

In The
District of Columbia
Court of Appeals

**DISTRICT OF COLUMBIA,
DEPARTMENT OF INSURANCE, SECURITIES AND BANKING,**

Petitioner and Appellee,

v.

D.C. CHARTERED HEALTH PLAN, INC.,

Respondent and Appellee,

D.C. HEALTHCARE SYSTEMS, INC.,

Party in Interest and Appellant.

ON APPEALS FROM NO. 2012 CA2 008227 IN
THE DISTRICT OF COLUMBIA SUPERIOR COURT, CIVIL DIVISION,
THE HONORABLE MELVIN R. WRIGHT, JUDGE PRESIDING

BRIEF OF APPELLANT D.C. HEALTHCARE SYSTEMS, INC.

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APPELLANT'S CORPORATE DISCLOSURE STATEMENT

Appellant D.C. Healthcare Systems, Inc. is a private corporation that has no parent
corporation; no publicly-held corporation holds any of its stock; and its only subsidiary is
Appellee D.C. Chartered Health Plan, Inc.

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I. STATEMENT OF ISSUES

1. Did the trial court err in denying D.C. Healthcare Systems, Inc. (DCHSI), as both creditor and shareholder of D.C. Chartered Health Plan, Inc. (Chartered), standing to object to the Settlement Agreement between D.C. Chartered Health Plan, Inc. (in rehabilitation by the District of Columbia) and the District of Columbia (the “District Settlement” or “Settlement Agreement” or “Settlement”)?

2. Did the trial court err in basing its decision not to consider the Towers Watson Report – a report obtained by the Rehabilitator – on DCHSI’s standing to object to the District Settlement?

3. Did the trial court abuse its discretion in approving District Settlement when the trial court did not have sufficient facts before it to make an informed judgment in the absence of any discovery, any evidentiary hearing or any consideration of the Towers Watson Report and when the Settlement Agreement was so manifestly unfair as to preclude judicial approval?

II. INTRODUCTION

By persistent unwillingness to review relevant evidence presented to it with regard to the District Settlement and an unblinking deference to the District, the trial court’s “oversight” of the Chartered Rehabilitation amounted to nothing more than a rubber stamp of the District’s plan to create a financial windfall for itself while at the same time ensuring the final, business demise of Chartered and its owner DCHSI. Now, with judicial acquiescence, the District has accomplished the two actions it intentionally set out to accomplish – either one of which would have been fatal to the business of Chartered, and both of which were wrongful. First, the District knowingly and intentionally set actuarially unsound capitation rates for Chartered. Second, even given the unsound actuarial rates forced on Chartered by the District, the District acted intentionally to fail and to refuse to pay not less than \$62 million in fees due and owing to Chartered for Medicaid and Alliance services, provided by Chartered pursuant to contract, services that had been provided by Chartered for at least three years. Having done so, the District then relieved itself of that obligation with a bogus, unilaterally negotiated “settlement” with itself for which it sought

and received court approval – without so much as a nod in the direction of meaningful judicial oversight or supervision.

On or about June 11, 2013, the Rehabilitator sought and obtained an actuarial opinion from Towers Watson Pennsylvania, Inc. (“Towers Watson Report”). SA-233.¹ The Towers Watson Report examined only *one* of numerous categories of the District’s breaches of contract and intentional underpayments to Chartered. *As to just that one category alone* (relating to *only* twenty-two months out of a five-year contract), the Towers Watson Report concluded that the District owed Chartered over \$51.4 million. SA-240-45. The Towers Watson Report also showed that the District and its retained rate-setting actuary, Mercer, ignored significant information repeatedly provided by Chartered to the District, as well as information in DHCF’s possession, and engaged in a willful pattern of actuarially unsound and inadequate rate setting **that caused the capital depletion that purposefully drove Chartered into rehabilitation.** SA-264-67.

The District knew, understood, and intended that setting actuarially unsound rates, coupled with non-payment, would result in a material reduction of Chartered’s level of risk-based capital and would place Chartered in a financial position that would create a pretext for a regulatory take-over of the company followed by its prompt liquidation under the fraudulent guise of “rehabilitation”. The purpose for all of this was clear. The District needed to assert control over Chartered by way of a bogus “rehabilitation” through the Department of Insurance, Securities and Business (“DISB”) in order to obtain the veneer of administrative and judicial sanction for a plan to self-deal a gross reduction in the amount of the debt the District through

¹ The Supplemental Appendix (“SA”) will be designated as SA-*page(s)*. Appendix citations to the initial three volume Appellant’s Appendix (“AA”) (filed with this court on April 29, 2013), will follow: *volume-AA-page(s)*.

the Department of Health Care Finance (“DHCF”) owed Chartered (which would at that point be controlled by the District of Columbia through the Rehabilitation). At the same time, the District would achieve a corollary goal of removing DCHSI from control of Chartered and placing that control in the hands of a hand-picked, friendly bidder (AmeriHealth Mercy), in a sweet-heart deal, for minimal consideration. This is not speculation. This is what happened.

Prior to October 2012, the District had established with AmeriHealth Mercy what they intended to be the successor relationship to Chartered in terms of running the DC health care program – which prior to that date had been run for years successfully by Chartered. Finding a pretext to place Chartered into Rehabilitation and then pass the contract with the District over to AmeriHealth Mercy was a necessary component of the plan to dismantle DCHSI’s business and relieve the District of the burden of its legitimate debt to Chartered. The rehabilitation was also needed to cement the relationship with AmeriHealth Mercy because the District could rig **both** the bidding process for the new DHCF contract **and** the bidding process for Chartered. In other words, the District decided **in advance** that AmeriHealth Mercy would win the bid for the DHCF Contract **and** that they would take over Chartered’s business for a song.

With this scheme in place, the District initiated the bogus rehabilitation process of Chartered. Within six weeks of entry of the initial rehabilitation order specifically providing for the rehabilitation of Chartered as a business (and requiring a specific showing to the Court for any other plan of action), Chartered was in a state of complete liquidation – without any further action by the Court having been sought or received.

The District decided from the outset that their scheme would be simplified considerably if it could obtain DCHSI’s and Thompson’s consent rather than their opposition to the idea of a “rehabilitation.” To do this, the District intentionally misrepresented to DCHSI and Thompson

that in a proposed “rehabilitation” process, Chartered – whose sole business was its DHCF Contract with the District – would, in fact be subject to a legitimate rehabilitation process, ie., it would proceed with preparing and bidding on the new DHCF Contract in December 2012, thus preserving and maintaining the value of the business, and that Chartered’s parent and sole shareholder, DCHSI, would be consulted and cooperated with on any subsequent sale of Chartered or other corporate activity by way of reorganization or rehabilitation. None of these representations were true.

The District had already decided that Chartered would not submit a bid to renew its contract. The District had already decided that AmeriHealth Mercy would take over Chartered, submit that bid and win the bid. The District had already decided that all of the material assets of Chartered would be transferred to AmeriHealth for minimal consideration to assist AmeriHealth in making its bid and taking over Chartered’s position. Thompson and DCHSI relied on the materially false representations of the District in agreeing to the rehabilitation and in taking actions requested by the District to further the supposed “rehabilitation” process and were extinguished as viable companies thereby.

Within six weeks of obtaining Thompson’s and DCHSI’s consent to a rehabilitation that was never going to happen, Chartered, now controlled by the District, did not bid on its own DHCF contract. Instead, with the full knowledge, cooperation and approval of the District, AmeriHealth Mercy used the bid that Chartered had already prepared prior to the phony rehabilitation to win the DHCF Contract, and in a sham bidding process, AmeriHealth Mercy became the owner of Chartered’s assets, paying no consideration for them. The first stage of the Defendant’s scheme was complete. Chartered was out of business. DCHSI’s sole source of revenue – as the parent of Chartered – was extinguished.

The District was now in a position to effectuate the second stage of their scheme – the unilateral, gross reduction in the amount of debt owed by the District to Chartered. As **both** the rehabilitator of Chartered **and** the principle debtor to Chartered, the District now **controlled both sides of the negotiation of the debt** owed to Chartered. Because of the phony rehabilitation, the District was able to negotiate with itself, thereby paving the way for a huge, unilateral reduction of Chartered’s asserted claims against the District and the suppression of valid, still-to-be asserted claims, that had Chartered remained an independent entity would have and should have been fully and vigorously pursued and collected from the District.

Instead, in a truly Kafka-esque scenario, because the District stands as both principle debtor and controls the Rehabilitation estate as creditor, no legitimate effort has been made by the District to collect the largely undisputed debt from itself. Instead, the debt has been unilaterally forgiven in the guise of a “settlement agreement” the District negotiated with itself and the anticipated resulting shortfall to the Estate is being sought in a lawsuit against the residuary beneficiary, DCHSI, and its sole shareholder, Thompson. And all of this received the blessing of the Superior Court without so much as a hint of investigation or review of the compelling facts presented in opposition to the District’s scheme.

III. STATEMENT OF THE CASE

On July 23, 2013, the Rehabilitator filed a *Notice of Filing of Settlement Agreement between D.C. Chartered Health Plan, Inc. and the District of Columbia*, and attached “for the convenience of the court” a copy of the District Settlement Agreement, which was fully endorsed the previous day. SA-21-38. Two days later, on July 25, 2013, the Rehabilitator filed a “consent” motion and a supporting memorandum, requesting the court (i) to set a briefing schedule for any opposition to the Settlement Agreement, as well the Rehabilitator’s reply, (ii) to

schedule an expedited hearing on the deadlines for the briefing schedule, (iii) to conduct an evidentiary hearing on any opposition to the Settlement Agreement at the previously scheduled status conference of August 21, 2013, and (iv) “at or before the hearing on August 21, to enter an order approving, and authorizing the Rehabilitator to consummate the Settlement, **thereby allowing Chartered to liquidate its primary asset** and pay priority provider claims under the Plan of Reorganization.”² SA-39-40 (emphasis added).

The following day, July 26, 2013, DCHSI informed the court that it had not consented to the Rehabilitator’s *Consent Motion* or “to the proposed effort to insulate the proposed settlement from adequate review by precluding discovery.” SA-78. DCHSI requested “a reasonable period for discovery,” and status conference in mid-November 2013 after discovery to determine “the final steps to an evidentiary hearing on the merits” of the Rehabilitator’s settlement with the District of Columbia. SA-81. On July 31, 2013, the Rehabilitator filed a reply, reiterating its initial request – as enumerated above for briefs and oral argument on August 21, 2013 – and arguing further that there should be no delay in the court’s approving the settlement. SA-88.

On Friday, August 9, 2013, DCHSI filed its *Memorandum in Opposition to Motion to Approve Settlement Agreement*, which included among other things, an expert declaration from Drew Joyce (Ex. 1), Rector’s Report dated November 8, 2012 (“Rector’s Report”) (Ex. 2), Letter dated April 11, 2013 to Rehabilitator from DCHSI Counsel (Ex. 3), D.C. Department of Health Care Finance Memorandum dated April 4, 2011 (“Turnage Letter”) (Ex. 4), and discovery requests dated August 8, 2013 (Ex. 5).³ SA-96-198. After DCHSI filed its *Memorandum in Opposition*, the Rehabilitator provided DCHSI with a 50 plus page actuarial report from Towers Watson, an actuarial firm, which the Rehabilitator had received back in June 2013. SA-233-291.

² “Plan of Reorganization” is at pages 7-9 of the Second Status Report. 1-AA-61-63.

³ 10 Interrogatories and 13 Requests for Production focused on the Settlement. SA-186-98.

Two days later, on Friday, August 16, 2013, DCHSI provided to the Court an immediate *Supplement* to its *Memorandum in Opposition*, which included the Towers Watson Report (Ex. A) and a Summary of Statutory Equity prepared by Drew Joyce dated August 15, 2013 (Ex. B). SA-220-308. On this same day, the Rehabilitator filed a *Motion for Leave to File a Reply* together with a Reply brief. SA-199-205.

On Wednesday, August 21, 2013, the Honorable Melvin Wright informed the parties that he was prepared to rule, but would “give each party an opportunity to say something before [he] rule[d].” SA-310:25-311:2. The court informed the parties that he was “not going to be listening to any evidence” (SA-314:16-17), that he would not read or consider the Towers Watson Report – a document obtained by the Rehabilitator – because DCHSI did not have standing, (SA-315:20-21), that there was no need for an expedited hearing “to determine what people think about the settlement” (SA-316:7-9), and that discovery “would be useless” (SA-318:13-15). Instead, Judge Wright approved the Settlement Agreement, and it is that order that DCHSI appeals. Judge Wright also granted the Rehabilitator’s motion to file the reply, which was filed on the same day as DCHSI’s *Supplement*. SA-5.

IV. STATEMENT OF FACTS RELATED TO THE DISTRICT SETTLEMENT

Eleven years after DCHSI purchased Chartered, DISB and DHCF increased their financial oversight of Chartered due to expressed concerns over the adequacy of Chartered’s risk-based capital reserves. As reflected in Chartered’s audited financial statements, Chartered had the following total stockholder’s equity in the years from 2004 and 2011:⁴ (i) 2004: \$11,843,556; (ii) 2005: \$15,945,518; (iii) 2006: \$20,717,538; (iv) 2007: \$21,312,995; (v) 2008: \$21,059,187; (vi) 2009: \$13,656,951; (vii) 2010: \$17,444,611; and (vii) **2011: \$ 5,949,445.** See

⁴ The 2011 financial report, finalized under the Rehabilitator’s supervision, changed the terminology from “stockholder’s equity” to “total capital and surplus.”

2-AA-393 n.3, 412-13 n.3, 430 n.3, 454 n.8; 1-AA-34. The significant decrease in 2011, which led to the appointment of the Rehabilitator, the subsequent abandonment of Chartered's business, and the current liquidation of Chartered, was the result of District imposed false rate setting and non-payment of debts owed to Chartered and by multiple instances of misrepresentations by the District.⁵

A. Prior to Rehabilitation, the District imposed actuarially unsound rates and underpaid Chartered on the DHCF Contract.

Under the DHCF Contract, the District was required to pay Chartered at rates that were actuarially sound. See DCHC-2007-R-5050 Solicitation, Contract and Award ("DHCF Contract") at Section B.3.⁶ Under the DHCF Contract, there are at least two circumstances where the District can become obligated to pay additional compensation beyond the original contract sum. First, notwithstanding the requirement that an actuary certify the rates as sound (*see* DHCF Contract, § L.3.2.2.3), if the rates prove to have been unsound, then Chartered is entitled to recover from the District the amount it would have been paid had the rates been actuarially sound (i.e., the full sound rates plus the 13.5% surcharge, as well as interest). SA-123, ¶ 20. Second, even if the rates are sound when set, if the District subsequently changes or adds requirements to the contract, the District is responsible for a retrospective rating adjustment. See DHCF Contract, § B.3.1. Chartered experienced both circumstances. The District repeatedly

⁵ See 3-AA-589 (noting that "[t]he projections are [] based on the member months for the current DCHFP population and do not consider the additional enrollment related to the coverage expansion up to 133% of the federal poverty level (FPL)"); 3-AA-615 (Mercer's DCHFP Data Book for Rates Effective May 1, 2012) (noting that "childless adults were added to the coverage expansion effective July 2010 for individuals up to 133% the federal poverty level" and those with "incomes between 134% and 200% of the FPL [] were enrolled in the MCOs effective December 2010").

⁶ The DHCF Contract is available in its entirety at http://app.ocp.dc.gov/RUI/information/scf/solicitation_detail.asp?solicitation=DCHC-2007-R-5050. It is 424 pages long.

failed to adequately account for underpayments due to unsound rates and ignored Chartered's repeated communications regarding the adverse experience with changed or additional covered populations (e.g., the 774 and 775 populations, discussed below). SA-233, 243, 268.

B. The Towers Watson Report -- which Judge Wright would not consider before approving the Settlement -- revealed the District's Scheme on Unsound Rate Setting.

On or about June 11, 2013, Towers Watson Pennsylvania, Inc. provided an actuarial opinion to the Rehabilitator ("Towers Watson Report"). The Towers Watson Report examines *only one* of numerous categories of the District's underpayments to Chartered and breaches of contract, and concludes that, *as to that one category alone relating to only twenty-two months out of a five-year contract*, the District owes Chartered over \$51.4 million. SA-240-45. The Towers Watson Report also shows that the District and its retained rate-setting actuary, Mercer, ignored significant information repeatedly provided by Chartered, as well as information in DHCF's possession, and engaged in a pattern of actuarially unsound and inadequate rate setting that caused the capital depletion that drove Chartered into rehabilitation. SA-264-67.

As to the single category of underpayment examined in the Towers Watson Report – addressing the same subject and time period at issue in the Retrospective Claim the Rehabilitator filed on February 22, 2013 for \$51.2 million against the District (which claim Towers Watson has valued higher, at \$51.45 million) – the Towers Watson Report examined the adequacy of the rates the District paid to Chartered by “construct[ing] a summary of revenue and benefits incurred by population and calendar month for the period of August 1, 2010 to April 30, 2012 ('Observation Period') using data files that were provided to [Towers Watson] by Chartered.” SA-238.

The analysis started after the District transferred the 774 Population to Medicaid, and examines the actuarial soundness of the District's rates for the 774 Population, the 775

Population, and the pre-existing Medicaid population (termed the Legacy Population). SA-242. Based on this analysis, and informed by the governing federal regulations as well as CMS and actuarial guidance (SA-238-39), Towers Watson made a number of important conclusions about the unsound rates set by DHCF:

1. Chartered's losses began to emerge in early 2011 and accumulated to \$51.5 million during the Observation Period.⁷
2. Capitation rates in place during the Observation Period for the 774 and 775 Populations were not actuarially sound.
3. Capitation rates in place during the Observation Period for the Legacy Population were not actuarially sound.
4. Key Contract requirements were not met [by the District].
5. Applying actuarially sound capitation rates retroactively would reduce Chartered's losses by \$47.2 million.

See SA-240; 244.

C. Chartered's losses due to unsound rate setting by the District began to emerge in early 2011 and accumulated to \$51.5 million during Towers Watson's Observation Period.

Chartered's losses began to occur in January 2011 for the Legacy and 775 Populations and in May 2011 for the 774 Population. With few exceptions, monthly losses persisted throughout the remainder of Towers Watson's observation period, demonstrating a consistent inadequacy of capitation rates. SA-240. Chartered incurred not less than \$51.5 million in losses from inadequate capitation rates forced on Chartered during Towers Watson's observation period. Id.

Chartered's losses from the inadequate capitation rates that the District imposed for the 774 and 775 populations were 14.8% and 59.4% of revenue respectively during Towers Watson's observation period (i.e., August 2010 to April 2012). The 774 and 775 losses were

⁷ Chartered's losses in fact began to escalate in 2010 due to the transfer of the 774 population and the impact of other actuarially unsound rates.

proportionately greater than the 5.2% loss that arose for the Legacy Population (what Towers Watson defined as Chartered's remaining population). SA-242. The significantly higher costs demonstrate that the District should have established separate capitation rate schedules for these two patient populations, as it is required to do. Id. The District did not because the apparent goal was to regulate Chartered into rehabilitation.⁸

The rate-setting process required the District to make "special population adjustments" when there are changes in the population between the time of the data exposure and the time for which the capitation rates are applicable and when there are anticipated changes in the general health of the population. SA-243. Despite this, the District and Mercer ignored Chartered's concerns about the higher costs for the 774 and 775 populations and did not make these adjustments, thereby creating the financial losses that the District used to take Chartered over by rehabilitation. Id.

D. Capitation rates in place during Towers Watson's Observation Period for the Legacy Population were also not actuarially sound.

The District also imposed rates for the Legacy Population that were not actuarially sound. Id. Of the \$21.7 million of losses that Towers Watson found arising from inadequate capitation rates for the Legacy Population during Towers Watson's observation period, \$17.4 million is attributable to the District imposing rates below target rates. Id. According to Towers Watson, the rates for the Legacy Population were not actuarially sound because:

⁸ Despite applicable federal regulations and standard actuarial practices that required separate capitation rate schedules for these two patient populations, the District and its actuary never suggested separate rates for the 774 population and delayed any suggestions for the 775 Population until 2012. Id. Neither the District nor its actuary attempted to obtain credible experience data for or separately review emerging experience data for the 774 and 775 populations prior to the separate rate for the 775 Population in 2012. Id. The District ignored several efforts by Chartered to demonstrate its emerging experience with these two patient populations. Id.

1. There was no negotiation bid process as capitation rates were imposed by the District;
2. The high degree of uncertainty of the incoming new 774 and 775 Populations meant that a decreased margin in overall rates presented additional unanticipated risk to Chartered; and
3. Chartered's financial condition as a single-state, mono-line, Medicaid managed care organization reporting adverse experience should have been considered in setting actuarially sound rates.

See SA-244.

E. The District breached its Contract with Chartered prior to the Rehabilitation as Key Contract Requirements between the District and Chartered Regarding Rates and Payments Were Not Met.

Payments to Chartered are required to be actuarially sound in accordance with both federal regulations and the Contract between the District and Chartered (Section G.1.6).⁹ Notwithstanding this, the District imposed capitation rates that were not actuarially sound in breach of its Contract with Chartered. SA-245. The DHCF Contract requires an annual review of the capitation rates that:

Will take into account factors such as inflation, significant changes in the demographic characteristics of the member population, or the disproportionate enrollment selection of [Chartered] by members in certain rate cohorts.

SA-245; see also DHCF Contract, Section B.3.2

The influx of the 774 and 775 Populations represented both a significant change in the demographic characteristics and disproportionate enrollment which were not adequately taken into account by the District and Mercer in setting rates during Towers Watson's observation period. SA-245. The DHCF Contract required an equitable adjustment where contract changes result in increased costs:

⁹ See Footnote 6, *supra*.

Contracting Officer may ... make changes in the contract within the general scope hereof. If such a change causes an increase or decrease in the cost of performance of this contract, or in the time required for performance, an equitable adjustment shall be made.

SA-245; see also DHCF Contract, Section 15 of Amendment J.5.

The 774 and 775 Populations caused a significant increase in the cost of performance. SA-245. Despite its clear contractual obligation to Chartered, the District did not make an equitable adjustment.

F. Applying actuarially sound capitation rates retroactively would have reduced Chartered's losses by \$47.2 million and obviated any pretext for Rehabilitation.

Applying actuarially sound rates retroactively would have reduced Chartered's losses. SA-245. If the District had selected the "target level" recommended by Mercer, whose rates were the product of an improper analysis and the exclusion of important data, virtually the entire "loss" experienced by Chartered (upon which the District relied to seek rehabilitation of Chartered) would have disappeared. SA-240, 245. Applying the target level recommended by Mercer for the Legacy Population would have eliminated \$17.4 million of the losses. SA-245. Calculating and applying actuarially sound rates for the 774 and 775 Populations would have eliminated \$29.8 million of the losses. In other words, based on the Towers Watson Report and focusing on Towers Watson's observation period alone, the District wrongly imposed not less than \$47 million in losses immediately before it sought to take Chartered over in rehabilitation.

G. The District's intentionally set actuarially unsound rates in seven other categories and owes additional money to Chartered – the Joyce Declaration.

Based on the Towers Watson Report and Chartered's financial statements, DCHSI's expert, Drew Joyce, prepared an analysis for the Superior Court judge showing that, even without information sufficient to calculate all categories of the District's underpayments, Chartered was entitled to retrospective rate adjustments *exceeding \$82 million*. SA-293. In

addition to the single underpayment category that Towers Watson calculated, the District also underpaid Chartered in *seven other significant categories*:

1. The District set actuarially unsound rates under the Alliance program from July 2010 through July 2011. For this “Alliance Claim,” the District owes Chartered an additional \$9,086,929 (plus interest). SA-103, 293.

2. The District set actuarially unsound rates for certain dental benefits that DHCF imposed on Chartered, but for which the District did not pay from January 2011 through November 2012. For this “Dental Crown Claim” the District owes Chartered an additional \$2.2 million (plus interest). Id.

3. The District set actuarially unsound rates for the Alliance program for the period August 2011 through December 2011 (subsequent to the period addressed in the Alliance Claim). The Towers Watson Report does not address such underpayments. See SA-236-37. The Alliance program in particular requires comprehensive retrospective adjustments because, as described in the Towers Watson Report, Director Turnage of the DHCF admitted in an April 4, 2011 letter to the Mayor that Mr. Turnage’s predecessor [i.e., Julie Hudman] had directed Mercer, the District’s rate-setting actuary, “to set the MCO [Managed Care Organization, e.g., Chartered] rates for the Alliance **below** the lowest level considered actuarially sound.” See SA-266. Mr. Turnage further admitted that the goal was to use Medicaid funds (70% of which are paid by the federal government) “to offset predicted Alliance losses,” but that this did not work and Chartered consequently was injured in two ways. Id. First, because “members with higher health care costs” were transferred into the Medicaid program, “the expected margins on the Medicaid side have not materialized.”¹⁰ Second, “[Chartered] experienced substantial losses on their Alliance business.” Id. The District took no action to correct these issues.

4. The District set actuarially unsound rates, not otherwise claimed, for the year ended December 31, 2012, both in the Alliance program (the full calendar year) and the Medicaid program (May 2012 through year end). The Towers Watson Report does not address such underpayments and the Rehabilitator has not asserted any right to recover them (but releases them in the Settlement). See SA-236-37. DCHSI does not possess the information necessary to calculate these amounts with precision, but notes that both the Rehabilitator and Towers Watson have stated that the District undoubtedly improperly set these rates too low. See SA-269-70; SA-26, Recital K. As an estimate of the District’s underpayments in

¹⁰ These margins failed to materialize, of course, due to the increased costs imposed due to the 774 and 775 Populations, and because the District set unsound rates.

this category, DCHSI's expert assumed a 4% underpayment rate, conservative when compared to the 8.2% underpayment rate for the prior period.¹¹

5. The District set actuarially unsound rates for January 1, 2013 until the end of the contract period, April 30, 2013, for both the Alliance program and the Medicaid program. The Towers Watson Report does not address such underpayments and the Rehabilitator has not asserted any right to recover them (but releases them in the Settlement). See SA-236-37. Both the Rehabilitator and Towers Watson also have stated that rates undoubtedly were too low in this period (see SA-269-70; SA-26, Recital K, and DCHSI's expert again applied a conservative 4% underpayment assumption for his calculations).

6. The District set actuarially unsound rates prior to the period addressed in the Rehabilitator's asserted Alliance Claim, i.e., from May 1, 2008 through June 2010 ("Early Alliance Retrospective Period"). The Rehabilitator has not asserted any right to recover these amounts (but released them in settlement). See SA-236-37.

7. The District set actuarially unsound rates for the Medicaid program prior to the period addressed in the Retrospective Claim and the Towers Watson Report, i.e., from May 1, 2008 through July 31, 2010 ("Early Medicaid Retrospective Period"). The Towers Watson Report does not address such underpayments and the Rehabilitator has not asserted any right to recover them (but releases them in the Settlement). See SA-236-37. DCHSI's expert was unable to estimate any value for these claims, but would do so if the Rehabilitator makes the necessary information available.

The court refused to consider or account for the Joyce Declaration or to hear any evidence with regard to the data supplied notwithstanding its direct relevance to the issue of the fairness of the proposed District Settlement in light of the Towers Watson Report.

H. The District also underpaid administrative expenses, thereby contributing still more losses pre-Rehabilitation.

Even beyond these medical expense related payment deficiencies, it appears that the District underpaid Chartered's administrative expenses, further contributing to Chartered's District-engineered losses prior to taking over Chartered. Before the District implemented the

¹¹ The underpayment percentage was calculated by dividing Tower Watson's figure for the shortfall from an actuarially sound "target" payment (\$47.2 million) by the total premium for the period (\$574.8 million).

2% premium tax, it had determined that the actuarially sound non-medical rate load was 13.5%, composed of 11.5% for administration and 2% for profit. During 2010, the District began to impose a 2% premium tax, which necessarily affected what would constitute an actuarially sound non-medical rate. As the Towers Watson Report makes clear, rates are actuarially sound only if the “projected premiums ... provide for all reasonable, appropriate and attainable costs, including ... any state-mandated assessments and taxes.” SA-260 (quoting *Actuarial Certification of Rates for Medicaid Managed Care Programs*) (emphasis added).

After the imposition of the premium tax, however, the District did not adjust Chartered’s non-medical rate load (and at the same time imposed a host of new, costly administrative burdens on Chartered and the other MCOs). Thus, the District’s view of actuarially sound administrative rates was based on an aberrant, obviously self-serving formula: $11.5\% + 2\% = 11.5\%$.

I. Without the District’s Intentional Underpayments, Chartered was Solvent and Not Subject to Rehabilitation.

DCHSI’s expert, Drew Joyce, using the best data available – without the benefit of discovery – estimated how most of these categories of underpayment would impact Chartered’s financial statements as of year ends 2011 and 2012, and as of March 31, 2013, assuming the District had honored its obligation to pay retrospectively adjusted rates with respect to some but not all of the underpayment categories set forth above. SA-293. Mr. Joyce relied upon the newly-produced Towers Watson Report and Chartered’s financial statements.

In an attempt to estimate the value of underpayments for Alliance after July 2011 and for Medicaid after April 2012, Mr. Joyce first calculated that the District fell short of paying actuarially sound rates by 8.2% during the Observation Period (i.e., July 2010 through April 30, 2013). See Footnote 11, *supra*. For sake of analysis, Mr. Joyce used a conservative factor (4%)

to estimate the extent to which the District fell short of paying actuarially sound rates to Chartered during the *post*-Observation period as to Medicaid, and for periods after July 2011 (when the Rehabilitator's Alliance Claim cuts off) as to Alliance.

Although the extent of the District's intentional underpayments to Chartered cannot be estimated with complete precision, Mr. Joyce concluded that Chartered's total adjusted capital and surplus as of December 31, 2012 should have been \$37.2 million, an amount that would have precluded Chartered's rehabilitation. SA-293. Mr. Joyce further concluded that Chartered's total adjusted capital and surplus as of March 31, 2013 should have been \$22.3 million.¹² *Id.* In short, the Towers Watson Report articulates an analysis of the District's misconduct that, when extrapolated to fewer than all categories of underpayment examined (as Mr. Joyce was constrained to do), demonstrates that Chartered was solvent and not a proper subject of rehabilitation.

J. DISB Determined that the District Owed Chartered for the Increased Pharmacy Costs and More.

On November 30, 2011, Chartered filed a pre-rehabilitation claim with the District to recover \$25.8 million for pharmacy-related losses incurred due to the 774/775 Population transfer ("Pharmacy Claim").¹³ As of June 30, 2012, Chartered booked the Pharmacy Claim as a

¹² The estimated capital as of March 31, 2013 (again, a partial estimate because some losses cannot yet be calculated) reflects an approximately \$12 million reduction of assets due to Cardinal Bank having taken possession of certain collateral during the first quarter of 2013. Of course, that collateral was taken because of an event of default – Chartered's liquidation – that would not have occurred but for the District's misconduct in breach of the DHCF Contract.

¹³ That claim proceeded substantially through the administrative process. Chartered won a motion in December 2012 compelling DHCF Director Turnage to testify, and with discovery set to close on April 12, 2013, Chartered was building substantial leverage over DHCF. *See DCHSI Memorandum in Support of Motion to Compel Rehabilitator to Pursue Chartered Claim* (April 2, 2013) at 2. Upon the commencement of the rehabilitation, the Rehabilitator, although acknowledging that depositions were important to Chartered's claim, took no depositions and

premium receivable based on its conclusion that the DHCF Contract was retrospectively rated, meaning that Chartered was entitled to recover retrospective premiums if DHCF imposed additional contract requirements not accounted for in the existing rates. DISB hired an outside insurance regulatory consulting firm, Rector & Associates, Inc. (“Rector”), to conduct a Limited Scope Financial Examination to determine the appropriateness of Chartered’s accounting.

On November 27, 2012, DISB Commissioner White entered an administrative Order officially adopting the Rector’s Report and entering it as a final administrative decision. SA-295-308 (Order and attached Report). In the report, Rector concluded that Section B.3.1 of the contract “require[s] that if the Contract is changed to add, delete or change services covered by DC Chartered, the DHCF must review the effect of the change and equitably adjust the capitation rate,” SA-303 (emphasis added), and as such, the DHCF Contract is retrospectively rated. Chartered thus was entitled to “receive premium adjustments based on [its] loss experience relating to the Contract,” and the adjustment “should take into account its *entire* loss experience to determine its final policy premium, not just the loss experience resulting from the transfer of the 774 and 775 populations from the Alliance Program to the [Medicaid] Program.” SA-301 (original emphasis), 306. In short, the transfer of members from Alliance to Medicaid was a “change [that] created a liability for DHCF and an asset (premium receivable) for DC Chartered.” SA-304.

In addition to a retrospective premium payment, Rector also concluded that the District was required to adjust Chartered’s capitation rates prospectively to account for Chartered’s loss experience following the transfer of the 774/775 Populations. The DHCF Contract requires “that any changes to the capitation rate be actuarially sound,” defined in accordance with federal

surprisingly withdrew the Pharmacy Claim. See Consent Motion to Stay All Proceedings (March 18, 2012) at 1. The District thus far has avoided all depositions.

standards. SA-305 (rates must be set in accordance with generally accepted actuarial principles and practices, be appropriate given the populations to be covered and services to be provided, and be certified by a qualified actuary). If DHCF failed “to perform the required annual review,” or its review “failed to establish actuarially sound rates,” then any “deficiency in the capitated rates would be a liability for the DHCF and an asset (premium receivable) for DC Chartered.” SA-305-06.

Because the DISB Commissioner adopted the Rector’s Report and made it an official administrative ruling. As such, it is settled that the DHCF Contract is retrospectively rated, that the transfer of the 774/775 Populations from Alliance to Medicaid constituted a change triggering the right to retrospective compensation accounting for Chartered’s “entire loss experience” and to an actuarially sound rate adjustment prospectively. The District, however, has never paid the retrospective premium adjustment, and its prospective rate adjustment was inadequate.

K. The Settlement of the District’s Debt by the District.

On July 22, 2013, after wrongfully withholding tens of millions of dollars it was contractually obligated to pay to Chartered and after causing the very capital depletion that permitted it to compel Chartered’s rehabilitation, the District, through the DISB commissioner as Rehabilitator, negotiated a settlement of the amount it owed to Chartered with the DHCF director – both political appointees serving at the pleasure of the Mayor.¹⁴ The Settlement Agreement was negotiated among, and signed only by, representatives of the District. SA-70-71.

¹⁴ DISB, under the supervision of its Commissioner, is a cabinet level agency of the District government pursuant to D.C. Code § 31-102. The Commissioner of DISB is appointed by the Mayor, with the advice and consent of the D.C. Council (see D.C. Code § 31-104). DISB’s and specifically, the Commissioner’s, decisions represent the official policy of the District of Columbia. By law, the Commissioner is the Rehabilitator of Chartered.

The Settlement Agreement—purporting to somehow be “at arm’s length” – released all of Chartered’s claims, asserted and unasserted, arising from the Medicaid and Alliance programs (“Released Claims”), which claims constituted “Chartered’s most significant asset”, while at the same time reserving the District’s claims to be asserted against Chartered, DCHSI, and Thompson. SA-44; SA-31-32 ¶¶ 8-9. The Settlement Agreement resolved all Released Claims for \$48 million, to be distributed in two parts. First, \$18 million (Part I) would be paid to Chartered upon Court approval and approval by CMS (the Rehabilitator did not disclose the likelihood or expected timing of CMS’s approval). This \$18 million would be distributed “in accordance with the Plan of Reorganization to providers with undisputed Class 3 claims allowed by the Rehabilitator.” SA-47. Second, the remaining \$30 million (Part II) would bypass Chartered altogether, and instead would be paid either (1) directly to Chartered’s providers with undisputed, allowed Class 3 claims or (2) if the Fiscal Year 2013 District Litigation Fund otherwise first would lapse, to an unnamed third-party selected by the District, which would hold the funds and pay them to providers, presumably charging an undisclosed fee out of the settlement fund. Id.

The District’s insistence on using the litigation fund is for a transparent purpose. By using the litigation fund, there was no need for D.C. Council approval. See D.C. Code § 47-355.02 (“D.C. Anti-Deficiency Act” prohibiting District agencies from making unauthorized expenditures). If Council approval were required, DHCF or the Mayor would have had to explain

DHCF is a separate, cabinet level agency and is headed by a director who is appointed by the Mayor, with the advice and consent of the D.C. Council, and who serves at the pleasure of the Mayor. See D.C. Code § 7-771.04. The Director is tasked with collaborating with DISB and other District agencies. See D.C. Code § 7-771.05. DHCF’s and specifically, the Director’s, decisions represent the official policy of the District of Columbia.

that Chartered provided services and was entitled to payment, but that the District had intentionally **underpaid** Chartered for years and thereby drove it into rehabilitation.

Beyond that, for at least those claims based on retrospective rating adjustments, the amount of the District's liability to Chartered is not some theoretical amount that may only be subject to some reasonable estimate. . Rather, **the District's debt is objectively calculable as a matter of straightforward arithmetic**, based on Chartered's known and finally determined obligation to pay providers. SA-123, 125 (¶¶ 20, 28). **As such, there was no justification for any discount**, let alone the significant give-away the District negotiated with itself, from the known amount of the District's debt (without even accounting for the failure to recover the District's other debts to Chartered). There was no defense to payment, particularly as to all retrospective rating claims. SA-125 (¶¶ 25-26) (observing that the District has already held, by administrative order, that the DHCF Contract is retrospectively rated, that the transfer of the 774/775 Populations triggered a retrospective rating event, and that as a consequence, Chartered is entitled to a recovery that "take[s] into account its *entire* loss experience"); SA-295, 301.

The Rehabilitator conceded that the claims he had asserted at the time of the District Settlement were not comprehensive of the District's debts to Chartered. SA-48-49; SA-26, Recital K. Yet the Rehabilitator provided no information to assess the nature or value of the unasserted claims. SA-45-46 (merely asserting that potential claims were "considered" and that Chartered was "investigating" them).

The Rehabilitator has all of the data required to permit calculation of the debt to Chartered to a mathematical certainty. This information was not shared with either the court of the parties. DCHSI has estimated that as a matter of objective, mathematical certainty the District owes Chartered at least **\$50 million beyond** the \$48 million settlement payment. SA-

123, ¶¶ 19-20, SA-126, ¶ 28, SA-128 ¶ 40 ¶ 44. Because the claims are based on retrospective rating and services already rendered, there simply is no defense to any of them given the District's determination that the DHCF Contract is retrospectively rated and the right to payment had been triggered. SA-125, ¶¶ 25-26. The currently asserted claims by the Rehabilitator, including interest, only totaled approximately \$64 million – with no value for as-yet unasserted claims. The Rehabilitator provided no basis for that apparently partial calculation of the total claims, omitting as-yet unasserted retrospective rating claims as well as other unasserted claims. Under the Rehabilitator's calculation, Chartered was effectively given *no* value in the District Settlement. By contrast, from the Towers Watson Report and Chartered's audited financial statements, the District forgave itself no less than \$16 million of its asserted obligations under the DHCF Contract to Chartered and at least \$30 million in unasserted claims.

There is no way to determine if the Superior Court, exercising supervisory authority over this Rehabilitation, considered, or even understood, any of this. To the contrary, the court went out of its way to stake out a position that it was not going to even consider the gravamen of these facts in a process that evidenced no discernible, substantive review of a blatant, one-sided “settlement” between related parties arising out of a Rehabilitation tainted from the outset by misconduct by the same parties now benefitting from this “settlement.”

V. STANDARD OF REVIEW

This Court reviews the issue of standing *de novo*. See e.g., Richman Towers Tenants' Ass'n v. Richman Towers LLC, 17 A.3d 590, 597 (D.C. 2011). Regarding the District Settlement, Appellant DCHSI must show that the Court abused its discretion, which “requires a showing of either that the agreement in question was so manifestly unfair as to preclude judicial approval, or that the court did not have sufficient facts before it to make an informed judgment.”

Weil v. Markowitz, 829 F.2d 166, 171-172 (D.C. Cir. 1987) citing Patterson v. Stovall, 528 F.2d 108, 114 (7th Cir. 1976) (requirement in judging appropriateness of settlement is whether trial court had sufficient facts before it to make informed judgment); Glicker v. Bradford, 35 F.R.D. 144, 151 (S.D.N.Y. 1964) (question raised as to whether settlement, taken as a whole, was so facially unfair as to preclude judicial approval); Boyle v. Giral, 820 A.2d 561, 566-567 (D.C. 2003) citing Shepherd Park, *infra*.

VI. ARGUMENT

A. DCHSI had standing as creditor/claimant and sole shareholder of Chartered to object to the District Settlement and has standing to maintain this appeal of the order approving the District Settlement.

1. The Standing Issue as framed by the Lower Court at the August 21 hearing.

In approving the District Settlement, the court would not consider the Towers Watson Report – the actuarial report obtained by the Rehabilitator, *not* DCHSI, – because according to the court DCHSI did not have standing to bring evidence to the court’s attention. With regard to the Towers Watson Report, the court was unfazed by the Rehabilitator’s two month nondisclosure of the critical actuarial report and instead raised for the first time at the final hearing whether DCHSI had any standing to participate in the rehabilitation as a party in interest.

The court’s statements concerning standing at the August 21, 2013 hearing form such a confused and contradictory whole that it is difficult to pronounce what the court’s actual ruling on standing is – especially in light of the court’s implied consideration of DCHSI’s initial *Memorandum in Opposition* and invitation for argument from DCHSI at the opening of the hearing:

- * I have read all of the submissions (SA-310:24-25)
- * I’ll give each party an opportunity to say something before I rule (SA-310:25 - SA-311:2)

- * I do not intend to look at [the Towers Watson Report] because you do not have standing. (SA-315:20-21)
- * [DCHSI] really doesn't have standing. (SA-316:12)
- * [T]he court permitted you to be in here because you assisted the court in deciding whether or not they were acting in an appropriate manner. (SA-317:21-23)
- * The objections by [DCHSI] who is not a party has (sic) been considered by the court and the court will rule that they are not a party to this case and really didn't have a right to be permitted to do what they have done. The court has permitted them to do that. Because had they filed a motion to intervene, the court probably would have grant (sic) it, but it did serve a purpose to have the court examine the record. (SA-318:20 - 319:2)
- * Well, I don't need to hear your argument on standing because that's one you're going to raise with the Court of Appeals. (SA-324:17-19)
- * So, if there wasn't an issue of standing before, you wouldn't have been able to participate. What – what would you have done, if the court had granted you – granted your motion that you haven't done now? (SA-328:23 - 329:2)
- * [H]ad you been a party, I would have overruled your objection anyway. (SA-329:8-10)
- * It may be moot because even if the Court of Appeals find (sic) that you have standing, I find my – my finding still appear (sic) because I've considered all the things you would have raised, had you been granted standing. (SA-329:13-17)
- * [H]ad standing been granted, the court would have approved the settlement anyway over your objection. (SA-330:5-8)

In the main, the court seems to have said that DCHSI did not have *de juris* standing to participate at any time in the rehabilitation proceeding, much less to object to the settlement agreement with the District of Columbia, but the court nevertheless accorded DCHSI *de facto* standing to participate in any event.

What makes the court's statements so stunning is DCHSI's active and vigorous participation in the rehabilitation proceeding as a party in interest (as both sole shareholder and creditor-lessor) after noticing an appearance in January 2013, without any mention that DCHSI

as simply being permitted to participate as some sort of *ad hoc* legal assistant to the court, not as a *bona fide* party in interest.¹⁵

In the eight months since that initial appearance in January, DCHSI filed two motions, filed five oppositions and substantively participated in five hearings, arguments, and status conferences. See SA-5-17. If the court had considered the Towers Watson Report, the Joyce affidavit, the supplemental spreadsheet analyzing the impact of the Report on DCHSI's earlier calculations, allowed some limited discovery or heard evidence as requested, DCHSI would not need to raise the standing issue with this Court of Appeals. See Boyle v. Giral, 820 A.2d 561, 563 (D.C. 2003) ("We conclude that it is unnecessary to resolve the consumer class objectors' intervention arguments, because the objectors filed written statements in opposition to the settlement agreement and were permitted to make oral arguments during the trial court's final hearing to determine the fairness of the agreement. Thus, the denial of intervention has caused them no prejudice").

But the court did not do any of this. Rather, the court excluded the Towers Watson Report and the other material presented by DCHSI from any consideration based on DCHSI's standing. There is no indication that the court considered the detailed evidence proffered by Mr. Joyce with regard to the impact of the Towers Watson Report and the request to make a record with live evidence available at the hearing or to permit some limited discovery to flesh out the obvious and manifest unfairness presented by the settlement outline that had been presented by the Rehabilitator to the court. The absence of any judicial consideration of these issues is manifestly unfair to DCHSI, and indicative of the insufficiency of the facts necessary for an

¹⁵ In contrast to the court's recent take on DCHSI's status, the Rehabilitator designated DCHSI as an "*interested party in this matter*" in the first filing to commence the rehabilitation. 1-AA-3 (¶ 4) (emphasis added).

informed judicial determination as to the fairness of the District Settlement or the entire Rehabilitation proceeding pending before the court. Given the incriminating evidence in the Towers Watson Report, the Turnage Letter, the Joyce Affidavit, etc., DCHSI's standing *vel non* should not have precluded the court's review of that document. A settlement that was fair, adequate, and reasonable to the Chartered estate and its stakeholders mandated its review. However, to the extent at least part of the court's stated rationale for such a dismissive approach to clearly relevant evidence can be found in the court's view of the standing issue, that issue becomes important for review and resolution by this Court.

2. DCHSI had standing to object to the court's approval of the District Settlement.

The court's somewhat muddled ruling on standing at the August 21st hearing is flatly contradicted by the D.C. Code governing the rehabilitation of Chartered. D.C. Code § 31-1305(c) expressly recognizes DCHSI's "right to resist" (as the owner of Chartered) the proceedings within a rehabilitation¹⁶ and any orders that issue out of the rehabilitation of Chartered.¹⁷ That "Chartered consented in the initial filing to the Rehabilitator taking over and acting as a Board of Directors would" does not impede DCHSI's "right to resist" in D.C. Code § 31-1305(c). SA-316:13-15.

¹⁶ D.C. Code § 31-1301(3) defines "delinquency proceeding" to include the rehabilitation or reorganization of an insurer.

¹⁷ This principle of "shareholder" standing in the rehabilitation of an insurer under the D.C. Code is validated by the analogous Chapter 11 reorganization of a business under the U.S. Bankruptcy Code:

A party in interest, including the debtor, the trustee, a creditors' committee, an equity security holders' committee, **a creditor, an equity security holder**, or any indenture trustee, may raise and may appear and be heard on any issue in a case under this chapter.

11 USCS § 1109(b) (emphasis added). See Acord v. Floyd (In re Supplement Spot, LLC), 2009 U.S. Dist. LEXIS 50576, *7, 2009 WL 1684577 (S.D. Tex. June 16, 2009) (sole shareholder standing to object to settlement agreement).

This principle is carried through Chapter 13 of Title 31. DCHSI stands as both a shareholder and a creditor of Chartered. As such, DCHSI is within a protected class under the Code as the sole shareholder, see D.C. Code § 31-1340(8), and as Chartered's lessor, see D.C. Code § 31-1340(6). DCHSI is further recognized as a protected class in the Rehabilitator's plan of reorganization, which was approved by the court, as both general creditor (Class 6) and shareholder (Class 9). See 1-AA-62-63. As a result of this statutory scheme, DCHSI has standing to resist any order approving the District Settlement. See e.g., Warth v. Seldin, 422 U.S. 490, 500 (1975) (Under Article III of the Constitution, "the standing question in such cases is whether the ... statutory provision on which the claim rests properly can be understood as granting persons in the plaintiff's position a right to judicial relief."); Goto v. District of Columbia Board of Zoning Adjustment, 423 A.2d 917, 930 (D.C. 1980) ("One test is the person's "'direct', 'immediate', 'pecuniary' and 'substantial' interest in the subject matter of the litigation").¹⁸ Compare Advantage Healthplan, Inc. v. Potter, 391 B.R. 521, 540 (D.D.C. 2008) (the standing requirement in bankruptcy appeals is more restrictive than the 'case or controversy' standing requirement of Article III – limited to "'persons aggrieved,' i.e., to those 'whose rights or interests are 'directly and adversely affected pecuniarily' by the order or decree of the bankruptcy court.'")

Whether analyzed under Article III or the analogous bankruptcy setting, DCHSI as both creditor and sole shareholder has a personal stake in the court's approval of the District Settlement, which has financially harmed DCHSI in both capacities "as to warrant [its] invocation of ... jurisdiction and to justify exercise of the court's remedial powers on [its]

¹⁸ W.H. v. D.W., 2013 D.C. App. LEXIS 687, **21-23, 2013 WL 5745933 (D.C. Oct. 24, 2013) ("Even though we are an Article I court under the Constitution, 'our cases consistently have followed the constitutional minimum of standing' required by Article III").

behalf.” W.H. v. D.W., 2013 D.C. App. LEXIS 687, **21-23 (D.C. Oct. 24, 2013) quoting Warth, 422 U.S. at 498-99. To wit, the District Settlement walked away from tens of millions of dollars of precisely definable obligations to Chartered – for which the District had no defense – effectively extinguishing DCHSI’s claims as Chartered’s landlord and insuring that the residual interest of Chartered to which DCHSI is entitled after the rehabilitation is worthless.

If the “gist of the question of standing” is whether DCHSI has “such a personal stake in the outcome of the controversy as to assure that concrete adverseness which sharpens the presentation of issues upon which the court so largely depends for illumination of difficult [] questions,” then DCHSI has met that standard. See Baker v. Carr, 369 U.S. 186, 204 (1962). The court certainly appeared to recognize as much on August 21st: “[T]he court permitted you to be in here because you assisted the court in deciding whether or not they were acting in an appropriate manner.” SA-317:21-23.

3. *Treated as a party throughout the Rehabilitation, DCHSI has standing to maintain this appeal.*

The general rule that one must have been a party to the trial court proceeding in order to appeal the trial court’s ruling is subject to a number of well-recognized exceptions – one of which is applicable here: “appeals by those who participated as if parties are frequently entertained despite a failure to achieve formal status as a party.” In re Orshansky, 804 A.2d 1077, 1090 (D.C. 2002) citing 15A Wright, Miller & Cooper, Federal Practice and Procedure: Jurisdiction and Related Matters § 3902.1 (2d ed. 1992). “Most of these appeals involve persons who participate in trial court proceedings as if they had intervened, and who seem to have been treated on all sides as de facto parties.” Id. citing SEC v. Forex Asset Mgmt. LLC, 242 F.3d 325, 329-330 (5th Cir. 2001) (applying a three-part test to decide whether a non-party may appeal, and inquiring whether (1) the non-party actually participated in the proceedings, (2) the equities

weigh in favor of hearing the appeal, and (3) the non-party has a personal stake in the outcome) and Devlin v. Scardelletti, 536 U.S. 1, 122 S. Ct. 2005, 2013 (2002) (holding that nonnamed class members who are bound by class action settlement to which they objected at the fairness hearing may appeal the approval of the settlement even though they did not intervene and become named parties).

Until the court backtracked for the first time at the August 21st hearing, DCHSI held the status as a party in interest. If DCHSI was not formally a party, it “was a party by any other measure.” In re Orshansky, 804 A.2d at 1090. DCHSI “made motions and arguments, presented evidence ... all without objection. The court directed its orders at [DCHSI] by name and informed [DCHSI] that it could appeal.”¹⁹ Id.; SA-324:17-19. By virtue of DCHSI’s status as a creditor and sole shareholder of Chartered, not to mention being subject to the court’s orders, including the approval of the District Settlement, which has devastated the value of Chartered to the prejudice of its creditors and its sole shareholder, DCHSI “has a personal stake in the outcome of the proceeding.” Id. citing In re Phy. W., 722 A.2d 1263, 1264 (D.C. 1998) (holding that foster parent has standing as a “party aggrieved” to appeal from order granting natural parent’s motion for reunification). Given that personal stake, the court’s treatment of DCHSI as a party, and the lack of any unfair prejudice in treating DCHSI as a party for purposes of appeal,²⁰ DCHSI has standing to maintain this appeal. Id.

B. The District Settlement is so manifestly unfair as to preclude judicial approval and its approval by the court was the result of insufficient facts necessary to make an informed judgment.

1. The standard of review that the court employed was in error and the court’s approval of the District Settlement was therefore manifestly unfair.

¹⁹ SA-324:17-19; SA-329:13-17.

²⁰ The Rehabilitator designated DCHSI as an “interested party in this matter.” 1-AA-3 (¶ 4).

It is true that the court cited an almost correct judicial standard of review of a settlement agreement:

The court is to determine under the facts and circumstances of each case whether the settlement is fair, adequate, and reasonable and the court is to consider where there's arm-length bargaining, whether there's an opinion offered by experienced counsel²¹ and whether the terms of the settlement – what the terms of the settlement are in relationship to the strength of the litigation at the time of the settlement.

See SA-316:22 – SA-317:12 (citing Shepherd Park Citizens Ass'n v. General Cinema Beverages, Inc., 584 A.2d 20 (D.C. 1990)).²² But the court completely abandoned that judicial standard of review for one not found in the case law,²³ or in the D.C. Code, and one that rises no further than a rubber stamp of the District Settlement and a judicial echo of DISB's and DHCF's duplicitous collaboration:

As I have stated before and which has been cited in the pleadings, the court's role in the rehabilitation process is to supervise the Rehabilitator and to review the actions for abusive indiscretion and not to substitute the court's judgment or the judgment of the parent company, which you are, for that of the Rehabilitator.²⁴

²¹ The case law typically adds “**after meaningful discovery.**” Wal-Mart Stores, Inc. v. Visa U.S.A. Inc., 396 F.3d 96, 116 (2d Cir. N.Y. 2005); United States v. North Carolina, 180 F.3d 574, 581 (4th Cir. 1999) (the “**court should consider the extent of discovery that has taken place ...**”); Williams v. Vukovich, 720 F.2d 909, 923 (6th Cir. 1983) (“**the deference afforded counsel should correspond to the amount of discovery completed and the character of the evidence uncovered.**”). The court permitted no discovery.

²² Shepherd Park included “in this standard ... ‘consideration of . . . [the] extent of investigation, proof problems, strength of defenses, costs of litigation, good faith, possible collusion, the experience of counsel *and extent of opposition to the settlement*’” – considerations that the trial court did not make. Shepherd Park, 584 A.2d at 23 (emphasis added).

²³ See e.g., In re Final Analysis, Inc., 417 B.R. 332, 341 (Bankr. D. Md. 2009) (citing Depoister v. Mary M. Holloway Foundation, 36 F.3d 582, 587 (7th Cir.1994) (bankruptcy settlement) (Court must make a substantive determination to some degree in order to “actually exercise discretion and not simply rubber stamp the Trustee’s proposal.”)

²⁴ Assuming *arguendo* that the trial court was correct, the court could not be accused of supervising the Rehabilitator vis-à-vis the District Settlement. “Supervise” means to “oversee with the powers of direction and decision,” Webster’s Third New International Dictionary, 2296 (1993), or means to “oversee, direct, or manage.” Webster’s New World Dictionary, 1430 (2d ed. 1974). The court provided no direction and no management, and went so far as to prohibit

The court's reference to "As I have stated before" is found in the Order dated May 9, 2013, wherein the Court would not compel (on DCHSI's motion) the Rehabilitator to pursue a claim against the District of Columbia that Chartered had commenced pre-rehabilitation because the court's "role in the rehabilitation process is to supervise the Rehabilitator and review the Rehabilitator's actions for abuses of discretion."²⁵ The court's reference to "and which has been cited in the pleadings" is found in the Rehabilitator's Reply – a citation to a vintage 1968 Washington State, not Washington, DC, opinion. SA-208. Neither reference supports the court's jettisoning the proper elements of a proper judicial review of the District Settlement. See Flinn v. FMC Corp., 528 F.2d 1169, 1173 (4th Cir. 1975) (a court should not blindly accept the terms of a proposed settlement).

In contrast to a proper review, the court unquestioningly accepted settlement terms, *without any discovery*, which were unreasonable on their face and contrary to the best interest of the Chartered estate. St. Paul Fire & Marine Ins. Co. v. Vaughn, 779 F.2d 1003, 1010 (4th Cir. 1985) (in the face of objection, settlement must be in best interest of estate); Wal-Mart Stores, Inc. v. Visa U.S.A. Inc., 396 F.3d 96, 116-117 (2d Cir. N.Y. 2005) (A "presumption of fairness, adequacy, and reasonableness may attach to a class settlement reached *in arm's-length negotiations* between experienced, capable counsel *after meaningful discovery*"). Among many examples set forth more particularly below is the court's inattention to the bifurcated structure of the payment of District Settlement amount. Two thirds of the settlement amount bypassed the Chartered estate to a third party recipient; only 1/3 was paid to Chartered. SA-28. The court did not question that disposition, did not require the third party to be identified or credit worthy, did

any decision other than the Rehabilitator's (i.e., DISB's) by expressly stating he would not substitute his judgment.

²⁵ This turnabout is surprising since the court ordered the Rehabilitator, at the commencement of the Rehabilitation, to seek the court's approval of any settlement. 1-AA-9.

not ask to see the escrow agreement between the District and the third party, did not determine what fee the third party would pay or the reasonableness of the fee arrangement, and did not insure (or seek assurances) that the money would be protected by District guarantee or contract or bond or otherwise.

The source of the 2/3 portion of the payment was apparently the FY2013 Litigation Fund. SA-28. By funding the settlement payment in this way, the District avoided the need for D.C. Council oversight and approval. See D.C. Code § 47-355.02 (“D.C. Anti-Deficiency Act” prohibiting District agencies from making unauthorized expenditures). In other words, the executive branch of the District government cleverly avoided any legislative oversight, which should have impressed upon the court the need for some greater scrutiny as the District sat astride this settlement as both principal debtor and creditor.

To justify the absence of any judicial scrutiny, the court improperly elevated the Rehabilitator to a position he does not hold and clearly misunderstood its own role in the rehabilitation process and specifically in review and approval of the District of Columbia Settlement. First, a rehabilitator is not *summum bonum*, but rather a fiduciary to all who come within the scope of its Rehabilitation, including DCHSI as both a claimant and the equity stakeholder. See e.g., Sovereign Bank v. Schwab, 414 F.3d 450, 454 (3d Cir. Pa. 2005) (citing Warner v. Conn, 347 Pa. 617, 32 A.2d 740, 741 (Pa. 1943) (explaining that a Rehabilitator has the duty “to protect and preserve, for the benefit of the persons ultimately entitled to it, an estate over which the court has found it necessary to extend its care”)); Resolution Trust Corp. v. Moskowitz, 1994 U.S. Dist. LEXIS 20553, **18-19 (D.N.J. Aug. 12, 1994) (a Rehabilitator has a duty to the corporation and its stockholders); 65 Am Jur 2d Rehabilitators § 90 (A Rehabilitator

is often referred to as a fiduciary of all claimants and parties interested in the estate); D.C. Code § 21-1701.²⁶

Second, Chapter 13 of Title 31 of the D.C. Code repudiates the court's inaction in a rehabilitation proceeding. For example, D.C. Code § 31-1312(e) permits the court to approve the plan of reorganization or to disapprove it or to modify the plan and approve it as modified.²⁷ The court cannot presume the plan to be reasonable simply because the rehabilitator proposes it; rather, the court is directed to decide what is "fair and equitable to all parties concerned."²⁸ In re Rehabilitation of Mut. Benefit Life Ins. Co., 1993 N.J. Super. LEXIS 940, *44 (Ch.Div. Aug. 12, 1993) aff'd, 297 NJ Super 179, 687 A2d 1035 (App. Div. 1997), cert. denied, 149 N.J. 408, 694 A.2d 193 (1997) (analyzing the same statute under New Jersey law). Those parties referenced in the statute are the claimants, like DCHSI, **not the regulators** – in this case, the District. Id.

Similarly, the court's approval of the District Settlement – which represents the primary source of funds for the Rehabilitator's plan of reorganization – must be fair and equitable to

²⁶ See also McGivern v. Amasa Lumber Co., 77 Wis. 2d 241, 253, 252 N.W.2d 371, 376 (1977); Phelan v. Middle States Oil Corp., 154 F.2d 978, 991 (2d Cir. 1946); Martin v. Luster, 85 F.2d 833, 843 (7th Cir. 1936); Security Pac. Nat'l. Bank v. Geernaert, 245 Cal. Rptr. 712, 716 (Ct. App. 1988); In re Portex Oil Co., 43 F. Supp. 859, 860 (D. Ore. 1942).

²⁷ Under this statutory scheme, the court must also review accountings from the Rehabilitator no less than semi-annually (D.C. Code § 31-1311); the court shall determine the rights of any parties subject to voidable preferences and liens (D.C. Code § 31-1326(g)); the court shall "approve, disapprove, or modify the report on claims" (D.C. Code § 31-1341(b)); the court shall direct the liquidator to pay distributions in a manner approved by the court (D.C. Code § 31-1342); after proceedings have concluded, the court may grant discharge and make any other orders deemed appropriate – not by the rehabilitator. (D.C. Code § 31-1344(a)).

²⁸ See also, 3-AA-750, ¶¶ 21-22 (The Rehabilitator's "discretion is not absolute by any means ... the court's role [is] critical to both serving a check on the Rehabilitator's powers as well as serving as the venue in which objections to a rehabilitation plan can be heard ... the court's role is substantive, primary and integral to the integrity to the rehabilitation process"). 3-AA-750. Compare Matter of Union Indemnity Insurance Co. of New York, 2009 N.Y. Misc. LEXIS 3911, **31-32, 2009 NY Slip Op 30387(U) (N.Y. Sup. Ct. Feb. 6, 2009) ("a court's oversight of the liquidation **requires a careful examination** of the Liquidator's proposal to assure a proper recognition of priorities and a reasonable balance between expeditiousness and protection") (emphasis added).

DCSHI, among others, and not the product of the court's lesser standard of self-imposed inaction in favor of the District. On the contrary, the District's views as both regulator and rehabilitator should have been at best one factor only in the court's review of the terms of the agreement; the court had to ensure that the District Settlement was fair, adequate, and reasonable to the Chartered estate, its claimants and stakeholders.

Contrary to any determination that the District Settlement was fair, adequate, and reasonable to the Chartered estate, its claimants, and stakeholders, the court wrongly relied upon the presence of the two District agencies *ipso facto* to ensure the legitimacy of the settlement. See United States v. District of Columbia, 933 F. Supp. 42, 48 (D.D.C. 1996) (quoting United States v. Telluride Co., 849 F. Supp. 1400, 1402 (D. Colo. 1994) ("fairness" requires the court to examine "the negotiating process and attempting to gauge its candor, openness, and bargaining balance"). Sounding a mere "judicial echo" to the conclusions and recommendations of DISB and DHCF in collaboration – and evading any review of the Towers Watson Report with its profound implications on the genesis of rehabilitation *and* the settlement amount – is not enough. See *e.g.*, Eilers v. District of Columbia Bureau of Motor Vehicles Services, 583 A.2d 677, 685 (D.C. 1990) (review of agency decision). Nor is judicial oversight of these two District agencies supposed to be a "toothless" deference to a District agency recommendation. See Georgetown Univ. Hosp. v. District of Columbia Dep't of Employment Servs., 916 A.2d 149, 151 (D.C. 2007). Instead "fairness" must incorporate "concepts of corrective justice and accountability: a party should bear the cost of harm for which it is legally responsible," *Id.* (quoting United States v. Cannons Eng'g Corp., 899 F.2d 79, 87 (1st Cir. 1990)), and must also embrace the statutorily protected classes of stakeholders in the Chartered estate that are directly affected by the terms of the District Settlement through the extinction of their claims against Chartered (i.e., insufficient

funds to pay class members including DCHSI as landlord) or the stripping of Chartered's claims against the District (to which DCHSI holds as sole shareholder). See e.g., In re Global Crossing Sec. & ERISA Litig., 225 F.R.D. 436, 455 (S.D.N.Y. 2004) (court "has a 'fiduciary' duty to the non-representative class members who were not party to the settlement agreement"); Kullar v. Foot Locker Retail, Inc., 168 Cal. App. 4th 116, 130, 85 Cal. Rptr. 3d 20 (Cal. App. 1st Dist. 2008) ("to protect the interests of absent class members, the court must independently and objectively analyze the evidence and circumstances **before it in order to determine whether the settlement is in the best interests of those whose claims will be extinguished**"). The court could not, and indeed did not, say that the District Settlement was fair and accounted for the District's misconduct. On the contrary, the District, through the efforts of its two agencies, received a deep discount for asserted claims, paid nothing for unasserted claims, and gave less than nothing for complete release from Chartered, while leaving it a target for future litigation.

Ironically, the court has not consistently held to self-imposed inaction. Cloistered in an *in camera* review of the Rehabilitator's Fees and Expenses, which totaled approximately \$4 million at the time (see Fifth Status Report at 5, Exhibit 8), the court assured all interested parties that "an extensive and in depth analysis of the fees and expenses of the ten (10) laws firms and consultants/experts" had been conducted.²⁹ But the court curiously eschewed any such analysis with the District Settlement *ab initio*, and expressly *would not* review the Towers Watson Report or entertain its implications in the face of a profoundly greater sum at issue than the attorneys' fees. SA-120, ¶ 2 (an additional \$50 million in debt forgiveness to the District of Columbia).

²⁹ It should be noted, however, that this "in depth and extensive" review was without the benefit of any input from any party or interested party other than the Rehabilitator himself. Although invited to comment if they so desired, no other party was permitted to access or to review of any of the material related to the fee applications and they were not subject to any adversarial process before approval by the court.

While deference is typically accorded the court's views "because he is exposed to the litigants, and their strategies, positions and proofs [and he] is aware of the expense and possible legal bars to success," the court did not stand in that position in review of the District of Columbia Settlement and the approval of that settlement is not entitled to any deference. Shepherd Park Citizens Ass'n v. General Cinema Beverages, Inc., 584 A.2d 20, 22 (D.C. 1990). Reluctant to exercise, much less substitute, his judgment "for that of the Rehabilitator," the court wrongly ignored the judgment of others who are unrelated to DCHSI: (i) Wayne Turnage, Director of DHCF, in his Letter to Mayor Vincent Gray, April 4, 2011; (ii) Rector & Associates, an outside insurance regulatory firm in the November 8, 2012 Report; and (iii) Towers Watson, the outside actuarial firm, in the June 2013 Report.

Each of these individuals/entities had highly relevant evidence to provide to the court demonstrating that the District egregiously breached the DHCF Contract and caused Chartered to incur the very financial losses the District used to initiate the rehabilitation, thereafter setting up the mechanism for dramatic debt forgiveness and ironclad releases to the unmistakable prejudice to the Chartered estate, its creditors (which includes DCHSI), and its residual interest holder (DCHSI as sole shareholder). The Turnage Letter confirms that the District, and in particular the Mayor's Office, knew pre-Rehabilitation in 2011 what the Towers Watson Report subsequently uncovered in 2013: that the District categorically set unsound rates, breached the DHCF Contract and caused substantial losses in the millions of dollars to Chartered. Instead of repudiating or correcting that breach by re-setting the actuarially sound rates and making retroactive payments based on those sound rates in order for Chartered to survive, after learning of the breach, the District leveraged the substantial losses *it created* as an artificial pretext for the rehabilitation of Chartered.

The court ignored this credible “non-DCHSI” evidence of unmistakable harm to the Chartered estate and of probable collusion between DISB (the Regulator/Rehabilitator) and DHCF (the Debtor/Breaching Party) in covering up – *and forever releasing* – the District’s intentional misconduct by a speedy District Settlement. At a minimum, the self-dealing and the bar of claims against the District called for either the “extensive and in depth analysis” that the court employed when looking at the fees and expenses being charged to the Chartered estate, or a review of the Towers Watson Report, or permitting the limited discovery requested by DCHSI. The court’s failure to do these most basic things before rubber stamping the District Settlement was an abuse of discretion.

2. *The lower court was simply wrong. The District Settlement is anything but the result of an arm’s length transaction and therefore not entitled to blind deference.*

The court’s determination that the District Settlement is the result of an arm’s length transaction, and corresponding deference to that mischaracterization in approving the District Settlement, is overwhelmingly contradicted by the evidence. The District of Columbia is Chartered’s largest debtor, and after the Rehabilitator transferred Chartered’s assets to AmeriHealth Mercy, the District’s debt represented Chartered’s remaining asset of any financial significance. SA-44. Now, by dint of the rehabilitation, the District controls Chartered with *the power to determine the outcome of the Rehabilitation, the survival of Chartered, and Chartered’s residual value*. As of that point, the District simultaneously controlled the negotiations of its own debt to Chartered, its own settlement of that debt, the timing and vigor with which it pursued claims against itself in favor of the Chartered estate and its stakeholders – and ultimately what claims against or stake in Chartered would be extinguished. The District’s doubly dominant roles vis-à-vis Chartered mock any suggestion of an arms-length negotiation.

Standing alone, the District's position on both sides of the District Settlement, DISB on the one side, DHCF on the other, with both serving at the pleasure of the Mayor, called for greater scrutiny by the judiciary.³⁰ Beyond that, the evidence of pre-Rehabilitation misconduct demanded it.

Although consistently ignored by the court, the rehabilitation of Chartered and its *de facto* liquidation have been mired since the outset in a morass of pervasive conflicts of interests. 3-AA-749, ¶ 17; 3-AA-758, ¶ 41. The most critical conflict relates to the District's debt to Chartered. Once the District forced Chartered into rehabilitation because Chartered had inadequate capital (when its capital would be more than adequate if the District had paid its obligations under the DHCF Contract), the District through DHCF – the agency that owed Chartered the money – imposed suspect conditions on Chartered's ability to win renewal of the DHCF Contract that it had successfully managed for a decade. Then the District through DISB – the agency that now controls Chartered in rehabilitation – failed to have Chartered even bid on the new DHCF Contract, leaving the claims against the District as the only remaining asset, with no resources, revenue, or ability to generate any revenue to fight for its asserted claims and unasserted claims against the District. 3-AA-758, ¶ 41. At that point, the game was up for Chartered. The rehabilitation façade fell away and what remained was what was always intended – a forced liquidation which had the effect of putting Chartered, as a major creditor of the District, in the weakest possible position to collect from the District. *Id.*

³⁰ Community Nat'l Bank v. Medical Benefit Adm'rs, LLC, 242 Wis. 2d 626, 626 N.W.2d 340, 2001 Wisc. App. LEXIS 208 (Wis. Ct. App. 2001) (“The United States Supreme Court has opined that a **Rehabilitator may not place itself in a position where its personal interests may be antagonistic to those of the estate it is administering.** Jackson v. Smith, 254 U.S. 586, 588 (1921). **It may not deal with Rehabilitation property to benefit itself at the expense of the estate,** Crites, Inc. v. Prudential Ins. Co. of America, 322 U.S. 408, 414 (1944)).

It is unusual in an insurer Rehabilitation that all the key players are so closely related in a rehabilitation. Given that the controlling players are two governmental agencies, it should have been relatively easy for the Rehabilitator, if acting truly in good faith, to facilitate a readily-available remedy for Chartered rather than the death sentence that was delivered. Id. ¶ 42. But it was always the plan of the District to bring about the end of Chartered and to irreparably harm DCHSI and they used and abused their conflicting position to do just that.

A small amount of cooperation among interested governmental parties – involving, at a minimum, the District paying its accrued debts to Chartered! – could have resolved Chartered’s capital depletion – resulting from the actuarially unsound rates and the District’s nonpayment. But instead the cooperation amongst two agencies of the District of Columbia was designed to remove any chance of Chartered coming out of rehabilitation, to remove any chance of paying claims and to erase any residual value of Chartered’s sole shareholder, DCHSI. Id. Instead, what should have been a genuine rehabilitation was frustrated by the District’s self-interest and their desire to irreparably harm DCHSI. Id. Thus, the District has engineered a situation where, instead of the Rehabilitator serving the interests of Chartered and its stakeholders, rehabilitation and in particular the District Settlement serves the District’s interests. Id. This could not be more readily apparent than in the non-arm’s length settlement between the District and itself on the amounts it owed to Chartered and the releases the District obtained. The District had every incentive to pay as little as possible, while the District’s *full* satisfaction of its debt obligations to Chartered would have allowed Chartered to pay its creditors in full (including DCHSI as lessor) and left surplus capital available for distribution to Chartered’s residual interest holder, DCHSI.

3. ***In light of the conclusions of the Towers Watson Report, the court abused its discretion in approving the District Settlement without considering the Report. Without the Report, the court could not determine whether the District Settlement was fair, adequate, or reasonable.***

The District, as the sole signatory and proponent of the District Settlement Agreement, did not present the court with a factual basis necessary to permit the court to make an informed, independent evaluation of the reasonableness of the settlement. Instead, the District sought an expedited approval of the settlement agreement. The District's desire to avoid delay is none too surprising given the content of the Towers Watson Report – **a document that remained undisclosed to the court until DCHSI filed the report with the court five days before the August 21, 2013 “hearing.”** The Towers Watson Report – which the court would not consider – established the unreasonableness of District Settlement and at a minimum raised material questions of the fairness, adequacy, and reasonableness of the District Settlement.

In order to properly exercise its discretion in making an independent evaluation of the District Settlement, the court must have sufficient information to render a knowledgeable decision. In re Panache Cuisine, LLC, 2013 Bankr. LEXIS 3966, *15, 2013 WL 5350613 (Bankr. D. Md. Sept. 23, 2013). By failing to review the Towers Watson Report, the court did not have sufficient information to render a knowledgeable decision. The Towers Watson Report examined only one of numerous categories of underpayments by the District and concluded that the District owed Chartered over \$51.4 million as to that single category, which Towers Watson limited to 22 months of a 5 year contract. SA-240-245. The Towers Watson Report also described how the District and its retained actuary, Mercer, ignored significant information from Chartered, as well as information in the District's possession, and engaged in a pattern of actuarially unsound and inadequate rate setting that caused the capital depletion the District relied upon to put Chartered in to rehabilitation. SA-264-267. The Towers Watson Report provided abundant details that support the inescapable conclusions that (i) the District, by breaching the DHCF Contract, engineered the very financial problems that the District then used

to justify the Rehabilitation; and (ii) the proposed settlement falls far short of reasonableness or fairness. SA-240-245 (detailing the actuarial unsoundness of the capitation rates paid by the District to Chartered and documenting one aspect of the large, cumulative losses to Chartered attributable to these inadequacies).

4. *The court also abused its discretion by failing to consider the analysis of Drew Joyce, DCHSI's expert witness, in the Supplement to DCHSI's Memorandum in Opposition.*³¹

In addition to the single category for 22 months out of the 45 year contract that Towers Watson described, the District underpaid Chartered in at least seven other significant categories, *supra* at Section IV, Statement of Facts, I. Based on the Towers Watson Report and Chartered's financial statements, DCHSI's expert, Drew Joyce, calculated (albeit without the benefit of discovery to more completely calculate all of the categories of underpayments) the retrospective rate adjustments to which Chartered is entitled to exceed \$82 million. Beyond these medical expense related deficiencies, the District also underpaid Chartered's administrative expenses per the DHCF contract, further compounding the Chartered's losses. Prior to 2010 when the District began imposing a 2% premium tax on Chartered, the District had determined that the actuarially sound non-medical load rate was 13.5%, which consisted of 11.5% for administrative expenses and 2% for profit Chartered. The imposition of the 2% tax adversely affected what had theretofore been the actuarially sound non-medical load rate. As the Towers Watson Report makes clear, rates are actuarially sound only if the "projected premiums ... provide for all reasonable, appropriate and attainable costs, *including ... any state-mandated assessments and taxes.*" SA-260 (quoting *Actuarial Certification of Rates for Medicaid Managed Care Programs*)

³¹ DCHSI brought Drew Joyce to August 21, 2013 hearing/status conference. DCHSI was prepared to explain further the details of the TW Report and Mr. Joyce's own analysis of the available data. As noted *supra*, the court would not listen to any evidence as the court was already prepared to rule. SA-310:25, SA-314:16-17.

(emphasis added). After the imposition of the premium tax in 2010, the District did not adjust Chartered's non-medical load rate accordingly reducing Chartered's profits by 2% for the balance of the DHCF Contract.³²

In addition, Mr. Joyce – using the best data available without the benefit of discovery – estimated what the impact of most of the categories of underpayment would be on Chartered's financial statements as of year-ends 2011 and 2012, and as of March 31, 2013 (after the time period reviewed by Towers Watson). In Mr. Joyce's estimation assumed that the District had honored its contractual obligations to pay retrospectively adjusted rates with respect to several but not all of the underpayment categories in Exhibit B to the Supplement – a document that the court did not consider. SA-293.

A consideration of these facts would have been necessary before any judicial determination that the District Settlement was fair, adequate, or reasonable given the District's pattern of setting actuarially unsound rates and repeated breaches of the DHCF Contract, and the near certainty that the rates set for Alliance after July 2011, and for Medicaid after 2012, were also unsound. In fact, both the Rehabilitator and Towers Watson have agreed that the rates in these more recent periods were unsound, but neither quantified the amount of that category of the District's underpayment. SA-269-70, SA 26, Recital K.

Although Mr. Joyce could not calculate the full extent of the underpayments for the above periods with precision because of the absence of any discovery, Mr. Joyce concluded that

³² Under the District Settlement, Chartered would be responsible to pay interest to providers out of its own funds (i.e., the monies received under the settlement agreement), but the Rehabilitator failed to secure from the District the interest on the principal amounts due – that deficiency is in addition to failing to secure all of the principal owed. SA-29. This prejudicial provision contravenes the underlying term of the DHCF Contract that the District is to pay Chartered the provider cost plus 13.5%. The prejudice of this settlement provision is particularly egregious because the District's failure to pay Chartered, which in turn delayed or prevented payment to providers, caused the providers's interest payment claims on monies owed them.

Chartered's total adjusted capital and surplus as of December 31, 2012 should have been \$37.2 million – an amount that would have precluded the District's rehabilitation of Chartered. Mr. Joyce further concluded that Chartered's total adjusted capital and surplus as of March 31, 2013 should have been \$22.3 million. SA-293. In short, the Towers Watson Report articulated an analysis of the District's misconduct that – even when extrapolated to fewer than all of the categories of underpayment – demonstrates that Chartered was solvent, and not the proper subject of rehabilitation in the first instance.

The court abused its discretion by not taking into account these financial deficiencies directly engineered by the District before approving the District Settlement without any judicial inquiry into these multiple categories of non-payment.

5. *The Towers Watson Report, coupled with Mr. Joyce's calculations, calls into serious question the legitimacy of the dollar amount of the Settlement. The Rehabilitator has done nothing to assure the veracity of the number.*

On January 4, 2013, the Rehabilitator filed a claim seeking \$2.2 million for dental benefits that DHCF had required Chartered to provide from January 2011 through November 2012, but for which the District did not pay.³³ The Rehabilitator filed two additional claims on February 21, 2013. The first included the Pharmacy Claim that Chartered had asserted pre-Rehabilitation. The Rehabilitator walked away from that claim, losing the ability to depose Mr. Turnage, director of DHCF, and resetting the procedural clock on \$26 million of asserted claims. Instead, the Rehabilitator filed a Retrospective Claim covering the Medicaid program for the period from August 2010 through April 30, 2012 for \$51,287,369.³⁴ The second claim in the amount of \$9,086,929 covers the Alliance program for the period from July 2010 through July

³³ The Dental Claim failed to assert the required 13.5% surcharge. SA-124, ¶ 22.

³⁴ This Medicaid Retrospective Claim is under-inclusive. SA-123, ¶ 19.

2011.³⁵ Nevertheless, the Rehabilitator did not disclose the methodology for calculating these asserted claim amounts. Without disclosure, either through discovery, or the court's insistence on reviewing that methodology, there is no way to confirm whether these asserted claims were appropriately calculated. SA-126, ¶ 30.

Chartered's unasserted claims against the District were not valued either. By letter dated April 11, 2013, DCHSI attempted to inform the Rehabilitator that the District had underpaid Chartered in several other respects. SA-151-157. The District Settlement Agreement recited – at Recital K – that “Chartered has been investigating and believes that it could file additional claims against DHCF, including claims for what Chartered believes may be actuarially unsound rates during the last year of Chartered's contract with DHCF (May 2012 – April 2013).” SA-26. But the Rehabilitator did not articulate the nature of the District's additional debts to Chartered or their estimated value – other than to suggest that they were considered and were being investigated. SA-45-46.

The Rehabilitator stated that the District Settlement of \$48 million “constitutes roughly 60% of Chartered's outside estimate of its actual damages, and approximately 80% of Chartered's estimated damages for its pending claims.” SA-49. That statement is erroneous because it fails to include interest due on the underpayments and, as stated in the Settlement Agreement, no value was assigned to the unasserted claims.

In addition, the District's final debt to Chartered could not be determined until Chartered's obligations to plan providers were determined after the August 31, 2013 bar date,³⁶ a little over a week after the court approved the District Settlement. Those obligations could not

³⁵ The Alliance Claim is too limited in time. SA-124, ¶ 21.

³⁶ The Rehabilitator requested, and obtained from the court, a bar date for claims to be formally made against the Chartered estate.

be known until (i) the August 31, 2013 bar date passed; (ii) all provider claims were evaluated and reduced to account for such common billing problems as double billings or wrong billing codes; and (iii) disputed claims between Chartered and the providers were resolved. SA-123-24, ¶¶ 18, 20, SA-126, ¶ 30. The court would not wait until the August 31, 2013 bar date to approve the District Settlement. There is simply no justification for underpaying providers simply because the Rehabilitator has decided not to pursue recovery of the entire indebtedness to Chartered. The Rehabilitator has provided an inadequate basis for approval of the District Settlement, which substantially diminishes the Chartered estate and puts providers, creditors and the equity shareholder at risk on non-payment.

The court's failure to confirm the accuracy of these numbers through discovery or to permit some greater certainty by waiting until the provider claims had been resolved – taking instead the District's assertions at face value, and allowing the settlement of an unknown amount of claims for a deep discount of only the known claims – was an abuse of discretion in approving the District Settlement.

6. *The District's debt to Chartered can be calculated. It is the product of simple mathematical formulas to which the District has no defense.*

The Rehabilitator cannot explain why settling claims for a minimum admitted value of \$64 million for \$48 million is more advantageous for the Chartered estate given the absence of any defenses asserted by the District. Whether or not the \$64 million in claims asserted were calculated properly, that sum excludes as much as \$50 million in other underpayments – and yet the Rehabilitator received zero dollars for these amounts. The full extent of the retrospective rating adjustments to which Chartered is entitled – i.e., the sum total of the money that the District owes Chartered and has owed for at least three years – is objectively calculable as a matter of straightforward arithmetic, as evidenced in the Towers Watson Report, and the Joyce

Declarations and Supplement. The settlement amount with its deep discount of something less than the total debt owed is nothing more than rank speculation. See e.g., SA-123-26.

The Rehabilitator has never identified a single defense that the District, the breaching party, had to payment; there is no defense because the DHCF Contract is retroactively rated and the debt ascertainable based on services provided under the DHCF Contract. In other words, the District could not mount any credible defense (and thus Chartered would likely succeed on the merits of any litigation pursued by the Rehabilitator) because the District had already determined that the DHCF Contract is retrospectively rated and the right to retrospective payment was triggered. SA-125, ¶¶ 25-26 (discussing the District's administrative order holding that the DHCF Contract was retrospectively rated); SA-295, SA-301. The trigger of the right to a retrospective payment on a retrospectively rated contract militates against any discount at all, much less walking away from tens of millions of dollars of unasserted claims.

The Rehabilitator's contention that litigation would be "measured in years, not months" (SA-49) cannot be taken seriously. A review of the District Settlement Agreement's signature pages underscores the hollowness of this concern: all signatories of the Agreement are members of the executive branch of the District government, all reporting to Mayor Gray. The District reached an agreement with itself here; it is difficult to imagine a setting where the District, acting through DISB, would ever vigorously pursue claims against the District, acting through DHCF, in protracted litigation. Protracted litigation was never a reality in this rehabilitation of Chartered, much less a possibility. The dubious history leading up to this Settlement Agreement confirms this: the District used financial losses it engineered to take Chartered over in rehabilitation, then reset the procedural clock on Chartered's pending \$26 million Pharmacy Claim, folding it into its Medicaid Retrospective Claim (abandoning a significant near term

benefit to Chartered) and then secured for itself a deep discount on asserted claims and complete forgiveness of unasserted claims.

7. *The District Settlement was not fair, adequate, or reasonable vis-à-vis the broad releases provided to the District and withheld from Chartered and the court's approval of the releases in the Settlement was an abuse of discretion.*

The District Settlement provides non-parallel releases and covenants not to sue, giving the District – and its past and present employees and officers – far broader protections than Chartered and its past and present employees and officers. The District Settlement released the District from asserted claims and “any and all claims, demands, suits and causes of action that Chartered could have asserted against the District ... related to both the Medicaid and Alliance programs.” SA-31-32, ¶¶ 8-9. This necessity for obtaining this broad release – at least from the District’s vantage point is obvious – especially in light of the Towers Watson Report and the Turnage Letter: the District intentionally set actuarially unsound rates, creating a financial pretext for the rehabilitation, and thereafter driving Chartered out of business by transferring its business and assets to AmeriHealth Mercy and paying Chartered a fraction of what it owed. Of course, the District obtained a broad release for itself.

In contrast, the District reserved claims against Chartered, DCHSI and Thompson as follows:

[S]uing Chartered (a) for any criminal or other intentional misconduct occurring prior to October 19, 2012; (b) for submission of any false claims in violation of federal or District law; (c) for taxes, or (d) nominally, where it is being named in a suit is deemed by the District to be a necessary prerequisite to commencing an action against former members of Chartered’s Board, the parent entity of Chartered [i.e., DCHSI] or the sole shareholder of Chartered’s parent entity [i.e., Thompson], as to whom the District expressly reserves its right to sue.

and would provide only a covenant not to sue Chartered limited to “any legal or equitable theory that seeks recovery or indemnification from Chartered of amounts paid to providers by the

District under [the Settlement Agreement].” SA-32, ¶ 9. The Settlement Agreement leaves Chartered exposed to future suits from the District stemming from Chartered’s services and involvement in the Medicaid and Alliance programs. However, it forever releases Chartered’s ability to collect the amounts the District owes Chartered, even if the Rehabilitator has not pursued collection of those amounts, and releases Chartered’s ability to pursue claims for the District’s misconduct in engineering the rehabilitation through the setting of actuarially unsound rates as uncovered by Towers Watson. This Settlement Agreement does not serve Chartered’s best interests, only the District’s.

Just as importantly, the District paid no value for its broad release. The settlement of a cause of action held by the Chartered estate against the District is the equivalent of a sale of that claim. In re Telesphere Communications, 179 B.R. 544, 552 (Bankr. N.D. Ill. 1994) (There is no difference in the effect on the estate between the sale of a claim by way of assignment to a third party and a settlement of the claim with the adverse party). Here, contrary to receiving any consideration for the release of claims the Towers Watson Report uncovered, **Chartered gave** the District a deep discount on uncertain asserted claims, receiving in return potential future litigation. In other words, the District paid less than nothing for the full releases. The District Settlement Agreement is so disproportionately one sided, as evidenced by these non-parallel releases for which Chartered received no value, that the court abused its discretion in approving it.

VII. CONCLUSION

In approving the District Settlement, the trial court did not even meet the low bar it set for itself. That degree of judicial apathy begs the question why the D.C. Code requires any judicial oversight at any stage of the rehabilitation process at all if the statutes simply translate into

stooped judicial deference to the District's executive branch in its request for the approval of a settlement agreement like this one. As set out above, the executive branch evaded legislative oversight in the way in which the settlement payments were structured. So, if the judicial branch is going to beg off any analysis for fear of substituting its judgment for the executive branch, then who is going to review the settlement agreement for fairness, adequacy, or reasonableness?

Several components of the District Settlement demanded a closer look, whether that be the District's position on both sides of the settlement and of course the rehabilitation or the failure to account for and value unasserted claims or the ironclad releases the District secured for itself during "arm's length" negotiations with itself. Even with no discovery permitted, these issues in and of themselves should have prodded the trial court away from a passive, rubber-stamp posture and into a robust examination of a Rehabilitation and a settlement that is manifestly unfair on its face. On the record presented, it was an abuse of discretion to approve the District Settlement at this modest level of inquiry.

The ultimate *coup de grace* to the reviewing court's non-review process was the failure to even consider the Towers Watson Report – a document withheld by the Rehabilitator from the court and the parties for two months. The Towers Watson Report, together with the Turnage Letter, exposed the District's misconduct and the seamy underside of the proffered settlement agreement. To advance its own financial self-interest, the District intentionally caused Chartered to hemorrhage over several years by setting actuarially unsound rates, and not paying what it owed even under those unsound rates. The District then exploited that weakened financial condition to move Chartered into a rehabilitation that was nothing but a filmy disguise for a pre-planned liquidation. At that point, the fox was in the hen house and the demise of Chartered and the injury to DCHSI as both landlord and shareholder was a *fait accompli* **unless** the court

vigorously undertook its oversight obligation to the Chartered estate and its stakeholders. It did not; essentially adopting the role of a bystander while the District looted Chartered to the injury of plan participants, providers, creditors, and shareholder – but most clearly to its own benefit.

The trial court never asked how a business could survive the non-payment of \$64 million in asserted claims or what possible justification could lie for stiffing plan participants, providers, creditors, and shareholder through that indefensible non-payment. In the face of objectively discernible as yet unasserted claims, the court had an obligation, which it shirked, to insure an adequate value for **all claims**, especially when the District is *the* debtor of Chartered and now *is* Chartered in rehabilitation. Whatever “hard bargain” was going to occur here was not going to be between DISB and DHCF. The court was the only one in a position to impose that hard bargain by proper judicial review. DCHSI as both Chartered’s landlord and its sole shareholder rightly stood before the court and now before this Court to respectfully request that the rehabilitation of Chartered be injected with some rational judicial oversight and inquiry. The court’s approval of the District Settlement should be rejected as an abuse of discretion.

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