COMMONWEALTH OF PENNSYLVANIA
HOUSE OF REPRESENTATIVES
INSURANCE COMMITTEE

Gannon University
Waldron Campus Center
Yale Room
124 West 7th Street
Erie, Pennsylvania 16541

Monday, August 25, 2008
1:20 p.m.

Public Hearing on Proposed Merger between
Independence Blue Cross and Highmark

Before:

Anthony DeLuca, Allegheny County, Chairman

Florindo J. Fabrizio, Erie County

Thomas Petrone, Allegheny County

Nick Kotic, Allegheny County

Edward P. Wojnaroski, Sr., Cambria County

Brad Roae, Crawford County

Patrick Harkins, Erie County

Also Present:

Rick Speese, Executive Director

Reported by Tamara Y. Doxey
Ferguson & Holdnack Reporting, Inc.

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MR. DELUCA: Good afternoon. We call this Insurance Hearing to order. And we want to welcome the House Insurance Committee to this Hearing today. Before I do that, I would like to have the members introduce themselves. From my left.

MR. KOTIC: Representative Nick Kotic, Allegheny County.

MR. PETRONE: Representative Thomas Petrone, Pittsburgh, 27th District, Allegheny County.

MR. FABRIZIO: Flo Fabrizio, right here.

MR. DELUCA: This is my Executive Director, Rick Speese, to my left. I'm Representative Tony DeLuca from Allegheny County, Chairman of the Insurance Committee.

MR. WOJNAROSKI: Ed Wojnaroski, Cambria County.

MR. ROAE: Brad Roae from Crawford County and Gannon University graduate.

MR. DELUCA: As I said, ladies and gentlemen, I welcome you to this House Insurance Committee meeting today on the proposed consolidation of Independence Blue Cross and Highmark.

I would first like to thank my good friend Representative Fabrizio for hosting this Committee. Thank you very much. Representative Fabrizio has been and continues to be an effective and forceful leader in Harrisburg and in this Committee.

I would also like to thank the good folks here at Gannon University for graciously allowing the Committee to hold our hearing here this afternoon.

Act 62 passed by the legislature in July and signed by the Governor, provided, among other important provisions, this Committee and the Senate Banking and Insurance Committee with the same specific authority regarding the review of proposed consolidations and mergers regarding Pennsylvania's Blue Cross plans.

In addition, the Act provides the Insurance Commissioner with added authority to more closely peruse such proposed mergers. Specifically, the Act provides that the two committees can review all documents and all filings hold hearings and, most importantly, to develop written comments and recommendations regarding all such mergers or consolidations.

The Committee must submit any such comments within 45 days of the close of the public comment period set by the Insurance Commissioner.

The Insurance Department shall publish a date for the close of the public comment period in the Pennsylvania Bulletin.

The Commissioner may then issue a final order on or after 105 days following that public comment period.

Also, the Commissioner and his staff shall be

available to provide testimony to the Committees as they determine.

In this regard, I would like to thank Insurance Commissioner Ario for appearing before this Committee today.

This will not be the last hearing the committee will hold on this issue. We had a joint hearing in Harrisburg between the Senate and the House. This will be the first one with the House Committee. And we will be having others throughout the Commonwealth.

Act 62 provides the Insurance Committee with this important responsibility, so it's incumbent upon the members to familiarize themselves with the many issues involved regarding this proposed consolidation.

The Insurance Commissioner has been tasked to decide whether or not this proposed merger is, in fact, a good deal for Pennsylvanians.

Some of the questions which he must consider are: No. 1, how will this consolidation affect competition in the health insurance marketplace. Two, what is the benefit for the policyholders of both companies after the merger. Three, what effect will this have on health insurance rates now and in the future. Four, what will this mean to the Blue's social mission.

These are just a few of the hundreds of

questions that must be answered before the Commissioner makes his final decision.

As I said, the House Insurance Committee will be a participant in this discussion. And, hopefully, will be able to assist the Commissioner in this difficult task.

Finally, since the combined companies will, if their merger is approved, be one of the largest health insurers in this nation, so we must get it right.

And this decision will have far-reaching consequences on our state and on the people we represent.

Published reports of the two CEO's salaries, after they merge, indicate at least two people will certainly benefit by this consolidation. It's troubling to read of such salaries for running a benevolent nonprofit health insurer.

So we need to ensure that the remaining 12 million residents of Pennsylvania benefit as well.

Again, I would like to thank the members of this Committee. And I also would like to thank the public and the people who are here who are going to offer testimony to educate this Committee so that we can bring this information back to our colleagues in Harrisburg.

Before we start, I would like to have Representative Fabrizio say a few words.

MR. FABRIZIO: Thank you, Mr. Chairman. Just very

simply, I would like to welcome all the Committee members here. I would like to thank the Committee members here for conducting this hearing within the fine confinements of the Second Legislative District in the great Northwest. We welcome everybody here. For those of you who have been here before, welcome, again. For those of you who haven't been here before, enjoy Erie. It's beautiful. Thank you.

MR. DELUCA: Thank you, Representative Fabrizio. The first individual we have to testify is Dan Vukmer, the Vice President and General Counsel for UPMC Health Plan. Welcome, Dan. Thank you for coming today to testify.

MR. VUKMER: Thank you, Mr. Chairman, Committee Members. Good afternoon. My name is Dan Vukmer. I'm the General Counsel for UPMC Insurance Division. I'm testifying on behalf of Diane Holder, Vice President and CEO of the Health Plan.

I appreciate the opportunity to come before you to provide testimony related to the potential consolidation of Highmark and IBC.

For those of you who may be less familiar with the UPMC, we are an integrated delivery and financing system and the second largest non-governmental employer in Pennsylvania.

Our health insurance companies provide healthcare financing services to over 1.2 million members

through a variety of insurance and prepaid health plan programs.

These programs include commercial insured and self-funded arrangements, Medicare, Medicaid, Behavioral Health programs and workplace plans like short-term disability, employee assistance and wellness programs.

We pay more than $2 billion annually in healthcare claims and healthcare costs for our Pennsylvania customers.

Our health plans were created twelve years ago in response to the need for alternatives to the Blue Cross and commercial companies that existed. We have grown to serve more than 6,000 employers in Western Pennsylvania. We have developed a strong working relationship with the Department of Public Welfare, and are proud that we have been the fastest growing Medicaid plan in our HealthChoices zone for the past two years.

In fact, nearly two out of every three newly eligible Medicaid recipients in our HealthChoices zone choose our plan, UPMC for You, over the competitive options. We also serve Medicaid members statewide through our behavioral health company, Community Care.

Additionally, we have seen strong growth in our Medicare programs, in part, driven by our exceptionally high retention rates of over 95 percent. We also have the

only large Special Needs Plan for dually-eligible Medicaid and Medicare members in our region that has experienced growth at all.

Our two-year-old Children's Health Insurance Program exceeded 5,000 children in record time, and we are also pleased that our EAP and wellness programs have been well received by our large and mid-sized employers. We focus on clinical quality outcomes and have received recognition for our quality outcomes, innovation and ethics.

The landscape in Pennsylvania has been competitive, but we have succeeded in growing our companies across all lines of business within Western Pennsylvania and, in some cases, across the Commonwealth. We focus on bringing affordable options, innovative programs, high quality outcomes and an exceptional level of service to our customers.

Although commercial membership growth is challenging, we have had some success. However, our greatest growth in recent years has been across all of our government programs, where historical distribution channels are less relevant than in commercial products. A competitive insurance market benefits the public and drives innovation, cost containment and quality. We are very concerned that the proposed Highmark/IBC merger will reduce the competitive opportunities in the State across commercial

and governmental business, resulting in fewer choices for consumers and ultimately higher cost, less innovation and lower quality. Consequently, we oppose the consolidation.

There are three key reasons for our opposition. First, the newly created entity will create a dominant statewide company that will diminish competition from other health insurers. Second, the transaction will harm consumers, because diminished competition increases costs, reduces access and leads to less innovation and quality improvement. Finally, an entity the size of the combined Highmark/IBC will have the ability to unduly influence health policy and regulation in the Commonwealth of Pennsylvania in ways that will not be in the best interest of Pennsylvania consumers.

We greatly appreciate that the role of the Pennsylvania Insurance Department is to protect consumers and ensure that those consumers have access to high quality, affordable care. The Insurance Company Holding Act provides that the focus of the Department should be the impact of the proposed merger on the competitiveness of the health insurance market. At the heart of that discussion is the question: Do these companies operate on a regional basis or are they statewide competitors?

The fact is, Pennsylvania is one of the few states with separate Blue Cross and Blue Shield licensees.

Highmark controls the Blue Shield license for the entire state of Pennsylvania and can compete across the entire state. It utilizes its license in Western Pennsylvania in conjunction with its Blue Cross license, but it also competes in Northeast Pennsylvania in conjunction with Blue Cross of Northeast PA, and it competes in the center of the state directly against Capital Blue Cross.

The fact that Highmark does not compete in the eastern portion of the state, in and around Philadelphia, is not a function of separate licensed geographic areas for Highmark and IBC, but rather of a recently expired agreement between the plans not to compete. An agreement not to compete should not be the basis on which the Department defines the market.

The size of the new entity that would be created would be unprecedented in any one geographical market in the United States. It takes a moderately competitive market, as Pennsylvania now stands, and creates a new dominant competitor with a statewide footprint. Highmark/IBC would account for approximately 75 percent of the statewide HMO enrollment, and 64 percent of the PPO enrollment for commercially insured residents. Collectively, they would provide coverage to seven out of 10 Pennsylvania commercially insured residents under the age of 65.

Additionally, the combined entity will operate the largest administrative-services-only provider for large employers in Pennsylvania, a platform it will use to solidify its dominant health insurance market position. The combined entity will be a megainsurer, the eighth largest in the nation. The other mega insurers operate in at least four states, most of them in 20 or more states.

In contrast, almost all of the new entity's business will be concentrated in one state: Pennsylvania. It will hold more than $10 billion in assets and almost $7 billion in capital and surplus. It's 2007 Pennsylvania derived premium revenue of more than $12 billion will be almost seven times more than the next largest health insurer operating in the Commonwealth.

Let me now turn to public sector government business, which is of equal importance in understanding the problems inherent in this potential consolidation. Currently, Medicare Advantage and Medicaid Managed Care markets are more competitive than commercial markets in Pennsylvania. Highmark and IBC separately have less than 50 percent of MA, and even less in Medicaid. The consolidation will enable the new entity to become even more dominant in the Medicare market.

For example, in the Lehigh Capital region, post this merger, 80 percent of the Medicaid members will be

covered through the new entity versus only 40 percent covered by IBC and Highmark today. Similarly, it will be in a position to use its enormous surplus to potentially drive Medicaid competitors from the market. This new entity will be positioned to control market pricing over the long run, deciding when to bid aggressively and when to raise pricing significantly, as we have seen occur repeatedly over the years in the commercial group business where pricing bounces significantly.

This consolidation also positions the new entity to take advantage of any new Federal insurance changes that may be on the horizon, which are procured and implemented at the statewide level. This could include group purchasing coalitions or individual coverage programs, with or without premium support from government.

In short, the proposed consolidation is one of the largest of its kind in U.S. history, and will convert a competitive market to one controlled by a monolithic competitor overnight. Highmark/IBC will control all markets in which it competes: Commercial, Medicaid, Medicare, stop loss, dental, vision and ASO business.

Our second key reason for opposing the merger is the concern that it will harm consumers and not improve affordability, access or quality.

Value to the consumer comes in the form of

more affordable healthcare. Affordability requires lower costs. Healthcare costs have two parts: What is spent on medical care, and what is spend on administrative expenses.

When we evaluate the reasons for the healthcare cost increases in the United States, the most significant cost drives, for the past two decades, have been the increase in the prevalence of chronic conditions and the increase in what is called the "treated prevalence" of disease. That is, more people have diseases, and more people who have diseases are being treated for those conditions, including treatment with new technologies.

Administrative costs, although very important to control, do not appear to have contributed to the trend in cost increases. If healthcare is going to become more affordable, there has to be a way to deal with the cost factors that are actually driving the trends. Highmark and IBC have yet to show that the proposed merger will enable them to control medical spending more effectively together than they can independently.

Are they planning to adequately reimburse hospitals and physicians? Pennsylvania hospitals are already, on average, financially fragile, and Pennsylvania is already losing physicians to markets where reimbursement is more attractive. New and innovative ways are needed to prevent and treat chronic disease. There is no reason to

think larger insurers are more effective in producing higher quality outcomes.

In fact, most of the insurers nationwide that score the highest in quality outcomes for their members are small, often regional plans, which have the ability and the primary mission to focus on local care strategies with their members and the local physician and hospital communities.

The second way to reduce costs is to lower the administrative portion of the expense. Highmark and IBC contend they will do this as part of the value of the consolidation. There is no evidence, however, that mergers of health insurance companies result in lower administrative costs.

Our testimony includes a chart showing administrative costs before and after mergers of Blues plans across the country. It shows that, post merger, there is virtually no reduction in administrative costs as a percentage of premiums. We would ask for specific substantive evidence that health insurance mergers, like this one, will result in administrative savings that benefit premium pricing and consumer affordability.

Is a merger required to reduce administrative costs? The answer is clearly, no. It is possible to be a smaller plan and have lower administrative costs. The UPMC Health Plans have consistently run at or below 8 percent

administrative costs and we have not needed the alleged scale economies to achieve this relatively low administrative cost structure.

What we have needed is efficient methods and a competitive need to keep costs low to grow our business. Lower overhead is one of the reasons we have been successful.

We would ask the Department to evaluate what the track record has been for other mergers, including the merger between Blue Cross and Blue Shield to create Highmark in 1996.

Did the merger create administrative efficiencies that led to lower administrative expense ratios? It does not appear to us that it did. A review of Blues' mergers in other parts of the U.S. suggests the same result. We find that there is little reason to believe that either scale or scope economies will result in savings.

Are premiums higher in states with more concentrated markets? The answer is yes. In general, our evaluation shows that in states where there is more competition among health insurers, consumers win. Where companies compete, they develop new and innovative ways of delivering their products or services and seek out the highest level of efficiency for that delivery. The result is more affordable prices for consumers. Health insurance

is no different.

An examination of data from 31 states generated by the Department of Justice and the Association of Health Insurance Plans, of which both Highmark and IBC are members, shows that the average cost of health insurance premiums in states with higher-than-average levels of competition is 12 percent lower than premiums in states with lower-than-average competition.

Will the merger improve access to quality healthcare? To answer that question, the Department must consider the impact of the merger on healthcare providers - physicians and hospitals. If the merger reduces access to quality healthcare, consumers are hurt.

After their consolidation, Highmark/IBC will have even more negotiating power, enabling it to reduce the prices it pays to providers. If healthcare providers are forced to leave the state or close operations in areas of the state that currently have marginal access, or have no resources to invest in aging plants or improved technology, consumers will suffer.

In fact, data shows that healthcare providers are on more tenuous financial ground in those states where there are dominant health insurance companies. The healthcare providers - doctors and hospitals - have older facilities, less money available for upgrading care and

services, and limited opportunity to save for future needs.

Pennsylvania hospitals, on average, already perform below national averages across key financial indicators, as reflected in the chart included in our written testimony. The system is fragile, and in Pennsylvania, we have the additional responsibility of caring for one of the nation's oldest populations.

Pennsylvania's hospitals are not the only healthcare providers suffering from the consequences of lower reimbursement. In addition to the adverse impact to be felt by hospitals, an already oppressed physician market will simply get worse. There was a reduction of 1632 physicians involved in direct patient care in Pennsylvania between 2004 and 2006. This reduction has been reflected in just about every physician specialty and geographic region in the Commonwealth.

Approximately, 6 percent of Pennsylvania physicians are under 35, while 50 percent are over the age of 50. Residency retention, for those who stay in Pennsylvania to actively practice, has dropped from 60 percent in 1992, to approximately 22 percent in 2006.

Coincidentally, Pennsylvania physicians receive some of the lowest insurance reimbursement in the nation from both Medicaid and commercial insurance for evaluation and management services. Based on the conduct of

dominant Blues in other states, as well as Pennsylvania, reimbursement to Pennsylvania's physicians will be driven even lower by the Highmark/IBC entity as the super dominant carrier, thus exacerbating Pennsylvania's physician exodus problem.

Therefore, the answer to the second question, will the proposed merger benefit consumers is, no. It will not improve affordability of healthcare, access to healthcare or quality of care. In fact, the merger will be harmful to all three.

The third reason we oppose the merger relates to the role an entity this size has in influencing health policy and healthcare regulatory issues. Questions such as: What should be the size of allowable reserves? How can reserves be used? What is considered a community benefit? What services such as pharmacy or mental health should be carved in or carved out of certain benefits? What should pay-for-performance plans look like? How should risk pools be established? What is the role of consumer oversight or legislative oversight? As well as a myriad of other questions that are the purview of not only the Insurance Department, but also the Department of Health, Department of Public Welfare, and the Office of healthcare Reform and our legislators, among others.

The proposed merger will concentrate even

greater influence in policymaking matters into the hands of one organization. It will be difficult, if not impossible, for officials to manage an organization that represents eight million citizens on complex, industry-specific issues that are often shades of grey rather than black and white. In other states, when market share has been highly concentrated, the influence of the dominant entity appears to grow. For example, there is significant documentation of concerns among citizens in Michigan related to consolidation and the resulting influence there.

We will be able to provide the presentation from the Coalition for Access and Affordability that was given to the Michigan legislature in April, 2008 for your further review, if you would like to have one.

On a final note: The merged companies would reportedly return one billion dollars to the Commonwealth in the form of community investment. The size of the investment being offered by the two companies, in return for approval of the consolidations, seems woefully inadequate for the premium revenue they will derive from the Pennsylvania insurance market, which we estimate to be at least $500 billion over a ten-year period. A similar transaction among publicly traded companies would require an investment of tens of billions of dollars.

All of Highmark and IBC's conduct paves the

way for these two companies to create a single dominant statewide insurer for all government and commercial products. We are concerned that if this consolidation occurs, the combination is more likely to convert to a publicly traded company in the future, as is happening in a number of other states. The market value of what will be created is something that we believe the Department should appraise. A billion dollars seems like an unusually low contribution for the opportunity to control virtually all market segments in such a large state.

Finally, I would like to urge the Commissioner, and ask that this Committee urge the Commissioner, to keep the public comment period open such that the legislature's 45-day review period will occur when the legislature is actually in session for 45 days.

We are very concerned that there will be a push by Highmark and IBC to close the comment period by September 16th so that the legislature's review period can occur prior to sine die. This would be a serious problem in that the House will only be in session for 16 days and the Senate for 10 days prior to sine die. This is clearly not enough time for the legislature to perform all of the review of the question-and-comment activities that it is legally entitled to perform following the close of the public comment period. This becomes especially important given

that this transaction is clearly the most significant healthcare event in the history of Pennsylvania with far reaching, long-lasting and irreversible consequences.

In summary, I would like to thank you for the opportunity to provide this testimony. We believe that Pennsylvania has never faced a more important health policy decision.

Whether to allow the creation of a behemoth health insurer, within the boundaries of Pennsylvania, will have a more profound and lasting impact on health outcomes for the citizens of Pennsylvania and any other decision that will be made regarding health policy for the foreseeable future. We see the obvious benefit to Highmark and IBC. We do not see a public benefit for consumers or a benefit of this transaction for other healthcare stakeholders.

Thank you very much.

MR. DELUCA: Thank you, Dan. Thanks for the excellent testimony. Let me start off, if I could. In your testimony you keep referring to "competition." This merger will, in effect, incite the competition, as I listened to your comments. As you know, I'm from Western Pennsylvania.

MR. VUKMER: Yes, sir.

MR. DELUCA: And I don't see much competition out there, as it is today, so what competition are we talking about? And I don't see that happening with IBC either out

there in their section of the state. So when we keep throwing out this "competition," I'm wondering how, UPMC, if this merger doesn't go through, how you can say that other carriers are going to create this competition 15 years or 20 years, all this competition you hear about in the healthcare industry? And I'm just wondering, how do we create this competition if this merger doesn't go through? Are you permitted to go all over the state?

MR. VUKMER: Yes.

MR. DELUCA: Do you go all over the state, UPMC?

MR. VUKMER: Yes. The insurance division does through several channels. One is through our Medicaid Program. We're in a -- I can't recall all the counties, but a number of counties across the state. Our behavioral health company, Community Care, is in most counties across the state. Our commercial insurance is mostly in Western Pennsylvania at this time.

MR. DELUCA: Okay. There is no merger now, so what incited you from building your competitive market without this merger? And I go back to when John Paul first started the insurance business with UPMC, so I'm wondering why we have this competition. There was no merger then, there was no merger proposed, so why hasn't all of this competition came out in the last 20 years?

MR. VUKMER: Well, it's been an extremely

difficult environment to compete, so I will agree with you there, but we have managed to grow. The health plan was created 11 and a half, 12 years ago, in part, to create some competition in Western Pennsylvania, and we've done that. It's been an enormous challenge to compete against Highmark, but we've been able to do it.

But what's going to happen following this consolidation, however, we're going to end up in an entity with such a massive reserve and such control across the state, potentially, purchasing Northeast Blue Cross, which Highmark already owns 40-something percent of; potentially closing in on Capital Blue Cross, which is in the center of the state; and now you'll have reserves at such levels that if they decide to shoot that buying power towards Western Pennsylvania, competition could be much, much more difficult than it has been. If they decide to fire that laser in another part of Pennsylvania, then you can expect the competition in that area as well.

So we believe it's the growth in A, the amount of reserves and B, in the amount of influence it has across the state. If you look at Michigan, for example, it has one of the largest tax in the state. And if Michigan Blue wants something to happen, it happens. And so, that's what we don't want to see for Pennsylvania or for some of the regional insurers.

MR. DELUCA: Well, I agree with you on that. You know, you talk about the reserves, I have to start looking at UPMC, when you talk about reserves. I think it was last year, the first time they said close to a million dollars, Tom, UPMC? Not the healthcare, the hospital.

Now, I just read in the paper the other day that we're going to open up seven cancer centers throughout -- open up seven more cancer centers, which cost a lot of money.

MR. VUKMER: Right.

MR. DELUCA: And I keep hearing about this investment, they make their money on the investment. But I wondered if this money is being generated -- I understand about the invested part of it being generated by investments, I'm sure that the premiums are coming in for -- the reimbursements to the hospitals are coming in. Health provider money to be invested, so they can make the money; is that correct? They just don't get this money out of clear air to invest. It's got to come out of somebody's pocket. The same way as the Blues. I would imagine they would have a surplus and some of that surplus is invested.

MR. VUKMER: Sure.

MR. DELUCA: I'm just wondering if we're going to drive down healthcare, how does all of this expansion drive down healthcare? Tell me that.

MR. VUKMER: Sure. Well, unfortunately, I can't speak --

MR. DELUCA: I know you can't do that. I mean as part of being an insurance company, as we go through these expansions, as we expand these places, we got to pay. And the ratepayers have to pay for it in their rates. So I'm wondering -- you continue to say you want to drive down costs, get a handle on costs, and then we continue to expand. How are we ever going to drive down rates?

MR. VUKMER: Well, I'm not sure if expansion and building newer facilities for cancer treatment, for example, is somehow driving up the cost of those treatments. I would think that the more vicious we come at that, the lower the cost is going to be over time. But, again, I really can't speak to --

MR. DELUCA: I know you can't. I'm just trying -- the bottom fact is, we need to get a handle on cost. That's what we're looking for in the House. We know if we're ever going to get a handle on healthcare, we need to drive down the cost. But, about the fact that they're saying their going to save three to 400-billion dollars on administrative costs, you disagree with that; is that correct?

MR. VUKMER: Yes. We've had our economic's expert look at this and determine that A, we really haven't seen it across the country when there's been other mergers. We see

no reason for it to happen here. And B, when you actually look at what's being proposed, we believe those things could be done independently without having to merge the companies to do that.

MR. DELUCA: Okay. And the other aspect -- one thing you bring up -- I'm not certain I agree with your statement about the expansion, we'll work on that with the Commissioner if it's meaningful to doing something like that. But one of the things that really stuck out in your testimony about the healthcare is about how our doctors are leaving. And I know that we continue to say that. And some studies show they haven't left and some studies show they have. Depending on what study you have. I have a problem when we keep saying that we're losing doctors. Well, one of our universities, medical universities, only has a hundred slots. And a friend of mine who is an alumni of that medical facility -- I'm not going to say what medical facility it is -- tried to get his son in that facility to be a doctor, he's in the top of his class and everything, but in a different field, he wants to transfer over. But he's only competing for 33 percent of those slots, because as I understand, a third of those slots have to go to overseas students, a third have to go to their students and he was down to the other third.

Now, if we have such a shortage of doctors,

then why don't we open up some slots in our medical schools to get some of these physicians. Let's face it, if his son has to go out of state to a medical school, chances are that's where he's going to stay, out of state.

MR. VUKMER: That's my point.

MR. DELUCA: That's right. And naturally, if we had them studying here, they might stay here. Now, as far as the reimbursement, we have to look at what other states offer and stuff like that.

I keep hearing about physicians retiring. Well, you know what, if you can retire at your age limit -- retire at 50 years old -- I'm sure you're not going to go in another profession -- so if you can retire at 50, it can't be too bad. Unless they're going to be a salesmen or selling real estate or something like that, but I haven't heard they're going in another profession when they retire.

So I just wondered, you keep throwing out the fact that physicians are leaving, we're short of physicians; maybe we got to train more of those physicians to stay in this county. I just wanted to throw that out to you.

I keep hearing about a loss of physicians. It's been a -- we keep hearing it in Harrisburg. We keep seeing statistics on both sides of the ledger here. And I think the public needs to know that. Any questions on the left-hand side? Representative Nick Kotic.

MR. KOTIC: Thank you, Mr. Chairman. I'm just wondering whether UPMC has been involved with any other carriers since you've been in business?

MR. VUKMER: UPMC Health Plan or the insurance division?

MR. KOTIC: Yes.

MR. VUKMER: No, we have not.

MR. KOTIC: Okay. You have not been involved --

MR. VUKMER: No we have not.

MR. KOTIC: Okay. Thank you.

MR. DELUCA: I want to recognize Mr. Harkins in the audience. Representative Harkins, come on up here and join us, please. Representative Petrone?

MR. PETRONE: Thank you, Mr. Chairman. Just a comment and then a question. We want, living in this country, we want the best medical care, doctors, technology, research, doctors, diagnostics. We want the best of everything. You can't have it both ways. We just can't have the best of everything no matter how much we pay for it. Now, how we end up, that's up to you guys.

No. 2, I spent, two weeks ago, two days with people involved in the health system in Nova Scotia, Oshawa and other points of Canada. I don't know if you know much about what's going on up there, but I certainly hope we do not arrive at a situation with a healthcare system like

them. They have a disaster. I couldn't believe what I heard. I spent some time with a doctor and a nurse for a couple of days, and they related what they have to go through to get healthcare. Shocking.

My question to you, Dan, is the recent acquisition of the Mercy Health System of Pittsburgh, my hometown; what does it do for UPMC's competitive edge and what does it do for UPMC as a provider?

MR. VUKMER: As for the insurance division, it doesn't really add very much, because Mercy was already in our network and a participating hospital. I'm completely unable to answer the question on behalf of the medical center, but I'll be happy to get an answer for you in writing, for the Committee.

MR. DELUCA: Represent Fabrizio.

MR. FABRIZIO: Thank you, Mr. Chairman. Thank you, Mr. Vukmer, for being here. In your testimony you mentioned the noncompete clause or not-to-compete agreement that IBC and Highmark had.

MR. VUKMER: Yes.

MR. FABRIZIO: And then you go on to say the agreement to not compete should not be the basis on which the department defines the market. Could you kind of elaborate on that a little bit.

MR. VUKMER: Sure. The analysis that the

Commissioner will perform under the Insurance Company Holding Act is different, depending on whether it is a statewide market or is not determined to be a statewide market for insurance.

Now, you can speak with some very channeled antitrust folks who will do a federal analysis to say, we don't believe that it's a statewide market. However, the Commissioner is not bound, at all, to follow some antitrust law. It will follow the definition of a statewide market within the Statute.

So Highmark has argued, many times, that because they're noncompetitors, it's not the statewide market for insurance. We said no, it isn't. Absolutely, a statewide market for insurance, we just chose not to be. We believe it's important for the Commissioner to evaluate this transaction on the scenario it's a statewide insurance market.

MR. FABRIZIO: Thank you very much.

MR. DELUCA: Any more questions to my right?

Dan, I just have one question. I just want to have your opinion. We do have a piece of legislation -- and I'm talking on behalf of the Legislatures out there pertaining to a consumer advocate. Would you be opposed to having a consumer advocate in Harrisburg? Would your position be opposed to having a consumer advocate for

insurance?

MR. VUKMER: Absolutely not.

MR. DELUCA: Okay. Thank you. Thank you very much.

The next individual to testify will be Insurance Commissioner, Joel Ario. We'd like to thank Joel for coming all the way out here. I want to thank him for the great job he's been doing as our Insurance Commissioner of Pennsylvania. I've been working with him on diversity, hospital contract convention rates and this legislation. We give you the authority to overview this merger. And to thank you for the fine job you're doing.

MR. ARIO: Thank you very much, Mr. Chairman. First of all, I'd like to say that I look forward to working with you and this Committee on this consolidation for this insurance issue.

For the record, my name is Joel Ario, I'm the Insurance Commissioner. I'm here today to talk about the process we're going through on the Highmark/IBC proposed consolidation.

But before I do that, let me start with a couple of preparatory remarks. First of all, thank you for having these hearings, they're important for me. Two, as the Chairman already referenced, we will be working closely with this Committee and with the Senate Insurance Committee

on a 45-day period after the public comment period closes on whatever comments or recommendations the two committees want to make. I take that process very seriously. I believe they both will produce some new information that will be helpful to us in making the right decision on this.

Second, it's important to me, because we've had our own hearings. We've heard from all of the witnesses you're having here today, and I expect that we will hear new information. I already heard new information from UPMC. What was said today was somewhat different and more developed than what Dan Vukmer testified to at our hearings down in Pittsburgh. Jon Greer assured me that he's going to have some new information for the Federation from what he already testified to. And I'm sure the two representatives of the companies will have some more information for us too.

So I continue to absorb as much information as I can, along with my staff, to make the very best decision here, because we want the very best, fair process as possible. And I would like to say that the very worst outcome, from my perspective, would be to issue a decision and then to have somebody say a week later, gee, did you think about X in your decision and say, no. And then maybe think we made the wrong decision, because we didn't consider that. So I want all stones overturned now before the decision is made. So we welcome your participation and I

look forward to listening to the other witnesses today.

Having said all of that, I put an emphasis on the word "process," because that's what I can talk to you about today. My lawyer is not with me and he has implanted, firmly, in my brain that I need to stay on "process." That I cannot give any commenting, pro or cons with this. I enjoy being on this side of the table during these public hearings, I get to ask a lot of questions, hard questions, of the companies. I don't have to answer any of them yet, but my day is coming and I will have to answer all of them. But in order to ensure that I give an unbiased and fair decision, I need to stay far, far away from public comments one way or another about any substantive issues. So I'm going to talk about the process today.

So I'm going to talk just for a few minutes and then I'll be happy to answer questions. The chronology, which follows the cover sheet of my testimony, it's going to be repetitious for some of you. As the Chairman already indicated, I already talked about this issue on one earlier occasion, but I will certainly go back to it so that we all have the right context. And I'll be brief in my comments so you can ask questions.

The filing that we first received -- this is what we call a Form A filing to the Insurance Department -- was filed by Highmark and IBC to us on April 30th, 2007. At

that time, it was a rather big filing for a major deal like this. That being the fact, we took our first appeal. And then August of last year there were 71 additional questions that we needed answered. We got the first answer to the first questions about two months after that, so last fall in October. And that answer was more than a thousand pages long. And then we continued to get answers to our first 71 questions.

The first set of answers to all 71 questions were received by February of this year. So it did take the companies a bit of time to get together all of the information that we asked for. And then, they've been following up answers to those questions, and the process continues. And there's no doubt it will continue until this transaction is ruled upon, because each answer these companies give us, when our staff gets those, we comb through those answers and we ask more questions. So the process continues with those 71 questions.

The second point on the chronology is that we reviewed this under Legislative standards. But the decision is ultimately made by the Insurance Department, generally. We have to be accountable for that decision, but it operates under the standards of the Legislature settings. So as you see on that page the standards that we use to evaluate the transactions elaborately.

The three key ones that I draw your attention to are the second one which is, "Does this transaction substantially lessen the competition?" There's a lot more involved in exactly what that means. That was the subject of the Chairman's question for the UPMC representative. That, obviously, is a critical question of this transaction of what the competitor or other competitors impact of this transaction might be.

Secondly, though, there are two other standards that are broad and important. And I draw your attention to No. 4 on that list which is: Does this -- will this transaction involve any material change in the business that will be, "unfair or unreasonable," or "fail to confer benefits on policyholders," or "not in the public interest." So that's a very broad standard to look at the changes that will transpire, if this consolidation was to be approved. So we're taking a very careful look at those. That's an important question.

And then, finally, on the next page, Standard 6, "Is this acquisition likely or this consolidation likely to be hazardous or prejudicial to the insurance-buying public?" So we don't only look at the direct impact on the current policyholders, but also ask a much broader question about how this will affect, or be hazardous, or potentially hazardous or prejudicial to the broader insurance-buying

public.

So let's say they've given us direction here, but it's included in a very broad set of issues to be considered. That is, in my opinion, that's important.

The next set of bullets on the list goes through the process of us announcing this, putting it on our website. This proposed transaction has been filed, we put it on our website. I'm going to take a minute to make a commercial pitch.

Looking at the website -- I'm very, very proud of the website. Not only do we have all of the information, all of the public information has gone into this transaction up there. Every question we've asked, every answer the companies have provided; the public comments, the companies' responses to the public comments. By the way, every time we get a public comment our process is, we ship that off to the two companies and ask them to comment, specifically, on that public comment. And then we review those responses too. So that's all organized on the website. So you can go up there and look at, you know, what the doctor said about this, what the competitor said, what the consumer group said, what the Legislature said. It's an enrichable system for understanding what's going on with this transaction. And that will continue to get updated on a daily basis. I'm going to talk about something that was

updated just this morning.

The Justice Department has a note here that's ruled that this doesn't violate Federal Competition Standards, which means they're not going to take any action. They haven't actually ruled it doesn't, they just simply issued a no action letter.

Then we go through the different questions, some of the process there. We have three sets of experts for this transaction. First, we hired legal experts back in May of 2007, Wolf, Block and a law firm, Hangley Aronchick. In November we hired The Blackstone Group to be our principal financial advisor on this transaction. Everybody knows that Blackstone is a top Wall Street firm, a national firm. Because of that, most of us probably have some negative association with them. But on the insurance front, I got to say, they're topnotch.

One of the reasons we've picked people like them is because when we look at the way they've advised the states, and we have a speciality here of advising State regulators. They work primarily with regulators of insurance fields. They have been on both sides of the equation. They have helped states like Maryland and Washington to say no to proposed Blues transactions. They have helped New York City say yes to proposed Blues transactions. So they're a balanced and fair firm not

afraid to say yes or no, depending on the facts.

Then you will see on the next page we have also hired Magnowski (phonetic) Advisors to look more deeply into those competition questions. I think if you look at the tabs, you'll see the competition Statute goes into great effort. I think there are three or four pages of details there about how to look at margins and things. UPMC has testified already about more questions about statewide.

And we have obtained LECG as our economic advisor. Again, I think we did a good job there. One of the questions that Jim Langenfeld, who is the Director of that company, asked us in the interview was whether we were prepared for the answers to go either way. I said, well, that's an interesting question, why do you ask that. He said, because I've been approached from most of the other parties to this transaction, and they seem to have some pretty strong ideas about where I should come out on the transaction. I'm interested to be involved with this, it's a very interesting transaction, but if you already know or think you know how it's going to come out, I'm not interested. I said, that's exactly why we were interested in you, because we want that kind of alliance. And he's proven himself to be a very narrow-minded, a very detailed person along with the rest of his crew.

We did announce last December, and actually

that's an attachment here, the press release. A process like, there could be no end to it. With so many issues and so many attachments, we could spend the next 15 years -- maybe that will be a good thing to do with my life, but I'm a decision-maker, and so we have to get to a decision. So we announced last December that we intended to hold public hearings in the early summer of this year, which we did. We held hearings in Philadelphia, Harrisburg and Pittsburgh in early July. We intended to make a decision by November, so at those hearings I announced that we intended to close the public record at the end of August. That was already a generous public comment period after the public hearings. We typically do 15 to 30 days, that would have been the middle of August, but we extended it to the end of August. Not surprisingly, we've heard from a number of people that's not long enough, we need more time, we need more like 60 days. So we extended it again. If there is news to be made, we got to bring you the news today. The news today from us is that we have put in the Pennsylvania Bulletin, it will be published on Saturday of this week -- and we're announcing it to some of you folks here for the first time that the public comment period will close September 30th. So one month after that public notice on August 30th.

We think most of the record -- almost all of the material will be provided up there by the end of this

month, so we will give the public a full 30 days with some additional information that comes in this month. Most of it, of course, are the rest of the public hearings and that.

Now, some people will come forward and say well, there may be additions to the record. Well, there will always be additions to the record, because every public comment that comes in before August 30th will be sent to the Blues for comment. And then, potentially, people want to comment on the responses that are coming in, so the responses could be unending, as I said. So this is the way we're trying to put an end to it, as an example. So it would clearly be important for the public record would be whatever recommendations and comments the Legislature makes. Those will be in the public record, but it will be after the close of the public comment for 45 days.

So now you know what that 45 days will run, from September 30th to the 45 days. And then there's a 60-day period after that that we are told that, you know, make sure -- we listen carefully to the Legislature, the law says you can't actually make a decision until 60 days after that. So we'll carefully listen to our Legislature and that will allow the decision to be made.

We're slipping a little bit on the timetable that we would like; by the end of the year. We're looking at about the second week of January, but we think it's

important. Again, barring unforeseen circumstances. I say to everybody that I talk to, if something appears here that hasn't really been answered or a point that we really need to address, we can always come forward and open the record again. We'll do whatever we need to do to make the right decision. I doubt that that will happen, and the goal is that we make a decision sometime in early January. And, Chairman, you've said this to me on a number of occasions, because there's a lot of other insurance-related issues in the health department that will be influenced by how this comes out. And so that will be the next Legislative session, and you'll have the benefit of this decision to make appropriate level policy as a result of that.

So that, I think, basically takes us to the end of the chronology here. There are a lot of exhibits that I have. Just to run through them; the 71 questions. If you want to see what kind of questions we've asked, that's the first exhibit attached to my testimony. That was dated August 7th of last year. There's December '07 news release. There are statements from our experts of the public hearings, The Blackstone Company and LECG. The lawyers don't do any paperwork, they just question everybody else's.

The September 30th notice is in here. The same one that will appear in the bulletin on September 30th.

There's another letter from me, updated, coincidentally, August 7th of this year. So one year after that first letter is this letter that says, basically, here are the things we need by the end of August or earlier. So, basically, they've been responsive to those questions. I keep saying record, I mean public comment.

The record will remain open. The public comment will close September 30th.

And then finally, to refresh everybody's memory, I'm sure this is right at the top of your mind, the Competitive Standards. My comments are quite detailed, as you'll see. With Competitive Standards, there's a lot of work to put into those. With that, I'll be more than happy to answer any questions.

MR. DELUCA: Well, I appreciate it. I know you can't comment on some of the stuff that I would like to ask you, Commissioner. And I'm glad to hear that September 30th, you announced that today.

And the fact -- just so the public out there understands, the previous testimony from UPMC mentioned the fact about the sine die, we have up to November 30th to do our 45-day comment period. There's nothing in the law that says that we can't call a meeting up to November 30th when we're in session -- not in session, but we're still in office. And we do have up to November 30th to make the

comments. And I'm sure Senator White will utilize his time, over on the Senate's side, to get his insurance committee together to make his comments. So there is sufficient time for us to do that.

Just one question, and it's not related to any -- well, it's related to some of the testimony, because of the fact we keep hearing about competition. And I want to ask you, Insurance Commissioner, will this House Bill 205 help create this competition that we're talking about?

MR. ARIO: Mr. Chairman, the short answer would be, yes. The more complicated answer would be, some people, I think, would argue, with some correctness, could give certain advantages to certain players over other players. So there's more to the story than a simple yes.

MR. DELUCA: In general.

MR. ARIO: In general, that Bill creates a level playing field. Historically, in every state that has small group laws, it even gives a little bit of benefit to certain players on the level of the playing field. And that is what every other state that has worked in this area has. And the only people who used to have an unlevel playing field was Michigan, who was talked about negatively here today, and correctly, for having different rules for different people. So I think that answer is best to that. But I think to continue to work that Bill in the Senate there may be some

way in which you can modify some parts of that.

MR. DELUCA: With the general public out who's watching, I want to commend UPMC for coming to these Hearings. They do an excellent job in Pennsylvania's healthcare.

We are one of a few states that has an Insurance Commissioner to do that; am I correct?

MR. ARIO: There are two states, Pennsylvania and Hawaii and the District of Columbia. Every other state has created some rules about small group insurance. The reason is simple, you're a large group, you already have a big pool. A couple of people get sick, that doesn't make the rates sky rocket, it stays on an even playing field. A small group market, if you have everybody on your own, one or two people get sick, that could cause a big rate increase.

MR. DELUCA: Thank you. Any questions? Representative Wojnaroski.

MR. WOJNAROSKI: Thank you, Mr. Chairman. Good afternoon, Commissioner. I have one question. Has the Pennsylvania Medical Society and the Hospital Association here in Pennsylvania taken a position on this merger?

MR. ARIO: Representative, excellent question. One I can answer, because I'm just giving you facts. The Pennsylvania Medical Society and the Hospital Association

have both formally opposed the merger or consolidation. And there has been mixed testimony from some of those providers are for it, some providers are against it. On an individual basis at the hearings, some say they are for it, some say they are against it. Those numbers will be on the web page. But the majority of those individual members are against it.

MR. WOJNAROSKI: Thank you, Mr. Chairman.

MR. DELUCA: Representative Fabrizio?

MR. FABRIZIO: Thank you, Mr. Chairman. Thank you, Commissioner. Referencing your 71 queries. Query No. 1, will this information be made public?

MR. ARIO: Representative, another excellent question. All of the information will be made available to me.

MR. FABRIZIO: Will this information be made available to this Committee?

MR. ARIO: Everything that's of the public record is already available and has already been passed to the specialist and the staff. More so, the hard part is organizing this information, because there's so much material. But in the nature of our inquiries, we're asking for some very detailed trade secret type of information about financial plans and so forth. So some of that has to be made confidential. But I got my lawyers scrutinizing everything the Blues give us that they claim is

confidential. And they're saying, wait, why does that have to be confidential. So a lot is labeled confidential, but it doesn't turn out to be confidential. But there are some things that have to be confidential.

MR. FABRIZIO: Have they responded to all 71 questions at this point?

MR. ARIO: They have responded to them, but their initial responses were sent back on February 7. And in the August 7th letter, we asked for some final outstanding items related to those 71, and we got answers to them. I do want to emphasize that every time they give us some new information, we scrutinize them and we usually have some more questions. So it's not completely done, but they've been responsive to all 71, yes.

MR. FABRIZIO: Thank you. Thank you, Mr. Chairman.

MR. DELUCA: Representative Roae.

MR. ROAE: Thank you, Mr. Chairman. Thank you, Commissioner for being here to testify. If you could look at the seven standards that you talked about briefly. Could you expand on the one, a little bit, about would the effect of the merger would substantially lessen competition. What exactly would be looked at, the number of carriers percentagewise; the number of policyholders? What types of things would go into that decision?

MR. ARIO: Thank you for that question. A number of things, but I'll take you through the very simple, three steps.

MR. PETRONE: Okay.

MR. ARIO: The first step, as suggested in the earlier testimony, is to do a numerical test, how many competitors are in the market today, what market shares do they have and what market shares do they have posted. So, basically, it's a numbers game to start. But one important question to this number game is, are you counting this as one statewide market or are you counting it as a regional market. And if it's suggested that you're counting it as a statewide market, pretty clearly it would have a more broadened competitive impact. If you're counting it as a regional market, there would be less of that. Although, still, with all the standards, there might be some of that competitive impact. So that question; is it statewide, is it regional.

And then there's also questions of all of the other health insurances, commericial over here, Medicare over here and so forth. All of those questions are a part of answering those questions. So there will be a lot of numbers in the report that comes out in the expert's opinion.

Second question is, after you add all of

those numbers together, if there are any competitive impact. And even if there aren't, really, that Statute calls for a second test, which is to run a more commonsense look at the market and say, are those other factors pushing towards competition as compared to other things in the market, or are there other competitors that can reduce the number and what competitive impact that would make to make the market more competitive. It might look like more numbers or vice versa.

As I look at this it does say just look at numbers. I have to look at the numbers and then look at several factors to see whether they push the numbers one way or the other. That's Test No. 2. I was going to read you this, but I'm not. If you want to, you can.

The third issue that is very important after that is, if there is a decision that there is some competitive impact, then the Legislature does call for looking at whether there are economies of scale, so called synergies, from a consolidation that big. Whether we have a competitor impact or does this effect the availability of insurance. Even if there's no competitive impact, if this is better for the market.

So numbers first, the competitive economic scale and then finally, if there is any competitive impact, does the benefits outweigh, essentially, the other

competitive impacts. All of that is part of the analysis.

MR. PETRONE: Okay. Thank you. One other question. All the insurance companies that offer health insurance in Pennsylvania, are they all filed to Odgrey (phonetic) in the entire state, or do companies just file Odgrey regionally?

MR. ARIO: That's a good question. And I think the answer is if they're under license, they cannot rate statewide. They put regional restrictions on that. But let me double-check that. I'll get back to you on that. I think that's true, although there's clearly different plans operating in different parts of the state.

MR. PETRONE: All right. Thank you, sir.

MR. ARIO: Thank you.

MR. DELUCA: Any other questions? Thank you, Mr. Commissioner. I look forward to working with you on this Insurance related consolidation.

MR. ARIO: One last comment. We will close the public record September 30th. There is time to meet after the election, it's in November. Some people have said to us that the Legislature only can operate during two periods of time. We take issue to that.

MR. DELUCA: Right. Thank you, Commissioner.

The next individual to testify would be Jonathan Greer. He's the Vice President of the Insurance

Federation of Pennsylvania. Welcome, Jon.

MR. GREER: Mr. Chairman, thanks for having the Hearing today in Erie. I've never been to Erie before. It's good to be able to come here with one of our largest member, Erie Insurance. So thank you.

MR. DELUCA: I think Representative Fabrizio appreciates that, especially when Erie is your largest insurer in your Federation.

MR. GREER: Thank you for the opportunity, again, to be here today. I'm Jonathan Greer, Vice President of the Insurance Federation of Pennsylvania. We're a nonprofit trade association representing commercial insurers in all lines of insurance in Pennsylvania. Our members include many of the large national health insurers and some of the few remaining small local health insurers. We represent some familiar names like Aetna, United, HealthAmerica and CIGNA, to name a few. But none with significant market shares when compared with the four regional Blues with which we struggle to compete.

Last month Governor Rendell signed into law Act 62, which amongst other things, establishes a formal framework for the House Insurance Committee and the Senate Banking and Insurance Committee to submit recommendations to the Insurance Department on the proposed consolidation of Highmark and Independence Blue Cross. This unique 45-day

process begins when the public comment period ends.

While the Insurance Department has yet to determine a date -- well, it has now -- for ending the public comment period, it could happen as early as next month, which it will. Given the massive dimensions of this proposed consolidation, it will determine the way healthcare is insured, financed and delivered throughout this Commonwealth for the next generation as much or more than any of the Legislation you are dealing with, and I'd include the ABC Bill in that. That emphasizes why your involvement is so important, and why we urge the Committee to fully engage in the review of this consolidation. We appreciate this hearing is part of doing that, and we ask that you consider the following thoughts as you prepare your own comments.

Last month the Insurance Department conducted a series of hearings throughout the state on the proposed consolidation. Much of the testimony focused on whether the proposed consolidation is good or bad, or whether Highmark and IBC are good or bad.

But that's not the statutory standard on which this proposed consolidation is to be measured. The questions are whether the proposed consolidation lessens competition. And if so, whether it, nonetheless, will make health insurance more available. And whether it produces

sufficiently unique benefits, benefits that occur only through the consolidation. Those are the things that should allow it to move forward.

Our position is, absent significant controls imposed as a condition of approval, this proposed consolidation will have a lasting negative impact on the ability of other insurers, both those already here and those who come here, to compete with this new giant. We do not believe consumers of any kind, health insurance or otherwise, are well-served by limited choices and private monopolies.

We also don't believe the consolidation produces unique benefits and savings that justify this loss of competition. Highmark and IBC talk about "$1 billion in savings" over the next six years. But from what we've seen, that's just talk and leads to the question of whether they should be saving more already.

Highmark and IBC say the proposed consolidation won't have any competitive impact since they don't compete with each other now. If nothing else, the consolidation eliminates the potential for them to compete with each other.

That loss of potential competition is bad for consumers. We've seen that Blue-on-Blue competition works, just as competition among insurers generally works. In the

central part of Pennsylvania, Highmark and Capital Blue Cross have competed for years, and both companies have said it has made them better.

And remember, the only reason Highmark and IBC do not compete now is because in 1996, they entered into a 10-year pact to not compete. If these companies wanted to, they could be competing against each other today, just as insurers in all lines compete. Imagine if other large insurers started entering into those agreements.

Highmark and IBC also say they have no intention of expanding into each other's markets. Highmark says it is too hard to compete against IBC in the Southeast. And IBC says competing against Highmark would ruin a beautiful friendship. Given that they already enjoy veritable monopoly status in their own regions and they do not, at least at this time, intend to expand outside of them, the consolidation will enable them to crush or discourage any competitive forces.

This won't be because they'll be better than other companies, but because they will solidify their status, the only real games in their towns, especially in negotiating with providers, which is the biggest key to being competitive in health insurance.

If this happens, if you allow it to happen, it will undermine the ability of other insurers to invest

the time and capital it takes to be viable competitors. However hard it is for Highmark to envision entering the Southeastern Pennsylvania market, imagine how difficult it is now, and how much more difficult it will become, for insurers with a limited presence in the state to stay here or for new insurers to come here.

Given that Highmark now owns a significant portion of Blue Cross of Northeastern's HMO affiliate, we also wonder what will happen to that market. If this consolidation is approved without significant controls and our concerns on stifled competition are realized, the potential exists for there to be a single Blue Company that dominates the state. The prospect of one company controlling the vast majority of the Pennsylvania's commercially insured market is not in the best interest of consumers.

We harp on competition because it works. Every line of insurance has, at some point, faced the crisis we see in health insurance now, consumers not getting the coverage they want at a price they can afford. The only approach that has worked is more competition.

The most prominent example is Pennsylvania's auto market. Back in the late 1980's, the state faced a limited and expensive market. A number of reforms were tried, but the only one that worked was a law in 1990 that

encouraged and rewarded new carriers, new ideas and more competition. The result over the last 18 years has been flat rates and broad availability for all drivers in every region of the state.

Workers' Compensation is probably the second most prominent example. It was a bad market, various reforms were tried, but the only one that worked was a law that was passed in 1993 that brought in new carriers, new ideas and more competition.

It is no coincidence that over the past twenty years the two toughest lines of insurance have also been the two most concentrated ones, medical malpractice and health insurance. We're seeing some improvement in the malpractice area, because of some recent reforms that have encouraged more competition.

But we haven't seen much in the way of reforms that have encouraged competition in the health insurance market. And I think that's one of the main reasons we haven't seen anywhere near the progress consumers need and desire.

Some reforms have helped stem the tide of medical inflation, consumer-driven alternative like health savings accounts come to mind. Though, by and large, health insurance consumers continue to struggle with rising premiums.

We admit competition alone isn't the answer to all of the Commonwealth's health insurance problems. But any objective analysis has to conclude that a vibrant, competitive marketplace that induces innovation, consumer responsiveness and true efficiency is good for consumers.

This also goes to the $1 billion in savings Highmark and IBC have promised will come out of this merger. That's a catchy number, maybe that's how it was arrived at, but when you look at it, it is vague, temporary and unenforceable. It is premised on being more efficient. The bigger the better theory of monopolies.

The reality of businesses and markets goes the other way: The best way to ensure that any company operates more efficiently and passes those savings on to consumers is to make sure it faces real competition, and consumers have real choices and alternatives.

Any market that becomes a private monopoly is in danger of becoming a hostage to that monopoly, no matter how extensive or well-intentioned the regulatory oversight. It's not just that competition gets stifled and with it, the pressure to do better, it's that consumers are harmed by the absence of the checks, balances and safety valves that come from a competitive market.

That doesn't mean consolidations. Even one of this magnitude is inherently flawed. It does mean that

consolidations, such as this one, have to be scrutinized and only approved if they come with conditions that ensure the chance for other carriers to thrive and new ideas to emerge. That's what we've recommended to the Insurance Department and what we hope is the final outcome.

Thank you again for the opportunity to be here. I am happy to answer any questions.

MR. DELUCA: Thank you, Jon. I just have one question for you. We hear about this $1 billion, you think it's going to be more and so does UPMC. Would you be opposed to this merger or would the Insurance Federation if we put something in this Statute that says these savings could only be used to reduce premiums for the ratepayers out there? If this money was to go into a special account that could only be used to reduce premiums, not to compete with other insurance companies, to lower the cost to be used for capital improvements to go directly to the ratepayers of the Commonwealth of Pennsylvania, would you be opposed to that?

MR. GREER: The two words that you heard a lot throughout the testimony is competition and consumers, and what's best for both. And what we've said, as part of our submissions to be a part of the public record, is that if the CHR agreement is signed, what happens then. There should be, as a part of this consolidation, something that's long-term, not something that's going to expire for the next

generation. There's been some discussion of returning the surplus back to the ratepayers. We think one, if that, in fact, does occur, it shouldn't go to the ones today, it should go to the ones that paid that over a period of time in the past. The former policyholders are the ones that contributed that, not the future ratepayers. And two, we think their surpluses should go into a separate account. Those are a part of our submissions.

MR. DELUCA: Thank you. Any questions? Representative Roae?

MR. ROAE: Thank you, Mr. Greer, for your testimony. I come from a property casualty background. I worked for Erie Insurance for 14 years, so I'm more familiar with that side of the insurance business. But just for comparative purposes, do you know, roughly speaking, how many companies in Pennsylvania offer personal auto insurance?

MR. GREER: Hundreds.

MR. ROAE: Roughly.

MR. GREER: I don't know, a lot. Hundreds.

MR. ROAE: Hundreds. And roughly, how many companies offer health insurance in Pennsylvania?

MR. GREER: A lot. But only about four or five have a limit consequence. I actually have a list of all of the companies and what they provide and it does drop when

you go below the Blues and a couple of our members. It goes down to 10 percent that covers a statewide margin.

MR. ROAE: And, you know, as far as polices that people are familiar with, homeowner policies, auto policies, are there any companies that have any kind of a significant market share, you know, that we could compare to the market share that the new company would have after the merger?

MR. GREER: No. Nothing close. The largest auto insurer is State Farm. State Farm, I think, has a stabilized market share of 18 to 20 percent, that's the largest. Erie Insurance is somewhat close to that. I think they're around 15 percent, statewide, something like that.

What we heard earlier about part of the reason we have so much difficulty competing with them now -- again, we're here because Highmark and IBC want to consolidate.

MR. ROAE: Right.

MR. GREER: And it's not about State Farm and Erie Insurance. The reason we struggle to compete with them now is, because unlike any other auto insurance, they have carved their four regions, service areas -- a term of ours -- and that has allowed them to focus on those regions as opposed to going statewide. So that's why those markets are so concentrated, and that's why we've had the inability to compete against them. And one of the things that was

mentioned earlier was the 10 years noncompete clause. Well, one of the things that we've heard from Highmark and IBC is we can't, as a condition of our brand. If it's owned by Blue Cross/Blue Shield Association, we can't go statewide. Then why do you have a 10-year pact with Highmark and IBC not to compete with each other. If you weren't going to get the permission, why do you need the agreement?

In the health insurances, as far as I know, and it continues in Pennsylvania, where the state is allowed to be divided into four regions for health insurance. No other line of insurance does that. Auto insurance doesn't do that, life insurance certainly doesn't do that, home owner's insurance doesn't do that. It's unique in Pennsylvania and it's certainly unique in health insurance.

MR. ROAE: Thank you. I do appreciate that. And I am trying to learn as much as I can about health insurance, since my background is in property casualty. And it just does seem odd that, you know, if homeowners insurance was done away with one company insured this part of the state, and another company in this part, it seems like that could have a negative impact on the competition. So I am concerned about one company controlling too much of the market. But, that being said, if there could be something being said for economies of scale, I don't know -- you know, if you look at the expense ratio of this bigger

company, some say it would be a bit better, some say it wouldn't change. What's your take on that?

MR. GREER: We've heard that the economies of scale, the bigger is better. One, I don't necessarily agree with that in the context of insurance, healthcare insurance particularly. And two, health insurance is more of a labor intensive industry as opposed to a capital intensive industry. So that's why I think some of those arguments are pertaining to a capital intensive industry than for a labor intensive industry. The large scale numbers aren't for health insurance.

MR. ROAE: All right. Thank you so much.

MR. DELUCA: Any other questions? Jon, just one question. This is in follow up to Representative Roae's statement. Are you saying the Blues do compete in other states?

MR. GREER: Well, that's probably a question better for the Blues than it is for me.

MR. DELUCA: Well, you mentioned the fact that --

MR. GREER: Well, I don't know if there are any other states -- well, that was in the context of property casualty -- I don't know of any other states that have four Blues. And I don't know -- I think that's a question better for the Blues.

MR. DELUCA: Any other questions? Representative

Petrone.

MR. PETRONE: Hello, Jon. HealthAmerica, how much of the state do they have?

MR. GREER: According to 2005, that's the most recent one I have, about 20 percent.

MR. DELUCA: Thank you very much, Jon.

MR. GREER: Thank you.

The next individuals to testify will be -- if I mess up on this name here, I apologize. Steve Udvarhelyi. Is that close or not?

MR. UDVARHELYI: That's close enough.

MR. DELUCA: Senior Vice President and Chief Medical Officer, Independence Blue Cross; and Deborah Rice, Senior Vice President of Regional Markets, Highmark. Welcome.

MS. RICE: Thank you, Mr. Chairman. My name is Deborah Rice, and I am Senior Vice President of Regional Markets for Highmark. Also with me today is Dr. Steve Udvarhelyi. You can ask me to say it, but I can't spell it. But he's the Senior Vice President and Chief Medical Officer of Independence Blue Cross. We want to thank the Committee for the opportunity to speak to you today about why the proposed combination of Highmark and Independence Blue Cross into a new company is good for Pennsylvania, and how it will create value for the communities in which we operate, for

our customers, for healthcare providers and, most of all, for the people of Pennsylvania.

Since our boards of directors agreed to combine the two companies in March 2007, we have been engaged in an extensive review process involving state and federal regulatory agencies, with input from state and federal public officials. As you know, the Pennsylvania Insurance Department in July held a series of public hearings across the state on the consolidation. We have also provided responses to all of the Department's original and supplemental questions. This has been an important, cooperative and open review process. Today, we continue this open dialogue about how this combination will better serve the needs of the Pennsylvanians.

Our companies have a proud tradition of serving Pennsylvania as nonprofit companies. For 70 years, IBC and Highmark have had a common mission: To help ensure that healthcare is available, affordable and of high-quality for all Pennsylvanians.

Throughout our history, we have made health insurance programs available to everyone, regardless of age, gender and health status. We have provided assistance to people in financial need, by subsidizing health insurance programs for children, lower-income individuals and families, and older adults. Moreover, we have provided

financial support for the health education and community health programs.

At the same time, according to a study we commissioned, Highmark and IBC have had a significant, positive impact on Pennsylvania, with a total annual economic impact of $4.2 billion on the state's economy. The companies employ approximately 18,000 people in high-quality jobs in the state and purchase a significant amount of goods and services from Pennsylvania-based businesses.

This transaction, however, is not about the past or the present. It is about the future and about preserving our nonprofit status. And it is about laying the foundation for positive change in the way healthcare is delivered and paid for in Pennsylvania.

Coming together, our two companies can remain a financially vibrant Pennsylvania-based company and achieve tangible savings and growth opportunities of more than $1 billion that will be used to address healthcare costs, quality and access to medical care in Pennsylvania.

This combination will allow us to strengthen our contribution to the Pennsylvania economy, by the way we employ people, by creating new business opportunities for Pennsylvania-based businesses and by supporting the community through programs and services that we have historically embraced.

The proposed combination is important given the challenging health environment. Healthcare costs are rising dramatically. We know that the cost of healthcare is making health insurance less affordable for businesses today. As a result, fewer businesses are able to maintain healthcare coverage and more people are joining the ranks of the uninsured. We are also seeing more people moving to public health insurance programs, which means more healthcare coverage is being financed through the federal and state governments.

The demographics of Pennsylvania also present challenges. The state has an aging population that is creating more demand for healthcare services. We also have an aging workforce in many industries, including healthcare. This places an added strain on the healthcare system as the aging population uses more medical services. Questions are being raised about the quality of healthcare today and the variation in medical care from community to community for people with the same medical condition.

With these critical issues facing us across Pennsylvania and nationally, rapid change is occurring in healthcare. Consumers are taking greater responsibility for their personal healthcare decisions and their costs. This change is creating the need for investments in technology so people can access their own personal health information and

have programs available to better manage their own health.

As these forces shape healthcare, two points have become very critical for business success. First, scale has become increasingly important to achieve greater efficiency and lower administrative costs. The scale of competition has shifted from a local to a regional and national basis. We have a growing need to be a multiproduct, multimarket company to compete in the future, to spread our risks and to better serve our customers. Second, there is a growing need for capital for investments to meet the marketplace demands that we outlined earlier.

The health insurance industry is responding by consolidating. In the past 15 years, the top 20 insurers have substantially increased their share of subscribers in the commercial health insurance market. Even more significant, during the same period, large, well-capitalized for-profit insurers have gained a much larger share of commercial health insurance subscribers compared to nonprofit health insurance companies.

The largest players in healthcare today are WellPoint, United HealthCare, Aetna and CIGNA with anywhere from 13 million to 35 million subscribers. They have the scale, the product diversity and the geographic diversity to spread their operating costs over more members. They also can leverage their large subscriber base to obtain better

pricing from national suppliers of laboratory services, durable medical equipment, radiology services and pharmaceuticals. In contrast, Highmark and IBC, combined, have eight million subscribers.

Consolidation isn't unique to the for-profit health insurance companies. It's happening in the Blue Cross and Blue Shield system in the United States as well. Today, there are 39 independent Blue Cross and Blue Shield companies. That is one-third the number since 1980, when there were 115 Blue Cross and Blue Shield companies. In fact, some Blue Cross and Blue Shield companies operate in multistates. These companies have gained operating efficiencies and better serve their customers.

Pennsylvania stands alone in that we have four independent Blue Cross and Blue Shield companies. This is problematic, because we are operating less efficiently than we could be by investing in redundant technologies and capabilities that add more cost to the state's healthcare system.

As the two companies have looked at the changing healthcare environment and the need for greater scale and more capital, it has become clear that the combination of IBC and Highmark is a natural fit that would bring significant benefits to the people of Pennsylvania. The two companies have almost identical missions and have

worked together for over 50 years to better serve the community, through programs like the Caring Foundation. We also have complementary products. Highmark's vision, dental and stop loss lines of business complements IBC's pharmacy benefit, management, third party administration and workers' compensation programs. Together, our two companies can offer a core blend of products to better serve our customers on a common platform.

What's most important is that bringing our companies together will not lessen competition in commercial health insurance or reduce choice in any market in Pennsylvania in the future. Our subscribers will continue to have the same wide variety of choice from a competitive health insurance market as they do today.

Although over 100 witnesses appeared at the recent Pennsylvania Insurance Department hearings, and many others have filed comments with the Insurance Department, we are not aware of any of our over 50,000 commercial group customers that have complained that they will have less choice for insurance the day after the transaction than they have today.

And lastly, the United States Department of Justice has twice reviewed the proposed consolidation of the two companies and both times cleared the transaction under federal antitrust law.

Thank you.

MR. DELUCA: Thank you. Okay, Doctor?

MR. UDVARHELYI: I also want to thank the Committee for the opportunity to speak with you today. My name is Steve Udvarhelyi, I'm the Senior Vice President and Chief Medical Officer for Independence Blue Cross. As Deb mentioned, we have a proud tradition of serving our subscribers and our local communities. Our two organizations have had a long-standing and positive partnership, and we have a responsibility to promote the value and enhance the trust of the Blue brand, which serves more than one in three Americans.

So while coming together is a logical extension of our historical partnership, we believe that the business growth opportunities and anticipated efficiencies and savings will enable us to achieve several real and important goals. First and foremost, we re committed to help make health insurance more affordable. Affordability is the number one issue with our subscribers, and we have a responsibility to do better on this issue.

At the same time that our subscribers are demanding that we help control costs, they also want us to continue to invest in products and services to help improve quality and healthcare outcomes and to expand our efforts in health promotion and wellness programs.

Physicians, hospitals and other healthcare providers have been valued partners in our companies' mission of assuring access to high-quality networks of providers. We are committed to maintaining our well-established relationships with providers and enhancing incentive programs to help ensure the delivery of high-quality care.

We will continue to be a viable and successful leader in our communities. Our combined resources are expected to generate new business, which will bring more jobs to Pennsylvania and stimulate additional business opportunities for Pennsylvania-based businesses.

And our goal is to more effectively use technology to make it easier for our subscribers and providers to do business with us. We are committed to work tirelessly to achieve these goals.

To support these goals, we have identified tangible benefits that the proposed combination will achieve. By combining our two companies, and I will add, only by combining only our two companies, will we be able to generate more than $1 billion in additional economic benefits over six years. This is new money and goes beyond any commitments we've made today.

These additional monies will be generated by savings from business efficiencies and growth opportunities

that the companies could not produce individually. And unlike with consolidations of publicly-held companies where the savings flow to shareholders, every dollar of the economic benefits of this combination will go back to improving healthcare in Pennsylvania.

In addition to the $1 billion in savings, we have also agreed to voluntarily extend the Community Health Reinvestment Agreement with the Commonwealth for three more years. That agreement is currently set to expire in 2010. And this represents an additional estimated $350 million that can be used to help more Pennsylvanians obtain needed healthcare coverage.

Let's now look at the specific benefits for different stakeholders. For our subscribers, we pledge to freeze administrative fees of their health insurance premiums for two years. This will save our subscribers approximately $295 million in their premiums over six years. Now, we know that some of the premium dollar that we collect already goes out to pay physicians and hospitals for their services that they give to our subscribers. And that is why we want to focus on the controllable part, the healthcare dollar that we control, our administrative expenses.

In addition to the administrative cost commitments, we expect to save our subscribers an additional $285 million over six years on prescription drug costs by

capturing higher rebates and pharmacy discounts and lowering administrative cost-savings possibly, only, with a larger subscriber base.

We expect an estimated $100 million of the efficiencies generated by the consolidation will be used to fund expanded healthcare quality programs. These could include continuing and expanding each company's ePrescribing programs and encouraging implementation of standardized personal health records and electronic medical records. Greater use of these tools leads to higher quality care, fewer medication errors and, also, reducing these errors will result in greater savings for subscribers in the long run.

The new company also plans to combine and expand the best of the health promotion and wellness programs offered today by Highmark and IBC to help improve the health and well-being of our subscribers. And over time, this type of a focus will lead to a healthier workforce, which would be more productive at work and consume fewer health services. Moreover, we will offer our subscribers a wider array of products and services by integrating vision, dental and disability programs to their medical and pharmacy health plan choices.

We are proud of our long-standing relationships with physicians, hospitals and other

providers. And the value of our brand is based on the fact that we offer our subscribers broad, high-quality provider networks - and healthcare providers who will remain important partners in the future. We believe the consolidation will benefit healthcare providers in a number of ways.

In the past few years, IBC and Highmark have pioneered a technology tool called NaviNet to help simplify administrative transactions with physician offices and hospitals. And the consolidation will enable us to build on this capability so that physician offices and hospitals can, obviously, spend more time improving patient outcomes, patient safety, as well as improving the patients, and worrying less about administrative tasks.

We will be committed to provider payment levels that preserve our networks and help promote optimal quality care. That is why we plan to expand pay-for-performance programs that provide incentives for healthcare providers to deliver increasingly high-quality care. We all recognize that payments simply based on the volume of services are no longer sustainable in today's healthcare environment, and that incentives must be aligned to promote quality of care and the delivery of evidence-based care.

And here is one very important point I'd like

to emphasize now. Not one dollar of the $1 billion in economic benefits will leave the path line that will result in reductions in provider reimbursement.

Over the past few years, Highmark and IBC have developed close working relationships with hospitals and physicians which are focused on improving patient safety and reducing errors. The new company will seek to expand its partnership to help raise the bar in the delivery of high quality care.

Lastly, let me talk about how the consolidation will benefit our local communities, where our employees, our subscribers and their families live and work. IBC and Highmark have carried out our community mission in many ways, none more critical than offering coverage to individuals and families who the large, for-profit insurers will not insure. Our coming together will enable us to continue to subsidize programs for the uninsured, lower-income families and older adults. In addition, we will commit $300 million to new and existing programs for the uninsured, the underinsured and small business employees. The new company intends to work with key stakeholders and public officials to identify the most effective ways of using these monies.

So together, these commitments total $1 billion in new money, plus additional $350 million to extend

our commitment to the Community Health Reinvestment Agreement.

The new company will build upon our long-standing support for programs and services aimed at addressing community health needs. We believe there will be tremendous opportunity to expand our companies' current programs statewide, such as grieving centers for children and families, funding for medical and dental clinics for the uninsured, addressing childhood health issues, such as childhood obesity, and providing scholarships to increase the supply of nurses. Just last year, IBC and Highmark provided about $200 billion in community contributions to expand access to health insurance and to support a variety of community health and human services programs and services.

So, in conclusion, the consolidation is important for us to remain a viable, nonprofit company that will strengthen our commitment ot the community and economy of Pennsylvania. Do we expect to grow our business? Absolutely. And this business growth and the resulting revenue will be supported by additional jobs and investments in Pennsylvania.

Although, no one company or organization, alone, can solve all the problems of the healthcare system. We believe this consolidation offers a pathway to positive

change in our healthcare system that Pennsylvanians are looking for.

Thank you.

MR. DELUCA: Thank you. Let me just ask a couple of questions here. You mentioned the fact that it will give you more buying power with the consolidation; am I correct?

MR. UDVARHELYI: Chairman, I think --

MR. DELUCA: Discounts. You'll be able to get bigger discounts in your buying power?

MR. UDVARHELYI: It would allow us to consolidate certain programs, certainly, yes. For example, like system investments. Today, both companies invest separately in system investments. In the future, if we're one company, we could simply invest in one system. So a good example of that is the Federal Department of Health and Human Services has just announced that we, as an industry, will need to move to an ICD-10. That is going to be a tremendously expensive investment from the system standpoint. Without this consolidation moving forward in a timely manner, both companies will invest millions of dollars each in our separate systems to make that change. If we're one company, we will make that investment once.

MR. DELUCA: So that's on that situation. Did I hear something about prescriptions and all of that, you'll have more buying power? Did I hear that?

MR. UDVARHELYI: Yes. We believe that we will be able to, for prescriptions, save about $285 million.

MR. DELUCA: Okay. What prohibits you, both companies, from using that buying power you have now to buy prescriptions? Is there something that's prohibiting you from doing that right now to save money? I mean, in your industry and other industries like -- we can pick a guy from the state -- is there anything that prohibits you from doing that right now to save money? I'm talking about on the prescription plan. I understand the different systems. I don't know, is there anything that prohibits you from doing that right now to save?

MR. UDVARHELYI: Mr. Chairman, I believe that today we are operating under separate companies, and the savings that we've outlined would not be possible if we did not come together.

MR. DELUCA: Oh, no. I understand that. I'm just trying to get a feel for this. There's nothing that prohibits your two companies from going out and buying together, is there? I mean, not on a system, I'm talking about other products that you would be saving money on if you would be buying from one company; am I correct?

MR. UDVARHELYI: Today we use different -- they use MedCo as a vendor for that, we have our own company. So today we can't do that.

MR. DELUCA: I understand that. But there is nothing that prevents you from getting together to save money, you're talking about saving money, you could save money on one product.

MR. UDVARHELYI: There could be some incremental savings by working together, but those savings would be less than what we've outlined in the consolidation.

MR. DELUCA: Okay. You've heard some of the comments from the other individuals. And as Representative Wojnaroski mentioned before to the Insurance Commissioner, I'm wondering why, since the reimbursement rate is going to be cut, why a lot of the physicians would be against this merger, and why the hospitals would be against this merger. What are their concerns?

MR. UDVARHELYI: Well, I think you would need -- to be candid, you would need to ask them. I think Commissioner Ario stated correctly that not all physicians and not all hospitals are against this merger. In fact, at the Insurance Department Hearings, several physicians and several hospital executives testified favorably on the consolidation.

MR. DELUCA: To your knowledge, is the Hospital Association opposed to the merger?

MR. UDVARHELYI: The Hospital Association is opposed to the merger.

MR. DELUCA: How about the Pennsylvania Medical Association?

MR. UDVARHELYI: The Medical Society is opposed to it.

MR. DELUCA: And I guess this is the hearing that this comes out, Commissioner. Why are they opposed to it?

MR. UDVARHELYI: That's a question you would have to pose to them.

MR. DELUCA: Okay. Well, we have them coming in in September and we will do that. Now, as far as -- I think we will start hearing some of their concerns, but you don't believe that this will incite a competition; is that what you're saying?

MS. RICE: I'll take that.

MR. DELUCA: You'll take it.

MS. RICE: No, we don't believe it's going to start any competition, because we're not currently competing in the commercial health insurance market today. So whenever you look at Western Pennsylvania, as an example, the same competitors that are there today, UPMC, Aetna, HealthAmerica, Cigna, they would still be in that environment competing just as they are today, and that's true with every market.

MR. DELUCA: The same way they compete today?

MS. RICE: The same way they compete today.

MR. DELUCA: From my perspective, back in the West, obviously, we got much more competition. I understand where this competition comes in at. So you believe that we'd see a status quo, we wouldn't see any more competition, because right now there's no competition, I mean, a limited amount. If you have 70 percent of the market, there's only 30 percent to go around.

MS. RICE: Right. About 58 percent.

MR. DELUCA: You only have 58 percent?

MS. RICE: In Western Pennsylvania. With that said, we don't see competition looking different in the marketplace whether it's in Western Pennsylvania, Central Pennsylvania. We do believe Capital Blue Cross and Highmark will continue to compete also with HealthAmerica and Aetna. And the same in Southeastern Pennsylvania, they see competition with Aetna, Cigna and others, and we believe that will continue.

MR. DELUCA: Now, with this merger, it's my understanding that we would see -- I'm more concerned about what the consumers are going to see. Are the consumers going to see their premiums reduced with the merger? Because I have seen other mergers, and after we get everybody into this, we merge, we all come together, everybody else is out of the business and then we have control of what we want to pay and what we do. So will the

consumers see any benefits from this as far as the rates coming down?

MS. RICE: Well, what we believe they'll see, as in Dr. Udvarhelyi's testimony, is they'll see a savings immediately over a two-year period of holding our rates flat, our administrative fees flat, because that's what we control, of $295 million. Through other technology investments, our hope is that, with improved quality and with being able to provide more insurance for more Pennsylvanians, that that will help, at least, level some of what they might experience.

MR. DELUCA: Thank you. Any other questions? Representative Petrone?

MR. PETRONE: Thank you. I just have a question. This is for the Commissioner. Commissioner, my understanding is, and correct me if I'm wrong, one person will make this decision and that is you; is that correct?

MR. ARIO: That is correct until the Courts get a hold of it, correct.

MR. PETRONE: I thought there was like a six or seven member crew that will get with you and vote on it; but no, just one person.

MR. ARIO: There's more than a dozen people that think they will make it for me.

MR. PETRONE: Thank you, Mr. Chairman.

MR. DELUCA: Representative Roae?

MR. ROAE: Thank you, Mr. Chairman. The combined company would have how many people insured? I read eight million; is that right?

MS. RICE: Eight million contractholders.

MR. ROAE: Okay. So there would be, basically, eight million customers out of the 12 million people in Pennsylvania?

MR. UDVARHELYI: I don't think all of those individuals would necessarily be residents of Pennsylvania.

MS. RICE: That's right.

MR. UDVARHELYI: We do have some businesses for -- companies, for example, that have employees that we insure where these workers reside out of state and some of the product lines such as dental and vision are out of state.

MR. ROAE: Okay.

MR. UDVARHELYI: So it's not all residents of Pennsylvania.

MS. RICE: That's right. We have many national clients, for example, PBG has members not only in the state of Pennsylvania, but also internationally.

MR. ROAE: Okay. Now, if we look at the $295 million dollars of projected savings, because of, you know, freezing administrative fees; is that each year, or is that over the course of six years?

MS. RICE: Over the course of six years.

MR. ROAE: Okay. So that would be about 50 million a year?

MR. UDVARHELYI: The savings -- the freezing of the fees would be in the first two years, but, obviously, that benefit continues forward. It would be calculated, all of the savings over a six-year period.

MR. ROAE: Right. I did some rough math here. I'm thinking, okay, 295 million over six years, and there's eight million customers, that's about 50 million a year. So you'd be looking at about $6 a year, per customer in savings, roughly?

MR. UDVARHELYI: The calculations, I don't think that you can necessarily proportion that evenly with everybody. And we provided in our filings to the Insurance Department a lot of detail on this.

I would like to comment that the economic benefits from the consolidation, we did not come up with these just on our own. We have retained a well-known consulting firm, Lewis & Company, and asked them to provide guidance to us on how these savings will be generated, to make sure that they were all new savings that will come about from the consolidation, not things that we were already doing. But they will not come at the expense of payments to the providers and other sorts of conditions.

They worked with us to identify these, they validated them. And, further, to make sure that we have clear line of sight on how to do this. Both companies worked together with Lewis & Company over many months to create a very detailed implementation plan on exactly how these efficiences will be generated. And so there's a very specific plan to achieve these savings.

MR. ROAE: You know, roughly speaking, what are the combined administrative fees for both companies, currently?

MS. RICE: That number would actually vary by customer, so it's very difficult to give an average, because.

MR. ROAE: I mean, companywide.

MR. UDVARHELYI: I don't have that number.

MS. RICE: But as Steve indicated in his testimony, 88 to 90 percent of all premiums collected go to the buyers.

MR. ROAE: And what are your premiums per year for combined?

MS. RICE: And so if you look at what administrative fees will be, somewhere around 10 to 20 percent.

MR. UDVARHELYI: I believe the approximate annual premiums for both companies together generate about 20

billion dollars.

MR. ROAE: Twenty billion. So you're looking at about, roughly, two billion?

MS. RICE: And also, what you need to recognize is some customers are self-insured and some fully insured, so you have premiums and --

MR. ROAE: Okay. I mean, I think the part that we save money, I think that's great. But it seems like it would be just a relatively drop in the bucket, you know, for the whole expense of everything. It sounds like a lot of money, 295 million, but when you divide that out over six years and then divide it out over eight million customers, it's not really, you know, very much.

MS. RICE: Well, we're trying to have an impact. So holding administrative fees flat for two years is significant. And that's the part that we can control. There's other activities, as we have indicated, and have been in past testimonies that we think will help start controlling the bigger cost, which is care cost. So that's new technology, prescribing better quality there.

That's also working with providers through pay-for-performance programs to really generate the quality, because we know that has a significant impact in medical cost alone.

As Dr. Udvarhelyi and I had indicated, the

wellness programs and care management programs, we do believe that they're our best practices, but each organization can impact their cost. So we think that it all has to come together. We want to make immediate impact on where we have control, and that's the administrative fees.

MR. ROAE: Okay. Thank you for your information. I appreciate it.

MR. DELUCA: Representative Kotic?

MR. KOTIC: Thank you Mr. Chairman. I'm firmly concerned with all of our efforts to help the uninsured; that has been a focus of the Committee. We've taken great steps in the House to try to look for a compromise that all parties can agree on. How would this merger affect or correlate with our legislation in the past, or future legislation, may we pass the legislation, to help the uninsured?

MR. UDVARHELYI: Excellent question. So there are a couple of specific things we've outlined. One that I mentioned is about $300 million is targeted to help expand access coverage to the uninsured, underinsured and also to the small employers. We, obviously, are willing to work with you and others on exactly how these moneys are spent.

The other thing I'd like to underscore is, both companies have a strong commitment to the communities, to our mission and to doing things. For example, in my part

of the state, we work with a number of clinics that serve really only the uninsured. And we have given the additional funding to those clinics to help expand coverage there. Our ability to do that and the level to which we can invest in that shows how financially solid we are. And as our facility likes to say, the margin of mission.

So we do believe that by coming together to continue our viability as a strong, not-for-profit company committed to the health and well-being of Pennsylvanians, we will continue that mission moving forward. But, again, our ability to do that is predicated on us remaining as a strong, financial company.

MR. KOTIC: Thank you for your testimony.

MR. DELUCA: Let me just say this, we're not trying to say anything bad about the companies, we're just trying to get information, that's why we have these hearings.

Unless I misunderstood you, you said that the billion dollars in savings is not coming from the providers or the administration department, right?

MR. UDVARHELYI: The billion-dollar savings, most of that is coming from reducing our administrative expenses.

MR. DELUCA: Most of it is coming from --

MR. UDVARHELYI: There is some that is coming from synergies that come out of growth by bringing our companies

together, but the majority is coming out of reducing our administrative expenses.

MR. DELUCA: And I heard you say that your administrative cost is 10 percent, or did I misunderstand you?

MR. UDVARHELYI: What we --

MR. DELUCA: Approximately, 10 percent.

MR. UDVARHELYI: It's probably less than that.

MR. DELUCA: Today.

MR. UDVARHELYI: It's probably less than that on a consolidated basis. But those numbers are available. I think they've been shared by our department.

MR. DELUCA: On a consolidated basis you're saying?

MR. UDVARHELYI: Yeah. I don't have the specific financials, but.

MR. DELUCA: Approximately, what are your administration fees?

MR. UDVARHELYI: Just under 10 percent.

MR. DELUCA: Just under 10 percent. I wonder why UPMC is under 8 percent, and they didn't have a merger. Is there a difference in the way you operate? I know you can't testify about their operations. I wonder why such a smaller company has such a substantially smaller administrative cost. Their's is 8 percent, yours is a little over that.

MS. RICE: Right. we can't really respond to what's included in their administrative fees, but we have found that we've been competitive in the marketplace.

MR. DELUCA: Okay. I know you don't have it right now, but you can provide it to the Committee. But you do have on Page 3 a substantial amount of money that is provided to Pennsylvania-based businesses. Could you guys provide us with how much of that money goes into the Pennsylvania-based businesses? Can you provide us with that information. Not right now, but, according to you, you say, "A significant amount of goods and services from Pennsylvania-based businesses." Significant can be anything. So you provide us with how much of that money goes into Pennsylvania-based businesses. Okay.

MS. RICE: Sure.

MR. DELUCA: Representative Roae?

MR. ROAE: One final question, if I may. Both of your companies are nonprofit corporations?

MR. UDVARHELYI: Yes.

MR. ROAE: Thank you. Thank you, Mr. Chairman.

MR. DELUCA: Okay. Thank you very much for your testimony. And this meeting will be adjourned until tomorrow at City Hall.

(Hearing adjourned at 3:15 p.m.)