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IN THE COMMONWEALTH COURT OF PENNSYLVANIA

In Re: Senior Health Insurance Company of Pennsylvania (in Rehabilitation)	**:** **:** **:**	**No. 1 SHP 2020**

STATE INSURANCE REGULATORS' REBUTTAL POST-HEARING MEMORANDUM

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TABLE OF CONTENTS

Table of Authorities

Cases

Statutes

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

In Re: Senior Health Insurance	**:**	
Company of Pennsylvania	**:**	
(in Rehabilitation)	**:**	**No. 1 SHP 2020**

STATE INSURANCE REGULATORS' REBUTTAL POST-HEARING MEMORANDUM

In accordance with the Court's Order of May 24, 2021, the Intervenors Superintendent of Insurance of the State of Maine, Commissioner of Insurance of the Commonwealth of Massachusetts, and Insurance Commissioner of the State of Washington submit this rebuttal memorandum to respond to certain arguments made by the Rehabilitator[1] in the Rehabilitator's Proposed Findings of Fact and Conclusions of Law (the "Rehabilitator Filing" or, when particular findings or conclusions of law are cited, "Rehabilitator Findings ¶ __" or "Rehabilitator Conclusions ¶ __").[2]

[1] In this rebuttal memorandum, the State Insurance Regulators use terms as defined in the State Insurance Regulators' Post-Hearing Memorandum ("SIR Mem.") and Proposed Findings of Fact and Conclusions of Law ("SIR Findings").

[2] The State Insurance Regulators address only salient issues in this memorandum. That the State Insurance Regulators may not address an issue or proposed finding or conclusion does not indicate agreement with the Rehabilitator. The Rehabilitator's post-hearing submission did not include a memorandum. The Rehabilitator has thus avoided addressing substantive issues until her rebuttal filing so that the State Insurance Regulators will not have an opportunity to respond.

I. THE REHABILITATOR DOES NOT ADDRESS GUARANTY ASSOCIATION SUPPORT AND THE BEST INTEREST OF POLICYHOLDERS.

The most notable flaw in the Rehabilitator's post-hearing submissions is the omission of any reference to the support available from Guaranty Associations. The Rehabilitator fails to address the financial interest of policyholders in enforcement of their existing policies and the ability of Guaranty Associations to provide substantial benefits to fulfill SHIP's obligations under those policies. The Rehabilitator focuses on subsidiary rationales, not the core issue – the best financial interest of policyholders.

A. The Rehabilitator Ignores The $800 Million Benefit Of Guaranty Association Coverage And The Impact Of The Plan In Reducing That Coverage.

The Rehabilitator's Findings and Conclusions simply ignore the undisputed evidence that policyholders stand to receive at least $800 million more in benefits in a liquidation than they will receive under the Plan.

Under the Plan, the present policyholders bear the entire $1.224 billion Funding Gap. SIR Findings ¶¶ 60, 63. In a present liquidation, the Guaranty Associations would be triggered and provide benefits based upon the policyholders' current policies so that policyholders would only bear a loss of $397 million. SIR Findings ¶ 64. The Guaranty Associations would bear the difference. The Guaranty Associations would receive a 49% dividend from the

SHIP estate, but they would contribute over $800 million in additional support. SIR Findings ¶ 65. Guaranty Associations thus would spread the loss from SHIP's insolvency beyond SHIP's remaining policyholders. *See* SIR Findings ¶ 18.

The Rehabilitator does not even attempt to explain how the Plan could be in the policyholders' best financial interest given this huge impact.

The effect of the Plan is to reduce the benefits that would be available from Guaranty Associations in a future liquidation. This is because in a future liquidation the Guaranty Associations would only provide coverage for the policies as modified under the Plan. SIR Findings ¶¶ 30, 70-71. The Rehabilitator's vague proposed finding that policyholders do not give up "absolute rights" to Guaranty Association coverage (Rehabilitator Finding ¶ 102) obscures the fact that (a) those who select Options 1, 2, 2a, or 3 retain Guaranty Association coverage only for the reduced benefits under the modified policies (SIR Findings ¶¶ 69-71), and (b) those who select Option 4 retain Guaranty Association coverage for the original benefits only if Phase Two is not reached. *See* SIR Findings ¶ 27.

The Rehabilitator has now conceded that the Plan is unlikely to eliminate the Funding Gap (SIR Findings ¶ 90), so the Plan is clearly just a way-station for SHIP on its way to liquidation. The Plan serves principally to give 30,000 of the remaining policyholders a "haircut" and reduce the cost to the Guaranty Association system.

B. The Rehabilitator's Articulated Goals Do Not Justify Ignoring The Benefit Of Guaranty Association Coverage.

The hearing and Rehabilitator's Filing make clear that the Rehabilitator is seeking approval of the Plan in pursuit of goals other than the best financial interest of policyholders. In her filing, the Rehabilitator offers a three-part rationale consisting of "meaningful choice," addressing rate "inequities," and reducing the deficit. Rehabilitator's Findings ¶¶ 57-59. None of these rationales support depriving policyholders of $800 million in Guaranty Association coverage.

1. The Plan's Goal of Reducing the Funding Gap Does Not Benefit Policyholders.

The Rehabilitator contends that the Plan seeks to "substantially reduce or eliminate" the Funding Gap (Rehabilitator's Findings ¶ 59) and that she "offered expert and factual testimony for the proposition that Phase One of the Plan is reasonably anticipated to reduce SHIP's deficit materially" (*id.* ¶ 106). But that deficit reduction on the backs of policyholders is not a "proper objective" (Rehabilitator Conclusions ¶ 32). It is actually adverse to policyholders because it results from benefit cuts and premium increases. SIR Findings ¶¶ 60, 63. That the Funding Gap may be reduced and policyholders receive less under the Plan is a detriment, not an advantage. Policyholders will receive more in a liquidation.

The Rehabilitator has lost sight of the actual purpose of a rehabilitation proceeding – to protect policyholders by honoring their policies. The goal of

rehabilitation is not just to restore the company to solvency, but to do so in a way that benefits policyholders. The intent of the rehabilitation statutes is to "minimize the harm to all affected parties." *Foster v. Mutual Fire, Marine & Inland Ins. Co.*, 614 A.2d 1086, 1094 (Pa. 1992) ("*Mutual Fire II*"). *See* 40 P.S. § 221.1. This requires that a rehabilitation plan minimize harm to policyholders, as the statutes aim to protect them. *See* 40 P.S. § 221.44; Ex. RP-55 at 21.

The Plan, however, seeks to restore SHIP's fiscal health merely by reducing benefits and increasing premiums. Indeed, the Rehabilitator's Filing does not contend that the Plan is good for policyholders (except in addressing rates prospectively and providing "choice") but "good for SHIP." Rehabilitator Findings ¶ 108. The company may be better off, but the policyholders are worse off. A plan that attempts to restore solvency at the expense of policyholders is not a proper rehabilitation plan.

The Rehabilitator asserts that public policy dictates rehabilitating an insurer if at all possible. Rehabilitator Conclusions ¶ 18. But this assertion assumes that rehabilitation will protect contractual policy benefits and that liquidation will not. *See In re Rehabilitation of American Investors Assur. Co.*, 521 P.2d 560, 562 (Utah 1974) ("The company either must be liquidated and its assets distributed to the creditors with the consequence of injury to the policyholders who are deprived of insurance protection or the business must be rehabilitated."); *Carpenter v. Pacific*

Mut. Life Ins. Co., 74 P.2d 761, 775 (Cal. 1937) ("*Carpenter*") ("Either the company must be liquidated, and its assets distributed to its creditors, thus immeasurably injuring many of its policyholders who are thus deprived of insurance protection, or the business must, if possible, be rehabilitated."), *aff'd sub nom. Neblett v. Carpenter*, 305 U.S. 297 (1938) ("*Neblett*"). The Commonwealth Court articulated this in *Mutual Fire*, stating that the goals of Article V "are better served by a rehabilitation which effectively ensures more distribution in a shorter period of time than would occur in a liquidation." *Grode v. Mut. Fire, Marine and Inland Ins. Co.*, 572 A.2d 798, 803 (Pa. Commw. Ct. 1990) ("*Mutual Fire I*"), *aff'd*, *Mutual Fire II*, 614 A.2d 1086 (Pa. 1992).

That is not the case here. This Plan does not protect contractual benefits – it cuts them. It does not ensure "more distribution" than a liquidation, but less. "Rehabilitation" is desirable only if it protects policyholders' contractual rights better than the alternative. Here, liquidation better serves policyholders because it would make available more than $800 million in additional support from Guaranty Associations for the benefit of policyholders. It does not benefit policyholders to have a less insolvent insurer (made so only because policyholders have suffered reduced benefits and increased premiums) that offers less protection than could be obtained through liquidation.

2. "Meaningful Choice" Is Not a Substantial Benefit, and It Is Available from Guaranty Associations in Liquidation.

The Rehabilitator asserts that the Plan will offer policyholders "meaningful choice." Rehabilitator Findings ¶ 57. In her opening, the Rehabilitator said that the availability of choice matters because it "gives the policyholders a choice in allocating the loss for themselves." Tr. 7. But it makes no sense to say that policyholders benefit from choosing how to allocate the loss when the liquidation alternative actually reduces the loss by triggering Guaranty Association coverage. Policyholders are not better off agreeing how to allocate a $1.2 billion loss instead of triggering Guaranty Associations and suffering a lesser $400 million loss.

Moreover, "meaningful choice" is not available only under the Plan. The Rehabilitator's proposed findings on this issue (¶¶ 57, 61, 95, 99, 132) disregard the evidence at the hearing showing that meaningful choice is also available to policyholders in a liquidation. To the extent that policyholders may want to reduce their benefits (and be charged lower premiums) or maintain their coverage (for increased premiums), the evidence at the hearing was that Guaranty Associations could provide options that reduce coverage below Guaranty Association limits at lower premium or retain coverage (up to Guaranty Association limits) at higher premium. *See* SIR Findings ¶¶ 51-52. The option that Guaranty Associations clearly could not provide – Option 4's retaining of full coverage in excess of

Guaranty Association limits for If Knew premium (*see* SIR Findings ¶ 53) – is illusory in rehabilitation because policyholders choosing Option 4 in Phase One face substantial premium increases or benefit cuts in Phase Two based on Self-sustaining Premium. *See* SIR Findings ¶¶ 27, 101. Against this background, the unquantifiable "intangible benefit" of "choice" cannot justify depriving policyholders of the substantial economic benefits of Guaranty Association coverage. SIR Findings ¶ 48.

3. Using If Knew Premium Does Not Benefit Policyholders as a Group, and Guaranty Associations Can Use If Knew Premium in a Liquidation.

The Rehabilitator contends that the Plan remedies rate discrimination and subsidies by applying If Knew Premium nationwide. Rehabilitator Findings ¶ 58. But remedying asserted rate discrimination does not benefit policyholders as a group. It just adjusts relative benefits and burdens among SHIP's remaining policyholders. The Rehabilitator's findings do not explain how all policyholders are better off by the application of If Knew premium methodologies. That 30,000 of SHIP's 646,000 historical policyholders may share the $1.2 billion burden of SHIP's insolvency in what the Rehabilitator views as a more equitable manner does not make those policyholders, as a class, better off in comparison with a liquidation where the loss would be reduced to $400 million.

Moreover, the adjustment of rates that the Rehabilitator seeks can in great part be achieved in a liquidation. The Rehabilitator's proposed findings on this issue (¶¶ 58, 73) ignore the evidence that, in a liquidation, the Guaranty Associations can seek rate increases and, based on the Penn Treaty experience, will do so based on If-Knew Premium. SIR Findings ¶¶ 54-58. If Knew rates are likely to be the rates that apply prospectively in a liquidation, and the Guaranty Associations' rate methodology thus will largely address the Rehabilitator's concerns. SIR Finding ¶ 56. *See* Rehabilitator Findings ¶ 112 (noting that the If Knew premium methodology "is consistent" with the Guaranty Associations' methodology in Penn Treaty).

In sum, none of the Rehabilitator's three articulated rationales for the Plan justify imposing the burden of insolvency on the remaining SHIP policyholders when that burden can be greatly reduced by triggering the Guaranty Associations in a liquidation. The Rehabilitator's proposal of the Plan on these grounds is an abuse of discretion.

C. The Plan Cannot Be Justified On The Ground That The Policyholders Do Not Deserve Guaranty Association Coverage.

The Rehabilitator's findings are silent on this issue, but the evidence is clear that the Rehabilitator chose the Plan in great part based on a belief that that SHIP's policyholders are undeserving of Guaranty Association protection. *See* SIR Findings ¶¶ 75-77. This constitutes legal error and an abuse of discretion.

During the hearing, the Rehabilitator's principal witness – Mr. Cantilo, the Special Deputy Rehabilitator – made clear several times that the Rehabilitation team believed that SHIP policyholders had been "underpaying" for coverage (Tr. 78, 295), that the coverage they had purchased was "rich" (Tr. 102) or "not necessary" (Tr. 86) and that the policies should be "right size[d]" (Tr. 79, 194). *See* Tr. 78-79, 86-87, 102, 194-195, 295. *See also* Tr. 88-89 (asking what the policyholders' "legitimate interests" were).[3] Indeed, in opening, the Rehabilitator's counsel referred to "expensive, sometimes unwanted or unneeded benefits." Tr. 7. As a consequence of this view, the Rehabilitation team believed that it would be "unjustified" to trigger Guaranty Association support which would be funded by member insurers and ultimately rest on taxpayers or other companies' policyholders. Tr. 78-79, 172, 295.

In the most revealing passage, Mr. Cantilo testified:

> [W]e knew that a lot of policyholders had been underpaying for their policies for a long period of time, decades, and we knew that if we came to this Court requesting a liquidation order, that a likely consequence is that the guaranty associations would be triggered, then, ultimately, the taxpayers would be asked to step up and contribute hundreds of millions of dollars to pay claims under those policies.
>
> And the question that we were debating is, is it reasonable, if a policyholder has been paying a quarter for a dollar's worth of

[3] Mr. Cantilo acknowledged policyholders "are paying everything they were asked to pay" and are not "at fault." Tr. 295, 296.

> insurance for decades, to adopt, as the workout plan, a plan in which the taxpayers step up to pay their remaining 75 cents.
>
> And what we concluded is that we could right size the policy, and we could create a set of options for policyholders that would enable them to get fundamental LTC coverage but pay reasonable rates like the rest of the country and not shift all that burden to taxpayers.

Tr. 78-79.

This is a "policy judgment" (Tr. 295) that the Rehabilitator was not authorized to make because it conflicts with the statutory scheme. The policyholders paid the lawfully approved rates and have enforceable contracts. SIR Findings ¶ 3. As set forth in the State Insurance Regulators' Post-Hearing Memorandum, the state legislatures established Guaranty Associations to protect policyholders by fulfilling the contractual obligations of insolvent insurers (subject to specified limits), and they chose how to fund the Guaranty Associations and thus how to spread the burden caused by an insurer's insolvency. SHIP's policyholders are entitled to the protections that the legislatures have created and that reflect the public policy of their States. It is an error of law and an abuse of discretion for the Rehabilitator to propose a Plan to avoid providing Guaranty Association coverage because the policyholders do not, in the Rehabilitator's estimation, deserve that legislatively established protection.

D. The Rehabilitator's Vague Proposed Findings Should Be Rejected And In Any Event Are Insufficient To Support The Plan.

The Rehabilitator proposed many findings that attempt to sweep away the State Insurance Regulators' evidence by saying in various ways that "no evidence" or "no contravening evidence" was offered on various points. *See, e.g.*, Rehabilitator's Findings ¶¶ 46, 47, 49, 87, 88, 99, 102, 122, 130, 131, 134. The Court should decline these proposed findings because they disregard evidence presented by the State Insurance Regulators both on cross-examination of the Rehabilitator's witnesses and through their own witness and exhibits. That evidence is summarized in the State Insurance Regulators' Proposed Findings of Fact, Post-Hearing Memorandum and this Memorandum, and the State Insurance Regulators will not repeat all that evidence here. However, a few points warrant comment:

The Rehabilitator fails to acknowledge the undisputed evidence – based on the Rehabilitator's own Comparison File – that the Guaranty Associations will provide over $800 million in additional support in a liquidation so that policyholders will suffer a much greater loss under the Plan than in liquidation.

The Rehabilitator's assertions that the Plan should be approved because it provides choice are vague and disregard the evidence that Guaranty Associations can provide similar choices in a liquidation, subject to their limits.

The Rehabilitator's claims that the Plan should be approved because it prospectively addresses asserted rate discrimination through If Knew rates ignores the evidence that Guaranty Associations can use If Knew rates in a liquidation.

The Rehabilitator's arguments that the Plan satisfies *Neblett* disregard the evidence that only under the inappropriate MPV metric could all policyholders fare as well in rehabilitation as in liquidation (in Phase One); that MPV does not measure value; that under other comparisons including the proper net present value measure substantial percentages of policyholders are worse off in rehabilitation (in Phase One); that none of the Rehabilitator's comparisons consider the impact of Phase Two; and that Phase Two premium increases on Option 4 selectors reduce the percentage of policyholders that could fare better in rehabilitation – a 100% increase in the net present value scenario reduces that percentage to less than 50%.

The Rehabilitator's assertions that there is no evidence of harm to the State Insurance Regulators from the Plan's displacement of their statutory authority and that the "opt-out" provision cures any violation ignores the Maine, Massachusetts and Washington statutes and the coercive requirements imposed by the opt-out provision.

II. THE PLAN IS NOT FEASIBLE.

The Rehabilitator does not contend that the Plan has a reasonable likelihood of restoring SHIP to solvency. That, however, is the proper goal for a plan

(assuming it can be achieved other than by just imposing the loss on the policyholders). *See Mutual Fire II*, 614 A.2d at 1094 (ultimate goal of plan is that company "reemerge as a solvent insurer"), 1096 (goal is to manage company's affairs "with the intended result of restoring the entity to sound fiscal status"). The Rehabilitator's findings say only that Phase One of the Plan "is reasonably anticipated to reduce SHIP's deficit materially." Rehabilitator Findings 106.[4] Accordingly, the Plan is not feasible, and it should be disapproved. In any meaningful sense, the Plan is futile. *See* 40 P.S. § 221.18.

The Rehabilitator attempts to get around this by arguing that there is in fact no feasibility requirement (Rehabilitator' Findings ¶ 34),[5] and also that the Plan has "substantial benefits" even if SHIP is not restored to solvency and must be liquidated. *See* Rehabilitator's Findings ¶¶ 107-108, 121-122. These positions should be rejected.

[4] The finding continues that Phase One "could even" eliminate the deficit altogether. Rehabilitator Findings 106. This is speculation. The Rehabilitator's principal witness conceded that it was not likely the Plan would "magically" do so. *See* SIR Finding ¶ 90.

[5] The Rehabilitator also reiterates her argument that feasibility means "properly conserving and equitably administering the assets of the involved insurer." Rehabilitator Finding ¶ 35. This deprives the standard of any meaning. The quoted language is found in *Mutual Fire II*, but only in noting that a plan need not restore the company "to its exact original condition." 614 A.2d at 1094. Merely conserving and administering SHIP's assets without some actual policyholder-protective goal serves no purpose. The Rehabilitator can cite to no precedent anywhere for this proposition.

A showing of feasibility is required to approve the Plan. The Rehabilitator acknowledged this in her application for approval of the original plan of rehabilitation and subsequent filings. Application for Approval of The Plan of Rehabilitation for Senior Health Insurance Company of Pennsylvania ¶ 2 (April 22, 2020); Rehabilitator's Response to Intervenor State Insurance Regulators' Renewed Application for Order Directing the Rehabilitator to Provide Reports and Analyses at 11 (November 24, 2020). The Court also recognized that a reasonable likelihood of success was required during the February 24, 2021 pre-hearing conference. February 24, 2021 Tr. 31. While the Pennsylvania cases do not expressly require feasibility, *see Mutual Fire II*, 614 A.2d at 1090 (referring to feasibility reports), that is because it is a self-evident requirement that is not usually at issue. (If a rehabilitator believed that a plan was not likely to rehabilitate the company by restoring solvency, then as a general matter she or he would not propose it because it would be futile.).

The feasibility requirement serves to protect policyholders. In this case, implementing the Plan will lead to reductions in policy benefits without any reasonable prospect of the company being returned to solvency. Nevertheless, under the Plan, those reductions will be permanent. They will thus reduce the coverage available to the policyholders when SHIP is eventually liquidated. SIR Findings ¶¶ 31, 70-71.

The Rehabilitator contends that Phase One of the Plan offers unspecified "substantial benefits" even if SHIP will be liquidated. Rehabilitator Findings ¶¶ 121-122; *see id.* ¶¶ 107-108. The potential "substantial benefits," however, are objectives distinct from benefits to policyholders, and can also be obtained in a liquidation. As described above, the first asserted benefit, "meaningful choice," only serves to allocate loss and can be substantially achieved in a liquidation through choices offered by Guaranty Associations, as in Penn Treaty. The second benefit, addressing asserted rate discrimination and subsidies by use of If Knew Premium prospectively, does not benefit policyholders as a group and can be achieved by Guaranty Associations in liquidation, as in Penn Treaty. The third asserted benefit, reducing the Funding Gap, just gives the current policyholders a haircut and does not advantage policyholders but rather benefits the insurance companies and others who fund the Guaranty Association system.

The Rehabilitator's attempt to avoid a feasibility determination appears to be an effort to allow her to adjust policyholder contract rights in advance of liquidation because her team views the policies as extravagant "Cadillac" policies (Tr. 102) not worthy of Guaranty Association protection.

III. THE PLAN DOES NOT SATISFY *NEBLETT*.

The Rehabilitator offers vague proposed findings concerning the "no worse than liquidation" standard of *Neblett v. Carpenter*, 305 U.S. 297 (1938). As the

State Insurance Regulators have previously contended, *Neblett* requires that all policyholders have an option that provides at least the value they would obtain in liquidation. SIR Post-Hearing Mem at 21-24. Only one of the comparisons offered by the Rehabilitator purports to show that all policyholders fare at least as well in rehabilitation as in liquidation, and that "maximum policy value" comparison is not meaningful and is not a measure of contract damages as required by *Neblett*. Furthermore, all of the comparisons offered by the Rehabilitator are limited to Phase One and so necessarily understate the impact of the Plan on policyholders.

The Rehabilitator's assertion that under the five methodologies she now proposes "all or the vast majority of policyholders do at least as well under the Plan as they would in liquidation" (Rehabilitator's Findings ¶¶ 114, 129; *see id*. at 110, 130) is a vast overstatement. Under only <u>one</u> of those measures – "maximum policy value" – do all policyholders have a Phase One rehabilitation option at least as good as liquidation. *See* Ex. RP-47. Under all the other measures between 21% and 4% of policyholders are better off in liquidation than under Phase One of the Plan. Exs. RP-43 to RP-46.

The Rehabilitator's late-arriving (with her Pre-Hearing Rebuttal Memorandum on April 19, 2021) maximum policy value ("MPV") comparison in Exhibit RP-47 has little meaning. That measure is only the maximum daily benefit

times maximum benefit period. It ignores the premium charged for the policy and the expected claims under the policy. *See* SIR Post-Hearing Mem. at 27. Under that measure, a policy that provides $10 of daily coverage for 10 years has the same "value" as a policy providing $100 of daily coverage for one year,[6] and that would be the case even if the premium for the first policy were 10 times the premium for the second. MPV is not a measure of value, just maximum exposure.

Moreover, as the Rehabilitator recognizes (Rehabilitator Conclusions ¶ 55), *Neblett* set a policy's value at the amount of damages recoverable on breach. 305 U.S. at 305. *See* SIR Post-Hearing Mem. at 25-28. MPV is not such a measure. *See* SIR Findings ¶¶ 121-126. The standard is not whether the policyholder retains "as much coverage" as liquidation (Rehabilitator Findings ¶ 92, Conclusions ¶ 62), but whether the policyholder retains as much value. The Rehabilitator's argument that policyholders have individual preferences (*e.g.*, Rehabilitator's Findings ¶¶ 116-120) similarly disregards the constitutional standard established in *Neblett*. That standard looks to economic value – contract damages – not subjective individual preference.

[6] The Plan keeps Option 2 MPVs at Guaranty Association limits or present MPV by extending maximum benefit periods. Ex. RP-55 at 49 ("The adjustments will be made by lengthening the MBP."), 52, 54, 55, 57. Of course, longer benefit periods are not necessarily valuable where the policyholders' life expectancies are short. *See* Tr. 87.

Where the *Neblett* standard is economic, it is properly assessed using net present value. The Rehabilitator acknowledges that net present value is the appropriate measure to assess the value of a policy for purposes of reporting the insurer's financial condition. Rehabilitator's Findings ¶ 115. At the hearing, Mr. Cantilo acknowledged that net present value can be described as "Carpenter value" (SIR Findings ¶ 105), and that using net present value to compare rehabilitation and liquidation is not unreasonable (SIR Findings ¶ 108). Indeed, the Rehabilitator used net present value in the rehabilitation/liquidation comparison posted to the data site – the Rehabilitator's Comparison File (Ex. RP-6) and comparison exhibit (Ex. RP-7). *See* Ex. RP-32. *See also* SIR Findings ¶¶ 103-104, 119, 130-133. The RP-7 comparison exhibit was later included (without text) as Exhibit RP-43. The Rehabilitator's proposed findings conspicuously omit any reference to Exhibits RP-6 and RP-7 except as general background.

The Rehabilitator's proposed findings that the State Insurance Regulators did not offer evidence contravening the Rehabilitator's evidence that "at least in Phase One" all policyholders have an option that would enable them to fare as well as in liquidation (Rehabilitator's Findings ¶¶ 129-130) are simply wrong. Those findings depend exclusively on MPV, and that measure is (1) incorrect under *Neblett*, and (2) reflective only of maximum exposure, not economic value. *See* SIR Findings ¶¶ 121, 124-126.

In any event, even if *Neblett* only required that some substantial majority of policyholders have an option with a value at least that of liquidation (which it does not), the Rehabilitator's reliance on Exhibits RP-43 to RP-47 is misplaced. Those exhibits only concern Phase One, as do the Rehabilitator's proposed findings (¶¶ 122, 129). The percentages of policyholders with a Phase One option at least as good as liquidation depends principally upon the availability of Option 4. SIR Findings ¶ 111-112. Option 4 will likely look substantially different in Phase Two, when Option 4 selectors will be subject to adjustments based on Self-sustaining Premium. *See* SIR Findings ¶ 25-27. The Rehabilitator pointedly has not analyzed Phase Two (SIR Findings ¶ 102), and that Phase will produce a worse result for policyholders who selected Option 1 and Option 4 in Phase One. *See* SIR Findings ¶¶ 25-27. The Rehabilitator's proposed findings disregard the undisputed evidence that Phase Two premium increases can readily reduce the percentage of policyholders who fare at least as well in rehabilitation as in liquidation to less than 50%. *See* SIR Findings ¶ 116.

The Health Insurers contend that *Neblett* does not require that all policyholders receive what they would receive in a liquidation because individual interests can be "sacrificed or compromised to preserve the ultimate goal of [the rehabilitation] process." Health Insurer's Post-Hearing Memorandum at 23 (quoting *Mutual Fire II*, 614 A.2d at 1102). However, that presumes that the Plan

has a legitimate rehabilitative goal and could satisfy the test of *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, 459 U.S. 400 (1983). *See Mutual Fire II*, 614 A.2d at 1094 n. 4. Here, the Plan substantially impairs contract rights at least because Phase Two substantially reduces benefits even for those who select Option 4 in Phase One. SIR Findings ¶¶ 27, 114. Further, as discussed at pages 2-11, 13-16, the Plan has no legitimate rehabilitative purpose and is unreasonable. It does not seek to restore SHIP to solvency but to impose and allocate loss on policyholders in the face of the Guaranty Association system intended to protect them. The Plan does not claim to make all policyholders better off in the long-run by imposing a short-term burden on some policyholders, as suggested by the California Supreme Court in *Carpenter* (but not by the United States Supreme Court in *Neblett*). *See Commercial National Bank v. Superior Court*, 17 Cal. Rptr. 2d 884, 890-891 (Cal. Ct. App. 1993) (discussing *Carpenter*, 74 P.2d at 778-779)).

IV. THE PLAN'S DISPLACEMENT OF STATE INSURANCE REGULATORS' AUTHORITY IS UNLAWFUL.

The Plan attempts to oust state regulators of jurisdiction over rates in their States by substituting the Rehabilitator and Court as rate-approving authorities. The Rehabilitator's arguments on this point have no merit.

The Rehabilitator first contends that the Plan does not harm the State Insurance Regulators. *See* Rehabilitator's Findings ¶¶ 87-91. However, the Rehabilitator's witnesses agreed that the standard rule is that issue states control

rates, *see* SIR Findings ¶¶ 78-80, and the State Insurance Regulators have identified the state statutes that require them to approve rates for policies issued to their residents. 24-A Me. Rev. Stat. § 2736; Mass. G.L. c. 175, § 108(8)(A); Wash. Rev. Code § 48.83-.84, 48.18.110. The Plan, by its terms, states that the Rehabilitator will not request such approval and that the Commonwealth Court will approve the rates in all states. Ex. RP-55 at 33-34, 95-96. That in and of itself constitutes harm to the regulators charged with enforcing their state insurance laws (24-A Me. Rev. Stat. § 211; Mass. G.L. c. 175, § 3A; Wash. Rev. Code § 48.01.020, 48.02.060) and whose authority is being deliberately disregarded.

The Rehabilitator makes the related argument that the state statutes are not violated because they do not say that the State Insurance Regulators' rate approval authority is exclusive. Rehabilitator Conclusions ¶¶ 29, 46. This is absurd. Where statutes require approval of rates in the State by the State's insurance regulator, it violates the statutes to substitute someone else (*e.g.*, the Rehabilitator or Commonwealth Court) as the approving authority. The statutes do not need to say that no one else can approve the rates to be used in their States. That is implicit in the requirement that the rates be approved by the applicable State Insurance Regulator.

The Rehabilitator also suggests that that there is no harm because If Knew rates satisfy the rate statutes. *See* Rehabilitator's Findings ¶¶ 48-49. *See also id.*,

¶¶ 69, 71, 74. There is no basis to conclude that the Rehabilitator's If Knew rates necessarily comply with state requirements. The proposed findings disregard the testimony elicited on cross-examination that state insurance regulators do not always accept If Knew rates, and that each state's approval process is different and applies varying procedures and standards. SIR Findings ¶ 87. In any event, the Plan provides for Self-sustaining Premiums in Phase Two, and the Rehabilitator's witnesses did not address whether Self-sustaining Premium would comply with rate statutes. SIR Findings ¶ 86.

Further, Mr. Bodnar testified that If Knew rates under the Plan are not supported by a "traditional" actuarial memorandum, and that memorandum, when prepared, will be provided to the Rehabilitator so that she (as Insurance Commissioner) can review the rates. Tr. 458, 460, 461. *See* Rehabilitator Findings ¶ 79. Where the Rehabilitator herself has not yet been provided with the actuarial support for If Knew rates and has not yet approved them, she cannot reasonably contend that the rates necessarily satisfy the requirements of other states (which are to be enforced by those States' regulators under their own statutes and procedures).

The Rehabilitator's contention that the issue state rate approval provision "cure[s] entirely" (Rehabilitator Finding ¶ 88) harm to the State Insurance Regulators should also be rejected. That provision effectively requires regulators

to approve the Rehabilitator's rate submission "in full" within 60 days (Ex. RP-55 at 111), or else policyholders in the State will be disadvantaged. *See* SIR Findings ¶¶ 35-36, 38, 81-84; Rehabilitator's Findings ¶ 84 (if opt out state insurance regulator does not "timely" approve the Rehabilitator's rates, the policies issued in that state "may face a benefit modification"). The provision nominally "allows" state regulators to review rates but, given the timeframes and consequences of non-approval, effectively coerces approval of the Rehabilitator's rates lest policyholders in the State be placed in an even worse position. It does not preserve the issue state's authority over rates.

Finally, the Rehabilitator's suggestion that the Commonwealth Court's *in rem* jurisdiction encompasses setting rates for policies in other states (Rehabilitator Conclusions ¶¶ 52-53) is unsupported. The Court's control over SHIP's assets and business does not somehow encompass or displace the regulatory roles that regulators in other States have under their own laws concerning business transacted in their States. *See Hanson v. Denckla*, 357 U.S. 235, 246 (1958) ("Founded on physical power, the *in rem* jurisdiction of a state court is limited by the extent of its power and by the coordinate authority of sister States.") (citation omitted); *In re Rehabilitation of National Heritage Life Ins. Co.*, 656 A.2d 252, 259-261 (Del. Ch. 1994) (*in rem* nature of domiciliary proceeding does not support turnover orders directed to persons in other States). *Cf. Robbins v. Reliance Ins. Co.*, 102 S.W.3d

739, 742-743 (Tex. Ct. App. 2001) (Pennsylvania Commonwealth Court in rehabilitation proceeding does not have authority to order a stay of litigation in another state). The independent roles of the States in this regard are longstanding and must be respected under the Full Faith and Credit Clause.

The Health Insurers continue to contend that the question of rate approval is merely a choice of law issue. However, this is not a dispute about interpretation of an insurance policy.[7] It is about an "unprecedented" (Tr. 82) effort to displace State regulation. The question whether a Pennsylvania court operating under rehabilitation statutes can be substituted for the regulators of other States and their statutes in determining rates is not "procedural" or a "false conflict." Nor is it just a question of choice of law to be determined based on an aggregation of interests. It is an attempt to project the Rehabilitator's policy preferences into other States which, prior to SHIP's rehabilitation, unquestionably had the exclusive responsibility to protect their residents by reviewing rates to be charged, and to assume control of the rates in those States. The rehabilitation statutes do not authorize this, and the Full Faith and Credit Clause prohibits it.

[7] Even where an insurer is in liquidation, the law of the domiciliary state does not displace the law that would otherwise govern a policy. *In re Liquidation of Midland Ins. Co.*, 947 N.E.2d 1174, 1179-1182 (N.Y. 2011); *Viacom, Inc. v. Transit Cas. Co.,* 138 S.W.3d 723, 726 (Mo. 2004). *See also In re Liquidation of Integrity Ins. Co./Sepco Corp.*, 49 A.3d 428, 435 n. 3 (N.J. App. Div. 2012) (rejecting blanket rule).

V. THE INTERVENOR STATE INSURANCE REGULATORS ARE PROPERLY HEARD.

The Rehabilitator now seeks to remove the State Insurance Regulators from this matter by proposing – in her second-to-last conclusion of law – that the State Insurance Regulators "have not established any interest such that they should remain involved in the implementation of the Plan" and that they be dismissed as intervenors. Rehabilitator Conclusions ¶ 67. The Court should reject the Rehabilitator's attempt to have the Court reconsider allowing the State Insurance Regulators to intervene (without even filing an application).

First, the Court has already recognized that the State Insurance Regulators have the requisite interest in the Plan by granting their application to intervene, which allows them to participate in the plan approval proceedings as parties. The State Insurance Regulators applied to intervene for several reasons as set forth in their application:

- The initial Proposed Plan specifically identified other state insurance departments as "affected parties," and the Rehabilitator seeks to have them "bound by the Court's approval of the Plan, and its modification of policies and premium rates as part of the Plan." *See* Proposed Plan at 80. The Proposed Plan acknowledged that state insurance departments should be "provided an opportunity to object." *Id*.[8]

[8] The Second Amended Plan continues to provide that "[s]o long as all affected parties (including other state insurance departments) are provided an opportunity to object, they will be bound by the Court's approval of the Plan, and its modification of policies and premium rates as part of the Plan." Ex. RP-55 at 96.

- Each of the State Insurance Regulators is the public official charged by the laws of their States with enforcing state insurance laws and regulating insurers. *See* Maine Insurance Code, Title 24-A of the Maine Revised Statutes, specifically, 24-A Me. Rev. Stat. § 211; Massachusetts General Laws, Chapter 175; specifically, M.G.L. c. 175, § 3A; Wash. Rev. Code §§ 48.01.020; 48.02.060.[9]

- The State Insurance Regulators have a direct and substantial interest in the Plan because SHIP was licensed and does business in each of their States. The State Insurance Regulators review and approve SHIP's long-term care policy rates based on its rate applications in their respective States. The Plan seeks to displace their regulatory authority.

- The State Insurance Regulators have a direct and substantial interest in the Plan because SHIP policyholders in each of their States will be subject to the Plan, if approved. Those policyholders will be affected by the premium increases and the benefit reductions proposed under the Plan, including – for policyholders in the State on premium waiver – the Plan provisions regarding premium waiver.

- The State Insurance Regulators have a regulatory interest in seeing that the contract rights of policyholders in their States are respected; that the standards and protections of the statutory rate-setting process are honored for the protection of policyholders; and that the rate-setting process established by their States' statutes are preserved to protect state sovereignty and inter-state comity.

These interests were set forth in the Maine Superintendent of Insurance's and the Massachusetts Commissioner of Insurance's Joint Application for Intervention

[9] *See Bankers Life & Cas. Co. v. Superintendent of Ins.*, 60 A.3d 1272, 1273 (Me. 2013) ("The Superintendent of Insurance has licensing and oversight authority over insurance companies and agents who sell insurance and annuity products to the public."); *Premera v. Kreidler*, 131 P.3d 930, 940 (Wash. App. Ct. 2006) ("To protect the public in insurance matters, 'the legislature created the office of Insurance Commissioner and conferred upon that office the duty of enforcing the provisions of the code.'") (quoting *Ins. Co. of North America v. Kueckelhan,* 425 P.2d 669 (Wash. 1967)).

(July 31, 2020) and the Joinder of the Washington Insurance Commissioner in that Joint Application (September 15, 2020).

The Court granted the request of the Maine Superintendent of Insurance and the Massachusetts Commissioner of Insurance to intervene by Order dated September 15, 2020 and ordered that the Washington Insurance Commissioner was permitted to join with the intervention by Order dated September 18, 2020.

Where allowed to intervene, the State Insurance Regulators had the right to participate in the hearing on the Plan. They were not required to establish during the hearing that they have interests implicated by the Plan that warrant their being heard. That issue was determined when the Court allowed them to intervene. Accordingly, the Rehabilitator's attempt to attack the ability of the State Insurance Regulators to oppose the Plan should be rejected.

Second, the Rehabilitator's effort to prevent the State Insurance Regulators from being heard conflicts with the Plan and the process established by the Rehabilitator and Court. The Plan recognizes that it seeks to displace regulation by other States: "The Rehabilitator will not seek separate approval of rate increases or benefit reductions from insurance regulators in the states in which the policies were issued." Ex. RP-55 at 33-34. Recognizing that this is controversial and that the assertion of *in rem* jurisdiction aggressive, the Plan expressly contemplates that other States will have the opportunity to be heard:

> So long as all affected parties (including other state insurance departments) are provided an opportunity to object, they will be bound by the Court's approval of the Plan, and its modification of policies and premium rates as part of the Plan.

Id. at 96. The Rehabilitator recognized that state insurance regulators were "interested parties" in her Application for Approval of Form and Distribution of Notice ¶ 7 (April 22, 2020) (defining "Interested Parties" to include "the insurance regulatory authorities in the jurisdictions in which SHIP issued policies that remain in effect"). The Court similarly recognized the state regulators' interests in the Case Management Order ¶ 2 (June 12, 2020) (defining "Interested Parties" to include "the insurance regulatory authorities in each jurisdiction in which SHIP issued policies that remain in effect").

The Plan, Notice Application and Case Management Order all contemplate that insurance regulators may be heard on the Plan. The State Insurance Regulators followed the process set forth in the Case Management Order and applied for and obtained Intervenor status. They are entitled to rely on the Court's Order granting them that status.

Third, the Rehabilitator cannot both contend that the rates set by the Rehabilitator and approved by the Court as part of the Plan are binding on state regulators (*see* Ex. RP-55 at 96; Rehabilitator's Conclusions 52-54) and simultaneously attempt to prevent the State Insurance Regulators from being

heard.[10] Any argument that the Court's approval has binding extraterritorial effect requires that the State Insurance Regulators have a full and fair opportunity to be heard in this proceeding. If the State Insurance Regulators in fact may not be heard in objection to the Plan, it cannot arguably bind them.

Conclusion

For the above reasons and those in the State Insurance Regulators' Post-Hearing Memorandum, their Application to Reconsider Order Granting Rehabilitator's Oral Motion Regarding Issue State Rate Approval Issue, and their pre-hearing submissions, the Court should disapprove the Plan.

June 28, 2021

Respectfully submitted,

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[10] The State Insurance Regulators dispute that the Court is authorized to set extraterritorial rates under Pennsylvania law and contend that any such determination would violate the Full Faith and Credit Clause and principles of comity.

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PROOF OF SERVICE

I, Stephen G. Harvey, hereby certify that on June 28, 2021, I served the foregoing document on all parties appearing on the Master Service List.

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