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12 Company Asbestos Settlement Trust

13 UNITED STATES BANKRUPTCY COURT
14 CENTRAL DISTRICT OF CALIFORNIA
15 LOS ANGELES DIVISION

16 In re) Chapter 11
17)
18 THORPE INSULATION COMPANY,¹) Case No. LA 07-19271-BB
19)
20 Debtor.) Jointly Administered with Case No. 2:07-
21) 20016-BB
22)
23) **THIRD ANNUAL REPORT AND**
24) **ACCOUNTING, AUDITED FINANCIAL**
25) **STATEMENTS, AND CLAIM REPORT**
26)
27) **Hearing:**
28)
Hearing Date: June 5, 2013
Hearing Time: 10:00 a.m.
Place: Courtroom 1475
255 E. Temple St., 14th Floor
Los Angeles, CA 90012

¹ The Debtors are Thorpe Insulation Company, a California corporation, 5608 Bayshore Walk, Long Beach, CA 90803, Fed. Tax I.D. No. 95-1559386 (Main Debtor) and Pacific Insulation Corporation, 2741 South Yates Ave., Los Angeles, CA 90040, Fed Tax I.D. No. 95-4812741.

1 **TO THE HONORABLE UNITED STATES BANKRUPTCY JUDGE AND OTHER**
2 **PARTIES IN INTEREST:**

3 The Trustees of the Thorpe Insulation Company Asbestos Settlement Trust by and
4 through their counsel, Stutman, Treister & Glatt, hereby file the Third Annual Report and
5 Accounting, Audited Financial Statements, and Claim Report.

6
7 DATED: April 30, 2013

8 Respectfully submitted,

9 /s/ Gabriel I. Glazer
10 EVE H. KARASIK, and
11 GABRIEL I. GLAZER, Members of
12 STUTMAN, TREISTER & GLATT
13 PROFESSIONAL CORPORATION

14 Bankruptcy Counsel for the Thorpe Insulation
15 Company Asbestos Settlement Trust
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1 **THIRD ANNUAL REPORT AND ACCOUNTING OF THORPE INSULATION**
2 **COMPANY ASBESTOS SETTLEMENT TRUST**

3 The Trustees of the Thorpe Insulation Company Asbestos Settlement Trust ("Trust")
4 hereby submit this Third Annual Report and Accounting (the "Annual Report") covering Trust
5 activities that occurred during the period from January 1, 2012 to and including December 31, 2012
6 (the "Accounting Period") and cover certain activities of the Trust that took place outside the
7 Accounting Period. This Annual Report is submitted to the United States Bankruptcy Court for the
8 Central District of California, Los Angeles Division, *In re Thorpe Insulation Company, In re Pacific*
9 *Insulation Company, Debtors*, Case Nos. 2:07-19271-BB and 2:07-20016-BB (jointly administered
10 under Case No. 2:07-20016-BB) in accordance with the Fifth Amended Joint Plan of Reorganization
11 of Thorpe Insulation Company and Pacific Insulation Company (the "Plan"); Order Confirming Fifth
12 Amended Joint Plan of Reorganization of Thorpe Insulation Company and Pacific Insulation
13 Company dated February 1, 2010 ("Confirmation Order"); this Court's *Order Approving Continued*
14 *Operation of the Thorpe Insulation Company Asbestos Settlement Trust in the Ordinary Course of*
15 *Business Pending Further Instruction* entered on February 28, 2012 (the "First Continued Operations
16 Order") and *Order Approving Post-Remand Report, Recommendation and Petition for Instructions*
17 *Regarding the Thorpe Insulation Company Asbestos Settlement Trust* entered on July 11, 2012 (the
18 "Second Continued Operations Order" and collectively, the "Post-Remand Operation Orders"); the
19 Trust Agreement, Bylaws, Trust Distribution Procedures, and Case Valuation Matrix, as amended
20 from time to time, established pursuant to the Plan,² and pursuant to the laws of the State of Nevada,
21 where the Trust is organized and where it resides. The factual statements in this Annual Report are
22 supported by the Declaration of Sara Beth Brown, Executive Director, in Support of Motion to
23 Approve and Settle Thorpe Insulation Settlement Trust's Annual Report and Accounting, Audited
24

25 ² The Appendix includes the Plan; Confirmation Order; Post-Remand Operations Orders; Sixth Amendment to and
26 Complete Restatement of Thorpe Insulation Company Asbestos Settlement Trust Agreement ("Trust Agreement");
27 First Amendment to and Complete Restatement of Thorpe Insulation Company Asbestos Settlement Trust Bylaws
28 ("Trust Bylaws"); Second Amendment to and Complete Restatement of Thorpe Insulation Company Asbestos
Settlement Trust Case Valuation Matrix ("Matrix"); Third Amendment to and Complete Restatement of Thorpe
Insulation Company Asbestos Personal Injury Settlement Trust Distribution Procedures ("TDP"); other controlling
documents approved by this Court; and other documents as indicated.

1 Financial Statements, and Claim Report as described in paragraphs 6, 7, and 8 *infra*. Capitalized
2 terms not defined herein are as defined in Article 1 of the Plan.

3 1. Effective Date: As stated above, on February 1, 2010, this Court entered the
4 Confirmation Order. On February 16, 2010, certain of Thorpe's non-settling insurers filed appeals
5 from the Confirmation Order. Following the denial of requests to stay the Confirmation Order by
6 each of the United States District Court for the Central District of California (the "District Court"),
7 the United States Court of Appeals for the Ninth Circuit (the "Ninth Circuit"), and Supreme Court
8 Justice Anthony M. Kennedy, the Plan became effective and the Trust was established. On January
9 24, 2012, the Ninth Circuit issued an Opinion in the Plan Appeal (as amended following the petition
10 for rehearing described below, the "Opinion"). The Opinion: (a) affirmed this Court's rulings on a
11 number of issues, (b) concluded that, "[a]lthough the plan has proceeded to a point where it may be
12 inequitable to toss it out entirely, we also conclude that there are likely viable remedies available to
13 Appellants, short of entirely tossing the plan out, within the broad remedial discretion of the
14 bankruptcy court, if it determines that Appellants' claims (discussed in footnote one) have merit;"
15 and (c) "reverse[d] the judgment of the district court, and remand[ed] [the matter] to the district court
16 with instructions that it remand to the bankruptcy court to permit Appellants to submit their proof on
17 all issues they previously preserved."

18 On February 7, 2012, Thorpe, the Official Committee of Unsecured Creditors
19 appointed in Thorpe's bankruptcy case and the Futures Representative filed a petition for rehearing
20 in the Plan Appeal. That petition was denied on April 3, 2012, and the Ninth Circuit issued its
21 mandate to the District Court on April 12, 2012, with instructions that it remand the matter to this
22 Court. The Opinion became final on July 2, 2012.

23 After issuance of the Opinion, on February 28, 2012 and July 11, 2012, this Court
24 entered the Post-Remand Operations Orders which authorized the Trust to continue paying claims
25 during the post-remand period. The First Continued Operations Order provided that the Trust could
26 pay up to \$5,000,000 in claims. The Trust implemented a program to make partial payments to as
27 many claimants as possible while conserving Trust resources consistent with the Continued
28 Operations Order. The Second Continued Operations Order removed the \$5,000,000 cap on claims

1 payments during the post-remand period, subject to future order of this Court.

2 On December 14, 2012, Thorpe and certain related entities entered in to a global
3 settlement with Century Indemnity Company, Century National Insurance Company of Omaha, and
4 Motor Vehicle Casualty Company (collectively, the "Century Insurers"). Soon after, on February
5 13, 2013, Thorpe and certain related entities entered into global settlement agreements with the two
6 remaining non-settling insurers: (i) The Continental Insurance Company and National Fire
7 Insurance of Hartford ("CNA"), and (ii) Middlesex Insurance Company ("Middlesex").

8 Having reached these settlements, Thorpe commenced the process to confirm its
9 "Sixth Amended Joint Plan of Reorganization of Thorpe Insulation Company and Pacific Insulation
10 Company (Following Remand)," which would also effectuate the settlements (the "Sixth Amended
11 Plan"). Thorpe filed the Sixth Amended Plan (See Docket No. 3397) and various related documents
12 on March 20, 2013. The confirmation hearing on the Sixth Amended Plan is scheduled for May 1,
13 2013.

14 2. Appointment of Trustees: In the Confirmation Order, this Court approved the
15 appointment of Mr. John F. Luikart and Dr. Sandra R. Hernandez as the Trustees of the Trust, who
16 have acted in that capacity since the Effective Date of the Trust.

17 Pursuant to Section 4.1 of the Trust Agreement, the number of Trustees was increased
18 to three (3) on January 11, 2011, and on February 17, 2011, Mr. Stephen M. Snyder was appointed
19 to serve as the third Trustee. Mr. Snyder has acted as a Trustee of the Trust since February 17, 2011.
20 Further, on April 21, 2011, in accordance with Section 4.1 of the Trust Agreement, Mr. Snyder was
21 designated by the other two Trustees as Managing Trustee, with the consent of the Trust Advisory
22 Committee and Futures Representative.

23 3. Appointment of Trust Advisory Committee ("TAC"): Pursuant to Section 6.1
24 of the Trust Agreement, Alan R. Brayton, Ron C. Eddins, David McClain, Jerry Neil Paul, and
25 David A. Rosen were designated as the initial members of the TAC. Mr. Brayton was elected Chair
26 of the TAC by its members on October 25, 2010, and has served in that capacity since that time.
27 Messrs. McClain, Paul and Rosen continued to serve as members of the TAC during the Accounting
28 Period. In early January 2012, Mr. Eddins passed away. Pursuant to Section 6.4 of the Trust

1 Agreement, Peter A. Kraus was selected by a majority vote of the Trustees to succeed the late Mr.
2 Eddins as a member of the TAC. The selection of Mr. Kraus to replace the late Mr. Eddins as a
3 member of the TAC was approved by this Court on July 11, 2012.

4 4. Appointment and Continuation of Futures Representative: The Honorable
5 Charles B. Renfrew was appointed as the Futures Representative in the Bankruptcy Case on
6 December 20, 2007 and has continued to act in that capacity since the Effective Date of the Trust.

7 5. Fiscal Year and Tax Obligations: The Trust is required by the Internal
8 Revenue Code to account for and report on its activities for tax purposes on a calendar-year basis.
9 Therefore, the Trust's fiscal year is the calendar year. Section 2.2(b) of the Trust Agreement requires
10 the Trustees to file income tax and other returns and statements in a timely manner, and comply with
11 all withholding obligations as legally required, including fulfilling requirements to maintain the
12 Trust's status as a Qualified Settlement Fund. The federal tax return for 2012 will be filed on or
13 before September 16, 2013. The Trust resides in Nevada, and Nevada has no state income tax.
14 Although the Trust is not subject to tax in California, the Trustees file a tax return in California,
15 attaching a copy of the Trust's federal tax return but showing no California taxable income or state
16 tax liability.

17 6. Annual Report: Section 2.2(c)(i) of the Trust Agreement provides in pertinent
18 part:

19 The Trustees shall cause to be prepared and filed with the Bankruptcy
20 Court . . . an annual report containing financial statements of the Trust
21 (including, without limitation, a statement of the net claimants' equity
22 of the Trust as of the end of such fiscal year and a statement of
23 changes in net claimants' equity for such fiscal year) audited by a firm
24 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 principals generally accepted in the United
States, except for the special-purpose accounting methods

25 The Trust's financial statements are prepared using special-purpose accounting methods that depart
26 from Generally Accepted Accounting Principles (GAAP) in certain instances in order to better
27 disclose the amount and changes in net claimant's equity.

28 7. Financial Report: In accordance with the requirements of Section 2.2(c)(i) of

1 the Trust Agreement, the Trust has caused its accounts to be audited by independent certified public
2 accountants, Grant Thornton, LLP. The Trust's audited financial statements ("Audited Financial
3 Statements") are attached hereto as Exhibit "A". These include a Statement of Net Claimants'
4 Equity, a Statement of Changes in Net Claimants' Equity, a Statement of Cash Flows and
5 explanatory Notes. The Statement of Net Claimants' Equity, which is the equivalent of a corporate
6 balance sheet, reflects total assets of the Trust at market value and on the other comprehensive basis
7 of accounting utilized by the Trust. These Audited Financial Statements show, among other things,
8 that as of December 31, 2012, total Trust assets were \$153,010,305, total liabilities were \$6,385,068,
9 and Net Claimants' Equity was \$146,625,237.

10 8. Claim Report: Section 2.2(c)(ii) of the Trust Agreement provides that along
11 with the Audited Financial Statements, the Trustees shall file with the Court a report containing a
12 summary regarding the number and type of claims disposed of during the period covered by the
13 financial statements. The Thorpe Insulation Settlement Trust Claim Report As Of December 31,
14 2012 ("Claim Report") is attached hereto as Exhibit "B". During the Accounting Period, the Trust
15 received 1,397 claims, paid 404 claims, and made settlement offers on 525 claims. Since the Trust
16 received its first Trust Claim,³ the Trust has received 2,575 Trust Claims, paid 912 Trust Claims, and
17 153 Trust Claims have been withdrawn.⁴

18 Section 5.4 of the TDP provides that, "As soon as practicable after the Effective Date,
19 the Trust shall pay all Trust Claims that were liquidated by (i) a settlement agreement entered into
20 prior to the Petition Date for the particular claim, or (ii) a judgment of any kind entered on or before
21 October 15, 2007 (collectively, the "Pre-Petition Liquidated Claims")." As described in the Trust's
22 First Annual Report and Accounting, all Pre-Petition Liquidated Claims were paid by the end of
23 January 2011 in trust to the representative law firms for disbursement to the claimants upon the
24 Trust's receipt and approval of a properly executed release.

25 During the Trustees' meeting on February 8, 2013, it was decided that the Trust shall

26 _____
27 ³ "Trust Claims" are any claims submitted to the Trust after the Effective Date.

28 ⁴ "Withdrawn Claims" include claims which are not qualified and/or claims with deficiencies that have not been cured
beyond a certain time period, and/or claims that have remained on hold beyond a certain time period.

1 be authorized to set aside 250% of the face value of the Term Sheet Settlements, which are the
2 subject of three separate lawsuits styled as follows: (1) *Abma, et al. v. Thorpe Insulation Company*,
3 San Francisco Superior Court Case No. CGC-05-446216; (2) *Boen, et al. v. Thorpe Insulation*
4 *Company*, San Francisco Superior Court Case No. CGC-06-452029; and (3) *Benjamin, et al. v.*
5 *Thorpe Insulation Company*, San Francisco Superior Court Case No. CGC-06-453165 (the “Term
6 Sheet Settlements”), less payments made by the Trust, upon receipt of settlement funds from certain
7 insurers pending final resolution of the Term Sheet Settlements, and the Trust shall also be
8 authorized to enter into an agreement to this effect. At such time as the Trust receives the settlement
9 funds referred to in the agreement, the Trust shall set aside the funds.

10 9. Public Inspection: In compliance with Section 2.2(c)(iii) of the Trust
11 Agreement, the Annual Report, including the Audited Financial Statements and Claim Report, has
12 been provided to the TAC and Futures Representative, filed with the Office of the United States
13 Trustee with responsibility for the Central District of California, Los Angeles Division, and made
14 available for inspection by the public.

15 10. Trustees' Meetings: Article II, Section 4 of the Trust Bylaws provides that the
16 Trustees shall meet in Nevada, or a state other than California, at least four times a year, as close as
17 practicable on a quarterly basis. The Trustees held four meetings during the Accounting Period
18 (February 16, 2012, April 19-20, 2012, September 20-21, 2012, and November 28, 2012). All
19 meetings were held in Reno, Nevada.

20 11. Arbitrations: During the accounting period, no arbitrations were held
21 pursuant to Section 5.9 of the Trust Distribution Procedures.

22 12. Funds Received Ratio: Section 4.2 of the TDP provides for the Trustees to
23 reconsider the Funds Received Ratio on the first day of January after the Plan has been confirmed.
24 As described in the Trust's First Annual Report and Accounting, on November 17, 2010, based upon
25 the analysis and advice of the Trust's expert economist, the Trust, with the consent of the TAC and
26 Futures Representative, set the Initial Funds Received Ratio at 17.5%. The Initial Funds Received
27 Ratio has not changed since that time.

28 13. Maximum Annual Payment: Section 2.4 of the TDP requires that the Trust

1 calculate a maximum annual payment for claims based upon a model of the amount of cash flow
2 anticipated to be necessary over the entire life of the Trust to ensure that funds will be available to
3 treat all present and future claimants as similarly as possible. At the November 28, 2012 meeting,
4 the Maximum Annual Payment for 2013 was set at \$7,600,000, plus the amount of \$47,533,527.33
5 of excess funds carried over from prior years, which Section 2.5 of the TDP requires to be rolled
6 over and remain dedicated to the respective Disease Category in the Jurisdiction to which they were
7 originally located.

8 14. Inflation Adjustment: Section 5.3(d) of the TDP requires that all claims
9 payments be adjusted for inflation annually beginning with the calendar year after the Effective Date
10 of the Trust. Beginning in 2011, all claims payments made during a calendar year include a cost of
11 living adjustment based upon the Federal Bureau of Labor Statistics' *Consumer Price Index for*
12 *Urban Wage Earners and Clerical Workers* (CPI-W) announced in January each year. Thus as of
13 January 1, 2011, all claims payments made during the calendar year were increased by 4.95% to
14 account for inflation.

15 At the November 28, 2012 meeting, the CPI-W to be published in January 2013 was
16 approved for use by the Trust in making the 2013 cost of living adjustment for claims payments.
17 The CPI-W of 1.7% was issued on January 16, 2013. Consequently, all claims payments made
18 during the 2013 calendar year will have a compounded inflation rate of 6.74% added to the payment
19 amount.

20 15. Budget and Cash Flow Projection: Section 2.2(d) of the Trust Agreement
21 requires the Trust to prepare a budget and cash flow projections prior to the commencement of each
22 fiscal year covering such fiscal year and the succeeding four fiscal years. The Trustees approved the
23 2013 budget and the required four-year budget and cash flow projections on November 28, 2012.
24 Pursuant to the Trust Agreement, these were provided to the Approving Entities. The budget for
25 operating expenses in 2013 totals \$1,803,000.⁵

26 16. Trust Facilities and Services Sharing Agreement with Western Asbestos

27 ⁵ This figure is net of claimant payments which are budgeted for \$7,600,000 and net of extraordinary legal fees that
28 are budgeted for \$3,150,000.

1 Settlement Trust: As described in the Trust's First Annual Report and Accounting, the Trust and
2 Western Asbestos Settlement Trust ("Western Trust") entered into a Trust Facilities and Services
3 Sharing Agreement in 2010 and amendments to that agreement were approved on April 21, 2011,
4 with the consent of the Futures Representatives and TAC. The Trust agreed to pay a negotiated
5 monthly amount. Such arrangement was approved by this Court in the order approving the Trust's
6 First Annual Report. The annual reconciliation presented on February 16, 2012 set the Advance
7 Payments at \$35,000 per month for 2012. The annual reconciliation for 2012 was presented on
8 February 7, 2013 and set the Advance Payment at \$29,000 per month for 2013.

9 17. Settlement Fund: The Settlement Fund was established at Wells Fargo Bank,
10 N.A. to pay valid claims.

11 18. Operating Fund: The Operating Fund was established at Wells Fargo Bank,
12 N.A., to pay anticipated operating expenses of the Trust as described in the Trust's Annual Reports.
13 During the Accounting Period, transfers were made from the Settlement Fund to the Operating Fund
14 to pay anticipated operating expenses of the Trust.

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

20 In November of 2010, the Trust established an indemnity fund at Wells Fargo Bank,
21 N.A., in the amount of \$5,000,000, as described in the Trust's First Annual Report and Accounting.
22 All interest earned by the fund is returned to the Trust quarterly. During the Accounting Period, no
23 claims were made against the fund and nothing was paid from the fund.

24 20. Legal Disputes:

25 a. *Thorpe Insulation Co. v. Argonaut Insurance Co., et al.*, Superior Court of the
26 State of California, County of Los Angeles (the "Superior Court"), Case No CGC 05-46682: This
27 case involves an insurance coverage action against Thorpe's insurers. Thorpe has recently concluded
28 settlements with all of the remaining insurers in this action. Accordingly, at the request of the

1 remaining parties, the Court vacated all trial and pre-trial dates, pending final dismissals with
2 prejudice, which are anticipated to be filed upon conclusion of the bankruptcy proceedings described
3 above. Additionally, the arbitration between Thorpe and the Trust, on the one hand, and California
4 Union Insurance Company (“Cal Union”), on the other hand, has been withdrawn in light of the
5 settlement reached with Cal Union.

6 b. *Continental Insurance Company v. Thorpe Insulation Company (In re Thorpe*
7 *Insulation Company)*, United States Court of Appeals for the Ninth Circuit, Case No. 10-55744: On
8 July 21, 2009, this Court entered an order disallowing a claim filed in the Bankruptcy Case by
9 Continental Insurance Company (“Continental”) and denying a motion by Continental that sought to
10 compel Thorpe to arbitrate the dispute over the validity of that claim. Those orders were appealed to
11 the District Court, which affirmed this Court's orders by order entered May 4, 2010, and to the Ninth
12 Circuit. On January 30, 2012, the Ninth Circuit issued its opinion affirming the disallowance of
13 Continental's claim and this Court's denial of Continental's motion to compel arbitration. That
14 matter became final on April 30, 2012. Continental timely filed a Petition for Certiorari in the
15 United States Supreme Court, but the petition was denied on October 1, 2012.

16 Thorpe filed a motion in the Ninth Circuit Court of Appeals for its prevailing
17 attorneys' fees relating to the appeals of the arbitration denials and claim disallowance. Continental
18 opposed that motion. On July 3, 2012, the Ninth Circuit granted in part and denied in part Thorpe's
19 motion, and referred the determination of an appropriate amount of attorneys' fees on appeal to the
20 court's special master.

21 c. *Non-Settling Insurers' Appeals of Orders Related to First and Second Annual*
22 *Report and Second Continued Operations Orders (Case Nos. CV 12-6098 DSF; CV 12-6184DSF;*
23 *CV 12-6441 DSF; and CV 12-6442 DSF)*: In June 2012, this Court entered its orders approving the
24 Trust's 2011 annual report and the order approving the Trust's 2010 annual report, as that order had
25 never been entered. The non-settling insurers appealed the orders approving the Trust's 2010 and
26 2011 annual reports (as well as the Bankruptcy Court's order denying reconsideration of its order
27 approving the Trust's 2010 report) primarily on the grounds that given the Ninth Circuit's reversal of
28 the confirmation order and remand of the case, this Court no longer had jurisdiction to enter such

1 orders.

2 In addition, post-remand, this Court entered the Post-Remand Operations Orders
3 granting, for the most part, the relief requested by the Trust in the two petitions for instructions
4 governing Trust operations during the post-remand period. The non-settling insurers appealed
5 Second Continued Operations Order.

6 All of these appeals have been resolved in connection with the global settlements
7 with the three remaining non-settling insurers. The Trust anticipates that these appeals will be
8 dismissed after the Sixth Amended Plan confirmation process is completed.

9 d. *Settlement Motions Filed in Bankruptcy Court With Respect to the Remaining*
10 *Non-Settling Insurers:* On January 9, 2013, Thorpe filed its "Motion for Order Approving: (I)
11 Settlement with Century Insurers; (II) Sale of Insurance Policies Free and Clear of Claims and
12 Interests; and (III) Modification of Fifth Amended Joint Plan of Reorganization; Post-Remand
13 Petition for Instructions Regarding the Thorpe Insulation Company Asbestos Settlement Trust
14 [Docket No. 3368] (the "Century Settlement Motion"). In the Century Settlement Motion, Thorpe
15 sought approval of a Settlement Agreement that provided for (i) payment to the Trust of \$36 million;
16 (ii) mutual releases and covenants between Thorpe and related entities and Century Insurers; and (iii)
17 the purchase by the Century Insurers of certain Insurance Rights (as such term is defined in the Plan)
18 free and clear of all rights, liens, claims, and interests. Additionally, Thorpe requested approval to
19 modify the Plan to designate the Century Insurers as "Settling Asbestos Insurers" and to effectuate
20 the terms of the Settlement Agreement. On February 6, 2013, this Court entered its order approving
21 the Continental Settlement Motion.

22 On February 13, 2013, Thorpe filed its "Motion for Order Approving: (I) Settlement
23 with Continental Insurers; (II) Sale of Insurance Policies Free and Clear of Claims and Interests; and
24 (III) Modification of Fifth Amended Joint Plan of Reorganization; Post-Remand Petition for
25 Instructions Regarding the Thorpe Insulation Company Asbestos Settlement Trust [Docket No.
26 3368] (the "Continental Settlement Motion"). In the Continental Settlement Motion, Thorpe sought
27 approval of a Settlement Agreement that provided for (i) payment to the Trust of \$45 million; (ii)
28 mutual releases and covenants between Thorpe and related entities, and the CNA; and (iii) the

1 purchase by the CNA of certain Insurance Rights (as such term is defined in the Plan) free and clear
2 of all rights, liens, claims, and interests. Additionally, Thorpe requested approval to modify the Plan
3 to designate the CNA as "Settling Asbestos Insurers" and to effectuate the terms of the Settlement
4 Agreement. On March 12, 2013, this Court entered its order approving the Continental Settlement
5 Motion.

6 Additionally, on February 13, 2013, Thorpe filed a motion seeking similar relief with
7 respect to Middlesex Insurance Company (the "Middlesex Settlement Motion"). In the Middlesex
8 Settlement Motion, Thorpe sought approval of a settlement agreement (the "Middlesex Settlement
9 Agreement") providing for (i) payment to the Trust of \$12 million; (ii) mutual releases and
10 covenants between Thorpe and related entities and Middlesex, and (iii) the purchase by Middlesex of
11 certain Insurance Rights (as such term is defined in the Plan) free and clear of all rights, liens,
12 claims, and interests. In addition, Thorpe requested approval to modify the Plan to designate
13 Middlesex as a "Settling Asbestos Insurer" and to effectuate the terms of the Middlesex Settlement
14 Agreement. On March 12, 2013, this Court entered its order approving the Middlesex Settlement
15 Motion.

16 e. *Thorpe Insulation Company Asbestos Settlement Trust v. Michael J.*
17 *Mandelbrot and Mandelbrot Law Firm*, Case No. 12-02183-BB. During the Accounting Period, the
18 Trust (along with Western Asbestos Settlement Trust (the "Western Trust") and the J.T. Thorpe
19 Settlement Trust (the "J.T. Thorpe Trust"), collectively, the ("Trusts")) continued their audit and
20 investigation (the "Investigation") into matters concerning evidentiary support for certain claims
21 submitted by Michael Mandelbrot and the Mandelbrot Law firm ("Mandelbrot") with the Trusts.
22 The Trusts were concerned that Mandelbrot had engaged in a pattern of submitting unreliable
23 evidence in support of claims provided to the Trust as set forth in section 5.7(a) of the Trust
24 Distribution Procedures. The Bankruptcy Court entered an order on March 14, 2012 granting the
25 J.T. Thorpe Trust's Application for Examination Pursuant to Bankruptcy Rule 2004, pursuant to
26 which the J.T. Thorpe Trust sought authority to conduct the examinations of eight (8) claimants in
27 furtherance of the Investigation. Mandelbrot appealed the order, which appeal was later dismissed by
28 the parties, and has largely refused to voluntarily cooperate with the Trusts in the Investigation. To

1 date, the Trusts have taken only one claimant examination.

2 Thereafter, pursuant to Bankruptcy Court order granted over the objection of
3 Mandelbrot, the Trusts conducted the examination of John Lynch, a former employee of the Western
4 Trust, and Mandelbrot.

5 Notwithstanding the Bankruptcy Court's orders, Mandelbrot demanded the
6 Investigation cease and threatened to directly sue the Trusts, the Trusts' fiduciaries and Trusts'
7 representatives on the grounds that the Investigation was improper or frivolous. Accordingly, on
8 September 19, 2012, the Trust filed its "Complaint for Declaratory Judgment" and on October 24,
9 2012, its "First Amended Complaint for (I) Declaratory Judgment and (II) Equitable Relief" (the
10 "Amended Complaint") in the Bankruptcy Court (Adversary Case No. 2:12-ap-02183-BB) against
11 the Defendants (the "Adversary Proceeding"). The Amended Complaint (i) requests a declaratory
12 judgment from the Bankruptcy Court "confirming that the Investigation to determine whether the
13 Defendants have engaged in a pattern or practice of submitting unreliable information to the Thorpe
14 Insulation Trust is authorized and appropriate under the circumstances," and (ii) seeks related
15 equitable relief.

16 The Adversary Proceeding has been procedurally consolidated with a nearly identical
17 adversary proceeding brought by the J.T. Thorpe Trust in this Court. In addition, the Western Trust
18 commenced a similar adversary proceeding against the Defendants in its bankruptcy case pending in
19 the United States Bankruptcy Court for the Northern District of California. The Trusts and the
20 Western Trust are supervised by the same Trustees and the same Futures Representative, and all
21 three trusts evaluate and process claims through the same facility and processing staff.

22 This Court has ruled on three substantive motions filed by the parties in the
23 Adversary Proceeding. See 2:12-ap-02183-BB Docket Nos. 65 (*Order Granting in Part Motions for*
24 *Approval of Continued Claim Payment by the Thorpe Trusts in Accordance with Additional*
25 *Evaluation Criteria*); 67 (*Order Denying Defendants' Motion to Transfer Venue of Adversary*
26 *Proceedings*); and 73 (*Order Denying Defendants' Motion to Dismiss Second Claim for Relief*). The
27 Bankruptcy Court has held two status conferences in the Adversary Proceeding and the next status
28 conference is set for April 30, 2013. The Bankruptcy Court has set an August 31, 2013 discovery

1 deadline. The parties are presently engaged in discovery efforts.

2 On March 19, 2013, the Futures Representative filed a motion to intervene in the
3 adversary proceedings. See Docket No. 83 (*The Futures Representative's Notice of Motion and*
4 *Motion to Intervene; Memorandum of Points and Authorities*). Defendants opposed the motion and
5 a hearing was held on April 9, 2013. On April 10, 2013, the Bankruptcy Court entered its order
6 approving the Honorable Charles B. Renfrew's motion to intervene. See Docket No. 96 (*Order*
7 *Granting the Futures Representative's Motion to Intervene*). The Futures Representative then filed
8 his *Complaint in Intervention* (Docket No. 97) on April 10, 2013.

9 21. Amendments to the Trust Documents: During the Accounting Period, there
10 were no amendments to the Trust Documents. However, on February 7, 2013, Section 4.1 of the
11 Trust Agreement was amended to reflect that if the Trustees cannot agree by a majority vote, that the
12 dispute shall be resolved by the Bankruptcy Court. A copy of the *Seventh Amendment to and*
13 *Complete Restatement of Thorpe Insulation Company Asbestos Settlement Trust Agreement* is
14 included in the Appendix filed herewith.

15 22. Notifications to Beneficiaries: During the Accounting Period and,
16 additionally, from January 1, 2013 to and including April 15, 2013, the following notifications were
17 placed on the Trust's web site:

18 a. Notice regarding actions by Thorpe Insulation Settlement Trust in light
19 of Opinion (posted February 28, 2012);

20 b. Notice regarding hearing on Trust's Second Annual Report and
21 Accounting (posted April 27, 2012); and

22 c. Notice of modification to the TIST Site List (posted October 17,
23 2012).

24 23. Filing Fee: Pursuant to Section 6.4 of the TDP, the filing fee was reviewed at
25 the September 20, 2012 meeting and there were no recommended changes to the existing \$250.00
26 fee during the Accounting period or as of the date hereof.

27 24. Trustees' Compensation: Section 4.5(c) of the Trust Agreement requires the
28 Trusts to report the amounts paid to the Trustees for compensation and expenses. During the

1 Accounting Period, the Trustees each received per annum compensation in the amount of \$40,000
2 paid in quarterly installments. The total paid to all Trustees for hourly compensation was \$283,519
3 and \$13,272 was the total amount of expenses incurred by all Trustees.

4 25. Significant Vendors:

5 Although the Trust has many vendors, those who were paid more than \$100,000
6 during the Accounting Period are listed alphabetically below:

- 7 a. Clark & Trevithick: Counsel to the Reorganized Debtor.
8 b. Fergus, a Law Office: Counsel to the Honorable Charles Renfrew, Futures
9 Representative.
10 c. Jones Day: Co-counsel to the TAC.
11 d. Klee, Tuchin, Bogdanoff & Stern LLP: Counsel to the Debtors and now
12 counsel to the Trust in the pending appeals as described in paragraph 20, *supra*.
13 e. Morgan Lewis & Bockius LLP: Counsel to Debtors and now counsel to the
14 Trust in the pending insurance coverage litigation and the Mandelbrot Litigation, as described in
15 paragraph 20, *supra*.
16 f. Pachulski Stang Ziehl & Jones LLP: Counsel to the Debtors.
17 g. Snyder Miller & Orton, LLP: Counsel to the Debtors and former counsel to
18 the Trust in the pending insurance coverage litigation as described in paragraph 20, *supra*.
19 h. Stutman, Treister & Glatt P.C.: Bankruptcy counsel to the Trust.
20
21 i. Western Asbestos Settlement Trust for shared services pursuant to the Trust
22 Facilities and Services Sharing Agreement, as described in paragraph 16, *supra*.

23 26. Trust Investment Management: Article 3 of the Trust Agreement authorizes
24 the Trust to administer the investment of funds in the manner in which individuals of ordinary
25 prudence, discretion and judgment would act in the management of their own affairs, subject to
26 certain limitations. The Trust closely monitors any market volatility with its investment advisors
27 and continues to be in compliance with its Investment Policy Statement. Callan Associates, Inc.
28 continued to assist the Trust during the Accounting Period as its manager of investment managers.

1 BlackRock Financial Management, Inc., Eagle Capital Management, LLC, Harding Loevner, LP,
2 and State Street Global Advisors have continued to act as the Trust's investment managers. On
3 February 16, 2012, it was determined that the Trust would engage Westwood Management
4 Corporation as an additional investment manager for the Trust and on September 1, 2012, Segall
5 Bryant & Hammill replaced Dwight Asset Management Company as the Trust's taxable fixed
6 income manager.

7 The Trust's Investment Policy Statement was amended on February 16, 2012 and
8 November 28, 2012, copies of which are included in the Appendix filed herewith.

9 In addition, pursuant to the Trust's Investment Policy Statement at page 3, a formal
10 asset allocation study was prepared by Callan Associates and presented to the Trustees and
11 Executive Director on March 25, 2013.

12 ***

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

EXHIBIT A



Financial Statements and Report of Independent
Certified Public Accountants

Thorpe Insulation Settlement Trust

December 31, 2012 and 2011

Contents

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Report of Independent Certified Public Accountants

Trustees
Thorpe Insulation Settlement Trust

We have audited the accompanying financial statements of Thorpe Insulation Settlement Trust (“the Trust”), organized in the State of Nevada, which comprise the statements of net claimants’ equity as of December 31, 2012 and 2011, and the related statements changes in net claimants’ equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management’s responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Trust’s other basis of accounting; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor’s responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Trust’s preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust’s internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the assets and liabilities of Thorpe Insulation Settlement Trust as of December 31, 2012 and 2011, and the changes in net claimants' equity and cash flows for the years then ended in accordance with the Trust's other basis of accounting.

Basis of accounting

We draw attention to Note A.2 of the financial statements, which describes the basis of accounting. The financial statements are prepared on the Trust's other basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Supplementary information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The Schedule of Operating Expense for the years ended December 31, 2012 and 2011 is presented for purposes of additional analysis and is not a required part of the financial statements. Such supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures. These additional procedures included comparing and reconciling the information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Restriction on use

Our report is intended solely for the information and use of the management of the Trust and Trustees, the beneficiaries of the Trust, the Futures Representative, the Futures Counsel, the members of the Trust Advisory Committee, and the United States Bankruptcy Court for the Central District of California, Los Angeles Division and is not intended to be and should not be used by anyone other than these specified parties.

Grant Thornton LLP

Reno, Nevada
April 15, 2013

Thorpe Insulation Settlement Trust

STATEMENTS OF NET CLAIMANTS' EQUITY

December 31,

| | <u>2012</u> | <u>2011</u> |
|---|-----------------------|-----------------------|
| ASSETS | | |
| Cash and cash equivalents and investments available-for-sale | | |
| Restricted | \$ 5,000,000 | \$ 5,000,000 |
| Unrestricted | <u>134,353,197</u> | <u>142,059,732</u> |
| Total cash and cash equivalents and investments | 139,353,197 | 147,059,732 |
| Accrued interest and dividend receivables | 727,108 | 13,971 |
| Deferred tax asset | <u>11,002,000</u> | <u>10,038,000</u> |
| Total assets | <u>\$ 151,082,305</u> | <u>\$ 157,111,703</u> |
| LIABILITIES | | |
| Accrued expenses | \$ 935,185 | \$ 916,710 |
| Claim processing deposits | 465,250 | 234,000 |
| Unpaid claims (Note D) | | |
| Outstanding offers | 4,636,633 | 3,455,127 |
| Facility and staff sharing agreement payable | <u>348,000</u> | <u>420,000</u> |
| Total liabilities | <u>\$ 6,385,068</u> | <u>\$ 5,025,837</u> |
| NET CLAIMANTS' EQUITY | <u>\$ 144,697,237</u> | <u>\$ 152,085,866</u> |

The accompanying notes are an integral part of these statements.

Thorpe Insulation Settlement Trust

STATEMENTS OF CHANGES IN NET CLAIMANTS' EQUITY

For the years ended December 31,

| | <u>2012</u> | <u>2011</u> |
|---|------------------------------|------------------------------|
| Net claimants' equity, beginning of year | \$ 152,085,866 | \$ 84,998,600 |
| Additions to net claimants' equity | | |
| Initial funding | 4,500,000 | 83,000,000 |
| Investment income | 1,739,384 | - |
| Provision for income taxes, deferred | 964,000 | 1,292,000 |
| Net decrease in facilities and staff sharing agreement | 72,000 | - |
| Net realized/unrealized gains on available-for sale securities | 4,902,521 | - |
| Total additions | <u>12,177,905</u> | <u>84,292,000</u> |
| Deductions from net claimants' equity | | |
| Operating expenses | 4,924,672 | 4,003,183 |
| Court ordered bankruptcy fees | - | 383,756 |
| Claims settled | 13,460,356 | 10,744,411 |
| Investment fees | - | 2,220 |
| Net increase in outstanding claim offers | 1,181,506 | 2,023,164 |
| Net increase in facility and staff sharing agreement | - | 48,000 |
| Total deductions | <u>19,566,534</u> | <u>17,204,734</u> |
| Net claimants' equity, end of year | <u>\$ 144,697,237</u> | <u>\$ 152,085,866</u> |

The accompanying notes are an integral part of these statements.

Thorpe Insulation Settlement Trust

STATEMENTS OF CASH FLOWS

For the years ended December 31,

| | <u>2012</u> | <u>2011</u> |
|--|-----------------------|-----------------------|
| Cash inflows: | | |
| Initial funding | \$ 4,500,000 | \$ 83,000,000 |
| Investment income receipts | 1,026,247 | - |
| Increase in claim processing deposits | 231,250 | 52,750 |
| Net realized gains on available-for-sale securities | 32,551 | - |
| Total cash inflows | <u>5,790,048</u> | <u>83,052,750</u> |
| Cash outflows: | | |
| Claim payments made | 13,460,356 | 12,071,356 |
| Investment fees | - | 3,513 |
| Disbursements for Trust operating expenses | 4,822,947 | 15,101,839 |
| Disbursements for Court ordered bankruptcy fees | 83,250 | 1,514,274 |
| Total cash outflows | <u>18,366,553</u> | <u>28,690,982</u> |
| Net cash outflows | (12,576,505) | 54,361,768 |
| Non-cash changes: | | |
| Net unrealized gains on available-for-sale securities | 4,869,970 | - |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | (7,706,535) | 54,361,768 |
| Cash, cash equivalents, and investments available-for-sale, beginning of year | <u>147,059,732</u> | <u>92,697,964</u> |
| Cash, cash equivalents, and investments available-for-sale, end of year | <u>\$ 139,353,197</u> | <u>\$ 147,059,732</u> |

The accompanying notes are an integral part of these statements.

Thorpe Insulation Settlement Trust

NOTES TO FINANCIAL STATEMENTS

December 31, 2012 and 2011

NOTE A - SUMMARY OF ACCOUNTING POLICIES

1. Description of Trust

The Thorpe Insulation Settlement Trust (the Trust), organized pursuant to the laws of the state of Nevada with its office in Reno, Nevada, was established pursuant to the Pacific Insulation Company and Thorpe Insulation Company (collectively the "Debtors") Fifth Amended Joint Plan of Reorganization, dated December 17, 2009. The Trust was formed to assume the Debtors' liabilities resulting from pending and potential litigation involving individuals exposed to asbestos who have manifested asbestos-related diseases or conditions, for which the Debtors have legal responsibility; liquidate, resolve, pay and satisfy all valid asbestos-related claims in accordance with the Plan, preserve, hold, manage and maximize the Trust assets for use in paying and satisfying allowed asbestos-related claims, prosecute, settle and manage the disposition of the asbestos in-place insurance coverage, and prosecute, settle and manage asbestos insurance coverage actions. Upon the effective date of the Plan, the Trust assumed liability for existing and future asbestos-related claims against the Debtors. The Trust became effective on October 22, 2010.

The Trust was initially funded with cash, notes receivable and insurance settlement proceeds. The Trust's funding is dedicated solely to the settlement of asbestos-related claims and the related costs thereto, as defined in the Plan.

The Trust processes and pays all asbestos-related claims in accordance with the Thorpe Insulation Settlement Trust Agreement, as amended and restated, the Case Valuation Matrix, as amended and restated, (Matrix) and Trust Distribution Procedures, as amended and restated, (TDP) (collectively, the Trust Documents).

2. Special-Purpose Accounting Methods

The Trust's financial statements are prepared using special-purpose accounting methods that differ from accounting principles generally accepted in the United States. The special-purpose accounting methods were adopted in order to present the amount of equity available for payment of current and future claims. These special-purpose accounting methods are as follows:

- The financial statements are prepared using the accrual basis of accounting, as modified below.
- The funding received from Thorpe Insulation Company, Pacific Insulation Company, Farwest Insulation Contracting and their liability insurers is recorded directly to net claimants' equity. These funds do not represent income of the Trust. Offers for asbestos-related claims are reported as deductions from net claimants' equity and do not represent expenses of the Trust.
- Costs of non-income producing assets, which will be exhausted during the life of the Trust and are not available for satisfying claims, are expensed when incurred. These costs include acquisition costs of computer hardware, software and software development.
- Future fixed liabilities and contractual obligations entered into by the Trust are recorded directly against net claimants' equity. Accordingly, the future minimum commitments outstanding at period end for non-cancelable obligations have been recorded as deductions from net claimants' equity.

Thorpe Insulation Settlement Trust

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2012 and 2011

NOTE A - SUMMARY OF ACCOUNTING POLICIES - Continued

2. Special-Purpose Accounting Methods - Continued

- The liability for unpaid claims reflected in the statement of net claimants' equity represents settled but unpaid claims and outstanding offers. A claims liability is recorded once an offer is made to the claimant at the amount equal to the expected pro rata payment. No liability is recorded for future claim filings and filed claims on which no offer has been made. Net claimants' equity represents funding available to pay present and future claims on which no fixed liability has been recorded.
- All interest income is recorded net of investment expenses on the statement of changes in net claimants' equity.
- Available-for-sale securities are recorded at fair value. All interest and dividend income on available-for-sale securities, net of investment expenses, is included in investment income on the statements of changes in net claimants' equity. Realized and unrealized gains and losses on available-for-sale securities are recorded as separate components on the statements of changes in net claimants' equity.
- Realized gains/losses on available-for-sale securities are recorded based on the security's amortized cost. At the time a security is sold, all previously recorded unrealized gains/losses are reversed and recorded net, as a component of other unrealized gains/losses in the statement of changes in net claimants' equity.

3. Cash and Cash Equivalents

Cash and cash equivalents include demand deposit accounts and cash invested in money market funds.

4. Investments

Fair value measurements are determined through the use of an independent, nationally recognized pricing service. For securities that have quoted prices in active markets, market quotations are provided. For securities that do not trade on a daily basis, the pricing service provides fair value estimates using a variety of inputs including, but not limited to, benchmark yields, reported trades, broker/dealer quotes, issuer spreads, bids, offers, reference data, prepayment spreads and measures of volatility. The Trust reviews on an ongoing basis the reasonableness of the methodologies used by the pricing service, as well as determines the aggregate portfolio price performance and reviews it against applicable indices.

5. Deposits

Claims processing deposits represent filing fees collected for each unliquidated claim, which fees are refunded by the Trust if the claim is paid.

Thorpe Insulation Settlement Trust

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2012 and 2011

NOTE A - SUMMARY OF ACCOUNTING POLICIES - Continued

6. Use of Estimates

The preparation of financial statements in conformity with the special-purpose accounting methods described above requires the Trust to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of additions and deductions to net claimants' equity during the reporting period. Actual results could differ from those estimates.

7. Concentration of Risk

Financial instruments that potentially subject the Trust to concentrations of risk consist of cash and cash equivalents. Cash equivalents consist of money market accounts. Cash equivalents and demand deposits are in excess of Federal Deposit Insurance Corporation limits.

The Trust utilizes risk controls to meet investment objectives authorized by its Trustees. Such risk controls include the use of outside investment advisors meeting predetermined criteria, and third-party quantitative and qualitative risk measurement evaluation tools. The Trust believes its risk control practices are appropriate to meet investment objectives.

Investment securities, in general, are exposed to various risks, such as interest rates, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the financial statements.

8. Income Taxes

The Trust's policy is to recognize interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense. As of December 31, 2012, the Trust did not have any accrued interest or penalties associated with any unrecognized tax benefits, nor did it incur any interest and penalties expense with any unrecognized tax benefits for the year then ended. The Trust is unaware of information concerning any tax positions for which a material change in the unrecognized tax benefit or liability is reasonably possible within the next twelve months. The Trust files income tax returns in the United States. Although the Trust owes no tax to the State of California, it files an annual tax return in California reporting no taxable income or tax owed.

Thorpe Insulation Settlement Trust

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2012 and 2011

NOTE B - CASH, CASH EQUIVALENTS AND INVESTMENTS

The Trust has classified its investments as available-for-sale, and recorded the securities at estimated fair value, as follows:

| | December 31, 2012 | |
|-----------------------------|----------------------|----------------------|
| | Cost | Fair Value |
| <u>Restricted</u> | | |
| Cash equivalents | \$ 94,431 | \$ 94,431 |
| U.S. Government obligations | 2,270,323 | 2,270,707 |
| Municipal bonds | 139,249 | 138,360 |
| Mortgage backed securities | 79,183 | 79,656 |
| Corporate and other debt | 2,429,483 | 2,416,846 |
| | <u>\$ 5,012,669</u> | <u>\$ 5,000,000</u> |
| <u>Unrestricted</u> | | |
| Cash demand deposits | \$ 732,606 | \$ 732,606 |
| Cash equivalents | 17,942,286 | 17,942,286 |
| Equity securities | 46,420,660 | 50,912,336 |
| U.S. Government obligations | 10,307,038 | 10,319,952 |
| Municipal bonds | 43,136,147 | 43,524,190 |
| Mortgage backed securities | 296,897 | 298,696 |
| Corporate and other debt | 10,634,925 | 10,623,131 |
| | <u>\$129,470,559</u> | <u>\$134,353,197</u> |
| December 31, 2011 | | |
| | Cost | Fair Value |
| <u>Restricted</u> | | |
| Cash equivalents | <u>\$ 5,000,000</u> | <u>\$ 5,000,000</u> |
| <u>Unrestricted</u> | | |
| Cash demand deposits | \$ 519,342 | \$ 519,342 |
| Cash equivalents | 141,540,390 | 141,540,390 |
| Equity securities | - | - |
| U.S. Government obligations | - | - |
| Municipal bonds | - | - |
| Mortgage backed securities | - | - |
| Corporate and other debt | - | - |
| | <u>\$142,059,732</u> | <u>\$142,059,732</u> |

Thorpe Insulation Settlement Trust

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2012 and 2011

NOTE B - CASH, CASH EQUIVALENTS AND INVESTMENTS - Continued

The Trust accounts for investments according to a fair value hierarchy that distinguishes between assumptions based on market data (observable inputs) and the Trust's assumptions (unobservable inputs). The hierarchy consists of three broad levels as follows:

Level 1 - Quoted market prices in active markets for identical assets or liabilities.

Level 2 - Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; or valuations based on models where significant inputs are observable or can be corroborated by observable market data.

Level 3 - Valuations based on models where significant inputs are not observable, and for which the determination of fair value requires significant management judgment or estimation.

Assets and liabilities measured at fair value on a recurring basis, including financial instruments for which the Trust accounts, were as follows at:

| | December 31, 2012 | | |
|-----------------------------|----------------------|---------------------|---------------|
| | Level 1 | Level 2 | Level 3 |
| <u>Assets</u> | | | |
| Cash demand deposits | \$ 732,606 | \$ - | \$ - |
| Cash equivalents | 18,036,717 | - | - |
| Equity securities | 50,912,336 | - | - |
| U.S. Government obligations | 1,732,597 | 10,858,062 | - |
| Municipal bonds | - | 43,662,550 | - |
| Asset-backed securities | - | 378,352 | - |
| Corporate debt | 13,039,977 | - | - |
| | <u>\$84,454,233</u> | <u>\$54,898,964</u> | <u>\$ -0-</u> |
| | | | |
| | December 31, 2011 | | |
| | Level 1 | Level 2 | Level 3 |
| <u>Assets</u> | | | |
| Cash demand deposits | \$ 519,342 | \$ - | \$ - |
| Cash equivalents | 146,540,390 | - | - |
| Equity securities | - | - | - |
| U.S. Government obligations | - | - | - |
| Municipal bonds | - | - | - |
| Asset-backed securities | - | - | - |
| Corporate debt | - | - | - |
| | <u>\$147,059,732</u> | <u>\$ -0-</u> | <u>\$ -0-</u> |

The Trust's policy is to recognize transfers in and out of levels within the fair value hierarchy at the actual date the event or change in circumstance caused the transfer. Between the measurement dates of December 31, 2011 and December 31, 2012, no securities were transferred between Level 1 and Level 2.

Thorpe Insulation Settlement Trust

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2012 and 2011

NOTE B - CASH, CASH EQUIVALENTS AND INVESTMENTS - Continued

The maturities of the Trust's available-for-sale securities at market value (excluding cash equivalents) are as follows as of December 31, 2012:

| | Less than 1 Year | After 1 Year Through 5 Years | After 5 Years Through 10 Years | After 10 Years |
|-----------------------------|---------------------|---------------------------------------|---|---------------------|
| U.S. Government obligations | \$ 150,864 | \$ 4,201,235 | \$ 2,257,546 | \$ 5,981,014 |
| Municipal bonds | - | 21,663,480 | 16,446,407 | 5,552,663 |
| Mortgage backed securities | - | 140,102 | 238,250 | - |
| Corporate and other debt | 1,990,138 | 4,336,533 | 6,365,485 | 347,821 |
| | <u>\$2,141,002</u> | <u>\$30,341,350</u> | <u>\$25,307,688</u> | <u>\$11,881,498</u> |

NOTE C - FIXED ASSETS

The cost of non-income producing assets that will be exhausted during the life of the Trust and are not available for satisfying claims are expensed as incurred. Since inception, the cost of fixed assets expensed, net of disposals, include:

| | |
|-----------------------------------|-----------------|
| Acquisition of computer equipment | \$11,241 |
| Acquisition of computer software | <u>44,629</u> |
| | <u>\$55,870</u> |

These items have not been recorded as assets, but rather as operating expenses and direct deductions from net claimants' equity in the accompanying financial statements. The cost of fixed assets that were expensed during the years ended December 31, 2012 and 2011 was \$1,382 and \$54,488, respectively. Total depreciation expense related to asset acquisition using accounting principles generally accepted in the United States would have been approximately \$17,270 and \$16,818 for the years ended December 31, 2012 and 2011, respectively.

Thorpe Insulation Settlement Trust

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2012 and 2011

NOTE D - CLAIM LIABILITIES

Pursuant to the Trust Documents, the Trust distinguishes between claims that were liquidated prior to the establishment of the Trust (Pre-Petition Liquidated Claims) and claims processed after the creation of the Trust (Trust Claims). The Pre-Petition Liquidated Claims are grouped into two categories: settlement and judgment claims.

The cases underlying the Pre-Petition Liquidated Claims were stayed by the court until the Plan became effective. The Trust reviewed, processed and paid each Pre-Petition Liquidated Claim at the approved Funds Received Ratio. The Pre-Petition Liquidated Claims were paid in trust to the representative law firms for disbursement to the claimants upon the Trust's receipt and approval of a properly executed release.

For all Trust claims, a liability for unpaid claims is recorded at the time the offer is extended. Funds are mailed after the approved release is signed, received, and approved by the Trust. Unpaid claims liabilities remain on the Trust's books until the offer is accepted, rejected, withdrawn or expires after six months. Offers may be extended an additional six months upon written request and good cause. As of the years ended December 31, 2012 and 2011, there were no expired offers.

All claimants are entitled to the full liquidated value of their claim. Under the TDP, claimants receive an initial pro rata payment equal to the approved Funds Received Ratio of the claim's liquidated value. The remaining obligation for the unpaid portion of the liquidated amount is not recorded and is not a liability of the Trust, unless the Funds Received Ratio is increased. In that instance, the Trust would be obligated to retroactively pay the increased percentage to all previously paid claimants (see Note G).

In the interest of treating all claimants equitably in accordance with the Plan and pursuant to the TDP, all payments made during each calendar year ended December 31, 2010 through December 31, 2012 and future years shall include a Cost of Living Adjustment for inflation based upon the Federal Bureau of Labor Statistics' *Consumer Price Index for Urban Wage Earners and Clerical Workers* (CPI-W). Claims liabilities at year end are adjusted for any approved Inflation Adjustments. Inflation Adjustments are cumulative. Cumulative Inflation Adjustments of 6.74% and 4.95% are included in outstanding claims liabilities as of December 31, 2012 and 2011, respectively.

The Trust processed and approved approximately \$14,641,661 and \$12,766,926 of Trust Claims during the years ended December 31, 2012 and 2011, respectively.

NOTE E - LEGAL FEES - COVERAGE LITIGATION

For the year ended December 31, 2012 and the period from inception (October 22, 2010) through December 31, 2011, the Trust incurred a total of \$0- and \$840,275, respectively, of contingent and hourly fees for coverage litigation. Of this amount, \$400,687 and \$165,275 were paid, and \$337,500 and \$675,000 are represented in accrued expenses on the accompanying Statement of Net Claimants' Equity.

Thorpe Insulation Settlement Trust

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2012 and 2011

NOTE F - FACILITY AND STAFF SHARING AGREEMENT

The Trust has entered into a facilities and staff sharing agreement with the Western Asbestos Settlement Trust, (the Western Trust). The two trusts are related through common trustees. Under the agreement, and in exchange for advance monthly payments, the Western Trust provides use of its facilities and services relating to administration and claims processing. The agreement automatically renews for additional one-year periods unless either party provides written notice. The amounts of advance monthly payments are agreed upon between the trusts from time to time. As of December 31, 2012, the equitable amount agreed upon is based on the required written calendar year reconciliation of annual services that is performed by the Western Trust. The reconciliation is performed and recorded in the period subsequent to the reconciliation period. The reconciliation performed for the year ended December 31, 2012 resulted in an additional payment to the Western Trust of approximately \$50,000. The reconciliation performed for the fourteen months ended December 31, 2011 resulted in an additional payment to the Western Trust of approximately \$21,000. The next reconciliation period will be the twelve-month period ending December 31, 2013. Any excess of cost over payments or payments over cost is required to be repaid by the benefited party with interest. The future payments under this agreement have been recorded as a liability on the accompanying statement of net claimants' equity.

NOTE G - NET CLAIMANTS' EQUITY

The Trust was created pursuant to the Plan confirmed by the United States Bankruptcy Court for the Central District of California, Los Angeles Division. The TDP was adopted pursuant to the Plan and concurrently with the Trust Agreement. It is designed to provide fair and equitable treatment for all Trust claims that may presently exist or may arise in the future. The TDP prescribes certain procedures for distributing the Trust's limited assets, including pro rata payments and initial determination of claim value based on scheduled disease values, and individual factual information concerning each claimant as set forth in the Trust Documents.

Under the TDP, the Trust forecasts its anticipated annual sources and uses of cash until the last projected future claim has been paid. A pro rata Funds Received Ratio is calculated such that the Trust will have no remaining assets or liabilities after the last future claimant receives his/her pro rata share.

The Trustees, with the consent of the Trust Advisory Committee ("TAC") and Futures Representative, set the Initial Funds Received Ratio at 17.5%, based upon the analysis and advice of the Trust's expert economist. The TDP requires the Trustees, with the consent of the TAC and the Futures Representative, to periodically review the Funds Received Ratio and, if appropriate, propose additional changes in the pro rata Funds Received Ratio based on updated assumptions regarding the Trust's future assets and liabilities.

Thorpe Insulation Settlement Trust

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2012 and 2011

NOTE H - RESTRICTED CASH, CASH EQUIVALENTS AND INVESTMENTS

To avoid the high costs of director and officer liability insurance, and pursuant to the Trust Agreement, the Trust has elected to be self-insured and has established a segregated security fund of \$5,000,000. These funds are devoted exclusively to securing the obligations of the Trust to indemnify the current Trustees and officers, employees, agents and representatives of the Trust. The funds are held in a separate Trust bank account; and interest income accrues to the benefit of the Trust. As of December 31, 2012 and 2011, cash, cash equivalents and investments of \$5,000,000 were restricted for these purposes.

NOTE I - INCOME TAXES

For federal income tax purposes, the Trust is taxed as a Qualified Settlement Fund (QSF). Income and expenses associated with the Trust are taxed in accordance with Section 468B of the Internal Revenue Code. The statutory income tax rate for the Trust is 35% for the years ending December 31, 2012 and 2011 and 39.6% for subsequent periods, which caused the deferred tax asset discussed below to increase by \$1,277,000.

The Trust records deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the book and tax basis of assets and liabilities.

The Trust has recorded a deferred tax asset of approximately \$11 million reflecting the benefit of approximately \$33 million in loss carryforwards, which expire in varying amounts between 2030 and 2032. Realization is dependent on generating sufficient taxable income prior to expiration of the loss carryforwards. Although realization is not assured, the Trust believes it is more likely than not that all of the deferred tax asset will be realized. The amount of the deferred tax asset considered realizable, however, could be reduced if estimates of future taxable income during the carryforward period are reduced.

The provision for income taxes consists of the following for the years ended December 31, 2012 and 2011:

| | <u>2012</u> | <u>2011</u> |
|------------------------------|------------------|--------------------|
| Federal income tax – current | \$ - | \$ - |
| Deferred income tax benefit | 964,000 | 1,292,000 |
| | <u>\$964,000</u> | <u>\$1,292,000</u> |

The components of the deferred income tax asset, as presented in the statements of net claimants' equity consisted of the following at December 31, 2012 and 2011:

| | <u>2012</u> | <u>2011</u> |
|-------------------------------|---------------------|---------------------|
| <u>Deferred tax asset</u> | | |
| Depreciation and amortization | \$ 41,000 | \$ 44,000 |
| Facility-sharing obligation | - | - |
| Unrealized appreciation | (1,928,000) | - |
| Loss carryforward | 12,887,000 | 9,991,000 |
| Other | 2,000 | 3,000 |
| | <u>\$11,002,000</u> | <u>\$10,038,000</u> |

Thorpe Insulation Settlement Trust

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2012 and 2011

NOTE J - SUBSEQUENT EVENTS

The Trust evaluated subsequent events through April 15, 2013, the date the financial statements were available to be issued. There were no material subsequent events that required recognition or disclosure, except that discussed below.

In 2010 several non-settling insurers ("Appellants") appealed the confirmation order from which the Trust was created, to the United States Court of Appeals for the Ninth Circuit ("Ninth Circuit"). In 2012, the Ninth Circuit issued an opinion which upheld several significant matters on appeal and reversed and remanded the plan confirmation in order to allow the Appellants to be fully and fairly heard on issues related to insurance neutrality. The Trust received an order from the Bankruptcy Court which stated that it could continue the operation of the Trust in the ordinary course of business pending written instructions. On March 13, 2013, the Bankruptcy Court issued a scheduling order for the confirmation of the sixth amended joint plan of reorganization after receiving oral approval for the settlements from the remaining non-settling insurers. The confirmation hearing will be held on May 1, 2013. The Trust is certain that the outcome of the hearing will not impact its ability to continue operating.

SUPPLEMENTAL INFORMATION

Thorpe Insulation Settlement Trust

SCHEDULE OF OPERATING EXPENSES

For the years ended December 31,

| | <u>2012</u> | <u>2011</u> |
|--|---------------------|---------------------|
| Accounting | \$ 33,837 | \$ 39,609 |
| Claims processing/claims system development | 60,294 | 117,744 |
| Computer equipment | 1,382 | 174 |
| Futures representative | 567,751 | 366,704 |
| Information technology support | 12,311 | 11,632 |
| Legal fees | 3,249,421 | 1,863,831 |
| Legal fees - Court ordered | - | 840,275 |
| Trust Advisory Committee | 142,275 | 153,270 |
| Trust facility and staff sharing expense | 440,610 | 372,000 |
| Trustee fees | 416,791 | 236,966 |
| Trustees professional | - | 978 |
| | <u>\$ 4,924,672</u> | <u>\$ 4,003,183</u> |

EXHIBIT B

EXHIBIT "B"

Thorpe Insulation Settlement Trust Claim Report As of December 31, 2012

This report is submitted pursuant to Section 2.2 (c)(ii) of the Sixth Amendment to and Complete Restatement of Thorpe Insulation Company Asbestos Settlement Trust Agreement, which requires the Trust to file with the Bankruptcy Court a summary of the number and type of claims disposed of during the time period covered by the financial statements ("Accounting Period"). This report summarizes the Trust's processing of claims liquidated by settlement agreement or judgment on or before October 15, 2007, the Petition Date, ("Pre-Petition Liquidated Claims") and unliquidated Trust Claims.

Pre-Petition Liquidated Claims

On October 27, 2010 and November 17, 2010, the Trust implemented procedures to pay the Pre-Petition Liquidated Claims in accordance with the Plan, the Confirmation Order and Section 5.4 of the Trust Distribution Procedures. The Trust was authorized to approve for payment all settlements and judgments listed on the Schedule F filed in the bankruptcy case, as well as settlements and judgments which the Trust was able to verify as unpaid.

By the end of January 2011, the Trust reviewed, processed and paid all 326 Pre-Petition Liquidated Claims in the total amount of \$9,822,489.50, which amount was paid in trust to the representative law firms for disbursement to the claimants upon the Trust's receipt and approval of a properly executed release. All Pre-Petition Liquidated Claims were paid at the approved Funds Received Ratio of 17.5% and the Pre-Petition Liquidated Claims that were paid in 2011, included 1.7% to account for inflation based upon the Federal Bureau of Labor Statistics' Consumer Price Index for Urban Wage Earners and Clerical Workers ("CPI-W").

Unliquidated Trust Claims

Unliquidated Trust Claims reviewed by the Trust from January 1, 2012, through December 31, 2012, in accordance with the Second Amendment to and Complete Restatement of Thorpe Insulation Company Asbestos Settlement Trust Case Valuation Matrix ("Matrix") and Third Amendment to and Complete Restatement of Thorpe Insulation Company Asbestos Personal Injury Settlement Trust Distribution Procedures ("TDP") are as set forth below.

The value of each compensable disease is determined by the Matrix and TDP. Claim compensation is adjusted for individual claimants based upon jurisdiction and tort related individual characteristics including, but not limited to: age, marital status, dependents, medical specials, economic loss, and whether living at the time of commencement of litigation or filing the claim with the Trust. Each valid claim is awarded a total liquidated value. All unliquidated Trust Claims were paid at the

approved Funds Received Ratio of 17.5%. Payments made on Trust Claims in 2012 included an additional 4.95% to account for inflation based upon the CPI-W.

During the Accounting Period, 1,397 unliquidated Trust Claims were received, 404 unliquidated Trust Claims were paid, and 525 unliquidated Trust Claims received offers.

Below is a summary of the number and type of claims disposed of (paid) in 2012.

| Compensable Disease | Number of Claims |
|---|------------------|
| Grade II Non-Malignant | 92 |
| Grade I Non-Malignant | 43 |
| Grade I Non-Malignant Enhanced Asbestosis | 16 |
| Grade I Non-Malignant Serious Asbestosis | 13 |
| Colo-Rectal | 8 |
| Esophageal | 4 |
| Kidney | 3 |
| Laryngeal | 2 |
| Non-Hodgkin's Lymphoma | 0 |
| Other Cancer | 1 |
| Lung Cancer | 79 |
| Mesothelioma | 143 |
| Total | 404 |