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IN THE COMMONWEALTH COURT OF PENNSYLVANIA

Michael Humphreys, Acting Insurance Commissioner of the Commonwealth of Pennsylvania in his capacity as the Statutory Rehabilitator of Senior Health Insurance Company of Pennsylvania, Plaintiff	:	
	:	DOCKET NO.: 1 SHP 2022
v.	:	
Brian Wegner 12862 Tuskany Boulevard Carmel, IN 46032	:	
Paul Lorentz: 214 Wellington Parkway Noblesville, IN 46060	:	JURY TRIAL DEMANDED
Barry Staldine 6789 South Foster Branch Court Pendleton, IN 46064	:	
Protiviti Inc. 2884 Sand Hill Road Menlo Park, CA 94025 Defendants.	:	

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PLAINTIFF'S BRIEF IN OPPOSITION TO DEFENDANT BARRY STALDINE'S OBJECTIONS TO THE AMENDED COMPLAINT

Michael Humphreys, Acting Insurance Commissioner of the Commonwealth of Pennsylvania, in his capacity as the Statutory Rehabilitator of Senior Health Insurance Company of Pennsylvania ("SHIP")[1], by and through his undersigned counsel, files this Brief in Opposition to the Preliminary Objections filed by Defendant Barry Staldine ("Staldine") and respectfully requests that the Court overrule the objections and order Defendant Staldine to file an Answer to SHIP's Amended Complaint within twenty (20) days.

I. INTRODUCTION

Defendant Staldine's Preliminary Objections mischaracterize the law governing the statute of limitations and either dispute or ignore the facts averred in the Amended Complaint. They may be appropriate arguments for trial, or even for summary judgment (depending upon what discovery shows). But they are not appropriate at the pleading stage and must be overruled.

The Amended Complaint alleges years of clear misconduct and misrepresentations by Staldine, in concert with Wegner, Lorentz, and Protiviti. SHIP claims that Staldine caused SHIP to execute the Beechwood Re and Roebling Re

[1] As used throughout this Brief, the term "SHIP" refers to both the Senior Health Insurance Company of Pennsylvania and, where indicated by context, the Acting Insurance Commissioner of the Commonwealth of Pennsylvania, in his capacity as Statutory Rehabilitator.

transactions by misrepresenting them as beneficial to SHIP despite knowing that they were extraordinarily risky, likely to lose SHIP hundreds of millions of dollars, designed to conceal or misrepresent SHIP's true financial condition, and violated regulatory oversight requirements. SHIP further claims that Staldine consistently and repeatedly misrepresented SHIP's financial position by manipulating its actuarial and liability estimates. SHIP asserts that Staldine engaged in this malfeasance and made these misrepresentations as part of a conspiracy with the other Defendants, who were also officers at SHIP, to continuously conceal SHIP's true financial position and avoid regulatory, employment, or other consequences for their egregious mismanagement and falsehoods. Their plan was successful for many years.

Staldine engaged in this misconduct up until the time SHIP was placed into rehabilitation. He, along with Lorentz and Wegner before him, controlled SHIP, controlled SHIP's information, controlled SHIP's consultants, and prevented its Trustees and the PID from discovering their malfeasance or SHIP's true financial problems until such rehabilitation. Under these circumstances, Pennsylvania law provides that SHIP's claims did not accrue until after the rehabilitator was appointed on January 29, 2020, rendering SHIP's claims timely.

Staldine attempts to confuse these well-pled claims by disputing the facts in the Amended Complaint. Those arguments are simply inappropriate at this stage.

For the reasons set forth below, Defendant's preliminary objections must be overruled.

II. RELEVANT ALLEGATIONS IN AMENDED COMPLAINT

This action was initiated on January 28, 2022, by Michael Humphreys, acting on behalf of SHIP in his role as SHIP's statutory Rehabilitator by virtue of his appointment as the Acting Insurance Commissioner of the Commonwealth of Pennsylvania (the "Rehabilitator"), to recover funds SHIP lost as a direct result of Defendants' malfeasance and misrepresentations. SHIP filed its Amended Complaint on June 22, 2022, asserting the following claims: Breach of Fiduciary Duty against Defendants Wegner, Lorentz, and Staldine (Count 1); Breach of Fiduciary Duty against Defendant Protiviti (Count 2); Civil Conspiracy against all Defendants (Count 3); Negligence against all Defendants (Count 4); Breach of Contract against Protiviti (Count 5); and Negligent Misrepresentation against Defendants Wegner, Lorentz, and Staldine.

Each of the four Defendants filed Preliminary Objections to the Amended Complaint. As explained below, Staldine's objections are entirely without merit and improperly rest upon his disagreement with the facts alleged in the Amended Complaint and the reasonable inferences drawn therefrom. While some of Staldine's arguments may be appropriate for consideration at summary judgment, they are not proper at the pleadings stage.

The claims in the Amended Complaint are based upon misconduct the Defendants committed principally between 2014 and 2020. SHIP's claims relate to three categories of egregious mismanagement, each of which was concealed by the Defendants, who acted in concert to prevent SHIP's Trustees and the PID, from discovering or remedying their malfeasance. The specific allegations supporting each instance of misconduct are set forth in SHIP's Amended Complaint, and, for brevity, are merely summarized below.

Failing to Request Appropriate Rate Increases and Underestimation of Future Liabilities

As alleged in the Amended Complaint, Defendants Wegner, Lorentz and Staldine were aware of the underpricing of SHIP's policies due to the underestimation of future policy liabilities. In particular, these Defendants knew or should have known that SHIP's actuarial projections were based on faulty assumptions that, for example, understated morbidity, overstated morbidity improvement, overstated mortality, and overstated policy lapse and termination rates. (Am. Compl. ¶¶ 30 – 41). Defendants failed to request appropriate rate increases to respond to this problem.

Defendants Wegner (as CEO), Lorentz (as CFO) and Staldine (as COO and then CEO) operated in concert to oversee and maintain an interactive process with SHIP's appointed actuary, Milliman, that resulted in the faulty actuarial assumptions. Those faulty assumptions resulted in erroneous actuarial reports,

memoranda, and opinions that led to gross understatements of SHIP's future liabilities. These gross understatements appeared in SHIP's official Annual Statements at least for the years 2014 through and 2019. (*Id.*, ¶ 32), and led to an overstatement of SHIP's financial strength by creating the appearance of surpluses that did not exist, at least for the years 2014 through 2018. (*Id.*, ¶ 33).

Defendants Wegner, Lorentz and Staldine operated in concert to oversee and maintain a management enterprise that overstated SHIP's projected investment income and failed to acknowledge and properly account for lower-than-anticipated yields and other poor investment results. (*Id.*, ¶ 34).

They also operated in concert to oversee and maintain a management enterprise that initiated, designed, contributed to, oversaw, maintained and/or failed to report to the PID the grossly understated future liabilities and the grossly overstated projected investment income. The concerted activity was ongoing and deliberate and sought to evade discovery, scrutiny, oversight and/or intervention by the PID. (*Id.*, ¶ 35).

The company management enterprise which injured SHIP included, but was not limited to:

a) Oversight and maintenance of the interactive process with the appointed actuary, Milliman, that resulted in grossly understating future liabilities of SHIP;

b) Working with investment advisors to conceive of and implement the Beechwood transaction which cost SHIP millions of dollars in losses;

c) Working with investment advisors to conceive of and implement the Roebling Re transaction which resulted in misrepresenting SHIP's financial condition and cost SHIP millions of dollars in losses;

d) Intentionally designing the Roebling Re transaction to conceal SHIP's true financial condition so that it would not require PID approval;

e) Seeking to convert SHIP to a property and casualty company to avoid PID intervention;

f) Seeking to re-domesticate SHIP to a different state to avoid PID intervention;

g) Failing to alert the Trustees and PID of Defendant Wegner's self-dealing and un-waivable financial conflicts that directly injured SHIP; and

h) Failing to alert the Trustees and PID of Defendant Wegner's inexcusable personal failures that directly injured SHIP.

(*Id.*, ¶ 36).

The company management enterprise operated and maintained by Defendants Wegner, Lorentz and Staldine was in place at least from 2014, and remnants of that management enterprise continued to impact SHIP and SHIP's business operations until SHIP was placed in rehabilitation in January 2020. (*Id.*, ¶ 37). It was only then that the PID, through Special Deputy Rehabilitator Patrick Cantilo, had sufficient access to SHIP's financial and operating documents, analyses, communications, and

attorney-client materials to discover and address Defendants' injurious concerted activity that caused injury to SHIP and its policyholders.

The Beechwood Transactions

First, between May 2014 and March 2015, Defendants caused SHIP to enter into a series of investments totaling $320 million with a group of reinsurance and asset management companies called Beechwood Re. SHIP was induced to make these investments, and to enter related Investment Management Agreements ("IMAs"), based upon several material misrepresentations, including false statements about the quality and risk of the investments, SHIP's rights under the relevant agreements, and the guaranteed rate of return. (*Id.*, ¶ 43-79).

SHIP alleges in the Amended Complaint that Defendants either knew of these misrepresentations or consciously avoided specific knowledge of them. SHIP further alleges that each of the Defendants failed to advise SHIP's Trustees and the PID board of the misrepresentations or take any action consistent with their fiduciary duties to either prevent SHIP from investing or avoid the substantial financial losses that resulted.

In truth, Beechwood either did not invest SHIP's funds at all, instead using those funds to pay themselves or other investors, or Beechwood invested SHIP's funds in extremely risky assets, some of which financially benefitted Defendant Wegner's family.

None of the Defendants informed SHIP's Trustees or the PID of these misrepresentations.

In June 2016, a co-founder of one of the funds under the Beechwood umbrella was arrested on bribery charges and the offices were raided under suspicion of running a Ponzi scheme that potentially implicated SHIP's $320 million investment. Following that arrest, SHIP requested that its internal auditor, Protiviti, and another third-party consultant investigate the Beachwood investments. That investigation and analysis confirmed that there was insufficient oversight and deficient documentation of the Beechwood investments, but it did not reveal the extent of Beechwood's misrepresentations or the extent of malfeasance by the Defendants.

Unbeknownst to the rest of SHIP's Board, this was not the first time that Protiviti had been engaged to review the Beechwood transactions. In fact, at the end of 2014, Defendants Wegner and Lorentz, in secret and without informing the Trustees or the PID, requested that Protiviti review the Beechwood IMAs. In February 2015, Protiviti completed its review and provided Defendants with a report identifying several problems with the IMAs underlying SHIP's Beechwood Re investments. This Protiviti report was not delivered to the appropriate committees or individuals at SHIP until November 2016.

By the end of 2016, SHIP began the process of ending its relationship with Beechwood Re. Yet as a result of the secretive actions of Defendants Wegner and

Lorentz—as well as the actions of Defendant Staldine, the admitted driver of the Beechwood deal—complete and accurate information regarding the Beechwood Re transaction remained hidden from SHIP, its Board, and later, the Rehabilitator. (*Id.*, ¶¶ 60, 72, 115.)

Roebling Re

Between September 2016 and April 2018, the Defendants engaged in additional malfeasance and misrepresentations related to the Roebling Re re-insurance scheme. (*See* Am. Compl. ¶¶ 80-101). Roebling Re was created through the Bruckner Investment Trust ("BIT") for purposes of receiving and re-insuring up to 49% of SHIP's long-term care policy liability. However, Roebling Re was entirely funded by SHIP, which transferred $100 million to the BIT in exchange for a note with a 2.5% coupon rate and a 15-year maturity date.

Because Roebling Re had no other funding, it was not a legitimate re-insurer and it would have been unable to meet its future obligations as they arose. Millions of SHIP's funds were spent on management and consulting fees. The BIT invested $88.2 million of SHIP's funds into securities, which Defendants Wegner and Lorentz misrepresented as having almost twice that value. The remaining funds were re-paid to SHIP to avoid penalties under the note. Within 15 months of the initial September 2016 investment, nearly all of Roebling Re's and BIT's assets were exhausted.

With no material reinsurance protection, SHIP had expended millions of dollars with nothing to show for it except a worsened financial position.

Defendant Staldine's Involvement

Defendant Staldine worked for SHIP's predecessor CNO for over 16 years. CNO originated as Conseco, the company that originally sold the long-term care policies that later formed the core holdings of SHIP. (Am. Compl. ¶ 172).

Defendant Staldine had vast experience with long-term care policies by virtue of his time with Conseco; his work as a consultant for SHIP in 2014; his tenure as COO of SHIP from 2015 to 2017; and his tenure as CEO of SHIP from 2017 to 2020. (*Id.*, ¶ 173). More than anyone else in SHIP's senior management, Defendant Staldine knew or should have known and understood the importance of SHIP's actuarial landscape. (*Id.*, ¶ 174).

Working for Conseco, Staldine worked directly on rate increase and compliance matters related to long-term care insurance. He was also working at Conseco in 2012, when the Commonwealth Court issued its pivotal decision in the Penn Treaty matter which, among other things, re-emphasized the need for long-term care insurers to closely monitor their actuarial assumptions. (*Id.*, ¶ 175). In addition, Defendant Staldine knew that SHIP was a long-term insurer in run-off and could not absorb the financial impact of mismanagement of actuarial projections and poor investment decisions.

Thus, based on his experience, at the time he served as senior management for SHIP, Mr. Staldine was or should have been familiar with the extensive financial difficulties faced by the long-term care industry and how those issues might impact SHIP—including the meaning and impact of the Penn Treaty proceedings, which arose out of what was and still is the largest long-term care insolvency and involved a Pennsylvania-domiciled long-term care insurer like SHIP. (*Id.*, ¶ 176).

Defendant Staldine took a lead role specifically in driving the Beechwood deal. In June 2014 emails exchanged between Defendants Wegner and Staldine, Defendant Staldine stated that his "position responsibilities" during those upcoming months would include "driv[ing] the Beechwood deal" and "extend[ing] the Beechwood relationship to other blocks of business to the benefit of all parties." (*Id.*, ¶ 115). Then, in July 2014, Fuzion's VP of Human Resources confirmed that Defendant Staldine would be a consultant working on the Beechwood Re project. (*Id.*, ¶ 116).

In or around November 2014, Defendant Wegner tasked Defendant Staldine with preparing a presentation for SHIP's board on Beechwood Re. In an email on this topic, Defendant Wegner told Defendant Staldine that it was "critical to make a great impression" in the upcoming meeting and Defendant Staldine replied that his intent was to make the presentation "Fortune 500 worthy." Defendant Wegner's daughter also assisted in preparing the Beechwood Re materials and Defendant

Staldine was involved in Beechwood Re's quarterly business review that fall. (*Id.*, ¶ 117).

During his tenure in senior management with SHIP from 2015 to 2020, Defendant Staldine contributed to SHIP's financial losses by, among other things:

a) Failing to affirmatively and timely report Defendant Wegner's clear management failures to the Trustees and/or to PID;

b) Failing to ascertain the reliability of Milliman's actuarial projections and to assure that SHIP management would rely on appropriate actuarial projections;

c) Failing to assure the propriety of the advice and services provided by Eide Bailly;

d) Providing final approval and signoff on SHIP's inaccurate and misleading Annual Statements for the years 2016, 2017, and 2018, knowing that the PID would justifiably rely on those Annual Statements;

e) Failing to affirmatively and adequately disclose problems relating to personnel issues, consultants and management to the PID, the SDR and the Chief Rehabilitation Officer in a prompt fashion; and

f) Participating in and perpetuating a management enterprise that contributed to SHIP's financial losses from 2015 to 2020.

(*Id.*, ¶ 177).

SHIP's True Financial Position and Defendants' Misconduct is Uncovered

By March 2019, SHIP's management, including most notably Defendant Staldine, could no longer successfully conceal SHIP's deeply troubling financial position. On March 1, 2019, SHIP filed with the PID its statutory financial statement for the year ending December 31, 2018. (Am. Compl. ¶ 102). That financial

statement reflected that SHIP had declined from a reported surplus of more than $12 million as of year-end 2017 to a reported deficit of more than $466 million, a drop of $478 million in just one year, apparently rendering the Company statutorily insolvent as defined in 40 P.S. § 221.3.[2] (*Id.*, ¶ 103).

The Company's most recent RBC report indicated that its reported total adjusted capital was substantially below its mandatory control-level RBC, thereby triggering a "mandatory control level event" as defined in 40 P.S. § 221.1-A.[3] (*Id.*, ¶ 104). SHIP was directed to provide the PID a corrective action plan to remedy this decline, but failed to do so. (*Id.*, ¶ 105).

On January 29, 2020, the Commonwealth Court of Pennsylvania placed SHIP into rehabilitation at the request and application of the then Pennsylvania Insurance Commissioner. (*Id.*, ¶ 106). The purpose of this rehabilitation is, *inter alia*, to identify and address the causes of SHIP's financial deterioration for the benefit of policyholders and creditors. (*Id.*, ¶ 107). The Court then appointed Commissioner

[2] SHIP remains in rehabilitation, not liquidation, and no court has declared SHIP to be insolvent or placed it in liquidation. While SHIP's deficit appears to bring SHIP within the definition of insolvency in § 221.3, the Rehabilitator continues to pursue a Plan for SHIP's rehabilitation and he does not suggest through this allegation that SHIP should be liquidated.

[3] When a mandatory control level event is triggered, insurance regulators are required to take control of an insurer (as they did in this case) for the protection of policyholders and creditors.

Altman and her successors, including Acting Commissioner Humphreys, as SHIP's Rehabilitator. (*Id.*, ¶ 108).

As Rehabilitator, the Commissioner appointed Patrick H. Cantilo as Special Deputy Rehabilitator, and subject to the oversight of the Commissioner and the Commonwealth Court, Mr. Cantilo has been tasked with designing and implementing SHIP's rehabilitation and exercising the Rehabilitator's authority. (*Id.*, ¶ 109). On August 24, 2021, the Commonwealth Court approved the Rehabilitator's proposed Plan of Rehabilitation ("the Plan"). While certain intervening insurance regulators from other states appealed the Plan's approval, their request for stay was denied, and thus the Rehabilitator is proceeding with the implementation of the Plan, which involves, *inter alia*, offering policyholders certain options for modifying their policies. (*Id.*, ¶ 110).

Promptly following the order of rehabilitation on January 29, 2020, the Rehabilitator began to investigate the events that led to the dramatic deterioration in SHIP's financial condition. For the first time, the PID had unimpeded access to SHIP's financial and operating documents, analyses, communications, and attorney-client materials. This access allowed the PID to see how SHIP's management mismanaged its actuaries and auditors, and to see how Wegner, Lorentz, and Staldine concealed their poor and injurious management of SHIP. Ultimately, the investigation has revealed that incorrect or inappropriate actuarial assumptions and

the imprudent Beechwood Re and Roebling Re investments caused or contributed to SHIP's financial difficulties.

Moreover, this investigation revealed that each Defendant knew – or consciously avoided knowing – that SHIP's prior financial statements were materially false because they incorporated incorrect or inappropriate actuarial assumptions and mischaracterized the imprudent Beechwood Re and Roebling Re investments. (*Id.*, ¶ 140). It also revealed that the Defendants knew that the Beechwood Re and Roebling Re transactions were ill-advised, lacked appropriate due diligence, and ultimately were likely to prove harmful to SHIP. Yet Defendants concealed these facts from the PID, SHIP's policyholders and creditors, and the public. (*Id.*, ¶ 141).

Moreover, Defendants knew of SHIP's precarious financial condition, but failed to disclose these facts to the PID, SHIP's policyholders and creditors, and the public. Rather, Defendants worked with SHIP's consultants to produce financial statements and reports, which were required to be submitted to the PID, falsely declaring that SHIP's reserves were adequate and in compliance with Pennsylvania's insurance laws and regulations. (*Id.*, ¶ 143).

Defendants further knew that these statements contradicted the analysis of outside consultants, or otherwise significantly overestimated the adequacy of SHIP's reserves. Throughout the PID's investigation, Defendants concealed these relevant

facts from regulators. (*Id.*, ¶ 144). As a result of Defendants' misconduct, including Defendant Staldine's malfeasance and misrepresentations, SHIP suffered extraordinary financial losses leading to its current rehabilitation.

III. RESPONSE TO PRELIMINARY OBJECTION NO. 1: SHIP'S CLAIMS AGAINST DEFENDANT STALDINE ARE TIMELY

Defendant Staldine's objection pursuant to the relevant statutes of limitations is little more than an effort to be rewarded for working jointly with his co-Defendants to conceal their wrongdoing, and SHIP's deteriorating financial situation, from the Trustees and the PID. Moreover, it relies upon Staldine's disagreement with the allegations in the Amended Complaint and the reasonable inferences that should be drawn therefrom, rendering it entirely improper as a Preliminary Objection. It is without merit under fundamental principles of Pennsylvania law and must be overruled.

Staldine's statute of limitation defense is properly raised in "New Matter," not by preliminary objection. *See* Pa. R.C.P. 1030(a) ("all affirmative defenses including but not limited to . . . statute of limitations . . . shall be pleaded in a responsive pleading under the heading 'New Matter.'"). Indeed, the rule governing Preliminary Objections specifically states that "[t]he defense of the bar of a statute of frauds or statute of limitations can be asserted only in a responsive pleading as new matter under Rule 1030" rather than by Preliminary Objection. Defendant argues that, despite these rules, the defense of statute of limitations may

be considered at the preliminary objections stage where the untimeliness of the claims is apparent from the face of the complaint. *Baney v. Fisher*, No. 752 M.D. 2018, 2020 WL 5033421, at *4, n. 16 (Pa. Commw. Ct. 2020) (citing cases). This exception, even if it exists, does not overcome the underlying rule that, at the preliminary objection stage, the Court is obligated to accept the allegations in the complaint as true and to draw all reasonable inferences in favor of the plaintiff.

Under this standard of review, Staldine's objection to the timeliness of the claims against him fails for three reasons: (1) SHIP's claims are timely under fundamental application of the discovery rule; (2) SHIP's claims are timely under the adverse domination doctrine, as the Defendants were the senior managers of SHIP until the time it entered rehabilitation; and (3) SHIP's claims are timely because the public policies "surrounding the rehabilitation process" warrant a finding that SHIP's claims did not accrue until it was placed in the control of the Rehabilitator, rather than culpable management.

Furthermore, the Rehabilitator should be given the opportunity to conduct discovery on these matters to build its case to hold Defendants accountable and to pursue redress for SHIP's policyholders.

A. SHIP'S claims are timely under Pennsylvania's discovery rule

First, SHIP's claims are timely under the discovery rule, which tolls the statute of limitations "until a plaintiff could reasonably discover the cause of his action,

including in circumstances where the connection between the injury and the conduct of another are not readily apparent." *In re Risperdal Litig.*, 665 Pa. 649, 661 (Pa. 2019) (citing *Wilson v. El-Daief*, 964 A.2d 354, 365 (Pa. 2009)).

Under the rule, a claim accrues only when the plaintiff would have discovered both the injury and its cause at the hands of the defendant through reasonable diligence. *Gleason v. Borough of Moosic*, 15 A.3d 479, 485 (Pa. 2011). Reasonable diligence is a question for the *jury at trial*, and not one for the Court to resolve at preliminary objections. *Id.*

Here, SHIP has alleged it was prevented from discovering its claims against the Defendants – principally due to the Defendants' own misrepresentations and concealment – until after the rehabilitator was appointed on January 29, 2020. The Amended Complaint avers in detail that each of the Defendants, and Staldine in particular, made numerous misrepresentations and concealed key facts relating to Beechwood, Roebling Re, and the actual value of SHIP's reserves. Indeed, by way of a simple example, Defendant Staldine affirmed SHIP's financial statements, which were materially false and incorporated misrepresentations regarding Beechwood, Roebling Re, and actuarial assumptions, between 2015 and 2018.

The Defendants, as senior officers of SHIP, controlled the flow of information related to these transactions and SHIP's financial and actuarial position. Those same Defendants, including Staldine, used their position as officers of SHIP to make both

affirmative misrepresentations and material omissions regarding the true nature of these transactions and their impact on SHIP's financial position, effectively preventing SHIP from discovering the facts underlying its claims.

Staldine knew that Wegner had been fired by SHIP's Board for a number of reasons. He was aware, or should have been aware, of Wegner's numerous failures in management, judgment, and character. Staldine was aware, or should have been aware, of SHIP's plummeting surplus and inaccurate financial forecasts. Despite what should have been obvious warning signs, Staldine did not assess the financial health of SHIP or the accuracy of SHIP's financial statements. Nor did he assess the performance of SHIP's appointed actuary (Milliman), SHIP's external auditor (Eide Bailly) or SHIP's internal auditor (Protiviti). He did not even interview relevant managers and other employees to assess the company's processes.

Instead, Staldine continued with the self-serving and injurious strategies and systems designed by Wegner. These strategies and systems led SHIP's reported surplus to plummet from $102M in 2012 to only $28M in 2016. Rather than conduct an investigation and alert the Trustees and PID, Staldine kept the Wegner plans and consultants in place, kept silent, and watched SHIP's surplus plummet exponentially from a reported surplus of $12M in 2017 to a reported deficit of $466M in 2018.

Against this clear application of the discovery rule, Staldine essentially alleges that SHIP failed to exercise reasonable diligence because it was aware of certain

facts prior to January 29, 2020. This argument is not proper at the preliminary objection stage, which requires the Court to accept the facts pled as true and to make all reasonable inferences in favor of SHIP. Indeed, the Pennsylvania Supreme Court has instructed trial courts to avoid resolving questions of reasonable diligence at any stage and instead advised courts to leave the issue for the jury. *See Gleason v. Borough of Moosic*, 15 A.3d 479, 484-88 (Pa. 2011) (reasonable awareness of injury and cause of injury are to be decided by jury unless "facts are so clear that reasonable minds cannot differ").

Moreover, none of the cherry-picked facts identified by Staldine would have notified SHIP that it had suffered significant financial losses because of the Defendants' misconduct. Staldine notes that the Trustees and/or PID were aware prior to January 29, 2020, that there were "issues" with Beechwood, that the PID considered the Beechwood and Roebling Re transactions "problematic," and that SHIP's reserve assumptions were not correct.

None of these averments is sufficient to show inquiry notice or a lack of reasonable diligence by SHIP as a matter of law, particularly at the pleading stage. *Gleason v. Borough of Moosic*, 15 A.3d 479, 485 (Pa. 2011). They do not indicate, let alone prove as a matter of law, that SHIP knew the full extent of its financial deterioration or the malfeasance that occurred related to the Beechwood and Roebling Re transactions. Equally important, Wegner's averments do not address

how SHIP, the Trustees, or the PID would have been on notice of Wegner's gross mismanagement and lack of oversight of the appointed actuary, the external auditor, and/or the internal auditor. Nor do they indicate, let alone prove as a matter of law, that SHIP was aware that its losses were the result of Defendants' malfeasance and that Defendants had been misrepresenting the Beechwood and Roebling Re transactions and SHIP's actuarial and financial position while knowing the true circumstances.

Accordingly, the discovery rule renders SHIP's claims timely and Staldine's arguments to the contrary, while they might be revived at trial, are no basis for dismissal at the preliminary objection stage.

B. SHIP's claims are timely under the adverse domination doctrine.

Second, SHIP's claims are timely under the adverse domination doctrine because the Defendants exerted control over the organization until it entered rehabilitation on January 29, 2020. The adverse domination doctrine delays the running of the statute of limitations where a corporate entity seeks to bring claims against directors' or officers' wrongful actions adverse to the entity. *See Marine Chestnut Partners, L.P. v. Lenfest*, 152 A.3d 265, 280 (Pa. Super. Ct. 2016) ("a statute of limitations is tolled against director/officer misconduct so long as a majority of the board is controlled by the alleged wrongdoers"). Courts applying the doctrine in Pennsylvania rely on the fact that "no non-culpable party could have

brought suit before the receiver…was appointed because of the control the defendants exerted over the organization and others' lack of sufficient knowledge of the wrongdoing." *See id. at* 281.

The adverse domination doctrine tolls the statute of limitations for claims against bad-actor directors, officers, accountants, auditors, actuaries, and attorneys. *See, e.g., Resolution Trust Corp. v. Farmer*, 865 F.Supp.1143 (E.D. Pa. 1994) (applying doctrine to board's attorneys); *see also In re O.E.M.*, 405 B.R. 779, 786 (Bankr. W.D. Pa. 2009) (finding that the court could not decide the adverse domination issue on a motion to dismiss because the doctrine raised "various questions of material fact"). Pennsylvania courts assess (i) the degree of influence by the dominating/controlling directors or officers on the company, and (ii) the degree of culpability of the dominating/controlling directors or officers. Under the doctrine of adverse domination, the statute of limitations is tolled for as long as a corporate plaintiff is controlled by the alleged wrongdoers. *Id*. at 1151.

SHIP has alleged in its Amended Complaint that the Defendants controlled its management from the inception of the misconduct at issue through SHIP's placement into rehabilitation on January 29, 2020. Indeed, Defendants were the senior officers of SHIP during that entire period, ending only when Defendant Staldine – whom Wegner groomed as one of his successors – stepped down as CEO and was replaced by the Rehabilitator. *See Farmer*, 865 F. Supp. at 1158-59 (noting

that "the fact that a regulatory body—even the eventual plaintiff—acquired knowledge of the wrong and possessed certain power over the institution…does not negate the adverse domination doctrine or constitute, standing alone, the necessary cessation of domination so that it could or should have brought a lawsuit"). These allegations appropriately invoke the adverse domination doctrine and SHIP is entitled to discovery on the issues identified in *Farmer*, namely the degree to which Defendants influenced SHIP during this period and their degree of culpability.

C. SHIP's claims are timely in light of the public policies surrounding rehabilitation.

Finally, SHIP's claims are timely because, in this case, the public policy "surrounding the rehabilitation process" weighs heavily in favor of a finding that SHIP's claims did not accrue until the order of rehabilitation was entered on January 29, 2020.

While rehabilitators are not exempt from the statute of limitations, courts must weigh the public policies "surrounding the rehabilitation process . . . in determining when the action accrues." *Foster v. Alexander & Alexander Servs.*, No. 91-1179, 1995 U.S. Dist. LEXIS 711, at *19 (E.D. Pa. Jan. 20, 1995). The purpose of Pennsylvania's insurance receivership statutory scheme "is to protect the general public against the substantial costs and exigencies related to a major commercial insolvency." *Foster v. The Mutual Fire, Marine & Inland Ins. Co.*, 614 A.3d 1086, 1084 (Pa. 1992), *cert denied sub nom. Allstate Ins. Co. v. Maleski*, 113 S. Ct. 1047

(1993). Accordingly, the Commissioner is afforded broad powers to "effectuate equitably the intent of the Rehabilitation statutes, i.e., to minimize the harm to all affected parties." *Id.* The Commissioner has a fiduciary duty to "marshall [sic] and preserve all assets of the insolvent entity," and due to the exigent circumstances surrounding a major insolvency, it may be necessary to compromise "individual interests…to avoid greater harm to a broader spectrum of policyholders and the public." *Id.* at *19-20 (citing *Vickodil v. Commonwealth Ins. Dep't*, 559 A.2d 1010, 1013 (1989)).

Foster is strikingly on point. In materially identical circumstances – where the Pennsylvania insurance company plaintiff brought claims under the direction of Rehabilitator – the *Foster* court found that the plaintiff's claims did not accrue until it requested supervision from the PID and was further tolled until the Order of Rehabilitation pursuant to 40 P.S. § 221.17(b). In so doing, the court rejected the very same argument that Defendant Staldine raises here – that the plaintiff and the PID were aware of the losses resulting from the defendant's alleged misconduct prior to requesting supervision by PID. *Id.* The court noted that "indeed, [the insurer] must have been aware of its losses, as it sought supervision from the Insurance Department." *Id.* But the insurer did not know who was responsible for those losses, and reasonable diligence did not include discovering the defendants' wrongdoing because the defendants had fiduciary obligations to the plaintiff. *Id.*

Courts in other jurisdictions have reached similar results, adding to the persuasiveness of *Foster's* reasoning. *See Ky. Cent. Life Ins. Co. v. Deloitte & Touche LLP*, 2001 Ky. App. LEXIS 73 (Ky. Ct. App. 2001); *Banco de Desarrollo Agropecuario, S.A. v. Gibbs*, 709 F. Supp. 1302 (S.D.N.Y. 1989) ("Where an action is brought by a trustee or liquidator on behalf of a corporation that has been looted by persons who completely dominated and controlled it, the statute of limitations is tolled as against the control persons until the appointment of the independent trustee or liquidator."); *Washburn v. Brown*, 1987 U.S. Dist. LEXIS 495 (N.D. Ill. 1987); *Shapo v. O'Shaughnessy*, 246 F. Supp. 2d 935 (N.D. Ill. 2002).

The case at bar is materially identical to *Foster*. The Defendants owed fiduciary duties to SHIP; they used those fiduciary duties to conceal their wrongdoing from the Trustees and the PID; while SHIP (and, to a lesser extent, PID) had some indication that it had suffered financial losses, it did not know – and had no reason to investigate – that those losses were caused by malfeasance and deception by the Defendants; and, the Defendants were officers of SHIP who controlled the company until supervision by the PID was requested.

Pursuant to *Foster*, public policy considerations dictate that Defendants – who were the officers in control of SHIP until its entry into Rehabilitation – be precluded from avoiding liability for the extraordinary financial losses caused by their malfeasance by virtue of their coordinated concealment. The fact that control of the

company rested with these Defendants is undisputed. Multiple Pennsylvania legal doctrines are designed specifically to avoid such an unjust result, particularly at the pleading stage.

Accordingly, Defendant Staldine's preliminary objection based upon the statute of limitations must be overruled.

IV. RESPONSE TO PRELIMINARY OBJECTION NO. 2: SHIP ADEQUATELY PLED A CLAIM FOR BREACH OF FIDUCIARY DUTY IN COUNT I

Defendant Staldine's preliminary objection to Count 1 is, essentially, a trial argument that ignores or mischaracterizes the allegations in the Amended Complaint. It must be overruled.

The Amended Complaint pleads numerous breaches by Staldine of the fiduciary duties he owed to SHIP as an officer. It alleges that he knew the Beechwood investments were misrepresented to SHIP's Trustees and on SHIP's financial statements, and yet he perpetuated and did nothing to correct those misrepresentations or to prevent or unwind obviously inappropriate investments. The Amended Complaint alleges that Staldine knew the Roebling Re transaction was not legitimate re-insurance and its structure was substantially misrepresented to the SHIP Trustees and PID, and yet he perpetuated and failed to correct those misrepresentations, again leading to significant financial losses for SHIP. And the Amended Complaint alleges that Staldine knew SHIP's actuarial assumptions and

liability estimates were faulty but, again, including those misrepresentations in SHIP's financial statements and did nothing to correct them.

These are all clear violations of the fiduciary duties owed by corporate officers. Fiduciary duties of care and good faith owed by directors and officers of a Pennsylvania corporation are defined by statute. *See* 15 *Pa. Cons. Stat. Ann.* § 5712(a)-(c) (2011). Officers must use "reasonable inquiry, skills and diligence in the performance of their duties" and they must act at all times in good faith and while avoiding self-dealing. *Id*.

Moreover, Staldine was subject to fiduciary duties as a consultant:

> A fiduciary duty arises when the relationship between the parties is one of trust and confidence such that the party in whom trust and confidence is reposed must act with scrupulous fairness and good faith in his dealing with the other and refrain from using his position to the other's detriment and his own advantage. *Young v. Kaye*, 443 Pa. 335, 279 A.2d 759, 763 (1971). Fiduciary duty demands undivided loyalty, prohibits conflicts of interest and its breach is actionable. *See, e.g., Maritrans v. Pepper, Hamilton Scheetz*, 529 Pa. 241, 602 A.2d 1277, 1283 (1992), citing, *inter alia*, *Stockton v. Ford*, 52 U.S. (11 How). 232, 13 L.Ed. 676 (1850). A business relationship may be the basis of a confidential relationship if one party surrenders substantial control over some portion of his affairs to the other. *Chrysler Credit Corp. v. B.J.M., Jr., Inc.*, 834 F. Supp. 813, 842 (E.D. Pa. 1993) citing *Commonwealth, Dep't. of Transportation v. E-Z Parks*, 153 Pa. Cmwlth. 258, 620 A.2d 712, 717 (1993). "A fiduciary duty arises when the relationship between the parties is one of trust and confidence such that the party in whom trust and confidence is reposed must act with scrupulous fairness and good faith in his dealing with the

> other and refrain from using his position to the other's detriment and his own advantage."

Tyler v. O'Neill, 994. F. Supp. 603, 611-12 (E.D. Pa. 1998).

The knowing and material misrepresentations by Staldine were not in good faith and plainly qualify, if proven, as breaches of the fiduciary duties he owed as an officer.

Defendant Staldine's arguments to the contrary directly violate the rules governing Preliminary Objections. Specifically, the Court is obligated to assume the allegations in the Amended Complaint are true and to make all reasonable inferences in SHIP's favor. Staldine seeks to turn that standard of review on its head by disputing the averments in the Amended Complaint. However, a review of the full scope of facts alleged against Defendant Staldine makes plain that the claim is well plead.

The Amended Complaint alleges that Staldine knew the Beechwood Re and Roebling Re transactions were ill-advised, lacked appropriate due diligence, and were likely to be harmful to SHIP, but he concealed those facts from regulators, creditors, policyholders, and the public. (Am. Compl. ¶141).

The Amended Complaint alleges that Staldine knew that SHIP's financial position was precarious and misrepresented in financial statements, but instead of disclosing the truth, Staldine worked with Wegner, Lorentz, and SHIP's consultants to produce inaccurate financial statements stating that SHIP's reserves were

adequate and in compliance with Pennsylvania insurance laws and regulations. (*Id.*, ¶ 142).

The Amended Complaint alleges that Staldine published, perpetuated and failed to correct these misrepresentations first as a consultant beginning in 2014, where his principal task was to work with Wegner and Lorentz on the Beechwood Re transactions, and later as an officer of SHIP from 2015 until 2020, where he continued the financial misrepresentations passed on from Wegner and Lorentz and approved false and misleading Annual Statements for the years 2016, 2017, and 2018. (*Id.*, ¶¶ 173-78).

Defendant Staldine's alleged malfeasance and misrepresentations squarely violated his fiduciary duties of loyalty and candor, as well as his duties to avoid conflicts of interest and waste, while an officer of SHIP. 15 Pa. C.S. § 5715. His preliminary objection must be overruled.

V. RESPONSE TO PRELIMINARY OBJECTION NO. 3: SHIP HAS ADEQUATELY PLED A CLAIM FOR CIVIL CONSPIRACY IN COUNT 3

Defendant Staldine's preliminary objection to SHIP's Civil Conspiracy claim once again ignores the averments in the Amended Complaint. SHIP has averred a civil conspiracy among the Defendants to misrepresent and conceal the true nature of the unjustifiable financial transactions set forth in the Amended Complaint. SHIP has alleged that each of the Defendants, including Staldine, knew the true facts

surrounding these transactions but agreed to conceal them in order to continue managing SHIP, avoid personal liability, and avoid regulatory action by the PID.

Defendant Staldine began conspiring with Wegner and Lorentz while working as a consultant on the Beechwood transactions. Despite knowing the true, and unwise and unjustifiable, nature of the investments and absence of oversight, the three co-conspirators actively concealed those facts and instead promoted Beechwood as a safe investment for $320 million in funds. Staldine, Wegner, and Lorentz further agreed to misrepresent the Roebling Re transactions and SHIP's actuarial and financial position. Accordingly, the Amended Complaint adequately alleges an agreement by the Defendants to commit intentional misrepresentation against SHIP, its Trustees, and the PID. Defendants carried out this conspiracy over the course of years. Those allegations squarely meet the elements of civil conspiracy in Pennsylvania.

Finally, Defendant Staldine argues that Pennsylvania law precludes a civil conspiracy claim by a corporation against its officers. This is simply not correct. While, generally, Pennsylvania law holds that a corporation cannot conspire *with itself or its agents, Doe v. Nest Graf, P.C.*, 862 F. Supp. 1310, 1328 (E.D. Pa. 1994); there is no legal rule precluding a corporate entity from claiming that its officers conspired *against* it. Indeed, even the Pennsylvania rule Defendant misstates has an exception that would squarely apply to SHIP's claims:

> [A] corporation can conspire with its agents or employees if the agents or employees are acting not for the corporation, but for personal reasons and one of the parties to the conspiracy is not an agent or employee of the corporation. This rule has been liberally construed, however, so as to allow a civil conspiracy claim to proceed where agents or employees act outside of their corporate roles even in the absence of a co-conspirator from outside the corporation.

Tyler v. O'Neill, 994 F. Supp. 603, 613 (E.D. Pa. 1998) (internal citations omitted); *see also Denenberg v. American Family Corp.*, 566 F. Supp. 1242, 1253 (E.D. Pa. 1983) and *O'Neill v. ARA Services, Inc.*, 457 F. Supp. 182, 188 (E.D. Pa. 1978).

Accordingly, Defendant Staldine's preliminary objection to SHIP's claim for civil conspiracy is without merit and must be overruled.

VI. RESPONSE TO PRELIMINARY OBJECTION NO. 4: SHIP HAS ADEQUATELY PLED A CLAIM FOR NEGLIGENCE IN COUNT 4

Defendant's preliminary objection to Count 4 of the Amended Complaint once again ignores the majority of the averments against him. Those averments are set forth multiple times herein and will not be repeated at length again here. Notably, Defendant Staldine does not challenge that he had a duty to act with reasonable care while a consultant and officer for SHIP.

The Amended Complaint sets forth misconduct that satisfies the negligence standard – Defendant Staldine plainly did not act with reasonable care – and, in fact, was either reckless, knowing, or intentional. Therefore, the preliminary objection has no merit whatsoever and must be overruled.

VII. RESPONSE TO PRELIMINARY OBJECTION NO. 5: SHIP HAS ADEQUATELY PLED A CLAIM FOR NEGLIGENT MISREPRESENTATION IN COUNT 5

Defendant Staldine misrepresented many material facts as alleged in the Amended Complaint. He misrepresented several aspects of the Beechwood transactions. He misrepresented the essential nature of the Roebling Re transactions. He misrepresented SHIP's actuarial positions and liabilities. And he incorporated these misrepresentations into SHIP's Annual Statements, which he approved of despite their inaccuracy.

Defendant Staldine just simply ignores all of these allegations in his preliminary objection to SHIP's claim for negligent misrepresentations. Nonetheless, these misrepresentations plainly meet the elements of the claim. In each instance, Defendant Staldine knew or should have known the true facts and yet perpetuated material falsehoods that SHIP and PID relied upon to their clear detriment. The averments meet the elements of this claim squarely, and therefore, the preliminary objection must be overruled.

VIII. RESPONSE TO PRELIMINARY OBJECTION NO. 6: SHIP'S AVERMENTS AGAINST STALDINE ARE SUFFICIENT SPECIFIC

SHIP's 246-paragraph Amended Complaint sets forth Defendant Staldine's malfeasance in detail and with particularity. SHIP alleges that Staldine caused SHIP to enter into the Beechwood and Roebling Re transactions, despite knowing that they

were ill-advised, extremely risky, lacked oversight, and involved conflict of interest, and he did so by misrepresenting the transactions. SHIP further alleges that Staldine consistently and over the course of years misrepresented SHIP's financial position. SHIP has identified numerous specific misrepresentations, including statements to SHIP's board, to PID, and in SHIP's Annual Statements.

Simply put, the averments in the Amended Complaint easily meet the particularity requirements in Pennsylvania's pleading rules and provide notice to Defendant Staldine of the facts supporting the claims against him. The Court must overrule his objection.

IX. CONCLUSION

For the foregoing reasons, SHIP respectfully requests that the Court overrule Defendant Staldine's Preliminary Objections and order him to file an Answer to SHIP's Amended Complaint within twenty (20) days.

Dated: October 17, 2022

Respectfully submitted,

COZEN O'CONNOR

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