

December 7, 1999

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121 East Wilson Street
P.O. Box 7873
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VIA HAND DELIVERY

Re: Application for Conversion of Blue Cross & Blue Shield United of Wisconsin
Case No. 99-C26038

Dear Mr. Junior:

This letter is in response to your letter or inquiry dated November 23, 1999.

Governance Issues

- 1. Under the stock holding company's articles of incorporation, shareholders have no right to remove any director or the whole board unless the director or the entire board is convicted of a felony or found liable for gross negligence or willful misconduct in a matter of substantial importance to the corporation, where such adjudication is no longer subject to direct appeal. Even then, the holders of 75% of the issued and outstanding common shares must vote in the affirmative to remove the director or offending board. Is this a specific requirement of the Blue Cross Blue Shield Association? On what basis should this provision be considered reasonable?*

Although the Blue Cross Blue Shield Association does not endorse a particular corporate form, the stock holding company Articles of Incorporation were modeled upon the charter documents proposed as part of the RightChoice conversion in Missouri and which were previously approved by the Association. Further, these provisions promote continuity in the Plan's Directors and are consistent with the core interest of independence that the Association seeks to protect through the Licensing Agreements. The Association

provides broad guidelines regarding control and independence of the Plan and reviews each Plan's Articles of Incorporation, Bylaws and Board composition to ensure that none are inconsistent with the goal of Plan independence. Through the license rules and requirements, all Plans must be committed to independence and be free from the domination of any single entity whose interests may be distinct from the interests of the Plan and its subscribers. As a result, the above-provisions further the commitment to independence and afford the Plan Directors the freedom to discharge their obligations in accordance with their fiduciary duties - the duty of care, the duty of loyalty and the duty of obedience.

- 2. Under Article IV of the stock holding company's articles of incorporation, each director has immunity for breach of fiduciary duty on any votes for or against any proposal or course of action that, in his judgment, would breach any requirement of the Blue Cross Blue Shield Association or lead to the termination of any license issued by that organization. In the Voting Trust and Divestiture Agreement, the public health foundation is required to assert in the recitals that the Blue Cross Blue Shield licenses will contribute substantially to the stock holding company's value and its future prospects. What is the purpose of allowing the directors to take actions that would breach the requirements of the Blue Cross Blue Shield Association? How does the plan protect or compensate the public health foundation for any diminution of value resulting from such decisions?*

Article IV does not provide immunity for taking actions which breach the Association's requirements. Rather, the Article provides just the opposite. Directors would have immunity from liability for votes (either affirmative or negative depending upon the issue presented) which in the director's judgment are required in order to preserve adherence to the Association's requirements.

Role of the Limited-Life Public Health Foundation

- 3. The public health foundation is obliged to pay numerous expenses on its own behalf, including, but not limited to the following: its share of the fees and expenses of the trustee of the voting trust, expenses related to the registration and sale of its share holdings in the stock holding company, and the expenses of seeking extensions to the divestiture schedule from the Blue Cross Blue Shield Association. How will the public health foundation achieve sufficient liquidity prior to the sale of its shares in the stock holding company?*

If the conversion is approved, Blue Cross will be filing for permission to issue a 2 million dollar extraordinary dividend. The dividend would be distributed to the holding company created as a result of the conversion. The holding company would then pass on the dividend to the Foundation, which would then be able to utilize the funds to cover the cost of necessary administrative activities.

4. *What staffing needs are anticipated for the limited-life public health foundation? How will these needs be met?*

There likely will be some staffing needs for the public health foundation to perform administrative duties, including for example, coordinating meetings, responding to inquiries and correspondence and taking minutes at Board meetings. Blue Cross & Blue Shield is prepared to provide staffing to the new Board as needed and requested at no cost to the foundation until such time that the new Board decides to hire its own staff. Also, there will likely be a need to hire legal counsel to ensure compliance with all applicable laws. It is anticipated that the Board would choose its own legal counsel. It is anticipated that the extraordinary dividend referred to in the answer to question 3 would be sufficient to pay for these costs until such time that the capital stock of United Heartland Group, Inc. is sold, or is otherwise available to provide for liquidity.

5. *Who is the intended trustee of the voting trust that will hold the stock holding company's shares on behalf of the proposed public health foundation?*

A trustee has not yet been chosen, however, it is anticipated that an institution conducting trust business that is based in Wisconsin will be named as the trustee of the voting trust.

Ultimate Successors to the Nonprofit Interests of Blue Cross

6. *How does the plan for the use of conversion proceeds meet the test of not being contrary to the public interest?*

Under the plan of conversion, the Foundation will receive 100% of the equity value of the converted Blue Cross entity. The plan of Conversion provides for the Foundation to serve the health care interests of the people of the state of Wisconsin. The mission of the Foundation is to support public health initiatives through the University of Wisconsin Medical School and the Medical College of Wisconsin. Using 100% of the proceeds of the conversion to serve public health needs in the State of Wisconsin is not contrary to the public interest. On the contrary, the proposed use of these funds should greatly enhance the well-being of the citizens of this state. The report issued by the two medical schools more fully explains how the money will be used. Moreover, the testimony adduced at the Class 1 hearing held on November 29, 1999 more fully explains how the plan of conversion is not contrary to the public's interest.

7. *An article in the Milwaukee Journal-Sentinel dated Monday, October 4, 1999, quotes Linda Brei, a spokeswoman for UW-Madison, as saying there will be a supervisory committee for Blue Cross conversion funds. What criteria will UW-Madison use to select the Annual Stewardship review panel, and who will appoint them?*

The Annual Stewardship review panel mentioned by Linda Brei actually refers to a Medical School Advisory Board. This Board is being reconstituted and one of its

responsibilities will be to participate in the stewardship of the conversion proceeds. Current plans regarding the Medical School Advisory Board, which are subject to ongoing development, contemplate representation from the Department of Health and Family Services, minority communities, rural areas, statewide health advocacy groups, the UW-Madison Chancellor's office and other distinguished citizens from around the state. The members of the Advisory Board would be appointed by the UWMS Dean with the approval of the UW-Madison Chancellor. Some of the appointments will be based on nominations provided by community-based organizations.

8. *What ongoing provisions does the plan of conversion provide for the successor nonprofits' accountability and responsiveness to Wisconsin's health care needs in general, and particularly with respect to the five-year reviews after the limited-life public health foundation ceases to exist?*

The two medical schools prepared a report entitled "Advancing the Health of Wisconsin's Population" which was adopted by the Blue Cross & Blue Shield United of Wisconsin Board of Directors and filed as a supplement to the application for conversion. This report contains several ongoing provisions that address the successor nonprofits' accountability and responsiveness to Wisconsin's health care needs. According to the report, the medical schools will be accountable to the public through a variety of ongoing reporting requirements. For example, initiatives supported by the endowment fund must provide annual reports regarding budgets, expenditures and progress in meeting program goals. In addition, the medical schools will prepare annual stewardship reports detailing the use of the endowment funds which will be made available to the public. Every fifth year, the medical schools will provide expanded stewardship reports and conduct a detailed reassessment of program initiatives funded through the endowment, which will include input from the public. The report also provides for stewardship of the funds by various oversight boards of the medical schools which contain public representation.

In addition to the requirements set forth in the report, the medical schools will be accountable to the public through other requirements imposed by law. For example, the medical schools will be required to file annual reports regarding their operations with the Internal Revenue Service which will be made available to the public for inspection and/or duplication. Because the medical schools and their respective foundations are tax-exempt, they are subject to certain restrictions under the Internal Revenue Code that will ensure that their activities are conducted on terms which are fair and reasonable and do not unduly benefit private individuals or entities. Furthermore, the medical schools' directors and trustees are subject to certain fiduciary obligations that are required by law. For example, the directors and trustees are subject to the duty of care, which requires them to act in the same manner as an ordinarily prudent person would act in a like position under similar circumstances.

9. *Please provide a copy of the board minutes and resolution evidencing the adoption of the report on the intended use of foundation resources from the University of Wisconsin Medical School and The Medical College of Wisconsin, following board approval of the same.*

The Blue Cross & Blue Shield United of Wisconsin Board of Directors has not yet approved the minutes from that meeting. However, it is anticipated that at the next regularly scheduled meeting of the Board of Directors, which is to be held on December 8, 1999, the Board will approve those minutes. We will submit those minutes to OCI immediately after the Board meeting.

10. *What criteria will be used to appoint The Medical College of Wisconsin's Endowment Fund Commission?*

MCW is still in the process of developing criteria for members of the Endowment Fund Commission. Such criteria will strive to identify a broad cross section of individuals who have an interest in the health of the citizens of Wisconsin. Members of MCW's Board of Trustees will not be allowed to serve on the Commission.

11. *How will the grant review committee of the University of Wisconsin's Enhancing Community and Rural Health Fund be appointed?*

Under current plans, the Enhancing Community and Rural Health Fund Committee will be appointed by the UWMS Dean with the approval of the UW-Madison Chancellor and will include representatives from governmental health agencies, voluntary health organizations, UW faculty and community leaders.

12. *How will The Medical College of Wisconsin's Institute of Public and Community Health engage in public outreach, particularly with respect to providing funding in collaborative efforts with other organizations?*

The Institute of Public and Community Health will engage in public outreach by addressing the health concerns of various communities, supporting prevention and wellness programs, and facilitating diverse areas of health services research through collaborations with various health care organizations, especially in underserved urban and rural communities throughout the state. An advisory board, in consultation with Institute staff, periodically will develop and evaluate strategic priorities for the Institute with an objective of building effective community partnerships. MCW will then unveil these strategic priorities to the public and will identify and solicit public health agencies and community organizations to collaborate with MCW to advance these priorities. In addition, community organizations and health groups will be encouraged to submit their own proposals for collaborations with MCW to advance the strategic priorities identified by the advisory board. At this time, MCW is developing specific criteria for establishing and funding these community collaborations.

Miscellaneous

13. What is the opinion of Blue Cross' management with respect to the tax consequences of the conversion transaction?

Blue Cross' tax consultants and advisors have opined that the conversion will not have a material impact on Blue Cross tax status.

14. Does Blue Cross need to notify any regulatory agencies other than OCI of the proposed conversion?

Blue Cross does not believe any further notifications are required. After giving effect to the conversion, however, the Securities and Exchange Commission will need to be notified with respect to a change in the beneficial ownership of United Wisconsin Services, Inc. and American Medical Security Group, Inc.

15. Have any side agreements, written plans, or assurances been made concerning staff retention, salaries and benefits, or severance packages, for the officers or employees of Blue Cross & Blue Shield United of Wisconsin?

All agreements between Blue Cross & Blue Shield United of Wisconsin and its employees and officers concerning staff retention, salaries and benefits, or severance packages have been disclosed to OCI.

16. Does the company have any plans, within the foreseeable future, to enter into discussions or negotiations with other entities carrying the Blue Cross trademark concerning the purchase, sale, merger, or affiliation with such entities? Is the company aware of any such entities which have an interest to acquire control or merge with Blue Cross & Blue Shield United of Wisconsin after its conversion, should such conversion be approved?

Currently, Blue Cross & Blue Shield United of Wisconsin is in discussions with another Blue Cross & Blue Shield plan to purchase a block of medical insurance business from that plan. No definitive agreements have been reached and the negotiations are subject to confidentiality agreements. In the future it is expected that Blue Cross & Blue Shield United of Wisconsin will attempt to enter into discussions or negotiations with other Blue Cross plans concerning the purchase, sale, merger or affiliations with other Blue Cross & Blue Shield plans for the purpose of growing the business of Blue Cross & Blue Shield United of Wisconsin. Any extended delay of the conversion creates an added risk that those opportunities will no longer be available.

No Blue Cross & Blue Shield plans have notified Blue Cross & Blue Shield United of Wisconsin of an intention to acquire control or merge with Blue Cross & Blue Shield United of Wisconsin. However, Blue Cross & Blue Shield United of Wisconsin recognizes that in the rapidly consolidating health insurance marketplace, it is possible that one or more entities

would desire to acquire control, merge or affiliate with Blue Cross & Blue Shield United of Wisconsin after a conversion occurs.

Blue Cross & Blue Shield plans regularly work together. Today, Blue Cross & Blue Shield United has a contractual relationship with Wellpoint (California Blue Cross) to administer pharmacy benefits and with South Carolina Blue Cross for data processing. Blue Cross Wisconsin's United Government Services subsidiary, which prior to 1999 was an unincorporated division of the company, has assumed government processing from Blue plans in Michigan, Minnesota, Virginia and West Virginia. The UWS affiliate of Blue Cross has joint venture or outsourcing contracts with Blue Cross and Blue Shield of Alabama, Blue Cross and Blue Shield of Arizona, Blue Cross and Blue Shield of Illinois, Anthem Insurance (Blue Cross and Blue Shield of Colorado, Connecticut, Indiana Kentucky, Nevada, New Hampshire, and Ohio), Blue Cross and Blue Shield of Delaware, Empire Blue Cross (Blue Cross and Blue Shield of New York), and Blue Cross and Blue Shield of Kansas City.

In addition, in 1995, there were merger discussions between Blue Cross & Blue Shield United of Wisconsin and IASD (Blue Cross of Iowa and South Dakota). Those discussions terminated in that same year. Finally, as your office is aware, Wisconsin Blue Cross participated in discussions with Illinois and Iowa Blue Cross regarding consolidation in the early 1990's. Those discussions publicly terminated in 1992. There are no continuing discussions in that area.

If you have any questions or need any additional information, please do not hesitate to give me a call.

Sincerely,

Stephen E. Bablitch

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