HIGHMARK. West Virginia

HIGHMARK.

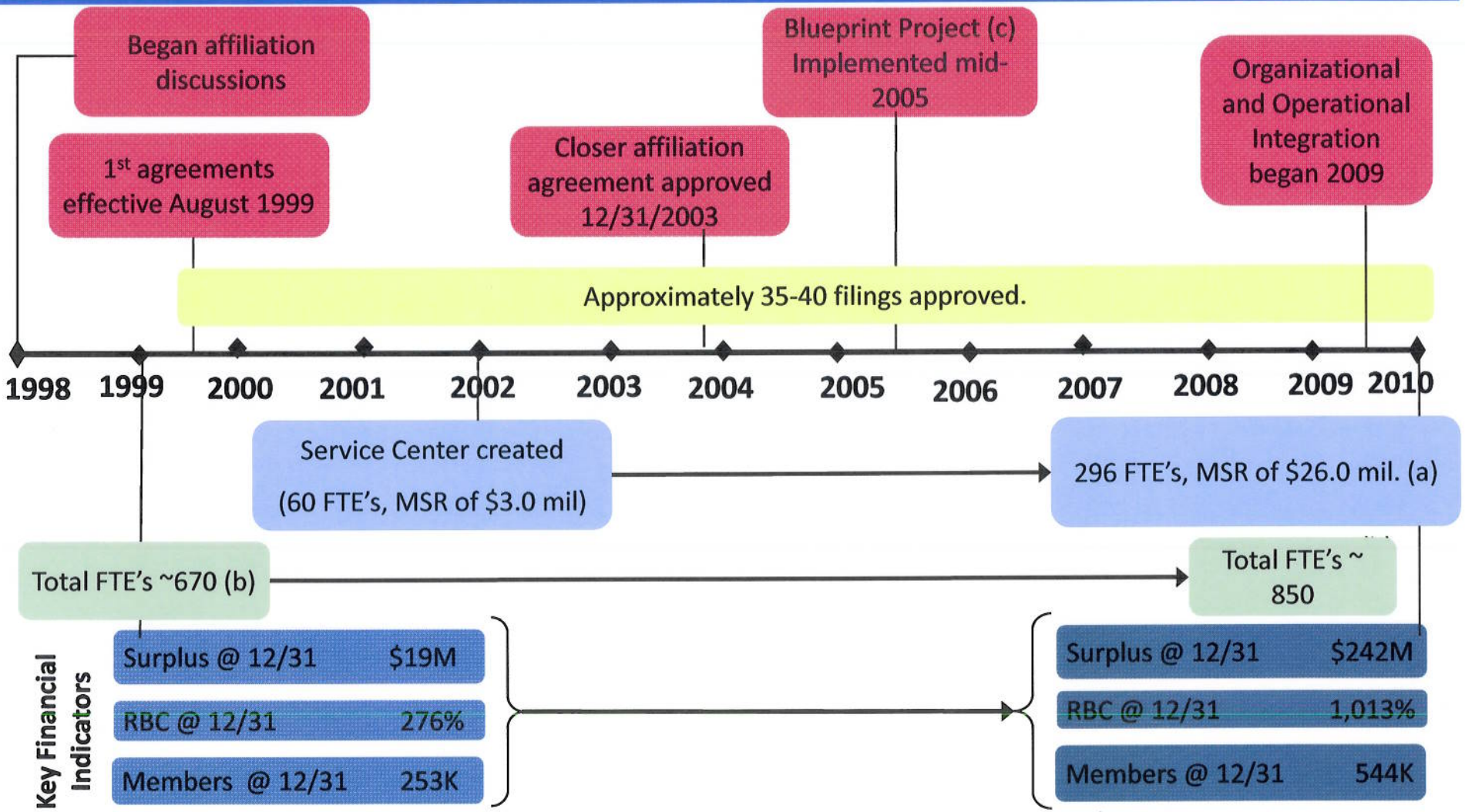
Highmark/West Virginia Affiliation

Operational Update and Cost Structure

EXHIBIT
JOINT-18.1

Proprietary & Confidential Draft

Highmark/West Virginia Relationship



(a) Over the past five years, the Service Center has contributed significantly to Highmark's generation of more than $106 million in economic activity for the Parkersburg region.

(b) Note: 1999 FTE count included 125 FTE's that worked on the PEIA account, which was lost in 2000. Those FTE's were redirected to other work, rather than displaced, due to the noted enrollment growth and creation of the service center.

(c) BluePrint – implementation of Highmark WV on Highmark core systems.

Blueprint Update - Today

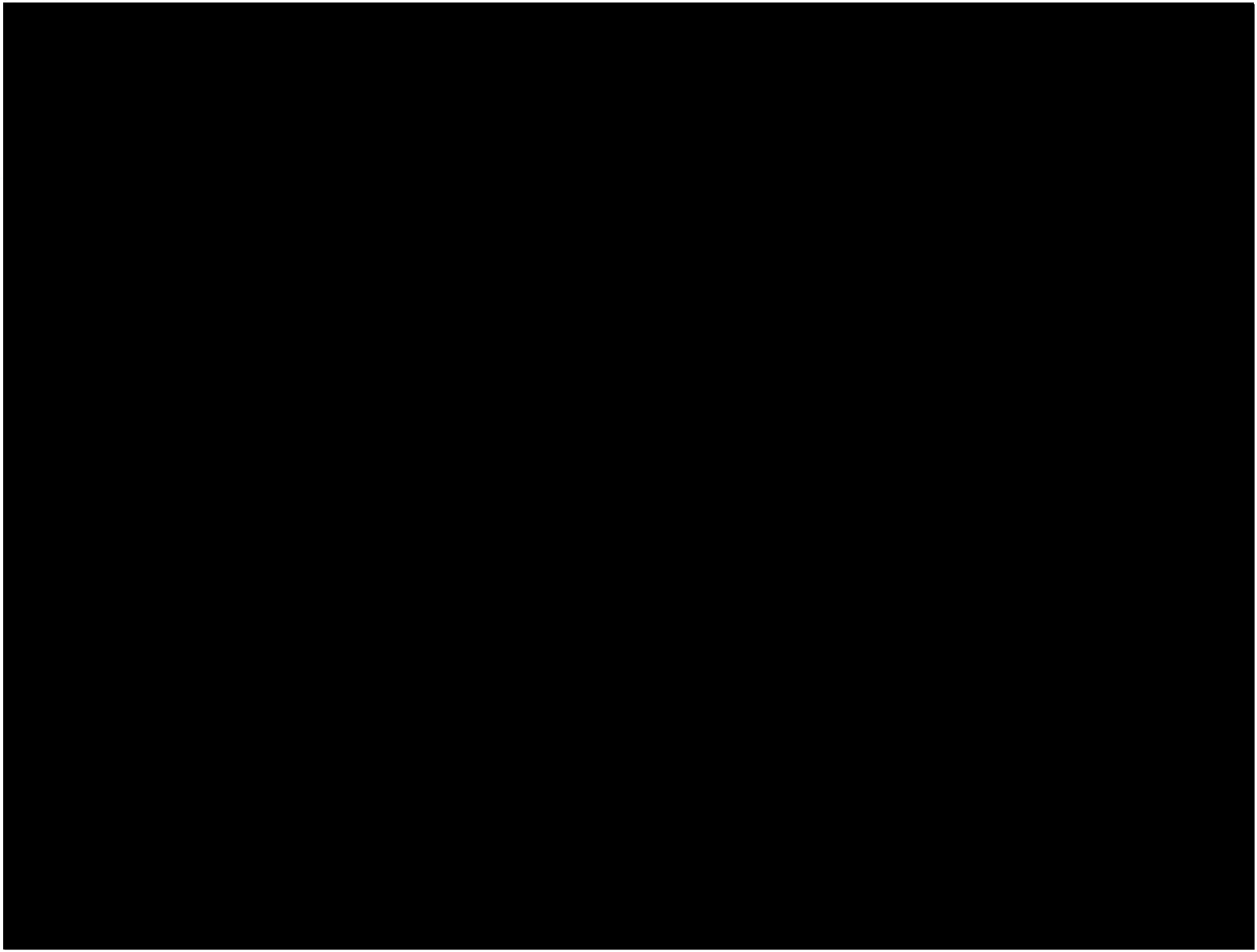
Blueprint has Exceeded Expectations ….

- **Potential Cost Reductions –**
  - **Exceeded FTE efficiency target by 50% – Annual savings of $3.6M**
  - **FTE efficiencies have been instrumental in providing capacity for Blue Card business for which revenue has grown by almost 50%, or $8M annually since 2003**
- **Creation of Service Center**
  - **Positions eliminated via Blueprint cost reductions were redirected to the Service Center**
  - **Service center positions are reimbursed at cost + overhead**
  - **296 FTE's in service center today, generating $26M of annual revenue**

Blueprint Update - Today

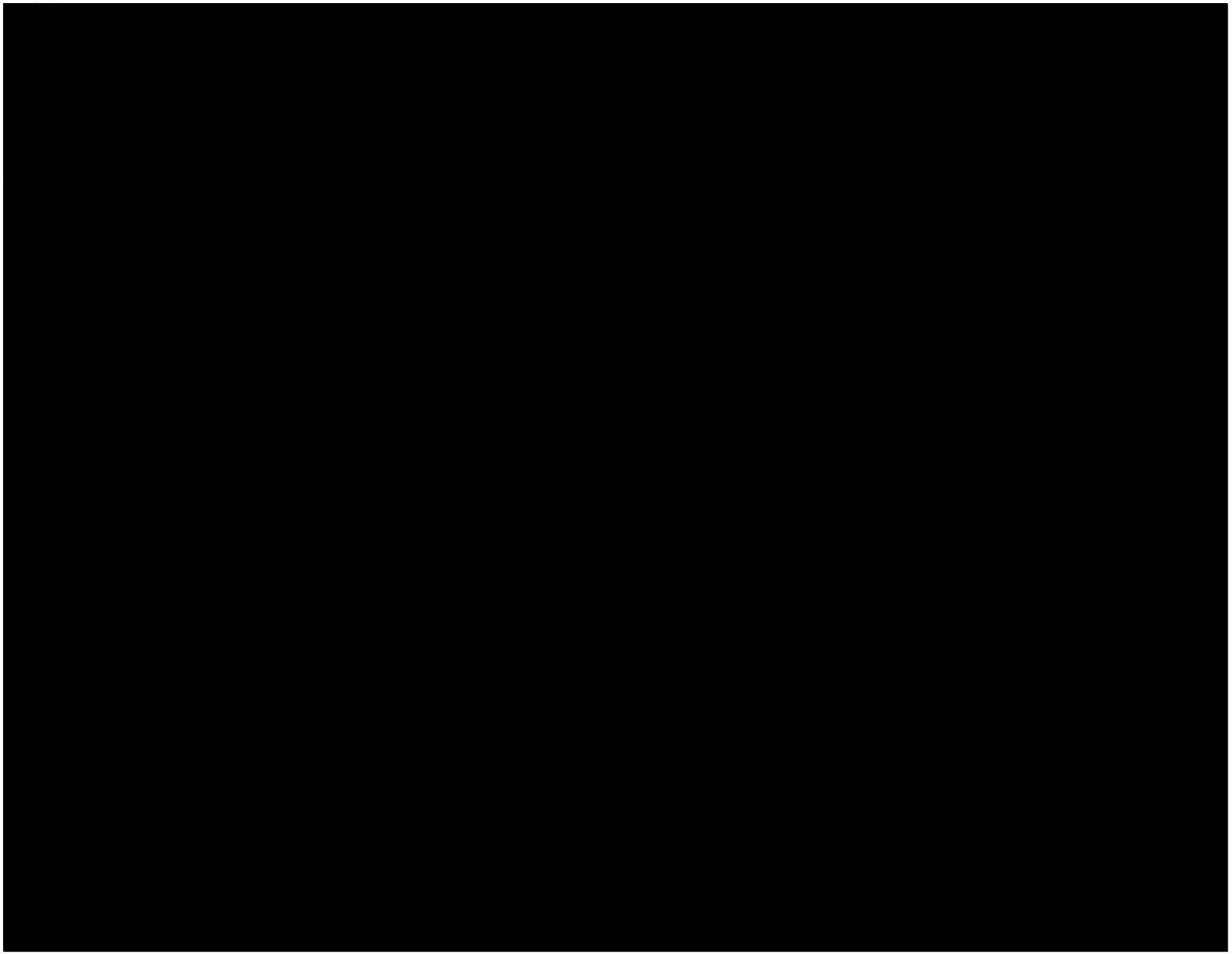
Increased Functionality, Automation

- Highmark WV continues to gain efficiencies through technology and processes. Synergies continue between Highmark WV and PA to leverage best practices and gain cost efficiencies.
- Highmark WV has gained the ability to offer new products and features of products through more efficient product development, expanded reporting capabilities and management programs for clients.
- New capabilities and offerings include PHO (Physician Hospital Organization) tiered benefits, Value Based benefits, Blue Branded Dental, Blues on Call Plus, Patient Center Medical Home, Radiology and Oncology Management Programs
- Leveraged Highmark's portal capabilities – employer/employee and provider (Navinet)
- Associated new account wins: International Coal, Concept Mining, Alcan, ARH (represents 16,000 new members)
- PPACA (Health Care Reform) Compliance



Other Integration Activities

- Medicare Advantage product in West Virginia
- Organizational/Operational Integration
  - Began 2009
  - Strategy Alignment
  - Wellness and Care Management
    - Blues on Call
    - Blue Distinction Centers
  - QualityBlue Provider programs
  - Consistent Procurement processes
  - Pharmacy Benefit Management (PBM)



HIGHMARK.

About Highmark
Vision, Mission & Values
Board and Officers
Newsroom
Corporate Profile
Public Policy
Procurement
Careers
Highmark Direct Stores
Government Business
Community Involvement
Highmark Companies

About Highmark

Corporate Profile

Fast facts about Highmark

In This Section:

Who We Are
What We Do
Fast Facts
Our History
Awards We've Received
Corporate Report

Membership in our health care programs in Pennsylvania and West Virginia numbers 4.8 million people.

Our health, dental, vision, and supplemental health products businesses serve 32.6 million customers nationwide.

The company posted $14.6 billion in total combined revenue in 2010.

Highmark has maintained an "A" rating from Standard & Poor's and A.M. Best.

We received nearly 5.8 million customer and provider inquiries at our call centers in Pittsbur Camp Hill, Erie, and Johnstown.

The company processed 84.9 million health care claims.

Approximately 19,500 people are employed by Highmark, including about 10,500 in Pennsyl

Highmark contributed $175.1 million for programs in support of its corporate mission.

About Highmark's economic impact

Highmark's annual economic impact in Pennsylvania exceeds $2.5 billion. Highmark is a maj contributor to the economic vitality of the state as well as to the individual counties in which operate. Households, businesses, government, and other organizations throughout Pennsylv are recipients of substantial Highmark-related revenue.

The company paid nearly $260 million in federal, state, and local taxes, including property ta in 2010.

Highmark employees logged 111,000 hours of volunteer service, valued at $2.19 million, an raised more than $2.74 million for communities in western and central Pennsylvania through Highmark's United Way campaign.

Learn about Our h

EXHIBIT
JOINT-19

ANNUAL STATEMENT

For the Year Ended December 31, 2010
of the Condition and Affairs of the

Highmark Inc.

NAIC Group Code..... 00812 , 00812 (Current Period) (Prior Period) NAIC Company Code..... 54771 Employer's ID Number..... 23-1294723

Organized under the Laws of Pennsylvania State of Domicile or Port of Entry Pennsylvania Country of Domicile United States

Licensed as Business Type Hospital, Medical & Dental Service or Indemnity Is HMO Federally Qualified? Yes [ ] No [ ]

Incorporated/Organized..... December 6, 1996 Commenced Business..... December 6, 1996

Statutory Home Office	1800 Center Street..... Camp Hill ..... PA ..... 17011 *(Street and Number) (City or Town, State and Zip Code)*	
Main Administrative Office	120 Fifth Avenue Suite 924..... Pittsburgh ..... PA ..... 15222-3024 *(Street and Number) (City or Town, State and Zip Code)*	412-544-7000 *(Area Code) (Telephone Number)*
Mail Address	120 Fifth Avenue Suite 924..... Pittsburgh ..... PA ..... 15222-3024 *(Street and Number or P. O. Box) (City or Town, State and Zip Code)*	
Primary Location of Books and Records	120 Fifth Avenue Suite 924..... Pittsburgh ..... PA ..... 15222-3024 *(Street and Number) (City or Town, State and Zip Code)*	412-544-6902 *(Area Code) (Telephone Number)*
Internet Web Site Address	www.highmark.com	
Statutory Statement Contact	Janine Kopas Colinear *(Name)* janine.colinear@highmark.com *(E-Mail Address)*	412-544-6902 *(Area Code) (Telephone Number) (Extension)* 412-544-8674 *(Fax Number)*

OFFICERS

Kenneth Rudolph Melani, M.D. .....President and CEO
Nanette Paden DeTurk .....Treasurer and CFO
Maureen Loftus Hogel, Esquire #.....Corporate Secretary

OTHER OFFICERS

Ray Hunter Carson, Jr. #	Executive Vice President	Elizabeth Ann Farbacher	Executive Vice President
David Lynn Holmberg	Executive Vice President	Thomas William Kerr	Executive Vice President
Daniel Jay Lebish	Executive Vice President	David Michael O'Brien	Executive Vice President
Matthew Vincent Thomas Ray #	Executive Vice President	Deborah Lynn Rice	Executive Vice President

DIRECTORS OR TRUSTEES

John Robert Baum, Ph.D.	David Arthur Blandino, M.D.	Rosario Yvonne Campos	Thomas John Castellano, M.D.
John Sanderson Cramer	John Henry Damcott, D.M.D.	Don Parks Foster, Esquire	Rufus Ayers Fulton, Jr.
William Michael George	Joseph Clinton Guyaux	Gretchen Frances Robinson Haggerty, Esquire	Calvin Barksdale Johnson, M.D., MPH #
Mark Scott Kamlet, Ph.D.	David Michael Matter	Glen Theodore Meakem	Kenneth Rudolph Melani, M.D.
Victor Alverez Roque	Susan Weiss Shoval	William John Stallkamp	William Elton Trueheart, Ed.D.
Doris Annette Carson Williams			

State of..... Pennsylvania
County of..... Allegheny

The officers of this reporting entity being duly sworn, each depose and say that they are the described officers of said reporting entity, and that on the reporting period stated above, all of the herein described assets were the absolute property of the said reporting entity, free and clear from any liens or claims thereon, except as herein stated, and that this statement, together with related exhibits, schedules and explanations therein contained, annexed or referred to, is a full and true statement of all the assets and liabilities and of the condition and affairs of the said reporting entity as of the reporting period stated above, and of its income and deductions therefrom for the period ended, and have been completed in accordance with the NAIC *Annual Statement Instructions* and *Accounting Practices and Procedures* manual except to the extent that: (1) state law may differ; or, (2) that state rules or regulations require differences in reporting not related to accounting practices and procedures, according to the best of their information, knowledge and belief, respectively. Furthermore, the scope of this attestation by the described officers also includes the related corresponding electronic filing with the NAIC, when required, that is an exact copy (except for formatting differences due to electronic filing) of the enclosed statement. The electronic filing may be requested by various regulators in lieu of or in addition to the enclosed statement.

Kenneth Rudolph Melani, M.D.
President and CEO

Nanette Paden DeTurk
Treasurer and CFO

Maureen Loftus Hogel, Esquire
Corporate Secretary

Subscribed and sworn to before me
This 24th day of February, 2011

a. Is this an original filing? Yes [X] No [ ]

b. If no: 1. State the amendment number
2. Date filed
3. Number of pages attached

COMMONWEALTH OF PENNSYLVANIA
Notarial Seal
Patricia F. Woltjen, Notary Public
City of Pittsburgh, Allegheny County
My Commission Expires Sept. 5, 2011
Member, Pennsylvania Association of Notaries

EXHIBIT
JOINT-20

ASSETS

	Current Year			Prior Year
	1 Assets	2 Nonadmitted Assets	3 Net Admitted Assets (Cols. 1 - 2)	4 Net Admitted Assets
1. Bonds (Schedule D)	1,420,855,915	0	1,420,855,915	1,365,408,680
2. Stocks (Schedule D):				
2.1 Preferred stocks	5,655,603	0	5,655,603	2,417,052
2.2 Common stocks	2,840,973,930	0	2,840,973,930	2,583,739,473
3. Mortgage loans on real estate (Schedule B):				
3.1 First liens	0	0	0	0
3.2 Other than first liens	0	0	0	0
4. Real estate (Schedule A):				
4.1 Properties occupied by the company (less $.....0 encumbrances)	71,314,623	0	71,314,623	74,905,035
4.2 Properties held for the production of income (less $.....0 encumbrances)	0	0	0	0
4.3 Properties held for sale (less $.....0 encumbrances)	0	0	0	0
5. Cash ($.....(5,334,617), Sch. E-Part 1), cash equivalents ($.....16,997,873, Sch. E-Part 2) and short-term investments ($.....211,766,055, Sch. DA)	223,429,311	0	223,429,311	273,617,793
6. Contract loans (including $.....0 premium notes)	0	0	0	0
7. Derivatives	11,770,891	0	11,770,891	9,351,755
8. Other invested assets (Schedule BA)	228,440,961	0	228,440,961	239,853,930
9. Receivables for securities	482,448	0	482,448	80,336
10. Securities lending reinvested collateral assets	312,719,328	0	312,719,328	216,127,125
11. Aggregate write-ins for invested assets	0	0	0	0
12. Subtotals, cash and invested assets (Lines 1 to 11)	5,115,643,010	0	5,115,643,010	4,765,501,179
13. Title plants less $.....0 charged off (for Title insurers only)	0	0	0	0
14. Investment income due and accrued	14,940,224	0	14,940,224	16,806,899
15. Premiums and considerations:				
15.1 Uncollected premiums and agents' balances in course of collection	270,903,666	22,247,405	248,656,261	254,090,162
15.2 Deferred premiums, agents' balances and installments booked but deferred and not yet due (including $.....0 earned but unbilled premiums)	0	0	0	0
15.3 Accrued retrospective premiums	28,900,053	0	28,900,053	38,836,458
16. Reinsurance:				
16.1 Amounts recoverable from reinsurers	2,408,410	0	2,408,410	2,455,181
16.2 Funds held by or deposited with reinsured companies	3,879,861	0	3,879,861	2,208,871
16.3 Other amounts receivable under reinsurance contracts	0	0	0	0
17. Amounts receivable relating to uninsured plans	171,290,043	3,767,975	167,522,068	70,389,766
18.1 Current federal and foreign income tax recoverable and interest thereon	75,496,281	0	75,496,281	92,413,005
18.2 Net deferred tax asset	191,217,216	86,253,595	104,963,621	5,219,478
19. Guaranty funds receivable or on deposit	0	0	0	0
20. Electronic data processing equipment and software	176,144,496	166,432,095	9,712,401	15,745,844
21. Furniture and equipment, including health care delivery assets ($.....0)	27,121,419	27,121,419	0	0
22. Net adjustment in assets and liabilities due to foreign exchange rates	0	0	0	0
23. Receivables from parent, subsidiaries and affiliates	68,522,541	708,294	67,814,247	48,964,975
24. Health care ($.....86,201,621) and other amounts receivable	168,589,975	54,350,628	114,239,347	188,386,980
25. Aggregate write-ins for other than invested assets	366,039,429	292,553,699	73,485,730	85,950,723
26. Total assets excluding Separate Accounts, Segregated Accounts and Protected Cell Accounts (Lines 12 to 25)	6,681,096,624	653,435,110	6,027,661,514	5,586,969,521
27. From Separate Accounts, Segregated Accounts and Protected Cell Accounts	0	0	0	0
28. TOTALS (Lines 26 and 27)	6,681,096,624	653,435,110	6,027,661,514	5,586,969,521
DETAILS OF WRITE-INS				
1101.	0	0	0	0
1102.	0	0	0	0
1103.	0	0	0	0
1198. Summary of remaining write-ins for Line 11 from overflow page	0	0	0	0
1199. Totals (Lines 1101 thru 1103 plus 1198) (Line 11 above)	0	0	0	0
2501. Cash surrender value life insurance	71,373,268	0	71,373,268	67,820,406
2502. Prepaid postretirement plan asset	74,800,184	74,800,184	0	0
2503. Prepaid pension plan asset	140,649,518	140,649,518	0	0
2598. Summary of remaining write-ins for Line 25 from overflow page	79,216,459	77,103,997	2,112,462	18,130,317
2599. Totals (Lines 2501 thru 2503 plus 2598) (Line 25 above)	366,039,429	292,553,699	73,485,730	85,950,723

LIABILITIES, CAPITAL AND SURPLUS

		Current Period			Prior Year
		1 Covered	2 Uncovered	3 Total	4 Total
1.	Claims unpaid (less $.....118,878 reinsurance ceded)	496,975,947	0	496,975,947	506,210,079
2.	Accrued medical incentive pool and bonus amounts	10,693,000	0	10,693,000	10,800,000
3.	Unpaid claims adjustment expenses	9,616,614	0	9,616,614	12,273,563
4.	Aggregate health policy reserves	302,356,835	0	302,356,835	258,247,950
5.	Aggregate life policy reserves	0	0	0	0
6.	Property/casualty unearned premium reserve	0	0	0	0
7.	Aggregate health claim reserves	9,907	0	9,907	4,773
8.	Premiums received in advance	124,243,219	0	124,243,219	133,361,067
9.	General expenses due or accrued	321,201,041	0	321,201,041	293,921,944
10.1	Current federal and foreign income tax payable and interest thereon (including $.....0 on realized capital gains (losses))	0	0	0	0
10.2	Net deferred tax liability	0	0	0	0
11.	Ceded reinsurance premiums payable	5,654	0	5,654	0
12.	Amounts withheld or retained for the account of others	2,575,646	0	2,575,646	7,046,771
13.	Remittances and items not allocated	0	0	0	0
14.	Borrowed money (including $.....50,000,000 current) and interest thereon $.....6,315,198 (including $.....6,315,198 current)	369,343,750	0	369,343,750	427,742,358
15.	Amounts due to parent, subsidiaries and affiliates	44,015,813	0	44,015,813	39,055,171
16.	Derivatives	11,770,891	0	11,770,891	9,351,755
17.	Payable for securities	3,814,865	0	3,814,865	2,423,985
18.	Payable for securities lending	312,719,328	0	312,719,328	216,127,125
19.	Funds held under reinsurance treaties with ($.....0 authorized reinsurers and $.....0 unauthorized reinsurers)	0	0	0	0
20.	Reinsurance in unauthorized companies	0	0	0	0
21.	Net adjustments in assets and liabilities due to foreign exchange rates	0	0	0	0
22.	Liability for amounts held under uninsured plans	225,530,704	0	225,530,704	132,711,715
23.	Aggregate write-ins for other liabilities (including $.....63,481,290 current)	78,548,578	0	78,548,578	142,925,959
24.	Total liabilities (Lines 1 to 23)	2,313,421,792	0	2,313,421,792	2,192,204,215
25.	Aggregate write-ins for special surplus funds	XXX	XXX	0	0
26.	Common capital stock	XXX	XXX	0	0
27.	Preferred capital stock	XXX	XXX	0	0
28.	Gross paid in and contributed surplus	XXX	XXX	0	0
29.	Surplus notes	XXX	XXX	0	0
30.	Aggregate write-ins for other than special surplus funds	XXX	XXX	0	0
31.	Unassigned funds (surplus)	XXX	XXX	3,714,239,722	3,394,765,306
32.	Less treasury stock at cost:				
	32.1 .....0.000 shares common (value included in Line 26 $.....0)	XXX	XXX	0	0
	32.2 .....0.000 shares preferred (value included in Line 27 $.....0)	XXX	XXX	0	0
33.	Total capital and surplus (Lines 25 to 31 minus Line 32)	XXX	XXX	3,714,239,722	3,394,765,306
34.	Total liabilities, capital and surplus (Lines 24 and 33)	XXX	XXX	6,027,661,514	5,586,969,521

DETAILS OF WRITE-INS

2301. Funds held as agent for others	55,228,241	0	55,228,241	120,984,572
2302. Highmark Foundation commitment	0	0	0	19,276,046
2303. Caring Foundation commitment	19,067,288	0	19,067,288	2,026,046
2398. Summary of remaining write-ins for Line 23 from overflow page	4,253,049	0	4,253,049	639,295
2399. Totals (Lines 2301 thru 2303 plus 2398) (Line 23 above)	78,548,578	0	78,548,578	142,925,959
2501.	XXX	XXX	0	0
2502.	XXX	XXX	0	0
2503.	XXX	XXX	0	0
2598. Summary of remaining write-ins for Line 25 from overflow page	XXX	XXX	0	0
2599. Totals (Lines 2501 thru 2503 plus 2598) (Line 25 above)	XXX	XXX	0	0
3001.	XXX	XXX	0	0
3002.	XXX	XXX	0	0
3003.	XXX	XXX	0	0
3098. Summary of remaining write-ins for Line 30 from overflow page	XXX	XXX	0	0
3099. Totals (Lines 3001 thru 3003 plus 3098) (Line 30 above)	XXX	XXX	0	0

STATEMENT OF REVENUE AND EXPENSES

		Current Year		Prior Year
		1 Uncovered	2 Total	3 Total
1.	Member months	XXX	19,165,517	19,743,602
2.	Net premium income (including $.....0 non-health premium income)	XXX	6,274,489,936	6,107,969,441
3.	Change in unearned premium reserves and reserve for rate credits	XXX	3,560,864	(24,672,260)
4.	Fee-for-service (net of $.....0 medical expenses)	XXX	0	0
5.	Risk revenue	XXX	0	0
6.	Aggregate write-ins for other health care related revenues	XXX	0	0
7.	Aggregate write-ins for other non-health revenues	XXX	0	0
8.	Total revenues (Lines 2 to 7)	XXX	6,278,050,800	6,083,297,181
Hospital and Medical:				
9.	Hospital/medical benefits	0	4,535,424,349	4,674,248,485
10.	Other professional services	0	0	0
11.	Outside referrals	0	0	0
12.	Emergency room and out-of-area	0	0	0
13.	Prescription drugs	0	953,936,994	744,138,400
14.	Aggregate write-ins for other hospital and medical	0	21,596,244	21,984,825
15.	Incentive pool, withhold adjustments and bonus amounts	0	24,251,175	24,797,135
16.	Subtotal (Lines 9 to 15)	0	5,535,208,762	5,465,168,845
Less:				
17.	Net reinsurance recoveries	0	(13,146,899)	(18,801,286)
18.	Total hospital and medical (Lines 16 minus 17)	0	5,548,355,661	5,483,970,131
19.	Non-health claims (net)	0	0	0
20.	Claims adjustment expenses, including $.....98,479,223 cost containment expenses	0	201,551,973	190,300,721
21.	General administrative expenses	0	282,254,560	341,671,578
22.	Increase in reserves for life and accident and health contracts including $.....0 increase in reserves for life only)	0	45,660,218	8,381,824
23.	Total underwriting deductions (Lines 18 through 22)	0	6,077,822,412	6,024,324,254
24.	Net underwriting gain or (loss) (Lines 8 minus 23)	XXX	200,228,388	58,972,927
25.	Net investment income earned (Exhibit of Net Investment Income, Line 17)	0	227,736,271	168,311,442
26.	Net realized capital gains or (losses) less capital gains tax of $.....0	0	84,622,434	15,854,553
27.	Net investment gains or (losses) (Lines 25 plus 26)	0	312,358,705	184,165,995
28.	Net gain or (loss) from agents' or premium balances charged off [(amount recovered $.....0) (amount charged off $.....0)]	0	0	0
29.	Aggregate write-ins for other income or expenses	0	(220,383,138)	(160,540,757)
30.	Net income or (loss) after capital gains tax and before all other federal income taxes (Lines 24 plus 27 plus 28 plus 29)	XXX	292,203,955	82,598,165
31.	Federal and foreign income taxes incurred	XXX	10,999,653	8,392,570
32.	Net income (loss) (Lines 30 minus 31)	XXX	281,204,302	74,205,595
	DETAILS OF WRITE-INS			
0601.		XXX	0	0
0602.		XXX	0	0
0603.		XXX	0	0
0698.	Summary of remaining write-ins for Line 6 from overflow page	XXX	0	0
0699.	Totals (Lines 0601 thru 0603 plus 0698) (Line 6 above)	XXX	0	0
0701.		XXX	0	0
0702.		XXX	0	0
0703.		XXX	0	0
0798.	Summary of remaining write-ins for Line 7 from overflow page	XXX	0	0
0799.	Totals (Lines 0701 thru 0703 plus 0798) (Line 7 above)	XXX	0	0
1401.	Dental claims expense	0	6,834,296	6,328,608
1402.	Vision claims expense	0	14,761,948	15,656,217
1403.		0	0	0
1498.	Summary of remaining write-ins for Line 14 from overflow page	0	0	0
1499.	Totals (Lines 1401 thru 1403 plus 1498) (Line 14 above)	0	21,596,244	21,984,825
2901.	Community Health Reinvestment expense	0	(66,265,784)	(58,681,794)
2902.	Other expense	0	(154,117,354)	(101,858,963)
2903.		0	0	0
2998.	Summary of remaining write-ins for Line 29 from overflow page	0	0	0
2999.	Totals (Lines 2901 thru 2903 plus 2998) (Line 29 above)	0	(220,383,138)	(160,540,757)

STATEMENT OF REVENUE AND EXPENSES (Continued)

CAPITAL AND SURPLUS ACCOUNT	1 Current Year	2 Prior Year
33. Capital and surplus prior reporting period	3,394,765,306	3,063,137,999
34. Net income or (loss) from Line 32	281,204,302	74,205,595
35. Change in valuation basis of aggregate policy and claim reserves	0	0
36. Change in net unrealized capital gains and (losses) less capital gains tax of $ 0	(33,342,424)	382,202,446
37. Change in net unrealized foreign exchange capital gain or (loss)	0	0
38. Change in net deferred income tax	10,712,931	(2,188,103)
39. Change in nonadmitted assets	60,899,607	(122,592,631)
40. Change in unauthorized reinsurance	0	0
41. Change in treasury stock	0	0
42. Change in surplus notes	0	0
43. Cumulative effect of changes in accounting principles	0	0
44. Capital changes:		
44.1 Paid in	0	0
44.2 Transferred from surplus (Stock Dividend)	0	0
44.3 Transferred to surplus	0	0
45. Surplus adjustments:		
45.1 Paid in	0	0
45.2 Transferred to capital (Stock Dividend)	0	0
45.3 Transferred from capital	0	0
46. Dividends to stockholders	0	0
47. Aggregate write-ins for gains or (losses) in surplus	0	0
48. Net change in capital and surplus (Lines 34 to 47)	319,474,416	331,627,307
49. Capital and surplus end of reporting period (Line 33 plus 48)	3,714,239,722	3,394,765,306

DETAILS OF WRITE-INS

4701.	0	0
4702.	0	0
4703.	0	0
4798. Summary of remaining write-ins for Line 47 from overflow page	0	0
4799. Totals (Lines 4701 thru 4703 plus 4798) (Line 47 above)	0	0

WTAE.com

Highmark To Buy West Penn Allegheny Health System

Related To Story

Health Insurer Will Be In Competition With UPMC In Pittsburgh

POSTED: 10:23 am EDT June 28, 2011
UPDATED: 5:00 pm EDT June 28, 2011

PITTSBURGH -- Highmark, Pennsylvania's largest health insurer, said Tuesday that it will buy West Penn Allegheny Health System -- a move that administrators said will save jobs and create growth.

"We have been starved for capital," West Penn Allegheny chairman David McClenahan said. "We need a capital partner."

An immediate $50 million grant will be pumped into WPAHS to shore up and strengthen West Penn Hospital in Bloomfield and the Forbes Regional campus in Monroeville.

"This is about maintaining the jobs we have in the system. Without this transition, we've got 11 or 12,000 jobs that would have been in jeopardy," Highmark president and CEO Dr. Ken Melani said.

There will be a total financial commitment of up to $475 million over four years, Highmark said, including $75 million to fund scholarships for students attending WPAHS-affiliated medical schools and to support other health professional education programs.

"It's only going to grow, so, from that perspective, this will be a win for the community in terms of overall job growth over time," Melani said.

Highmark said subscribers who currently use UPMC can continue to do so -- as long as the Pittsburgh health care giant signs on as an in-network insurer. Terms of such a contract would have to be negotiated.

At a news conference, Highmark and West Penn Allegheny hammered UPMC for focusing on competition and profits in health care. They said UPMC has dominated the Pittsburgh market, as well as the payment process, by not allowing patients to have access to WPAHS facilities.

Highmark said it will open contracts to all willing insurers, including local health care giant UPMC, but terms would have to be negotiated. They said they want patients to have access to as many facilities as possible and do not want to engage in competition, which they said UPMC has done aggressively so far.

"Do you see the Red Cross trying to take down the Salvation Army? I don't think so," McClenahan said. "But that's what has happened over the past 10 years as UPMC has tried to put our health care system out of business."

EXHIBIT
JOINT-21

In a statement, UPMC told Channel 4 Action News that West Penn Allegheny created its own problems over the last 10 years by mismanaging its health care system, and that UPMC will remain committed to competition and choice.

Highmark said it will not aggressively go after patients but will offer guidance for those who want to make the transition if UPMC doesn't sign on as an insurer.

"If, for some chance, UPMC continues to say it will not contract with Highmark, then that's a decision they will have to make, and we will have to deal with that," Melani said.

"Patients will have to make a decision on which health care plan they choose," McClenahan said.

The Highmark-West Penn Allegheny deal still has to pass governmental regulations before final approval.

As part of the deal, West Penn Allegheny President Dr. Christopher Olivia will step down and be a consultant to Highmark.

Previous Stories:

- April 13, 2011: Highmark Shoots Down West Penn Allegheny Merger Rumor

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BEFORE THE INSURANCE COMMISSIONER
OF THE STATE OF DELAWARE

In the matter of:	:	
Proposed Affiliation of	:	
BCBSD, Inc. Doing Business As	:	**Docket No. 99-09**
Blue Cross and Blue Shield Of	:	
Delaware, With CareFirst, Inc.	:	

FINAL ORDER AND DECISION

WHEREAS, on December 23, 1998, CareFirst, Inc., a not-for-profit Maryland corporation (hereafter "CareFirst") and BCBSD, Inc., doing business as Blue Cross and Blue Shield of Delaware, a Delaware non-profit health services corporation (hereafter "BCBSD"), entered upon a Business Affiliation Agreement, and thereafter sought review and approval of their plan of affiliation by the Delaware Department of Insurance, pursuant to Chapters 3, 50 and 63 of the Title 18, Delaware Code; and

WHEREAS, on June 18, 1999, I appointed retired judge Battle R. Robinson as Hearing Officer herein, pursuant to 29 Del. C., § 10125; and

WHEREAS, on July 7, 1999, the Attorney General's unopposed application for party status was granted by the Hearing Officer; and

EXHIBIT
JOINT-22

WHEREAS, in accordance with 29 Del. C., Chapter 101 et seq. and 18 Del. C., Chapters 3 and 50, a hearing was held before Hearing Officer Battle R. Robinson, Esquire, on October 25, 26, 1999; and

WHEREAS, at the hearing all parties and interested persons were heard with respect to the proposed affiliation and a period for further comment was provided; and

WHEREAS, the Hearing Officer thereafter issued her Proposed Findings, Recommendations and Order on January 4, 2000; and

WHEREAS, all parties of record were given the opportunity to submit comments and exceptions to the Hearing Officer's Proposed Findings, Recommendations and Order; and

WHEREAS, the findings of fact and conclusions of law contained in the Proposed Findings, Recommendations and Order are well reasoned and amply supported by the summary of evidence also contained therein.

NOW, THEREFORE, IT IS ORDERED, that the summary of evidence, findings of fact, and conclusions of law contained in the Hearing Officer's Proposed Findings, Recommendations and Order (attached hereto as Exhibit A), with the

exceptions and modifications noted below, are incorporated by reference and adopted herein as an integral part of this Final Order and Decision.

Attached to Hearing Officer Robinson's proposed decision as "Attachment A" thereto are a series of recommended conditions upon which she believes approval of this transaction should be based. Retaining most of the intent and substance of those suggested conditions, I have modified and augmented certain of them to strengthen and give more specificity to this Department's (and the Attorney General's) oversight ability hereafter with respect to future activities and transactions of CareFirst and BCBSD and to better assure that no substantial alteration of BCBSD health services as currently provided in Delaware can occur absent prior notice and approval of the Insurance Commissioner and the Attorney General. These revised conditions on which approval of this transaction is predicated and which must be observed by CareFirst and BCBSD as adopted in this Final Order and Decision are attached hereto as Exhibit B. The conditions as set forth by Hearing Officer Robinson and referred to in her proposed recommendations and order are amended as necessary to conform to Exhibit B hereto.

With the exceptions as noted, in all other respects the Proposed Findings, Recommendations and Order of Hearing Officer Robinson are confirmed as correct and adopted.

For the reasons set forth herein, including Exhibits A and B, the affiliation of CareFirst and BCBSD, as outlined in the Business Affiliation Agreement, is hereby

APPROVED, subject to scrupulous adherence to Conditions Nos. 1-20 set forth in Exhibit B.

SO ORDERED this 20th day of March, 2000.

Donna Lee H. Williams

DONNA LEE H. WILLIAMS
Insurance Commissioner

EXHIBIT B

REQUIRED CONDITIONS

1. BCBSD, GHMSI and BCBSMD and CareFirst must maintain their separate corporate identities for legal, financial, accounting, tax and insurance regulatory purposes.

2. BCBSD will continue to be bound by, and conduct its affairs pursuant to, the requirements of 18 Del. C. Ch. 63.

3. CareFirst and BCBSD must agree to comply with the provisions of 18 Del. C. Ch. 50 (Insurance Holding Company System Registration). CareFirst must also agree to the general supervisory authority of the Delaware Insurance Commissioner pursuant to 18 Del. C. Ch. 3.

4. The Boards of Directors of BCBSD and CareFirst shall be restructured, to the extent necessary, to (i) comply with the terms of the draft amended Certificates of Incorporation and By-Laws of the two companies (Joint Exhibits 9, 10, 11, and 12); (ii) minimize interlocking directors by assuring that no less than two members of the Board of Directors of each Board are outside directors who shall not at the same time also serve on the Board of BCBSD or any subsidiary or affiliate of BCBSD (in the case of CareFirst Directors) or on the Board of GHMSI, BCBSMD, CareFirst or any of their subsidiaries or affiliates (in the case of BCBSD Directors); (iii) ensure that no officer or employee of BCBSD or CareFirst is on either Board and (iv) provide that all of the members of the BCBSD Board shall be residents of the State of Delaware. Any change in this structure must receive prior approval of the DOI.

5. The following transfers of assets by BCBSD to GHMSI, BCBSMD, CareFirst or its subsidiaries or any of their affiliates, or any subsequent agreement providing for or facilitating such transfers, are subject to the following conditions and prior approval of the Commissioner, as follows:

(i) Cost allocations: Payment pursuant to cost allocation agreements, service contracts, management, rental and any similar intercompany agreements which exceed $500,000 in the aggregate in any fiscal year (which shall not be less than 365 calendar days) shall be subject to the prior approval of the Commissioner;

(ii) Mandatory transfers: For any transfer for capital reserves, claims payments and other legally enforceable obligations, as defined in the Amended and Restated Intercompany Agreement, from the assets of BCBSD, such transfers shall be in the form of a loan or surplus note, subject to reasonable commercial terms, including but not limited to proper loan or surplus note documentation. Any such mandatory transfers from BCBSD to GHMSI, BCBSMD, CareFirst or its subsidiaries or any of their affiliates which exceed $500,000 in the aggregate in any fiscal year (which shall not be less than 365 calendar days) shall be subject to the prior approval of the Commissioner. Prior to making a "mandatory transfer," as defined in the Amended and Restated Intercompany Agreement, the company receiving the transfer from BCBSD must develop a business

plan to eliminate the problem(s) that created the need for the transfer. The plan must include a timeframe within which the funds transferred will be repaid to BCBSD. In addition, the plan must be filed with and approved by the receiving company's domiciliary insurance commissioner and the Delaware Insurance Commissioner;

(iii) Discretionary transfers: For any discretionary transfers, as that term is defined in the Amended and Restated Intercompany Agreement, from the assets of BCBSD (including the assets of its subsidiaries), such transfers shall be in the form of a loan or surplus note, subject to reasonable commercial terms, including but not limited to proper loan or surplus note documentation. Any such discretionary transfers which exceed $500,000 in the aggregate in any fiscal year (which shall not be less than 365 calendar days) shall be subject to the prior approval of the Commissioner. A discretionary transfer may not be made if the transfer would cause the aggregate balance of outstanding mandatory and discretionary transfers to 1) exceed 10 percent of BCBSD's total admitted assets, 2) exceed 50 percent of its policyholder surplus or 3) cause the RBC ratio to fall below 250% of the authorized control level.

(iv) BPIC Modification: Notwithstanding any provision in the Amended and Restated Intercompany Agreement or any of the related agreements to the contrary, BCBSD shall not assume any liability for, or pay any portion of, the BPIC Modification, as that term is defined in the Amended and Restated Intercompany Agreement, without the express written approval of the DOI. Further, any such assumption of the liability for or payment of the BPIC Modification by BCBSD shall be conditioned upon the submission of a business plan by the entity responsible for such obligation as to the necessity for the assumption or payment by BCBSD, the steps to be taken to remedy the problem which necessitates the involvement of BCBSD, the method of repaying BCBSD for any such assumption or payment, the time within which such repayment shall be made, and the financial benefit to BCBSD of such assumption or payment.

BCBSD must notify the Commissioner in writing of its intention to engage in any transfer that requires the approval of the Commissioner under this paragraph at least 30 days prior to the actual transfer and may engage in the transfer only if the Commissioner approves the transfer in writing. Such transfer shall not be deemed to be approved if the Commissioner has not responded to the request for approval by the end of the 30 days.

A transfer shall not be made, and the Commissioner shall not approve a transfer, which 1) does not meet all requirements of applicable law, 2) does not comply with the terms of the Amended and Restated Intercompany Agreement, 3) would cause the policyholder surplus of BCBSD to fall below statutory reserve requirements of the BCBSA, or 4) would cause the RBC ratio to fall below 250% of the authorized control level.

All transfers of money, notes, investments, equipment or other assets among BCBSD and GHMSI, BCBSMD and CareFirst or any subsidiaries or other affiliates must be properly recorded in the financial

records of BCBSD and documented by a note or other evidence of indebtedness, as an asset of the transferring company and as a liability of the transferee company, unless adequate, reasonable consideration for the transfer has been obtained and documented.

All obligations of BCBSD pursuant to Section II of the Amended and Restated Intercompany Agreement shall cease as of the date of termination of such agreement under Section VII of that agreement; except any obligations of BCBSD to make mandatory transfers pursuant to Section II(a) or transfer for other legally enforceable obligations pursuant to Section II(c) of that agreement, subject to the other conditions set forth herein, for which BCBSD received prior notice of such request under Section II(a) or Section II(c) for the Requesting Party prior to notice by any party of the intent to terminate the agreement. In no event shall any transfers by BCBSD be permitted to be made pursuant to Section II(b) after notice of termination of the agreement has been given.

6. BCBSD shall not participate in any joint venture(s) with CareFirst, BCBSMD, GHMSI or any of their subsidiaries or affiliates to purchase any asset or assets having a total purchase price aggregating more than $500,000 for any fiscal year without the prior written approval of the DOI.

7. Based upon further review of the entire record herein by the Department, it was disclosed that BCBSD had a Rabbi Trust with a balance of $5.5 million as of record date, June 30, 1999. This Rabbi Trust was established in 1991. On a statutory basis, the Rabbi Trust was considered to be a non-admitted asset and as such, reduced surplus. The Rabbi Trust will be funded with an additional $9.9 million of the approximate $15 million cost prior to the close of the affiliation. The $9.9 million combined with the existing balance will be the source of payments for early retirement options under the officer employment agreements. On a statutory basis, the $9.9 million funding will cause an additional reduction in policyholder surplus. The financial impact hereafter upon BCBSD of its officer employment agreements is not prohibited under the Delaware Insurance Code. However, it is strongly recommended that the Attorney General of the State of Delaware, as the party representing the public beneficiaries of BCBSD, hereafter continue to review BCBSD/CareFirst executive compensation issues as they relate to the interest of such public beneficiaries pursuant to the other relevant conditions set forth herein, including prior notice of all significant transactions to the DOJ as well as the DOI.

8. Any contracts between BCBSD and its executive officers which contain provisions for compensation to be paid in the event of a change of control shall not be renewed or extended beyond their current expiration dates without the prior approval of the DOI. For a period of two years following the effective date of affiliation, any new agreements entered into by BCBSD or CareFirst with any of the ten executives covered by the current contracts and which provide for compensation in the event of a change of control shall be filed with the DOI and the DOJ.

9. BCBSD shall maintain its not-for-profit status for at least two years from the date the Affiliation becomes effective. Thereafter, as provided in paragraph 10, it shall not convert to a for-profit status without the approval of the Commissioner and of such other governmental entities as may be required.

10. Any change in the corporate status of BCBSD, including dissolution, merger or change (or conversion) to a for-profit status must receive the prior written approval of the DOI. Likewise, any change in the financial, accounting, or tax reporting methodologies of BCBSD must receive prior written approval of the DOI. No sale or transfer of all, or substantially all, of the assets of BCBSD shall take place without prior written approval of the DOI. Any change in the corporate structure of CareFirst or any of the affiliates which is required to be filed with another regulator must also be simultaneously filed with the DOI.

11. The By-Laws of BCBSD shall provide that upon any dissolution its assets shall be distributed to another non-profit entity. Article Eight of the draft Amended and Restated Certificate of Incorporation of BCBSD which was admitted into the record at the October 25, 1999 hearing as Joint Exhibit 9 and which was approved by the DOI and the DOJ shall not be amended or altered without prior approval of the DOI and the DOJ.

12. Within 60 days of the date the Affiliation becomes effective, BCBSD shall provide to the DOI for approval a proposal outlining the method for performing a valuation of BCBSD as of the date the Affiliation is effective. The purpose of such valuation is to facilitate a future distribution of assets, in the event of a future dissolution or conversion to a for-profit entity. The proposal should be consistent with the approach being taken to develop similar evaluations of GHMSI and BCBSMD under the direction of the District of Columbia Division of Insurance and Securities Regulation and the Maryland Insurance Administration and include the same information. Such evaluation methodology shall also take into consideration any changes in the value of BCBSD from the date the Affiliation becomes effective through the date of such dissolution or conversion to a for-profit entity.

13. BCBSD and CareFirst shall cooperate in any effort by the DISR, the MIA and the DOI to establish identical categories of information on all statutory financial statements and reports.

14. BCBSD and CareFirst shall cooperate in a market conduct examination by the DOI, possibly in conjunction with DISR and MIA, pursuant to Chapter 3 and Chapter 50 of Title 18 of the Delaware Code.

15. Within 180 days of the effective date of the Affiliation and annually thereafter, prior to any changes, BCBSD shall report to DOI in detail any planned rate increases, integration of products, service and administrative functions, any projected cost savings, and timetables for any proposed integration. Within 180 days of the effective date of the Affiliation and quarterly thereafter, BCBSD, prior to any changes, shall report to DOI in detail, and for each county of the state, proposed rate increases, changes in products, services and provider contractors, and proposed reduction in staff, and any proposed reduction in the size of, or the closing of, any facility.

16. After the effective date of the Affiliation, all rate increases, benefit changes and product changes of BCBSD shall be filed with the DOI for approval at least 60 days prior to the effective date of such change; provided, however, that such changes shall be deemed approved if the DOI does not object in writing to such change within such 60 day period.

17. Without the prior approval of the DOI, the Delmarva Health Plan shall not use the BCBS marks.

18. Whenever prior approval must be obtained from the DOI under any of these conditions, simultaneous notice shall be given to the DOJ.

19. These conditions are subject to further order as circumstances may require. These Findings and Recommendations and the Commissioner's Order are subject to further modification or amendment or further review either sua sponte by the Commissioner or by motion of a party.

20. BCBSD and CareFirst shall continue to be subject to the jurisdiction of the DOI for the purpose of implementing the terms of these conditions and the Final Order and Decision.

3/20/00

BEFORE THE INSURANCE COMMISSIONER
OF THE STATE OF DELAWARE

In the matter of	:	
Proposed Affiliation of	:	
BCBSD, Inc. Doing Business as	:	Docket No. 99-09
Blue Cross and Blue Shield of	:	
Delaware, With CareFirst, Inc.	:	

DECISION AND AMENDED ORDER

BACKGROUND

On March 20, 2000, I issued a Final Order and Decision ("Affiliation Order") approving the affiliation (the "Affiliation") of BCBSD, Inc., a Delaware non-profit health services corporation ("BCBSD"), and CareFirst, Inc., a not-for-profit Maryland corporation ("CareFirst" and together with BCBSD, the "Companies"), in accordance with the terms of that certain Business Affiliation Agreement dated as of December 23, 1998, the Affiliation Plan appended thereto, and an Amended and Restated Intercompany Agreement dated as of March 22, 2000 (the "Intercompany Agreement").

Under the Affiliation, CareFirst became the sole member of BCBSD, and BCBSD relinquished its primary Blue Cross® and Blue Shield® license and began operating under a controlled affiliate license issued by the Blue Cross and Blue Shield Association (the "Association") to BCBSD through CareFirst. As discussed in prior Orders in this matter, the Affiliation represented neither a change of control under the Delaware holding company act, 18 Del. C. Chapter 50, nor an acquisition of assets of BCBSD by CareFirst. Rather, the Affiliation Order was premised on the benefits to be gained by the affiliated companies through a consolidation of services and expense reduction mechanisms as opposed to the integration of BCBSD into CareFirst through a purchase and sale agreement. Under the Affiliation, as proposed, approved, and implemented, Carefirst would not and did not pay BCBSD, the State of Delaware or any other person or entity any consideration for the transfer of the membership interest in BCBSD or the transfer of the primary licenses for use of the Blue Cross® and Blue Shield® trademarks (the "Marks") in Delaware.[1]

My approval of the Affiliation was conditioned upon strict adherence to certain enumerated Conditions, attached as Exhibit B to the Affiliation Order. Among others, the required Conditions included:

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[1] I note that the record reflects that Carefirst continues to recognize that the right to use the Marks in Delaware has been and continues to be an asset of BCBSD, and not of Carefirst. *See* letter of John Picciotto, Esquire to Lester Schott, dated March 2, 2004. (Stipulated Exhibit No. 36.)

CareFirst and BCBSD were to comply with the provisions of Chapter 50 of the Delaware Insurance Code and the general supervisory authority of the Delaware Insurance Commissioner (the "Commissioner"). (Stip. Exh. 1 ¶ 3).

Any change in CareFirst's Board structure could only be made with the prior approval of the Delaware Department of Insurance (the "Department"). (Id. ¶ 4).

Certain transfers of assets were subject to the prior approval of the Delaware Insurance Commissioner. (Id. ¶ 5).

Any change in BCBSD's corporate status (including conversion to for-profit status) needed the prior written approval of the Department. (Id. ¶ 10).

The Conditions were subject to further Order as circumstances may require, and the Findings and Recommendations and the Commissioner's Order were subject to further modification, amendment or review, either sua sponte by the Commissioner or by motion of a party. (Id. ¶ 19).

SUMMARY OF THE PROCEEDINGS

In April 2003, the Maryland General Assembly passed legislation (the "Maryland Legislation") directly affecting CareFirst that had the potential to adversely affect BCBSD and its Delaware subscribers. As a result of concerns regarding such legislation as detailed in the record of the Hearing (as defined below), I issued a standstill order on April 10, 2003 (the "Standstill Order") as the first of a series of efforts to protect Delaware consumers.

Subsequently, on May 22, 2003, I issued a Rule to Show Cause why (1) the effect of the Maryland Legislation would not contravene the Affiliation Order, (2) the Affiliation Order should not be terminated, (3) BCBSD's participation in the Affiliation should not be withdrawn, (4) any assets, licenses, authorities, or the like yielded by BCBSD to CareFirst should not be returned, and (5) any other and necessary Order should not be entered protecting the rights of Delaware citizens to the full benefits offered prior to the Affiliation Order (the "Rule to Show Cause").

On November 4, 2003, in accordance with 29 Del. C. § 101 et seq. and 18 Del. C. § 323, a hearing was held before me, as hearing officer, where all parties were heard with respect the issues set forth in the Rule to Show Cause (the "November Hearing"). At the November Hearing, BCBSD and CareFirst jointly proposed a modified affiliation arrangement between the Companies on the terms and conditions set forth in the forms of an Administrative Services and Business Affiliation Agreement (the "ASBAA") and related documents. Among other things, the ASBAA and related documents provided for (i) restoration of majority membership of BCBSD to the BCBSD Board of Directors; (ii) an ongoing business relationship between BCBSD and CareFirst; (iii) oversight by, and reporting requirements to, the Commissioner; and (iv) CareFirst's surrender of the primary licenses to use Blue Cross®

and Blue Shield® trademarks (the "Marks") in Delaware. The record reflects that the parties desired to preserve the benefits of their prior Affiliation by replacing the structural corporate relationship with one that was based on a contractual agreement. The parties agreed that this new contractual relationship would avoid the deleterious consequences of the Legislation on BCBSD and its subscribers.

In my Order of December 1, 2003, I approved the ASBAA and the associated transactions on the condition that, inter alia, the closing of the ASBAA be consummated by December 31, 2003. Although BCBSD and CareFirst agreed that the ASBAA would not become effective unless approved by the relevant insurance regulatory authorities (i.e., Maryland and the District of Columbia), my Order was not so subject. The December 1, 2003 Order provided that the Rule to Show cause would be reinstated should the ASBAA not be executed and implemented by December 31, 2003. As set forth more fully below, on December 23, 2003, the Maryland Insurance Commissioner disapproved the ASBAA pending the MIA's completion of its review of the proposed modified Affiliation Agreement between BCBSD and CareFirst. To date, the ASBAA and related documents remain under review before the Maryland Insurance Administration and therefore, the ASBAA remains unconsummated.

On December 30, 2003, BCBSD notified me that the parties would be unable to meet the deadline set by my Order of December 1, 2003. As a result, the Rule to Show Cause was reinstated. In anticipation of the hearing set for March 9, 2004 (the "Show Cause Hearing" or "Hearing"), I ordered the parties to submit memoranda on two issues: (1) whether the Affiliation Order has been violated by the effect of provisions of the Maryland Legislation, and (2) if the Affiliation Order has been violated, the appropriate remedy for such violation(s). Following the submission of memoranda by BCBSD, CareFirst, the Department of Insurance ("Department") and the Attorney General's Office, I convened a hearing on March 9, 2003 to hear evidence on those two issues. At the conclusion of the proceedings on March 9, I determined that sufficient evidence had been presented concerning a possible violation of the Affiliation Order that it was appropriate to receive evidence concerning an appropriate range of remedies should a violation be found. Accordingly I continued the hearing until April 15, 2004 to consider evidence with respect to what remedy, if any, would be appropriate should a final Order issue that a violation of the Affiliation Order had occurred.

At the conclusion of the April hearing, I asked the parties to separately submit their respective proposed findings of fact, conclusions of law and recommendations by May 3, 2004.

SUMMARY OF THE EVIDENCE

Evidence was presented in the form of briefs and exhibits thereto, through a stipulation of facts, and through the sworn testimony of the following witnesses:

Max S. Bell, Jr., chairman of the board of directors of BCBSD and a Class III director of CareFirst;
John A. Picciotto, executive vice-president and general counsel of CareFirst;

Darryl Reese, director of the Delaware Insurance Department's Examination Rehabilitation and Guaranty;
Timothy J. Constantine, president of BCBSD;
Ann Pruett, senior financial analyst for the Delaware Insurance Department; and
Harold Sandstrom, a principal of Sandler O'Neill and Partners, L.P., an investment banking firm.

During the course of these proceedings, the parties submitted evidence regarding four broad issues: (1) whether the Maryland Legislation conflicted with the terms of the Affiliation Order and the relationships created thereunder; (2) the effect, if any, a partial or total disaffiliation would have upon BCBSD's ability to provide vital services under the Marks; (3) the likelihood of timely approval of the ASBAA by the Maryland Insurance Commissioner; and (4) the effect a partial or total disaffiliation would have on BCBSD's business, operations, and ability to provide service to its subscribers and the residents of the State of Delaware. The evidence presented is summarized below.

A. Evidence Regarding Violations of the Affiliation Order

BCBSD and the Department presented evidence that the Maryland Legislation has caused a violation or violations of the Affiliation Order in four principal ways.

Alteration Of The Corporate Structure

First, BCBSD and the Department submitted evidence that the Legislation has had the effect of significantly altering the corporate structure agreed to by the parties. For instance, the Maryland Legislation mandated that five new Class II members of the CareFirst board be nominated by a committee designated by the Maryland General Assembly and Governor by December 31, 2003 (the "Nominating Committee"), and that seven new class II directors be selected by the Class II directors by July 1, 2004 from a pool of applicants determined by the Nominating Committee to meet the minimum qualifications established by the Maryland Legislation. (Stip. Exh. 6, 7 at §14-115).

On January 1, 2004, five persons selected by the Nominating Committee replaced five of the Class II directors on the CareFirst Board. (Pre-Trial Stip. ¶ 16; see also Stip. Exh. 34). The remaining seven directors will be removed and replaced effective July 1, 2004. (Stip. Exh. 8; Testimony of M. Bell, Tr. at 85). Mr. Bell testified that "the Maryland General Assembly has taken away the company we had become affiliated with and has replaced it with a very different entity." (Tr. at 87).

Mr. Bell testified that prior to agreeing to become affiliated with CareFirst, the BCBSD Board conducted due diligence on the CareFirst Board and its management, and developed a full understanding of the philosophy and principles guiding CareFirst's Board and management. Mr.

Bell testified that the BCBSD Board came to believe that CareFirst was a company that was focused on fiscal discipline, market competitiveness, stabilization of surplus, and product innovation. (Tr. at 85-86).

Mr. Bell further testified that by July 1, 2004, all of the Maryland directors of CareFirst, constituting a majority of the Board, will be replaced by persons who lack institutional memory regarding CareFirst and its affiliates. (Id. at 88). He expressed concern with the fact that the new directors were all either appointed by the State of Maryland, or will be appointed from "a limited pool of applicants screened by the State of Maryland." (Id.).

According to the testimony of Mr. Picciotto, the process by which Class II directors are nominated and appointed represents a departure from what had been the process under the then-existing CareFirst bylaws and charter. (Id. at 65-66). However, Mr. Reese testified that neither BCBSD nor CareFirst has ever applied to the Department for approval of mechanisms for the selection and election of board members (other than that which was approved in the Affiliation Order). (Id. at 124; Pre-Trial Stip. at 16).

In addition to a change in the composition of the Class II directors, BCBSD and the Department presented evidence of other changes in the corporate governance and structure of CareFirst. For instance, the Maryland Legislation, by its terms, provides for, inter alia:

An increase in the size of the Board. Section 14-115(d) of the Legislation increases the maximum size of the CareFirst Board from 21 to 23. (Stip. Exh. 6, 7). Mr. Reese testified that there has been no application to the Department of Insurance regarding any change in the composition, size or structure of the CareFirst Board. (Tr. at 124).

The creation of oversight committees. (Stip. Exh. 6, 7 at §§ 14-115(d)(6)(V), (VI). The provisions cited herein mandate the creation of a Mission Oversight Committee and a Service and Quality Oversight Committee for the CareFirst Board. (See also BCBSD Memo at 6-7; Testimony of M. Bell, Tr. at 89).

A limitation of the compensation of CareFirst board members. (See Stip. Exh. 6, 7 at § 14-115(g)(1); BCBSD Memo at 7-8; Dept. Memo at 9).

A reduction in length of board terms. Section § 14-115(e) reduces the length of a term on the CareFirst Board from three to two years (Stip. Exh. 6, 7; BCBSD Memo at 7, Dept. Memo at 9).

Given the regulatory and legislative environment in Maryland, and the changes in the CareFirst Board, Mr. Bell testified that BCBSD saw little prospect that CareFirst would be managed the way it was prior to the enactment of the Maryland Legislation. To the contrary, Mr.

Bell testified to BCBSD's concern that the new Board will take CareFirst in a different direction, one that might put BCBSD and its subscribers at risk. (Testimony of M. Bell, Tr. at 86-92).

Control Over BCBSD Management Decisions

BCBSD and the Department further submitted evidence that the Maryland Legislation requires routine management decisions made by CareFirst or any affiliate or subsidiary of CareFirst to be pushed up to the CareFirst Board or a Board committee for approval. According to Mr. Bell, "these are decisions that are not limited to policy but involve substantial operations and, in effect, have board members without the expertise of their officers having to pass on actions not traditionally coming to board attention." (Tr. at 85). Mr. Reese testified that no party has applied to the Department with respect to such a change. (Id. at 123-24).

Specifically, Section 14-115(d)(11)(I) of the Maryland Legislation provides that the approval of the CareFirst board is required before BCBSD or CareFirst may (1) modify benefit levels; (2) materially modify provider networks or provider reimbursement; (3) modify underwriting guidelines; (4) modify rates or rating plans; (5) withdraw a product or withdraw from a line or type of business or geographic region; or (6) impact the availability or affordability of health care in the State of Maryland. (Stip. Exh. 6, 7; BCBSD Memo at 7; Dept. Memo at 9-10).

During the April 15, 2004 portion of the Hearing, counsel for CareFirst asserted that the Maryland General Assembly had recently passed a bill (the "2004 Legislation") that may mitigate certain of the more onerous provisions of the Maryland Legislation.[2] The 2004 Legislation was introduced as evidence in this proceeding as Stip. Exh. 67.[3]

The 2004 Legislation purports to address certain issues of concern to both the Department and BCBSD, including, inter alia, a clarification that the mission statement does not apply to BCBSD. Under the Maryland Legislation, this new mission statement applies to insurers or health maintenance organizations "owned or controlled" by a non-profit health service plan that is issued a certificate of authority in Maryland. The 2004 Legislation would amend this by requiring that the non-profit health plan that owns or controls the subject insurer also be doing "business in this state." While the intent of this provision appears to have been to limit the scope of the state-mandated non-profit mission to entities doing business in Maryland, the practical effect of the amending language may be otherwise. CareFirst is a non-profit health service plan doing business in the State of Maryland and, to the extent CareFirst is considered by Maryland authorities to "own or control" BCBSD, the amendment provides no relief to BCBSD whatsoever. To the extent the Maryland Legislation included BCBSD within the scope of the

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2 The implementation of certain aspects of the Maryland Legislation may be modified by a Consent Judgement entered into the United States District Court for the District of Maryland among parties to that litigation: Carefirst, the Association, and the State of Maryland. BCBSD and the Department were not parties to that litigation. In any event the uncertain effect of the modifications does not alter the facts before me, or the result reached.

3 We take notice of the fact that the Legislation was subsequently signed into law by Maryland Governor Ehrlich on May 11, 2004.

non-profit mission requirement before the 2004 Legislation, it may continue to do so. In all events, the 2004 Legislation does not address numerous other provisions of the Maryland Legislation, which impact BCBS and its subscribers, including:

- The five-year moratorium on conversion;
- The appointment of the two non-voting members to the CareFirst Board;
- The requirement to replace the seven remaining Class II directors by July 1, 2004;
- Elimination of the Oversight Committee;
- Exemption of BCBSD disaffiliation from the requirement of Maryland approval; and
- Repeal of Board compensation caps.

Imposition of a New Not-For-Profit Mission

BCBSD and the Department set forth evidence that Section 14-102(f) of the Maryland Legislation adds additional language to the Maryland Insurance Article emphasizing the "nonprofit mission" of CareFirst. (See BCBSD Memo at 5; Dept. Memo at 10).

According to the testimony of Mr. Picciotto, the not-for-profit mission statement is different from "what had been used in the past in the individual companies." (Tr. at 60). However, Mr. Reese testified that no party had sought Departmental approval for the new mission statement. (Id. at 123). According to Mr. Bell's testimony, "the Maryland [L]egislation has now locked CareFirst into a mission that is inconsistent with the mission of The Delaware Plan, and that cannot be changed without a further act by the Maryland General Assembly. We consider this to be a most unacceptable change of circumstance." (Id. at 87).

As noted above, the 2004 Legislation will not insulate BCBSD, directly or indirectly, from the negative impact of the Maryland Legislation.

Imposition of a Five-Year Acquisition Moratorium Affecting BCBSD

Section 7 of the Maryland Legislation provides that a nonprofit health service plan that is subject to the Legislation (including CareFirst and CareFirst of Maryland, Inc., the Maryland Blue plan subsidiary) may not be acquired for a period of five years after the effective date of the Maryland Legislation, irrespective of whether the board feels that such a merger is in the best interests of the company and its subscribers. (Stip. Exh. 6, 7; BCBSD Memo at 9; Dept. Memo at 10-11; Testimony of M. Bell, Tr. at 85).

According to Mr. Bell's testimony, "[g]iven the commitment to the so-called 'nonprofit mission' that all CareFirst directors are now required to demonstrate, any acquisition that would involve a conversion to for-profit status is effectively foreclosed for the indefinite future. Even if another potential strategic partner were to come forward with a proposal to replicate the original arrangement we had with CareFirst ... that strategic alternative is effectively off the table for The Delaware Plan[4] so long as it remains subject to the current structural affiliation." (Tr. at 91-92).

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[4] In his testimony, Mr. Bell refers to BCBSD as "the Delaware Plan".

Both BCBSD and the Department note the negative effect this provision will have in BCBSD's ability to participate in any transaction that might be in the interest of BCBSD and its subscribers. (BCBSD Memo at 16; Dept. Memo at 10-11).

B. Evidence Regarding the Effect of the Return of the Marks to BCBSD

The parties further presented evidence regarding the effect, if any, a total or partial disaffiliation would have upon BCBSD's ability to provide uninterrupted service under the Marks. Among other evidence, the parties introduced a letter from Scott P. Serota, president and chief executive officer of the Association, stating that Association and the Department shared a common interest in ensuring continued Blue Cross® coverage for Delaware subscribers. (Stip. Exh. 51). Mr. Serota's letter affirmed that should CareFirst no longer hold the licenses to use the Marks in Delaware, the Association "would seek to award those licenses to BCBSD." (Id.). That letter further represented that in the event of a dispute about BCBSD's licensure status, provided the *status quo* is maintained, the Association would "continue to deem BCBSD a Controlled Affiliate in good standing, with all attendant rights and responsibilities under the Licenses, until its status were finally determined." (Id.).

Through the testimony of Max Bell, BCBSD asserted that the surrender of the Marks to BCBSD would not affect coverage under the Marks. (Tr. at 95). He testified that

> the single most important asset held by The Delaware Plan is its right to use the [Marks] in Delaware, and it remains critical that we preserve this asset. As you will recall, the ASBAA called for surrender of the marks by CareFirst so that The Delaware Plan could return to the status of primary licensee. We worked closely with the Association last fall and obtained a commitment from it that The Delaware Plan would qualify for, and receive, the primary license once it was relinquished by CareFirst. We have not abandoned our resolve on this issue, and the salient features of The Delaware Plan that caused it to qualify for primary licensee status last fall remain in place today. We have every confidence that the Association will again agree to grant us primary licensee status when the rights are surrendered by CareFirst. I have experience with [the] Association and I know that its interests in protecting our customers is just as great as ours.

(Id.). According to the testimony of Mr. Constantine, if CareFirst refuses to surrender the Marks, the Association would likely take the Marks from CareFirst because it cannot meet the Association's criteria for maintaining a license in Delaware without BCBSD. Were this to occur, Mr. Constantine testified that correspondence and contacts with the Association led him to believe that the Association would award the Marks to BCBSD. (Tr. at 149-50). He further testified that BCBSD is confident that "either limited or total disengagement from CareFirst can be achieved without disruption to or negative impact on our subscribers." (Id. at 136).

C. Evidence Regarding the Likelihood of Timely Approval of the ASBAA

Additionally, the parties presented evidence that the Maryland Insurance Commissioner disapproved of the parties' application for approval of the ASBAA, pending receipt of sufficient information for him to make a decision. (Testimony of J. Picciotto, Tr. at 77; Testimony of M. Bell, Tr. at 82; Dept. Memo at 12). During the March 8 portion of the Show Cause Hearing, counsel for CareFirst stated that he understood that the Maryland Insurance Administration would rule on CareFirst's ASBAA application or before April 15, 2004, provided CareFirst's informational responses were deemed complete. (Tr. at 27).

The Maryland Insurance Commissioner did not rule on the parties' application for approval of the ASBAA as of the date of the April 15, 2004 portion of the Show Cause Hearing. According to the testimony of Mr. Constantine, the parties "see little likelihood that an approval will be forthcoming" from the Maryland Insurance Commissioner in the foreseeable future. (Tr. at 135). Mr. Bell testified that "[w]e do not have a date certain when we might expect [a] decision. Instead, we have been told only that a decision might be produced on or about April 15, and this depends on how [the] Commissioner ... views the information recently submitted to him by CareFirst." (Id. at 82). As of the date of this Order, no decision of the MIA has been issue, or is expected in the immediate future.

D. Evidence Regarding the Impact of Partial or Total Disaffiliation on BCBSD's Operations

Mr. Constantine's testimony provided evidence regarding the impact on BCBSD that would result from a limited or total disengagement from CareFirst. Mr. Constantine testified that even under the most conservative projections, BCBSD was confident that either limited or total disengagement from CareFirst "can be achieved without disruption to or negative impact on our subscribers." (Tr. at 136).

Mr. Constantine noted that in many areas of the operation of BCBSD subsequent to the affiliation with CareFirst – such as maintenance of provider networks, claims handling and payment and most of its information systems – BCBSD has continued to perform the primary functions involving those areas. (Id. at 136-137). As to others, such as marketing, product development, market research and product marketing as well as payroll, human services and employee benefits, BCBSD is confident that it can cost effectively resume these functions on behalf of an autonomous BCBSD. (Id. at 136-39).

Mr. Constantine testified that BCBSD would face projected increases in administrative costs in connection with its return to independent status in the following amounts: $1.8 million for the last six months of 2004; $3.8 million for 2005; and $3.9 million for 2006. (Id. at 141). In the event of a complete disaffiliation, the net incremental administrative expense increase would be $1.3 million for the last six months of 2004; $2.7 million for 2005; and $2.8 million for 2006. (Id. at 142, see also Stip. Exh. 63).

Mr. Constantine's forecasts were based on the assumption that the BCBSD membership would be returned on July 1, 2004. His calculations further assumed that BCBSD's membership rate would grow at a slower rate in 2005 and 2006 than has historically been the case and, for purposes of a sensitivity analysis, that BCBSD would encounter a three-percent decrease in membership for 2005 and 2006. (Tr. at 141, see also Stip. Exh. 63).

Mr. Constantine then took the projected expenses discussed above and used them to model what the impact of these expenses would be on BCBSD's overall financial performance under a one percent membership growth and a three percent membership decline scenario for three years. He assumed that BCBSD's medical loss ratio would increase from 88.4 percent in 2003 to 89.4 percent, 89.6 percent, and 89.9 percent for 2004, 2005 and 2006, respectively. Under this model, BCBSD would "remain in a solid financial position even if CareFirst is unable or unwilling to continue a business relationship" with BCBSD." (Tr. at 144, see also Stip. Exh. 63). Specifically, the model demonstrated projected results for 2005 as follows:

Revenue: $976,000,000
Incurred care: $875,000,000
Operating expense ratio: 8.7 percent (excluding HIPAA costs)
Net income ratio from operations: 1.1 percent
Risk based capital as a percentage of ACL RBC: 1,340 percent

(Stip. Exh. 63). With respect to 2006, the model demonstrated the following projected results:

Revenue: $1,022,000,000
Incurred care: $918,000,000
Operating expense ratio: 8.6 percent
Net income ratio from operations: 1.1 percent
Risk based capital ratio: 1,370 percent

The Department's review of BCBSD's testimony and projections was performed by Ann Pruett, a senior financial analyst at the Delaware Department of Insurance, who testified on behalf of the Department. Ms. Pruett, who is responsible for the review and analysis of health insurance companies licensed in Delaware, reviews company statements to assure compliance with the Delaware insurance code and statutory accounting practices. She reviewed the projections prepared by BCBSD and presented by Mr. Constantine in his testimony to determine if BCBSD would still be in regulatory compliance under Delaware law if it became disaffiliated with CareFirst. (Tr. at 168-70). In that regard, Ms. Pruett reviewed not only the BCBSD projections but the financial statements for BCBSD from 1999 through 2003. She also interviewed BCBSD's corporate controller regarding the financial projections discussed by Mr. Constantine. (Id. at 170).

Ms. Pruett specifically focused on the projections to ensure that BCBSD took into account services the Company would need to obtain if they were no longer receiving those services from CareFirst. Ms. Pruett concluded that BCBSD did in fact take these services into consideration as part of its projections. (Id. at 171). Ms. Pruett specifically focused on the capital surplus, operating results and management of BCBSD in performing this analysis. She examined the three capitalization ratios traditionally employed by the

Department to measure a company's financial health: the RBC ratio, the premium surplus ratio and the combined ratio. (Id. at 172). She noted that the RBC ratio for 2003 was $118.4 million – a figure well above the minimum standard, and one which has remained stable since 1999. The RBC ratio has increased $29.3 million from 1999. (Id. at 172). As to the premium surplus ratio, Ms. Pruett noted that for a healthy insurance company, the Department likes to see a maintained ratio of less than 5:1. In 1999, BCBSD had a premium surplus ratio of 1.78:1. In 2003, such ratio was 2.26:1. (Id. at 173). Finally, Ms. Pruett calculated the combined ratio (the sum of the medical loss ratio and the administrative expense ratio). BCBSD's combined 2003 medical loss and administrative expense ratios were 93.9%. (Id. at 173).

Ms. Pruett testified that while there had been some minor changes in management as a result of the affiliation, staffing had generally increased following the affiliation and there were no changes for BCBSD that were out of line with any other health insurance company doing business in the State. (Id. at 174). In her professional judgment, Ms. Pruett concluded that the principal expense incurred under disaffiliation would occur in administration, and that the total increases in costs as a result of disaffiliation would be relatively small compared to the Company's total expenses. (Id. at 175).

In addition, Ms. Pruett testified that she "stressed" BCBSD's projections and increased the administrative expense figure by 50%. She found even at that level, BCBSD would not face any financial difficulty or be out of regulatory compliance should its administrative expenses increase to such an extent. (Id.). She concluded that BCBSD's projections were appropriate, and were a realistic measure for valuing a scenario in which BCBSD would disaffiliate from CareFirst. She concluded that BCBSD would, in her judgment, be able to meet all the applicable regulatory and statutory requirements to remain a solvent and viable health service corporation under Chapter 63 of the Delaware Insurance Code. (Id. at 176).

Finally, Mr. Harold Sandstrom, a principal of the firm of Sandler O'Neill & Partners, L.P. ("Sandler O'Neill"), presented testimony on behalf of the Department. Mr. Sandstrom had previously testified as an expert for the Department at its November 4, 2003 hearing in this matter. He testified that he had been asked to reconsider his opinion of November 4 based on an assumption that BCBSD and CareFirst would disaffiliate, that there would be no ASBAA agreement between them, and that BCBSD would have to obtain the services provided for under ASBAA from other sources. Mr. Sandstrom submitted and summarized a letter report introduced into evidence in this proceeding as Stip. Exh. 68. He noted that the Department of Insurance had asked Sandler O'Neill to update its previously submitted November 4, 2003 report to consider the impact on BCBSD of a modification of its relationship with CareFirst, the principal provisions of the proposed modification being that: (1) CareFirst would no longer provide certain services for BCBSD; (2) BCBSD would continue to operate as a Blue Cross® Blue Shield® licensee; and (3) that BCBSD's operative corporate documents would be amended to accommodate the transfer of a majority

membership in BCBSD back from CareFirst to the BCBSD board of directors. (Tr. at 183-84).

Mr. Sandstrom testified that his firm's conclusion, while financial in nature, is predicated on BCBSD retaining its Blue Cross Blue Shield status. (Id. at 184). Beyond the earlier work performed by it, Sandler O'Neill examined the previously referenced BCBSD management financial forecast (Stip. Exh. 63) as well as various other information available regarding BCBSD, including:

> · a member Touchpoint Service update for the second half of 2003 with results dated April 2, 2004;
> · a Standard and Poor's Insurance Rating Analysis dated December 2003;
> · interviews conducted with BCBSD senior management including Phillip A. Carter, corporate controller for BCBSD, Timothy J. Constantine, and William E. Kirk, BCBSD's vice president, general counsel and corporate secretary, regarding the business financial condition results of operation and prospects of BCBSD in the impact of the proposed assumption of services previously provided by CareFirst.

(Tr. at 185-86).

Mr. Sandstrom testified that, based upon his Company's review and analysis of the information and data referenced in the letter report, Sandler O'Neill believes that the assumption by BCBSD of the services heretofore provided by CareFirst, together with the assumption of the related cost of such services as projected by BCBSD, would cause no material adverse effect on the financial condition of BCBSD. Moreover, Sandler O'Neill noted that the significant consolidation of the health insurance sector and the likely impact on smaller insurers indicate that an affiliation with a substantial regional or national health insurer will continue to be important to BCBSD's operating and financial condition. (Id. at 187-88).

Carefirst, for its part, offered no separate evidence or meaningful cross examination to dispute or contradict the testimony cited above. Indeed, although Carefirst has urged a different standard of review and result, it does not seriously challenge the applicability or credibility of the testimony presented by the other parties to this proceeding.

FINDINGS OF FACT AND DECISION

I have carefully reviewed the extensive evidence presented in this matter and have considered all of the legal arguments of the parties and the law applicable to the issues under consideration. Based on the extensive record in this matter and the findings made below, the relief ordered herein is appropriate, supported by substantial evidence, and, as set forth more fully below, within my broad statutory power to grant. Moreover, in light of the numerous violations of the Affiliation, such relief is justified on the basis of the evidence before me.

The Maryland Legislation (which failed to appropriately distinguish any of the Maryland CareFirst companies from each other or from BCBSD) creates conflicts in various ways with the terms of the Affiliation Order and the relationships created thereunder. BCBSD identified thirteen such issues, but both BCBSD and the Insurance Department focused on four fundamental problems arising from the Maryland Legislation involving corporate governance and board composition; Board review of routine management decisions; imposition of a newly configured Maryland not-for-profit mission; and the imposition of a five-year acquisition moratorium affecting BCBSD. I shall address each of these below.

Restructuring of CareFirst Governance

The Maryland Legislation, even as allegedly modified by the Consent Judgment, has caused the removal and replacement of five of the initial twelve Class II directors by January 1, 2004. The five new Class II directors, seated on January 1, 2004, were selected by the Nominating Committee created by the Maryland Legislation, and the remaining Class II directors had no voice in their selection. The remaining seven Class II directors must be replaced on or before July 1, 2004. The replacement directors are selected by the now existing Class II directors (five of whom are brand new) out of a finite pool of applicants screened by the Nominating Committee. This action forces the replacement of a voting majority of a Board upon which BCBSD conducted careful due diligence before deciding to proceed with the Affiliation. These changes to the CareFirst Board, none of which have been approved by the Department, put a significantly different Board, with significantly different goals, objectives and responsibilities, in control of CareFirst, a result inconsistent with the terms of the Affiliation I reviewed and approved. I find there is substantial risk that the new Class II directors, a majority of the CareFirst board, will not and cannot exercise the judgments and attitudes about the company's governance and strategic direction that characterized the CareFirst Board at the time I approved the Affiliation. I further find that there is a substantial risk that this new majority will govern CareFirst in a manner that is inconsistent with the present long term objectives of the BCBSD Board.

Board Review of Routine Management Decisions

The Maryland Legislation, as originally enacted, imposed on CareFirst and its affiliates including BCBSD, a new requirement providing that six categories of routine management actions be approved by the CareFirst Board or a committee of the Board. Specifically, Board approval must be obtained in order to modify benefit levels, materially modify provider networks or reimbursement; modify underwriting guidelines, modify rates, withdraw a product

or withdraw from a line of business, and any other action that would impact the availability or affordability of healthcare in "the state."

The 2004 Legislation, modifies this new requirement to clarify that it only applies to action that affects Maryland residents. However, this clarification addresses only certain of the concerns expressed in this proceeding, because BCBSD engages in none of the activities in question in the State of Maryland. I find that the requirements of this section, even as modified by the 2004 Legislation, place new, specific and detailed requirements on the CareFirst Board which did not exist at the time of my review and approval of the Affiliation. In addition, I also find that the CareFirst charter and Bylaws that I approved in connection with my approval of the Affiliation do not contain provisions limiting the authority of management in this manner.

The New Not-For-Profit Mission of CareFirst

As revised by the Maryland Legislation, Section 14-102 of the Insurance Article now contains a provision mandating that the mission of CareFirst shall be to:

(1) Provide affordable and accessible health insurance to the plan's insureds and those per
(2) Assist and support public and private health care initiatives for individuals without hea
(3) Promote the integration of a statewide health care system that meets the needs of all M

CareFirst is charged with developing goals, objectives and strategies for carrying out this statutory mission, and is required to make a report of such to the oversight committee created by the Maryland Legislation. (Md. Ins. Code § 14-102(d)). This mission was not a part of CareFirst's corporate Charter and Bylaws when I approved the Affiliation.

As noted previously, the 2004 Legislation as a practical matter and in light of the Maryland authorities' apparent view that CareFirst "owns or controls" BCBSD, does not fix the imposition of this mission on BCBSD. In all events, I must assume that the Maryland Insurance Administration will enforce the non-profit mission on CareFirst.

This may well include the view of the Maryland Insurance Administration that the non-profit mission of CareFirst requires that it remain in, or otherwise subsidize, unprofitable markets and lines of business. A non-profit mission which causes CareFirst to be governed, managed and operated in a way that does not give first priority to its financial safety and soundness is not consistent with the type of Company CareFirst was when BCBSD sought Affiliation, and at the time I reviewed and approved the Affiliation. Further, continued structural Affiliation with such a company is not in the best interest of BCBSD and its Delaware subscribers.

The Five Year Moratorium on Acquisition

Section 7 of the Maryland Legislation provides that a nonprofit health service plan that is subject to the Legislation (including CareFirst and CareFirst of Maryland, Inc., the Maryland Blue plan subsidiary) may not be acquired for a period of five years after the effective date of the Legislation (May 22, 2008). This assures that BCBSD, whose sole member is CareFirst, will not be sold, combined or converted as a part of CareFirst, even if the BCBSD Board determines such a transaction is in BCBSD's best interest. I further see little possibility that, under the present structural affiliation, BCBSD could be acquired independently of CareFirst, because this would require the consent of CareFirst as BCBSD's sole member. New Class II Board members cognizant of and accountable to a new set of non-profit principles and a moratorium on sales compelled by Maryland law are most unlikely to allow BCBSD to be sold and converted. CareFirst Board approval is necessary to authorize this transaction under the present BCBSD Certificate of Incorporation. (See Stip. Exh. 45 at Article ELEVEN(b)). This is particularly the case if the financial condition of CareFirst deteriorates, a circumstance in which BCBSD is most likely to determine that it needs to leave the CareFirst fold.

I find that the five-year moratorium included in the Maryland Legislation, when coupled with the statutory non-profit mission of CareFirst, effectively precludes BCBSD from being acquired by a third party at least through May 22, 2008, and very likely for the indefinite future thereafter, notwithstanding that such an acquisition might be in the best interests of BCBSD and its subscribers. It also precludes me from considering and approving such an acquisition, which is contrary to my retained authority to do so under conditions 9 and 10 of Exhibit B to the Original Order.

Effect of Return of the Marks to BCBSD

I have also carefully considered the record with respect to the effect, if any, the return of the Marks would have upon BCBSD's ability to provide services to its customers. Evidence on this issue was presented, inter alia, in the form of (1) a letter from the president and CEO of the Association, affirming that in the event CareFirst no longer held the Marks, the Association would seek to award them to BCBSD (Stip. Exh. 51); (2) the testimony of Max Bell, stating among other things that BCBSD obtained a commitment from the Association that it would receive the primary license once it was relinquished by CareFirst (Tr. at 95); and (3) the testimony of Tim Constantine, who stated that BCBSD was confident that "either limited or total disengagement from CareFirst can be achieved without disruption to or negative impact on our subscribers." (Tr. at 136).

None of the parties have offered evidence indicating that the Association would not promptly return the Marks to BCBSD in the event of a partial or total disaffiliation. Indeed, the parties presented evidence that a failure to promptly return the Marks to BCBSD is not in the best interest of the Association. CareFirst has no ability to use the Marks in Delaware except through BCBSD, and if BCBSD is not a controlled affiliate of CareFirst under the Association's rules, CareFirst would no longer be in a position to exercise any rights as "primary licensee." In such instance, the Association would be required to find another plan to serve as a "primary licensee."

Mr. Constantine testified that, other than through BCBSD, CareFirst would not be able to meet the Association's criteria for licensing in Delaware. Mr. Bell testified that BCBSD would qualify under the Association's criteria to serve as a "primary licensee" in connection with the contemplated closing of the ASBAA, and that nothing had changed that would prevent BCBSD from qualifying as primary licensee today. For all of the foregoing reasons, I find that a return of the Marks to BCBSD would have no adverse effect on BCBSD's ability to provide services to its customers and the residents of the State of Delaware under the Marks.

I have also considered the effect of any disaffiliation of CareFirst and BCBSD on the financial condition of BCBSD. Based on the record evidence, including testimony of Mr. Reese, Mr. Pruett, Mr. Constantine and Mr. Sandstrom, I find that disaffiliation will not have any internal adverse financial effect on BCBSD and that, if disaffiliation occurs, BCBSD will be able to satisfy all applicable regulatory and statutory requirements to remain a solvent and viable health service corporation under Chapter 63 of the Delaware Code.

CONCLUSIONS OF LAW

Approval of the Affiliation was premised upon an order that BCBSD "must maintain" its separation from CareFirst for insurance regulatory purposes (Stip. Exh. 1, Exhibit B at ¶ 1) and that the Department would retain "oversight ability [after the Affiliation] with respect to the future activities and transactions of CareFirst and BCBSD" in order to ensure "no substantial alterations of BCBSD health services as currently provided in Delaware can occur absent prior notice and approval of the Insurance Commissioner and Attorney General." (Id. at p. 3).
Based upon the factual evidence in this matter, it is obvious that CareFirst cannot or will not be able to adhere to various conditions set forth in the Affiliation Order (the "Required Conditions") and conditions ordered subsequent to the Affiliation Order. A prominent example of such a violation is the alteration of the CareFirst Board without the approval of the Delaware Insurance Commissioner. The provision of the Affiliation Order that is most clearly affected by the Maryland Legislation is condition 4, which provides:

> The Boards of CareFirst and BCBSD shall be *restructured*, to the extent necessary, to (i) comply with the terms of the draft amended Certificates of Incorporation and By-Laws of the two companies (Stip. Exh. 9, 10, 11 and 12);
>
> * * *
>
> Any change in this *structure* must receive prior approval of the Insurance Department.
>
> (Stip. Exh. 1, Exhibit B at ¶ 4) (emphasis added).

The structure of the Boards must not change without the prior approval of the Insurance Department. If for *any* reason the structure of either Board is altered, such alteration cannot be accomplished until after the Department has been apprised of it, and approves it. Such approval

was neither sought nor obtained in connection with the passage of the Maryland Legislation, nor was it sought or obtained in connection with the Consent Order entered by Judge Motz on June 6, 2003. Still further, no approval was sought or obtained pursuant to the Standstill Order when the first five new Class II Directors took office in January. Consequently, I find that both my Original Order and the Standstill Order have been, and continue to be, violated as a result of the Maryland Legislation and the changes that resulted from it.

The Delaware Insurance Commission is an administrative agency responsible for enforcing the provisions of the Insurance Code. See State Farm Mut. Auto. Ins. Co. v. Hale, 297 A.2d 416, 418 (Del. Ch. 1972). In order to fulfill that responsibility, the Insurance Commissioner has been granted broad statutory powers. See 18 Del. C. § 310(b) ("The Commissioner shall have the powers and authority expressly vested by or reasonably implied from this title."); see also 18 Del. C. § 5008 ("The Commissioner may, upon notice and opportunity for all interested parties to be heard, issue such rules, regulations and orders as shall be necessary to carry out the provisions of this chapter."). This broad statutory power carries with it the authority to do all that is reasonably necessary to execute that power. Dep't of Correction v. Worsham, 638 A.2d 1104, 1107 (Del. 1994); Atlantis I Condo. Ass'n v. Bryson, 403 A.2d 711, 713 (Del. 1979). The implied authority of Delaware administrative agencies has been described by the Court of Chancery as follows:

> [I]t is . . . well established that an express legislative grant of power or authority to an administrative agency includes, by implication, the grant of power to do what is reasonably necessary to be done to implement such power and authority. And in determining whether or not there is an implied grant of authority, a particular statutory scheme must be viewed in its totality. When an agency is vested with a broad range of discretionary powers it is likely that the General Assembly intended to vest implied authority in such agency to do that which is incidental, implied, necessary and proper in light of the objectives sought to be gained and in light of the express powers granted.

Retail Liquor Dealers Ass'n of Delaware, et al. v. Delaware Alcoholic Beverage Control Comm'n, 1980 WL 273545 (Del. Ch. Apr. 23, 1980).

It has also been frequently held that when an administrative agency makes a decision, it has the inherent power to vacate it so long as it has retained jurisdiction over the matter. See Lyons v. Delaware Liquor Comm'n, 58 A.2d 889, 895 (Del. Gen. Sess. 1948); Henry v. Dep't of Labor, 293 A.2d 578, 581 (Del. Super. 1972). As the following excerpts from the Affiliation Order demonstrate, I expressly retained jurisdiction in this matter in order to enforce the provisions of the Affiliation Order:

> For the reasons set forth herein, including Exhibits A and B, the affiliation of CareFirst and BCBSD, as outlined in the Business Affiliation Agreement, is hereby APPROVED, subject to scrupulous adherence to Conditions Nos. 1-20 set forth in Exhibit B. (Stip. Exh. 1 at 3-4).
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> * * *

3. CareFirst must agree to comply with the provisions of 18 Del. C. Ch. 50 (Insurance Holding Company System Registration). CareFirst must also agree to the general supervisory power of the Delaware Insurance Commissioner pursuant to 18 Del. C. Ch. 3. (Id., Exhibit B at 1).

* * *

19. These conditions are subject to further order as circumstances may require. These Findings and Recommendations and the Commissioner's Order are subject to further modification or amendment or further review either sua sponte by the Commissioner or by motion of a party. (Id., Exhibit B at 5).

For all of the foregoing reasons, I have the power to reopen and amend the Affiliation Order if circumstances warrant.

The changes brought about because of the Maryland Legislation, as evidenced by the extensive record in this matter and summarized above, have not only detrimentally affected the rights of the parties, they have ignored and impaired the authority of the Delaware Commissioner of Insurance, under Delaware law, to independently regulate a major domestic Delaware health insurer. The conscious disregard of this authority and the conditions contained in my prior orders cannot pass unaddressed without undermining the authority of the Commissioner and the Department. See Eastern Commercial Reality Corp. v. Fusco, 654 A.2d 833, 836 (Del. 1994).

The State of Maryland removed the CareFirst with which BCBSD became affiliated and has effectively replaced it with another entity. This action was taken without consultation with Delaware authorities and entirely without the consent of the BCBSD Board. The Maryland Legislation gives rise to a number of substantial risks to the safety and soundness of CareFirst, and it also precludes the acquisition and conversion of BCBSD in the future, even if BCBSD determines such to be in the best interests of its subscribers. I do not believe it is appropriate to take a "wait and see" attitude with respect to these concerns. If the financial condition of CareFirst deteriorates as a result of the changes in its mission and governance, it may be too late at that time to disentangle a structurally affiliated BCBSD from CareFirst before irreparable damage to the financial condition or reputation of BCBSD occurs. Real damage to the Affiliation has been done and action must be taken now.

With respect to the 2004 Legislation, while it does provide some relief as to certain items in the Maryland Legislation, it falls far short of the reforms needed to fully address the many concerns of the changes which have been and will continue to be implemented.

I have carefully considered all of the arguments raised by CareFirst in its memorandum, including, without limitation, those asserting that I lack authority to order any remedy, excuse of violation of my Orders based on the concept of "impossibility of performance" or lack of "just cause" to order disaffiliation. For the reasons presented by BCBSD and the Insurance Department in their memorandum, I am not persuaded by CareFirst's view of the facts or the law.

The remedy proposed both by BCBSD and the Department is reasonable not only because of the gravity of the difficulties created by the Maryland Legislation and the infringement upon my authority, but also because the remedy has, for a number of reasons, little prejudicial impact on CareFirst. First, the remedy sought mirrors quite closely the fundamental terms and conditions of the ASBAA; for instance, the Marks shall be restored to BCBSD, but the practical aspects of the affiliation may be preserved. Second, CareFirst's current membership in BCBSD does not equate to "ownership" in the sense that ownership of shares of a stock corporation does. BCBSD is not an asset of CareFirst and no part of the value of BCBSD could ever be distributed to CareFirst. Third, CareFirst has recognized that the right to use the Marks under any license of the Association is an asset of BCBSD's, and because CareFirst can not transact "Blue" business in Delaware except through BCBSD, permitting CareFirst to hold the right to use the Marks would be useless absent an affiliation with BCBSD. Fourth, no consideration was paid by CareFirst in return for becoming sole member of BCBSD and for becoming primary licensee with respect to the Marks in Delaware.

Changes in the CareFirst Board and other violations of my Orders can be ameliorated by return of the membership of BCBSD to the BCBSD Board. Such a remedy will remove BCBSD, by definition, from various onerous provisions of the Maryland Legislation. Achieving this, along with CareFirst's surrender of the Marks in Delaware – which is appropriate since the Marks are assets of BCBSD and CareFirst cannot transact business in Delaware under the Marks except through BCBSD – will eliminate significant problems arising under the Maryland Legislation; avoid the uncertainty of decisions of CareFirst's new management, which itself faces considerable challenges and pressures from the changed environment in Maryland; and will allow, if the parties so elect, the continuation of a contractual affiliation between BCBSD and CareFirst.

Based on all the foregoing, **IT IS HEREBY ORDERED THAT**:

The Affiliation Order has been violated by the effect and implementation of the Maryland Legislation, including, inter alia, by provisions which have the practical effect of altering the corporate governance of CareFirst and BCBSD and impinging upon the ability of the Insurance Commissioner to maintain supervisory authority over BCBSD for the benefit of the residents of the State of Delaware.

Neither BCBSD nor the residents of the State of Delaware will be adversely affected if BCBSD were required to operate as a primary licensee of the Blue Cross® and Blue Shield® Association in the State of Delaware.

Subject to the further terms and conditions of this Order, henceforth BCBSD's further participation in the surviving aspects of the 1998 Business Affiliation Agreement and the Amended and Restated Intercompany Agreement (the "1998 Agreement") is prohibited.

Within 30 days of the date of this Order, CareFirst and BCBSD shall execute and file all documents and otherwise take such steps as are necessary to transfer corporate membership in BCBSD from CareFirst to the board of directors of BCBSD. CareFirst and BCBSD are directed to consult and cooperate with the Association and to undertake to ensure that the transfer of

membership does not jeopardize BCBSD's use of the Marks following the transfer of membership to the BCBSD Board.

Within 30 days of the date of this Order, CareFirst shall take such steps as are necessary to surrender its rights to use the Marks as "Primary Licensee" in Delaware, CareFirst shall cooperate with BCBSD and the Association as necessary to facilitate BCBSD's attainment of "Primary Licensee" status in Delaware. BCBSD shall take all necessary steps to ensure that its right to use the Marks is not interrupted or lost.

If, within 10 days following receipt of this Order, CareFirst and BCBSD separately give notice in writing to the Insurance Department of their respective intentions to continue the Affiliation on a contractual basis, then, notwithstanding the prohibition set forth in Paragraph 3 hereof, CareFirst and BCBSD may continue to operate pursuant to the surviving terms and conditions of the 1998 Agreement that do not prevent the parties thereto from either the transfer of membership in BCBSD to the BCBSD Board, or the surrender by CareFirst of its licenses to use the Marks in Delaware.

CareFirst and BCBSD shall submit to the Insurance Department for approval such contracts and agreements as they may jointly propose to implement, in order to continue the affiliation of the companies on a non structural basis, within 60 days from the date of this Order.

If no notice is forthcoming from the parties pursuant to paragraph 6 of this Order, CareFirst and BCBSD shall cooperate fully in the orderly termination of the affiliation. In this event, BCBSD shall submit, within 30 days of the date of this Order, a plan for the orderly termination of the affiliation and replacement of services presently provided to BCBSD by CareFirst.

For such time as BCBSD and CareFirst remain structurally affiliated, and prior to any subsequent Order issued in connection with any approval of a future contractual relationship between BCBSD and CareFirst, I retain jurisdiction over this matter and the parties to this Docket, and all of the conditions set forth in Exhibit B to the Affiliation Order and of the Standstill Order shall remain in effect until expressly rescinded.

SO ORDERED this 30th day of June, 2004.

Donna Lee H. Williams

DONNA LEE H. WILLIAMS
Insurance Commissioner

BEFORE THE INSURANCE COMMISSIONER
OF THE STATE OF DELAWARE

In the matter of	:	
Proposed Affiliation of	:	
BCBSD, Inc. Doing Business as	:	Docket No. 99-09
Blue Cross and Blue Shield of	:	
Delaware, With CareFirst, Inc.	:	

DECISION AND AMENDED ORDER

In this proceeding, I am asked by Blue Cross and Blue Shield of Delaware, Inc. ("BCBSD") to review and approve a change in the affiliation status between BCBSD and CareFirst, Inc. ("CareFirst") (collectively the "Parties"). The Parties have either refused to provide the documents needed to analyze and evaluate the proposed change, or have insisted upon doing so under conditions of secrecy that are contrary to the law of this State. Therefore, I am denying the Parties' application.

PROCEDURAL BACKGROUND

The Parties' affiliation status and their ongoing relationship have been at issue before the Delaware Insurance Department for over seven years. Within the last three years, BCBSD has sought the Department's permission to change its structural affiliation with CareFirst to a contractual affiliation, withdrawn that request and sought to terminate its affiliation with CareFirst altogether, withdrawn that request and submitted a second request to change its structural affiliation to a contractual affiliation, withdrawn and then resubmitted its second request for a contractual affiliation, and most recently sent a letter to the Department indicating that it intends to seek yet another type of affiliation, perhaps with a different company altogether, in the near future.

BCBSD Seeks A Structural Affiliation with CareFirst

On December 23, 1998, BCBSD and CareFirst executed an affiliation agreement whereby BCBSD would continue to provide health insurance and related services in Delaware as part of the CareFirst organization. In return, CareFirst would become the sole member of BCBSD and BCBSD would give up its Blue Cross® and Blue Shield® primary license (the "Marks") and operate under an affiliate license through CareFirst. The affiliation agreement was reviewed and approved by the Delaware Insurance Department (the "Department") in the above-captioned docket pursuant to a March 20, 2000 Final Order and Decision ("Original Order"). The Original Order was subject to certain conditions, which remain in effect to this day.

At the original hearing on the affiliation status of the Parties, BCBSD asserted that such a structural affiliation was essential if BCBSD was to remain competitive in the Delaware marketplace, and that BCBSD was engaged in a "life and death search for a strategic

partner." (January 4, 2000 PROPOSED FINDINGS, RECOMMENDATIONS AND ORDER at Page 10)(hereinafter "January 4, 2000 PROPOSED FINDINGS"). Furthermore, it was BCBSD's opinion that the structural affiliation of the Parties would allow BCBSD access to capital for investments in technology and overall would allow BCBSD to achieve "significant economies of scale and lower its administrative costs." (January 4, 2000 PROPOSED FINDINGS at Page 16). The Parties' original application to affiliate was not entirely unopposed, and numerous concerned members of the public submitted letters to the Department that focused primarily on the quality of services or products that BCBSD provided. (January 4, 2000 PROPOSED FINDINGS at Page 33). Due in part to the Hearing Officer's concerns regarding the separate corporate and operating status of BCBSD and to maximize responsiveness to local concerns, several conditions for approval were recommended by the Hearing Officer, whose recommendations were substantially approved by Insurance Commissioner Donna Lee Williams. (January 4, 2000 PROPOSED FINDINGS at Page 37, et. seq.).

BCBSD Seeks to Change Its Relationship With CareFirst from Structural to Contractual

In 2003, events occurred which caused BCBSD to seek an alteration of its relationship with CareFirst from a structural affiliation to a contractual relationship.

As a result of the unanimous passage of legislation in 2003 by the Maryland General Assembly, which the Department believed adversely impacted BCBSD and its Delaware subscribers, Commissioner Williams issued a Standstill Order on April 10, 2003. The Standstill Order was quickly followed by a Rule to Show Cause why (1) the effect of the Maryland Legislation would not contravene the Original Order, (2) the Original Order should not be terminated, (3) BCBSD's participation in the affiliation should not be withdrawn, (4) any assets, licenses, authorities, or the like yielded by BCBSD to CareFirst should not be returned, and (5) any other and necessary Order should not be entered protecting the rights of Delaware citizens to the full benefits offered prior to the Original Order (the "Rule to Show Cause"). In accordance with the Delaware Administrative Procedures Act and the Insurance Code, a hearing on the Rule to Show Cause was held before Commissioner Williams presiding as the Hearing Officer on November 4, 2003.

At the November 4, 2003 hearing, the Parties jointly proposed a modified affiliation agreement between the Parties on the terms and conditions set forth in an Administrative Services and Business Affiliation Agreement ("2003 ASBAA"). The hearing record reflects that the Parties desired to preserve the benefits of their prior Affiliation by replacing the structural corporate relationship with one that was based on a contractual agreement.

In Commissioner Williams' Order of December 1, 2003, she approved the 2003 ASBAA and the associated transactions on the condition that the closing of the 2003 ASBAA be consummated by December 31, 2003. Although BCBSD and CareFirst agreed that the 2003 ASBAA would not become effective unless approved by the relevant insurance regulatory authorities (i.e., Maryland and the District of Columbia), Commissioner Williams' Order was not subject to approval by other authorities.

On December 30, 2003, BCBSD notified Commissioner Williams that the Parties would be unable to meet the deadline set by the Order of December 1, 2003. As a result, the Rule to Show Cause was reinstated, a new hearing date was set, and the Parties were ordered to submit memoranda on two issues: (1) whether the Affiliation Order had been violated by the effect of provisions of the Maryland Legislation, and (2) if the Affiliation Order had been violated, the appropriate remedy for any violations. Following the submission of legal memoranda, a hearing was convened on March 9, 2004 to hear evidence on those two issues.

BSBSC Seeks to Terminate Its Affiliation with CareFirst

By the time of the March 9, 2004 hearing—less than five months after BCBSD and CareFirst had presented their affiliation agreement to the Department—BCBSD had decided that it no longer wished to be affiliated with CareFirst. BCBSD Chairman of the Board, Max Bell, testified at the hearing that "the Maryland General Assembly has taken away the company we have become affiliated with and has replaced it with a very different entity." (June 30, 2004 Decision and Amended Order at Page 4, citing March 9, 2004 Hearing Transcript at Page 87). In addition, Mr. Bell testified that BCBSD saw little prospect that CareFirst would be managed the way it was prior to the enactment of the Maryland Legislation. (March 9, 2004 Hearing Transcript at Pages 87-93). Finally, it was Mr. Bell's testimony that "[i]f conditions at CareFirst deteriorate, it may be too late to disentangle the management and governance interlocks that bind the companies together before irreparable damage to the reputation and finances of [BCBSD] result." (March 9, 2004 Hearing Transcript at Pages 92-94).

The Parties were also asked to present evidence regarding the fiscal impact upon BCBSD of a total disaffiliation of BCBSD and CareFirst. Timothy Constantine, BCBSD's President, testified that even under the most conservative projections, BCBSD was confident that "either limited or total disengagement from CareFirst can be achieved without disruption to or negative impact on our subscribers." (June 30, 2004 Order at Page 15, *citing*, March 9, 2004 Hearing Transcript at Page 136). Whereas in the original hearing, BCBSD offered testimony that a structural affiliation would allow it to be sustainable in a competitive marketplace and would achieve "significant economies of scale and lower its administrative costs" (January 4, 2000 PROPOSED FINDINGS at Page 16), BCBSD presented evidence in 2004 that BCBSD continued to handle many areas of operation after the affiliation with CareFirst. (June 30, 2004 Order at Page 9 *citing*, March 9, 2004 Hearing Transcript at Pages 136-137). As a result, BCBSD was confident that it could cost effectively resume pre-affiliation functions on behalf of an autonomous BCBSD. (June 30, 2004 Order at Page 9 *citing*, March 9, 2004 Hearing Transcript at Pages 136-139).

On June 30, 2004, Commissioner Williams issued a Decision and Amended Order withdrawing her approval of the Affiliation between BCBSD and CareFirst. In the order, Commissioner Williams concluded that a dramatic change in circumstances had occurred and that a structural affiliation between the Parties was no longer in the best interests of BCBSD or its Delaware subscribers. Among other things, the June 30, 2004 Order prohibited BCBSD's further participation in the surviving aspects of the original 1998 Business Affiliation Agreement and required CareFirst to take such steps as necessary to surrender its rights to use the Marks as "Primary Licensee" in Delaware, including cooperating with BCBSD, as necessary, to facilitate

BCBSD's attainment of "Primary Licensee" status in Delaware. (June 30, 2004 Order at Page 20).

The June 30, 2004 Order also expressly retained jurisdiction over the Parties for such time as the Parties remained structurally affiliated and required the Parties to submit to the Department for approval all contracts and agreements that the Parties jointly proposed to implement in order to continue any affiliation of the Parties on a non-structural basis. The June 30, 2004 Order was appealed by CareFirst to the Delaware Superior Court, which affirmed the June 30, 2004 Order on October 5, 2004. The Delaware Supreme Court affirmed the Superior Court decision on December 17, 2004. Before both the Superior Court and the Supreme Court, BCBSD supported the Department's disaffiliation Order.

BCBSD Withdraws Its Disaffiliation Request and Renews Its Contractual Affiliation Request

On November 18, 2005, less than a year after the Delaware Supreme Court upheld the Department's Order of disaffiliation, BCBSD formally asked the Department to reopen Docket No. 99-09 in order to obtain the "review and approval of changes in the affiliation status of BCBSD and CareFirst, Inc." BCBSD now wished once again to be affiliated with CareFirst, through the implementation of a new and somewhat different Administrative Services and Business Affiliation Agreement, dated October 21, 2005. ("2005 ASBAA"). (Letter from David S. Swayze, Esq. to the Honorable Matthew Denn, dated November 18, 2005 at Page 1).

The Parties were made aware of my decision to grant the request for review of the 2005 ASBAA via an April 6, 2006 letter from the Department's Special Counsel ("Special Counsel"). The letter informed the Parties that, due to changes in circumstances since the June 30, 2004 Order, including, but not limited to, a significant in-state transaction by BCBSD that has had the apparent effect of reducing its RBC ratio, the completion of an internal analysis by BCBSD of its capital needs, explicit statements by both BCBSD and CareFirst regarding their corporate missions, disclosures concerning certain areas of operating expense, and almost two years of experience of BCBSD working with CareFirst under the new Maryland statutory structure, the application for approval of their affiliation status would include a factual inquiry and expert analysis prior to a public hearing on the Parties' application.

As a result, on May 5, 2006 I issued a Pre-Hearing Order for a hearing on the application for approval of the 2005 ASBAA. At the request of the Parties, the timing of the procedural schedule contained in the May 5, 2006 Pre-Hearing order was expedited. As part of the required factual inquiry, and pursuant to 18 Del. C. §326, separate *Subpoenas Duces Tecum* were served on BCBSD and CareFirst for the production of certain documents relating to the Department's inquiry as to whether the change in the affiliation status of the Parties was in the best interests of BCBSD policyholders or the Delaware insurance-buying public.

The Parties' response to the May 5, 2006 Pre-Hearing Order and subpoenas was to withdraw their request for review and approval of the 2005 ASBAA. The Parties renewed their request for approval of the change in the affiliation status of the Parties on June 19, 2006. On June 26, 2006 I issued a Pre-Hearing Order and concurrently issued separate subpoenas,

which were nearly identical to the May 5, 2006 subpoenas, for the production of certain documents relevant to the Department's inquiry as to whether the change in the affiliation status of the Parties was in the best interests of BCBSD policyholders or the Delaware insurance-buying public. The June 26, 2006 Subpoenas (hereinafter, the "Subpoenas") and Pre-Hearing order gave the parties until July 31, 2006 to comply, and otherwise extended the timeframe by which the Parties' application would be considered.

In addition, the June 26, 2006 Pre-Hearing Order outlined a procedure for the Department to evaluate claims by the Parties that documents were confidential and should not be made available to the public. That procedure was designed to ensure that the Department complied with its responsibility under the Freedom of Information Act for classifying any document as confidential. Mell v. New Castle County, 835 A.2d 141, 145 (Del. Super. 2003).

On July 10, 2006, the Parties requested that the Department refrain from inquiring into certain factual issues in connection with the application. In a letter dated July 13, 2006 from Special Counsel, the Department made clear that it would not limit the scope of the inquiry but that if the Parties had specific concerns about particular document requests contained in the subpoena that the Parties should provide the Department with a specific description of the concern, the basis for the concern, and a reasonable proposal to alleviate the concern. In addition, the Parties were directed that, if they felt a particular request was burdensome, the Parties should provide the Department with some quantification of the burden – such as the estimate of the number of documents falling within the request – and a reasonable proposal for narrowing the request.

On July 31, 2006, the date documents were to be produced pursuant to the Subpoenas, the Parties filed responses to the Subpoenas by making sweeping and often obtuse objections and indicating that the Department would not be permitted to inquire into any factual issues that the Parties deemed inappropriate – including examining any documents or information predating the June 30, 2004 Order.

In their July 31, 2006 response to the Subpoenas, the Parties also refused to submit any documents that they deemed confidential until the Department allowed the Parties to label documents as being presumptively confidential rather than having to justify the basis for keeping those documents secret. In total, the Parties withheld at least 7,650 pages of responsive documents dated after June 30, 2004 that they deemed to be confidential, but refused to follow the confidentiality procedure in my Pre-Hearing Order for any of those documents.

Finally, the Parties objected to providing a list and description of documents that they were withholding under claims of attorney-client (or other) privilege. The Parties asserted that the requirement to prepare a privileged documents log was overbroad and unduly burdensome. The Parties failed to cite a single legal authority for their assertion.

In one final effort to persuade the Parties to comply with their legal obligations, Special Counsel sent the Parties a letter on August 3, 2006, requesting that they produce all documents responsive to the Subpoenas, including all confidential documents pursuant to the procedures outlined in the June 26, 2006 Pre-Hearing Order, by the end of business on August

10, 2006. Again, instead of complying with the subpoenas and producing the documents requested, the Parties responded on August 10, 2006 with letters reiterating their broad objections and concerns and requesting a meeting with the Department to discuss those concerns.

DECISION AND ORDER

As Insurance Commissioner, I have a responsibility to protect the interests of BCBSD policyholders and the insurance buying public at large, and to uphold the laws of this State. The Parties' refusal to provide the documents necessary for me to exercise those responsibilities, their refusal to articulate the reasons for their withholding documents in any fashion capable of legal review, and their insistence that I violate the Freedom of Information Act as a condition to viewing necessary documents, requires that I deny the pending application.

Throughout all of the Department's proceedings involving BCBSD and CareFirst, the Department has applied the standard enumerated at 18 Del. C. §5003 to analyze the propriety of any proposed transaction. That analytical standard was upheld by the Delaware Superior Court in its review of the Department's June 30, 2004 Order. In the Matter of: Proposed Affiliation of BCBSD, Inc., d/b/a Blue Cross Blue Shield of Delaware, with CareFirst, Inc., 2004 WL 2419161 at * 8 (Del. Super. Oct. 5, 2004). The Section 5003 standard explicitly requires that the Department assess: (a) Whether the Parties would be able to satisfy the requirements for the issuance of a license to write the line or lines of insurance for which it is presently licensed; (b) Whether the effect of the merger would substantially lessen competition in insurance in this State or tend to create a monopoly therein; (c) Whether the financial condition of any acquiring party might jeopardize the financial stability of the insurer, or prejudice the interest of its policyholders; (d) Whether the plans or proposals which the acquiring party has to make any other material change in its business or corporate structure or management, are unfair and unreasonable to policyholders of the insurer and not in the public interest; (e) Whether the competence, experience and integrity of those persons who would control the operation of the insurer are such that it would be in the interest of policyholders of the insurer and of the public to permit the merger or other acquisition of control; and (f) Whether the acquisition is likely to be hazardous or prejudicial to the insurance buying public. 18 Del. C. §5003(d)(1).

In an application before the Department, the burden of proof always rests with the applicant. *See* 29 Del. C. §10125(c) and 18 Del. C. §323(f) ("To the extent that it does not conflict with the provisions of [18 Del. C. Ch. 3], the Administrative Procedures Act, Chapter 101 of Title 29, shall govern all aspects of the Department's administrative proceedings"); *See also*, Weinfeld v. Delaware Bd. of Med., 1999 WL 743803 (Del. Super. 1999). By virtue of presenting an application to the Department for the review and approval of the proposed change in their affiliation status, BCBSD and CareFirst bear the burden to prove that the proposed change in the affiliation status reflected in the 2005 ASBAA satisfies the §5003 criteria.

Instead of attempting to meet this burden, the parties have consistently refused to comply with the Subpoenas and Pre-Hearing Orders that I have issued. The parties' refusal, and their further refusal to even disclose sufficient information to permit the Department to assess whether any of their sweeping objections have legal merit, has rendered it impossible for the

Department to carry out its legal responsibility carefully to review and assess the proposed transaction.

The only objection that the Parties have clearly articulated is their claim that the Department is prohibited from inquiring into any facts predating the Department's last order involving the Parties as part of its inquiry into the current proposed transaction. That objection, besides being firmly contradicted by case law specifically applicable to this very matter, reflects a crabbed view of the Department's responsibilities in reviewing the pending application.[1] There are a myriad of issues before me: whether the effect of the 2005 ASBAA would substantially lessen competition in insurance in this State or tend to create a monopoly therein; whether the financial condition of CareFirst jeopardizes the financial stability of BCBSD, or prejudices the interest of its policyholders; whether the terms of the 2005 ASBAA are unfair and unreasonable to policyholders of BCBSD and not in the public interest; whether the competence, experience and integrity of those persons who would control BCBSD are such that it would be in the interest of policyholders of the insurer and of the public to approve the 2005 ASBAA; and whether the 2005 ASBAA is likely to be hazardous or prejudicial to the insurance buying public. Even if, as the Parties have repeatedly asserted, the changes to the 2005 ASBAA when compared to the 2003 ASBAA are relatively minor in substance, since the approval of that 2003 ASBAA, there has been i) the passage of almost three years in time, ii) a significant in-state transaction by BCBSD that has had the apparent effect of reducing its RBC ratio, iii) the completion of an analysis of BCBSD's capital needs, iv) explicit statements by both BCBSD and CareFirst regarding their corporate missions, and v) at least two wholesale revisions by BCBSD of the relationship it has sought with CareFirst. The occurrence of these events and changes in circumstances mandate that the Department undertake more than a rubber stamp review of the 2005 ASBAA.

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[1] Judge Slights concluded that a Delaware administrative agency has the inherent power, even without statutory authority, to reopen and reconsider a decision until it loses jurisdiction. Slights Opinion, In the Matter of: Proposed Affiliation of BCBSD, Inc., d/b/a Blue Cross Blue Shield of Delaware, with CareFirst, Inc., 2004 WL 2419161 at * 9 n.51 (citing Henry v. Dept. of Labor, 293 A.2d 578, 581 (Del. Super. 1972). More generally, the Delaware General Assembly has vested me with broad statutory powers. See 18 Del. C. § 310(b) ("The Commissioner shall have the powers and authority expressly vested by or reasonably implied from this title."); see also 18 Del. C. § 5008 ("The Commissioner may, upon notice and opportunity for all interested parties to be heard, issue such rules, regulations and orders as shall be necessary to carry out the provisions of this chapter."). It is well settled that this broad statutory power carries with it the authority to do all that is reasonably necessary to execute that power. Dep't of Correction v. Worsham, 638 A.2d 1104, 1107 (Del. 1994); Atlantis I Condo. Ass'n v. Bryson, 403 A.2d 711, 713 (Del. 1979). Even without express statutory authority, the Delaware Insurance Commissioner has the inherent power to reopen and reconsider a decision until the Department loses jurisdiction. Henry v. Dept. of Labor, 293 A.2d 578, 581 (Del. Super. 1972).

Furthermore, with no disrespect to the regulatory authority of my predecessor, I am entitled to my own individual assessment of whether the terms and conditions of the proposed contractual affiliation meets the Section 5003 standard, and as noted above, it is the Parties' burden to meet that standard. While the Department's substantive review of the 2005 ASBAA would certainly have focused on more recent facts and circumstances, it is not for the Parties to place an arbitrary and unilateral limit on the scope of the Department's review.

The need for careful review is magnified by the inconsistent positions that the Parties, particularly BCBSD, have taken before the Department in previous proceedings. In 1999, it was BCBSD's position that structural affiliation was in the best interests of BCBSD policyholders because it was critical to BCBSD's very existence. By 2004, BCBSD's position was that the new CareFirst Board would likely take CareFirst in a different direction that might put BCBSD and its subscribers at risk. Two years later, BCBSD sought once again to be formally affiliated with CareFirst—on an expedited basis, no less. BCBSD then withdrew that application, only to renew it some three weeks later. Adding to the confusion, BCBSD recently indicated that it wanted a contractual affiliation with CareFirst only on a temporary basis because it plans to return to the current structural affiliation, or some other affiliation with a larger insurer, in the foreseeable future. (*See,* July 10, 2006 Letter from David S. Swayze, Esq. to Special Counsel). BCBSD's constantly changing perception of CareFirst's overall financial and structural viability is disconcerting and at a minimum merits a thorough review by the Department.

In short, it is my view that the pending application warrants a thorough review of the entire relationship between the Parties. The interests of BCBSD policyholders and the insurance buying public at large, which I am tasked by law to protect, make it not only appropriate but necessary for the Department to conduct a thorough and complete examination.

Finally, that analysis must occur in a manner consistent with this state's open government laws. BCBSD has objected to the conditions I established in my June 26, 2006 Pre-Hearing Order, placing the burden of establishing the need for a document's confidentiality on the party requesting confidential treatment. BCBSD stated that it does not believe there "is any precedent for the burdensome gauntlet the Commissioner would interpose in this proceeding for determining confidentiality or privilege." (August 10, 2006 letter David S. Swayze, Esq. to Special Counsel at Page 3).

While the procedure for determining confidentiality outlined in the June 26, 2006 Pre-Hearing Order was admittedly thorough, there is precedent in other administrative contexts. 7 Del. Code. Regs. §102 at 6.0. More importantly, the standard I set attempts to balance the obligations this Department has to the public and the public interest as a whole with the obligations to insurers being investigated by the Department to keep certain documents confidential. While it may represent a departure from past practice, since my tenure as Commissioner began, this Department has placed an appropriate emphasis on the public's right to examine, comment upon and inspect non-confidential information in the possession of the Department. A unilateral determination by a party in a proceeding before the Department that its

documents are confidential is an insufficient basis upon which to withhold that document from public scrutiny.

My decision in this matter is not, and in fact cannot be, based on the underlying merits of the Parties' application. The Parties have made it impossible for me to render such a decision in a responsible way. The Parties may resubmit the application at a later time if they determine that they are willing to comply with the law. In the interim, the Department will not be bullied into making a decision that has implications for the health care of tens of thousands of Delawareans without adequate information to make that decision in a responsible manner.

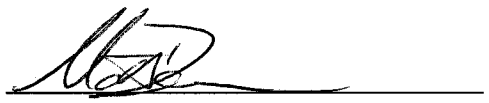
Accordingly, and based on all the foregoing, IT IS HEREBY ORDERED THAT:

1. Because the Parties have refused to provide the documents the Department believes are necessary to evaluate whether the proposed change in the affiliation status of the Parties is in the best interests of the BCBSD policyholders and its Delaware subscribers, the Parties have failed to meet their burden of proof on their application. As a result, the Parties' Application to have the Department review and approve the proposed changes in the affiliation status of BCBSD and CareFirst, Inc. is denied.

2. Effective 60 days from the date of this Order or, should a timely Superior Court appeal be filed, immediately following disposition of that appeal by the Superior Court, any stay of the June 30, 2004 Order is rescinded.

3. For such time as the Parties remain structurally affiliated and until any subsequent Order issued in connection with any approval of a future contractual relationship between the Parties, I retain jurisdiction over this matter and the Parties, and all of the conditions set forth in the June 30, 2004 Order, Exhibit B to the original Affiliation Order and of the Standstill Order shall remain in effect until expressly rescinded.

SO ORDERED this 23rd day of August, 2006



MATTHEW DENN
Insurance Commissioner

533791

BCBSD, INC.
BOARD OF DIRECTORS MEETING
DECEMBER 1, 2006

A special meeting of the BCBSD, Inc. Board of Directors was held pursuant to notice on December 1, 2006, at 12:30 p.m. in the corporate offices. The following members, who constituted a quorum, were present:

Max S. Bell, Jr., Chairman
Ben Corballis, M.D., Vice Chairman
Thomas E. Archie
Bernard J. Daney
Garrett B. Lyons, D.D.S.
Frances M. West

Also in attendance were the following members of staff: Timothy J. Constantine, President & Acting CEO; William E. Kirk, III, Vice President, General Counsel & Corporate Secretary; and Ellen M. Johnson, Executive Assistant to the President & Acting CEO. External Counsel included Grover C. Brown, Esq., of Gordon, Fournaris & Mammarella (counsel to the BCBSD Board); David S. Swayze, Esq. and Michael W. Teichman, Esq. of Parkowski, Guerke & Swayze, P.A. (counsel to BCBSD, Inc.).

I. Letter from the Chairman of the Board of CareFirst, Inc. (CFI)

The Board discussed a letter from Michael R. Merson, Chairman of CareFirst, Inc., dated November 21, 2006. Mr. Merson's letter stated that the return of BCBSD, Inc. to CFI on a structural basis remains a top priority of the CFI Board and management. He proposed to the Board four principles to govern BCBSD's potential re-entry. After discussion, and based upon advice from the Board's consultant and legal counsel, the Board unanimously agreed that the following actions be taken:

- Immediately following today's meeting, Counsel will draft a response to Mr. Merson from Mr. Bell requesting clarification of the principles outlined in Mr. Merson's letter along with additional points as discussed by the Board. The letter would also request a future meeting, at CFI's convenience, among representatives of BCBSD and CFI to further consider BCBSD's potential re-entry process. The Board then discussed who would represent BCBSD once a meeting is scheduled between BCBSD and CFI.

- No members of the BCBSD Board would attend the CFI Board Annual Meeting and Planning Conference scheduled for December 3 and 4, 2006. The Board's opinion is that attendance at this time would not be productive. Mr. Constantine will notify CFI management of the Board's decision immediately following today's meeting.

II. Strategic Planning

Mr. Bell reported that BCBSD has been approached recently by various Blue Cross Blue Shield plans expressing interest in a potential strategic partnership with this company in the future. Mr. Constantine discussed a document outlining various recommended steps for management in order to assist the Board in successfully navigating BCBSD through an affiliation search process. The document also identified potential external advisors that the company would need to engage throughout the process. In addition, the Board reviewed documents that provided historical reference to past affiliation arrangements considered by BCBSD and a list of suggestions from the Board's consultant for consideration by the Board prior to the company engaging in discussions with potential partners.

After discussion, the Board agreed to the following:

- Management would develop a recommendation regarding the engagement of external advisors and associated costs for review by the Board before its next meeting on December 13, 2006.

- A set of general principles and objectives desired from an affiliation would be developed to guide the Board and management throughout future negotiations.

III. Other

IV. Adjournment

There being no further business, the meeting adjourned at 2:00 p.m.

Respectfully submitted:

Ellen M. Johnson
Executive Assistant to the President & Acting CEO

BCBSD, INC.
BOARD OF DIRECTORS
FEBRUARY 7, 2007

A meeting of the Board of Directors of BCBSD, Inc. was held pursuant to notice on February 7, 2007, at the DuPont Country Club, Wilmington, Delaware. The meeting commenced at 9:00 a.m. and the following members of the Board, who constituted a quorum, were present:

Max S. Bell, Jr., Chairman
Ben Corballis, M.D., Vice Chairman
Thomas E. Archie
Bernard J. Daney
Garrett B. Lyons, D.D.S.
Robert F. Rider
Frances M. West

Also in attendance were the following members of staff: Timothy J. Constantine, President & Acting CEO; Christine L. Alrich, Vice President of Corporate Marketing; George H. English, Jr., Vice President of Operations; William E. Kirk, III, Vice President, Corporate Secretary & General Counsel; Ellen M. Johnson, Executive Assistant to the President & Acting CEO; and Diane M. Coates, Assistant to the Vice President of Corporate Marketing. Outside Legal Counsel: Grover C. Brown, Esq., of Gordon, Fournaris & Mammarella (representing the BCBSD Board); David S. Swayze, Esq., and Michael W. Teichman, Esq., of Parkowski, Guerke & Swayze, P.A. (representing BCBSD, Inc.); and David C. McBride, Esq. of Young, Conaway, Stargatt & Taylor (representing BCBSD, Inc.). Also attending: Robert C. Cole, Jr. (Consultant for BCBSD, Inc.); Louis Pavia, Jr., President of CareCompanion; Dr. Martin Silverstein, Senior Vice President & Global Leader of Health Care Practice; and Anne Wilkins, Vice President & Head of North American Payer Practice, The Boston Consulting Group; and Jody Voss, Vice President of Business Development, Blue Cross and Blue Shield Association.

Today's meeting was conducted in two parts:

PART ONE: STRATEGIC PLANNING

I. Long-Range Strategic Plan

In advance of today's meeting, the Board received a copy of the long-range strategic plan that was prepared by The Boston Consulting Group (BCG) for CareFirst, Inc. (CFI) and its subsidiaries. Since development of the plan was in process prior to the disaffiliation between CFI and BCBSD, there was reference to BCBSD throughout the report relative to long-range vision and strategic priorities.

The following are highlights of BCG's report presented at today's meeting:

- High-level summary of the health care finance and service environment and the challenges facing BCBSD and CFI in the marketplace.
- Major forces impacting health care today.
- Discussion regarding health care reform proposals that will figure prominently in many candidate platforms during the upcoming national and state elections.
- Discussion regarding the Blues position, especially in the national account business, as well as various challenges and opportunities to consider in the next 10 years to ensure a strong position in the marketplace.

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Representatives from BCG, Anne Wilkins and Martin Silverstein, described the major strategic priorities and core components that CFI and BCBSD, as non-national players, would need to focus on in order to remain competitive in the marketplace over the long term. There was also discussion of the current managed care environment and regulatory oversight in the health care insurance industry.

Dr. Silverstein and Ms. Wilkins departed the meeting at 10:15 a.m. with thanks from the Board for attending today's meeting.

II. Overview of Blue Cross Blue Shield System Affiliations

Ms. Voss, Vice President of Business Development for the Blue Cross and Blue Shield Association (BCBSA), was invited today to present an analysis of Blue Cross Blue Shield (BCBS) mergers and affiliations during the past decade. She noted that BCBS Plans lead the industry in enrollment, brand strength, service and have enjoyed solid financial performance. The Blues are also experiencing record enrollment nationwide, due in large part to the success of the Blue Card product. Ms. Voss presented an overview of the types of Plans that make up the nationwide Blues System. She also detailed the experiences of four BCBS Plans that have merged or affiliated during the last ten years.

Ms. Voss also gave an overview of the Association's Blue Health Care Bank. She noted an increase in the outsourcing of Blues Plan capabilities to other Blues Plans and the joint development of shared assets.

After discussion, Ms. Voss departed the meeting at 11:50 a.m. with the appreciation of the Board for attending today's meeting.

III. Potential Affiliation and Conversion Options

Messrs. Swayze and Teichman presented an overview of the types of affiliation and conversion options available for a potential partnership between BCBSD and another Blue Plan, as well as the regulatory and structural considerations of each option. They described the following scenarios for the Board to consider as part of its strategic planning activities:

- Three forms of organization that are potentially available – health service corporation, stock company, and mutual company.
- Conversions and affiliations options – affiliation with another non-profit, conversion to stock for-profit in connection with affiliation, conversion to standalone mutual, and conversion to mutual in connection with affiliation.
- Overview of not-for-profit conversion statute.

Mr. Swayze described a set of constants that would be part of any conversion or affiliation partnership from a governance, BCBSA, and regulatory standpoint. Mr. Teichman stated that any arrangement the Board decides to pursue would require a lengthy regulatory process.

PART TWO: BOARD OF DIRECTORS MEETING

I. Sale of BCBSD Corporate Headquarters Facility

II. President's Report

- **Interim Administrative Service Agreement with CareFirst** – Messrs. Swayze and Teichman gave an update on the administrative service fees that BCBSD currently pays to CFI following the disaffiliation. As part of the disaffiliation transition plan, an evaluation of the major services provided to BCBSD by CFI is underway. Management and counsel proposed to the Board that BCBSD and CFI enter into an interim service agreement, which will be in effect until either party provides a six-month notice of intent to terminate. BCBSD can also revise parts of the agreement whenever it deems appropriate.

  After discussion and upon motion made and seconded, the Board agreed with the recommendation of management and counsel to work with CFI management in developing and executing an interim service agreement between BCBSD and CFI.

III. CFI and Other Affiliation Options

- There was discussion regarding the process that the Board and management would undertake to accomplish a partnership with another entity that would prove the most beneficial to BCBSD and its stakeholders in the future. A logical process and uniform list of criteria would need to be developed for evaluating potential bidders. To accomplish these tasks, a list of BCBSD's major requirements and expectations for use in negotiating with potential bidders would need to be produced. In addition, the Board agreed that revised Mission and Vision statements that mirror BCBSD's current corporate status and long-range plans would be developed for the Board's approval at a meeting in the near future.

  In order to begin the process, the Board agreed with management's recommendation that Louis Pavia, Jr., President of CareCompanion, be engaged by BCBSD to work with management in developing the following:

  - Mission and Vision Statements
  - Criteria for analyzing potential partners

- The Board also discussed the desire of CareFirst, Inc. to resume a structural relationship with BCBSD in the future. Mr. Bell stated that at some point during the search process for a strategic partner, a meeting would be arranged between CFI and an appropriate representative of BCBSD to discuss CFI's proposal.

  Mr. Constantine reported on the following CFI activities:
  - Search committee activities are underway for the new Chief Executive Officer.
  - John Colmers (former Chairman of the Board of BCBS of Maryland) resigned from the CFI Board effective January 2007 to assume the position of Cabinet Secretary of the Maryland Department of Health & Mental Hygiene.
  - A hearing is being scheduled by the Maryland Insurance Commissioner regarding the severance package of the former Chief Executive Officer of CFI (Mr. Jews).

IV. Adjournment

Respectfully submitted:

Ellen M. Johnson
Executive Assistant to the President & Acting CEO

BCBSD Strategy Session II

Board of Directors
March 7, 2007

CareCompanion

EXHIBIT
JOINT-27

Agenda

- Market Trends and BCBSD Issues
- Mission and Vision
- Scenario Based Requirements
- Strategic Alternatives
- Next Steps

Trends and Issues Overarching

- Globalization
  - Worldwide workforces
  - Business partners with global reach (bankers, lawyers, accountants, insurers)
  - Competition for Accounts among Blues and between Blues and other National players
  - BCBSA supports international aspects
- Technology
  - Information expectations
  - Instant/customized solutions
  - Scale economies
- Consolidation
  - Finance and Insurance
  - Big getting bigger
  - Niche plays
- Declining Brand Loyalty

Trends and Issues
Health Insurance

- Clinical Performance Orientation
  - Wide gaps/variation in care, outcomes and quality
  - Rising consumer awareness of issues, gaps
  - Information/knowledge intensive
  - Decision driver
  - Individual plus clinician
  - Hard work
- Competition
  - Comprehensive (health, workers comp, disability, life, LTC, etc), scale economies
  - Specialty (Medicaid, Medicare Advantage, CDHP, Health Management, Consumer support) niche exploitation
- Health Benefits
  - Continued cost shifting to Employees
  - Erosion of employer support for retirees
  - CDHP concept still questionable

Trends and Issues
Health Insurance

- Providers
  - Outpatient national consolidation (Lab, Imaging, Surgery, Urgent Care)
  - Physician – Hospital reintegration and competition
  - Maldistribution of physicians
  - Little competitive advantage available in Delaware/limited negotiating power
  - Aging physician population portends future shortages, malpractice reform might help
- Segments
  - ASO vulnerable to cost pressure
  - Profitable insured niches vulnerable to cherry- picking
  - Small insurers vulnerable to adverse selection, predatory pricing

Trends and Issues
Health Insurance

- Government
  - Uncertainty at Federal level
  - Incremental changes in near term
  - Potential for more fundamental change
  - Delaware near term changes
    - Expanded SCHIP
    - High-Risk Pools
    - Rate Review tightened
    - Experience rating for small group tightened

Trends and Issues
BCBSD

- High share limits upside except individual and very large groups
- Non-risk business dependent on 2 large accounts, highly leveraged, cross subsidized
- Aetna displacing Coventry in State account could increase competition in small group segment from both
- BCBSD workforce aging, strained
- New skills, knowledge and systems required to handle change and growth
- External documentation and reporting requirements significant burden, investment
- Consolidation among Blues could jeopardize DE exclusive “franchise”

Mission and Vision

Draft Mission

Provide benefits solutions that enable our customers to access high quality, cost effective health services and offer the knowledge and guidance necessary to improve their health and well being.

Draft Vision

BCBSD will be the leading provider of health insurance and related services in the markets we serve.

We will be recognized for our exceptional customer satisfaction and value through:

- **Our innovative product designs;**
- **Effective wellness and health management programs;**
- **Operational efficiency;**
- **Local knowledge; and**
- **Demonstrated responsiveness**

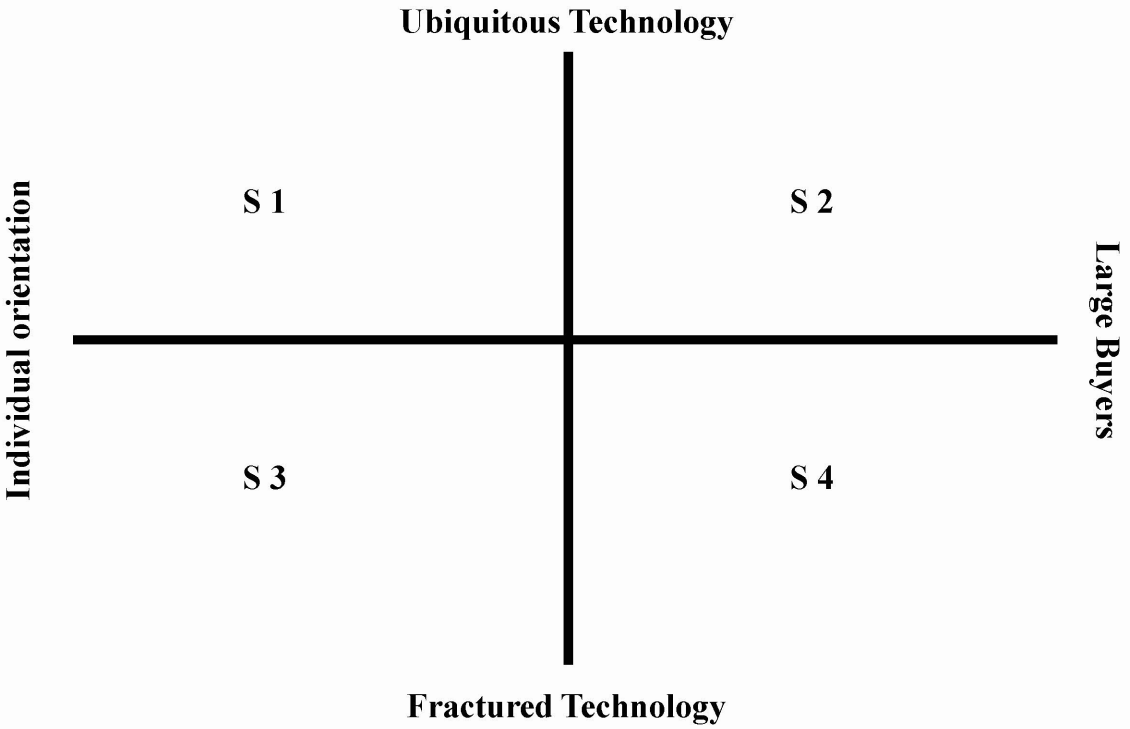
Operating with high integrity, we will be a trustworthy business partner, excellent steward of our resources, a preferred employer and a good corporate citizen.

Scenario Based Requirements

Scenario Planning

- **Strategic Question**
  - **Can we achieve our vision?**
- **Two independent variables with high degree of uncertainty and large potential impact**
  - **Government/consumer role**
    - **Large group/pool buyers, expanded M'care, M'caid, highly regulated, standard plans, ASO vs. High deductible, individualized, portable insured plans purchased through employers, aggregators or internet**
  - **Technology use**
    - **Ubiquitous EMRs, ERx, Clinical Decision Support, interoperability, electronic payment (claims, reimbursement, deductibles, co pays) on line tracking and reporting, performance ratings vs. use by few large providers and other organization, few accepted standards, multiple platforms and approaches, sketchy information**

Scenarios


Ubiquitous Technology
Individual orientation
S 1
S 2
Large Buyers
S 3
S 4
Fractured Technology

Requirements for Success

- Capital
  - Invest in people and systems
  - War chest for competitive battle
- Provider Network Advantage
  - Price
  - Relationship
  - Selection and management
- Exceptional Medical Management
- High Consumer Satisfaction, Renewed Commitment
- Infrastructure/Systems for Efficient Operations
- Motivated and skilled workforce
- Ability/Capability to Use Information for Competitive Advantage
- Strong Brand
- Integral part of local community, knowledgeable, responsive
- Agile and Aggressive, Sense of Urgency
- Value added, niche products/alternative revenue streams

Strategic Alternatives

Alternative Strategies

- The Health Partner
- The Maestro
- The Wizard of Delaware
- The Collaborator

The Health Partner

Concept

Focus on insured products (i.e. small group, individual, HMO) and provide intensive health, disease and case management. Partner for large group/ASO business and support with personal health management services

Rationale

Brand, local presence and responsiveness most valuable to smaller, local companies. Health management has greatest payoff in insured products. Cost sensitive ASO/large group market requires infrastructure, economies of scale not available to BCBSD or appropriate for small group.

Health Partner

- **Business Relationship Options for Large Group**
  - Joint Venture (Blue or Non-Blue)
  - "Royalty" agreement (Blue)
  - Outsourcing Agreement (Blue, Non-Blue, Non-Insurer)
  - Management Services Contract (Blue, Non-Blue, Non-Insurer)

The Maestro

Concept

Orchestrate best of breed partners for each major segment (i.e. small group/individual, large group, Medicare, Medicaid), leverage brand, network and marketing to establish unassailable position

Rationale

No single player can meet unique needs of all segments, multiple partners protects role of BCBSD, adds value and leverages brand and market position.

The Maestro

- **Business Relationship Options for Each Segment**
  - **Joint Venture (Blue or Non-Blue)**
  - **“Royalty” agreement (Blue)**

The Wizard of Delaware

Concept

Acquire economies of scale necessary to compete by outsourcing administration to vendor, invest in health and medical management, use brand and local position to differentiate

Rationale

Customers will pay small premium for local partner with strong health and medical management orientation, leapfrog legacy systems for ISP technology, maintain control of core business and secure sufficient share to remain viable

The Wizard of Delaware

- **Business Relationship Options**
  - **Outsourcing Agreement (Blue, Non-Blue, Non-Insurer)**
  - **Management Services Contract (Blue, Non-Blue, Non-Insurer)**
  - **Joint Venture (Blue, Non-Blue, Non-Insurer)**

The Collaborator

Concept

Select a strong business partner and leverage their resources and capabilities with local market position to create solid market leadership. Market BCBSD and partner branded products to all segments, focus on local network and medical management and capitalize on their administrative capabilities.

Rationale

BCBSD requires access economies of scale and other branded products to maintain and expand share. A single partner limits complexity and maximizes value and potential.

The Collaborator

- **Business Relationship Options**
  - Merger (Blue)
  - Affiliation (Blue or Non-Blue)
  - Holding Company (Blue or Non-Blue)
  - Joint Venture (Blue or Non-Blue)

Next 30 Days

- Develop BCBSD Business Strategy
  - Market Analysis
  - Management strategy sessions
- Delineate Potential Partner Roles and Requirements
- Outline Request for Proposal
- Identify Potential Partners
- Define Solicitation Process