

Public Hearings re: NJ Senate Bill 1581 and Assembly Bill 2739

Statutes Proposed to Protect the Charitable Assets of Blue Cross and
Blue Shield of New Jersey Upon its Conversion from a Charity to a
Domestic Stock (For Profit) Corporation

Testimony of:
Renée Steinhagen, Executive Director
Public Interest Law Center of New Jersey
833 McCarter Highway
Newark, NJ 07102

INTRODUCTION:

Good morning Ladies and Gentlemen. My name is Renée Steinhagen; I am the Executive Director of the Public Interest Law Center of New Jersey (PILC.) The PILC is a nonprofit organization established to provide legal advocacy that addresses systemic social and political problems facing residents of New Jersey. The PILC has initiated a broad advocacy project regarding the restructuring of nonprofit health maintenance organizations, insurance companies, and hospitals upon the conversion of such entities from nonprofit to for profit status or the acquisition of such entities by companies with different corporate purposes. The PILC seeks to provide a legal voice for those community interests that otherwise would not be represented in the administrative processes that govern such corporate changes and in the judicial system where controversies surrounding the transactions often take place.

We were active as counsel to *amici* in the judicial proceedings initiated by BCBS of NJ two years ago, participated in the litigation surrounding the privatization of Bergen Pines Hospital (now Bergen Regional), obtained documents underlying the HIP-PHP transaction through the judicial process and negotiated an approved settlement agreement with the Department of Banking and Insurance to investigate the charitable trust issues arising from the State's approval of the HIP-PHP transaction. In addition, I personally served as counsel to the American Civil Liberties Union of NJ and FirstChoice of NJ who were found to be interested parties in what turned out to be a successful court action to obtain a charitable trust settlement as a result of the merger between St. Elizabeth and Elizabeth General Hospitals.

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SUMMARY OF PUBLIC INTEREST LAW CENTER OF NEW JERSEY'S POSITION ON
BLUE CROSS BLUE SHIELD OF NEW JERSEY'S PROPOSED CONVERSION TO FOR-
PROFIT STATUS:

The Public Interest Law Center (PILC) feels strongly that the essential goal of this legislation should be the preservation of the charitable assets of the Blue Cross and Blue Shield of New Jersey for generations to come. Across the United States, over 100 foundations have been created by the conversion of nonprofit health providers and insurers, with assets totaling several billions of dollars. The creation of a new health foundation for New Jersey will be a significant event in the philanthropic resources available to New Jersey residents. As written, however, the statute does not offer sufficient safeguards that will ensure the creation of an independent foundation that will receive the full fair market value of the charitable assets of BCBS of NJ.

Given that the Courts of New Jersey have held that BCBS of NJ is a charity, several inescapable conclusions of law and policy follow. Stated broadly, the common law doctrine of *cy pres*, the decisional law of the courts of NJ specific to BCBS of NJ, and the precedents set by BCBS conversions in other states mandate the endowment of the creation of an independent charitable foundation with 100 percent of the charitable assets of BCBS of NJ, devoted to increasing access to care for the uninsured residents of New Jersey. One-hundred percent of the value of BCBS of NJ cannot be simply equated with one-hundred of the stock if that stock is severely restricted and not freely alienable. Specifically:

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- I. An amount equal to the fair market value of the charitable assets of BCBS of NJ must be used to create one or more private and independent foundations to carry on the original mission of BCBS of NJ. Information necessary to a proper evaluation of the fair market value of BCBS of NJ must be deemed non-confidential. The proposed legislation does not adequately ensure either of these requirements.
- II. The application process must be transparent and allow for meaningful public input in order to ensure that the interests of the charitable beneficiaries, the residents of New Jersey, are protected. All information necessary to a proper evaluation of the impact of the conversion on the health care services available to the public should be freely available to allow public scrutiny. The Attorney General, with the assistance of the Commissioner of Banking and Insurance, should make that evaluation using pre-determined criteria such as those established by the recently enacted "Community Health Care Assets Protection Act."
- III. The Board(s) of Director(s) of any new foundation(s) must be completely and devoted solely to fulfilling the mission of the foundation. There should be no unreasonable restrictions placed on how Foundation Directors may vote on any aspect of their governance of the new foundation, including when to sell stock of the for profit, to whom, and how to vote the stock of the for profit. The Foundation(s) Board(s), as representative of the public, must be able to control and diversify its asset base in order to maximize the value of the foundation and to pursue its charitable mission. The proposed

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bill permits the imposition of voting and registration restrictions on the stock held by the foundation(s) without imposing any standard of reasonableness contrary to model legislation proposed by the National Association of Attorneys General (NAAG).

- IV. The mission of the new foundation(s) should correspond to the original goals of BCBS of NJ: to promote access to medical care for those residents of New Jersey who are under or uninsured. Further, the foundation's assets may not be applied to activities that to date have been assumed by governmental entities. Whether the new foundation(s) will have grant making and/or programmatic functions should be decided before the conversion is approved.
- V. The applicability of the common law of *cy pres* should be explicitly stated in the legislation. Under that law, any and all aspects of the conversion plan agreed to by BCBS of NJ and any agencies of the State of New Jersey (including the composition, structure, and activities of the foundations' board) must be reviewed by a judge in the Chancery Division of the Superior Court pursuant to a full fact-finding hearing. Summary proceedings are inappropriate given the complexity of the issues and magnitude of the public impact involved in the rededication of BCBS's charitable assets. Further, beneficiaries of BCBS of NJ must have standing in court to challenge the recommendations of state government, as recognized in the Community Health Care Assets Protections Act.

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HISTORY AND BACKGROUND OF BCBS of NJ's ATTEMPTS TO CONVERT ITS
CORPORATE STATUS TO FOR PROFIT:

The Blue Cross and Blue Shield plans that exist throughout the United States were conceived during the first part of the 20th century of as a national network of plans to provide health insurance when health insurance was virtually unknown. The American Hospital Association (AHA) and its state chapters pursued enabling legislation in the various states that facilitated the creation of such plans, and for many decades the Directors of the AHA and the national Blue Cross Association were overlapping. The original model of the plans was to provide affordable health insurance to the broad population, to use community rating to achieve that end, and to serve as the source of last resort for health insurance for individual subscribers. In the 1930s and 1940s, New Jersey enacted legislation that led to the formation of plans that eventually became Blue Cross and Blue Shield of New Jersey. BCBS of NJ's Certificate of Incorporation contained explicit references to its charitable purposes.

In 1986, the U.S. Congress ended the across the board tax exempt status of the BCBS organizations, recognizing the tremendous changes in the healthcare industry and the commercialization of BCBS plans nationally. In 1992 the NJ legislature removed many of the requirements imposed on Blue Cross by previous legislation, such as to be the insurer of last resort and to provide continuous open enrollment. In 1994 the national BCBS Association, which controls the BCBS trademark, abolished the requirement that member organizations be nonprofit.

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In 1995, Blue Cross and Blue Shield of New Jersey (BCBS of NJ) worked to pass legislation that would permit it to convert from a health services corporation to a mutual insurance company. It then announced its plan to purchase BCBS of Delaware (BCBSD) for \$103 million. Shortly thereafter, BCBS of NJ announced that it would merge with Anthem Insurance Companies, Inc., a for-profit mutual insurance company based in Indiana. In October 1996, BCBS of NJ filed proposals to convert to a mutual company and merge with Anthem. Both BCBS of NJ and Anthem denied that the proposal obligated them to protect and preserve BCBS of NJ's charitable assets. In response, the Attorney General issued an advisory opinion stating that BCBS of NJ was a charitable organization. In February 1997, BCBS of NJ filed a lawsuit against the Department of Banking and Insurance, asking the court to declare that the plan was not and never had been a charity. In March 1997, the trial court ruled that BCBS of NJ is a charitable corporation. In April 1997, BCBS of NJ and BCBSD announced that they would let their agreement expire and no longer would pursue the merger, citing legal and regulatory hurdles in both states. In June 1997, BCBS of NJ and Anthem announced that they also would let their merger proposal expire, again citing legal and regulatory hurdles. In October 1997, the appellate court ruled in favor of the Department of Banking and Insurance, affirming the trial court's decision that BCBS of NJ is a "charitable and benevolent institution." BCBS of NJ then sought review of the case by the New Jersey Supreme Court. In January 1998, the New Jersey Supreme Court denied BCBS of NJ's petition for certification. The appellate court decision is now final. In P.L. 1998, Ch.132, BCBS sought and obtained permission to uncap its investments

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in its for profit subsidiaries and thus began its “creeping conversion” to a for profit. The legislation currently under review should set an objective standard by which it can be determined whether BCBS has made a de facto conversion, at which time the formal conversion process and review by the appropriate state agencies and the chancery court would be triggered.

Since 1994, many BCBS plans throughout the nation have sought to convert from a nonprofit to a for profit status. A website maintained by Consumer Union identified thirty such conversion efforts.¹ The experiences and legislation emerging from these states should inform this Legislature’s efforts to rationalize the conversion of BCBS in New Jersey; and New Jersey citizens should not settle for weaker protections than those imposed by Attorneys General and legislatures in other states.

Also it must not be forgotten that BCBS organizations are not the only health care institutions that are seeking changes in their corporate status, or are acting more and more like for profits without changing their status. Throughout NJ and the country, direct care providers such as hospitals and nursing homes are increasingly engaged in joint ventures with for profit firms, creating for profit subsidiaries, and formally changing their status. Recently, the New Jersey legislature enacted the “Community Health Care Assets Protection Act” [A1439] which addresses the transfer of ownership of nonprofit hospitals. Both nonprofit hospitals and BCBS

¹ Conversion efforts listed by Consumer’s Union were in Cal., Colo., Conn., Del., Ga., Idaho, Ill., Kan., Ky., Me., Md., Miss., Mo., Nev., N.H., N.M., N.Y., N.C., N.D., Ohio, Or., Pa., S.D., Tex., Utah, Va., W.Va., Wis., the Commonwealth of Puerto Rico and the District of Columbia (data as of May 31, 2000.) (<http://www.consumersunion.org>)

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are charities organized for health purposes and the transfer of BCBS of NJ's assets require treatment similar to that of New Jersey hospitals. The "Community Health Care Assets Protection Act" thus provides many safeguards that should be used to protect the charitable assets of BCBS of NJ should it continue on its path to for profit status. Succinctly, there is no valid legal or policy reason for BCBS of NJ to be treated differently than other charitable health care organizations that convert to for-profit status.

DETAILED RECOMMENDATIONS TO STRENGTHEN THE PROPOSED LEGISLATION
TO ENSURE THAT THE CHARITABLE ASSETS OF BCBS of NJ ARE NOT
UNDERVALUED OR LOST TO THE INTENDED BENEFICIARIES--THE RESIDENTS OF
NEW JERSEY:

- I. AN AMOUNT EQUAL TO THE FAIR MARKET VALUE OF THE CHARITABLE ASSETS OF BCBS of NJ MUST BE USED TO CREATE ONE OR MORE PRIVATE AND INDEPENDENT FOUNDATIONS TO CARRY ON THE ORIGINAL MISSION OF BCBS of NJ. INFORMATION NECESSARY TO A PROPER EVALUATION OF THE FAIR MARKET VALUE OF BCBS of NJ MUST BE DEEMED NON-CONFIDENTIAL. THE PROPOSED LEGISLATION DOES NOT ADEQUATELY ENSURE EITHER OF THESE REQUIREMENTS.
 - A. A threshold consideration is when the application and review process should begin. As written, it begins only at the discretion of BCBS of NJ's Board, when it makes a formal motion and files an application to become a stock insurance company. However, in NJ's own Community Health Care Assets Protection (CHAP) Act and in other state's statutes and model legislation proposed by leading authorities, a review begins when the nonprofit entities' for profit activities grow to such an extent that it is no longer acting like a nonprofit. In

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NJ's CHAP Act, the application and review process is triggered whenever "a substantial amount of assets" have been transferred to another entity by "purchase, lease, exchange, conversion, restructuring, merger, division, consolidation, transfer of control or other disposition . . . whether through a single transaction or a series of transactions, with one or more persons or entities." In model legislation proposed by NAAG, the triggering event is the transfer of a "material amount" of the nonprofit's assets.² Consumers Union, a leader in the protection of charitable health assets, has proposed a similar model statute which further defines material amount to be more than 20%.³ In more than one state, residents have been concerned as their local Blues convert into for profit organizations without the necessary formal conversion, thus effecting a stealth transfer of charitable assets from non-profit purposes to for profit ventures that drain resources from the core, statutory charitable purpose of BCBS. In Missouri, a trial court determined that such a stealth conversion had taken place in violation of the charitable trust created by the legislature and an appeals court confirmed

² Model Act for Nonprofit Health Care Conversion Transactions, National Association of Attorneys General, § 1.01 (July 1998).

³ A Model Act (An Act concerning nonprofit hospitals, medical -surgical facilities, health maintenance organizations or health service corporations) Consumer's Union/Community Catalyst, §1(a)(1) (Summer 1998).

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that ruling.⁴ In Philadelphia, similar concerns are voiced about BCBS of Southeastern Pennsylvania. We have some indications that a substantial portion of charitable assets are already dedicated to for profit activities and the conversion process cannot be limited to BCBS of NJ's application to become a stock company. This proposed legislation must include a provision that the Attorney General and the Department of Banking and Insurance be given the authority to request information to enable them to determine whether and what proportion of BCBS's charitable assets have already been transferred to for profit joint ventures or subsidiaries. Such a loss of charitable assets, owed to the residents of New Jersey as beneficiaries, shall be accounted for in estimating the fair market value of BCBS of NJ's assets. In any event, transfer of more than 20% of BCBS of NJ's assets to any for profit, even if a wholly-owned subsidiary, must trigger a conversion application. This is the case because a nonprofit cannot fulfill its charitable mission if a substantial percentage of its assets are dedicated to profit making activities. As stated before, financial data that will indicate such transfers should be made available in quarterly reports to the Department of Banking and Insurance.

⁴ Blue Cross and Blue Shield of Mo. v. Angoff, 1998 WL435697 (Mo. Ct. of App., August 4, 1998).

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- B. An independent evaluation of the fair market value of the business of BCBS of NJ (its "charitable assets") must be undertaken by a private consultant under the auspices of the Attorney General and the Department of Banking and Insurance. Such a valuation is necessary to identify and quantify the tangible and intangible assets of BCBS, such as BCBS's subscriber lists, physician contracts, licenses, physical facilities, trademark, etc. Conversion of Blue Cross plans in stock transactions (the only type of transaction contemplated in the proposed legislation), does not per se determine value. The assets to be transferred must be valued under well known valuation principles. What a willing buyer would pay a willing seller involves the likelihood of a initial public offering (IPO) or sale of the company, potential private placements, licensing agreements, and inherent limits on value as a result of restrictions on voting rights and registration rights agreements. As in other states, New Jersey officials should be given broad authority to hire financial experts to help them review the details of the proposed transaction, especially since the legislation does not require BCBS's successor to create a market in which the foundation can liquidate any of the stock it holds and the legislation does not require the stock transferred to the foundation to be otherwise freely alienable.

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1. The independent valuation will look at the business plan proposed by BCBS, including its proposals to obtain additional capital, to see if it realizes maximum value for the public.
2. Under the presently proposed plan there are still many open questions related to the IPO (that is allowed but not mandated by the current legislation), which could affect shareholder value, including, but not limited to: restrictions on the resale of stock, issuance of different classes of stock, adverse tax consequences for the foundation, possible future dilution of interest, and issues of imprudent concentration of assets in a single company.
3. The uncertainties inherent in the creation of a foundation with 100% of the stock of the for-profit company require state officials to obtain an independent valuation to ensure that the fair market value of the converting entity has not been and will not be adversely affected by any of the parties involved in the transaction. Further, there must be an analysis presenting alternative business plans, perhaps recommending alternative paths for raising capital such as sale of the company through an open competitive bidding process rather than issuance of publicly traded stock.
4. In any event, the relevant state agencies, courts and residents of New Jersey must have a broad range of options to choose from in order to

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maximize the value of BCBS of NJ's charitable assets; and thus, the Attorney General and Insurance Commissioner must be given the authority and resources to conduct an independent evaluation of BCBS of NJ both from a financial and business standpoint, in the same manner as provided in New Jersey's CHAP Act.

5. Determination of fair market value should take into account all relevant considerations. According to NAAG's model legislation , *"[k]ey items in any fair market value analysis include the following: (1) whether the nonprofit entity has been aggressively marketed by investment bankers in a public auction to generate multiple bidders and maximum value; (2) whether there are competing offers and the proper evaluation of those offers; (3) whether appropriate business valuation appraisals have been obtained; (4) whether adequate professional assistance has been retained by the governing board to fulfill its duty of reasonable inquiry and due diligence; and (5) whether there is evidence of lucrative contracts with officer or employees, or lucrative buy-outs of related subsidiaries or entities, at the expense of the charitable interest."*⁵

⁵ Supra. n.2.

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6. Legislation proposed in New York deals with fair market value in the following way: *“Fair market value will be determined as of the time of conversion and shall take into account all relevant considerations, including, but not limited to, market value, investment or earnings value, net asset value, a control premium, the value of any licenses that may be transferred . . .”*⁶ Similar language should be included in the proposed legislation under consideration herein.

C. As a charitable trust and policy matter, we recommend that the assets transferred to the new foundation(s) should consist at the outset of cash at least equal to 20% of the fair market value of the charitable assets of BCBS of NJ. As currently written, the proposed statute would allow the new foundation to be funded solely with stock of the new for profit corporation. Consumer’s Union has stated “particular concerns arise when initial foundation assets are in the form of stock in the successor for profit corporation. In order to ensure its financial strength over the long term, the foundation will need to sell this stock to diversify its investments. . . rules of the national BCBS Association require that the foundation complete the process within a limited time period.”⁷ Foundations need cash for

⁶ NYS Assembly, A08846 (proposed)

⁷Schneider, H. & Cowan, D., eds., Building Strong Foundations (Consumer’s Union, 2000) at p. 20.

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operations, grant making, program startup, capital acquisitions, investment income, the diversity of the foundation's portfolio, etc. It has been suggested that there is a need for cash as a critical element in the creation of a foundation.⁸ The current legislation would create a foundation whose only assets consists of shares of stock in BCBS of NJ' successor, for profit corporation. Such a foundation serves only as a passive stock holding company, and cannot perform its charitable mission. The remainder of the assets transferred to the new corporation may be in stock of the newly created for profit corporation, but no unreasonable restrictions may be placed on the foundation's voting rights relative to that stock, or the foundation's ability to sell or otherwise transfer the stock. (See Recommendation III, infra., on the importance of the independence of the new foundation from the for profit successor to BCBS of NJ.) Also, Internal Revenue Service regulations require that charities disburse a certain percentage of their assets/income each year and not merely collect revenues or act as a shell corporation. Providing the new foundation only with stock, with numerous restrictions on how, to whom, and when it can sell that stock, does not satisfy these regulations and places the new foundation's tax exempt status unnecessarily at risk.

⁸"The Sierra Health Foundation," in New Foundations in Health: Six Stories (Milbank Memorial Fund, 1999)

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II. THE APPLICATION PROCESS MUST BE TRANSPARENT AND ALLOW FOR MEANINGFUL PUBLIC INPUT IN ORDER TO ENSURE THAT THE INTERESTS OF THE CHARITABLE BENEFICIARIES, THE RESIDENTS OF NEW JERSEY, ARE PROTECTED. ALL INFORMATION NECESSARY TO A PROPER EVALUATION OF THE IMPACT OF THE CONVERSION ON THE HEALTH CARE SERVICES AVAILABLE TO THE PUBLIC SHOULD BE FREELY AVAILABLE TO ALLOW PUBLIC SCRUTINY. THE ATTORNEY GENERAL, WITH THE ASSISTANCE OF THE COMMISSIONER OF BANKING AND INSURANCE, SHOULD MAKE THAT EVALUATION USING PRE-DETERMINED CRITERIA SUCH AS THOSE ESTABLISHED BY THE RECENTLY ENACTED "COMMUNITY HEALTH CARE ASSETS PROTECTION ACT."

A. The public comment period in the proposed legislation can be as little as 50 days.⁹

This is not a sufficient period of time for meaningful review, analysis, preparation of comments, and coordination of responses among the millions of beneficiaries of BCBS of NJ. The conversion application and supporting documents can be expected to be voluminous. Further, the governmental response will itself require review and comment, outside of judicial proceedings, which is not provided for in the legislation. Independent parties (*i.e.*, other than the government and BCBS of NJ) are operating outside the familiar and ongoing relationship between the government and BCBS of NJ and typically have limited resources to conduct an review on an expedited basis. A period of 120 days from the date that the application is deemed complete by the Commissioner and

⁹ The proposed time line begins with BCBS' filing of a plan of conversion with the Insurance Commissioner; within 20 days, the Commissioner publishes a public notice; public hearings are completed within 60 days from date of filing; written comment period ends 10 days after public hearings are completed.

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Attorney General is a reasonable time to allow independent, but highly interested, parties to review a complicated application and the government's response.

- B. Only one public hearing is required by the legislation. Given that BCBS of NJ covers the entire state it seems reasonable to hold at least three hearings, one each in the northern, central, and southern regions of the state. This will provide all interested parties reasonable geographic access to hearings.
- C. Parts of the application, specifically the business plan of the new for profit corporation, are to be "confidential" and not open for public review. Under the proposed legislation the only assets transferred to the future charitable foundation consists of stock in the for-profit corporation. Therefore the business plan is integral to valuing the for-profit corporation and of paramount interest to the charitable beneficiaries -- the residents of New Jersey. The business plan will contain specific information about proposed premium increases and the anticipated effects on policyholders and subscribers and the expected impact on insurance reserves. All of this information is germane to the valuation analysis and the ultimate bequest to the new foundation, but also to the employers and enrollees who have supported BCBS of NJ for generations. There are ample precedents in law and statute for full disclosure. The Community Health Care Assets Protection Act provides that "the Attorney General shall make the information received pursuant to this [application], and the Department of Health

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and Senior Services shall make any information in its records relating to the proposed acquisition, available for inspection at no cost to the public.”¹⁰ Superior Court Justice Karchman in his opinion on HIP’s attempt to limit release of information to the Public Interest Law Center regarding the HIP-PHP sale and lease transaction addressed this precise issue:

“the changing landscape of the medical profession and medical industry requires that the public, more than ever, has available to it those facts and information which will bear directly on their well-being and ultimately on the delivery of medical services. Included in the public’s right to know is the element of cost, a critical and complex element of this ever-growing and complex industry. . . The dramatic shift of assets from a non-profit medical provider to a profit making entity requires close scrutiny not only by the Department [of Banking and Insurance] but by the public as well.”¹¹

A similar policy of unfettered disclosure should be applied to the BCBS of NJ conversion legislation. At a minimum, the statute should expressly allow any beneficiary involved in a cy pres proceeding in the Chancery Division to have

¹⁰ P.L. 2000, Ch. __ (A1439, §2(f)).

¹¹ HIP of New Jersey v. New Jersey Dept of Banking and Insurance, 309 N.J. Super 538, 555 (1998) (*emphasis added*)

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access to all documents under an appropriate confidentiality agreement enforced by the court.

- D. Any and all documents related to BCBS's conversion application that are filed, submitted, maintained, created or otherwise obtained by the state agencies, and not deemed confidential by those agencies (pursuant to objective standards that balance the public's need to know with BCBS's competitive concerns) shall be available to the public as soon as is feasible, preferably through posting on government websites, or by photocopies provided by BCBS of NJ.
- E. The evaluation of the conversion plan by the various state agencies, the Chancery Division, and interested parties must be guided by some agreed upon criteria. The Community Health Care Assets Protection Act has a useful list of criteria as does the model legislation proposed by the NAAG. Some of the criteria address fair market value assessments, the affect on the beneficiaries, the due diligence and conflicts of interest of current board members, the structure and mission of the new foundation and more. There is no valid reason for not incorporating those standards into the legislation herein at issue.
- F. No current officer of BCBS of NJ should be allowed to benefit directly or indirectly from the conversion. To do so would be an illegal usurpation of charitable assets and contrary to fundamental principles of the law governing nonprofit corporations. The proposed legislation, however, permits the

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distribution of stock options in the for-profit successor to officers, directors and employees of BCBS of NJ upon the conversion.¹² This exception overwhelms the general principle that no officer, director or employee of BCBS should benefit in any way from the conversion and thus should be eliminated. Instead, we recommend that language such as that found in proposed New York legislation regarding the conversion of Empire Blue Cross Blue Shield be incorporated. It provides that “the fair market value of the applicant has not and is not being manipulated, or otherwise altered in connection with the proposed conversion, in any manner that causes the charitable assets to decrease or be undervalued; the conversion will not result in inurement to any private person or entity, including stock options, agreements not to compete, and other private benefits.”¹³

- III. THE BOARD OF DIRECTORS OF ANY NEW FOUNDATION MUST BE COMPLETELY INDEPENDENT AND DEVOTED SOLELY TO FULFILLING THE MISSION OF THE FOUNDATION. THERE SHOULD BE NO UNREASONABLE RESTRICTIONS PLACED ON HOW FOUNDATION DIRECTORS MAY VOTE ON ANY ASPECT OF THEIR GOVERNANCE OF THE NEW FOUNDATION, INCLUDING WHEN TO SELL STOCK OF THE FOR-PROFIT, TO WHOM, AND HOW TO VOTE THE STOCK OF THE FOR PROFIT. THE FOUNDATIONS’ BOARD, AS REPRESENTATIVE OF THE PUBLIC, MUST BE ABLE TO CONTROL AND DIVERSIFY ITS ASSET BASE IN ORDER TO MAXIMIZE THE VALUE OF THE FOUNDATION AND TO PURSUE ITS CHARITABLE MISSION. THE PROPOSED BILL PERMITS THE IMPOSITION OF VOTING AND REGISTRATION RESTRICTIONS ON THE STOCK HELD BY THE FOUNDATION WITHOUT

¹² A2739, §3(d); S1581, §3(d).

¹³Supra. n.6.

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IMPOSING ANY STANDARD OF REASONABLENESS CONTRARY TO MODEL
LEGISLATION PROPOSED BY THE NAAG.

- A. The Board of Directors of the new foundation will have, as any Board does, a fiduciary duty to further the interests of its beneficiaries and fulfill its mission. To do that the board must be a self-perpetuating board completely independent of the successor for-profit corporation, independent of state government and populated by persons with expertise in philanthropy, health policy, representatives of the under insured and uninsured. The proposed legislation will create a board composed of 15 members appointed by the governor, upon recommendation by various elected official and trade associations. Such a board will be dominated by partisan political considerations and the interests of the powerful provider groups. None of the model legislation (Consumers Union, NAAG) or state statutes enacted (North Carolina) or proposed (New York, Pennsylvania) reviewed for this testimony use such a procedure for creating or perpetuating a foundation board. Consumer's Union recommends that "State, county or municipal government also should not control conversion foundations . . . it would violate the charitable trust doctrine to allow those assets to come under governmental control."¹⁴ The North Carolina statute provides for a prudent process for creating an independent and appropriately qualified board of directors.

¹⁴Supra. n. 7., at p. 10.

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That statute mandates the appointment of an advisory board which, with the assistance of an executive recruiting firm, shall identify 22 prospective directors to be submitted to the Attorney General for consideration. The Attorney General shall choose 11 members for the Board, which then becomes a self perpetuating board.¹⁵ In New Jersey, we recommend a similar process as enacted in North Carolina, except that we further recommend that the Attorney General's responsibilities be explicitly supervised by the Chancery Division. The role of the court is necessary to ensure the independence, loyalty and competency of the Board appointed to the new foundation. Emphatically, this foundation cannot be seen as a pot of money to be controlled by either elected or appointed officials, trade groups or other special interests.

- B. There should be no unreasonable restrictions placed on how Foundation Directors may vote on any aspect of their governance of the new foundation, especially with respect their shares in the for- profit. The proposed legislation allows a voting agreement under which the Board of the new foundation would be required to vote, in the foundation's role as shareholder of the stock of the new for- profit, as directed by the board of the for- profit. This violates the laws of charitable trusts, under which a Board or trustee must operate and manage its assets for the sole

¹⁵ N.C. Gen. Stat. §58-65-133(c)(d)

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benefit of the intended beneficiaries. Fiduciaries must exercise reasonable care in the implementation of their duties and relinquishment of control over the foundation's assets, without retaining appropriate reserve powers, cannot be considered reasonable. Accordingly, we recommend the elimination of such provision. On the other hand, reasonable restrictions on the foundation's stock, if any, must be negotiated between BCBS of NJ, the national BCBS Association, and the Attorney General (depending on the ultimate structure of the conversion, the expected liquidity of the stock and several other factors noted previously) in order to ensure that the value of the stock held by the foundation is maximized.

- C. The non-compete clause of the proposed legislation is unnecessary and may be wrongfully construed to restrict the activities of the new foundation. As discussed above, the original charitable mission of BCBS of NJ was to provide access to medical insurance for the residents of New Jersey. The historical mission of BCBS of NJ largely determines the mission of the foundation to be created, according to the doctrine of trust law known as cy pres (see below.) Therefore, the new foundation will work to increase access to medical care, and may well choose to do so by, for example, subsidizing insurance to working families whose employers do not offer health insurance. The conversion of this charity to a for-profit entity must leave behind a new foundation with a mission similar to that envisioned in the creation of BCBS of NJ, and that is to provide access to medical

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care. The non-compete clause of the proposed legislation would hamper the new foundation in pursuing such a mission, and that clause must be either eliminated or radically narrowed. It may be possible to confine the new foundation to serving the "medically indigent," however defined, or to bar it from serving the commercial market. However, the new foundation's manifest status as a tax exempt charitable foundation would forbid it from competing with the for-profit BCBS of NJ because doing so would jeopardize its tax exempt status. The fundamental legal status of the two entities - a for-profit domestic stock corporation on the one hand, and a charitable foundation on the other - would not allow any competition. The non-compete clause is unnecessary and may be wrongfully construed in later years to prevent the foundation from creating or funding innovative insurance programs for persons who do not have access to the commercial insurance offered by the new BCBS of NJ .

- D. Annual reports of the work of the foundations, including audited financial statements, shall be available to the public and must be reviewed by the Attorney General as primary, but not exclusive, enforcer of charitable trusts. Under New Jersey law, persons with a special interest in a charitable organization, such as

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beneficiaries, have a recognized role in ensuring that directors satisfy their

fiduciary duties to the charity and stated missions are not transgressed.¹⁶

IV. THE MISSION OF THE NEW FOUNDATION(S) SHOULD CORRESPOND TO THE ORIGINAL GOALS OF BCBS OF NJ: TO PROMOTE ACCESS TO MEDICAL CARE FOR THOSE RESIDENTS OF NEW JERSEY WHO ARE UNDER OR UNINSURED. FURTHER, THE FOUNDATION'S ASSETS MAY NOT BE APPLIED TO ACTIVITIES THAT TO DATE HAVE BEEN ASSUMED BY GOVERNMENTAL ENTITIES. WHETHER THE NEW FOUNDATION(S) WILL HAVE GRANT MAKING AND/OR PROGRAMMATIC FUNCTIONS SHOULD BE DECIDED BEFORE THE CONVERSION IS APPROVED.

A. That the new foundation's mission should correspond closely to the original mission of BCBS of NJ merely restates one axiom of the law of trusts (see definition of cy pres below.) The National Association of Attorneys General has written the "newly created foundation must utilize the assets for a charitable purpose benefitting the same class of beneficiaries." Further, "the charitable purposes of these new [foundations] is, generally, to meet the healthcare needs of the uninsured/underinsured populations in [the] particular states."¹⁷ New York's proposed legislation states explicitly that the "mission of the [foundation] shall include expansion of access to health care by extending health insurance coverage to state residents who cannot afford to purchase their own coverage or who have

¹⁶City of Paterson v. Paterson General Hosp., 97 N.J. Super 514 (Ch. Div. 1967).

¹⁷ Supra. n. 2.

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coverage that is inadequate to meet their needs.”¹⁸ The proposed Pennsylvania statute states “The charitable mission and grant-making function of the [foundation] shall be dedicated to serving the community’s unmet healthcare needs, particularly with respect to the uninsured and underinsured populations.”¹⁹ In New Jersey there are currently an estimated 1,329,000 uninsured persons, or 16% of the total state population.²⁰ NJ hospitals provided \$520 million worth of care to medically indigent persons in 1999, with the burden falling disproportionately on inner city hospitals. The NJ Department of Health and Senior Services reimbursed the hospitals \$350 million for that care leaving a gap of approximately \$170 million.²¹ Since this data includes only acute care providers (excluding all other providers and levels of care) and ignore the health effects of care not received (unnecessary mortality, disability, economic productivity), the magnitude of the problem of the uninsured is only hinted at by these statistics. Clearly there is a tremendous need in our state for additional resources and innovative programs to address the critical issue of access to care,

¹⁸ Supra. n. 6.

¹⁹ Pa. Senate Bill 810 (proposed, 1999).

²⁰ Health Insurance Coverage, Current Population Reports (U.S. Census Bureau, October 1999).

²¹ NJ Hospital Association Daily Message, June 6, 2000.

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which is mostly a matter of access to insurance. The original purpose of the tax exempt BCBS of NJ -- to provide care for the broad community and to be a part of the safety net for medical insurance - is far from completed and should be explicitly incorporated in the statute..

- V. THE APPLICABILITY OF THE COMMON LAW OF *CY PRES* SHOULD BE EXPLICITLY STATED IN THE LEGISLATION. UNDER THAT LAW, ANY AND ALL ASPECTS OF THE CONVERSION PLAN AGREED TO BY BCBS OF NJ AND ANY AGENCIES OF THE STATE OF NEW JERSEY (INCLUDING THE COMPOSITION, STRUCTURE, AND ACTIVITIES OF THE FOUNDATIONS' BOARD) MUST BE REVIEWED BY A JUDGE IN THE CHANCERY DIVISION OF THE SUPERIOR COURT PURSUANT TO A FULL FACT-FINDING HEARING. SUMMARY PROCEEDINGS ARE INAPPROPRIATE GIVEN THE COMPLEXITY OF THE ISSUES AND MAGNITUDE OF THE PUBLIC IMPACT INVOLVED IN THE REDEDICATION OF BCBS's CHARITABLE ASSETS. FURTHER, BENEFICIARIES OF BCBS OF NJ SHOULD HAVE STANDING IN COURT TO CHALLENGE THE DETERMINATIONS OF STATE GOVERNMENT, AS RECOGNIZED IN THE COMMUNITY HEALTH CARE ASSETS PROTECTION ACT.

- A. As noted above, BCBS of NJ is one of many BCBS plans across the country which is attempting to convert to for-profit status or already has. A website maintained by Consumer Union identified thirty such conversion efforts.²² In New Jersey, as elsewhere in the United States, the charitable obligations of a non profit corporation can be enforced under the common law doctrine of *cy pres*. The phrase *cy pres* comes "from French, meaning as close as possible. When a gift is made by will or trust . . . for charitable or educational purposes and the

²²Supra. n.1.

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named recipient of the gift [here BCBS of NJ], has dissolved or no longer conducts the activity for which the gift is made, then the estate or trustee[s] must make the gift to an organization which comes closest to fulfilling the purpose of the gift.”²³ New Jersey Courts have consistently upheld the application of *cy pres* in private trusts and nonprofit hospitals wherein the Chancery Division has interceded to protect the intended beneficiary(ies).

- B. In many states, legislation has been enacted to confirm the common law or constitutional role of the chancery courts in *cy pres* proceedings for charitable trusts generally and for health care conversions specifically. The NJ legislature enacted The Community Health Care Assets Protection Act, regarding the conversion of nonprofit hospitals, which provides for a cy pres review of any hospital conversion. A hospital seeking to convert shall “satisfy the requirements of this act before applying to the Superior Court of New Jersey for approval, . . . The Attorney General shall review the application in furtherance of his common law responsibilities as protector, supervisor, and enforcer of charitable trusts and charitable corporations.” (*emphasis added*), Similarly unambiguous language defining the respective roles of the Attorney General and the Superior Courts should be included in BCBS conversion legislation. The fact that BCBS

²³ (DICTIONARY OF THE LAW, <http://dictionary.www.law.com>)

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was deemed a charitable and benevolent organization by the Legislature does not remove the Chancery Division's ultimate supervision over its activities as a "charity" nor its conversion to a for-profit entity.

- C. As a constitutional matter, the Legislature cannot abrogate the special jurisdiction of the Chancery Division over charitable trusts. This jurisdiction involves the supervision and administration of trusts of all kinds.²⁴ The original basis for such equitable jurisdiction is the interest of the public in charitable trusts. For example, the authority to give instructions to a trustee had always been within the jurisdiction of the pre-1947 Chancery Court and the legislature could not impair the jurisdiction of Chancery by giving another tribunal concurrent jurisdiction of a subject matter which, at the time of adoption of the former constitution, belonged exclusively to Chancery.²⁵ Jurisdiction over charitable uses, or trusts, has traditionally been within the exclusive domain of the chancery courts, inherited from the English common law. See generally David Villar Patton, *The Queen, the Attorney General, and the Modern Charitable Fiduciary: A Historical Perspective on Charitable Enforcement Reform*, 11 U. FLA J.L. & PUB. POL'Y

²⁴ De Geeter v. Wolklin, 136 N.J. Eq. 510, 512 (1945); Frank v. Clover Leaf Park Cemetery Ass'n, 29 N.J. 193, 208 (1959).

²⁵ Blauvelt v. Citizens Trust Co., 3 N.J. 545, 551 (1950) (repeating the holding of In re Roth's Estate, 139 N.J. Eq. 588 (1947)).

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131 (2000). The powers of this court are a constitutional matter,²⁶ and thus may not be impaired by the Legislature.²⁷ Therefore, if the Legislature tries to eliminate (as the proposed legislation does) or severely restrict the court's review in a summary proceeding, a compelling argument can be made that the statute would be unconstitutional as well as violative of the due process rights of the public that are the "owners" of this charitable organization.

If this State is to learn anything from the experience surrounding the dissolution of HIP, it is the importance of an independent financial evaluation, public scrutiny and a thorough process of judicial review (that were so lacking therein). These three elements are also missing from the proposed legislation. We therefore urge you to take the time to consider our recommendations and follow the principles found in New Jersey's CHAP Act, recently enacted with regard to the conversion of nonprofit hospitals.

Thank you for the opportunity to present PILC's views, and I welcome any questions that you may have.

²⁶N.J. Const. (1947), Art. VI, §3.

²⁷ Board of Educ. of City of Asbury Park v. Asbury Park Educ. Ass'n, 145 N.J. Super. 495, 510 (Ch. Div. 1976). See also O'Neill v. Vreeland, 6 N.J. 158 (1951) (stating that jurisdiction of the Superior Court is fixed by the Constitution and cannot be altered by court rule or by an act of the Legislature); Plaza v. Flak, 7 N.J. 215, 222 (1951) (reiterating that under the letter and spirit of the Constitution of 1947 actions formerly maintainable in the Court of Chancery, where the primary right or relief sought is equitable, should be brought in the Chancery Division of the Superior Court).

Public Hearings re: Assembly Committee Substitute for
NJ Assembly Bill 2739

Statute Proposed to Protect the Charitable Assets of Blue Cross and
Blue Shield of New Jersey Upon its Conversion from a Charity to a
Domestic Stock (For Profit) Corporation

Testimony of:
Renée Steinhagen, Executive Director
Public Interest Law Center of New Jersey
833 McCarter Highway
Newark, NJ 07102

INTRODUCTION:

Good morning Ladies and Gentlemen. My name is Renée Steinhagen; I am the Executive Director of the Public Interest Law Center of New Jersey (PILC.) The PILC is a nonprofit organization established to provide legal advocacy that addresses systemic social and political problems facing residents of New Jersey. The PILC has initiated a broad advocacy project regarding the restructuring of nonprofit health maintenance organizations, insurance companies, and hospitals upon the conversion of such entities from nonprofit to for profit status or the acquisition of such entities by companies with different corporate purposes. The PILC seeks to provide a legal voice for those community interests that otherwise would not be represented in the administrative processes that govern such corporate changes and in the judicial system where controversies surrounding the transactions often take place.

We were active as counsel to *amici* in the judicial proceedings initiated by BCBS of NJ two years ago, participated in the litigation surrounding the privatization of Bergen Pines Hospital (now Bergen Regional), obtained documents underlying the HIP-PHP transaction through the judicial process and negotiated an approved settlement agreement with the Department of Banking and Insurance to investigate the charitable trust issues arising from the State's approval of the HIP-PHP transaction. In addition, I personally served as counsel to the American Civil Liberties Union of NJ and FirstChoice of NJ who were found to be interested parties in what turned out to be a successful court action to obtain a charitable trust settlement as a result of the merger between St. Elizabeth and Elizabeth General Hospitals.

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The Public Interest Law Center (PILC) feels strongly that the essential goal of this legislation should be the preservation of the charitable assets of the Blue Cross and Blue Shield of New Jersey for generations to come. Across the United States, over 100 foundations have been created by the conversion of nonprofit health providers and insurers, with assets totaling several billions of dollars. The creation of a new health foundation for New Jersey will be a significant event in the philanthropic resources available to New Jersey residents. As written, however, the statute, though much improved from that first proposed, does not offer sufficient safeguards that will ensure the creation of an independent foundation that will receive the full fair market value of the charitable assets of BCBS of NJ.

Although the bill currently before you recognizes the complexity of the conversion process, the fact that Blue Cross may choose to become a for-profit company in ways other than applying to become a domestic stock corporation, and the Attorney General's and Superior Court's role in supervising charitable organizations (all lacking in the first version), it still departs from the recently enacted "Community Health Care Assets Protection Act" [A1439] in ways crucial to ensuring the role of and accountability to the public in the decision to convert and in determining the activities of the resulting foundation. Differences between the Community Health Care Assets Protection Act--the Assets Protection Act-- and the proposed conversion statute with respect to **criteria for approval, information provided to the public for review, the nature of the proceeding before the Chancery Division of the Superior Court and the**

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composition of the new foundation's board all point to aspects of the proposed bill to which we recommend further changes.

Succinctly, it is PILC's position that the Assets Protection Act provides many safeguards that should be used to protect the charitable assets of BCBS of NJ should it continue on its path to for-profit status. And, we do not see, nor has anyone presented, any valid legal or policy reason for BCBS of NJ to be treated differently than other charitable health care organizations that convert to for-profit status.

I. Section 1: Definition of "Material change in form"

A threshold consideration is when the application and review process should begin. As written, it begins at the discretion of BCBS of NJ's Board, when it makes a formal motion and files an application to become a stock insurance company, or when it notifies the government that it intends to engage in any action that constitutes or may constitute a material change in form. Material change in form is defined negatively to "not be deemed to occur so long as, during the most recent four prior consecutive calendar quarters: (1) the aggregate revenues of all nonconforming affiliates do not exceed 50% of the aggregate revenues for the health service corporation and all affiliates; (2) the aggregate revenues of all nonconforming affiliates derived from providing individual or group health coverage to residents of New Jersey equal or exceed 50% of the aggregate revenues from all nonconforming affiliates; or (3) the aggregate assets of all nonconforming affiliates do not exceed 50% of the aggregate assets of the health service corporation and all affiliates." However, in NJ's own Community Health Care Assets

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Protection Act and in other state's statutes and model legislation proposed by leading authorities, a review begins when the nonprofit entities' for profit activities grow to such an extent that it is no longer acting like a nonprofit—a point that is typically below the 50% threshold legislated in the proposed bill.

In NJ's Assets Protection Act, the application and review process is triggered whenever "a substantial amount of assets" have been transferred to another entity by "purchase, lease, exchange, conversion, restructuring, merger, division, consolidation, transfer of control or other disposition . . . whether through a single transaction or a series of transactions, with one or more persons or entities." In model legislation proposed by NAAG, the triggering event is the transfer of a "material amount" of the nonprofit's assets.¹ Consumers Union, a leader in the protection of charitable health assets, has proposed a similar model statute which further defines material amount to be more than 20%.²

We have some indications that a substantial portion of BCBS' charitable assets are already dedicated to for-profit activities and thus, the conversion process cannot be limited to BCBS of NJ' application to become a stock company or to reaching the 50% threshold. This high threshold invites manipulation of business subsidiaries or accounting practices to avoid

¹ Model Act for Nonprofit Health Care Conversion Transactions, National Association of Attorneys General, § 1.01 (July 1998).

² A Model Act (An Act concerning nonprofit hospitals, medical -surgical facilities, health maintenance organizations or health service corporations) Consumer's Union/Community Catalyst, §1(a)(1) (Summer 1998).

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reaching the “magic number” and severely limits the Attorney General from fulfilling his common law and statutory duties to protect charitable assets. The proposed bill makes the procedures set forth therein the “exclusive” means by which the Attorney General can discharge its historical function in this area. Accordingly, we recommend adopting the language in the Assets Protection Act and eliminating the 50% threshold. At minimum, we recommend lowering the threshold to 30%, tightening the test employed in the definition of “material change in form” to use the word “and” instead of “or,” and amending Section 19(d)(1), dealing with the new foundation, to reflect that the foundation plan submitted pursuant to that section does not just follow BCBS of NJ’s conversion to a domestic stock health insurer, but also its creeping conversion through a material change in form in accordance with Section 18.³

II. Criteria for Approval

There is little doubt that the substitute bill delineates more specifically than the initial version the criteria to be employed by the Commissioner of Banking and Insurance and the Attorney General when considering BCBS of NJ’s application to convert. However, a comparison of Section 4(a) governing the Commissioner’s approval decision and Section 19(c) regulating the Attorney General’s review with the criteria set forth in Section 2 of the Assets

³Specifically we propose the following language to Sect. 19(d)(1): “The foundation plan shall provide for the establishment of one or more foundations that will receive the fair market value of the health service corporation following its conversion to a domestic stock health insurer or otherwise pursuant to Section 18, and that meet the following requirements:”

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Protection Act indicates that some key standards that frame the regulators' decision as to whether the proposed conversion is in the public's interest are missing.

The Community Health Care Assets Protection Act specifically provides:

2(b). The proposed acquisition shall not be considered to be in the public interest unless the Attorney General determines that appropriate steps have been taken to safeguard the value of the charitable assets of the hospital and to ensure that any proceeds from the proposed acquisition are irrevocably dedicated for appropriate health care purposes; and the Commissioner of Health and Senior Services determines that the proposed transaction is not likely to result in the deterioration of the quality, availability or accessibility of health care services in the affected communities.

No where in the proposed BCBS of NJ conversion bill is the Commissioner or the Attorney General explicitly given similar mandates. Accordingly, we strongly recommend that the Commissioner of Banking and Insurance, like the Commissioner of Health and Senior Services in the case of hospital acquisitions, be required to assess the impact of the proposed conversion on premium rates and rates of coverage and determine, prior to approving the conversion, that the proposed transaction is not likely to result in unacceptable decreases in access to health care services, insurance coverage, community benefits and employment levels. Similarly, the Attorney General's authority to determine whether (i) charitable funds are placed at unreasonable risk, (ii) the converting health care organization considered the proposed transaction as the only alternative or as the best alternative in carrying out its mission and purposes; and (iii) the nonprofit exercised due care in assigning a value to the existing entity and its charitable assets in proceeding to negotiate the proposed conversion, found in Section 2(d) of the Assets Protection Act, be stated herein as well.

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In addition, PILC and other consumer groups contend that no current officer of BCBS of NJ should be allowed to benefit directly or indirectly from the conversion. To do so would be an illegal usurpation of charitable assets and contrary to fundamental principles of the law governing nonprofit corporations. The proposed legislation, however, permits the distribution of up to 5% of the aggregate shares of capital stock to be issued by the converted insurer to the officers, directors and employees of BCBS of NJ upon the conversion,⁴ and this limitation does not even appear to apply if the stock offering occurs after the first anniversary of the effective date of conversion⁵. These exceptions overwhelm the general principle that no officer, director or employee of BCBS should benefit in any way from the conversion and thus should be eliminated. Instead, we recommend that language such as that found in proposed New York legislation regarding the conversion of Empire Blue Cross Blue Shield be incorporated. It provides that "the fair market value of the applicant has not and is not being manipulated, or otherwise altered in connection with the proposed conversion, in any manner that causes the charitable assets to decrease or be undervalued; the conversion will not result in inurement to any private person or entity, including stock options, agreements not to compete, and other private benefits." At minimum, the 5% limitation should be lowered to 2% and the limitation should explicitly apply to any stock offering made within three years of the effective date of conversion or only after the new foundation has divested a certain percentage of the stock. It is simply not clear that BCBS

⁴ S1581, §6(e).

⁵ S1581, §9.

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of NJ will offer any stock to the public within a year of its conversion to a for-profit entity and thus the one-year limitation provides no protection at all.

III. Public Information

Although the proposed bill purports to involve the public in the regulatory process by requiring both the Commissioner and Attorney General to hold a public hearing, either separately or jointly, the proposed legislation stymies public scrutiny by unnecessarily limiting the public's access to certain documents. Unlike the Assets Protection Act, crucial parts of the application, specifically the business plan of the new for profit corporation and financial projections are to be "confidential" and not open for public review. Under the proposed legislation, the assets transferred to the future charitable foundation consist of stock in the for-profit corporation or some amount of cash. Therefore, the business plan is integral to valuing the for-profit corporation and of paramount interest to the charitable beneficiaries -- the residents of New Jersey. The business plan will also contain specific information about proposed premium increases and the anticipated effects on policyholders and subscribers and the expected impact on insurance reserves. All of this information is germane to the valuation analysis and the ultimate bequest to the new foundation, but also to the employers and enrollees who have supported BCBS of NJ for generations. There are ample precedents in law and statute for full disclosure. The Community Health Care Assets Protection Act provides that "the Attorney General shall make the information received pursuant to this [application], and the Department of Health and Senior Services shall make any information in its records relating to the proposed acquisition,

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available for inspection at no cost to the public.”⁶ Superior Court Justice Karchman in his opinion on HIP’s attempt to limit release of information to the Public Interest Law Center regarding the HIP-PHP sale and lease transaction addressed this precise issue:

The changing landscape of the medical profession and medical industry requires that the public, more than ever, has available to it those facts and information which will bear directly on their well-being and ultimately on the delivery of medical services. Included in the public’s right to know is the element of cost, a critical and complex element of this ever-growing and complex industry. . . The dramatic shift of assets from a non-profit medical provider to a profit making entity requires close scrutiny not only by the Department [of Banking and Insurance] but by the public as well.⁷

A similar policy of unfettered disclosure should be applied to the BCBS of NJ conversion legislation. Members of the public will simply not be able to participate effectively in any hearings held by the Commissioner and/or Attorney General if they too are not given access to the very information necessary to evaluating the proposed plan of conversion. At a minimum, the statute should expressly impose the finding of harm requirement currently applicable to the release of “other information” under Section 10 to the business plan and financial projects submitted as part of the conversion application (either as part of the fair market evaluation or separately) and specifically, allow any beneficiary involved in a *cy pres* proceeding in the Chancery Division to have access to all documents under an appropriate confidentiality agreement enforced by the court.

⁶ P.L. 2000, Ch. __ (A1439, §2(f)).

⁷ *HIP of New Jersey v. New Jersey Dept of Banking and Insurance*, 309 N.J. Super 538, 555 (1998) (*emphasis added*)

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IV Chancery Court Proceeding

This brings us to yet another aspect of the substitute bill that remedies blatant defects in the initial bill, but, from our perspective, only half-way. That is the role of the Chancery Division in assessing the adequacy of the conversion and foundation plan pursuant to the doctrine of *cy pres*. New Jersey Courts have consistently upheld the application of *cy pres* in private trusts and nonprofit hospitals wherein the Chancery Division has interceded to protect the intended beneficiary(ies). Jurisdiction over charitable uses, or trusts, has traditionally been within the exclusive domain of the chancery courts, inherited from the English common law. See generally David Villar Patton, *The Queen, the Attorney General, and the Modern Charitable Fiduciary: A Historical Perspective on Charitable Enforcement Reform*, 11 U. FLA J.L. & PUB. POL'Y 131 (2000). Since the powers of this court are a constitutional matter,⁸ the Legislature cannot abrogate or impair the special jurisdiction of this court over charitable trusts.⁹ Therefore, if the Legislature tries to eliminate (as the initially legislation did) or severely restrict the court's review in a summary proceeding (as the substitute bill does) a compelling argument can be made

⁸N.J. Const. (1947), Art. VI, §3.

⁹ Board of Educ. of City of Asbury Park v. Asbury Park Educ. Ass'n, 145 N.J. Super. 495, 510 (Ch. Div. 1976). See also O'Neill v. Vreeland, 6 N.J. 158 (1951) (stating that jurisdiction of the Superior Court is fixed by the Constitution and cannot be altered by court rule or by an act of the Legislature); Plaza v. Flak, 7 N.J. 215, 222 (1951) (reiterating that under the letter and spirit of the Constitution of 1947 actions formerly maintainable in the Court of Chancery, where the primary right or relief sought is equitable, should be brought in the Chancery Division of the Superior Court).

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that the statute is unconstitutional as well as violative of the due process rights of the public that are the “owners” of this charitable organization.

Furthermore, there is simply no policy reason to transform the *cy pres* hearing in the Chancery Division into a summary proceeding. The Court, as supervisor of charitable trusts, and members of the public, are entitled to full hearing on the merits, at which time, the latter must be given the opportunity to be heard in accordance with common law. Although the proposed bill does not deny the public, as “owners” of BCBS of NJ or its beneficiaries, standing in the *cy pres* proceeding, PILC recommends that the Legislature adopt the language in Section 2(1) of the Assets Protection Act which explicitly provides that

Any person adversely affected by the final decision of the Attorney General that participated in the public hearing required by this act shall be considered a party to the proceeding, including consumers or community groups representing the citizens of the State, and shall receive appropriate notice of the proceeding from the nonprofit hospital in accordance with the Rules of Court.

The final legislation must explicitly recognize and support the role of the public in the conversion process; for otherwise, the public’s confidence in government and BCBS of NJ as well as the viability and success of the resulting foundation will be seriously undermined.

V. The New Foundation, Its Board and its Mission

Finally, as a representative of the general public-- in this case, health care consumers and tax payers — PILC has serious concerns that the new foundation will not be able to fulfill its community mission with the board structure currently proposed. The Board of Directors of the new foundation will have, as any Board does, a fiduciary duty to further the interests of its

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by the Chancery Division. The role of the court is necessary to ensure the independence, loyalty and competency of the Board appointed to the new foundation. Emphatically, this foundation cannot be seen as a pot of money to be controlled by either elected or appointed officials, trade groups or other special interests; it must be directly responsive to real community health care needs, and conflicts of interests involving trustees and grantees must be avoided. See Annette Fuentes and Rosemary Metzler Lavan, "No Health, No Wealth," The Nation, (December 18, 2000) at pp. 11-18 (indicating that an examination of six foundations established as a result of healthcare conversions reveals a pattern of problems in how the boards operate and the grants they make). Toward this end, we applaud the mission of the new foundation that is adopted in the current legislation, but, unfortunately, view with skepticism the ability of the board, as currently appointed, to effectively implement that mission.

In conclusion, if this State is to learn anything from the experience surrounding the dissolution of HIP, it is the importance of an independent financial evaluation that is subject to public scrutiny and a thorough process of judicial review in which the public has sufficient information in which to participate. These elements, so lacking in the HIP/PHP sale and lease transaction, are also missing from the proposed legislation. We therefore urge you to take the time to consider our recommendations and follow more closely the principles found in New Jersey's Asset Protection Act, that were recently enacted with regard to the conversion of nonprofit hospitals, and which are necessary to ensure that BCBS of NJ's and the government's actions are fair, legally sound and in the public interest.

*Protection of the Charitable Assets of Blue Cross and Blue Shield of New Jersey
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Thank you for the opportunity to present PILC's views, and I welcome any questions that you may have.