

**THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION**

In re:)	Chapter 11
)	
UAL CORPORATION, et al.,)	Case No. 02-B-48191
)	(Jointly Administered)
Debtors.)	
)	Honorable Eugene R. Wedoff
)	
)	Hearing Date: January 20, 2006 at 9:30 a.m.
)	
)	Objection Deadline: January 16, 2006
)	

NOTICE OF MOTION

TO: SEE ATTACHED SERVICE LISTS

PLEASE TAKE NOTICE that on the 20th day of January, 2006, the Debtors shall appear before the Honorable Bankruptcy Judge Eugene R. Wedoff in the room usually occupied by him at the United States Bankruptcy Court for the Northern District of Illinois, Eastern Division at 219 S. Dearborn St., Chicago, Illinois 60604, and present the attached **Debtors' Motion for Order Approving Entry into Settlement Agreement and Insurance Policy Buy-Back Agreement Regarding Hull and Liability Insurance Policies Issued by London Market Insurers.**

PLEASE TAKE FURTHER NOTICE that you may obtain further information concerning these Chapter 11 cases:

At the United States Bankruptcy Court, Northern District of Illinois at either www.ilnb.uscourts.gov (home page); or

At the Debtors' private website at www.pd-ual.com.

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Dated: Chicago, Illinois
January 6, 2006

Respectfully submitted,

/s/ James J. Mazza, Jr.

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**DEBTORS' MOTION FOR ORDER APPROVING ENTRY INTO SETTLEMENT
AGREEMENT AND INSURANCE POLICY BUY-BACK AGREEMENT
REGARDING HULL AND LIABILITY INSURANCE
POLICIES ISSUED BY LONDON MARKET INSURERS**

The above-captioned debtors and debtors-in-possession (collectively “the Debtors,” or “United”) hereby move (the “Motion”) for authority to settle a long-standing insurance coverage dispute by: (i) entering into settlement and release (the “Agreement”) of all pollution and asbestos claims against the London Market Insurers (defined below) under the London Policies (as defined below); (ii) selling back certain policies of insurance severally subscribed to by London Market Insurers (as defined below) free and clear of any pollution or asbestos claims and/or interests in the policies for a gross consideration of \$27 million (the “Buy Back”); (iii) obtaining injunctive relief prohibiting any person from prosecuting any pollution or asbestos insurance coverage claims against the London Market Insurers under the London Policies; (iv) providing adequate protection to parties who prove valid interests in the London Policies by setting aside a fund in an amount not to exceed \$5 million (the “Claims Fund”); and (v) obtaining approval of the notice of the Agreement and Buy Back. In support of this Motion, the Debtors respectfully state as follows.

I. BACKGROUND

A. Jurisdiction and Venue

1. This Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157(b)(1) and 1334(b). This proceeding is a core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A), (M), (N), and (O). Venue of this Motion is proper under 28 U.S.C. §§ 1408 and 1409.

2. The statutory predicates for this Motion are Sections 105, 361 and 363 of the Bankruptcy Code, 11 U.S.C. § 101 *et seq.* (the "Bankruptcy Code") and Rules 2002 and 9019 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules").

B. General Background

On December 9, 2002, (the "Petition Date") UAL Corporation and twenty seven wholly owned direct or indirect subsidiaries, each a Debtor, filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code ("collectively the "Chapter 11 Cases") with the United States Bankruptcy Court for the Northern District of Illinois. The Debtors are continuing to operate their businesses and manage their properties as debtors-in-possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code.

C. The London Market Insurers and the London Policies

United has reached a settlement with Certain Underwriters at Lloyd's, London and Certain London Market Companies (collectively the "London Market Insurers") who severally subscribed to certain hull and liability policies in favor of United for the period October 1, 1956 to October 1, 1998 (the "London Policies"). A list of the London Policies that are presently known is annexed as Exhibit A to this motion and incorporated by reference. A list of the subscribing London Market Insurers that are presently known is annexed as Exhibit B to this motion and incorporated by reference. The settlement would resolve a dispute spanning seven

years in which United has sought reimbursement from the London Market Insurers of amounts incurred by United to remediate environmental damage at various airports sites, and for defense and indemnification for other known or projected environmental liabilities at airport sites and other locations.

Under the Buy Back transaction, which is similar to the buyback approved by this Court in the Allied Products case,¹ United proposes to sell the London Policies under Bankruptcy Code Section 363 to the issuing London Market Insurers free and clear of any pollution or asbestos claims and/or interests in the London Policies for a gross consideration of \$27 million. Insolvency and non-participation of certain London Market Insurers and the inability to identify certain of the subscribing insurers will reduce the actual payment initially received immediately from the settlement by approximately \$5.5 million, yielding a net payment of approximately \$21.5 million.²

United considers the terms of the Buy Back transaction to be in the best interest of the estate because of the anticipated expense and delay of protracted litigation, the substantial litigation risk inherent in United's claims, and the indeterminate value of the London Policies. See generally Affidavit of Clifford Hew ("Hew Aff.," attached hereto as Exhibit C) ¶¶ 30-42.

The value of the London Policies is constrained by their unique structure. One set of policies, incepting October 1, 1956 and ending October 1, 1969, consists of excess policies, providing coverage on a per occurrence basis, for hull and liability claims in amounts that exhaust primary limits of \$500,000 per occurrence. Primary coverage was provided during this period by another insurer, United States Aviation Underwriters, with whom United previously reached settlement. The London Policies provided per occurrence limits during this period in

¹ See Case No. 00-B-28798 (Docket No. 2472, Order Approving Buyback Transaction).

² United anticipates substantial recovery from the insolvent insurers, payable over a period of several years.

amounts ranging from \$15 million in 1960 to \$75 million in 1969. The London Market Insurers contend that United has not exhausted the \$500,000 primary limit as to each “occurrence” – defined by the insurers as each instance of fuel leakage, for example – and therefore for most of United’s claims, their excess policies during this period are not triggered.

A second set of London Policies covered by the United settlement comprises policies incepting June 1, 1970 and ending October 1, 1998. In this period, the London Market Insurers wrote hull and liability coverage on a quota share basis, with each insurer subscribing severally to a discrete percentage of the first dollar of risk. For example, in 1970, United purchased \$50 million in coverage, of which the London Market Insurers assumed 45% of each dollar of coverage, United States Aviation Underwriters assumed 35%, and other insurers assumed 20%. Because these percentages varied from year to year, each of United’s environmental claims may be entitled to different percentages of coverage from the London Market Insurers. United estimates that the London Market Insurers’ aggregate share of United’s hull and liability insurance coverage during this period is approximately 50%.

D. United’s Environmental Claims

Over the past fifteen years, United has incurred substantial expense to investigate and remediate soil and ground water and to provide engineering and monitoring reports by order of state environmental agencies or responsible airport authorities. To date, United has incurred in excess of \$78 million in such costs. See Affidavit of Daniel Tisoncik (“Tisoncik Aff.,” attached hereto as Exhibit D) ¶7. In addition, United will incur response costs in the future. United has reserved \$45 million for all future environmental expenses, including response costs associated with historic releases. Tisoncik Aff. at ¶ 7.

As United was compelled to perform such cleanup work, United tendered its claims to its insurers, including the London Market Insurers, for defense and indemnification. Hew. Aff. at ¶19. The London Market Insurers have reserved their rights or denied coverage on virtually all of the tendered claims. *Id.* at ¶¶20-22. The insurers have interposed numerous defenses and exclusions, including the various forms of pollution exclusions found in the London Market Policies. *Id.* at ¶¶20. United's London Policies purchased during the period 1970 through 1985 incorporated an exclusion for environmental claims, with the exception of claims arising from "sudden and accidental" pollution events. This limited "sudden and accidental" form of the pollution exclusion was replaced in 1985 with a stronger form of pollution exclusion drafted by the London Market Insurers for the aviation market, designated AVN 46. Although United has vigorously disputed their interpretation, the London Market Insurers regard this current form of pollution exclusion as "absolute." Other defenses alleged include late notice, the lack of "fortuity" regarding jet fuel releases, and the absence of proof of releases in the relevant policy periods.

E. Delay of Settlement May Negatively Affect United's Interests.

As noted above, many of the largest London Market Insurers subscribing to United's policies have filed schemes of arrangement in the United Kingdom (a procedure similar to bankruptcy), with bar dates for filing claims and a wide range of payment terms. These insolvent (and in some cases solvent) insurers may seek to avoid payment of amounts allocated to them under the proposed settlement. United anticipates that over time additional London Market Insurers may seek protection under a scheme of arrangement or other insolvency proceedings, further reducing United's potential recoveries.

Where necessary, United has preserved its rights of recovery against insolvent London Market Insurers, including the filing of the equivalent of proofs of claim with the scheme administrators. In fact, United has recently received distributions on claims filed with two insurers – Aviation & General Insurance Co. (under scheme of arrangement) and Andrew Weir (under scheme of arrangement) – totaling approximately \$950,000 and \$80,000, respectively. These funds are being held in escrow for the benefit of United, pending approval of this Motion.

It is also relevant to this Motion that the Lloyd's syndicates subscribing to the London Policies have been relieved of liability by order of English courts who approved the appointment of an entity known as Equitas to assume and run off all environmental and asbestos liabilities for policies placed in the London Market prior to 1993. Equitas has limited funds and a mandate to close its books as soon as possible. Thus, United could not be guaranteed a recovery from Equitas should United fail to settle with the London Market Insurers promptly.

Therefore, in light of the defenses and exclusions asserted by the London Market Insurers, the limited coverage attributable to the London Policies based upon United's claims, and the desire to avoid protracted litigation over which there is no guarantee of success, United determined that the Buy Back transaction at the proposed settlement amount was favorable to the estate at this time. See Hew Aff. at ¶¶27, 30-42, 46.

F. Summary of Agreement³

The Agreement provides, in summary, for the following terms and conditions:

1. The London Market Insurers will pay to United and United will accept a gross amount of \$27,000,000.00 in full satisfaction of all past and future pollution and asbestos claims. Of this amount, approximately \$1 million has been paid already, and is being held in escrow by United's outside counsel pending approval of this Motion. Of the remaining \$26.5 million,

United expects to receive approximately \$20.5 million within the time periods specified within the Agreement.

2. United will place \$5,000,000.00 of the net proceeds in a separate account (the "Claims Fund") to provide adequate protection to parties who prove valid interests in the policies (each an "Environmental/Asbestos Claim" that are asserted timely as provided in the Notice). To assert a "valid" pollution or asbestos claim for purposes of the Claim Fund, a potential claimant must demonstrate: (a) a valid legal interest in the London Policies, either as an additional insured or as the holder of a final non-appealable judgment, or allowed claim, against United; (b) it has adequately verified the amount of its pollution or asbestos claim using commercially accepted and reliable cost accounting and estimation procedures, and (c) its claim is covered under specific London Policies. United will maintain the Claims Fund until such time as there is a full and final disposition of all claims in the Debtors' Bankruptcy Estate, or a period not to exceed 18 months from the date of Court approval of this Agreement, whichever occurs first. The Claims Fund may be used to pay any and all Environmental/Asbestos Claims, in United's sole discretion and in accordance with the Debtor's Plan of Reorganization and the Bankruptcy Code. Upon the disposition of all claims in the Bankruptcy, or the passage of eighteen months from the date of approval of the Settlement Agreement, whichever occurs first, the balance of the Claims Fund (if any) will revert to United.

3. Entry of a permanent mandatory injunction directing that neither United nor any other person, including but not limited to any named insured, creditor, or additional insured under the London Policies, may bring a claim or present a demand for insurance coverage for pollution or asbestos claims as to, against, or related to the London Market Insurers under the London Policies. This term is vital to the London Market Insurers, whose primary concern in

³ Attached hereto as Exhibit E is a term sheet outlining the terms of the Agreement.

entering this settlement was to prevent future pollution and/or asbestos claims from being asserted by third parties after the London Market Insurers had paid United. Absent such injunctive protection, the London Market Insurers would require indemnification from United against third party claims -- a term rejected by United as contrary to the interests of the estate.

4. The Agreement includes a full release between the parties with respect to claims concerning pollution or asbestos. Pursuant to the Agreement, United specifically releases any right to present claims under the London Policies for past or future pollution and asbestos claims in connection with the London Policies. Pollution is broadly defined in the Agreement to include all forms of actual, alleged or threatened damage, injury or harm to any land, soil, air or water. The release of such claims against each of the subscribing London Market Insurers contained in the Agreement shall become effective as to each London Market Insurer only upon receipt of the full amount allocated to such Insurer. Accordingly, upon Court approval and final payment, no other person, including but not limited to any other named insured, creditor and/or additional insured can bring a claim against the London Market Insurers under the London Policies with respect to pollution or asbestos claims.

II. Relief Requested

United seeks a Court order approving: (i) United's entry into the Agreement settling and releasing all pollution and asbestos claims against the London Market Insurers under the London Policies; (ii) the London Market Insurers Buy Back of the London Policies free and clear of any pollution or asbestos claims and/or interests in the policies for a gross consideration of \$27 million; (iii) entry of a permanent mandatory injunction prohibiting any person from prosecuting any pollution or asbestos insurance coverage claims against the London Market Insurers under

the London Policies; (iv) the Claims Fund as adequate protection for parties who prove valid interests in the London Policies; and (v) the notice of the Agreement and Buy Back.

A. The Agreement Is In The Best Interest of United's Creditors

United's compromise of its claims against the London Market Insurers satisfies Fed. R. Bankr. P. 9019(a), and should be approved under the standards articulated in Protective Comm. for Indep. Stockholders of TMT Trailer Ferry, Inc. v. Anderson, 390 U.S. 414, 424 (1968); see also, In Re American Reserve Corp., 841 F.2d 159, 161 (7th Cir. 1987) (noting that benchmark for determining propriety of bankruptcy settlement is whether settlement is in the best interest of the estate); Depoister v. Mary M. Holloway Found., 36 F.3d 582, 585-88 (7th Cir. 1994) ("In conducting a hearing under Rule 9019(a), the bankruptcy court is to determine whether the proposed compromise is fair and equitable...and in the best interest of the bankruptcy estate.") (citations omitted). This Court has set forth the following factors that must be addressed in determining the fairness and adequacy of any proposed compromise of a bankruptcy estate's claims: (1) the probability of success in litigation; (2) the complexity of the litigation; (3) the expense, inconvenience and delay necessarily attendant to litigation; and (4) the possibility that litigation will consume assets of the estate that would otherwise be distributable to creditors. In re Universal Electric Sign Co., 255 B.R. 732, 734 (Bankr. E.D. Wis. 2000).

It is equally well settled that a proposed settlement need not be the best result that the debtor could have achieved. In re Energy Co-op., Inc., 886 F.2d 921 (7th Cir. 1989). Rather, the settlement is approvable so long as it "fall[s] within the reasonable range of litigation possibilities", see In re Artra Group Inc., 300 B.R. 699, 702 (Bankr. N.D. Ill. 2003) (citation omitted).

As set forth in the Affidavits of Clifford Hew and Tisoncik, all of these factors militate in favor of approval of the Agreement. The London Market Insurers have been vigorously defending against suits and demands for decades, from United as well as from other airlines, and other types of insureds, seeking to hold the London Market Insurers liable for insurance coverage for historic environmental contamination. There are reasonable doubts with respect to United's claims for coverage that could substantially impact United's recovery from the London Market Insurers. In light of the insurer's coverage defenses and the increasing resort of the London Market Insurers to insolvency proceedings, the amount to be received by United under the Buy Back transaction represents, in United's business judgment, a fair settlement of all claims. See Hew Aff. at ¶¶ 30-42.

The Debtors have determined that the Agreement is in the best interest of their respective estates and creditors. The significant expense and delay that would be occasioned by litigation, including the strong likelihood of appeals, would be substantial. It is undeniable that the claims that Debtors have asserted against the London Policies present complex non-bankruptcy law issues. While the debtors are confident in their positions on these legal issues, given the number of policies, defenses, sites and claims involved, litigation presents significant uncertainty as to the resolution of these claims with a high cost. Because of the availability of injunctive relief against future suits concerning insurance coverage for pollution or asbestos claims regarding the London Policies, the Agreement provides for United to be paid a sum certain and ensures that United will not face liability for indemnity claims that the insurers could otherwise assert. Additionally, the exposure for indemnity claims could theoretically exceed the settlement amount. By executing the Agreement, Debtors will avoid further litigation and the costs and

uncertainties that attend it. Therefore, the Motion for Approval of the settlement and Buy Back should be granted.

B. The Debtors' Entry Into The Buy Back of The London Policies Is The Product Of A Proper Exercise Of The Debtors' Business Judgment

Section 363 of the Bankruptcy Code provides that a debtor, "after notice and a hearing, may use, sell or lease, other than in the ordinary course of business, property of the estate." 11 U.S.C. § 363(b). To approve the use, sale or lease of property outside of the ordinary course of business, this Court need only determine that the Debtors' decision to enter into the Agreement and Buy Back of the London Policies is supported by an articulated business justification. See, e.g., In re Schipper, 933 F.2d 513, 515 (7th Cir. 1991); Committee of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.), 722 F.2d 1063, 1070 (2d Cir. 1983); see also Stephens Indus., Inc. v. McClung, 789 F.2d 386, 389-90 (6th Cir. 1986); In re Abbott Dairies of Pa, Inc., 788 F.2d 143, 145-47 (3d Cir. 1986); In re Continental Airlines, Inc., 780 F.2d 1223, 1226 (5th Cir. 1986); In re Telesphere Communications Inc., 179 B.R. 544, 552 (Bankr. N.D. Ill. 1999); In re Delaware & Hudson R.R. Co., 124 B.R. 169, 175-76 (D. Del. 1991). In re Engineering Prods., Co., 121 B.R. 246, 247 (Bankr. E.D. Wis. 1990) (noting that Courts apply a 'business justification' standard to motions seeking to use or sell property outside the ordinary course of business).

A court will authorize a debtor to sell property of the estate pursuant to section 363(b)(1) of the Bankruptcy Code when the transaction meets the "sound business judgment" test articulated by the courts. A transaction meets this test when:

1. There is a sound business reason for the transaction;
2. The interested parties received adequate notice, including full disclosure of the terms of the deal;

