GOVERNMENT OF THE DISTRICT OF COLUMBIA
DEPARTMENT OF INSURANCE AND SECURITIES REGULATION

In Re: National Capital Reciprocal Insurance Company	))))	**RICC-98-01**

DECISION AND ORDER

Jurisdiction

Jurisdiction, for the purpose of considering the proposed reorganization of the National Capital Reciprocal Insurance Company ("NCRIC"), a reciprocal malpractice insurance company for physicians domiciled in the District of Columbia, properly resides before the District of Columbia Department of Insurance and Securities Regulation ("DISR") pursuant to the Holding Company Systems Act of 1993, D.C. Code § 35-3701 et seq. ("HCS Act"), the D.C. Administrative Procedure Act, D.C. Code § 1-1501 et seq. ("D.C. APA") and the Reciprocal Insurance Company Conversion Act of 1998, D.C. Act 12-301; D.C. Code § 35-3741 et seq. ("RICC Act").

Procedural History

On August 26, 1998, NCRIC filed a Statement Regarding the Acquisition of Control of or Merger with a Domestic Insurer (Form A) with DISR. DISR # 29[1]. In brief, NCRIC proposed to reorganize pursuant to the RICC Act by forming a mutual insurance holding company (NCRIC, a Mutual Holding Company), which would control two downstream intermediate holding companies (NCRIC Holdings, Inc. and NCRIC Group, Inc.). NCRIC Ex. 2; DISR # 73. These intermediate holding companies would control a stock insurance company (NCRIC , Inc.). NCRIC Ex. 2; DISR # 43. The mutual holding company would retain ownership and control of at least a majority of the outstanding voting shares of NCRIC , Inc. (the stock insurance company). NCRIC Ex. 2. Each policyholder would, as a result of the reorganization, become a member of the mutual holding company. Id. As a result, each present member of NCRIC would retain his or her insurance contract rights with the stock insurance company (NCRIC, Inc.), while at the same time retaining his or her membership interest in the mutual holding company which, through the intermediate holding companies, would control the stock insurance company. NCRIC Ex. 2, Summary p. 8.

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[1] Citations to written documentation or oral testimony will be as follows: Transcript ("Tr. [page]"); Exhibits received into evidence at the Hearings ("Gov't. Ex. ___"); "NCRIC Ex. _____" (for NCRIC Exhibits); All correspondence and legal documents received by DISR ("DISR # _____"). In some instances, documents will be included both in the DISR Document record and the Hearing Record.

On July 24, 1998, NCRIC forwarded a notice of the public hearing along with an information statement to NCRIC policyholders, holders of reporting endorsements issued by NCRIC, and holders of subordinated surplus loan certificates issued by NCRIC. DISR # 42, 43; NCRIC Exs. 2, 3. Notice of a hearing pursuant to the RICC Act (the "Notice") was published in the *D.C. Register* on August 7, 1998, DISR # 71, and in *The Washington Post*, DISR # 49, NCRIC Ex. 9, and *The Washington Times*, DISR # 48, NCRIC Ex. 10, on August 9, 1998.

The Notice established that any "person whose interest may be affected", D.C. Code Ann. § 35-3703(g)(2), would have certain rights and opportunities to participate in the hearing. However, any such person would be obliged to notify DISR both of the person's interest and the extent to which the person proposed to participate in the prehearing and hearing process. Only two entities notified DISR of their interest and the extent to which they proposed to participate in the prehearing and hearing process. One was from NCRIC, DISR #51, and the other was from the Medical Society of the District of Columbia ("MSDC"). DISR #54. On September 4, 1998, the Commissioner issued a Prehearing Order which set forth the rules for participation in the hearing consistent with the interests of justice and the efficient administration of the regulatory process. DISR #71.

On September 9 and 10, 1998, a public hearing was held before Patrick E. Kelly, Commissioner of DISR ("Commissioner"), along with Leslie E. Johnson, Hearing Officer. The following individuals presented testimony at the hearing on behalf of NCRIC: Nelson Trujillo, MD, Chairman of the Board of Governors of NCRIC; R. Ray Pate, Jr., President and Chief Executive Officer of NCRIC's Attorney-in-Fact, National Capital Underwriters, Inc.; Patrick Coyne, MD, a member of NCRIC; Eric Van Nispen, a managing director of Sandler, O'Neil & Partners, LP; and Carson P. Porter, James B. Halpern and John P. Foley of Arent, Fox, Kintner, Plotkin & Kahn, PLLC, counsel for NCRIC. David A. Covington of Deloitte & Touche, LLP and E. Dow Walker, Jr. of Willis Corroon submitted written statements on behalf of NCRIC. Edward Shanbacker, Executive Director of MSDC, along with Lawrence Lamade of Jones, Day, Reavis & Pogue, counsel for MSDC, presented testimony on behalf of MSDC. Participating on behalf of DISR were the following: Acting Deputy Commissioner Reginald Berry, Attorney/Advisor Rhonda Davis, Senior Attorney Dana G. Sheppard, Assistant Deputy Commissioner Thomas Hampton, and Robert H. Myers, Jr., Special Counsel to the Commissioner.

The hearing terminated on September 10. However, the hearing record remained open by Order of the Commissioner through September 23, 1998. Tr. 296. Several submissions, including a proposed Decision and Order from NCRIC, were submitted before the record closed on that date. DISR #85-94.

A Proposed Decision and Order was forwarded to NCRIC and MSDC on November 4, 1998, as "persons whose interests may be affected", D.C. Code § 35-3703(g)(2). NCRIC and MSDC were instructed to submit their comments, if any, to the

DISR on or before 5:00 p.m. on November 13, 1998. The Commissioner received comments and recommended changes from NCRIC and MSDC. The Commissioner reviewed and considered the comments and recommended changes prior to rendering his final Decision and Order.

Issues Considered

The following issues were considered by the Commissioner at the hearing:

(1) Whether NCRIC's plan complies with the RICC Act?

(2) Whether testimony from interested persons for or against NCRIC's Plan of Reorganization was solicited and taken into consideration at the hearing?

(3) What is the present financial condition of NCRIC before the reorganization and whether the subsequent reorganization will have any adverse impact upon the financial condition of NCRIC, Inc.?

(4) Whether the interests of the policyholders (members and reporting endorsement holders) are properly protected and whether the Plan of Reorganization is fair and equitable to the policyholders (members and reporting endorsement holders)?

(5) Whether additional regulatory requirements are necessary to comply with the law, to comply with the intent of the law or to protect the interests of NCRIC's policyholders and/or the public?

Analysis of Issues

1. Whether NCRIC's Plan complies with the RICC Act?

The purpose of the RICC Act is to "allow a reciprocal insurance company to restructure itself by forming a mutual insurance holding company that directly or indirectly owns the insurance company, with the reorganized insurance company continuing its existence as a stock insurance company". Preamble, D.C. Act 12-301. Compliance with the RICC Act requires that certain steps be taken.

The Commissioner held a public hearing to determine whether the proposed reorganization complies with the dictates of the RICC Act. Tr. 1-297. NCRIC, through its witnesses, presented testimonial and documentary evidence, on each of the following issues to demonstrate that NCRIC's plan of reorganization complies with the RICC Act.

a) Upon approval of the Commissioner, NCRIC intends to form NCRIC, a Mutual Holding Company (a District of Columbia mutual insurance holding company) that will initially own one hundred percent (100%) of the voting shares of NCRIC Holdings, Inc. (a District of Columbia stock holding company), which will own one

hundred percent (100%) of the voting shares of NCRIC Group, Inc. (a District of Columbia stock holding company), based upon a conversion plan ("Plan"). NCRIC Ex. 2; D.C.Code Ann. § 35-3742(a); Plan Section 2.1; Tr. 70-71.

b) Pursuant to NCRIC's Plan of Reorganization, NCRIC intends to reorganize the stock insurance company, NCRIC, Inc., as an indirectly owned stock insurance company subsidiary of the mutual holding company, NCRIC, a Mutual Holding Company. As proposed, the reorganized insurance company would continue its existence without interruption. D.C. Code Ann. § 35-3742(a); Plan Sections 2.1, 2.5; Tr. 70. During the hearing, DISR questioned NCRIC's intent to form two (2) intermediate holding companies rather than the traditional one (1) intermediate holding company. Tr. 127, 167.

NCRIC stated that it decided to form two (2) intermediate holding companies between NCRIC, Inc. and NCRIC, a Mutual Holding Company, because of issues relating to the declaration and payment of dividends. First, NCRIC intends to conduct any public offering at the intermediate holding company level rather than through the stock insurance company. Accordingly, an initial public offering by a single intermediate holding company and a subsequent payment of a dividend would result in the receipt of cash by NCRIC, a Mutual Holding Company, as the holder of at least fifty-one percent (51%) of the shares of the intermediate holding company's stock. Because NCRIC, a Mutual Holding Company, proposes to function as a holding company and not an operating company, the declaration and payment of a dividend would result in both insurance and securities regulatory problems should NCRIC, a Mutual Holding Company, attempt to move the money downstream into one its operating subsidiaries. For that reason, NCRIC asserts that placing NCRIC Holdings, Inc. between NCRIC, a Mutual Holding Company and NCRIC Group, Inc. and conducting any public offering through NCRIC Group, Inc. would eliminate the aforementioned problem because any dividend declared and paid by NCRIC Group, Inc. would be paid to NCRIC Holdings, Inc., where it could be used for acquisitions and other purposes. Tr.129-131, 167-175.

While the Commissioner is mindful of the representations made by NCRIC on the need for two (2) intermediate holding companies, the inclusion of an additional holding company between the NCRIC, Inc. and NCRIC, a Mutual Holding Company, present certain regulatory concerns, specifically, the authority to regulate the activities of an additional intermediate holding company. Accordingly, as a condition of approval, the Commissioner deems it necessary to reaffirm its regulatory authority over both intermediate companies in the Conditions and Undertakings Section of this Decision and Order.

c) All of the initial shares of the capital stock of the reorganized stock insurance company shall be issued to the mutual insurance holding company. Plan Section 2.2; Tr. 70; D.C. Code Ann. § 35-3742(c).

d) The policyholders of the reorganized stock insurance company shall be members of the mutual insurance holding company in accordance with the articles of incorporation and bylaws of the mutual insurance holding company. Further, policyholders of the reorganized stock insurance company shall retain the same membership rights owned as members of NCRIC, the reciprocal insurance company. D.C. Code Ann. § 35-3742(d); Plan Section 2.3; Articles of Incorporation of NCRIC, a Mutual Holding Company, Art. VII; Bylaws of NCRIC, a Mutual Holding Company, Art. II.

e) The mutual insurance holding company shall at all times indirectly own a majority of the voting shares of the capital stock of the reorganized insurance company through its ownership and control of the two (2) intermediate holding companies. NCRIC Ex. 2, Summary p. 8; Tr. 40.

2. **Whether testimony from interested persons for or against NCRIC's Plan of Reorganization was solicited and taken into consideration at the hearing?**

At the hearing, extensive testimony was presented by NCRIC, through its representatives R. Ray Pate, Jr., President and Chief Executive Officer of National Capital Underwriters, Inc. and Nelson Trujillo, Chairman of NCRIC, and its counsel, Carson Porter and James Halpern.

Mr. Pate testified that the physician's malpractice industry in the District of Columbia and the Mid-Atlantic Region has become an increasingly competitive marketplace. He stated that in order for NCRIC to remain competitive and effective, NCRIC must continue to grow. In its current form as a reciprocal insurance company, NCRIC is severely limited in its ability to raise substantial amounts of capital, which can be used to facilitate acquisitions and other strategic opportunities. Moreover, Mr. Pate, in his testimony, assured the Commissioner "that funds raised from capital sources will be directed to the Reorganized Stock Company on an as-needed basis to improve the quality of its malpractice insurance product, maintain a competitive pricing structure, and ensure the stability and longevity of the Reorganized Stock Company." DISR #78, p. 9.

In support of the transaction, Dr. Trujillo testified that in October 1997, the Board of Governors of NCRIC considered and approved Strategic Plan 2000, which provides for NCRIC to become a comprehensive healthcare financial services company. The Board reached its decision after consideration and with the assistance of financial and legal experts. It is Dr. Trujillo's belief, that NCRIC, in its current form, would not be able to compete effectively and successfully without reorganizing into a mutual insurance holding company structure. Finally, Dr. Trujillo stated that the purpose of the reorganization is to raise an adequate amount of capital to finance its growth plans. Tr. 27-43.

In addition, testimony was presented by Patrick Coyne, MD, a member policyholder of NCRIC, who is not affiliated in any way with management. Dr. Coyne

was generally supportive of the reorganization based on his understanding that it was in the NCRIC's best interest to restructure in order to remain competitive. Tr. 92-103.

The investment banking firm of Sandler, O'Neill and Partners, LP, opined that "the exchange of Membership Interests in the Company for Membership Interests in the Mutual Holding Company pursuant to the Plan is fair, from a financial point of view, to Policyholders who are Members of the Company, taken as a group." NCRIC Ex. 14. In addition, Eric Van Nispen of Sandler O'Neill and Partners, LP submitted a statement for the record, NCRIC Ex. 14, and then testified, Tr. 176, that the transaction was "fair from a financial point of view" to policyholders.

In addition, two other witnesses, who were unable to testify personally due to time constraints, David Covington of Deloitte & Touche, LLP and E. Dow Walker, Jr. of Willis Corroon, submitted written statements on behalf of NCRIC. Mr. Covington's statement indicated that "the carrying values of NCRIC's equity in NCRIC MSO, Inc. and NCRIC Physician Organization, Inc. of zero and deficit $17,000, respectively, at December 31, 1997, have been eliminated from the investment account." He further stated that the "subtraction of the negative amount of $17,400 resulted in a corresponding increase in the investment in unconsolidated subsidiaries on a pro forma basis." DISR # 80. Mr. Walker's statement outlined the current conditions in the medical malpractice insurance field. DISR #89.

Only one other entity, MSDC, expressed an interest in testifying. MSDC's testimony was generally supportive of the proposed reorganization. DISR # 54. However, MSDC urged that DISR provide close oversight to ensure that policyholder interests would continue to be protected. Tr. 294; DISR #54 .

3. **What is the present financial condition of NCRIC and whether the subsequent reorganization will have any adverse impact upon the financial condition of NCRIC, Inc.?**

NCRIC submitted information regarding its financial condition and the effects the proposed reorganization would have upon it. E.g., DISR #11 (NCRIC's 1996 Annual Report); DISR #12 (statement regarding Best's upgrade of NCRIC's rating (1997)), DISR #18 (NCRIC's 1997 Annual Report); DISR #29 (NCRIC's Form A); DISR #35 and NCRIC Ex. 13 (Deloitte & Touche's independent accountant's report). In addition, the issue of NCRIC's financial condition was discussed on various occasions during the testimony. See e.g., Tr. 29. The testimony supported the conclusion that the reorganization, other than the legal, accounting, and related transactional expenses, Tr. 30-34, should not affect NCRIC's financial condition, particularly capital and surplus. The Deloitte & Touche Condensed Pro Forma study concluded that the equity in NCRIC would only be reduced as a result of the reorganization by the assumed expense of the transaction ($300,000) less a credit ($17,400) resulting from the transfer of two subsidiaries of NCRIC (NCRIC MSO, Inc. and NCRIC Physicians Organization, Inc.) that currently have a negative net worth. Those subsidiaries would become subsidiaries

of NCRIC Group, Inc. DISR #35, NCRIC Ex. 13. On the other hand, testimony was received from various quarters supporting the conclusion that the reorganization would allow NCRIC to obtain capital, form subsidiaries to provide products complementary to the core insurance product and, in general, allow more competitive operation of the business. See e.g., DISR #89, Tr. 49, 112-113.

4. **Whether the interests of the policyholders (members and reporting endorsement holders) are properly protected and whether the Plan of Reorganization is fair and equitable to the policyholders (members and reporting endorsement holders)?**

The issues of whether the interests of policyholders are properly protected and whether the conversion plan is fair and equitable to their interests are logically linked and, therefore, will be considered together.

NCRIC presented lengthy and persuasive testimony in support of the proposed reorganization. E.g., Tr. 36-42, 47-50. In brief, the management of NCRIC concluded that, in order for NCRIC to grow and remain competitive, it needs to restructure to gain access to capital, Tr. 36-37, to facilitate acquisitions consistent with NCRIC's business objectives, Id., to enhance operating efficiencies, Tr. 47, and to streamline a constraining organizational form. Tr. 48-50.

NCRIC's management made the recommendation to reorganize only after substantial study and discussion among the members of NCRIC's Board of Governors. E.g., Tr. 31-32. In addition, a substantial effort was made to educate the physician members of NCRIC regarding the proposed reorganization in mailings to members and in face-to-face meetings. Tr. 38-49. Not only did the management of NCRIC obtain a "fairness" opinion from the investment banking firm of Sandler, O'Neill & Partners, LP, which was presented in testimony, Tr. 176-185, NCRIC Ex. 14, but the Board obtained an opinion from counsel, Jackson & Campbell, regarding the Board's due diligence. Tr. 19-20, NCRIC Ex. 12. NCRIC policyholders voted overwhelmingly to approve the reorganization. Tr. 40; DISR #86.

Most importantly, testimony was presented that the members of NCRIC will, after the conversion, continue to control NCRIC's management and operation. Tr. 86-87. Policyholder contract rights will continue with the reorganized stock insurance company while the members of NCRIC will continue to exercise control of the mutual holding company. Tr. 52; NCRIC Ex. 2, p. 8. As a result, it is reasonable to conclude that the interests of NCRIC's members, assuming those members exercise reasonable oversight, should not be "diluted" in the future. Tr. 154, 159.

Significantly, no written submissions or testimony were received contradicting the assertion by NCRIC that the proposed transaction was "fair and equitable" to policyholders. The Plan does not discriminate among policyholders in terms of their rights and obligations. However, while the policyholders of NCRIC are members and,

accordingly, are granted subscription rights in the event of an initial public offering, reporting endorsement holders are not. NCRIC Rules, Regulations, and Bylaws, Art. II; DISR #27 (reporting endorsement holders do not qualify for membership because they are not actively involved in the practice of medicine, osteopathy, dental surgery or dental medicine). The Commissioner finds after considering the testimony and evidence that that the differentiation among two classes of policyholders (members and retired or inactive members) is not fair and equitable. Accordingly, to remedy the differentiation among the two classes of policyholders the Conditions and Undertakings portion of the Order will require comparable treatment regarding subscription rights.

The testimony of MSDC supported NCRIC's position that the proposed reorganization would improve the quality of NCRIC's services to policyholders and enhance its financial stability. Tr. 291-292. However, MSDC acknowledged its need for assistance from DISR in order to safeguard policyholder interests in the future. Tr. 294.

Therefore, it is the finding of the Commissioner that the proposed reorganization adequately protects the interests of policyholders and is fair and equitable, subject to the regulatory requirements referenced below and in the Conditions and Undertakings Section of this Order.

5. **Whether additional regulatory requirements are necessary to comply with the law, to comply with the intent of the law or to protect the interests of the policyholders and/or the public?**

The RICC Act clearly establishes that it is the obligation of the Commissioner to determine both that (1) "the interests of policyholders are properly protected" and (2) "the conversion plan is fair and equitable to policyholders". D.C. Code Ann. § 35-3742(b). Much testimony was presented on these issues. In addition, substantial testimony was presented, and numerous questions were posed, to examine the nature of regulatory safeguards that could be imposed for the purpose of ensuring that the interests of policyholders were protected and that the Plan was fair and equitable not only at the time of conversion, but, just as importantly, in the future. Testimony was elicited, and assurances were given, on the following issues, which will be incorporated into the Conditions and Undertakings of this Order.

First, in regard to the issue of adequate representation and control of the mutual holding company, NCRIC agreed that the interests of policyholders could best be served by a requirement that at least two-thirds of the members of the board of directors of the mutual holding company be policyholders. Tr. 57.

Second, concerns were expressed by MSDC that the funds to be raised subsequent to the reorganization be utilized for the benefit of policyholders. NCRIC offered its assurance that "the funds raised from capital sources will be directed to the reorganized stock company on an as-needed basis to improve the quality of its malpractice insurance

product, maintain a competitive pricing structure, and ensure the stability and longevity of the reorganized stock company". Tr. 58-59.

Third, NCRIC similarly affirmed that it would "not diversify out of the health care and insurance-related fields". Tr. 61.

Fourth, in response to concerns expressed regarding the security of assets of the insurance company after the reorganization, NCRIC pledged that it would not pledge "assets of the reorganized stock company having a value in excess of 49 percent of the equity of the insurance company without the approval of the Commissioner". Tr. 64-65, 138, 240-42.

Fifth, the scope of the jurisdiction of DISR under the RICC Act was considered to be a matter of substantial importance. Accordingly, NCRIC acknowledged that DISR would maintain jurisdiction over the mutual holding company and any amendments to its corporate documents, Tr. 65, as well as jurisdiction over all intermediate holding companies and the insurance company, Tr. 128, 224-5.

Sixth, concerns were expressed regarding the rights of reporting endorsement policyholders. NCRIC pledged that in the event that an initial public offering ("IPO") should occur, reporting endorsement policyholders would have subscription rights. Tr. 232-33.

Seventh, in response to concerns expressed regarding the availability and timeliness of financial information, NCRIC agreed to file with DISR quarterly reports for all companies within the holding company system on a non-consolidated basis for the purpose of allowing DISR to determine that policyholder interests were being protected. Tr. 234-35, 238.

Eighth, in response to concerns expressed by MSDC regarding policyholder control after the reorganization, NCRIC agreed to a requirement that a super majority of two-thirds (2/3) seats on the board of the stock insurance company be set aside for NCRIC policyholders, Tr. 243-44, and that the articles of incorporation be changed to that effect, Tr. 295.

Findings of Fact

After a careful evaluation and analysis of the evidence, the Commissioner makes the following findings of fact:

1. In conformity with D.C. Code Ann. § 35-3742, NCRIC filed an application for approval of its proposed reorganization. NCRIC Ex. 25.

2. The Plan was unanimously approved by NCRIC's Board of Governors on April 20, 1998. NCRIC Ex. 1.

3. NCRIC provided its policyholders, reporting endorsement holders, and supplemental surplus loan holders with a detailed information statement, a copy of the plan and a copy of the notice of the hearing. NCRIC Exs. 2, 3. The notice of the hearing was published in the *D.C. Register*, *The Washington Post* and *The Washington Times*. NCRIC Exs. 9, 10; DISR #45.

4. Only NCRIC and MSDC responded to the notice by designating an interest as a "person whose interest may be affected". DISR #51, #54

5. At the hearing, NCRIC presented four witnesses to testify and be cross-examined. Two additional witnesses presented statements at NCRIC's request. No other policyholders or representatives appeared at the hearing to present testimony, other than MSDC. Tr. 297.

6. NCRIC's witnesses presented testimony that was substantially unrebutted that the Plan would permit NCRIC to reorganize to develop new businesses and to obtain capital, to obtain greater flexibility and to facilitate acquisitions, all of which was consistent with the needs of NCRIC's members. E.g., Tr. 27-42, 47-50.

7. The testimony of NCRIC's witnesses that the reorganization is in the best interests of NCRIC and, therefore, of its policyholders was unrebutted by any policyholder.

8. Representatives of NCRIC met on various occasions with NCRIC members or their representatives and provided substantial information to permit members to make an informed decision. Tr. 37-40.

9. On September 16, 1998, a special meeting of policyholders of NCRIC was held at which policyholders voted to approve the Plan by a vote of 526 For and 21 Against. DISR# 87.

10. The financial condition of NCRIC before the reorganization and the subsequent financial condition of NCRIC, Inc., as a stock insurance company, have been assessed, and the financial condition of the companies succeeding NCRIC will not be diminished by the reorganization. NCRIC Ex. 13.

11. The Commissioner finds that the proposed reorganization adequately protects the interests of policyholders and is fair and equitable, subject to the regulatory requirements referenced below and in the Conditions and Undertakings Section of this Order.

Conclusions of Law

After careful evaluation of the evidence and the Findings of Fact, the Commissioner makes the following Conclusions of Law:

Continuation of Existence without Interruption, D.C. Code § 35-3742(a)

NCRIC's conversion plan is authorized by the Reciprocal Insurance Company Conversion Act of 1998, D.C. Code § 35-3742 (a), which permits NCRIC, a reciprocal insurance company to form a mutual insurance company, subject to the approval of the Commissioner. The Commissioner concludes that NCRIC's plan of reorganization ensures that NCRIC, the reorganized insurance company, shall continue, without interruption, its existence as NCRIC, Inc., a stock insurance company subsidiary of NCRIC Group, Inc., a subsidiary of NCRIC Holdings, Inc. NCRIC Holdings, Inc. will be a subsidiary of NCRIC, a Mutual Holding Company, as required by the RICC Act. Id. The Commissioner carefully considered NCRIC's testimony in support of its reasons for including an additional intermediate holding company and will permit such a structure, subject to the provisions set forth in the Conditions and Undertakings Section of this Decision and Order.

Conversion is Fair and Equitable to Policyholders, D.C. Code § 35-3742(b)

The Commissioner is satisfied that the interests of NCRIC's policyholders are properly protected and that the conversion is fair and equitable to all of the policyholders, including reporting endorsement holders, subject to the provisions set forth in the Conditions and Undertakings Section of this Decision and Order, as required by D.C. Code § 35-3742 (b). The Commissioner reaches this conclusion on the uncontradicted testimony of Drs. Trujillo and Coyne, and Messrs. Pate and Walker. All of the testimony received from these three witnesses supports NCRIC's assertion that the reorganization from a reciprocal insurer to a mutual holding company structure is in the long-term best interests of NCRIC. Moreover, the statements received from Messrs. Covington and Van Nispen and the aforementioned four witnesses support the conclusion that the Plan is fair and equitable to policyholders. Finally, the Commissioner carefully considered the concerns raised by MSDC and will consider its position in crafting the Conditions and Undertakings to be imposed on NCRIC pursuant to this Decision and Order. D.C. Code § 35-3742(b).

Commissioner's Continuing Jurisdiction Over the Mutual Insurance Holding Company, D.C. Code § 35-3742(b)

The Commissioner through the insurance laws of the District of Columbia, in general, and this Decision and Order, in particular, intends to maintain close regulatory control over NCRIC, Inc., NCRIC Group, Inc., NCRIC Holdings Inc., and NCRIC, a Mutual Holding Company, and related entities in the NCRIC mutual holding company

structure, to ensure compliance with the insurance laws of the District, as required by D.C. Code § 35-3742(b).

Merger of Membership Interests in the Mutual Insurance Holding Company, D.C. Code § 35-3743(a)

Pursuant to the Plan of Reorganization, NCRIC intends to merge its policyholders' membership into NCRIC, a Mutual Holding Company, without interruption. In addition, the Plan of Reorganization provides that NCRIC, without interruption, will continue the existence of NCRIC as NCRIC, Inc., a stock insurance company subsidiary of NCRIC Group, Inc., which will be a subsidiary of NCRIC Holdings, Inc. NCRIC Holdings, Inc. will be a subsidiary of NCRIC, a Mutual Holding Company, in compliance with D.C. Code § 35-3743(a).

Ownership of at Least a Majority of the Shares of the Reorganized Stock Insurance Company, D.C. Code § 35-3743 (c) and (d)

The Commissioner has determined that NCRIC's Plan of Reorganization provides that all of the initial shares of NCRIC, Inc., the reorganized stock insurance company, shall be issued indirectly to NCRIC, a Mutual Holding Company. Such indirect ownership satisfies the requirements of D.C. Code § 35-3743(c) and (d) because NCRIC, a Mutual Holding Company, will initially own all of the shares of stock of NCRIC Holdings, Inc., which will initially own all of the shares of stock of NCRIC Group, Inc., which will initially own all of the shares of stock of NCRIC, Inc., the reorganized stock insurance company. This indirect ownership is contemplated and permitted by D.C. Code § 35-3742(a).

In the event of any public offering, the Plan of Reorganization provides that the members of NCRIC, a Mutual Holding Company, will always own at least a majority of the shares of stock of NCRIC, Inc., the reorganized stock insurance company. The Commissioner concludes that the Plan satisfies the requirements of D.C. Code § 35-3743 (d).

Accordingly, the Commissioner concludes that NCRIC's Plan of Reorganization complies with the requirements of D.C. Code § 35-3741 *et seq.*

ORDER

It is, ORDERED that the proposed reorganization of NCRIC, pursuant to the RICC Act, be and is hereby AUTHORIZED AND APPROVED, subject to the satisfaction of the following Conditions and Undertakings, each of which shall be deemed to be supplementary to, and not in derogation of, existing applicable statutes, regulations, and orders:

CONDITIONS AND UNDERTAKINGS

1. NCRIC must receive a ruling from the Internal Revenue Service or an opinion from tax counsel or accountants on tax matters pursuant to § 3.3(c) of the Plan.

2. At least two-thirds (2/3) of the members of the Board of Directors of NCRIC, a Mutual Holding Company, must at all times be policyholders of NCRIC, Inc. and the Articles of Incorporation of NCRIC, a Mutual Holding Company, must be amended accordingly.

3. NCRIC, a Mutual Holding Company, NCRIC Holdings, Inc., or NCRIC Group, Inc. are prohibited from pledging assets having an aggregate value in excess of 49% of the equity of NCRIC, Inc. (based on the most recent financial statements prepared and calculated in accordance with statutory accounting principles) without the prior approval of the Commissioner.

4. NCRIC, a Mutual Holding Company, will provide the Commissioner with financial statements on a non-consolidated basis (based on statutory accounting principles) of each of its subsidiaries used in preparing consolidated financial statements of NCRIC, a Mutual Holding Company.

5. The Board of Directors of NCRIC, a Mutual Holding Company, shall first utilize funds raised from capital sources, if needed in its best judgment, to improve the quality of NCRIC, Inc.'s malpractice insurance product, maintain its competitive pricing structure, and ensure the stability and longevity of the reorganized stock insurance company.

6. In the event that NCRIC, Inc. NCRIC, Holdings, Inc., or NCRIC Group, Inc., or any other company in the NCRIC holding company structure, proposes to make an initial public offering or a subsequent public offering, the terms of the proposed offering must be submitted to the DISR for the Commissioner's prior review and written approval.

7. NCRIC, NCRIC, a Mutual Holding Company, NCRIC Holdings, Inc., NCRIC Group, Inc., or other entity shall not establish any additional intermediate holding companies without obtaining prior approval in the form of an official written order from the Commissioner.

8. The Commissioner of the DISR shall retain full regulatory authority over NCRIC, Inc., NCRIC, a Mutual Holding Company, NCRIC Holdings, Inc., and NCRIC Group, Inc., and any other intermediate holding companies that may be later included in the NCRIC holding company structure, consistent with the laws and regulations of the District of Columbia.

9. NCRIC shall provide fair and equitable subscription rights, in the event of an Initial Public Offering, or any subsequent public offering, to reporting endorsement policyholders pursuant to the Insurance Demutualization Act of 1996, D.C. Code § 35-4201 *et seq.*

10. NCRIC shall not, without prior approval from the Commissioner, by way of an acquisition or investment in a subsidiary, or otherwise, diversify out of the health care and insurance fields.

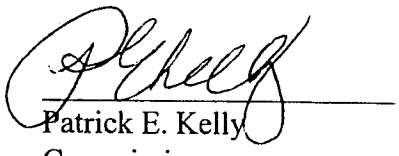
11. The Employment Agreement of R. Ray Pate, Jr. shall be amended to eliminate a "Change of Control", as referenced in Item 6 b(iii), from being deemed a termination "without cause", such amendment to remain in effect for two (2) years from the date of this Order.

12. This transaction is subject to further orders and further conditions and undertakings as the circumstances may require.

13. This Order is subject to further modification or amendment and further review either *sua sponte* or on petition of NCRIC.

14. NCRIC shall continue to be subject to the jurisdiction of DISR pursuant to the provisions of the RICC Act for purposes of implementing the terms of this Order, and the employing of experts necessary for such purpose, until further order of DISR.

Signed and Dated this 25th day of November, 1998.



Patrick E. Kelly
Commissioner