

By early 1999, insurers that were briefly the life of the Hollywood financing party began waking up to their exposure, and several pulled out of the business, including AIG and AXA, which fired the Paris-based underwriter handling its business, court papers say.

Among these, AXA has possibly the largest exposure, having written gap financing risks as a direct insurer, as a reinsurer of other participants and through fronting companies. According to court filings, deals in which AXA has participated include:

- * \$200 million in financing for Village Roadshow Ltd., an Australian producer and distributor of such films as "The Matrix" and "Analyze This."

- * Start-up financing for Destination Film Funding Corp., which completed a \$100 million private placement of debentures through AXA subsidiary Donaldson Lufkin & Jenrette Securities Corp. AXA and several other insurers wrote a \$118 million policy insuring principal and interest payments on the bonds. Destination, whose principals invested none of their own money in the company, has since released a handful of pictures, including "Bats," "Eye of the Beholder" and "Drowning Mona."

- * A portfolio of more than \$100 million in production loans by Imperial Bank of Los Angeles.

- * Production financing involving Flashpoint, a United Kingdom film finance company whose projects are expected to produce claims totaling \$56 million to \$90 million, according to Chase court filings.

Aggressive in its pursuit of film finance risks, AXA is now the most aggressive of the participating insurers in fighting the resulting claims in U.K. and U.S. courts.

Seven lawsuits are now pending in the U.K., most involving losses from four Chase-financed films: "The Mirror Has Two Faces" and "The People vs. Larry Flynt," produced by Los Angeles-based Phoenix Pictures Inc.; and "The Phantom" and "Beautician and the Beast," produced by Para-mount Pictures Corp.

According to AXA court filings, Chase has filed claims amounting to \$21.9 million for "Mirror"; \$16.6 million for "Larry Flynt"; \$8.8 million for "Phantom"; and \$7.7 million for "Beautician."

Some insurers have paid claims on these films: X.L. Insurance Ltd. settled its participation on the Phoenix pictures and is believed to have paid more than \$15 million, according to sources familiar with the deal. An X.L. spokesman could not be reached.

Eight insurers, though, including AXA Colonia Versicherung A.G., filed the first U.K. complaint, suing to rescind coverage on the two Phoenix films and charging that they were misled by Chase and Heath brokers about the risk. Chase itself has filed four lawsuits seeking recovery on each of the films (BI, Jan. 10).

In March, Chase filed a new action in a New York state court against AXA Reinsurance UK P.L.C. and six other insurers to collect a \$4.5 million claim related to "A Texas Funeral," part of

a \$175 million, multi-picture financing for London-based producer J&M Entertainment Ltd.

Participants in the "Texas Funeral" loss are AXA with 33.6%; Royal & SunAlliance Insurance P.L.C. with 25.2%; AIG's New Hampshire with 21%; HIH Casualty & General Insurance Ltd. with 8.4%; General Star International Indemnity Ltd. with 6.3%; Odyssey Re (London) Ltd. with 3.1%; and Great Lakes Reinsurance (UK) P.L.C. with 2.4%

In this case, AXA has not only denied liability but is leveling expansive fraud charges in complaints against Chase, Heath, J&M and London-based ICE Media Ltd., a consultant on the deal.

AXA alleges that it was duped into insuring the J&M financing in an ongoing conspiracy among Heath, ICE Media and Chase that extended as far back as 1992 and involved deals insuring more than a dozen films by several producers.

According to AXA's complaint, Heath in 1992 placed an insurance program with Lloyd's of London underwriters backing film production loans made by Berliner Bank A.G. By 1996, four of the films had generated claims ranging from \$87,628 to \$1 million, but Heath did not notify insurers and in one case paid the claim itself "to avoid legal action and bad press," according to the suit.

Heath went on to place programs covering Chase loans to Phoenix Pictures for a slate of five films -- "Mirror," "Larry Flynt," "Swept from the Sea," "U-Turn" and "Apt Pupil" -- and Paramount for a slate of four films: "Phantom," "Beautician," "In and Out" and "The Truman Show."

By the time they approached AXA in 1998 to join a \$175 million line slip covering eight J&M Entertainment films, Chase, Heath and ICE Media were concealing a variety of facts, AXA charges. They included that:

- * The Berliner Bank program generated claims and that large losses were expected on the Phoenix and Paramount programs.

- * Lloyd's underwriters withdrew from the Phoenix placement over alleged non-disclosures by Heath, and CNA Financial Corp. withdrew out of concerns about the program's structure. Heath told AXA that Lloyd's withdrew because the program was too much like a financial guaranty, which Lloyd's could not write, and that CNA withdrew because of a political fight between the London and Chicago offices, AXA contends.

If AXA had known of the allegedly concealed facts, it would not have backed J&M's financing, the insurer argues.

Chase, Heath and ICE Media also specifically misled AXA in various ways about J&M's "Texas Funeral," among other things by grossly inflating the film's projected revenues and understating its losses, AXA says.

-- General Star International -- has cited AXA's charges in reserving its rights to deny coverage, Chase alleges.

AXA has likewise induced AIG's New Hampshire unit to deny coverage under a policy covering another money-losing film, "Looking for an Echo." AXA reinsures nearly 50% of New Hampshire's risk on the policy, according to Chase; the bank filed suit against New Hampshire in New York state court in March to recover on a \$4.2 million claim.

"AXA Reassurance had evidently overextended itself in this class of business and is seeking to reduce its exposure by improper means," Chase contends. "This action is part of that strategy."

Stirling Cook also denies AXA's charges: "We do not see any basis for (the allegations), and we will defend them vigorously," said James Lawless, the broker's general counsel.

Mr. Litto, a longtime Hollywood producer and head of Litto Pictures, was blunt in his reaction to AXA's actions: "It's very unprofessional, very unbusinesslike and completely outrageous behavior," he said. "I can't make four more pictures under that deal because that financing is no longer available."

Mr. Litto said he has begun arbitration proceedings -- which AXA is contesting -- and is seeking \$225 million in damages for the collapse of his program.

The fighting over insurance-backed gap financing deals is far from over: As more films covered by AXA and other insurers are released and hit their claims reporting dates, more losses are likely to emerge.

"We are in very, very early days on possible litigation," said an insurance industry source familiar with the programs. "Unless something is resolved shortly, which it will not be, it will get bigger and bigger."

"The way things are going," said another source familiar with the litigation, "it's hard to be optimistic."
