

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

In Re: Penn Treaty Network America
Insurance Company in Rehabilitation

DOCKET NO. 1 PEN 2009

In Re: American Network Insurance
Company in Rehabilitation

DOCKET NO. 1 ANI 2009

AFFIDAVIT OF PATRICK CANTILO

I, Patrick Cantilo, having been first duly sworn on oath, depose and say:

1. I currently reside in Austin, Texas and am over the age of 18 years.
2. I understand that I will be called to testify on November 9, 2016 in the matter captioned above. I will testify to and in accord with the statements made in this Affidavit, and believe that I can do so competently.
3. My education, business and professional experience are summarized in the resume attached hereto as Commissioner (“C”) Exhibit (“Ex.”) C-10.
4. I am, and have served as, the Special Deputy Rehabilitator (“SDR”) of Penn Treaty Network America Insurance Company (“PTNA”) and American Network Insurance Company (“ANIC”, together the “Companies”) since 2012, and am compensated for that work.
5. I submit this Affidavit and related documents in support of the Verified Petitions to Convert Rehabilitation to Liquidation (the “**Liquidation Petitions**”) filed herein on July 27, 2016, as to each of the Companies. This Affidavit constitutes my direct testimony in support of the Liquidation Petitions.
6. I have personal knowledge of the facts set forth in this Affidavit. My testimony is based upon my service as the SDR of PTNA and ANIC since July 2012, my education, my business and professional experience, and materials that I have reviewed.
7. The Court records in the Companies’ receiverships evidence years of contested proceedings and rehabilitation efforts that culminated in the July 27, 2016, filing of the Liquidation Petitions.
8. The Companies’ boards of directors and PTAC have consented to the Companies’ liquidations. See Exhibits C7-9, true and correct copies of which have been provided to the Court and are attached hereto.

**Exhibit
C-1**

9. As detailed below, I have concluded that the Companies are insolvent and that further attempts to rehabilitate their business would substantially increase the risk of loss to creditors, policy and certificate holders, and the public, and would be futile.

10. On pages 108 *et seq.* of the Second Amended Plan of Rehabilitation (“**Plan**”), filed October 8, 2014, I detailed early efforts to rehabilitate the Companies.

11. I have prepared the following tables from financial reports compiled by the Companies that detail the financial condition of the Companies, both separately and combined beginning at year-end 2008, just before they were placed in rehabilitation.¹

PTNA

(\$ MILLIONS)	2008	2009	2010	2011	2012	2013	2014	2015
ASSETS	1,001	936	889	848	788	718	647	509
LIABILITIES	1,225	3,102	3,267	3,355	2,795	3,659	4,220	3,842
SURPLUS/(DEFICIT)	(224)	(2,166)	(2,378)	(2,507)	(2,007)	(2,942)	(3,573)	(3,333)
NET INCOME/(LOSS)	.2	(2,153)	(219)	(129)	501	(937)	(628)	241

ANIC

(\$ MILLIONS)	2008	2009	2010	2011	2012	2013	2014	2015
ASSETS	123	129	139	143	152	153	155	146
LIABILITIES	118	262	341	369	433	540	649	586
SURPLUS/(DEFICIT)	5	(134)	(203)	(226)	(280)	(387)	(495)	(439)
NET INCOME/(LOSS)	2	(143)	(69)	(18)	(60)	(105)	(105)	58

PTNA & ANIC COMBINED

(\$ MILLIONS)	2008	2009	2010	2011	2012	2013	2014	2015
ASSETS	1,124	1,064	1,027	991	940	871	802	656
LIABILITIES	1,344	3,364	3,608	3,724	3,228	4,200	4,870	4,428
SURPLUS/(DEFICIT)	(219)	(2,300)	(2,580)	(2,732)	(2,288)	(3,329)	(4,067)	(3,772)
NET INCOME/(LOSS)	2	(2,296)	(288)	(147)	(441)	(1,042)	(733)	299

12. On August 31, 2016, PricewaterhouseCoopers (“PwC”), the Rehabilitator's consulting actuaries, completed their report of Actuarial Findings & Recommendations as of December 31, 2015 (the “**2015 Actuarial Report**”), for the Companies, a true and correct copy

¹ A significant reduction in the discount rate in 2015 to reflect changes in the broader economy resulted in a material reduction in the Companies' premium deficiency reserves and produced the appearance of net income. This net income is solely a consequence of the reductions in reserves and not of improvements in financial performance.

of which has been provided to the Court and is attached hereto as Exhibit C-6. The 2015 Actuarial Report concludes that as of year-end 2015 PTNA had a deficit of \$ 3,332.5 million while ANIC had a deficit of \$ 493 million. At my request, PwC also determined that, in the absence of liquidation, PTNA can be expected to fully consume its remaining cash by year-end 2018 and that ANIC will do so by year-end 2023.

13. Also provided with this Affidavit and attached hereto in support of my testimony are true and correct copies of the following documents, which have been provided to the Court, and were prepared at my direction and pursuant to applicable statutory and regulatory requirements:

- Exhibit C-2: ANIC 9.30.16 Balance Sheet
- Exhibit C-3: PTNA 9.30.16 Balance Sheet
- Exhibit C-4: ANIC 2015 Annual Statement
- Exhibit C-5: PTNA 2015 Annual Statement

14. As documented in the tables above and in the Annual Statements provided herewith as Exhibits C-4 and C-5, I have concluded, and advised the Rehabilitator, that both PTNA and ANIC are insolvent because their admitted assets do not exceed their liabilities plus the greater of the capital and surplus required by law or their authorized and issued capital stock.

15. I have also concluded, and advised the Rehabilitator, that further efforts to rehabilitate the business of the Companies would be futile and serve no useful purpose because, in summary: (1) multiple efforts to rehabilitate the business have failed; (2) multiple other alternatives were considered and ruled out; and (3) I have not been able to devise, nor have I been made aware of, another proposed rehabilitation plan that would be feasible, would have a reasonable chance of success, or would serve any useful purpose.

16. From the time the Companies were first placed in Rehabilitation nearly eight years ago, many alternatives were considered and many efforts were made to rehabilitate them. Early efforts and considerations of alternatives are documented in the Plan beginning at page 97 and the efforts undertaken during my involvement are described in the July 2015 Transcript at “**Day 1**” (July 13, 2015, as corrected): 134:11 – 35:10; 36:7 – 40:3; 104:9 – 110:13; 228:18 – 240:5; “**Day 2**” (July 14, 2015, as corrected): 49:8 – 52:13, including (i) the efforts of a Rehabilitation Advisory Committee (“**RAC**”) comprised of the Rehabilitator's representatives and consultants as well as those of PTNA's parent company, Penn Treaty America Corporation and its chairman, Eugene Woznicki (collectively “**PTAC**”); and (ii) the development of Plans of Rehabilitation for PTNA and ANIC that were filed with this Court on April 30, 2013 (the “**2013 Plans**”). See July 2015 T. at Day 1: 39:19 – 39:23; Day 2: 43:3 – 49:7 (re addressing inadequate and unfairly discriminatory premium rates for “OldCo [pre=2002] business”); Day 1: 37:6 – 38:1; 39:15 – 39:18; 104:20 – 106:14; Day 2: 49:8 – 50:16 (re interim policy benefit modifications and suspensions); Day 1: 36:13 – 37:5; 204:14 – 205:8; 210:22 – 214:12 (re reduction of the asset-liability gap), Day 1: 38:2 – 38:15; 45:16 – 46:5; Day 2: 49:8 – 50:16 (re objections).

17. Following the filing of the 2013 Plans and the filing of well over a hundred objections thereto, extensive discussions ensued with a group of the Companies' agents and brokers (the "**Agents**"), a group of health insurers (the "**Health Insurers**"), PTAC, Broadbill Partners LP (a PTAC shareholder), the Court-appointed Policyholders Committee, and the National Organization of Life and Health Insurance Guaranty Associations ("**NOLHGA**"), all of whom became active participants in the Multi-Party Rehabilitation Group ("**MPRG**").

18. Over the course of many meetings, the Second Amended Plan of Rehabilitation was developed, which Plan was recently withdrawn. The key attributes of the Plan were described in that document, as well as during the July 2015 hearing. See Day 1 at 18:18 – 21:20; 33:7 – 36:6; 53:17 – 55:6; 55:22 – 57:20 (segregation of business between PTNA and ANIC as Companies "A and B"), Day 1 at 55:22 – 60:10 – 65:6 (premium rate adjustments to effect "Self-Sustaining" policies), Day 1 at 57:9 – 62:6; 65:8-16; 70:5 – 72:1 (alternative rate increases and/or benefit modifications for "Non-Self-Sustaining" policies), Day 1 at 57:9 – 62:6; 62:18 – 65:6; 130:7 – 132:11; 146:5 – 149:8 (policyholder options), Day 1 at 19:5-14; 201:7-19; 209:1-7; 249:12-22 (potential release from receivership or run-off for ANIC). Objections to the Plan are described in the July 2015 T. at Day 1 12:12 – 13:24; 142:2-18; 113:7 – 114:2; 193:9 – 194:15; 214:18 – 216:19.

19. The Plan reflected my best effort and that of the Rehabilitator to reconcile vigorously competing views about how to address the Companies' severe financial challenges.

20. While efforts to resolve the remaining objections to the Plan continued after the July 2015 hearing, the Rehabilitator, at the request of the Court, also conducted survey and focus groups seeking to ascertain likely policyholder elections. The results suggested that a relatively small number of policyholders would have elected under the Plan to continue with Company A outside of liquidation and only a small subset of these would have realized an economic advantage from that selection. Combined with the inexorable dissipation of scarce assets as efforts to resolve objections continued, this led me to conclude that the Plan would not be viable, and I reported this to the Court in the spring of this year during conferences aimed at resolving continuing objections to the Plan.

21. I have concluded and advised the Rehabilitator that continuing efforts to rehabilitate the business of the Companies would be futile. In late July, therefore, we filed petitions to have the Companies placed in liquidation.

22. The development of rehabilitation plans, and the efforts to overcome objections to such plans over the last seven years, have been costly. Apart from the substantial sums spent on counsel and consultants during this period, the Companies continued paying far more substantial sums in claims and operating expenses. As we discussed with the Court, the uncertainty of the Companies' circumstances and prospects made asking for premium rate increases an impracticable option. Thus during the period in which efforts have been made to rehabilitate the business of the Companies, they have seen their aggregate assets decline nearly in half from \$1.1

billion to less than \$600 million and their deficit increase from less than \$300 million to nearly \$4 billion.²

23. One consequence of this deterioration in financial condition is that many fewer assets remain available to pay the amounts owed to policyholders and creditors. In addition, as more policyholders' claims continued to be paid in full, it became unavoidable that more future claims would receive a smaller proportionate payment from the Companies' assets. This effect was compounded by continuing payment of agent commissions, taxes and other payables that would be suspended in liquidation. I am aware that the Companies' policyholders have expressed to the Companies and the Court their view that this continuing uncertainty has been very distressing. On the whole, therefore, it is my conclusion, and I have advised the Rehabilitator, that continuing efforts to rehabilitate the business of the Companies would substantially increase the risk of loss to creditors, policyholders and the public.

24. At no time since the July 2015 hearing have the MPRG parties come together in uniform support of a rehabilitation plan.

25. The transition from rehabilitation to liquidation and resulting triggering of guaranty association coverage will not disrupt the continued delivery of benefits to policyholders.

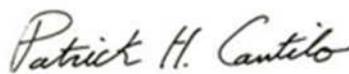
26. There are ample grounds for converting the Companies from rehabilitation to liquidation.

27. Mechanics of the administration of liquidation will be addressed in subsequent filings; *e.g.*, allocation of the assets and future premiums (including distributions to guaranty associations) as contemplated by 40 P.S. § 221.36.

28. I am prepared to elaborate on the subjects discussed in this Affidavit.

Pursuant to 18 Pa. C.S.A. § 4904, I swear that the foregoing is true and correct to the best of my knowledge, information and belief.

November 4, 2016



Patrick Cantilo

² To be sure, some of the deterioration can be attributed to differences in actuarial assumptions. Nonetheless, the financial condition of the Companies has declined steadily throughout this period.