Examination Warrant Number 09-NP-308-T
Examination Warrant Number 09-NP-309-T

Report of Limited-Scope Examination of

Independence Blue Cross
Philadelphia, PA

and

Highmark Inc.
Pittsburgh, PA

Executive Compensation

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June 29, 2009

Honorable Stephen J. Johnson, CPA
Deputy Insurance Commissioner
Commonwealth of Pennsylvania
Insurance Department
Office of Corporate & Financial Regulation
Harrisburg, Pennsylvania 17120

Dear Sir:

In accordance with Examination Warrant Number 09-NP-308-T and Examination Warrant Number 09-NP-309-T, both dated February 5, 2009, a limited-scope examination of executive compensation was made of:

INDEPENDENCE BLUE CROSS

AND

HIGHMARK INC.

both Pennsylvania domiciled not-for-profit health plans. The last full-scope examinations of Independence Blue Cross ("IBC") and Highmark Inc., were each conducted by the Pennsylvania Insurance Department as of December 31, 2006.

As this examination is limited in scope, this examination report is not intended to communicate all numbers of importance for an understanding of either company's financial condition. The Reports of Examination of IBC, dated April 30, 2008, and Highmark, dated July 18, 2008, should be referred to for additional historical and background information.

A report of this limited-scope examination is hereby respectfully submitted.

Executive Summary

On April 27, 2007, Highmark Inc. ("Highmark") and Independence Blue Cross ("IBC") filed an application with the Pennsylvania Insurance Department to consolidate the two companies. In connection with that application, and pursuant to its authority granted under 40 P.S. § 991.1402(f)(1)(vi) to determine whether the proposed consolidation would be likely to be hazardous or prejudicial to the insurance-buying public, the Department commissioned an analysis of the executive compensation

Highmark and IBC had authorized both for their own executives and for the executives of the combined company should the consolidation be approved.

On January 21, 2009, Highmark and IBC withdrew their application. After that withdrawal the Department ordered the analysis of the executive compensation of Highmark and IBC continued pursuant to its authority under 40 P.S. § 323.1 et seq. to examine the affairs of all persons subject to its jurisdiction. This report is the product of that analysis. It reviews the executive compensation of Highmark and IBC and determines the extent to which that compensation complies with applicable legal standards. It also places Highmark and IBC executive compensation in context by comparing it with the executive compensation authorized by other Blue Cross plans, by leading for - profit health insurers, and by leading Pennsylvania non-profit hospital systems, as well as by major non-profit organizations and by the Medicare and Medicaid programs. The report's findings include the following:

1. Eleven Highmark executives as of the date the application was withdrawn were potentially eligible for payments of at least 200% of their annual salary had the Highmark-IBC merger[1] been consummated and thereafter they had been terminated without cause or they had resigned for certain reasons. In addition, one Highmark executive who would have been a senior executive of a merged Highmark-IBC was potentially eligible for a payment of 150% of his annual salary on termination following the merger. Those twelve Highmark executives, and their positions as of January 1, 2009, are as follows:

[1] Highmark and IBC structured their combination as a consolidation – two corporations becoming a new corporation with both original corporations ceasing to exist--rather than as a merger, in which one of the corporations ceases to exist. Both consolidations and mergers are Changes of Control ("COC's"). In this report, the terms are used interchangeably.

Executive	Position
Kenneth Melani, M.D.	President and Chief Executive Officer
S. Tyrone Alexander	Executive Vice President, Human Resources and Administrative Services
Ron Cain	Senior Vice President, Strategic Business Operations
Nanette DeTurk	Executive Vice President, Treasurer and Chief Financial Officer
Elizabeth Farbacher	Senior Vice President, Corporate Audit
Gino Francavilla	Senior Vice President, Strategic Business Operations
David Holmberg	President and CEO, HVHC, Inc.
James Klingensmith	Executive Vice President, Health Services, and Chief Integration Officer
Daniel Lebish	President and CEO, HM Insurance Group and UCCI, Inc.
David O'Brien	Executive Vice President, Government Services
Thomas Tabor	Senior Vice President, Chief Information Officer
Gary Truitt	Senior Vice President, General Counsel and Corporate Secretary

For each of the most recent five years, the total compensation of each of those 12 executives has been as follows:

Table ES 1

Highmark Executives: Total Compensation

Name	2004	2005	2006	2007	2008
Melani	1,621,311	2,487,477	3,156,825	3,646,331	3,565,599
DeTurk	482,913	644,135	727,715	1,049,895	1,269,699
O'Brien	730,858	1,033,297	1,118,822	1,372,651	1,268,684
Lebish	468,120	569,342	810,484	773,123	930,414
Holmberg	-	-	-	51,923	935,763
Tabor	443,455	596,116	630,353	687,547	668,480
Alexander	797,700	1,196,053	1,287,895	1,436,895	1,328,890
Truitt	707,764	984,382	1,020,800	1,132,852	1,050,387
Klingensmith	1,113,176	1,589,761	1,595,557	1,738,743	1,635,479
Francavilla	505,918	664,120	687,123	742,913	737,169
Cain	298,190	407,916	467,554	521,565	540,269
Farbacher	385,137	518,042	546,388	592,381	568,846

2. Seven IBC executives as of the date the application was withdrawn were potentially eligible for payments of at least 200% of their annual salary had the Highmark-IBC merger been consummated and they had been terminated without cause or they had resigned for certain reasons. Those executives, and their positions as of January 1, 2009, are as follows:

<u>Executive</u>	<u>Position</u>
Joseph A. Frick	President and Chief Executive Officer
Yvette D. Bright	Senior Vice President, e-Business and Operations
Christopher D. Butler	Executive Vice President and Chief Operating Officer
Christopher Cashman	Senior Vice President, Corporate and Public Affairs
William F. Haggett	Chief Marketing Executive
Paul A. Tufano	Senior Vice President and General Counsel
I. Steven Udvarhelyi, M.D.	Senior Vice President and Chief Medical Officer

For each of the last five years, the total compensation of each of those seven executives has been as follows:

Table ES 2

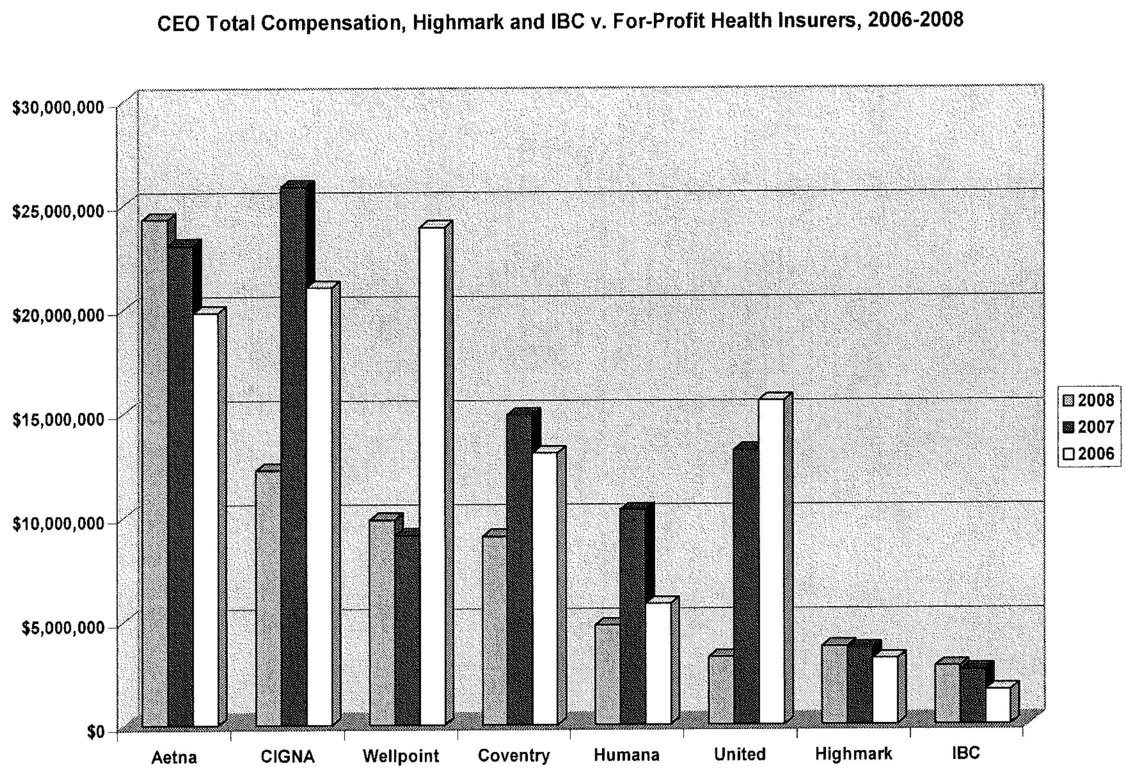
IBC Executives: Total Compensation

Name	**2004**	**2005**	**2006**	**2007**	**2008**
Frick	916,406	1,064,283	1,637,754	2,587,416	2,781,275
Butler	889,925	1,027,806	1,311,735	1,453,923	1,648,118
Tufano	760,245	849,124	819,285	944,652	1,050,604
Bright	291,990	336,992	422,161	517,168	994,846
Haggett	506,170	556,324	696,032	758,785	855,765
Udvarhelyi	779,510	850,200	869,341	964,443	1,059,500
Cashman	629,105	679,570	689,509	765,449	824,967

3. As nonprofit corporations, Highmark and IBC are subject to the Pennsylvania Nonprofit Corporation Law ("NPC Law"), 15 Pa. C.S.A. sec. 5101 et seq. That law requires nonprofit corporations to pay only that compensation which is reasonable in amount. Compensation is reasonable in amount, according to the Internal Revenue Service, if it is "such amount as would ordinarily be paid for like services by like enterprises under like circumstances." Because the annual compensation of the Highmark and IBC executives is similar to that paid to executives of other Blue Cross companies of similar size, that compensation is reasonable.

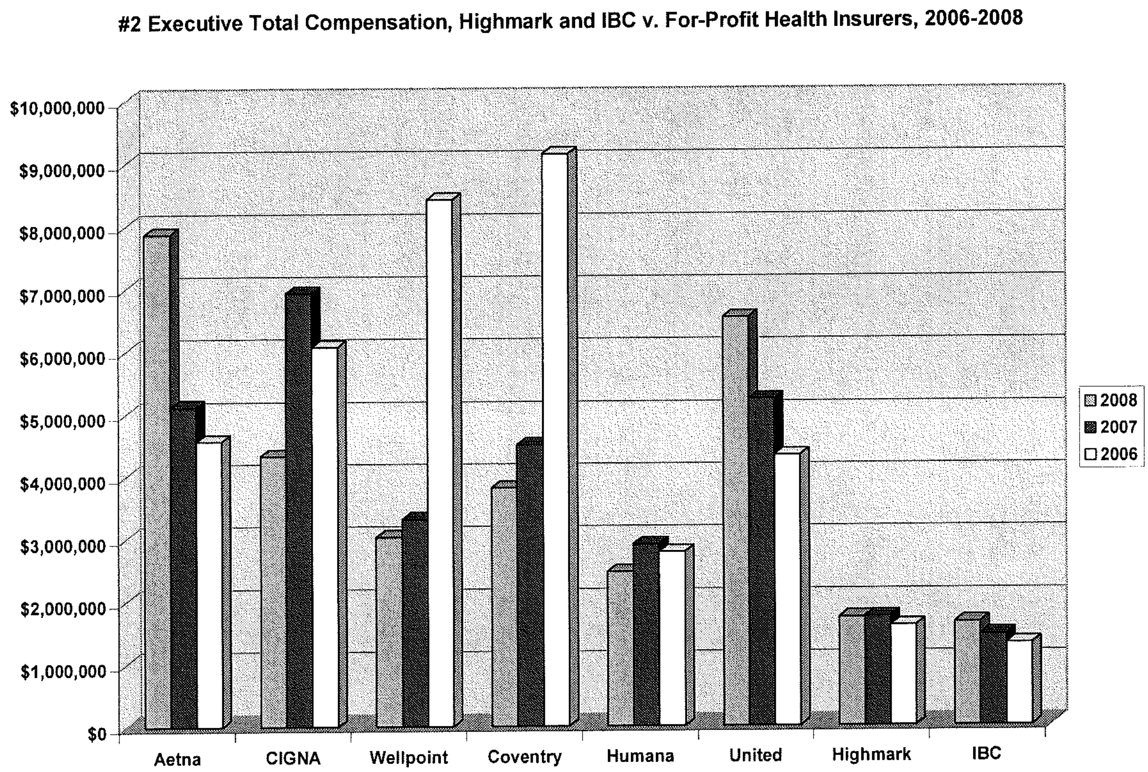
4. The compensation of the Highmark and IBC CEO's is substantially less than the compensation of the CEO's of the leading for - profit health insurers as reported in their proxy statements filed with the SEC, as shown in the following chart:

Table ES 3



5. The cash compensation of the high-ranking Highmark and IBC executives is also substantially less than the compensation of high-ranking executives of the leading for - profit carriers, as typified by the following chart:

Table ES 4



6. The compensation of the Highmark and IBC executives is also generally in line with the compensation of the highest-paid employees of the leading hospital systems in and around Pennsylvania, as shown in the following table:

Table ES 5

2006 Total Compensation, 5 Highest Paid Employees: Leading PA Hospital Systems v. Highmark and IBC

Executive	UPMC	Virtua	Penn*	CHOP	Jefferson Health System	Geisinger	Cooper Health	Temple	Highmark	IBC
CEO	$4,012,329	$3,371,663	$3,455,767	$2,060,574	$1,741,709	$1,720,052	$1,016,474	$1,010,097	$3,156,825	$1,637,754
#2	$1,341,435	$1,549,970	$2,314,931	$1,266,901	$738,793	$822,302	$1,089,571	$763,179	$1,595,557	$1,311,735
#3	$1,278,610	$1,358,580	--	$1,085,411	$686,775	$729,506	$873,372	$580,465	$1,287,895	$869,341
#4	$1,164,710	$1,288,997	--	$818,825	$408,863	$699,803	$825,578	$572,486	$1,118,822	$819,285
#5	$1,159,988	$1,198,928	--	$775,617	$124,282	$670,540	$793,434	$493,858	$1,020,800	$689,509

Source: 2006 Form 990's; Highmark and IBC.

*The University of Pennsylvania Health System and School of Medicine do not file separate tax returns. The CEO of UPHS and the Dean of the School of Medicine, whose compensation is set forth above, are included on the University's Form 990.

7. Had the Highmark-IBC merger been approved, all twelve Highmark executives and all seven IBC executives would have been eligible for certain payments had they been terminated without cause or they had resigned for Good Reason. Those executives and those payments are as follows:

Table ES 6

Highmark Executives:
Payments on Termination without cause or due to a reduction in responsibilities in connection with a COC

Executive (multiple)	Base Salary x multiple	Annual bonus '08	Annual bonus '09 pro-rated	Full LT bonus '07-'09	Full LT bonus '08-'10	Pro-rated LT bonus '09-'11	Retention bonus	L & H benefits	RWB's ***	280G/ 4999 Gross-up	Total
Melani (3)	$3,300,303	$910,142	*	$1,012,752	$1,130,795	*		$21,011			$6,375,003
Klingensmith (1.5)	$982,800	$325,238	*	$405,101	$425,356	*	$1,965,600	$46,418**	**	****	$4,150,513 *****
DeTurk (2)	$960,784	$291,456	*	$367,772	$389,838	*		$18,285			$2,028,135
Alexander (2)	$979,692	$297,192	*	$337,754	$344,509	*		$18,285			$1,977,432
O'Brien (2)	$891,808	$274,759	*	$306,253	$318,504	*		$21,011			$1,812,335
Truitt (2)	$900,156	$223,416	*	$226,781	$231,318	*		$21,011			$1,602,682
Farbacher (2)	$549,988	$106,171	*	$109,391	$111,579	*		$21,011			$898,140
Francavilla (1.5)	$585,245	$141,912	*	$135,505	$139,053	*	$390,163	$22,331		******	$1,414,209
Tabor (1.5)	$526,086	$135,410	*	$125,873	$132,554	*		$18,285			$938,208
Cain (1.5)	$459,959	$95,121	*	$88,946	$93,181	*	$306,639	$22,331		******	$1,066,177
Lebish (2)	$804,590	$213,170	*	$236,593	$264,118	*		$21,011			$1,539,482
Holmberg (2)	$960,000	$455,763	*	--	--	*	--	$27,515			$1,443,278

*The figures in this table are based on the assumption that a COC occurs and the executive terminates on January 1, 2009. Under this assumption, because the executive receives pro-rated bonuses for the year of termination, the executive's annual bonus for 2009 and his long-term bonus for 2009-11 are negligible: his annual bonus for 2009 would be 1/365 of a full annual bonus, and his long-term bonus for 2009-2011 would be 1/1095 of the full long-term bonus. The later in 2009 a COC occurred and the executive resigned, the higher his 2009 annual bonus and 2009-11 long-term bonus would be.

**Calculated as if executive had worked an additional 18 months, and includes 40% tax gross-up on that additional 18 months.

***These are the same retiree welfare benefits receivable by all Highmark employees.

****Authorized. However, according to Highmark, no §4999 tax liability will be triggered.

*****Includes additional $47,027 of deferred compensation benefits calculated as if executive had worked an additional 18 months.

******Authorized unless reducing total payments by 10% or less would eliminate any §4999 tax liability. According to Highmark, no such liability would be triggered in any event.

Table ES 7

IBC Executives:
Payments on Termination without cause or due to a reduction in responsibilities in connection with a COC

Executive (multiple)	Base salary x multiple	Annual bonus '08 x multiple	Annual bonus '09 pro-rated	LT bonus '07-'09, pro-rated	LT bonus '08-'10, pro-rated	LT bonus 09-'11, pro-rated	Life & health benefit	Total
Frick (3)	$2,940,000	$2,940,000	*	$640,167	$326,667	*	$14,378	$6,861,212
Butler (3)	$2,055,000	$1,438,500	*	$357,333	$182,667	*	$14,378	$4,047,878
Cashman (2)	$805,000	$402,500	*	$170,625	$87,208	*	$14,378	$1,479,711
Tufano (2)	$1,005,000	$502,500	*	$180,583	$108,875	*	$14,378	$1,811,336
Haggett (2)	$865,200	$432,600	*	$183,863	$93,730	*	$14,378	$1,589,771
Udvarhelyi (2)	$1,060,600	$530,300	*	$224,315	$114,898	*	$14,378	$1,944,491
Bright (1.5)	$507,000	$253,500	*	$120,267	$67,600	*	$14,378	$962,745**

*The figures in this table are based on the assumption that a COC occurs and the executive terminates on January 1, 2009. Under this assumption, because the executive receives pro-rated bonuses for the year of termination, the executive's annual bonus for 2009 and his long-term bonus for 2009-11 are negligible: his annual bonus for 2009 would be 1/365 of a full annual bonus, and his long-term bonus for 2009-2011 would be 1/1095 of the full long-term bonus. The later in 2009 a COC occurred and the executive resigned, the higher his 2009 annual bonus and 2009-11 long-term bonus would be.

**This total does not include any amounts Ms. Bright receives pursuant to the Retention Agreement she has with IBC. Under that agreement, she receives $125,000 if she remains with IBC until March 29, 2008, an additional $250,000 if she remains with IBC until September 28, 2008, and an additional $125,000 if she remains with IBC until March 28, 2009.

8. The Highmark and IBC executives are also eligible for benefits under Supplemental Executive Retirement Plans—so-called "SERP" plans. Such retirement benefits are calculated based on years of service and age at retirement. Once vested, those benefits are payable on termination regardless of the reason for termination, and regardless of whether termination occurs in connection with a COC or not in connection with COC. The value of the SERP benefit payable to each Highmark executive if he terminated on January 1, 2009 is as follows:

Table ES 8

Highmark Executives: SERP benefit earned as of January 1, 2009

Executive	SERP benefit
Melani	$6,084,000
Klingensmith	$2,509,000
DeTurk	$375,000
Alexander	$1,453,000
O'Brien	$2,610,000
Truitt	$2,413,000
Farbacher	$229,000
Francavilla	$2,466,000
Tabor	$1,713,000
Cain	$1,710,000
Lebish	$286,000
Holmberg	--

The value of the SERP benefit payable to each IBC executive if he terminated on January 1, 2009 is as follows:

Table ES 9

IBC Executives: SERP Benefit Earned as of January 1, 2009

Executive	SERP benefit
Frick	$5,292,000
Butler	$6,761,000
Cashman	$1,307,000
Tufano	$700,000
Haggett	$2,037,000
Udvarhelyi	$2,058,000
Bright	$520,000

9. Under the Pennsylvania NPC Law payments potentially receivable on termination following a merger by the executives of non-profit corporations must be "for services rendered." Under the IRS regulations relating to such payments, compensation for a covenant not to compete can be characterized as compensation for services rendered, i.e., the services of not competing. The executives who remain with Highmark and IBC and are potentially eligible to receive payments following a merger have all entered into covenants not to compete that prohibit them from competing for at least as long as the term of the payments they would receive. Those payments therefore can be characterized as compensation for services rendered to the extent that the covenants are enforceable and enforced.

10. Three Highmark executives and one IBC executive[2] have received retention bonuses--payments that become payable if the executive remains with the company until a certain date. The three Highmark executives receiving retention bonuses have all terminated--two were terminated by the terms of their retention agreements, and

[2] Another IBC employee who is not among the highest paid IBC executives and would not have been a member of the management team of a merged Highmark-IBC also received a retention bonus.

Highmark and the third executive had an understanding that he would terminate after receiving his retention bonus. The one IBC executive receiving a retention bonus has not terminated. The payments the terminating executives are receiving on termination can reasonably be characterized both as reasonable and as compensation for services rendered. That is because the companies could reasonably believe that those executives were essential to the successful integration of the two companies, and that paying them a substantial bonus only if they remained with the company throughout the Department's review process increased the likelihood that they would do just that.

11. As with annual compensation, the payments executives of the leading for - profit health insurers are eligible to receive on termination substantially exceed those potentially receivable by the Highmark and IBC executives.

Introduction

This report examines the compensation of the executives of Highmark and Independence Blue Cross.

The report was originally commissioned in connection with the proposed consolidation of Highmark and IBC. It originally sought to analyze both the annual compensation of the most highly compensated Highmark and IBC executives and the compensation those executives would receive if they were terminated without cause or they resigned under certain conditions after the consolidation occurred. Because Highmark and IBC withdrew their consolidation application on January 21, 2009, no such payments will be made. However, the employment-related agreements the Highmark and IBC executives have entered into continue to provide for certain severance payments to the executives on termination, including termination in connection with a change-of-control ("COC"). In addition, certain payments to certain executives were triggered by the withdrawal of the consolidation agreement and/or their termination. Accordingly, this report analyzes both the annual compensation of the most highly compensated Highmark and IBC executives and the compensation they have received or are eligible to receive on termination in connection with a COC. In order to place that compensation in context, this report also analyzes the executive compensation of the leading for - profit health insurers and non-profit hospital systems, and compares the compensation of the Highmark and IBC executives with the compensation of the executives of those entities.

This report is divided into two Parts. The first Part concerns the annual compensation that the most highly paid officers of Highmark and IBC have received during each of the last five years. In this Part we describe the different types of annual compensation each of those officers has received, and set forth the amount of each type of compensation received by each officer. We then discuss the laws that such compensation must comply with, and determine whether the compensation of the Highmark and IBC executives complies with that law. In the course of this discussion, we also analyze the annual compensation of the executives of the for - profit health insurers with whom Highmark and IBC compete, as well as of the major hospitals who receive payment from Highmark and IBC.

The second Part of this report describes and quantifies the different types of payments the Highmark and IBC executives are eligible to receive on termination. Such payments include both the retirement benefits the executives have earned which are payable on termination for any reason, and severance benefits that are payable on termination in connection with a COC. In addition, the report compares the payments the Highmark and IBC executives are eligible to receive on termination in connection with a COC with those the executives of the leading for - profit health insurers are eligible for. Finally, it discusses some alternative interpretations of the law.

PART ONE

I. The annual compensation receivable by the Highmark and IBC executives

A. The Highmark officers

This section reviews the annual compensation of the eleven executives employed by Highmark or its subsidiaries as of January 1, 2009, who were potentially eligible for payments of at least 200% of their annual salary if Highmark and IBC had merged and they had thereafter terminated under certain circumstances following a Highmark-IBC merger. It also reviews the annual compensation of one executive who was eligible for a payment of 150% of his annual salary had he terminated following a Highmark-IBC merger but who would have been among the ten highest paid executives at a combined Highmark-IBC. The twelve Highmark executives whose compensation is reviewed in this report, and their current positions, are as follows:

Executive	Position
Kenneth Melani, M.D.	President and Chief Executive Officer
S. Tyrone Alexander	Executive Vice President, Human Resources and Administrative Services
Ron Cain	Senior Vice President, Strategic Business Operations
Nanette DeTurk	Executive Vice President, Treasurer and Chief Financial Officer
Elizabeth Farbacher	Senior Vice President, Corporate Audit
Gino Francavilla	Senior Vice President, Strategic Business Operations
David Holmberg*	President and CEO, HVHC, Inc.

James Klingensmith	Executive Vice President, Health Services, and Chief Integration Officer
Daniel Lebish*	President and CEO, HM Insurance Group and UCCI, Inc.
David O'Brien	Executive Vice President, Government Services
Thomas Tabor	Senior Vice President, Chief Information Officer
Gary Truitt	Senior Vice President, General Counsel and Corporate Secretary

*Officer of Highmark subsidiary.

With the exception of Mr. Holmberg, who joined Highmark in mid 2007, each of the Highmark executives had an agreement with Highmark several years before Highmark and IBC agreed to merge which provided for severance payments based on several different types of annual compensation.[3] Each executive also entered into at least two additional agreements – one or more at about the same time that the parties entered into a merger agreement, and another after the parties withdrew their merger applications. As discussed in Part Two, the succeeding agreements change the payments the executive would potentially be eligible for on termination in connection with a COC and the length of the covenant not to compete the executive would be subject to on termination. The successive agreements do not change the annual compensation payable to the executives, however. That annual compensation consists of the following elements:

1. Annual salary

Each executive receives a base annual salary. For each of the last five years, the base salaries of each of the twelve Highmark executives have been as follows:

[3] The sources for all Highmark and IBC compensation data are the Summary Compensation Tables attached to the Oct. 8, 2008 e-mail of Tom Hutton (hereinafter "Summary Compensation Tables"), unless otherwise stated.

Table 1

Highmark Executives: Annual Salary

Name	**2004**	**2005**	**2006**	**2007**	**2008**
Melani	888,180	942,500	979,630	1,037,630	1,100,101
DeTurk	315,829	330,343	390,668	452,615	480,392
O'Brien	377,204	398,319	416,492	433,411	445,904
Lebish	327,564	339,410	347,687	361,593	402,295
Holmberg	-	-	-	51,923	480,000
Tabor	290,675	304,139	318,904	335,529	350,724
Alexander	434,434	454,325	464,694	477,746	489,846
Truitt	409,715	423,698	429,098	444,924	450,078
Klingensmith	611,981	622,336	605,364	622,943	680,400
Francavilla	326,327	334,248	344,123	358,281	390,163
Cain	229,942	246,060	260,321	275,844	306,639
Farbacher	246,546	252,726	258,793	267,095	274,994

2. Annual bonus

Each of the twelve executives also receives a bonus under Highmark's annual bonus plan, called the Annual Employee Incentive Plan ("AEIP"). Under this plan, Highmark authorizes a bonus equal to a certain percentage, called the target percentage, of the employee's salary. Highmark also establishes performance goals that the employee must meet to obtain his target bonus. If he exceeds these goals he can obtain more than his target percentage, but not more than 150% of the target. If he does not attain these goals he can still receive 50% of his target bonus, as long as he attains some minimum threshold goal.

The document describing the Highmark AEIP sets forth these principals, but it does not set forth any particular performance goals. Rather, it states that the Personnel and Compensation Committee of the Board of Directors will establish these goals. It also states that the goals the Committee establishes may be based on financial success, enrollment, quality and/or achievement of strategic initiatives, as well as other factors.

As a practical matter, as the table below indicates, the Highmark executives receive substantial bonuses every year. The combination of an executive's annual bonus and his long-term bonus--which is explained and tabulated in the next section--typically exceeds the executive's salary.

Table 2

Highmark Executives: Annual Bonus

Name	2004	2005	2006	2007	2008
Melani	436,294	780,840	975,056	1,027,084	910,142
DeTurk	109,983	160,822	159,126	299,350	291,456
O'Brien	169,180	304,941	303,027	320,168	274,759
Lebish	93,937	128,211	207,951	182,032	213,170
Holmberg	-	-	-	-	455,763
Tabor	101,590	148,419	147,106	153,755	135,410
Alexander	198,026	349,558	344,056	356,527	297,192
Truitt	167,977	267,680	258,647	268,022	223,416
Klingensmith	282,287	392,016	371,006	379,135	325,238
Francavilla	115,787	165,807	159,942	167,172	141,912
Cain	68,248	101,126	101,449	108,446	95,121
Farbacher	74,833	126,091	122,913	127,368	106,171

3. LTIP bonus

In addition to their annual AEIP bonuses, each of the twelve executives also receives a bonus each year under Highmark's Long-Term Incentive Plan ("LTIP"). Highmark's LTIP is similar to its annual bonus except that it is based on performance during a three-year period, referred to as a Performance Period, and it establishes goals and a target bonus that apply to each three-year Performance Period. Any given day is thus part of three LTIP-related Performance Periods, as well as one annual bonus period. The LTIP bonuses received by each of the twelve executives for each of the last five years are as follows:

Table 3

Highmark Executives: Long-Term Bonus
For Performance Period Ending In:

Name	2004	2005	2006	2007	2008
Melani	174,837	699,137	1,132,139	1,521,617	1,495,356
DeTurk	57,101	152,970	177,921	297,930	497,821
O'Brien	86,474	275,037	369,303	484,072	443,021
Lebish	46,619	101,721	254,846	229,498	314,949
Holmberg	-	-	-	-	-
Tabor	51,190	143,558	164,343	198,263	182,346
Alexander	110,240	342,170	424,145	547,622	486,852
Truitt	85,072	248,004	288,055	369,906	326,893
Klingensmith	198,908	525,409	579,187	671,665	589,841
Francavilla	63,804	164,065	183,058	217,460	195,094
Cain	-	60,730	105,784	137,275	128,509
Farbacher	38,758	114,225	139,682	177,918	157,681

4. Other compensation.

In addition to their base salary, annual bonus and long term bonus, some executives also received other types of compensation during the last five years. Such other compensation includes signing bonuses, special project bonuses, financial planning services, and vehicle allowances. Such other compensation, not including compensation of less than $15,000 annually, was as follows:

Table 4

Highmark Executives: Other Compensation

Name	2004	2005	2006	2007	2008
Melani	122,000	65,000	70,000	60,000	60,000
DeTurk	-	-	-	-	-
O'Brien	98,000	55,000	30,000	135,000	105,000
Lebish	-	-	-	-	-
Holmberg	-	-	-	-	-
Tabor	-	-	-	-	-
Alexander	55,000	50,000	55,000	55,000	55,000
Truitt	45,000	45,000	45,000	50,000	50,000
Klingensmith	20,000	50,000	40,000	65,000	40,000
Francavilla	-	-	-	-	10,000
Cain	-	-	-	-	10,000
Farbacher	25,000	25,000	25,000	20,000	30,000

5. Totals

Based on the four elements discussed above—base salary, annual bonus, LTIP bonus, and other compensation—the total compensation received by each of the twelve Highmark executives for each of the last five years has been as follows:

Table 5

Highmark Executives: Total Compensation

Name	2004	2005	2006	2007	2008
Melani	1,621,311	2,487,477	3,156,825	3,646,331	3,565,599
DeTurk	482,913	644,135	727,715	1,049,895	1,269,669
O'Brien	730,858	1,033,297	1,118,822	1,372,651	1,268,684
Lebish	468,120	569,342	810,484	773,123	930,414
Holmberg	-	-	-	51,923	935,763
Tabor	443,455	596,116	630,353	687,547	668,480
Alexander	797,700	1,196,053	1,287,895	1,436,895	1,328,890
Truitt	707,764	984,382	1,020,800	1,132,852	1,050,387
Klingensmith	1,113,176	1,589,761	1,595,557	1,738,743	1,635,479
Francavilla	505,918	664,120	687,123	742,913	737,169
Cain	298,190	407,916	467,554	521,565	540,269
Farbacher	385,137	518,042	546,388	592,381	568,846

In addition to this cash compensation, the executives also receive the employee benefits all Highmark employees receive, and accrue additional benefits which may become payable when they leave the company. Those benefits are discussed in Part Two.

B. The IBC officers

This section reviews the annual compensation of the seven executives employed by IBC as of January 1, 2009 who were potentially eligible for payments of at least 200% of their annual salary if Highmark and IBC had merged and thereafter they had terminated under certain circumstances. Those executives, and their current positions, are as follows:

Executive	Position
Joseph A. Frick	President and Chief Executive Officer
Yvette D. Bright	Senior Vice President, e-Business and Operations
Christopher D. Butler	Executive Vice President and Chief Operating Officer

Christopher Cashman	Senior Vice President, Corporate and Public Affairs
William F. Haggett	Chief Marketing Executive
Paul A. Tufano	Senior Vice President and General Counsel
I. Steven Udvarhelyi, M.D.	Senior Vice President and Chief Medical Officer

Like the Highmark executives, each of the IBC executives had an agreement providing for severance payments based on several different types of annual compensation several years before Highmark and IBC agreed to merge. Also like the Highmark executives, the IBC executives entered into new employment agreements at about the same time that the merger agreement was signed, and a third agreement after the parties withdrew their merger applications. The changes made by those agreements, which will be discussed in Part Two, do not change the types of annual compensation the executives receive. That compensation is as follows:

1. Annual salary

Each IBC executive receives a base annual salary. For each of the last five years, the base salaries of each of the seven IBC executives has been as follows:

Table 6

IBC Executives: Annual Salary

Name	**2004**	**2005**	**2006**	**2007**	**2008**
Frick	505,800	604,346	901,246	941,715	980,000
Butler	497,000	567,796	625,923	655,923	685,000
Tufano	437,700	451,750	466,508	483,115	502,500
Bright	221,500	255,553	288,248	318,615	338,000
Haggett	309,465	321,627	400,492	416,511	432,600
Udvarhelyi	439,880	457,770	480,769,	505,779	530,300
Cashman	345,550	356,600	368,523	385,538	402,500

2. Annual bonus

Each of the IBC executives also receives an annual bonus. IBC's annual bonus program for its officers, called the Officer Incentive Program ("OIP"), works in the same way as Highmark's AEIP: it establishes a bonus equal to a target percentage of salary for each officer, and then pays the officer a bonus equal to that percentage if he meets certain performance goals, pays him a higher percentage if he exceeds those goals, and pays him less than his target percentage if he fails to meet those goals but meets lesser goals.

Notably, IBC's annual bonus program both sets forth more concrete goals than does Highmark's annual bonus program, and more specifically explains how the officer's bonus is calculated than does Highmark's. Specifically, officers are awarded points in seven different areas. The maximum number of points they can receive from all these areas combined is 150; if they receive the maximum 150 points, they get 150% of their target bonus. If they receive 100 points they get their target bonus, and if they receive fewer than 100 points they get less than their target bonus. The seven different areas in which they can earn points are (1) attaining individual goals; (2) reducing administrative costs; (3) implementing IBC's "consumerism" strategy; (4) executing IBC's pricing strategy; (5) increasing membership; (6) attaining the customer acquisition and retention, financial, operational, consumer satisfaction, and strategy implementation goals that all IBC employees share (which together account for 50% of all points); and (7) obtaining additional points awardable by the CEO at his discretion. The specific milestones an officer must reach to attain a given number of points in each of the above seven categories is set forth in a goal document.

Like Highmark's annual bonus program, IBC's annual bonus program results in all officers receiving bonuses each year, as the table below indicates.

Table 7

IBC Executives: Annual Bonus

Name	2004	2005	2006	2007	2008
Frick	181,098	186,480	380,550	900,000	1,011,038
Butler	168,525	190,960	365,070	412,500	426,405
Tufano	159,094	181,355	210,617	227,408	221,950
Bright	70,490	81,439	116,642	130,080	145,135
Haggett	102,000	105,060	159,787	182,400	189,197
Udvarhelyi	157,343	175,600	200,447	220,800	231,846
Cashman	127,300	136,275	156,284	158,093	172,942

3. LTIP bonus

Like the Highmark executives, for each of the last five years each of the IBC executives also has received a bonus based on his performance during the preceding three year period. The document explaining the IBC LTIP is much less detailed than the document explaining its annual bonus plan, and the IBC Executive Committee appears to have substantially more discretion in administering the LTIP—e.g., in establishing performance goals and selecting the individuals eligible for the plan—than it does in administering the annual bonus plan. The concept underlying both the long-term and annual bonuses, however, is the same: the executive's bonus depends on the target the company has established for him and the number of points he earns based on the extent to which he has achieved various goals.

Table 8

IBC Executives: Long-Term Bonus For Performance Period Ending In:

Name	2004	2005	2006	2007	2008
Frick	229,508	273,457	205,849	505,701	790,237
Butler	224,400	269,050	200,655	369,500	461,746
Tufano	163,451	216,019	142,160	234,129	288,670
Bright	-	-	17,271	68,473	136,711
Haggett	94,705	129,637	89,697	159,874	233,968
Udvarhelyi	182,287	216,830	143,092	237,864	297,354
Cashman	156,255	186,695	134,680	221,818	249,525

4. Other compensation

Like the Highmark executives, some of the IBC executives also received additional compensation--such as signing bonuses, special project bonuses, and retention bonuses--in some or all of the last five years. Such compensation was as follows:

Table 9

IBC Executives: Other Compensation

Name	2004	2005	2006	2007	2008
Frick	-	-	150,109	150,000	-
Butler	-	-	120,087	16,000	74,967
Tufano	-	-	-	-	37,484
Bright	-	-	-	-	375,000
Haggett	-	-	46,056	-	-
Udvarhelyi	-	-	45,033	-	-
Cashman	-	-	30,022	-	-

5. <u>Totals</u>

Based on the four components discussed above, the total compensation received by each of the nine IBC executives for each of the last five years has been as follows:

Table 10

IBC Executives: Total Compensation

Name	2004	2005	2006	2007	2008
Frick	916,406	1,064,283	1,637,754	2,587,416	2,781,275
Butler	889,925	1,027,806	1,311,735	1,453,923	1,648,118
Tufano	760,245	849,124	819,285	944,652	1,050,604
Bright	291,990	336,992	422,161	517,168	994,846
Haggett	506,170	556,324	696,032	758,785	855,765
Udvarhelyi	779,510	850,200	869,341	964,443	1,059,500
Cashman	629,105	679,570	689,509	765,449	824,967

II. Legal analysis of the annual compensation of the Highmark and IBC officers

A. What law applies?

Three different statutes are relevant to the compensation of the Highmark and IBC executives. The first two statutes—the Health Plan Corporation Law and the Non-profit Corporation Law—require the compensation of Blue Cross executives to be reasonable. The third statute—the Internal Revenue Code, along with the Treasury Regulations promulgated pursuant thereto—sets forth standards that control the determination of what compensation is reasonable. This section discusses the relevant provisions of all three statutes.

First, the law under which Blue Cross and Blue Shield plans are authorized is the Health Plan Corporation ("HPC") Law, 40 Pa.C.S.A. § 6101 et seq. Blue Cross plans originally provided coverage for hospital stays and thus were known as hospital plan corporations, while Blue Shield plans originally provided coverage for physician and surgical services and thus were known as professional health service corporations. See 40 Pa. C.S.A. §§ 6101- 6127 (governing hospital plan corporations); 40 Pa. C.S.A. §§6301-6335 (governing professional health service corporations). Today, Blue Cross plans and Blue Shield plans both cover both types of healthcare costs, either directly or through subsidiaries, and both are deemed health plan corporations under Pennsylvania law. The HPC statute provides that both hospital plan corporations and professional health service corporations are not-for-profit plans. 40 Pa.C.S.A. §§ 6101, 6302. It further declares that all HPC's are "charitable and benevolent institution[s]," and that they are exempt from all state and local taxes. Pa. C.S.A. §§ 6103(b), 6307(b).

HPC's clearly are not "charitable and benevolent institutions" in the same way as organizations like the Red Cross and the United Way are: unlike those charities, their purpose is not to make grants but to operate a health plan, they are not exempt from federal income taxation, they neither seek nor receive contributions from the public, and if they did receive such contributions those contributions would not be deductible by the contributor. They also do business through for - profit subsidiaries. Nevertheless, by reason of their legal status as non-profit charitable and benevolent institutions, no part of their income can inure to the benefit of their members, officers or directors. Due to this proscription on private inurement, the compensation of executives of non-profit charitable and benevolent institutions, unlike the compensation of executives of for - profit corporations, must be reasonable.

The second statute relevant to Blue Cross executive compensation is the general Non-profit Corporation Law, 15 Pa.C.S.A. § 5101 et seq. (hereinafter sometimes referred to as the "NPC Law"). That statute requires a non-profit corporation to be "not incorporated for a purpose or purposes involving pecuniary profit, incidental or otherwise." 15 Pa.C.S.A. § 5103. It provides that such a corporation "may make an incidental profit," but that "all such incidental profits shall be applied to the maintenance and operation of the lawful activities of the corporation, and in no case shall be divided or distributed in any manner whatsoever among the members, directors, or officers of the corporation." 15 Pa.C.S.A. § 5545. Similarly, section 5551(a) of the NPC Law provides that a non-profit corporation "shall not...distribute any part of its income or profits to its members, directors, or officers." Finally, section 5551(b) provides that "a non-profit corporation may pay compensation in a reasonable amount to members, directors, or officers for services rendered," while section 5502(16) provides that one of the powers of the non-profit corporation is to fix the "reasonable" compensation of its officers. Thus, reasonable compensation to the Highmark and IBC executives for services rendered complies with the NPC Law, and does not constitute an unlawful distribution to those officers. Unreasonable compensation to such executives for services rendered, in contrast, would not comply with the NPC Law, and would constitute an unlawful distribution.

The third statute providing guidance regarding the lawfulness of the annual compensation of Blue Cross executives is the Internal Revenue Code. One Code provision, section 162(a)(1), provides that only reasonable compensation for personal services actually rendered is deductible. Prior to 1987, this provision would not have affected Blue Cross plans, since up until that time they had been exempt from federal income tax. However, Code section 501(m), enacted in 1986, eliminated the federal income tax exemption for Blue Cross plans. The prohibition on deducting unreasonable compensation thus today applies to Blue Cross plans.

Code section 162(a)(1) does not set forth any test for determining the reasonableness of compensation. The Treasury Regulations interpreting section 162, however, provide that reasonable compensation is "such amount as would ordinarily be paid for like services by like enterprises under like circumstances." Treas. Reg. 1.162-7(b)(3). Several courts have set forth a list of factors that should be considered in determining whether compensation is reasonable. E.g., Eberl's Claim Serv., Inc. v. Com'r, 249 F.3d 994, 999(10th Cir. 2001) (documenting the different factors used by different courts); Elliott's, Inc. v. Com'r, 716 F.2d 1241, 1245 (9th Cir. 1983) (citing factors including (1) role in company, (2) external comparison, (3) character and condition of the company, (4) conflict of interest, and (5) internal consistency); Mason Mfg. Co. v. Com'r, 178 F.2d 115, 119 (6th Cir. 1949) (nine different factors, including "the prevailing rates of compensation for comparable positions in comparable concerns"). Unfortunately, such lists of factors, unlike an objective test or formula, do not provide any definitive guidance, since they do not specify the weight each factor must be given, or the number of factors that must be present or satisfied in order for compensation to be deemed reasonable. As a practical matter, therefore, to determine whether annual compensation for services rendered is reasonable under the Internal Revenue Code, and is thus lawful under section 5551(b) of the NPC Law, we must determine the compensation paid for like services in like enterprises under like circumstances: we must look for comparables.

B. What are the proper comparables for Highmark and IBC?

1. For - profit health insurers?

Highmark and IBC provide health insurance coverage just as the for - profit health insurers do, and they compete for business with the for - profit health insurers. In addition, many if not all of the same skills necessary to manage a for - profit health insurer are also necessary to manage a non-profit health plan corporation. There is therefore a strong argument for compensating the Highmark and IBC executives at roughly the same level as the executives of for - profit health insurers.

a. CEO compensation

Notably, the compensation of the CEO's of the for - profit health insurers typically far exceeds that of the Highmark and IBC CEO's. The three tables below set forth the compensation, by component, of the CEO's of each of the six leading for - profit carriers and of the Highmark and IBC CEO's for each of the last three years. As the tables indicate, in most cases the compensation of the CEO's of the for - profit health carriers substantially exceeds the compensation of the Highmark and IBC CEO's.

Table 13

CEO Compensation by Component, 2008, For - profit Health Insurers v. Highmark and IBC

CEO	Company	Salary ($)	Stock & Options Awards ($)	Cash Bonuses ($)	Increase in Pension/Deferred Comp Value ($)	All Other Comp ($)	Total ($)
Ron Williams	Aetna	1,095,785	19,993,995	1,950,000	1,162,866	101,487	24,300,112
Ed Hanway	CIGNA	1,142,855	3,601,966	6,650,000	820,097	21,792	12,236,740
Angela Braly	WellPoint	1,135,538	8,453,333	73,810	11,970	169,561	9,844,212
Dale Wolf	Coventry	965,000	7,596,022	0	--	486,447	9,047,469
Michael McCallister	Humana	1,017,308	3,078,897	0	--	668,104	4,764,309
Stephen Hemsley	United	1,300,000	0	1,822,019	--	119,023	3,241,042
Ken Melani	Highmark	1,100,101	0	2,405,498	--	60,000	3,565,599
Joseph Frick	IBC	980,000	0	1,801,275	--	0	2,781,275

Source: 2009 Proxy Statements; Highmark and IBC.

Table 14

CEO Compensation by Component, 2007, For - profit Health Insurers v. Highmark and IBC

CEO	Company	Salary ($)	Stock & Options Awards ($)	Cash Bonuses ($)	Increase in Pension/Deferred Comp Value ($)	All Other Comp ($)	Total ($)
Ron Williams	Aetna	1,095,785	18,196,473	1,900,000	1,749,414	104,162	23,045,834
Ed Hanway	CIGNA	1,110,000	5,079,202	17,999,970	1,618,584	32,021	25,839,777
Angela Braly	WellPoint	922,269	7,400,308	588,311	3,706	179,677	9,094,271
Dale Wolf	Coventry	925,000	9,535,407	3,821,226	--	588,190	14,869,823
Michael McCallister	Humana	973,558	2,438,685	1,950,000	4,438,993	511,321	10,312,557
Stephen Hemsley	United	1,300,000	8,134,691	3,635,000	--	94,838	13,164,529
Ken Melani	Highmark	1,037,630	--	2,548,701	--	60,000	3,646,331
Joseph Frick	IBC	941,715	--	1,495,701	--	150,000	2,587,416

Source: 2008 Proxy Statements; Highmark and IBC.

Table 15

CEO Compensation by Component, 2006, For - profit Health Insurers v. Highmark and IBC

CEO	Company	Salary ($)	Stock & Options Awards ($)	Cash Bonuses ($)	Increase in Pension/Deferred Comp Value ($)	All Other Comp ($)	Total ($)
Ron Williams	Aetna	1,073,077	9,628,084	7,732,500	1,298,160	70,655	19,802,476
Ed Hanway	CIGNA	1,101,923	7,972,501	11,249,389	626,756	63,917	21,014,486
Larry Glasscock	WellPoint	1,290,385	15,932,399	2,013,206	4,320,893	329,286	23,889,169
Dale Wolf	Coventry	85,000	8,518,822	3,174,110	--	491,194	13,034,126
Michael McCallister	Humana	900,000	2,378,837	1,552,419	542,896	424,461	5,798,613
Stephen Hemsley	United	1,300,000	11,290,311	2,875,000	257,229	106,873	15,549,028
Ken Melani	Highmark	979,630	0	2,107,195	--	70,000	3,156,825
Joseph Frick	IBC	901,246	0	586,399	--	150,109	1,637,754

Source: 2007 Proxy Statements; Highmark and IBC.

The compensation of the for - profit carriers' CEOs exceeds that of the Highmark and IBC CEO's primarily because the for - profit health insurers, but not Highmark and IBC, have available stock and stock options to compensate their executives. As the tables indicate, the annual salaries of all the CEO's are all roughly $1 million, due to the $1 million cap on the deductibility of non-performance-based compensation under section 162(m) of the Internal Revenue Code. The value of the stock and stock option awards granted to the for - profit CEO's, however, far exceeds their $1 million salaries--the most striking examples being WellPoint's Larry Glasscock's $15.9 million in stock-based compensation in 2006, and Aetna's Ron Williams's stock-based compensation of more than $18 million in both 2007 and 2008. In addition, in a few cases the large compensation gap between the for - profits and the Blues is also due to the substantially larger cash bonuses received by the for - profit CEO's: CIGNA's Ed Hanway, for example, received cash bonuses of $11.2 million in 2006, $17.9 million in 2007, and $6.7 million in 2008, while Aetna's Ron Williams received a cash bonus of $7.7 million in 2006.

It should also be emphasized that the value of the for - profit health insurers' stock, like most stock, plummeted in 2008: each company's stock lost over half its value. One might therefore expect the compensation of the CEO's of those companies to decline accordingly. The compensation of four executives did decline in 2008: United's Stephen Hemsley's pay declined by 75%, the compensation of CIGNA's Ed Hanway and Humana's Michael McAllister declined by 50%, and Coventry's Dale Wolf saw his compensation fall by a third. On the other hand, the compensation of WellPoint's Angela Braly and Aetna's Ron Williams both increased slightly, not withstanding the sharp decline in their stock price during 2008: Ms. Braly's compensation increased from $9.1 million to $9.8 million, and Mr. Williams' from $23.0 million to $24.3 million.

Due both to fluctuations in performance and to the manner in which stock-based compensation is valued, the total compensation of the CEO's of the for - profit health insurers can vary significantly from year to year. Looking at CEO compensation over a three-year period may therefore be more meaningful than looking at compensation for any given year. Accordingly, the table below sets forth the total compensation during the last three years of the CEO's of the leading for - profit health insurers and of the CEO's of Highmark and IBC:

Table 16

CEO Total Compensation, Highmark and IBC v. For Profit-Health Insurers, 2006-2008

	Aetna	CIGNA	Wellpoint	Coventry	Humana	United	Highmark	IBC
2008	$24,300,112	$12,236,740	$9,844,212	$9,047,469	$4,764,309	$3,241,042	$3,737,932	$2,781,275
2007	$23,045,834	$25,839,777	$9,094,271	$14,869,823	$10,312,557	$13,164,529	$3,646,331	$2,587,416
2006	$19,802,476	$21,014,486	$23,886,169	$13,034,126	$5,798,613	$15,549,028	$3,156,825	$1,637,754
TOTAL	$67,148,422	$59,091,003	$42,824,652	$36,951,418	$20,875,479	$31,954,599	$10,541,088	$7,006,445

As Table 16 indicates, during the most recent three-year period only the CEO of Humana made less than twice as much as Dr. Melani or less than three times as much as Mr. Frick, while the Aetna and CIGNA CEO's each made more than five times as much as Dr. Melani and more than eight times as much as Mr. Frick. At the same time, it should be noted that the compensation of the for - profit CEO's as set forth in their proxy statements in some cases includes the increase in the value of their pensions, whereas the compensation reported by Highmark and IBC does not. For Humana's Mr. McAllister in 2007, this value—$4.4 million—was substantial. If that $4.4 million is excluded from Mr. McAllister's total compensation, his compensation over the most recent three year period would exceed Dr. Melani's by 56% and Mr. Frick's by 135%. The $4.3 million increase in the value of WellPoint's Larry Glasscock's pension in 2006 is also significant. However, that $4.3 million, which is set forth in Table 15, is less than the $7.6 million Mr. Glasscock received in 2007 as WellPoint's CEO for part of that year, which is not shown in Table 15. Table 16 therefore somewhat understates—not overstates—total WellPoint CEO compensation.

Finally, the following table sets out the 2008 revenues of both Highmark and IBC and the six leading for - profit health insurers.

Table 17

Revenues v. Compensation: For - profit Health Insurers and Highmark and IBC

Company	**2008 Revenues**	**2006-08 CEO Compensation**
United	$81.2 billion	$32.0 million
WellPoint	$61.3 billion	$42.8 million
Aetna	$31.0 billion	$67.1 million
Humana	$28.9 billion	$20.9 million
CIGNA	$19.1 billion	$59.0 million
Coventry	$11.9 billion	$37.0 million
Highmark	$12.4 billion	$10.5 million
IBC	$11.0 billion	$7.0 million

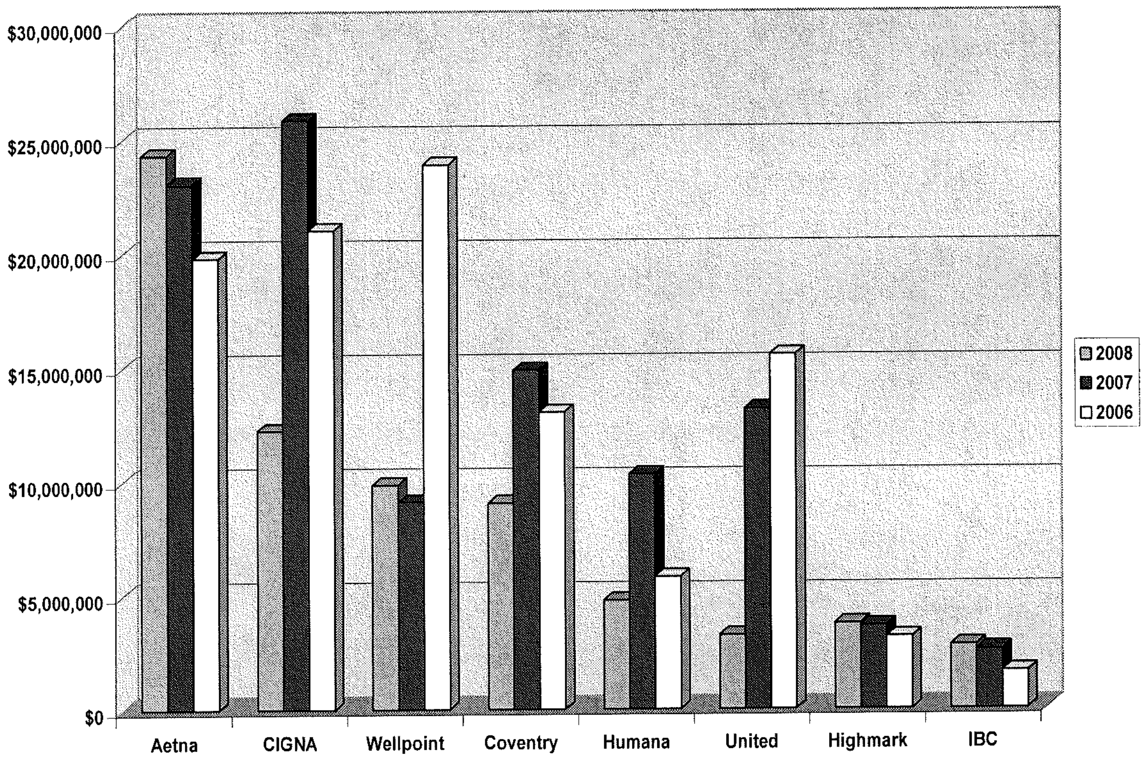
As the table indicates, both Highmark and IBC are roughly the same size as Coventry, the smallest of the six for - profit carriers. As the table also indicates, among the leading for - profit carriers there is not a significant correlation between revenues and CEO compensation. CIGNA, for example, is the second smallest company of the six for - profit health insurers, but its CEO's compensation is the second highest among the six CEO's. Conversely, the compensation of the Humana CEO is the lowest of the six CEO's, even though Humana is larger than CIGNA and Coventry and almost as large as

Aetna, which pays its CEO more than three times as much as Humana's CEO receives. And although United is the largest of the six for - profit carriers, United CEO Stephen Hemsley's compensation was the second lowest among the six CEO's. (On the other hand, Mr. Hemsley's predecessor, William McGuire, had total compensation of $124.8 million in 2005. See http://www.forbes.com/static/pvp2005/LIRRI3M.html.)

In any event, the above discussion concerns equity among the for - profit health insurers, not between the for - profits and Highmark and IBC. Regardless of which for - profit carrier or which group of for - profit carriers Highmark and IBC are compared to, the compensation of the Highmark and IBC CEO's remains substantially lower than that of the CEO's of the for - profit health insurers.

The following chart displays the total compensation in each of the last three years of the Highmark, IBC, and for - profit health insurer CEO's graphically.

CEO Total Compensation, Highmark and IBC v. For-Profit Health Insurers, 2006-2008



b. Compensation of non-CEO executives

In addition to disclosing their CEO's compensation, the for - profit health insurers are also required to disclose in their proxy statements the total compensation of their next four highest-paid executives. The three tables below set forth, for both the leading for - profit HMO's and Highmark, the total compensation in each of the last three years of each of their five highest paid executives.

Table 18

2008 Total Compensation, 5 Highest Paid Executives, Highmark and IBC v. For-Profit Health Insurers

Executive	Aetna	CIGNA	Wellpoint	Coventry	Humana	United	Highmark	IBC
CEO	$24,300,112	$12,236,740	$9,844,212	$9,047,469	$4,764,309	$3,241,042	$3,737,932	$2,781,275
#2	$7,869,824	$4,321,161	$3,023,907	$3,811,823	$2,467,361	$6,531,406	$1,730,106	$1,648,118
#3	$5,566,280	$4,235,548	$2,579,813	$3,769,809	$1,772,851	$5,635,177	$1,421,188	$1,059,500
#4	$2,675,841	$2,184,674	$2,428,361	$2,760,899	$1,588,624	$5,016,808	$1,301,575	$1,050,604
#5	$2,446,294	$1,951,088	$2,264,581	$1,547,286	$1,588,048	$4,638,870	$1,216,809	$994,846

Table 19

2007 Total Compensation, 5 Highest Paid Executives, Highmark and IBC v. For-Profit Health Insurers

Executive	Aetna	CIGNA	Wellpoint	Coventry	Humana	United	Highmark	IBC
CEO	$23,045,834	$25,839,777	$9,094,271	$14,869,823	$10,312,557	$13,164,529	$3,646,331	$2,587,416
#2	$5,112,352	$6,919,827	$5,399,980	$7,381,163	$4,352,029	$5,385,576	$1,738,743	$1,453,923
#3	$4,276,344	$4,671,320	$4,878,008	$5,018,875	$2,903,116	$5,267,845	$1,436,895	$964,443
#4	$3,939,836	$3,111,096	$4,296,206	$4,500,398	$2,751,270	$5,228,132	$1,372,651	$944,652
#5	$2,478,118	$3,050,542	$3,308,352	$2,720,505	$2,175,308	$4,770,555	$1,132,852	$765,449

Table 20

2006 Total Compensation, 5 Highest Paid Executives, Highmark and IBC v. For-Profit Health Insurers

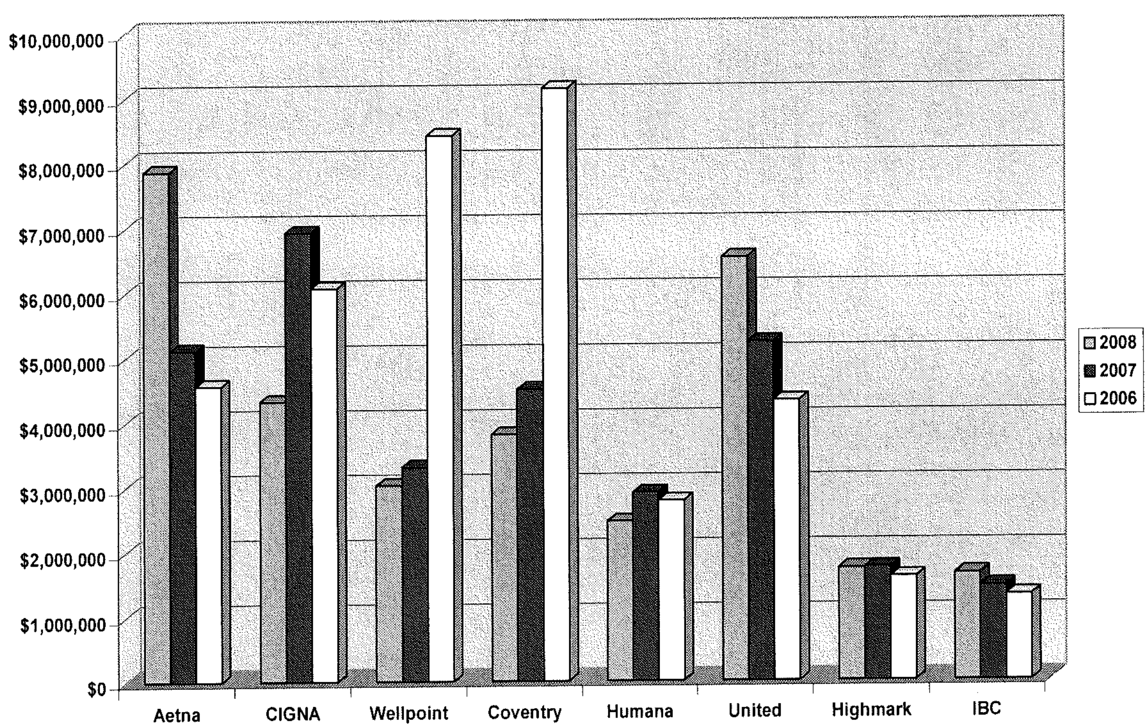
Executive	Aetna	CIGNA	Wellpoint	Coventry	Humana	United	Highmark	IBC
CEO	$19,802,476	$21,014,486	$23,886,169	$13,034,126	$5,798,613	$15,549,028	$3,156,825	$1,637,754
#2	$4,561,374	$6,068,254	$8,415,077	$9,139,438	$2,778,690	$4,325,612	$1,595,557	$1,311,735
#3	$4,095,043	$3,497,800	$6,651,786	$4,174,453	$2,197,128	$4,194,685	$1,287,895	$869,341
#4	$3,896,224	$3,134,642	$6,622,360	$3,507,560	$2,103,072	$3,812,299	$1,118,822	$819,285
#5	$3,410,341	$2,690,100	$6,554,745	$2,690,012	$2,086,710	$3,339,278	$810,484	$689,509

Source: Proxy Statements; Highmark and IBC.

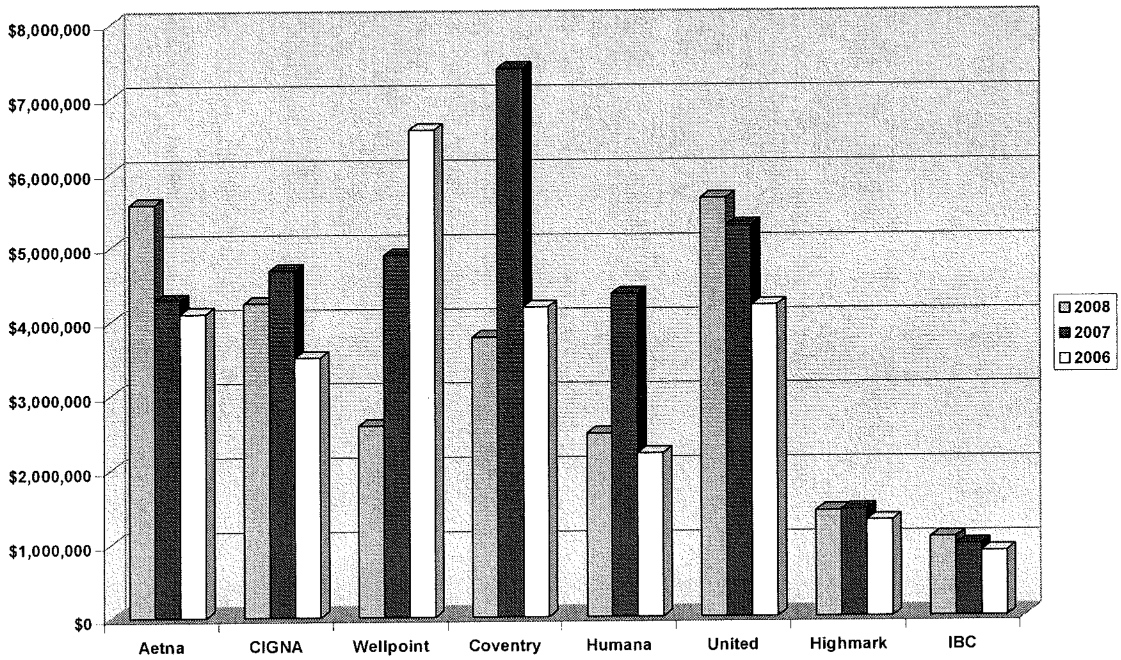
As the above tables indicate, there is a substantial non-profit/for - profit compensation differential for the non-CEO executives just as there is for the CEO's.

The following charts display the total compensation of the four highest-paid Highmark, IBC, and for - profit health insurer non-CEO executives graphically.

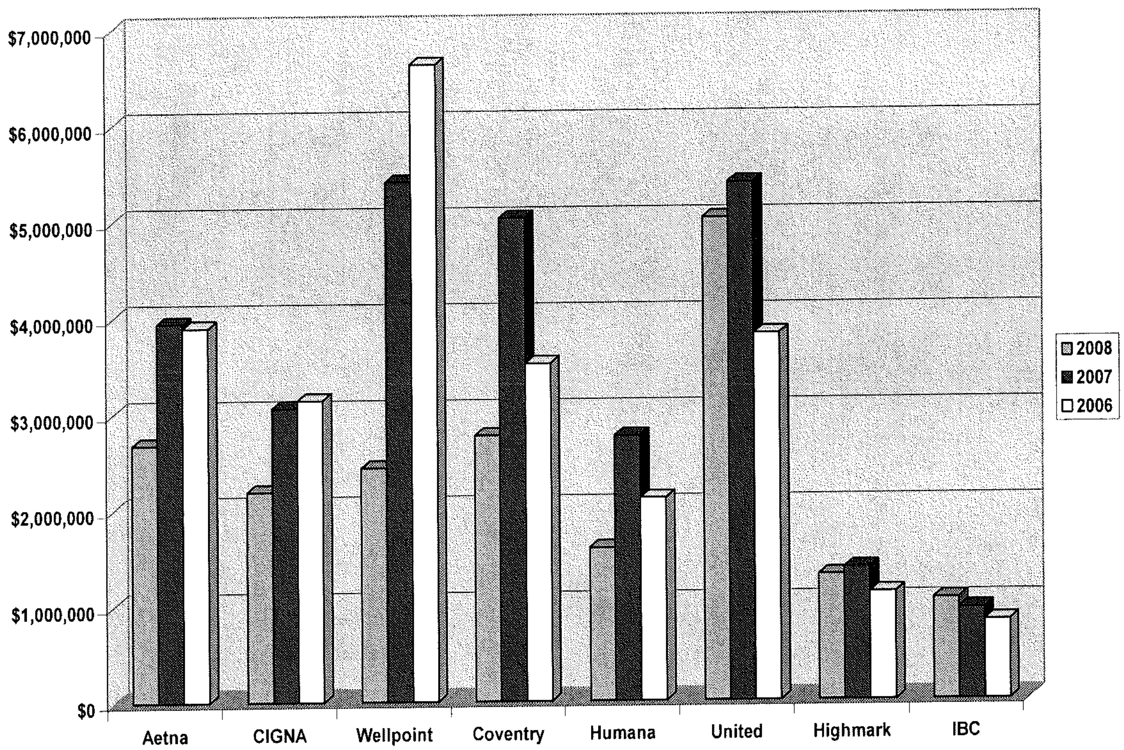
#2 Executive Total Compensation, Highmark and IBC v. For-Profit Health Insurers, 2006-2008



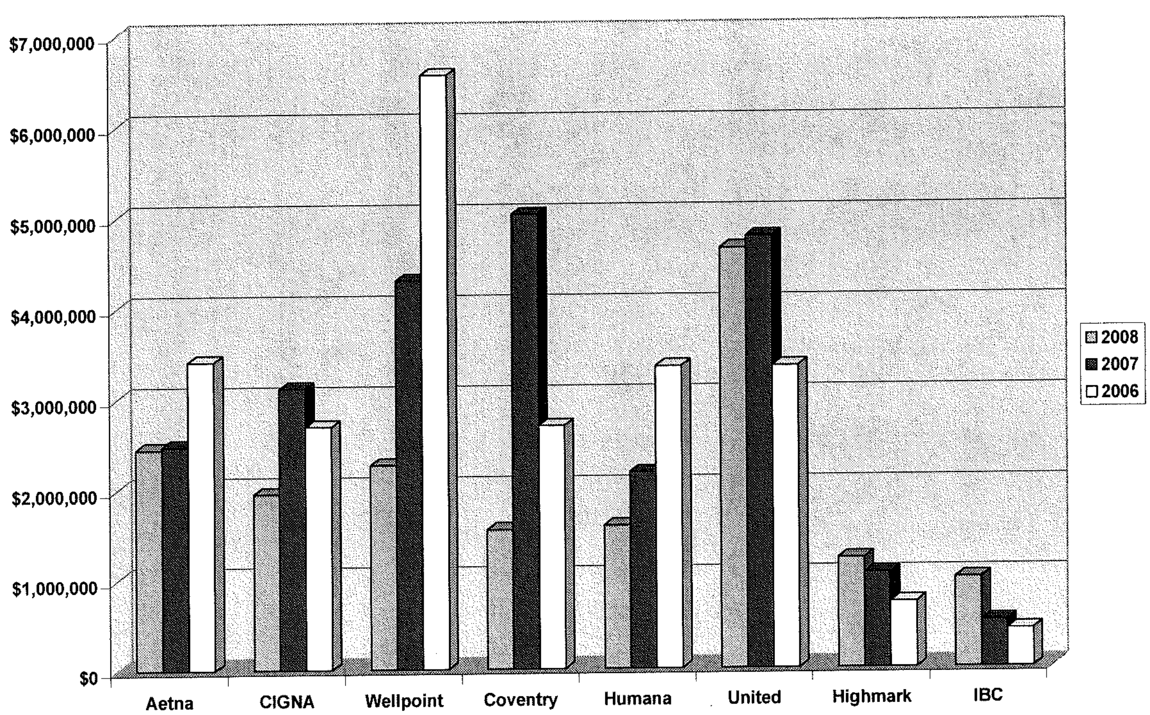
#3 Executive Total Compensation, Highmark and IBC v. For-Profit Health Insurers, 2006-2008



#4 Executive Total Compensation, Highmark and IBC v. For-Profit Health Insurers, 2006-2008



#5 Executive Total Compensation, Highmark and IBC v. For-Profit Health Insurers, 2006-2008



2. Large non-profit organizations?

The compensation of the Highmark and IBC executives could also be compared to that of executives of other non-profit organizations. Like other non-profit organizations, Highmark and IBC have no duty to operate in such a way as to increase shareholder value; to the contrary, they have a legal duty to serve their non-profit purposes and to operate as charitable and benevolent institutions. See Pa. C.S.A. §§ 6101, 6103(b), 6302, 6307(b).

Several organizations survey the compensation of non-profit executives each year. According to the most recent available data, the highest paid CEO's of various types of non-profits in 2007 were as follows:

Table 21

Highest Paid Non-Profit CEO's, By Type of Non-Profit, 2007

Type of Non-Profit	CEO Compensation	Name of Organization
Education	$2,065,143	Vanderbilt University
Religion	$1,520,000	Inspiration Network
Arts, Culture, Humanities	$1,203,145	Metropolitan Opera
Health	$991,190	Scripps Research Institute
Public Benefit	$908,927	Jewish Community Federation of Cleveland
International	$654,500	Council on Foreign Relations
Animals	$618,101	Wildlife Conservation Society
Human Services	$589,143	Boy Scouts of America National Council
Environment	$427,465	The Nature Conservancy.

Source: For Education, Annual Executive Compensation Survey by the Chronicle of Higher Education, as reported in "College Campuses Debate Administrators' Lofty Pay," Business Week, Feb. 16, 2009. For Religion, 2007 federal tax return of The Inspiration Network, as reported in "Surging Ministry, Growing Questions," Charlotte Observer, May 23, 2009. For all other data, Charity Navigator, 2008 CEO Compensation Study, August 1, 2008, available at www.charitynavigator.org.

The Chronicle of Philanthropy also conducts an annual survey of non-profit organization compensation. While its findings regarding non-profit CEO compensation are generally in line with those of Charity Navigator, it also lists the compensation of employees of non-profit organizations whose compensation exceeds that of the CEO. The 20 highest-paid such people were the following:

Table 22

Non-Profit Employees Earning More Than Their CEO

Organization	Employee	2007 Compensation
Columbia University (New York)	David N. Silvers, Clinical Professor of Dermatology	$4,301,018
University of Southern California (Los Angeles)	Peter Carroll, Head Coach, Football	$3,953,648
Cornell University (Ithaca, NY)	Zev Risebwaks, Professor	$3,101,231
New York University	James Grifo, Professor, Obstetrics and Gynecology	$2,362,270
Duke University (Durham, NC)	Mike Krzyzewski, Head Coach, Men's Basketball	$2,180,409
Partners HealthCare System (Boston)	Jon P. Warner, Surgeon	$2,068,606
Yale University (New Haven, CT)	David F. Swensen, Chief Investment Officer	$2,041,270
University of Pennsylvania (Philadelphia)	Arthur Rubenstein, Executive Vice President	$1,817,214
Stanford University (California)	Frank Hanley, Professor of Cardiothoracic Surgery	$1,735,417
University of Chicago	James L. Madara, Dean of the Biological Sciences	$1,327,390
University of Notre Dame (Indiana)	Scott C. Malpass, Chief Investment Officer	$1,242,998
John F. Kennedy Center	Leonard Slatkin, Music Director, National	$1,232,467
The Johns Hopkins University (Baltimore)	Henry Brem, Professor of Neurosurgery	$1,185,317
Washington University in St. Louis	Roberta Sengelmann, Professor of Medicine	$1,171,748
J. Paul Getty Trust (Los Angeles)	James Williams, Chief Investment Officer	$1,058,340
Cystic Fibrosis Foundation (Bethesda, MD)	C. Richard Mattingly, Chief Operating Officer	$1,054,698
Ford Foundation (New York)	Linda Strumpf, Vice President	$1,035,841
William and Flora Hewlett Foundation (Menlo Park, CA)	Laurance R. Hoaland Jr., Chief Investment Officer	$1,012,135
Duke Endowment (Charlotte, NC)	Jeffrey French, interim Chief Investment Officer	$1,002,400
John D. and Catherine T. MacArthur Foundation (Chicago)	Susan Manske, Chief Investment Officer	$988,465

Source: The Chronicle of Philanthropy, October 2, 2008.

As the above table indicates, most of those on the above list are either medical school professors, coaches, or chief investment officers.

As the two preceding tables indicate, compensation of the Highmark and IBC CEO's substantially exceeds the compensation of the CEO's of most of the non-profit organizations surveyed by Charity Navigator or the Chronicle of Philanthropy. As noted in section IIA, supra, however, Highmark and IBC are not the same type of non-profit as these other non-profits.

3. Non-profit hospitals and hospital systems?

A closer set of comparables to Blue Cross plans than non-profit organizations in general are large non-profit hospital systems in and around Pennsylvania. Both the Blues and such hospitals are non-profit; both are major institutions in the region; both are in the health care business; and both compete with for - profit entities.

The table below sets forth the 2006 compensation of the five highest paid employees of Highmark and IBC and of eight of the larger and better-known hospital systems in and around Pennsylvania, including the two largest in the Philadelphia area—Jefferson Health System and the University of Pennsylvania—and the largest in the Pittsburgh area—UPMC. Compensation for 2006 rather than 2007 was used in all cases because 2007 compensation is not yet available for the hospital systems.

Table 23

2006 Total Compensation, 5 Highest Paid Employees: Leading PA Hospital Systems v. Highmark and IBC

Executive	UPMC	Virtua	Penn*	CHOP	Jefferson Health System	Geisinger	Cooper Health	Temple	Highmark	IBC
CEO	$4,012,329	$3,371,663	$3,455,767	$2,060,574	$1,741,709	$1,720,052	$1,016,474	$1,010,097	$3,156,825	$1,637,754
#2	$1,341,435	$1,549,970	$2,314,931	$1,266,901	$738,793	$822,302	$1,089,571	$763,179	$1,595,557	$1,311,735
#3	$1,278,610	$1,358,580	--	$1,085,411	$686,775	$729,506	$873,372	$580,465	$1,287,895	$869,341
#4	$1,164,710	$1,288,997	--	$818,825	$408,863	$699,803	$825,578	$572,486	$1,118,822	$819,285
#5	$1,159,988	$1,198,928	--	$775,617	$124,282	$670,540	$793,434	$493,858	$1,020,800	$689,509

Source: 2006 Form 990's; Highmark and IBC.

*The University of Pennsylvania Health System and School of Medicine do not file separate tax returns. The CEO of UPHS and the Dean of the School of Medicine, whose compensation is set forth above, are included on the University's Form 990.

In addition, in February 2009 the IRS published a report that analyzed both the community benefit activities and the executive compensation of non-profit hospitals. The

IRS calculated the average compensation both of the CEO's of all 421 hospitals which responded to its questionnaire, and of the CEO's of 20 hospitals which it selected based on their responses to the questionnaire. Those hospitals were generally larger hospitals which paid their executives higher amounts than other similarly-sized hospitals. The IRS found that the average compensation for the CEO's of all the hospitals responding to its questionnaire was $490,431, and that the average compensation for the CEO's and CFO's of the 20 hospitals it examined was $1,381,274 and $571,152 respectively.

The IRS also found that the average compensation of nonprofit hospital CEO's increased as hospital size increased, as the following table indicates:

Table 24

Compensation of Non-Profit Hospital CEO's, by Hospital Size

Hospital Size (Revenues)	Avg. CEO Compensation
< $25 million	$171,000
$25 million to $100 million	$338,000
$100 million to $$250 million	$554,000
$250 million to $500 million	$791,000
> $500 million	$1,092,000

Source: IRS Report on Nonprofit Hospitals, Feb. 12, 2009.

The substantial difference between the IRS data and the individual Pennsylvania data set forth in Table 23 may be due to the fact that the IRS surveyed individual hospitals, whereas the Table 23 data is all hospital system data. In any event, the compensation of the Highmark and IBC executives appears to be in line with that of major hospital systems executives, and substantially higher than that of individual hospital executives.

4. Medicare and Medicaid?

A fourth possible universe to which Highmark and IBC could be compared is that of administrators of health insurance benefits. The largest such administrators are each state's Medicaid program and the federal Medicare program. The administrator of the federal Medicare program is the administrator of the Center for Medicare and Medicaid Services. The current maximum annual compensation for that position is $177,000. The administrators of each of the state Medicaid programs are all state employees; all state Medicaid program directors earn less than $200,000, and many earn less than $100,000. There are obviously significant differences between the administrators of Medicare and Medicaid and the CEO's of Highmark and IBC: most fundamentally, Medicare and Medicaid are government entities, and Highmark and IBC are not. On the other hand, the Blues, Medicare and Medicaid all provide health care benefits to individuals, and they all pay health care providers. Highmark and IBC thus do have some of the same characteristics that Medicare and Medicaid have.

5. Other Blue Cross plans—the best comparables

Because all Blue Cross plans have some characteristics common to for - profit health plans, some common to large non-profit organizations, and some common to administrators of Medicare and Medicaid, and because they all have similar histories, the best set of comparables for Highmark and IBC may be other Blue Cross plans. Data on Blue Cross executive compensation is more difficult to obtain than executive compensation data for public companies, since non-profit corporations do not file executive compensation data with the SEC. However, in many states all insurers domiciled in the state, whether for - profit or non-profit, must file a special compensation supplement with their Annual Statements which discloses the compensation of the company's ten highest-paid employees. Unlike the SEC, most state insurance departments do not put executive compensation data on line. Nevertheless, most departments do not deem executive compensation data confidential, and a private company, Atlantic Information Services, ("AIS") compiles Blue Cross executive compensation data from the state insurance departments and augments it with data from other sources. The following table sets forth the 2007 compensation of the CEO's of 31 Blue Cross plans covering 45 states, along with the membership of each Blue Cross plan.

Table 25
2007 Compensation – Selected Blue Cross CEO's

Company	CEO	Salary	Bonus	Other	Total	# Members
Health Care Service Corp. (TX, IL, OK, NM)	Raymond McCaskey	1,561,154	8,682,541	44,814	10,288,509	15,000,000
WellPoint, Inc.	Angela Braly[4]	922,269	588,311	7,579,985	9,597,045	25,000,000
	Larry C. Glasscock[5]	570,000	467,628	6,512,392	7,550,020	
Blue Cross Blue Shield of Florida, Inc.	Robert Lufrano, M.D.	936,974	2,500,000	3,778,110	7,215,084	4,300,000
Horizon Blue Cross Blue Shield of New Jersey	William Marino	898,538	4,084,716	0	4,983,254	3,600,000
Highmark Inc. (PA)	Kenneth Melani, M.D.	1,037,630	2,548,701	60,000	3,646,311	4,600,000
Blue Cross Blue Shield of Massachusetts	Cleve Killingsworth	935,481	1,877,642	789,570	3,602,693	3,000,000
Blue Cross & Blue Shield of North Carolina	Robert Greczyn, Jr.	880,000	2,322,014	27,649	3,229,633	2,700,000
Blue Cross and Blue Shield of Alabama	Gary Pope	679,108	1,656,220	253,200	2,588,528	3,600,000
Independence Blue Cross (PA)	Joseph Frick	941,715	1,495,701	150,000	2,587,416	3,400,000
Excellus Health Plan, Inc. (NY)	David Klein	881,937	1,447,716	21,309	2,563,731	2,000,000
HealthNow New York Inc.	Alphonso O'Neil-White	732,000	1,216,820	288,208	2,237,028	815,000
BlueCross BlueShield of South Carolina	Malcom Edward Sellers	393,111	1,555,325	171,080	2,119,516	1,000,000
Wellmark, Inc. (IA, SD)	John Forsyth	800,000	1,234,782	68,099	2,102,881	1,733,000
Premera Blue Cross (WA, AK)	H.R. Brereton Barlow	686,895	1,247,942	136,647	2,071,484	1,515,000
Blue Cross Blue Shield of Michigan	Daniel Loepp	670,000	696,777	290,778	1,657,555	5,000,000
Blue Cross Blue Shield of Arizona	Richard Boals	777,108	0	867,004	1,644,112	1,000,000
Blue Cross Blue Shield of Kansas City	Tom Bowser	707,787	822,534	21,905	1,552,226	880,000
BlueCross BlueShield of Tennessee	Vicky Gregg	778,986	0	758,207	1,537,193	2,300,000
CareFirst, Inc.[6] (MD, DC)	David Wolf	782,803	766,471	0	1,549,274	3,100,000
	Chester Burrell	47,154	0	0	47,154	
Capital BlueCross (PA)	Anita M. Smith	795,585	570,000	19,645	1,385,230	1,000,000
Triple-S Management Corp. (PR)	Ramon M. Ruiz-Comas	541,500	431,000	91,924	1,064,424	1,200,000
Blue Cross and Blue Shield of Rhode Island	James Purcell	558,420	399,312	7,914	965,646	500,000
Blue Cross and Blue Shield of Nebraska	Steven Martin	600,000	185,683	4,951	790,634	717,000
The Regence Group (OR, WA, ID, UT)	Mark Burns Ganz	315,690	451,160	20,190	787,040	3,000,000
Blue Cross of Northeastern Pennsylvania	Denise Cesare	515,364	192,993	20,263	728,620	600,000
Arkansas Blue Cross Blue Shield	Robert Shoptaw	487,696	65,218	62,701	615,615	413,000
Noridian Mutual Insurance Co. (Blue Cross Blue Shield of North Dakota)	Michael Unhjem	354,711	207,435	2,030	564,236	350,000
Blue Cross and Blue Shield of Vermont	William Milnes, Jr.	264,560	204,666	3,686	472,912	300,000
Blue Cross Blue Shield of Wyoming	Timothy Crilly	315,817	137,287	17,973	471,077	100,000
Blue Cross Blue Shield of Delaware	Timony J. Constantine	291,663	174,751	0	466,414	800,000
Blue Cross and Blue Shield of Montana	Sherry Cladouhos	363,219	91,351	9,884	464,454	240,000

[4] Angela Braly was appointed CEO on June 1, 2007. Her "other" compensation includes stock awards worth $2,160,159 and stock-option awards worth $5,240,149.
[5] Larry C. Glasscock retired as CEO on May 31, 2007. His "other" compensation includes stock awards worth $1,377,840 and stock-option awards worth $4,155,120.
[6] David Wolf served as interim CEO and president from late 2006 until Chester Burrell assumed the office on Dec. 1, 2007.
SOURCES: The AIS Report on Blue Cross & Blue Shield Plans, Nov. 2008, at 10, for all companies but Highmark and IBC; Highmark and IBC data has been provided by Highmark and IBC.

a. Actual Highmark and IBC CEO Compensation

Based on the data in the preceding table, and assuming that CEO compensation should increase as the number of members in a plan increases, neither Dr. Melani's nor Mr. Frick's 2007 annual compensation appears to be unreasonable. Dr. Melani's compensation of $3,646,311 was near the top of the pay scale for Blue Cross plans – only four Blue Cross plans pay their CEO more than Dr. Melani – but only three Blue Cross plans have more members than Highmark. And Mr. Frick's 2007 compensation of $2,587,416 ranks ninth among the 31 Blue Cross plans in the table, while IBC is the eighth largest of the 31 Blue Cross plans ranked by number of members. Thus, when compared to the compensation of other Blue Cross CEO's, neither Dr. Melani's nor Mr. Frick's total compensation appears to be excessive.

PART TWO

I. Payments receivable on termination following a Change of Control ("COC") or on remaining with the company throughout the Department's merger review process

Each of the executives has been subject to at least three different agreements regarding the payments he is potentially eligible to receive on termination in connection with a COC and regarding the conditions which would trigger those payments. The executives entered into their first such agreement substantially before the parties signed their merger agreement; they entered into a second agreement on or about the date the parties signed their merger agreement; and they entered into a third agreement--actually an amendment to the second agreement--after the parties withdrew their merger application on January 21, 2009. Their current Highmark agreements expire on December 31, 2009, while the current IBC agreements have no expiration date.

This section discusses the payments that would be payable to the executives on termination following a COC under each of the three different agreements they have entered into.[7] It also discusses the payments that Highmark was legally obligated to make to three different executives if they remained with Highmark until March 31, 2009, and the series of payments IBC was legally obligated to make to one executive by March 28, 2009, whether or not a merger was consummated by that date.

A. The Highmark executives' agreements

Ten of the twelve Highmark executives had letter agreements entitled "Re: Severance" in place substantially before the March 28, 2007 date on which Highmark and IBC formally agreed to merge (hereinafter sometimes referred to as "Old Agreements"). Another executive, James Klingensmith, had an "Executive Employment Agreement" in place long before the Highmark-IBC merger agreement was signed (hereinafter also sometimes referred to as an "Old Agreement"). The twelfth executive, David Holmberg, joined Highmark after Highmark and IBC had agreed to merge.

Under their Old Agreements, the Highmark executives were entitled to certain benefits if they terminated under certain circumstances before or after a COC. At about the time the Highmark-IBC merger agreement was signed, Highmark entered into one or more new letter agreements, in most cases also entitled "Re: Severance" with each of the executives (hereinafter sometimes referred to as "New Agreements"). In some cases, the New Agreements provided for substantially the same benefits as did the Old Agreements. In others, the New Agreements provided for more generous benefits than did the Old Agreements. In all cases, the New Agreements expanded the conditions under which those benefits were payable in connection with a COC. Finally, after the parties

[7] Highmark also entered into a fourth agreement with one executive, as discussed in section IIB2, infra.

withdrew their merger application Highmark entered into an amendment to its new agreement ("Amended New Agreement") with each of the executives which extended the term of the covenant not to compete the executive would be subject to on termination. This section discusses the benefits the twelve Highmark executives would receive and the conditions under which they would receive them under their three different agreements. It also discusses the payments that Highmark was legally obligated to make to three different executives if they remained with Highmark until March 31, 2009, whether or not Highmark had consummated a merger by that date.

1. SERP benefits for all executives

Like most large corporations, Highmark has a standard retirement plan for all its employees, and a separate supplemental plan, called a SERP—for Supplemental Executive Retirement Plan—for a limited number of high-ranking executives and other highly-paid employees. Corporations establish SERPs because the maximum compensation based on which an employee's retirement benefit can be calculated in the company's standard retirement plan, which is tax-advantaged and is known as a "qualified" plan, is currently $245,000. See Int. Rev. Code § 401(a)(7). Highmark's SERP enables executives earning more than $245,000 annually to obtain the same benefits they would have received under its qualified plan had there been no ceiling on those benefits.

Like qualified retirement benefits, an executive's SERP benefit is calculated based on his years of service and his final average compensation: the longer he has worked for the company and the higher his final average compensation, the greater is his SERP benefit. Once vested, the Highmark employees will receive their SERP benefits when their employment with Highmark terminates, regardless of whether that termination occurs in connection with a COC or not in connection with a COC, and regardless of whether they terminate voluntarily, are terminated without cause, or are terminated for cause. The value of the SERP benefit payable to each executive if he terminated on January 1, 2009 is as follows:

Table 27

Highmark Executives: SERP benefit earned as of January 1, 2009

Executive	SERP benefit
Melani	$6,084,000
Klingensmith	$2,509,000
DeTurk	$375,000
Alexander	$1,453,000
O'Brien	$2,610,000
Truitt	$2,413,000
Farbacher	$229,000
Francavilla	$2,466,000
Tabor	$1,713,000
Cain	$1,710,000
Lebish	$286,000
Holmberg	--

2. Dr. Melani, Messrs. Alexander, Truitt, O'Brien, Lebish, Holmberg, and Tabor, and Ms. DeTurk and Ms. Farbacher

Under the Old Agreements, Highmark agreed to provide these executives with certain benefits if they were terminated without cause, or if they resigned due to a Material Change as defined in the Agreement, before or after a COC. The benefits they would receive after a COC included a multiple of their annual salaries (300% for Dr. Melani, 200% for the others except Mr. Tabor, 150% for Mr. Tabor), a full annual bonus for the most recent calendar year and full long-term bonuses for all pending Performance Periods, and life and health insurance benefits, as well as the retiree welfare benefits all employees receive. In addition, they receive the same SERP benefits they would receive if they terminated not in connection with a COC. All the Agreements also contained a covenant not to compete and a non-solicitation clause. Dr. Melani's covenant not to compete and non-solicitation obligation ran for two years, while those of the other executives ran for one year.

Highmark entered into New Agreements with all these executives at about the time the merger agreement was signed, and into Amended New Agreements with each executive after it withdrew its merger application. Table 28 compares the terms of the Old Agreement, New Agreement and the Amended New Agreement of each such executive.

Table 28

Melani, Alexander, Truitt, DeTurk, O'Brien, Lebish, Farbacher, Holmberg and Tabor: Benefits potentially receivable on termination

	Under Old Agreement	Under New Agreement	Under Amended New Agreement
When payable:	If terminated without cause or terminates due to Material Change, before or after COC	No Change	No Change
Salary	300% (1) 200% (2), (3) 150% (4)	300% (1) 200% (2) 150% (4) 100%-300%, depending on compliance with non-compete (3) (under 10/08 amendment)	No Change – (1), (2), (4). 200% (3)
AEIP	last full calendar year plus pro-rated for year of termination	No Change	No Change
LTIP	no COC: entitled to pro-rated awards for pending LTIP periods in which executive has participated for at least 12 mos.; after COC: all awards for pending periods considered vested and earned	Pursuant to Nov. 2008 amendment to LTIP document: no COC: No Change; after COC: LTIP for periods beginning on or after January 1, 2009 pro-rated.	No Change
Health benefits	COBRA premiums for 18 months	No Change	No Change
Life ins. benefits	lump sump = 18 mos. of premiums	No Change	No Change
SERP	no COC, qualify even if < 55, but need 5 yrs service, receivable at 55; after COC: same as above if < 55, if >55, don't need 5 yrs. service	No Change*	No Change

Retiree welfare benefits	If 10+ yrs. svc, Retiree Welfare Plan benefits receivable at 55	If 10+ yrs service and >55, receivable. If 10+ yrs svc, < 55, lump sum = present value of cost of hlth cvg	No Change
Non-solicitation:	2 years (1) 1 year (2), (3), (4)	No Change	No Change
Non-compete:	2 years (1) 1 year (2), (3), (4)	2 years (1) 1 year (2), (4) 0-3 years, at executive's option (3) (under 10/08 amendment)	3 years (1) 2 years (2) (3) 18 mos. (4)
Definition of "Material Change":	(1) reduction in base salary; (2) reduction in AEIP or LTIP target percentage; (3) reduction of > 10% in potential bonuses; (4) material reduction in benefits.	No Change, plus after a COC: (5) substantial reduction or reassignment of duties; (6) relocation > 50 miles.	No Change
Consulting svcs required?	No (1) (2) (3) (4)	No (1) (2) (4) 18 hrs./wk for 3 mos (3) (under 10/08 amendment)	No (1) (2) (3) (4)

Note: (1) = Dr. Melani
(2) = Messrs. Alexander, O'Brien, Lebish, and Holmberg, Ms. DeTurk and Ms. Farbacher
(3) = Mr. Truitt
(4) = Mr. Tabor

* On Dec. 15, 2008, Highmark informed the PID that for Dr. Melani, Mr. Alexander and Mr. Truitt it had reduced the so-called "early retirement reduction factor" on the basis of which the SERP benefit is calculated from 6% to 2%, and that the reduction in this factor had the effect of increasing Mr. Alexander's SERP benefit by $443,545, Mr. Truitt's SERP benefit by $492,184, and Dr. Melani's SERP benefit by $2,114,000, assuming a severance date of April 1, 2009.

As Table 28 indicates, the New Agreements of all the executives except Mr. Truitt set forth the same payments and covenants as did the Old Agreements, but expand the conditions under which the payments are payable by broadening the definition of Material Change.[8] Specifically, under the terms of their Old Agreements the executives are entitled to receive the payments described therein if their compensation is reduced after a Change of Control and they resign, but not if their responsibilities are reduced or re-assigned and they resign; the New Agreements make them eligible for such payments under both sets of circumstances.[9]

[8] In the New Agreement column, Table 28 also reflects an amendment to Mr. Truitt's New Agreement that he entered into on October 23, 2008. This is a different amendment than his Amended New Agreement, and is discussed in section IIB2, infra.

[9] It should be noted that the New Agreements of all these executives except Mr. Tabor expressly provide that they will receive LTIP bonuses, a SERP payment and retiree welfare benefits. Mr. Tabor's agreement

In addition, in the Amended New Agreements Highmark increased the term of the covenant not to compete so that it matched the number of years salary the executive would receive on termination in connection with a COC. Thus, Dr. Melani would receive 300% of his salary on such termination and would be prohibited from competing with Highmark for three years, rather than two years as under his New Agreement; Messrs. Alexander, Truitt, O'Brien, Lebish, and Holmberg, Ms. DeTurk and Ms. Farbacher would receive 200% of their salary on such termination and would be prohibited from competing with Highmark for two years, rather than one year as under their New Agreements; and Mr. Tabor would receive 150% of his salary on such termination and would be prohibited from competing with Highmark for 18 months, rather than one year as under his New Agreement.

Although Highmark and IBC withdrew their merger applications, the agreements of the nine executives discussed in this subsection continue to entitle them to receive, if they are terminated without cause or they resign due to a Material Change in connection with a COC occurring before January 1, 2010,[10] the same payments they would have received on termination in connection with a Highmark-IBC merger. Table 29 sets forth the value of each benefit each of those executives is eligible to receive under his Amended New Agreement and in accordance with the various plan documents if he is terminated without cause or resigns due to a Material Change after a COC, assuming that a COC occurred and the executive resigned on January 1, 2009.

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does not expressly so provide, but the LTIP and SERP plan documents entitle him to those benefits, and he is automatically entitled to retiree welfare benefits by reason of his status as a Highmark employee. As a result, he is eligible for the same benefits as the other executives, except that his salary multiple is 150% rather than 200% or 300%.

[10] All the Highmark Amended New Agreements—the executives' current agreements—expire on December 31, 2009. The benefits potentially payable to an executive following a COC occurring after January 1, 2010 would be governed by whatever agreement Highmark and the executive enter into which becomes effective January 1, 2010.

Table 29

9 Highmark Executives: Payments on Termination Without Cause or due to a Material Change in connection with a COC

Executive (multiple)	Base salary x multiple	Annual bonus '08	Annual bonus '09 pro-rated	Full LT bonus '07-'09	Full LT bonus '08-'10	Pro-rated LT bonus '09-'11	Life & health insurance benefits	RWB's **	Total
Melani (3)	$3,300,303	$910,142	*	$1,012,752	$1,130,795	*	$21,011		$6,375,003
DeTurk (2)	$960,784	$291,456	*	$367,772	$389,838	*	$18,285		$2,028,135
Alexander (2)	$979,692	$297,192	*	$337,754	$344,509	*	$18,285		$1,977,432
O'Brien (2)	$891,808	$274,759	*	$306,253	$318,504	*	$21,011		$1,812,335
Truitt (2)	$900, 156	$223,416	*	$226,781	$231,318	*	$21,011		$1,602,682
Farbacher (2)	$549,988	$106,171	*	$109,391	$111,579	*	$21,011		$898,140
Tabor (1.5)	$526,086	$135,410	*	$125,873	$132,554	*	$18,285		$938,208
Lebish (2)	$804,590	$213,170	*	$236,593	$264,118	*	$21,011		$1,539,482
Holmberg (2)	$960,000	$455,763	*	--	--	*	$27,515		$1,443,278

*The figures in this table are based on the assumption that a COC occurs and the executive terminates on January 1, 2009. Under this assumption, because the executive receives pro-rated bonuses for the year of termination, the executive's annual bonus for 2009 and his long-term bonus for 2009-11 are negligible: his annual bonus for 2009 would be 1/365 of a full annual bonus, and his long-term bonus for 2009-2011 would be 1/1095 of the full long-term bonus. The later in 2009 a COC occurred and the executive resigned, the higher his 2009 annual bonus and 2009-11 long-term bonus would be.

** These are the same retiree welfare benefits receivable by all Highmark employees.

Source: For Base Salary, Summary Compensation Tables; for 2008 Annual Bonus, new data submitted by Highmark in April 2009; for 2007-09 LT Bonuses and Life and Health Insurance benefits, Towers Perrin Tables accompanying the Oct. 31, 2008 e-mail from Jacki Bauer (hereinafter "Towers Perrin Tables").

3. Mr. Cain and Mr. Francavilla

Unlike the other executives, Messrs. Cain and Francavilla entered into a separate Retention Agreement as well as a New Agreement at about the time Highmark and IBC agreed to merge. Their Old, New, and Amended New Agreements are identical to those of Mr. Tabor, and thus entitle them to the same payments and benefits as Mr. Tabor--e.g., 150% of salary on termination without cause or resignation due to a Material Change after a COC. And like Mr. Tabor's Amended New Agreement, Cain's and Francavilla's Amended New Agreements prohibit them from competing with Highmark for 18 months, rather than for only one year as under their New Agreements. In addition, as Table 30 indicates, their Retention Agreements entitled them to another 100% of salary if they remained with the company until the earlier of March 31, 2009 or the consummation of the Highmark-IBC merger; or if they terminated without cause or they terminated due to a Material Change before March 31, 2009.

Table 30
Ronald Cain and Gino Francavilla:
Benefits potentially receivable on termination

	Under Old Agreement	Under New Agreement Plus Retention Agreement	Under Amended New Agreement
When payable:	If terminated without cause or terminates due to Material Change, before or after COC	All benefits except retention bonus and gross-up payment: same. Retention bonus and gross-up payment: (1) stay until earlier of March 31, 2009 or closing, or (2) terminated w/o cause or terminates for Good Reason before 3/31/09.	No Change
Salary	150%	150% (sev. agreement) plus 100% (ret. agreement)	No Change
AEIP	last full calendar year plus pro-rated for year of termination	No Change	No Change
LTIP	no COC: entitled to pro-rated awards for pending LTIP periods in which executive has participated for at least 12 mos.; after COC: all awards for pending periods considered vested and earned	Pursuant to Nov. 2008 amendment to LTIP document: no COC: No Change; after COC: LTIP for periods beginning on or after January 1, 2009 pro-rated.	No Change
Health benefits	COBRA premiums for 18 months	No Change	No Change
Life ins. benefits	lump sump = 18 mos. of premiums	No Change	No Change
SERP	no COC, qualify even if < 55, but need 5 yrs service, receivable at 55; after COC: same as above if < 55, if >55, don't need 5 yrs. service	No Change	No Change
Retiree welfare benefits	If 10+ yrs. svc, Retiree Welfare Plan benefits receivable at 55	If 10+ yrs service and >55, receivable. If 10+ yrs svc, < 55, lump sum = present value of cost of hlth cvg, plus any early retirement benefits authorized < 6 mos. after termination	No Change
Gross-up payment (§ 4999 parachute tax plus tax thereon)	None	Receivable if Highmark finds payment is 280G excess parachute payment, thus triggering the 4999 excise tax, unless reducing aggregate payments by 10% or less avoids the 4999 tax	No Change
Non-compete and non-solicitation:	1 year	No Change	18 mos.
Definition of "Material Change":	(1) reduction in base salary; (2) reduction in AEIP or LTIP target percentage; (3) reduction of > 10% in potential bonuses; (4) material reduction in benefits.	No Change, plus after a COC: (5) substantial reduction or reassignment of duties; (6) relocation > 50 miles.	No Change

Notably, their Retention Agreements provide that Cain and Francavilla will be terminated on the earlier of March 31, 2009, or the consummation of the merger. Following their termination, they will receive most, though not all, of the benefits they would have received had they terminated following a COC. For example, both on termination following a COC and on termination on March 31, 2009 not in connection with a COC, 250% of their base salary plus their annual bonus for the current year pro-rated to their termination date become payable. However, whereas on termination in connection with a COC they would have received full long-term bonuses for the 2007-2009 and 2008-2010 Performance Periods, on termination not in connection with a COC they receive pro-rated bonuses for those periods. In addition, because under the LTIP document they must be employed for at least 12 months of a Performance Period in order to receive any long-term bonus, they will not receive any long-term bonus for the 2009-2011 Performance Period upon their March 31, 2009 termination.[11]

Table 31 sets out the value of each benefit payable to Mr. Cain and Mr. Francavilla following their March 31, 2009 termination.

[11] The Cain and Francavilla Retention Agreements also contain an additional provision that could have had an effect only in connection with a COC. Specifically, they require Highmark to pay Cain and Francavilla the amount of any excise tax Highmark determines they would be legally obligated to pay had the payments they would have received on COC constituted an "excess parachute payment" within the meaning of section 280G of the Internal Revenue Code. As more fully explained in section IIA, infra, any payment contingent on a COC which exceeds three times the recipient's average annual compensation over the previous five years--referred to in the Code as the "base amount"-- is considered an "excess parachute payment" under section 280G of the Code. IRC §280G(b). Such payments are not deductible as reasonable compensation by the corporation to the extent that they exceed the individual's average annual compensation over the last five years. IRC §§280G(a), 280G(b)(1). Highmark agreed to pay Cain and Francavilla an amount that would enable them to retain the full amount of their payments after they pay any excise tax triggered by the receipt of such payments, with one exception: if reducing Highmark's payments to Cain or Francavilla by 10% or less would cause those payments to be less than their base amounts, and would thus eliminate any liability for any parachute tax, then Highmark could reduce its payments by the amount necessary to eliminate the parachute tax.

Table 31

Cain and Francavilla: Payments on March 31, 2009 Termination

Executive (multiple)	Base salary x multiple	Annual bonus '08	Annual bonus '09 pro-rated	LT bonus '07-'09 Pro-rated as of 3/31/09	LT bonus '08-'10 Pro-rated as of 3/31/09	LT bonus '09-'11 Pro-rated as of 3/31/09	Retention bonus	SERP benefit *	Life & health insurance benefits	RWB's ****	Total
Francavilla (1.5)	$585,245	$141,912	$35,478 **	$95,439	$53,694	0 ***	$390,163	$2,628,580	$22,331		$3,952,842
Cain (1.5)	$459,959	$95,121	$23,780 **	$63,500	$36,098	0 ***	$306,639	$1,896,936	$22,331		$2,904,364

*N.B.: The SERP benefit has been fully earned. It is payable on termination whether or not a COC has occurred. The SERP values shown here are greater than the SERP values in Tables ES9 and 27A because the values in this table are based on a termination date of March 31, 2009 rather than January 1, 2009.

**Three months (i.e., 1/4) of an annual bonus for 2009, assuming 2009 bonus is equal to 2008 bonus.

***Executive receives no LT bonus for 2009-11 Performance Period because he has not worked for Highmark for at least 12 months during that Period, as he is required to do to receive a LT bonus.

****These are the same retiree welfare benefits receivable by all Highmark employees.

Source: For Base Salary and Retention Bonus, Summary Compensation Tables; for annual and long term bonuses, new data submitted by Highmark in April 2009; for Life and Health Insurance benefits, Towers Perrin Tables; for SERP benefit, Dec. 2, 2008 and Dec. 15, 2008 Presentations by Steve Wall.

4. Mr. Klingensmith

Mr. Klingensmith's agreements with Highmark are the most complex and also the most generous of any of the executives' agreements. While like the other executives he entered into both an Old Agreement and a New Agreement, unlike those of the other executives his New Agreement also provides for a retention bonus (the Cain and Francavilla retention bonuses were provided for in a separate agreement). Further, Mr. Klingensmith's New Agreement is not a stand-alone document but rather sets forth new language to take effect and old language to be deleted from his Old Agreement. Accordingly, Table 32 both sets forth the payments authorized by Mr. Klingensmith's Old Agreement, New Agreement and Amended New Agreement and includes citations to the Old Agreement and New Agreement paragraphs authorizing each payment.

Table 32

James Klingensmith: Benefits potentially receivable on termination

	Under Old Agreement	Under New Agreement	Under Amended New Agreement
When payable:	If terminated without cause at any time, or terminates for Good Reason after a COC (5.7)	All benefits except 300% of salary: If terminated without cause at any time (new 5.7) terminates for Good Reason at any time (new 5.7), or terminates without Good Reason at any time (new 5.6). 300% of salary: if (1) stays until earlier of March 31, 2009 or closing, or (2) is terminated without cause before March 31, 2009 or Highmark withdraws from the transaction (new 4.6).	No Change
Salary	150% (5.5.1), plus gross-up payment for all taxes payable thereon (5.5.1)	No Change (new 5.5.1), plus 300% if (1) stays until earlier of March 31, 2009 or closing, or (2) is terminated without cause before March 31, 2009 or Highmark withdraws from the transaction (new 4.6).	No Change
LTIP	None	No COC: LTIP for periods beginning on or after Jan. 1, 2007 pro-rated After COC: LTIP for periods beginning on or after Jan 1, 2009 pro-rated (new 5.5.1, new 5.1.4, new 4.5, LTIP plan document)	No Change
STIP	Pro-rated STIP in year of termination, equal to minimum of 20% of base salary (5.5.4, 4.4)	No Change (new 5.5.1, 5.1.3, 4.4)	No Change
Supplemental pension benefits	((Total QRP + SERP + DCSP* benefits, including add'l 18 mos. and assumed vested) – pension payable for credited service as of retirement date), plus gross-up payment for all taxes payable on the add'l 18 mos. (Sched. A p. 10)	No Change	No Change

Non-qualified deferred comp:	Contributions under QSP and DCP**, including add'l 18 mos. (Sched. A p. 11, 5.5.1)	Lump sum = ER match receivable had he worked another 18 mos. = 3.3% of (base salary + AIP) for 18 mos. (new 20, Sched. A p. 11)	No Change
Employee welfare benefits	Health and Life ins. coverage for 18 mos., retiree welfare benefits calculated based on additional 18 mos., gross-up payment for all taxes payable on above (Sched. A p. 11)	No Change (new 5.5.2), plus any increase in retirement benefits Highmark implements within 6 mos. after term. (new 4.7)	No Change
Gross-up payment: (§ 4999 parachute tax plus tax thereon)	None	Receivable if Highmark finds any payment is 280G excess parachute payment, thus triggering the 4999 excise tax (new 8)	No Change
Non-compete:	6 mos. (9a) to 18 mos. (9b), depending on whether 150% of salary taken in lump sum or ratably over 18 mos.	18 mos. (new 7(d))	2 years
Non-solicitation	None	18 mos. (new 7(c))	
Definition of "Good Reason":	(1) diminished responsibilities; (2) removal from position; (3) reduction in base salary; (4) failure to increase base salary by co-wide avg.; (5) reduction in benefits; (6) relocation >25 miles(5.7)	No Change	No Change

*QRP = Qualified Retirement Plan
DCSP = Deferred Compensation Supplement Plan
Highmark no longer includes DCSP benefits in calculating supplemental pension benefits.

**QSP = Qualified Savings Plan
DCP = Deferred Compensation Plan
Highmark no longer includes QSP benefits in calculating non-qualified deferred compensation.

As Table 32 indicates, on termination in connection with a COC under his Old Agreement Mr. Klingensmith would receive 150% of his salary, a pro-rated short term bonus, supplemental pension benefits calculated as if he had worked an additional 18 months, deferred compensation benefits calculated as if he had worked an additional 18 months, health and life insurance coverage for 18 months, and retiree welfare benefits calculated as if he had worked an additional 18 months. In addition, he would receive a gross-up payment equal to the taxes he would pay both on his health and life insurance benefits and on the increase in his supplemental retirement benefit, so that he would retain the net amount of each such benefit.

Mr. Klingensmith's New Agreement includes substantially these same benefits, but in addition provides that he will receive another 300% of salary if he remains with the company until the earliest of (1) March 31, 2009; (2) the closing of the Highmark-IBC merger; (3) his termination without cause; or (4) Highmark's withdrawal from the Highmark-IBC merger agreement. That 300% of salary is payable 30 days after the triggering event. Thus, because Highmark and IBC withdrew their application on January 21, 2009, and officially terminated their consolidation agreement on March 6, 2009, under the terms of his New Agreement Highmark was required to pay Klingensmith 300% of his salary by April 5, 2009. Had the Highmark-IBC merger been approved, Highmark would have been required to pay Klingensmith 300% of his salary 30 days after the approval.

Notably, Mr. Klingensmith's New Agreement provides that he will receive another 150% of his salary, plus the other payments it authorizes, if he resigns from the company <u>at any time and for any reason</u>. The Klingensmith New Agreement includes this unusual provision because his Old Agreement allowed him to terminate and receive the payments authorized by the agreement not only if his responsibilities were reduced but also if his base salary were increased by less than the company-wide average. Because in one year his base salary was so increased, Mr. Klingensmith already had the legal right to terminate and collect the payments set forth in his Old Agreement before he signed his New Agreement.

Mr. Klingensmith resigned from Highmark on March 31, 2009. He thereby became eligible for the same benefits he would have received had the Highmark-IBC merger been approved on January 1, 2009 and he had resigned thereafter, except that, like Messrs. Cain and Francavilla, he receives pro-rated long-term bonuses for the 2007-2009 and 2008-2010 Performance Periods, rather than the full long-term bonuses he would have received for those Performance Periods had there been a COC. Unlike the Cain and Francavilla New Agreements, Mr. Klingensmith's New Agreement guarantees him a minimum payment of $385,500 for each Performance Period for which he becomes vested by March 31, 2009. However, because like Cain and Francavilla he was employed for only three months of the 2009-2011 Performance Period, and because the LTIP document requires an executive to be employed for at least 12 months of a Performance Period to receive any award for that Period, his long-term bonus for the 2009-2011 Performance Period has not vested, and thus he receives no long-term bonus for the 2009-2011 Performance Period.[12]

Finally, Mr. Klingensmith's Amended New Agreement extends the term of his covenant not to compete from 18 to 24 months.

Table 33 sets forth the benefits payable to Mr. Klingensmith upon his March 31, 2009 termination.

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[12] Had Mr. Klingensmith terminated in connection with a COC, he would have received a full gross-up payment if the payments to him that were contingent on a COC had constituted a 280G excess parachute payment. Unlike the Cain and Francavilla New Agreements, the Klingensmith New Agreement entitles the executive to all payments set forth in the agreement even if they exceed the 280G excess parachute payment threshold and even if by reducing those payments only slightly Highmark could both avoid any excise tax and fully deduct those payments.

Table 33

Klingensmith: Payments on March 31, 2009 Termination

Executive (multiple)	Base salary x multiple	Annual bonus '08	Annual bonus '09 pro-rated	LT bonus '07-'09 Pro-rated as of 3/31/09	LT bonus '08-'10 Pro-rated as of 3/31/09	LT bonus '09-'11 Pro-rated as of 3/31/09	Retention bonus	SERP benefit *	Life & health insurance benefits	RWB's	Total ******
Klingensmith (1.5)	$1,020,600	$325,238	$81,310 **	$290,238	$165,438	0 ***	$2,041,200	$2,947,303 ****	$46,418 ****	*****	$6,917,745

*N.B.: The SERP benefit has been fully earned. It is payable on termination whether or not a COC has occurred. The SERP values shown here are greater than the SERP values in Tables ES9 and 27A because the values in this table are based on a termination date of March 31, 2009 rather than January 1, 2009.

**Three months (i.e., 1/4) of an annual bonus for 2009, assuming 2009 bonus is equal to 2008 bonus.

*** Executive receives no LT bonus for 2009-11 performance period because he has not worked for Highmark for at least 12 months during that period, as he is required to do to receive a LT bonus.

****Includes 40% tax gross-up and is calculated as if executive had worked an additional 18 months.

*****Executive receives the same retiree welfare benefits receivable by all Highmark employees, except calculated as if executive had worked an additional 18 months.

******Includes additional $47,027 of deferred compensation benefits calculated as if executive had worked an additional 18 months.

Source: For Base Salary and Retention Bonus, Summary Compensation Tables; for annual and long-term bonuses, new data submitted by Highmark in April 2009; for SERP benefit and Life and Health Insurance benefits, Dec. 2, 2008 and Dec. 15, 2008 presentations by Steve Wall.

B. The IBC executives' agreements

Like the Highmark executives, the IBC executives entered into three different agreements--an Old Agreement, a New Agreement, and an Amended New Agreement--regarding the payments they would be entitled to on termination and the conditions under which they would be entitled to such payments. This section compares the benefits the IBC executives would be entitled to on termination following a COC, and the conditions under which they would be entitled to them, under those three agreements. It also discusses the payments that IBC was legally obligated to make to one executive if she remained with IBC until March 28, 2009, whether or not the merger was consummated by that date.

1. SERP benefits for all executives

Like Highmark and most other large corporations, IBC has a standard, qualified retirement plan for all its employees and a Supplemental Executive Retirement Plan, or SERP, for a limited number of high-ranking executives. IBC's SERP, like Highmark's, enables executives earning more than $245,000 annually to obtain the same benefits they would have received under its qualified plan had there been no ceiling on those benefits. Like the Highmark executives, once vested the IBC executives receive their SERP benefits when their employment with IBC terminates regardless of whether that termination occurs in connection with a COC or not in connection with a COC, and regardless of whether they terminate voluntarily, are terminated without cause, or are terminated for cause. The value of the SERP benefit payable to each IBC executive if he terminated on January 1, 2009 is as follows:

Table 33A

IBC Executives: SERP benefit earned as of January 1, 2009

Executive	SERP benefit
Frick	$5,292,000
Butler	$6,761,000
Cashman	$1,307,000
Tufano	$700,000
Haggett	$2,037,000
Udvarhelyi	$2,058,000
Bright	$520,000

2. Mr. Frick and Mr. Butler

Mr. Frick's and Mr. Butler's Old Agreements provided them with 200% of their annual salary, an annual bonus for the most recent year, a pro-rated long-term bonus for the Performance Period ending in the year of termination, and five years of life and health insurance benefits if they terminated without cause at any time or resigned for Good Reason, which is defined to include a reduction in responsibilities after a COC.

In their New Agreements, IBC increased the benefits Mr. Frick and Mr. Butler would be entitled to if they were terminated without cause before a COC, and increased them further if they were terminated without cause or resigned for Good Reason after a COC. First, the New Agreements provided that if Mr. Frick or Mr. Butler were terminated without cause before a COC they would receive 200% of their annual bonus plus a pro-rated portion of that bonus for the current year rather than a single bonus as under their original agreements, and they would receive bonuses for all three pending LTIP cycles, pro-rated based on the number of months of each cycle that would have elapsed at termination, rather than receiving only the bonus ending in the year of termination. On the other hand, in one respect the New Agreements provided for less generous benefits than did the Old Agreements; they provided for two years of health and life insurance benefits rather than five years as under the Old Agreements.

Second, the New Agreements provided for additional benefits if Mr. Frick or Mr. Butler were terminated without cause or resigned for Good Reason on or after a COC. Specifically, they authorized payment of 300% of their annual salary, 300% of their annual bonus plus a pro-rated bonus for the year of termination, a pro-rated LTIP bonus for all pending LTIP cycles, and three years of health and life insurance benefits.[13]

Finally, in the Amended New Agreements, IBC increased the term of the covenant not to compete that would apply to Messrs. Frick and Butler so that it matched the number of years salary and bonus they would receive on termination in connection with a COC: they would receive 300% of their salary plus annual bonus on such termination, and would be prohibited from competing with IBC for three years, rather than for only two years as under their New Agreements. Table 34 shows the benefits potentially receivable on termination by Mr. Frick and Mr. Butler under their three different agreements.

[13] It should also be noted that in December 2008 IBC amended the Frick and Butler New Agreements to provide that should they receive payments in connection with a COC that are determined to constitute excess parachute payments within the meaning of section 280G, then those payments would be reduced to the maximum amount at which they would not constitute 280G excess parachute payments.

Table 34
Frick and Butler:
Benefits potentially receivable on termination

	Under Old Agreement	Under New Agreement		Under Amended New Agreement
When payable	If terminated without cause at any time; If resigns for Good Reason during 2-yr. period following COC.	If terminated w/o cause before a COC	If terminated w/o cause in anticipation of COC or during 3-yr. period following COC; If resigns for Good Reason during 2 yr. period following COC	No Change
Salary	200%	200%	300%	No Change
AIP	100% of prior calendar year	200% of > of target or 3-yr. avg. plus yr. of term. pro-rated.	300% of > of target or 3-yr. avg. plus yr. of term. pro-rated.	No Change
LTIP	For cycle ending in yr. of termination, pro-rated	For all pending cycles, pro-rated based on target or actual if available	For all pending cycles, pro-rated based on target or actual if available	No Change
Health benefits	5 years	2 years	3 years	No Change
Life ins. Benefits	5 years	2 years	3 years	No Change
Non-compete	1 year	2 years	No Change	no COC: 2 yrs after COC: 3 yrs
Non-solicitation	2 years	2 years	No Change	no COC: 2 yrs after COC: 3 yrs
Definition of "Good Reason"	(i) reduction in base salary; (ii) reduction in duties and responsibilities; (iii) relocate > 50 miles	N/A	(i) reduction in base salary (ii) material reduction in total target compensation (iii) material reduction in annual or long-term bonus (iv) material reduction in duties and responsibilities (vi) relocate > 50 miles	No Change

Table 35 sets forth the value of each benefit potentially receivable by Messrs. Frick and Butler on termination in connection with a COC under their Amended New Agreement, assuming that a COC occurred and the executive resigned on January 1, 2009.

Table 35

Frick and Butler: Payments on Termination Without Cause or for Good Reason in connection with a COC

Executive (multiple)	Base salary x multiple	Annual bonus '08 x multiple	Annual bonus '09 pro-rated	LT bonus '07-'09, pro-rated	LT bonus '08-'10, pro-rated	LT bonus '09-'11, pro-rated	Life & health benefit	Total
Frick (3)	$2,940,000	$2,940,000	*	$640,167	$326,667	*	$14,378	$6,861,212
Butler (3)	$2,055,000	$1,438,500	*	$357,333	$182,667	*	$14,378	$4,047,878

*The figures in this table are based on the assumption that a COC occurs and the executive terminates on January 1, 2009. Under this assumption, because the executive receives pro-rated bonuses for the year of termination, the executive's annual bonus for 2009 and his long-term bonus for 2009-11 are negligible: his annual bonus for 2009 would be 1/365 of a full annual bonus, and his long-term bonus for 2009-2011 would be 1/1095 of the full long-term bonus. The later in 2009 a COC occurred and the executive resigned, the higher his 2009 annual bonus and 2009-11 long-term bonus would be.

Source: Towers Perrin Tables.

3. Messrs. Haggett, Cashman, Tufano and Udvarhelyi

The Old Agreements IBC had in place with each of these four executives prior to the Highmark-IBC merger negotiations provided that they would receive a year's salary and a year of health insurance benefits if they were terminated without cause. Those agreements authorized no payments or benefits for the executives if they voluntarily terminated, for any reason, in connection with a change of control.

The March 2007 New Agreements provided that if these executives were terminated without cause before a COC they would receive, in addition to 100% of their annual salary and health insurance benefits, a full annual bonus, an additional annual bonus for the year of termination pro-rated to the termination date, and life insurance benefits.

Further, the New Agreements provided that if the executives were terminated without cause or resigned for Good Reason after a COC, they would receive 200% of their annual salary, 200% of their average or target annual bonus plus a pro-rated bonus for the year of termination, and pro-rated LTIP bonuses for all pending LTIP cycles. In addition, they would receive one year of both life and health insurance benefits.

Finally, like Messrs. Frick and Butler these executives entered into Amended New Agreements that increased the number of years they would be required to refrain from competing with IBC so that it matched the number of years salary plus bonus they would receive on termination in connection with a COC: they would receive two years of such benefits and would also be required to refrain from competing with IBC for two years, rather than for only one year as under their New Agreements. Table 36 shows the benefits potentially receivable on termination by Messrs. Cashman, Haggett, Tufano and Udvarhelyi under their three different agreements.

Table 36

Cashman, Haggett, Tufano, and Udvarhelyi:
Benefits potentially receivable on termination

	Under Old Agreement	Under New Agreement		Under Amended New Agreement
When payable	Only if terminated without cause	If terminated w/o cause before a COC	If terminated w/o cause or if resigns for Good Reason w/i 2 years following COC	No Change
Salary	100%	100%	200%	No Change
OIP	None	100% of > of target or 3-yr. avg. plus yr. of term. pro-rated.	200% of > of current target or 3-yr. actual avg. plus 1 yr. pro-rated.	No Change
LTIP	None	None	For all pending cycles, pro-rated (para. 10 of LTIP doc)	No Change
Health benefits	1 year	No Change	1 year	No Change
Life ins. Benefits	None	1 year	No Change	No Change
Non-compete	1 year	No Change	No Change	no COC: 1 yr after COC: 2 yrs
Non-solicitation	2 years	1 year	No Change	no COC: 1 yr after COC: 2 yrs
Definition of "Good Reason"	N/A	N/A	(i) reduction in base salary (ii) material reduction in total target compensation (iii) material reduction in annual or long-term bonus (iv) material reduction in duties and responsibilities (v) material reduction in EE benefits (vi) relocate > 50 miles	No Change

Table 37 sets forth the value of each benefit potentially receivable by Cashman, Haggett, Tufano, and Udvarhelyi on termination in connection with a COC under their amended New Agreements, assuming that a COC occurred and the executive resigned on January 1, 2009.

Table 37

4 IBC Executives: Payments on Termination Without Cause or for Good Reason in connection with a COC

Executive (multiple)	Base salary x multiple	Annual bonus '08 x multiple	Annual bonus '09 pro-rated	LT bonus '07-'09, pro-rated	LT bonus '08-'10, pro-rated	LT bonus '09-'11, pro-rated	Life & health benefit	Total
Cashman (2)	$805,000	$402,500	*	$170,625	$87,208	*	$14,378	$1,479,711
Tufano (2)	$1,005,000	$502,500	*	$180,583	$108,875	*	$14,378	$1,811,336
Haggett (2)	$865,200	$432,600	*	$183,863	$93,730	*	$14,378	$1,589,771
Udvarhelyi (2)	$1,060,600	$530,300	*	$224,315	$114,898	*	$14,378	$1,944,491

*The figures in this table are based on the assumption that a COC occurs and the executive terminates on January 1, 2009. Under this assumption, because the executive receives pro-rated bonuses for the year of termination, the executive's annual bonus for 2009 and his long-term bonus for 2009-11 are negligible: his annual bonus for 2009 would be 1/365 of a full annual bonus, and his long-term bonus for 2009-2011 would be 1/1095 of the full long-term bonus. The later in 2009 a COC occurred and the executive resigned, the higher his 2009 annual bonus and 2009-11 long-term bonus would be.

Source: Towers Perrin Tables.

4. Ms. Bright

Ms. Bright's Old Agreement is identical to those of Messrs. Tufano, Haggett, Cashman and Udvarhelyi. Ms. Bright's March 28, 2007 New Agreement was identical to the others' New Agreements except that it provided that she would receive 150% of salary and annual bonus, rather than 200% of salary and annual bonus like the other four, if she were terminated without cause or resigned for Good Reason following a COC. In addition, Ms. Bright entered into a separate Retention Agreement on July 26, 2007 with IBC providing that she would receive an additional $125,000 if she continued to work for IBC until March 29, 2008, another $250,000 if she stayed until September 28, 2008, and another $125,000 if she stayed until March 28, 2009.

Finally, like the other executives Ms. Bright entered into an Amended New Agreement that increased the number of years she would be required to refrain from competing with IBC so that it matched the number of years salary plus bonus she would receive on termination in connection with a COC: she would receive 150% of her salary plus annual bonus on such termination and would be prohibited from competing with IBC for 18 months, rather than for one year as under her New Agreement. Table 38 shows the benefits potentially receivable on termination by Ms. Bright under her three different agreements.

Table 38

Bright:
Benefits potentially receivable on termination

	Under Original Agreement	Under March 2007 Agreement		Under Amended Agreement
When payable	Only if terminated without cause	All benefits except retention bonus: If terminated w/o cause before a COC Retention bonus: 125,000 on 3/29/08 250,000 on 9/28/08 125,000 on 3/28/09	All benefits except retention bonus: If terminated w/o cause or if resigns for Good Reason w/i 2 years following COC Retention bonus: 125,000 on 3/29/08 250,000 on 9/28/08 125,000 on 3/28/09	No Change
Salary	50%	100%	150%	No Change
OIP	None	100% of > of current target or 3-yr. actual avg. plus 1 yr. pro-rated.	150% of > of current target or 3-yr. actual avg. plus 1 yr. pro-rated.	No Change
LTIP	None	None	All LTIP bonuses to extent accrued, pro-rated to termination date	No Change
Health benefits	6 mos.	1 year	No Change	No Change
Life ins. Benefits	None	1 year	No Change	No Change
Non-compete	1 year	1 year	1 year	no COC: 1 yr. after COC: 18 mos.
Non-solicitation	2 years	1 year	No Change	no COC: 1 yr. after COC: 18 mos.
Definition of "Good Reason"	N/A	N/A	(i) reduction in base salary (ii) material reduction in total target compensation (iii) material reduction in annual or long-term bonus (iv) material reduction in duties and responsibilities (v) material reduction in EE benefits (vi) relocate > 50 miles	No Change

Unlike the Retention Agreements of Mr. Cain and Mr. Francavilla, Ms. Bright's Retention Agreement does not terminate her. And while Highmark and Mr.

Klingensmith had an understanding that Mr. Klingensmith would leave the company after receiving his retention bonus, IBC and Ms. Bright intended that Ms. Bright would continue her employment with IBC after receiving her retention bonus.

Table 39 sets forth the value of each benefit potentially receivable by Ms. Bright on termination in connection with a COC under her Amended New Agreement, assuming that a COC occurred and the executive resigned on January 1, 2009.

Table 39

Bright: Payments on Termination Without Cause or for Good Reason in connection with a COC

Executive (multiple)	Base salary x multiple	Annual bonus '08 x multiple	Annual bonus '09 pro-rated	LT bonus '07-'09, pro-rated	LT bonus '08-'10, pro-rated	LT bonus '09-'11, pro-rated	Life & health benefit	Total **
Bright (1.5)	$507,000	$253,500	*	$120,267	$67,600	*	$14,378	$962,745

*The figures in this table are based on the assumption that a COC occurs and the executive terminates on January 1, 2009. Under this assumption, because the executive receives pro-rated bonuses for the year of termination, the executive's annual bonus for 2009 and his long-term bonus for 2009-11 are negligible: his annual bonus for 2009 would be 1/365 of a full annual bonus, and his long-term bonus for 2009-2011 would be 1/1095 of the full long-term bonus. The later in 2009 a COC occurred and the executive resigned, the higher his 2009 annual bonus and 2009-11 long-term bonus would be.

**Ms. Bright also had a Retention Agreement which provided for a payment of $125,000 if she remained with IBC until March 29, 2008, an additional $250,000 if she remained with IBC until September 28, 2008, and an additional $125,000 if she remained with IBC until March 28, 2009.

Source: Towers Perrin Tables.

II. Legal analysis of the payments receivable on termination following a COC, or on remaining with the company throughout the Department's merger review process

A. What law applies?

Section 5551(b) of the NPC Law provides that "a non-profit corporation may pay compensation in a reasonable amount to members, directors, or officers for services rendered." Thus, payments potentially receivable by the Highmark and IBC executives on termination in connection with a COC must meet two tests to be lawful. First, they must be reasonable in amount; and second, they must be "for services rendered." The meaning of these terms as used in NPC Law § 5551(b) has never been construed by the Pennsylvania courts. However, the Internal Revenue Code and the Treasury Regulations promulgated pursuant thereto set forth standards for determining both whether payments on termination in connection with a COC are reasonable and whether they are for services rendered. Based on that guidance, in this section we determine whether the payments potentially receivable by the Highmark and IBC executives on termination in connection with a COC meet each of those tests. We also determine whether the payments to certain executives that are triggered by the executive's remaining with the company until a certain date meet those two tests.

1. When is a payment payable on termination in connection with a COC reasonable?

Section 280G of the Internal Revenue Code is entitled "Golden parachute payments." It defines as an "excess parachute payment" any payment that is "contingent on" a COC and exceeds three times the recipient's "base amount," which the Code defines as his average compensation for the previous five years. IRC §§ 280G(b)(2)(A); 280G(b)(3); 280G(d)(2). If a payment constitutes an excess parachute payment as described in 280G, then to the extent it exceeds the recipient's base amount it is non-deductible by the corporation making the payment, and under Code section 4999 the recipient of the payment must pay a 20% excise tax on it. Importantly, once the three-times-base-amount threshold is met, it is not the excess over this threshold that is penalized, but rather the excess over the base amount.

Excess parachute payments as defined in 280G are thus not reasonable compensation for at least three reasons. First, because 280G characterizes such payments as "excess" parachute payments, they can not, by definition, be reasonable parachute payments. Second, because section 4999 of the Code imposes a 20% excise tax on such payments, they can't be reasonable, since if they were reasonable the Code would not penalize them. Third, by making excess parachute payments non-deductible, section 280G(a) necessarily makes such payments not "a reasonable allowance for salaries or other compensation for personal services actually rendered" under 162(a)(1), and thus makes them unreasonable by definition.

Importantly, however, not all payments that are receivable after a merger are subject to section 280G and taxable under section 4999. Rather, 280G and 4999 apply only to payments that are "contingent on" a COC. Under the Treasury Regulations, only payments that are payable in connection with a COC but are not payable not in connection with a COC are "contingent on" a COC and thus subject to 280G and taxable under 4999.

As will be seen in section IIB1, <u>infra</u>, a substantial portion of the payments to which the executives would be entitled if they are terminated without cause or resign for Good Reason or due to a Material Change after a COC would also be payable to the executives absent a COC. Such payments should not be included in determining whether a payment, or a series of payments, constitutes an excess parachute payment, and thus unreasonable compensation, under section 280G.

2. When is a payment on termination in connection with a COC compensation "for services rendered"?

The Treasury Regulations interpreting section 280G also explain the circumstances under which a payment may be characterized as compensation "for personal services actually rendered." Because essentially the same term – "for services rendered" – is used in section 5551(b) of the NPC Law as is used in section 280G(b)(4)(B) of the Internal Revenue Code, the Treasury Regulations interpreting that phrase can provide guidance in determining whether a payment payable on termination in connection with a COC should be considered compensation "for services rendered" under section 5551(b).

Qualifying as compensation "for services rendered," however, has different consequences under section 280G of the Internal Revenue Code than it does under section 5551 of the NPC Law. Specifically, under 280G, if a payment is compensation for services rendered then that payment is excluded from the excess parachute payment calculation; by definition, it can not be an unreasonable COC payment. Thus, COC payments must both exceed the three-times-base-amount excess parachute payment threshold and be not for services rendered to constitute an excess parachute payment in violation of section 280G. In contrast, a payment that either exceeds the excess parachute payment threshold or that is not for services rendered violates NPC Law § 5551(b), since that statute requires compensation to be both reasonable in amount and for services rendered. Thus, because only payments that are not for services rendered can be counted in determining whether a payment exceeds the excess parachute payment threshold, and all payments that are not for services rendered are unlawful under NPC Law § 5551(b) regardless of their amount, the sole test for whether a payment on termination in connection with a COC violates section 5551(b) is whether it is compensation for services rendered.

Importantly, the Treasury Regulations describe certain payments that can be characterized as compensation for services rendered and certain payments that can not be so characterized. Specifically, they provide that a covenant not to compete--an agreement not to perform services--can be considered personal services actually rendered. Treas. Reg. 1.280G-1, 26 CFR 1-280G-1 (hereinafter "Treas. Reg."), Q&A 40(b). They further provide that such a covenant will be considered personal services rendered if there is clear and convincing evidence that it substantially constrains the ability to perform services, and there is a reasonable likelihood that it will be enforced. Id. at Q&A 42(b).

In contrast, the Treasury Regulations provide that severance payments are not reasonable compensation for services rendered. The regulations define severance payments as follows:

> the term severance payment means any payment that is made to (or for the benefit of) a disqualified individual on account of the termination of such individual's employment prior to the end of a contract term, but does not include any payment that otherwise would be made to (or for the benefit of) such individual on the termination of such individual's employment, whenever occurring.

Id. at Q&A 44(a). A payment payable on termination and a COC is by definition payable prior to the end of the contract term. Whether such a payment should be characterized as a severance payment therefore depends on whether it would also be made on termination regardless of when the employee terminated.

With that background, we now turn to an analysis of the extent to which the payments potentially receivable by the executives following a COC may reasonably be characterized as compensation "for services rendered."

B. The Highmark executives' agreements

1. Payments potentially receivable by all the executives

Table 24, supra, sets forth the value of the benefits each of the nine Highmark executives who has not terminated would have received under their Amended New Agreements on termination in connection with a COC, based on the assumption that a COC occurs and the executive terminates on January 1, 2009.

a. SERP benefits

Once vested, on any termination for any reason the Highmark executives would also receive their SERP benefits, as set forth in Table 27A, supra. Those benefits clearly are compensation for services rendered, since they are earned by the executive based on his years of service, and they are payable to the executive when he terminates regardless of the reason for that termination. The SERP payments of the Highmark executives therefore are not fairly includible in any excess parachute payment calculation.

b. Payments for a covenant not to compete

Certain other payments potentially receivable by all the executives can be considered compensation for services rendered because they are characterizable as compensation for a covenant not to compete. The Treasury Regulations provide that for such a covenant to be considered personal services rendered, the taxpayer must demonstrate by clear and convincing evidence that the agreement substantially constrains his ability to perform services and is reasonably likely to be enforced against him. Q&A 42(b). The regulations also provide that the "clear and convincing evidence" standard is met if, among other things, the payments are made "only for the period the individual actually performs such personal services." Q&A 42 (a)(1). Thus, a payment of one year's compensation may properly be characterized as payment for a one-year covenant not to compete—i.e., for the performance of the personal services of not competing for one year; a payment of two years' compensation may properly be characterized as payment for a two-year covenant—i.e., the performance of the personal services of not competing for two years; and so forth. This is the same logic recently employed by the Maryland Commissioner in disapproving a portion of the payments CareFirst, Inc., the Maryland Blue Cross plan, had agreed to make to its CEO if it terminated him without cause, as it did in November 2006. See Ins. Com'r v. CareFirst, Inc., Case No. MIA-2007-10-027, at 47 (July 14, 2008) ("paying him one year of post-termination salary beyond the expiration of his non-compete obligation is not 'for work actually performed' for the benefit of CareFirst.").

The payments potentially receivable by the executives following a COC that are based on their annual compensation can thus reasonably be characterized as compensation for services rendered as long as the term of those payments is no greater than the term of the covenants not to compete in the executives' agreements. Notably, the multiples of salary plus the single earned annual bonus provided for in all the Highmark Amended New Agreements do not run afoul of this test.

In addition, all the long-term bonuses payable under the Amended New Agreements of each of the Highmark executives can be characterized as compensation for services rendered. That is because each long-term bonus can be characterized as payment for either working for Highmark or agreeing not to compete with Highmark during the term of the Performance Period for which that bonus is paid. Because assuming termination on January 1, 2009 the executives with two year covenants not to compete will all have agreed not to compete with Highmark until January 2, 2011, their long-term bonus for the 2007-2009 performance period is payment for working for Highmark during 2007 and 2008 and not competing for 2009; their long-term bonus for the 2007-2010 performance period is payment for working for Highmark during 2008 and not competing for 2009 and 2010; and their pro-rated bonus for the first day of the 2009-2011 performance period is payment for not competing with Highmark for the first day of 2011. The same analysis applies to Dr. Melani, except that Dr. Melani has a three-year covenant not to compete. Thus, Highmark could have paid Dr. Melani a full long-term bonus for the 2009-2011 performance period rather than only one day's worth of that performance period, and such payment would still have been characterizable as compensation for services rendered.

2. Mr. Truitt's October 23, 2008 Agreement

On October 23, 2008, after the execution of the New Agreements but before the execution of the Amended New Agreements, Highmark entered into a unique agreement with Mr. Truitt. That agreement increased the multiple of salary Mr. Truitt would be potentially eligible to receive upon a merger with IBC to 300%. It also included a general statement extending the term of his covenant not to compete to three years, but then provided that if he violates that covenant he waives all his COC payments "up to an aggregate amount equal to 100% of your base annual salary at the time of termination." Under his October 23, 2008 agreement, therefore, Mr. Truitt had the power to abrogate his covenant not to compete in exchange for his giving up his right to receive 100% of his salary. He thus had the option on COC of complying with the three-year covenant not to compete and collecting three years worth of salary, or going to work for a Highmark competitor immediately and collecting 200% of salary. At the same time, under the October 23, 2008 agreement Highmark did not waive any legal right it might have had had Mr. Truitt abrogated his covenant not to compete.

Mr. Truitt's October 2008 agreement also required him to provide consulting services to Highmark for one year, not to exceed 18 hours a week, with the obligation to perform such services terminating 90 days after his termination if performing such services would impair his ability to serve his other clients.

Because of the conditional nature of the obligations in the October 23, 2008 Truitt agreement, the extent to which the payments therein authorized on termination in connection with a COC constitute compensation for services rendered is unclear. In any event, that agreement has now been superseded by an Amended New Agreement which includes the same terms as all the other Amended New Agreements.

3. Messrs. Cain, Francavilla and Klingensmith

As explained in sections IA3 and IA4, supra, Messrs. Cain, Francavilla and Klingensmith terminated on or about March 31, 2009. On termination, they are receiving both the severance payments set forth in their New Agreements and an additional retention bonus, as described in sections IA3 and IA4. This section explains the extent to which their retention bonuses and the other payments they will receive on termination may reasonably be characterized as "reasonable in amount" and "for services rendered" within the meaning of section 5551(b) of the NPC Law.

a. Cain and Francavilla

(1) Retention Bonuses

The case to be made in support of the retention bonuses being paid to Cain and Francavilla is as follows:

Highmark and IBC agreed to merge in March 2007. Cain and Francavilla would not be needed to run the new company and they knew it, but Highmark needed them to both do their current jobs and help integrate the two companies during the time the Department was reviewing the merger. Highmark anticipated that the Department's review of the merger could take up to two years and could be extremely frustrating. To maximize the likelihood that Cain and Francavilla would remain with the company throughout a long and frustrating process even though they knew that at the end of that process they would no longer have a job with the company, Highmark believed it was reasonable to pay them a bonus if, but only if, they remained with the company until the Department approved the merger.

That is a reasonable argument. On the other hand, even if Highmark did not authorize a retention bonus to provide an incentive for Cain and Francavilla to remain with the company, the fact that they would forfeit their severance benefits--including 150% of salary plus annual and long-term bonuses--if they voluntarily resigned before the Department finished its review would seem to provide a sufficient incentive for them to remain with the company during the pendency of that review. Notably, Messrs. Cain and Francavilla receive their severance benefits only if either they are terminated without cause or they resign "within sixty days after you have knowledge of a Material Change before or after a Change in Control." They do not receive severance benefits if they voluntarily resign and there has been no Material Change. The stick of losing 150% of salary plus annual and long-term bonuses if they don't remain with the company while the Department reviews the merger would seem to make unnecessary the carrot of their receiving an additional 100% of salary if they do remain with the company during that time.

The rejoinder to this argument is that Cain and Francavilla's knowing that they will receive a retention bonus if they stay with Highmark until approval of the merger or March 31, 2009 necessarily makes it more likely that they will not go to work for another employer during that period, since they would be giving up more by forfeiting 250% of salary than they would by forfeiting 150% of salary. It is not possible to know whether paying Cain and Francavilla an additional 100% of salary if and only if they remained with Highmark throughout the Department's merger review process was truly necessary to keep them at Highmark during that time. But Highmark may well have believed that Cain and Francavilla were so important to the company that it was reasonable to do so. While one could argue that retention bonuses, by definition, are not compensation for services rendered, since the executive has already been compensated for providing services before he receives his retention bonus, such bonuses may also be characterizable as an additional component of the executive's compensation for services rendered.

Are the Cain and Francavilla bonuses reasonable in amount? Highmark has submitted no data regarding retention bonuses paid by other Blue Cross plans or by other arguably comparable companies, nor are we aware of any such data. In the absence of data clearly indicating to the contrary, considering all the facts and circumstances it would appear that the Cain and Francavilla retention bonuses are not unreasonable in amount. For both Cain and Francavilla they are no greater than their base annual salary, and they are less than 60% of the total of their salary, annual bonus and long-term bonus for 2008: Mr. Cain's $306,639 retention bonus equals 56% of his total 2008 compensation of $549,491, while Mr. Francavilla's $390,163 retention bonus equals 57% of his total 2008 compensation of $763,359.

(2) <u>Payments receivable on termination in addition to retention bonuses</u>

On their March 31, 2009 termination Messrs. Cain and Francavilla also became eligible pursuant to their Amended New Agreements for payments of 18 months of salary, an annual bonus for 2009 pro-rated through March 31, 2009, and long-term bonuses for the 2007-2009 and 2008-2010 Performance Periods pro-rated through March 31, 2009. Because all those bonuses are pro-rated through March 31, 2009, they are compensation for the service Cain and Francavilla rendered to Highmark while working for Highmark through that date. In addition, because their Agreements provide for an 18 month covenant not to compete, the 18 months of salary Messrs. Cain and Francavilla will receive can reasonably be characterized as compensation for the services they will render of not competing with Highmark for the next 18 months.

b. <u>Klingensmith</u>

(1) <u>Retention Bonus</u>

Mr. Klingensmith's retention bonus differs from Mr. Cain's and Mr. Francavilla's in several ways.

Most obviously, Mr. Klingensmith's retention bonus is significantly larger than Mr. Cain's and Mr. Francavilla's, both as a percentage of salary and in absolute dollars: whereas Cain and Francavilla are entitled to a retention bonus of 100% of their salary, Mr. Klingensmith's retention bonus is 300% of his, or $1,965,600--three times the Cain and Francavilla bonuses as a percentage of salary, and at least five times the Cain and Francavilla bonuses in dollars.

On the other hand, Mr. Klingensmith, unlike Cain and Francavilla and alone among all the executives, is expressly given a new title and new job duties in his New Agreement. Specifically, he is to serve as Chief Integration Officer; to have responsibility for all of Highmark's integration activities; to produce an Integration Plan; to hire staff to assist with the integration; and to chair the Executive Sponsor Committee.

The Klingensmith retention bonus differs from the Cain and Francavilla retention bonuses in three additional ways. Klingensmith, but not Cain and Francavilla, immediately becomes eligible for a retention bonus if Highmark formally withdraws from the merger agreement; Klingensmith's retention bonus is not provided for in a separate amendment to his New Agreement, as are Cain's and Francavilla's, but is authorized in the body of his New Agreement; and unlike Cain and Francavilla, who are terminated by their retention agreement, Klingensmith can collect his retention bonus and thereafter continue to work for the company. Notably, however, according to Highmark both Highmark and Klingensmith understood that Klingensmith would not be working for the new company.

Notwithstanding the size of the Klingensmith retention bonus, that bonus can be reasonably characterized as for services rendered, for two reasons. First, it can be viewed as compensation for assuming his new duties as Chief Integration Officer, which as articulated in his New Agreement are substantial, as well as for continuing his old duties as Group Executive Vice President. Second, when he signed his New Agreement Mr. Klingensmith, unlike Mr. Cain and Francavilla, already had a legal right to receive the severance payments provided for in that agreement if he terminated voluntarily. That is because Mr. Klingensmith had received an increase of less than the companywide average in one year, and under the unique terms of his Old Agreement receiving a less-than-average increase was a "Good Reason" enabling him to resign and collect severance payments. Unlike Mr. Cain and Francavilla, therefore, Mr. Klingensmith was entitled to his 150% of salary, plus all his other severance benefits, whether he resigned voluntarily or was terminated without cause. Thus, other than continuing to be paid his annual compensation, the only economic incentive Mr. Klingensmith had to remain with Highmark rather than to take a job with another company was the retention bonus he would receive at the end of the Department's review process. As with Mr. Cain and Mr. Francavilla, whether Mr. Klingensmith would in fact have had job offers during the Department's review process, and if so whether it would have made economic sense for him to have accepted such offers, can't be known. But Highmark could reasonably believe that paying Klingensmith a retention bonus if and only if he remained with the company during the pendency of the Department's review would increase the likelihood that he would remain with the company throughout that period. That retention bonus therefore can be characterized as compensation for services rendered.

Is Mr. Klingensmith's retention bonus reasonable in amount? There is no question but that it is large, whether viewed in absolute terms, percentage-of-salary terms, or percentage of total compensation terms: it exceeds Mr. Klingensmith's total compensation for 2008, including base salary, annual bonus, and long-term bonus. On the other hand, at the time Highmark agreed to pay Klingensmith his retention bonus he may have had Highmark over a barrel, since he already had the right to walk away at any time and collect 150% of salary plus bonuses. Highmark may well have thought that Klingensmith was so valuable, and his willingness to walk away so great, that $2 million was a reasonable amount to hold out as a carrot to have him remain with the company through the Department's merger review process.

In sum, the size of Klingensmith's retention bonus is troubling. So is the provision in his Old Agreement that enabled him to terminate and receive severance payments unless Highmark gave him a raise of at least the company-wide average. And so is Highmark's giving him a raise of less than that amount when it knew that by so doing it would trigger his ability to walk away and receive 150% of his salary plus bonuses and other benefits. Nevertheless, there is no evidence that Highmark did not act in good faith with regard to all these issues. We therefore cannot say that Mr. Klingensmith's retention bonus was unreasonable in amount as a matter of law.

(2) Payments receivable on termination in addition to retention bonus

The 18 months of salary Mr. Klingensmith is entitled to receive by walking away is also characterizable as compensation for services rendered. Even though he need not have Good Reason to resign in order to receive this payment, if he does resign his agreement requires him not to compete with Highmark for 24 months. Therefore, that payment may be construed as compensation for the services of not competing with Highmark through March 30, 2011, based on the assumption that he terminates on March

31, 2009. His 24-month covenant also enables the additional retiree welfare benefits, deferred compensation and SERP benefit that Highmark has agreed to calculate as if he had worked an additional 18 months to be characterized as compensation for his rendering the service of not competing for 18 months. In addition, because both his annual bonus for 2009 and his long-term bonuses for the 2007-2009 and 2008-2010 Performance Periods are pro-rated through his date of termination, those bonuses are compensation for the services Mr. Klingensmith rendered to Highmark while working for Highmark through that date.

C. The IBC executives' agreements

1. Payments potentially receivable by all the executives

Table 40, below, sets forth the value of the benefits each of the IBC executives will receive if he or she is terminated without cause or terminates for Good Reason in connection with a COC, based on the assumption that a COC occurs and the executive terminates on January 1, 2009.

Table 40

IBC Executives: Payments on Termination Without Cause or for Good Reason in connection with a COC

Executive (multiple)	Base salary x multiple	Annual bonus '08 x multiple	Annual bonus '09 pro-rated *	LT bonus '07-'09, pro-rated	LT bonus '08-'10, pro-rated	LT bonus '09-'11, pro-rated *	Life & health benefit	Total
Frick (3)	$2,940,000	$2,940,000		$640,167	$326,667		$14,378	$6,861,212
Butler (3)	$2,055,000	$1,438,500		$357,333	$182,667		$14,378	$4,047,878
Cashman (2)	$805,000	$402,500		$170,625	$87,208		$14,378	$1,479,711
Tufano (2)	$1,005,000	$502,500		$180,583	$108,875		$14,378	$1,811,336
Haggett (2)	$865,200	$432,600		$183,863	$93,730		$14,378	$1,589,771
Udvarhelyi (2)	$1,060,600	$530,300		$224,315	$114,898		$14,378	$1,944,491
Bright (1.5)**	$507,000	$253,500		$120,267	$67,600		$14,378	$962,745

*The figures in this table are based on the assumption that a COC occurs and the executive terminates on January 1, 2009. Under this assumption, because the executive receives pro-rated bonuses for the year of termination, the executive's annual bonus for 2009 and his long-term bonus for 2009-11 are negligible: his annual bonus for 2009 would be 1/365 of a full annual bonus, and his long-term bonus for 2009-2011 would be 1/1095 of the full long-term bonus. The later in 2009 a COC merger occurred and the executive resigned, the higher his 2009 annual bonus and 2009-11 long-term bonus would be.

**Ms. Bright also had a retention agreement which provided for a payment of $125,000 if she remained with IBC until March 29, 2008, an additional $250,000 if she remained with IBC until September 28, 2008, and an additional $125,000 if she remained with IBC until March 28, 2009.

Source: Tables 30, 32, 34, and 36.

a. SERP benefits

On any termination for any reason the IBC executives, like the Highmark executives, would also receive their SERP benefits, as set forth in Table 33A, supra. Those benefits clearly are compensation for services rendered and thus are not fairly includible in any excess parachute payment calculation, since they are earned by the executive based on his years of service, and are payable on termination for any reason.

b. Payments for a covenant not to compete

The COC payments to the IBC executives, like those to the Highmark executives, are lawful if the term of the covenant not to compete to which the executive has agreed does not exceed the number of years' compensation the executive is receiving. The COC payments in all the original agreements satisfied this test: Mr. Frick and Mr. Butler were to receive 24 months of annual salary plus corresponding bonuses and agreed to a 24-month covenant not to compete; and Tufano, Haggett, Cashman, Udvarhelyi and Bright were to receive 12 months of annual salary plus corresponding bonuses and agreed to a 12 month covenant not to compete.

The COC payments in the New Agreements, in contrast, did not satisfy this test, because the number of years of salary they provided for on termination in connection with a COC exceeded the number of years of the covenant not to compete by one: Mr. Frick and Mr. Butler were eligible to receive three years of salary on termination in connection with a COC but were required to refrain from competing with IBC for two years, while the other five executives were eligible to receive two years of salary on such termination but were required to refrain from competing with IBC for one year.[14]

[14] In addition, as noted in Part Two section IB, supra, only Mr. Frick and Mr. Butler were entitled to payments under their Old Agreements if they either were terminated without cause or resigned for Good

Significantly, in January 2009 IBC entered into another agreement ("Amended New Agreement") with each of the seven executives. Under these agreements, the term of each executive's covenant not to compete is equal to the number of years salary he or she is eligible to receive on termination in connection with a COC. Under the Amended New Agreements, therefore, the payments the executives are potentially eligible for on termination in connection with a COC are all compensation for services rendered – the service of not competing with IBC – and thus do not violate §5551(b) of the NPC Law.

Finally, in December of last year, IBC amended its agreements with Messrs. Frick and Butler to cap the payments they could receive on termination following the merger at the maximum level at which they would not exceed the 280G threshold. That amendment makes economic sense for both the executives and the company. Because Mr. Frick and Mr. Butler would not be liable for a 20% section 4999 excise tax on the portion of any parachute payment exceeding their five-year average annual compensation, the net amount they would retain will be substantially greater than it would have been if they received a payment exceeding the 280G threshold and had to pay that excise tax. At the same time, the entire payment would be fully deductible to IBC.

2. Ms. Bright's retention bonus

The principles applying to Ms. Bright's retention bonus are the same as those applying to the Cain, Francavilla and Klingensmith retention bonuses. On the one hand, whether absent the ability to collect such a bonus at the end of the Department's merger review process the executive would resign early in that process can not be known. On

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Reason after a COC; the other executives were entitled to the payments set forth in their original agreements only if they were terminated without cause. The New Agreements make the payments authorized for all the executives payable on resignation for Good Reason after a COC as well as on termination without cause.

the other hand, to the extent that the company views retaining an executive throughout that process as essential it is reasonable for the company to pay the executive a bonus if, and only if, she remains with the company throughout that process.

That Ms. Bright's retention bonus is structured slightly differently than those of Messrs. Cain, Francavilla and Klingensmith—it is actually a series of three successive retention bonuses--does not change the analysis. Her Retention Agreement provides that she receives $125,000 if she remains with the company until March 28, 2008, another $250,000 if she stays until September 28, 2008, and a final $125,000 if she stays until March 28, 2009. Because it was reasonable for IBC to believe that the payment of these amounts increased the likelihood that she would continue to perform services for the company through those dates rather than resigning before those dates, those payments can reasonably be characterized as compensation for services rendered.

D. Payments on termination following a COC: Highmark and IBC v. For - profit Health Insurers

Unlike non-profit HPC's, the payments authorized by for - profit health insurers for their executives on COC need be neither reasonable nor for services rendered. If the payments that for - profit corporations make are unreasonable they and their executives are subject to tax penalties under sections 280G and 4999, but unlike non-profit corporations they may still permissibly make those payments.

The table below, which is derived from the for - profit carriers' 2009 proxy statements, sets forth the payments on termination following a COC for which the Highmark and IBC CEO's are potentially eligible and for which the CEO's of each of the leading for - profit health insurers are potentially eligible. It assumes that a COC occurs and the executive terminates on December 31, 2008, and it values all stock-based compensation based on the closing price of the company's stock on December 31, 2008.

Table 41

**Payments to CEO's on Termination Following COC:
December 31, 2008 Termination and Valuation Date**

Name	Company	Cash Severance ($)	Stock-Based Severance ($)	Other ($)	Gross-Up ($)	Total ($)
Ed Hanway (1)	CIGNA	13,965,000	49,067,000	19,000	23,370,000	86,420,000
Ron Williams (2)	Aetna	9,900,000	8,201,759	--	Authorized but not triggered	18,101,759
Dale Wolf (3)	Coventry	7,840,575	2,027,400	51,292	Authorized but not triggered	9,919,267
Angela Braly (4)	WellPoint	9,843,416	1,810,537	222,600	3,311,743	15,188,296
Stephen Hemsley (5)	United	5,004,594	--	--	No	5,004,594
Michael McCallister (6)	Humana	7,687,500	--	38,346	Authorized but not triggered	7,725,846
Joseph Frick (7)	IBC	6,861,212	0	0	No	6,861,212
Ken Melani (8)	Highmark	6,375,003	0	0	No	6,375,003

(1) Total does not include a $29,361,000 SERP benefit.
(2) Total does not include SERP benefit of $5,594,642.
(3) Total does not include any SERP Benefit.
(4) Total does not include any SERP Benefit.
(5) Total does not include a $10,703,229 SERP benefit.
(6) Total does not include a $6,655,980 SERP benefit and $10,412,692 in vested stock options.
(7) Total does not include a $5,292,000 SERP benefit.
(8) Total does not include a $6,084,000 SERP benefit.

Source: 2009 Proxy Statements; Highmark and IBC.

When the termination and valuation date is assumed to be December 31, 2007 rather than December 31, 2008, the for - profit/non-profit differential regarding potential COC payments appears to be much more substantial. The following table sets forth the identical data as the previous table, but assuming a termination and valuation date of December 31, 2007 rather than December 31, 2008.

Table 42

Payments to CEO's on Termination Following COC:
December 31, 2007 Termination and Valuation Date

Name	Company	Cash Severance ($)	Stock-Based Severance ($)	Other ($)	Gross-Up ($)	Total ($)
Ed Hanway (1)	CIGNA	13,830,000	40,922,000	29,000	17,308,000	72,089,000
Ron Williams (2)	Aetna	9,900,000	36,320,760	--	Authorized but not triggered	46,220,760
Dale Wolf (3)	Coventry	7,839,626	17,889,863	49,218	Authorized but not triggered	25,778,707
Angela Braly (4)	WellPoint	8,699,544	11,532,796	222,600	4,301,036	24,845,976
Stephen Hemsley (5)	United	6,104,744	13,656,625	--	No	19,761,369
Michael McCallister (6)	Humana	7,312,500	7,399,922	37,231	Authorized but not triggered	14,749,643
Joseph Frick (7)	IBC	6,861,212	0	0	No	6,861,212*
Ken Melani (8)	Highmark	6,375,003	0	0	No	6,375,003*

(1) Total does not include a $29,628,000 SERP benefit.
(2) Total does not include SERP benefit of $4,449,381.
(3) Total does not include any SERP Benefit.
(4) Total does not include any SERP Benefit.
(5) Total does not include a $10,703,229 SERP benefit.
(6) Total does not include $8,602,150 SERP benefit and $31,218,942 in vested stock options.
(7) Total does not include a $5,292,000 SERP benefit.
(8) Total does not include a $6,084,000 SERP benefit.
* Assumes December 31, 2008 Termination.

Source: 2008 Proxy Statements; Highmark and IBC.

The difference between the two tables is a result of the decline in the market value of each carrier's stock during 2008. That decline has substantially affected the value of each CEO's stock-based compensation on termination. For Aetna's Mr. Williams, for example, that value declined by more than $28 million, or 77%, while for the CEO's of Coventry, WellPoint, United and Humana the decline was even greater in percentage terms. And even CIGNA's Mr. Hanway--the only CEO whose potential payments on termination in connection with a COC increased between 2007 and 2008--lost $43,604,000 in 2008 in exercisable stock options.

Whether one believes the 2007 data or the 2008 data better reflects the true differential between the potential COC payments authorized by the for - profit health insurers and those authorized by the Blues depends on whether one believes the stock market will recover or will either remain at its current level or continue to decline.

III. Arguments supporting a more permissive interpretation of NPC Law § 5551(b)

The language of section 5551(b) of the NPC Law has never been construed. Good faith policy and legal arguments can be raised as to why the interpretation adopted here of "reasonable in amount" and "for services rendered" within the meaning of the NPC Law are unduly restrictive. This section sets forth those arguments and explains why, although we believe those arguments are reasonable, we do not adopt them.

A. Blue Cross executives should be compensated in the same manner and at the same level as executives of for - profit insurers, since the Blues and for - profit insurers must compete for the same executives and require the same skill set of their executives

As explained in Part One section IIB, supra, notwithstanding the Blues' legal status as non-profit health service corporations and the commercial carriers' status as for - profit corporations, both types of corporations are in the health insurance business, and the people running those corporations must have many of the same skills. In addition, both Highmark and IBC have for - profit subsidiaries.

Nevertheless, the Blues are different from for - profit health insurers in one fundamental way. Whereas the sole duty of directors of for - profit corporations is to maximize profits for the benefit of the corporation's shareholders, the duties of the directors of the Blues, which have no shareholders, are broader. In particular, the Blues are required by statute to provide coverage to low income people. See 40 Pa. C.S.A. §§ 6303(a); 6325(a); 6325(c).[15] Accordingly, Highmark has acknowledged that the Blues have "unique obligations to make health care coverage available to all segments of the community." Letter from Highmark Executive Vice-President David O'Brien to Pennsylvania Insurance Commissioner Diane Koken, Oct. 8, 2004, at 4. The Blues therefore subsidize their individual product rates to provide low-cost coverage for the uninsured. Id. They offer "guaranteed issue, continuous open enrollment programs available to any individuals in [their] service area[s], at any time, regardless of health status." Id. This is one of the reasons, and may well be the most significant reason, that Pennsylvania historically has had one of the lowest rates of uninsured among the 50 states. See id.

Providing below-cost coverage to those who can't afford to pay actuarially sound rates--whether because they are low income or in poor health, or both--is obviously not the only purpose of the Blues, nor could it be. However, it is one of their purposes. We therefore do not believe that it is proper for the Blues to determine the compensation they pay their executives by looking solely at what for - profit insurers pay their executives. On the other hand, because the Blues compete with the for - profit carriers and obviously

[15] The language regarding the legal duty to provide coverage to low income people is more specific with respect to health services plan corporations —Blue Shield plans—than it is with respect to hospital plan corporations, i.e., Blue Cross plans. For example, the professional health services plan corporation statute provides that "every professional health service corporation shall…fix the requisites for persons of low income," Pa. C.S.A. sec 6325(a)(1), and that such requisites must be consistent with the declaration of necessity set forth in that statute. That declaration provides that "it is necessary that provision be made for adequate professional health services to persons of low income who are unable to provide such services for themselves." Pa. C.S.A. sec. 6303(a). There is no analog to sections 6330(a) and 6325(a) in the hospital plan corporation section of the statute.

have many characteristics in common with those carriers, the Blues need not completely disregard the compensation paid to executives of for - profit carriers in determining their executives' compensation.

B. The determination of how much to pay executives is protected by the business judgment rule, and thus in the absence of bad faith the Commissioner does not have the authority to disapprove such compensation.

It is true that the business judgment rule insulates corporate directors and officers from liability as long as they act in good faith, keep reasonably informed, and reasonably believe their actions are in the best interests of the corporation. Cuker v. Mikalauskas, 547 Pa. 600, 606-07 (1997). The business judgment rule, however, does not strip the Commissioner of his authority under the Health Plan Corporations Act to oversee these statutory non-profit corporations. See 40 P.S. §§ 6101, 6302. Because the Blues have no shareholders, who at least in theory can serve as a check on management, only the Commissioner can serve as that check on the Blues. Put another way, if a for - profit corporation pays excessive compensation to its executives, that compensation is paid for by the shareholders. With the Blues, on the other hand, if the directors authorize excessive executive compensation, that compensation is paid for by the public: every dollar of such compensation is another dollar that can not be used to pay for coverage for the uninsured. The oversight role of the Commissioner with respect to the Blues' compensation of their executives is thus both extremely important and is authorized by the Commissioner's general authority to enforce the Health Plan Corporations Act, whether or not the directors of the Blues have complied with the business judgment rule.

C. Whether a parachute payment is unreasonable for purposes of section 280G of the IRC does not necessarily mean that it is unreasonable for purposes of section 5551(b) of the NPC Law

This argument has some merit because any compensation that an executive defers is excluded from the calculation of the threshold above which a payment is characterizable as an excess parachute payment. Treas. Reg. Q&A 34(e). Thus, an executive who has deferred substantial compensation will have a substantially lower § 280G "base amount" than an identically compensated executive who has not deferred compensation. See Part Two section IIA1, supra. As a result, the same COC payment may constitute an excess parachute payment and thus unreasonable compensation for the first executive but not for the second executive. This is unjust, and thus there is a reasonable argument that a payment to an executive should not be characterized as unreasonable for purposes of NPC Law § 5551(b) solely because his deferral of compensation has caused it to be deemed unreasonable for purposes of section 280G.

The distortion caused by the manner in which section 280G treats deferred compensation, however, does not mean that 280G should be ignored in determining whether COC payments are reasonable. More fundamental, the treatment of deferred compensation by section 280G has no impact in determining whether compensation meets the "for services rendered" test.

D. The Committee Comment in the Pennsylvania Business Corporation Law stating the Committee's intent to authorize golden parachute payments by for - profit corporations should also be interpreted as reflecting legislative intent to authorize golden parachute payments by nonprofit corporations

Section 1502 of the general Business Corporation law, 15 Pa. C.S.A. sec 1501 et. seq., enumerates the general powers of a domestic business corporation. One of the powers of such a corporation is to "fix the[] compensation" of its officers and employees and to "pay bonuses or other additional compensation...for past services." 15 Pa.C.S.A. sec. 1502(a)(16). A Committee Comment to that subsection provides as follows:

> It is intended that the types of compensation authorized to be paid by this subsection will include, among other things, compensation payable upon termination of employment (including, without limitation, arrangements with executives, commonly referred to as "golden parachutes," and with other employees, commonly referred to as "tin parachutes").

The Committee Comment thus clearly expresses the intention that section 1502(a)(16) of the Business Corporation Law be interpreted to authorize Pennsylvania business corporations--i.e., for - profit corporations--to provide their executives with golden parachutes.

Did the legislature through that Committee Comment also intend to authorize non-profit corporations to provide their executives with golden parachutes? On the one hand, the NPC Law contains a provision similar to section 1502(a)(16), and an Official Source Note to section 5502 of the NPC Law states that that section is "patterned after" section 1502. On the other hand, there is a fundamental difference between section 1502(a)(16) of the Business Corporation Law and section 5502(a)(16) of the Nonprofit Corporation Law. Specifically, section 1502(a)(16) empowers domestic business corporations to fix the "compensation" of their officers and employees; if they wish to pay compensation that is unreasonable as a matter of law—as golden parachute payments are, see section IIA1, supra—they are free to do so, as long as they pay the penalties that attach to the payment of such unreasonable compensation. In contrast, section 5502(a)(16) empowers non-profit corporations to fix only "reasonable compensation" of their officers and executives. Section 5502(a)(16) thus does not authorize non-profit corporations to pay unreasonable compensation such as golden parachutes.

If the legislature truly did intend to authorize golden parachute payments by non-profit corporations, it could have included a Committee Comment to the General Powers section of the Nonprofit Corporation Law expressly so stating. Because it did not do so, we should not impute its intent regarding the general powers of for - profit corporations to nonprofit corporations. This is particularly true because sections 5502(a)(16) and 5551(b) of the Nonprofit Corporation Law, unlike any section of the general Business Corporation law, expressly require compensation paid by non-profit corporations to be reasonable, and sections 280G and 162(a)(1) of the Internal Revenue Code deem golden parachute payments to be unreasonable. Further, we should be particularly reluctant to assume that the legislature intended to authorize nonprofit HPC's like Highmark and IBC to make golden parachute payments. That is because, as explained in section IIIB, supra, while such payments when made by for - profit corporations are paid for by shareholders, golden parachutes by nonprofit HSC's, which have no shareholders, are necessarily paid for by policyholders or by the beneficiaries of the Blues' social mission.

In short, the Committee Comment expressing the intention that golden parachute payments by for - profit corporations are permissible can not reasonably be interpreted as applying to nonprofit corporations.

IV. Conclusion

The compensation paid to the Highmark and IBC executives is in line with that paid to executives of other Blue Cross companies of similar size, and in general is substantially less than that paid to executives of for - profit health insurers. Thus, while the appropriateness of the level of executive compensation throughout the private health insurance industry may well be questioned, the compensation authorized by Highmark and IBC for their executives can not be said to be unreasonable within the meaning of section 5551(b) of the Pennsylvania Nonprofit Corporation Law. In addition, for the reasons explained in section II of this report, that compensation can also be characterized as "for services rendered" within the meaning of the Pennsylvania Nonprofit Corporation law.