**SB 773**

# Department of Legislative Services

Maryland General Assembly
2003 Session

## FISCAL AND POLICY NOTE
**Revised**

Senate Bill 773 (Senator Middleton, *et al.*)

Finance Health and Government Operations

**Study of CareFirst and the Laws Affecting Nonprofit Health Service Plans**

This bill requires the Maryland Insurance Commissioner and the Office of the Attorney General (OAG) to determine whether any conduct identified in MIA No: 2003-02-032 violates any provisions of federal or State law.

The bill takes effect June 1, 2003 and terminates September 30, 2003.

## Fiscal Summary

**State Effect:** The bill's review and reporting requirements could be handled with existing budgeted resources of the Maryland Insurance Administration (MIA) and OAG. No effect on revenues.

**Local Effect:** None.

**Small Business Effect:** None.

## Analysis

**Bill Summary:** The bill requires the Insurance Commissioner to: (1) determine whether any conduct identified in MIA No. 2003-02-032 violates any provisions of the Insurance Article; (2) take any action deemed appropriate in light of the determinations made; (3) report by July 1, 2003 on the determinations made to the board of directors of a nonprofit health service plan and the Governor and the General Assembly; and (4) make recommendations regarding changes to State law that would ensure that the regulatory oversight of nonprofit health service plans is sufficient to protect the public interest and

report those recommendations by July 1, 2003 to the Governor, the General Assembly, and OAG.

OAG must: (1) determine whether any conduct identified in MIA No. 2003-02-032 violates any provision of federal or State civil, criminal, or administrative law, other than those provisions reviewed by the Insurance Commissioner; and (2) report by September 1, 2003 to the Governor and the General Assembly.

**Current Law:** Acquisitions of nonprofit health entities (nonprofit hospitals, health service plans, or HMOs) are governed by statute. An acquisition includes: (1) a sale, lease, transfer, merger, or joint venture that results in the disposal of the assets of a nonprofit health entity to a for-profit corporation, a mutual benefit corporation, or any entity when a substantial and significant portion of a nonprofit health entity's assets are involved; (2) a transfer of ownership, control, responsibility, or governance of a substantial or significant portion of the assets or operations of a nonprofit health entity to any for-profit corporation or mutual benefit corporation; (3) a public offering of stock; or (4) a conversion to a for-profit entity. The appropriate regulating entity cannot approve an acquisition unless it finds the acquisition is in the public interest.

**Background:** On November 20, 2001, CareFirst BlueCross BlueShield announced its intention to convert to a for-profit company and subsequently be acquired by WellPoint Health Networks, Inc. CareFirst is statutorily obligated to file a conversion application with all three jurisdictions to which its charitable assets would inure: Maryland, the District of Columbia, and Delaware. The application was filed with MIA on January 11, 2002. The $1.37 billion purchase price is one indication of the value of the company's charitable assets. Independent valuations have estimated a value between $1.7 billion to $1.8 billion.

The Maryland Insurance Commissioner Steven B. Larsen announced on March 5, 2003 that he had denied the CareFirst BlueCross BlueShield application to convert to a for-profit company and be acquired by WellPoint Health Networks, Inc. The proposed transaction was not in the public interest because of several disqualifying factors. In his order, MIA No: 2003-02-032, *The Consolidated Application for the Conversion of CareFirst, Inc. and CareFirst of Maryland, Inc. to For-Profit Status and the Acquisition of CareFirst, Inc. by WellPoint Health Networks, Inc.*, and accompanying 250-page report, Commissioner Larsen explained his rationale for the decision, including: (1) the auction to sell CareFirst was flawed and did not produce fair market value; (2) the original merger bonuses violated the anti-inurement requirements of the conversion statute; (3) the new, renegotiated "retention bonuses" violated the anti-bonus provision in the conversion statute because they were not compensation for work performed with WellPoint; (4) the board breached its fiduciary obligations in deciding to convert because

it failed to recognize the nonprofit mission of the company to offer insurance at "minimum cost and expense;" (5) the board permitted the use of selection criteria for bidders that largely benefited management, such as the willingness of the buyer to pay the merger incentive, and the role that the CEO would play in the successor organization; (6) although the board appeared to weigh certain factors in the selection process, such as the locations of corporate headquarters, possible job loss, "downside protection," and maintaining current benefit levels for CareFirst employees, on closer scrutiny, these factors appear to have little or no merit; (7) unbeknownst to the board, an attorney who previously represented the CEO in his employment negotiations with the board played a significant role in advising CareFirst management during negotiations with potential bidders; (8) CareFirst's investment bankers were asked by the board to issue an opinion on the "fairness" of WellPoint's purchase price and the bankers' compensation largely depended on the issuance of an opinion that the price they negotiated was fair; and (9) WellPoint did not make available to MIA and its experts pricing and underwriting information that would have permitted a complete "impact analysis."

## Additional Information

**Prior Introductions:** None.

**Cross File:** None.

**Information Source(s):** Maryland Insurance Administration, Office of the Attorney General, Department of Legislative Services

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Analysis by: Susan D. John

Direct Inquiries to:
(410) 946-5510
(301) 970-5510