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OFFICE OF THE COMMISSIONER OF INSURANCE

STATE OF WISCONSIN

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In the Matter of Application

for Conversion of Blue Cross & Blue Shield United of Wisconsin

Case No. 99-C26038

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CLASS I CONTESTED CASE HEARING

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Proceedings had and evidence taken before Connie L. O'Connell, Commissioner of Insurance, on the 10th day of March, 2000, at the Holiday Inn, 3871 East Washington Avenue, Madison, Wisconsin, commencing at 9:05 a.m.

APPEARANCES:

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APPEARANCES: Cont'd

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by MR. STEPHEN E. BABLITCH, on behalf of Blue Cross.

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Milwaukee, Wisconsin, 53203
by MR. JOSEPH C. BRANCH, MR. BARTHOLOMEW F. REUTER and
MR. THOMAS M. ROSE, on behalf of Blue Cross.

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JR., on behalf of ABC for Health, Wisconsin AARP, and
Wisconsin Coalition for Advocacy.

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by MS. VALERIE L. BAILEY-RIHN, on behalf of the Medical College of Wisconsin.

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by MS. HELEN H. MADSEN, on behalf of UW-Madison Medical School.

I N D E X

E X H I B I T S

None

(The original exhibits were retained by Commissioner O’Connell.)

(The original transcript was delivered to Cmmissioner O’Connell.)

P R O C E E D I N G S

COMMISSIONER O'CONNELL: Good morning. I'm Connie O'Connell, Commissioner of Insurance residing over case number 99-C26038 concerning Blue Cross & Blue Shield United of Wisconsin's application for conversion. This hearing is being transcribed by Halma-Jilek.

The purpose of the application for conversion is to permit Blue Cross & Blue Shield United of Wisconsin to convert from a nonprofit service insurance corporation to a stock insurance corporation in accordance with Sections 613.75 and 611.76 Wisconsin Statutes.

This hearing is being held as a Class I contested cases hearing in accordance with Chapter 227 Statutes and Section INS 5.39(2) Wisconsin Administrative Code. This is a continuance of the contested case hearing that commenced on November 29th, 1999 and continued on February 25th, 2000. Today's hearing is being held at the Holiday Inn, Madison, Wisconsin at 9 a.m. on March 10th, 2000.

Will the participants please state for the record the name of your organization and your legal representative. Please speak into

the microphones and speak only at one time.

MR. BABLITCH: Blue Cross Blue Shield United of Wisconsin appears by its general counsel Stephen Bablitch and outside lawyers Foley & Lardner represented by Joe Branch, Tom Rose and Bart Reuter.

MS. BAILEY-RIHN: The Medical College of Wisconsin appears by its counsel Quarles & Brady, Valerie L. Bailey-Rihn.

MS. MADSEN: The UW Medical School appears by Helen Madsen, counsel.

MR. SPITZER-RESNICK: The coalition of consumer groups, which includes Wisconsin Coalition for Advocacy, AARP, and ABC for Health is represented by Jeffrey Spitzer-Resnick, myself, and Wisconsin Coalition for Advocacy, Robert Peterson from ABC for Health and Wade Williams for ABC for Health.

COMMISSIONER O'CONNELL: As I said in the prehearing memorandum, I will govern this hearing to exclude or limit a line of inquiry or testimony that repeats what was -- what was or could have been offered at the public hearing that relates to areas that are already fully developed in the record of the proceeding, that

is argumentative, or that relates to proprietary or trade secret material that is more appropriately dealt with by the office directly. The scope of questioning will be limited to the scope identified in the prehearing memorandum.

I will also limit questioning to ensure that the hearing proceeds on a timely basis. The hearing today is scheduled to conclude at 4 o'clock p.m. with a half hour break at approximately noon.

The Coalition is allocated four-and-a half hours to present its case. The medical schools are allocated two hours. You should plan your questioning within those time limits. Please also remember that in fairness to the witnesses, I will permit only one attorney from each movant or applicant or examine any one witness.

Now, Mr. Peterson or Mr. Resnick, who will be calling your first witness?

MR. PETERSON: Well, I'd like to make a brief opening statement and then call Thomas Hefty as a witness.

Good morning. On behalf of the Consumer Coalition, ABC for Health, AARP,

Wisconsin Advocacy Coalition, we're grateful for this opportunity to present additional information to the Commissioner and to the public.

As you know, we've expressed our concerns about the conversion and the proposed designation of the two medical schools as the recipients of the funds of the converted organization.

The plan proposed by nonprofit Blue Cross Blue Shield of Wisconsin to convert to a for-profit corporation we believe is not in the public's best interest. Under the proposal, Blue Cross Blue Shield United of Wisconsin would move its initial stock into a new limited life foundation which in turn would funnel proceeds from a stock sale into Wisconsin's two medical schools.

While officials from the two medical schools may be thrilled about this potential financial windfall, this plan does not distribute the public's assets fairly. It's important to remember that these -- that the stock is not a gift from the company. These nonprofit assets belong to the people of

Wisconsin.

If the Commissioner of Insurance allows Blue Cross Blue Shield to abandon its nonprofit mission, the law requires the company to hand over its full value to a charitable organization dedicated to supporting the historic mission of the nonprofit insurer.

Since Blue Cross Blue Shield United of Wisconsin was originally established in 1939 to make low cost health care accessible on a nonprofit basis, passing the public’s money to the medical schools to support research and education would fall well short of this historic charitable mission.

For decades the public paid premiums in to Blue Cross Blue Shield United of Wisconsin and supported it with a variety of tax breaks. As a result, the public should be given an ongoing role in helping to determine how the foundation assets are spent.

Unfortunately, executives of Blue Cross Blue Shield United of Wisconsin have usurped the public’s role by announcing its unilateral decision to turn over all the funds to the medical schools.

Wisconsin should take cues from other states that have handled conversions and create a publicly accountable foundation that can serve the public health needs of many citizens. The foundation created through the conversion must be truly independent from the company and governed by diverse group of community health leaders empowered to determine the best use of the foundation's endowment.

Under the original conversion plan Blue Cross Blue Shield United of Wisconsin and the medical schools would hand pick the directors of the foundation and have complete control over its operation. This is simply unacceptable to our Coalition.

The Blue Cross Blue Shield United of Wisconsin conversion ruling will be the most important and far-reaching decision that Commissioner O'Connell will make during her tenure as Insurance Commissioner. We are impressed at the way she has handled the conversion in a fair and open manner and has welcomed participation by the public and consumer groups. Ultimately, she must ensure that a new foundation is structured in a way

that will make it accountable for the public and not individual or corporate interests.

Now we'd like to call Thomas Hefty as our first witness.

THOMAS HEFTY, called as a witness herein by the Coalition, after having been first duly sworn, was examined and testified as follows:

COMMISSIONER O'CONNELL:

Mr. Peterson, you may begin.

EXAMINATION

BY MR. PETERSON:

Q Good morning. Would you state your full name for the record?

A Thomas R. Hefty.

Q And when were you hired at Blue Cross Blue Shield?

A I was hired as General Counsel in July of 1982.

Q And what was your previous occupation?

A I was a Deputy Commissioner of Insurance for the State of Wisconsin.

Q And how long did you work at the Insurance Commissioner's Office?

A I believe three years.

Q So that would be from 1979 was it about when you

started?
A Yes.
Q Do you remember about when in ’79?
A I recall summer, so June or July of 1979.
Q And what was your chief area of responsibility at the Insurance Commissioner’s Office?
A That’s a long time ago. It was at various times overseeing legislative matters and at other times overseeing the regulatory side, the enforcement side of the office.
Q Did you have an opportunity during that time to regulate the Blue Cross Blue Shield plan as -- during the new period as Deputy Commissioner?
A Yes. The Insurance Commissioner’s Office regulates every insurer in the state.
Q Were you involved during the time period that Blue Cross & Blue Shield became a single organization?
A Only at the end of that transaction. It had begun under the earlier administration when Hal Wilde was Commissioner of Insurance somewhere in probably 1977, ’78.
Q Do you remember your involvement in that transaction?
A Not really. The Attorney General was involved

at that time and had been involved under Commissioner Wilde, and I remember the merger was approved in 1979 or 1980.

Q So it was approved after you were Deputy Commissioner of Insurance?

A Yes.

Q Okay. When did you become the Chief Executive Officer at Blue Cross Blue Shield?

A August of 1986.

Q And you were hired by the board of directors?

A Yes.

Q And who did you replace?

A Ed Edwards.

Q And did you bring in a new management team at that time to Blue Cross Blue Shield?

A Some, but it was a real mixture of -- of promotions from inside the company in terms of continuing executives and some new ones.

Q Do you remember some of the people that you brought in as a part of the new management team?

A The only notable one that I can recall at this time from outside the company would have been Jeff Knoll, who was the Chief Actuary.

Q So you hired him after you were -- you were named CEO of Blue Cross Blue Shield?

A Yes.
Q That was one of your initial hires, okay. How would you describe the financial condition of Blue Cross Blue Shield when you took over in 1986?
A At that time the company was below the minimum capital guidelines for the State of Wisconsin and it had lost over $80 million in the preceding four or five years.
Q Now, at that point had you already created United Wisconsin Services as a -- a for-profit wholly-owned subsidiary?
A The holding company United Wisconsin Services were created on January 1, I believe, of 1983. The subsidiaries within that go as far back as 1959 when the predecessor of United Wisconsin Insurance Company was created. Its original name was the Health Insurance Corporation. I think that was 1959.
Q So as the General Counsel you were quite involved in the creation of that holding company?
A Yes.
Q During the creation of that holding company were concerns raised about the possible mixture of

nonprofit and the for-profit mission?

A I don’t remember in my time as a competitor of Blue Cross, as a regulator, or at that time any discussion at all of Blue Cross structure. It had been taxable in the state since 1972.

Q But was your -- was your opinion then at that point since it was taxable it was no longer a nonprofit organization?

A I don’t think the issue ever came up.

Q Okay. So the issue didn’t come up over your role as -- as reviewing it. You didn’t feel that the issue came up in terms of concerns about the possible conflict between a nonprofit corporation and a holding company that was a for-profit institution?

A I think I said earlier the subsidiaries had existed from 1959 on, and in 1959 I was in sixth grade, and so it had not been an issue since long before that.

Q My question wasn’t whether they had existed previously. My question was were there concerns about the distinct mission perhaps of the nonprofit arm and the -- the holding company?

A I think I said earlier the issue never came up.

Q So there were no concerns?

A I don’t -- All I can say is the issue never came up either inside or outside the company.
Q Okay.
A Again, the subsidiaries had existed for 20 years.
Q What’s your understanding of the history of the predecessor organization to Blue Cross Blue Shield United of Wisconsin? And by that I mean Associated Hospital Services created in 1939 and Surgical Care in 1941.
A Well, my understanding sort of starts with competing with them in the -- the mid 1970’s, and -- and they competed as a regular health insurer in the State of Wisconsin. Beyond that, I have no personal knowledge other than -- than sort of published history.
Q So as -- as in your role as General Counsel or as Chief Executive Officer you did not have the opportunity to review the original mission of the charitable organization that was created in 1939?
A I think I said earlier it never came up.
Q So you didn’t review it?
A It never came up.
Q Right, it didn’t come up. So I’m trying to get

to if it didn't come up, then you didn't review it. So it's just a simple yes or no. You didn't review it.

A It never came up and I did not review it.

MR. PETERSON: Okay. Well, I think the record should reflect that, you know, Mr. Hefty is not answering the question that I'm asking him.

MR. BABLITCH: I'd object to that. He answered it fully the record will reflect.

MR. PETERSON: I asked for a yes or no answer.

COMMISSIONER O'CONNELL: Could you read back the last response from Mr. Hefty?

MR. BABLITCH: If he doesn't like it, that's not the witness's problem.

BY MR. PETERSON:

Q We'll just move on. That's fine. We can move forward. So let's see now. You described the financial situation in 1986 when you took over as CEO as being quite dire. Those are my words, but I'm just characterizing what you said. Is that accurate?

A The company was below the minimum capital guidelines.

Q What changes did you implement as CEO to improve the financial situation at Blue Cross Blue Shield during that time initially?

A In terms of business, I decentralized the company. Blue Cross had focused from somewhere in the late 1970's to mid 1980's at the large groups self-insured processing principally, in Milwaukee. They were losing significant amounts of money in that self-insured business, and the company's operating expenses exceeded the fees that they were charging for processing those large accounts. They were viewed as prestige accounts, but they were very unprofitable.

I decentralized the company with regional offices around the state providing local service serving a -- a broader mix of customers, and also reduced expenses in terms of -- of everyone's pay at that time and replaced it with a profit sharing plan for all employees.

And the third piece was to continue diversifying the product offering of Blue Cross and its subsidiaries because the subsidiaries had been profitable, in order to balance the company's financial situation. So there were

really three; decentralize, reduce expenses, and diversify the mix of products.

Q What were the -- What were the different -- I mean you talk about diversifying the product line. What types of product lines were developed or how were they diversified specifically?

A The -- The company had a life insurance subsidiary at that time then called United Wisconsin Life Insurance Company. It had a casualty insurance subsidiary, the previous Health Insurance Corporation, which had been renamed United Wisconsin Insurance Company. The company created or started in that time United Wisconsin Pro-Services that sells software and electronic clearing house services, and we began looking at things in again subsidiaries using the -- the United Wisconsin Insurance Company of offering worker’s compensation insurance in the state. That may not be a complete list, but --

Q Were any concerns raised during this period by the National Association over your use of the Blue Cross Blue Shield trademark?

A We were very careful to look at the National Association rules in terms of -- of the use of

subsidiaries, the mixture of the Blue Cross & Blue Shield logos with other products, and in general the rules at that time required that those activities be conducted in separate subsidiaries and under separate names. So it was not possible to offer those in the corporation Blue Cross & Blue Shield United of Wisconsin.

Q In terms of the creation of these -- the holding company and the subsidiaries and the diversified product line, there were transfers -- Well, let me rephrase that. How were funds transferred between the nonprofit Blue Cross Blue Shield and the -- the holding company? And by that I'm asking what type of structures were in place to govern those transfers from a nonprofit to the for-profit subsidiaries?

A Well, but the transactions that you -- I know you questioned Gail Hanson earlier, who was our treasurer who handled those transactions, and they were done on an arm's length basis, so to speak.

They were investments for Blue Cross and they were approved by the appropriate board and committee and submitted under the holding

company rules to the Insurance Commissioner.

Q Were there concerns expressed to you by board members or by other senior management about the -- about those transfers between the -- the for-profit and the holding company at any time during that period?

A There were no concerns expressed. We took great care both as a management team, as a board, to make certain that they were appropriate, and -- and periodically the board would either have the outside audit firm or an outside law firm review them in addition to the regular reviews to make certain that they were appropriate legal and fair because in addition to the activities already mentioned, Blue Cross and its United Government Services subsidiary are large government contractors, and those have special rules on cost allocations and fairness of transactions. And so the company's always taken great care to assure that transactions were appropriate.

Q Could you tell us who your auditors were at that time and who your legal counsel was at that time? I'm not talking about general counsel. Your outside law firm.

A Arthur Young, which became Ernst & Young, were the outside auditors for the entire period. Periodically other outside audit firms were used for special projects and reviews. Again, that doublechecking to make certain the transactions were appropriate.

And during that period of time the law firms involved would have been Foley & Lardner, Michael, Best & Friedrich, or Whyte & Hirschboeck, depending on the period of time.

Q Now, the management of these -- of United Wisconsin Services and Blue Cross Blue Shield, I'd like to develop a line of questions along that. You served as the Chief Executive Officer of both of those organizations; isn't that correct?

A Yes, I did.

Q Could you explain how the overlapping responsibilities between those two organizations were handled by you and what direction you were given by your board of directors in terms of dealing with potential conflicts?

A Well, first of all, the structure was largely dictated by insurance law and the Blue Cross Blue Shield Association rules. As I mentioned,

a number of the other activities were not permitted under either licensing requirements of the Insurance Commissioner or the Blue Cross Association rules.

For example, Blue Cross cannot sell worker's compensation insurance. It cannot sell directly life insurance. And so the -- the different corporations were required either by state regulation or the Blue Cross Association rules.

In terms of -- of the activities, you know, the goal was to grow the entire enterprise. Blue Cross at one time owned 100 percent of United Wisconsin Services. It's owned 80 percent. It owned 60 percent. At a low point I think it owned 38 percent, and now it owns 47 percent. And so the United Wisconsin Services subsidiaries were major assets of Blue Cross & Blue Shield, and care was taken each time to ascertain that the transactions were fair, and cost allocations were reviewed regularly and audited regularly not only by the Insurance Commissioner, but by the federal government because of the -- as I indicated, we're a large federal contractor.

Q The Blue Cross Blue Shield National Association rules require independence. How would you say this was achieved?

A The board of directors acted separately and again the transactions were handled in a way and again audited by the various state and federal agencies in a way to be appropriate and fair.

And I think if you look at those audits or if you look at the report of the appraisal committee and the outside advisor to the Commissioner, they were not only appropriate, they created great value for Blue Cross Blue Shield United.

Q Okay. When you were hired as CEO who were the members of the board of directors of both companies at that time, if you can recall?

A I cannot recall. They are matter of public record at the Insurance Commissioner’s Office.

Q But -- But there were members of the board on both companies that were the same.

A At that time, yes. In fact, several of the subsidiaries, United Wisconsin Services subsidiaries, had outside board members as well.

Q But did that raise concerns in terms of potential conflicts of having a board structure

of both organizations being very similar?

A I don't think it was a matter of concern. Care was always taken that the transactions were appropriate. They were audited, they had been reviewed several times, and the audits are all of public record.

Q One of the reports that we reviewed from your investment banking firm that conducted the initial evaluation of Blue Cross Blue Shield, DLJ, indicated that there were concerns over perceived conflicts of interest due to the overlapping boards. That recommendation was made to you as part of your filing with the Insurance Commissioner.

What steps did your board take in terms of addressing these perceived conflicts of interest?

A Well, they had taken steps from the beginning to again make sure the costs were allocated properly, value was created, and the transactions were appropriate.

I think the filing before the Commissioner of the conversion was directed at simply finding the organization, giving it more flexibility, and giving it capital resources to

continue to grow and -- and be successful, but I don't think there is anything beyond that.

Q But there were perceived conflicts of interest as pointed out by your -- your investment banking firm.

A I don't know what specifically they were speaking of. I've frequently said if I have a good idea in the morning when I get up, who do I give it to?

Q Let's talk about that. How do you deal with your role as CEO of both organizations? Do you have separate offices? Do you wear a different suit on one day and a different suit on the next day?

A Gray and gray. I think historically the Blue Cross Association rules and the separation required by corporate charities answered those questions. In other words, life insurance, worker's compensation and the like. And originally, HMO coverage had totally separate corporate structures. You'll find a separate statute actually on the subject from traditional health insurance coverage. So that's -- that division was answered by the Blue Cross Association rules and by state laws.

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Going forward, and I think one of the -- the sort of forward-looking ideas of the board at proposing this transaction was the fact that the lines of health coverage are likely to blur in the future. At one time an HMO was a pure HMO. An indemnity was a pure indemnity plan. And going forward, the variety of PPO and point of service and modified point of service plans blur that line.

And so I think the board by proposing this transaction was really preparing for what's going on in the health care industry.

Q So in other words, the -- the line between the nonprofit and the for-profit and you in those -- in both of those roles is a blurry line. There really isn't --

A No, it isn't a blurry line, but I said the products have changed, and going forward that issue of -- of instead of having this is a pure HMO, state law requires it to be in a separate corporation. The Blue Cross Association rules require it to be in a separation. That was a clear line.

As the products evolve today, the line is less clear and the rules are less clear

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in terms of -- of the state law. What's a point

of service product? Who can offer a point of service product? And those rules are less clear. And so the board in proposing the conversion really cleans up the corporate structure, gives the company flexibility, and gives it access to capital to grow.

Q I think that, you know, the -- that the distinction between the nonprofit and the for-profit arm from a public's perspective is something that is -- raises concern.

I guess my question to you is what has the board done and what has the organization done to try and address misconceptions of the public between the for-profit arm and the nonprofit arm?

A I think I stated earlier, in my time in the industry going back to the mid 1970's as a competitor, as a regulator, and executive, because the company was taxable already and because it had subsidiaries since 1959, the issue has never come up. Only recently have you raised it and I don't know where you were in 1959.

Q I was born that year.

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A Oh. So this issue has existed since the year you were born.

Q The -- Okay. Let me go with another -- another

question then. The issue has been around since 1959, but what about the original charitable mission since 1939 that was created?

A I can't tell you anything about that other than it has not come up in my time in 25 years.

Q So when this issue was first raised by the Consumer Coalition and by Consumer's Union and folks at Community Catalyst, were you surprised by that, by the -- the early history of Blue Cross Blue Shield and the organization, the previous organizations?

A I wasn't surprised by the early history, but something that 60 years ago that changed 25 years ago, it's -- it was hard to understand.

I think the confusion on some people's part is understandable because in other states Blue Cross maintained there tax exemption all the way to the date they converted to a stockholder-owned corporation. And so you had very present day tax advantages and -- and restrictive laws. That has not been the case in Wisconsin for over 25 years.

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Q The -- The -- Just a couple more questions on the nonprofit/for-profit distinction. In terms of the -- sort of the original charitable mission, which we've sort of brought to the attention of the regulators and to the folks at Blue Cross Blue Shield, does that original creation of Blue Cross Blue Shield in 1939 or the Associated Hospital Group, does that have an impact on how you view the nonprofit Blue Cross Blue Shield today? Has that had any influence on your impression of the organization today?

A I really can't make any comment on it. I have no personal experience with it. It's not existed in my lifetime in the business. And I think the confusion is those who look at the other states which had tax exemptions until the date they converted to a stockholder-owned company, those are very different situations than exist in Wisconsin.

Q Well, you know, you point to other states, and we know that there have been conversions that have occurred across the country for a number of years. So in terms of you're not being aware of the issue in Wisconsin of -- in terms of some of the original purposes of Blue Cross Blue Shield

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when it was created, were you aware of -- of

litigation and action that was occurring in other states, for example, in California, when that Blue plan was converting?

A Generally, yes.

Q But in terms of the specifics of the conversion and the examination of its original charitable mission, that wasn't something that you spent a lot of time with?

A They have a separate state law. They have a separation between health care regulation and insurance regulation in California, and California was one of those which tried to maintain its tax exemption right up to the date of conversion.

And again, the -- the tax exemption in Wisconsin was first addressed in 1972 and -- and so long ago that I think the facts and circumstances are entirely different here.

Q So your testimony today then is that during your tenure as Chief Executive Officer, and I'm talking wearing your Blue Cross Blue Shield United Wisconsin hat, you were unaware of the original charitable mission of Blue Cross Blue Shield when it started in 1939?

A I early on, in order to focus employees on improving the company, put in a very well-publicized profit sharing plan that rewarded every employee for both profitability and customer satisfaction, and -- and it was all over the newspapers and no one raised the issue. I mean if there was any public concern about nonprofit, we had a well-publicized profit sharing program for all employees. No one contacted me publicly or -- or any regulator at the time.

Q Was that profit sharing plan reviewed by the regulators?

A I assume that it was in terms of -- of their regular examinations. I can't tell you specifically, but I can tell you that the Milwaukee newspapers at the time both publicized it very widely with headlines, so I suspect that knowledge was widespread.

Q I'm sorry. Excuse me for interrupting you. But basically then, I think that what I'm -- what I'm hearing from you is that Blue Cross Blue Shield was acting in ways that a for-profit organization would by having a profit sharing plan. It gives an impression that it's a

profit-making entity and not under the normal structures of a nonprofit as most people in the public would understand it to be.

A You make a distinction. I think the business distinction is if you're a taxable corporation like any other business you compete like any other business whether you're a nonstock, a mutual, or a stockholder-owned company. And -- And so Wisconsin relies on a competitive market and -- and Blue Cross competed in that very competitive world.

Q Were there concerns raised by -- by your board of either organization over private inurement?

A Again, the board takes care to make sure that the transactions are appropriate. They have outside law firms, outside compensation advisors, outside auditors, to make certain that the transactions are appropriate.

Q Okay. We've talked about the -- the DLJ, your investment banking concerns over perceived conflicts of interest. I'd like to move on now to an explanation from you of the -- the compensation of and performance incentives that senior management receive at Blue Cross Blue Shield and United Wisconsin Services.

Could you describe to me the -- how the compensation plans are put together and incentive plans are determined?

A Both boards employ an outside advisor, Hewitt & Associates, on compensation matters, and the current plan for all employees is a base salary with a profit sharing plan, which includes customer satisfaction measures.

At the management level there is an additional annual management incentive based on their targets or the -- their managers or supervisors or executives or -- or the board's review of their performance, and then at the executive level there are stock options or stock appreciation rights today.

That is simpler than it has been over the past 14 years. Actually, 18 years. There have been various plans that have come and gone of long-term incentives in addition to those three core elements; base profit sharing, annual incentives, and -- and then stock appreciation rights or stock options.

Q What type of stock options within the last six months have senior management at Blue Cross Blue Shield or United Wisconsin Services received?

A Stock options are awarded to new executives upon joining the company and they're awarded annually, generally at the beginning of the year, and an award was given this year by the compensation committees for both boards.

Q Could you give us specifics on the size of those awards this year?

A I can tell you mine and I think I can tell you generally the other awards. I was awarded roughly 140,000 options, the same number as the previous year in terms of number of option shares, and those options are always given at market. You'll see some firms that give discounted options, and our board does not reprice options and they do not grant options below the current market price.

Q What -- How many shares of stock do you currently own?

A Do I currently own? I can't tell you precisely. Perhaps 30,000. That information is publicly available in -- on the SEC, so you get it publicly. It's not something I keep track of.

Q Do you know what -- If you exercised all of your stock options, what percentage of the company you would own?

A Oh, less than one percent.
Q And there's a requirement by National Association rules that no one can own more than -- an individual investor could own more than five percent of a Blue Cross Blue Shield plan?
A I'm not aware of that, but I'll take your word for it.
Q That was my understanding. Let's talk about the decision to convert. And can you explain to us the -- the decision-making process that went into that that you went through and your board went through in terms of deciding to convert to a for-profit entity?
A I didn't go through it. The board appointed a special committee in December of 1998, I believe, to look at all the different structures. The spinoff of American Medical Security was completed in the fall of 1998, and I think the board viewed it as appropriate to look at the structure of the company and alternatives, and they appointed a special committee to do that and I did not participate in the committee other than on request to provide information.

Q In your testimony before the Commissioner on November 29th you indicated some reasons for the conversion, that it was a changing business marketplace. That -- That was really one of the precipitating factors in terms of -- of moving to a for-profit. Is that your testimony today? I'm characterizing what you said, but in summary your basic statement was that it was a dynamic changing marketplace and your organization had to convert to be competitive in that marketplace and access capital markets.

A The competitors today in Wisconsin are largely tax-exempt funded organizations that have either tax-exempt earning streams or access to tax-exempt bond proceeds or are large national competitors, much larger than Blue Cross or any of our individual companies.

And so I think one of the goals was to provide flexibility in terms of the changing marketplace. Things like Internet marketing are expensive, and at the same time participate in the consolidation, if you will, of health plans that is going on nationally. The world is changed rapidly, the Blue Cross world is changing rapidly, and I think our board wanted

again to be structured for the future.

Q Was your board or were you concerned about the activities of the Consumer Coalition and Consumer's Union in terms of meetings with the Insurance Commissioner's Office or with the Justice Department in terms of questions being raised about transfers of assets, cross-fertilized board of directors and potential breaches of fiduciary duty?

A No. As I indicated, going back as long as I have been at the company the board has taken great care to make certain that the transactions were fair and appropriate and that the cost allocations were fair and accurate. And they have periodically retained special outside counsel or special auditors in addition to their direction to management and regular auditors to make certain that those were accurate and fair transactions. And I believe the last time that was done was 1997, in terms of a special review.

And so there was not any -- any particular concern, other than I think everyone felt good that the board had taken care over the years to make certain that the transactions were appropriate.

Q So you're -- you're calling it there weren't particular concerns. Was there discussion of the involvement of consumer groups in reviewing transactions that had occurred throughout the -- the -- the '80's and early '90's by Blue Cross Blue Shield?

A They were advised of that fact and again, more in the sense of the periodic special reviews that they had done over the -- the prior decade. The special review was not done every year, but it was done every several years.

Q I'd just like to show you an exhibit that we've marked Exhibit J50. This exhibit is minutes of the special board meeting of December 9th, 1998 and special report to the board made by Mr. Tom Hefty.

And in that report I direct your attention to the -- the first full paragraph, middle of the paragraph where the minutes reflect that there were discussions of the Consumer's Union contacting Wisconsin officials and legal media regarding the allegations of conflicts of interest between Blue Cross Blue Shield United of Wisconsin and United Wisconsin Services, Inc. And question had been raised

regarding the issue whether Blue Cross Blue Shield United of Wisconsin itself is a charitable trust.

So that issue, based on these board minutes, did come up at your December 9th meeting and apparently there were some discussions related to that fact.

A I think that’s what I said.

Q I think that -- Well, that’s fine. So what was the -- You appointed a special committee to review the process of conversion and they provided review and analysis and came up with a plan to convert. How was that plan presented to the board?

A The board selected a special committee. It was -- The board consisted of board members who had some special expertise in -- in terms of public policy as well as health care policy.

Jim Hickman, the former Dean of the Business School at UW-Madison. Jim has served as the National Actuarial Society chairman and is also, I believe, chair of one of the National Church Pension and Health Care boards. Janet Steiger, former foreman of the Federal Trade Commission.

Ken Viste, past head of the State Medical Society, active on the American Medical Association, as well as the State Medical Society foundation. Ken also serves on the Physician Payment Review commission for the federal government, and then Michael Joyce, who heads the Bradley foundation, which is the largest private foundation in the state, that was created by the sale of the Allen-Bradley Corporation in Milwaukee.

So they selected four directors with particular expertise in not only health care, but public policy as well as foundation matters.

Q Did you also review what their participation was in -- I mean -- Let me strike that. Did you examine whether or not they served on both boards of -- by that I mean United Wisconsin Services and any of the for-profit subsidiaries and the nonprofit Blue Cross Blue Shield board?

A That issue was discussed, which is why Jim Hickman, who was the only common director to United Wisconsin Services and Blue Cross, was there. I was not at the meeting, but I understand that he would note that fact and remind the other directors of that on certain

discussions so that the three Blue Cross-only directors were always aware of that fact, but given his expertise as an actuary, as a -- a nationally-recognized actuary and former Dean of the Business School, I think his expertise was -- was viewed as valuable by the other directors.

Q So the board at that time felt it was important that there not be perceived conflicts of interest in the special committee?

A I think I testified earlier the board has always taken great care to make certain that --

Q I'm just asking about this specific instant because what we're learning is that the board takes care to make sure that -- in terms of this special committee that the members of the review were members of the nonprofit board. Only James Hickman was on both boards because of his special expertise.

A Well, there are only three directors on both boards; Jim Hickman, Jim Forbes, and myself.

Q That hasn't always been the case, has it?

A It's varied over time depending on Blue Cross's ownership of United Wisconsin Services. It has tended to vary as Blue Cross's ownership has

dropped.

Q Now, the decision of the special committee was made at the June 2nd board meeting; isn't that correct?

A Yes.

Q Now, those discussions -- Did Tim Cullen of your staff participate in that meeting?

A I don't recall specifically, but he would generally be at the meetings.

Q And there was discussion of the plan to convert and publicity related to that plan to convert?

A Again, I don't recall that that came up at the board meeting, but it may have.

Q We have another exhibit. It's Exhibit J51. It's the second page of that where it discusses the point that Mr. Cullen briefly commented on several planned public relations activities related to the public announcement of the stock conversion.

A Yes.

Q What were those public relations activities?

A Well, there was an announcement planned of the plan to convert and to contribute 100 percent of the value of the company to public health through the two medical schools.

Q Was there discussions of communications that had been made with the Attorney General's office and with the Governor's office to participate in that event?
A I don't recall specifically, but I believe it was known that both of them would be participating.
Q Was there discussion of a joint letter to be sent by Senator Chuck Chvala and representative Scott Jensen to the Commissioner's office to try and expedite this process and to move it along quickly?
A I don't think so because I don't even think that was known at the time.
Q Was there discussion of participation in the med schools in that event?
A Yes. I mean they had been contacted to find out whether they would be willing to serve that role in terms of -- of conveying the funds for public research, teaching, and outreach for the entire State of Wisconsin.
Q When were they notified of the plan of the special committee and the board? And by them I mean the med schools.
A I don't recall specifically. Sometime in the

spring after the special committee had reached a consensus on the direction they were contacted to find out whether they would in fact be willing to do that.

Q Were the dollars characterized as a gift to the two med schools at that time?

A I don’t remember specifically. It was the use of the proceeds, the full value of Blue Cross, for the three areas that I mentioned.

Q Do you consider the -- the proceeds to be a gift today?

A I think it was a voluntary act by the board to contribute 100 percent of the value of Blue Cross, something that has not been done in other states before their decision and has not been done since their decision.

In other states the Blue board has tried to negotiate, if you will, an agreed dollar amount generally relative to the prior tax advantages, and so you see numbers $45 million, $65 million, both before the decision by the Wisconsin board of directors and since the announcement, and our board committed 100 percent of the value in -- in the proposal before the Commissioner.

Q And are you familiar with the WellPoint conversion in California?
A Again, generally.
Q Are you aware of the value of that, what that conversion netted the foundation?
A Oh, it was a significant amount of money. I don't know if it was 2 or $3 billion, but they tried to avoid any substantial contribution at all in their original transaction even though they were tax exempt right up to the day before the conversion.

And I think our board again made the right decision in committing 100 percent of the value even though the Wisconsin tax advantages ended many years ago.

Q What were the reasons that were given by the special committee to designate the two med schools as the recipients of the foundation or of the -- the assets of the company?
A Again, I did not participate in their discussion of how they arrived either at 100 percent or at the two med schools. As I have heard it expressed since then, they did not want the money, I'll use my term, frittered away in extra administrative costs in terms of administration,

and they used the California example where one of the beneficiaries of the foundation was apparently the International Tofu foundation, because in California, maybe in Wisconsin, or at least in Madison, tofu is viewed as a health food, and -- and so their contribution to that was viewed as frivolous even though some groups might view that as a worthwhile expenditure.

So they wanted lower administrative costs, they wanted a focus on -- on the overall health of the state, they wanted something that was flexible in terms of research, teaching, and public health, and they wanted a state-wide effort, recognizing that the two medical schools were in the southern half of the state.

Q Were concerns ever raised about administrative expenses that might be incurred by the medical schools? For example, looking at what their administrative overhead expenses are or indirect expense rates are at those institutions?

A Again, I don’t know what they looked at specifically. I think their view was that the two schools every year, since they both receive both private and public funding, go through the allocation process of what portion of the budget

goes to research, what portion goes to teaching, what portion goes to community service, and so the belief was that that infrastructure existed because it goes on every year in those institutions and it has gone on for, I guess, a century in both institutions. I do not know if they look specifically at it, but they relied on the same institutions that the people of Wisconsin have relied on for 100 years.

Q So let me try and -- and understand. The impression is that the board looked at the two med schools as existing institutions and therefore there wouldn't be administrative expenses related to any type of a start up of a new organization, but that they did not necessarily look at costs associated with the two medical schools in administering those funds.

A Again, I do not know precisely what they looked at. I mentioned the expertise on the special committee. You have Ken Viste, who's involved nationally on health care public policy matters. You have Jim Hickman, the Dean of the Business School, serves on the National Church Health and Pension board. You have Janet Steiger, and --

and most importantly Michael Joyce, who runs the largest private foundation in the State of Wisconsin. I assume they were not simply taking their sort of off-the-street views, but brought considerable expertise to making that decision, but I was not there. I did not participate.

Q You mentioned Michael Joyce of the Bradley foundation as a participant, and you represented concerns that foundations may fritter away the -- the foundations assets. Is it -- I mean do you -- do you -- Well, was it the opinion of the board that the Bradley foundation would not be a good example to follow because perhaps they may fritter away the assets of their organization as well, and likewise a new foundation could be in a similar situation?

A I do not know precisely what they discussed because I was not at their meetings.

Q Okay. Let’s talk about the control over the assets after they’re transferred. Was the board interested in maintaining control over the assets and the stocks that the foundation would control?

A I think the board’s goal was to complete the transaction expeditiously, comply with the Blue

Cross Association rules and the requirements of state law and the Commissioner, and -- and have a process that was enduring and flexible for the State of Wisconsin. And beyond that, in my presence there was never any discussion of control beyond making certain that they complied with not only the state law but the regulations of the Blue Cross Association.

Q So you weren't involved in decisions in terms of the structure of the new foundation to have five members of Blue Cross Blue Shield or five appointees from Blue Cross Blue Shield be on that foundation board?

A I was not.

Q At the testimony that you provided on November 29th, 1999 you indicated that the new entity that's proposed would be a first mover in the marketplace. Do you mean by this as a purchaser of other health insurance plans?

A In terms of the consolidation that's going on not only in Wisconsin, but nationally in terms of health plans. Wisconsin is a mid-sized state, and in terms of national consolidation, you know, we aspire to places like Iowa and Missouri, similar size or smaller states where

Wisconsin can in fact be a -- a leader, if you will, first mover to use the term that I think I used last fall, in terms of -- of survival.

You can look at -- at the state and -- and I think you view the advantages in terms of corporate headquarters and employment, as well as the diversity of product offerings that come with a larger size company as positive for the state and the Wisconsin economy.

Q Just from a -- like a lay perspective and public's perspective, how would Blue Cross Blue Shield purchase new plans initially when much of the value of the company is in the new foundation?

A It has stock that can be used for acquisitions in terms of other states.

Q Do you plan -- Then would there be a plan to issue more stock?

A I think the goal of any stockholder-owned company is to grow and access capital for that growth. In order to access capital for growth you can only do it through loans, indebtedness, or by issuing more stock for the value received. That is the standard corporate transaction.

Q Will the issuance of additional stock devalue

the stocks held by the foundation?

A No, because the goal of the transaction is to enhance value for all the shareholders because you're acquiring assets with either cash or stock or debt, and those assets acquired and the synergies that come with the transaction create value. That's true in every corporation. You could pick up the Wall Street Journal or the business page of the paper today and see those transactions every day.

Q One of the other documents that was a part of your filing, which was from Donaldson, Lufkin & Jenrette, indicated some of the options of what the advantages, relative advantages and disadvantages of converting, and one of the advantages to Blue Cross Blue Shield is the possibility of stock incentives for management and key employees.

From what you're telling me here, to grow the company, to be a first mover in the marketplace, to issue additional stock, to grow the company, this would have a significant benefit to -- to management and key employees, upper management at Blue Cross Blue Shield; isn't that correct?

A I think the goal of incentives is for the executives to accomplish the goals of the company as set by the board of directors. If the value of the stock increases, the value in terms of the contribution increases. And so I think those goals are consistent.

Q If the development of the for-profit Blue Cross Blue Shield tracks some of the developments in other states, management, upper management, could be in a position to make a lot of money off of this; isn't that true?

A Well, I think --

Q I'm just saying they could be in the position to make a lot of money off of this.

A If the value goes up and the company achieves its goal, I think traditionally incentive compensation theory is that the people who accomplish that are rewarded.

Q So traditional compensation theory in layperson's term is companies getting bigger are going to give you more money.

A People receive an incentive for achieving the goals of the organization.

Q I'd like to just introduce J52, which is an exhibit, and it just outlines the

0054

recommendations of the investment banking firm, which outline the stock incentives as an advantage for management and key employees to help the company provide stock incentive.

MS. BAILEY-RIHN: Commissioner, I would just like to point out that the Commissioner's pretrial memorandum did have a deadline in which exhibits were to be filed. I don't have any specific objections to these exhibits, but I wonder if there are additional exhibits that we have not yet seen.

MR. PETERSON: Those are already a part of the record. We're just referencing items that are already in the record.

MS. BAILEY-RIHN: Okay. Fine.

THE WITNESS: Is there a question about the exhibit?

BY MR. PETERSON:

Q No. I'm just bringing it to your attention. We discussed it. I think that -- I wanted just to bring it to your attention that that was an issue that had been indicated as one of the advantages of converting.

A I think that's what I said.

Q And that's right and I'm introducing it because

0055

we had it marked as an exhibit. Could you --

One final question. The new organization is going to be a holding company, Heartland -- United Heartland of Wisconsin, is that the name? What would you -- How do you feel that this new organization will have an opportunity to continue any type of charitable activities for organizations in the State of Wisconsin that are consistent with the original charitable mission of -- of the corporation as it moves on to a for-profit entity?

A Well, at least since the Wisconsin code was rewritten in the late 1960's and early 1970's, the mission of the company is to provide innovative products and compete to serve consumer needs in a market that relies on competition. And I think the belief of the revisor of the code, who was then Dean of the Wisconsin Law School and wrote extensive annotations to the insurance code was that that service to the public is best accomplished by a healthy competitive market and healthy companies within that market who can offer innovative product. And the conversion permits Blue Cross to do that by accessing capital both for growth,

as well as for additions of new products to serve those customers.

So I think that meets the original need and certainly meets the statutory test that has been there since the code was rewritten in about 1970.

Q Do you think that the conversion merely formalizes what has been going on within the organization, or does it change any type of mission of the organization?

A I think the conversion and the commitment of 100 percent of the value of the company to serve the public needs is certainly consistent with the entire history of the company and as well as the statutes.

MR. PETERSON: No further questions for Mr. Hefty. Thank you.

COMMISSIONER O'CONNELL: Miss Madsen, do you have any questions?

MS. MADSEN: No questions.

COMMISSIONER O'CONNELL: Ms. Bailey-Rihn?

MS. BAILEY-RIHN: No questions, Commissioner.

COMMISSIONER O'CONNELL:

Mr. Bablitch?

MR. BABLITCH: No questions.

COMMISSIONER O'CONNELL: Thank you, Mr. Hefty. Mr. Peterson, you may call your next witness.

MR. PETERSON: We'll call Stephen Bablitch.

STEPHEN BABLITCH, called as a witness herein by the Coalition, after having been first duly sworn, was examined and testified as follows:

COMMISSIONER O'CONNELL: You may begin, Mr. Peterson.

EXAMINATION

BY MR. PETERSON:

Q Thank you. Good morning.

A Good morning.

Q We've had some discussion by -- by Thomas Hefty about the corporate structure of Blue Cross Blue Shield, and I guess we'd like to just follow a line of questioning similar to that. Would you just identify your position within the -- within the company?

A I'm the Vice President and General Counsel and Secretary for Blue Cross Blue Shield United of

Wisconsin.

Q And how long have you been in that capacity?

A Since October 1, 1996.

Q And previous to that?

A I was a partner in the Madison law firm of Dewitt, Ross & Stevens for -- since 1991 to ’96.

Q Now, one of the issues that we’ve been discussing is the original creation of Blue Cross Blue Shield in 1939 as a charitable and benevolent institution pursuant to Wisconsin statute 180.032. Have you evaluated that statute?

A I’ve read it.

COMMISSIONER O’CONNELL: Mr. Bablitch, can you speak more directly into the microphone for the court reporter.

THE WITNESS: Sure. I’ve read it, yes.

BY MR. PETERSON:

Q Have you -- Do you have a -- a legal opinion on -- on the validity of that statute, or do you feel that it applies to Blue Cross Blue Shield in terms of any relevance today?

A I think it’s been changed a number of times, so -- and it was written in 1939, so I don’t

know what -- what significance it would have in context of today's terms.

Q So do you feel that the original mission, historic mission as outlined in this statute for Associated Hospitals, is irrelevant today in terms of the nonprofit Blue Cross Blue Shield organization?

A As I recall the statute, it doesn't talk in terms of a mission. I think what it -- the legislature declared on Blue Cross at the time of Associated Hospitals Services, they did a number of things. It's about a three page statute, I think. One of the items that I think you're asking about is the tax exemption or -- or what?

Q Well, I was -- I was just trying to get at your sort of understanding of the sort of historical antecedents to the current organization and the relevance of those, particularly this statute to the organization today.

A Like I said, it's -- I think the statute has changed and I don't think that it reads the same today, so, you know, it's 60 years old. I don't think it applies to Blue Cross Blue Shield United of Wisconsin today.

Q Do you think that Blue Cross Blue Shield today, the nonprofit, is a charitable trust?

A No, I do not.

Q Why not?

A Well, this might be -- I don't want to be evasive here, but we have outside counsel who have advised the company regarding this question, so the basis of my knowledge is really confidential communication between outside counsel and myself.

I'm not an expert in trust doctrine or tax law so we typically rely on outside counsel, and in this case we hired the law firm of Foley & Lardner to advise the board. And as a part of that I've been privy to those communications, so I'm a little bit hesitant to answer questions. In fact, not only am I hesitant, but I don't believe that I can as a lawyer answer questions that would abridge the attorney/client privilege.

COMMISSIONER O'CONNELL: Mr. Bablitch is the attorney for the applicant in this proceeding, and as such if this is calling for attorney/client work product then you should only answer to the extent that you

can without revealing any attorney/client privilege or work product.

THE WITNESS: Okay.

MR. BRANCH: I think the record will show he has answered the question. He was asked whether he believes it's a charitable trust and he said no, he does not believe.

MR. PETERSON: We were merely asking for Mr. Bablitch to illuminate on issues that he's already discussed publicly that are part of the record in a letter dated December 13, 1999 to the Commissioner. Some of his analysis that he -- he describes the fact that it's not a charitable trust, but -- but we're trying to understand some of the underpinnings of that analysis and why he feels that way. I don't believe that it's a privileged communication since it's already made public to you in correspondence of December 13.

MR. BRANCH: Perhaps you could show that correspondence to the witness if you're going to ask further questions on this.

COMMISSIONER O'CONNELL: Do you have an additional copy? Let's -- We'll go off the record to mark the exhibit.

(Discussion off the record.)

THE WITNESS: I've got it.

BY MR. PETERSON:

Q Was that letter written by you?

A Actually, it wasn't, but I signed it.

Q Okay.

A I read it before I signed it, too.

Q Okay. Is there -- Are you more comfortable in answering my question then?

A Could I have it reread to me, please.

(Record read.)

BY MR. PETERSON:

Q Let me just ask the question again. I mean your position is that Blue Cross Blue Shield is not a charitable trust. You said no.

A Yes, correct.

Q In looking at this letter, I believe you or your counsel articulated part of the reason, but I wanted -- was wondering if you could further illuminate on why you believe that Blue Cross Blue Shield is not a charitable trust, particularly in light of the fact that in many other states the courts have determined that they were indeed a charitable trust.

A I can't really comment on the other states since

I haven't read the legislation and the statutes or the rules of the other states. My knowledge on this, like I said, I'm not an expert in this area, this is not an area of practice that I ever practiced, so I rely a lot on outside counsel advice on this, but I've read the enabling legislation from 1939, I've read the current statutes, I read the case law that you had marked and the 40 year old AHS case, and in nowhere does it ever declare Blue Cross or its predecessor to be a charitable trust. And now I'm really going back into trust and estates and my recollection, for what it's worth, is that in order to create a trust there has to be a specific intent.

So I've never seen this referred to as a charitable trust. I've reviewed our articles of incorporation and the bylaws going back to 1939, and we've never been referred to as a charitable trust, we've never, to my knowledge, acted like a charitable trust, and other than that, I'm relying on the advice of people who actually practice this for their daytime job.

Q Are you familiar with other Blue Cross Blue

Shield plans that have been considered charitable trusts by the courts?

A I'm familiar with other Blue Cross plans that have converted to a for-profit entity, but very generally.

Q So I mean at this point we'd say that your particular area of expertise, you would not be familiar with the Charitable Trust Doctrine or the Cy Pres Doctrine?

A Like I say, I'm not an expert in those areas. I've heard of them, but I think it would be beyond my expertise to give you much enlightenment with respect to what those doctrines truly mean.

Q Would you say that in 1939 the legislature created Blue Cross Blue Shield with a charitable purpose?

A No. They gave them a tax exemption which was then removed in 1972.

Q Okay. Let's talk a little bit about the -- the work that you were involved with, and I'll respect the attorney/client privilege and again we'll be discussing issues that are either part of the public record and trying to get a little better understanding of the information

testified to or information that has been communicated to us.

A Are we done with this letter then?

Q Yeah. Thank you. In terms of the decision of the special committee to designate the two medical schools as the recipients of these funds, you were involved in -- in those discussions and you've spoken publicly about those.

A Yes.

Q The -- The committee was concerned about issues related to administrative structures that would be needed for a new foundation; isn't that correct?

A That was part of what they talked about, yes.

Q In your role of advising the special committee, did discussions ever come up about administrative expenses and costs that might be related to funds that are received by the medical schools? And by that I mean specifically overhead or indirect expenses.

A You mean that the medical schools would have to incur?

Q No. This is the expense of operation so that a percentage of the money would be allocated as

overhead expense in a budget. So let's just use an example to help you understand this.

You give $100,000 to an institution organization. They have to include in their budget what their actual expenses are and overhead. Typically that could be 10 percent. In some situations it might be 40 percent. That's things that really aren't directly expensed by the grant, but the grant has to support all of the other activities like the building. Was that discussed by the specialty committee or information presented by the special committee?

A Not at that level of detail.

Q So your understanding of the -- of the discussion that was conducted by the special committee was that the med schools would be appropriate recipients of these funds because they already exist and administrative expenses would be low?

A Well, that's a bifurcated question. Let me answer both parts. One was yes, that they already exist. I think that the special committee placed a lot of trust and faith that the two med schools had 100 years of knowledge

and were actually public bodies and that they felt that they were a good institution to address the concerns of -- of what the committee was trying to get at.

With respect to the administrative costs, I think one of the concerns, and I'd say was maybe a secondary or even tertiary concern, was that they didn't want, that is the special committee, did not -- I think they viewed the two schools as already having an infrastructure and that that had some appeal to them from the standpoint of starting up a whole new foundation and all the costs that would be borne by staff resources and buildings and rent and overhead in that light. So that was a concern, but it wasn't their primary.

Q Were there concerns raised about the -- about designating the two med schools as the recipients? And let me -- let me illuminate on that a little bit. By designating the two med schools as the recipients of these funds, were there concerns raised that there should be a public process in terms of determining the best use of these funds?

A Yes, they did talk about that, and that's why

the two schools, they -- The special committee wanted the two schools to go out, and like they did do, the listening sessions, and go out around the state, solicit input, which the two schools did, and so the special committee I think conveyed that message to the two schools that they wanted that sort of public input process. And then they wanted a report on that, a preliminary report, I think it was due in like late August of last year, so they did convey that thought to them.

Q Was it your understanding that Blue Cross Blue Shield had the legal authority to designate the recipients of those funds?

A Yes.

Q The first proposal that was submitted by the med schools was unsatisfactory to the special committee; isn't that right?

A Not completely. Parts of it were unsatisfactory, though, yes.

Q And what was unsatisfactory about it?

A Let me see. I think that the -- the special committee or the board, I can't remember which one, wanted more specificity on accountability; in other words, how the money was going to be

spent, and I think they directed the schools or asked the schools to put more specificity into that part of the -- the plan.

Q Was an actual budget ever submitted to Blue Cross Blue Shield by the two schools?

A In the -- In the final draft that -- or the final report that came out, the two schools, as I recall, have some sort of a budget in the sense that they divided it up. The report is divided kind of in half; the first part being one of the two schools and the second part being the other school, and then they divide up -- each school kind of did a division or percentage of what they wanted to spend on a variety of different programs. And to the extent that you consider that a budget, I guess it’s an allocation of how the money would be spent, so.

Q But I guess -- Let me ask you this. Was there -- A detailed budget that distributed costs between direct expenses and indirect expenses was never developed by the two schools.

A I don’t know if it was ever developed, but I don’t recall seeing one.

Q Let’s talk a little bit about the board of directors of the two organizations that we’re

discussing for the most part here, United Wisconsin Services and Blue Cross Blue Shield.

A Um-hum.

Q What type of conflicts policy does the board of directors have for those two organizations?

A Well, we have a rather extensive, in fact volumes of contracts going back and forth between Blue Cross Blue Shield United and United Wisconsin Services. They're all -- All of these agreements are memorialized in formal contracts just like you would see if you were purchasing a service out on the open market, and the board approved all of those. Each board approved them I believe by a resolution, and I think that every -- every other year or so if there are changes to be made we will occasionally update those, but virtually everything that you can think of between the two companies in the way of services or provisions are accounted for by these agreements.

And then the agreements go into great detail about cost and the allocation method and the services that are going to be provided and, in fact, I believe Deutsche Bank did a rather thorough analysis of that,

presented it to the appraisal committee on the January 14th meeting. In fact, I believe that Mr. Johnson or Mr. Harrison's statement was they've got these things right down to the paperclips. So it's a rather extensive set of agreements that takes care of all the agreements between the two companies, and the board is well aware of it. I believe I had to brief the board on these things and -- and that's how it's done.

Q Would it be easier if -- to avoid conflicts if there were not overlapping boards?

A No. I think the issue of conflicts by their very nature, even with attorneys, attorneys, as you know, face conflicts all the time. The matter is how you protect against conflicts. For example, in the legal profession you protect against them by informing your client that you may have represented this party in the past and then you seek a waiver.

So it's -- A conflict in and of itself doesn't create a problem. If the conflict is not, or the potential of a conflict is not addressed and made publicly aware and then procedures are -- if procedures are not taken, then you probably have a problem, but in

our case they were addressed, there were fully executed agreements, so I don’t think that there was that kind of a problem.

Q Did you review the report from your investment banking firm, DLJ, that raised concerns about perceived conflicts of interest?

A I’ve reviewed a lot of stuff from DLJ, but nothing recently.

Q Okay. Would you -- In the discussion of conflicts would you agree that a public perception of conflict can be just as bad as an actual conflict?

A I think it depends upon the circumstances.

Q Would you say that concerns raised by your investment banking firm about perceived conflicts of interest was communicated to the board as something that needed to be addressed because there was -- because this perception could have a negative impact on the organization?

A You know, I don’t think so. I don’t think it came up in that context. I think they were talking about the investor community not in terms of conflicts of interest per se, but in terms of from the investor community standpoint,

that is, large institutional investors, you've got a Blue Cross plan and United Wisconsin Services, and institutional investors, although I am not a finance person, but based upon listening to DLJ, investors like a clean story so that they can understand it. They hate it when you have an HMO and a life company and a worker's comp because they can't understand the story and then they don't like to cover you. And so I think that's kind of the conflict that they were talking about if I -- if I remember correctly.

Q Now, back in -- in January Mr. Hefty reported that management received stock options. Did you also receive stock options?

A In January of what year?

Q Of this year.

A Of 2000, yes, I did.

Q And what was the total of the stock options that you received?

A I think it was like 120 or 121,000.

Q Do you know what the share value of those are right now?

A The value of those stock options right now are zero.

Q Why you mean -- What's the value of the shares right now that you have options on?
A Zero. I have no stock options that have any value because of -- the ones that are vested are all, as they say in the business, under water, and the rest have not vested. So they're -- the short simple answer is my stock options have no value.
Q Okay. What -- What -- How many shares of stock do you own in the current for-profit subsidiaries of Blue Cross Blue Shield?
A You mean that I personally like bought or --
Q Or that you have options on.
A I think I -- my wife and I probably bought something in the area of, over the last four years, something like 4,000 stock options -- or not options, stock. So we just, you know, go to our broker and bought them. So I own like those 4,000, and then as a part of my 401K plan I think I purchased some stock through that as well, instead of going through like Fidelity or something. So I don't know. Those might equal 1,000. So I think the total combined stock that I own in the company might be close to 5,000, although I can't give you a precise number, but

it's somewhere around there.

MR. PETERSON: Okay. I think in the interest of time we're going to move on now to our other witnesses. Thank you.

THE WITNESS: Thank you.

COMMISSIONER O'CONNELL: Miss Madsen, do you have any questions for this witness?

MS. MADSEN: No questions.

COMMISSIONER O'CONNELL: Ms. Bailey-Rihn?

MS. BAILEY-RIHN: No questions.

COMMISSIONER O'CONNELL: Mr. Branch?

MR. BRANCH: No questions.

COMMISSIONER O'CONNELL: Let's take a short break.

(Recess taken.)

COMMISSIONER O'CONNELL: Let's reconvene. We'll go back on record. Mr. Peterson, you may call your next witness.

MR. PETERSON: Wade Williams, from ABC for Health will be calling the next witness, Deborah Cowan.

MR. WILLIAMS: I'd like to call Deborah Cowan.

DEBORAH COWAN, called as a witness herein by the ABC for Health, after having been first duly sworn, was examined and testified as follows:

COMMISSIONER O'CONNELL: Again, if the witness will speak directly into the microphone.

EXAMINATION

BY MR. WILLIAMS

Q Good morning, Miss Cowan. I hope you don't mind if I refer to you as Deb at some point.

A That's quite all right.

Q Would you please state your name and your occupation?

A My name is Deborah Cowan. I work for Community Catalyst in Boston. Community Catalyst is a national health care organization, health care advocacy organization, and we work with consumer and community groups on a variety of health care issues around the country.

We have a particular interest in the conversion of nonprofit organizations and have been working for the last three years on a national initiative related to nonprofit conversions in partnership with Consumer's

Union.

Within that project my particular expertise is on philanthropy, so my focus is on the start up of new health foundations and the processes that communities and regulatory bodies are involved in around the formation or around the disposition of conversion assets. That's my current work.

Q How many conversion transactions has Community Catalyst being involved in?

A Community Catalyst and Consumer's Union together have worked on conversion transactions in more than 35 states now, and I personally have had experience over the last two-and-a-half years with 12 to 14 of those, particularly in situations dealing with questions about subsequent use of charitable assets.

My professional background is actually in foundation management. I have spent 18 years in the foundation field both as a foundation administrator and also as a consultant to family and private foundations, and in my previous work was the Administrator of a health conversion foundation, as well as a public health foundation.

Q Would you describe your position at the previous health foundation?
A I worked at a community foundation in New Hampshire, and we had essentially a management contract for a health conversion foundation, which was one of our clients, so I was the Administrator of that health foundation. That was actually how I came to learn about and be interested in conversions of nonprofit corporations.
Q Based on your experiences in 12 to 14 other conversion transactions throughout the nation, and specifically with your experience with health conversion foundations, how would you -- how would you view Blue Cross Blue Shield United Wisconsin’s proposal to create a public health foundation with the -- the requirement that the proceeds be designated and distributed for the med schools’ use?
A Well, clearly it’s -- it is different from most of the plans that -- where I have had a direct involvement and most of the recent conversion experience around the country. So more typically, the result is the creation of a new health foundation, and there are now some 134 of

such foundations around the country with assets totaling $15 billion.

So there is a growing body of experience with these health foundations and growing, I think, body of -- sort of growing record in terms of what have they been able to accomplish and how they have been organized. And -- And so in general, that -- that -- that's an area where I spend quite a bit of time currently.

Q This -- Those other conversion transactions which created health foundations which are unique or which are not unique -- Excuse me. In those other transactions in which public health foundations were created that are different from the one as proposed in Wisconsin, did those also involve a regulatory process or a court proceeding?

A Yes. Typically there are both regulatory review and very often a court review as well, and I would say that especially in -- in -- over the last five to eight years that there has been more attention paid to designing public process and regulatory review which is actually open to and involves the public in meaningful ways.

And so I think in general we've gotten better at doing that in recent years.

Q So am I -- would I be correct in saying that in conversion transactions in other states that you've dealt with, regulatory and court -- regulatory processes and court proceedings ended up in foundations -- in creating foundations which were created with public input? Would that be correct?

A Particularly recently I would say there -- there is more -- more -- more attention paid to that. I would say initially it was more common for attention to be focused on the review of the transaction itself. In many of the early conversions that -- there wasn't as much attention paid to questions about the subsequent use of charitable assets, but -- but because of a number of -- of high visibility foundations that -- that -- where there has been important questions raised about the -- the public origins of the assets, I think now it's -- it is more common to pay an equal amount or a good amount of attention to those questions as well, and it's more common now for extensive public hearings, often actually for the transaction

review to be sort of divided and for a piece of the process to be focused on what happens to the assets subsequently.

Q So in your opinion, would it be -- in your opinion would the proposal by Blue Cross to distribute all of the proceeds of the conversion transaction to the medical schools, would that be unusual or unprecedented?

A Well, it is -- it is unusual and it is -- it is certainly untypical. And I think what -- what is unusual about it is that it makes a decision about the ultimate recipient of the funds and the ultimate beneficiary, if you will, of the funds without a full discussion of what might be some alternative approaches and without a full involvement of the public in -- in that decision.

Q In the other conversion transactions in which you've dealt with creating public health foundations or health foundations, have you noticed a theme or a -- a system of rules in which the original use of the funds or the assets were to be carried over to the new health foundation?

A Well, that is typically a focus of the review

and -- and requirement in most -- in most states either under the common law standards or under specific conversion laws that have been passed in recent years. So there's a clear requirement that there be a relationship between the original purposes of the nonprofit organization and the foundation. So much of the discussion then becomes about, you know, how to make that translation, how to best capture that original purpose in a new form.

Q In your experience with those transactions has the -- has the doctrines -- have the doctrines of charitable trusts and Cy Pres been the subject of the legal discussions?

A Those are typically the important considerations that guide the discussion, yes.

Q Are you -- Are you very familiar with those doctrines?

A I am familiar with those -- those doctrines. I want to clarify that. I'm not an attorney. I work with many attorneys, but I am the foundation expert on our staff, and so -- and so my -- my expertise as it relates to those doctrines comes from that background rather than from law school training.

Q Well, I think just because you're not an attorney doesn't mean that you can't explain what charitable trust or continuing purposes mean.

A Okay.

Q So for the interest of our education, would you describe your view of what charitable trust and Cy Pres are all about?

A Well, what the doctrines together require first is that a nonprofit corporation that is dissolved to fundamentally change, that its assets nonetheless remain in the nonprofit sector and continue to be dedicated for public benefit purposes, and secondarily that -- that the -- that the purposes be as closely tied as possible to the original. Recognizing circumstances have changed, the application of funds may not be identical, but it should be as close as near as possible to the original purposes.

Q Are you aware of any transactions that you've been involved in in which you would say in your opinion that the Cy Pres doctrine in which -- or to specify in which the assets which were proposed to be used in the new foundation were

different, were very different from the original purposes that the assets were attached to?

A In the transactions where I've had direct involvement I think there has been a good deal of attention paid to the requirements of both charitable trust and Cy Pres doctrine, so there has been a close tie. There certainly are, early on in the record of how nonprofit conversions have been handled, there are examples where I think that that didn't happen, and there generally, I think, has been a lot of good learning from those examples.

So more recently, and certainly in the ones where I've had direct involvement, there has been a -- a close correlation.

Q Could you give us a national perspective on how many grant-making health conversion foundations exist today and how many charitable assets from health care conversions such as Blue Cross & Blue Shield have been preserved for the public?

A Well, there are, as I said earlier, 134 health foundation -- at least 134 health foundations that have been formed from the conversion of nonprofit organizations. That includes hospitals, health plans, and Blue Cross & Blue

Shield organizations. The health plan conversions actually account for about 44 percent of the -- of the 15 billion in assets that are currently in those organizations.

And particularly with regard to the record of Blue Cross & Blue Shield conversions, the -- nearly all of them have -- have actually led to the creation of new health foundations. That's happened in two different forms. First of all, as the result of Blue Cross & Blue Shield sales and conversions new health foundations have been created, and in some cases where there's actually been litigation to settle the question of are there charitable assets or not, there have been funds agreed to in settlement, and in those cases as well the vehicles have been -- the vehicles chosen for the resulting assets have been foundation vehicles.

New health foundations have been created in most circumstances. In the case of several of the settlements where the asset totals are smaller the vehicles selected have been funds within existing community foundations, but they have nonetheless been

grant-making foundations. That's been the choice in almost all cases.

Q Now, Mr. Hefty and Mr. Bablitch both testified that they believed that the Blue Cross Blue Shield United of Wisconsin organization was neither a charitable trust nor a charitable organization. Could you describe as a way of background what the historic mission of Blue Cross & Blue Shield has been in the United States?

A Well, I believe the formation of the Blue Cross & Blue Shield plan in this state was part of the national movement that began in the '30's and gathered momentum in the '40's and really was an effort throughout the country to find and create locally-rooted solutions to the problems of how to make health care affordable and accessible to people, both the cost of hospitalization and subsequently physician services. So it was -- it was within that context that this Blue Cross & Blue Shield plan also was formed.

Q Were you surprised to hear Mr. Hefty testify that he was not aware of any charitable purpose of Blue Cross & Blue Shield?

A Yes, I was surprised because I think that many of the Blue Cross & Blue Shield plans that I am directly, you know, familiar with have actually taken pride in their nonprofit and charitable origins and character and that that has, you know, influenced their behavior as corporate citizens and -- and with, you know, whether or not they have been taxed at the state level, in many instances they have still seen themselves as part of that nonprofit movement. So I was surprised.

MR. BABLITCH: I'm going to raise an objection at this time on relevancy grounds. We're talking about the witness's expertise in other states and what those other conversions may have been. This is uniquely state law issues, both statutory and if common law does play in, common law is a state issue. And so to the extent that the witness's comments are reflective of her opinions of what happens in other states and other plans, I think that's largely irrelevant as to what happens in Wisconsin.

COMMISSIONER O'CONNELL: I'll sustain the objection. Questions should refer

to Wisconsin's Blue Cross mission and charitable purpose.

MR. WILLIAMS: Yes, ma'am.

MR. BABLITCH: And to that extent I would like the last answer struck.

COMMISSIONER O'CONNELL: I'll take that under advisement.

MR. BABLITCH: Thank you.

BY MR. WILLIAMS:

Q Are you familiar with what the mission of Blue Cross Blue Shield United of Wisconsin is?

A I have seen a number of documents referring to the charitable -- the original mission of Blue Cross & Blue Shield which seemed to me consistent with other such missions that I have seen, yes.

Q So the relevance of the discussion of national -- the national Blue Shield & Blue Cross movements would be regarding the mission that was underlying the creation of Blue Cross in Wisconsin?

MR. BABLITCH: I'd object on the same grounds, and it's up to the Commissioner to determine relevance.

COMMISSIONER O'CONNELL: Objection

sustained.

BY MR. WILLIAMS:

Q Could you share with us, Miss Cowan, about what you know about state laws governing conversions that include provisions for health foundations?

MR. BABLITCH: I object on the same grounds.

MS. BAILEY-RIHN: Commissioner, I don’t think she has the foundation. She’s not an attorney.

THE WITNESS: Let me just say --

COMMISSIONER O’CONNELL: Just a second. I’m sorry. Could you repeat your objection?

MS. BAILEY-RIHN: He asked her whether she was aware, and I believe he was going to ask her about state law issues and I believe statutory issues. She’s not an attorney. She can answer whether she knows of the law, but I don’t think she can interpret them as a nonattorney. Or I should say give her legal opinion on that.

COMMISSIONER O’CONNELL: Mr. Williams, I’ll give you some latitude with this witness. We acknowledge that she’s a

national expert on foundation issues, but she should not be asked to provide legal analysis or legal opinions. She's not an attorney. So we'll give you some latitude in terms of asking these questions, but keep in mind that what is relevant to our discussion today is the Wisconsin Blue Cross plan.

BY MR. WILLIAMS:

Q Miss Cowan, please share with us what you know about precedents set by other Blue Cross Blue Shield conversions in other states as they relate to the formation of a charitable foundation in Wisconsin.

MR. BABLITCH: I'm going to raise the same objection. What happened in other states is uniquely up to them because this is a matter of state law, state law interpretation, and if common law comes into the practice that is uniquely state. No federal law regarding this. Therefore, what happened in other states is largely irrelevant here, other than maybe it serves some interest of general curiosity. If that's the case, then I don't think this is the appropriate forum for that.

COMMISSIONER O'CONNELL: I will

allow the question.

THE WITNESS: You would like me to talk a little bit about the other health foundations that have been created from Blue Cross & Blue Shield plans in other states?

BY MR. WILLIAMS:

Q Yes, ma'am.

A Because that -- that record is now, I think, informed by quite a bit of experience that -- that does represent some alternatives that would be available for the use of these assets.

There are health conversion foundations now operating in California that were formed from assets of a Blue Cross & Blue Shield conversion, and there are also foundations that have been created in New Hampshire, Colorado, and Missouri, and as well as the settlement funds in Kentucky and Connecticut and Ohio. So your specific question about those foundations?

Q Could you describe the foundations in terms of -- of independence to make grants?

A Right. First of all, these are all health foundations which have a board, an independent board, whose job it is to make decisions about

the use of the funds available for grant making. So these are foundations which actually have a perpetual responsibility to make decisions about the allocation of funds to address the original public health purpose of these Blue Cross plans.

They would have the ability to make grants to medical schools certainly and -- and generally health conversion foundations do that, but they would also have the opportunity to make grants and to support a wide variety of other organizations. And so that is a key part of the responsibility of the governing boards of all health conversion foundation.

MR. BABLITCH: I object to that statement of all health care foundations. That's not -- That's a legal conclusion for all. That's not the case here. It's up to the Commissioner to make those kinds of determinations. Therefore, this witness is not qualified to give that kind of an opinion and it's largely irrelevant what happened in other plans as it's compared to Wisconsin. That's a continuing objection.

COMMISSIONER O'CONNELL: Your objection will be noted on the record. I will

allow the question regarding -- or I will allow questions regarding the foundations in other states. It is an element that is relevant to my decision in terms of the structure of the foundation and therefore, I will allow the question, but your objection is noted on the record and the question will be allowed subject to that objection.

MR. BABLITCH: Thank you.

BY MR. WILLIAMS:

Q Miss Cowan, you mentioned earlier public input into the regulatory processes and I would -- I'm wondering if you would like to comment on public input in foundations in terms of the ongoing governance of the foundations that you're experienced with.

A Right. Well, first of all, I think that public input into the formation of these new foundations has typically been part of the regulatory process and has involved the -- both consultation with people about health needs, perceptions of what ought to be the priorities of those foundations, but also input into the very important questions about governance. Who should sit on such a foundation board? What

kinds of people should be represented? What should the qualifications of those people be? How should they be selected? And those kinds of issues have typically been a very major part of the discussion that's -- that's within the public review of the conversion foundation formation.

In California, which was the experience that in many ways I think raised the visibility and helped people to understand why this was so important, the result of public input into the regulatory process was that there was a broad outreach effort designed to seek the members of the new governing board, and that has become a standard that many other conversion foundations have looked to.

In Colorado there was a public process organized to actually recruit members of a community advisory committee who subsequently named the first board of the foundation, and a similar process has just been organized both in Maine and in Missouri to try to create not only the opportunity for public discussion about who ought to sit on such a foundation board, but actual an ongoing mechanism for influencing the

choice or feeding into the choice about what -- who controls the foundations that hold these assets.

Q Have you done some analysis on the missions of the medical school, the Medical College of Wisconsin and the University of Wisconsin Medical School?

A Well, I have read the statements from those institutions about their missions and, you know, and I generally understand that they characterize their missions as including research, education, clinical service, and community support, community service.

Q So you've read the medical school's proposal?

A Right.

Q That's incorporated in the Blue Cross application?

A Yes, that's right.

Q In your view, how does the original mission of Blue Cross Blue Shield United of Wisconsin, which you described as charitable, how does that fit with the missions as you understand -- as you understand it of the medical schools?

MS. BAILEY-RIHN: I'm going to object on foundation grounds. I don't think she

has established foundation that she knows the original mission.

COMMISSIONER O'CONNELL: Can you repeat the question, Mr. Williams?

MR. WILLIAMS: Yes, ma'am. I'd like Miss Cowan to comment on how the Blue Cross Blue Shield's original mission of providing access to health care on a nonprofit basis fits in with the missions that have been stated in the medical school proposal.

MR. BABLITCH: I'm going to object to that question because it assumes a fact not in evidence. As far as I know, there has never been a quote, "mission." And so in order to clarify the record, I think we need to ask questions that have some basis for fact in the record. There has been a law in 1939, there's an existing law, there's articles of incorporation. If you can point me to a mission statement, I'd like to take a look at it. Until then, I object to any characterization of a charitable mission.

MR. WILLIAMS: Commissioner O'Connell, if I could direct everyone's attention to the enabling statute from 1939, I

could ask Miss Cowan to read it if that would be helpful in terms of establishing what the original mission of Blue Cross was.

MS. BAILEY-RIHN: I'd just ask to see -- I'm not sure if he's referring to the 1939 statute or some sort of legislation or what. If you have copies --

MR. WILLIAMS: No, I don't know if they're marked.

MR. BABLITCH: I will stipulate that the language in that statute reads as follows: "Every such corporation is hereby declared to be a charitable and benevolent corporation and its property, real, personal" --

MR. WILLIAMS: What --

MR. BABLITCH: -- "and property transferred to it shall be exempt from taxation."

MR. WILLIAMS: What section of the statute is that, Mr. Bablitch?

MR. BABLITCH: That's Chapter 118 of the laws of 1939, Section 8.

MR. WILLIAMS: Would you like to read the first section?

COMMISSIONER O'CONNELL: Excuse me,

Mr. Williams.

MR. BABLITCH: I'd be happy to.

COMMISSIONER O'CONNELL: I understand there are two objections to your last question -- objection regarding foundation to the question. We also have an objection from Mr. Bablitch. I will allow the question subject to the objections that have been received. So you may continue to pursue this line subject to the objections.

MR. WILLIAMS: Thank you, Commissioner.

COMMISSIONER O'CONNELL: Do you want to repeat the question for the witness?

BY MR. WILLIAMS:

Q Do you know what question I have just asked you?

A I think so. I think that -- I believe that what you asked was --

COMMISSIONER O'CONNELL: Why don't -- We could have the court reporter repeat the last question for Mr. Williams.

(Record read.)

THE WITNESS: I think the purposes of providing access to health care are different from the purposes cited by both of the medical

schools of research, education, clinical services, and support, community support.

BY MR. WILLIAMS:

Q Miss Cowan, from a national perspective what sorts of foundations -- or excuse me, what sorts of health priorities are viewed as most important by health conversion foundations particularly as they relate to medical research?

A Right. There is, as I said earlier, now quite a bit of experience of health conversion foundation grant making which -- which answers the question, you know, what kinds of purposes do the boards of those foundations find most relevant to the continuing mission of health -- nonprofit health organization and health plans, and the best -- the best information about grant-making patterns actually comes from a survey conducted by the Senate for Health and Social Policy two years ago about the 1998 grant making of 55 established health conversion foundations. That included distribution of $267 million altogether. One percent of that actually went for research and 10 percent approximately went for health profession education.

So the vast majority of those grants were actually made to support health and human services more generally and that was about -- accounted for about 32 percent of all the distributions and 25 percent to health and human services policy research and analysis.

So the other information I think on how -- on grant-making patterns actually comes from the National Trade Association of Health Philanthropy Grant Makers and Health which does an annual survey of what kinds of grant-making interests have been identified by their members.

And in the most recent version of that survey research is actually listed as a current area of activity for nine percent of the reporting foundations and -- and higher -- and education for health professions by 14 percent.

Q But these foundations, are they all Blue Cross Blue Shield conversion foundations?

A No. These are all health conversion foundations.

Q Health conversion foundations?

A Um-hum, that’s right. My own analysis of the grant-making health conversion foundations included a look at four that had completed

annual reports, and what that confirmed for me was the understanding that medical schools are certainly among the grantees of all health conversion foundations. They are well represented and they certainly have very important capacity to -- to contribute to public health goals in their communities, but generally they account for well under 25 percent of the funds that are distributed.

And for example, in the most recent report of the California endowment, the operating Blue Cross & Blue Shield derived conversion foundation, there were 175 grants accounting for $113 million distributed. About nine percent of the number of grants awarded and about 11-and-a-half percent of the dollars awarded actually went to institutions of higher education altogether, so that would include medical schools, but also other higher education institutions. And the California health care foundation which has a clearer research and policy agenda similarly reported 18.7 percent of its grants and 12.7 percent of the dollars awarded went to institutions of higher education.

So those -- And I had some other -- I've done some other analysis which shows a similar pattern and -- and I think is -- is typical of the grant-making patterns of organizations that have available to them a wide range of beneficiary options.

Q So it sounds like that about nine percent of funds that are made by grants of health conversion foundations actually go for -- actually to go medical schools. Does that sound --

A Actually, the rate varies. What I -- I think the rate varies, but is in no instance that I have identified even as much as 20 percent. So -- So I would -- I would recite that fact because it contrasts with the proposal here in Wisconsin, which is to give 100 percent of the funds to two medical schools, whereas in the case of other conversion foundations those institutions are -- represented, as I say, account for less than 20 percent.

Q So in essence, Blue Cross has created a foundation and required the foundation to grant 100 percent of the funds to the state's two medical schools; is that correct?

A Well, I think that's what the plan accomplishes. The foundation is essentially a mechanism for transferring the funds to the two medical schools, is my understanding of the plan.

Q From the point of view of foundation best practices, can you tell us how you would assess the process by which the decision to grant 100 percent of the funds to the medical schools?

A Well, I think it departs from the best practice in the sense that the important decision was made by a very small committee, it's been explained this morning of four or five people, and -- and that determined -- obviously, that was a very limited amount of consultation.

The subsequent public hearings that were held around the state to gather input about health priorities I think were encouraging evidence that the two medical schools, you know, intend and hoped to be open and inclusive in their processes for making subsequent decisions, but the most important decision was really, or the most important question was not on the table at those hearings as I understand it. The most important question being are these two institutions the best -- do those two

institutions represent the best option for continuing the -- the purposes of Blue Cross & Blue Shield United of Wisconsin.

Q As 100 percent beneficiaries?

A Correct.

Q How does the public input process in our Blue Cross & Blue Shield transaction compare with the opportunities for public input here in Wisconsin?

A Well, I think increasingly we have seen hearings -- First of all, public hearings are different in character than -- than -- than listening -- listening sessions and -- and suggested a different way that public input will influence ultimately the decisions.

We have increasingly seen regulators, as I indicated earlier, focus a good deal of attention and invite a good deal of public comment on these questions. The most recent Blue Cross & Blue Shield conversion experiences that I participated in directly were in New Hampshire and Maine, and in those -- in those states there were, I think, seven and 12 public hearings actually held at which all of the questions were -- were open in terms of the

important structure of these proposed entities and their mission definition and their governance.

Q Would you describe the experience in California and Colorado in terms of public input?

A Well, I think the -- I think the most -- among the most important lessons from those two conversion foundations were how to structure a selection process for governing boards so that the result is actually the sort of balanced and representative and diverse board that will have to make all of the decisions going forward about resource allocation and fundamental location, and there’s been increasing attention paid to how do people come to sit on these foundation boards both initially and going forward because it’s understood to be a very important question that -- that will fundamentally determine how -- how resources are allocated going forward and these, you know, the understanding obviously is that -- that what you -- what you need to have is a board which has the -- the wisdom and the skill and the expertise and the diversity of background to make those resource allocation decisions wisely.

And so increasingly I think we're seeing public processes that is designed to achieve that result.

Q Could you please describe the hallmarks of a well managed conversion foundation?

A I think the best conversion foundations have a distinguished board which is diverse and reflective of the community that's served. They have in many instances actually as a matter of their -- of the way that their bylaws are written a continuing dedication to openness, transparency in their operation and the involvement of, you know, community members in key decisions, and I think increasingly it's understood that those -- those commitments have to be structured into the design of health foundations in order to achieve the goal of making them accountable to the public.

Q Well, in your view, how does the Wisconsin proposal to create a foundation which will distribute all the funds to the medical schools, how does that measure up compared to what you've seen?

A First of all let me -- let me say that the issue of, you know, how the board is constituted is

very, very much at the forefront of thinking about how health conversion foundations should be organized. It was identified by grant makers in health as the most -- single most important characteristic in determining how -- how effective a new health foundation would actually be. And for that reason they track the issue of board independence and board makeup in this annual survey, and their research shows an increasing emphasis on board independence and board diversity and community participation.

So those are -- those are obviously important characteristics that are not -- that are not included in the -- in the proposal here in Wisconsin where really the board which will be controlled by the company and the two beneficiary institutions does not have any -- any -- any public character and, in fact, isn't really intended, as I understand it, to make resource allocation decisions, but rather simply to convey funds to two institutions.

Q Now, Blue Cross has selected a board for -- or proposed a slate of directors for the proposed foundation and they appear to be, you know, very well-qualified people. Would you agree with

that?

A I actually haven't seen the nominees for the board. I'm sorry.

Q Okay. If Blue Cross were to propose a slate of directors to manage the nonprofit conversion foundation, what would be the purpose of having experts in public health, in foundation finance, et cetera, what would be the purpose of having these -- these -- this expertise represented on the board if there were no real decision making regarding how the funds would be spent?

A I'm not sure. The issue -- I'm not sure what the purpose would be. The issue of -- of course, you know, finding the right expertise is very, very central to the formation of these new health foundations. It occupies a great deal of attention, and rightly so because probably the constitution of the first board is the single most important decision that -- that is made about these new health foundations, but I do want to emphasize the issue of independence because I think qualification is sort of a second order question, and I have no reason to -- to challenge, since I don't even know who has been appointed to this board, I have no

reason to challenge or question their background, but it's -- it's clear that because they are appointed by the company and -- and -- and the remaining members by the beneficiary institutions, that they are a very different kind of board than what we are seeing with most of the independent health conversion foundations where there is a decreased incidence of carry forward of board from the converting nonprofit.

And -- And actually, I think the most recent report showed that excluding joint ventures, which have a different character, but excluding joint ventures, there's actually only one conversion foundation that -- that's been identified as having a board member appointed by the successor for-profit company. So that's quite unusual.

Q So how could the Wisconsin governance or how could the governance of the proposed Wisconsin foundation be improved?

A Well, I think -- I think the fundamental question is, you know, should there be actually a foundation created which is an independent foundation and which is responsible for answering the question year after year after

year what are the best opportunities to use these funds. That's the traditional assignment of foundation boards, and that would require the -- that would require the creation of a very different kind of plan than the one that's being presented here.

Q So would it be your recommendation to the Commissioner that an independent board of governors be established which would have authority to decide on its own what grants were worth funding in terms of -- of the overall public health system in Wisconsin?

A That certainly would be consistent with the -- the vast majority of decisions about how to use -- how to provide for the disposition of assets of a nonprofit corporation.

Q As far as your recommendation would go, you said that would be consistent with other plans that you have seen. Are you satisfied with the performance of the results and the performance of those plans that have had these independent boards?

A Well, you know, I think the performance of health conversion foundations, you know, obviously varies. There are some foundations

that I think do extraordinarily, effective and sophisticated work, and there are -- there are certainly some that are -- that are less skillful, but I think the important thing to recognize about them is that they do offer the -- they do offer the advantages that are traditional to -- to philanthropy in terms of their structure and they do offer a mechanism for balancing the competing needs of various interest groups and the different kinds of opportunities about how to use funds and -- and that -- that decision-making structure is really missing from this proposal.

So the important decision in this particular case would be made at one point in history and then subsequently all -- all subsequent decisions would be really made by the two beneficiary institutions with no -- no further input from -- from the public unless they elected to structure some such mechanism, advisory mechanism.

Q So would it be your recommendation to the Commissioner that from a broader philanthropic perspective, that the post-foundation should have an independent grant-making authority?

A I believe there are great advantages to that structure, yes, and I believe those advantages would be available in Wisconsin and would serve the public health needs of the state very well if such a foundation were skillfully designed and organized.

Q Miss Cowan, in your experience in working with and analyzing foundations, what have you found to be the case concerning administrative overhead expenses in foundations?

A Well, I think that we understand from earlier testimony that that has been a significant area of concern, and I think there's quite clear research on that. The Council on Foundations, which is the National Membership Organization of Philanthropy, actually does an annual management survey and tracks, you know, administrative costs or management costs as a percentage of assets and as a percentage of grants, and in the most recent management survey that I consulted the -- the average cost of administration expressed as a percentage of the grant budget was 12 percent for all foundations. That figure actually ranked from 20 percent for small foundations with a small asset base to 10

percent for foundations with assets of $250 million.

So I think that -- that that's the figure that I would -- would believe is -- is reasonable to imagine might need to be spent on the organization of a new philanthropy with a $250 million asset base, and that figure I think does compare favorably to the kinds of overhead costs that -- that are -- that are typically expressed for major research and teaching institutions.

Q Have you reviewed the overhead costs of either the Medical College of Wisconsin or the University of Wisconsin Medical School?

A I have looked at the indirect cost rate chart for the University, and the range that I recall was 25 percent for off-campus projects to 44 percent for on-campus. And that is quite typical of what research institutions and major teaching institutions would have as an overhead rate.

Q Okay. Miss Cowan, how are charitable grant-making foundations regulated?

A They are typically regulated by the Attorney General's office in their state, and in some

cases also there's some involvement by the Secretary of State, but they report their activities also, of course, on a tax return for charitable activities.

Q Based on your review of the Medical College of Wisconsin and University of Wisconsin Medical School proposals, would you compare the level of public scrutiny that would likely be the case would be less than what would be expected of a charitable organization regulated by the AG's office?

A By the AG's office?

Q The Attorney General's office.

A I'm not sure whether -- whether I could do that, really whether I have any knowledge that would allow me to understand whether one institution or the other is more closely regulated.

What I do think is very clear, though, is that the structure of a grant-making foundation and the operations of a grant-making foundation are quite easily understood and quite easily penetrated by members of the general public, if you will. It's very easy to understand what they're doing and it is, in fact, very easy to find out what they are doing

because they are required to file an annual tax return which lists all of their grants, and because that information is required to be available on demand and is, in fact, collected and disseminated through a national system of -- of library collections it's quite easy for someone to -- to say so what -- how is this foundation spending its money, and very quickly learn the answer and perhaps do some analysis on that.

I would contrast that to the challenges that people face in looking at any large institution and trying to figure out, you know, what kinds of resource allocations have been made by the budget management structure and, you know, where are there opportunities to influence that.

MS. MADSEN: Commissioner, I'd like to object to that last answer since it does not address at all the Wisconsin context. She's making a very general statement about analyzing institutions in general, and I don't think that's relevant or should be given any weight in this proceeding.

COMMISSIONER O'CONNELL: I recognize

that there -- I recognize ongoing objection to the line of questioning relative to national comparisons and will allow the questions similarly as earlier subject to the objection.

BY MR. WILLIAMS:

Q Miss Cowan, in your opinion would an independent grant-making foundation be more easily penetrated, as you said, as far as their activities go than something that might be embedded within a medical school?

A Well, let me just answer the question by saying that -- repeating my comment that I think that -- I think it is -- it is relatively easy to understand and analyze the activities of grant-making foundations and that has, of course, produced, you know, some -- in some places some lively dispute about what choices have been made by grant-making foundations.

I personally think that that kind of dispute and discussion is very healthy and a good sign that these kinds of institutions are being -- are being held to account.

Q Miss Cowan, you reviewed the bylaws of the proposed Blue Cross Blue Shield public health foundation?

A Yes.

Q And what would be your opinion of those proposed bylaws?

MS. BAILEY-RIHN: I'm going to object I guess on relevancy and I don't -- again, if it's asking for a legal opinion, I think that she doesn't have the foundation.

COMMISSIONER O'CONNELL: Can you repeat the question, Mr. Williams?

MR. WILLIAMS: Yes. I'd like Miss Cowan to comment on her opinion of the proposed bylaws of the foundation which, of course, go to -- which are relevant to the governance and ultimately the mission of the foundation.

MR. BABLITCH: I'll renew my objection. This is like having a doctor on the witness stand and we're asking him about complicated tax law. I just don't understand how laws in other states, what happened in other states may be relevant here and how a nonlawyer can give time after time legal conclusions. So I'm just going to continue to state that as a continuing objection.

COMMISSIONER O'CONNELL: And again I will allow this line of questioning subject to

the objections.

MR. WILLIAMS: Yes. Commissioner, we're just offering Miss Cowan as an expert based on her experience and what she's seen in other states.

MR. BABLITCH: But you're asking legal conclusions.

MR. WILLIAMS: I'm not asking for a legal conclusion. I'm asking for her opinion on the effect of the bylaws of the proposed foundation.

COMMISSIONER O'CONNELL: Before we have an ongoing debate, I do understand, Mr. Bablitch, your objection. I understand your objection, Miss Bailey-Rihn. I do understand that you are objecting based on that you are asking her to interpret laws and suggesting legal conclusions. I understand those objections. We'll allow the questions subject to those objections.

I should note that we have -- we're nearly approaching the noon hour. I would like to finish with this witness before we break, but I should ask you, are you near wrapping up, Mr. Williams?

MR. WILLIAMS: Yes, ma'am. That's my last question.

COMMISSIONER O'CONNELL: Oh, okay. Miss Madsen, do you have any questions?

MR. WILLIAMS: She hasn't answered yet.

COMMISSIONER O'CONNELL: Oh, I'm sorry.

BY MR. WILLIAMS:

Q I'd like her opinion on the proposed structure of the -- of the proposed foundation which, of course, would be influenced by the bylaws.

A Let me just repeat that I actually -- I actually do look at a lot of foundation bylaws. That is the subject of my consultation to other regulators and to other community groups. I -- I am an advisor to our experts on the structure and organization of foundations and certainly looked at -- looked at and have commented on and have generated many foundation bylaws.

And as I said earlier, I think these bylaws do not establish an independent grant-making foundation with any responsibilities for ongoing decision making about how the funds are used.

Q So would it be your opinion -- or excuse me. Would you say that -- that the -- these bylaws would be among the best you've seen or among the worst?

COMMISSIONER O'CONNELL: Is this your last question, Mr. Williams, or was the last question your last question?

MR. WILLIAMS: This was my last, yeah.

MR. BABLITCH: This question is just -- I know you're going to allow it in, Commissioner, but I just got to state very strongly, the best or the worst compared to what?

MR. WILLIAMS: The bylaws she's seen in her experience.

MR. BABLITCH: Bylaws are uniquely a conclusory legal decision, and -- and I think you've got -- if you're going to ask the question, and obviously it's going to come in, put some framework around it so we know compared to what. The worst compared to what? Walt Disney? I mean come on.

BY MR. WILLIAMS:

Q Well, compared to what we've been talking about

all morning, other proposed conversion foundations.

A Could I try to very, very quickly add a little to what I -- what I'm talking about when I say I think that an independent grant-making foundation would offer significant advantages in terms of being a decision-making body that would think about how to get funds used to improve the public health, I think that such -- I think that such a foundation would distribute funds in Wisconsin to a wide variety of beneficiary organizations and agencies.

The record of conversion foundations in -- in fact, of all health foundations suggest that would -- would be the case, and that seems to me to be the opportunity that we should really be focusing on here rather than quarreling about -- about the bylaws and -- and what they might compare -- how they might compare to other bylaws is to really think about the advantages of having a foundation that -- that would have the ongoing responsibility for thinking about the public health needs of this state and embracing a wide variety of different ideas about how to make a difference and

responding to those ideas.

COMMISSIONER O'CONNELL: Miss Madsen, do you have any questions for this witness?

MS. MADSEN: Could I give my place to Val Bailey and then I go after her, please?

EXAMINATION

BY MS. BAILEY-RIHN:

Q Miss, is it Cowan or Cowan?

A Cowan.

Q Excuse me. You're from Boston, correct?

A (Witness nods.)

Q And you are a -- have dealt with different public conversions prior to today?

A Correct.

Q Of those conversions, have any of those conversions that you've dealt with either directly or indirectly involved a proposal to put 100 percent of the asset of the converting entity into, and I should limit it to the Blue Cross Blue Shield conversions, into a public foundation?

A Well, yes. I believe so.

Q But you're not personally aware of any proposal -- for instance, the California

proposal, isn't it true that the California conversion initially dealt with the issue of whether or not any assets would be put into the foundation?

A Yes. There has been dispute about the amount, and that dispute happens in -- in different forms with the conversion as opposed to a sale, but -- but in at least two of the recent cases the -- the -- the proposal brought forward from the company was -- was to preserve 100 percent of the assets in the foundation vehicle.

Q And which two cases were they?

A In Maine and in New Hampshire.

Q Have those conversions taken place yet?

A In -- In New Hampshire the transaction is complete. In Maine the foundation formation is complete, though the sale is actually still under review.

Q You indicated that a private foundation set up would have about $2.5 million of overhead costs to set up a private foundation?

A No.

Q You said about 10 percent of the value of the assets.

A No. No. Of the annual distribution.

Q How much --
A Annual grant making.
Q So --
A That would be more like 1.2 million.
Q And that includes such things as lease, buildings, staff?
A Correct.
Q And that’s the initial start-up cost of a private foundation?
A No. That’s actually the annual operating expense. That research that I cited was about the -- what are the ongoing operating costs of foundations expressed as a percentage of their grant budgets.
Q Good. Thank you. What is the -- Expressed as a percent of the grant operations, what is the initial start-up percentage?
A I actually don’t know of any research on -- on that. You know, my common sense would say that -- that in the first year you might spend more to set up an office, for example, than you would spend annually, but there -- I don’t think there’s a reason to believe that you would spend, you know, 10 times as much.
Q Okay. But there is obviously start-up expenses.

A There are start-up expenses, yes.
Q And if I understand you correctly, your belief -- your belief is to -- the Blue Cross Blue Shield mission relates to the health of the public; is that correct?
A That’s right.
Q Have you had a chance to read the articles of the UW -- the UW Medical School or the Medical College of Wisconsin?
A The governing documents?
Q Correct.
A No.
Q Okay. So you don’t know what’s in their governing documents?
A What I know about their mission comes from their -- their own statements in the plan that -- that was -- was developed for this proposal.
Q Are you aware that the University of Wisconsin is a land grant institution that is a public entity?
A Yes.
Q Are you aware of proposals by the University Medical School and the Medical College concerning the oversight and supervision of the

funds that they will receive from the public health foundation?

A I have read in the -- in one case a proposal for the creation of an advisory committee, and in my -- and my understanding otherwise is that the -- the decisions about resource allocation would be made in -- within the usual process for budget setting and -- and so on.

Q So the advisory committee, is that referring to the Medical College proposal --

A Yes.

Q -- to put a public health foundation --

A I believe there was a proposal for an advisory committee of either -- either one -- one focusing area for that plan or -- or -- I believe that’s how it was.

Q And that advisory committee will be from the members of the public health area?

A Correct. That’s how it was -- That was how it was designed.

Q Are you also aware of the Medical College proposal to have an endowment fund which is composed of members from the public health area?

A No.

Q And you said you had read the proposal. Have

you studied the joint proposal in any detail?
A I have actually read it carefully, yes.
Q But you're not aware of the fact that the actual proposal itself includes a proposal to have public input on the endowment fund which will be distributing the funds throughout the years from the Medical College?
A Could you describe the -- the governance proposal a bit more carefully because I did not gather from reading the document that there would be any sort of new structure created that would -- that would stand -- stand between the, you know, the institutional decision makers and the use of these funds.
Q I'll be glad to. Let's see. I -- I just need to put my fingers on it.
COMMISSIONER O'CONNELL: We can go off the record for a minute while you locate that.
(Discussion off the record.)
BY MS. BAILEY-RIHN:
Q I'd like to direct your attention to page 31. Basically it provides "In addition to the advisory board of the Medical College of Wisconsin Institute for Public and Community

Health, the Medical College of Wisconsin board of trustees will create and appoint an endowment fund commission. This commission will have seven members. Commission members will represent a broad cross-section of individuals who have an interest in the health of the citizens of the state.

This commission shall have the duty to review and report to the board of trustees annually whether the projects funded by the endowment fund are in substantial accord with the Blue Cross Blue Shield public health foundation's general purpose statement and this plan's principles of stewardship."

A Thank you for reminding me. I did read that section and I do remember it now, and -- and my -- my understanding actually differed. My understanding is that this group would have a function quite different than the function of an independent health foundation in that it would be reviewing decisions already made and essentially serving as a check do these fall within the purposes or not, but it would not be reviewing a wide menu of possible uses and making decisions about A versus B versus C.

That was the distinction in my mind that seemed important.

Q Do you recall how the Medical School, Medical College decided to initially set forth their proposals regarding what to do with -- with the funds?

A I -- I certainly have read about the public -- the public hearing process, the public meeting process. I have not read about or don't know anything about what other internal discussions went on that led to the framing of these sort of rough allocations for the use of funds.

Q Would you agree with me that the citizens of the State of Wisconsin should have -- Obviously your concern is that there's public input to the proposed use of funds.

A Correct.

Q And are you also aware that the Medical College board of directors or board of trustees are appointed by the governor, a third is appointed by the governor of the State of Wisconsin?

A Yes.

Q Are you also aware that there were public hearings held in this matter contested when it became a contested case status where people

could provide public input into the proposed conversion?

A There certainly has been opportunity for people to be heard on this plan, but my understanding about the earlier set of public hearings, certainly the ones conducted by the institutions, is that that did not include really discussions about whether the institutions themselves were the ideal vehicles. The earlier hearings that were held in November I didn’t attend.

Q Okay. Would you agree that whether or not you feel that the Medical School and the Medical College are the ideal vehicles, certainly their proposal falls within improving the health of the public of Wisconsin?

A I -- I -- I certainly understand that they are institutions with important health focus, obviously, yes. I would be more concerned if they were, you know, institutions that -- if they were graduate schools of music, for example. That would be really alarming.

Q Right.

A Right.

Q You were also aware that they do have specific

proposals for public review of how the funds are being utilized through web pages set up and the fact that they are charitable or 501(C)(3) or equivalent status so that there are public records of how the money is used?

A I did notice the attention to reporting through a web site and so on, which again I would characterize together with the public hearings as, you know, very encouraging evidence that the institutions intend to be public in how they use these funds, you know, to the best of their ability.

I do think, however, that it is very -- it is very different to have a, you know, a board which reviews actions is very different from a board which makes decisions.

Q Well, you're also aware that there will be annual reports on a five-year supplemental or additional reports, public reporting on the uses of the -- of the funds?

A Correct.

Q Okay. And you are also aware that the proposal is that every five years that there be additional input from the public and additional input as to what the prospective five years

should look to?

A Yes, but I -- I believe again that the public will not have available to it in those reviews and forums the full range of -- of other alternatives, and that's simply a limitation on any institution that I think would be very difficult to transcend.

Both institutions have said forthrightly that -- there is a minor exception for one program which will actually distribute grants to community partners, but the two institutions have very forthrightly stated that they will use the funds within their own purpose, to enhance their own purposes to build on their own areas of strength, and have outlined uses of funds that involve the hiring of additional staff and the undertaking of initiatives by these institutions.

That is different than alternatives which would otherwise exist to distribute the funds to community groups, to public agencies, and so on, for their use. And it is -- it is one of the real advantages that I think philanthropy offers to any community is the opportunity to actually build and distribute

capacity broadly.

Q What about the proposals for partnership grants? The fact is that -- I guess I don't understand how the proposals set forth in great detail by the two colleges are any different than the proposals that would be initially approved by a private foundation. You still have a board of directors of the foundation making the determinations.

A Right. Well, let me try to illustrate what I think is the difference. There is a proposal for a small community grant program included, a way of funding partnerships with the institutions. That would distribute somewhere, the estimate is between 250 and half a million dollars out to community groups. The remaining funds would be spent, you know, by University researchers, by University deans, by University program staff to accomplish things, but it would be spent by the institutions.

If it were a private foundation, for example, then the amount distributed to community groups would not be up to half a million, but would be closer to 12 million. That money would be going out to a wide variety

of different kinds of organizations to help address public health needs.

Q Are you aware of the proposal to not overlap or to duplicate what is already in the public arena as far as public health? In other words, to not duplicate monies and funds and things that are already either statutory or already receiving funding.

A I think that’s a very important, you know, principle and -- and commitment, but I think the fundamental challenges that I see with this plan are about where you decide -- it’s about who you believe has the capacity and the ability to make a difference on health concerns. Do you believe that all that capacity is lodged within the two medical schools, or do you believe that if you took -- if you undertook a search you would find organizations distributed throughout Wisconsin who have the capacity to make a difference?

The experience of health conversion foundations around the country suggests that when you look broadly you find many, many actors who can be effective and make a difference.

Q When you say you look broadly, wouldn’t that include the public input that the public of the

people of the State of Wisconsin addressed as their concerns that was the basis for the formulation of the plan?

A I think fundamentally that people were never asked the kinds of questions that I believe are important. For example, you know, would -- if people were really -- people, for example, working in rural communities were asked how the -- what the best way to spend the funds, an annual budget of 12 million, would they be interested in rural health clinics, in transportation, in vans to deliver medical services to isolated elderly, or would they believe it was more important to invest in osteoporosis research? Those are the kinds of choices that I think are basically not available once you have made a decision to invest in two institutions exclusively.

Q But you weren't at the -- the public hearings that were held by the Medical School and the Medical College, so you don't know what the questions were asked.

A I was not there, that's correct.

MS. BAILEY-RIHN: Thank you. I have no other questions.

COMMISSIONER O'CONNELL: Miss Madsen?

EXAMINATION

BY MS. MADSEN:

Q Yes, I have a couple questions. Miss Cowan, other than reading the missions of the Medical School and the Medical College in the joint proposal, do you have any -- or other than -- other than reading the joint proposal, do you have any information on the public health service records and the public health outreach records of either of the two schools to the citizens of Wisconsin?

A I have made only one earlier trip to Wisconsin and -- and in that earlier trip I participated in community forums at which I actually heard from a number of people in the public health community, particularly people working in rural health districts, who expressed the difficulty of their mission, who expressed how much they could benefit from small additional amounts of funding, such as a health foundation might be able to convey, and who spoke about how little help they -- they felt they received from the schools two institutions. So I did hear from

people that kind of input on my earlier visit.

Q On one trip; is that right? You said one trip?

A It was one trip, three meetings. Three community meetings.

Q You testified about the -- or in answer to Miss Bailey’s questions you testified about the -- the national reports on the administrative overhead to a grant -- in a grant-making foundation.

A Right.

Q Isn’t there also, once the foundation makes grants to entities to deliver services, isn’t there then also administrative overhead in the recipient organizations?

A Well, of course, yes, it does take, you know, it takes money to run all kinds of organizations, universities and, you know, small rural health clinics. Yes, that’s true, but I think that it is very, very well understood in the grant-making community, and I believe this is a reason why you see the kinds of patterns that I’ve described earlier today which really do not emphasize funding for research, it is widely understood that the overhead costs associated with the universities and medical schools are

much higher than they are for community-based organizations.

You would not see anything like an administrative cost charge of 44 percent with a community -- a community organization. That would be very unusual.

Q Yes, but I was asking you, Miss Cowan, using your model, that's what you're saying is the national model, grant-making foundations having an overhead, administrative overhead of say 10 to 20 percent, and then you were then attempting to compare it to what you think is the administrative overhead at the University, although you demonstrated no basis for that, I think, isn't there -- don't you also have to add the administrative overhead of the organizations that are receiving in order to make a valid comparison?

A I think valid comparisons around this issue are in fact difficult as -- as you suggest. It costs money to do all kinds of things.

I think the key question here, though, is about the investment of these funds and what kinds of organizations and how broad a net you're willing to cast in terms of answering

who shall benefit from these funds. All organizations do have overhead, and if you elect to give the funding entirely to two medical schools you'll be paying only the overhead of the two medical schools.

If you have a foundation with a broader mission you may be paying overhead at a wider range of different kinds of organizations, and I'm suggesting, or my belief is that -- that the public ought to have an opportunity to make that choice.

Q Yes. We're aware of your opinion on that, Miss Cowan, but I would ask the Commissioner to strike that last answer as not responsive to the question.

COMMISSIONER O'CONNELL: I will allow the -- the answer at this time subject to your objection.

MS. MADSEN: No further questions.

COMMISSIONER O'CONNELL:

Mr. Bablitch?

EXAMINATION

BY MR. BABLITCH:

Q I have a few questions. You are not a lawyer, correct?

A I am, that’s correct.
Q What is your degree in?
A I have a Bachelor’s Degree and a career in Grant Making Institutions and Foundation Management.
Q Do you have a Ph.D. or a master’s degree?
A No, I don’t.
Q Is there a science of philanthropy?
A There certainly is -- you know, there certainly is a career track in philanthropy and there are in fact some educational programs in foundation management. I’m not aware of a degree program in foundation management.
Q With respect to your testimony about your opinions, is this a scientifically based opinion?
A It is an experientially based opinion.
Q And so when you look at foundations in other places, in other states, and compare them to here, it’s based upon more or less your experience and preference?
A It’s actually based on my work in the field and my specific work over the last two-and-a-half years in -- in participating in the start up and observing the operations of these foundations.
Q When you talk about the mission of Blue Cross

Blue Shield United of Wisconsin in response to one of the questions you said that you believed that that was for the health of the public, correct?

A (Witness nods.)

Q Is that a yes?

A Yes, that is correct. For the health of the public and for specifically improving access to health.

Q You would agree, wouldn’t you, that research improves public health in medicine?

A I would agree that research is one of the things that improves public health, yes.

Q Well, you would agree that the research that led to the polio vaccine improved the public health, wouldn’t you?

A I would actually agree that the research that lead to the polio vaccine improved public health, yes.

Q In a big way, right? In a big way?

A In a big way.

Q So if research that one of the two schools did actually found the cure for cancer, that would be quite an improvement in the public health, wouldn’t it?

A There are many ways to address improvements in the public health.

Q Well, answer this one.

A Research and certainly finding a cure for cancer would have a major impact on the public health, but let me add to that that -- May I add to that?

Q Sure. You'll be allowed to I'm sure.

A That it is widely -- it is widely understood that in addressing efforts to improve public health we -- we are faced with the fact that many of the things that make us ill are -- are affected by issues of environment and lifestyle and social condition and even economics. And that is why many institutions, grant-making institutions charged with improving the public health look for a wider range of potential avenues other than just research.

Q Did you read the transcripts from the November 29th and 30th hearings?

A You know, I can't recall.

Q Did you read any of the testimony that was submitted to the Commissioner in response to the plan of conversion and those hearings?

A I have read some of it. I probably have not

read all of it.

Q Did you -- Do you recall reading anything from Dr. Carbone at the University of Wisconsin Medical Research?

A No.

Q With respect to some of the other conversion plans you mentioned specifically the number of hearings that were held in Maine and New Hampshire.

A Um-hum, that's correct.

Q Those in fact weren't conversions, were they? They were rather sales to Anthem of Blue Cross, which is the Indiana Blue plan?

A In what way would you consider that not --

MR. WILLIAMS: I'd like to object to that question. Doesn't that call for a legal conclusion of those transactions?

MR. BABLITCH: What's sauce for the goose is sauce for the gander.

COMMISSIONER O'CONNELL: I'll allow the question.

THE WITNESS: Without getting into the technical question that you're raising, those were certainly both proposals in which the company, the nonprofit plan, was not going to

continue and its assets were going to be transferred to a new health foundation.

BY MR. BABLITCH:

Q They were actually sold.

A They were sold, correct. Those were sales.

Q You mentioned the hallmarks of a good foundation board and you listed the number one criteria as that it should have distinguished board members, correct?

A I actually listed several criteria and distinguished board members of relevant experience and diversity.

Q But you are not familiar with the board members that are proposed for this foundation?

A I have not heard their names or their background.

Q So you are unfamiliar with, for example, Howard Fuller?

A I haven’t -- I don’t know who in terms of what people are appointed to that board.

MR. WILLIAMS: The witness has answered that she is not aware of who the members of the proposed public health foundation are.

BY MR. BABLITCH:

Q Well, if you heard that one of the members of the proposed board is a person by the name of Louise Trubek, who is the Executive Director of the Center for Public Representation in the state, wouldn't you say that she meets the criteria that you've listed for a foundation board?

A What I would say in answer to any question about the people on that foundation board is that the foundation board doesn't have any decision-making role. It simply conveys the funds to the two institutions and they make all of the subsequent decisions. So who sits on that board would really not be of very great interest.

Q In terms of the WellPoint conversion, were you aware that WellPoint, that is, Blue Cross of California, was -- had a tax exemption to the day that it converted?

A Yes.

Q And so that's quite a different scenario than what we face here, correct?

A Well, I have not understood tax exemptions, the current tax exempt status, to be the primary issue determining whether there are nonprofit

assets that need to be preserved or not.
Q Well, with respect to the other Blue plans that have converted, are you aware that when WellPoint converted their initial offer to put into a public foundation was $20 million?
A Yes, I'm aware of that history.
Q And through negotiations they came up with their 3.2 billion. You're aware of that?
A Yes.
Q And with respect to Trigon, that is, Blue Cross of Virginia, when they converted they contributed $175 million essentially into the general fund or the state, correct?
A Correct.
Q And when Kentucky was recently purchased by Anthem, they contributed $45 million into a foundation. Do you know that?
A I'm familiar with all of that history and --
Q Are you also familiar that in the Right Choice example, that they were actually taken to court and as a result of that court settlement that they came up with less than 100 percent of the existing value of the Missouri Blue Cross plan?
A Yes, and I -- and I -- I was favorably impressed and -- and can remember my response when I heard

that the proposal in Wisconsin did not dispute whether or not there were assets that needed to be preserved. My first reaction on hearing that news was well, that's good. That part is good.

Q Good. We agree. With respect to the -- the document from the two schools entitled Advancing the Health of Wisconsin's Population, I believe the exhibit is still in front of you. Have you read that document?

A I have.

Q Have you talked to anybody at the two schools about its proposal?

A No.

Q Have you read any of the survey data that was used to -- by the two schools to determine the public health needs in Wisconsin?

A I have read the report, including the summary of the survey document.

Q And so you're familiar with the plan of the two schools contained in this document?

A Yes.

Q Would you say that -- in your opinion that this plan does not improve the health of Wisconsin?

A What I would say about this plan is that any one of the ideas included in this document would be

valid ideas to be brought forward for consideration and that it would be ideal to have the proposal to establish the office of an Assistant Dean for Rural Health to be considered as a way, a fundamental way of improving the health of people who live in rural communities, but my own opinion is that it would be preferable to have that idea evaluated next to other proposals to improve the health of people living in rural communities.

Q So it's safe to say that if the two schools do everything that they say they're going to do here, they will improve the health of the citizens of Wisconsin.

COMMISSIONER O'CONNELL: That is a yes or no question.

BY MR. BABLITCH:

Q That is a yes or no question.

A I actually don't know.

MR. BABLITCH: Thank you. Nothing further.

COMMISSIONER O'CONNELL: Okay. We'll take -- I'm sorry. Redirect.

EXAMINATION

BY MR. WILLIAMS:

Q We have one question. Miss Cowan, is it your understanding that either the Medical College of Wisconsin or the University of Wisconsin Medical School would be expected to apply for grants to an independent public health foundation if one would be created?

A I've just said that I think any of the ideas in here ought to be brought forward for consideration together with other ideas. My quarrel is not with do they have any ideas about how to improve the public health. I think they do, and I think that those ideas should be considered in the context with other ideas because my own opinion is that many other organizations distributed around Wisconsin know a lot about and have a lot of ability to work on health improvement goals.

COMMISSIONER O'CONNELL: Okay. We'll take a 30 minute break and reconvene at approximately 1:05.

(Lunch recess taken.)

COMMISSIONER O'CONNELL: We'll reconvene the hearing. It is now approximately 1:15. Mr. Peterson, you may call your next witness.

MR. PETERSON: We'd like to call Peggy Hintzman, who's President of Wisconsin Public Health Association, as the next witness.

PEGGY HINTZMAN, called as a witness herein by the Coalition, after having been first duly sworn, was examined and testified as follows:

EXAMINATION

BY MR. PETERSON:

Q Good afternoon. Peggy, as I mentioned, we're calling you as a -- as a witness today as a public health expert. Can you tell us a little bit about your expertise and what qualifies you in terms of a public health expert?

A As you mentioned, I am the current President of the Wisconsin Public Health --

COMMISSIONER O'CONNELL: Can you speak up? The court reporter is having trouble hearing you.

BY MR. PETERSON:

Q Is your microphone turned on?

A I am the current -- I am the current President of the Wisconsin Public Health Association. I'm also a member of the executive committee of the Public Health Advisory committee. I have 20

years of work experience with Public Health Laboratory, and I am one of three persons that is responsible for leading the Turning Point state's process for establishing a public health improvement plan for the next 10 years.

Q One of the areas that we would like you to comment on is just briefly going through for us what public health is because there's some confusion in terms of medical care versus research versus public health. Could you briefly describe for us what public health is?

A No. Public health is broad and it is very encompassing, and the testimony that has been given over the course of the last eight months or so I think underscore how difficult it is to understand public health.

Public health is a crucial element of our society. It's easy to look and see police and fire, very visible components of our society that provide specific purposes. Public health is usually considered very invisible until something goes wrong.

So putting a name to it and giving definition depends on where you are in the public health system as to how you see the

practice and role of public health, but let me give you a couple of definitions that I think encompass that broad range.

One is public health, the purpose of public health is to ensure that communities are -- excuse me, to ensure conditions in which communities can be healthy. Public health is healthy people in healthy communities. The one I like best is public health is the science and art of preventing disease and injury, prolonging life, and promoting health through organized community efforts.

Sometimes it’s easier to understand what public health is by seeing what public health does. A national group in 1994 tried to specify the essential elements of an effective public health foundation and they codified these -- I’m sorry, they put these in something they called the 10 Essential Services of Public Health.

Those things consist of monitoring the health of the community. These are ongoing, real and important functions that public health does to assure that the community is free from disease and from unsafe practices.

They investigate health problems. These could be as dramatic as outbreaks that involve E-coli infections, or they could -- and tuberculosis, or they could be small community related issues regarding the inappropriate disposal of waste and other garbage. They're responsible for educating, empowering people about health. Helping people have the right information on which to base their own decisions and healthy lifestyle choices.

The public health system mobilizes partnerships. They get others in the community who have resources and skills to help address the needs of their communities. They do enforce laws, conduct inspections of your restaurants to make sure that they are safe, conduct inspections of your water systems to make sure that you have good water. They link people to needed personal health services and provide those services where appropriate.

There's a vulnerable population in the State of Wisconsin, as throughout the nation, and this group needs special attention to get them to the resources that are needed to attend to their needs.

They assure a competent public health workforce. They evaluate the effectiveness, the accessibility, and look at population-based health services. And they do research.

Q Thank you. But who actually is out there and responsible for doing the work of public health?

A Many. Government certainly has a statutory mandate both at the state and local level to carry out the primary functions of promoting and protecting the health of the public, but this is done through a public health system which collaborates with many partners throughout the State of Wisconsin, including our institutions of higher education, including the medical delivery system, including law enforcement and the faith community, nonprofit organizations. It's a group of folks committed to a single purpose, which is the promotion of health in our communities.

Q Are public health and medicine the same thing?

A No. Public health and medicine, medical care, are different. Medicine and medical care tend to focus on the individual patient. You present yourself to your doctor and you want your doctor

to be fully focused on you as an individual patient understanding what symptoms you're presenting, what cures and treatments would best relieve you from pain or improve your life.

Public health has as its patient the population as a whole. We look at populations of people and ask how can we make them more healthy, and more importantly how can we keep them healthy. Public health focuses primarily on prevention rather than treatment.

Q What about public health research and medical research? We heard general counsel, Mr. Bablitch, discuss polio research, for example. What's the difference there?

A Right. Sometimes I'm not sure it's important for us to make that distinction because in so doing we -- we create a situation of identifying what the research is for instead of how medicine and public health may use the same research, but, for example, medical research might be an example of drug trials where you're investigating whether a certain drug A or certain drug B is better at lowering cholesterol levels. Since the effect of that research will impact on an individual patient, that would be

primarily medical research.

If we're looking at a population of folks with poor dental health and we're seeing if the influx of fluoride in the water system makes an improvement on that, that would be public health research because it is basically intervening at a population level.

We acknowledge that the studies and research done in our research institutions often lead to important results for public health. The example that -- that you asked about, polio, is one that's very personal to me. My brother and I were little when he was a victim of polio, and so I've been very interested about that time of our lives.

Yes, polio vaccine was an amazing discovery for all the world, but before everyone became inoculated and we had irradicated polio in the world, or in the United States, there were a sequence of trials that led to vaccines that also caused more polio. When the new vaccine, the working vaccine, finally was available, some physicians were advising their patients not to take it because they weren't sure. When that vaccine was available, how did

it get to the public? What were the mechanisms that needed to be activated in order for each of us to benefit from that discovery? It was the public health system. Public health workers, professionals organizing their communities to make sure that that population-based intervention reached everybody.

So you can see the two things blend together and they're very important. You can't just do the research and let it move on to individual interventions. You need to actually get it out into the communities, and that's where the public health system becomes essential.

Q There seems to be an overall misunderstanding of public health, and I'm wondering how does the public generally understand what public health is?

A When you ask the -- There are several polls that are done every so often. The Charitable Trust organization does some polling, as does the Harris poll, and when people are asked about the importance of public health or even what public health is, their responses certainly indicate a lack of understanding of what public health is,

but when the poll continues to mention specific components of public health, such as the prevention of disease, such as the importance of immunizations, the public generally responds most favorably to providing support for those functions.

So without knowing what label to put on those functions, the public in general is very supportive of the activities that public health provides.

Q Why do you think it’s so important for us to fully understand public health?

A Well, I think it’s important for our decision makers, state and local decision makers, to understand what public health is so that they better understand their role and responsibilities and the opportunities that are available to support public health.

I think as we look forward to the decisions on this foundation, this public health foundation, it is important that we know what public health is so that we might create a foundation with a true, clear, sole mission of serving public health and not confuse that motion with the multi-faceted missions of any of

the partners who support the public health system.

Q What are the priority setting mechanisms in Wisconsin for public health?

A There are two major ones. One is a statutorily required creation of a state health plan. This is responsibility that is led by our Division of Health and Family Services. Excuse me.

In other years we've produced a public health improvement plan that has had 300 objectives. This year we are so excited about the new shift in the way we are doing this. This is the Turning Point project I provided some information to you earlier on this.

Turning Point will result in more than just a state health plan. It is a paradigm shift for the way we assemble and carry out public health in Wisconsin. We're going to define what public health is so that the communities all have a shared definition of public health, and we are going to lay out the functions of public health as a part of that.

This group is working as a basis from those 10 essential services I mentioned. However, the group is also looking beyond those

services and saying what is -- what is appropriate for Wisconsin? How do we enhance this particular picture for Wisconsin? And they'll be adding, I suspect, two additional features. One is underscoring the importance of access to health care and another related to the social and economic impact, the underpinnings of that that are important to sustaining good health.

This is a highly collaborative process. It involves a transformation team, which is our strategic planning group of 45-persons representing broad sector leadership throughout the public health community. We have members from the medical community. We have health care payers on our team. We have the faith community, the workforce labor community, we have academia, we have state departments and local departments all involved in this process.

It has been a scientifically-driven process collecting data from -- by starting with community review teams and identifying the needs of those communities as individual communities and then assembling those to get a bigger picture of what's happening within our state.

Another amazing change that will happen with respect to this plan is that in other years the recommendation, the goals, the objectives, have related to disease conditions; cancer, heart disease. This year we are trying to push ourselves to understand the underlying causes of disease, the root causes of disease, the risk factors, and select those as our priorities. That way we can assemble a wide state commitment to carrying out the health plan and achieve advances across many different diseases that share those same risk factors.

Q Are there other formal assessments that are going on right now in the State of Wisconsin?

A Each community is also required to do an assessment. These assessments are led normally by our local health departments, but again, these are highly collaborative. They involve the whole range of persons in that population.

The beauty of the local health assessments are that the people who live there are doing them. They know how to tap into their own community. Where are the pockets of folks who are unrepresented, and get them to the table.

They also know that once they've identified the needs of our community -- their communities, what are the best interventions that fit that community. It certainly isn't one size fits all.

Q Sounds to me that there's state-wide planning, local planning, going on in terms of public health needs and that the time is -- is right for a public health foundation to help address some of those needs. Would that be a fair characterization?

A Absolutely. There is no single source of support in Wisconsin for public health. There is much to be done and there's much that could be done with the support of a foundation that is focused on public health needs.

Q You heard CEO Tom Hefty talk about concerns that funding could be frittered away by a foundation. Do you think that would happen with the public health foundation in Wisconsin?

A With all due respect to Mr. Hefty, that was very insulting, but it also has been written in the newspaper by others, so I know that he is not the only one that shares that opinion.

I think that stems from the lack of

understanding of what public health contributes to our society. There are very visible things that happen. Before looking at cancer research, as an example, and the opportunities afforded by the advances in medicine for people to live longer with that disease or even to put that disease in remission, that is wonderful, but many people can’t access those treatments and those cures and those surgeries. 60 to 70 percent of all of the advances that would help make our population healthier are related to behavior and risk modifications. These fit very nicely with public health.

Public health does simple things and they do things for our most vulnerable population. Those are not things that generally get a lot of attention. And so when people think that public health dollars are frittered away, I think it really is a result of not understanding the use of those dollars and how people at the lowest level in our society are improved by simple things that make their life better.

An example. We have in our northwest area a group of counties, this would

be around Dunn, Eau Claire, Chippewa, that area, who have decided or have through their assessment process seen a need for dental care in the youth of those communities and they have put together a bus that is fully equipped that they drive from community to community staffed with volunteers, and their goal was to see 500 patients in their first year. They have seen in less than one year over 3,000. The need is great.

Yesterday when someone learned that I was going to be testifying today they asked me, I work in Madison. I need dental health for these children that are coming to my community clinic. What can you do for me?

The need is great, and the opportunities to serve in small ways, not ways that are going to be glitzy and grab the attention of the newspapers, but ways that are going to substantial change the lives of our citizens.

Q How is public health currently funded?

A Glibly she says poorly. Most of the public health funding comes through federal, state, and local tax dollars. And to give you a couple of

numbers on those, in a national study done by the MMRW, the Morbidity and Mortality Weekly, which is produced by the CDC, they reported that $34 per person are spent annually throughout the United States on public health. To put that in context, we spend a little over $3,000 per person on health care.

In Wisconsin we have a state-wide expenditure, this is looking at all the dollars that go in from our state to our local communities. That expenditure is $95 million, and that is for a population of about 5.2 million people. That isn't very many dollars per person to carry out the essential services of public health. 56 percent of those dollars come from the local tax base, which as you know is a very competitive place to be trying to acquire greater funding.

Q Would you say it's difficult for -- for public health to access funds for services?

A Yes, it is. Public health has as a national funder the Centers for Disease Control. The Centers for Disease Control budget is about $2.8 million, as opposed to the NIH, which -- the National Institutes of Health, which fund a lot

of the medical research. Their budget is about $17.8 million. It is fairly limited.

Competing nationally is always very difficult for precious dollars. Being able to have dollars available in Wisconsin would be a most important improvement for our ability to tap into programs that are working and extend those programs to more people.

Q So right now there isn't a state-wide foundation that has identified many of the public health needs for people that -- that -- public health that agencies could go to to look for funding to help with innovative solutions to address public health needs?

A That is correct. There's no single source devoted to supporting public health needs of our state.

Q You've mentioned access to funds, the limited access to funds for local public health programs. How does this relate to access for funds for medical research?

A I was curious about that as well, so I wanted to see about our two medical schools and their ability to acquire research dollars, because that is important. And what I found was that

the total extramural research award for the University of Wisconsin Medical School is about $115 million annually.

Q Now, that's more than the whole public health budget for the state.

A Yes. And it represents 32 percent of the total extramural funding for the whole university. So they're extraordinarily successful at tapping into other sources of funds.

Likewise, the Medical College of Wisconsin reports that in 1998 they received $66 million of external support for research and training.

Q What does this mean with respect to a public health foundation?

A Well, to me it means that there ought to be an independent foundation with the sole mission of supporting public health in Wisconsin and that it should be focused on community-based initiatives and partnerships, that it must be focused on prevention, that it should elevate our most vulnerable populations, and that it should in the end improve the life of all.

Q Do you think that the medical schools should be prohibited from applying for any grants from an

independent foundation?

A No. That I think the medical schools are an important component of the public health system. Our ability to work more collaboratively with our medical institutions is essential and no, they're a valuable partner and they should also be a respected applicant to an independent foundation.

Q Okay. What do you think -- How do you think the state of public health will be affected if the current proposal as put forward for the monies to be designated to the two medical schools is approved? Do you want me to restate the question?

A Yes, please.

Q Under the current proposal, Blue Cross Blue Shield has designated that the two medical schools would be the recipients of the 100 percent equity value of the organization. How will that decision affect public health in Wisconsin?

A I think it will limit the access to funds for some of the most important community-based needs. It may also limit access to some of the basic infrastructure recommendations coming out

of Turning Point. One of these is surely to be an integrated data system of which all public health partners, medical community partners, may have access.

These things we will find difficult to fund without the ability to go to an independent foundation with a sole purpose of supporting public health.

Q In terms of a proposed independent public health foundation, what is your opinion in terms of the type of input that should be provided to create a public health foundation?

A Could you say that in a different way?

Q One of the options available is for an independent foundation to be developed. How would you and the Public Health Association and groups that you're affiliated with be able to contribute to the development of an independent public health foundation?

A I think the public health community has very good collaboration and ability to organize things. We would be excellent consultants and we would be excellent participants on an independent foundation.

Q You also mentioned that you serve on the Public

Health Advisory committee which includes representatives from the two medical schools. Could you talk about the resolution that was passed by the Public Health Advisory committee?

A Yes. The resolution that was passed was forwarded to the Commissioner late last year, I believe. This resolution endorsed an independent foundation that would be -- on that foundation would be representatives from the many different partners that participate in the health of our public.

MR. PETERSON: Thank you. We have no further questions?

COMMISSIONER O'CONNELL: Miss Madsen, do you have any questions?

MS. MADSEN: I'd ask if Ms. Bailey could proceed first, please.

EXAMINATION

BY MS. BAILEY-RIHN

Q I believe you previously indicated that one of the definitions of public health is healthy people and healthy communities; is that correct?

A Yes.

Q And that some of the focus of the Turning Point is now, at least one of the focuses, disease

conditions and underlying causes of disease; is that correct? Or restate it. I may not have gotten it down correctly.

A I get a little uncertain because we had in our Turning Point process great care over labeling what our focus areas and what our recommendations are, so.

Q Okay.

A That's all I'm asking for, but we are looking at -- there were probably five overlying recommendations coming out of Turning Point, and would you like me just to say what those are?

Q Yeah. Why don't you?

A One will generally be related to partnerships and collaborations. One will generally be related to finance and funding. Another will address the issue of vulnerable populations. The integrated data system is a fourth, and a fifth is -- I don't remember right now.

Q Was it prevention or something to do with --

A Prevention will under -- undergird all of that. If it comes to me I would add that.

Q Okay. That would be great. So have you had a chance to read and look at the joint proposal that the two medical schools have put together?

A Yes.
Q And, you know, some of the proposals for the UW Medical School is to enhance community in the role of health funds through the form of partnership. Is that something that the various community public health groups would be able to partnership with the UW Medical School on?
A From -- From what description I've been able to read and having further explanations of it, that does sound very compatible with some of the goals that we have stated.
Q In the same way the commitment of serving the underserved populations of Wisconsin?
A Again, the proposal sounds interesting.
Q Okay. But that is some of the concerns of your group is the underserved population?
A Yes.
Q And rural health I'm assuming is also a concern?
A So are you relating that right to Turning Point, or in terms of the public health community as a whole?
Q I would say the public health community.
A Yes. Rural health, again, because of the special needs that exist in those communities are a concern.

Q And another concern is preventing underlying causes of disease by -- through research or modifying or controlling factors?

A Right, though much of the research has been done and we know what those underlying risk factors are already. What we need to do is do something about it. We need to activate community systems or plans that relate right to that community to help people change their behaviors so that they do the right thing.

So the underlying risks are pretty clear what they are. So research into that is probably not needed in-depth anymore.

Q So if I understand you correctly, your proposal is you'd like to have some form of partnership or collaboration to access funds for certain areas that you perceive are needed public health issues?

A What I want to present is not a list of things that we want funded. What I want to present is the need to be able to access a source of funding for public health needs that are based on the assessment processes that are currently being carried out very effectively in our communities.

So I don't want to say what is most important to us in terms of the kinds of programs, but it's more how we can access those programs and convey to the foundation what our needs are, and then as you said how do we develop the collaborations, tune into all of the skill sets that are needed to activate the interventions.

Q So would you be comfortable -- I mean you talk about a foundation, but would you be comfortable if you felt that you could access the funds under the current proposal from either the UW Medical School or the Medical College?

A I think the key word there, to be frank, is would we feel comfortable, and getting comfortable is part of the issue for us right now because we are skeptical of the commitment to really carry this out in a true collaborative fashion.

Our skepticism comes from the fact that up to this point I am not aware that there have been announcements or bulletins saying that funds are available to communities from either of the institutions. So there's not a history on which to base our sense of confidence that

this will actually happen in the way that would be most effective for public health.

If we get by that, yes, it could work, but it's the track record of convincing us that putting our eggs into this boat is better than going with an institution that is created for the sole purpose of tapping and supporting public health.

MS. BAILEY-RIHN: I don't think I have any other questions.

COMMISSIONER O'CONNELL: Miss Madsen?

EXAMINATION

BY MS. MADSEN:

Q Yes. Miss Hintzman, I'd like to refer you to a letter you wrote to Commissioner O'Connell on September 11, 1999. It is in the record as Exhibit I21 and I'll just read -- this was the one that you referred to in your earlier testimony about the WPHA board passing a motion recommending certain things, and I'll just read you the third recommendation.

"A permanent endowment be created from these community assets to be held in perpetuity with the proceeds being used to meet

current and future public health priorities as they develop in the future," right?

A That sounds correct.

Q And you said earlier in answer to Miss Bailey’s question that you had read the joint proposal.

A Yes.

Q I ask you, isn’t that exactly what the two medical schools propose to do, is to set up a permanent endowment from these assets from the Blue Cross conversion to be held in perpetuity with proceeds to be used to meet current and future public health priorities?

A I think there is a component in the plan that does call for the endowment, so from that perspective I would have to say they have met that qualification, but it doesn’t meet the spirit of what we’re asking for in terms of the totality of accessing all of the funds that are available.

Q But isn’t it true that the bulk of both the schools’ allocation of the funds will be for a permanent endowment to use to address public health priorities?

A No.

Q Does the joint proposal of the UW -- the part

relating to the UW Medical School's proposal address the state's Turning Point project?

A I do think that in there they have referenced the opportunity to look at the recommendations that come out of Turning Point. And in fairness, the recommendations have yet -- have not yet emerged, and so the match is yet to be made.

Q So would it be fair to say that in the joint proposal the UW Medical School has made a commitment to use the Turning Point recommendations in its work and in utilizing these Blue Cross funds?

A I would like to think they made that commitment.

Q Okay. Miss Hintzman, you I believe alluded in your direct testimony that you're employed by the State Laboratory of Hygiene, right?

A I said I was employed by a state public health lab, but I am employed by the state lab.

Q Wisconsin State Lab of Hygiene?

A Yes.

Q And are you aware who founded the State Lab of Hygiene, what entity founded it?

A It came from a public health -- I can't remember.

Q Would it be correct that the Medical School, the UW Medical School founded the state lab?
A I think it was founded in conjunction with the Medical School and the Department of Bacteriology and was later connected to a State Board of Health. So yes, I would say that that was part of the fundamental organization.
Q And the Department of Bacteriology that you referred to is the UW-Madison Department of Bacteriology?
A Yes.
Q Okay. And the Director of the State Lab of Hygiene currently and probably for the last 10 to 15 years is a gentleman by the name of Ron Laessig; is that correct?
A That is correct.
Q And does he hold a faculty appointment at UW-Madison?
A He does.
Q And what is that?
A He’s a Professor in the Department of Preventive Medicine.

MS. MADSEN: Okay. That’s all I have of this witness.

COMMISSIONER O’CONNELL:

Mr. Bablitch?

EXAMINATION

BY MR. BABLITCH:

Q I have a few questions. Miss Hintzman, prior to today we were given your vitae. If I could just ask you a few questions about that. It was one page, so I'm assuming that that was complete. It indicates that you have a Bachelor of Arts degree in English; is that correct?

A Yes.

Q And it also indicates an MBA from the University of Wisconsin-Madison in 1987, but it doesn't indicate what that degree was in. Could you tell me what that was?

A It was in administration.

Q Administration as in public administration?

A No, management. It was a general administration management major.

Q Okay. It doesn't list any kind of formal medical training, so I take it that you have had no formal medical training?

A Correct.

Q And it lists that in -- your work history from 1980 to the present you have been the Assistant Director of the Wisconsin State Laboratory of

Hygiene?
A Yes.
Q What do you do as the Assistant Director of the Wisconsin State Laboratory of Hygiene?
A I work in the administration function. I do not work at the bench. I am not a chemist or microbiologist. I look at -- Some of the major things that I have done relate to organizational structure, making the lab more efficient, and I spend a lot of time in strategic planning.
Q Okay. And I take it that you're here today not as a state employee, but rather in your role as a member of the Wisconsin Public Health Association?
A Yes, that's right.
Q It also on your vitae it lists your what's called relevant activities, and it lists that you are a member of the Wisconsin Public Health Association. That's correct, right?
A Yes.
Q It says that you were a board member or officer from 1995 to the present?
A Yes.
Q I don't see anything prior to 1995 in terms of the Wisconsin Public Health Association. Am I

to assume from that that you started in that association in 1995?

A I became a member I think at the end of 1989.

Q So it would be -- your vitae then would not be absolutely correct if it says 1995?

A It’s apparently incomplete.

Q Okay. So from 1989 to the present you’ve been a member of the Wisconsin Public Health Association?

A Yes.

Q And you’ve been an American Public Health Association member from ’95 to the present?

A Yes.

Q So for the last five years you’ve been a member of that association?

A Yes.

Q In that association there are a variety of members, aren’t there? It’s comprised of a number of people?

A You’re talking about APHA?

Q No. Let’s stick with the Wisconsin Public Health Association.

A A variety of members, and so you’re talking about the professions that they come from?

Q Yes.

A Yes, that is correct.
Q And do you know who Cathleen Blair is?
A Yes.
Q If she were to have testified on November 29th, 1999 in this matter as follows, I'm going to ask you whether or not you agree with her. "Current proposal creates a prominent role for the University of Wisconsin Medical School and the Medical College of Wisconsin. These two institutions are recognized centers of excellence in medical research and teaching, and as such contribute greatly to improving medical practice and ultimately the individual health of our population." Would you agree with Cathleen Blair's statement?
A Yes.
Q Likewise, are you familiar with a person by the name of Dr. Scheckler, S-C-H-E-C-K-L-E-R?
A Yes.
Q And who's he?
A Dr. Scheckler is on the faculty of the University of Wisconsin. My acquaintance with Dr. Scheckler is that he is also a member of the executive committee of the Public Health Advisory committee.

Q And you are a member of that committee as well?
A Yes.
Q If Dr. Scheckler were to testify, as he did, on November 29, 1999 as a supporter of the concept of -- of the conversion of Blue Cross Blue Shield -- or strike that. Let me read you a statement of Dr. Scheckler and see if you agree with him.

"There would be absolutely no need for establishing an additional foundation or infrastructure if the funds were deposited as currently envisioned, and I can see no persuasive reason why the existing foundations for both medical schools could not be used as the repository of funds." Would you agree with him?

A No.
Q So there is, it’s safe to say, a diversity of opinion within your association.
A I do -- I guess that would be true. I suspect there’s a diversity of opinion within any association, and what we try to do is represent the opinion of most of our participants.
Q So what you’re presenting today is one part of the opinion. Dr. Scheckler might have another

opinion with respect to the use of these funds. Yes or no?

A Dr. -- It sounds like Dr. -- I know something else. Can I say that after I say yes or no?

Q Why not.

A I'm not sure of the dates of -- Is the letter from Dr. Scheckler --

Q It's his testimony at the public hearing of November 29, 1999.

A I believe subsequent to that testimony Dr. Scheckler, as a member of the Public Health Advisory committee, signed off on the Public Health Advisory committee's recommendations for an independent foundation.

Q Do you have that document with you?

A It should be --

MR. PETERSON: It's part of the record.

THE WITNESS: I can make it available.

MR. PETERSON: It should be a part of the record that was submitted to the Commissioner. It was a letter that was sent in.

MS. WALSH: Any idea of approximate dates?

MR. WILLIAMS: Before December 14th.
THE WITNESS: It was signed by four or five people.
BY MR. BABLITCH:
Q I trust you.
A Thank you.
Q Did you listen to any of the testimony at those two days of hearings back in late November?
A I was at the hearing.
Q So did you hear Dr. Paul Carbone at that hearing?
A Yes.
Q Are you familiar with Dr. Carbone and his work?
A I am familiar with it as a layperson, yes.
Q Would you say that he has an excellent reputation in the community as a medical researcher?
A Yes.
Q So you recognize him as a professor emeritus from the University of Wisconsin Medical School?
A Yes.
Q And did you know also that he was a member of the -- he was a retired Public Health Services officer at the National Institute of Health?
A I did not know that.

Q It wouldn't surprise you, though?
A No.
Q Okay. Dr. Carbone testified as follows, and I wondered if you care to dispute Dr. Carbone's testimony or not. "I'd like to make -- the point I'd like to make is that the model of public health center is as separate from the research as backward looking. It represents the old model of infectious diseases where you can prevent disease by isolating people from those who have the disease from those that don't.

Today's problems are completely different. They are not going to be handled by individuals in separate county public offices. Those people have to be tied in closely with the medical schools and the research that's going on in the medical schools and not just in our own schools but nationally and internationally." Would you agree with that?
A It's hard for me to say I would correct Dr. Carbone given his credentials, but I think what he is saying is true in one respect, and that respect is the need for medicine and public health to work together. That the need to use the research is important.

I think the fact that -- What I'm thinking he's saying is that public health needs to be tied to medicine. I would say medicine needs to be tied to public health, and it is a different direction. Instead of looking out the windows from our institutes of higher learning, from our research institutes, we want to be sitting and -- having them sitting in our communities looking in and then carrying out the principles that will help improve the public.

Q Well, when Dr. Carbone testified in support of the plan proposed by the two schools, I take it that you and he just plain disagree with respect to the expenditure of those funds?

A Plain disagree. We are in disagreement.

Q So reasonable people can differ when it comes to how these funds are going to be expended, correct?

A Certainly.

MR. BABLITCH: Thank you. Nothing further.

COMMISSIONER O'CONNELL: Thank you. Do you have any redirect?

EXAMINATION

BY MR. PETERSON:

Q I just want to clarify one point. Peggy, the Public Health Advisory committee adopted a resolution that the public health foundation should be independent and that it should be through a public process, and it's your understanding that Dr. Scheckler signed on to that resolution?

A Yes.

MR. PETERSON: Thank you.

COMMISSIONER O'CONNELL: Thank you. Mr. Peterson, you may call your next witness.

MR. SPITZER-RESNICK: My turn. I'm going to call Mark Orloff at this point.

MARK ORLOFF, called as a witness herein by the Coalition, after having been first duly sworn, was examined and testified as follows:

EXAMINATION

BY MR. SPITZER-RESNICK:

Q Mr. Orloff, please state your name for the record.

A Mark Orloff, O-R-L-O-F-F.

Q And you testified at the public hearing on November 29th, 1999, correct?

A Yes, sir.

Q And that testimony was scripted, correct?
A I'm not sure what you mean.
Q Well, there was a prepared script of your testimony prior to your actual giving it, wasn't there?
A Yes, that's correct.
Q Okay. Now, please describe just briefly what your position is in terms of employment.
A I'm the Vice President and Deputy General Counsel of the Blue Cross & Blue Shield Association in Chicago, Illinois.
Q And in that capacity you are, I take it, quite familiar with the conversion plan as offered by Blue Cross Blue Shield United of Wisconsin?
A I'd say I'm familiar. I don't know that I'd say I'm quite familiar with all the details.
Q Well, is it not a fact, Mr. Orloff, that the plan was presented to you and the association for at least approval pending regulatory approval?
A Yes.
Q And is it not a fact that the association has approved the plan as presented to it?
A Yes.
Q And that is, however, pending regulatory

approval?
A Yes.
Q Now, that procedure of submission of a plan by Blue Cross Blue Shield, plan anywhere in the country that chose to convert, first to the association for, call it tentative approval pending regulatory approval, it would be the normal procedure based on Blue Cross Blue Shield Association guidelines, correct?
A Yes. I would want to clarify one thing, though. When you talk about association approval, what we're talking about there is approval of the right to continue to use the Blue Cross & Blue Shield marks to continue as a licensee subsequent to a proposed conversion. That's the nature of the limit of the approval.
Q Appreciate that -- that clarification. And just to actually go down that road for a minute, the Blue Cross Blue Shield Association is the holder of the trademarks, the Blue Cross & Blue Shield that are all so familiar to probably everyone in this room, correct?
A The association owns those marks.
Q Right. And you in turn license them under certain conditions to various plans around the

condition?

A Correct.

Q And is it fair to say, Mr. Orloff, that if you do not agree to license the Blue marks, as they're known, to a given plan, the value of that plan is widely known to be not nearly as great as if it holds the Blue Cross & Blue Shield trademark?

A I am of that opinion, yes.

Q Now, the -- you have testified in -- on November 29th that there are specific conditions that the association holds out for conversions, correct?

A Yes.

Q And one of those, or among the conditions is related to the foundation and how it would hold stock, correct?

A Yes.

Q So the foundation, as you testified, is initially allowed to hold 100 percent of the plan's stock, correct?

A In this case, yes. For a period of time that's correct, yes.

Q Well, and the period of time that you have testified as under the association guidelines would be five years, correct?

A Not five years for 100 percent.
Q Well, in fact, what the association has requested of this plan is that it be reduced at approximately 20 percent per year for five years?
A I don’t think the requirement is based on a per year reduction. I think there’s an initial requirement to get down to 80 percent by some relatively brief time. I don’t recall the specific --
Q One year?
A I think it’s within one year.
Q And then another 20 percent, and by the second year another 20 percent by the third year?
A No, I don’t think so. I believe there’s a third year target and a five-year target.
Q Okay. Fair enough. Now, that selldown is based upon a foundation that is created with 100 percent stock, correct?
A Yes.
Q There has been no opinion rendered by the association as to whether or not the foundation could hold a mixture of stock and cash, correct?
A That’s correct.
Q In fact, under normal association guidelines

you, the association, I say you, I assume you can speak on behalf of the association, would prefer it for the association to hold less stock rather than more?

A I don’t think I can agree with that, but certainly there’s no -- If your question is does the association have a problem if that were to be the case, the answer is no.

Q And the that you’re talking about holding cash as opposed to stock?

A Less than 100 percent of the stock, yes.

Q The concern about selling down the stock is related to control over the for-profit Blue Cross Blue Shield, correct?

A I’m not sure I understand your question.

Q Well, what -- why don’t I just ask you the open question. Why does the association care that the foundation would sell down stock within five years?

A As I think as was outlined in my prior testimony, our basic concern is that an independent entity, be it a foundation or any other entity not be in a position to exercise undue influence or control or domination of the plan, and when there are exceptional

circumstances such as this and a foundation's formed, we like to see that foundation reduce its power, reduce its ownership stake as quickly as possible.

Q Well, you're well aware that under this plan, and which was approved by the association, the foundation, whether it holds 100, 80, 60, 40, or 20 percent of the stock has absolutely no voting control over that stock, correct?

A The voting control is limited, as I understand the proposal, to the terms of a voting agreement or voting trust agreement, and that would restrict the ability of the foundation to cast its votes on many matters in a way that the foundation would otherwise do.

Q Virtually all matters, in fact. In fact, they could not control the activities of the for-profit, if the Commissioner allows the conversion to go forward, the foundation would have absolutely no ability to control the practices, economic or otherwise, of the Blue Cross Blue Shield for-profit entity.

MR. BRANCH: Commissioner, I'd like to object to Mr. Spitzer-Resnick's testifying, and ask that he would kind of limit himself to

questions. And I would like the record to note that we have now reached the four-and-a-half hour mark on the Coalition's witnesses. So do whatever you want, but I'd like the record to note that.

MR. SPITZER-RESNICK: Commissioner, I would say that I'm not testifying. I am cross-examining this witness as per your order, and I believe that was a leading question, which by all rules of evidence, even if we were in court, would be specifically permitted.

As to the four-and-a-half hours, I would suggest that if we had not had the extensive cross-examination of Deborah Cowan, which was not in our control, we would not have the current problem that counsel is suggesting.

COMMISSIONER O'CONNELL: I will allow the question, and I will note that in terms of the time, we also took an additional 15 minute break or so earlier in the day and did not start at 1:05 as indicated.

BY MR. SPITZER-RESNICK:

Q Do you have the question before you?

A I do not. Can you repeat it?

MR. SPITZER-RESNICK: Can the

reporter read it back?

(Record read.)

MR. BRANCH: I don't believe I heard a question. Was there a question?

COMMISSIONER O'CONNELL: Could you rephase that as a question, Mr. Resnick?

BY MR. SPITZER-RESNICK:

Q If the plan is approved, would the foundation be able to control any of the economic practices or other practices of the proposed for-profit Blue Cross Blue Shield?

A Well, I would -- I'd answer your question this way. I think as we talked about, the voting -- the voting power of the foundation as owner is significantly constrained by the voting trust agreement. Whether or not ownership in and of itself brings some measure of an ability to control I think is a separate question.

So if you're talking about voting control, I would -- I would leave my answer as it stands. If you're talking about some other form of control, I need to understand further what you mean by control.

Q Well, could the foundation direct, for example, the plan, the Blue Cross Blue Shield plan, merge

with another plan or any other health insurance entity?

A Under the proposed agreement?

Q Yes.

A No, I don't believe they could.

Q Could it decide to sell off significant assets? I'm not talking about stock of the foundation, but other assets?

A Could the foundation direct --

Q The foundation direct, the Blue Cross Blue Shield United of Wisconsin proposed for-profit, to sell off any significant assets?

A I'd have to review the language of the -- the agreement to give you an answer to that. I don't recall the specifics in terms of the limitation on the foundation's ability to exercise its voice or make that kind of a direction.

Q Would the foundation have any power to hire and fire management?

A No. I believe that would rest with the board of the company.

Q Would the foundation have any power to appoint any or dismiss any of the for-profit's board of directors?

A If I’m recalling the agreement correctly, I believe that the foundation’s shares are voted according to the terms of the voting trust agreement on that issue.

Q Which means the foundation itself cannot direct any dismissal or retention or hire or appointment of the for-profit’s board of directors, correct?

A I believe that’s right.

Q Thank you. Now, in your testimony on November 29th you also stated that it was critical to the association, the foundation board, and I’m quoting, "Will be impartially and independently selected and be free from any concentration of special interest involving the state or local government," correct?

A I’ll take your word for that, yes.

Q I’m reading, just for the record, from page 95, lines 1 through 4 of the November 29th testimony. You wouldn’t disagree with that statement, would you?

A No, I would not.

Q Okay. Fair enough. Now, if there were an independent public health foundation not connected with the current proposal that the

medical schools would be the recipients and current proposed board members, so long as there was not any special interest involving the state or local government, you wouldn’t have any problem with that as an association, would you?

A I believe that’s correct, yes.

Q And in fact, such entities have been created and approved by the association in other locations in other conversions, correct?

A I’m not sure what you mean by the entities being approved, but if you mean that the association approved the conversion from its perspective with such a public -- that type of foundation, the answer is yes.

Q Okay. Now, the -- your testimony was also that, in answer to one of the Commissioner’s questions, and now I’m reading from page 99, was that the association would, and I quote -- excuse me. I’ll state what I’m quoting. The association would approve a conversion, and I quote, "with the creation of the foundation that at least initially possesses all or much of the plan’s stock," unquote. Does that sound like something that you would have said or still agree with, Mr. Orloff?

A I don’t remember that in response to any question.
Q Well, let the record reflect that I’m reading from page 99 of November --
COMMISSIONER O’CONNELL: What line, Jeff?
BY MR. SPITZER-RESNICK:
Q Line 10 and 11 was where I quoted from.
A Yes, I -- I see that now. I think that’s a lengthy answer and that’s a fragment of the answer that you read, yes. I recall this now.
Q Okay. The point I’m getting to, Mr. Orloff, is the association has -- would most likely not object, and -- Well, let me step back for a moment.
If the Commissioner, in her wisdom, were to decide to let’s say partially approve the plan and suggest certain changes, and one of those changes were to be that the foundation not be a totally 100 percent stock foundation, that would first go for approval to the association related to holding of the marks, correct?
A I don’t know if that’s where it would first go, but in order to --
Q It would eventually go there.

A I would assume, yes.
Q Yes. And, in fact, if it doesn't go there, at some point the association could pull the marks, pull the license for the Blue marks.
A Correct.
Q And you have in fact, and by you again I'm talking about the association, approved other conversion plans where the foundation is not 100 percent stock foundation, correct?
A Yes.
Q And in fact, if the Commissioner were to suggest that there be a different selldown period, in other words, not a five-year selldown period, that would also be something that the association would consider, correct?
A Yes.
Q And in fact, has approved other periods of selldown for other conversions, correct?
A I'm not sure if you're referring to the Right Choice transactions. Maybe you can tell me which one you're referring to and I can answer with specific reference to that.
Q All I want to know, Mr. Orloff, is whether or not there has historically been flexibility at the association related to selldown plans?

A I would say that we've considered periods beyond five years in certain transactions under certain circumstances. I don't know -- I can't say whether that's flexibility or not. Certainly we've considered them.

Q Five years is not an absolute that cannot be changed, is it, Mr. Orloff?

A I would say that we would have to look at the totality of the circumstances, the totality of the proposal, and make our judgment there. There certainly could be situations where it is an absolute.

Q And in the Empire plan there was a different selldown period, correct? Or at least there's proposed to be a different selldown period that the association has considered, correct?

A The association has considered it but not approved it.

Q And that's because the regulatory agency has not completed its work?

A No, that's not correct.

MR. SPITZER-RESNICK: Julie, are you -- you have possession of the exhibits that we marked earlier?

MS. WALSH: I have -- We only had

five of the first set that you gave me, which meant each of the parties, so I need a different set to go to the witness.

COMMISSIONER O'CONNELL: Off the record.

(Discussion off the record.)

COMMISSIONER O'CONNELL: Back on record.

BY MR. SPITZER-RESNICK:

Q Okay, Mr. Orloff. Referring to Exhibit J35, can you initially identify what that document is?

A This is a -- a copy of a letter that I wrote and signed to Thomas M. Rose of Foley & Lardner dated November 15th, 1999.

Q And behind that letter what -- what is attached to the letter?

A Well, there looks to be a three-page attachment which bears the heading on the first page Statement of Principles, BCBSA for-profit Rules.

Q And that is what you've just said it is. This is something that you attached in fact to the letter, correct?

A Yes.

Q Directing your attention to the second page of the statement of principles, the third -- Well,

strike that. This statement of principles contains five chief principles, correct, that are requirements of the association in terms of a for-profit plan retaining the Blue marks, correct?

A No, that's not correct. The five -- The five items that are called out separately are what we refer to as commitments, and these are commitments that describe the obligations generally of all licensees.

Q And the third commitment is a commitment to independence, correct?

A Yes.

Q All right. And one of the concerns you have related to that independence is a concern about any single individual or entity getting control over the -- over the plan or the Blue marks, correct?

A Any single unlicensed entity, meaning unlicensed by us, yes.

Q And from your previous testimony, Mr. Orloff, would it be fair to say that under no conditions with the plan having its votes -- excuse me, the foundation having its vote in stock sitting at a voting trust, very specific restrictions, would

it ever have control over the Blue marks or the Blue plan?

A I think the concern is over, as it says here on the paper, over influence or domination, and using that as the -- as the principal concern, I would say the answer is no, that’s not true.

Q Oh, you believe that this foundation would have influence or domination of the for-profit Blue plan?

A Some, yes.

Q And -- Okay. Would it -- What influence or domination would it have, Mr. Orloff?

A It would have the influence in our view of any shareholder of an organization that owned that amount of shares.

Q But it’s not just any shareholder, is it? I mean, Mr. Orloff, when you or I own stock in a company we get to vote free of restriction on that company, correct?

A Yes.

Q And we receive proxy statements. We get to vote based on the number of shares we hold, correct?

A Yes.

Q This voting -- This foundation will not be able to do that, will it?

A Its voting power will be constrained by the terms of the voting trust agreement, yes.

MR. BRANCH: Commissioner, I would express a concern. I hope we have some flexibility perhaps at the end of the day, but there is not two-and-a-half hours left of the announced schedule.

COMMISSIONER O'CONNELL: Mr. Branch makes a valid point. We do have some flexibility at the end of the day. However, if we could move the questioning along as expeditiously as possible, that would be helpful.

MR. SPITZER-RESNICK: I'm doing my best. You know, if you give me a guideline I'll do my best to follow it in terms of how much time you are permitting me for Mr. Orloff. As I've stated before, the length of testimony is not completely within our control given the length of cross-examination particularly of Miss Cowan.

COMMISSIONER O'CONNELL: At this juncture I hesitate to give you a real firm guideline because I'd like you to be able to explore the areas you need to explore, but just

be very sensitive to the timeframe.

BY MR. SPITZER-RESNICK:

Q I appreciate that. Now, can I move your attention then, in the interest of time, Mr. Orloff, to Exhibit J36. This is an excerpt from the Blue Cross license agreement, correct?

A Yes, it appears to be that.

Q It's the first few pages of the Blue Cross license agreement, correct?

A Yes.

Q And I'll state for the record, just so I can draw attention to specific parts rather than introducing the entire agreement, I've excerpted, which is a part of the record before the Commissioner, I've essentially stapled a few separate parts, and certainly you'll have the opportunity to suggest that if I've missed something somewhere else, but this is just for purposes of moving testimony along.

Now, one question. Would the -- The foundation would not be considered a controlled affiliate as is referred to in association documents, would it?

A No, it would not.

Q So the -- all the rules applied to controlled

affiliates simply don’t apply to the foundation, correct?

A That’s correct.

Q Now, the -- the fact of what happens in the actual for-profit plan is controlled in part by the license agreement, correct? In other words, in order to maintain the license and hold the marks the Blue plan, whether it be a nonprofit or for-profit, must abide by the license agreement, correct?

A Yes.

Q All right. So listed -- Well, on what is the page after page 2, unfortunately it doesn’t have a number underneath it, there’s a series of conditions about what can happen with a -- a Blue plan, correct?

A I don’t understand.

Q Listed 1 through 9, the kinds of things that a Blue plan can do?

A No, that’s not correct.

Q What is that then?

A What you’re seeing on the third page under sub -- or paragraph 2(b) of the license agreement are some specific provisions that apply to controlled affiliates, as you’ll note

in the first paragraph, that have less -- I'm trying to find the exact language for you.

Q Well, isn't it the case, Mr. Orloff --

A Excuse me. Can I complete my answer?

Q Sure. I'm sorry. I thought you were stuck.

A Well, I am a little stuck, but I do want to answer your question.

Q Sure.

A These -- These are provisions that apply solely to controlled affiliates and they relate to the measure of control that the primary licensee, what we commonly refer to as a plan, must have in certain circumstances over the controlled affiliate in order for the controlled affiliate to continue as a licensee of the association.

Q Now, would it be fair to say that the controlled affiliate in the Wisconsin example might be something like Compcare?

A Compcare currently possesses a controlled affiliate license, yes.

Q Okay. So the controlling plan, which is Blue Cross Blue Shield United of Wisconsin, has to make sure that the controlled affiliate does this list of things, correct, in order to maintain its license?

A This list of things only applies in certain circumstances.
Q All right. Let's move on so we don't waste further time here. If we could move to Exhibit J37.
A Yes.
Q Okay. Now, this is the section -- Still part of the license agreement, right, beginning on page 5?
A Yes. It appears to be, yes.
Q Okay. And the -- up on paragraph 9(a) there's a discussion that if there is to be any termination of a license agreement or merger or disputes about noncompliance, there are very specific rules related to mediation and mandatory dispute resolution, correct?
A Could you point me to the line that you're reading from?
Q Sure. Line 6. Starts except as.
A What's the question?
Q Well, my point being, Mr. Orloff, and maybe you don't even need to refer to this document, if there is a dispute between the plan and the association, okay, quite frankly about virtually anything related to the license, the association

doesn’t have the power to just yank the license like that, right?

A There are -- There are terms of the license agreement which call for an automatic termination of the license, so there are conditions under which the license automatically terminates, and then there are a series of other circumstances under which the license could terminate after a process of some sort as defined in the license agreements.

Q And in the vast majority of disputes there is a mandatory dispute resolution process between the association and the plan, correct?

A Yes. As the agreement says, "except as to the termination of a plan’s license or the merger of two or more plans, disputes as to noncompliance and all other disputes between or among BCBSA, the plan, other plans and/or controlled affiliates, shall be submitted promptly to mediation, mandatory dispute resolution pursuant to the rules and regulations of BCBSA, current copy of which is attached at Exhibit 5 hereto."

Q And just for the record, Exhibit 5 would be -- that you’ve referred to is Exhibit J39, if you could quickly flip to that, in this proceeding.

Is that correct?
A No.
Q My copies aren’t numbered. If you’d just do me the courtesy of -- I do have the mediation -- Exhibit 5, mediation, mandatory dispute resolution rules before you, I believe.
A No, I’m not -- I’m not locating them.
Q Okay. Let’s move on. Exhibit 38, J38, are you there?
A Yes.
Q You would agree that the association acknowledges that it does not own any of the assets of the plan?
A Are you referring to specific language?
Q Yes. I believe it’s subparagraph F on that page.
A Yes. It states "BCBSA acknowledges that it is not the owner of assets of the plan."
Q Let me move now to what I believe and hope it’s marked as Exhibit J39. That would be first page of the table of contents for membership standards, correct?
A Yes.
Q All right. Now, let’s go to Exhibit J40. Are you there?

A Yes.
Q There's a series of blank pages other than it says Standard 3 Financial Responsibility.
A Yes.
Q And these are the pages that were submitted to the OCI, correct?
A I don't know.
Q Did you provide -- And actually flip to the Standard 4, which I believe is the last page of Exhibit J40, Responsiveness to Consumers. Am I correct in that?
A Yes.
Q And that is also blank?
A Yes.
Q That is the information on guidelines to administer membership that was submitted to the OCI as part of this proceeding, correct?
A As I say, I have no reason to doubt that, but I have no knowledge of that.
Q Okay. You have no idea why the Commissioner was not privy to financial performance standards and the customer -- excuse me, financial responsibility standards?
A Of course I have an idea.
Q And why is that then, Mr. Orloff?

A This information that was contained and apparently redacted in what was submitted is confidential trade secret information of the association that we did not submit for public -- public distribution.

Q Or for even the Commissioner of Insurance to review as part of the application.

A I don’t have any knowledge of that.

Q And the responsiveness to consumers would also be somehow trade secret?

A The particular information that’s on the page that you’re referring to, yes, we consider it as such.

Q So the Commissioner of Insurance doesn’t know apparently how the plan is going to administer guidelines related to responsiveness to consumers or financial responsibility.

A Well, what these -- what these standards do is lay down the particular measurement, the matrix, if you will, that we use to assess a plan’s financial condition and financial responsibility, as well as service to consumers. As to what the Commissioner knows, I can’t answer that.

Q Well, why don’t you flip to J41. That’s another

set of blank sheets and at the top it says Financial Performance Requirements, correct?

A Yes.

Q And that, I guess, also was not submitted or was redacted because the Commissioner was not allowed to have trade secrets apparently?

MS. BAILEY-RIHN: I'm going to object, Commissioner, just because of the time and the relevancy and I don't see the -- I mean he's already testified that he considered it as trade secret, and I believe your ordered said that to -- to the extent it was a trade secret, that type of testimony would be excluded or -- or not discussed.

MR. SPITZER-RESNICK: Well, trade secret is a legal conclusion, and certainly Mr. Orloff has an opinion about whether this is a trade secret. I obviously at this point have no opportunity to -- because I've never been able to see what is behind this blank document. I think the public is certainly entitled to know, and this is a public hearing, that there is certain information that the Commissioner does not have in making her decision.

COMMISSIONER O'CONNELL: I will

sustain the objection. Mr. Branch, do you have further -- The redacted portions of this document are not relied on by me in making the decision relative to the conversion and therefore are not relevant to the hearing, and so I'll sustain that objection.

BY MR. SPITZER-RESNICK:

Q Fine. I'll move on to J42, and this would also be part of the guidelines to administer membership, and there's a paragraph there of policies applicable to all employees, officers, and directors. Do you see that?

A Yes.

Q Or it's more than one paragraph. I mischaracterized it. It's a section under that.

A There's a section. These are model policies which are attached to the guidelines. They're not part of the guidelines themselves.

Q So they either need to be adopted as is by the plan or with acceptable variations, correct?

A Correct.

Q And one of those is to avoid conflicts of interest including where, and I'm going to quote, "where their personal" -- this again applies to employees, officers, and directors,

"where their personal interests could conflict or reasonably appear to conflict with the interest of the plan," correct?

A It doesn't use those words as I read it.

Q Did I not read that correctly? Why don't you read the first sentence?

A Talking about paragraph 2?

Q Yeah.

A Conflict of interest?

Q Um-hum.

A "All plan personnel should avoid situations" -- I'm sorry. I see where you're reading now. "All plan personnel should avoid situations where their personal interests could conflict or reasonably appear to conflict with the interest of the plan." I was looking at the next sentence. I'm sorry.

Q Fair enough. Let me just ask one more question. I believe it's final, but I've known for many years that you have to be careful when lawyers say they have a final question.

Has the association taken a position related to the -- Well, let me move back one step. Has the association reviewed the appraisal committee's report and

recommendations?

A Yes.

Q And has it taken a position related to the appraisal committee’s recommendations that certain aspects of the plan be changed?

A We have looked at it and we do have reaction on -- on those issues.

Q And what is that reaction, Mr. Orloff?

A Well, do you want to go -- We have to do it line by line. There are a series of recommendations, as I understand it.

Q That’s correct.

A And so we have looked at it and we have a reaction to each of those recommendations.

Q And I’m asking you what those reactions are.

A Then if you could -- I can’t do it from memory. I’m sorry. If you could supply me a copy, I can try to give you an answer.

Q Do you have it before you now, Mr. Orloff?

A No.

MR. SPITZER-RESNICK: Julie, were you able to --

MS. WALSH: I’m just not fast enough for you, Jeff.

MR. SPITZER-RESNICK: I’m not

pushing you.

MS. WALSH: He has the report and the resource book in front of him.

MR. SPITZER-RESNICK: Great. Thank you.

Q Are you familiar enough with the document to find the recommendations that you need to refer to?

A Yes.

Q All right. Why don’t you just let us know when you’re there what page you’re referring to?

A Okay. I’m looking at page 24, the heading of which is Recommendations.

Q And you had previously stated that you had a -- or you being the association, had a reaction to is it each of the recommendations?

A Yes.

Q Okay. Now, just to be clear for the record, is this an official, in other words, the association has voted, we support or do not support each of these recommendations, or is this more of an unofficial this is our -- this is how we’re feeling, so to speak? Do you know what I mean by the difference?

A I think so, but the way I would put it is we’ve

reviewed at the staff level at the association, that would include myself and others, the report and recommendations, and have come to conclusions at the staff level. Any such conclusions to the extent they were implemented with a change to the proposal would have to go back through our governance process and be finally approved at that level.

Q By the association as a whole?

A The board acting through the plan performance committee, yes.

Q Okay. All right. So these are the staff recommendations, essentially, or staff analysis that you are about to provide us with?

A Yeah, that would be a good way to say it.

Q All right. Proceed then, and just tell us which recommendation you’re referring to and what the staff’s analysis or reaction to it is.

A Okay. Well, the first recommendation in the underlined portion is Regulatory Oversight to Prevent Potential Equity Dilution Post-Conversion. I don’t believe we had any material comment on that -- on that section.

Q Just so I understand it, if you, the staff, did not have any material comment, does that mean

you did not have any concern with it either? In other words, if the plan were changed accordingly with that first recommendation, you would not make a recommendation to the association governing board that it should be rejected?

A If it is -- If changes were made in accordance with how we interpret this language, the answer is yes.

Q Okay. Okay.

A The second recommendation is Mechanism to Ensure Adequate Short-Term Liquidity for Foundation and/or Meet BCBSA Divestiture Schedule, and I would first refer to (i), which is the first paragraph, and I'd indicate that the reaction here was that the paragraph as we read it appeared to be suggesting that the same potential extensions of the deadlines that are resident in the Right Choice documents would be applied here.

And if that were the case, assuming no other changes in the proposal, no other material changes, then the -- our -- our view was that would be an acceptable change from our perspective as it was in the Right Choice case.

Q Okay.
A 2(ii) or -- Our reaction on this particular recommendation was that our primary concern would be to assure that the structure, whatever structure was adopted pursuant to this recommendation, if it were different than the original proposal left all licensed entities still in compliance with all of our requirements.

If that were the case, and we don’t have any reason to believe currently that that wouldn’t be the case, but if that were the case, then the association would have no further reaction on this point.

Q Okay.
A And the same would hold true of 2(iii). With regard to item 3(iv) --
Q Okay. And here you’re talking about Tighter Governance Structure to Better Align Interests between the Foundation and UHG?
A Thank you, yes. And under the first set of comments there’s a heading Foundation, and then there are a series little i through little vi, and the association’s first comment or reaction to these would be on (iv) which states "The

foundation shall have unrestricted voting rights to the extent of its shares with regards to all UHG-related change of control transactions, excluding a merger with UWS."

We in reviewing this did not have the benefit of what we think would be the -- the -- what we thought was the thinking behind this at least spelled out. If this is indicating that the foundation shall have unrestricted voting rights to the extent of its shares on proposals for a change of control submitted by the board of the plan, then the answer or our reaction would be that would be an acceptable change.

Q Okay. And the items preceding that that you're not commenting on you had no concerns with; is that correct? In other words, 3(i), (ii) and (iii)?

A Yes.

Q Okay.

A On (v), as we read this language we interpreted it as suggesting adoption of the same language that accomplishes this purpose as it appears in the Right Choice documents.

And to the extent that that

interpretation is correct, and to the extent there are no other material changes in the proposal, such a change would be acceptable to the association.

Q All right. Let me do this in the interest of moving things along, Mr. Orloff. Are there any items in the recommendation, and there's another page or so of them, that the association does have concerns with that would be unacceptable?

A Well, I think I'm -- I don't know that I can save you much time. To give you an accurate, complete answer I need to review it, and I'll try to move as fast as I can.

Q Fine.

A As we interpreted the language in (vi) under 3, Foundation, we didn't have any comments on that. The next series is under a heading UHG. Again -- We're still in paragraph 3. We were unable to reach any definitive conclusion on this language without further explication of what observation rights mean or what consult with the foundation means. So we would need more detail in terms of what is particularly being proposed here before we could provide a reaction.

Q Okay.
A On (ii) under UHG, consistent with the -- the Right Choice transaction we would require that 80 percent of the UHG board have independent directors as defined in the relevant documents.
Q And so that is consistent with this recommendation, correct?
A I don’t believe so.
Q How does it -- Oh, they want -- The recommendation is that it be reduced to 50 percent?
A Right.
Q Okay.
A Under 3, UHG, (iii), we were unclear in reading this whether the recommendation included within the term shareholders the foundation as an excessive shareholder having the ability to independently cast its votes on such an action. And if that were the case, we would not be able to approve that transaction.
Q So if I understand that correctly, even if a director were -- of the for-profit were convicted of a felony, you don’t want the foundation to have any power to remove that -- including embezzlement, for example, you would

not want to have the foundation have any power to remove that director?

A That's -- That particular hypothetical is not presented by this recommendation. I would need to think about that, frankly.

Q Okay.

A The balance of the paragraph 3 we had no comment on.

Q Okay.

A And I'm happy to report that the items 4, 5, and 6 also drew no comment.

Q All right. The association doesn't require foundation directors in general in a conversion plan creating a foundation to be appointed by Blue Cross -- Blue Cross Blue Shield itself and the entity receiving the funds; in this case the two medical schools, does it?

A There's no such requirement.

MR. SPITZER-RESNICK: Okay. I have no further questions.

COMMISSIONER O'CONNELL: Ms. Madsen?

MS. MADSEN: No questions.

MS. BAILEY-RIHN: No questions.

COMMISSIONER O'CONNELL: Mr. Branch?

MR. BRANCH: We have no further

questions.

COMMISSIONER O'CONNELL: Thank you. And I believe that is your final witness?

MR. SPITZER-RESNICK: That is our final witness.

COMMISSIONER O'CONNELL: I should note for the record then that we have a lot of time for additional witnesses. We have gone considerably over the four-and-a-half hours. I understand that there was extensive cross-examination of Ms. Cowan; however, I believe there was only 30 minutes allotted or scheduled for direct-examination, and I believe the direct-examination was nearly twice that long. So we have provided broad latitude to the Coalition and its witnesses, and we will do the same for the other participants.

MR. SPITZER-RESNICK: And we appreciate that, Commissioner.

MS. BAILEY-RIHN: Commissioner, one housekeeping before Helen. One of our witnesses we needed to -- we need -- one of our rebuttal witnesses was going to be Steve Bablitch on a very -- one question, but maybe we can stipulate to it with the Coalition so we don't have to put

him back on.

And that is that -- stipulate that the initial tax exempt status of Blue Cross Blue Shield predecessor and Blue Cross Blue Shield up to 1986 and the tax law change was as a 401(C)(4) corporation. 501, excuse me, (C)(4).

MR. SPITZER-RESNICK: Sure. We'll stipulate to that. That's our understanding.

MR. BRANCH: No objection.

COMMISSIONER O'CONNELL: All right. Miss Madsen, you may call your first witness.

MS. MADSEN: Yes. I call Philip Farrell.

PHILLIP FARRELL, called as a witness herein by the University of Wisconsin-Madison, after having been first duly sworn, was examined and testified as follows:

EXAMINATION

BY MS. MADSEN:

Q Dean Farrell, would you briefly state your education and training, and then direct some brief comments to your background and training and experience in public health, please?

A Yes. I have an AB degree with a joint major in Chemistry and Biology, and M.D. degree, and a

Ph.D. degree in biochemistry. I also have completed a residency in pediatrics, fellowship training in subspecialty areas of neonatology and pediatric pulmonology.

I also have extensive training in epidemiology from the University of Michigan School of Public Health, Harvard School of Public Health, and the world's first school of public health, London School of Hygiene and Tropical Medicine.

And I've been on the faculty of the University of Wisconsin Medical School since 1977 in the Department of Pediatrics. It's also relevant that I'm an Officer in the United States Public Health Service. I served on active duty for five years, and I've been in the inactive Reserve Corps for approximately 25 years with intermittent assignments.

Q Thank you. Did you hear the testimony of Peggy Hintzman today relative to the difference between the focus of public health and the focus of medicine?

A I did.

Q Could you explain for the Commissioner whether you agree with that opinion and if you do, why,

or if you don't, why, please?

A Well, I don't agree with some of her comments because public health and medicine are not distinct. They overlap. In fact, there are many areas where they overlap, and she made three comments that I thought were relevant, and this is a quote I think you'll find from the record. First, "It was not important to make the distinction," in quotes. I agree with her because they do overlap and they do have synergistic features.

Secondly, I quote, "Medical schools are an important component of the public health system," unquotes, and I certainly agree with that. And then her comment also about the State Laboratory Hygiene where she was corrected about how it started, points out the importance of the medical profession and medical schools and the field of public health because indeed, Miss Hintzman is correct, it's the University of Wisconsin Medical School that founded and has operated the State Laboratory of Hygiene, which is this state's major leader in the field of public health.

The synergism between the two fields

has been quite evident in recent years. There are many overlaps and there are examples throughout the lifespan all the way from prenatal care, which is delivered as a preventive medicine component by the medical profession, to immunizations of children, which are provided both by practicing physicians and nurses and in public health clinics, and the many other examples. Cancer screening is a public health practice. For example, pap smears to detect cervical cancer. Breast cancer gene screening. These are areas where the field of public health and medical profession overlap, and even for elderly people and Alzheimer's disease, for example, there's very good overlap and synergism.

There can be some difference in the emphasis, but in fact, both fields are concerned about both individuals and populations. Both are concerned about prevention of disease. Both are concerned about population health.

Q Okay. Would the Newborn Screening program in Wisconsin be an example of the synergy that you've discussed?

A Yes. I think the newborn screening in general,

which some consider the most significant public health program developed for a single population; namely, the population of newborn babies in this country, is a good example, and here in Wisconsin it has been the collaboration of the State Laboratory of Hygiene, public health organizations, practicing physicians, the two medical schools, that have made that such an important component of our public health system.

Q Did you hear Deborah Cowan’s testimony this -- or today?

A Yes, I heard most of it.

Q Okay. Did you hear her testify about emerging best practice standards for public health granting foundations?

A Yes. I heard her comments and I have an outline of her testimony where she’s referred to best practice standards.

Q Okay. Do you agree with her opinion that there is -- there has emerged a -- best practice standards for these type of grant-making foundations?

A Not in my judgment. I’ve been involved with a number of -- of foundations nationally and community foundations and I’ve also examined to

some extent the literature in this area, and there's a great deal of -- of variation and opinion and it's very hard to say there's any established best practices.

I do think that some of the items that are listed here about independence and -- and diverse governance, flexibility, infrastructure in place, efficiency and cost effectiveness are all things that the two medical schools have adhered to in their programs.

So if there are best practice standards, I don't have any doubt that we meet them, but this is an evolving area and it's very hard to be able to claim that there's any one best practice.

Q Have you yourself served on any grant-making foundations or institutional boards?

A Yes, I have. I've served on several. I've been involved with the March of Dimes National Foundation, the American Lung Association, and Cystic Fibrosis foundation, three national groups, as well as the National Institutes of Health.

In fact, for five years I chaired

one of the committees, the principal committee that makes decisions about grants at the National Cystic Fibrosis foundation. And I've been serving on the Madison Ronald McDonald House Corporation, which makes -- on the board of directors, which makes grants to community organizations here in this area.

Q Did you hear Miss Cowan testify this morning about overhead rates for UW-Madison? I believe she said --

A I heard her testimony to that, yes.

Q Could you please tell the Commissioner what -- whether or not there will be indirect cost rates assessed against -- if the Blue Cross conversion plan should be implemented and funds come to UW Medical School, what indirect costs --

A The answer is unequivocally no. There was never any intent to use these funds for anything but direct costs. And so that the information that was provided about the indirect cost rate for University of Wisconsin is actually irrelevant to this topic.

Q Are you in fact aware of -- of the UW-Madison's policy about how to apply or how it applies, how it can apply indirect cost rates to various

grant-making -- grant-granting agencies?
A Yes. It's actually the granting agencies that determine the percentage allowed for indirect cost or overhead. For example, the University of Wisconsin-Madison negotiates with federal government for our NIH grant-related 44 percent figure. Other organizations provide much less. For example, some provide no overhead allowance, only direct cost awards, and others might provide 10 or 20 percent. So it's determined by the organization that -- that transfers the funds to the university.
Q Has Blue Cross in this situation at all had any discussions with the UW Medical School stipulating that there would have to be a certain indirect cost rate?
A No, absolutely not. It was always understood that these funds would be used for direct costs.
MS. MADSEN: That's all I have.
COMMISSIONER O'CONNELL:
Mr. Peterson, do you have any questions?
MR. PETERSON: Yes, I do.
EXAMINATION
BY MR. PETERSON:
Q Mr. Farrell, were you here this morning for the

testimony of Tom Hefty?

A No, I wasn't.

Q All right. Let me ask you a question, though, that was related to that testimony, and we had some discussion on that, but are you familiar with the -- the Cy Pres or the Charitable Trust Doctrine?

A No, I'm not.

Q I want to direct your attention to your testimony on November 29th, 1999. I'm looking at page 51 and it's line 16, and there you indicate that the UW Medical School receives some $160 million a year.

MR. BABLITCH: Excuse me. Could I have the page?

BY MR. PETERSON:

Q That was page 51. That you receive $160 million a year in public research funds; is that correct?

A I believe that's correct. For the past academic year that's right. I think the figure this morning was an underestimate of our total amount of grant funds.

Q So you actually get more than what was estimated this morning?

A That's correct.
Q Okay.
A But it varies from year to year, and this money is generated by a variety of mechanisms. The University of Wisconsin Medical School is only approximately 10 percent supported by the State of Wisconsin. In other words, 90 percent of the funding comes from nonstate sources.
Q So you heard the testimony of Peggy Hintzman that the entire budget for public health in the state is a little over $95 million per year?
A I heard her say that, but I know she's incorrect because part of the funding for public health is coming from sources that she's not familiar with. In fact, our medical school receives some funding for public health-related activities. I myself have a grant of over $1 million from National Institutes of Health for public health-related research.
Q Are you familiar with any granting -- state-wide granting institutions that fund public health for the State of Wisconsin?
A I'm sorry.
Q Are you familiar with any granting institutions that fund public health activities across the

State of Wisconsin currently?
A I'm not -- I don't understand what you mean by that.
Q Are there any state -- Are there any foundations in the State of Wisconsin that operate state-wide that fund local public health activities?
A Educational activities. I just don't know beyond that what's provided with regard to services other than funds available from the State of Wisconsin, but my knowledge of that is limited.
Q So as far as you know, there isn't an independent public health foundation that serves the State of Wisconsin, is that --
A I don't know that there is, no.
Q Okay. Questions about the indirect rate. You said that the indirect rate for National Institutes of Health grants are 44 percent?
A It varies from university to university, but I believe currently UW-Madison's federally negotiated rate is 44 percent.
Q So if you receive funding from another source and you don't charge any indirect expenses to that, then your indirect expense for your other

grants would necessarily go up, wouldn't they?
A Not necessarily.
Q How do you charge for your bookkeeping and overhead services for those grants if you don't have an indirect rate on that line?
A We don't charge for those things.
Q How is it accomplished then?
A It's accomplished through the budgeting at UW-Madison.
Q So the budgeting would amount to some cost shifting then so increasing indirect rates elsewhere, or you'd have to budget it somehow in the line of Blue Cross Blue Shield because there are expenses related to that accounting bookkeeping --
A No. These administrative infrastructure costs are already covered, so there's no need to use any of the Blue Cross Blue Shield money for administrative infrastructure.
Q But your proposal calls for creating a new Dean's office, doesn't it?
A No.
Q Doesn't it -- Isn't it in your proposal that you would be creating an Office of Rural Health or a Dean for Rural Health?

A You mean the Assistant Dean for Rural Community Health.
Q Yes.
A Yes. I thought you meant another Medical School Dean. One's enough.
Q An Assistant --
MR. SPITZER-RESNICK: We can stipulate to that.
BY MR. PETERSON:
Q Let the record reflect that that's true.
A That is a -- a position identified for a leader of programs in the area of community rural health, correct, as described in the plan.
Q So an Assistant Dean's office for Rural Health would include staff, including administrative staff, so that the office can function?
A It's already in place.
Q It's already in place?
A Yes.
Q So those expenses would be covered in different places in the University's budget?
A That's correct.
Q So there would be expenses, but -- and so necessarily those expenses would increase. If you're not charging --

A I don’t know that those expenses would increase, no.

Q Okay. In terms of the testimony that you heard this morning about best practices and foundations and the testimony of Peggy Hintzman, were you pleased to hear that generally the opinion of experts from the Coalition were willing to -- to -- Strike that. Let me rephrase the question.

Were you pleased to hear that if a new independent foundation were created, that the other organizations within the State of Wisconsin would welcome the med school submitting applications to such a foundation?

A I really wasn’t pleased to hear that. I thought it was a foregone conclusion that if you have an open process with a foundation, that any organization could submit applications.

Q All right. But the opposite isn’t true. Indeed, the University of Wisconsin and the Medical College of Wisconsin are not grant-making institutions, as has been testified to previously, and other institutions would not necessarily be eligible for funding from those institutions except for some small grants, maybe

five percent of the total award of the -- of the foundation.

A You are correct. We're not a grant-making institution and -- and yet as we've specified here in the component entitled Enhancing Rural and Community Health, we are interested in strengthening partnerships with community organizations as was requested when we traveled through the State of Wisconsin and conducted the listening sessions, the public hearings.

This was something that Mr. Bolger and I heard over and over again, the interest of community organizations and strengthening partnerships with us. And so in response to those requests we included this component in the -- in the proposal, yes.

Q So you heard it over and over again, but it translated only to about five percent of the allocation and only from the University of Wisconsin Med School's proposal for community grants?

A That was one of 1700 things that we heard.

Q Did you hear anything about dental needs across the state?

A Yes, we did.

Q Did you hear about that there's a -- many children aren't receiving dental care because of chronic access problems?

A We heard that many people -- It wasn't -- The emphasis was not on children, actually. It was on the elderly population and their difficulty with access to dental care.

Q Is there anything in your proposal to deal with acute shortages of dental services?

A We are a medical school and we reached a conclusion along the way that we would concentrate on what is immediately apparent to us as the needs and priorities that we can address.

However, we have been asked to consider addressing issues that relate to oral health on dental problems, and in fact we're going to do that. Our Wisconsin network for health policy directed by Dr. David Kindig in fact has made that one of their initiatives for this year.

We also have recognized the need to pay more attention to the effect of oral health on nutritional status and cancer as it relates to oral health, so yes.

Q But you are a medical school, and your primary activities are outlined in your report, which is research, education, and community service; isn't that right?

A Yeah. Our core missions are research, broad spectrum of educational activities, and service to people and to communities.

Q So in that -- following up on that, totality of public health needs, and using dental needs as an example, are not necessarily within the mission of the Medical School?

A I would say that the mission of the Medical School covers if not the totality, almost all of what is encompassed by the field of public health because we even have three environmental health sciences organizations on the UW-Madison campus. Two of them are federally funded.

Q But not all of them. I'm gathering from your testimony that you're admitting that you don't cover the full -- you're not a school of public health; isn't that right?

A We do not cover the entire spectrum. As I mentioned, we do not have dental programs within the Medical School, for example, and in fact, we recognized from the beginning of time that this

funding was not intended to solve all the problems of people of Wisconsin, but rather that it should be used most effectively to address the highest priorities and also to deal with emerging public health priorities in a dynamic fashion.

MR. PETERSON: We have no further questions.

COMMISSIONER O'CONNELL: Miss Bailey?

EXAMINATION

BY MS. BAILEY-RIHN:

Q I have one question for you, Dean. Earlier today in answer to my -- I had asked Peggy Hintzman regarding whether she thought that research was important regarding the underlying causes of disease, and she answered me by saying that the research had all been done, most of it had been done, and now it was just public needs to implement the research.

What do you -- What is your opinion as to whether the research to underpin the underlying causes of disease has been all accomplished?

A Well, unfortunately it's not all accomplished.

There are many, many challenges now that have to be addressed through research in order to improve the health of the public. In fact, we heard some discussion about the polio vaccine. This is an example where it's really the research that provided the breakthrough, the major advance, not the delivery system, for prevention of polio. Cancer, as an example, where it's unlikely that in any of our lives cancer will be completely understood and be completely preventable, and so there really is a great need for more research.

In the elderly population, for example, areas like Alzheimer's disease, the key will be research. It will not be continuation of the current system we have, which is custodial care. We really need earlier identification and -- and prevention of Alzheimer's disease.

MS. BAILEY-RIHN: Thank you, Dean.

COMMISSIONER O'CONNELL: Mr. Bablitch?

MR. BABLITCH: I have no further questions.

COMMISSIONER O'CONNELL: Any

redirect?

MS. MADSEN: No, I don't.

COMMISSIONER O'CONNELL: You may call your next witness.

MS. MADSEN: I do not have any further witnesses, Commissioner. However, I believe in the prehearing memorandum you indicated that you would entertain a motion. I do have testimony by affidavit that I would like to submit by witnesses who could not be here, and they are in the nature of rebuttal testimony.

COMMISSIONER O'CONNELL: Is there any objection to that?

MS. MADSEN: It is the affidavit of Dr. David Kindig and the affidavit -- who is Professor of Preventive Medicine at the Medical School and is Director of the Wisconsin Network for Public Health Research which Dr. Farrell referred to, and the brief affidavit of John Torphy, who's the Chief Financial Officer of the University, as to its tax status.

MR. PETERSON: I'm going to object to that. I don't have an opportunity to review or to examine the documentation or provide

cross-examination of the witnesses. I think it defeats the spirit of the intent of this event right here.

COMMISSIONER O'CONNELL: I'll allow the submission subject to the objection, and you're welcome to provide further comments related to that objection once you have an opportunity to review it. I should note at this time supplemental briefs are due March 17th.

MS. MADSEN: Would you like to take that now?

COMMISSIONER O'CONNELL: Yes.

MR. PETERSON: Can we go off the record for a second?

(Discussion off the record.)

COMMISSIONER O'CONNELL: Miss Bailey, you may call your first witness.

MS. BAILEY-RIHN: Thank you, Commissioner. I'd like to call David Kinnamon.

MR. SPITZER-RESNICK: At this point the Coalition objects to any testimony from David Kinnamon. David Kinnamon is a partner in Quarles & Brady. Therefore, what we have is an extreme violation of the ethical rules preventing an attorney to testify on behalf of

his client in this case. Quarles & Brady is representing the Medical College of Wisconsin. Quite frankly, I'm shocked by Quarles & Brady even attempting to present Mr. Kinnamon at this point.

MS. BAILEY-RIHN: Your Honor, there's no ethical problem at all by us having Mr. Kinnamon testify as an expert in the area of tax exempt law. He's -- We are -- The ethical violation would occur if I attempted to be a witness and also an advocate at the same time in a hearing. This, again, is not a legal proceeding.

Having a witness who's an expert in the area of tax exempt organizations and who had been properly named and there wasn't any objection made to him or his proposed testimony, seems to me that it's completely proper and -- and is not used to be -- he's not an advocate in this matter at all.

MR. SPITZER-RESNICK: If I may just present comment briefly because I don't know if Ms. Bailey-Rihn misspoke, but this is a hearing. It's a contested Class I hearing as the Commissioner stated both in writing and orally

this morning.

As a partner in the firm of Quarles & Brady it is as if Miss Bailey-Rihn were going up there right now to testify. There is no difference between Mr. Kinnamon not happening to sit at counsel table and him now going as a witness, and he represents his client right now regardless of whether or not he happens to be sitting at counsel table.

COMMISSIONER O'CONNELL: I will allow the testimony. This is a hearing, but it is not a hearing before a jury. As a fact finder in this proceeding I can distinguish between his testimony as an advocate and as a witness, and therefore will allow the testimony.

MS. BAILEY-RIHN: Thank you, Commissioner.

DAVID KINNAMON, called as a witness herein by the Medical College of Wisconsin, after having been first duly sworn, was examined and testified as follows:

EXAMINATION

BY MS. BAILEY-RIHN:

Q Mr. Kinnamon, can you please state your full name for the record?

A Sure. My name is David, middle initial L, last name Kinnamon, spelled K-I-N-N-A-M-O-N.

Q And as we have heard, you are a partner in the law firm of Quarles & Brady. What area of law do you practice in?

A I practice in several areas, actually. I practice in the area of tax exempt organizations and also trusts and estates.

Q How long have you practiced in this area, sir?

A For more than 30 years. Close to 35 years.

Q Have you had a chance to review the proposed Blue Cross Blue Shield conversion?

A I have.

Q Are you aware of a proposal to set up a public health foundation?

A Yes, I am.

Q Do you know what type of tax status that public health foundation will have?

A It’s my understanding that it has applied for and received exemption as a Section 501(C)(4) social welfare organization.

Q Do you know what assets the public health foundation will consist of?

A It’s my understanding that it will hold the common stock of the Blue Cross Blue Shield

holding company.

Q Do you know what the -- Have you had a chance to review the articles and bylaws of the public health foundation?

A Yes, I have.

Q What will be the purpose of the public health foundation?

A The purpose generally stated is to support the Medical College of Wisconsin and University of Wisconsin Medical School.

Q Do you have an understanding as to what the tax exempt status of the Medical College and Medical School is?

A The Medical College of Wisconsin is tax -- a tax exempt charitable and educational organization under Section 501(C)(3). The University of Wisconsin Medical School is part of the University of Wisconsin, which is a state agency, and is exempt from taxation under Section 115. 115 of the Internal Revenue Code.

Q Earlier today you heard testimony by Deborah Cowan regarding the doctrine of -- Charitable Trust Doctrine or Cy Pres Doctrine. Do you know if Wisconsin has such doctrines?

A Yes.

Q And where are these doctrines codified in?
A They're codified in Section 701.10 of the Wisconsin Statutes, which is part of the chapter dealing with charitable trusts, and Section 701.10 by its terms applies to charitable trusts.
Q Do you have opinion as to whether Blue Cross Blue Shield -- Blue Cross Blue Shield assets are subject to Section 701.10?
A I do.
Q Do you hold this opinion to a reasonable degree of legal certainty?
A I do.
Q And what is your opinion?
A My opinion is that Blue Cross Blue Shield is not a charitable trust. That Section 701.10, which codifies both the Charitable Trust Doctrine, which if you'd like I can explain, and also the Doctrine of Cy Pres would not apply to it.
Blue Cross Blue Shield since its inception has been a nonprofit hospital service corporation incorporated initially under subsections of the Wisconsin corporation laws, and since the early 1970's it's been incorporated under the insurance laws in the

state.

Q What is a Charitable -- What is the Charitable Trust Doctrine?

A The Charitable Trust Doctrine is -- it's been codified in Section 701.10(1) of our statutes, and -- and briefly, it's -- it's -- it says that a gift to charity will not be allowed to fail. That if the purpose is indefinite or if a trustee is supposed to select a charitable beneficiary, that the court will intervene to address those issues and in fact the court may appoint a trustee to execute a charitable trust.

The Doctrine of Cy Pres is related, it's kind of a corollary principle, and that applies when a charity -- the purpose of a charitable trust becomes impossible, impracticable, or unlawful. That's the common law formulation. In our statutes it's been broadened a little bit to include not only impracticality and unlawfulness, but inconvenience and undesirability. So it's a little bit broader than the common law doctrine, but it still applies only if the original charitable purpose of an organization is no longer lawful or practicable, and then the court

will intervene to basically modify the purpose to some other charitable purpose that is closely related as is possible under the circumstances.

Q Explain to the Commissioner and the members of the public why you do not believe the 701.10 applies to the Blue Cross Blue Shield entity?

A As I indicated, Blue Cross Blue Shield is a hospital service corporation that is incorporated under the corporation laws in the state originally and then under the insurance laws. That's the -- That is the technical answer.

The -- Sort of the broader substantive answer is that the activities of Blue Cross Blue Shield are not charitable in the traditional sense of that word, and the -- the law of charities is -- there tends to be a little bit of confusion, and I think we've had some semantic confusion today.

There really are three separate terms that we're dealing with here. We're talking about charity in sort of the traditional common law sense of what constitutes a charitable trust, we're talking about tax exemptions, and we're talking about nonprofit,

and these things are not synonymous.

The broadest circle, as it were, would be nonprofit. Nonprofit does not necessarily mean tax exempt or charitable. You can have taxable nonprofits. In fact, Blue Cross Blue Shield is a taxable nonprofit.

Tax exempt means exempt in -- sort of in the technical sense of that term refers to tax exemptions under the Internal Revenue Code, under Section 501 of the Internal Revenue Code. The list of exempt organizations is found in Section 501(C). There are 27 subsections of 501(C). Only one of them addresses charitable organizations, and that’s Section 501(C)(3).

And then the final issue is charitableness itself as a concept, and that’s the narrowest of -- of all these three. And we could -- we can get into -- The traditional law of charitable purposes is codified again in Section 701.10(1) and -- and I’m looking at the language of the statute now, and it says the -- and these are consistent with the common law list of charitable purposes. "Relief of poverty, advancement of education, advancement of religion, promotion of health, governmental

or municipal purposes, or any other purpose the accomplishment of which is beneficial to the community."

Now, subsumed in that charitable theory of charitability is that the benefits of the charitable activity have to accrue predominantly, if not exclusively, to the benefit of the public as opposed to private individuals. And that is -- it is that particular test upon which the -- the Blues traditionally foundered when trying to get status as a 501(C)(3) charitable organization.

The laws said their primary purpose was to provide hospitalization benefits to the subscribers. In other words, a hospital service plan is a risk pooling device to allow low income people to obtain hospitalization insurance. That is essentially a private purpose as opposed to a public one, and that is why the IRS from the get-go refused to recognize the Blues as charitable organizations under 501(C)(3).

At the time they were created, the IRS did recognize that they --

MR. SPITZER-RESNICK: I would like

to interject an objection at this point. As was mentioned this morning repeatedly by Mr. Bablitch, we're dealing with state law here, and I think I let Mr. Kinnamon go on for a while. His repeated references to the IRS Code I believe are irrelevant here. We're dealing with state law, State Charitable Trust Doctrine, State Nonstock and Nonprofit Doctrine, and not the IRS code here.

MS. BAILEY-RIHN: Your Honor, or Commissioner, I think the issue here and the issue that has been raised over and over by the Coalition is that the non -- the non -- the tax exempt status is the determining factor.

MR. SPITZER-RESNICK: Never. Never. In fact, we have acknowledge that --

COMMISSIONER O'CONNELL: This is not an opportunity for debate.

MS. BAILEY-RIHN: I think that the issue here is the tax exempt status is under not only state law, but under federal law, and to the extent that there are differences, and frankly that the IRS has taken the position that the Blues are not a charity and therefore they are not subject to a charitable trust.

COMMISSIONER O'CONNELL: I'll allow the -- the testimony. I think that everyone can attest that this morning I offered broad latitude to the Coalition to pursue issues outside of strictly state law, and I'll do the same for this witness.

MS. BAILEY-RIHN: Thank you, Commissioner.

Q Briefly, if you could tell us the difference between a 501(C)(3) corporation and a 501(C)4 corporation, which is what Blue Cross Blue Shield's tax exempt status was prior to 1986, it would perhaps be helpful.

A There are a number of significant tests both in the Internal Revenue Code and in the treasury regulations under Section 501(C)(3) that you have to meet in order to get qualified as a -- a public charitable organization.

You have to be organized and operating exclusively for an exempt purpose. There can be no inurement to private benefit in a 501(C)(3) organization. The assets of the 501(C)(3) organization by regulation have to be dedicated to an exempt purpose, and a 501(C)(3) organization cannot engage in more than an

insubstantial amount of lobbying or legislative activity, and it's precluded from engaging at all in political activity. Those are the tests under (C)(3).

Under (C)(4), it has to be organized exclusively for social welfare. Until 1996 there was no preclusion of inurement to private benefit. That's a fairly modern addition to 501(C)(4). That came long after the Blues had lost their 501(C)(4) status.

It is true that a (C)(4) cannot involve itself in political activities, but it certainly can and typically does engage in legislative and lobbying activities.

Q So is there anything under federal IRS tax regulations of a nonprofit or exempt corporation that would prohibit or limit or somehow restrict Blue Cross Blue Shield's proposed distribution?

A Not that I'm aware of.

Q Turning now to state law, you've heard testimony regarding the enabling statutory language in 1939 which provided Blue Cross Blue Shield to receive tax exempt status, and in that statute there was a provision that Blue Cross Blue Shield or other similar organizations are

declared to be a quote, "charitable and benevolent corporation."

Does this language impact or change your opinion in any regard regarding whether the assets of Blue Cross Blue Shield are subject to a charitable trust?

A No, it doesn’t.

Q And why?

A The reason is that the terms charitable and benevolent were typically and have been typically used in the Wisconsin Statutes connected with tax exemptions, and benevolence is -- has been interpreted by our courts as being much broader than charity in the traditional law of charities. The -- The citation for that is the Milwaukee Protestant Home case, which was decided in 1969, I believe. Am I right, Mr. Branch?

MR. BRANCH: That is correct.

THE WITNESS: The -- In addition the Wisconsin Supreme Court, I believe it was in 1961 or 1962, in a case involving Associated Hospital Services was really directly invited to -- to hold that indeed the Blues were -- were a charitable organization. This was a dispute

over property taxes with the City of Milwaukee.

MR. SPITZER-RESNICK: Madam Commissioner, I'm sorry. I have to object again, and it is really based on my initial objection. At this point what Mr. Kinnamon is doing is giving you an oral legal brief. An oral legal brief from the same law firm that has an opportunity by 9 o'clock on March 20th to provide you with a written legal brief. They're getting two kicks at the cat here by legal counsel, and I simply object. It's not fair and I quite frankly still believe it's unethical, and I have grave concerns now we're going from statutory interpretation into case law interpretation. This reference checking with Mr. Branch, just checking if his testimony was correct. It's amazing.

THE WITNESS: In reference to a law review article.

MS. BAILEY-RIHN: Your Honor, the issue is whether or not the Cy Pres Doctrine applies under 701.10. That is something that's been raised by the Advocacy groups, their witnesses. I think this is a proper subject of expert opinion on. Everybody else has

testified, and I believe correctly they're not experts in this area. We named him as an expert and we believe that it's appropriate.

COMMISSIONER O'CONNELL: I do believe that the door was opened to the Cy Pres Doctrine and exploration of that this morning. However, the -- the legal brief of this issue, I think we should try to wrap up the legal discussion, and any further discussion you will be afforded an opportunity in your legal brief to explore.

BY MS. BAILEY-RIHN:

Q Sure. I just have one brief follow-up question. Based on the status of the Section 501(C)(4) corporation, Blue Cross Blue Shield's articles of -- and purposes, is there anything that the -- or under state law, does the proposed distribution of the funds to the Medical College and the Medical School violate any of those governing bodies or the IRS code sections or state law?

A In my opinion they do not.

Q And you hold that to a reasonable degree of legal certainly?

A Yes.

MS. BAILEY-RIHN: I have no other questions.

COMMISSIONER O'CONNELL: Mr. Spitzer-Resnick, do you have questions?

MR. SPITZER-RESNICK: Yes, I do have a few questions.

EXAMINATION

BY MR. SPITZER-RESNICK:

Q Mr. Kinnamon, you were retained here by the Medical College of Wisconsin?

A Yes.

Q And what -- Are you charging the Medical College of Wisconsin for your services?

A Yes.

Q At what rate are you charging them?

A At my normal billing rate.

Q And what is that?

A My normal billing rate is approximately $265 an hour.

Q And when Quarles & Brady submits a bill to the Medical College of Wisconsin, will your services be combined with the services of Miss Bailey-Rihn?

A I'm not certain.

Q Not familiar with the accounting practices of

your office?
A I am not the billing partner on the matter.
Q You are a partner, however?
A I am a partner.
Q And Mr. Bolger, the President of the Medical College, who will testify, I assume, after you, is a former partner of yours, is he not?
A That is correct.
Q Are you suggesting that in 1939 when the predecessor to Blue Cross Blue Shield United of Wisconsin was created it had no charitable purpose?
A I am suggesting that it had no charitable purpose as that term is used in the traditional law of charities.
Q And the traditional law of charities as it applied in 1939?
A That’s correct.
Q Let me quote from Section 180.32(1) from 1939, which I assume you’re familiar with?
A Yes, I’ve read it.
Q And ask you if this is not a charitable purpose. "While in" -- and this is quoting from the public policy. "The statement of public policy is declared to be to ease the burden of payment

for hospital services particularly in low income groups where the advent of scientific methods, the payment for adequate hospital service is a pressing problem with grave social ramifications. Nonprofit hospital service corporations based on the tested experience in many parts of the United States economically sound and socially benevolent are needed.

While in no way changing the present status of voluntary hospitals in the state, these corporations will enable a larger number to procure for themselves adequate hospital services and leave the use of the free and part-free services given by hospitals to those whose economic status makes self-procurement of such services impossible."

Are you suggesting that that is not a charitable purpose?

A I am suggesting that the predominant purpose that you in the language you quoted was the ability of individuals to procure hospitalization insurance for themselves, which is a -- a private benefit, and that that far outweighs the benefits to the public. That is not to say that there may not be some incidental

public benefits from the plan.

Q Is it not the case that many charities contribute to individual need, and in fact charities who are designated as 501(C)(3) charities, well, let’s take an example, the Salvation Army.

A Well, I’ve already testified that, for example, relief of poverty is one of the traditional charitable purposes.

MR. SPITZER-RESNICK: Nothing further.

COMMISSIONER O’CONNELL: Miss Madsen, do you have any questions?

MS. MADSEN: I do not.

COMMISSIONER O’CONNELL: Mr. Bablitch, Mr. Branch?

MR. BABLITCH: No.

COMMISSIONER O’CONNELL: You may call your next witness.

MS. BAILEY-RIHN: I’d like to call T. Michael Bolger to the stand.

T. MICHAEL BOLGER, called as a witness herein by the Medical College, after having been first duly sworn, was examined and testified as follows:

EXAMINATION

BY MS. BAILEY-RIHN:

Q Sir, can you please state your full name for the record?

A Yes. It's T. Michael Bolger. B as in boy, O-L-G-E-R.

Q Thank you, sir. Can you please tell us what your position is at the Medical College of Wisconsin?

A I'm the president --

COMMISSIONER O'CONNELL: Could you please speak directly into the microphone?

THE WITNESS: Sure. I'm the President and Chief Executive Officer of the Medical College of Wisconsin.

BY MS. BAILEY-RIHN:

Q What exactly is the Medical College of Wisconsin?

A The Medical College of Wisconsin is a national private medical school founded in 1893 to serve the people of the State of Wisconsin in its four distinct missions of education, research, patient care, and community service. It has established as a 501(C)(3) charitable organization and has existed in such throughout

its history.

It at one point was the Marquette University School of Medicine, but in 1971 became the Medical College of Wisconsin when Marquette terminated its sponsorship of the school.

Q Showing you what's been marked J28 and ask you to identify this document.

A Yes. Exhibit J28 is the exemption letter from the Internal Revenue Service granting the Medical College of Wisconsin status as a charitable organization, public charity.

Q Thank you. Turning your attention to G -- or excuse me, J29, I'd ask you to identify this document also for the record.

A J29 is the restated Articles of Incorporation of the Medical College of Wisconsin.

Q Are these the governing documents of the Medical College of Wisconsin?

A Yes.

Q Who governs the Medical College of Wisconsin?

A Medical College of Wisconsin is governed by an independent board of trustees, one-third of whom are appointed by the Governor of the State of Wisconsin, two of whom are appointed by the

County Executive of the County of Milwaukee, one of whom is appointed by the faculty, one of whom is appointed by the alumni association, and the remaining are selected from a group of highly regarded and diverse individuals with certain characteristics to help govern a school of this size. It is currently a 34 person board.

Q Earlier today we heard testimony that need for public -- or health of the public in the State of Wisconsin is partnership or collaboration with local organizations and community services. Can you describe for me what the Medical College does in that regard?

A Yes. The Medical College of Wisconsin is extensively involved in all its missions in dealing with the -- the -- with the public. I happen to agree somewhat with Miss Hintzman and her definition of public health.

What I would read into the record would be a definition from a task force headed by David Sacher, who’s the current Surgeon General of the United States from a document that he and his group prepared in 1994 called America Healthy People and Healthy Community, which states that "The mission of public health

is to promote physical and mental health and prevent disease, injury and disability."

And there were 10 areas, and Miss Hintzman referred to them; monitoring health status; diagnose and investigate health problems; inform, educate and empower people; mobilize community partnerships; develop policies and plans; enforce laws and regulations and protect health and insure safety; link people to needed personal health services; assure a competent public and personal health care workforce; evaluate effectiveness, accessibility and quality, and research for new insights and innovative solutions of health problems.

And I was, as she was, offended by some of the testimony in the record. I was offended a bit because I have 29 pages of a single-spaced document relating to the Medical College of Wisconsin and its connection to the public health mission.

MR. SPITZER-RESNICK: I'm sorry. Madam Commissioner, Just for clarification, is the witness referring to an exhibit or --

THE WITNESS: No, I'm not. I'm

referring this merely so that I can -- without having to refer to all 29 pages, I need to refresh my recollection of all of the things that we're doing in responses to the question, Mr. Spitzer-Resnick.

COMMISSIONER O'CONNELL: The 29 pages you're referring to are from what document?

THE WITNESS: This is from an internal document prepared by my office on a definition of public health and what the Medical College of Wisconsin is doing in the public health arena. It was in order so that I could testify from it; not to offer it as an exhibit. It's not to be offered as an exhibit. It's just to help my memory because I can't remember everything we're doing.

MR. SPITZER-RESNICK: That's fine. As I said, it wasn't even an objection. It was clarification.

THE WITNESS: That's all I need it for.

MR. SPITZER-RESNICK: Fine.

THE WITNESS: We have adopted -- We have started a Continuous Improvement of Health

Care office for patient safety in response to the Institute of Medicine report on patient safety. We have organizing the Wisconsin Patient Safety Stakeholder organization.

We are doing work in the inner city for asthma, which is the number one diagnosis of -- admitting diagnosis to Children's Hospital, trying to prevent asthma, and being an asthmatic myself I'm very much interested in that.

The College also runs the Center for AIDS Intervention in Milwaukee, which is the -- one of the models in the country. There are only three of them that are funded at our level to -- to engage in behavioral modification in order to prevent AIDS and in order to -- to provide services for living with AIDS, for caregivers who have to give AIDS care, reduction of high risk behavior, and also preventing HIV among women, which heterosexual women are the most at-risk population today in terms of HIV.

We also run the NCW Patient Care and Outcomes Center, outcome research, in order that we can determine what therapies are successful or not successful so that we can spend our money

wisely.

We have one of the largest epidemiology departments to do epidemiological studies on disease in human populations and trends and diseases. We have found -- Our researchers find new ways to immunize against deadly bacterial.

Under diagnosis and investigate health problems we run the downtown Health Center. We've created the Medical College Women's Health Initiative, the Wisconsin Injury Research Center, the Family Peace Project. We have also got public health strategies that we're working on to reduce family violence.

Under informing, educating, and empowering people we have our Speaker's Bureau, we write advice columns in Milwaukee metro newspapers. We have the Children at Risk Project in our Center for the Advancement of Urban Children run by Dr. Willis.

We run the North Division Clinic at North Division High School. We have MCW Cares where our students go out and teach high school students for AIDS prevention particularly.

BY MS. BAILEY-RIHN:

Q I think in the interest of time we may have to move on.

A As I said, what I -- what I want to state for the record, however, is that the Medical College of Wisconsin and its outreach mission is reaching out far into the State of Wisconsin in order to affect and impact the health of the people, and the way we do it is primarily through collaboration with other agencies.

And you will see in our plan that we try to put together that our principal goal is collaboration and to merge the lines that Dr. Farrell specified so well I thought in terms of the melding and merging of public health and medicine. The two are not opposed. The two must work together, especially for the future.

Traditional model of public health does not function as well as the new paradigm that Dr. Carbone spoke on at the hearing on November 29th.

Q Turning now to some of the other concerns expressed by the Advocacy group’s witnesses today, one of the concerns was the public input into the process. After the Medical College and the University Medical School became aware that

it was a potential recipient for certain funds, what did it do to get public input into its proposal?

A Well, we were told in no uncertain terms that the money was not without strings. We were told that we had to go out into the public and prepare a plan in order to -- to be approved by Blue Cross Blue Shield, and that if the plan did not respond to the overall needs of the public and public health priorities in the State of Wisconsin, we likely would not receive the money. And we had to file a preliminary plan at the end of August and then a final plan in October.

And so Dr. Farrell and spent the summer traveling around the state. We held nine informational hearings, we took testimony, we opened a web site, we put out an 800 number, we invited snail mail and E-mail, and we received over 1,000 responses from the public telling us what they thought the priorities were, and we tried to draft our plan as a result of what we heard.

We did not draft a plan based on what we wanted to do. We based our plan on what

the public told us they wanted. And they made it loud and clear they didn't want us to engage in spending this money on treatment, but they made it also very loud and clear that they wanted us to spend this money on prevention and wellness, on research to cure disease, to stop disease, and on education. And you will see that these three things are reflected in our plan.

When we came back from the hearings we sat down and we said all right, they want us to get into prevention, and so we decided to create, at least at the Medical College, the MCW Institute for Public and Community Health. Now, this institute was meant, and we were going to allocate 35 to 45 percent of the monies, and by the way, we decided very early on that we would place the money in a permanent separate endowment so that it could always be accounted for, that it could always be seen where the money was spent, and how it was going to be spent, and then we decided to appoint an eight to 12 person board for this institute that would determine the strategies and priorities, and on that board we were to pick a cross-section of

people from the public health community and other community leaders that are interested in health issues throughout the state to decide the priorities for this institute so that we could fund programs in collaboration and leverage this -- this money with other sources of funds to provide a -- a better hold in that arena.

We were also told in the research area that we should focus on the diseases that kill most and cause most concern in Wisconsin, and it was loud and clear what came through. Number one was cardiac disease, because that's the number one killer in Wisconsin; number two was cancer, because that's the number two killer in Wisconsin, and number three was the neuro sciences, especially diseases, mental diseases of the aging, including Alzheimer's, Parkinson's, senile dementia, and other such problems, and -- and then the -- the areas of human and molecular genetics, and the third area was education. They asked us to help educate the people of the State of Wisconsin in health care issues and public health issues. We therefore chose to expand our Master's in Public Health Program.

We are, by the way, the only Medical School in America that has a fully accredited Distance Learning Program to get an MPH degree, and we are going to open that under this rubric to when -- we had limited it to M.D.'s and now it will be open to non-M.D.'s as well.

Q And MPH is Master's in --

A Master in Public Health. And so the plan was very carefully put together based on what we heard in the comments all last summer, and was finally approved by the Blue Cross Blue Shield board in October.

Q And referring to J30, is that the plan you're referring to which is advancing the health of Wisconsin's population? It's the brown --

A Yes, if it's this one.

Q Correct.

A It's a copy of it.

Q The other concerns we heard was about oversight not over the public input going into the process, but also the public input and the oversight and the review of what the funds are used for.

First of all, there was a concern that somehow the UW and the Medical College

would use the funds in any way that they wanted. How -- How are the funds going to be accounted for and determined that they're used in connection with the proposal that the public requested?

A Well, first of all, it all starts with -- obviously with the board of trustee of the Medical School, which is a public board with appointments by the state and -- and others. It's a board that is very highly regarded in the community. It has decided a couple of things with respect to this plan.

Number one, to appoint the advisory board to the Institution for Public and Community Health so that that will be open, to appoint an endowment commission which annually will review the expenditure and report as to -- to everybody. It will be put on a web site. It will be sent to the Commissioner of Insurance, sent to the Attorney General, to determine whether or not the monies have been spent in substantial accord with the stewardship principles laid down by Blue Cross Blue Shield and by our public hearings.

So the accounting end -- and every

five years the two schools will go back out into the state and hold public hearings again throughout the state in order to determine whether the priorities have changed in order to be responsible and responsive to the people.

One of the things that I think is missing in this whole discussion is that for over 100 years the two medical schools have been responsive and have been effective stewards of their corner of health care in the State of Wisconsin, and there's no reason I don't think to suspect that they won't continue.

Q You've also heard testimony today that there were concerns about indirect costs associated with the proposed use of funds. Is the Medical School going to be allocating any indirect costs to the funds it receives?

A No, there will be no overhead.

Q Explain the difference between an indirect cost and a direct cost.

A Indirect expense on a grant is associated with overhead and payment of overhead expenses such as heat, light, janitorial services, and so forth because every grant costs you money. There are some granting agencies that give you

indirect expenses or overhead and some that don't.

For example, the National Institutes of Health is the most generous for some -- we have been able to achieve 50 percent of indirect costs from the NIH for some grants, but the grants from like Eli Lily or Abbott Laboratories give us zero.

And the question was asked Dr. Farrell where do you pick that up from elsewhere? Well, we don't charge that to other grants. We can't and -- but where we can charge it is through our patient care activities, and that's where you pick it up because in terms of practicing, in terms of teaching, our faculty also practices medicine and they are employees of the school.

Q Finally, I think you've heard quite a bit of testimony regarding the difference in the mission of public health and the mission of the Medical College. Do you how address those concerns that somehow the Medical College's missions are broader than the public health mission?

A Well, I think they are broader than the public

health mission. I think we have within us, and this is what I meant by a new paradigm that Dr. Carbone testified to on November 29th, which I thought was quite eloquent frankly, that we are in terms of putting together the -- the merge idea of public health and medicine cooperating and collaborating in order to improve the health of the people, and that's truly what all of this -- when I said I had these 29 pages of all the things that the University of Wisconsin Medical School could replicate, it's the reaching out now to get out beyond the hospitals into the communities to provide service and to provide care, to provide prevention, as well as -- as doing the research that's ultimately going to cure disease and make prevention perhaps unnecessary in some year.

Q Do you believe that the proposal advanced by the UW Medical School and UW -- excuse me, the Medical College would provide a better mechanism for addressing the issues of health and public of Wisconsin than a private foundation which would be simply providing grants?

A Well, obviously that's a pretty leading

question, but -- but --

MR. SPITZER-RESNICK: You've noticed I've stopped objecting at this point.

THE WITNESS: -- but by the same token, you know, it's interesting when -- when Blue Cross Blue Shield first came to see me about this and asked me, you know, told me about the idea of the gift, which was June 6th, a day that will live in my mind for a long time, I wondered the same reason. I said why us? Why don't they create a separate foundation and have it function? Because I really do every once in a while put on my hat as a community citizen, but the more I thought about it, the more sense it made.

The reason it made sense is because the two schools really have the infrastructure both administratively, as well as all of the other things in place to do an effective job of sifting and widowing among those things that are appropriate and those things that perhaps are not as appropriate if they involve the collaborative efforts with other people, and that's what we're reaching out to do.

It seemed to me, and this we do

every day, we have to make decisions how best to spend our money in terms of advancing the health of the people in the State of Wisconsin because that's our mission.

And so it came back to me that it actually was a pretty wise decision by Blue Cross Blue Shield to do that, even though it was obviously in my best interest. I thought through and I came to the conclusion that it was also in the best interest of the people of the State of Wisconsin.

MS. BAILEY-RIHN: Thank you. I don't have any further questions.

COMMISSIONER O'CONNELL: Mr. Spitzer-Resnick?

MR. SPITZER-RESNICK: Thank you. Briefly.

EXAMINATION

BY MR. SPITZER-RESNICK:

Q Mr. Bolger, you acknowledged in your testimony on November 29th that the Medical College would spend approximately $12 million initially to start this grant up?

A Yes.

Q And one of your trustees, Dr. Peter Shindell --

Sidney Shindell, excuse me, testified, did he not, that he did not see any appreciable public health activity in the proposals that Blue Cross Blue Shield had supplied -- had received from the two medical schools in the state, and in fact he commented on your testimony, and I quote from page 40 at line 9, "Virtually none of the services described by Mr. Bolger this morning appear in the documents submitted to Blue Shield by MCW, nor am I aware of anyone with a public health background that was involved in developing of either the medical schools' proposals and no assurance has been given that the faculty of MCW's Department of Preventive Medicine will be the nucleus of the projected institute."

I take it, Mr. Bolger, that it did not sit well with you to have one of your trustees express such grievous concerns about the proposal.

A Well, the Medical College is a broad tent. I simply disagree with him.

Q The -- If patient care dollars are going to pay for the overhead costs of this grant, that then would generate increased costs for patient care

then, wouldn’t it?

A No, it wouldn’t.

Q So just from the already significant surplus or -- I know you’re not allowed to make a profit. How is it -- there’s just all this extra money here?

A No. It’s just that you don’t understand, obviously, the -- the financing of a medical school. All of the faculty are employees. As a result, they earn less money because it comes out of their salary. We pay them all a salary. So they provide patient care, but they don’t collect the fees. We collect the fees.

And so unfortunately, that’s why academic physicians don’t make as much money as physicians in the quote, "real world." And it’s getting harder and harder to keep academic physicians because we can’t pay them as much as we would like to be able to pay them to be competitive with what they can earn in the public sector.

Q Well, let’s face it, Mr. Bolger. It will cost the Medical College of Wisconsin money to run $125 million endowment program, correct?

A Sure.

MR. SPITZER-RESNICK: Okay. I have nothing further.

COMMISSIONER O'CONNELL: Miss Madsen, do you have any questions?

MS. MADSEN: No questions.

COMMISSIONER O'CONNELL: Mr. Bablitch?

MR. BABLITCH: No.

COMMISSIONER O'CONNELL: Do you have any additional witnesses?

MS. BAILEY-RIHN: No, but I do have one affidavit, again, as strictly rebuttal testimony, and I would offer that in subject to the same objections and limited ruling that you had regarding the other affidavits.

MR. SPITZER-RESNICK: We'd have the same objection to that. We understand the ruling.

COMMISSIONER O'CONNELL: It will be accepted subject to the objection. Okay. A number of exhibits have been offered today. There are the objections by the Coalition to the exhibits offered by Miss Madsen and Miss Bailey. I will receive the exhibits in the record. Are there any further objections related to exhibits

that have been offered today?

MS. BAILEY-RIHN: I believe their objection was to our affidavits; not the three previously identified exhibits.

MR. PETERSON: Correct.

COMMISSIONER O'CONNELL: Thank you for that clarification.

MR. BABLITCH: Are all the exhibits that were marked and referred to, have they been offered?

MR. SPITZER-RESNICK: I assume that's what you were just asking, Commissioner, and so I'm -- yes, they're being offered and so I'm obviously not objecting to what we've offered, and you've already heard objections that we had to others and ruled on them, I think, accordingly.

COMMISSIONER O'CONNELL: I want to thank all of the participants then for their presence and their patience today. I am not ready to concede Mr. Peterson's assertion that this is the most important issue that will face me as Commissioner. I hope to have a long tenure as Commissioner and face many other weighty issues, but I will agree this is

probably the most important issue that I have faced to date, and the testimony from the witnesses today is very helpful in moving forward with a decision in this matter, and I want to thank the participants for their testimony and for their comments today.

We have -- This will then conclude the contested case hearing in the matter of the application for conversion of Blue Cross Blue Shield United of Wisconsin.

MR. BRANCH: I'd like to suggest that perhaps the briefs that are due in the next 12 minutes might be filed now and made part of the record in this matter before you formally close it just so they're part of the record. That's all I'm concerned with.

MR. SPITZER-RESNICK: They're just closing the hearing; not the whole record.

COMMISSIONER O'CONNELL: Right. Right. Supplemental briefs may be submitted then no later than we agreed upon, 9 a.m. on March 20th. And it is now about 4:16. Thank you.

(At 4:16 p.m. the hearing ended.)

STATE OF WISCONSIN)
) ss:
MILWAUKEE COUNTY)

I, KIM M. PETERSON, CM, RPR, a court reporter with the firm of Halma-Jilek Reporting, Inc., 225 East Michigan Street, Milwaukee, Wisconsin, do hereby certify that I reported the foregoing proceedings taken on March 10, 2000, and that the same is true and correct in accordance with my original machine shorthand notes taken at said time and place.

_____

Notary Public

In and for the State of Wisconsin

Dated this 13th day of March, 2000,
Milwaukee, Wisconsin.
My commission expires June 16, 2002.