DC APPLESEED
Solving DC Problems

1111 Fourteenth Street, NW
Suite 510
Washington, DC 20005

Phone 202.289.8007
Fax 202.289.8009
www.dcappleseed.org

February 6, 2015

The Honorable Jacqueline K. Cunningham, Commissioner
Bureau of Insurance
Commonwealth of Virginia
P.O. Box 1157
Richmond, Virginia 23218-1157

The Honorable Alfred W. Redmer, Jr., Commissioner
Maryland Insurance Administration
St. Paul Plaza
200 St. Paul Place
Suite 2700
Baltimore, Maryland 21202-2272

Re: In the Matter of Surplus Review and Determination of Group Hospitalization and Medical Services, Inc., Order No. 14-MIE-012 (D.C. Dep't of Ins., Secs. & Banking Dec. 30, 2014)

Dear Commissioners Cunningham and Redmer:

We are writing to you concerning the December 30, 2014, Decision and Order of Chester A. McPherson, Interim Commissioner of the D.C. Department of Insurance, Securities and Banking, addressing GHMSI's surplus. We are also writing concerning the January 22, 2015, letters Mr. Chet Burrell sent you concerning that Decision and Order. In those letters, Mr. Burrell asked you to issue an order instructing GHMSI not to comply with Commissioner McPherson's Decision. He also asked you to convene a consolidated proceeding involving Maryland, Virginia, and the District, with a view toward redetermining Commissioner McPherson's Decision.

Because DC Appleseed, along with its experts and pro bono attorneys, has been involved for well over ten years in efforts to hold GHMSI accountable to its nonprofit mission, and because we were directly involved in the proceedings leading to Commissioner McPherson's December 30 Decision, we hope you will consider our views concerning the impact of that Decision on Maryland and Virginia. We also hope you will consider our suggestions concerning possible actions you might take in response to the Decision.

1. DC Appleseed's Prior Involvement

DC Appleseed has been involved in these proceedings since 2001. At that time, DC Appleseed was asked by a consortium of funders in the region to undertake an analysis of whether CareFirst's request to convert to for-profit status and sell itself to WellPoint was in

the public interest.

Assisted by our pro bono attorneys at Covington & Burling and Harkins Cunningham, along with assistance from experts at the Harvard Business School and FTI Consulting, DC Appleseed undertook this analysis. Working with a coalition of organizations in the District, Maryland, and Virginia, we concluded that the proposed conversion was not in the public interest. We reached this conclusion in part because the company proposed to sell itself for many hundreds of millions of dollars less than it was actually worth.

We therefore argued both before Commissioner Steve Larsen in Maryland and Commissioner Larry Mirel in the District that the conversion should be denied. In the proceedings before Commissioner Mirel, we worked directly with the Virginia Attorney General. As you know, Commissioner Larsen denied the conversion request, concluding both that CareFirst's proposed selling price was unfair and that the company had lost sight of its nonprofit mission.

After the conversion was denied, DC Appleseed, Covington & Burling, Harkins Cunningham, and Mathematica Policy Research issued a report detailing the ways in which we thought GHMSI was continuing to depart from its nonprofit mission, most particularly in the fact that it had accumulated surplus far in excess of the amount reasonably needed to ensure the financial soundness of the company.

In the wake of this report, CareFirst announced a new plan to devote additional funds to community reinvestment. DC Appleseed was subsequently invited to testify before the Maryland General Assembly about the company's obligations as a nonprofit. In addition, Commissioner Mirel held a hearing and issued a decision determining that GHMSI could and should be spending significantly more on community benefits from its (then) $500 million surplus.

When GHMSI instead reduced its community benefits and further increased its surplus, DC Appleseed worked with the D.C. Council to craft legislation requiring the D.C. Commissioner to conduct a formal hearing examining GHMSI's surplus. This legislation was modeled in part on comparable legislation in Maryland. *See* Md. Code Ann., Ins. § 14-117(e). But the D.C. statute, in addition to requiring that GHMSI's surplus not be unreasonably large, also required that the "corporation shall engage in community health reinvestment to the maximum feasible extent consistent with financial soundness and efficiency." D.C. Code § 31-3505.01.

The D.C. Commissioner held a hearing examining the surplus under this standard in 2009 and issued a decision in 2010. That decision found that the maximum permissible surplus for the company was at the level of 850% RBC. However, because the Commissioner failed in that examination to apply the stated "maximum feasible" standard or to explain her decision, in 2012 the D.C. Court of Appeals reversed the determination and remanded for a new examination of GHMSI's surplus by the Commissioner. *D.C. Appleseed Ctr. for Law & Justice v. D.C. Dep't of Insurance, Secs., & Banking*, 54 A.3d 1188 (D.C. 2012), *available at* http://www.dccourts.gov/internet/documents/10-AA-1461_mtd.pdf. Meanwhile, the surplus had increased to more than 1000% RBC, or nearly $1 billion.

2. Commissioner McPherson's December 30 Decision

As instructed by the Court of Appeals, in June 2014, Commissioner McPherson held a hearing examining GHMSI's surplus. He also engaged his own independent actuarial expert to assist

him in that examination. That expert (Rector & Associates) accepted some but not all of the recommendations of GHMSI's expert (Milliman). DC Appleseed, in turn, based on the work of our own actuarial expert (Mark Shaw of United Health Actuarial Services, Inc.), argued that some but not all of Rector's analysis fairly applied the governing D.C. law.

In the end, with the benefit of an extensive record that included both Rector's analysis and that of our expert, Mr. Shaw, the Commissioner rejected Rector's determination that GHMSI's current surplus met the statutory standard, and accepted our view that under that standard GHMSI's surplus was excessive. But he disagreed with our conclusion that the surplus should be between $400 and $500 million. Instead, he concluded that the company's surplus as of the end of 2011 should have been no higher than 721% RBC, or $696 million. Because the company's surplus was $964 million at the end of 2011, it was excessive by $268 million.

Commissioner McPherson also determined that 21% of the company's surplus is attributable to operations in the District, 53% to operation in Maryland, and 26% to Virginia. The Commissioner therefore directed the company to submit a plan to spend down the District's portion of the company's excess surplus ($56 million) by March 16. The Commissioner has denied motions for reconsideration of his decision filed by GHMSI and DC Appleseed.

Significantly, while the District's statute requires the entirety of GHMSI's surplus to meet the "maximum feasible" standard, the statute directs the Commissioner to order and approve a spend-down plan *only* for the portion of the excess attributable to the District. The $212 million of excess surplus attributable to Maryland ($142 million) and Virginia ($70) is therefore subject to the control of Maryland and Virginia. Any action concerning those amounts will be determined in the first instance by Commissioners Cunningham and Redmer.

3. Recommended Actions

As noted, Mr. Burrell has asked that you order GHMSI not to comply with Commissioner McPherson's Decision. He has also asked you to convene a consolidated proceeding to redetermine Commissioner McPherson's Decision. For several reasons, we believe these requested actions are legally unsound and contrary to the interests of both GHMSI subscribers and the public as a whole.

First, as mentioned earlier, Commissioner McPherson has directed a spend-down plan *only* with regard to the portion of GHMSI's surplus attributable to operations in the District. Just as it would be inappropriate for the District to order GHMSI to spend down excess surplus attributable to Maryland and Virginia, it would also be inappropriate for Maryland or Virginia to order GHMSI not to spend down excess surplus attributable to the District. Commissioner McPherson's spend-down order was issued pursuant to a District statute, enacted pursuant to regulatory authority conferred by Congress, and the order of the D.C. Court of Appeals.

Second, as we explained in our submission to Commissioner McPherson,[1] while all three jurisdictions have important regulatory authority over GHMSI, and all three coordinate with each other and avoid differences where possible, in rare cases there may be conflicts among the

[1] DC Appleseed Ctr. for Law & Justice, *Rebuttal Statement: D.C. Department of Insurance, Securities and Banking: Surplus Review and Determination of Group Hospitalization and Medical Services, Inc. ("GHMSI")* 62–65 (Nov. 7, 2014) [hereinafter DC Appleseed Rebuttal], *available at* http://disb.dc.gov/sites/default/files/dc/sites/disb/publication/attachments/DCACRebuttalLetter.pdf.

jurisdictions on an important regulatory issue concerning GHMSI. And where that happens, as we stated in our submission to Commissioner McPherson, under GHMSI's federal charter Congress has provided that the District regulation controls. That charter provides: "The corporation shall be licensed and regulated by the District of Columbia in accordance with the laws and regulations of the District of Columbia." Pub. L. No. 103-127, § 138(b), 107 Stat. 1336, 1349 (1993).

It is understandable and practical for Congress to place primary authority in the District; otherwise, conflicts among the jurisdictions might arise with no clear legal authority for resolving the conflict. In fact, the legislative history of the cited charter provision makes clear that Congress intended the District to exercise primary authority over GHMSI, rather than leaving uncertainty over which jurisdiction's regulations might control. This history makes clear that because the District had not previously had this primary authority, the result had been that "GHMSI has adeptly played Maryland, Virginia, and D.C. insurance regulators against one another." S. Rep. No. 104-92, at 54 (1995).

Mr. Burrell's letters continue this practice. For example, Mr. Burrell asserts that the Maryland Commissioner's previous determination that GHMSI should maintain surplus in the range of 1000%–1300% RBC conflicts with Commissioner McPherson's determination that GHMSI's maximum permissible surplus is 721% RBC. And he asks you to either issue orders negating Commissioner McPherson's order or implement a GHMSI-proposed procedure playing the regulators against each other.

But, again, the legislative history of the cited charter provisions illustrates that Congress intended to remedy such practices based in part on the proposition that "the primary oversight of an insurance carrier rests with the authorities in the company's 'State of domicile.'" *Id.* at 53. Accordingly, under the federal charter provision, the District's determinations prevail in the event there are conflicts over GHMSI's permissible surplus and how excess surplus is to be allocated. DC Appleseed Rebuttal at 63–64. A regulatory action by Maryland or Virginia that purports to negate a regulatory action of the District would conflict with Congress's grant of regulatory authority to the District.

Third, while both Maryland and the District have adopted standards to govern the surplus of the "corporation," that is, GHMSI as a whole, MIEAA's standard was enacted by the D.C. Council in the exercise of the primary regulatory authority conferred by Congress. The District standard obligates GHMSI to "engage in community health reinvestment to the maximum feasible extent consistent with financial soundness and efficiency." D.C. Code § 31-3505.01. That obligation is separate from the surplus-review provisions of the Act, which authorize the D.C. Commissioner to review under that standard the portion of surplus attributable to the District. *Id.* § 31-3506(e)–(i). Application by Maryland or Virginia of a different standard is highly likely to be an obstacle to realizing the purpose and objective of the maximum-feasible standard, and of Congress's grant of regulatory authority to the District over a corporation chartered as "a charitable and benevolent institution." Pub. L. No. 76-395, § 8 (1939). *See also Hillman v. Maretta,* 133 S. Ct. 1943, 1950 (2013) (preemption occurs when state action is "an obstacle to the accomplishment and execution of the full purposes and objectives of congress").

Fourth, Mr. Burrell is mistaken to suggest that the Maryland and Virginia Commissioners should call for a de novo consolidated hearing so the three jurisdictions can now jointly review GHMSI's surplus. As Commissioner McPherson stated in denying GHMSI's belated request for such action, "the Commissioner already has coordinated with the other jurisdictions in which

GHMSI conducts business"[2]— precisely as the District statute requires him to do. D.C. Code § 31-3506(e). Moreover, as the Commissioner also stated, if his December 30 Decision has produced "conflicts among jurisdictions," that is a matter that is "beyond the Commissioner's authority to address. The Commissioner is bound to follow the District of Columbia statutes and regulations governing this surplus review." Jan. 28 Order at 2.

Moreover, even if a consolidated hearing might have been a practical possibility at an earlier date, Mr. Burrell's request for it now, after the lengthy District proceedings are completed, is plainly untimely and contrary to the public interest. GHMSI could have asked for such a hearing when Maryland earlier reviewed the surplus, but it did not do so. Nor did the Maryland Commissioner suggest such action during Maryland's prior review of GHMSI's surplus. Nor did GHMSI ask Commissioner McPherson to seek such a consolidated review at any time in the year-long proceedings just completed.

Commissioner McPherson sought and received comments from both the Maryland and Virginia Commissioners concerning actions he should take both on the excess surplus issue and the allocation issue. And while the then-Maryland Commissioner suggested that "any formula for attribution should be subject to the agreement of all three jurisdictions," she offered no suggestions for what the formula should be nor how the Commissioner might fashion such an agreement through his proceedings. Statement of Therese M. Goldsmith, Maryland Insurance Commissioner, before the Government of the District of Columbia Department of Insurance, Securities and Banking 3 (Oct. 10, 2014), *available at* http://disb.dc.gov/sites/default/files/dc/sites/disb/publication/attachments/SurplusReviewandDeterminationforGHMSStatement.pdf.

It is worth noting that, while Mr. Burrell contends that a proceeding of all three jurisdictions is necessary because GHMSI faces "conflicting orders [that] place GHMSI in an untenable position," (Burrell letters at 2), the company's conduct belies his contention. As we pointed out in our submissions to Commissioner McPherson, GHMSI has intentionally lowered its surplus in the last several years to levels below what the Maryland Commissioner found GHMSI could permissibly maintain under Maryland law. DC Appleseed Rebuttal at 52.

Finally, if, despite the primacy of the District's regulatory authority with respect to surplus, you seek to conduct a new review of GHMSI's surplus and a method for allocating it, we urge you to give substantial weight to the work Commissioner McPherson has done. In the past year Commissioner McPherson has assembled a voluminous record and weighed the views of several conflicting experts, each of whom conducted extensive analysis. While we believe GHMSI's excess surplus is actually larger than Commissioner McPherson determined and that his allocation to the District is too low, his careful analysis deserves your serious consideration—whether you apply the District's statutory standards, which is the correct course, or apply your own standards.

That you give serious weight to Commissioner McPherson's findings is particularly important given that they are plainly in the interest of GHMSI subscribers in Maryland and Virginia. Commissioner McPherson strongly erred on the side of financial safety for the company and, in

---

[2] Order on GHMSI's Motion for Reconsideration and Coordinated Proceedings with Maryland and Virginia and on D.C. Appleseed's Request for Briefing Schedule, Order No. 14-MIE-014 2 (D.C. Dep't of Ins., Secs. & Banking Jan. 28, 2015) [hereinafter Jan. 28 Order], *available at* http://disb.dc.gov/sites/default/files/dc/sites/disb/publication/attachments/Order14-MIE-014.pdf.

addition, allocated nearly 80% of the excess surplus ($212 million) to Maryland and Virginia. While GHMSI may argue on appeal that the allocation to Maryland and Virginia should be even higher (while we argue that it should be lower), it is clear that significant excess surplus is attributable to the two jurisdictions. GHMSI might use the excess surplus attributable to Maryland and Virginia ($212 million in Commissioner McPherson's Decision) for the benefit of its subscribers and also, to the extent allowed, as reinvestment to address community health needs.

In other words, Maryland and Virginia now have an opportunity to bring GHMSI into compliance with its nonprofit mission, and do so in a way that both protects the company and brings great benefits to subscribers and the public. Given that the District intends to spend down its share of the excess surplus, it is plainly in the interest of Maryland and Virginia to do the same.
For these reasons, we urge you to decline Mr. Burrell's requests and consider how best to move forward to require GHMSI to spend down the significant excess surplus allocable respectively to Maryland and Virginia. We would be glad to answer any questions you have about these suggestions, provide further information explaining our suggestions, or meet with you at your convenience.

Sincerely,

Walter Smith, Executive Director
DC Appleseed Center

Richard B. Herzog
Harkins Cunningham LLP

Deborah Chollet, Ph.D.

Marialuisa S. Gallozzi
Covington & Burling LLP

cc: The Honorable Chester A. McPherson, Acting Commissioner
D.C. Department of Insurance, Securities and Banking

Mr. Philip Barlow, Associate Commissioner for Insurance
D.C. Department of Insurance, Securities and Banking

Mr. Adam Levi, Assistant Attorney General
D.C. Department of Insurance, Securities and Banking