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BEFORE THE COMMISSIONER OF SECURITIES AND INSURANCE
OFFICE OF THE STATE AUDITOR
STATE OF MONTANA

IN THE MATTER OF THE CONVERSION OF BLUE CROSS AND BLUE SHIELD OF MONTANA, INC. AND THE ALLIANCE WITH HEALTH CARE SERVICE CORPORATION, Applicants.	Case No. INS-2012-238 **APPLICANTS' JOINT PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW (<u>PUBLIC VERSION</u>)**

Dated: April 19, 2013

TABLE OF CONTENTS

Applicants Blue Cross and Blue Shield of Montana, Inc. and Health Care Service Corporation, a Mutual Legal Reserve Company, respectfully submit the following Proposed Findings of Fact and Conclusions of Law in support of a recommendation of approval of their November 15, 2012 Application for Approval of Alliance ("Application") pursuant to Montana Code Annotated §§ 35-2-609, 35-2-617 and Title 50, Chapter 4, part 7 ("Conversion Statute").

PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above-entitled matter came on regularly for public hearing on February 12, 2013 and March 12-14, 2013, before the Honorable W. William Leaphart, Hearing Examiner. Jacqueline T. Lenmark appeared for Blue Cross and Blue Shield of Montana, Inc. ("BCBSMT") and Health Care Service Corporation ("HCSC") (jointly the "Applicants"). Michael F. McMahon appeared for BCBSMT. Stanley T. Kaleczyc and Helen E. Witt appeared for HCSC. Jesse Laslovich, Nick Mazanec, and Jay Angoff appeared for the Office of the Commissioner of Securities & Insurance, Montana State Auditor ("Commissioner"). Kelley Hubbard and Michael Black appeared for the Montana Attorney General, Department of Justice ("Attorney General"). Witnesses were called and testified and evidence was introduced. The matter was submitted to the Hearing Examiner for decision.

The Hearing Examiner now makes his Findings of Fact as follows:

FINDINGS OF FACT

I. CONVERSION APPROVAL

1. Applicants jointly filed their Application with the Commissioner on November 15, 2012, seeking approval of the proposed Conversion Transaction pursuant to the Conversion Statute. Applicants served a copy of the Application on the Attorney General.

2. On December 3, 2012, the Commissioner issued a Notice of Application for Conversion and Public Hearing in accordance with the procedures under Montana Code

Annotated § 50-4-711. The Notice scheduled the public hearing for February 12, 2013. The notice informed the public of the process by which the hearing would be conducted and how public comment could be made and considered.

3. On December 6, 2012, the Commissioner published on the internet and by press release an "ADVISORY: Public Hearing on Blue Cross Blue Shield Acquisition Scheduled," and filed a Notice of Publication of Application for Conversion and Hearing by Press Release.

4. On February 12, 2013, a public hearing was conducted to take public comment.

5. On February 13, 2013, pursuant to the agreement of the parties, the Hearing Examiner ordered an additional public hearing to begin on March 12, 2013, to take further public comment and evidence in accordance with the provisions of Montana Code Annotated § 50-4-711.

6. On February 13, 2013, the Commissioner published on the internet and by press release an "ADVISORY: Second Public Hearing on Blue Cross Blue Shield Acquisition," and on February 15, 2013, filed a Notice of Publication of Additional Hearing by Press Release.

7. The Application, all of the foregoing Notices, and all of the pleadings in this matter have been posted on the Commissioner's public website.

II. BCBSMT

A. Corporate Structure

8. BCBSMT is a non-investor owned ("NIO"), nonprofit health service corporation. It provides comprehensive health insurance and third-party administrative services throughout the State of Montana. BCBSMT has operated in Montana for more than seventy years. It is organized as a nonprofit mutual benefit corporation and licensed as a health service corporation under Montana law. (Direct Testimony of Michael E. Frank, President and Chief Executive Officer, BCBSMT, dated March 5, 2013 ("Frank Direct") at 4:5-12, 5:3-7.)

9. BCBSMT is an independent licensee of the Blue Cross and Blue Shield Association ("BCBSA"). BCBSA is a national association of 38 independent, community-based and locally operated Blue Cross and Blue Shield ("Blue") companies. BCBSA owns and manages the Blue Cross and Blue Shield trade names and marks and has granted BCBSMT an exclusive license to use them in the State of Montana. The BCBSA license agreement prohibits the sale or transfer of the license to another insurer without the approval of BCBSA. (Frank Direct at 5:34, 6:5-11, 7:1-11.)

10. As an independent and locally operated BCBSA licensee, BCBSMT offers its Blue branded products and services to residents of the State of Montana and to employers headquartered here. This limits BCBSMT's market potential to approximately 500,000 members. The population of Montana is aging, and the potential market decreases as more people become eligible for Medicare. (Direct Testimony of Mark A. Burzynski, Senior Vice President and Chief Financial Officer, BCBSMT, dated March 5, 2013 ("Burzynski Direct") 15:16-22.)

11. As of December 31, 2012, BCBSMT had approximately 271,150 members. It has contracts with all sixty hospitals in Montana. There are also approximately 2,200 physicians and 3,480 allied healthcare providers in the BCBSMT provider network. (Frank Direct at 4:13-18.)

12. BCBSMT has a number of direct and indirect subsidiaries. Combined Benefits Management, Inc. ("CBMI") is a wholly-owned subsidiary holding company. CBMI has three wholly-owned subsidiaries: (1) Insurance Coordinators, Inc. ("ICMI"); (2) Health-e-Web, Inc. ("HeW"); and (3) Western States Insurance Agency ("WSIA"). ICMI owns a 49 percent interest in Peak1. WSIA is in the process of winding down. CBMI also owns small interests in WPMI,

LLC and TriWest. BCBSMT also owns a small interest in Prime Therapeutics and Regional Advantage Services, LLC. (Frank Direct at 5:14-6:1.)

13. BCBSMT has two charitable foundations: the BCBS Foundation for Healthy Montanans and the Caring Foundation of Montana, Inc. Each of these Foundations is a Section 501(c)(3) organization and a licensed affiliate of BCBSA. (Frank Direct at 6:1-4.)

B. Financial Condition and Challenges

14. BCBSMT has faced financial challenges for the past decade. In eleven of the last fifteen years, BCBSMT experienced underwriting losses. Underwriting gains or losses measure an insurer's ability to generate a profit based on its core business of underwriting insurance policies. BCBSMT's aggregate underwriting losses over the last fifteen years totaled approximately $63 million. BCBSMT has not had an underwriting gain since 2007; its underwriting losses since 2008 have ranged from -$0.8 million to -$17.6 million.[1] (Burzynski Direct at 10:11-12, 23:20-24:4; Direct Testimony of Maurice S. Smith, Divisional Senior Vice President Business Development and Subsidiary Management, HCSC, dated February 8, 2013 ("Smith Direct") at 9:9-12, 8:17-9:3.)

15. Although BCBSMT has generated a net profit in all years since 2007 except 2009, that net profit resulted from investment income and income from subsidiaries that was enough to cover the underwriting losses. In 2009, BCBSMT had an overall net loss. (Hearing Transcript, Vol. I, March 12, 2013 ("Burzynski Testimony") at 204:4-205:9.)

16. BCBSMT made significant efforts beginning in 2007 to reduce its administrative expenses to try to improve its underwriting results. In absolute dollars, administrative expenses

[1] The Application was filed on November 15, 2012, before BCBSMT's 2012 Annual Statement was filed with the Commissioner. BCBSMT reported a statutory underwriting loss of approximately $10.05 million for 2012. (CSI Ex. A at 28.)

were reduced by 3 percent in 2008, increased by approximately 1 percent in 2009, decreased by 5 percent in 2010, and decreased by 2 percent in 2011. BCBSMT engaged a process improvement consulting firm for assistance with these efforts in 2011 and 2012. These reductions did not result in a reversal of BCBSMT's underwriting losses, and BCBSMT's statutory and non-statutory administrative costs remain high compared to many other insurers. (Burzynski Direct at 5:1-4, 20:11-21:1.)

17. BCBSMT is unlikely to be able to further reduce its administrative costs and improve its underwriting performance on its own because of its small size and lack of economies of scale. Insufficient scale and limited access to capital makes it difficult for BCBSMT to innovate and expand its capabilities and service. (Burzynski Direct at 5:4-9, 20:9-21:1.)

18. Economies of scale are important in the health insurance market. Smaller competitors have a difficult time managing infrastructure costs effectively. Costs for expenses like financial accounting, enrollment and claims systems do not vary significantly in the cost of implementation and operations proportional to the number of customers served. This is often also the case with the costs of compliance with regulatory requirements, analysis of medical trends, actuarial services, information technology personnel and medical experts as well. These costs remain basically the same whether the membership base is 10,000 or 100,000. This means that the per member cost of all these services is always higher for a small insurer than it is for an insurer with more members over which to spread the costs. (Burzynski Direct at 18:19-21.)

19. Lack of scale results in a distinct competitive disadvantage for BCBSMT and other small health insurers, compared to larger health insurers. This disadvantage is illustrated by a comparison of BCBSMT's percentage of net premium revenues (excluding "Administrative Services Only" ("ASO") revenues) spent on total administrative costs net of ASO margins to that

of HCSC. BCBSMT's administrative costs on a per member basis were 3.5 to 4 percent higher than HCSC's. This difference is largely a result of BCBSMT's lack of scale. (Burzynski Direct at 19:1-13.)

20. As a result of these financial challenges, BCBSMT has not been able to make necessary capital expenditures and dedicate sufficient resources to improve operational efficiencies, more effectively compete in a changing market place and innovate. BCBSMT has identified an estimated $100 million in necessary capital requirements and incremental operating expenses in the next five years. It does not currently have the capital or reserves to make those investments. BCBSMT has very limited access to capital markets for these increasing needs. (Burzynski Direct at 5:10-7:15.)

21. If the proposed Transaction is not approved, BCBSMT will be required to out-source core functions and related jobs. [redacted] The economic impact to the State of Montana, and the Helena area in particular, would include the loss of salaries, benefits, taxes, and money spent in the local economy. (Burzynski Direct at 32:8-11, 31:21-32:2; [redacted]

III. HCSC

A. Structure and Financial Strength

22. HCSC is an Illinois mutual legal reserve company, doing business as a nonprofit health care service plan. HCSC was incorporated in 1936 as a nonprofit healthcare service plan. In 1982, it converted into a mutual insurance company. A mutual legal reserve company is a member-owned company that operates for the mutual benefit of its members. The Illinois Insurance Code does not include an option for an insurance company to form as a not-for-profit mutual legal reserve company; as a result, that corporate structure is not available to HCSC.

HCSC's Articles of Incorporation specify that it is a "non-profit health care service plan." Article IX of the HCSC By-laws provides that HCSC shall operate on a not-for-profit basis. The By-laws also prohibit any person from receiving any HCSC profits. Distribution of HCSC assets is only allowed upon liquidation or dissolution of the company. (Direct Testimony of Colleen F. Reitan, Executive Vice President and Chief Operating Officer of HCSC, dated March 5, 2013 ("Reitan Direct") at 3:22-4:7, 4:15-23; CSI Exs. N, O.)

23. HCSC has made a good faith commitment to maintain its nonprofit status for at least five years if the proposed Transaction is approved. HCSC has no current plans to become a for-profit company and doing so would run counter to its fundamental philosophy. (Applicants' Ex. 9 at ¶ 4; Hearing Transcript Vol. I, March 12, 2013 ("Smith Testimony") at 268:25-270:12; Hearing Transcript Vol. II, March 13, 2013 ("Reitan Testimony") at 333:4-16.)

24. HCSC is the largest NIO health insurer in the country, and the fourth largest overall. It currently has more than 13 million members in Blue Cross and Blue Shield divisions in four states: Illinois, New Mexico, Oklahoma and Texas. Like BCBSMT, HCSC is an independent licensee of BCBSA and is authorized to use the Blue Cross and Blue Shield names and marks. (Reitan Direct at 5:1-7; Smith Direct at 3:13-16, 3:22-4:3.)

25. HCSC is one of the financially strongest Blue Cross Blue Shield plans in the United States, with total annual revenue on a statutory basis of approximately $19.9 billion. HCSC has an A.M. rating of A+ (Superior), a Standard & Poor's rating of AA- (Very Strong) and a Moody's rating of A1 (Good). It is well positioned to make the necessary financial investments in the operations of BCBSMT and provide the economies of scale that BCBSMT currently lacks. It has the financial resources to pay the purchase price for the assets it would acquire from BCBSMT without borrowing or in any way straining its financial resources. HCSC

will have no trouble meeting the BCBSMT obligations it will assume. (Smith Direct at 4:4-8, 11:5-18, 12:19-22; Reitan Direct at 8:16-23.)

26. HCSC had a December 31, 2011, statutory surplus of approximately $8.9 billion, and a surplus of $9.5 billion as of September 30, 2012. In general terms, a surplus is the amount of assets a company has that exceeds its liabilities. A surplus is critically important for an insurer; it ensures that anticipated and unanticipated claims by policyholders can be paid promptly. HCSC's level of surplus is sufficient to comply with the surplus required under law and to provide for the security of HCSC's certificate holders and policyholders. (Smith Direct at 5:6-9, 4:9-12, 12:6-12.)

27. A health insurer's surplus is measured relative to its risk profile to determine the "risk-based capital" ("RBC") requirements for that company. RBC requirements were developed by the National Association of Insurance Commissioners to uniformly measure insurance companies relative to the degree of risk assumed by a company within its business operations. Companies with higher risk need a higher surplus amount to protect the company from insolvency. Meeting contractual obligations, maintaining corporate financial viability, and historically significant industry fluctuations in capital levels are among the many reasons companies seek to maintain their RBC levels comfortably above minimum regulatory standards. RBC levels are also often maintained well over regulatory levels because small changes in underwriting or asset risk can produce significant changes in RBC. (Smith Direct at 4:12-19; Smith Testimony at 261:12-14; Galasso Appraisal Definitions ¶ 49.)

28. HCSC has more than 13 million members so it needs sufficient RBC to protect against a catastrophic event, like a flu pandemic. A truly catastrophic health crisis could challenge even HCSC's surplus amount. Because HCSC is member owned, it does not have the

same access to capital markets that a public company has. A robust surplus provides security for HCSC's members and provides flexibility for HCSC to invest in enhancements and infrastructure, state of the art technology, cost containment programs, and wellness and other initiatives that benefit all HCSC members. HCSC's surplus also gives it opportunities to pursue strategic alliances like this one. (Smith Direct at 4:20-5:5, 5:10-6:2; Reitan Direct at 9:4-10:2.)

29. [redacted]

30. [redacted]

B. <u>Operational Strength</u>

31. HCSC has approximately 13 million members, which represents an increase of 12 percent in the last five years. It processes almost 750,000 claims per business day. Ninety-nine percent of those claims are processed within 30 days, at about a 99 percent financial accuracy rate. (Direct Testimony of James L. Kadela, Divisional Senior Vice President Financial Services and Internal Operations, HCSC, dated February 8, 2013 ("Kadela Direct") at 4:5-20.)

C. <u>HCSC's Interests in the Proposed Transaction</u>

32. HCSC is interested in the alliance with BCBSMT for several reasons. BCBSMT's membership will improve HCSC's scale. The increase in HCSC's membership will

contribute to improvements in HCSC's overall expense ratio. BCBSMT's membership also features a different industry mix. This mix and the geographic diversification that would result from the alliance will help make HCSC less susceptible to regional and industry-specific business cycles. BCBSMT also brings employee expertise and capable leadership that will strengthen HCSC and beneficial relationships with medical providers. (Reitan Direct at 10:22-11:19; Smith Testimony at 270:22-272:1.)

33. HCSC is also firmly committed to the NIO model of health insurers and to the Blue Cross and Blue Shield system. HCSC sees BCBSMT as an excellent "fit" in terms of nonprofit commitment and corporate culture. (Reitan Direct at 12:4-12.)

D. <u>Track Record Of Successful Alliances</u>

34. HCSC has previously completed successful alliances of various types with Blue plans in Texas (1998), New Mexico (2001) and Oklahoma (2005). As a result, it has significant expertise in how to manage the full scale integration of a plan without disrupting core operations, including claims and customer service. (Kadela Direct at 3:20-4:4, 9:8-10:3.)

35. HCSC uses a simple integration approach that converts the simplest lines of business first, establishing a foundation. In its three other integrations, customer service, claims processing productivity, and costs per claim were all improved. Membership was increased in all three states. (Kadela Direct at 10:13-11:16.)

36. A significant factor in HCSC's success in these other states has been its commitment to maintaining local leadership and strong local presence. HCSC is committed to the model of substantial local control. (Kadela Direct at 20:20-21:1.)

IV. THE UNCERTAINTIES OF THE AFFORDABLE CARE ACT

37. The passage and implementation of ACA has created substantial uncertainty, while creating challenges and opportunities, in the health insurance market. ACA requires

insurers to implement various market reforms, many of which create risks for insurers. The market reforms include such provisions as (a) guaranteed issue, which prohibits insurers from declining to provide insurance to people with pre-existing conditions or significant risks; (b) elimination of annual and lifetime benefit maximums; and (c) the creation of insurance "exchanges." These exchanges will create a new marketplace that will allow individuals who are currently uninsured to buy coverage, in some cases on a subsidized basis. Because many people who are currently uninsured are likely to have pent up demand for medical care, medical utilization, and therefore claims, are likely to increase. An insurer like BCBSMT, which has been unable to consistently generate underwriting gains for the last fifteen years, will be especially challenged by these new provisions. (Burzynski Direct at 12:8-13:12.)

38. ACA also imposes new Medical Loss Ratio ("MLR") requirements that will require increased operational efficiencies that will challenge small health insurers. For every dollar paid in premium, at least 80 or 85 cents, depending on the business segment, will have to be spent on medical claims and other specified expenses. These new MLRs have to be calculated on a yearly basis. If the margin in a particular year is more than the allowed amount, the difference must be rebated to premium payers. As a result, an insurer does not have the possibility of having a "good" year offset a "bad" year. (Burzynski Direct at 13:13-14:13.)

39. The health insurance exchanges created under ACA will likely increase competition in Montana. It will be considerably easier for the large, national for-profit insurers to reach Montana consumers on the electronic exchanges; products will be easy to list and market. Price competition will also increase, further straining BCBSMT's financial position. (Burzynski Direct at 15:14-17:13.)

40. HCSC is well positioned to manage the risks of and opportunities under ACA.

V. NEED FOR ALLIANCE AND DUE DILIGENCE

41. Section 50-4-717(2)(a) of the Conversion Statute specifies that in determining whether a conversion transaction is in the public interest, the Commissioner shall consider "whether the transferor exercised due diligence in deciding to engage in a conversion transaction, selecting the transferee, and negotiating the terms and conditions of the conversion transaction." (Mont. Code Ann. § 50-4-717(2)(a).)

A. BCBSMT Exercised Due Diligence by Deciding to Engage in this Conversion Transaction.

42. In the approximate fifteen years preceding the Conversion Transaction, the BCBSMT Board of Directors and Management had ongoing discussions about BCBSMT's ability to remain an independent Blue plan within the BCBSA. These conversations became more pointed in the three years preceding the Transaction and considered a range of possible solutions including outsourcing, shared services, and alliances with other Blue plans. (Frank Direct at 8:7-12.)

43. In early 2012, CEO Michael Frank initiated specific conversation with the BCBSMT Board Chair about BCBSMT's future options. This resulted in a small group at BCBSMT developing a White Paper in March 2012, which formally outlined BCBSMT's options for the future, including outsourcing, shared services, and alliances with other Blue plans. The White Paper was presented to the Executive Committee of the BCBSMT Board in May 2012, resulting in lengthy conversations regarding the outlined options. (Frank Direct at 8:12-17.)

44. The BCBSMT Board and executives recognized that change was necessary. BCBSMT's current business model was not sustainable: despite reductions in administrative expenses, primarily through a reduction of employee positions, it had consistently failed to make

an underwriting profit in eleven of the last fifteen years. BCBSMT's RBC was declining, and it did not have the resources to make necessary capital expenditure improvements. (Frank Direct at 9:3-7; Burzynski Direct at 7:7-9, 9:7-10, 10:11-12, 20:14-21, 23-24.)

45. BCBSMT had seen an increase in high-dollar claims utilization resulting in increased insurance risk exposure. (Burzynski Direct at 14:17-21.) At the same time, BCBSMT also was facing increasing competition from insurance companies with far greater size, membership, and scale, resulting in decreasing and shifting membership for BCBSMT and ongoing concerns over price and market competitiveness. (Frank Direct at 8:19-2, 9:14-17.) While BCBSMT currently has approximately 245,000 members, some of its main competitors range in membership size from 13-35 million members. (Burzynski Testimony at 240:21-25.)

46. The concerns BCBSMT faced were even more serious in view of the advent of ACA, which includes such measures as medical loss ratio requirements, potential rate increase limits, and elimination of underwriting protections. (Frank Direct at 9:17-20.)

47. The Board ultimately decided that an alliance with another health insurer would be in the best interest of BCBSMT and its policyholders, providers, and employees. Both outsourcing and shared services arrangements would have resulted in significant layoffs to employees. Further, neither outsourcing or shared services would have addressed the underlying issues under ACA, nor the lack of scale and ability to better manage risk. An alliance could preserve employee jobs, create necessary scale, provide for necessary technology upgrades, and result in a greater capacity to manage risk. (Frank Direct at 10:5-15.)

B. <u>BCBSMT Exercised Due Diligence in Selecting HCSC as the Transferee.</u>

48. In evaluating a potential alliance, the Board knew that it wanted to consider only other Blue plans because of BCBSMT's long-standing seventy-year history in Montana with the Blue mark. (Frank Direct at 10:2-9, 10:16-11:3, 11:9-12:2, 14:16-18.) Further, BCBSMT's

license through the BCBSA could only be transferred, with the consent of the Association, to another Blue plan. (Frank Direct at 11:19-22.)

49. Historically there were 130 Blue plans in the U.S., typically operating as separate state plans within the BCBSA. At the time the Board began considering an alliance with another Blue plan, there remained only 38 Blue plans in the U.S., due to previous Blue consolidations. (Frank Direct at 6:8-18.)

50. As a member of the Blue system and the BCBSA, the BCBSMT Board and executives have continual interaction with and extensive knowledge of all the other Blue plans on such topics as financial strength, operational performance, culture, and technology. (Frank Direct at 14:18-22, 15:3-7.)

51. The Board wanted to ensure that any alliance partner would be a nonprofit, NIO entity, due to BCBSMT's philosophical focus on affordable access to insurance for its policyholders, rather than maximizing profit for investors. (Frank Direct at 11:11-16.) This narrowed the realm of possible Blue plans to consider for an alliance by eliminating approximately fourteen plans. (Frank Direct at 15:9-10; Frank Testimony at 187:1-4.)

52. The Board and executives further narrowed the list by eliminating Blue plans that did not have sufficient financial stability or capital reserves for BCBSMT's needed technological upgrades, or large enough scale to compete in the future marketplace. BCBSMT knew that it needed to identify a partner large enough to spread potential risk, and not have to go through a consolidation process twice. (Frank Direct at 12:13-22, 13:1.) This consideration eliminated all other single-state plans and some smaller multistate plans. (Frank Direct at 15:10-12.)

53. The Board then evaluated the remaining Blue plans by looking at potential organizational and cultural fit, including a focus on local control. (Frank Direct at 13:14-21.)

The Board also eliminated certain multistate plans that were not in the same geographic region as Montana. (Frank Direct at 15:10-12.)

54. Using these factors and considerations, the Board narrowed the field of potential alliance partners to two main contenders. (Frank Direct at 15:13; Frank Testimony at 187:1-9.)

55. The BCBSMT Board Chair and Mr. Frank had phone conversations and in-person meetings with the CEOs of the two contenders in April and May of 2012. Both were interested in continuing conversations with BCBSMT about a possible alliance. (Frank Direct at 15:14-21.) A select group of BCBSMT executive team members then continued to research the two plans. (Frank Direct at 15:22-16:2.)

56. The President, CEO, and executive staff of each plan under consideration were invited to come to Three Forks, Montana, to make a presentation to the BCBSMT Board in June 2012. (Frank Direct at 16:4-11.) Each plan discussed their respective operations, future strategic direction, and partnership opportunities with BCBSMT. (Frank Direct at 16:11-16.)

57. After the Three Forks presentations, the BCBSMT Board discussed the two plans, carefully weighing the attributes of each and evaluating each against the factors the Board had outlined. (Frank Direct at 16:19-22.) The Board and executives had multiple follow-up conversations internally and with the respective plans. (Frank Direct at 16:22-17:1.)

58. After careful consideration, the Board decided that HCSC best met its criteria, and that it would continue to evaluate a potential relationship and do further due diligence with HCSC alone. (Frank Direct at 17:1-3.) The Board ultimately favored HCSC over the other plan because of its larger size as the nation's largest nonprofit insurer with more than 13 million members, greater financial strength as one of the strongest Blue plans in the nation, emphasis on local control in the other states in which it operates, successful track record in integrating other

Blue plans in the past, lower administrative costs resulting in lower premiums for members, and proprietary ownership of its own impressive technology platform. (Frank Direct at 17:3-15; Frank Testimony at 107:12-22, 108:1-21.)

59. BCBSMT designated two internal due diligence teams – transactional and operational – that continued to do further due diligence between June and October 2012. This entailed further research, exchange of information and documents, multiple in-person visits and site visits, and frequent teleconferences. (Frank Direct at 17:17-22.)

60. The transactional due diligence team concentrated on evaluating HCSC's commitment to remaining an NIO company, its financial strength, size and scale, technology, and local management. (Frank Direct at 18:12-17.) The transactional due diligence confirmed HCSC's commitment to the nonprofit model, its financial strength as evidenced by its reserves and RBC, while still growing membership, that its size at 13 million members maximizes its ability to spread risk, superior technological capabilities to serve consumers, and emphasis on local involvement and community presence in Texas, Oklahoma, and New Mexico. (Frank Direct at 18:19-19:16.)

61. The operational due diligence team focused on the operational and service impact to BCBSMT members, including areas such as information technology, privacy and security, operations, medical and behavioral care management, analytics and information management, healthcare services, and corporate culture. (Frank Direct at 19:19-20:3.) The team concluded that the services and benefits to BCBSMT's applicants, policyholders, groups, providers, producers and employees would be greatly expanded and improved. (Frank Direct at 20:5-7.) For example, HCSC's real-time claims processing system was state-of-the-art and would increase efficiency and speed. (Frank Direct at 20: 7-11.) HCSC had impressive customer

service software that used language-based analytics to record and interpret policyholder calls, which would enhance customer service interactions. (Frank Direct at 20:11-15.) HCSC data warehouses provided outstanding databases and reporting systems to improve provider care and reimbursement, as well as policyholder security and protection of sensitive health information. (Frank Direct at 20:15-22.) The team was impressed with HCSC's innovative benefit programs, such as Seasons of Life, which assists bereaved family members after a death. (Frank Direct at 21:3-7.) HCSC's mobile technology services can give applicants and policyholders easier access to shop for insurance, check on claim status, or find a provider. (Frank Direct at 21:11-15.)

62. The operational due diligence team also evaluated the legal, financial, and internal audit areas. The team concluded that BCBSMT would greatly benefit from the additional staff and resources at HCSC, especially at the federal level, which would free up BCBSMT resources to focus on state-specific laws, regulations, and assessments. (Frank Direct at 21:21-22:6.)

63. The results and conclusions of the two due diligence teams were presented to the BCBSMT Board in October 2012. (Frank Direct at 23:21- 24:1.) The Board voted on November 7, 2012, to approve moving forward with an alliance with HCSC. (Frank Direct at 24:4-8.)

64. Concurrent with BCBSMT's due diligence efforts, HCSC also implemented a due diligence team to review BCBSMT. (Reitan Direct at 12:16-21.)

C. BCBSMT Exercised Due Diligence in Negotiating the Terms and Conditions of the Transaction.

65. While due diligence was underway, BCBSMT and HCSC also engaged in extensive negotiation over the terms of the alliance beginning in August 2012. (Frank Direct at 25:12-16.)

66. The final terms of the alliance were set out in the Asset Purchase Agreement between Blue Cross and Blue Shield of Montana, Inc. and Health Care Service Corporation,

dated November 14, 2012 ("Asset Purchase Agreement"). (Application Ex. 3; Frank Direct at 25:17-22.)

67. BCBSMT also hired the firm of Graham & Dunn PC as outside counsel with specialized expertise in commercial transactions and antitrust matters to help it negotiate the terms of the agreement. (Frank Testimony at 134:3-5.)

68. The Applicants negotiated all of the terms of the Asset Purchase Agreement including but not limited to: which BCBSMT liabilities and assets would transfer to HCSC and which would be retained by the old BCBSMT, including BCBSMT's surplus; HCSC assumption of all existing policy risk and liabilities; HCSC assumption of contracted third-party administration services; HCSC retention of all currently employed BCBSMT employees at the employees' current seniority and salary, and with comparable benefits and retirement options; the distribution of BCBSMT subsidiaries; retention of BCBSMT provider and producer networks; typical commercial representations and warranties; and closing conditions. (Application Ex. 3; Frank Direct at 25:10-16, 26:11-29:15; Frank Testimony at 135:5-136:6; Reitan Direct at 15:14-18.)

69. In negotiating the consideration HCSC would pay to BCBSMT for the assets it would receive in excess of the liabilities it would assume, the Applicants mutually understood the Montana Conversion Statute to require that the consideration represent the assets' fair market value and that the fair market value be determined by an independent third party. (Frank Direct at 26:2-6.) The Applicants agreed that BCBSMT would hire an independent expert to value the assets and, upon receiving the independent valuation, HCSC would determine whether it would complete the Transaction by paying the value determined by the expert. (Frank Direct at 26:6-7; Frank Testimony at 169:13-21; Reitan Testimony at 363:13-364:3.)

70. BCBSMT hired James Galasso of Actuarial and Financial Modeling, Inc. to value its core health insurance business. (Frank Direct at 26: 6-8.) BCBSMT also retained Calvin Swartley, Senior Manager and member of the Valuation & Litigation Services Group of Moss Adams LLP in Portland, Oregon, to determine the fair market value of BCBSMT's total surplus, including the Galasso valuation of the core health insurance business as of June 30, 2012. (Frank Direct at 26:8-10; Direct Testimony of Calvin E. Swartley, CFA, ASA, Moss Adams LLP, dated February 8, 2013 ("Swartley Direct") at 2:1-4, 3:2-8.)

71. Consistent with its negotiated position, HCSC agreed to pay the value of $17.6 million, as determined by Mr. Galasso. (Reitan Testimony at 365:18-20.)

72. No conflicts of interest were discovered among BCBSMT or HCSC board members, executives or experts retained by the Applicants. (Frank Direct at 38:1-7; Reitan Direct at 13:15-18.)

VI. THE TRANSACTION

A. <u>Significant Features of the Transaction</u>

73. Under the Conversion Transaction Applicants seek to have approved, HCSC will acquire the insurance and ASO or self-funded operations ("Acquired Business") and specified associated liabilities of BCBSMT. After the Transaction, HCSC will operate the Acquired Business as the Montana division of HCSC under the name Blue Cross and Blue Shield of Montana. Current BCBSMT policyholders will become HCSC policyholders with no change in coverage or benefits. The Montana division of HCSC will continue to be regulated by the Montana Commissioner of Insurance under Montana law. (Frank Direct at 29:21-30:9; Reitan Direct at 17:4-14.)

74. The old corporate BCBSMT entity will retain the remaining assets and liabilities and will continue to operate only for the purpose of satisfying or otherwise discharging the

remaining liabilities. It will change its name to delete any reference to "Blue Cross" or "Blue Shield" and will eventually be dissolved. The remaining funds and assets of the company will be paid to a foundation. The purchase price will be paid by HCSC upon closing of the Transaction. It will be paid either directly to the foundation or to the old BCBSMT. (Frank Direct at 30:10-21.)

75. The BCBSMT Board of Directors will exercise its fiduciary duty to oversee the assets until the appropriate foundation is determined through the hearing process. (Burzynski Direct at 30:8-13.)

B. <u>The Asset Purchase Agreement</u>

76. The Conversion Transaction between BCBSMT and HCSC is structured as an asset purchase. The detailed terms of the Conversion Transaction are memorialized in the Asset Purchase Agreement. Under the terms of the Asset Purchase Agreement, BCBSMT will transfer specific assets to HCSC, including its insurance contracts, ASO contracts, provider contracts, and its rights to use the Blue Cross and Blue Shield names ("Purchased Assets"). HCSC will also acquire specific real property, furniture, fixtures and equipment, and other specified assets, including assets owned, leased or licensed by BCBSMT and used in the operation of its business. HCSC will assume specific BCBSMT liabilities, including claims liabilities and liabilities under the ASO and provider contracts, and certain pension liabilities. The liabilities to be assumed by HCSC amount to approximately $180 million. Upon closing of the Asset Purchase Agreement, BCBSMT will transfer to HCSC approximately $180 million in assets and cash to support the liabilities. (Application Ex. 3; Asset Purchase Agreement, Sections 2.01-2.02; Reitan Direct at 14:7-13.)

77. HCSC will pay $40.2 million for the Purchased Assets. (Stipulation, Applicants' Ex. 9; Smith Testimony at 272:9-11.)

78. No part of the payment will inure directly or indirectly to an officer, director, or trustee of BCBSMT, to an officer, director, trustee, shareholder, or employee of HCSC, or to any other person that is not a foundation authorized to receive the assets by the Montana Attorney General. Likewise, no officer, director or trustee of BCBSMT will receive any immediate or future remuneration as a result of the proposed Transaction except for the reasonable value of services rendered pursuant to a valid contract between the officer, director or trustee and BCBSMT. (Reitan Direct at 14:17-15:1; Frank Direct at 41:4-16; Stipulation, Applicants' Ex. 10.)

79. Certain BCBSMT assets not primarily related to BCBSMT's core insurance business are not being sold or transferred to HCSC under the Asset Purchase Agreement ("Excluded Assets"). Those assets include BCBSMT's surplus, CBMI, certain buildings, and various other assets. Certain pre-closing liabilities, such as litigation liabilities, are also excluded from the Transaction. HCSC is not acquiring most of the BCBSMT assets that generated investment or other gains; the assets HCSC is acquiring are the assets from BCBSMT's core health business, which has experienced underwriting losses in eleven of the last fifteen years. (Burzynski Direct at 23:20-24:2; Application Ex. 1 ("Schedule of Assets and Liabilities"); Smith Direct at 9:9-18.).

80. HCSC agreed in the Asset Purchase Agreement to make offers of employment to all employees of BCBSMT as of the closing date of the Transaction. The offers of employment are required to be at an annual base salary equal to or greater than the annual base salary of each employee immediately prior to the closing. The only BCBSMT employees excluded from this agreement are employees receiving long-term disability payments. No BCBSMT employee will

be required to move to retain employment with HCSC. (Asset Purchase Agreement Section 6.01; Frank Direct at 26:18-27:2.)

81. The Asset Purchase Agreement also requires HCSC to cover all BCBSMT employees who accept offers of employment under all HCSC's employee benefit plans. The benefits provided by these plans include health benefits, paid time off, short-term and long-term disability, retirement saving benefits and other standard employee benefit programs. Each retained employee's BCBSMT date of hire will be recognized by HCSC for purposes of determining benefit eligibility and accruals. There are some variations in the employee benefit plans sponsored by HCSC compared to those sponsored by BCBSMT, but overall, the benefits are comparable. For some benefits, HCSC's plan is better than BCBSMT's. (Asset Purchase Agreement Section 6.02(a); Frank Direct at 27:8-16, 28:4-14.)

82. The Asset Purchase Agreement also provides certain protections for the pension benefits BCBSMT employees currently have. BCBSMT will fund at closing post-closing benefit accruals for BCBSMT employees currently in its Defined Benefit Plan with specified years of service and age. BCBSMT employees who participate in the Annual Retirement Contribution and 401(k) programs will be eligible to participate in HCSC's cash balance and 401(k) plans. The combination of these two plans allows participants to accumulate 12 1/2 percent or more of pay each year for retirement. The combined benefits of these plans rank well within peer industry group benefit plan offering benchmarks. (Asset Purchase Agreement Sections 6.02(b), 6.03, 6.05, 6.06; Frank Direct at 27:17-29:15.)

83. The Asset Purchase Agreement includes two provisions that provide for ongoing input of Montanans into HCSC's operations in Montana. Subject only to HCSC's By-laws and corporate policies relevant to director qualifications, one current BCBSMT Board member will

be elected to HCSC's Board of Directors for a term of at least three years. HCSC further committed to create a Montana advisory board, having a majority of Montana residents, to advise HCSC's Board on Montana operations and issues. (Asset Purchase Agreement, Sections 5.09(a) and (b); Frank Direct at 29:16-20.)

84. HCSC will retain BCBSMT's current provider network and hopes to have providers with contracts with BCBSMT agree to assignment of those contracts to HCSC. Montana providers will benefit from access to HCSC's claims processing system, BlueChip, which is more efficient than BCBSMT's current system. (Reitan Direct at 17:15-23.)

C. <u>Other Necessary Financial Commitments</u>

85. In addition to the purchase price HCSC will pay for the Purchased Assets, HCSC will incur substantial additional financial commitments to operate the current BCBSMT as a division of HCSC. BCBSMT's surplus is not being transferred to HCSC. HCSC will have to dedicate resources to meet regulatory reserve requirements. HCSC will have to earmark a minimum amount in the range of $50 to $100 million to cover the surplus required for the BCBSMT operations. (Smith Testimony at 276:7-278:18.)

86. HCSC has estimated that it will cost approximately $28 million to connect BCBSMT to HCSC systems. This is a transition cost, not a development cost or the purchase price of new equipment and infrastructure. BCBSMT would incur a significantly higher cost -- likely more than $100 million -- to implement comparable systems on its own. (Kadela Direct at 12:20-13:7.)

D. <u>The Proposed Transaction Will Not Adversely Affect the Availability or Accessibility of Health Care Services or Health Insurance Coverage.</u>

87. The Applicants and the Commissioner hired separate experts to evaluate whether the proposed Transaction has the likelihood of creating a significant adverse effect on the

availability or accessibility of health care services or health insurance coverage in Montana. (Mont. Code Ann. §§ 50-4-717(2)(d).) As described below, both experts reached the same conclusion: the proposed Transaction will not have adverse effects on the availability or accessibility of health care services or health insurance coverage.

88. The Applicants hired Dr. Thomas R. McCarthy, who is an economist and head of the health care practice of NERA Economic Consulting. Before he joined NERA in 1983, Dr. McCarthy was a staff economist with the Federal Trade Commission conducting studies of regulation and competition in health care markets. Dr. McCarthy was previously retained by the State of Montana in connection with a Certificate of Public Advantage oversight of the Benefis Hospital. Dr. McCarthy has a Ph.D. in Economics from the University of Maryland. (Direct Testimony of Thomas R. McCarthy, Senior Vice President of NERA Economic Consulting, dated February 8, 2013 ("McCarthy Direct") at 2:2-19, 3:3-18; Hearing Transcript (Vol. III) March 13, 2013 ("McCarthy Testimony") at 40:22-41:9.)

89. Dr. McCarthy is qualified to offer an opinion on the community and market impacts of the proposed Transaction on the health insurance and health care markets.

90. To determine the likely effects of the proposed transaction on the availability or accessibility of health care services or health insurance coverage in Montana, Dr. McCarthy and his Firm reviewed various documents addressing the expected efficiencies and other benefits of the Transaction. He concluded that the proposed transaction would make BCBSMT a stronger competitor by giving it access to more capital and by generating a number of efficiencies. These benefits will ensure that BCBSMT has the financial strength to continue providing the services and coverage it has provided in the past while keeping premiums at competitive levels. As a result, Dr. McCarthy concluded that the proposed Transaction will not negatively impact either

availability or accessibility of health care services or health insurance coverage in Montana. (McCarthy Direct at 6:22-7:23.)

91. The Commissioner retained Dr. Timothy Tardiff, a Principal of Advanced Analytical Consulting Group, Inc. ("AACG"), to evaluate the impact of the Transaction on availability of health care services and health insurance in Montana. Dr. Tardiff has a B.S. in Mathematics from the California Institute of Technology, and a Ph.D. in Social Sciences from the University of California, Irvine. He has held a variety of academic positions and has worked as a consultant, specializing in market competition and economics in regulated industries, for almost twenty years. (Direct Testimony of Timothy J. Tardiff, Ph.D., Principal, AACG, dated February 12, 2013 ("Tardiff Direct") at 2:2-3:1, 4:10-17.)

92. Dr. Tardiff is qualified to offer an opinion on the economic and community impacts of the proposed Transaction.

93. Dr. Tardiff and a team working with him at AACG reviewed the Application and supporting materials, financial and other data provided by BCBSMT and HCSC, surveys and analyses of the Montana market, as well as data that AACG purchased from the National Association of Insurance Commissioners. Based on analysis of this information and data, Dr. Tardiff concluded that the proposed transaction will not adversely impact either the availability or accessibility of health care services or health insurance in Montana. (Tardiff Direct at 4:18-5:10, 8:14-16. *See also* AACG "Antitrust and Community Impact Report, January 29, 2013 ("AACG Report") at 4.)

94. Dr. Tardiff based his opinion that the proposed transaction would not have an adverse impact on the availability or accessibility of health care or health insurance in Montana on the following major factors:

- the sustained presence of providers, brokers and enrollees;
- continued competition in the marketplace; and
- the continued presence and stability of BCBSMT (whether in current or different form).

He concluded that the proposed Transaction is unlikely to cause a reduction in either provider contracts or provider rates and is also unlikely to lower the number of brokers operating in Montana. Because HCSC is assuming the contracts of all current BCBSMT members, and because no drop in membership was seen after HCSC's alliances in Texas, New Mexico and Oklahoma, Dr. Tardiff concluded that a drop in enrollees was not likely in Montana. Finally, based on Dr. Tardiff's comparative analysis of BCBSMT's and HCSC's efficiency, financial health and risk, he concluded that HCSC outperforms BCBSMT in all three areas. On that basis, Dr. Tardiff concluded that the proposed transaction would support the continued presence of BCBSMT in the Montana market, albeit as a division of HCSC rather than as a stand-alone entity. (Tardiff Direct at 17:8-20:2.)

E. The Proposed Transaction Will Not Adversely Impact Continued Access to Affordable Health Care.

95. Dr. McCarthy also testified that the Transaction will not adversely impact the future access of Montanans to affordable health care. He based this opinion on his conclusion that the Transaction will have no impact on competition in the market for health insurance. This means that there will be sufficient competitive safeguards to ensure that Montanans will continue to have access to affordable health care; BCBSMT will continue to face the same strong competitors it faces now, including Cigna, UnitedHealth, PacificSource, and a large third-party administrator called Employee Benefit Management Services, Inc. Any attempt by BCBSMT to

increase its premiums or fees could result in the loss of a substantial number of members to these competitors. (McCarthy Direct at 10:14-11:24.)

96. Dr. Tardiff also concluded that the Transaction will not prevent continued access to affordable health care in Montana. Based on his analysis of rate changes in Texas, New Mexico and Oklahoma after HCSC's alliances in those states, and HCSC's assurances about likely continuation of the benefit plans BCBSMT currently offers, Dr. Tardiff opined that HCSC was not likely to dramatically alter premium rates or coverage plans as competition and other adverse results of such actions would likely inhibit HCSC from doing so. (Tardiff Direct at 20:9-21:2, 21:18-22:7, 24:10-16.)

F. __The Proposed Transaction is Equitable To the Public Interest and Other Stakeholders.__

97. Dr. McCarthy also concluded that the proposed Transaction is equitable to the public interest and to all other persons and entities that could be impacted by it. He reached this conclusion based on his opinion that the alliance will make BCBSMT a more efficient and stable competitor, while having no adverse impact on competition in the Montana health insurance market. This means that enrollees and insureds will still enjoy competitive premiums and similar insurance options. Producers and brokers will likewise see no material impact on competition in Montana and will benefit from HCSC's enhanced technology and innovative services. Similarly, providers will not be adversely affected, as the Transaction will not impact competition in any of the markets for their services. Finally, Dr. McCarthy noted that other residents of Montana will benefit from the creation of a foundation with the proceeds of the purchase price HCSC will pay for the business it is acquiring and the surplus and other remaining assets of BCBSMT. (McCarthy Direct at 12:1-13:10.)

98. Dr. Tardiff also evaluated whether the proposed Transaction was equitable to the public interest, enrollees, insureds and certificate holders of BCBSMT. (Because BCBSMT has no shareholders, Dr. Tardiff did not have to perform any analysis of shareholder issues.) He concluded that the proposed Transaction would be equitable to all of those parties for numerous reasons, including (a) HCSC's commitment to hire all current BCBSMT employees at at least their current level of compensation; (b) the transfer of current BCBSMT employees to an HCSC pension plan; (c) the transfer of an estimated $120 million to a foundation for the benefit of Montanans; and (d) the likelihood that current health coverage plans, enrollment and rates will not be unreasonably changed. (Tardiff Direct at 24:17-26:5, 26:14-18.)

G. <u>The Proposed Transaction Will Improve Economies of Scale.</u>

99. Both Dr. McCarthy and Dr. Tardiff also concluded that the proposed Transaction will not result in any inefficient economies of scale; in fact, the transaction will significantly improve BCBSMT's scale.

100. Dr. McCarthy opined that the Transaction will improve scale economies by allowing HCSC and BCBSMT to spread their total administrative costs over their combined membership. He based this conclusion on the evidence that HCSC achieved reductions in administrative expense ratios in other states in which it has acquired plans, and on the fact that many of the expenses (such as computer hardware and software costs) are relatively fixed and will not vary much with the increase in membership that BCBSMT brings to HCSC. As a result, Dr. McCarthy concludes that the Transaction will result in real and significant improvements in economies of scale. (McCarthy Direct at 13:16-14:25.)

101. Dr. Tardiff likewise concluded that in light of the respective cost structures, sizes and nature of the businesses of HCSC and BCBSMT, the proposed Transaction would result in more efficient economies of scale. (Tardiff Direct at 15:17-17:6.)

H. <u>The Proposed Transaction Does Not Violate Any Antitrust Laws.</u>

102. All the evidence in the record on this matter supports the conclusion that the proposed Transaction does not raise any antitrust issues or violate any federal or state antitrust laws. Dr. McCarthy and Dr. Tardiff reached virtually identical conclusions based on undisputed facts described below.

103. BCBSMT and HCSC do not currently compete with each other. HCSC's members in Montana are primarily employees of companies headquartered in one of the four states in which HCSC operates a division. BCBSMT does not compete for these members since BCBSMT does not submit bids to companies outside of Montana. HCSC has no sales presence in Montana and cannot be considered an active competitor in the Montana health insurance market. Simply stated, BCBSMT and HCSC do not compete with each other for membership, so there is no lost competition if they come together. (Tardiff Direct at 9:17-10:7, 15:7-16; McCarthy Direct at 15:2-21.)

104. HCSC does not contract with Montana healthcare providers and BCBSMT already counts the HCSC members who live in Montana as part of its member volume when negotiating volume-based rates with Montana providers. The proposed Transaction will not change the structure of the Montana provider market. (McCarthy Direct at 15:22-26; Tardiff Direct at 13:19-14, 14:1-6.)

105. The conclusion that there are no anti-competitive concerns raised by the proposed Transaction is further bolstered by the fact that other competitors in the Montana health insurance market, such as Cigna and PacificSource, appear to be making inroads in the market. (Tardiff Direct at 13:13-15.)

106. The United States Department of Justice's Antitrust Division granted the Applicants' request for early termination of the waiting period under the federal Hart-Scott-

Rodino Antitrust Act based on the finding that the Transaction would cause no antitrust concerns. (McCarthy Direct at 16:22-26.)

VII. FAIR MARKET VALUE OF THE PURCHASED ASSETS

107. Section 50-4-715(2) of the Conversion Statute specifies that in determining whether a conversion transaction is in the public interest, the Montana Attorney General shall require that

> (a) the **fair market value** of public assets is preserved and protected;
>
> (b) the **fair market value** of public assets is expended or invested with reasonable and prudent consideration of the potential risk of financial loss associated with the conversion transaction; and
>
> (c) the **fair market value** of the public assets of a nonprofit health entity will be distributed as provided in 50-4-720.

(Mont. Code Ann. § 50-4-715(2)(a)-(c) (emphasis added).)

108. The Conversion Statute defines "fair market value" as the value "determined by an independent appraisal of the assets or operations performed and communicated by a qualified appraiser according to applicable professional appraisal standards." (Mont. Code Ann. § 50-4-701(4).)

109. The applicable professional standard for determining the "fair market value" of the Purchased Assets is the price at which the property would change hands between a willing buyer and a willing seller when the latter is not under any compulsion to sell, both parties having reasonable knowledge of relevant facts. (MDS Consulting's Fair Market Valuation of Blue Cross Blue Shield of Montana, AG Ex. I ("MDS Rpt.") at 5; Moss-Adams LLP Valuation Analysis, Blue Cross Blue Shield of Montana, as of June 30, 2012, Application Ex. 7 ("Moss-Adams Rpt.") at 1; Internal Revenue Service Revenue Ruling 59-60.)

110. The Conversion Statute reflects the Montana Legislature's determination that public assets impacted by a conversion transaction should be valued at their fair market value, so that the fair market value can be preserved and protected. The Legislature did not require public assets to be preserved or protected at the highest value attainable, which is a standard difficult to measure. Rather, it specified a fair market value standard, which is objective, rather than subjective, and can be independently verified.

111. The Conversion Statute provides that "[i]n determining fair market value, the attorney general may consider all relevant factors that may include but are not limited to:

> (a) the value of the nonprofit health entity or an affiliate or the assets of the nonprofit health entity or affiliate that are determined as if the nonprofit health entity or affiliate had voting stock outstanding and 100% of its stock was freely transferable and available for purchase without restriction;
>
> (b) the value as a going concern;
>
> (c) the market value;
>
> (d) the investment or earnings value;
>
> (e) the net asset value; and
>
> (f) a control premium, if any.

(Mont. Code Ann. § 50-4-716(3).)

112. The fair market value of the Purchased Assets proposed to be transferred to HCSC from BCBSMT in the Conversion Transaction, considering all these factors is $40.2 million. The evidence presented in the Application and in the hearing record provides ample factual support for this value, as described below.

113. The stipulation entered into among BCBSMT, HCSC and the Montana Attorney General on March 11, 2013, establishing that a fair market value of the Purchased Assets is $40.2 million and that HCSC will agree to pay $40.2 million for the Purchased Assets, is

reasonable and consistent with the record evidence. Thus, with respect to Montana Code Annotated § 50-4-715(2)(a)-(c), the proposed Transaction is in the public interest. (Stipulation, Applicants' Ex. 9.)

A. Evidence Supporting Fair Market Value

114. The parties presented independent valuations that bear on the issue of the fair market value of the Purchased Assets.

B. The Galasso Appraisal

115. BCBSMT retained James Galasso, President & Consulting Actuary of Actuarial Services & Financial Modeling, Inc. ("ActMod"), to do an independent actuarial cash flow appraisal of the health care contracts written and administered by BCBSMT that were to be assumed by HCSC under the terms of the Asset Purchase Agreement (the "Galasso Appraisal"). Mr. Galasso earned degrees in both Theoretical and Applied Mathematics, with honors, from the State University of New York at Stonybrook. He is a member of the Society of Actuaries and the American Academy of Actuaries. He is a Chartered Enterprise Risk Analyst. He has served various organizations as Chief Financial Officer, Chief Actuary and as an Actuarial Consultant. He has done consulting work for many Blue Cross and Blue Shield Plans and other major health insurance companies. Mr. Galasso has more than thirty years experience as an actuary in the health care field. Before his retention by BCBSMT in this matter, neither he nor his firm had ever worked or consulted for either BCBSMT or HCSC. (Direct Testimony of James P. Galasso, FSA, MAAA, CERA, President Consulting Actuary, Actuarial Services & Financial Modeling, Inc., dated February 8, 2013 ("Galasso Direct") at 2:7-18; 3:19-22; Report Prepared by Actuarial Services & Financial Modeling, Inc., Application Ex. 5 ("Galasso Report") at 5; Hearing Transcript, Vol. II, March 13, 2013 ("Galasso Testimony") at 103:23-105:16.)

116. Mr. Galasso is qualified to offer an opinion on the appraisal value of the health care contracts written and administered by BCBSMT. He has no apparent bias or interest that would be likely to affect the independence of his opinion.

117. Mr. Galasso knew when he was hired by BCBSMT that his valuation might be used in connection with a transaction, but he did not know what other company would be involved. Mr. Galasso had no involvement in the negotiation of the Transaction between BCBSMT and HCSC. His appraisal did not reflect in any way the fact that HCSC is the proposed acquirer of the assets appraised. Neither BCBSMT nor HCSC influenced or attempted to influence his opinion in any way. (Galasso Direct at 8:15-21; Galasso Rpt. at 3; Galasso Testimony at 106:2-9.)

118. The Galasso Appraisal valued the expected future cash flows of the health care contracts using various assumptions Mr. Galasso developed based on industry analysis and in conjunction with BCBSMT Management. All of the assumptions Mr. Galasso used were considered and validated in the context of his own industry knowledge, experience and independent industry information. There is no evidence in the record that any assumption used by Mr. Galasso was inappropriate or unreasonable for the appraisal he was conducting. (Galasso Direct at 3:3-8, 13-18, 4:21-5:22; Galasso Rpt. at 5; Galasso Testimony at 172:16-173:7.)

119. The Galasso Appraisal utilized two proprietary actuarial health care models developed specifically by ActMod. A model called the "Segmenter" analyzed thirty months of detailed BCBSMT historical financial information, while the model called the "Optimizer" projected future cash flows. Utilizing the assumptions developed with BCBSMT Management and industry analysis, Mr. Galasso used these models to analyze and project future cash flows for the nine distinct lines of business in BCBSMT's core insurance operations: (a) individual; (b)

small group; (c) large group; (d) Medicare supplement; (e) Medicare Part D; (f) Federal Employee Program ("FEP"); (g) student business; (h) self-funded; and (i) stop-loss. (Galasso Rpt. at 5, 7; Galasso Direct at 4:21-5:4, 11-22; 6:1-8; Galasso Testimony at 107:22-108:12.)

120. Mr. Galasso ran cash flow projections for the nine lines of business under four appraisal value scenarios. Scenario One, called the "base scenario," took into account the following factors and assumptions, among others: discount rates, medical loss ratio ("MLR"), BCBSMT actuarial medical trends, FEP business fee projections, policy/business lapse rates, new business generation assumptions, necessary risk-based capital levels, interest earnings, provider contract assignability, administrative expenses, premium taxes, commissions, and fees under ACA. (Galasso Direct at 6:9-19.)

121. The base scenario was only a starting point; it was not intended to be the best estimate of the actuarial value. (Galasso Testimony at 119:8-17.)

122. In Scenarios 2, 3 and 4 various assumptions were changed from the base scenario. Scenarios 2 and 3 were identical to Scenario 1, except that the discount rate was varied. A discount rate is an expected rate of return that an acquirer would seek to achieve on an investment in a particular business, considering risk and expected cash flows. It reflects an assumed after-tax return acceptable to a hypothetical purchaser of the business being appraised. Mr. Galasso used a base scenario discount rate of 8 percent for income streams generated by business that existed on the day of the assumed transaction. He used a discount rate of 13 percent for the new business it was assumed would be generated after the transaction. In Scenario 2, the discount rates were reduced by one percentage point, to 7 percent for existing business and 12 percent for new business. For Scenario 3, the discount rates were increased one percentage point over the base scenario rates, to 9 percent for existing business and 14 percent

for new business. (Galasso Appraisal at 18 (Table A), 19 (Table B), Definitions ¶ 16; Galasso Direct at 6:14-15; Galasso Testimony at 119:19-120:8, 157:21-158:2.)

123. In Scenario 4, the assumption about MLR Mr. Galasso used in Scenario 1 was varied to project a more negative impact of ACA. In its most basic form, an MLR is defined as incurred medical costs divided by earned premiums for a defined period of time. In Scenario 4, the assumed MLRs for the individual and small group business segments increased by one percentage point over the MLRs assumed for those segments in Scenario 1. All these MLRs were based on Mr. Galasso's discussions with BCBSMT about its understanding of its marketplace and its competitive position. Mr. Galasso believed the MLR assumptions he used were about as low as could reasonably be assumed for 2013 and 2014 because of concerns about likely negative effects of ACA implementation on MLRs. (Galasso Direct at 6:15-16; Galasso Appraisal at 18 (Table A), 19 (Table B), 25; Galasso Testimony at123:18-125:12.)

124. The higher the assumed MLR the lower the value, and vice versa. MLR assumptions were the biggest driver of value in the Galasso Appraisal. (Galasso Testimony at 127:3-6.)

125. The impact that ACA will have on MLRs beginning in 2014 is uncertain. Several factors suggest it is likely to increase medical costs, at least in the short term, in the individual and small group markets because of the elimination of medical underwriting. Based on his knowledge of the industry and the views of various actuarial organizations, Mr. Galasso concluded that MLRs are likely to be negatively affected in 2014 in the individual and small group markets as a result of an increase in Medical Trend. Medical Trend is the actual and/or expected change in medical claims costs over a defined period of time. Medical Trend is likely to increase in 2014 as people with poor health and pre-existing conditions who have been

uninsured become eligible for health insurance and seek postponed medical care. Increased Medical Trend increases claims costs, which adversely impacts MLR. Mr. Galasso's opinion about the likely effects of ACA on Medical Trend and MLRs was shared by BCBSMT's Chief Actuary, James Spencer, and others. No evidence was presented that supports a conclusion that Mr. Galasso's Medical Trend and MLR assumptions are unduly pessimistic or otherwise unreasonable. (Galasso Appraisal at ¶¶ 13, 23, 32; Hearing Transcript, Vol. III, March 14, 2013 ("Spencer Testimony") at 576:5-577:14, 594:14-18; Burzynski Direct at 12:20-13:12.)

126. For an appraisal date of January 1, 2013, the appraisal cash flow values generated in the four Scenarios in the Galasso Appraisal ranged from a low of $0.1 million to a high of $41.6 million. The values for a June 30, 2012 appraisal date ranged from $0.0 million to $39.5 million. The June 30, 2012 values were calculated as the present value of the January 1, 2013 values. (Galasso Direct at 5:1-10; Galasso Appraisal at 18 (Table A), 19 (Table B); Galasso Testimony at 111:6-15.)

127. Mr. Galasso's initial and preliminary valuation of the BCBSMT cash flows resulted in valuation numbers that were negative. In order to arrive at the final value ranges, Mr. Galasso incorporated certain more positive assumptions that BCBSMT believed were feasible, and that he agreed were within the range of reasonable assumptions. There is no evidence in the record that any of the assumptions Mr. Galasso used inappropriately or unreasonably overstated the projected appraised value of BCBSMT's future contract cash flows. (Galasso Testimony at 138:4-140:10.)

128. Some of the final assumptions used in the Galasso Appraisal, while reasonable, are nonetheless aggressive. For example, the assumption that there would be a 75 percent annual lapse replacement rate in 2018 and beyond increases the appraisal value in a way that many

buyers would reject. This assumption reflects that 75 percent of BCBSMT members or groups that terminate their coverage in a year will be replaced. The discounted value of the replacement business is included in the appraisal of the contracts as of January 1, 2013. In other words, a purchaser at the value calculated in the Galasso Appraisal would be paying BCBSMT a significant amount of money for contracts that the acquirer itself would be responsible for generating years after the acquisition. (Galasso Testimony at 150:10-154:20.)

129. The Galasso Appraisal supports and is consistent with the conclusion that $40.2 million is a fair market value for the Purchased Assets.

C. The Moss-Adams Valuation

130. BCBSMT also retained Calvin Swartley, Senior Manager and member of the Valuation & Litigation Services Group of Moss Adams LLP in Portland, Oregon. Moss-Adams was asked to determine the fair market value of the total surplus of BCBSMT as of June 30, 2012. As part of that analysis, Mr. Swartley determined the fair market value of the total equity of BCBSMT's subsidiary, HeW, and the fair market value of specific assets and liabilities. (Swartley Direct at 2:1-4, 3:2-8.)

131. Mr. Swartley earned a B.S. in Business Administration from Lewis & Clark College and an M.B.A. from Washington University in St. Louis. He is designated as a Chartered Financial Analyst by the CFA Institute and was named an Accredited Senior Appraiser by the American Society of Appraisers. He has been employed by Moss Adams for approximately fifteen years. (Swartley Direct at 2:5-15; Hearing Transcript, Vol. III, March 14, 2013 ("Swartley Testimony") at 470:5-25.)

132. Neither Mr. Swartley nor Moss Adams LLP had ever been retained by BCBSMT or HCSC before they were hired to do the valuation of BCBSMT. Neither BCBSMT nor HCSC

influenced or attempted to influence Mr. Swartley's opinion in any way. (Swartley Direct at 3:11-14, 11:6-12.)

133. Mr. Swartley is qualified to offer an opinion on the fair market value of the total surplus of BCBSMT.

134. Mr. Swartley valued the surplus of BCBSMT at $166.2 million as of June 30, 2012. He determined the value considering the factors identified in Internal Revenue Service Ruling 59-60 for determining fair market value: the price at which property would change hands between a willing buyer and a willing seller. He then considered three valuation approaches: (1) the Income Approach; (2) the Market Approach; and (3) the Asset-Based Approach. (Swartley Direct at 4:9-21.)

D. The Income Approach

135. The Income Approach estimates future returns of the business being valued and discounts them to the valuation date at an appropriate rate of return on investment. The value derived from the Income Approach represents the amount a prudent investor would pay for expected future cash flows based on market rates of return and specific risks of the investment. For the purposes of his Income Approach valuation, Mr. Swartley concluded that a discount rate of 15.1 percent was appropriate. This discount rate reflected a risk premium of 5 percent based on consideration of BCBSMT's operating and financial risks. These risks included BCBSMT's declining and lower than industry average profitability, efficiency and asset utilization, and liquidity. (Moss-Adams Rpt. at 22-24.)

136. Mr. Swartley calculated the present value of the BCBSMT cash flows for a five-year forecast period, and assumed the cash flows would grow at a constant rate into perpetuity to calculate an additional residual value. This resulted in a value of $66.193 million. He then deducted the present value of expected additional capital expenditures and related depreciation

tax savings of $20.842 million to get a total equity value of future cash flows of $45.351 million. (Moss-Adams Rpt. at 24 (Ex. 15).)

137. The last step in the valuation using the Income Approach was to add the fair market value of "non-core assets," defined as assets which could be liquidated without impairing the central operating business of BCBSMT. The fair market value of the non-core assets was determined by Mr. Swartley to be $80.055 million. This resulted in a total surplus value using the Income Approach of $125.406 million. (Moss-Adams Rpt. at 22-24, 56 (Ex. 15), 46 (Ex. 5), 65-66 (Ex. 22); Swartley Direct at 5:14.)

E. The Market Approach

138. A Market Approach utilizes valuation ratios derived from market transactions involving businesses that are similar to the subject business. Mr. Swartley used both a "Public Company Analysis" and a "Merger and Acquisition Analysis" Market Approach. A Public Company Analysis uses stock market transactions involving publically traded companies that are similar in nature to the subject business, while a Merger and Acquisition Analysis uses merger and acquisition transactions involving similar companies. (Moss-Adams Rpt. at 21, 25-30; Swartley Direct at 5:1-5.)

139. Mr. Swartley calculated the surplus value of BCBSMT to be $175.651 million using the Public Company Analysis, and $147.247 million using the Merger and Acquisition Analysis. (Swartley Direct at 5:15-16; Moss-Adams Rpt. at 60 (Ex. 18), 61-62 (Ex. 19).)

F. The Asset-Based Approach

140. The Asset-Based Approach values a business by restating its assets and liabilities from historical cost to fair market value. Mr. Swartley calculated the direct asset-based value of BCBSMT on a "going concern" basis; he did not consider the liquidation value of BCBSMT because liquidation was not considered imminent or probable. Mr. Swartley also valued

BCBSMT using a "Residual Income" Asset-Based Approach. The Residual Income Approach uses the results of the direct Asset-Based Approach and includes the present value of the company's expected future residual income. Mr. Swartley relied on Mr. Galasso's actuarial appraisal of BCBSMT's expected future residual income in his Residual Income Approach valuation. (Moss-Adams Rpt. at 21, 31; Swartley Direct at 5:6-11, 7:7-12.)

141. Mr. Swartley calculated the surplus value of BCBSMT to be $146.557 million using the direct Asset-Based Approach and $164.168 million using the Residual Income Approach. (Swartley Direct at 5:17-18; Moss-Adams Rpt. at 65-66 (Ex. 22); 64 (Ex. 21).)

G. <u>Overall Moss-Adams Valuation</u>

142. The range of values resulting from Mr. Swartley's various analyses was from $125.4 to $175.7 million. Mr. Swartley concluded, based on these various valuation methodologies, that the fair market value of the total surplus of BCBSMT is $166.2 million. He reached that final value number by weighting the results of the various approaches based on the (a) quantity and quality of available data, (b) the valuation function and purpose, (c) the value premise, and (d) the reliability of the analysis. (Swartley Direct at 5:19-6:2; Moss-Adams Rpt. at 39.)

143. The weights Mr. Swartley assigned to the results of various valuation approaches in his analysis were as follows:

Income Approach	5 percent
Market Approach (Public Company Analysis)	35 percent
Residual Income Approach	65 percent

Mr. Swartley assigned no weight to the Merger and Acquisition Analysis because of relative lack of recent transactions for closely similar companies and the difficulties using merger and acquisition data. He assigned no weight to the direct Asset-Based Approach because of significant overlap between that approach and the Residual Income Approach and his belief that the Residual Income Approach better captures future excess earnings in addition to the book value of surplus. (Swartley Direct at 5:12-18, 6:3-21.)

H. The MDS Consulting, LLC, Valuation

144. In addition to the valuation experts retained by BCBSMT, the Attorney General also requested an independent expert opinion regarding the fair market value of BCBSMT. The Attorney General asked MDS Consulting, LLC, to provide the additional independent valuation. Timothy J. Blackmer, a contractor to MDS Consulting, performed the valuation, with input from Phil Dalton, President and CEO of MDS Consulting, about trends in the health care industry. Mr. Blackmer is a Certified Public Accountant and holds several accreditations in business valuation, including Accredited Business Valuation from the American Institute of CPAs, Certified Business Appraiser from the Institute of Business Appraisers, and Accredited Senior Appraiser from the American Society of Appraisers. Mr. Blackmer earned a Master's degree in Business Administration, with an emphasis on Finance, from the University of Nevada. (Direct Testimony of Timothy J. Blackmer on Fair Market Valuation on Behalf of the State of Montana ("Blackmer Direct") at 1-2, 9-10.)

145. Like the experts retained by BCBSMT, Mr. Blackmer did his valuation without regard to the identity of HCSC as the proposed alliance partner so as not to change the standard of value from the required fair market value to investment value. Like Mr. Swartley, Mr. Blackmer used three different approaches as part of his valuation: an Income Approach, a Cost Approach, and a Market Approach. Mr. Blackmer's Income Approach was fundamentally the same as Mr. Swartley's. His Cost Approach was the same as the approach Mr. Swartley denominated the Asset-Based Approach. Mr. Blackmer's Market Approach was substantially the same approach that Mr. Swartley called his "Public Company Analysis" Market Approach.

Mr. Blackmer likewise conducted his valuation using a "going concern" premise, as he concluded that the highest and best use for the income producing assets of BCBSMT is an ongoing business. Thus, the methodologies used by the parties' respective experts were fundamentally the same and appropriate for the valuations being undertaken. (Blackmer Direct at 6, 10-11, 13-14.)

146. Based on his valuation analysis, Mr. Blackmer concluded that the fair market value of all tangible and intangible assets of BCBSMT as of June 30, 2012 was between $182.5 (Cost Approach) and $210.6 million (Income Approach). Applying equal weight to each of his three valuations resulted in a conclusion of total value of $193.8 million. Of this total value, Mr. Blackmer attributed approximately $25 million to the value of various intangibles including the value of the BCBSMT contracts, brand, goodwill and the value of the workforce. (MDS Rpt. at 4, 11, 55; Blackmer Direct at 28, 31, 33, 34.)

147. Among the major differences between the approaches of Messrs. Blackmer and Swartley were some of the assumptions used in their analyses. Mr. Swartley accepted as reasonable BCBSMT Management's projections of operating expenses for 2012-2015: BCBSMT Management believed it had cut expenses as far as they could be cut so that continued improvement was unlikely. Mr. Blackmer assumed significantly lower BCBSMT future operating expenses based on his opinion that Management projections were out of line with historical operating expenses. Mr. Blackmer also disagreed with Management's conclusion that certain "Projects-in-Progress" and certain software licenses were of no fair market value because no potential purchaser could use them; in Mr. Blackmer's opinion, they could have value to some potential purchasers and thus were fairly included in a fair market valuation. The experts also disagreed about the market values of specific items of tangible or real property. Mr.

Blackmer also discounted BCBSMT's Management's projection of necessary capital expenditures that would be required over the operational period for which cash flows were being valued. Mr. Swartley accepted Management's projections as reasonable. (Blackmer Direct at 18-21, 23-25; Swartley Direct at 7:1-6; Swartley Testimony at 5:18-6:13.)

148. Mr. Blackmer also calculated a specific value of $13.4 million for the BCBSMT "Assembled and Trained Workforce," which he opined was not otherwise captured in a Cost (or Asset-Based) Approach. It was Mr. Swartley's opinion that the value of the workforce was in fact captured in the broad residual in the cash-flow valuation. (MDS Rpt. at 4, 44-45; Swartley Testimony at 486:24-487:25.)

149. These differences of opinion account for a large portion of the difference between the Moss-Adams and the MDS Consulting value ranges. They reflect the types of judgments that must be made in connection with any valuation. It is not necessary to determine which assumptions are more appropriate, however, as the range of values calculated by the respective experts are both consistent with a fair market value of the Purchased Assets of $40.2 million.

150. Mr. Blackmer agrees that $40.2 million is a reasonable fair market value for the Purchased Assets. (Hearing Transcript, Vol. III, March 14, 2013 ("Blackmer Testimony") at 509:7-15.)

* * *

From these Findings of Fact and the complete record in this matter, the Hearing Examiner makes the following Conclusions of Law in support of approval of the Applicants' Conversion Transaction:

CONCLUSIONS OF LAW

The Application was properly filed, noticed, and reviewed as required by the Conversion Statute as follows:

1. The Application was filed with the Commissioner with a copy served upon the Attorney General. (Mont. Code Ann. § 50-4-707(1).)

2. The filing of the Application pursuant to the Conversion Statute satisfied the notice requirements of Montana Code Annotated §§ 35-2-609 and 35-2-617. (Mont. Code Ann. § 50-4-704(1)(b).)

3. The Attorney General's review of the Application under the Conversion Statute satisfies the review requirements of the Montana Nonprofit Corporation Act. (Mont. Code Ann. §§ 35-2-609-617, 50-4-715(3).)

4. The Commissioner gave proper public notice of the Application by the internet and by press release. (Mont. Code Ann. § 50-4-709.)

5. The Commissioner made all documents and records in this matter available to the public, except those records containing proprietary or confidential information as defined by law. (Mont. Code Ann. § 50-4-708.)

6. The public hearing was correctly scheduled within 90 days after the Application was filed. (Mont. Code Ann. § 50-4-710.)

7. The public was correctly advised when and how to file written comment and exhibits or make a statement at the public hearing. (Mont. Code Ann. § 50-4-710, -711(2).)

The proposed Conversion Transaction is in the public interest as defined in Montana Code Annotated § 50-4-715 as follows:

8. The fair market value of public assets is preserved and protected in the proposed Conversion Transaction. (Mont. Code Ann. § 50-4-715(2)(a).)

9. The fair market value of public assets is expended or invested with reasonable and prudent consideration of the potential risk of financial loss associated with the proposed Conversion Transaction. (Mont. Code Ann. § 50-4-715(2)(b).)

10. No part of the payment will inure directly or indirectly to an officer, director, or trustee of BCBSMT, to an officer, director, trustee, shareholder, or employee of HCSC, or to any other person that is not a foundation authorized to receive the assets by the Montana Attorney General. (Mont. Code Ann. § 50-4-715(2)(d).)

11. No officer, director, or trustee of BCBSMT receives any immediate or future remuneration as a result of the proposed Conversion Transaction except for the reasonable value of services rendered pursuant to a valid contract between the officer, director, or trustee and BCBSMT. (Mont. Code Ann. § 50-4-715(2)(e).)

The proposed Conversion Transaction is in the public interest as defined in Montana Code Annotated § 50-4-717 as follows:

12. BCBSMT exercised due diligence by deciding to engage in this Conversion Transaction. (Mont. Code Ann. § 50-4-717(2)(a).)

13. BCBSMT exercised due diligence in selecting HCSC as the transferee. (Mont. Code Ann. § 50-4-717(2)(a).)

14. BCBSMT exercised due diligence in negotiating the terms and conditions of the Conversion Transaction. (Mont. Code Ann. §§ 50-4-716 (3), -717(2)(a).)

15. BCBSMT used appropriate expert assistance and procedures in deciding to engage in this Conversion Transaction. (Mont. Code Ann. § 50-4-717(2)(b).)

16. There are no conflicts of interest of BCBSMT or HCSC board members, executives, or experts retained by BCBSMT or HCSC. (Mont. Code Ann. § 50-4-717(2)(c).)

17. There is little likelihood that the Conversion Transaction will create a significant adverse effect on the availability or accessibility of health care services or health insurance coverage in Montana. (Mont. Code Ann. § 50-4-717(2)(d).)

18. The Conversion Transaction will not have an adverse impact on continued access to affordable health care in Montana. (Mont. Code Ann. § 50-4-717(2)(e).)

19. No management contracts are being transferred to HCSC by BCBSMT as part of the Conversion Transaction. (Mont. Code Ann. § 50-4-717(2)(f).)

20. The Conversion Transaction is equitable to the public interest, and to BCBSMT's enrollees, insureds, and certificate holders. (Mont. Code Ann. § 50-4-717(g)(i).)

21. The Conversion Transaction is in compliance with Title 33, chapters 30 and 31. (Mont. Code Ann. 50-4-717(2)(g)(ii).)

22. The Conversion Transaction ensures that HCSC will possess surplus in an amount sufficient to comply with the surplus required under law and provide for the security of BCBSMT's certificate holders and policyholders. (Mont. Code Ann. § 50-4-717(2)(g)(iii).)

23. The Conversion Transaction will not result in inefficient economies of scale. (Mont. Code Ann. § 50-4-717(3)(a).)

24. The Conversion Transaction will not violate any federal or state antitrust laws. (Mont. Code Ann. § 50-4-717(3)(b).)

25. There has been no breach of the Asset Purchase Agreement by BCBSMT that requires payment of money as liquidated damages or otherwise. (Mont. Code Ann. § 50-4-717(4).)

* * *

WHEREFORE, in light of the findings of fact and conclusions of law determined above, the Hearing Examiner hereby recommends that:

(1) the Attorney General approve the Conversion Transaction and Alliance of the Applicants pursuant to Montana Code Annotated § 50-4-715;

(2) the Commissioner approve the Conversion Transaction and Alliance of the Applicants pursuant to Montana Code Annotated § 50-4-717; and

(3) the closing of the Conversion Transaction proceed.

/// ///

Dated: April 19, 2013

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Jacqueline T. Lenmark, KELLER, REYNOLDS, DRAKE, JOHNSON & GILLESPIE, P.C. certify that on April 19, 2013, I served a true and correct copy of the foregoing **APPLICANTS' JOINT PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW (PUBLIC VERSION)**, by e-mail and by mailing it first class postage prepaid to:

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DATED this 19th day of April, 2013

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