

**BEFORE THE INSURANCE DEPARTMENT
OF THE
COMMONWEALTH OF PENNSYLVANIA**

**Statement Regarding the Acquisition of Control of or Merger with
Domestic Insurers:**

**Hospital Service Association of Northeastern Pennsylvania
d/b/a Blue Cross of Northeastern Pennsylvania;
First Priority Life Insurance Company, Inc.;;
HMO of Northeastern Pennsylvania, Inc.,
d/b/a First Priority Health**

By Highmark Inc.

**HIGHMARK INC. (“Highmark”) RESPONSE TO INFORMATION
REQUEST 2.1.10 FROM
THE PENNSYLVANIA INSURANCE DEPARTMENT**

REQUEST 2.1.10:

Provide an analysis of how the Applicant has determined that there is no cash consideration for the Transaction in light of its commitments to employment and assumption of debt, including, without limitation, contingent debt and charitable commitments.

RESPONSE:

Highmark certifies to the best of its knowledge, information and belief as follows:

Highmark determined that there is no cash consideration for the Transaction primarily because the Transaction involves the combining of two nonprofit organizations, neither of which has equity owners. The commitments by Highmark set forth in the Merger Agreement are common in transactions of the nature of the Transaction and do not constitute cash consideration payable to any Person for the acquisition of any assets, business or property. Following is a discussion of specific provisions of the Merger Agreement. Capitalized terms used herein and not defined in the Request for Information have the meanings assigned to them in the Merger Agreement.

Section 1.4 of the Merger Agreement provides that the Merger will have the effects set forth in the Pennsylvania Nonprofit Corporation Law. Specifically, at the Effective Time, the separate corporate existence of BCNEPA will cease, and all the property, rights, privileges, powers and franchises and all choses in action of BCNEPA will be vested in Highmark as the surviving corporation, and all debts, liabilities and duties of BCNEPA will be the debts, liabilities and duties of Highmark as the Surviving Corporation. Section 1.4 thus simply restates the law. In every merger, the surviving person succeeds to the assets and liabilities of the merging person. In the case of the Transaction, Highmark is assuming BCNEPA’s debts, but it is also succeeding to its assets. Based

on its due diligence investigation, as well as its knowledge of the business and affairs of FPH and FPLIC as a result of its ownership interests in those entities, Highmark believes that the value of BCNEPA's assets exceeds the value of its liabilities. Thus, Highmark does not believe that its assumption of BCNEPA's debt (including contingent debt and charitable commitments) constitutes consideration for the Transaction. (Highmark also does not believe that assumption of debt constitutes cash consideration in any event.)

Section 3.1(c) of the Merger Agreement provides that BCNEPA has the right to (i) contribute, dispose of or otherwise transfer all or any portion of the business, operations or assets, together with all of the liabilities, or all or any portion of the ownership interests of, AllOne Health Group, Inc. ("AHG") and/or Health Resources Corporation ("HRC") (or the proceeds of any such disposition) to a Charitable Organization prior to the Effective Time. Section 3.1(c) provides further that on the Closing Date, but prior to the Effective Time, BCNEPA may make to one or more Charitable Organizations, out of its surplus capital, a contribution up to the amount of the Closing Contribution, which is defined in Section 8.14(rr) of the Merger Agreement to mean \$90,000,000 less any cash contributions made by BCNEPA to AHG and/or HRC prior to the Effective Time, not to exceed an aggregate of \$20,000,000. Notwithstanding the foregoing, if BCNEPA's RBC as of the end of the month immediately prior to the most recently completed calendar month prior to the Closing Date is or would be less than 375% after giving effect to the amount BCNEPA intends to contribute (together with any previous or contemporaneous Permitted Contributions), the amount of the Closing Contribution will be reduced by such amount as will be necessary to cause BCNEPA's RBC to be increased to 375% (provided, however, that in no event may the sum of the Closing Contribution and any Permitted Contribution be reduced to less than \$50,000,000).

Based on the foregoing, BCNEPA, and not Highmark, is the source of all amounts being contributed to the Charitable Organizations prior to the Effective Time.

Section 6.4(a) of the Merger Agreement provides that if BCNEPA's RBC as of the date set forth in the certificate required to be delivered at the Closing equals or exceeds 725% (before giving effect on a pro forma basis to any Permitted Contribution or the Closing Contribution) and the 2015 operating loss of the Acquired Business is less than \$15,000,000, Highmark as a subsequent charitable contribution will cause to be contributed an amount equal to \$10,000,000 to the Charitable Organization(s) designated by the BCNEPA Advisory Board Representatives. . While, by virtue of the structuring of the Transaction, payment of the additional \$10,000,000 charitable contribution (if made) will be made by Highmark following the Closing, the contingencies assure that the net contribution to Highmark's reserves, taking into account the value of the assets (including the value of the reserves) acquired by Highmark, and the contribution to Highmark's RBC will be accretive, even after giving effect to the contribution. In effect, then, BCNEPA's assets, not Highmark's, will fund the post-Closing contribution, and if they do not, the contribution will not be made. For this reason, Highmark does not believe that the post-Closing contribution constitutes cash consideration for the Transaction.

Section 6.4(e) of the Merger Agreement provides that in the event that Highmark effects a sale of the Business, or effects a conversion in which the Business operates as a for-profit Person, prior to the fifth (5th) anniversary of the Closing Date in which (in either case) Highmark or its Affiliates receive financial consideration in connection with such sale or conversion, Highmark will simultaneously with the consummation of such sale or conversion contribute or cause to be contributed an amount equal to twenty-five percent (25%) of the consideration so received to one or

more designated Charitable Organization(s). Highmark has no present intent to effect a sale or conversion of the Business. These provisions of the Merger Agreement are intended to assure that, if it does, another nonprofit organization will benefit from the sale or conversion. Given the contingent nature of the payment referred to in this Section and the fact that the payment would come only from the proceeds (if any) of any sale or disposition contemplated thereby (with Highmark retaining 75% of such proceeds), Highmark does not believe that this arrangement constitutes cash consideration for the Transaction.

Section 6.2(a) of the Merger Agreement provides that each BCNEPA employee of the Acquired Business who is in good standing as of the Closing Date will become an at-will employee of Highmark with annual cash compensation not less than the annual cash compensation in effect for such employee immediately prior to the Closing Date; and that each Affected Employee who remains in good standing will be retained, for a period of not less than eighteen (18) months following the Closing Date, in his or her position or in a comparable position, with no reduction in annual cash compensation. Sections 6.2(b) and (c) provide for severance payments to Affected Employees (x) who were BCNEPA employees for at least one (1) year before the Closing Date if their employment is terminated within eighteen (18) months following the Closing Date (Section 6.2(b)) or (y) if their employment is terminated within two (2) years following the Closing Date (Section 6.2(c)). Section 6.2(g) of the Merger Agreement provides that any individual who is an Affected Employee and entitled to the benefits determined pursuant to Section 6.2(b) or (c), but who is also party to a Contract listed on the BCNEPA Disclosure Letter with respect to Section 6.2(g), will be entitled to his or her benefits under such Contract but will not be entitled to any benefit under Section 6.2(b) or (c).

Section 6.3(a) of the Merger Agreement provides that, from and after the Effective Time, Highmark will operate the Acquired Business in a manner that is consistent with the historic corporate mission of BCNEPA and will cause its Affiliates to continue to seek innovative ways to provide reasonable support to community based programs in the BCNEPA Service Area. Section 6.3(b) of the Merger Agreement provides that, from and after the Closing, Highmark will (A) at all times maintain regional operations in the BCNEPA Service Area, and (B) until the fourth (4th) anniversary of the Closing Date, (1) use commercially reasonable efforts to cause the minimum number of full time equivalent employees of Highmark and its Affiliates (including the Affiliates of BCNEPA) who are resident in the BCNEPA Service Area to be equal to the lesser of (x) BCNEPA's average number of full time equivalent employees in the Business who were so resident during the one (1) year period immediately prior to the Closing Date or (y) the number of such employees on the Closing Date, (2) use commercially reasonable efforts to maintain employment levels in the Business that are in proportion to the employment levels that Highmark maintains in its other Pennsylvania operating locations that directly service its Pennsylvania-based health policy holders and subscribers, and (3) maintain the mean and median cash compensation of the Affected Employees at least at the same levels as in effect in the one (1) year period prior to the Closing Date. Section 6.3(b) further provides that from and after the Closing Date, Highmark will, and will cause its Affiliates to, act in good faith to attempt to identify and create new employment opportunities in the BCNEPA Service Area as business needs and conditions permit.

Highmark does not believe that its agreements to continue the employment of individual BCNEPA employees of the Acquired Business and to pay them for their continuing services in the ordinary course or to make payments to individual employees if Highmark determines to terminate the employment of such persons constitute cash consideration for the Transaction, particularly since none of the payments will be made to BCNEPA or any successor to any of its business, assets or

properties. Similarly, Highmark does not believe that its agreements to maintain BCNEPA operations, provide community support to the historical BCNEPA service area in a manner consistent with BCNEPA's historical mission (which is also consistent with Highmark's mission) and to maintain a presence in the northeastern Pennsylvania community, all of which, as noted above, are common in nonprofit transactions in which there is no owner of the equity of the "acquired" organization, constitute cash consideration.

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