

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

M. DIANE KOKEN	:	CIVIL ACTION
INS. COMM’R OF PA, IN HER	:	NO. 04-4342
OFFICIAL CAPACITY AS	:	
LIQUIDATOR OF RELIANCE INS.	:	
CO.,	:	
	:	
Plaintiff	:	
	:	
v.	:	
	:	
PENSION BENEFIT GUARANTY	:	
CORP. (PBGC),	:	
	:	
Defendant	:	

REPORT OF PATRICK CANTILO

I. DOCUMENTS REVIEWED

- A. 2001-05-29 Rehabilitation Order**
- B. 2001-10-03 Petition for Liquidation**
- C. 2001-10-03 Liquidation Order**
- D. 2002-01-22 Order re Subsidiaries**
- E. 2004-08-25 Declaratory Judgment action**
- F. 2005-07-14 Memorandum Opinion of Judge Robreno**
- G. 2005-08-08 Memorandum Opinion of Judge Robreno**

II. ASSUMPTIONS AND OBSERVATIONS

- A. PBGC claims that it has obtained after the date of the Rehabilitation Order a lien upon the assets of a wholly owned subsidiary of Reliance.**
- B. PBGC provided no new consideration in exchange for this lien.**
- C. PBGC also asserts a lien upon other assets held directly by Reliance.**
- D. It is undisputed that current U.S. law applies to this matter so that the claims of reliance’s policyholders hold a higher priority than**

that of PBGC in the distribution of Reliance's assets.

- E. The subsidiary in question was reported among the assets of Reliance.
- F. The October 3, 2001, Liquidation Order for Reliance Insurance Company contains at pages 2 and 3 typical provisions vesting in the Commonwealth Court jurisdiction over Reliance's assets, including subsidiaries.
- G. Similarly, the Liquidation Order (as did the May 29, 2001, Rehabilitation Order), among other things, enjoins the placement or enforcement of liens on Reliance's assets.

III. RELEVANT EXPERIENCE

- A. Attached is my Curriculum Vitae.
- B. I have worked in the area of insurance insolvency since 1980 and have been involved in the rehabilitation or liquidation of more than 50 insurers and insurance related entities. I have served as Special Deputy Receiver, Deputy Liquidator or Special Deputy Commissioner in many of these cases, and as counsel to the receiver or deputy receiver in most of the others.
- C. Among these matters, in those instances in which the insurer owned all or part of an operating subsidiary, we have treated that subsidiary (especially when wholly owned) as an asset of the insurer, to be sold if possible. Invariably, the proceeds of such sales were then included among the assets of the insolvent and distributed to policyholders and creditors under the applicable priority scheme.
- D. In every state in which I have been so involved, a court supervising the liquidation of an insurer (the "receivership court"), typically possesses and exercises *in rem* jurisdiction over all assets of the insolvent insurer, whether held directly or indirectly, including those held through subsidiaries.

IV. OPINIONS - IN MY EXPERIENCE:

- A. Receivership courts, such as the Commonwealth Court in this case, generally treat subsidiaries as the property and assets of the insurer in liquidation, whether or not the subsidiaries are themselves engaged in the business of insurance, whether or not they are incorporated separately, and independent of whether they are direct (“first tier”) subsidiaries or themselves owned by other subsidiaries (and thus “lower tier” subsidiaries).**
- B. The determination of value for a subsidiary typically takes into account a comparison of its assets and liabilities, and that value is then attributed to the parent in proportion to the parent’s ownership interest.**
- C. In determining the value of a subsidiary as an asset of the insolvent insurer, the liabilities of the insurer (that are not the liabilities of the subsidiary) are not taken into account, regardless of the manner in which they arose.**
- D. A lien placed on a subsidiary, or upon the assets of the subsidiary, generally would impair or bar the ability of the receiver to sell the subsidiary, or would reduce the proceeds of any such sale.**
- E. The effect of permitting a creditor of the insolvent insurer to place such a lien on the assets of a subsidiary would be to enable the lienholder to circumvent the injunction in the receivership order against imposition of such liens upon the assets of the insurer.**
- F. In that sense, such a subsidiary lien would enable its holder to obtain a position preferential to the position of policyholders and other creditors with respect to the assets of the subsidiary, and distributions from the parent insolvent insurer.**
- G. In the absence of such liens, the value of the subsidiary, as an asset of the insurer, would be distributed pro-rata in accordance with the applicable priority scheme, which typically places policyholders and insureds above governmental agencies, taxing authorities, and other creditors.**
- H. The Reliance Rehabilitation Order expressly enjoins any person from obtaining liens upon, or encumbering, the assets of Reliance.**

Based on my experience, liens imposed in derogation of such injunctions are disregarded.

- I. In this matter, the effect of disregarding PBGC's purported lien on the assets of the subsidiary is to place PBGC in the position of a creditor of Reliance, whose claim will be paid in accordance with the statutory priorities and other applicable law.**

**PATRICK H. CANTILO, P.C.
CANTILO & BENNETT, L.L.P.**

Having received a Bachelor of Arts degree with Honors from the University of Texas in 1977, and his Juris Doctorate degree from the University of Texas School of Law in 1980, Patrick Cantilo was admitted to practice law in the State of Texas in November 1980. He has since been admitted to practice in all Texas Courts, the United States District Courts for the Eastern, Northern, Southern, and Western Districts of Texas, the United States Courts of Appeals for the Fourth and the Fifth Circuits, and the United States Supreme Court.

Most recently Mr. Cantilo's practice has been concentrated on the reorganization of health services corporations and in the area of insurance regulation, rehabilitation, and liquidation. He has served as Counsel to the Receiver, as Special Deputy Receiver, Deputy Receiver, Deputy Liquidator, or in comparable capacities in a number of insurance and managed care insolvencies. As advisor to state regulators, he has become deeply involved in conversion, merger, reorganization, or initial public offering transactions for a number of Blue Cross and Blue Shield plans. Mr. Cantilo's law practice has also included litigation in the State and Federal Courts, both at the trial and appellate levels.

REPRESENTATIVE ENGAGEMENTS

Blue Cross transactions include:

- Demutualization of Trigon Insurance Company;
- Conversion to for profit of Blue Cross Blue Shield of Missouri;
- Litigation arising from the mutualization of Blue Cross and Blue Shield of Kansas, Inc.;
- Proposed sponsored demutualization of Blue Cross and Blue Shield of Kansas, Inc.;
- Proposed conversion of CareFirst of Maryland, Inc. and acquisition by WellPoint Health Networks, Inc.;
- Proposed conversion of PREMERA Blue Cross and Blue Shield;
- Conversion and sale of Blue Cross and Blue Shield of Colorado;
- Conversion to nonprofit mutual of Blue Cross and Blue Shield of North Dakota.

Receivership or conservation proceedings include:

- Baldwin-United Companies;
- Commodore County Mutual Insurance Company;
- Cotton Belt Insurance Company;
- East Texas Health Plans;
- Executive Life Insurance Company;
- Fidelity Bankers Life Insurance Company;
- First Service Life Insurance Company;
- First United Trust Company;
- Foundation Health Plan of New Jersey;
- General Protective Life Insurance Company;
- Group Health of El Paso;
- Home Owners Warranty Corporation;
- Kenilworth Insurance Company;
- Knickerbocker Life Insurance Company;
- Maxicare Health Plans;
- MedCenters of North Dakota;
- MetroCare;
- Mission Insurance Company of Texas;
- Mobile Insurance Company and Mobile County Mutual Insurance Company;
- Reciprocal of America;
- Texas Prepaid Health Plans;
- United Bankers Life Insurance Company;
- United Capital Life Insurance Company;
- Superior Lloyds Insurance Company;
- Colonial Title Insurance Company.

Publications

“Texas Health Maintenance Organizations: Lessons from Insolvency”, Texas Health Law Reporter, Vol. 1, Nos. 4 and 5, October and December 1984;

“Insurer Insolvency: A Primer for Malpractice Insureds”, Texas Health Law Reporter, Vol. 2, No. 5, December 1985;

“What To Do If You Believe Your Malpractice Carrier Is Insolvent”, Texas Medicine, Vol. 83, No. 3, March 1987;

Patrick Cantilo CV, April 2005, P. 2

“New Legislation Affects Fees, Taxes for Texas Third-Party Administrators”, Houston Insurance News, December 1, 1987;

“Health, HMO and Related Entity Insolvencies”, American Bar Association, Tort and Insurance Practice Section, Law and Practice of Life Insurance Company Insolvency, June 1993, 1996; and

“Rehabilitation of Managed Care Organizations: A Thumbnail Sketch of Certain Key Considerations”, The Insurance Receiver, International Association of Insurance Receivers, Winter 1999.

Presentations and Lectures

“HMO Issues: A Seminar for State Regulators”, Bureau of HMOs, U.S. Department of Health and Human Services, 1982, 1983, 1984 and 1986;

“How to Examine HMO Financial Viability”, seminars, N.A.H.M.O.R and O.H.M.O.-D.H.H.S., 1981;

“HMOs: What Do We Know?”, seminar, N.C.H.S.R., Texas Departments of Health and Insurance and Texas Senate, 1981;

Seminar on Agent's Liability, Texas Association of Life Underwriters Convention, 1985;

Group Health Institute, Group Health Association of America, Inc. and N.A.H.M.O.R., 1986;

“The Regulator's Response to the New Competitive Environment”, American Medical Care and Review Association and N.A.H.M.O.R., 1986;

“Current HMO Issues: A Seminar for Regulators”, N.A.I.C. and N.A.H.M.O.R., 1986;

“HMO Issues 1987: A Seminar for State Regulators”, N.A.H.M.O.R. and O.P.H.C., 1987;

“HMO Issues 1988: A Seminar for State Regulators”, N.A.H.M.O.R. and O.P.H.C., 1988;

“HMO Issues 1989: A Seminar for State Regulators”, N.A.H.M.O.R. and O.P.H.C., 1989;

HMO REGULATIONS: THE LATEST TRENDS IN STATE ISSUES – “Bankruptcy: A Federal or State Problem?”, Group Health Institute 1989, June 15, 1989, Atlanta Georgia;

“A Guide to Insurer Insolvency”, State Bar of Texas Professional Development Program entitled DEALING WITH THE FAILED INSURER, October 1989, Austin and Dallas, Texas;

“HMO Insolvency: State or Federal Jurisdiction?”, National Conference of Insurance Legislators, Austin, Texas, November 1989;

“1988 HMO Law Update”, National Health Lawyers Association Meeting, Chicago, December 1989;

“N.A.H.M.O.R. Education Foundation Advanced Seminar”, San Diego, California, April 27, 1990;

“NAIC/N.A.H.M.O.R. Committee and Industry Advisory Group”, Arlington, Virginia, October 2, 1990;

“HMO Issues 1991: Defining Managed Care”, N.A.H.M.O.R. Annual Meeting, Indianapolis, Indiana, June 6, 1991;

“LOMA Group Insurance Administration Committee”, Guest Speaker, Austin, Texas, March 3, 1992;

“Legal Issues Involved in the Liquidation of Insolvent Insurers”, Texas Department of Insurance, Guest Speaker, Austin, Texas, August 15, 1992;

“Receivership Appeal Procedures”, National Association of Insurance Commissioners/Society of Insurance Receivers, Guest Speaker, Orlando, Florida, February 18-19, 1993;

“Health, HMO and Related Entity Insolvencies”, American Bar Association National Institute on Life Insurer Insolvency, Guest Speaker, Chicago, Illinois, June 19-20, 1993;

“Mock Takeover”, Society of Insurance Receivers, Guest Speaker, New Orleans, Louisiana, December 3, 1994;

“Legal Issues in Managed Care Regulation”, National Association of Managed Care Regulators, Guest Speaker, San Antonio, Texas, May 1, 1995;

(EX) Special Committee on Blue Cross Plans, 1995 NAIC Winter National Meeting, San Antonio, Texas, December 4, 1995;

“HMOs, Warranty Insurers, and Other ‘Special’ Receiverships”, National Association of Insurance Commissioners and the Society of Insurance Receivers Insolvency Workshop, Albuquerque, New Mexico, January 25, 1996;

“Risk Retention Groups”, National Association of Insurance Commissioners Federal Preemption of State Insurance Laws, Detroit, Michigan, March 23, 1996;

Interim Meeting of the Special Committee on Blue Cross Blue Shield Plans, Dallas, Texas, April 26, 1996;

“Health, HMO, and Related Entity Insolvencies”, American Bar Association National Program, Insurance Regulation of Health Care Arrangements, New York, New York, June 2, 1996;

“Insolvency Issues, Historical Perspective”, (HCFA), Negotiated Rulemaking Committee on PSO Solvency Standards, Arlington, Virginia, October 22, 1997;

“Insurer Restructuring: A Framework for Regulatory Analysis”, (NAAG), National Training Conference for Regulators - Health Care Conversions and Acquisitions, Boston, Massachusetts, July 19, 1998;

“Blue Cross Blue Shield Conversions”, (NAMCR), 1998 Fall Conference, Managed Care's Future, Washington Perspective, Washington, D.C., October 26, 1998;

“Troubled Managed Care Organizations: A Return to Bad Old Times?”, (NAMCR), HMO Insolvency Seminar, San Antonio, Texas, February 18-20, 1999;

“Troubled Managed Care Organizations: Back to the Future!”, (NAMCR), HMO Insolvency Seminar, Charleston, South Carolina, November 3-4, 1999;

“Managed Care: a Different Millennium Bug”, IAIR/NAIC Insolvency Workshop; Tuscon, Arizona, January 20-21, 2000;

“HMO Insolvencies and Their Impact: Provider, Patient, Legal, and Financial Issues”, Mealey’s Insurance Insolvency & Reinsurance Roundtable, Scottsdale, Arizona, April 13-15, 2000;

“Managed Care Insolvencies: Just When You Thought it Was Safe to Go Back in the Water”, Society of Financial Examiners 2000 Career Development Seminar, Uncharted Waters: Fathoming the Depths of Fraud, San Diego, California, July 23-26, 2000;

“Delegation Agreements–The Legal Issues”, Downstream Contracting and Delegation Summit; National Assoc. of Managed Care Regulators, Philadelphia, Pennsylvania, November 13-15, 2000; and

“Lessons and Implications of Various Blue Cross Blue Shield Conversions”, New York, New York, June 21, 2003.

Public Service

Counsel for Texas Judicial Insurance Receiver, 1980-1983.

National Association of Insurance Commissioners, Liquidators Task Force, and Receivership and Insolvency Task Force, 1982 - present.

National Association of Health Maintenance Organization Regulators (now National Association of Managed Care Regulators) Associate Member, 1986 - present.

National Association of Insurance Commissioners/National Association of Health Maintenance Organization Regulators Joint Committee, Advisory Committee, 1986.

Chairman, Financial Subcommittee, H.M.O. Advisory Committee established by the State Board of Insurance, 1986.

NAIC/N.A.H.M.O.R. Continuation of Benefits Working Group, Contracts and Services Committee, 1989.

N.A.H.M.O.R. Advisory Committee, 1991.

Member

Travis County Bar Association (Litigation Section); American Bar Association (Litigation and Tort & Insurance Sections); State Bar of Texas (Litigation Section); International Association of Insurance Receivers (Principal Charter Member, 1991 - present).

Designations

Certified Insurance Receiver – Multiple Lines, International Association of Insurance Receivers.