

November 15, 1999

VIA HAND DELIVERY

Mr. Steven J. Junior
Senior Insurance Examiner
Bureau of Financial Analysis & Examinations
121 East Wilson Street
P.O. Box 7873
Madison, WI 53707-7873

RE: Blue Cross & Blue Shield United of Wisconsin Conversion Application

Dear Mr. Junior:

This letter is in response to your request for information dated October 26, 1999.

Public Health Foundation Issues

1. *The initial registered agent, the initial three (3) directors, the nine (9) successor directors, and the incorporator of the public health foundation are not specified in the application for conversion. Who will be the initial registered agent? Who will be the initial directors? Which nine (9) individuals will succeed the initial three (3) directors? Who will be the incorporator?*

As stated in the Articles of Incorporation filed October 22, 1999 with the Wisconsin Department of Financial Institutions, the initial registered agent is F&L Corp., 777 E. Wisconsin Avenue, Milwaukee, WI 53202. The initial interim directors are Joseph C. Branch, Lynette M. Zigman, and Richard S. Gallagher, all attorneys at Foley & Lardner. They will be replaced by the nine member foundation board if the conversion is approved. The incorporator is Lynette M. Zigman.

The names of the nine individuals who will replace the initial three directors will be provided once biographical information is received from each individual.

2. *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.*

These minutes are in draft form and will be approved at the December 8, 1999 board meeting.

3. *Is the nonprofit Blue Cross in possession of any assets received and held subject to limitations permitting their use only for certain charitable, religious, eleemosynary, benevolent, educational, or similar purposes? If so, what plans does Blue Cross have to convey such assets to a proper successor in interest?*

Blue Cross is not in possession of any such assets.

Business Plans

4. *Please provide a description of the types of policies that Blue Cross currently makes available. I am interested in the company's own internal descriptions of product types and customer types, that is, how the marketing department tracks the product mix.*

Blue Cross' marketing strategy is to appeal to a wide spectrum of consumers, and to offer a correspondingly wide array of insurance and administrative services products. This strategy will not change as a result of the conversion to shareholder owned status.

At the present time, Blue Cross offers the following products on a group basis:

PPO	Preferred provider plan
Comprehensive Major Medical	Traditional fee-for-service plan
Quality Choice	Primary care clinic-based point-of-service plan
Traditional Full-Pay	Plan covering full base and major medical care
Dental	Variety of dental plans, including Comprehensive and PPO
Pharmacy Benefit Plan	Prescription drug card program

In addition, Blue Cross offers indemnity PPO, and POS products on an administrative services only basis (“ASO”) to large groups who desire to self fund their employee health benefit plans.

Blue Cross also offers a variety of health insurance plans to individual consumers:

Personal Choice	Coverage for individuals not covered by a group plan
TempPlan	Coverage for individuals who need a temporary plan
Youth Med	Coverage for children ages 1-17
Value Plus	Medicare supplement plan
Long-Term Care	Provides coverage for care needed on a long-term basis
Medicare Blue	Medicare health maintenance organization (HMO)

5. *Which types of insurance programs and services will the converted for-profit Blue Cross prioritize for growth and development?*

See Response to Question 6.

6. *Which types of insurance programs and services will the converted for-profit Blue Cross seek to reduce or terminate?*

Blue Cross does not intend to change its marketing strategy as a result of the conversion. Independent of the decision to convert, Blue Cross has decided to put less emphasis on expanding its ASO line of business, and more emphasis on growing its insured lines. Blue Cross does not intend on completely terminating any lines of business as a result of the conversion. As always, changes in the product mix may occur in the future as necessary to respond to consumer demand.

7. *Will the converted Blue Cross seek to reduce or terminate services in any region of this State in which it is currently active?*

There are no plans to terminate or reduce services in any region.

8. *What effect, if any, would the conversion from a non-profit service insurance corporation to a stock insurance have on the factors determining rate levels?*

Many factors influence premium rates. Chief among them is medical inflation; that is, health care costs. Other factors that could influence premium rate increases

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include rising administrative and increased sales costs. Whether or not Blue Cross is a not
for

profit or shareholder owned entity does not effect medical inflation, nor does it necessarily effect sales or administrative costs. These factors affect not for profit and shareholder owned entities similarly. However, in order to maintain an appropriate level of capital and surplus a shareholder owned company has more alternatives when faced with rising medical costs than does a service insurance corporation. For example, a service insurance corporation when faced with the prospect of underachieving results has limited options. Among other things, it may choose to raise premium rates, or it may choose to take out a surplus note, that is borrowing more money. On the other hand, a shareholder owned company has more options which are not otherwise available to a not for profit entity. Alternatives include, but are not limited to; raising premium rates, borrowing money, issuing equity securities, or taking on an equity partner.

9. *Does management anticipate any changes in its marketing practices or distribution channels?*

Blue Cross currently uses independent agents and sales employees to market all its group and individual products except Value Plus and Medicare Blue. These two products are sold exclusively by telemarketers who are Blue Cross employees. Blue Cross also intends to add the Internet as a marketing channel in the near future. Although usage of independent agencies can fluctuate over time, there are no plans to alter present distribution channels as a result of the conversion. Any future changes in distribution channels would be the result of routine and ongoing business marketing strategy.

10. *Describe the company's plans for charitable contributions and commitment to community outreach after the conversion in comparison to past practices.*

Blue Cross has contributed to various charitable, educational, and health organizations which benefit the people of Wisconsin. For example, Blue Cross contributed over \$60,000 in 1999 and has contributed over \$225,000 since 1995 to the Trigger Lock program of the Child Safe Foundation, a non-profit foundation formed by the State Medical Society to promote injury intervention and safety among Wisconsin children. Blue Cross has helped to fund over 20,000 trigger lock distributions to gun owners throughout the state. Blue Cross also sponsors the annual Nurse of the Year award presented by the Wisconsin League for Nursing. This year Blue Cross contributed \$30,000 to this program honoring Wisconsin's outstanding nurses. Given our leadership in health industry, Blue Cross also sponsors anti-smoking campaigns which improve the overall wellness of Wisconsin citizens. We are proud of our participation in the American Cancer Society's Freshstart Smoking Cessation program, the Smoke Free Class of 2000 and Teens Against Tobacco Use. This year alone Blue Cross has contributed \$55,000 to these important programs. Aside from these major campaigns, Blue Cross supports various organizations that serve the state, including Milwaukee Public Television, African World Festival, a celebration of African-American culture, and the Coalition of Wisconsin Aging Groups. Blue Cross' commitment to the communities we

serve will continue regardless of whether Blue Cross is a shareholder owned or not for profit corporation.

In conjunction with the corporation's commitment to giving, members of the Blue Cross executive staff are actively involved in public interest organizations. For example, Senior Vice-President Penny Siewert is the President of the Board of Trustees for the LaFarge Lifelong Learning Institute, an organization devoted to the educational advancement of seniors. Ms. Siewert also serves on the board of the American Lung Association of Wisconsin and is a board member of the National American Lung Association's marketing initiative, Marketing Response Systems. Our executives' commitment to public service will continue regardless of whether Blue Cross is a shareholder owned or not for profit corporation.

11. *Does Blue Cross plan to purchase or sell any books of business over the next twelve months?*

Blue Cross is presently reviewing three possible acquisitions concerning blocks of insured business in Wisconsin. The negotiations concerning these blocks of business are the subject of confidentiality agreements.

12. *Is it anticipated that the number of people employed by Blue Cross and the holding company system that it presently controls will increase or decrease? If so, what is the anticipated magnitude of the change?*

There will be no material increases or decreases in staffing due to the conversion. As is always the case in business, adjustments in staffing (either increases or decreases) may occur as a result of normal business fluctuations.

13. *From what locations are Blue Cross operations conducted or regularly supported other than the home office in Milwaukee, Wisconsin? What general functions are conducted from these offices? Does management anticipate opening or closing any new offices over the next twelve months?*

Blue Cross corporate headquarters is currently located in downtown Milwaukee at 401 W. Michigan Street. Additionally, Blue Cross operates a regional service center at another downtown Milwaukee location. As previously announced, Blue Cross is in the process of consolidating its downtown Milwaukee operations into the 401 W. Michigan Street corporate headquarters site, a 200,000 square foot office building. Blue Cross also has previously announced an expansion of operations at its sales and service office in Ashland, Wisconsin.

As a not for-profit entity, it has been Blue Cross' business strategy to expand regionally in the state of Wisconsin to better service our customers throughout the state.

That strategy will not change as a result of the conversion. To date, Blue Cross has twelve sales and service offices located throughout the state, including five primary regional service center offices. (A complete listing of each office by location is attached as Attachment A)

The Stevens Point, Eau Claire, Fond du Lac, and Evansville offices provide service to group product subscribers in each region. Customer service, sales, underwriting, claims operations, and provider contracting departments are located in each regional office.

The Ashland office provides data entry support to the Stevens Point office. Personnel in the Ashland office also process Medicare Part A claims and Medicaid claims for United Government Services, LLC (UGS), a wholly owned subsidiary of Blue Cross. UGS anticipates that an additional 30 positions will be created for the Ashland office in the next 12 months.

The Platteville office provides operational support to the southeast region, including customer service, claims and enrollment.

Agency sales for the southwest region is located in our Sauk City office.

The Oshkosh office provides customer service and claims operations for Blue Cross individual products, including Medicare Supplement and Medicare + Choice products.

The Pewaukee office provides sales and underwriting services for individual products as well as telemarketing for group products. The Pewaukee office also provides production support, information systems, and marketing services.

The Brookfield office provides the southeast region with underwriting, sales and customer relations support.

By the end of the year, Blue Cross southeast operations will be conducted from the 401 Building. Corporate departments that provide services to Blue Cross, such as Legal, Finance, and Actuarial are also located at the 401 Building.

As mentioned previously, UGS is a wholly owned subsidiary of Blue Cross. Pursuant to a contract between Blue Cross and the United States Health Care Financing Administration (HCFA), UGS process Medicare Part A claims from eleven offices located in Wisconsin, Illinois, Michigan, New York, Virginia and West Virginia.

14. *What changes does management anticipate with respect to service, management, cost allocation, or other written agreements among members of Blue Cross' holding company system?*

If the conversion is approved and the new holding company becomes the primary Blue Cross and Blue Shield Association (BCBSA) licensee, current guarantee agreements between Blue Cross and Compcare Health Services Insurance Corp. and between Blue Cross and United Government Services will be changed so that the new primary licensee (the holding company) is the guarantor of the obligations of those companies. New guarantee agreements will be executed between the holding company and Blue Cross as a condition of Blue Cross' BCBSA licensure as a controlled affiliate of the holding company. Current inter-company agreements will also be amended to include the new holding company as a party to most agreements. Although there will be some changes to our cost allocation system to account for the new holding company, Blue Cross does not anticipate these changes to be material.

Miscellaneous

15. *The proposed "Officer's Certificate Regarding Approval of the Plan of Conversion by Members of BCBSUW" (Exhibit 1A) anticipates that 8 members will vote, rather than nine. Is it anticipated that the membership of the board will be reduced prior to the vote on this matter?*

Article IV of the Blue Cross Articles of Incorporation states that the *members* of the corporation are the *Elected Directors* and that only members may vote. Article II of the Blue Cross Bylaws states that the Chairman of the Board is an "ex officio" director and not an Elected Director. Therefore, Tom Hefty as Chairman of the Board is not a member of the corporation and not entitled to vote. All 8 members of Blue Cross will vote on the plan of conversation.

Sincerely,

Stephen E. Bablitch

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Enclosures
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