

BEFORE THE INSURANCE COMMISSIONER
OF THE
COMMONWEALTH OF PENNSYLVANIA

In Re:	:	Pursuant to Sections 1401, 1402
	:	and 1403 of the Insurance Holding
Application of Highmark Inc. in Support	:	Companies Act, Article XIV of the
of the Request for Approval to Acquire	:	Insurance Company Law of 1921, Act
Control of First Priority Life Insurance	:	of May 17, 1921, P. L. 682, <u>as</u>
Company, Inc.	:	<u>amended</u> , 40 P.S. §§991.1401,
	:	991.1402 and 991.1403; Chapter
	:	25 of Title 31 of the Pennsylvania
	:	Code, 31 Pa. Code §§25.1- 25.23.
	:	
	:	Order No. ID-RC-04-03

DECISION AND ORDER

AND NOW, on this 19th day of May, 2004, M. Diane Koken, Insurance Commissioner of the Commonwealth of Pennsylvania (“Commissioner”), hereby makes the following Decision and Order:

Pursuant to the Insurance Holding Companies Act and in consideration of the documents, presentations and reports received, as well as other inquiries and studies as permitted by law, the Commissioner hereby makes the following findings of fact:

FINDINGS OF FACT

Identity of Involved Persons

Acquiring Person

1. Highmark Inc. (“Highmark”) is a Pennsylvania nonprofit health plan corporation which operates a professional health services plan and a hospital plan under Article A, Health Plan Corporations, Part III, Special Provisions Relating to Particular Classes of Insurers, 40 P.S. §§6101 et seq. and §§6301 et seq. (“Health Plan Corporations Act,” or “HPCA”). Highmark’s principal place of business is in Camp Hill, Pennsylvania.
2. Highmark is an independent licensee of the Blue Cross Blue Shield Association and operates under the Blue Cross servicemark to provide hospital care coverage in the 29-county western region of Pennsylvania and operates under the Blue

Shield servicemark to provide professional health care coverage throughout Pennsylvania.

Domestic Insurer

3. First Priority Life Insurance Company, Inc. (“First Priority Life”) is a domestic stock life insurance company organized pursuant to the laws of the Commonwealth of Pennsylvania with its principal place of business in Wilkes-Barre, Pennsylvania.

Other Involved Person

4. Hospital Service Association of Northeastern Pennsylvania d/b/a Blue Cross of Northeastern Pennsylvania (“BCNEPA”) is a Pennsylvania nonprofit health plan corporation which operates a hospital plan under the Health Plan Corporations Act. BCNEPA has its principal place of business in Wilkes-Barre, Pennsylvania. First Priority Life is a wholly-owned subsidiary of BCNEPA.
5. BCNEPA is an independent licensee of the Blue Cross Blue Shield Association and operates under the Blue Cross servicemark to offer hospital care coverage in the 13-county region of northeastern Pennsylvania.

Acquisition Filing

6. On November 24, 2003, Highmark, BCNEPA and First Priority Life executed a stock purchase agreement (which together with all amendments received subsequently is collectively referenced as “Stock Purchase Agreement”) under which Highmark would acquire control of First Priority Life.
7. The Insurance Holding Companies Act, Article XIV of the Insurance Company Law of 1921, Act of May 17, 1992, P.L. 682, as amended, 40 P.S. §§991.1401 et seq. (“Insurance Holding Companies Act”), provides that all changes in control of domestic insurers must be filed with the Commissioner for approval or disapproval.
8. Chapter 25 of Title 31 of the Pennsylvania Code, 31 Pa. Code §§25.1 – 25.23, requires the filing of an application known as a “Form A” filing to seek approval of a change in control of domestic insurers or HMOs.
9. “Insurer” is defined in Section 1401 of the Insurance Holding Companies Act, as a company, association, or exchange authorized to transact insurance business in Pennsylvania. The definition includes HMOs but expressly excludes nonprofit health plans corporations operating hospital plans or professional health service plans.

10. On November 26, 2003, the Insurance Department of the Commonwealth of Pennsylvania (“Department”) received an initial application (which together with all material received subsequently is collectively referenced as “Application”) from Highmark for approval to acquire control of First Priority Life. On November 26, 2003, the Department received a companion application in which Highmark proposed to acquire control of HMO of Northeastern Pennsylvania, Inc. d/b/a First Priority Health (“First Priority Health”), an affiliate of First Priority Life and a subsidiary of BCNEPA.
11. The Application was filed pursuant to Section 1402 of the Insurance Holding Companies Act.

Department Procedures

12. On December 13, 2003, the Department published notice in the *Pennsylvania Bulletin* that the Application was received, and such notice invited interested persons to submit comments to the Department regarding the Application for 30 days following the date of the publication (“Comment Period”).
13. During the Comment Period, the Department received only one comment, and that comment related to Highmark’s proposed acquisition of control of First Priority Health (the companion application to this Application) and product pricing, provider agreements, the insurers’ surplus and policyholders in the northeast, and requested that the Department hold a public hearing.
14. The comment letter was forwarded to Highmark for response.
15. The Department reviewed and considered, in its analysis of the Application, the comment letter as well as Highmark’s response to the letter.
16. Section 1402 of the Insurance Holding Companies Act provides that the Commissioner shall conduct a hearing if either the acquiring party or the party to be acquired requests a hearing within ten days of the filing of the Application. A hearing may also be held if the Commissioner, in her discretion, elects to conduct a hearing as part of her review and analysis of a Form A filing.
17. Neither Highmark nor First Priority Life requested a hearing on the Application.
18. Because the parties to the Application did not request a hearing, any hearing conducted would have been an exercise of the Commissioner’s discretion under Section 1402 of the Insurance Holding Companies Act.
19. The Commissioner’s election to not hold a hearing was an appropriate exercise of the Commissioner’s discretion under Section 1402 of the Insurance Holding Companies Act.

Description of the Proposed Acquisition

20. As described in the Application, neither Highmark nor any person controlling, controlled by or under common control with Highmark currently holds any voting securities or securities which may be converted into voting securities of First Priority Life.
21. As described in the Application, First Priority Life will issue to Highmark, and Highmark will purchase from First Priority Life, 67 shares of First Priority Life's authorized common stock in addition to those previously issued to BCNEPA. Highmark proposes to pay \$4,029,400 for the stock to be issued by First Priority Life.
22. As described in the Application, Highmark will own 40% of the issued and outstanding common stock of First Priority Life.
23. Currently, BCNEPA is the sole shareholder of First Priority Life and holds 100% of the issued and outstanding common stock of First Priority Life. After the acquisition, BCNEPA's holdings will constitute 60% of the issued and outstanding common stock of First Priority Life.
24. As described in the Application, Highmark will have the right, after the effectuation of the proposed transaction, to nominate three (3) members to the seven (7) member board of directors of First Priority Life. Currently, BCNEPA, as the sole shareholder of First Priority Life, nominates all seven (7) members to the board of directors.
25. As described in the Application, the Highmark directors of First Priority Life will have supermajority voting power in such events as fundamental corporate changes and diminished Risk-Based-Capital levels of First Priority Life.
26. As stated in the Application, the consideration for the transaction was determined through negotiations among the parties, and BCNEPA will receive an opinion from an outside consultant as to the fairness of the transaction to BCNEPA.

Standards for Review

27. Section 1402(f)(1) of the Insurance Holding Companies Act establishes the standards for approval of an application for a change in control of a domestic insurer.
28. The application for a change in control must be approved unless the Commissioner finds any one of certain enumerated conditions to be present.

Licensing Requirements

29. When analyzing an application for change in control under Section 1402 of the Insurance Holding Companies Act, the Commissioner reviews the requirements for continued licensure of the domestic insurer being acquired.
30. The lines of insurance for which an insurance company may be incorporated and become licensed to write are set out in Section 202 of the Insurance Company Law, Act of May 17, 1921, P.L. 682, as amended, 40 P.S. §382 (“Insurance Company Law”).
31. The minimum paid up capital stock and paid in surplus required of a stock insurer for each line of insurance is set out in Section 206 of the Insurance Company Law.
32. In accordance with Section 206 of the Insurance Company Law, First Priority Life is required to maintain a minimum paid up capital stock of \$1,100,000 to write the lines of insurance for which it is presently licensed.
33. In accordance with Section 206 of the Insurance Company Law, First Priority Life is required to maintain a minimum paid in surplus of \$550,000 to write the lines of insurance for which it is presently licensed.
34. Upon completion of the transaction, First Priority Life will have paid up capital in an amount that will satisfy the statutory minimum required of a life insurance company licensed to write the lines of authority currently held by First Priority Life.
35. Upon completion of the transaction, First Priority Life will have paid in surplus in an amount that will satisfy the statutory minimum required of a life insurance company licensed to write the lines of authority currently held by First Priority Life.

Competitive Impact

36. The acquisition of control of First Priority Life is subject to review and analysis under certain specified provisions of Section 1403 of the Insurance Holding Companies Act to determine whether the effect of the acquisition of control would be to substantially lessen competition or tend to create a monopoly in the Commonwealth (“Competitive Standard”). The applicable portions of Section 1403 for the Competitive Standard analysis are 1403(c)(2) (informational requirements) and 1403(d)(2) (standards for analysis).
37. For purposes of reviewing the competitive impact of the change in control of First Priority Life, “product market” is defined in Section 1403(d)(2) of the Insurance Holding Companies Act as the direct written premium for the line of business as

- reported on the Annual Statement which is required to be filed by insurance entities doing business in the Commonwealth.
38. The relevant product market for the Competitive Standard analysis of the Application under Section 1403(d)(2) of the Insurance Holding Companies Act, as well as the companion application for the acquisition of control of First Priority Health, is the accident and health line of business.
 39. Although First Priority Life has had no business, it is authorized to write accident and health business, which is the business reported by its affiliate, First Priority Health, and its parent, BCNEPA.
 40. The applicable Annual Statement to be utilized for a Competitive Standard analysis of the Application is the 2002 Annual Statement which was available at the time the Application was filed.
 41. Section 1403(d)(2) of the Insurance Holding Companies Act provides that the relevant geographical market for a competitive standard analysis is the entire Commonwealth unless available information indicates that a smaller geographical market should be adopted.
 42. Because Annual Statements filed with the Department contain verified data which is reported for the entire Commonwealth of Pennsylvania, not by region or county, the geographical market for the Competitive Standard analysis is the entire Commonwealth.
 43. Section 1403 of the Insurance Holding Companies Act specifies the guidelines to be used for a competitive standard analysis if the market is considered a highly concentrated market.
 44. The total accident and health market for the Commonwealth of Pennsylvania, including the direct written premium of the health plan corporations, was approximately \$24.17 billion according to the 2002 Annual Statement data.
 45. After excluding the direct written premium for the accident and health line of business of entities expressly excluded from the definition of “insurer” in Section 1401 of the Insurance Holding Companies Act, the accident and health market for the Commonwealth of Pennsylvania, for purposes of the Competitive Standard analysis, was approximately \$18.65 billion as stated in the Application and as confirmed by the Department according to the 2002 Annual Statement data.
 46. Because Highmark and BCNEPA are health plan corporations and are specifically excluded from the purview of the Insurance Holding Companies Act, their portion of the direct written premium for the accident and health line of business written in Pennsylvania is specifically excluded from the Competitive Standard analysis

of this Application.

- 47. According to Section 1403 of the Insurance Holding Companies Act, a market is highly concentrated if the market share of the four (4) largest insurers is 75% or more of that market.
- 48. For purposes of this Competitive Standard analysis, insurer, as defined in Section 1403 of the Insurance Holding Companies Act, includes any company or group of companies under common management, ownership or control.
- 49. For purposes of this competitive Standard analysis, the accident and health premiums written by the top four (4) insurers, as stated in the application and as confirmed by the Department according to the 2002 Annual Statement data, was as follows:

Insurer subsidiaries of Independence Blue Cross	\$ 6,117,739,000	32.81%
Insurer subsidiaries of Highmark, Inc.	3,140,550,000	16.84%
Aetna, Inc. and subsidiaries	1,217,285,000	6.53%
Coventry Health Care Group	<u>1,093,190,000</u>	<u>5.86%</u>
Totals	<u>\$11,568,764,000</u>	<u>62.04%</u>

- 50. According to the 2002 Annual Statement data, the top four (4) insurers writing in the accident and health lines of business did not control 75% of this product market.
- 51. According to the 2002 Annual Statement data, the accident and health product market was not highly concentrated.
- 52. Section 1403 of the Insurance Holding Companies Act specifies the guidelines for the competitive standard analysis of a market that is not highly concentrated.
- 53. The guidelines are as follows:

Insurer A	Insurer B
5%	5% or more
10%	4% or more
15%	3% or more
19%	1% or more

- 54. The guidelines are applicable only to insurers who are in competition in the same market.
- 55. Section 1403 of the Insurance Holding Companies Act defines “involved insurer” as an insurer which either acquires or is acquired, is affiliated with an acquirer or

acquired or is the result of a merger.

56. For the purpose of this Competitive Standard analysis, the subsidiaries and affiliates of Highmark which report direct written premium for the accident and health line of business are the involved insurers of Highmark.
57. Because First Priority Life is the domestic insurer to be acquired and because it has First Priority Health as its affiliate which reports direct written premium for the accident and health line of business, First Priority Life and its affiliate are the involved insurers for purposes of this Competitive Standard analysis.
58. The total market share of the involved insurers of Highmark is considered Insurer A for purposes of this Competitive Standard analysis.
59. The market share of Insurer A, as stated in the Application and as confirmed by the Department in the 2002 Annual Statement data, was approximately \$3.14 billion or 16.84%.
60. The total market share of First Priority Life's direct written premium for the accident and health line of business is considered Insurer B for purposes of this Competitive Standard analysis.
61. The market share of Insurer B, as stated in the Application and as confirmed by the Department in the 2002 Annual Statement data, is approximately \$0.24 billion or 1.29%.
62. As a result, the accident and health market shares of Insurer A (16.84%) and Insurer B (1.29%) are within the guidelines for a market that is not highly concentrated.
63. The acquisition of control of First Priority Life will not lessen competition or tend to create a monopoly in the Commonwealth because the market shares of the involved insurers do not exceed the market share levels established in Section 1403 of the Insurance Holding Companies Act.

Financial Condition of Applicant

64. When analyzing an application for an acquisition of control under Section 1402 of the Insurance Holding Companies Act, the Department reviews the financial condition of the acquiring person(s).
65. The Department has reviewed financial statements submitted by Highmark as of December 31, 2003.

66. As of December 31, 2003, Highmark reported:

Assets of \$4,036,957,695

Liabilities of \$1,842,247,521

Shareholders' equity of \$2,194,710,174

67. The financial condition of Highmark will not pose any impediments to the change in control nor jeopardize the financial condition of First Priority Life.

Plans for the Acquired Insurer

68. When analyzing an application for an acquisition of control under Section 1402 of the Insurance Holding Companies Act, the Department reviews the plans or proposals which the acquiring party has for the insurer.

69. As provided in the Application, Highmark does not intend to liquidate First Priority Life, sell its assets or consolidate or merge it with any person or to make any other material change in its business or corporate structure.

70. As provided in the Application, the day-to-day operations of First Priority Life will continue to be handled by BCNEPA through an Administrative Services Agreement, as they are currently.

71. As provided under the Application, First Priority Life, by becoming a controlled affiliate of Highmark, will be able to offer products under both the Blue Cross and the Blue Shield servicemarks.

Management

72. When analyzing an application for an acquisition of control under Section 1402 of the Insurance Holding Companies Act, the Department reviews the competence, experience and integrity of the persons who will control the operations of the acquired insurer.

73. Biographical affidavits for all directors and executive officers of Highmark in addition to those new intended directors and executive officers of First Priority Life were reviewed by the Department.

74. The Department is satisfied that the persons who would control the operations of First Priority Life have such competence, experience and integrity that the interests of policyholders and the public would not be jeopardized.

75. If any of the above Findings of Fact are determined to be Conclusions of Law, they shall be incorporated in the Conclusions of Law as if fully set forth therein.

CONCLUSIONS OF LAW

1. A proposal for a change in control of a domestic insurer must be filed with the Commissioner for approval in accordance with the Insurance Holding Companies Act, 40 P.S. §§991.1401 – 991.1413.
2. The definition of “insurer” in Section 1401 of the Insurance Holding Companies Act includes insurers authorized to transact the business of insurance in the Commonwealth of Pennsylvania, including HMOs.
3. Nonprofit health plan corporations operating hospital plans and professional health services plans are excluded from the definition of “insurer” in Section 1401 of the Insurance Holding Companies Act.
4. Under Section 1401 of the Insurance Holding Companies Act, the Commissioner has jurisdiction to review and approve the change in control of First Priority Life.
5. Section 1402 of the Insurance Holding Companies Act requires that the Department review the Application with respect to the competitive standard analysis as provided in Section 1403.
6. For purposes of making a Competitive Standard analysis of the impact of the transaction proposed in the Application, the relevant product market is the direct written premium as reported on the 2002 Annual Statement for the accident and health line of business, and the relevant geographic market is the entire Commonwealth of Pennsylvania.
7. The Competitive Standard analysis under Section 1403 requires a comparison of the market shares of the involved insurers, including their affiliates.
8. The exclusion of the market shares of Highmark and BCNEPA from the Competitive Standard analysis is appropriate under the Insurance Holding Companies Act.
9. The acquisition of control of First Priority Life by Highmark does not cause a prima facie violation of the Competitive Standard of the Insurance Holding Companies Act.
10. A hearing is not required when reviewing an application for acquisition of control under Section 1402(f)(2) of the Insurance Holding Companies Act unless the parties to the filing so request. Otherwise, the Commissioner, in her discretion, may elect to hold a hearing.
11. Since neither party to the Application requested a hearing within ten days after the Application was filed, a hearing was not mandatory, and the Commissioner has

elected not to hold a hearing.

12. Under Section 1402 of the Insurance Holding Companies Act, the Commissioner must approve an application for a change in control unless the Department has found that:
 - a) The insurer will not be able to satisfy the requirements for the issuance of a license to operate the line or lines of business for which they are presently licensed;
 - b) The change in control will substantially lessen competition in insurance in this Commonwealth or tend to create a monopoly therein;
 - c) The financial condition of the acquiring company is such as might jeopardize the financial stability of the insurer or prejudice the interests of its policyholders;
 - d) Any plans to liquidate the insurer, sell its assets or consolidate or merge it with any person, or to make material changes in its business or corporate structure or management are unfair and unreasonable to policyholders of the insurers and not in the public interest;
 - e) The competence, experience and integrity of those persons who would control the operation of the insurer are such that it would not be in the interest of policyholders and the general public to permit the acquisition of control; or,
 - f) The acquisition is likely to be hazardous or prejudicial to the insurance buying public.
 - g) The acquisition of control is not in compliance with the laws of this Commonwealth, including Article VIII-A, Insurance Company Mutual-to-Stock Conversion Act.
13. Under Section 1402 of the Insurance Holding Companies Act, the Commissioner has not found that any of the above conditions are present with respect to the change in control of First Priority Life.
14. If any of the above Conclusions of Law are determined to be Findings of Fact, they shall be incorporated in the Findings of Fact as if fully set forth therein.

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:
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ORDER

Upon consideration of the foregoing, the Insurance Commissioner of the Commonwealth of Pennsylvania (“Commissioner”) hereby makes the following Order:

The application of Highmark Inc. (“Highmark”) in support of the request for approval to acquire control of First Priority Life Insurance Company, Inc. (“First Priority Life”) as set forth in the Application, is hereby approved, subject to this Order and the following conditions:

1. All necessary regulatory filings and approvals are obtained by the parties prior to consummation of the Stock Purchase Agreement.
2. Highmark shall provide to the Department a list of closing documents within five (5) days after consummation of the subject transaction and shall maintain the listed documents and make them available to the Department for a period of not less than five (5) years from the date of consummation.
3. Hospital Service Association of Northeastern Pennsylvania shall provide the Department with a copy of the independent opinion of the fairness of the consideration for the transaction.

This Order is effective immediately and valid for one (1) year, provided no material changes are made to the transaction prior to consummation.





M. DIANE KOKEN
Insurance Commissioner