Bay XXIV Discount Account are the same funds Plaintiffs contributed to the Chaucer Cell, because the Debtors' general counsel freely admitted as much to Chaucer's broker on November 1, 2023:



From: Ronit Scharf <ronit.scharf@vesttoo.com>
Sent: Wednesday, November 1, 2023 9:17 AM
To: Francis Paszylk
Cc: Simon Hammond; Brian Kirwan; Anthony Southern
Subject: Fwd: Chaucer/Vesttoo

External email >
First time sender >

Many thanks for your email Francis and trust all is well. With regards premiums paid under the Chaucer resinurance contract with the WhiteRock cell, we are still not receiving responses or information from WhiteRock, but can share what we are aware of:

- A balance of $18.8m of premium (which had been transferred from the cell) in the Israel Discount Bank (as of 21/09/23), statement attached, please note access to this account has been frozen given events, and any account transfers are subject to creditor committee authorisation

See id. at ¶ 7 (highlighting supplied).

4. But it was not until very recently that Plaintiffs first saw [redacted]. And it was not until today, and only after Plaintiffs sought emergency relief from this Court, that Plaintiffs were permitted to share [redacted] with the Court for purposes of this Motion. *See Order Granting Chaucer's Motion for a Temporary Restraining Order, Scheduling a Hearing for a Preliminary Injunction and Approving Briefing Schedule With Respect to Preliminary Injunction* [24-50010 (MFW), Docket No. 11] (the "**Chaucer TRO**"). Standing in the way has been the Debtors' and

XXIV Debtor's possession and made clear that nothing in such filed Proofs of Claim should be construed as an admission by Plaintiffs that any property held by any of the Debtors is property of their respective estates. *See* Chaucer Bay XXIV POCs, Attachments at ¶ 8.

the Creditors' Committee's coordinated refusal to make these documents available to Plaintiffs outside of mediation, while simultaneously asserting that the electronic versions of these documents Plaintiffs received during the mediation were subject to "mediation privilege" and therefore could not be shared with the Court. Only after the Court suggested at yesterday's hearing that the Debtors would need to provide this admittedly relevant information in connection with the hearing on February 22, 2024, did the Debtors and the Creditors' Committee finally agree to permit Plaintiffs to submit these records for the Court's consideration on this Motion.

5. Now, in this Amended Memorandum, Plaintiffs can for the first time set forth what these previously withheld [redacted] show. As set forth in detail further herein and in the attached Exhibit A, [redacted]. This critical evidence is, as counsel for the Creditors' Committee has put it, both "significant" to Plaintiffs' constructive trust claim, Hr'g Tr. 12:2-3, Feb. 6, 2024, and also "relevant" to Plaintiffs' objections to plan confirmation, Hr'g Tr. 19:7, Feb. 14, 2024, (which includes Plaintiffs' objection that the plan's improper de facto substantive consolidation would effectively terminate Plaintiffs' constructive trust before this Court has an opportunity to decide the merits of the claim).

6. One reason why these [redacted] are "significant" is because they evidence [redacted]

7. Another reason why these bank statements are "significant" is because they [redacted] In particular, at the February 6, 2024 status conference, the Creditors' Committee volunteered as a "fact" that their financial analysts, who had been "poring over" the Debtors' bank statements, had determined that numerous Vesttoo Bay entities had commingled funds in the parent company's consolidated account, that the commingled funds then "***were used to pay Vesttoo's normal operating expenses***," and, that "***while this commingling was going on or taking place***, the balance in that consolidated Vesttoo Ltd. account dropped to as low as $3 million or less." Hr'g Tr. 11:22-12:22, Feb. 6, 2024 (emphases supplied). The suggestion, of course, was that no cedent whose funds were commingled in this account could ever successfully trace more than approximately $3 million, which would "implicate possible constructive trust and substantive consolidation issues," *id.* at 11:25-12:1, by reducing the significance of those issues in these cases.

8. [redacted]

[redacted]

9. Outrageously, at yesterday's hearing, the Creditors' Committee's counsel—the very same counsel who on February 6, 2024, had said that "the Court [should be] made aware of" these records—took the ***opposite*** position that these [redacted] "shouldn't be available for [Chaucer's] contested preliminary injunction hearing." Hr'g Tr. 17:23-24, Feb. 14, 2024. This reversal reflects an inescapable reality: The very documents the Creditors' Committee sought to use as leverage—going so far as to say they "thought everyone should be aware of" the documents, and that "if we're not able to resolve the outstanding plan objections consensually, [they were] sure the Court [was] going to be hearing more about this issue in the coming weeks," Hr'g Tr. 12:2-13:3, Feb. 6, 2024—are, now seen in the light of day, [redacted].

10. As Plaintiffs show in detail below and in the attached Exhibit A, [redacted]

11. These Traceable Premiums held by the Bay XXIV Debtor are subject to a constructive trust for the benefit of Plaintiffs because (a) the Traceable Premiums were obtained

from Plaintiffs by fraud and (b) the Traceable Premiums can be traced from the money Plaintiffs ceded to the Chaucer Cell. As a result, the Traceable Premiums are not part of the Bay XXIV Debtor's (or any other Debtor's) estate and must be turned over to Plaintiffs.

12. At yesterday's hearing, counsel to the Debtors stated that "the [D]ebtors have not acknowledged a propensity to take cash, and certainly have not indicated or acted in such a way that Bay XXIV cash was at risk of being used." This statement was made notwithstanding the fact that, as of yesterday's hearing, in addition to the admitted commingling that occurred prior to the Petition Date, the Debtors and the Creditors' Committee were well aware that during these Bankruptcy Cases, "[t]he Debtors . . . used a portion[, equal to approximately $4 million,] of the Vesttoo Bay XIV Cash to pay the fees and expenses of estate professionals in these Chapter 11 Cases," referring to such use as the "**Disputed Transfers**" and acknowledging that the cedent associated with such Segregated Debtor, Clear Blue Specialty Insurance Company and its affiliates ("**Clear Blue**"), had "asserted that it is the only or primary creditor of Vesttoo Bay XIV and/or has a constructive trust over the Vesttoo Bay XIV Cash and therefore is entitled to all the Vesttoo Bay XIV Cash (together with the Disputed Transfers[])." *Motion of the Official Committee of Unsecured Creditors for Approval, Pursuant to Section 105(a) of the Bankruptcy Code and Rule 9019 of the Federal Rules of Bankruptcy Procedure, of the Settlement Among Committee and Clear Blue Regarding Vesttoo Bay XIV, Limited Partnership* [23-11160 (MFW), Docket No. 656] ("**Clear Blue 9019 Motion**") at ¶ 14. Plaintiffs also know [redacted]

[redacted] In Clear Blue's case, the proposed settlement providing for the return of the Disputed Transfers to Clear Blue's Segregated Debtor required that Clear Blue "waive[] its right to . . . 50% of the Bay XIV Cash," notwithstanding the acknowledgement that Clear Blue similarly believed that such segregated funds were subject to a constructive trust for Clear Blue's benefit. Clear Blue 9019 Motion at ¶ 14, Exhibit A to Exhibit A.

13. While Plaintiffs are able to trace their funds through the Debtors' pre-petition commingling, and while, as of today, the Debtors have, to Plaintiffs' knowledge, yet to remove any cash from the Bay XXIV Debtor (and the Court has temporarily enjoined the Debtors from doing so until the conclusion of the hearing on February 22, 2024), so long as these cases continue there is a significant risk that the Debtors will seek to use the Bay XXIV Debtor's cash to satisfy their substantial and ever-growing administrative expense burden. The reality of the Disputed Transfers and the other depletions of the Segregated Debtors' funds, and the significant rights waived by Clear Blue in the settlement agreement providing for the return of the Disputed Funds to the appropriate Segregated Debtor, in fact clearly demonstrates the significant risk faced by Plaintiffs if their requested injunctive relief is not granted.

14. Should the Debtors use the Traceable Premiums—funds that do not belong to their estates—to pay administrative expenses or for any other purpose, or the Traceable Premiums are allowed to be commingled, used or otherwise dissipated in connection with a chapter 11 plan, Plaintiffs would be irreparably harmed. Plaintiffs therefore seek preliminary relief from the Court to protect their interests in the Traceable Premiums pending the resolution of their claims for constructive trust.

FACTUAL BACKGROUND

15. On August 14 and 15, 2023 (the "**Petition Date**"), the above-captioned debtors (the "**Debtors**") filed voluntary petitions under chapter 11 of title 11 of the United States Code, 11 U.S.C. §§ 101, *et seq.* (the "**Bankruptcy Code**"), commencing these chapter 11 cases (these "**Bankruptcy Cases**").

16. The Debtors include numerous special purpose partnerships formed in Israel, and Vesttoo Bay XXIV, Limited Partnership (the "**Bay XXIV Debtor**") is one such special purpose partnership (such special purpose partnerships, together with the Bay XXIV Debtor, the "**Segregated Debtors**"). Prior to the Petition Date, the Segregated Debtors separately engaged in various purported reinsurance transactions intended to allow insurance and reinsurance companies, or cedents, to transfer their insurance risks and/or related collateral security obligations to capital market investors (such purported reinsurance transactions, the "**Reinsurance Transactions**"). *See Declaration of Richard Barnett in Support of the Omnibus (Non-Substantive) Objection of Chaucer Insurance Company DAC and Chaucer Syndicates Limited, as Managing Agent of Lloyd's Syndicate 1084, to Unenforceable Claims Against Vesttoo Bay XXIV, Limited Partnership for Voting Purposes and Joinder to Official Committee of Unsecured Creditors' Objection to JPL Claims for Voting Purposes Pursuant to 11 U.S.C. §§ 502(b), 502(e) and 1126(a) and Fed. R. Bankr. P. 3007 and 3018* [23-11160 (MFW), Docket No. 579] (the "**Barnett Declaration**") at ¶ 4.

17. Each Segregated Debtor engaged in Reinsurance Transactions with (a) a corresponding segregated account (the "**Segregated Cells**") formed pursuant to the Bermuda Segregated Account Companies Act (the "**Bermuda SAC Act**") and (b) one or more particular cedents. *Id*. at ¶ 5. The Bay XXIV Debtor's corresponding segregated account was that certain

Segregated Cell designated "T108 – Chaucer" (the "**Chaucer Cell**"), and the sole business of the Bay XXIV Debtor and the Chaucer Cell was to engage in Reinsurance Transactions with Chaucer (the "**Chaucer Transactions**"). *Id*. at ¶ 5, 10.

18. The purpose of the Segregated Debtors and the Segregated Cells was to segregate the assets and liabilities associated with the Reinsurance Transactions with particular cedents from the assets and liabilities of the Reinsurance Transactions with other cedents. *Id.* at ¶ 5, 7. In particular, the purpose of the Bay XXIV Debtor and the Chaucer Cell was to segregate the Chaucer Transactions from the remainder of the Debtors' business activities. *Id.* at ¶ 5, 7, 10.

19. In connection with the Chaucer Transactions, the Bay XXIV Debtor caused two letters of credit, purportedly issued by China Construction Bank and dated November 21, 2022, and January 27, 2023 (the "**Bay XXIV LOCs**"), to be delivered to Chaucer. *Id.* at ¶ 6; *see also*

Am. Ritter Declaration at ¶ 3. The Bay XXIV LOCs each listed the Bay XXIV Debtor, on behalf of the Chaucer Cell, as the "Applicant," and listed Chaucer as the "Beneficiary":

BENEFICIARY: CHAUCER SYNDICATES LIMITED (ACTING ON BEHALF OF TRUSTEES OF SYNDICATE 1084 AND CHAUCER INSURANCE COMPANY), 52 LIME STREET, LONDON, EC3M 7AF	APPLICANT: VESTTOO BAY XXIV ("VB") ON BEHALF OF WHITE ROCK INSURANCE (SAC) LTD. ACTING IN RESPECT OF ITS SEGREGATED ACCOUNT DESIGNATED AS "T108 - CHAUCER" C/O AON INSURANCE MANAGERS (BERMUDA) LTD. C/O AON INSURANCE MANAGERS (BERMUDA) LTD. 30 WOODBOURNE AVENUE PEMBROKE, HM08 BERMUDA

* * *

BENEFICIARY: CHAUCER SYNDICATES LIMITED (ACTING ON BEHALF OF TRUSTEES OF SYNDICATE 1084 AND CHAUCER INSURANCE COMPANY), 52 LIME STREET, LONDON, EC3M 7AF	APPLICANT: VESTTOO BAY XXIV ("VB") ON BEHALF OF WHITE ROCK INSURANCE (SAC) LTD. ACTING IN RESPECT OF ITS SEGREGATED ACCOUNT DESIGNATED AS "T108 - CHAUCER" C/O AON INSURANCE MANAGERS (BERMUDA) LTD. C/O AON INSURANCE MANAGERS (BERMUDA) LTD. 30 WOODBOURNE AVENUE PEMBROKE, HM08 BERMUDA

See Am. Ritter Declaration at ¶ 3 (highlighting supplied). The Bay XXIV LOCs were fraudulent. Barnett Declaration at ¶ 6.

20. As a result of the fraudulent Bay XXIV LOCs, Chaucer was fraudulently induced to make various premium payments to the Chaucer Cell in connection with the Chaucer Transactions, which premium payments equaled approximately $28.8 million in the aggregate (the "**Chaucer Premiums**"). *Id.* at ¶ 7.

21. [redacted], portions of the Chaucer Premiums equal to [redacted] were improperly transferred from the Chaucer Cell to [redacted] (such transferred premiums, together with any interest or other investment income earned thereon, the "**Transferred Premiums**" [redacted]

[redacted]

[4] Unlike with respect to the Transferred Premiums held by the Bay XXIV Debtor, Chaucer is not aware of facts suggesting an imminent risk to the portion of the Chaucer Premiums remaining in the Chaucer Cell. As a result, Chaucer is not seeking injunctive relief with respect to the portion of the premiums remaining in the Chaucer Cell at this time, although Chaucer reserves the right to seek additional injunctive relief with respect to such funds at a later date.

[5] [redacted]

22. [redacted]

23. [redacted]

24. [redacted]

[redacted]

25. [redacted]

26. [redacted]

27. [redacted]

28. [redacted]

29. Consistent with the above facts, on November 1, 2023, the Debtors' General Counsel, Ronit Scharf, admitted that the Traceable Premiums located in the Discount Account reflected premiums paid by Chaucer to the Chaucer Cell. *See id.* at ¶ 7.

30. The Traceable Premiums are the only amounts held in the Discount Account, [redacted].

LEGAL STANDARDS

A. Ability of Bankruptcy Court to Enter Preliminary Injunctions

31. Bankruptcy courts have broad equitable powers under section 105(a) of the Bankruptcy Code to "assure the orderly conduct of the reorganization proceedings." *In re AP Indus., Inc.*, 117 B.R. 789, 801 (Bankr. S.D.N.Y. 1990). Indeed, the "reach of bankruptcy jurisdiction encompasses all matters the outcome of which could affect the debtor or its reorganization." *In re Ionosphere Clubs, Inc.*, 111 B.R. 423, 430 (Bankr. S.D.N.Y. 1990).

32. This includes the ability to enter preliminary injunctions if needed as a temporary measure to maintain the status quo until the court renders a decision on the merits. *Anderson v.*

Davila, 125 F.3d 148, 156 (3d Cir. 1997); *see, e.g., United Air Lines, Inc. v. City of Los Angel*es (*In re UAL Corp.*), 391 B.R. 791, 806 (Bankr. N.D. Ill. 2008) (issuing preliminary injunction to preserve the status quo pending a final determination on a declaratory judgment).

33. Thus, section 105(a) of the Bankruptcy Code authorizes the issuance of a preliminary injunction, pending a final determination on the merits, barring Debtors from any use or transfer of the Traceable Premiums. As discussed below, an immediate injunction against the Debtors is warranted because any transfer and dissipation of the Traceable Premiums would irreparably harm Plaintiffs, but enjoining such use will not materially harm the Debtors.

34. Bankruptcy Rule 7065 provides for the issuance of preliminary injunctions in adversary proceedings. In the Third Circuit, courts consider the following factors to determine whether a preliminary injunction should be issued under section 105(a) of the Bankruptcy Code: (1) whether the movant has shown a reasonable probability of success on the merits; (2) whether the movant will be irreparably injured by denial of the relief; (3) whether granting preliminary relief will result in even greater harm to the nonmoving party; and (4) whether granting the preliminary relief will be in the public interest. *Allegheny Energy, Inc. v. DQE, Inc.*, 171 F.3d 153, 158 (3d Cir. 1999).

35. No one factor in the preliminary injunction analysis is dispositive, but "[t]he first two factors of the traditional standard are the most critical." *Reilly v. City of Harrisburg*, 858 F.3d 173, 179 (3d Cir. 2017) (quoting *Nken v. Holder*, 556 U.S. 418, 434 (2009)). Furthermore, "when the movant is more likely to succeed, the harm required to be shown is less." *Honeywell Intern., Inc. v. Universal Avionics Sys. Corp.*, 397 F. Supp. 2d 537, 548 (D. Del. 2005).

B. Recognition of Constructive Trusts in Bankruptcy Context

36. The Bankruptcy Code expressly excludes from the debtor's estate any property in which the debtor holds no equitable title. *See* 11 U.S.C. §541(d) ("Property in which the debtor

holds, as of the commencement of the case, only legal title and not an equitable interest . . . becomes property of the estate . . . only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold").

37. The exclusion in section 541(d) applies to "funds held in express trust" as well as "funds held in constructive trust." *In re Columbia Gas Systems, Inc.*, 997 F.2d 1039, 1059 (3d Cir. 1993). This Court has in fact directly addressed the recognition of constructive trusts in bankruptcy contexts, explaining:

> [T]he Bankruptcy Code does not preclude the application of constructive trust law. The Third Circuit has noted that Congress clearly intended the exclusion from property of the estate created by section 541(b) to include not only funds held in express trust, but also funds held in constructive trust. While the cases cited [for the proposition that bankruptcy courts favor a pro rata distribution of funds when such funds are claimed by creditors of like status] broadly state a reluctance to apply constructive trust law in the bankruptcy context, in fact those courts acknowledged that such relief was available and denied the relief only because the elements of a constructive trust were not met rather than because the filing of the bankruptcy case cut off that right.

In re Washington Mut., Inc., 450 B.R. 490, 501 (Bankr. D. Del. 2011) (citations omitted); *see also In re Bake-Line Group, LLC*, 359 B.R. 566, 575 (Bankr. D. Del. 2007) (finding the argument that "constructive trusts are not consistent with the policy of the Bankruptcy Code" to be "overly broad"); *In re Paul J. Paradise & Assocs., Inc.*, 249 B.R. 360, 371 (D. Del. 2000) (finding the Bankruptcy Court's reliance on the proposition "that, as a general rule, the policy of ratable distribution necessarily trumps state equitable trust law, [was] in error"); *In re Dwek*, No. 07-11757, 2009 WL 1119422, at *3 (Bankr. D.N.J. Apr. 27, 2009) ("the Third Circuit does not share [the] . . . view that it is inadvisable to impose constructive trusts in bankruptcy."); *In re United Auto Mart, Inc.*, 2009 WL 1749061, at *7 (Bankr. D.N.J. 2009) (noting that "funds held in a constructive trust are not property of the bankruptcy estate"); *In re Ursa Operating Co., LLC*, No. 22-1729, 2024 WL 278397, at *4 (3d Cir. Jan. 25, 2024) (holding "that a constructive trust is a

legally available remedy in this [bankruptcy] case"); *In re Trout*, No. 05 19591/JHW, 2006 WL 4452826, at *3 (Bankr. D.N.J. Feb. 1, 2006) ("The use of constructive trusts in the context of . . . equitable distribution and bankruptcy is not new").

38. "The determination of whether a constructive trust applies is a question of state law." *In re Bake-Line Grp.*, LLC, 359 B.R. 566, 571 (Bankr. D. Del. 2007); *see also In re Catholic Diocese of Wilmington, Inc.*, 432 B.R. 135, 147 (Bankr. D. Del. 2010) ("The Court looks 'to state law to determine whether the claimant has shown a trust relationship, but [it looks] to federal law to determine whether the claimant has traced and identified the trust funds.'"); *In re Brown*, 591 B.R. 587, 592 (Bankr. M.D. Pa. 2018) ("[A] bankruptcy court looks to state law to determine whether there is an enforceable claim against the debtor."); 11 U.S.C. §101(5) (defining "claim" as a "right to payment . . . whether or not such right is . . . equitable").

39. In Delaware as well as other states, a constructive trust will be recognized "[w]hen one party, by virtue of fraudulent, unfair or unconscionable conduct, is enriched at the expense of another to whom he or she owes some duty." *Hogg v. Walker*, 622 A.2d 648, 652 (Del. 1993); *see also In re Christenson*, 483 B.R. 743, 748 (Bankr. D. Kan. 2012) ("Property procured by fraud may be treated as being held in a constructive trust and excluded from the bankruptcy estate.").[6]

40. A constructive trust is formed at the time the improper conduct causes a defendant to become unjustly enriched. *See Adams v. Jankouskas*, 452 A.2d 148, 152 (Del. 1982) ("[A] constructive trust . . . is imposed when a defendant's fraudulent, unfair or unconscionable conduct causes him to be unjustly enriched at the expense of another to whom he owed some duty").

41. Where a party's improper conduct causes unjust enrichment, a constructive trust may be imposed upon all unjustly obtained property so long as it is traceable. *See Hogg*, 622 A.2d

[6] The same is true under English law, which governed the Chaucer Transactions.

at 652 ("The constructive trust concept has been applied to the recovery of money, based on tracing an identifiable fund to which plaintiff claims equitable ownership"); *Smith v. Smitty McGee's, Inc.*, 1998 WL 246681, at *4 (Del. Ch. May 8, 1998) ("[T]his Court may impose a constructive trust over any assets traceable to that conduct and still held by defendants"). Generally, a constructive trust can be formed if "money or property identified as belonging in good conscience to [a] plaintiff [can] clearly be traced to particular funds or property in the defendant's possession." *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 213 (2002). In other words, assets in "an intact, traceable fund" can allow for relief in the form of a constructive trust. *Leckey v. Stefano*, 501 F.3d 212, 230 (3d Cir. 2007).

42. Even where unjustly received money is later moved into or out of a commingled account, a constructive trust will be found so long as the transactions transferring trust assets are reasonably identifiable. *See, e.g., Volvo Com. Fin., L.L.C. The Americas v. Wells Fargo Bank, N.A.*, 163 P.3d 723, 726 (Utah Ct. App. 2007) ("funds transferred out of a commingled account . . . in some other identifiable form" are still held in trust for the beneficiary); *Brennan v. Tillinghast*, 201 F. 609, 614 (6th Cir. 1913) (if commingled funds are transferred "in a substituted form to another fund . . . the trust attaches to the substituted form in which the property is retained"). Indeed, the tracing analysis "permits the claimant to identify as the traceable product of his property the whole of any investment made by withdrawal from the commingled fund." *Restatement (Third) of Restitution and Unjust Enrichment* § 59 (2011).[7]

[7] Tracing a fungible asset, such as money, can become more difficult if the money is moved to an account where it is commingled with other funds not held in trust for the beneficiary and then the commingled funds in such account are dissipated. In appropriate situations, courts in the Third Circuit use the lowest intermediate balance test (the "**LIBT**") to resolve this difficulty. *See, e.g., In re Columbia Gas Sys. Inc.*, 997 F.2d 1039, 1064 (3d Cir. 1993); *In re Cath. Diocese of Wilmington, Inc.*, 432 B.R. 135, 151 (Bankr. D. Del. 2010). The LIBT assists in the reasonable identification of commingled funds by allowing trust beneficiaries the right to assume that trust funds are withdrawn last from a commingled account. The lowest intermediate balance in a commingled account therefore represents trust funds that have never been dissipated and remain reasonably identifiable. *See id.* Where funds reasonably identified

ARGUMENT

43. Plaintiffs are entitled to a preliminary injunction because: (A) the undisputed manner in which the Traceable Premiums were fraudulently obtained from Chaucer, and the straightforward traceability of the Traceable Premiums from Chaucer [redacted] to the Bay XXIV Debtor's Discount Account, evidence far more than the mere reasonable probability of success on the merits Plaintiffs must show; (B) Plaintiffs will be irreparably harmed if the preliminary injunction is not granted as a result of the Debtors' demonstrated willingness to utilize segregated funds for general purposes and the Debtors' inability to satisfy a monetary judgement; (C) a preliminary injunction will not harm the Debtors given that they have not conducted business since the Petition Date and are in the midst of liquidation; and (D) granting a preliminary injunction to protect defrauded claimants such as Chaucer is in the public interest.

A. Chaucer Has a Reasonable Probability of Success on the Merits Because the Traceable Premiums Are Held in Constructive Trust.

44. At the preliminary injunction stage, "[t]he Third Circuit has construed the likelihood of success on the merits to mean a reasonable probability of eventual success in the litigation." *Spark Therapeutics, Inc. v. Bluebird Bio, Inc.*, 2022 WL 605724, at *3 (D. Del. 2022). Thus, movants are not "require[d] at the preliminary stage" to make a "more-likely-than-not showing of success." *Reilly*, 858 F.3d at 179 n.3. In other words, a "movant need only show the prospect or possibility that he or she will succeed, and need not prove same with certainty." *In Re LTL Mgmt., LLC*, 640 B.R. 322, 335 (Bankr. D.N.J. 2022).

in accordance with the LIBT as those being held in trust are transferred out of the commingled account, the tracing exercise continues with respect to the transferred-out funds. *See Volvo*, 163 P.3d at 726.

45. Plaintiffs easily satisfy this standard. Here, it is undisputed that the Bay XXIV Debtor engaged in conduct significantly worse than the debtor in *Washington Mutual*. *See Washington Mut.*, 450 B.R. at 502 (finding that refusal to allow expressly permitted early distributions from benefit plan a year prior to bankruptcy filing and falsely telling plan participants that they were not entitled to such distributions "established sufficient inequitable conduct by the [d]ebtors to warrant the imposition of a constructive trust"). The Bay XXIV LOCs, the foundation of the Bay XXIV Debtor's fraud, were intentional fictions carefully tailored for the Chaucer Transactions in order to unjustly enrich the Bay XXIV Debtor at Chaucer's expense. The Bay XXIV Debtor's efforts were successful, and Plaintiffs were fraudulently induced to pay the approximately $28.8 million in Chaucer Premiums to the Chaucer Cell as a result of the Bay XXIV LOCs. This appalling fraudulent conduct by the Bay XXIV Debtor easily warrants the imposition of a constructive trust with respect to the Chaucer Premiums, including the Transferred Premiums and any other portions of the Chaucer Premiums that may be in the Debtors' possession or control.

46. Following Chaucer's fraudulently induced payment of the Chaucer Premiums to the Chaucer Cell, the Traceable Premiums are easily traced from the Chaucer Cell to where they are today—in the Bay XXIV Debtor's Discount Account. [redacted] What is more, as discussed above, the Debtors have also already ***admitted*** that the funds held in the Bay XXIV Debtor's Discount Account represent the Traceable Premiums.

47. Notably, Plaintiffs have not yet been afforded an opportunity to conduct discovery. Without that benefit, and with only the limited information currently available, [redacted]

[redacted]

48. [redacted]

49. Accordingly, the Traceable Premiums held by the Bay XXIV Debtor, identifiable from Chaucer's payments to the Chaucer Cell until deposited with the Bay XXIV Debtor in the Discount Account and acknowledged by the Debtors as Chaucer Premiums, are subject to constructive trust for Chaucer's benefit and are not part of the Bay XXIV Debtor's, or any other

Debtor's, estate. As a result, and for the reasons discussed above, Chaucer has demonstrated, at the very minimum, a reasonable probability of success on the merits.

B. Chaucer Will Be Irreparably Harmed If an Injunction Is Not Granted.

50. Chaucer will also be irreparably harmed if the injunction is not granted. Absent an injunction, there is an imminent risk that the Traceable Premiums will be transferred for the purpose of satisfying administrative expenses or other costs. The desire to do exactly that has been indicated by the Official Committee of Unsecured Creditors in these Bankruptcy Cases (the "**Creditors' Committee**"), as their proposed plan of liquidation clearly seeks to use the Traceable Premiums to subsidize the Debtors' satisfaction of the massive professional fees incurred in these Bankruptcy Cases in an effort to confirm such plan. Once the Traceable Premiums are transferred and dissipated, it is very likely that Chaucer would never be able to recover its funds due to the Debtors' insolvency (which, as discussed in Chaucer's objection to the proposed chapter 11 plan, may extend to administrative insolvency).

51. Courts have repeatedly held that this type of risk to assets potentially subject to a constructive trust constitutes irreparable harm. *See DuFour v. BE LLC*, No. CV 09-3770 CRB, 2009 WL 4730897, at *3 (N.D. Cal. Dec. 7, 2009) (granting preliminary injunction in connection with constructive trust in part because "if Plaintiffs are forced to wait until the conclusion of these proceedings before obtaining relief [from a bankrupt entity], there will be nothing left to satisfy a judgment" and that risk constituted irreparable injury); *see also In re Am. Tissue, Inc.*, No. 01-10370 KG, 2006 WL 3498065, at *4 (Bankr. D. Del. Dec. 4, 2006) (risk that assets would be sold in bankruptcy proceedings and insufficient assets would remain to pay a judgment qualified as irreparable harm sufficient to warrant entry of preliminary injunction); *cf. Van Horn, Metz & Co. v. Crisafulli*, No. CV 21-01128 (FLW), 2021 WL 4317186, at *4 (D.N.J. Sept. 23, 2021) (granting

preliminary injunction seeking imposition of a constructive trust because of risk that defendant would dissipate assets and would subsequently be unable to pay a judgment); *Crawford & Co. Med. Ben. Tr. v. Repp*, No. 11 C 50155, 2011 WL 2531844, at *4 (N.D. Ill. June 24, 2011) (same).

52. If the Court does not enter a preliminary injunction, then there is a real and substantial risk that Chaucer will never be able to recover the Traceable Premium, even if it subsequently prevails on the merits of its constructive trust claim, a quintessential case of irreparable harm. *See USACO Coal Co. v. Carbomin Energy, Inc.*, 689 F.2d 94, 98 (6th Cir. 1982) (holding district court had power to issue preliminary injunction preserving defendant's property where "property subject to the injunction may well be dealt with by a final decree in equity requiring an accounting by the defendants as constructive trustees for the plaintiffs").

C. The Balance of Harms Favors Plaintiffs.

53. To allow the Debtors or their estates (in connection with a chapter 11 plan or otherwise) to freely dispense with the Transferred Premiums they fraudulently obtained would be overwhelmingly unjust. Because the Debtors do not have any equitable right to the Transferred Premiums, an injunction will merely preserve the status quo and prevent the Debtors or the Creditors' Committee from using these Bankruptcy Cases to circumvent the clear provisions of section 541(d). An injunction would merely have the effect of preserving the protections section 541(d) affords Chaucer and leave intact the Bay XXIV Debtor's ability to satisfy a future judgment ordering it to return the Traceable Premiums. Especially in light of the strength of Chaucer's claims, and the fact that the Debtors have not operated a business for the duration of these Bankruptcy Cases and are merely seeking to accomplish a liquidation of their assets, the balance of equities weighs heavily in favor of Chaucer. *Gerardi v. Pellulo,* 16 F.3d 1363, 1373-1374 (3rd Cir. 1994) (where preliminary injunction is necessary to preserve non-movant's existing ability to

satisfy a future judgment, balance of equities weighs against the non-movant); *see also Van Horn,* 2021 WL 4317186, at * 8 (finding that "the balance of hardships favors an injunction" where defendant "admitted that she used some of the [funds] . . . and further dissipation of the funds would hinder the enforceability of any potential judgment"); *Berger v. Weinstein*, No. 07-994, 2008 WL 191172, at *10 (E.D. Pa. Jan. 23, 2008) (finding balance of hardships favored granting an injunction where "Plaintiff faces dissipation of any potential future judgment, [whereas] Defendant is merely asked to preserve the status quo").

D. Granting a Preliminary Injunction Is in the Public Interest.

54. The issuance of an injunction is also in the public interest. The Third Circuit has noted that, as a practical matter, "if a plaintiff demonstrates both a likelihood of success on the merits and irreparable injury, it almost always will be the case that the public interest will favor the plaintiff." *Am. Tel. & Tel. Co. v. Winback &Conserve Program, Inc.*, 42 F.3d 1421, 1427 n.8 (3d Cir. 1994). As discussed above, Plaintiffs have demonstrated both a likelihood of success on the merits and irreparable injury if relief is not granted. Thus, the public interest favors granting the preliminary injunction.

55. Additionally, "the prevention of unjust enrichment by means of fraud or misappropriation, even that affecting only private entities, is in the general public interest." *Allstate Ins. Co. v. Davidson Med. Grp.*, No. CIV.A. 01-5938, 2004 WL 2357797, at *4 (E.D. Pa. Oct. 18, 2004); *see also Van Horn*, 2021 WL 4317186, at *8 ("Public interest is also clearly served by preserving a potential judgment against claims of unjust enrichment, conversion, and fraudulent transfer."). As discussed above, the Bay XXIV Debtor defrauded Chaucer and induced it to transfer the Chaucer Premiums for the Bay XXIV Debtor's benefit. Preventing the Bay XXIV

Debtor (or any other Debtor) from profiting from its fraud would accordingly promote public interest.

E. No Bond Should Be Required.

56. No bond or other security should be required in the case before the injunction issues. Bankruptcy Rule 7065 expressly disclaims the bond requirement laid out in Fed. R. Civ. P. 65(c). And in any event, the Traceable Premiums themselves contain enough funds to meet any necessary expenses in the unlikely event that Chaucer does not prevail on its claims.

CONCLUSION

WHEREFORE, Chaucer respectfully requests that the Court issue an order preliminarily enjoining the Debtors from moving or using the Traceable Premiums in any way.

Dated: February 15, 2024
Wilmington, Delaware

ASHBY & GEDDES, P.A.

/s/ *Ricardo Palacio*
Ricardo Palacio (DE Bar No. 3765)
500 Delaware Avenue, 8th Floor
Wilmington, DE 19801
Tel: (302) 654-1888
Email: rpalacio@ashbygeddes.com

-and-

WIGGIN AND DANA LLP
Andrew Ritter, Esq.
Nathan E. Denning, Esq.
437 Madison Avenue 35th Floor
New York, New York 10022
Tel: (212) 551-2600
Email: aritter@wiggin.com
ndenning@wiggin.com

Counsel to Chaucer Insurance Company DAC and Chaucer Syndicates Limited as managing agent of Lloyd's Syndicate 1084

EXHIBIT REDACTED