

SAUCON MUTUAL INSURANCE COMPANY  
SEPTEMBER 1, 2015 INFORMATIONAL HEARING ON PLAN OF CONVERSION  
WRITTEN TESTIMONY  
OF  
ANTHONY LATINI, JR.

**I. Introduction**

My name is Anthony Latini and I am a Managing Director at Boenning & Scattergood, Inc. who has provided Saucon Mutual Insurance Company (Saucon) financial advisory services since 2012 and provided a fairness opinion with regard to the contemplated conversion transaction that is the subject of this hearing.

In my written testimony, I am briefly addressing four topics. First, the experience and background of myself and Boenning & Scattergood. Second, some background details regarding the financial advisory work Boenning provided to Saucon relating to its strategic alternatives analysis and the decision to proceed with a Plan of Conversion. Third, I will provide a summary explanation of the Boenning Fairness Opinion, and the work and analysis that supported that Opinion. Finally, I will call to your attention certain limitations relating to the Fairness Opinion.

I begin by addressing my background and that of Boenning & Scattergood. I am a Managing Director at Boenning specializing in providing investment banking services to insurance companies and other financial institutions. I have been with Boenning for approximately 4 1/2 years (and a predecessor firm for ~10 years) and have worked in the corporate finance, banking, insurance and investment banking fields since 1987, almost 30 years. My professional transaction experience includes approximately \$2 billion in M&A transaction value and capital raising in excess of \$1 billion. I have authored and delivered numerous presentations for industry conferences, corporate planning sessions, the National Association of Insurance Commissioners, the Pennsylvania Bar Institute and the Federal Reserve Bank and I have been quoted in numerous industry publications.

I have a Bachelor of Science in Economics degree from Wharton School of the University of Pennsylvania and hold the Chartered Financial Analyst (CFA) designation. In addition to the opportunity to serve corporate clients, I have had the opportunity to provide reports and testimony to the Pennsylvania Insurance Department as well as other states' Insurance Departments on a variety of transactions involving insurance companies.

Boenning & Scattergood is a 101 year old, Pennsylvania based, full-service investment firm that provides a combination of services to its corporate and retail clients including investment banking, retail brokerage, municipal finance, equity research, trading and institutional sales. Boenning is employee owned and privately held. Boenning has significant experience with transactions generally and, most specifically, transactions in the insurance industry. The collective experience of Boenning's professionals in providing merger and acquisition services, capital raising, and demutualization advisory services to insurance companies and brokers totals almost 100 clients. Boenning has been directly involved with eight insurance demutualization transactions, including almost every mutual-to-stock conversion transaction in Pennsylvania since the Mutual-to-Stock Conversion Act (the Act) became effective in 1996.

## **II. Financial Advisory Services**

Boenning's services to Saucon were pursuant to three engagements beginning in 2012.

- The first was a strategic alternatives engagement in which Boenning assisted Saucon's Board of Directors in a review of strategic options that could assist the Board in meeting its defined goals.
- The second assignment, formally signed October 10, 2013, included a further assessment, refinement, development and execution of a plan to raise capital and demutualize.
- The third engagement related to the issuance of a fairness opinion in connection with the proposed demutualization.

I will first discuss the two engagements relating to financial advisory services and then the Fairness Opinion. Boenning began working with Saucon in 2012. Boenning first worked with

the Company to develop strategic goals and objectives against which to judge various strategic alternatives. Saucon's goals and objectives were to:

- Modernize corporate structure and enable issuance of traditional financing instruments (e.g., equity for growth, retention of employees, borrow funds)
- Facilitate acquisitions
- Improve management of Company
- Attract management and employees
- Better allocate existing capital
- Re-enter the insurance underwriting business
- Establish a charitable foundation in furtherance of Saucon's ongoing commitment to the community
- Provide meaningful consideration to all policyholders
- Minimize confusion and complications for policyholders
- Realize satisfactory timing and execution / costs

Boenning also assisted the Board in developing a list of potential alternatives that could meet the Company's goals and objectives and to evaluate each opportunity or alternative based on the established criteria. Boenning presented a number of strategic alternatives including:

- Downstream stock company
- Separate holding company
- Mutual holding company conversion
- Alternative plan conversion
- Subscription rights conversion

Boenning's analysis and planning exercises with the Board took place over a period of almost a year and included an initial examination of the potential for Saucon to re-enter the insurance underwriting business. Ultimately Boenning presented eight different alternatives for Saucon to re-enter the insurance market. Saucon has not reached a definitive conclusion about which alternative would be optimal because of the unknowns relating to timing of the Conversion transaction. Saucon will determine exactly how to re-enter the insurance business once the

Company has a definitive transaction and moves forward with the capital and structure to execute on one of these alternatives.

Based on a series of meetings, including two meetings with the Pennsylvania Insurance Department, refinements to the initial analysis, and numerous Board discussions and presentations, the Board of Directors concluded that the alternative plan conversion method under the Act best met the Company's goals and objectives.

In connection with its assessment of alternatives, the Board noted that a very small percentage of policyholders actually exercised their subscription rights in previous ordinary subscription rights conversions. In other words, the vast majority of policyholders received NO economic compensation in connection with the transaction. One of the key objectives for the Board was to ensure that ALL Saucon members received cash and/or other valuable consideration

After a full presentation to the Board by its advisors on the mutual holding company conversion alternative, the Board determined that a mutual holding company also did not meet the strategic objectives of the Company. Specifically, a mutual holding company did not result in improved management, additional capital or policyholder consideration. In addition, mutual holding companies have been criticized by the courts and face substantial litigation risk.

The Board spent substantial time in reviewing alternatives, determining the consideration to policyholders and selecting the proposed Alternative Plan Conversion. The Board received a wide range of input from management and its advisors. The analysis was completed over several meetings and discussions and took into account the history of the Company, its financial condition, performance and future positioning.

As described in the written testimony of Brian Regan, the Board ultimately decided on its proposed Alternative Plan Conversion because it best met the Company's goals and objectives, including consideration to all policyholders.

### **III. Fairness Opinion**

On August 27, 2014 the Saucon Board of Directors met to evaluate the potential transaction. At this meeting, I reviewed the financial aspects of the proposed transaction and rendered a verbal opinion, which was confirmed by delivery of a written opinion dated as of the same date, stating that the Financial Consideration to Saucon Mutual's members pursuant to the Plan of Conversion is fair and equitable, from a financial point of view, to the members of Saucon taken as a whole. In addition, we opined that the Plan met certain specific criteria prescribed in the Act relating to determining fairness to members.

In rendering this Opinion, we reviewed a number of documents relating to the Plan as well as relating to the Company itself. In addition we met with members of senior management of Saucon to perform due diligence on the Company and the transaction. Our information request list was approximately three typed pages long.

The work, analysis and information review completed by Boenning was developed with an understanding of the Company, its financial condition, and the Board's rationale for a transaction. We summarized our understanding of the transaction and the applicable regulatory statutes in our presentation to the Board in order to establish context.

We also shared with the Board summaries of our analysis so that the Board would have an understanding of how Boenning reached its conclusion as to the fairness of the proposed transaction.

As for member consideration, we understood that the members of Saucon as of the date of the Board's adoption of the Plan of Conversion would receive approximately \$1 million in cash, as well as an allowance for an increase in coverage under the inflation adjustment endorsements of the perpetual policies with no additional cost to the policyholders (an annual cash savings benefit for as long as the policyholder maintains the policy) and that Saucon would contribute \$1 million to a charitable foundation to serve the local community that fostered it for 180 years.

The charitable foundation was proxy for the contribution of prior members of the Company who would not receive direct consideration. Details relating to how the cash payments would be calculated for each member is set forth in other written testimony. It is sufficient to state for our purposes that the members would be rewarded financially for longevity and size of policy (i.e., size of deposit for perpetual policyholders and amount of annual premium for term policies). Importantly, Boenning's Opinion addressed the members taken as whole, not any one specific class or member.

It is important to note that it was Boenning's understanding that an equity (stock) offering for stock of a stock holding company would occur in connection with the Conversion such that the capital and surplus of the Company that was depleted in connection with providing members their consideration and related expenses of the transaction, would be replaced entirely by new equity raised from the stock offering and paid by the holding company for the purchase of the converted insurer's stock.

Boenning also noted several non-compensation related benefits to policyholders including the fact that policyholders' coverage would not be diminished, and that Saucon's new organizational structure could improve its operations and provide access to capital, and thereby benefit policyholders via increased operations and surplus.

Boenning's understanding of the alternative plan of conversion provisions of the Act is that the Board of Directors may adopt a plan of conversion that does not rely in whole or in part upon issuing nontransferable subscription rights to members to purchase stock of the converted company if the Commissioner finds that (i) the plan does not prejudice the interests of members, (ii) is fair and equitable, and (iii) is not inconsistent with the purpose and intent of the Act. Boenning considered these criteria as well as other financial criteria in its determination of fairness.

In reaching its opinion, Boenning reviewed a number of factors:

- A review of other alternative plan conversion transactions that have occurred in Pennsylvania.

- A review of other transactions indicated that, relative to the other three alternative conversion transactions that have been approved and implemented, Saucon's proposed compensation to members was more valuable based on (i) the form of consideration (cash and other), (ii) aggregate value to be received, and (iii) the value to be received per member.
- Assessment of the proposed transaction relative to the previously noted criteria specified in the Act.
  - 1) Does not prejudice the interests of members.
    - Boenning noted that the Plan of Conversion did not prejudice the financial interests of members because:
      - Policyholders' insurance coverage will remain the same as it was under the status quo.
      - Access to capital markets should enable the Company to have an opportunity to achieve increased profitability, size and scale and to grow policyholder financial protection.
      - The transaction would align management and the Board with a strategy of growth and the closely held company can preserve its almost 200 year old culture.
      - The transaction would provide the means for the Company to attract and retain management and employees.
      - The transaction would provide the means for the Company to have more insurance offerings for policyholders and provide diversification benefits.
      - The policyholders today have no right to the Company's surplus; therefore, any compensation exceeds their current financial interest.
      - There are no anticipated negative consequences to the policyholders.
  - 2) Is fair and equitable.
    - Boenning noted that the Plan of Conversion appeared to be fair and equitable because:
      - The Saucon members will receive a combined \$1 million in cash compensation (subsequently enhanced to \$1.5 million) in addition to

increased coverage to perpetual policyholders under the inflation adjustment endorsements at no cost to the policyholders.

- Cash, being worth more than nothing, is of more value than policyholders' current financial interest.
- Financial consideration is liquid as compared to the non-cash benefits used in other alternative plan conversions (which, while beneficial, were different than cash).
- There will be no diminution in policyholder insurance coverage or potential benefits.
- Management estimates that Saucon Holding's assets and equity, on a consolidated basis, will exceed that of Saucon Mutual Insurance Company prior to the Conversion.

3) Is not inconsistent with a purpose and intent of the Act.

- Boenning noted that the Plan of Conversion was not inconsistent with the purpose and intent of the Act because:
  - The intent and purpose of the Act is to enable mutual insurance companies to have access to financial markets, attract capital, and thereby enhance the financial foundation of the insurer.
  - As noted previously, the Conversion gives Saucon access to traditional financing instruments and Saucon's future ability to generate new business will be enhanced and should allow for an improved financial foundation for the insurer.
  - Management estimates that Saucon Holding's assets and equity, on a consolidated basis, will exceed that of Saucon Mutual Insurance Company prior to the Conversion.

Taking all the analysis into account, Boenning concluded the following in its Opinion:

*The Financial Consideration to Saucon's policyholders pursuant to the Plan of Conversion is fair and equitable, from a financial point of view, to the policyholders of Saucon taken as a whole.*

*In addition, we understand that the insurance policies of Saucon grant no right to surplus to policyholders and it is the position of the Pennsylvania Insurance Department that policyholders of a mutual insurance company have no statutory or constitutional property right to surplus of the mutual insurance company. Based on this understanding, it is our opinion that, as of the date hereof, the Financial Consideration to Saucon's policyholders pursuant to the Plan of Conversion does not prejudice the financial rights of those policyholders.*

*Lastly, we understand that the purpose and intent of the Pennsylvania Insurance Company Mutual-to-Stock Conversion Act, 40 p.s. §§ 911-A et seq., is to enable mutual insurance companies to access the financial markets, attract investment capital and thereby enhance the financial foundation of the insurer. Based on this understanding, and because the Conversion will enable Saucon to pursue business strategies that could enhance its future viability, and the total assets of Saucon Holding Company on a consolidated basis after the closing of the Conversion are expected to exceed the total assets of Saucon before the closing, it is our opinion that, as of the date hereof, the Financial Consideration to Saucon's policyholders pursuant to the Plan of Conversion is not inconsistent with such purpose and intent of the Act from a financial point of view.*

The final point that I would like to address is the limitation of our Fairness Opinion. There are numerous limitations stated in the Opinion itself and the presentation that accompanied it, but I will try to summarize them here.

We relied upon and assumed the accuracy and completeness of all the financial and other information provided to us or otherwise made available to us or that was discussed with us or reviewed or was publicly available information. The Opinion speaks only to the date of the Opinion and does not address the fairness to any specific constituency except that which is specifically stated in the letter. The Opinion is directed to the Board of Directors of Saucon and addresses only the fairness from a financial point of view to the policyholders taken as a whole. Our Opinion was for the information of Saucon's Board of Directors in connection with its evaluation of the Conversion and does not constitute a recommendation to the Board of Directors

of Saucon in connection with the Conversion or a recommendation to any policyholder of Saucon as to how such policyholder should vote or act with respect to the Conversion.

The preparation of a fairness opinion is a complex analytical and qualitative process involving various determinations as to the most appropriate and relevant methods of financial analysis and the application of those methods to the particular circumstances; therefore, the Fairness Opinion is not readily susceptible to partial analysis or summary description. We also shared with the Board several disclosures mandated by FINRA, our primary regulatory body, relating to our relationship with Saucon, the approval of our Fairness Opinion by a committee and certain scope limitations to the Fairness Opinion.