

NATURE OF THE CASE

This appeal arises from a judicial review of an agency action under the Kansas Act for Judicial Review and Civil Enforcement of Agency Actions, K.S.A. 77-601 *et seq.* At issue is a Final Order by Insurance Commissioner Kathleen Sebelius disapproving a proposed conversion and acquisition of Blue Cross and Blue Shield of Kansas, Inc. (BCBSKS), which is the state's dominant health insurer, to Anthem Insurance Companies, Inc., an Indiana corporation, or its designated affiliate. The case focuses on what effect, if any, to give two factual determinations made by the Commissioner after a three-day evidentiary hearing.

The first is a finding that the proposed transaction will severely deplete BCBSKS's surplus and make it financially weaker. The second is that the acquisition will result in substantially higher premiums than will occur under current management. The district court concluded the Commissioner erroneously interpreted or applied K.S.A. 40-3304(d)(1)(C) and (E) when she found the proposal was unfair and unreasonable to policyholders, not in the public interest, and prejudicial to the insurance-buying public, which are the statutory standards. The district court ruled, as a matter of law, that so long as the newly-acquired company's surplus and premiums were within lawful limits, the Commissioner's findings cannot justify the transaction's denial.

The case was remanded for compliance with the court's order. Appeals followed from both sides. This court transferred the case from the Court of Appeals on the Commissioner's motion. For convenience, the district court's Memorandum Decision and Order, and the Commissioner's Final Order are attached pursuant to Rule 6.03 (2001 Kan. Ct. R. Annot. 37). Jurisdiction is pursuant to K.S.A. 20-3017.

ISSUE STATEMENT

The question on appeal is the interpretation to be given K.S.A. 40-3304(d)(1)(C) and (E), both of which are part of the Kansas Insurance Companies Holding Act, K.S.A. 40-3301 *et seq.* More specifically, the issue is whether the Commissioner must approve an acquisition she judges from the evidence to be unfair and unreasonable to policyholders, not in the public interest, and hazardous or prejudicial to the insurance-buying public, without an additional finding that the newly-acquired company will act illegally.

To put this issue in perspective, it is necessary to consider both K.S.A. 40-3304(d)(1)(C) and 40-3304(d)(1)(E), which state in pertinent part that the Commissioner must approve an acquisition unless she finds that:

(C). the plans or proposals which the acquiring party has to liquidate the insurer, sell its assets or consolidate or merge it with any person, or to make any other material change in its business or corporate structure or management, are unfair and unreasonable to policyholders of the insurer and not in the public interest; or

(E). the acquisition is likely to be hazardous or prejudicial to the insurance-buying public.

As more fully discussed below, the district court erred by concluding that this statutory language did not permit the Commissioner to contrast the differing surplus levels and premiums that are likely to occur both with – and without – the proposed acquisition, and then make conclusions based on that analysis after considering all the circumstances attendant to the company being acquired. In the district court’s view, surplus levels and premiums that remain within statutory requirements found elsewhere

in the insurance code, as a matter of law, are conclusively not “unfair and unreasonable to policyholders of the insurer and not in the public interest” under K.S.A. 40-3304(d)(1)(C), and not “hazardous or prejudicial to the insurance-buying public” under K.S.A. 40-3304(d)(1)(E). The Commissioner disagrees.

K.S.A. 40-3304 plainly requires the Commissioner to evaluate a proposed deal by investigating the company’s business both before, and after, the contemplated acquisition. The standards recited in K.S.A. 40-3304(d)(1) set the parameters for the Commissioner’s exercise of discretion based on evidence adduced during an administrative hearing called to decide whether any of the conditions set out in the statute exist and merit rejection of the proposed transaction. The Commissioner’s analysis is not simply about the acquired company’s compliance, or non-compliance, with the insurance code, as the district court’s opinion suggests. The district court should be reversed, and the case remanded back to the lower court for consideration of the remaining issues raised by Anthem and BCBSKS in this KJRA proceeding.

FACTUAL STATEMENT

More than 715,000 Kansas residents carry private health care coverage insured or administered by BCBSKS.¹ An additional 640,000 Kansans have their health care coverage administered by the company through their Medicare and Medicaid programs.² Without question, BCBSKS is the dominant health care insurer in our state.³ By acquiring

¹ ROA, Vol. I, p. 00177, Final Order, p. 3.

² *Id.*

³ *Id.*; ROA, Vol. I, p. 00187, Final Order, p. 13, ¶ 13.

BCBSKS, Anthem seeks to assume that status.

On May 30, 2001, BCBSKS and Anthem entered into an “Alliance Agreement” that contemplated, as a single transaction, both the conversion of BCBSKS from a mutual insurance company owned by its policyholders to a stock insurance company and the acquisition by Anthem (or its designated affiliate) of all BCBSKS common stock.⁴ On May 31, 2001, BCBSKS submitted a draft plan for its conversion to the Commissioner for preliminary examination and comment as permitted by K.S.A. 40-4002(b).⁵ The conversion contemplated depleting BCBSKS’s \$286 million surplus by \$131 million.⁶ On July 25, 2001, Anthem formally sought the Commissioner’s approval to acquire BCBSKS in accordance with K.S.A. 40-3304.⁷

The Insurance Commissioner’s authority in these matters derives from two different statutory schemes. The first is the state’s mutual insurer conversion statutes, found at K.S.A. 40-4001 *et seq.*, which govern the BCBSKS changeover to a stock insurance company. The second is the Kansas Insurance Companies Holding Act, found at K.S.A. 40-3301, *et seq.*, which governs the proposed transfer of control from BCBSKS to Anthem. This Act sets statutory standards the Commissioner must consider before approving a domestic insurer’s acquisition. K.S.A. 40-3304(d)(1). The court’s attention is directed to the Act because that is the statutory basis used to disapprove the acquisition.

⁴ ROA, Vol. I, p. 00188, Final Order, Findings of Fact, p. 14, ¶ 26.

⁵ ROA, Vol. I, p. 00186, Final Order, Findings of Fact, p. 12, ¶ 1.

⁶ ROA, Vol. I, p. 00188, Final Order, Findings of Fact, p. 14, ¶¶30, 31 and 32.

⁷ ROA, Vol. I, p. 00188, Final Order, Findings of Fact, p. 14, p. 27.

On August 21, 2001, the Commissioner issued a “Procedural and Scheduling Order” to govern further proceedings.⁸ This Order explained that the Commissioner had retained independent special counsel and independent advisors, and had appointed certain members of the Commissioner’s legal and technical staff to investigate, review, and comment on the proposed transaction.⁹ The statutes authorize the Commissioner to retain such experts to assist in the review of conversions and acquisitions. *See* K.S.A. 40-4013 and K.S.A. 40-3304(d)(3). This professional group was termed the “KID Testimonial Team,” and it served as an active participant in the proceedings.

The Commissioner also ordered the parties to circulate public notices and set a series of public comment meetings to occur before the final administrative hearing.¹⁰ She further determined she would personally preside at the hearing to receive testimony and evidence in accordance with the Kansas Administrative Procedure Act (KAPA), K.S.A. 77-501 *et seq.*¹¹ On October 23, 2001, the Commissioner authorized the Kansas Medical Society, Kansas Hospital Association, Kansas State Nurses Association, and the Kansas Association for the Medically Underserved to intervene in the proceedings.¹²

⁸ ROA, Vol. I, p. 00179, Final Order, p. 5; ROA Vol. I, pp. 00021-00035, Procedural and Scheduling Order, pp. 1-15.

⁹ *Id.*

¹⁰ ROA, Vol. I, pp. 00022-00025, Procedural and Scheduling Order, pp. 2-5.

¹¹ *Id.*

¹² ROA, Vol. I, p. 00181, Final Order, p. 7.

The public comment meetings convened at various locations across Kansas during the first two weeks in December of 2001.¹³ At these meetings, BCBSKS, Anthem, and the KID Testimonial Team made presentations, and then public comments were received.¹⁴ More than 1,200 Kansans attended, many of them choosing to voice their opinions, either in person or with written comments.¹⁵

Beginning January 7, 2002, the Commissioner presided over a three-day administrative hearing.¹⁶ In accordance with the timetable set out in the Procedural and Scheduling Order, the parties and intervenors submitted pre-filed written testimony and legal memoranda. At the hearing, the Commissioner received into evidence more than 70 exhibits and heard sworn testimony from 22 witnesses.¹⁷ The issue receiving the most attention was whether Anthem will raise premium rates in Kansas after the acquisition at a faster pace than BCBSKS will without the transaction.¹⁸ The KID Testimonial Team and the intervenors argued that rates will increase substantially more, while BCBSKS and Anthem took an opposing view. Both sides offered testimony and exhibits to support their positions.

¹³ ROA, Vol. I, p. 00182, Final Order, p. 8.

¹⁴ *Id.*

¹⁵ ROA, Vol. I p. 00182, Final Order, p. 8. In the Final Order, the Commissioner determined that the parties substantially addressed all issues raised during the public comment hearings and, therefore, she did not rely on these statements in reaching her decision. *Id.*

¹⁶ ROA, Vol. I, p. 00183, Final Order, p. 9.

¹⁷ ROA, Vol. I, pp. 00184-00186, Final Order, pp. 10-12.

¹⁸ ROA, Vol. I, p. 00212, Final Order, p. 38.

On January 11, 2002, BCBSKS held a special meeting for a designated group of its policyholders, who were the only one's eligible under the transaction's terms to approve the proposed conversion and acquisition.¹⁹ Of those 172,038 policyholders who were eligible, only 36.9% cast an affirmative vote.²⁰ A full 63.1% of these specially-designated policyholders either voted against the transaction or declined to vote.²¹ Those eligible to vote comprised only about one-fourth of BCBSKS's insureds.²² The affirmative votes, however, were legally sufficient to move the transaction through the required process, necessitating a ruling by the Commissioner. K.S.A. 40-4002(d).

On February 11, 2002, she issued a 45-page Final Order disapproving the proposed transaction based on the standards set out in K.S.A. 40-3304(d)(1)(C) and 40-3304(d)(1)(E). Specifically, the Commissioner found the contemplated transaction would be "unfair and unreasonable to policyholders and not in the public interest," pursuant to K.S.A. 40-3304(d)(1)(C).²³ She further concluded that "the acquisition is likely to be hazardous or prejudicial to the insurance-buying public" under K.S.A. 40-3304(d)(1)(E).²⁴ As noted by the district court,

¹⁹ ROA, Vol. II, p. 00552, Certificate of Voting Inspector Bob B. Ware, p. 1.

²⁰ ROA, Vol. II, p. 00552, Certificate of Voting Inspector Bob B. Ware, p. 1; ROA, Vol. VI, p. 01421, and ROA Vol. XII, pp. 02634-02702, Plan of Conversion, Ex. 1.

²¹ ROA, Vol. II, p. 00552, Certificate of Voting Inspector Bob B. Ware, p. 1.

²² ROA, Vol. II, p. 00552, Certificate of Voting Inspector Bob B. Ware, p. 1; ROA, Vol. VI, p. 01421, and ROA Vol. XII, pp. 02634-02702, Plan of Conversion, Ex. 1.

²³ ROA, Vol. I, p. 00218, Final Order, p. 44, Conclusion of Law, ¶ 7.

²⁴ ROA, Vol. I, p. 00218, Final Order, p. 44, Conclusions of Law, ¶¶ 7 and 8.

In reaching her decision, the record reflects that the Commissioner received extensive evidence in the case. Nothing in the record suggests that the Commissioner disregarded any evidence or entered her decision based upon information not presented at the public hearing.²⁵

The Commissioner found that Anthem's acquisition would have two effects implicating the statutory standards.²⁶ First, the Commissioner determined the transaction would severely deplete BCBSKS's surplus, which would make the post-acquisition entity financially weaker. Second, she concluded Anthem would raise premium rates at a substantially higher pace than would occur otherwise under BCBSKS's current management.²⁷

As to these points, the Commissioner said the KID Testimonial Team and intervenors carried the burden of proof.²⁸ The Commissioner then weighed the evidence adduced by both sides, and determined the KID Testimonial Team and intervenors satisfied their burden as to these claims under K.S.A. 40-3304(d)(1)(C) and (E).²⁹ She further concluded that K.S.A. 40-3304(d)(1) gave her authority to disapprove the transaction based on these findings.

Pertinent to this aspect of the KJRA proceedings, the Commissioner's Final Order rejected claims by Anthem and BCBSKS that the Act's statutory purpose is far more

²⁵ ROA, Vol. 52, p. 773, Memorandum Decision and Order, p. 11.

²⁶ ROA, Vol. I, p. 00211, Final Order, p. 37.

²⁷ *Id.*; ROA, Vol. I, p. 00191, Final Order, Findings of Fact, p. 17, ¶63.

²⁸ ROA, Vol. I, pp. 00196-00197, Final Order, pp. 22-23.

²⁹ *Id.*

limited than the interpretations she was giving it. They argued the statute is restricted to such things as protecting against nefarious or unlawful conduct. The Commissioner explained in the Final Order that:

The five criteria in 40-3304(d)(1) cover a broad array of potential pitfalls in a transaction of this sort: the general requirements of licensure for a domestic insurer; the financial condition of the acquiring party; any plans or proposals the acquiring party has, not merely those to deplete assets; the competence, experience, and integrity of the acquiring party; and, quite broadly, anything else that might be hazardous or prejudicial to the insurance-buying public. To be certain, the Legislature intended for the Commissioner to protect against undesirables seeking to deplete a domestic insurer's assets. But to restrict [the statute's] meaning to only that effect is a contortion of language and a stretch of reasoning that this Commissioner cannot adopt.³⁰

Against this backdrop, the Commissioner interpreted K.S.A. 40-3304(d)(1)(C), as follows:

The Commissioner shall approve the acquisition, unless Anthem's "plans or proposals... to make any other material changes in its business or corporate structure or management, are unfair and unreasonable to policyholders of the insurer and not in the public interest." K.S.A. 40-3304(d)(1)(C). When interpreting this provision, several items must be defined: "material," "unfair," and "unreasonable."

The "strict rule of statutory construction" requires that "ordinary words are to be given their ordinary meaning." *Director of Taxation v. Kansas Krude Oil Reclaiming Co.*, 236 Kan. 450, 455, 691 P.2d 1303 (1994). All of the terms at issue are ordinary words. "Material" is defined, as used in the statute, as "being both relevant and consequential." AMERICAN HERITAGE DICTIONARY OF THE

³⁰ ROA, Vol. I, p. 00217, Final Order, p. 43.

ENGLISH LANGUAGE (3rd Ed. 1996). “Unfair” is defined as “not just or evenhanded.” *Id.* “Unreasonable” is defined, as used in the statute as “exceeding reasonable limits; immoderate.” Thus, the Commissioner may disapprove the sponsored demutualization upon a finding that Anthem plans to make consequential changes to BCBSKS’s management or structure that are not just and are immoderate and not in the public interest.³¹

As to K.S.A. 40-3304(d)(1)(E), the Commissioner noted the three key words in interpreting this statute were “likely,” “hazardous,” and “prejudicial.”³² The Commissioner then stated:

“Likely,” “hazardous,” and “prejudicial” are terms in common usage and have ordinary meanings. “Likely” is defined as “possessing or displaying the characteristics or qualities that make something probable.” AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE (3rd Ed. 1996). “Hazardous” is defined as “marked by danger; perilous.” *Id.* “Prejudicial” is defined as “detrimental; injurious.” *Id.* Applying the “strict rule of construction,” the Commissioner may disapprove the acquisition upon a finding that it is probable that the insurance-buying public will be in danger or may be injured by the acquisition. The nature of this danger or injury does not matter under the plain, unambiguous language of the statute.³³

The Commissioner then determined that issues as fundamental to the insurance-buying public as their ability to buy health insurance at an affordable and competitive cost or their health insurer’s financial stability were well within the limits of the natural and ordinary meaning of the statutory language in K.S.A. 40-3304(d)(1)(C) and (E). As the

³¹ ROA, Vol. I, p. 00214, Final Order, p. 40.

³² ROA, Vol. I, p. 00215, Final Order, p. 41.

³³ ROA, Vol. I, p. 00217, Final Order, p. 43.

Commissioner stated in her Final Order,

Given the explicit statement of legislative intent and public policy in 40-3301, one would assume that if the Legislature intended to restrict the effect of this statute, it would have done so explicitly, either in 40-3301 or 40-3304.³⁴

By reaching the decision to deny the transaction, the Commissioner did not address her authority to approve the deal with conditions, which were suggested by the KID testimonial team as an alternative remedy, if the Commissioner did not simply disapprove the proposal.³⁵ Similarly, the Commissioner did not address any other conditions that she might deem appropriate under the circumstances, if she were to approve the transaction.

Anthem and BCBSKS each filed separate KJRA appeals, which were consolidated into a single case. They attacked the Final Order on six of the eight statutory grounds for challenging an administrative action under the KJRA. The case was fully submitted on briefs to the district court on May 28, 2002. Ten days later, the court issued its Memorandum Decision and Order invalidating the Commissioner's order solely on the basis of K.S.A. 77-621(c)(4).

The court's opinion began with a recitation of what the district court saw as the "Historical Background" to the acquisition. This was based, in part, on "facts" the court "judicially noticed" from an earlier 1997 lawsuit involving BCBSKS.³⁶ In doing so, the

³⁴ ROA, Vol. I, p. 00216, Final Order, p. 42.

³⁵ ROA, Vol. VI, p. 01425, Testimonial Team's Post-Hearing Brief, Proposed Findings of Fact and Conclusions of Law, p. 29, citing ROA Vol. VI, pp. 01202-01204, Testimonial Team's Pre-filed Brief, pp. 36-38.

³⁶ ROA, Vol. 52, pp.764-767, Memorandum Decision and Order, dated June 7, 2002, pp. 2-5.

district court departed from the findings stated in the Commissioner’s Final Order, and stated its own conclusions.³⁷

The district court stated its impression that BCBSKS’s insureds had enjoyed “expanded coverage at bargain prices.”³⁸ The court further concluded that without an acquisition with another entity, BCBSKS stood at the precipice of financial failure “with the attendant chaos that would be caused to both insureds and health care providers.”³⁹ The court also observed that BCBSKS management faced “a stark ‘Hobson’s’ choice” between raising premiums “to a level which will not be competitive in the market place” or merger with a larger health insurance entity.⁴⁰ Finally, the district court concluded that it was not possible for BCBSKS to continue “indefinitely into the future as a ‘stand alone’ entity.”⁴¹

From this premise, the district court then determined the reasons expressed by the Commissioner in support of her disapproval of the acquisition were not “legally sound” as a matter of law. Succinctly stated, the district court’s judgment was that:

Although the Commissioner is granted power to supervise insurers and to enforce the Kansas Insurance Code (K.S.A. 40-103), she is not authorized to add or change established legal requirements or take regulatory action based upon anticipated premium rates or levels of surplus that would be

³⁷ It should also be noted the district court incorrectly stated that it was Anthem that filed the application of conversion with the Commissioner to transform BCBSKS to a stock company. ROA, Vol. 52, p. 767, Memorandum Decision and Order, dated June 7, 2002, p. 5.

³⁸ ROA, Vol. 52, p. 765, Memorandum Decision and Order, dated June 7, 2002, p. 3.

³⁹ ROA, Vol. 52, p. 767, Memorandum Decision and Order, dated June 7, 2002, p. 5.

⁴⁰ ROA, Vol. 52, p. 766, Memorandum Decision and Order, dated June 7, 2002, p. 4.

⁴¹ ROA, Vol. 52, p. 768, Memorandum Decision and Order, dated June 7, 2002, p. 6.

either required by or consistent with the law under the
aforementioned statutory guidelines and case precedents.
[citations omitted].⁴²

The district court did not decide the other challenges made to the Final Order by Anthem and BCBSKS, including their claims that K.S.A. 40-3304(d)(1) is an unconstitutional delegation of a legislative function under Kan. Const. Art. 2, §1, or that the Final Order was not supported by substantial evidence.⁴³ The district court remanded the matter to the Commissioner with instructions “to proceed as she sees fit, consistent with this opinion and other provisions of the law which are or may become applicable.”⁴⁴

In doing so, the district court also recited a number of issues recently raised in local and national newspapers regarding the transaction.⁴⁵ The court then suggested that while those issues were not before it now, they might properly be investigated on remand within the Act’s statutory parameters.

Finally, the court revealed for the first time that it had considered voluntary recusal from the case based on highly-favorable, personal experiences with BCBSKS during “a near-fatal illness,” but had not mentioned this to the parties earlier. The court said it ultimately determined that “under the doctrine of necessity” it would decide the case.⁴⁶ This appeal ensued.

⁴² ROA, Vol. 52, p. 776, Memorandum Decision and Order, dated June 7, 2002, p. 14.

⁴³ ROA, Vol. 52, p. 779, Memorandum Decision and Order, dated June 7, 2002, p. 17.

⁴⁴ ROA, Vol. 52, pp. 779-780, Memorandum Decision and Order, dated June 7, 2002, pp. 17-18.

⁴⁵ ROA, Vol. 52, pp. 776-779, Memorandum Decision and Order, dated June 7, 2002, pp. 14-17.

⁴⁶ ROA, Vol. 52, p. 780, Memorandum Decision and Order, dated June 7, 2002, p. 18.

ARGUMENT AND AUTHORITIES

Standard of Review

The only issue involves the interpretation of statutes. This presents a question of law. As such, this court's review is unlimited. *Hartford Casualty Insurance Company v. Credit Union 1 of Kansas*, 268 Kan. 121, 124, 992 P.2d 800 (1999).

The fundamental rule when interpreting a statute is that the legislature's intent governs, where that intent can be ascertained. *Legislative Coordinating Council v. Stanley*, 264 Kan. 875, 879, 953 P.2d 1027 (1998). In determining legislative intent, the court may look to the purpose to be accomplished and the statute's necessity and effect. *State ex rel. Stephan v. Kansas Racing Comm'n*, 246 Kan. 708, 719, 792 P.2d 971 (1990). Legislative intent is also to be determined by a general consideration of the entire act. *ERC v. Sebelius*, 271 Kan. 253, 260, 21 P.3d 505 (2001). If, on its face, the statute leaves its construction uncertain, the court is not limited to merely considering the language used, but may look to its historical background, the circumstances attending its passage, the purpose to be accomplished, and the effect the statute may have under the various constructions suggested. *Hartford Casualty Insurance Company*, 268 Kan. at 125.

Special rules apply, however, when considering whether an administrative agency "erroneously interpreted or applied the law" under the KJRA. *In re Appeal of Harbour Brothers Construction Co., Inc.*, 256 Kan. 216, 221, 883 P.2d 1194 (1994). The court gives judicial deference under the doctrine of operative construction to a statute's interpretation by the administrative agency responsible for its enforcement. *Matjasich v. State of Kansas*, 271 Kan. 246, 250, 21 P.3d 985 (2001). This deference is particularly

appropriate when the agency is one of special competence and experience, such as the Insurance Commissioner. *Id.*, citing *In re Appeal of United Teleservices, Inc.*, 267 Kan. 570, 572, 983 P.2d 250 (1999); *Guardian Title Co. v. Bell*, 248 Kan. 146, 154, 805 P.2d 33 (1991) (“Here, we are dealing with the insurance commissioner, an expert in the regulation of the insurance industry, with a large staff and paid consultants available.”). As this court recently stated, “Usually, the legal interpretation of a statute by an administrative agency that is charged by the legislature with the authority to enforce the statute is entitled to great judicial deference.” *Mitchell v. Liberty Mutual Insurance Company*, 271 Kan. 684, Syl. ¶ 4, 24 P.3d 711 (2001).

These long-standing principles support the Commissioner’s analysis in this case, as does the Act’s legislative history, as explained below.

**The District Court Incorrectly Interpreted
K.S.A. 40-3304(d)(1)(C) and (E)**

In the district court’s view, surplus levels and premiums that remain within statutory requirements found elsewhere in the insurance code, as a matter of law, are conclusively not “unfair and unreasonable to policyholders of the insurer and not in the public interest” under K.S.A. 40-3304(d)(1)(C), and not “hazardous or prejudicial to the insurance-buying public” under K.S.A. 40-3304(d)(1)(E). If upheld, this interpretation would rob the Commissioner of the discretion the legislature intended her to have in the regulation of insurance company acquisitions.

Indeed, the fact that lawmakers established in another context other statutory devices for analyzing and setting such matters as premium rates or minimum surplus

levels only underscores the importance these subjects have to the insurance-buying public and the public interest in general. It does not serve policyholders or the public to declare these subjects off-limits for the Commissioner's consideration when a non-domestic insurer seeks to acquire a Kansas insurer. This is particularly true under the broad language used in K.S.A. 40-3304(d)(1)(C) and (E).

The insurance code comprises 49 separate articles contained in the Kansas Statutes Annotated at Chapter 40. Each licensed insurer is subject to a variety of these articles, but no insurer is subject to them all. The code is expansive in scope and deals with many industry-related factors under different statutory articles depending on the circumstances in which a particular subject matter is to be considered. The district court's opinion creates iron curtains between the various articles of this complex and interwoven insurance code. There is no reason to believe the legislature intended for the subject matters of premium rates or surplus levels to be within the conclusive purview of just one statutory scheme to the exclusion of all others.

For example, one of the articles with the broadest applicability is article 24, which concerns the regulation of certain trade practices. *See* K.S.A. 40-2401 *et seq.* It belies logic to contemplate a scenario in which the Commissioner could never consider unfair trade practices when analyzing the factors set forth in K.S.A. 40-3304(d)(1) just because those same activities fall within the realm of article 24. If so, K.S.A. 40-3304(d)(1) does not mean what it plainly states.

The fallacy of the district court's logic is illustrated by the testimony of BCBSKS's Donald R. Lynn, Vice President of Finance, who testified that the surplus

depletions required by the conversion and acquisition would be “inappropriate” from a proper business perspective for an independent insurance company. He stated as follows:

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- 9 Q. If we assume for a moment, Mr.
10 Lynn, that you don't have an agreement with
11 Anthem, that you're just out there on your
12 own, would you distribute \$131,000,000 of
13 your surplus?
14 A. Absolutely not.
15 Q. If that amount of surplus that you
16 left behind, that's not enough to make you
17 feel good about this company, is it?
18 A. Not -- not with the type of
19 expenditures that we see coming up in our
20 future.
21 Q. And what makes the difference and
22 the reason you can sit here in good
23 conscience and recommend this deal is your
24 reliance on Anthem. Isn't that correct?
25 A. That's correct.⁴⁷

From this testimony, it is reasonable to conclude the surplus reduction contemplated would be inappropriate from a business perspective – regardless of its legality. In the face of such testimony, the Commissioner would be derelict if she didn't scrutinize BCBSKS's post-acquisition financial strength, especially when the issue is being raised by parties to the proceedings.

But under the district court's analysis, even this admittedly inappropriate surplus level could not be an area of inquiry for the Commissioner because it is statutorily permissible elsewhere in the insurance code. When the facts of a case undisputedly show that there will be less money behind the newly-acquired company to provide financial

⁴⁷ ROA, Vol. XVI, p. 04497, Lynn Testimony, Hearing Transcript, p. 337

support for the insurer's risks than there would be without the acquisition, K.S.A. 40-3304(d)(1) may be reasonably read to permit the Commissioner to probe this circumstance and make conclusions based on it, which is what she did in this case.

What the district court did not do was view the Kansas Holding Companies Act within its own context, i.e., the transfer of control of a domestic insurer. In other circumstances, such as rate setting, different statutory schemes and standards are established. Put simply, something may be legal in one context, but still inappropriate in another, based on the circumstances being reviewed. Reading some sort of subject matter exclusivity into the Kansas insurance code is unjustified. The extension of this principle would cripple the Commissioner's ability to perform the duties of "general supervision, control, and regulation of insurers" that are vested in the Insurance Commissioner's office. *Mitchell v. Liberty Mut. Ins. Co.*, 271 Kan. 684, 700, 24 P.3d 711 (2001). There is no legal authority interpreting the insurance code as the district court suggests.

Similarly, in its haste to decide this case as a matter of law, the district court misconstrued the Commissioner's Final Order regarding future premium rate increases. First, the district court determined that the Commissioner's concern over rate increases was simply that, "[T]wo classes of Kansas policyholders would pay higher premiums sooner (perhaps as much as two years) under Anthem."⁴⁸ But the Commissioner's finding was not just that the rates would increase sooner, it was that those premiums would be

⁴⁸ ROA, Vol. 52, p. 774, Memorandum Decision and Order, dated June 7, 2002, p. 12.

significantly higher under Anthem than they would under BCBSKS.⁴⁹ The Commissioner found that Kansans would be paying more for the same level of insurance protection under Anthem's management. She then considered how this obvious fact weighed against the statutory considerations set out in K.S.A. 40-3304(d)(1). The Commissioner's analysis was not as trivial as it was portrayed by the district court.

But even assuming this were a situation in which the rates would increase two year's earlier than they would otherwise, it is not the business of the courts to re-weigh the evidence before the Commissioner, and then determine that this would be inconsequential to policyholders, the public interest, or the insurance-buying public. What is at issue in this case is the acquisition of the state's dominant health insurer. K.S.A. 40-3304(d)(1) leaves it to the Commissioner to decide whether two year's worth of premium increases would make a significant difference, especially when so many Kansans will be impacted by this increase. It is not for the district court to decide this is not meaningful. The Act imposes this responsibility squarely with our Commissioner of Insurance.

Second, the district court misinterpreted the Final Order as requiring cross-subsidization of rates, and then declared this to be illegal, citing *Blue Cross & Blue Shield v. Bell*, 227 Kan. 426, 607 P.2d 498 (1980). But the Commissioner's decision only noted that it was a common and accepted insurance company practice to use surplus, and income derived from invested surplus, to maintain or reduce premiums. In *Bell*, the Commissioner insisted that other classifications be allocated a part of the claim and

⁴⁹ ROA, Vol. I, p. 00211, Final Order, p. 37; ROA, Vol. I, p. 00191, Final Order, Findings of Fact, p. 17, ¶63.

operating expense experience of Plan 65, so as to subsidize the costs of that plan at the expense of other groups. 227 Kan. at 438. *Bell* does not make it illegal for an insurance company to use its surplus, or its income earned from surplus, to maintain or reduce premiums. Indeed, the evidence here showed that BCBSKS accumulated its surplus in order to allow it to operate without maximizing its underwriting gains.⁵⁰ As to these points, the district court also was in error, which in turn led to a ruling that was erroneous.

Finally, the district court declared it was inappropriate for the Commissioner to concern herself with surplus levels and premium rates in the context of a domestic insurer's acquisition because the Commissioner has the ability to regulate those concerns under other Kansas statutes.⁵¹ But this misses the point as to whether the Commissioner is authorized under the Act to consider these concerns prior to a change in control. The statute's plain language indicates that it is the Commissioner's decision whether to rely on post-acquisition controls to address problematic scenarios.

To be sure, the availability of a post-acquisition regulatory device may be relevant to whether a transaction should be disapproved, but the district court has made this availability conclusive. K.S.A. 40-3304(d)(1) is not so limited. It is up to the Commissioner – not the district court – to weigh what regulatory tools are available to control an issue. These options may include disapproval, approval with conditions, or approval with a recognition that post-acquisition controls are available. The district court erred in its rationalization of these statutes.

⁵⁰ ROA, Vol. I, p. 00213, Final Order, p. 39.

⁵¹ ROA, Vol. 52, p. 776, Memorandum Decision and Order, dated June 7, 2002, p. 14.

**Commissioner Sebelius Correctly Interpreted
K.S.A. 40-3304(d)(1)(C) and (E)**

A plain reading of K.S.A. 40-3304(d)(1) shows the Commissioner correctly determined that the Act requires her to consider the acquisition's effects on Kansas policyholders and the insurance-buying public, and to determine whether these effects create certain unacceptable conditions, which are enumerated in the statutory standards.⁵² If any enumerated condition exists, she has the discretion to disapprove the acquisition. K.S.A. 40-3304(d)(1).

When interpreting K.S.A. 40-3304(d)(1), and determining its legislative intent, it is important to construe the entire Act, *in para materia*, with the aim to reconcile its provisions into workable harmony if possible. *In the Matter of the Due Process Hearing of Margarete McReynolds*, No. 87,337, 2002 Lexis 135, at *13 (Kan. April 19, 2002), citing *State v. Bolin*, 266 Kan. 18, 968 P.2d 1104 (1998). Toward that end, particular consideration should be given to K.S.A. 40-3301(a), (b) and (c), which set forth public policy considerations when foreign insurers such as Anthem seek to acquire a domestic insurance company. K.S.A. 40-3301(a) states:

(a) It is hereby found and declared that it may not be inconsistent with the public interest and the interest of policyholders to permit insurers to:

(1) Engage in activities which would enable them to make better use of management skills and facilities;

(2) Diversify into new lines of business through acquisition or organization

⁵² ROA, Vol. I, p. 00211, Final Order, p. 37.

subsidiaries;

(3) Have free access to capital markets which could provide funds for insurers to use in diversification programs;

(4) Implement sound tax planning conclusions; and

(5) Serve the changing needs of the public and adapt to changing conditions of the social, economic and political environment, so that insurers are able to compete effectively and to meet the growing public demand for institutions capable of providing a comprehensive range of financial services.

While in K.S.A. 40-3301(a) the legislature indicated factors that “may not be inconsistent” with the public interest, the Commissioner found that “a careful reading of the statute indicates that these are factors the Commissioner may consider in making her determination, but are not unequivocal public policy statements.”⁵³ The provision’s plain language supports the Commissioner’s interpretation.

The Act also expressly sets out in K.S.A. 40-3301(b) factors that are not in the public interest. It states:

(b) It is further found and declared that the public interest and the interests of the policyholders are or may be adversely affected when:

(1) Control of an insurer is sought by persons who would utilize such control adversely to the interests of policyholders;

(2) acquisition of control of an insurer would substantially lessen competition or create a

⁵³ ROA, Vol. I, p. 00194, Final Order, p. 20.

monopoly in the insurance business of the state;

(3) an insurer which is part of a holding company system is caused to enter into transactions or relationships with affiliated companies on terms which are not fair or reasonable; or

(4) an insurer pays dividends which jeopardize the financial condition of such insurer.

As to this language, the Commissioner noted that, “[W]hile the statutory language in this section is stronger, the Legislature again left the ultimate determination of the public interest to the Commissioner’s discretion.”⁵⁴ The provision’s language supports this interpretation.

Finally, K.S.A. 40-3301(c) recites public policy declarations to be promoted by the Act. It states:

(c) It is hereby declared that the policies and purposes of this act are to promote the public interest by:

(1) Facilitating the achievement of the objectives enumerated in subsection (a) of this section;

(2) requiring disclosure of pertinent information relating to changes in control of an insurer;

(3) requiring disclosure by an insurer of material transactions and relationships between the insurer and its affiliates, including certain dividends paid by the insurer; and

⁵⁴ ROA, Vol. I, p. 00195, Final Order, p. 21.

(4) providing standards governing material transactions between the insurer and its affiliates.

The Commissioner found these public policy declarations to be “unequivocal,” and said that they indicated “the types of disclosures required by foreign insurance companies and the types of evidence that the Commissioner should take into consideration when making her determination.”⁵⁵ This statute’s plain language supports these conclusions.

The Commissioner’s determination that it is legally relevant to consider whether the acquisition will likely result in a greatly depleted surplus for BCBSKS or produce significantly higher premium rates falls squarely within the boundaries set by K.S.A. 40-3304(d)(1)(C). When the KID Testimonial Team and the intervenors raised these concerns, the Commissioner was obligated to consider them and determine whether they provided a basis to disapprove the acquisition. To do otherwise ignores the statute’s plain language.

Petitioners argued to the Commissioner that the application of K.S.A. 40-3304(d)(1)(C) is limited to such things as organizational form or leadership, and cannot be used to consider prospects for depleted surplus levels or increases in premium rates. But this interpretation ignores the statute’s plain language and fails to give K.S.A. 40-3304(d)(1)(C) the ordinary meaning that is derived from its terms. These statutory provisions clearly address substantial financial matters such as plans “to liquidate the

⁵⁵ ROA, Vol. I, p. 00195, Final Order, p. 21.

insurer, sell its assets...or merge it...or to make any other material change...” K.S.A. 40-3304(d)(1)(C).

Here, Anthem is proposing to takeover and control BCBSKS through an acquisition. This acquisition would instantly make Anthem the dominant health insurer in Kansas because BCBSKS would become its wholly-owned subsidiary. This transaction necessarily means there would be material changes in those ultimately responsible for the company’s operations, *i.e.* “management.” Similarly, it is apparent that this transfer of control would result in changes to the acquired business’s organization and financial positions. These factors also implicate K.S.A. 40-3304(d)(1)(C).

Finally, the depletion of BCBSKS’s surplus is certainly a substantial transfer of a significant asset. So, regardless of whether one considers plans to reduce BCBSKS’s surplus or raise its premiums to be a change in the company’s business, a depletion of current assets, or a consequential result from a change in its management, the statute requires the Commissioner to consider if such plans are material and whether they are unfair and unreasonable to policyholders and not in the public interest.

Again, the language in K.S.A. 40-3304(d)(1)(E) encompasses the issues raised by the KID Testimonial Team and intervenors, who presented evidence regarding their fear that the acquisition would weaken the financial standing of the state’s dominant health insurer and place a substantial financial burden on the insurance-buying public. Indeed, it is difficult to imagine issues more fundamental to the insurance-buying public than their ability to buy health insurance at an affordable and competitive cost or their health insurer’s financial stability.

The consideration of these issues was well within the limits of the natural and ordinary meaning of the phrase “hazardous or prejudicial to the insurance-buying public.” The Commissioner’s analysis of this statute has a rational basis and is entitled to deference. *National Council on Compensation Ins. v. Todd*, 258 Kan. 535, 539, 905 P.2d 114 (1995). The Commissioner did not err in her interpretation of this statute.

K.S.A. 40-3304 obviously requires the Commissioner to evaluate the proposed acquisition in the context of the company’s business and operation without the proposed acquisition. The comparison, then, is between the company before acquisition and after, not between compliance with other statutes and non-compliance. If it is determined that the acquisition’s effect would be “hazardous or prejudicial to the insurance-buying public,” for example, its rejection is authorized, even though the company might still comply with minimum capital and premium rate statutes. Were this not the case, the legislature would only have had to require the company “comply with applicable laws” after acquisition, and need not have promulgated the standards recited in K.S.A. 40-3304(d)(1), which in turn set the parameters for the Commissioner’s discretion. The Commissioner’s interpretation is supported by the Act’s plain language.

Legislative History Supports the Commissioner’s Interpretation

The Commissioner’s interpretation also is consistent with the Act’s legislative history. The Act, which was first enacted in 1974, was patterned after a model bill developed by the National Association of Insurance Commissioners (NAIC) concerning

the acquisition of certain insurance companies.⁵⁶ In presenting the legislation to the Senate Commercial and Financial Institutions Committee in 1974, the Kansas Insurance Department explained that the bill “would strengthen the department’s ability to safeguard the interests of the public.”⁵⁷ The provisions of what is now K.S.A. 40-3304(d)(1)(C) were enacted in 1974 when the Act was first adopted, and has remained unchanged since that date.

But the Act itself has been revised on multiple occasions.⁵⁸ These changes in large part were to ensure the Act conformed to NAIC standards, as the model act was also revised. The state’s interest in conforming to the NAIC model act has been, in large part, to preserve Kansas’ accreditation with that association.⁵⁹ The language that is now K.S.A. 40-3304(d)(1)(E) was enacted in 1992 for this same reason, and remains unchanged to this day.⁶⁰

When this provision was considered by the 1992 legislature, the Kansas Insurance Department explained to lawmakers that it “[a]dds consideration of whether an acquisition of a domestic insurer is likely to be hazardous or prejudicial to the insuring

⁵⁶ See L. 1974, ch. 183, §4; and ROA, Vol. 36, p. 330, Minutes of the Senate Commercial and Financial Institutions Committee on February 5, 1974, regarding 1974 Senate Bill 929.

⁵⁷ See ROA, Vol. 36, p. 330, Minutes of the Senate Commercial and Financial Institutions Committee on February 5, 1974, regarding 1974 Senate Bill 929.

⁵⁸ See L. 1976, ch. 217, §2; L. 1983, ch. 159, §1; L. 1988, ch. 356, §119; L. 1990, ch. 173, §3; L. 1990, ch. 159; L. 1991, ch. 138, §§1 and 2; L. 1992, ch. 288, §2; L. 1997, ch. 166, §3.

⁵⁹ See, for example, ROA, Vol. 36, p. 330, then-Insurance Commissioner Ron Todd’s 1991 testimony to the Senate Committee on Financial Institutions and Insurance, regarding 1991 SB 67 in the Minutes of the Senate Committee on Financial Institutions and Insurance, February 13, 1991.

⁶⁰ See L. 1992, ch. 288, §2.

public as a reason the Commissioner may disapprove the transaction.”⁶¹ No other limitations or qualifications were explained or promised during the legislature’s deliberations.

The present language in K.S.A. 40-3304(d)(1)(E) was developed earlier as part of revisions to the model act promulgated by the NAIC. In its published “Legislative History,” the NAIC explained that this provision was added to the model act “to show the commissioner could consider the [acquisition’s] effect on the insurance-buying public.”⁶² Again, no other limitations or qualifications were explained or promised.

In this case, the Commissioner understood that she must consider each standard set out in K.S.A. 40-3304(d)(1) in passing on the proposed BCBSKS acquisition by Anthem. This is what the legislature obviously intended. Her interpretations of K.S.A. 40-3304(d)(1)(C) and (E) are rationally based in the statute’s plain language, the intent and purposes stated in the Act, and the legislative history in which it is repeatedly explained that the Act’s “original and continuing purpose...is to protect the interests of policyholders.”⁶³ The Commissioner did not err in her interpretation of this Act.

⁶¹ See ROA, Vol. 36, p. 330, Testimony by Dick Brock, Kansas Insurance Department, before the House Committee on Insurance, regarding 1992 HB 2787; and identical testimony given to the Senate Committee on Financial Institutions and Insurance, regarding 1992 HB 2787.

⁶² See ROA, Vol. 36, p. 330, NAIC Model Regulation Service, January 1998, Insurance Holding Company System Regulatory Act, Legislative History, pp. 440-38-440-39.

⁶³ See ROA, Vol. 36, p. 330, then-Insurance Commissioner Ron Todd’s 1991 testimony to the Senate Committee on Financial Institutions and Insurance, regarding 1991 SB 67 in the Minutes of the Senate Committee on Financial Institutions and Insurance, February 13, 1991; Testimony by Dick Brock, Kansas Insurance Department, before the House Insurance Committee, regarding 1991 SB 67, March 25, 1991; See, also, testimony by Dick Brock, Kansas Insurance Department, before the House Committee on Insurance, regarding 1992 HB 2787.

CONCLUSION

This Act is designed to ensure that the Commissioner gives serious consideration to issues that the legislature has deemed to be fundamental to policyholders and the insurance-buying public when faced with a proposed acquisition. It requires evidentiary hearings, allows for the Commissioner's retention of outside experts, and mandates criteria for the Commissioner's review and exercise of her discretion. The district court's interpretation of this Act severely limits the Commissioner's authority, and reduces the legislative criteria to nothing more than a determination as to whether the newly-acquired company will comply with existing law. Contrary to the district court's reasoning, the Act does not require the Commissioner to approve an acquisition she judges from the evidence to be unfair and unreasonable to policyholders, not in the public interest, and hazardous or prejudicial to the insurance-buying public.

GATES, BILES, SHIELDS & RYAN, P.A.

By: _____
DAN BILES, No. 09711
10990 Quivira Road, Suite 200
Overland Park, Kansas 66210
(913) 661-0222; 913-491-6398/Fax

and

BRENT GETTY
Kansas Supreme Court No. 17747
Attorney at Law
Kansas Insurance Department
420 SW 9th Street
Topeka, Kansas 66661-1678
(785) 368-7164; (785) 296-2283/Fax
Attorneys for Kathleen Sebelius

CERTIFICATE OF SERVICE

A true and correct copy of the foregoing on August 19, 2002, was sent, via first-class mail, in accordance with Kansas Supreme Court rules, to the counsel of parties:

Gary D. McCallister, Esq.
Gary D. McCallister & Associates, Ltd.
29 S. La Salle Street, Suite 1210
Chicago, Illinois 60603
Attorneys for Blue Cross and Blue Shield
of Kansas, Inc.

Eric Unrein
Davis, Unrein, McCallister, Biggs &
Head, LLP
100 SE 9th Street, 3rd Floor
Topeka, KS 66601
Attorneys for Blue Cross and Blue Shield of
Kansas, Inc.

Sidney A. Shapiro
1647 Indiana
Lawrence, KS 66044
Attorneys for Blue Cross and Blue Shield
of Kansas, Inc.

William H. Pitsenberger, Esq
Blue Cross and Blue Shield of Kansas, Inc.
1133 SW Topeka Boulevard
Topeka, Kansas 66629-0001
Vice-President and General Counsel for
Blue Cross and Blue Shield of Kansas, Inc.

James C. Scoville, Esq.
Debevoise & Plimpton
919 Third Avenue
New York, New York 10022
Attorneys for Blue Cross and Blue Shield
of Kansas, Inc.

Doug Fauth, Esq.
Anthem Blue Cross and Blue Shield
120 Monument Circle
Indianapolis, Indiana 46204-4903
Attorney for Anthem Blue Cross and Blue
Shield

Randy J. Forbes, Esq.
Frieden, Haynes & Forbes
555 South Kansas Avenue, Suite 303
P.O. Box 639
Topeka, Kansas 66601-0639
Attorneys for Anthem Blue Cross and Blue
Shield

Douglas Laird, Esq.
Polsinelli, Shalton & White, PC
700 West 47th Street, Suite 1000
Kansas City, MO 64112-1802
Attorneys for Kansas Medical Society

Charles R. Hay, Esq.
Goodell, Stratton, Edmonds & Palmer, LLP
515 South Kansas Avenue
Topeka, Kansas 66603-3999
Attorneys for Kansas Hospital Association

Karen A. Eager, Esq.
SHAMBERG, JOHNSON & BERGMAN
2600 Grand Avenue, Suite 550
Kansas City, Mo 64108
Attorneys for Kansas State Nurses Association
& Kansas Association of the Medically
Underserved

DAN BILES