

December 29, 1999

Mr. Guenther H. Ruch
Administrator
Division of Regulation and Enforcement
Office of the Commissioner of Insurance
121 East Wilson Street
P. O. Box 7873
Madison, WI 53707-7873



Dear Guenther:

This letter is in response to your letter dated December 23, 1999 asking for a further response to your request for information dated December 7, 1999.

The nature of each request, the December 7 and the December 23, 1999 letters, are relative to prior inter-company transactions. As I understand, these requests are being made to satisfy the "numerous" requests being made about whether there was a de facto conversion of Blue Cross & Blue Shield United of Wisconsin ("BCBSUW") in the creation of United Wisconsin Services ("UWS"), and how these transactions bear on the valuation of BCBSUW. It appears that much of the interest in the prior transactions emanates from the handful of groups, including Consumer's Union of San Francisco, who have made their opposition to aspects of our conversion known. They have made these allegations for over a year both to your agency and to the Attorney General. The Attorney General has investigated these allegations and could find no basis for meriting further review. I have enclosed his letter to these groups dated April 28 1999. In pertinent part his letter states as follows:

Although we concluded that the transactions do not violate the Wisconsin laws governing BCBSUW's conduct of business, we also considered whether the transactions, including the consolidation of its directly-held for-profit assets under a for-profit subsidiary holding company, UWS, and BCBSUW's sale to the public of some of the UWS common stock has had a negative impact on BCBSUW's assets or business. On the contrary, based on information compiled by the Wisconsin Office of the Commissioner of Insurance, BCBSUW has significantly increased in size and value since the mid 1980's. (Emphasis added.)

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Despite the Attorney General's response, we have endeavored to help OCI conduct whatever investigation OCI deems necessary. In response to your December 7, 1999 request, we sent to OCI on December 17, 1999 two banker's boxes of documents. Although all of these documents were previously provided to OCI at the time of the prior transactions, we supplied them again in order to help expedite the review process. I understand that these documents have been provided to Deutsche Banc Alex. Brown ("DBAB"), OCI's investment banking advisor. Then on December 22, 1999 we received an extensive request for information directly from DBAB, a copy of their request is enclosed. On December 23, 1999 we sent to DBAB two additional banker's boxes of documents in response to their request, a copy of our response listing all of the documents we supplied is enclosed. It is my understanding that DBAB is conducting the review of transactions from 1983 to the present for purposes of determining the value of BCBSUW.

Furthermore, DBAB has requested a meeting with representatives of BCBSUW for the first week in January. We have a meeting scheduled for January 5, 2000 and are prepared to answer any questions they might have for us. In the meantime, we have asked our investment banking advisor, Donaldson, Lufkin and Jenrette ("DLJ") to cooperate with DBAB and to provide any information that would help with the review.

We have provided OCI and DBAB with as much information as possible to answer any allegations concerning previous transactions and valuation of BCBSUW. Some of the documents relative to prior transactions were omitted, as mentioned in our December 17 letter, because they were so old that they were not kept due to our record retention policies. These old materials are not required to be retained pursuant to Adm. Code Sec. Ins. 6.80. Due to this fact and pursuant to our own internal corporate document retention policies, documents dated 1992 and prior are no longer readily available from our formal corporate records. They should, however, be in the OCI files. Also, we are preparing a summary of the various reportable holding company transactions as requested. DBAB has requested copies of the summaries for their review, which appears to be coextensive with your request. I expect to have the summaries available for the DBAB review prior to their meeting with us next week. I will, of course, provide you with the same. Further, you requested a more recent report of shareholders owning 5% or more of United Wisconsin Services and American Medical Security Group, Inc. Based upon the most recent information available to BCBSUW, the only new controlling shareholder to report is Caxton International Limited, which owns 5.4% of American Medical Security Group, Inc. common stock

Finally you asked on what basis BCBSUW complied with applicable holding company laws. First of all, unlike most other Blue plans outside of Wisconsin, Blue Cross & Blue Shield United of Wisconsin must comply with a holding company law and has done so throughout the entire period of your inquiry. All applicable holding company laws have been complied with, as evidenced by the fact that BCBSUW duly filed all requisite documents with OCI contemporaneously with each and every reportable transaction, and that OCI either explicitly approved the transaction or implicitly approved the transaction by not disapproving them. Moreover, as you know, the triennial examination process involves the review of all of the

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reportable holding company transactions and a review of the minutes of the board of directors meetings. As pointed out in the NAIC Examiner's Handbook, one of the purposes of a financial condition examiner's review of affiliated transactions is to identify potential misuse of insurance company assets and siphoning of insurance company funds. See NAIC Financial Condition Examiners Handbook at 1-40. From 1982 to the present, which covers the time frame of your information request, there have been five triennial examinations conducted by your office, and copies of the corresponding Financial Examination Reports were included as exhibits offered by BCBSUW at the Class 1 Contested Administrative Hearing and accepted into the record by the Commissioner. At no time have we ever been informed by OCI that any of these transactions did not comport with the holding company laws or constituted a misuse of BCBSUW assets or a siphoning of BCBSUW funds. Additionally, the BCBSUW members and board of directors approved each of these reportable holding company transactions at the time the transactions occurred. At all times throughout the relevant period all of the directors and members complied with their fiduciary duties and the statutory standard to act in the best interests of the insurer.

As a side note, we have previously asked OCI whether the holding company law is being enforced with respect to all Wisconsin managed care plans. As you know there are managed care plans owned by tax-exempt entities, which should be subject to the holding company law. The original drafter's notes to Chapter 609 makes clear that the legislative intent was to have managed care plans subject to the holding company law. We would like to know if, and how OCI is enforcing the holding company law in this regard, particularly with respect to transactions with affiliated companies.

In summary, we have complied with all of the OCI's requests for information, regarding not only prior transactions, but also all questions relative to the conversion itself. Our request for a conversion has now been pending since June 14, 1999. The hearings in Milwaukee and Stevens Point took place one month ago. The law is clear and unequivocal, the conversion must be approved unless the Commissioner finds that it violates the law, or is contrary to the interests of the policyholders or citizens of the state. Nothing in this record indicates that what we have proposed violates the law or is contrary to the interests of the policyholders or the citizens. We are now awaiting the Commissioner's decision.

Very truly yours,

Stephen E. Bablitch

cc: Joe Branch, Foley & Lardner
Randy Blumer, Deputy Insurance Commissioner, OCI
Fred Nepple, Legal Counsel, OCI
Thomas W. Johnson, Deutsche Bank

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