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Volume 1

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STATE OF NEW HAMPSHIRE
DEPARTMENT OF STATE BUREAU OF SECURITIES REGULATIONS

No. C-2011000036

In the Matter of:

Local Government Center, Inc., et al.

BEFORE DONALD E. MITCHELL, ESQUIRE
PRESIDING OFFICER

* * * * *

REPORT OF PROCEEDINGS

April 30, 2012

9:46 a.m.

* * * * *

New Hampshire State Archives and Genealogical
Public Research Room
71 South Fruit Street
Concord, New Hampshire 03301

Court Reporter: Kimberly A. Smith, CSR, CRR, RDR

1 APPEARANCES:

2 BERNSTEIN, SHUR, SAWYER & NELSON, P.A.
3 By: Andru H. Volinsky, Esq.
4 and Roy W. Tilsley, Jr., Esq.
5 and Christopher G. Aslin, Esq.
6 670 North Commercial Street, Suite 108
7 Post Office Box 1120
8 Manchester, NH 03105-1120
9 (603) 623-8700
10 avolinsky@bernsteinshur.com
11 rtilsley@bernsteinshur.com
12 caslin@bernsteinshur.com

13 and

14 NH Bureau of Securities Regulation
15 By: Earle F. Wingate, III, Esq.
16 and Adrian LaRoche, Esq.
17 and Eric Forcier, Esq.
18 State House Room 204
19 107 North Main Street
20 Concord, NH 03301-4989
21 (603) 271-1463
22 earle.wingate@sos.nh.gov
23 adrian.larochelle@sos.nh.gov
eric.forcier@sos.nh.gov

for the Petitioner, Bureau of
Securities Regulation;

17 PRETI, FLAHERTY, BELIVEAU & PACHIOS, Chtd., LLP
18 By: William C. Saturley, Esq.
19 and Brian M. Quirk, Esq.
20 57 North Main Street
21 Post Office Box 1318
22 Concord, NH 03302-1318
23 (603) 410-1500
wsaturley@preti.com
bquirk@preti.com

and

1 APPEARANCES: (continued)

2 RAMSDELL LAW FIRM, PLLC
3 By: Michael D. Ramsdell, Esq.
4 69 Bay Street
5 Manchester, NH 03104
6 (603) 606-1766
7 mramsdell@ramsdelllawfirm.com

8 and

9 LOCAL GOVERNMENT CENTER
10 By: David Frydman, Esq.
11 25 Triangle Park Drive
12 Post Office Box 617
13 Concord, NH 03302-0617
14 (603) 224-7447
15 dfrydman@nhlgc.org

16 for the corporate and LLC respondents;

17 SHAHEEN & GORDON, P.A.
18 By: Steven M. Gordon, Esq.
19 and Benjamin Siracusa Hillman, Esq.
20 107 Storrs Street
21 Post Office Box 2703
22 Concord, NH 03302
23 (603) 225-7262
sgordon@shaheengordon.com
bsiracusahillman@shaheengordon.com

for the Respondent Maura Carroll;

HOWARD & RUOFF, PLLC
By: Mark E. Howard, Esq.
and Kimberly Myers, Esq.
1850 Elm Street, Suite 6
Manchester, NH 03104
(603) 625-1254
mhoward@howardruoff.com
kmyers@howardruoff.com

for the Respondent Peter J. Curro.

I N D E X

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(Whereupon the following proceedings were held in the presence of the Presiding Officer, counsel, the parties, and the public:)

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THE PRESIDING OFFICER: My name is Donald Mitchell and I'm the hearing officer in this matter. This matter is docketed as Local Government Center -- In The Matter of Local Government Center, Inc.; Local Government Center Real Estate, Inc. -- that's incorporated; Local Government Center HealthTrust, a limited liability company; Local Government Center Property-Liability Trust, a limited liability company; HealthTrust, Incorporated; New Hampshire Municipal Association Property-Liability Trust, Incorporated; LGC HealthTrust, a limited liability company; the Local Government Center Workers' Compensation Trust, limited liability company; and the following individuals were named: Maura Carroll, Keith Burke, Stephen Moltenbrey, Paul Beecher, Robert Berry, Robert MacDonald, Peter Curro, April Whittaker, Timothy Ruehr, Julia Griffin, and John Andrews.

09:48:26 1 Since the initial filing, some of
09:48:29 2 these respondents have had the charges against them
09:48:37 3 as stated in the complaint withdrawn. And so as we
09:48:39 4 enter the merits, we have all of the aforementioned
09:48:44 5 business entities; and remaining as individual-named
09:48:49 6 respondents, we have Ms. Maura Carroll and we have
09:48:57 7 Mr. Peter Curro.

09:49:00 8 The docket number is C-2011000036.
09:49:11 9 First announcement -- first
09:49:33 10 correction of the day, as of this point in the
09:49:37 11 proceedings, we still have Mr. Andrews as a named
09:49:39 12 representative, but we anticipate motions that -- or
09:49:44 13 a named respondent. We anticipate motions that will
09:49:51 14 change that status.

09:49:52 15 I've addressed you about phones. And
09:49:54 16 let me say this. Because of the statutes in the
09:50:02 17 State of New Hampshire, any observers here today who
09:50:06 18 are carrying firearms openly that I cannot see or are
09:50:09 19 concealed, I request that you leave the building now,
09:50:13 20 secure the firearm elsewhere. I'll reserve your seat
09:50:16 21 and you can come back and take your seat. But there
09:50:19 22 are no firearms in this building unless you are a
09:50:22 23 sworn law enforcement officer.

09:50:29 1 No food is to be ingested, no
09:50:32 2 beverages, all right? You'll notice that there are
09:50:42 3 pitchers of water; but that is for the counsel,
09:50:45 4 witnesses, and other speakers, if you will, who will
09:50:48 5 be at this process for some eight or nine hours
09:50:50 6 today.

09:50:50 7 The lady in front of me is taking a
09:50:55 8 stenographic record of these proceedings. And this
09:50:58 9 is paramount to the rights of every party who is
09:51:05 10 involved in this litigation. Anything can disrupt
09:51:12 11 her despite her efforts to concentrate. So once
09:51:15 12 again, I will say any disruptive behavior will be
09:51:18 13 addressed immediately.

09:51:29 14 Witnesses will appear here during the
09:51:32 15 course of this -- of this hearing. The story that
09:51:37 16 they have to tell will be the facts that are crucial
09:51:44 17 to a determination of this case. They are not to be
09:51:48 18 disturbed. We need to hear everything they have to
09:51:51 19 say.

09:51:55 20 To the media, please do not act in
09:51:57 21 any hectic manner or scurry around, as you may in
09:52:03 22 public hearings. The line of demarcation we're
09:52:08 23 approaching in this direction is the last row of

09:52:12 1 tables. Do not use any flashes or other disruptive
09:52:16 2 devices.

09:52:18 3 To the party witnesses -- to the
09:52:24 4 parties' witnesses. You are not under any
09:52:26 5 sequestration order. So you're free to remain in
09:52:29 6 this room. If you feel a desire or need to retreat
09:52:34 7 for any period of time, just please inform someone on
09:52:41 8 your team, if you will, and we have a holding room
09:52:45 9 for witnesses where you can wait until you are
09:52:49 10 called. The streaming, however, does not feed into
09:52:53 11 there.

09:52:55 12 Also, for some of the witnesses, this
09:52:58 13 may be a new experience for you. Others of you have
09:53:01 14 spent as much time in courtrooms as many of the
09:53:05 15 lawyers here. But please keep this in mind at all
09:53:10 16 times. And I'm speaking mostly to the witnesses.

09:53:14 17 I am the person who in the end will
09:53:16 18 be charged with making a determination in this
09:53:21 19 matter. And so it is of utmost importance that not
09:53:24 20 only can the stenographer hear what you're saying,
09:53:26 21 but that I hear it and understand what you're saying.
09:53:30 22 So anytime I may just interject quickly to keep your
09:53:34 23 voice up, please don't be embarrassed or taken off

09:53:38 1 your stride by that. My responsibility also is to
09:53:41 2 protect the record in the event of an appeal.

09:53:47 3 When your attorneys have completed
09:53:50 4 their questioning and cross-examination has been
09:53:52 5 completed, I may have a question of the witnesses.
09:53:57 6 Put no special significance to that. I am generally
09:53:59 7 asking for two reasons.

09:54:01 8 One, for matter of clarification
09:54:03 9 because I may have missed something as it went by.
09:54:08 10 And secondly, I may ask a question because I have a
09:54:14 11 responsibility to keep the record as complete as
09:54:18 12 possible. And to do that, if I believe that there's
09:54:20 13 a gap in that record and I need that fact, I will ask
09:54:25 14 you of that. If there's any counsel from your
09:54:29 15 lawyers, I'm sure they'll interject at that time.

09:54:32 16 To the counsel. I remind you of the
09:54:38 17 previous protective orders in this case having to do
09:54:42 18 with certain management aspects, certain aspects
09:54:46 19 having to do with medical identifying evidence.

09:54:57 20 I will say to the public that there
09:54:59 21 was an orientation session for counsel here on
09:55:05 22 Friday, which there were some informal agreements, if
09:55:08 23 you will. And I do want to change one of those. And

09:55:12 1 that is that if you are -- if you wish to approach
09:55:16 2 me, please ask leave to do so. If you wish to
09:55:20 3 approach the witness, feel free to do so without any
09:55:24 4 prior request. We wouldn't want to trip you up and
09:55:29 5 make you adopt any new rules. I will keep my eye on
09:55:35 6 you.

09:55:36 7 The conduct, as I have said from the
09:55:43 8 outset, is something that I'm very sensitive to. And
09:55:48 9 I will also say that these lawyers have been at a
09:55:51 10 very difficult task for what, for some, may seem a
09:55:56 11 short time. But you know, it's been eight months at
09:55:59 12 a minimum. And for those that were involved in the
09:56:02 13 initial investigation, it's longer than that. They
09:56:04 14 have shown not only their durability, but their
09:56:09 15 patience at dealing with at times highly-charged
09:56:12 16 issues. And we've made it to the evidentiary phase.
09:56:16 17 And for that again I'm appreciative of all the
09:56:19 18 cooperation and courtesies that have been extended,
09:56:24 19 if you will, to the tribunal here.

09:56:26 20 Also, with respect to counsel, the
09:56:30 21 Rules of Evidence, as you know, do not apply strictly
09:56:33 22 here. That is not to say that I am not familiar with
09:56:38 23 them. However, in an administrative proceeding, know

09:56:45 1 that all evidence that I believe is relevant/material/
09:56:53 2 reliable will be heard. I have the discretion and I
09:56:56 3 will exercise it to accord the appropriate weight to
09:57:02 4 whatever testimony or exhibits there are that one or
09:57:06 5 more of you are objecting to. But this proceeding
09:57:11 6 hopefully can be facilitated by moving forward.

09:57:18 7 Weight is more easily given as the
09:57:22 8 case proceeds because there's a relativity factor
09:57:27 9 that comes in to play. However, someone has to go
09:57:31 10 first. And to the best of my ability, I will keep
09:57:34 11 that strike zone at the same place, to borrow a
09:57:37 12 sports analogy, for all counsel, regardless of when
09:57:42 13 they're asking their questions.

09:57:48 14 By prior agreement, we have the
09:57:53 15 exhibits that are to be submitted already assigned
09:57:58 16 identification numbers. They still have to be
09:58:00 17 admitted as evidence. But I thank counsel for all
09:58:03 18 their work in that regard as well. I did solicit a
09:58:12 19 statement of agreed facts in this matter and have
09:58:15 20 been provided what counsel's best efforts would
09:58:22 21 yield, given the time allowed.

09:58:25 22 With that, because there is an audio
09:58:30 23 recording also being made of these proceedings, I'm

09:58:33 1 going to ask counsel who expect to speak today to
09:58:40 2 introduce themselves for the record. And I'll begin
09:58:44 3 with the moving party.

09:58:47 4 MR. VOLINSKY: Good morning, Mr. Mitchell.
09:58:49 5 My name is Andru Volinsky and I represent the Bureau
09:58:54 6 of Securities Regulation.

09:58:55 7 MR. TILSLEY: Good morning. Roy Tilsley on
09:58:56 8 behalf of the Bureau as well.

09:58:58 9 THE PRESIDING OFFICER: Thank you.

09:58:58 10 MR. WINGATE: Good morning. Earle Wingate,
09:59:02 11 staff attorney, Bureau of Securities Regulation.

09:59:06 12 THE PRESIDING OFFICER: And with the
09:59:07 13 respondents.

09:59:07 14 MR. SATURLEY: Good morning, Mr. Mitchell.
09:59:07 15 For the record, my name is William Saturley. I
09:59:10 16 practice with the firm of Preti Flaherty here in
09:59:11 17 Concord, and I represent the Local Government Center
09:59:14 18 business entities.

09:59:16 19 THE PRESIDING OFFICER: Thank you.

09:59:17 20 MR. QUIRK: Good morning. Brian Quirk,
09:59:19 21 also from the law firm of Preti Flaherty. I also
09:59:23 22 represent LGC and its affiliated entities.

09:59:25 23 THE PRESIDING OFFICER: Thank you.

09:59:27 1 MR. GORDON: Steve Gordon from the law firm
09:59:30 2 of Shaheen & Gordon, and I represent Maura Carroll.

09:59:33 3 THE PRESIDING OFFICER: Thank you.

09:59:34 4 MR. HOWARD: Good morning. Mark Howard
09:59:36 5 from the firm of Howard & Ruoff in Manchester. With
09:59:38 6 me is Attorney Kimberly Myers. And I represent Peter
09:59:43 7 Curro.

09:59:43 8 THE PRESIDING OFFICER: Thank you.

09:59:45 9 MR. RAMSDELL: Good morning, Mr. Mitchell.
09:59:48 10 Michael Ramsdell from Ramsdell Law Firm on behalf of
09:59:50 11 John Andrews. And with me today is Joshua Pantesco
09:59:54 12 from the law firm of Orr & Reno.

09:59:57 13 THE PRESIDING OFFICER: Thank you.

09:59:59 14 Mr. Ramsdell -- I'm sorry --
10:00:02 15 Mr. Volinsky.

10:00:03 16 MR. VOLINSKY: Sir.

10:00:04 17 THE PRESIDING OFFICER: You have a motion
10:00:05 18 this morning regarding Mr. Andrews?

10:00:08 19 MR. VOLINSKY: Yes. We move the hearing
10:00:11 20 officer to allow us to enter a voluntary non-suit to
10:00:13 21 dismiss all claims against Mr. Andrews pursuant to a
10:00:16 22 settlement reached on Saturday.

10:00:19 23 THE PRESIDING OFFICER: Thank you very

10:00:20 1 much.

10:00:20 2 Is there any objection to that?

10:00:23 3 All right. Then the charges are
10:00:25 4 withdrawn. Mr. Andrews is dismissed from these
10:00:28 5 proceedings.

10:00:31 6 Mr. Ramsdell, I understand that that
10:00:33 7 terminates your representation of Mr. Andrews, is
10:00:36 8 that correct, for these proceedings?

10:00:38 9 MR. RAMSDELL: It terminates Mr. Andrews'
10:00:42 10 status as a party in these proceedings. What I have
10:00:45 11 for you at this point is -- I have for you an
10:00:49 12 appearance for myself on behalf of the Local
10:00:58 13 Government Center business entities. And there's an
10:01:01 14 original and one copy. Do you want two copies or
10:01:04 15 what is it you'd like?

10:01:08 16 THE PRESIDING OFFICER: Two copies.

10:01:09 17 MR. RAMSDELL: You've got it.

10:01:35 18 THE PRESIDING OFFICER: Mr. Ramsdell, while
10:01:36 19 I have you, please, is it further my understanding
10:01:39 20 that both the LGC business entities obviously and
10:01:45 21 Mr. Andrews have consented to your representation of
10:01:49 22 the LGC business entities now?

10:01:52 23 MR. RAMSDELL: That is correct, Mr. Mitchell.

10:01:54 1 THE PRESIDING OFFICER: Thank you very much.

10:02:02 2 To the Bureau of Securities
10:02:04 3 Regulation, Mr. Volinsky or Mr. Tilsley, we have a
10:02:06 4 motion -- we have a motion with respect to video
10:02:10 5 streaming.

10:02:16 6 Could you step to the microphone,
10:02:18 7 please, Mr. --

10:02:19 8 MR. TILSLEY: Oh. That makes more sense.
10:02:23 9 Based on our discussions on Friday at the
10:02:27 10 orientation, I believe that all parties have assented
10:02:30 11 to our motion to allow live streaming.

10:02:33 12 We have agreed on one camera at a
10:02:37 13 fixed position, which shows a panoramic view from the
10:02:40 14 bench to the screen. We have agreed that the feed
10:02:45 15 goes dark when the hearing is not in session.

10:02:49 16 The hearing officer has control over
10:02:52 17 the microphone so that you can turn the sound off at
10:02:54 18 appropriate times for bench conferences and things
10:02:57 19 like that.

10:02:58 20 And finally, that there will be no
10:03:00 21 copies of the video record provided to any party or
10:03:03 22 anybody else without the hearing officer's permission.

10:03:06 23 THE PRESIDING OFFICER: Thank you very much.

10:03:09 1 Mr. Quirk, please.

10:03:11 2 MR. QUIRK: Thank you, Mr. Mitchell. On
10:03:13 3 behalf of Local Government Center, we assent and join
10:03:16 4 in that motion.

10:03:16 5 THE PRESIDING OFFICER: Thank you. Is there
10:03:17 6 any objection to this motion?

10:03:21 7 None being seen, the motion is granted.
10:03:30 8 I also have received a folder of joint exhibits.
10:03:37 9 Have you received this?

10:03:41 10 Would you please mark that as Joint 1
10:03:43 11 and 2. There are two joint exhibits.

10:04:38 12 (Joint Exhibits 1 and 2 marked
10:04:39 13 and admitted into evidence.)

10:04:46 14 THE PRESIDING OFFICER: Thank you very
10:04:48 15 much. Is there any party here today who is aware of
10:04:51 16 any pending motion on which I have not ruled?

10:04:57 17 Seeing that there are no outstanding
10:04:59 18 motions, I then ask, are there any motions that
10:05:04 19 should be brought to my attention at this time?

10:05:11 20 Very good. Then we will proceed with
10:05:16 21 openings. And it's my understanding that the Bureau
10:05:26 22 of Securities Regulation does have an opening. With
10:05:27 23 respect to respondents, you may contemplate giving

10:05:30 1 your opening at this time or reserving until your
10:05:33 2 direct case.

10:05:37 3 Mr. Volinsky.

10:05:42 4 MR. VOLINSKY: Thank you, Mr. Mitchell.

10:05:46 5 The evidence in this case will show
10:05:49 6 that the Local Government Center violated the spirit,
10:05:53 7 intent, and letter of the law that governs risk pool
10:05:59 8 management, RSA 5-B. Although the Bureau need not
10:06:05 9 prove intent in this matter -- the standards of the
10:06:09 10 statute are the standards -- the evidence will show
10:06:16 11 that the Local Government Center acted intentionally;
10:06:18 12 they acted unethically and they acted unscrupulously.

10:06:23 13 And I use those words intentionally
10:06:25 14 because those are the very words that the Local
10:06:34 15 Government Center boards used to describe the same
10:06:37 16 conduct when they thought their competitor Primex was
10:06:39 17 doing the same thing to them. Unethical.

10:06:45 18 Unscrupulous.

10:06:48 19 The Local Government Center
10:06:53 20 HealthTrust is the cash cow in this organization.
10:06:58 21 The evidence will show that the HealthTrust
10:07:03 22 intentionally charged more in premiums than they
10:07:06 23 needed to operate the HealthTrust. The money was

10:07:13 1 spent on investments that were unnecessary for the
10:07:18 2 operation of the HealthTrust. The money was spent to
10:07:24 3 subsidize a failing workers' comp program. The money
10:07:28 4 was spent to adopt a defined benefit pension plan
10:07:34 5 which included the former executive director just
10:07:38 6 less than two years before he retired, with knowledge
10:07:42 7 that he was going to retire.

10:07:45 8 And perhaps in a small way, but
10:07:48 9 emblematic, the money was spent to give the outgoing
10:07:52 10 executive director a \$100,000 no-work contract for
10:07:57 11 after he retired.

10:08:01 12 Oh. And the money was spent to
10:08:03 13 engage in multiple-year, multiple trips to the New
10:08:10 14 Hampshire Supreme Court litigation with the
10:08:11 15 firefighters in which Local Government Center claimed
10:08:17 16 they were exempt from the Right To Know Law because
10:08:19 17 they're not a governmental agency, at a time after
10:08:24 18 the director of the Local Government Center used the
10:08:28 19 Right To Know Law to get documents from Primex and
10:08:33 20 demand that Primex comply with the Right To Know law.

10:08:40 21 None of these expenditures could have
10:08:43 22 happened if the Local Government Center followed the
10:08:51 23 standards of the statute, which are to return

10:08:53 1 earnings and surplus excess of operations. Return
10:08:59 2 earnings and surplus excess of operations.

10:09:06 3 You will hear -- and it's in the
10:09:09 4 Local Government Center documents -- risk pool
10:09:11 5 surplus is taxpayer money. And in recessionary times
10:09:17 6 when taxes can't be raised, hoarding surplus at the
10:09:25 7 risk pool means teachers get laid off, police
10:09:28 8 officers have their hours reduced, and firefighters
10:09:30 9 don't get new equipment. This case is fundamentally
10:09:34 10 about a disrespect for taxpayers' dollars.

10:09:41 11 Let me provide you with some context.
10:09:44 12 The HealthTrust -- \$360 million a year passes through
10:09:50 13 the HealthTrust, taxpayer dollars, as premiums.
10:09:57 14 85 percent of the cities, towns, and school districts
10:10:01 15 in the state are insured by HealthTrust. HealthTrust
10:10:06 16 is the largest health risk pool in the nation. The
10:10:13 17 largest in the nation.

10:10:16 18 In 2003, a number of affiliated
10:10:21 19 programs went through a reorganization that we'll
10:10:26 20 hear a lot about. The reorganization placed the
10:10:45 21 three risk pools -- health, workers' comp, property-
10:10:51 22 liability -- in a subsidiary position to a parent.
10:10:55 23 It was done by forming Delaware corporations.

10:11:02 1 You will hear testimony that
10:11:05 2 Mr. Andrews claimed he was completely unaware that
10:11:10 3 Delaware was used and that prior to going to
10:11:14 4 Delaware, the lawyers for the Local Government Center
10:11:17 5 had been advised that it was illegal to combine in
10:11:21 6 this way under New Hampshire law. Didn't know. He
10:11:28 7 also didn't know that New Hampshire standards require
10:11:37 8 New Hampshire risk pools to be in New Hampshire
10:11:41 9 entities. And so going to Delaware was a violation
10:11:46 10 of that standard.

10:11:48 11 In 2003, when this happened, the
10:11:53 12 building, which is now worth \$10 million up on
10:11:57 13 The Heights, was owned 75 percent by HealthTrust,
10:12:05 14 25 percent by Property-Liability Trust. As part of
10:12:07 15 the reorganization, these were contributed to a
10:12:11 16 wholly-owned subsidiary of the parent for no
10:12:18 17 compensation. And that can be done because the
10:12:23 18 parent owes no fiduciary duty to the subsidiaries.

10:12:33 19 Mr. Andrews will testify that at the
10:12:35 20 time of that transfer, there was a promise made that
10:12:37 21 if the Local Government Center was ever dissolved,
10:12:42 22 the property would go back to the trusts, creating a
10:12:45 23 constructive trust. Of course, that's not written

10:12:50 1 down anywhere. It's not in a deed. It's not in any
10:12:53 2 of the transfer documents. But that will be his
10:12:55 3 testimony.

10:13:01 4 In 2007, because workers' comp was
10:13:06 5 being looked at carefully by the Labor Department
10:13:10 6 because it was a financially troubled program, the
10:13:17 7 Local Government Center put it together in one entity
10:13:20 8 with the Property-Liability Trust.

10:13:27 9 You will hear that since 2003,
10:13:34 10 HealthTrust has contributed \$34 million to the parent
10:13:42 11 in what's called strategic planning contributions.
10:13:46 12 It shows up on the financial statements: \$34 million.
10:13:52 13 What it actually is is \$18 million was a straight-up
10:13:58 14 subsidiary of the failing workers' comp program and
10:14:02 15 about \$11 million, which includes real estate, is for
10:14:06 16 support of the parent.

10:14:08 17 Now, NHMA, after the reorganization,
10:14:15 18 became essentially a lobbying group and a legal
10:14:18 19 education group. In order to belong to a trust to
10:14:20 20 get your insurance, member towns and cities and
10:14:24 21 school districts have to pay dues to NHMA. Those
10:14:30 22 dues recently are \$900,000 a year across all the
10:14:36 23 members, 300 of which is kicked over to the parent.

10:14:45 1 This \$34 million, in June of '11,
10:14:49 2 under the current director, Ms. Carroll, and under
10:14:53 3 pressure from member organizations, the board adopted
10:14:58 4 a note for \$17 million for Workers' Comp to repay
10:15:06 5 HealthTrust most of the subsidy. It's not a note
10:15:12 6 from the new combined entity. It's a note only from
10:15:15 7 Workers' Comp. It has no interest. It has no
10:15:20 8 payment schedule. The note provides that it's paid
10:15:23 9 from surplus only. And of course, parent determines
10:15:28 10 when, if ever, there will be a surplus in the
10:15:33 11 workers' comp program.

10:15:36 12 The only board that exists in this
10:15:38 13 whole enterprise now is up here at the parent where
10:15:43 14 the parent does not owe a fiduciary duty to the
10:15:49 15 subsidiary.

10:15:52 16 I mentioned unethical and
10:15:53 17 unscrupulous. In 1975, John Andrews came to the New
10:16:02 18 Hampshire Municipal Association from the Maine --
10:16:04 19 State of Maine counterpart. He had all of three
10:16:08 20 months' experience running a risk pool when the Maine
10:16:12 21 director was on sabbatical. Other than that, he was
10:16:16 22 a lobbyist for the Maine program.

10:16:21 23 A few years after he joined, in 1979,

10:16:25 1 he hired Paul Genovese. According to Andrews,
10:16:31 2 Genovese, who was operationally in charge of the
10:16:33 3 workers' comp program -- according to Andrews,
10:16:36 4 Genovese convinced the board of the workers' comp
10:16:39 5 program to break away from the New Hampshire
10:16:44 6 Municipal Association and form a separate
10:16:46 7 organization called Compensation Funds.

10:16:48 8 Compensation Funds, you will hear,
10:16:51 9 later became Primex. Mr. Andrews described Genovese
10:16:56 10 as a traitor, saying he was personally betrayed. He
10:17:01 11 felt hurt personally by the conduct of Mr. Genovese.
10:17:07 12 And you'll see how this animates a lot of the Local
10:17:11 13 Government Center's decision-making as we move
10:17:14 14 forward.

10:17:14 15 The Local Government Center, as the
10:17:17 16 evidence will show, took an extremely harsh attitude
10:17:20 17 towards its competitors, mostly Primex, but also
10:17:25 18 SchoolCare, which is the third risk pool. Indeed,
10:17:29 19 one of the board minutes reflects board member Julia
10:17:33 20 Griffin asking, How can we infiltrate the SchoolCare
10:17:43 21 board?

10:17:44 22 How does this play out? Let me give
10:17:45 23 you some examples. In 2001, a representative named

10:17:49 1 Bob Wheeler submitted a bill in the House designed
10:17:53 2 solely exclusively to strip capital from Primex. He
10:18:00 3 was a board member for one of the trusts at the time.
10:18:05 4 The outside auditor for the trust prepared the
10:18:08 5 financial documents. Julia Griffin testified and
10:18:12 6 provided written testimony on the part of Hanover,
10:18:17 7 where she was town manager, and on the part of the
10:18:20 8 Property-Liability board where she then sat.

10:18:24 9 She said in her written testimony on
10:18:27 10 behalf of that board, Primex is illegally hoarding
10:18:33 11 surplus. Surplus is taxpayer money. Primex will
10:18:37 12 illegally subsidize the property and liability rates
10:18:41 13 with workers' comp money.

10:18:43 14 That bill failed because the
10:18:46 15 committee to which it was assigned considered it to
10:18:49 16 be a shot at one business by another business.

10:18:54 17 Give you another example. The
10:18:58 18 individual boards had a couple of members each that
10:19:02 19 came together and formed what's called a Joint
10:19:07 20 Competition Committee. This happens to be one of
10:19:09 21 their PowerPoints. It's telling that they used, kind
10:19:16 22 of, war symbols and battle medals in their documents.

10:19:21 23 Julia Griffin at an October meeting

10:19:24 1 in '02, Is there any way to expose Primex for
10:19:31 2 hoarding surplus? John Andrews, he wants the
10:19:31 3 municipal association to take back workers' comp, so
10:19:34 4 there will be no competition.

10:19:36 5 Third example. In November of '03,
10:19:41 6 after the combination, the reorganization, Julia
10:19:46 7 Griffin -- now she's on the parent board -- Primex
10:19:49 8 has \$75 million in member balance. She complains
10:19:53 9 they use it to subsidize other programs. She calls
10:19:57 10 at this meeting, reflected in the board minutes,
10:20:00 11 Primex's conduct is unethical.

10:20:04 12 She later votes for the \$18 million
10:20:09 13 subsidy. John Andrews: Primex uses its member
10:20:10 14 balance to subsidize Property-Liability and they will
10:20:13 15 use it for Health. John Eich, a board member from
10:20:18 16 Stark: Primex has a war chest they will use to buy
10:20:23 17 us. And then he proposes that the Local Government
10:20:26 18 Center embrace the same concept and build its own war
10:20:31 19 chest.

10:20:31 20 Bob Wheeler, the representative:
10:20:34 21 Every dollar in the Primex war chest is a taxpayer
10:20:37 22 dollar. He, too, votes to start building a war chest.

10:20:42 23 Mr. Beecher, who was the chair:

10:20:45 1 Primex has no scruples. Andrews argues Primex uses
10:20:50 2 money from one program to the next and suggests that
10:20:54 3 the LGC board must overcome its reluctance to engage
10:20:59 4 in this practice.

10:21:00 5 Unethical. Unscrupulous. Surplus is
10:21:06 6 taxpayer dollars. These minutes were sealed.

10:21:10 7 Also in these minutes, Wheeler
10:21:13 8 explains that towns can't build up and hold surpluses
10:21:19 9 year to year. It's the very same concept expressed
10:21:23 10 in the amended petition.

10:21:26 11 So after the board makes decisions
10:21:28 12 and has discussions and decides to build a war chest,
10:21:31 13 they go to their actuary, Peter Riemer, who's been in
10:21:36 14 place for some 25 years -- he's still their
10:21:39 15 actuary -- and asks him how to do it. He recommends
10:21:42 16 the adoption of a concept called risk-based capital,
10:21:48 17 which relates to insurance companies. At the time --
10:21:53 18 Risk-based capital is expressed in factors or
10:21:57 19 percent. At the time the risk-based capital number
10:22:01 20 for the Local Government Center HealthTrust was
10:22:03 21 between 2.1 and 2.5. 210 percent, 250 percent.
10:22:11 22 He recommends doubling to 4.2.

10:22:14 23 And then the way they reach the 4.2

10:22:17 1 is they don't issue a specific open transparent
10:22:23 2 surcharge to members: We're going to increase
10:22:26 3 capital. They bake it into the rates by increasing a
10:22:31 4 factor called risk. And by increasing risk, premiums
10:22:35 5 come in at a higher level than necessary to support
10:22:39 6 the program and allow them to build their capital
10:22:44 7 from 2.1 to 4.2.

10:22:48 8 But they're not completely honest
10:22:50 9 about the 4.2 either. Because what they do is in
10:22:55 10 addition to the 4.2, is they adopt a 5 percent -- or
10:23:03 11 half a percent -- sorry -- for what are called admin
10:23:07 12 expenses. So the 4.2 is really 4.7. That admin
10:23:15 13 expense in '07 meant premiums came in \$7 million
10:23:22 14 higher than necessary. In '08, they came in
10:23:28 15 \$7.2 million higher. In '09, they were \$8.7 million
10:23:33 16 higher. In 2010, when the investigation is here,
10:23:42 17 they dropped the 5 -- the .5, and now they use
10:23:47 18 \$500,000 as their administrative expense.

10:23:53 19 They set targets of 4.2. The RBC in
10:24:00 20 '07 was 6.7. In '08 it was 6.4. In '09 it was 4.8.
10:24:09 21 '10, under scrutiny, 4.2. This translates to
10:24:20 22 surplus. \$90 million here. Just about \$90 million
10:24:22 23 here. \$77 million, \$84 million. If they'd stayed at

10:24:31 1 the pre-war-chest number, this \$84 million would be
10:24:36 2 half. That's what this case is about.

10:24:42 3 You will hear about two defenses.
10:24:45 4 Let me just touch on them briefly. The first
10:24:50 5 defense: everybody does it. Of the 500 exhibits that
10:24:54 6 LGC has in this case, about 100 of them are about
10:24:59 7 practices at Primex, SchoolCare, and risk pools that
10:25:03 8 no longer exist.

10:25:06 9 Even if the Bureau agreed that
10:25:11 10 everyone does it, as exhibits in this case are the
10:25:17 11 agreement the Bureau reached with Primex in March and
10:25:21 12 the agreement the Bureau reached with SchoolCare last
10:25:25 13 week to return between \$25 and \$30 million to members
10:25:31 14 of excess capital surplus and to -- to adopt
10:25:39 15 processes to prevent those levels of capital from
10:25:42 16 being built up again. There is no selective
10:25:46 17 prosecution in this case, and the Local Government
10:25:49 18 Center can't hide behind others.

10:25:52 19 The second defense is the business
10:25:54 20 judgment rule. First, it doesn't apply. We have a
10:26:00 21 statutory standard. As a matter of business
10:26:02 22 judgment, the board cannot decide to avoid/ignore the
10:26:07 23 standard, violate the standard. Second, even if it

10:26:10 1 did apply, they can't justify that they acted in
10:26:15 2 the -- under the business judgment rule in good faith
10:26:19 3 because by their own terms, the conduct at issue is
10:26:23 4 unethical and unscrupulous.

10:26:27 5 The third point is it's not true.
10:26:32 6 Their business judgment -- I'll use this. This is a
10:26:45 7 chart that compares what are called member
10:26:51 8 contributions in blue, light blue.

10:26:58 9 THE PRESIDING OFFICER: Mr. Volinsky, can
10:26:59 10 we attempt to focus that any better. Well, I mean
10:27:02 11 for others as well.

10:27:15 12 MR. VOLINSKY: Right there. A little
10:27:18 13 better?

10:27:18 14 THE PRESIDING OFFICER: Fine.

10:27:19 15 MR. VOLINSKY: What this chart shows,
10:27:21 16 member contributions in light blue, paid claims in
10:27:24 17 the health program in dark blue. Year after year
10:27:28 18 from '02 to 2010, member contributions exceed claims.
10:27:41 19 Always exceed claims. Then on top of premiums,
10:27:47 20 member contributions, is this green band that's
10:27:50 21 pretty constant throughout. That's an extra reserve
10:27:53 22 that the Local Government Center HealthTrust
10:27:56 23 maintains to pay claims as they come in. It deals

10:28:00 1 with incurred but not reported -- not-recorded-yet
10:28:04 2 claims.

10:28:05 3 So you have contributions and then
10:28:08 4 this claims reserve, which is about \$20 million each
10:28:12 5 year. It's pretty constant because they've predicted
10:28:16 6 pretty well.

10:28:16 7 So they have to blow through
10:28:18 8 contributions, claims, before they get to the red.
10:28:23 9 And the red is the surplus we're talking about. And
10:28:26 10 you can see that the red section doubles, a little
10:28:34 11 more than doubles over the course of this period.

10:28:38 12 The claims, which is what this
10:28:40 13 program is about -- and you'll hear the term "short
10:28:44 14 tail" because these are health claims and they turn
10:28:47 15 rather quickly -- are predictable so that we can set
10:28:51 16 up contributions that always exceed claims. We have
10:28:55 17 a pretty steady claims reserve. And then the net
10:28:59 18 assets are above it. This business is healthy
10:29:03 19 without that red section, without the red assets --
10:29:09 20 the net assets.

10:29:15 21 Let me tell you how I've come to that
10:29:18 22 conclusion. This is a document distributed in '97 --
10:29:26 23 I'll let Adrian try to get a little more focused for

10:29:30 1 me -- by the then-chief financial officer, Sandal
10:29:33 2 Keeffe. She's still the chief financial officer.
10:29:39 3 She's also now the deputy director.

10:29:40 4 This is in response to a Union Leader
10:29:43 5 article from a case that I was involved in where the
10:29:46 6 LGC is responding to a claim that their capital is
10:29:52 7 too low, that their net assets are insufficient.

10:29:56 8 And let me just read two quick
10:29:58 9 paragraphs. It should be first stated that a focus
10:30:03 10 on the members' balance, or -- as she calls it, free
10:30:09 11 surplus of the trust -- is not the sole, and
10:30:11 12 certainly not the best, measure of the trust's
10:30:14 13 financial strength. The members' balance represents
10:30:18 14 funds the trust has remaining after it has set aside
10:30:22 15 reserves sufficient to pay claims and related costs
10:30:25 16 of operations. The trust has fully-funded reserves
10:30:29 17 to pay those claims and costs. In addition, the
10:30:33 18 trust believes it has priced its products to remain
10:30:37 19 fully funded and financially sound. Now to the
10:30:42 20 details.

10:30:43 21 That chart confirms what Ms. Keeffe
10:30:49 22 represents the trust believes it has priced its
10:30:52 23 products to remain fully funded. Member contributions

10:30:55 1 always exceed claims.

10:30:56 2 In the next paragraph she explains
10:31:01 3 that there was an anticipated reduction of member
10:31:06 4 balance. It came about, quote, because the trustees
10:31:10 5 wanted to reduce the members' balance, as required by
10:31:13 6 RSA 5-B, the trust enabling legislation, and the
10:31:18 7 Internal Revenue Code. When the trustees established
10:31:20 8 rates for '96, the decision was made that a reduction
10:31:25 9 in members' balance would be accomplished through
10:31:28 10 lower rates.

10:31:30 11 So they lower the member balance;
10:31:33 12 they returned it there in rates.

10:31:39 13 Second page, same memo. Again, the
10:31:42 14 trust has fully-funded reserves to pay claims. These
10:31:49 15 figures are established based on reviews by Watson
10:31:54 16 Wyatt Worldwide -- that's Peter Riemer -- and is
10:31:56 17 fully funded by the trust. The trust's members'
10:32:00 18 balance is its free surplus -- that's the concept in
10:32:05 19 this case -- which is not associated with its reserve
10:32:08 20 for claims. The trust's financial position clearly
10:32:11 21 shows it is sound and is now meeting, and should in
10:32:14 22 the future meet, its claims reserves and other
10:32:16 23 financial requirements.

10:32:18 1 What we take from this is free
10:32:23 2 surplus isn't financially required. What we'd ask
10:32:29 3 you to do at the end of this case is to set a legal
10:32:34 4 means for establishing earnings and capital and
10:32:43 5 returning surplus so that surplus isn't built up year
10:32:47 6 over year over year.

10:32:50 7 We're going to ask you to require the
10:32:52 8 Local Government Center to disgorge its current
10:32:58 9 surplus back to its member communities. We're going
10:33:01 10 to ask you to set up and enforce essentially
10:33:06 11 constructive trusts to repatriate the real estate and
10:33:13 12 to repatriate the workers' comp subsidy, not with a
10:33:21 13 fake note, but with a real payment back to HealthTrust.

10:33:25 14 And we're going to find -- ask you to
10:33:27 15 find to the extent you hold -- Local Government
10:33:34 16 Center holds illegal surplus, that it acts as a
10:33:37 17 security, requiring registration and meeting those
10:33:39 18 standards.

10:33:41 19 And finally, we're going to ask that
10:33:42 20 you order that the parent model, formed illegally
10:33:52 21 through Delaware, which does not provide for a
10:33:55 22 fiduciary duty for HealthTrust, that that be
10:33:57 23 disbanded. And that that risk pool be supported by

10:34:02 1 premiums and operations designed to support that risk
10:34:08 2 pool and that earnings and surplus be returned to
10:34:12 3 members.

10:34:14 4 THE PRESIDING OFFICER: Thank you,
10:34:15 5 Mr. Volinsky.

10:34:20 6 Mr. Saturley, do you wish to make
10:34:23 7 your opening at this time?

10:34:25 8 MR. SATURLEY: I do, sir.

10:34:26 9 THE PRESIDING OFFICER: Please do.

10:34:39 10 MR. SATURLEY: I understand that I have
10:34:54 11 10 minutes, Mr. Mitchell; is that right?

10:34:56 12 THE PRESIDING OFFICER: Take what you need.

10:34:58 13 MR. SATURLEY: Thank you very much. For
10:34:59 14 the record again, my name is William Saturley, and in
10:35:02 15 this matter I'm honored and it is a privilege to
10:35:06 16 speak on behalf of the Local Government Center and
10:35:08 17 its various business entities.

10:35:13 18 I will take time now to respond to
10:35:16 19 what I consider to be misleading and misguided
10:35:21 20 characterizations of my client's actions, so
10:35:27 21 distorted and so taken out of context as to create a
10:35:32 22 fiction for what has occurred over the past decade.

10:35:38 23 As I said, I'm privileged to

10:35:40 1 represent the Local Government Center, and I want to
10:35:43 2 talk for a minute about what the evidence will show
10:35:46 3 in the next few weeks as you hear from its witnesses
10:35:49 4 and you hear its evidence.

10:35:52 5 The Local Government Center is 115
10:35:55 6 employees who have one mission: Provide the highest
10:35:59 7 benefits and the highest level of service of which
10:36:02 8 they're capable to public employees, consistent with
10:36:07 9 doing that at the lowest possible cost to the public
10:36:12 10 employers.

10:36:13 11 In doing that, they try to do that in
10:36:16 12 a way that makes sure they are always able to pay the
10:36:18 13 claims that are presented to them. And you will hear
10:36:21 14 from many of the staff at the LGC who will come in
10:36:25 15 and describe how they manage that balance, the
10:36:30 16 balance between providing the highest level of
10:36:32 17 benefits at the lowest possible cost.

10:36:37 18 One of the pools they administer is
10:36:39 19 the HealthTrust pool. There are 75,000 separate
10:36:45 20 individuals whose health depends on that trust. They
10:36:49 21 are public employees, their dependents, and retirees.
10:36:55 22 There are 38 separate medical plans within the
10:37:00 23 HealthTrust. There are seven prescription drug

10:37:05 1 plans.

10:37:06 2 Each year in the recent past there
10:37:08 3 have been in the nature of \$360 million worth of
10:37:14 4 claims presented on behalf of those 75,000
10:37:17 5 individuals to be paid. And in each and every
10:37:21 6 instance, the Local Government Center has been there
10:37:23 7 to pay those claims without question. And LGC plans
10:37:32 8 to continue to be there for those employees of the
10:37:35 9 cities, towns, and school districts that it insures.

10:37:43 10 A second pool that's part of the
10:37:45 11 Local Government Center group is the Property-
10:37:50 12 Liability Trust. That pool insures approximately
10:37:53 13 4,100 locations: buildings and contents within the
10:37:59 14 State of New Hampshire with a value of nearly
10:38:02 15 \$4 billion. You may recall last August when
10:38:09 16 Hurricane Irene swept through the New England area.
10:38:14 17 Thankfully it didn't hit New Hampshire very hard.
10:38:18 18 Nevertheless, there were hundreds of thousands of
10:38:21 19 dollars of claims made by the cities and towns and
10:38:25 20 school districts that insure with the Property-
10:38:30 21 Liability Trust, and LGC was there to pay them and
10:38:33 22 plans to be there to pay similar claims in the future.

10:38:39 23 Speaking of real estate for a moment,

10:38:42 1 the LGC offices hosted last year over 1,700 meetings --
10:38:51 2 classes, workshops, skill sets -- attended by 22,000
10:38:55 3 attendees. That's how they use that office building.

10:39:02 4 The third risk pool, the workers'
10:39:06 5 compensation risk pool. 22,000 -- 26,000, excuse me --
10:39:11 6 covered public employees in that pool. LGC has taken
10:39:19 7 an approach with that particular pool, and with all
10:39:22 8 of its coverages, of trying to integrate the coverages.
10:39:25 9 It's been a pioneer in approaching coverages by
10:39:29 10 looking at a totally integrated approach so that
10:39:33 11 there are no gaps in the coverages that might cover a
10:39:38 12 public employee, whether his injury or his health
10:39:44 13 problem arises from work or from private.

10:39:46 14 Consistent with that, LGC's approach
10:39:49 15 has been to offer workshop upon workshop to provide
10:39:53 16 the resources and the education to individuals so
10:39:56 17 that they can help manage their own health and their
10:40:00 18 own healthcare costs, so that they can learn how to
10:40:04 19 be safe at work and at home. Such things as offering
10:40:09 20 personal health assessments to people. 25,000
10:40:13 21 individuals took them up on that offer last year.

10:40:17 22 The types of workshops that they
10:40:19 23 offer to -- in the area of safety include everything

10:40:23 1 from chainsaw running to school bus driving to
10:40:25 2 managing crises in school buildings. That's an
10:40:35 3 approach to provide the individuals the tools and the
10:40:40 4 education and the resources they need to minimize
10:40:45 5 health costs, to manage their lives so that they're
10:40:51 6 happier and healthier.

10:40:56 7 In doing so, the Local Government
10:41:02 8 Center employees make themselves available to people.
10:41:04 9 Last year they fielded over 37,000 telephone calls
10:41:10 10 with inquiries on coverage and how to manage their
10:41:12 11 benefits.

10:41:16 12 All of those things I've described
10:41:20 13 take talented, creative people. LGC calls that
10:41:29 14 making a difference through caring and innovation.
10:41:33 15 The Bureau calls it wasteful spending. And that's
10:41:38 16 one of the differences between us.

10:41:43 17 Let me talk for a minute about who
10:41:44 18 runs this enterprise. LGC has a 31-member board of
10:41:53 19 directors. They're town administrators, school
10:41:55 20 business managers, city councilors, mayors, clerks,
10:42:01 21 teachers. People from Hollis to Hanover, from North
10:42:07 22 Hampton to New Hampton have all served on that board,
10:42:13 23 all without compensation, all committed to how to

10:42:18 1 manage that balance between the services that public
10:42:23 2 employers need and the protections they desire, on
10:42:26 3 the one hand, and minimizing the cost and the impact
10:42:32 4 of high rates.

10:42:36 5 Who better than the members of those
10:42:38 6 boards that I have just described, who better knows
10:42:43 7 the impact that high costs of insurance cause to
10:42:48 8 towns, cities, and school districts? The members who
10:42:53 9 run -- the members of the board who run that
10:42:56 10 organization, all when they leave their LGC board
10:43:00 11 meeting go back to their various cities, towns, and
10:43:04 12 school districts and must justify what they did.
10:43:07 13 They are the ones who are the most sensitive to the
10:43:11 14 costs.

10:43:14 15 And so therefore, I will suggest to
10:43:16 16 you that they're the ones who understand the balance
10:43:18 17 the best. And you'll meet several of those board
10:43:23 18 members in the next two weeks, past and present, to
10:43:28 19 talk about how seriously they took that charge and
10:43:31 20 how they managed it.

10:43:36 21 You'll also meet during the next two
10:43:37 22 weeks many of the advisors that they consulted over
10:43:42 23 this decade-plus that the Bureau wants to focus on.

10:43:46 1 You'll meet the actuary who helps them assess the
10:43:51 2 risk looking forward in the future. You'll perhaps
10:43:54 3 meet the accountant, if it's necessary, and the
10:43:57 4 auditor who prepares their financial records. You'll
10:44:00 5 meet the attorneys. You'll meet the other consultants.

10:44:02 6 They'll be available to you to
10:44:04 7 explain what it is that the board of directors did
10:44:10 8 and the approach that LGC took to this balance that
10:44:13 9 I've described of maximizing services and minimizing
10:44:18 10 the cost.

10:44:21 11 This hearing is a criticism of the
10:44:24 12 decisions made over a decade. What guidelines did
10:44:32 13 the board have to operate within? What were the
10:44:35 14 legal constraints on them? RSA 5-B, we know it
10:44:39 15 exists, we know it's the controlling statute. It's a
10:44:42 16 relatively simple statute. It says, Meet certain
10:44:45 17 tests and then, board, it's up to you. Figure out
10:44:51 18 how to strike the balance between service and cost.
10:44:55 19 Figure out what you need for reserves to manage your
10:45:02 20 business. And when there is surplus, return it.

10:45:07 21 This board, as you've heard, chose a
10:45:09 22 method called risk-based capital: RBC. And you will
10:45:16 23 hear that that's an appropriate choice that they

10:45:20 1 made. And you will hear how they made it, when they
10:45:22 2 made it, how they applied it, and why.

10:45:31 3 There is no other detail in the
10:45:34 4 statute as to what reserves should have been set
10:45:39 5 other than set them as appropriate. There is no
10:45:44 6 other detail in the statute as to how to return
10:45:48 7 surplus. There is no other detail in the statute as
10:45:52 8 to how you should run your business. And the Bureau
10:45:56 9 and the Secretary of State's office has refused to
10:46:01 10 issue any rules to specify the things that they now
10:46:04 11 say were inappropriate.

10:46:06 12 So in the absence of detail, in the
10:46:09 13 absence of specificity in the statute, in the absence
10:46:12 14 of rules, how do you measure what this board did and
10:46:18 15 how it acted for the past decade-plus?

10:46:23 16 And yes, you will hear about the
10:46:26 17 business judgment rule, because in the absence of
10:46:32 18 that specificity and in compliance with New Hampshire
10:46:37 19 law, a board of directors has a prerogative to run
10:46:41 20 its business the way it sees most fit consistent with
10:46:46 21 its duty to run it in good faith, exercising
10:46:54 22 prudence, and in the best interests of the
10:46:56 23 organization.

10:46:58 1 And again, we're talking about a
10:47:00 2 balance. We're talking about a balance between a
10:47:02 3 board having discretion and a board having
10:47:05 4 responsibility. The business judgment rule is the
10:47:12 5 expression of the respect that's given to that
10:47:15 6 balance. Courts have all long said, As long as
10:47:26 7 there's a rational business purpose for a board's
10:47:32 8 decision, as long as they have acted in good faith
10:47:35 9 with ordinary prudence in the best interests of the
10:47:40 10 organization, then we will not second-guess what a
10:47:44 11 board of directors has done. Because that's their
10:47:47 12 area of control.

10:47:52 13 And so with regards to the charges
10:47:56 14 that the Bureau has brought in the amended petition
10:47:59 15 and in this hearing, for each of the topics that the
10:48:05 16 Bureau considers and wants you to consider, you will
10:48:09 17 see as part of our evidence the process that the
10:48:16 18 board of directors went through.

10:48:18 19 For each one of these issues, you
10:48:22 20 will see a lengthy planning process. You will see
10:48:26 21 experts and consultants considered. You will see
10:48:29 22 counsel engaged. You will see robust extensive
10:48:35 23 discussion with multiple viewpoints solicited. And

10:48:39 1 you will see a board that adhered faithfully and
10:48:43 2 fully to its fiduciary duties. All this material
10:48:48 3 will be available through the meeting minutes, the
10:48:52 4 lengthy, extensive meeting minutes that are part of
10:48:54 5 the evidence that we will tender in this case.

10:48:58 6 For each one of the issues that the
10:49:03 7 Bureau considers, it must establish that this board
10:49:07 8 acted in bad faith. Lack of due care. No rational
10:49:12 9 business purpose. That's their burden. And the
10:49:15 10 decision you will need to render is whether or not --
10:49:19 11 how did the Bureau -- how do you determine that this
10:49:22 12 board acted with these decisions?

10:49:26 13 In contrast to the balance and the
10:49:30 14 reasonable balance and the reasonable approach that
10:49:34 15 this board has taken in the decade-plus that we're
10:49:37 16 talking about, the Bureau, through its witnesses,
10:49:42 17 will urge you to take and find that the board should
10:49:45 18 have taken an extreme position, a radical position.
10:49:50 19 The numbers that the Bureau is pushing now in
10:49:56 20 hindsight that the board should have established for
10:50:00 21 RBC is radical. It would leave LGC in a weakened
10:50:05 22 position. It would leave it out of balance in terms
10:50:10 23 of its size, in terms of its obligations, in terms of

10:50:15 1 its ability to move forward.

10:50:25 2 We believe that at the end of this
10:50:27 3 period of this hearing, you will be unable to
10:50:31 4 conclude that the board violated its duties. We
10:50:36 5 believe you will conclude instead that this is a
10:50:39 6 board that should be applauded for acting in its good
10:50:45 7 faith, for acting selflessly, for acting with great
10:50:49 8 care, and for acting always with a legitimate, sound
10:50:55 9 business purpose. This is a board whose mission was
10:51:01 10 dedicated to providing the best service available to
10:51:04 11 public employees at the least cost that it could do
10:51:09 12 for the public employers, consistent with always
10:51:13 13 being there to pay claims.

10:51:21 14 We ask you to contrast that balance
10:51:25 15 with the position, the extreme positions taken by the
10:51:27 16 Bureau. We know that you will hold your judgment
10:51:29 17 until all the evidence is in and all the witnesses
10:51:31 18 have testified.

10:51:33 19 We thank you for that and I thank you
10:51:35 20 for your time.

10:51:40 21 THE PRESIDING OFFICER: Is there any other
10:51:41 22 respondent that would like to make their opening at
10:51:43 23 this time?

10:51:44 1 MR. GORDON: I would.

10:51:45 2 THE PRESIDING OFFICER: Mr. Gordon, please
10:51:46 3 come forward.

10:52:03 4 MR. GORDON: Thank you, Mr. Mitchell.

10:52:04 5 As you know, I represent Maura Carroll.
10:52:10 6 And the directors of LGC faithfully exercising their
10:52:15 7 fiduciary duties, knowingly and prudently chose Maura
10:52:22 8 Carroll as their executive director. Their choice
10:52:28 9 was a prudent one.

10:52:30 10 After the long and dedicated service
10:52:32 11 of John Andrews that brought LGC to the national
10:52:38 12 forefront of pooled risk management programs, the
10:52:44 13 board sought a new and different kind of leadership,
10:52:50 14 a leader who would serve the organization with
10:52:52 15 integrity and intelligence. A leader possessing the
10:52:58 16 intangible qualities of grace, humility, and
10:53:05 17 strength. And a national search was undertaken.

10:53:11 18 A profile of the qualities necessary
10:53:15 19 to assume the mantle of leadership of an organization
10:53:20 20 that was dedicated to its members to provide the best
10:53:29 21 quality service at the lowest possible cost was
10:53:34 22 begun. Interviews were conducted of board trustees
10:53:37 23 and staff.

10:53:41 1 And then exercising their fiduciary
10:53:45 2 duties, the board described the ideal candidate as
10:53:50 3 follows: A leader of professional management with the
10:53:54 4 very background to include municipal and statewide
10:54:00 5 public experience, public policy experience,
10:54:05 6 familiarity with legislative and strategic planning,
10:54:10 7 familiarity with insurance pools, unquestionable
10:54:16 8 ethics and integrity.

10:54:18 9 And then the skills section. And this
10:54:21 10 will be Exhibit 450 when it gets introduced. Ability
10:54:26 11 to implement and execute the strategic plan as
10:54:30 12 developed by the board of trustees. The responsibility
10:54:37 13 was to execute the plan.

10:54:39 14 An ability to build a vision for the
10:54:41 15 future, work hard and build a consensus amongst
10:54:44 16 different groups of different constituencies and
10:54:47 17 interests with different roles and different
10:54:50 18 responsibilities.

10:54:51 19 A negotiator, a delegator, a problem
10:54:54 20 solver. And that person had to have the unique
10:54:58 21 capacity to balance these divergent interests.
10:55:03 22 Divergent interests to make the organization stronger
10:55:07 23 and better for a singular and dramatic purpose. That

10:55:13 1 purpose was to serve its members.

10:55:19 2 And in the end, as it goes through
10:55:21 3 the other personal characteristics, unquestioned
10:55:25 4 morals, integrity, ethics, they sought a high energy
10:55:30 5 individual with contagious enthusiasm, and thank
10:55:37 6 goodness, a sense of humor.

10:55:38 7 And I'd like you to meet Maura
10:55:40 8 Carroll. For she was the choice. Born in Concord.
10:55:50 9 She now lives in the house she grew up in, and she
10:55:55 10 lives there with her husband, who's seated right
10:55:57 11 beside her. She went to Bishop Brady and Holy Cross.
10:56:01 12 And the summer before attending Tulane Law School,
10:56:04 13 she worked at Health and Human Services.

10:56:11 14 Public service was in her bloodline.
10:56:14 15 Her dad was a public employee, a public servant for
10:56:18 16 58 years. Serving also as County Treasurer and a
10:56:28 17 Supervisor of the Checklist for as long as Maura can
10:56:31 18 remember. She served in the Legislature for three
10:56:33 19 terms, representing Ward 6 in the City of Concord.
10:56:37 20 She then served as a city councilor for 8-1/2 years.
10:56:43 21 And added to this broad array, she has served on
10:56:47 22 numerous nonprofit boards: United Way, Capital
10:56:51 23 Regional Development Council, and here in Concord,

10:56:55 1 our own Capitol Center.

10:56:57 2 She had a short stint as a private
10:56:59 3 attorney, nine months, and then she realized that her
10:57:05 4 passion, her devotion, and her commitment was to
10:57:10 5 serving people, to helping people. And she became a
10:57:18 6 staff attorney at the NHMA in 1988, government
10:57:22 7 affairs director in 1999, and in 2000 she became head
10:57:27 8 of both of those organizations.

10:57:31 9 For nearly a quarter of a century --
10:57:37 10 a quarter of a century -- she has devoted her
10:57:41 11 professional life to doing good and doing well. And
10:57:48 12 it bears note that certain of the issues in this
10:57:54 13 case -- RBC, corporate structure, surplus, return of
10:57:59 14 capital -- these were all decisions that were made by
10:58:02 15 the board and not by Maura. She had no principal
10:58:13 16 involvement in those decisions. And the bylaws that
10:58:17 17 you will read make it clear that it's the duty of the
10:58:21 18 directors to set the policy. It is the duty of the
10:58:25 19 executive director to carry out the policies of the
10:58:30 20 board.

10:58:35 21 In 2009, she was chosen as interim
10:58:39 22 director and then quickly after that, she became
10:58:41 23 appointed executive director, a position she now holds.

10:58:47 1 Once appointed, and consistent with
10:58:49 2 the charge that she was given by the board, she began
10:58:54 3 an immediate management review of the organization
10:58:59 4 and implemented internal structural changes designed
10:59:02 5 to make the LGC more efficient and effective, again,
10:59:08 6 when serving its members.

10:59:11 7 These changes were significant,
10:59:16 8 eliminating 20 percent -- 20 percent of staff
10:59:18 9 positions. There was also increased transparency.
10:59:24 10 With everything you want to know, you can find on the
10:59:27 11 LGC website. High-level changes have occurred.
10:59:29 12 There is now in-house counsel. Of the seven-member
10:59:34 13 leadership team -- of the seven-member leadership
10:59:41 14 team, four are new. But those who have the
10:59:43 15 institutional knowledge and expertise regarding the
10:59:47 16 management in the operation of the pools have
10:59:52 17 remained the same.

10:59:53 18 And as I heard some of the comments
10:59:56 19 today, the LGC is being attacked in part because of
11:00:01 20 its success, not for its failures. And woe be it for
11:00:10 21 anybody who's gone through the FRM debacle, woe be it
11:00:15 22 that this hearing was one about insolvency and not
11:00:18 23 having too much money.

11:00:22 1 This is not about embezzlement, this
11:00:25 2 is not about stealing, this is not about misapplication
11:00:28 3 of funds. This is an issue about return of surplus
11:00:32 4 and what that means under the statute.

11:00:38 5 I think, in part, success is
11:00:39 6 determined just simply not by money, but member
11:00:42 7 satisfaction, and member satisfaction can best be
11:00:46 8 memorialized, can best be quantified by the retention
11:00:49 9 of our members. Are our members unhappy with what we
11:00:54 10 are doing? If they are unhappy, they should be
11:00:57 11 leaving. If they think their costs are too high,
11:01:02 12 they should leave. They are free to do so. But they
11:01:07 13 have chosen not to leave. They have chosen to remain
11:01:12 14 with us for a dramatic and simple reason: what we do,
11:01:16 15 we do well. And we do better than others.

11:01:22 16 Our membership has increased, in fact,
11:01:26 17 by 1.6 percent. About 90 percent of the local
11:01:30 18 government entities able to participate in risk pools
11:01:34 19 have some sort of coverage with us. 90 percent:
11:01:38 20 medical, dental, FSA, property, vehicle, workers'
11:01:41 21 comp, unemployment comp. They are with us for a
11:01:44 22 reason. And the reason is we are fulfilling our
11:01:54 23 mission.

11:01:55 1 The actual number -- the actuarial
11:01:58 2 numbers in this case can be mind-numbingly complex.
11:02:03 3 And before this case I thought RBC was the Royal
11:02:07 4 Ballet Company. And I don't profess to have a deep
11:02:11 5 understanding of the issues, but having reached a
11:02:14 6 certain stage of my life, there is some issues that I
11:02:18 7 do believe in and that nothing or very few things can
11:02:24 8 ever be certain. The future is simply not predictable.

11:02:30 9 And this case involves, as Mr. Saturley
11:02:34 10 so eloquently stated, the decision-making of the
11:02:36 11 board and the exercise of their fiduciary duties.
11:02:43 12 And I heard some snippets in the opening by the BSR
11:02:51 13 about what minutes would show and say.

11:02:56 14 And I was thinking that there may be
11:03:00 15 one snippet that they were going to use -- it's going
11:03:03 16 to be Exhibit 32 -- and it was a quote of Julia
11:03:07 17 Griffin, a very simple one, short one in those
11:03:09 18 minutes where she talked about infiltrating the
11:03:12 19 school board. When you get these minutes and you
11:03:15 20 read them, you'll see that there was not even a
11:03:18 21 response to that statement. And when you want to
11:03:22 22 talk about robust, complete, dramatic, full dialogue,
11:03:28 23 these minutes are going to give you everything you

11:03:29 1 wanted to know about robust dialogue and were afraid
11:03:34 2 to ask because everything that was said -- it's
11:03:37 3 almost like a transcript.

11:03:39 4 But what the BSR did not include
11:03:42 5 after giving its dramatic statement about unethical,
11:03:46 6 unscrupulous conduct, you'll find in the minutes,
11:03:50 7 these are also some of the other things that were
11:03:53 8 said in that very meeting minutes spoken to by the
11:03:56 9 BSR. And I'm not going to read the whole thing. I'm
11:03:59 10 just going to give you little brief snapshots so you
11:04:02 11 can get a taste.

11:04:03 12 Keith Burke insisted, How can we
11:04:05 13 change our operation to make it better for our
11:04:07 14 members? I think that is what we have to focus on.

11:04:12 15 Paul Beecher concurred by stating,
11:04:14 16 That's a good point.

11:04:15 17 John Andrews stated, We are not
11:04:17 18 drawing the line with municipalities. One-stop
11:04:21 19 shopping. That is the integration plan -- one-stop
11:04:24 20 shopping, that's important. It enhances services.
11:04:27 21 I think better governance makes a better workplace.

11:04:32 22 Wendy Parker stressed that, This
11:04:35 23 exercise can make us stronger and give us more

11:04:38 1 resources for our members.

11:04:41 2 Julia Griffin pointed out that, The
11:04:43 3 cumbersome nature of having three entities with three
11:04:46 4 mission statements, as an organization, you can't
11:04:55 5 succeed.

11:04:56 6 Bob Lloyd, the counsel, who is
11:04:58 7 sitting at this meeting, he concurred and he said,
11:05:03 8 A facilitator would be beneficial. Combine the
11:05:06 9 products. And we should set a series of meetings to
11:05:08 10 see if this can be accomplished. I think you have to
11:05:16 11 keep on focusing on these goals.

11:05:18 12 In that meeting where one maybe silly
11:05:24 13 comment was made, these were the other comments
11:05:27 14 uttered by the board. And for each of those minutes
11:05:33 15 where you get a headline statement, when you look at
11:05:38 16 the context of the communication, you look at the
11:05:42 17 nature of the dialogue, the issues being addressed,
11:05:47 18 the complexity of the discussion, and the dramatic
11:05:55 19 attention and laser-like focus to serve the mission,
11:06:01 20 keep the organization competitive, and treat its
11:06:06 21 members well, you will see the living embodiment of
11:06:13 22 the business judgment rule being exercised
11:06:19 23 faithfully, prudently, and forcefully.

11:06:23 1 And I suggest with the application of
11:06:25 2 that rule, of the things I am somewhat certain of,
11:06:30 3 the law is such that when that rule is properly
11:06:35 4 exercised, it is not for the court to impose a
11:06:40 5 different judgment.

11:06:41 6 Thank you.

11:06:45 7 THE PRESIDING OFFICER: Mr. Howard, do you
11:06:49 8 wish to make your opening at this time or reserve?

11:06:52 9 MR. HOWARD: I do wish to make a statement,
11:06:55 10 Mr. Mitchell. Thank you.

11:06:56 11 THE PRESIDING OFFICER: Very good. Please
11:06:57 12 come forward.

11:06:59 13 MR. HOWARD: As the hearing officer is
11:07:02 14 aware, I represent Peter Curro, who is a current
11:07:04 15 member of the LGC Board of Directors. I will confess
11:07:09 16 to you right upfront, Mr. Mitchell, that I share with
11:07:12 17 Mr. Volinsky a skill that probably all trial lawyers
11:07:15 18 share. And that is a skill of hyperbole and
11:07:19 19 histrionics. Mr. Volinsky has shown his skill. I do
11:07:23 20 not intend to show mine this morning.

11:07:26 21 What I do not share with Mr. Volinsky
11:07:30 22 is a skill for revisionist history. And I do not
11:07:34 23 share with the Bureau the desire to disparage the

11:07:39 1 good work of an incredibly dedicated member of the
11:07:45 2 LGC Board of Directors with absolutely no evidence to
11:07:47 3 support it whatsoever.

11:07:51 4 Peter Curro is a current member of
11:07:53 5 the board and is chair of the Finance Committee.
11:07:58 6 He's served on LGC-related boards for about 17 years
11:08:02 7 now. Like all members of the board, his service is
11:08:07 8 on completely a volunteer basis. He is not
11:08:10 9 compensated save for being reimbursed his mileage.
11:08:16 10 He commits countless -- and as it turns out in the
11:08:21 11 eyes of the Secretary of State -- thankless hours
11:08:24 12 every year to understanding the complex issues
11:08:28 13 involved in the operation of the risk pools,
11:08:31 14 especially in the setting of rates in the health
11:08:34 15 coverage line of pooled risk management.

11:08:39 16 Peter brings nearly 30 years of
11:08:42 17 invaluable financial expertise and experience to the
11:08:45 18 LGC board, all that it gets for free. He's the
11:08:50 19 business administrator of the Londonderry School
11:08:54 20 District, a position he has held since the year 2000.
11:08:57 21 He previously was the finance director of the Town of
11:09:00 22 Londonderry from 1992 to 2000. And prior to that
11:09:05 23 position, he held various positions in finance at

11:09:09 1 Boston University, including the position of director
11:09:12 2 of finance and personnel for the Boston University
11:09:15 3 School of Management. He holds his bachelor's degree
11:09:19 4 from the University of Lowell and a master's in
11:09:22 5 business administration from Boston University.

11:09:27 6 The evidence, Mr. Mitchell, will
11:09:29 7 demonstrate conclusively that Peter has engaged in
11:09:32 8 countless robust discussions with his fellow board
11:09:36 9 members, debated numerous issues affecting the
11:09:39 10 organization, and voted on proposals, both in favor
11:09:43 11 of and in opposition to, alongside scores of other
11:09:50 12 individuals who have served on the various boards,
11:09:55 13 LGC-related boards over the years, this all being
11:09:58 14 done in the exercise of the board's best business
11:10:01 15 judgment in compliance with the law and his fiduciary
11:10:06 16 obligations as a director.

11:10:08 17 What are the bases for the claims
11:10:12 18 against Mr. Curro as the sole individual in this room
11:10:16 19 who's a member of the board? And Mr. Saturley and
11:10:22 20 Mr. Gordon reminded you, there are 31 members of the
11:10:25 21 board. Mr. Curro is the only one here.

11:10:30 22 As his counsel, I have complained to
11:10:33 23 you, Mr. Mitchell -- you're probably tired of hearing

11:10:36 1 of it -- that since the outset of this matter, the
11:10:41 2 BSR, despite naming Mr. Curro as an individual
11:10:44 3 respondent, and despite having several opportunities
11:10:48 4 to do so over the last eight months, and in blatant
11:10:53 5 disregard of Mr. Curro's due process rights to notice
11:10:57 6 and the opportunity to be heard on allegations
11:11:00 7 against him, the BSR still has not made any
11:11:04 8 allegation of wrongdoing against Mr. Curro.

11:11:10 9 The BSR -- and even Mr. Volinsky here
11:11:14 10 this morning -- has not identified one single action
11:11:20 11 that he took or one single proposal upon which his
11:11:26 12 vote made any difference whatsoever, nor has it
11:11:32 13 identified anything that Mr. Curro said or did
11:11:36 14 differently than any other board member to substantiate
11:11:40 15 the claims they've made in this case.

11:11:44 16 As a matter of constitutional law,
11:11:48 17 fairness and logic, and in the absence of any
11:11:50 18 specific allegation concerning any conduct by my
11:11:55 19 client, his mere membership on a board and his
11:11:57 20 participation and votes as a board member is wholly
11:12:02 21 inadequate to impose any liability on him.

11:12:05 22 Why the Bureau, as a representative
11:12:08 23 of the state -- of our state government doesn't

11:12:11 1 recognize that, is a complete mystery to me. They
11:12:14 2 are, after all, supposed to be the guardians of the
11:12:20 3 due process rights of our citizens. Yet they feel no
11:12:25 4 compunction whatsoever, no reservation whatsoever to
11:12:28 5 call him unethical, unscrupulous, and any other name
11:12:33 6 they can, just to disparage his good name, all in the
11:12:36 7 mission of what, I ask you.

11:12:43 8 In the March 26 hearing on the
11:12:45 9 dispositive motions, Mr. Mitchell, I, again, playing
11:12:52 10 the same tune, asked -- indeed challenged the Bureau
11:12:57 11 attorneys -- to just tell me one thing he did.
11:12:59 12 That's all I asked, was one thing. And the best they
11:13:02 13 could say was, Well, he's here as a representative
11:13:06 14 defendant of the Board of Directors.

11:13:09 15 There is no basis in law to impose
11:13:11 16 any liability upon any individual as a representative
11:13:15 17 defendant of an organization. And the Bureau knows
11:13:18 18 that. But they insist on dragging him through this
11:13:21 19 process. They want wasteful spending? They're
11:13:25 20 forcing wasteful spending.

11:13:32 21 As best as I can guess, the BSR
11:13:35 22 accuses Mr. Curro -- this is a little messy at this
11:13:42 23 point -- of causing the corporate reorganization in

11:13:46 1 2003. Mr. Curro sat on the HealthTrust board as one
11:13:51 2 of 10 members who voted for the reorganization. The
11:13:56 3 vote was 7 to 3, with 1 abstention. Therefore,
11:14:01 4 Mr. Curro's vote in support of the reorganization was
11:14:05 5 completely inconsequential. Without his vote, it
11:14:09 6 would have been 6 to 3. So what? It would have been
11:14:13 7 happened anyway.

11:14:14 8 What the Bureau consistently refuses
11:14:16 9 to acknowledge with respect to Mr. Curro, there were
11:14:21 10 two other boards existing at the time: the NHMA board
11:14:25 11 and the PLT board, the Property-Liability Trust.
11:14:29 12 Those were independent boards who also voted for the
11:14:33 13 reorganization, and not one member of those boards
11:14:37 14 was sued in this case, nor should they have been.
11:14:42 15 But more importantly, Mr. Curro had absolutely no
11:14:44 16 voting privilege or authority with respect to those
11:14:46 17 two boards. Yet he sits here in the eyes of the
11:14:50 18 Bureau as the one man who is to accept all
11:14:53 19 responsibility for that vote.

11:15:02 20 Mr. Volinsky said that there are two
11:15:05 21 defenses in this case. And he outlined them for you.
11:15:08 22 He forgot one. And it's a very important one. In
11:15:11 23 addition to the business judgment rule, Mr. Curro

11:15:16 1 also acted, as did all of these boards over the
11:15:20 2 entire relevant period of time -- in fact, the entire
11:15:24 3 history of these organizations -- with the advice of
11:15:27 4 legal counsel. The merger was voted on when the
11:15:32 5 lawyers told them that the reorganization was lawful.

11:15:41 6 When they -- when the board in 2007
11:15:46 7 was looking to decide what to do in terms of return
11:15:49 8 of surplus and how to make it happen, does it have to
11:15:53 9 be in cash back to the towns? Can it be in the form
11:15:56 10 of rate credit and rate stabilization? They sought
11:16:01 11 and obtained a letter from their counsel which
11:16:06 12 explained to them that the statute does not prohibit
11:16:08 13 them from doing return of surplus in the form of rate
11:16:12 14 credits.

11:16:13 15 When you have the advice of your
11:16:16 16 lawyer telling you that what you can do is lawful,
11:16:21 17 then your decision to follow that advice cannot under
11:16:24 18 any circumstances be unreasonable or a negligent
11:16:28 19 violation of a statute.

11:16:31 20 In terms of -- and this falls under
11:16:36 21 the category of robust discussion -- the RBC method
11:16:45 22 that was chosen, Mr. Curro was part of that
11:16:50 23 discussion and only part of that discussion. It was

11:16:53 1 made, a decision was made after fully vetting the
11:16:57 2 issue with outside consultants, just what you would
11:17:00 3 expect this board to do: The adoption of a strategic
11:17:04 4 plan done with the presence of legal counsel and with
11:17:08 5 a full vetting of the issue with outside consultants.

11:17:14 6 Mr. Curro has at all times acted in
11:17:17 7 compliance with his fiduciary duties. And in
11:17:22 8 Mr. Volinsky's opening remarks, he made no indication
11:17:26 9 to you whatsoever that Mr. Curro has violated any of
11:17:28 10 them.

11:17:29 11 He has at all times acted with the
11:17:31 12 advice of counsel. As such, his actions are
11:17:36 13 reasonable, always performed in good faith, and,
11:17:40 14 therefore, under the two relevant statutes, neither a
11:17:44 15 knowing or negligent violation.

11:17:46 16 Finally, Mr. Mitchell -- and I will
11:17:49 17 sit down and let the proceedings commence -- with
11:17:53 18 respect to Mr. Curro, we have to ask the question,
11:17:56 19 What are the possible remedies that could be imposed
11:17:59 20 against him that are pled by the Bureau. In this
11:18:04 21 case, there are none. The Bureau asks for injunctive
11:18:09 22 relief. And Mr. Volinsky laid out all the things it
11:18:14 23 wants the hearing officer to do. Not one of those

11:18:17 1 remedies that the Bureau is seeking can be imposed
11:18:21 2 against Mr. Curro as an individual member of the
11:18:24 3 Board of Directors.

11:18:26 4 If you were to say cease and desist
11:18:29 5 your violations of RSA 5-B, saying that to Mr. Curro
11:18:33 6 accomplishes absolutely nothing. He's one member of
11:18:37 7 the board. The statutes do allow for penalties of
11:18:41 8 \$2,500 per violation. The Bureau has rightly
11:18:46 9 withdrawn any request for that and is not seeking
11:18:49 10 imposition of those penalties, so that cannot be done
11:18:53 11 against Mr. Curro.

11:18:54 12 There is no other remedy sought. And
11:18:57 13 with all due respect to you, Mr. Mitchell, under the
11:18:59 14 relevant statutes, there is no remedy you can impose
11:19:01 15 against him. He doesn't belong here. He's going to
11:19:05 16 sit here for two to three weeks. And in the end
11:19:07 17 you're going to conclude, Why was he here, and you're
11:19:11 18 going to dismiss him.

11:19:12 19 Thank you.

11:19:13 20 THE PRESIDING OFFICER: Thank you,
11:19:17 21 Mr. Howard.

11:19:19 22 Mr. Volinsky, are you prepared to
11:19:21 23 call your first witness?

11:19:22 1 MR. VOLINSKY: I am.

11:19:23 2 THE PRESIDING OFFICER: All right. Why
11:19:24 3 don't we take maybe a 10-minute recess, and we'll
11:19:27 4 return. In the meantime, you can set up for him, or
11:19:31 5 her.

11:19:31 6 MR. VOLINSKY: Thank you.

11:19:33 7 (Recess at 11:19 a.m.,
11:37:52 8 resumed at 11:37 a.m.)

11:37:55 9 THE PRESIDING OFFICER: We've returned from
11:37:58 10 brief recess. Mr. Volinsky, are you ready to proceed?

11:38:01 11 MR. VOLINSKY: Yes.

11:38:03 12 THE PRESIDING OFFICER: Mr. Witness, would
11:38:06 13 you stand and raise your right hand.

11:38:07 14 (The witness was sworn by the
11:38:09 15 Presiding Officer.)

11:38:17 16 THE PRESIDING OFFICER: Please be seated.

11:38:18 17 Would you state your name -- and if
11:38:21 18 you allow me, gentlemen -- your business address --
11:38:25 19 please approach me if anyone has a need for any other
11:38:29 20 personal identifiers -- and your business address.
11:38:34 21 And then you may have your witness, Mr. Volinsky.

11:38:37 22 THE WITNESS: My name is Michael A. Coutu,
11:38:41 23 C-o-u-t-u. I'm retired so I don't have a business

11:38:46 1 address, but my residence is 805 Central Road. And
11:38:52 2 that's in Rye Beach, New Hampshire 03871.

11:38:59 3 THE PRESIDING OFFICER: Your witness,
11:39:00 4 Mr. Volinsky.

11:39:01 5 MR. VOLINSKY: Thank you, Mr. Mitchell.

11:39:01 6 MICHAEL A. COUTU,
11:39:01 7 having been first duly sworn, was examined
11:39:01 8 and testified as follows:

11:39:03 9 DIRECT EXAMINATION

11:39:03 10 BY MR. VOLINSKY:

11:39:04 11 Q. Mr. Coutu, you're here as an expert witness
11:39:05 12 so I want to ask you first about your background.
11:39:07 13 Tell us your educational background, please.

11:39:10 14 A. I graduated from the University of Rhode
11:39:17 15 Island. I would have been the class of 1993 [sic],
11:39:19 16 but I completed my program a year earlier with a
11:39:25 17 business degree in business administration with a
11:39:27 18 concentration in finance.

11:39:29 19 Q. Business with finance concentration?

11:39:33 20 A. Correct.

11:39:33 21 Q. Before or after, did you serve in the
11:39:35 22 military?

11:39:35 23 A. Before college, I served three years in the

11:39:39 1 United States Marine Corps.

11:39:41 2 Q. Honorably discharged?

11:39:42 3 A. Yes.

11:39:44 4 Q. As it's relevant to the expert testimony
11:39:49 5 you're going to be offering in this case, would you
11:39:51 6 outline your professional employment experience.

11:39:56 7 A. I think it's probably best to divide my
11:40:00 8 career into two -- into two pieces. From 1969
11:40:06 9 through 1984, I was primarily a banker, initially
11:40:15 10 with Industrial National Bank, which became known
11:40:20 11 later as Fleet National Bank. There I served
11:40:25 12 initially in the credit department, which was the
11:40:28 13 training ground for future lending officers.

11:40:35 14 Once I completed that training,
11:40:38 15 again, a couple years, I was asked to set up an
11:40:41 16 international credit department as the bank began its
11:40:44 17 lending to nonsovereign entities, borrowers. And
11:40:53 18 also part of that time in the credit function, I also
11:40:56 19 managed two workouts, workouts as in failing
11:41:00 20 operations. One of them was a subsidiary, the bank,
11:41:05 21 a commercial finance company located in Montreal,
11:41:08 22 Canada, and the second was a golf cart manufacturer,
11:41:16 23 which ultimately went bankrupt, managing that

11:41:18 1 business, having separated certain of the operations
11:41:22 2 prior to bankruptcy.

11:41:24 3 As far as my lending career, I was
11:41:29 4 made head of the trade finance group, which finances
11:41:34 5 the importation and exportation of goods from the
11:41:38 6 U.S. to foreign nations or the importation from
11:41:42 7 foreign nations to the U.S.

11:41:46 8 Those financing vehicles were largely
11:41:49 9 done in connection with government programs: the
11:41:55 10 Export-Import Bank of the United States, which
11:41:58 11 guaranties the payment obligation, and quasi-
11:42:03 12 governmental as in Foreign Credit Insurance
11:42:06 13 Association, which reinsures the political risk to
11:42:08 14 Ex-Im Bank, but otherwise provides coverage for
11:42:11 15 nonpayment by the foreign borrowers.

11:42:15 16 I then was asked -- I think it was in
11:42:17 17 1979 -- to run an international bank which was
11:42:23 18 located in New York City. That international bank
11:42:27 19 was, again, engaged in trade finance as well as
11:42:31 20 commodity finance and foreign correspondent banking.

11:42:37 21 And in 1982, I was recruited by
11:42:41 22 American Express to run American Express's commodity
11:42:45 23 trade and project financing lending group, which I

11:42:49 1 did till 1985.

11:42:54 2 While at American Express, in mid
11:43:00 3 1984, an insurance company owned by American Express
11:43:05 4 at that time, Fireman's Fund Insurance Company, had a
11:43:10 5 rather large credit-sensitive exposure to a company
11:43:17 6 by the name of Allis-Chalmers. I was asked by
11:43:22 7 American Express to provide financial guidance to
11:43:28 8 Fireman's Fund and how best to manage that exposure.
11:43:34 9 Allis-Chalmers at that time was teetering on
11:43:36 10 bankruptcy.

11:43:39 11 In 1985, I began changing my career
11:43:44 12 from banking into insurance. Fireman's Fund suffered
11:43:50 13 a \$300 million capital loss in 1993 -- excuse me --
11:43:55 14 1983. And American Express sent myself, along with a
11:43:59 15 couple of other fellows, to Fireman's Fund, the
11:44:04 16 thought being that perhaps banking-type people might
11:44:08 17 be able to better manage the insurance company.

11:44:12 18 My specific assignment at that time
11:44:14 19 was to run the financial guaranty division of
11:44:19 20 Fireman's Fund, which based on guaranties issued
11:44:24 21 primarily in respect of municipal borrowers, general
11:44:29 22 obligation bonds, and revenue bonds, and before giving
11:44:33 23 effect to reinsurance, was a book of \$26 billion in

11:44:38 1 liabilities.

11:44:41 2 While working at Fireman's Fund, a
11:44:44 3 decision was made by American Express to sell
11:44:47 4 Fireman's Fund, and I was working -- or I did work
11:44:51 5 primarily with Lehman Brothers on the due diligence
11:44:56 6 with respect to that sale. It did get sold in
11:45:00 7 September of 1985 in an IPO. And with that sale, I
11:45:08 8 then left Fireman's Fund and joined an investment
11:45:13 9 banking boutique by the name of Glucksman & Company.
11:45:17 10 Glucksman & Company was formed by Lew Glucksman, the
11:45:22 11 former chairman and CEO of Lehman Brothers. He and I
11:45:25 12 and several other ex-Lehman partners formed a -- I'll
11:45:29 13 call it an investment banking boutique. My specialty
11:45:33 14 at that time was primarily bankruptcy.

11:45:38 15 And I also was the advisor to
11:45:41 16 Fireman's Fund in the creation of a company which
11:45:45 17 exists today in New York City called Municipal Bond
11:45:50 18 Insurance Association in its corporate form as it's
11:45:53 19 constituted today.

11:45:53 20 Q. What kind of company is that? What does
11:45:56 21 that company do?

11:45:56 22 A. MBIA is -- issues credit enhancements. Its
11:46:02 23 initial charter was to do so in connection with,

11:46:05 1 again, municipal risk. These would be general
11:46:09 2 obligations and revenue bonds. Well after my
11:46:15 3 association with MBIA, they then unfortunately got
11:46:20 4 involved in providing credit enhancements with
11:46:24 5 respect to pools of mortgages, known as structured
11:46:29 6 financings, and that became a -- as part of the 2008
11:46:35 7 credit failings, major issues of that.

11:46:40 8 Q. So after Glucksman, what -- other than
11:46:45 9 MBIA, did Glucksman have other involvement with
11:46:46 10 insurance companies?

11:46:49 11 A. Well, Allis-Chalmers was a company that --
11:46:56 12 to whom Fireman's Fund had a substantial amount of
11:47:00 13 exposure. And after separating from Fireman's Fund,
11:47:03 14 I continued to advise Fireman's in connection with
11:47:08 15 Allis-Chalmers, which ultimately did file an order
11:47:11 16 for relief, a petition for relief in bankruptcy under
11:47:17 17 the Bankruptcy Code.

11:47:20 18 Q. Move me forward from there. I think
11:47:22 19 international --

11:47:23 20 A. Yes. Sandy Weil, who acquired Prime
11:47:37 21 America. Prime America included Smith Barney, the
11:47:42 22 investment banking firm. And Sandy asked Lew to come
11:47:47 23 over and run Smith Barney. And in concert with that

11:47:50 1 decision, then we wound up the Glucksman Company. I
11:47:55 2 went forward with my own business. It was called Oak
11:48:01 3 Hill Financial Group, continuing primarily in the
11:48:02 4 bankruptcy sector.

11:48:05 5 Q. And then after Oak Hill?

11:48:08 6 A. After Oak Hill, I was recruited by Xerox
11:48:13 7 Corporation, along with some other senior executives.
11:48:18 8 Xerox owned a large property and casualty company
11:48:23 9 called Crum & Forster, based out of Morristown, New
11:48:29 10 Jersey. Xerox had made substantial capital
11:48:33 11 contributions to Crum & Forster, made a decision that
11:48:37 12 it did not want to continue in the insurance space.
11:48:45 13 And I was hired for the purposes of finding an exit
11:48:51 14 strategy for Xerox to get out of the property and
11:48:53 15 casualty insurance business.

11:48:55 16 Q. Were you able to do that?

11:48:57 17 A. We -- we did accomplish that goal. We tried
11:49:04 18 not to get into a lot of technical insurance matters,
11:49:08 19 but we -- there was an intercompany pooling
11:49:10 20 arrangement, which is common in the property and
11:49:13 21 casualty sector -- we unbundled that arrangement and
11:49:18 22 created six standalone underwriting companies and
11:49:23 23 then created a separate company which became the

11:49:27 1 repository for lots of latent liabilities. That
11:49:36 2 entity, sometimes known as the bad bank, was known as
11:49:39 3 The Resolution Group. And in due course, it was my
11:49:42 4 responsibility to run the bad bank.

11:49:45 5 Q. And what business purpose did the bad bank
11:49:48 6 serve while you were running it?

11:49:51 7 A. Certain of the liabilities for the
11:49:53 8 continuing underwriting businesses that caused or
11:49:59 9 created the balance sheet stress, those liabilities
11:50:01 10 were transferred over to The Resolution Group.

11:50:05 11 In addition, the captive insurance
11:50:07 12 company, which was the hub of The Resolution Group,
11:50:13 13 International Insurance Company, had already a
11:50:16 14 substantial amount of latent liabilities, coupled
11:50:19 15 with approximately \$1.7 billion of uncollectible
11:50:26 16 reinsurance.

11:50:27 17 In addition to that, as part of The
11:50:34 18 Resolution Group, we formed a separate claims entity
11:50:37 19 to manage latent claims, which included many various
11:50:44 20 forms of toxic tort claims: asbestos probably being
11:50:47 21 the largest particular claims; breast implants,
11:50:51 22 pollution claims, and such other claims. And that
11:50:56 23 entity, which was known as The Division, provided

11:51:00 1 that service for all of the underwriting companies,
11:51:02 2 the 600 underwriting companies plus The Resolution
11:51:06 3 Group.

11:51:06 4 Q. And were you the president of this company
11:51:08 5 then?

11:51:09 6 A. I was.

11:51:10 7 Q. CEO?

11:51:10 8 A. I was the president and CEO of the
11:51:13 9 International Insurance Company, its sister company,
11:51:16 10 which is the International Surplus Lines Company, the
11:51:21 11 holding company which is The Resolution Group, and
11:51:23 12 then the sister or affiliate company called Envision
11:51:29 13 Claims Services.

11:51:29 14 Q. And when you say that they were underwriting
11:51:31 15 claims, that's a form of insurance, right?

11:51:33 16 A. That's correct.

11:51:34 17 Q. Take us forward in your experience in The
11:51:40 18 Resolution Group and how you moved forward from
11:51:42 19 there.

11:51:42 20 A. The International Insurance Company,
11:51:46 21 that -- the usual remedy for insurance companies
11:51:51 22 which were either failing or in financial difficulty
11:51:55 23 was to place the company into a formal proceeding.

11:52:00 1 And that would be done by the domiciliary regulator.
11:52:06 2 And the proceeding would either be a rehabilitation
11:52:10 3 or an insolvency.

11:52:12 4 What I had proposed to the regulators
11:52:16 5 for International, which is the State of Illinois,
11:52:21 6 was to manage International as a noncontinuing
11:52:25 7 business in runoff but to do so as a voluntary
11:52:32 8 runoff, thus to not place it into a formal proceeding.

11:52:36 9 At that time voluntary runoffs were
11:52:40 10 something that had not -- as far as I know, that had
11:52:44 11 not been done as an alternative to, again, a formal
11:52:47 12 proceeding. And so with the blessings of the
11:52:54 13 Illinois Insurance Department, International went
11:52:57 14 into this voluntary runoff.

11:52:57 15 Q. May I ask you a question about that. When
11:52:59 16 you're managing a company that's voluntarily running
11:53:02 17 off its business, how closely do you work with the
11:53:04 18 regulator?

11:53:05 19 A. It's a glove-in-hand relationship. At
11:53:12 20 least in the initial goings of the runoff, it would
11:53:15 21 not be uncommon for me to have conferences calls to
11:53:20 22 the regulators every week. As time goes on and if
11:53:23 23 the, quote, runoff plan is successful, it is that our

11:53:28 1 operations is the plan that we cast, then the level
11:53:34 2 of supervision becomes less intense.

11:53:36 3 But if I contrast runoffs versus
11:53:39 4 underwriting companies, the level of interaction with
11:53:43 5 regulators is a hundredfold increase.

11:53:47 6 Q. Let me also ask you, as the chief executive
11:53:52 7 of an underwriter versus being the chief executive of
11:53:56 8 a runoff company, how familiar do you have to be with
11:54:00 9 the finances of the company at issue and your
11:54:03 10 understanding of the details of those finances?

11:54:08 11 A. You really can't successfully manage a
11:54:11 12 runoff company if you don't have intimate knowledge
11:54:14 13 of the financial side. There are two key elements --
11:54:16 14 There are a lot of elements in a runoff. But the two
11:54:19 15 most critical elements are you have to have
11:54:22 16 sufficient liquidity, i.e., cash to pay claims when
11:54:26 17 due. And then second is you have to have enough
11:54:31 18 continuing surplus to avoid the presumption of being
11:54:36 19 insolvent, requiring the regulatory domicile
11:54:41 20 regulator from intervening into the business.

11:54:43 21 Q. And did you have to deal with both of these
11:54:47 22 issues as the person leading this company through
11:54:50 23 voluntary runoff?

11:54:51 1 A. Yes.

11:54:53 2 Q. How did you do the voluntary runoff?

11:54:59 3 A. International Insurance Company was at that
11:55:01 4 time the largest runoff measured by reserves, which
11:55:05 5 was \$3-1/2 billion, when it went into runoff. And
11:55:09 6 this would be '93-ish.

11:55:15 7 To give some scale to that in
11:55:17 8 comparison to a global statement, International was
11:55:19 9 the largest runoff in the world with the exception of
11:55:24 10 Equitas. Equitas was the runoff mechanism for
11:55:29 11 Lloyd's of London. That was significantly bigger.

11:55:32 12 That runoff was ultimately successful
11:55:37 13 in part because another company based in Toronto,
11:55:42 14 Canada by the name of Fairfax Financial Services,
11:55:47 15 Limited had its own stressed businesses -- stressed
11:55:55 16 as in financially stressed -- and the chairman of
11:55:58 17 that company approached me with respect to potentially
11:56:02 18 acquiring The Resolution Group in order to get the
11:56:06 19 benefit of the skills and services of that group.
11:56:09 20 That transaction was consummated in August of 1999.
11:56:15 21 And The Resolution Group then became part of the
11:56:19 22 Fairfax Financial family of companies.

11:56:23 23 Because Fairfax had its own troubled

11:56:27 1 companies, I then created a separate entity called
11:56:30 2 the RiverStone Resources Group, LLC. And the
11:56:35 3 RiverStone Group was for the purposes of managing
11:56:37 4 Fairfax Financial's troubled, distressed businesses,
11:56:45 5 both in the U.S., Canada, and in London and in Paris.

11:56:52 6 International's journey continues a
11:57:00 7 bit. It was -- ultimately got to the point that the
11:57:05 8 success in managing that runoff created such a large
11:57:09 9 surplus balance -- when I say "large," it was in
11:57:14 10 excess of \$500 million. And because it was a runoff,
11:57:20 11 the regulators would not allow me to extract some of
11:57:24 12 that excess surplus, excess of the size that the
11:57:30 13 balance sheet would find, and as a result of another
11:57:33 14 runoff in the Fairfax family called TIG Insurance
11:57:40 15 Company. TIG --

11:57:41 16 Q. T-I-G?

11:57:42 17 A. -- T-I-G -- company, in working with the
11:57:48 18 California regulators for TIG where TIG was
11:57:49 19 domiciled, I ultimately merged International into
11:57:52 20 TIG, which had no capital, thus creating a mechanism
11:57:56 21 for TIG to have a successful runoff under the
11:58:01 22 auspices of the California Insurance Department.

11:58:03 23 Q. So you worked closely with regulators in

11:58:05 1 California as well as in Illinois for these runoffs?

11:58:08 2 A. I have, as well as other states. The way
11:58:15 3 to think of the regulatory community in the U.S. is
11:58:18 4 the domiciliary regulator is sort of the lead. But
11:58:22 5 because insurance companies will write large books of
11:58:24 6 businesses in a multitude of states, the regulator
11:58:29 7 for a given state also will wade in the waters of a
11:58:34 8 runoff.

11:58:36 9 California is a good example. Many
11:58:38 10 of the companies that I managed had large California
11:58:44 11 exposures. And in that case, it would not be
11:58:46 12 uncommon to have another regulator, California in the
11:58:51 13 case of International, or Illinois in the case of
11:58:53 14 TIG, to wade in on how the runoff plan is constituted
11:58:59 15 and managed.

11:59:00 16 Q. Based on all of this experience, do you
11:59:03 17 consider yourself a runoff specialist?

11:59:08 18 A. I do.

11:59:08 19 Q. How does that compare to being a chief of a
11:59:11 20 non-runoff insurance company?

11:59:14 21 A. Let me just say that while the mission of a
11:59:18 22 runoff is to curtail underwriting altogether, that
11:59:25 23 doesn't always occur. And it doesn't occur because

11:59:27 1 there are outstanding contractual matters that need
11:59:31 2 to be addressed and honored. So there are elements
11:59:35 3 of continued underwriting which is usually part and
11:59:40 4 parcel of the runoff. But again, the goal is to
11:59:43 5 curtail all underwriting.

11:59:45 6 The key difference between someone
11:59:47 7 who's running a company in runoff and someone who's
11:59:51 8 running an ongoing continuing underwriting company,
11:59:54 9 the key and critical mission of runoff is to fully
12:00:00 10 discharge all of the contractual obligations to
12:00:04 11 policyholders. And in the case of the companies
12:00:06 12 which I've managed, most of those policyholders were
12:00:10 13 corporate entities.

12:00:13 14 In order to -- again, to be able to
12:00:17 15 fully discharge 100 percent of those obligations, you
12:00:22 16 have to have sufficient cash to pay claims in capital
12:00:28 17 or surplus in order to avoid being placed in an
12:00:31 18 insolvency proceeding.

12:00:32 19 With respect to an ongoing
12:00:35 20 underwriting company, the challenge -- the
12:00:39 21 fundamental challenge is to generate new business.
12:00:43 22 And new business is in the form of premiums. It may
12:00:47 23 be in concert with long-established programs. It may

12:00:52 1 be new programs of insurance. And the skill there is
12:00:56 2 to price the business at a level that would suggest
12:01:02 3 that the level of claims and expenses would be less
12:01:06 4 than the amount of premium that is charged in concert
12:01:11 5 with those programs.

12:01:13 6 The goal, I might add -- that is not
12:01:15 7 always accomplished.

12:01:20 8 Q. As a person who ran all of these companies,
12:01:23 9 did you ever sue a regulator?

12:01:25 10 A. No.

12:01:28 11 Q. Were you ever forced into involuntary when
12:01:32 12 you started the voluntary runoff process?

12:01:34 13 A. None of the companies that I've managed
12:01:42 14 were entities that ultimately failed, meaning were
12:01:47 15 placed into an insolvency proceeding.

12:01:52 16 Q. After TIG, do you have further relevant
12:01:55 17 experience in the insurance field?

12:01:56 18 A. I do. I might -- First, I retired after
12:02:06 19 TIG, so that would have been in 2002. I probably
12:02:14 20 would have stayed retired. I, however, was approached
12:02:19 21 by some individuals which had made a large equity
12:02:22 22 investment in a Canadian company by the name of
12:02:28 23 Kingsway Financial Services.

12:02:31 1 Q. Case- - -

12:02:31 2 A. Caseway. Kingsway. K-i-n-g-s-w-a-y.

12:02:39 3 Kingsway.

12:02:40 4 Q. What happened with Kingsway?

12:02:42 5 A. Initially the board had me come in to
12:02:45 6 determine what to do with respect to its largest
12:02:49 7 subsidiary. The largest subsidiary of Kingsway was a
12:02:54 8 company by the name of Lincoln General Insurance
12:02:58 9 Company, based in York, Pennsylvania. It underwrote
12:03:04 10 a substantial amount of long-haul trucking and
12:03:10 11 nonstandard auto. It's a company which -- which
12:03:17 12 wrote, on a fairly regional basis, perhaps \$40-45-50
12:03:27 13 million worth of premium a year.

12:03:29 14 When it was acquired by Kingsway --
12:03:31 15 and I believe it was 1997 -- Kingsway grew that
12:03:38 16 company from roughly \$45 million in premiums a year
12:03:44 17 to over \$1 billion in premiums by 2007. It was an
12:03:55 18 unprecedented growth in business. Long-haul trucking
12:04:01 19 is known to be a very difficult business to
12:04:04 20 underwrite. It has -- almost all writers of that
12:04:12 21 business experience losses in excess of premiums.
12:04:15 22 That turned out to be the case with respect to
12:04:18 23 Lincoln General.

12:04:23 1 And as losses mounted, the need for
12:04:26 2 severe, if not dramatic, reserve actions suggested
12:04:31 3 that Lincoln may not make it. I was brought in by
12:04:35 4 Kingsway to determine what was potentially a
12:04:43 5 salvageable business. If not, then what would be the
12:04:46 6 best result with respect to preserving the economic
12:04:50 7 value of that entity.

12:04:54 8 Q. And in part, was this based on a detailed
12:04:58 9 financial analysis by you?

12:05:00 10 A. Yes. One would prepare a substantial
12:05:07 11 analysis to examine the business. But what happened
12:05:13 12 in the case of Lincoln is from the time that I was
12:05:18 13 engaged as a consultant and began to write the report
12:05:21 14 that you're questioning about, a regulatory action
12:05:27 15 level event occurred.

12:05:28 16 Q. What does that mean?

12:05:30 17 A. There was some discussion this morning
12:05:33 18 about risk-based capital. Risk-based capital, which
12:05:39 19 was promulgated by the National Association of
12:05:42 20 Insurance Commissioners pursuant to the Model Act of
12:05:44 21 1983 -- excuse me, 1993 -- is a model which
12:05:55 22 determines, based on the type of business, meaning
12:05:58 23 insurance business, and the various elements of the

12:06:03 1 balance sheet, what the appropriate level of capital
12:06:06 2 should be.

12:06:09 3 Insurance companies have been
12:06:13 4 grappling with the issue of capital adequacy for many
12:06:16 5 years. But incidents of insurance insolvencies is
12:06:20 6 quite substantial. And the intent of developing this
12:06:27 7 risk-based capital was to provide a guidepost to
12:06:29 8 regulators in both determining capital adequacy, as
12:06:32 9 well as intervention potentials if levels of capital
12:06:40 10 declined.

12:06:42 11 Q. You used the term "capital adequacy." What
12:06:46 12 does that mean?

12:06:46 13 A. "Capital," first of all, is a generic term.
12:06:50 14 But in insurance-speak, it's surplus. And "surplus,"
12:06:55 15 I might note, is shorthand for the technical term of
12:07:01 16 policyholder surplus. So when insurance business is
12:07:07 17 referred to in terms of capital, the word "capital"
12:07:11 18 and the word "surplus" are interchangeable words.

12:07:15 19 And I might note for the record,
12:07:18 20 because we'll be discussing it a bit later, that the
12:07:21 21 word "net assets" or "member balances" all mean
12:07:25 22 capital. It does not mean reserves.

12:07:28 23 Q. Okay.

12:07:29 1 A. So going back to the risk-based capital,
12:07:33 2 when that act was promulgated by NAIC, they have
12:07:38 3 certain triggers. First of all, under the risk-based
12:07:43 4 capital, I might note that there are different
12:07:47 5 formulations that are required, depending on the
12:07:51 6 business.

12:07:51 7 So property and casualty has a
12:07:55 8 different mathematical configuration for determining
12:07:58 9 its capital adequacy than does healthcare. And both
12:08:03 10 of those have a different mathematical calculation
12:08:07 11 for capital adequacy than does a life insurance
12:08:11 12 company.

12:08:11 13 Notwithstanding the different
12:08:13 14 calculation methodologies, a company is deemed to be
12:08:18 15 capitally -- sufficiently capitalized if its RBC
12:08:24 16 ratio is 200 percent or higher.

12:08:27 17 Now, so that I don't confuse the
12:08:30 18 numbers, sometimes RBC is referred to as a percentage
12:08:34 19 and sometimes it's referred to in decimal notation.
12:08:38 20 So if I were to convert 200 percent to a decimal, it
12:08:42 21 would be 2.0.

12:08:45 22 The second aspect of risk-based
12:08:49 23 capital is something called the authorized control

12:08:54 1 level.

12:08:55 2 Q. What does that mean?

12:08:56 3 A. The authorized control level -- again,
12:08:59 4 going back to this methodology, this mathematical
12:09:02 5 formula that's used -- is a calculation used to
12:09:08 6 determine the hypothetical amount of capital a given
12:09:14 7 insurance company needs.

12:09:15 8 So again, hypothetical. And it was
12:09:21 9 the decision of the NAIC and its advisors that to
12:09:25 10 create a margin of comfort, that two times the
12:09:31 11 authorized control level would provide a sufficient
12:09:35 12 capital structure to support a given insurance
12:09:38 13 business.

12:09:40 14 So ACL, or authorized control level,
12:09:43 15 equals 100. And then when we say an RBC of 200
12:09:48 16 percent, we're simply saying twice the authorized
12:09:52 17 control level.

12:09:53 18 Q. Twice the hypothetical need?

12:09:56 19 A. The hypothetical level of capital needed.
12:10:00 20 A regulatory action level event is -- first, is if
12:10:06 21 you fall below 200 percent, the regulators will
12:10:11 22 require you to file a plan how you will restore the
12:10:17 23 capital so that the capital RBC calculation is

12:10:24 1 200 percent again or more. Then --

12:10:29 2 Q. Let me just ask, have you filed those kinds
12:10:31 3 of plans?

12:10:32 4 A. Yes.

12:10:32 5 Q. And sometimes are they as simple as, Next
12:10:35 6 year's premiums will be higher?

12:10:38 7 A. Unfortunately, when I usually get involved
12:10:40 8 in insurance companies, it's sort of the story of
12:10:42 9 being in the -- a big city emergency room. And that
12:10:47 10 is to say that the damage has been done before I pop
12:10:51 11 up on the scene. It's been so substantial that I'm
12:10:54 12 already into the regulators, not as a, Let's make it
12:11:01 13 a better story, which would portend that this would be
12:11:03 14 a continuing underwriting situation, but rather that
12:11:07 15 the company is not going to make it as an underwriting
12:11:10 16 company, and therefore, it's going to go into a runoff
12:11:14 17 or a formal proceeding.

12:11:15 18 Q. Okay.

12:11:16 19 A. So what happens, going back to the earlier
12:11:17 20 question of writing a report for the board of
12:11:20 21 Kingsway, because of the regulatory event that
12:11:23 22 occurred, it went from maybe writing an analysis to
12:11:29 23 now filing a formal runoff plan.

12:11:31 1 Now, the statute doesn't call it a
12:11:34 2 runoff plan. But effectively that's what it is.
12:11:36 3 It's demonstrating to the regulators how a particular
12:11:41 4 company can be run off successfully so that all of
12:11:46 5 the contractual obligations, as defined by policies
12:11:49 6 of insurance, can be fully discharged.

12:11:52 7 So that runoff plan was filed in the
12:11:54 8 case of Lincoln General.

12:11:57 9 Q. I interrupted you when you were describing
12:11:59 10 what happens when you reach the RBC of 200 percent.
12:12:06 11 There are other standards in that RBC category that
12:12:10 12 result in different kinds of regulatory actions.

12:12:13 13 Would you just quickly describe them.

12:12:15 14 A. Yes. If the RBC falls below 100 percent,
12:12:20 15 theoretically -- and the statute provides -- the
12:12:23 16 regulator could intervene in the business of that
12:12:27 17 insurance company and put it into proceeding. I've
12:12:28 18 never seen that happen. I won't say that it's never
12:12:30 19 happened. But at the minimum it would be quite
12:12:32 20 unusual.

12:12:32 21 As the RBC continues to decline and
12:12:36 22 falls below 70 percent, then the RBC statute in most
12:12:42 23 states requires the regulator to intervene in that

12:12:46 1 business. The level of intervention is at the
12:12:51 2 discretion of the regulator. It may need to place
12:12:53 3 the company into a formal rehabilitation. It may be
12:12:56 4 to place the company into insolvency. Or it may
12:13:01 5 involve placing the company into a conservatorship,
12:13:05 6 which is the least severe of those three options.

12:13:11 7 Q. We're talking about RBC because it's part
12:13:15 8 of insurance regulation statutes, correct?

12:13:18 9 A. When the Model Act was promulgated in 1993,
12:13:27 10 RBC, substantially in the form as promulgated by the
12:13:30 11 National Association of Insurance Commissioners, was
12:13:33 12 adopted by all 50 states. New York and the
12:13:39 13 Superintendent of Insurance for the State of New York
12:13:41 14 took a slightly different variation. But in
12:13:45 15 conceptual construct, it's the same thing.

12:13:49 16 Q. And in all of those states where there are
12:13:52 17 insurance carriers domiciled, those insurance carriers
12:13:54 18 have to use this RBC methodology for their --

12:13:59 19 A. It's not discretionary.

12:14:00 20 Q. You understand in this case, the Local
12:14:04 21 Government Center has been given an exemption from
12:14:07 22 all insurance regulation if they comply with the
12:14:11 23 standards of RSA 5-B, correct?

12:14:14 1 A. There was no obligation of the health
12:14:22 2 trusts to adopt RBC as a basis for calculating
12:14:27 3 capital adequacy. It did so for its own choosing.
12:14:31 4 There are other capital methodologies that could have
12:14:35 5 been used to determine the appropriate level of
12:14:38 6 capital. But in the case of HealthTrust, they did
12:14:43 7 adopt RBC and did apply it in a manner consistent
12:14:48 8 with the NAIC Model Act.

12:14:50 9 Q. And so let me just ask you on this point.
12:14:55 10 If I represent to you that the minutes of HealthTrust
12:15:00 11 and the Local Government Center reflect that they had
12:15:04 12 an RBC of between 2.1 and 2.5 before they voted to
12:15:12 13 enhance the member balance amounts, if they had been
12:15:17 14 required to use RBC, that would have been an
12:15:22 15 acceptable level of capital?

12:15:25 16 A. Again, the presumption is that in an RBC of
12:15:30 17 200 percent or better, the regulatory community, all
12:15:36 18 right, would determine or conclude that the level of
12:15:39 19 capital is sufficient. Again, absent some unique
12:15:43 20 aspect that might warrant a different answer.

12:15:47 21 Q. It sounds as though you have extensive
12:15:50 22 experience as a practitioner working with RBCs?

12:15:54 23 A. I do.

12:15:55 1 Q. Pick up with what happened with Fairfax.
12:16:06 2 Kingsway, I'm sorry.

12:16:07 3 A. When Kingsway's regulatory action level
12:16:10 4 occurred, the gears shifted and instead of, again,
12:16:13 5 writing a report about options, I had to file a
12:16:16 6 report which became the runoff plan. And that had to
12:16:23 7 be submitted -- first it was approved by the company,
12:16:25 8 and then -- the holding company, Kingsway -- and by
12:16:29 9 the respective board of directors. And then that
12:16:31 10 plan was submitted to the Department of Insurance for
12:16:36 11 the State of Pennsylvania.

12:16:39 12 At this particular point, I'm still a
12:16:41 13 consultant. There was some discussion with the
12:16:48 14 Department about my coming in to run the company.
12:16:51 15 That was still in the works. But as a consultant, I
12:16:55 16 appeared before the Pennsylvania Insurance Department
12:16:57 17 to explain all of the elements of the runoff plan and
12:17:03 18 to invite any potential changes that the Department
12:17:06 19 may require or desire.

12:17:14 20 Q. And what happened after that?

12:17:15 21 A. The Board of Directors of Kingsway asked me
12:17:19 22 to run the runoff, to manage the runoff of the
12:17:25 23 Lincoln General Insurance Company. There were a lot

12:17:28 1 of discussions. I had put the chances of that runoff
12:17:33 2 being successful at about 50/50. So I wasn't
12:17:35 3 particularly keen on taking on the assignment. I'll
12:17:41 4 spare the details.

12:17:42 5 Ultimately, an arrangement was worked
12:17:44 6 out. I brought in one of the fellows who works for
12:17:47 7 me under the banner of a company by the name of
12:17:51 8 Rockwall Financial Advisors, LLC, which was the
12:17:55 9 contracted party to manage the runoff of Lincoln.
12:17:59 10 And I served as the chairman of the board of that
12:18:02 11 insurance company. And in a somewhat unique
12:18:07 12 situation, in addition to serving as the chairman of
12:18:11 13 the board, the claims function for that company
12:18:13 14 reported to me, not to the CEO.

12:18:18 15 Q. And those claims were of what nature?

12:18:19 16 A. Mostly long-haul trucking, nonstandard
12:18:24 17 auto, and fleet -- you know, vans, buses, taxies.

12:18:30 18 Q. Property-casualty-type coverage?

12:18:33 19 A. It's all considered P&C. It's mostly
12:18:36 20 dedicated in a fairly finite area of the business.

12:18:41 21 Q. How did things end with Lincoln?

12:18:45 22 A. The incumbent board -- unfortunately,
12:18:49 23 because of the company going to runoff, most of the

12:18:53 1 directors -- or in fact, all of the directors
12:18:56 2 resigned except for four of us. Two incumbent
12:19:04 3 directors that represented the then-president and CFO
12:19:06 4 of the company, myself, and another Rockwall fellow
12:19:10 5 who was the CEO of the company. And almost
12:19:14 6 immediately we got into issues associated with the
12:19:21 7 directors -- both adding more directors, as well as
12:19:26 8 choice of consult.

12:19:27 9 And in the midst of that battle,
12:19:30 10 Kingsway did something that was unprecedented in the
12:19:32 11 history of insurance. It donated the stock of
12:19:37 12 Lincoln General's immediate parent to 20 New York
12:19:42 13 City-based charities. That occurred on October the
12:19:46 14 19th, 2009. It was done as a prophylactic measure.
12:19:53 15 The Pennsylvania Insurance Department was making
12:19:56 16 noises about Kingsway putting capital -- additional
12:20:00 17 capital into Lincoln General. I believe that
12:20:03 18 Kingsway decided to cut off that possibility by
12:20:07 19 donating the stock.

12:20:11 20 Q. What did the stock donation do to you?

12:20:13 21 A. It was a breach of the runoff management
12:20:17 22 agreement. The agreement was a tripod agreement
12:20:20 23 between Rockwall, Lincoln General, and Kingsway.

12:20:23 1 There was a provision in the agreement with respect
12:20:27 2 to change of control. It required Kingsway to own
12:20:30 3 100 percent of Lincoln stock during the pendency of
12:20:35 4 the runoff agreement, which was five years. And as a
12:20:39 5 result of the donation of the stock, it breached the
12:20:42 6 contract.

12:20:44 7 Q. Was there ultimately a suit between you and
12:20:49 8 Kingsway?

12:20:50 9 A. Not a suit. What happened was, is that the
12:20:56 10 breach of the contract resulted in the claim of
12:21:00 11 Rockwall as against Kingsway for \$21 million. That
12:21:05 12 claim then created a potential conflict of interest
12:21:12 13 for me with respect to my position on the board.

12:21:17 14 I brought the claim to the attention
12:21:21 15 of the other board members, other non-Rockwall board
12:21:26 16 members and to the outside lawyers and to the
12:21:28 17 regulators, that in my judgment I had a substantial
12:21:33 18 conflict and took the position that I needed to
12:21:35 19 recuse myself from any decisions that touched upon
12:21:39 20 Kingsway.

12:21:43 21 Q. And were you allowed to remain on the
12:21:45 22 board?

12:21:46 23 A. The incumbent directors took the position

12:21:49 1 that because of my conflict, I could not serve as a
12:21:52 2 director. It changed legal counsel and brought in
12:21:59 3 new lawyers. Those new lawyers took the position
12:22:03 4 that I could not serve in light of my conflict. That
12:22:08 5 ultimately led to my termination as the chairman.
12:22:12 6 The CEO was also terminated. And the contract was
12:22:17 7 unilaterally terminated.

12:22:19 8 They then ordered a declaratory
12:22:23 9 judgment action to have the court make a finding that
12:22:26 10 determinations both individually and corporately were
12:22:29 11 appropriate. We countersued for exactly the opposite
12:22:33 12 reasons. That is, the conflict did not require me to
12:22:36 13 step down, et cetera.

12:22:37 14 Q. Ultimately was there a confidential
12:22:40 15 settlement reached in that lawsuit?

12:22:41 16 A. There was.

12:22:44 17 Q. After that was resolved -- and by the way,
12:22:52 18 International and Resolution were physically located
12:22:56 19 in Manchester, and RiverStone --

12:22:59 20 A. Well, for the preponderance of the early
12:23:03 21 years, it was located in Chicago. I was getting
12:23:05 22 ready to retire in 2000. And so I moved the company
12:23:10 23 from Chicago to Manchester, New Hampshire.

12:23:14 1 Q. And RiverStone is still in --

12:23:17 2 A. It's still here in New Hampshire, in
12:23:19 3 Manchester.

12:23:20 4 Q. After the experience you had with Lincoln
12:23:27 5 and Kingsway, did you go on to manage other companies?

12:23:31 6 A. No. With that -- Well, after concluding
12:23:35 7 the litigation between Rockwall and Lincoln, I then
12:23:40 8 focused on the arbitration between Rockwall and
12:23:43 9 Kingsway where the \$21 million claim rested. That
12:23:49 10 was an arbitration proceeding, and that matter settled
12:23:54 11 in due course. Once that was completed, I retired in
12:23:58 12 December of 2010.

12:23:59 13 Q. And have you stayed retired at this time?

12:24:02 14 A. Other than this engagement.

12:24:06 15 Q. It's probably evident from the positions
12:24:11 16 you've held, but let me ask you if you could, in
12:24:15 17 short summary form, describe for us the particular
12:24:19 18 training and experience that you've had relevant to
12:24:25 19 financial analysis, to understanding balance sheets
12:24:29 20 and income statements, particularly how it relates to
12:24:31 21 the work you did in this case.

12:24:33 22 A. I mentioned that I had spent a couple years
12:24:38 23 in the commercial credit function. The commercial

12:24:41 1 credit department, as I also mentioned, is sort of
12:24:43 2 the training ground for future lending officers. You
12:24:48 3 start off at a very fundamental level, spreading
12:24:55 4 financial statements to a common sheet, sort of a
12:24:57 5 spreadsheet. You learn the basic concepts of a
12:25:00 6 balance sheet and an income statement. You learn
12:25:02 7 various accounting practices that may have relevance
12:25:07 8 with respect to financial reporting. You understand
12:25:09 9 and learn cash flow analysis.

12:25:10 10 That whole process may take well over
12:25:12 11 a year. And then after the year's time, you tend to
12:25:18 12 specialize. So in my case I specialized in lending
12:25:23 13 to REITs, real estate investment trusts. I also
12:25:27 14 specialized in finance companies. And I also became
12:25:31 15 proficient in analyzing Fortune 100-type companies,
12:25:37 16 large conglomerates.

12:25:38 17 That kind of training then becomes
12:25:41 18 the hub or the cornerstone of everything you do as a
12:25:47 19 lending officer. That is to say, the fundamental task
12:25:49 20 of a lending officer, besides generating business, is
12:25:52 21 to make sure that the obligations and the loans are
12:25:55 22 going to be repaid. That's all about financial
12:25:57 23 analysis and credit.

12:25:58 1 I might also say that in my bankruptcy
12:26:01 2 practice, again, financial skills are very substantial.
12:26:06 3 You're evaluating the plan of reorganization. And
12:26:11 4 before that you're trying to decide perhaps how the
12:26:12 5 plan of reorganization might be shaped with respect
12:26:15 6 to distributions to various creditor classes. All of
12:26:18 7 that requires financial analysis.

12:26:23 8 And I would say virtually my whole
12:26:25 9 career, even though I switched from banking over to
12:26:27 10 insurance, because of the acuity of a runoff company
12:26:34 11 that may ultimately fail and go into an insolvency
12:26:38 12 proceeding, understanding precisely where you are
12:26:40 13 from a financial point of view is absolutely
12:26:43 14 critical.

12:26:46 15 Q. Same kind of question. With respect to
12:26:49 16 bankruptcy, which you mentioned you worked in and
12:26:53 17 around in a number of capacities, did you also have
12:26:57 18 to deal with your own fiduciary duties as a
12:27:04 19 potentially bankrupt organization and the fiduciary
12:27:07 20 responsibilities of other board members?

12:27:10 21 A. The answer is yes. I would say that the
12:27:16 22 issue of fiduciary duties is far more acute in the
12:27:21 23 context of a runoff company which may ultimately

12:27:25 1 fail. Consequently, I made sure that I had a very
12:27:33 2 firm grasp on all of the fiduciary duties and
12:27:37 3 obligations that a board needed to fulfill.

12:27:41 4 Early on in my career, I brought in
12:27:44 5 two large law firms to help guide in the form of a
12:27:51 6 memorandum all of the fiduciary duties that I ought
12:27:54 7 to be concerned with. That was LeBoeuf, Lamb &
12:28:01 8 Walters, then LeBoeuf Lamb, and then I think it
12:28:02 9 became Dewey LeBoeuf, and I think it's something else
12:28:06 10 today; probably the number one regulatory firm with
12:28:09 11 respect to insurance matters.

12:28:11 12 The other firm that I brought in was
12:28:16 13 Locke, Lord & Bissell. Their construct and their
12:28:20 14 guidance was different. Theirs was to look at issues
12:28:22 15 associated with insolvency; and that is, if an
12:28:27 16 insurance company became insolvency [sic], what are
12:28:28 17 some of the things that could be asserted as potential
12:28:29 18 claims against directors.

12:28:32 19 Q. So although you are not a lawyer, you are
12:28:36 20 experienced with fiduciary duties as a practitioner
12:28:40 21 in the business area?

12:28:43 22 A. I would consider myself to be someone who
12:28:46 23 is a student of fiduciary duties, who spent a lot of

12:28:51 1 time understanding it. I will say that as a
12:28:54 2 practical matter, whenever I take on the running of a
12:28:56 3 company, usually one of the first things I do is go
12:29:00 4 through with precision, what are the fiduciary duties
12:29:05 5 that a board of directors needs to discharge to meet
12:29:08 6 the higher standards associated with runoffs.

12:29:11 7 Q. Associated with --

12:29:12 8 A. Runoffs.

12:29:13 9 Q. Okay. In your spare time, Mr. Coutu, have
12:29:19 10 you managed to find time for elected or appointed
12:29:23 11 office?

12:29:24 12 A. I did. Prior to the Kingsway/Lincoln
12:29:30 13 engagement, after I retired with respect to the TIG
12:29:33 14 runoff, which was 2002, I ran -- I, first of all,
12:29:39 15 became a member of the Municipal Budget Committee for
12:29:42 16 the Town of North Hampton. And then that led to my
12:29:49 17 heading up the Labor Negotiating Committee with
12:29:53 18 respect to the Town as their negotiator for the
12:29:57 19 Police, Fire, and Highway Department contracts.

12:30:02 20 And then in due course, I ran for
12:30:06 21 office, Select Board, and was elected in 2008.

12:30:11 22 Q. As a person involved in collective
12:30:14 23 bargaining, did you have to deal with issues related

12:30:16 1 to insurance coverages, particularly health?

12:30:18 2 A. I did.

12:30:19 3 Q. And what was your involvement with respect
12:30:20 4 to healthcare coverage for public employees in North
12:30:25 5 Hampton?

12:30:26 6 A. I led the negotiating team for the Town for
12:30:29 7 five years. In healthcare over that course of time,
12:30:36 8 which would be 2008 to -- up until last year, I'd say
12:30:43 9 on an increasing note, healthcare became an ever-
12:30:46 10 higher issue with respect to negotiating an equitable
12:30:54 11 contract as between the Town as the employer and the
12:30:57 12 various unions as employees.

12:31:00 13 Q. Was there a single insurer for healthcare
12:31:04 14 during that time you were involved with collective
12:31:07 15 bargaining?

12:31:08 16 A. The only insurer for healthcare at that
12:31:11 17 time that I was involved -- and I think it's still
12:31:15 18 today -- was the HealthTrust of the LGC.

12:31:19 19 Q. And are you aware of North Hampton's
12:31:23 20 experience during that five-year period with respect
12:31:25 21 to health insurance rates?

12:31:26 22 A. There were two back-to-back increases which
12:31:31 23 occurred. And if my memory serves me right, I think

12:31:35 1 it was 27.3 percent and followed by an 18.6 percent
12:31:40 2 increase. I believe that those were 2009 and 2010
12:31:45 3 increases.

12:31:48 4 Second, it was the practice of the
12:31:53 5 HealthTrust to provide a so-called GMR, guaranteed
12:31:59 6 rate structure. And the applicable rate which
12:32:03 7 developed some months later historically would come
12:32:05 8 in less. In the case of 27.3 percent GMR, the actual
12:32:12 9 rate and the GMR were the same rate. There was no
12:32:16 10 economic benefit or lift.

12:32:19 11 Q. So in the course of negotiating with
12:32:21 12 firefighters, police officers, teachers, highway
12:32:25 13 people, you had to deal with a 27 percent health
12:32:28 14 insurance premium increase?

12:32:30 15 A. Again, the way the negotiations went was to
12:32:33 16 either change the program -- there are other programs
12:32:39 17 offered by LGC HealthTrust that have different
12:32:42 18 economics associated with it -- or alternatively go
12:32:47 19 with a different allocation of the premium course,
12:32:53 20 which for the collective bargaining agreement
12:32:57 21 purposes was 90 percent town and 10 percent employee.

12:33:03 22 So changing that dynamic, maybe
12:33:05 23 making it a 20, changing the plan, were part and

12:33:10 1 parcel of the negotiations with the labor unions.

12:33:13 2 Q. I take it that as a Budget Committee
12:33:16 3 member, the town wasn't particularly happy with
12:33:18 4 seeing 27 and 18 percent rises?

12:33:22 5 A. It was not. I might note that I resigned
12:33:29 6 from the board -- excuse me -- yes, the Select Board
12:33:34 7 in, oh, 2010. So I served about two years. And the
12:33:38 8 reason I stepped down, again, was because of the
12:33:40 9 litigation involving Lincoln General and the
12:33:43 10 arbitration involving Kingsway.

12:33:47 11 As those two issues got under control,
12:33:52 12 the Municipal Budget Committee came to me and asked
12:33:56 13 me if I would be willing to serve on a subcommittee
12:34:03 14 of the Budget Committee to analyze why the rates were
12:34:11 15 where they were, whether there was something unique
12:34:15 16 about North Hampton from a risk point of view. And
12:34:18 17 also to consider whether or not providing or obtaining
12:34:22 18 coverage away from HealthTrust was an option.

12:34:26 19 Q. And did you agree to serve on that
12:34:28 20 subcommittee?

12:34:28 21 A. I did.

12:34:29 22 Q. And tell us what you found.

12:34:32 23 A. What I found is I didn't know a whole lot

12:34:35 1 about HealthTrust's working operations. So I
12:34:41 2 initially compiled quite a long list of documents
12:34:44 3 that I thought needed to be reviewed to answer such
12:34:47 4 questions as what were the driving forces behind the
12:34:50 5 rate increases and some other related issues.

12:34:56 6 That list of documents was sent to
12:34:59 7 Mr. Fournier, who is the town administrator, then and
12:35:02 8 now, for the Town of North Hampton. And my
12:35:06 9 understanding is that that list was ultimately sent
12:35:11 10 to LGC to respond to.

12:35:13 11 Q. Was Mr. Fournier also on the Local
12:35:18 12 Government Center board?

12:35:19 13 A. At the time of the formation of the
12:35:23 14 subcommittee, he was. Was and still is. I believe
12:35:26 15 still is.

12:35:27 16 Q. So he was both a town administrator for
12:35:29 17 your town and an LGC board member?

12:35:32 18 A. Correct.

12:35:32 19 Q. So the request for documentation so you
12:35:36 20 could get an understanding goes to Mr. Fournier.
12:35:41 21 What happens from there?

12:35:42 22 A. Some documents come in. For the most part
12:35:44 23 the documents that I thought were more salient were

12:35:47 1 not produced. Based on some of the documents that
12:35:49 2 were produced, it triggered additional questions, and
12:35:53 3 a secondary list was generated by me, which went to
12:35:57 4 Mr. Fournier, which was sent to LGC.

12:36:00 5 Q. Let me ask you, were you doing any of this
12:36:02 6 in connection with the Bureau of Securities Regulation
12:36:06 7 at this point?

12:36:06 8 A. No, I was not.

12:36:08 9 Q. It was all on behalf of your town?

12:36:10 10 A. Right.

12:36:11 11 Q. What happens with the second request?

12:36:12 12 A. Again, some documents were provided, but
12:36:17 13 not what I would call the key and critical documents
12:36:21 14 that answered a number of questions -- oh, which
12:36:24 15 potentially could have answered a number of questions
12:36:26 16 that I had about the workings of HealthTrust.

12:36:28 17 Q. Can you give me some idea what those
12:36:31 18 missing documents might have revealed.

12:36:32 19 A. Oh, I wanted some information with respect
12:36:35 20 to incurred but not reported claims, IBNR. I wanted
12:36:41 21 information with respect to what I called at that
12:36:47 22 time dividends being made by HealthTrust up to LGC,
12:36:51 23 which has been re-characterized as distributions.

12:36:56 1 I had --

12:36:57 2 Q. Let me stop you. Are those now in the
12:36:59 3 context of this case strategic plan distributions?

12:37:03 4 A. Yes. They were explained to me. I might
12:37:06 5 mention that these document requests ultimately led
12:37:08 6 to a meeting between the Budget Committee -- the
12:37:12 7 budget subcommittee and two representatives from LGC,
12:37:18 8 which occurred on, I think, February the 11th of 2011.

12:37:27 9 Q. And who was there for the LGC?

12:37:28 10 A. Representing the LGC was Sandal Keefe who
12:37:33 11 was then and who still is, I believe, the chief
12:37:37 12 financial officer, and I think, deputy director. And
12:37:40 13 I believe it's pronounced Merelise O'Connor, who is
12:37:44 14 the program director for LGC.

12:37:48 15 Q. And were you able to satisfy your request
12:37:51 16 for information at this meeting?

12:37:55 17 A. I was not.

12:37:56 18 Q. Why not?

12:37:59 19 A. I can't say for sure. And please understand
12:38:02 20 that I was not interacting directly with LGC, but
12:38:06 21 through Mr. Fournier. So I'm not sure, and I can't
12:38:10 22 say just what of everything that transpired on the
12:38:16 23 budget subcommittee actually migrated over to LGC.

12:38:20 1 I just -- I don't have that factual knowledge.

12:38:21 2 I think there was -- fair to say
12:38:24 3 there was some disagreement between myself and my
12:38:30 4 characterization and how Ms. Keeffe characterized
12:38:35 5 this so-called strategic plan.

12:38:37 6 Q. What was that distinction?

12:38:38 7 A. I said that -- in my judgment that while
12:38:45 8 this was not a business model that involved the
12:38:50 9 ownership of stock -- again, the way this is
12:38:55 10 constructed is that the risk pools are owned by the
12:38:59 11 participating political subdivisions. Unlike a
12:39:03 12 typical parent/subsidiary model, the parent would own
12:39:09 13 100 percent typically of the stock of the underlying
12:39:13 14 subsidiaries.

12:39:14 15 And so it's not uncommon in the
12:39:17 16 corporate sense that dividends would be declared by
12:39:21 17 the subsidiaries and then sent upstairs to the
12:39:25 18 holding company.

12:39:27 19 So when I looked at the distributions
12:39:31 20 that were being made by healthcare -- again, I wasn't
12:39:37 21 focusing on the other risk pools at that time -- I
12:39:40 22 used the word and I characterized those distributions
12:39:43 23 as dividends.

12:39:45 1 Ms. Keeffe objected to the term and
12:39:48 2 said it's not a dividend. She said, These are
12:39:51 3 payments for the strategic plan. I said at the
12:39:55 4 meeting, What is the strategic plan? And while she
12:40:00 5 responded, it seemed to me that the strategic plan
12:40:07 6 was along the lines of the various businesses that
12:40:10 7 were being offered by the consolidated LGC entities.
12:40:17 8 And it seemed like that might have involved marketing
12:40:22 9 and other kinds of activities, most likely at the
12:40:24 10 holding company.

12:40:25 11 I did not realize at that time that
12:40:29 12 these dividends -- these distributions were going over
12:40:33 13 to the Workers' Comp Trust because, again, at that
12:40:37 14 time, I did not examine that particular risk pool.

12:40:42 15 Q. So you, at that time, simply saw the
12:40:44 16 distributions going from HealthTrust to the parent?

12:40:47 17 A. Correct. And in large amounts, which
12:40:50 18 questioned just what services were being provided as
12:40:53 19 consideration for these large distributions.

12:40:56 20 Q. Just -- I know we'll go through this in
12:40:58 21 more detail in a moment, but give us an idea of the
12:41:01 22 scale of those distributions you were seeing going
12:41:04 23 from HealthTrust to parent?

12:41:06 1 A. Three to five million. Of particular note
12:41:10 2 is that in 2009, the HealthTrust sustained a loss, if
12:41:18 3 my memory serves me right. We have the documents
12:41:20 4 here. But I think it's roughly \$8.4 million. And
12:41:24 5 the loss notwithstanding, there was a distribution
12:41:27 6 made that year -- and again, I think around \$4 million.
12:41:33 7 We have a chart on this, if we want to . . .

12:41:52 8 MR. VOLINSKY: Excuse me just one second.

12:41:54 9 THE PRESIDING OFFICER: Mr. Volinsky, you
12:41:56 10 are excused, but would you also tell me how much
12:41:59 11 longer you are considering going in this phase of
12:42:02 12 your inquiry of the witness?

12:42:04 13 MR. VOLINSKY: I would say 10 minutes and
12:42:08 14 that would be a very appropriate time to break, if
12:42:11 15 that's all right.

12:42:11 16 THE PRESIDING OFFICER: That's my thought.

12:42:14 17 MR. VOLINSKY: Okay.

12:42:20 18 THE WITNESS: In two thousand --

12:42:22 19 Q. BY MR. VOLINSKY: Go ahead.

12:42:23 20 A. In 2009 healthcare sustained a loss of
12:42:28 21 \$8.8 million, okay.

12:42:33 22 THE PRESIDING OFFICER: Do you have this in
12:42:34 23 a hard form that I might see?

12:42:36 1 MR. VOLINSKY: Yes. This is Exhibit --

12:42:38 2 THE PRESIDING OFFICER: There you go.

12:42:39 3 MR. VOLINSKY: -- 7 in your notebook. The
12:43:07 4 lower left --

12:43:07 5 THE WITNESS: I can show it right here.

12:43:08 6 I'm not sure where to stand. Let me see.

12:43:11 7 MR. VOLINSKY: Just hang on a second.

12:43:13 8 THE WITNESS: Oh.

12:43:13 9 THE PRESIDING OFFICER: Let me jump back in
12:43:15 10 and help you all with some structure.

12:43:17 11 MR. VOLINSKY: Yes.

12:43:17 12 THE PRESIDING OFFICER: The chart that
12:43:20 13 you're referring to has been marked for identification
12:43:23 14 as BSR Exhibit No. 7; is that correct, Mr. Volinsky?

12:43:30 15 MR. VOLINSKY: Yes. And I'd move to strike
12:43:31 16 the ID.

12:43:32 17 THE PRESIDING OFFICER: All right. And is
12:43:33 18 there any --

12:43:34 19 You're going to put this in, I assume?

12:43:36 20 MR. VOLINSKY: Yes.

12:43:37 21 THE PRESIDING OFFICER: Any objection?

12:43:47 22 MR. SATURLEY: I have no objection.

12:43:50 23 THE PRESIDING OFFICER: Seeing no

12:43:50 1 objection, it's admitted. And do we want to begin
12:43:51 2 the count now, or do we want to leave it as your
12:43:53 3 BSR 7 for admission as an exhibit?

12:43:58 4 MR. VOLINSKY: I would hope to leave it as
12:43:59 5 No. 7.

12:44:00 6 THE PRESIDING OFFICER: Thank you very
12:44:01 7 much.

12:44:01 8 Am I going to see this again in
12:44:03 9 another form from the respondents?

12:44:05 10 MR. SATURLEY: No. You're not going to see
12:44:06 11 this chart, your Honor. So I think the idea of
12:44:09 12 moving with the -- continuing with the designation as
12:44:12 13 it exists is by far the preference.

12:44:15 14 THE PRESIDING OFFICER: Very good. I just
12:44:17 15 wondered if I was going to see a sister number. So
12:44:19 16 this will be then BSR No. 7.

12:44:19 17 (BSR 7 admitted into evidence.)

12:44:23 18 THE PRESIDING OFFICER: Please proceed.

12:44:25 19 Q. BY MR. VOLINSKY: You were going to show us
12:44:26 20 the loss it --

12:44:27 21 A. Besides the size of the chart and the
12:44:30 22 limitation of the overhead, this is HealthTrust
12:44:33 23 No. 1. Number two, the column that I'm pointing to

12:44:35 1 is the year ending 12/31/2009. Down here is the net
12:44:40 2 income/loss. I might note just to be clear this is a
12:44:48 3 not-for profit enterprise so there are no taxes that
12:44:51 4 are being paid, federal or state. So this pretax
12:44:55 5 loss and post tax loss is actually the same number.
12:44:58 6 This is the \$8,774,000 loss that was posted in 2009.

12:45:07 7 And my comment was that notwithstanding
12:45:11 8 that HealthTrust lost money in 2009, it still paid to
12:45:16 9 LGC, the holding company, \$4,431,000.

12:45:25 10 Q. And while you're there, am I right to
12:45:28 11 understand that they paid \$6.54 million the year
12:45:31 12 before?

12:45:32 13 A. In 2008, they -- operations produced a
12:45:39 14 profit of \$7.7 million. And in addition to that,
12:45:46 15 there was a distribution made by HealthTrust to LGC
12:45:52 16 in the amount of \$6,545,000.

12:45:58 17 Q. And 2010, since this happens to be up?

12:46:01 18 A. 2010, operations produced a profit of
12:46:07 19 \$11,175,000. And again, there was a distribution
12:46:12 20 made by HealthTrust to LGC Holding Company,
12:46:20 21 \$3,875,000.

12:46:23 22 Q. Thank you. If you'll return to your seat,
12:46:27 23 I'll get this out of your way.

12:46:28 1 So as you're having this discussion
12:46:31 2 asking about the distributions, were you given
12:46:35 3 sufficient information to understand or explain why
12:46:37 4 the 27 percent and then 18 percent increases suffered
12:46:41 5 by your town in health insurance premiums?

12:46:44 6 A. There was -- when I received -- and I don't
12:46:47 7 remember exactly when it was received -- there is a
12:46:52 8 rating formulation that is used to establish the
12:46:56 9 rate. And the methodology for doing that, that
12:46:59 10 template, as it were, was given to me. So I was able
12:47:04 11 to discern based on the template what elements were
12:47:10 12 being considered.

12:47:11 13 But again, it was a template. I don't
12:47:14 14 recall receiving the actual figures that supported
12:47:17 15 the 27.3 and the 18.6 premium increases.

12:47:23 16 Q. So let me ask you this. It sounds like, if
12:47:26 17 I'm understanding your testimony, you as a
12:47:28 18 representative of your town and your town were not
12:47:32 19 particularly happy with getting hit with these large
12:47:35 20 premium increases? Is that a fair statement?

12:47:39 21 A. Just to be clear, I was not serving in any
12:47:42 22 official capacity at that time. Again, my time on
12:47:45 23 the Budget Committee came to an end. My time as a

12:47:48 1 Select Board member had come to an end. So I'm
12:47:50 2 really a private citizen who is serving as an advisor
12:47:57 3 to the Municipal Budget Subcommittee.

12:48:00 4 Q. Okay.

12:48:00 5 A. The Budget Committee of North Hampton had
12:48:04 6 been concerned about the cost of healthcare for a
12:48:09 7 fairly considerable period of time, so these large
12:48:11 8 increases were not the first time that the Budget
12:48:14 9 Committee had on its radar screen the cost of
12:48:17 10 healthcare. It became an acute issue with the
12:48:21 11 increases that I've mentioned.

12:48:22 12 Q. So you heard during the opening statements
12:48:24 13 that the municipalities so like the Local Government
12:48:31 14 Center programs, that they stay year after year and
12:48:35 15 that's evidence of their acceptance, appreciation of
12:48:41 16 the Local Government Center. Did North Hampton
12:48:44 17 leave?

12:48:44 18 A. It did not, all right? It did leave LGC
12:48:58 19 Workers' Comp and joined Primex.

12:48:59 20 Q. Okay.

12:48:59 21 A. It did not leave healthcare.

12:49:03 22 Q. Why not?

12:49:04 23 A. The analysis that we're talking about,

12:49:06 1 okay, never really got completed -- and again, in
12:49:10 2 large measure because all the kinds of documents
12:49:13 3 necessary to do the kind of exhaustive analysis was
12:49:17 4 not something that was available through Steve
12:49:20 5 Fournier to me.

12:49:21 6 Second is there was -- there was at
12:49:26 7 least the concern that the ability to find
12:49:30 8 alternative coverage may not be available as a
12:49:35 9 capacity statement or may be available but at a rate
12:49:40 10 and price structure that may not be preferential to
12:49:43 11 what LGC or HealthTrust was charging. Again, that
12:49:46 12 was a concern. The homework had not yet been
12:49:50 13 completed.

12:49:51 14 The third issue was there's a
12:49:53 15 lockdown or lockout arrangement that is part of being
12:49:56 16 a member of LGC.

12:49:58 17 Q. What kind of arrangement?

12:49:59 18 A. A lockout.

12:50:01 19 Q. A lockout? Okay.

12:50:05 20 A. A lockout.

12:50:05 21 Q. What does that mean?

12:50:06 22 A. There's a provision that LGC has -- I think
12:50:09 23 it's in its bylaws -- that basically says if you

12:50:12 1 leave the program -- and I'm talking about healthcare
12:50:16 2 in this instance, okay? -- you cannot come back in as
12:50:20 3 a member of that pool for two years unless and until
12:50:25 4 the board of directors of LGC grants an exception for
12:50:30 5 you to come back in that pool. Absent that, absent
12:50:35 6 that, you're locked out for two years.

12:50:38 7 Additionally, you cannot, sort of, go
12:50:41 8 around LGC to go to Blue Cross Blue Shield directly
12:50:46 9 to obtain a quote for healthcare; part of the lockout
12:50:51 10 arrangement. So if one's going to begin the journey
12:50:55 11 of potentially leaving LGC, one has to understand
12:50:58 12 what the potential consequences were. So consequently,
12:51:02 13 work was beginning on what might be alternative
12:51:06 14 markets for North Hampton to consider, but that work
12:51:12 15 wasn't complete -- was not completed by me at least.

12:51:15 16 Q. And part of that consideration was the
12:51:17 17 understanding that North Hampton could not go to Blue
12:51:21 18 Cross because of the lockout. And if they left, they
12:51:25 19 were out for two years absent discretion of the board?

12:51:29 20 A. Right. Absent the board granting on an
12:51:33 21 exception basis the ability of the town to come back
12:51:35 22 in as a member of that risk pool.

12:51:38 23 MR. VOLINSKY: This would probably be an

12:51:39 1 appropriate time.

12:51:40 2 THE PRESIDING OFFICER: All right. Very
12:51:41 3 good. At this time we'll take a lunch recess,
12:51:44 4 returning at 2:00 p.m., where we'll pick up with this
12:51:48 5 same witness.

12:51:49 6 Counsel, you can leave your materials
12:51:55 7 here. And we'll see you at 2:00.

12:51:58 8 (Whereupon, at 12:52 p.m.,
12:52:02 9 the proceedings were recessed,
12:52:03 10 to reconvene at 2:00 p.m.
12:52:05 11 this same date.)

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AFTERNOON SESSION

(2:06 p.m.)

THE PRESIDING OFFICER: Good afternoon, ladies and gentlemen. We will reconvene after a lunch break. Mr. Volinsky has a witness, Mr. Coutu, on direct.

Please continue, sir.

MR. VOLINSKY: Thank you.

MICHAEL A. COUTU,

the witness at the time of recess, having been previously duly sworn, was further examined and testified as follows:

DIRECT EXAMINATION (continued)

BY MR. VOLINSKY:

Q. Mr. Coutu, did you ever attend any of those meetings that were mentioned this morning at Local Government Center?

A. I did.

Q. In what capacity?

A. The LGC has a seminar for newly elected Select Board members. I think it's called the Select Board Institute or words to that effect. And I attended it, I think within four or five months of

02:07:23 1 being elected.

02:07:24 2 Q. When you attended that seminar, did you try
02:07:26 3 to assist the Local Government Center around the
02:07:29 4 issue of municipal bank accounts?

02:07:42 5 A. First, I had a discussion with the program
02:07:45 6 director, whose name, I believe, was Jack Calhoun.
02:07:48 7 And the discussion I had with Jack was to share with
02:07:50 8 him some of the findings that I came across as a
02:07:53 9 newly elected official from the Town of North
02:07:57 10 Hampton. And he and I spoke, and that led to my
02:08:07 11 distributing through Jack a handout relating to the
02:08:10 12 professional security interest and collateralized
02:08:14 13 securities.

02:08:15 14 Q. Without going through much detail on that,
02:08:17 15 you found that North Hampton's bank accounts were not
02:08:21 16 collateralized at a time when banks were failing?

02:08:26 17 A. This was 2008. You know, the whole
02:08:28 18 financial meltdown was occurring. The failure of
02:08:31 19 banks in 2008 was unprecedented. There were 161
02:08:37 20 banks that had failed already. I was concerned that
02:08:39 21 the public funds of our town was properly protected,
02:08:45 22 investigated it, met with the banks that provide
02:08:49 23 various municipal services, and discovered that

02:08:54 1 notwithstanding the representation of the banks that
02:08:56 2 the public funds were properly collateralized, they
02:08:59 3 were not.

02:09:00 4 THE PRESIDING OFFICER: Mr. Volinsky, can
02:09:02 5 you tell me where we're going with collateralized
02:09:05 6 bank accounts of North Hampton?

02:09:06 7 MR. VOLINSKY: Yes.

02:09:07 8 Q. BY MR. VOLINSKY: Just real quickly, you
02:09:09 9 offered to help the Local Government Center get out
02:09:10 10 the word on this issue to its member municipalities?

02:09:13 11 A. I did. I had several conversations with a
02:09:16 12 Barbara Reed. I'm not sure what her position was.
02:09:19 13 I think working with communities and municipalities
02:09:23 14 on financial kinds of matters.

02:09:25 15 I shared with her the work product
02:09:27 16 that I had written about collateralization and
02:09:31 17 suggested that if North Hampton had that kind of
02:09:34 18 problem, since we're talking about the largest banks,
02:09:37 19 the three largest banks in the state, arguably other
02:09:41 20 towns, villages, and cities have comparable problems.

02:09:44 21 Q. Local Government Center ever take you up on
02:09:47 22 your offer to help?

02:09:47 23 A. No, they did not.

02:09:51 1 Q. You had at North Hampton a nonlapsing
02:09:58 2 account to deal with premiums for health insurance;
02:10:00 3 did you not?

02:10:00 4 A. We did.

02:10:01 5 Q. What did that account do?

02:10:02 6 A. It became clear to us that because the
02:10:09 7 HealthTrust provided a two-tiered rating scheme, that
02:10:15 8 to the extent the actual rate was lower than the
02:10:19 9 guaranteed maximum rate, and to the extent that the
02:10:23 10 budget for the town was based on the guaranteed
02:10:26 11 maximum rate, or GMR, then to the extent the voters
02:10:30 12 have approved the budget, then potentially there's a
02:10:35 13 windfall that arise in the delta between the actual
02:10:39 14 rate and the guaranteed maximum rate if, in fact,
02:10:44 15 that -- there was a positive result.

02:10:47 16 And I testified earlier that I
02:10:50 17 believe in respect of the 27.3 percent increase, the
02:10:53 18 GMR and the actual rate were the same. So that --
02:10:58 19 but for the most part, there was a positive variance
02:11:01 20 between actual and GMR.

02:11:03 21 Q. And so your town actually went through the
02:11:05 22 trouble to have a taxpayer-approved nonlapsing
02:11:10 23 account to hold these funds to use in later years

02:11:13 1 against premiums, correct?

02:11:14 2 A. It is. The actual final piece of that was
02:11:18 3 approved by the voters, I think I'd already stepped
02:11:21 4 down. My recollection is that the town administrator
02:11:25 5 makes a projection of what should go into that
02:11:27 6 account, and whatever that amount is. But the theory
02:11:31 7 is it's available to subsidize future healthcare
02:11:35 8 costs.

02:11:35 9 Q. So you were, at your town level, able to
02:11:40 10 create an account to subsidize future premium
02:11:43 11 payments for healthcare?

02:11:45 12 A. That was the intent of the program. I can't
02:11:47 13 speak to whether it's being done or --

02:11:49 14 Q. Because you've gone?

02:11:50 15 A. I stepped down in 2010.

02:11:51 16 Q. One last point. The issues that you're
02:11:54 17 about to talk about today concerning Local Government
02:11:58 18 Center's finances, have you ever offered to assist
02:12:01 19 the Local Government Center in straightening out the
02:12:05 20 issues that you see and that you'll talk about?

02:12:08 21 A. I have. As I've testified earlier, the
02:12:13 22 town administrator for the Town of North Hampton is a
02:12:17 23 Mr. Steve Fournier. Mr. Fournier also sits on the

02:12:23 1 LGC board.

02:12:24 2 When -- I'll say when Mr. Wingate's
02:12:28 3 report of August 2, 2011 was released, I had a number
02:12:35 4 of discussions with Mr. Fournier in the nature of
02:12:40 5 making suggestions or recommendations to him, such as
02:12:46 6 the board retaining independent counsel to vet the
02:12:50 7 assertions and allegations. And he, in turn, had
02:12:53 8 said to me that it was likely the board would have me
02:12:56 9 come in to work through all the technical issues and
02:13:01 10 help the board understand them.

02:13:04 11 Q. Did the Local Government Center ever take
02:13:06 12 you up on that offer?

02:13:07 13 A. It did not other than one meeting which
02:13:11 14 occurred in October of 2011. When I met with
02:13:20 15 Mr. Fournier in -- and -- I think his name is David
02:13:29 16 Caron --

02:13:30 17 Q. C-a-r-o-n?

02:13:33 18 A. C-a-r-o-n.

02:13:34 19 -- who is on the board. There was a
02:13:35 20 third gentleman who was supposed to be at the meeting
02:13:38 21 but couldn't make it at the last minute. I'm drawing
02:13:40 22 a blank on his name. The purpose of the meeting --
02:13:44 23 and this was all prefaced by my coming in to meet

02:13:47 1 with the board. And my understanding was that
02:13:49 2 Mr. Caron and this other gentleman, whose name, again,
02:13:54 3 I'm not recalling, wanted to get a sense of my view
02:13:56 4 of things. So we had the meeting on October the 5th.

02:13:59 5 And what I explained to Mr. Caron and
02:14:01 6 Mr. Fournier was issues associated with the level of
02:14:06 7 capitalization or surplus. And I contrasted that as
02:14:11 8 respects the investments and the duration of the
02:14:14 9 investments made by HealthTrust.

02:14:17 10 Q. Well, we'll get into that in a moment. Did
02:14:20 11 they take you up on your offer to help beyond that?

02:14:22 12 A. Well, Mr. Caron wrote me an email, I'm
02:14:27 13 going to say a week or so later, and attached a
02:14:33 14 report that was written by Milliman. Milliman is
02:14:40 15 one, if not the largest, actuarial consulting firm in
02:14:44 16 the U.S. And the Milliman report, in effect, was
02:14:49 17 seeking to support, maybe even justify the level of
02:14:54 18 RBC that HealthTrust was utilizing. And Mr. Caron
02:15:02 19 asked me to, in effect, evaluate their evaluation,
02:15:06 20 which I did.

02:15:07 21 Q. Which you did?

02:15:07 22 A. In writing, correct.

02:15:10 23 Q. Were you in communications at all with the

02:15:12 1 Bureau during the summer/fall of '11?

02:15:20 2 A. I sent an email to Mr. Earle Wingate, I'm
02:15:23 3 going to say within a week or so of the report that
02:15:26 4 he wrote or his department wrote, which, again, was
02:15:30 5 October 2, 2011.

02:15:35 6 Q. And did Mr. Wingate have you come in and
02:15:37 7 help the Bureau?

02:15:38 8 A. No, he did not.

02:15:39 9 Q. When was the first time that you were
02:15:41 10 contacted substantively by anyone to get involved and
02:15:44 11 work through the finances of this organization?

02:15:50 12 A. The first -- the first time I was contacted
02:15:52 13 was by yourself. And that occurred, I believe, the
02:15:58 14 third or fourth week of January this year.

02:16:01 15 Q. Let's switch topics. I want you to -- as a
02:16:06 16 preface to your financial analysis, I want you to
02:16:08 17 explain to us the LGC landscape as you understood it
02:16:15 18 and as it will relate to the specific financial
02:16:18 19 analysis that you're going to describe for us.

02:16:23 20 A. LGC underwent a substantive reorganization
02:16:31 21 in 2003. Prior to that time, it was cast as
02:16:39 22 separate -- independent with separate boards, meaning
02:16:41 23 trustees in respect of the two risk pools. In 2003 --

02:16:57 1 I should have said three risk pools. The third being
02:17:01 2 Workers' Comp Trust in about the year 2000.

02:17:04 3 The change which occurred in '03, the
02:17:07 4 reorganization was to follow a typical corporate
02:17:12 5 business model of a holding company/subsidiary
02:17:18 6 structure. I distinguished in my earlier comments
02:17:21 7 and testimony today that since these were not a stock
02:17:24 8 corporation, the somewhat nonconforming piece is the
02:17:30 9 fact that the holding company did not own, quote, the
02:17:33 10 stock of the risk pools. Indeed, the risk pools are
02:17:37 11 owned by the participating members.

02:17:40 12 In going through all of the related
02:17:44 13 materials, my observations is that, number one,
02:17:50 14 HealthTrust has been a very successful operation.
02:17:54 15 I think it's been mentioned earlier that they have
02:17:56 16 approximately 85 percent of the state healthcare.
02:18:02 17 If you measure it in dollars and cents, in 2010,
02:18:06 18 the total premiums collected by healthcare were
02:18:12 19 \$392 million.

02:18:15 20 If I contrast that against LGC on a
02:18:18 21 consolidated basis, meaning the other risk pools, on
02:18:23 22 a consolidated basis, LGC is \$415 million, again, in
02:18:29 23 2010. So by dint of the 392, HealthTrust really is

02:18:34 1 the story behind LGC, at least from a numbers point
02:18:38 2 of view, and represents 95 percent of 2010 revenues.

02:18:42 3 Therefore, most of my analysis and my
02:18:45 4 comments about the financials will be centered on
02:18:49 5 HealthTrust, although there are other points that
02:18:51 6 I'll be making with respect to the other risk pools.

02:18:54 7 Q. Let me pause you for a second. I drew a
02:18:58 8 real quick schematic in my opening. This is, as you
02:19:10 9 call it, a typical holding company --

02:19:13 10 A. Structure.

02:19:14 11 Q. -- structure. But ordinarily in a holding
02:19:20 12 company, all of the stock in the subs is owned by the
02:19:25 13 parent, correct?

02:19:26 14 A. Correct.

02:19:26 15 Q. And the distinction here is what?

02:19:28 16 A. Number one, there is no stock to evidence
02:19:32 17 ownership with respect to the subsidiary companies.
02:19:35 18 Number two, unlike a corporate parent/subsidiary
02:19:39 19 model, the legal owners of the three risk pools are
02:19:44 20 the participating members, not LGC holding.

02:19:48 21 Q. So the towns, cities, and school districts?

02:19:51 22 A. And counties.

02:19:52 23 Q. Counties. But in this holding company

02:20:00 1 model, the fiduciary responsibilities all go up to
02:20:05 2 the parent, correct?

02:20:08 3 MR. SATURLEY: Mr. Mitchell, at this
02:20:10 4 point --

02:20:11 5 THE PRESIDING OFFICER: Mr. Saturley.

02:20:12 6 MR. SATURLEY: -- at this point I'm going
02:20:14 7 to object to the questions that have been asked
02:20:17 8 recently and, I venture to guess that are about to be
02:20:21 9 asked, with regards to Mr. Coutu's qualifications to
02:20:24 10 answer legal questions about legal structure and
02:20:27 11 fiduciary duties with regards to corporate entities.

02:20:30 12 While he's been -- he's got numerous
02:20:32 13 credentials in a particular field, he's not a lawyer;
02:20:40 14 he's had no legal training; he's made no particular
02:20:44 15 study of 5-B.

02:20:45 16 To the extent that we've heard
02:20:47 17 anything about fiduciary duty, we've heard that what
02:20:50 18 he did was hire a great big law firm and then another
02:20:54 19 great big law firm to write him a long memo with
02:20:58 20 regard to fiduciary duties.

02:21:00 21 I do not believe he has been
02:21:02 22 sufficiently qualified to be offering legal opinions
02:21:04 23 with regards to the fiduciary duties and how they run

02:21:07 1 up and down in this particular structure, or indeed,
02:21:10 2 how they would work with regards to anything under
02:21:14 3 RSA 5-B.

02:21:17 4 THE PRESIDING OFFICER: Mr. Volinsky, do
02:21:18 5 you want to make your response from the microphone,
02:21:20 6 please.

02:21:21 7 MR. VOLINSKY: Sorry. Yes. I'll represent
02:21:23 8 to the hearing officer that I asked pretty much that
02:21:25 9 same question of Ms. Carroll, the executive director,
02:21:29 10 to get her understanding of how that fiduciary duty
02:21:33 11 runs --

02:21:33 12 THE PRESIDING OFFICER: Um-hum.

02:21:34 13 MR. VOLINSKY: -- and she told me that she
02:21:36 14 understands the parent does not own -- owe fiduciary
02:21:41 15 duties to the subs. It's the subs who owe it to the
02:21:45 16 parent.

02:21:45 17 I don't think this is a point that's
02:21:47 18 seriously contested, because of that deposition.
02:21:53 19 I don't think, given the absence of the Rules of
02:21:56 20 Evidence in this case, that this is a point on which
02:21:59 21 we should spend a whole lot of time.

02:22:03 22 THE PRESIDING OFFICER: I understand that.
02:22:04 23 But I believe Mr. Saturley's point, among other

02:22:08 1 things, was qualifications in law, qualifications
02:22:13 2 with respect to his experience or study, education in
02:22:23 3 fiduciary relationships. And you telling me that you
02:22:27 4 are asking what is a relevant question is the same as
02:22:35 5 me considering whether or not this gentleman has
02:22:37 6 special expertise in the area. So I need to hear
02:22:41 7 more from you.

02:22:42 8 MR. VOLINSKY: Yes. I offer this as a
02:22:44 9 practitioner, not as a lawyer. Mr. Coutu has
02:22:47 10 testified that he has acted and managed and been a
02:22:51 11 participant in numerous holding companies exactly in
02:22:55 12 this model. And he's also testified that he's been
02:22:59 13 very careful to understand the fiduciary relationships.

02:23:02 14 So I think as a practitioner
02:23:05 15 businessman in the field, he can offer his
02:23:08 16 understanding.

02:23:08 17 THE PRESIDING OFFICER: Okay. I'm going to
02:23:10 18 deny the objection. But I will assign appropriate
02:23:13 19 weight as he goes forward, and we'll see --

02:23:18 20 MR. VOLINSKY: Fair enough.

02:23:19 21 THE PRESIDING OFFICER: -- where he goes
02:23:20 22 when he gets to the statute.

02:23:24 23 MR. VOLINSKY: Fair enough.

02:23:27 1 THE PRESIDING OFFICER: Mr. Gordon?

02:23:30 2 MR. GORDON: Can I speak from here? Is that
02:23:32 3 appropriate?

02:23:33 4 THE PRESIDING OFFICER: I think you should
02:23:33 5 come forward just a little bit. You're far back
02:23:34 6 there in the back row.

02:23:34 7 MR. GORDON: One of the issues and following
02:23:37 8 up with what Mr. Saturley said is that I thought I
02:23:39 9 heard Mr. Coutu say -- give an opinion or a statement
02:23:43 10 about legal ownership. And I think that is a far
02:23:48 11 different cry than from his, I would say,
02:23:51 12 practitioner's view of what fiduciary duties are.

02:23:56 13 Precise testimony as to what legal
02:23:59 14 ownership interests are, I think are beyond his
02:24:01 15 expertise. And understanding your ruling, I would
02:24:04 16 suggest that he is not to weigh in on legal opinions
02:24:08 17 for which he's not qualified. If he wants to give
02:24:10 18 his practitioner's point of view as to what he did
02:24:14 19 and why he did it in his practice, but not to offer
02:24:19 20 legal opinions as to such things as ownership of
02:24:22 21 stock or interest in these entities.

02:24:26 22 THE PRESIDING OFFICER: Mr. Volinsky, any
02:24:27 23 response?

02:24:28 1 MR. VOLINSKY: That's fine. We won't have
02:24:31 2 him offer legal opinions about ownership.

02:24:33 3 THE PRESIDING OFFICER: Okay. So we will
02:24:37 4 strike the reference to legal ownership, and you can
02:24:41 5 ask your question in a different way, or you can
02:24:43 6 respond in a different way, Mr. Coutu. We'll proceed.

02:24:47 7 So Mr. Gordon, your objection is
02:24:52 8 granted as clarified.

02:24:55 9 MR. GORDON: One for one. Good.

02:24:57 10 THE PRESIDING OFFICER: Please be seated.

02:24:58 11 Mr. Volinsky.

02:25:00 12 MR. VOLINSKY: Okay.

02:25:05 13 Q. BY MR. VOLINSKY: Just very basic,
02:25:06 14 Mr. Coutu, fiduciary duties as a practitioner, they
02:25:09 15 run down from the parent or up to the parent?

02:25:13 16 A. The fiduciary duty of the board serves at
02:25:17 17 the local government level. The holding company
02:25:21 18 level is up, not down.

02:25:26 19 MR. VOLINSKY: I just wrote the word
02:25:27 20 "board" on here.

02:25:29 21 Q. BY MR. VOLINSKY: Let's go back to the
02:25:30 22 landscape. So you were describing what you
02:25:34 23 understood the size of the pool was driven by

02:25:39 1 HealthTrust with its 90 percent of premiums. After
02:25:47 2 the reorganization, they're in this model.

02:25:50 3 Can you, for us, compare in a general
02:25:53 4 way the activities of the Local Government Center
02:26:01 5 versus the activities of a true insurance company.

02:26:04 6 A. Notwithstanding the caveat that Chapter 5-B
02:26:09 7 makes clear that the LGC risk pools are exempt from
02:26:16 8 the insurance regulation and notwithstanding that
02:26:22 9 from just a technical point of view, they're not
02:26:26 10 insurance companies, if measured and examined from an
02:26:29 11 operating point of view, the kinds of activities that
02:26:36 12 LGC HealthTrust and insurance companies perform --
02:26:41 13 property and casualty specifically -- are literally
02:26:47 14 mirror imaged.

02:26:48 15 Number one, HealthTrust collects
02:26:50 16 premiums. Number two, it issues policies of
02:26:55 17 insurance or coverages. Number three, through a
02:27:01 18 third-party administrator -- in the case of
02:27:03 19 HealthTrust, Anthem, Blue Cross and Blue Shield --
02:27:09 20 settles and pays claims, the settlement being Blue
02:27:08 21 Cross Blue Shield; the payment coming from the
02:27:16 22 coffers of HealthTrust.

02:27:18 23 It has loss prevention programs that

02:27:23 1 go to the issue of mitigating loss as a sort of a
02:27:26 2 consulting service to insureds. They have -- to the
02:27:30 3 extent there is reinsurance involved -- and in the
02:27:34 4 past there has been reinsurance for HealthTrust, not
02:27:38 5 currently -- but it would purchase reinsurance and
02:27:41 6 then to the extent of losses meeting the threshold
02:27:48 7 requirements of reinsurance, it would cede those
02:27:52 8 losses, cede meaning to transfer those losses.

02:27:55 9 Q. So in all those aspects, HealthTrust acts
02:27:58 10 like an insurance company?

02:27:59 11 A. Just like it.

02:28:00 12 Q. You have experience managing insurance
02:28:02 13 companies?

02:28:03 14 A. Quite a few, yes.

02:28:09 15 Q. Talk to us now a little bit about the
02:28:10 16 nomenclature that we need to understand in order to
02:28:13 17 follow the financial analysis and what the Local
02:28:18 18 Government Center does in the course of its handling
02:28:19 19 of taxpayer money.

02:28:24 20 A. I testified earlier with respect to surplus
02:28:27 21 and pointed out that surplus is sort of the shorthand
02:28:32 22 term for policyholder surplus. I also made the
02:28:35 23 comment that surplus net assets and members' balances

02:28:39 1 all have the same meaning and in general financial-
02:28:45 2 speak, that would be referred to as capital.

02:28:47 3 I think the second term that's
02:28:48 4 helpful is an insurance term that's quite common.
02:28:53 5 It's been mentioned here at least once this morning:
02:28:57 6 "short tail" versus "long tail." You can take the
02:29:02 7 property/casualty issue and you can divide it into
02:29:06 8 two buckets: short tail. Short tail generally is
02:29:11 9 coverages in which the claims payout pattern -- that
02:29:15 10 is, the period of time it takes for claims to come
02:29:18 11 in -- is generally within 30 to 36 months.

02:29:23 12 Long tail is typically where the
02:29:28 13 claims manifestation period can be much longer. If I
02:29:31 14 use asbestos as an example, there were insurance
02:29:35 15 companies which insured companies that manufactured
02:29:41 16 asbestos products back in the 1920s, '30s, and '40s
02:29:46 17 when asbestos found its way as a common material in
02:29:52 18 building supplies: linoleum, siding, roofing shingles,
02:29:56 19 et cetera.

02:29:58 20 Because asbestos mineral was not
02:30:01 21 known to be hazardous to one's health, the claims
02:30:06 22 that arose from exposure to asbestos in many cases
02:30:11 23 did not manifest for 20-30-40 years after an

02:30:17 1 individual was exposed. So you had situations where
02:30:21 2 companies writing insurance in the '20s and '30s
02:30:25 3 ended up with losses that they paid in the '70s,
02:30:29 4 '80s, '90s, and later, once it could be proven that
02:30:34 5 the event -- that is, what gave rise to the exposure
02:30:38 6 to asbestos -- occurred in the '20s-30s as the case
02:30:43 7 may be.

02:30:44 8 Within the short tail bucket -- and
02:30:47 9 my comments, that's typically 30 to 36 months -- some
02:30:50 10 examples of short tail insurance coverage would
02:30:53 11 include auto, homeowners, and healthcare.

02:30:58 12 In the case of healthcare, the claims
02:31:03 13 manifestation period is generally two years or less.
02:31:11 14 And indeed, we have, I think, an exhibit that will
02:31:14 15 show what it is specifically for HealthTrust.

02:31:18 16 MR. VOLINSKY: Okay. That's a nice run-up
02:31:20 17 for me. So I will refer everybody to Exhibit 69,
02:31:24 18 which is the compilation of the consolidated and
02:31:28 19 nonconsolidated financial statements for the Local
02:31:34 20 Government Center and the subsidiaries.

02:31:44 21 THE PRESIDING OFFICER: Book 3?

02:31:46 22 MR. VOLINSKY: It is 69, which is Book 5 by
02:31:48 23 itself.

02:31:49 1 THE PRESIDING OFFICER: Book 5.

02:31:51 2 MR. VOLINSKY: 5. That book is all
02:31:59 3 financial statements. And I have added numbers to
02:32:11 4 the bottom of each page consecutively, starting from
02:32:17 5 1 going through 1,300, I think. And there should be
02:32:21 6 a table of contents at the beginning of it.

02:32:36 7 THE PRESIDING OFFICER: Give me a moment,
02:32:38 8 please.

02:32:39 9 MR. VOLINSKY: Yes.

02:32:40 10 THE PRESIDING OFFICER: There's only 1,300
02:32:42 11 or so pages in this exhibit. And I just want to
02:32:45 12 correlate that the exhibit number BSR 69 for
02:32:56 13 identification has Exhibit 1 within it?

02:33:00 14 MR. VOLINSKY: It has a number of exhibits
02:33:01 15 within it because this was used as a deposition
02:33:03 16 exhibit for Ms. Sandal Keeffe's deposition. So I
02:33:09 17 recopied it, left the other sticker on.

02:33:12 18 THE PRESIDING OFFICER: And everything then
02:33:13 19 that is in Exhibit 1 represents -- or falls within
02:33:18 20 the description you had in the table of contents?

02:33:20 21 MR. VOLINSKY: Yes.

02:33:28 22 THE PRESIDING OFFICER: Can I assume that
02:33:29 23 that goes through page 15?

02:33:33 1 MR. VOLINSKY: Exhibit --

02:33:34 2 THE WITNESS: Exhibit 69, sub 1?

02:33:37 3 MR. VOLINSKY: I don't remember if it's
02:33:38 4 broken up exactly that way. But the Keeffe exhibit
02:33:43 5 numbers are no longer relevant to this proceeding
02:33:47 6 other than to allow my colleagues to recognize that
02:33:51 7 that's where this exhibit comes from.

02:33:54 8 THE PRESIDING OFFICER: Okay.

02:33:55 9 MR. VOLINSKY: We'll use the numbers on the
02:33:56 10 lower right of each page --

02:33:59 11 THE PRESIDING OFFICER: Very good.

02:34:00 12 MR. VOLINSKY: -- so that we can keep
02:34:01 13 track.

02:34:02 14 And I would move to strike the ID on
02:34:04 15 69.

02:34:06 16 THE PRESIDING OFFICER: Okay. And moving
02:34:13 17 for admission at the same time?

02:34:15 18 MR. VOLINSKY: Yes, sir.

02:34:16 19 THE PRESIDING OFFICER: Any objection from
02:34:17 20 the respondents as to BSR Exhibit 69? Let me make
02:34:25 21 this --

02:34:27 22 MR. RAMSDELL: Can we take one second?

02:34:30 23 THE PRESIDING OFFICER: Sure. Let me make

02:34:31 1 one other observation. Can I assume further that if
02:34:36 2 there were to be objections, there can be objections
02:34:40 3 to the several sub-exhibits of BSR 69?

02:34:52 4 Has there been any discussion among
02:34:54 5 counsel with respect to that? All right. Then I'll
02:34:58 6 recognize Mr. Saturley who has risen for purposes of
02:35:00 7 being recognized.

02:35:01 8 MR. SATURLEY: Thank you, Mr. Mitchell.
02:35:04 9 LGC has no objection to the proffered content.

02:35:09 10 THE PRESIDING OFFICER: Understood.

02:35:10 11 MR. SATURLEY: However, I do want to make
02:35:11 12 it clear that we've not had an opportunity to check
02:35:13 13 whether or not these are complete. In other words,
02:35:19 14 the first --

02:35:20 15 THE PRESIDING OFFICER: Understood.

02:35:21 16 MR. SATURLEY: -- one, for instance, says
02:35:23 17 it's the consolidated financial statement. I have no
02:35:25 18 idea whether it's complete or not.

02:35:27 19 And secondly, there are other --
02:35:30 20 certainly other statements which we have tendered as
02:35:33 21 part of our exhibits. For instance, there's only --
02:35:37 22 a quick scan indicates there are only a couple of --
02:35:41 23 I'm not sure whether all of them are here.

02:35:45 1 THE PRESIDING OFFICER: Understood.

02:35:45 2 MR. SATURLEY: So as long as you're aware
02:35:47 3 that we're not sure they're complete and we do intend
02:35:50 4 to proffer others, so that I don't want this
02:35:54 5 recognized as the only financial statements that can
02:35:57 6 be used in this case, then I have no objection with
02:36:00 7 those caveats.

02:36:01 8 THE PRESIDING OFFICER: It's admitted then
02:36:02 9 as BSR 69.

02:36:02 10 (BSR 69 admitted into evidence.)

02:36:05 11 THE PRESIDING OFFICER: And I understand
02:36:05 12 that if you have an objection, you'll reiterate it
02:36:11 13 further in these proceedings. If you should find in
02:36:14 14 your review that these are not complete, as the fact
02:36:19 15 finder, I do not want to be left in the end with
02:36:23 16 competing financial statements without having you all
02:36:28 17 at my disposal to tell me which one is the complete
02:36:31 18 one.

02:36:31 19 So to the extent that you can
02:36:33 20 identify any holes that Mr. Volinsky might leave in
02:36:40 21 exhibit references, please just bring them to my
02:36:42 22 attention at the next convenience in the proceedings.

02:36:46 23 MR. SATURLEY: Happy to do so.

02:36:47 1 THE PRESIDING OFFICER: Will that fit?

02:36:48 2 MR. SATURLEY: That fits.

02:36:49 3 THE PRESIDING OFFICER: Very good.

02:36:50 4 Please continue, Mr. Volinsky.

02:36:52 5 Q. BY MR. VOLINSKY: If I may, let me turn you
02:36:54 6 to page 836. 836, well into the exhibit. And I've
02:37:07 7 put 836 up on the screen.

02:37:26 8 THE PRESIDING OFFICER: Go ahead.

02:37:30 9 Q. BY MR. VOLINSKY: We were talking about
02:37:31 10 short tail lines and how health is an example of a
02:37:34 11 short tail line. You mentioned a reference to the
02:37:41 12 10-year claims development of the Local Government
02:37:46 13 Center HealthTrust, correct?

02:37:47 14 A. Correct.

02:37:47 15 Q. In the financial statements, is there a
02:37:50 16 document called 10-year claims development?

02:37:55 17 A. The outside auditors for the preponderance
02:37:59 18 of the financial information that will be discussed
02:38:03 19 today is Berry Dunn McNeil. The financial information
02:38:10 20 includes the notes -- the financial statements,
02:38:13 21 balance sheet, income statement, reconciliation of
02:38:17 22 cash flows, notes of the financial statement.

02:38:19 23 There is an additional section to the

02:38:21 1 financial statement called supplementary information.
02:38:24 2 This piece, which is referred to as the 10-year
02:38:28 3 claims development schedule, is part of the
02:38:31 4 supplemental information prepared or included by
02:38:39 5 Berry Dunn in its audit financials for the year
02:38:44 6 ending December 31, 2010.

02:38:46 7 Q. So we can see the captions on the left of
02:38:53 8 836, do you see that?

02:38:55 9 A. Yes.

02:38:56 10 Q. Tell us how this relates to short tail
02:38:59 11 lines.

02:39:00 12 A. Let me start at Arabic 3, Estimated claims
02:39:04 13 and expense. And I just want to note very quickly
02:39:06 14 that back in 2001 and 2002 and 2003, all the way up
02:39:14 15 to 2008 -- if we can go back -- you'll see the word
02:39:21 16 "ceded claims." That simply means that they had
02:39:24 17 reinsurance. And so the claims, however that
02:39:28 18 reinsurance was put together, whether it was on an
02:39:31 19 individual loss basis or aggregate of the portfolio
02:39:35 20 of losses, I don't know. But clearly they ceded some
02:39:39 21 of these claims to the reinsurers. That's why in
02:39:43 22 Arabic 4, you have the word "net paid." "Net" means
02:39:48 23 net after giving effect to ceded claims.

02:39:51 1 Now, what this schedule does, it's a
02:39:55 2 very common display of losses. If you saw the whole
02:40:01 3 picture at one time, it's a triangular form picture,
02:40:05 4 okay? And if I start way over at the right, just so
02:40:09 5 that the audience has a sense of it -- it should be
02:40:12 6 2010, I believe, right? Yes. 2010. You only see
02:40:16 7 one number there because this was the 2010 financials.

02:40:19 8 And loss development, i.e., loss
02:40:22 9 claims coming in, this is what we call an
02:40:25 10 underwriting year in which the losses are still too
02:40:30 11 green. So all we have is losses being reported for
02:40:32 12 that one period, which is the policy period.

02:40:36 13 Q. And this is in thousands, so that's 345 --

02:40:40 14 A. \$345 million. Okay. So if we switch -- if
02:40:45 15 we toggle back to the left. Okay. Let's start with
02:40:51 16 the nomenclature. What this says is based on time --
02:40:57 17 can we show the top for a second.

02:41:00 18 Q. Yes.

02:41:00 19 A. 2001, all right -- now back down -- all
02:41:03 20 right. For policies issued in 2001 or underwriting
02:41:08 21 year 2001, all right, at the end of the policy
02:41:15 22 period, \$131 million of claims were paid. One year
02:41:23 23 later -- so that's one year after the policy period

02:41:26 1 expired -- again, this is a 12-month policy period,
02:41:30 2 all right? And I can't quite read it. I think it's
02:41:33 3 128? Am I reading it right? This number right here.

02:41:37 4 THE PRESIDING OFFICER: 126.

02:41:39 5 Q. BY MR. VOLINSKY: 126,479.

02:41:42 6 A. 126,479. Okay. Now, that went down
02:41:46 7 between this number and this number, and I'm guessing
02:41:48 8 there aren't any notes on the financial statements;
02:41:51 9 refunds, rebates, cancellations, other reasons caused
02:41:56 10 this claims paid to drop a bit.

02:41:58 11 And then two years later, it's
02:42:06 12 127,253, if I'm reading it correctly?

02:42:07 13 Q. Yes.

02:42:08 14 A. And then 127,253, 127,253. What that tells
02:42:13 15 you is that whenever I read a piece like that, there
02:42:19 16 are no new claims that came in beyond the second year
02:42:21 17 after the policy period.

02:42:23 18 The second thing that should be clear
02:42:25 19 is that the preponderance of the claims, the 131,
02:42:29 20 whatever it is, million, came in during the policy
02:42:33 21 period. There was a little bit of true-up one year
02:42:36 22 after the policy period. And then virtually no
02:42:40 23 change afterwards.

02:42:42 1 If I switch to 2002, which is this
02:42:45 2 next column -- is that 169? I can't --

02:42:51 3 Q. 169 and 163.

02:42:53 4 A. Again, 169. So there's more claims that
02:42:57 5 came in in the second year because there were more
02:43:00 6 writings, all right? There was a slight reduction in
02:43:04 7 the period one year after the expiry of the policy;
02:43:08 8 again, I'm assuming rebates, refunds. And then the
02:43:11 9 number stays flat for the remaining years. That,
02:43:13 10 again, says that after one year following the policy
02:43:15 11 period, there was no statistically significant claims
02:43:19 12 filed.

02:43:20 13 We can keep going the same way and go
02:43:22 14 through all 10 columns. What this tells you --

02:43:25 15 THE PRESIDING OFFICER: Excuse me just a
02:43:27 16 moment for clarification. You commented that the --
02:43:32 17 in the second year it dropped down again because of
02:43:37 18 the ceded or rebates --

02:43:39 19 THE WITNESS: Well, no, ceded would be up
02:43:41 20 here --

02:43:43 21 This is net paid. Rebates, refunds,
02:43:46 22 cancellations, other reasons.

02:43:47 23 THE PRESIDING OFFICER: If there had been

02:43:48 1 none, would that figure remain the same --

02:43:51 2 THE WITNESS: Yes.

02:43:52 3 THE PRESIDING OFFICER: -- year one, year
02:43:53 4 two, all the way through?

02:43:54 5 THE WITNESS: Well, they could have been --
02:43:56 6 this -- I think this is 2002 I'm looking at.

02:44:00 7 THE PRESIDING OFFICER: 2002.

02:44:01 8 THE WITNESS: There could be two things
02:44:03 9 going on here, Mr. Mitchell. There could have been,
02:44:07 10 (a), some new claims coming in, and (b), some
02:44:10 11 credits, all right? This is the net of that.

02:44:14 12 So I can't say from looking at this
02:44:15 13 chart that we got from 169 to 163 solely because of
02:44:22 14 credits and refunds and rebates. It may have gotten
02:44:26 15 there as the net of some additional claims that came
02:44:29 16 in and other refunds.

02:44:30 17 But once we got to the third year,
02:44:33 18 the second year following the expiry of the policy,
02:44:36 19 because it stays 163,720, they're out. I know that
02:44:40 20 from this point there were no further new claims that
02:44:43 21 came in.

02:44:46 22 THE PRESIDING OFFICER: Well, since it's at
02:44:47 23 the beginning, I'll belabor the topic. In 2001, so

02:44:51 1 that I understand what you would have me take from
02:44:55 2 these numbers, you'll see that the first three
02:44:58 3 numbers, 131, 126, and then it goes back up to 127
02:45:03 4 and stays constant.

02:45:05 5 THE WITNESS: Right.

02:45:05 6 THE PRESIDING OFFICER: And your
02:45:06 7 explanation for that was that they were rebates and
02:45:08 8 such that happened in year two that brought the
02:45:10 9 figure down to 126, right?

02:45:14 10 THE WITNESS: I'm -- that's my hypothetical
02:45:17 11 because there aren't notes and I'm only offering what
02:45:19 12 I believe may have happened.

02:45:20 13 THE PRESIDING OFFICER: All right. So for
02:45:23 14 some reason, it went to that number.

02:45:27 15 THE WITNESS: Right.

02:45:28 16 THE PRESIDING OFFICER: And then in year
02:45:31 17 three, it went to 127,253.

02:45:31 18 THE WITNESS: And became constant.

02:45:33 19 THE PRESIDING OFFICER: And it became
02:45:33 20 constant. In 2002, you indicated that in the second
02:45:35 21 year a similar event occurred -- again,
02:45:38 22 hypothetically -- but yet 163 stays constant
02:45:43 23 throughout.

02:45:47 1 THE WITNESS: Right. That's correct. In
02:45:48 2 this case --

02:45:49 3 THE PRESIDING OFFICER: Why don't I have
02:45:50 4 that middle step?

02:45:51 5 THE WITNESS: Because if there was, (a), no
02:45:53 6 additional claims that came in and no credits that
02:45:57 7 splash over into what would be the second year
02:45:59 8 following, then it just bottomed out, if I can use
02:46:03 9 that term, one year earlier in 2002 than it did in
02:46:07 10 2001.

02:46:08 11 THE PRESIDING OFFICER: Okay. I'll let it
02:46:10 12 go.

02:46:10 13 THE WITNESS: All right. In either case,
02:46:12 14 in either case, what this is telling you -- we could
02:46:14 15 do this every year -- is that, (a), the preponderance
02:46:17 16 of the claims comes in during the policy period. And
02:46:23 17 then you have some -- you know, some noise, if I can
02:46:25 18 call it that, occurring one year and two years -- in
02:46:30 19 this case two years; in this case one year -- after
02:46:33 20 the policy expired.

02:46:35 21 The import of this really is that
02:46:39 22 when these numbers repeat, it really tells you that,
02:46:43 23 (a), this is a very short tail line; that the claim

02:46:47 1 period, claims manifestation period, is mostly within
02:46:51 2 12 months, a little bit of dribble thereafter, all
02:46:56 3 right? And if I can use 2001 as an example, clearly
02:47:00 4 nothing was happening beyond the second year.

02:47:02 5 THE PRESIDING OFFICER: I see the noise in
02:47:03 6 2001, to use your term. I don't see the noise in
02:47:06 7 2002.

02:47:08 8 THE WITNESS: Only because of this factor:
02:47:10 9 169 versus 163.

02:47:11 10 THE PRESIDING OFFICER: But then all the
02:47:12 11 rest of them stay at 163.

02:47:14 12 THE WITNESS: That's correct.

02:47:15 13 MR. VOLINSKY: So it was even shorter
02:47:18 14 during '02 than in '01.

02:47:19 15 MR. HOWARD: Your Honor -- Mr. Mitchell,
02:47:22 16 it's fine for the witness to testify. We don't need
02:47:26 17 Mr. Volinsky to testify.

02:47:27 18 MR. VOLINSKY: We'll take as long as we
02:47:28 19 need to go step by step. I'm trying to be of
02:47:31 20 assistance, Mr. Mitchell.

02:47:32 21 THE PRESIDING OFFICER: That's quite all
02:47:34 22 right.

02:47:36 23 My question was that in explaining

02:47:39 1 year two in the 2001 column, the noise -- and you
02:47:48 2 know, you have hypotheticals for it, but "noise" is
02:47:51 3 good enough for me -- that occurred in the second
02:47:56 4 year, and then you've drawn our attention to the fact
02:47:59 5 that it plateaued out and stayed the same, which
02:48:02 6 meant no new claims.

02:48:04 7 Is that correct?

02:48:05 8 THE WITNESS: Yes, it is.

02:48:06 9 THE PRESIDING OFFICER: With respect to
02:48:07 10 2002, the second year is the number that stays
02:48:13 11 constant. Can I assume that in each one of those
02:48:18 12 years, there was no new claims?

02:48:21 13 THE WITNESS: Yes. And no noise.

02:48:23 14 THE PRESIDING OFFICER: Correct. So
02:48:24 15 there's no noise in 2002?

02:48:27 16 THE WITNESS: Other than within a policy
02:48:30 17 year, which is the 169, if I'm reading that
02:48:33 18 correctly --

02:48:34 19 THE PRESIDING OFFICER: Right.

02:48:34 20 THE WITNESS: -- and the 163. So there was
02:48:37 21 a little bit of noise in these two columns. Once it
02:48:41 22 hit one year after the expiration of a policy, from
02:48:45 23 that point to here it plateaued.

02:48:49 1 THE PRESIDING OFFICER: You can go forward,
02:48:51 2 Mr. Volinsky. Thank you very much.

02:48:54 3 Q. BY MR. VOLINSKY: Not to belabor it, the
02:48:55 4 next year you have noise for one year and then it
02:48:58 5 plateaus at 216?

02:49:02 6 A. Again, it's very hard for me to see the
02:49:05 7 numbers. But it's at 196 and 216. And then you'll
02:49:08 8 see it dropped a point between 4 and 3 and 3 and 2.
02:49:14 9 That is pretty statistically insignificant.

02:49:16 10 Q. And so this establishes by the
02:49:20 11 supplementary document to the financial statements
02:49:24 12 that HealthTrust is what you call short tail?

02:49:27 13 A. That's correct. And again, the thrust of
02:49:30 14 this exhibit is to demonstrate that it is short tail.
02:49:35 15 But to give meaning to that, number one,
02:49:39 16 preponderance of the claims come within the policy
02:49:42 17 period, within 12 months, and then a little bit of
02:49:42 18 dribble, noise, whatever you want to call it,
02:49:50 19 manifesting one year later. And at least in the case
02:49:53 20 of 2002, it was sort of a final story in one year.
02:49:58 21 There was no dribble and no noise in the second year.

02:50:01 22 Q. Thank you. Go ahead and sit down.

02:50:11 23 You were talking about nomenclature

02:50:14 1 and landscape, and I want to ask you about investment
02:50:19 2 portfolios in insurance companies.

02:50:26 3 A. Whether it's an insurance company or
02:50:28 4 corporation doesn't make much difference. But the
02:50:34 5 common rule of investments is that the liabilities
02:50:36 6 and the assets have to match up.

02:50:39 7 It is of particular importance in an
02:50:42 8 insurance company to ensure that you have cash and
02:50:45 9 cash equivalents in sufficient amounts to pay claims
02:50:49 10 when they become payable. That is, the claim's been
02:50:54 11 settled. The obligation to pay the claim is
02:50:56 12 determined. And the amount has been determined and
02:50:59 13 it needs to be paid.

02:51:01 14 So there are guiding factors with
02:51:04 15 respect to investments. In the insurance world --
02:51:07 16 and here I'm talking about the insurance world
02:51:10 17 generally speaking, not risk pool specifically -- the
02:51:15 18 overwhelming preponderance of investments are made
02:51:19 19 in, quote, marketable securities, end quote.

02:51:24 20 Marketable securities are those
02:51:25 21 securities that could be liquidated typically
02:51:29 22 overnight or within a day and converted from a
02:51:33 23 security to cash. Typical securities would include

02:51:37 1 U.S. government obligations. There are also
02:51:41 2 obligations that are commonplace that are referred to
02:51:44 3 as GSC, government-sponsored enterprise obligations.

02:51:52 4 Fannie Mac [sic], Freddie Mac would
02:51:55 5 be examples of GSCs. There's also something called
02:51:58 6 Ginnie Mae. Ginnie Mae, however, has full faith and
02:52:02 7 credit of the United States Government. It might --

02:52:04 8 Q. Let me stop you. Why do you need
02:52:07 9 marketable securities in the insurance business?

02:52:10 10 A. Liquidity.

02:52:11 11 Q. Why do you need liquidity?

02:52:16 12 A. Again, your securities are the cash to pay
02:52:23 13 claims tomorrow.

02:52:25 14 Q. Okay.

02:52:26 15 A. If your investments were in real estate, to
02:52:29 16 make a contrasting argument, you wouldn't be able to
02:52:33 17 liquidate the real estate literally overnight if you
02:52:38 18 needed the proceeds from that real estate to
02:52:41 19 discharge claim obligations. So the benefit of
02:52:46 20 marketable securities is that there is a secondary
02:52:49 21 market in which those securities could be sold and
02:52:52 22 converted to cash.

02:52:57 23 Q. So the business of insurance is in large

02:53:00 1 part to collect premiums and pay claims, and the
02:53:03 2 purpose of investments is to make sure that there are
02:53:05 3 funds available should the claims exceed the
02:53:12 4 premiums. And also is there a lag time in there
02:53:17 5 also?

02:53:17 6 MR. SATURLEY: I --

02:53:18 7 THE WITNESS: Between the --

02:53:21 8 MR. SATURLEY: I --

02:53:22 9 THE PRESIDING OFFICER: Go ahead,

02:53:24 10 Mr. Saturley.

02:53:24 11 MR. SATURLEY: Objection. Leading.

02:53:25 12 THE PRESIDING OFFICER: Well, it's an
02:53:26 13 administrative proceeding. We're going to proceed.
02:53:28 14 Denied.

02:53:30 15 Q. BY MR. VOLINSKY: Go ahead.

02:53:30 16 A. Between the time that the premium is
02:53:33 17 collected by the insurance company and the time that
02:53:36 18 it's paid out as a claim, insurance companies,
02:53:41 19 including HealthTrust, will invest those dollars in
02:53:44 20 various securities of various duration. The longer
02:53:50 21 the claims manifestation period, then the longer the
02:53:55 22 duration of those investments. By "duration," I mean
02:53:59 23 maturity.

02:54:00 1 So if I'm in the business of
02:54:03 2 insurance that's providing casualty coverage where a
02:54:07 3 claims manifestation period is 10 or 15 years, then
02:54:12 4 you would expect those investments to be invested for
02:54:15 5 a duration of 10 to 15 years.

02:54:18 6 Alternatively, if I insure automobiles,
02:54:22 7 then I may see those investments being a year, maybe
02:54:26 8 a year and a half, but not more.

02:54:28 9 Q. And if you were in another short tail line
02:54:31 10 like health, where should the investments be?

02:54:35 11 A. Well, when you look at the loss profile --
02:54:39 12 loss development profile 10 years, I made the
02:54:41 13 observation that the preponderance of claims
02:54:43 14 manifests within a policy period -- that's 12 months --
02:54:47 15 and some dribble and noise that was visible in the
02:54:50 16 second year, or the first year following the expiry,
02:54:54 17 and in one case -- 2002 -- and the second year
02:54:59 18 following the expiry of the policy.

02:55:02 19 Q. Have you made an analysis from the
02:55:04 20 financial statements of the maturity levels, maturity
02:55:07 21 durations of the investments held by LGC HealthTrust?

02:55:13 22 A. I have.

02:55:13 23 Q. Have you put together a table that we've

02:55:18 1 marked as BSR 9?

02:55:25 2 MR. VOLINSKY: So I'll refer everyone
02:55:26 3 to 9.

02:55:36 4 Q. BY MR. VOLINSKY: And is this your table?

02:55:37 5 A. Yes, it is.

02:55:38 6 MR. VOLINSKY: I move to strike the
02:55:39 7 identification on 9 and admit it as an exhibit.

02:55:43 8 THE PRESIDING OFFICER: Any objection?

02:55:46 9 No objection. Please proceed, and it
02:55:51 10 is admitted as --

02:55:51 11 MR. SATURLEY: I have no idea where this
02:55:52 12 information comes from. I don't know how he put it
02:55:53 13 together, so therefore, I do not assent.

02:55:55 14 THE PRESIDING OFFICER: Let's back up a
02:55:56 15 little bit. Give me a sign that you have an
02:56:01 16 objection before I go further. I understand you have
02:56:03 17 an objection now.

02:56:04 18 MR. SATURLEY: Yes, sir.

02:56:05 19 THE PRESIDING OFFICER: Would you please
02:56:05 20 restate it.

02:56:06 21 MR. SATURLEY: Yes, sir. I have an
02:56:07 22 objection to the admission of the table and the
02:56:10 23 striking of the identification since I have no idea

02:56:14 1 where the information came from nor how it was put
02:56:16 2 together.

02:56:17 3 THE PRESIDING OFFICER: You understand how
02:56:20 4 it was put together: by the witness, correct?

02:56:22 5 MR. SATURLEY: I heard that.

02:56:24 6 THE PRESIDING OFFICER: Okay. Mr. Volinsky,
02:56:25 7 would you please elicit where these figures came
02:56:28 8 from?

02:56:29 9 MR. VOLINSKY: Yes.

02:56:29 10 Q. BY MR. VOLINSKY: This table was in your
02:56:30 11 report; was it not?

02:56:31 12 A. It was.

02:56:32 13 Q. So it's been disclosed for months?

02:56:34 14 A. It has.

02:56:35 15 Q. Where did it come from?

02:56:37 16 A. The source of this information is the
02:56:40 17 audited financial statements for HealthTrust, in this
02:56:44 18 case for years 2008, 2009, 2010. And actually the
02:56:49 19 information was actually prepared by the outside
02:56:52 20 auditor, Berry Dunn McNeil & Parker.

02:56:58 21 THE PRESIDING OFFICER: Thank you.

02:56:59 22 MR. VOLINSKY: Thank you.

02:57:00 23 THE PRESIDING OFFICER: If that was an

02:57:01 1 objection, it was denied. And please proceed.

02:57:04 2 Q. BY MR. VOLINSKY: So this is HealthTrust's
02:57:08 3 investments '08-10. Would you please describe -- and
02:57:11 4 I'll move this as you need -- what's depicted on this
02:57:14 5 table.

02:57:19 6 A. Staying first with the left-hand notations,
02:57:23 7 nomenclature, these ranges referred to are the
02:57:27 8 maturities of the investment securities. The ranges
02:57:31 9 that have been captured in this exhibit are the same
02:57:36 10 ranges and amounts in a similar table that was
02:57:42 11 constructed by the outside auditors, Berry Dunn.

02:57:46 12 The first entry is not applicable.
02:57:48 13 The second entry is within one year. Then I have a
02:57:52 14 subtotal less than one year. The next one is one to
02:57:56 15 five. Berry Dunn did not create a more granular
02:58:02 16 table. That is, I don't know what's matured between,
02:58:04 17 let's say, more than one year and, let's say, less
02:58:07 18 than three years or less than two years. They grouped
02:58:09 19 it into one to five.

02:58:12 20 Then we have investments of five, but
02:58:14 21 less than ten years. And then we have investments
02:58:16 22 that are ten-plus years. Whether that's 15 years,
02:58:20 23 20 years, longer, I don't know. That information was

02:58:24 1 not detailed in the financial statement.

02:58:27 2 If we can, counsel, move to the
02:58:31 3 right. Conceptually, what I'm about to explain for
02:58:38 4 2010 applies to the two prior years, '08 and '09.
02:58:43 5 The math will be a little bit different and the
02:58:45 6 percentages will be a little different. But here
02:58:49 7 is -- these two buckets, which adds up to this
02:58:54 8 number: ten million one, are your very short-term
02:58:57 9 investments defined as those investments which mature
02:59:00 10 within a 12-month period from the statement reporting
02:59:06 11 date. So it's 12 months from 12/31/2010.

02:59:11 12 This next bucket is investments
02:59:13 13 between one and five. That is more than one year and
02:59:17 14 less than five years. This one here is between five
02:59:21 15 and ten. More than five, but less than ten. And
02:59:27 16 this last bucket is -- at 14.3, is ten-plus years.

02:59:34 17 Now, if we go back. Now, I've added
02:59:38 18 this number, 8.5 and 14.3, and that equals the 22.8.
02:59:45 19 And I would start off by saying that for a healthcare
02:59:52 20 short tail company to have investments going out five
02:59:57 21 to ten years, in this case ten-plus years, is, (a),
03:00:04 22 unusual; and (b), since those securities have such a
03:00:10 23 long investment maturity date, it tells me that

03:00:15 1 the -- that HealthTrust is not anticipating needing
03:00:20 2 those funds in the short run. The short run is
03:00:26 3 defined as 12 months from the statement date.

03:00:31 4 The same can be true here. We don't
03:00:34 5 have a breakdown other than to say it's more than one
03:00:39 6 and less than five. But as we demonstrated from the
03:00:44 7 claims loss development exhibit that was here earlier
03:00:50 8 before this one, the preponderance of the claims
03:00:52 9 mature within 12 months. So I would venture to bet
03:00:56 10 that this 12.9, which is the one to five corridor of
03:01:01 11 investments, is likely also funds not needed in the
03:01:05 12 short run. And short run is the 12-month period
03:01:10 13 following 12/31/10.

03:01:14 14 Q. So what is needed to satisfy the short-term
03:01:18 15 nature of this health insurance operation?

03:01:23 16 A. If I may answer one question before I get
03:01:26 17 to that one.

03:01:26 18 Q. Yes.

03:01:27 19 A. Because it wasn't on the screen. I just
03:01:29 20 want to show that there are some percentages that
03:01:32 21 have been calculated -- and if I can scroll to the
03:01:34 22 right, okay? Investments, first of all, ten-plus
03:01:39 23 years, 31.1 percent of the total invested portfolio

03:01:46 1 is excess of ten years. In the five to ten bracket,
03:01:52 2 50 percent of HealthTrust's invested assets are
03:01:57 3 invested in securities in excess of five years, but
03:02:01 4 less than ten years of maturity -- ten years to
03:02:04 5 maturity.

03:02:05 6 Q. Let me just correct you because -- so that
03:02:08 7 number is actually excess of five years.

03:02:10 8 A. Oh, strike that.

03:02:11 9 Q. Okay.

03:02:12 10 A. Okay. So this is excess of five and excess
03:02:15 11 of ten. So this tells me that 50 percent, rounded,
03:02:21 12 of HealthTrust investments is more than five years
03:02:24 13 out, which is a substantial portion of its investments
03:02:28 14 for a company that has a very short tail, it's a lot
03:02:34 15 of tail.

03:02:34 16 Q. Okay.

03:02:35 17 A. Now, if we can scroll up, to answer your
03:02:38 18 question, when looking at the -- when looking at the
03:02:41 19 question, what does the company have that could be
03:02:44 20 considered short term, and that is investments which
03:02:49 21 mature in less than 12 months, that's this \$10 million
03:02:53 22 number, okay? And if I can, counsel, get you to
03:02:59 23 scroll to the bottom of the page.

03:03:00 1 Q. Sorry.

03:03:01 2 A. Got to go up a little higher. No, the
03:03:05 3 other way. Okay.

03:03:08 4 Now, you'll see here this Footnote 2.
03:03:12 5 The above investments excludes in each year something
03:03:16 6 that is called cash and cash equivalents. So if I
03:03:20 7 scroll over to 2010, in cash -- right here -- cash
03:03:26 8 and cash equivalents was \$52.5 million. So if I take
03:03:34 9 this number and the number that I showed you earlier
03:03:41 10 that mature within 12 months at \$10 million, I can
03:03:43 11 tell you that on a short-term basis, HealthTrust has
03:03:50 12 \$62 million very liquid funds to pay claims or
03:03:55 13 expenses.

03:03:56 14 So again, the indication of investing
03:04:03 15 in longer than 12 months, and certainly investing
03:04:07 16 12 -- I mean, excuse me -- 24 to 10-plus years tells
03:04:12 17 me that that is, (a), cash that is not needed in the
03:04:16 18 short term to pay either expenses or claims, and (b),
03:04:20 19 as we'll see in a bit, is also perhaps the leading
03:04:25 20 indicator for a comment that I'll make that says that
03:04:29 21 HealthTrust is over capitalized. Overcapitalized
03:04:34 22 means that there's more surplus on the balance sheet
03:04:38 23 than what is necessary to support the financial

03:04:40 1 operation known as HealthTrust.

03:04:47 2 Q. A couple of basic points of clarification.
03:04:51 3 This reference to \$52.5 million in cash or cash
03:04:57 4 equivalents for 2010, where did you get that number?

03:04:59 5 A. That, as well as all the numbers in this
03:05:02 6 chart, other than these percentages that I calculated
03:05:05 7 right here, come from the financial -- those are the
03:05:08 8 financial statement for the audited financials
03:05:13 9 prepared by Berry Dunn, in this case for years 2008,
03:05:18 10 2009, and 2010.

03:05:22 11 I think I should make one point so I
03:05:24 12 don't get everybody confused. Just because
03:05:27 13 securities are invested for longer periods does not
03:05:30 14 mean they can't be converted, all right?

03:05:35 15 Q. What does that mean?

03:05:36 16 A. If I have a security that's been invested
03:05:39 17 for 10 years and I needed that cash, I could have my
03:05:44 18 broker-dealer sell that security and convert it to
03:05:48 19 cash very quickly.

03:05:50 20 However, in selling off a security
03:05:55 21 that has a longer-term investment duration, I will
03:05:59 22 incur what is referred to in the business as breakage
03:06:05 23 cost. And breakage cost means that because the

03:06:07 1 maturity is 10 years and I need it to be cashed out
03:06:11 2 immediately, you're going to pay money in order to
03:06:15 3 have that security converted to cash.

03:06:18 4 So it isn't that marketable
03:06:21 5 securities cannot be converted to cash. They can.
03:06:23 6 But to the extent that you do so prior to the
03:06:26 7 maturity of the underlying investment, you will incur
03:06:29 8 additional costs and charges in order to convert the
03:06:34 9 security to cash.

03:06:36 10 Q. But to go back to the opinion you stated
03:06:38 11 beforehand, do you have an opinion as to whether
03:06:43 12 HealthTrust, a short tail line company, holding
03:06:47 13 securities with -- or investments with durations
03:06:51 14 excess of five years is appropriate for their capital
03:06:54 15 structure or not?

03:06:55 16 A. I don't think I'd use the word
03:07:00 17 "appropriate." I would use -- I think the better
03:07:02 18 term would say "not necessary."

03:07:04 19 Q. Fair enough. Last point of clarification.
03:07:07 20 All of your financial analysis ends with the end of
03:07:14 21 calendar 2010?

03:07:16 22 A. The 2011 financials for HealthTrust have
03:07:20 23 not yet been promulgated.

03:07:22 1 Q. And that's why we deal with 2010 numbers?

03:07:24 2 A. That is correct.

03:07:24 3 Q. Stay with nomenclature. "Loss" and "claims
03:07:41 4 reserves," what do those terms mean?

03:07:44 5 A. Some of the confusion which has arisen in
03:07:50 6 connection with the report prepared by Mr. Wingate or
03:07:55 7 the BSR, some of the comments made by LGC, are
03:08:02 8 basically cobbling together two things: one, reserves,
03:08:07 9 and second, I'll call it surplus. They're not the
03:08:10 10 same.

03:08:12 11 In the business of insurance, you
03:08:17 12 post the reserve based on your statement date equal
03:08:25 13 to, (a), the amount of claims that are reported but
03:08:33 14 not fully settled; (b), an actuarial estimation of
03:08:40 15 claims that have been incurred; that is, the event
03:08:43 16 that gives rise to the claim has happened, but the
03:08:47 17 claim has not been reported; and (c), loss adjustment
03:08:52 18 expenses related to both.

03:08:54 19 So one, the claims that have not been
03:08:58 20 fully settled is usually the claims handler or
03:09:02 21 handlers that give you an indication of that value.
03:09:06 22 IBNR, incurred but not reported, an actuarial
03:09:10 23 determination based on the practices common in

03:09:15 1 healthcare and the history specific to healthcare,
03:09:19 2 come up with an estimate. And that again is on the
03:09:21 3 reserve side of the balance sheet. "Reserve" means
03:09:28 4 it's a liability.

03:09:29 5 So the next comment is surplus.

03:09:33 6 Q. Right.

03:09:34 7 A. Okay? And if I may start with something
03:09:38 8 that we all have, on an individual basis, we have a
03:09:42 9 home. We likely have a car. We may have other
03:09:48 10 items. In all likelihood, we may have a mortgage; we
03:09:52 11 may have a car loan outstanding. Now, the value of
03:09:56 12 the home and the car less the liabilities owing on
03:10:01 13 account of those two items equals my net worth.
03:10:08 14 So assets minus liabilities equals net worth.

03:10:10 15 It's not any different in the
03:10:11 16 insurance world; it's just different terms, okay? In
03:10:16 17 the insurance world, it's assets minus liabilities
03:10:20 18 equals net assets, which is what you're going to see
03:10:24 19 in a second. Another term for net assets is surplus,
03:10:28 20 which is what was captured in Chapter 5-B with
03:10:32 21 respect to distributions, and member balances is an
03:10:36 22 older term that was used by LGC prior to 2003.

03:10:44 23 Q. To mean what?

03:10:45 1 A. To mean capital. The excess of assets over
03:10:51 2 liabilities.

03:10:52 3 Q. Okay.

03:10:53 4 A. Capital or surplus.

03:10:55 5 Q. One more term: earnings.

03:10:58 6 A. This is a not-for-profit institution.

03:11:05 7 Not-for-profit does not mean they don't make profits.
03:11:09 8 The HealthTrust, with the exception of 2009, has been
03:11:12 9 a very profitable business. The fact is that it has
03:11:18 10 applied for an exemption for tax purposes at the
03:11:23 11 federal level and enjoys that exemption as well from
03:11:28 12 the state level.

03:11:29 13 So while they don't pay income taxes,
03:11:31 14 I want to make it clear that they do produce profits.
03:11:36 15 Another word that's used for "profits" is "earnings."

03:11:39 16 Q. I'm going to take you into some more charts
03:11:42 17 that you prepared, one of which happens to be on the
03:11:46 18 easel there. And before we go to it, I just want to
03:11:50 19 ask you, where does the information come from that
03:11:53 20 are on the charts we're about to discuss?

03:11:58 21 A. Everything on this chart comes from the
03:12:02 22 audited financial statements, again, prepared by
03:12:07 23 Berry Dunn. And the only thing that doesn't, there's

03:12:11 1 something you can't see but we'll see it on the
03:12:13 2 screen and I'll point it out. But there's a category
03:12:16 3 here that says RBC confidence level. These numbers
03:12:21 4 here came from the Segal Company.

03:12:30 5 THE PRESIDING OFFICER: Wait for the rest
03:12:31 6 of us to catch up with you. Exhibit number, please?

03:12:33 7 MR. VOLINSKY: We're about to go to BSR
03:12:35 8 No. 7.

03:12:36 9 THE PRESIDING OFFICER: Okay. BSR 7. Give
03:12:50 10 us a moment.

03:12:51 11 MR. VOLINSKY: Yes.

03:12:55 12 THE PRESIDING OFFICER: Do you intend to
03:12:56 13 request admission of this?

03:12:58 14 MR. VOLINSKY: Yes.

03:13:00 15 MR. TILSLEY: 7's already in.

03:13:04 16 MR. VOLINSKY: 7's already in.

03:13:06 17 THE PRESIDING OFFICER: Thank you. And
03:13:07 18 it's only day one.

03:13:10 19 Please proceed.

03:13:12 20 Q. BY MR. VOLINSKY: So Exhibit 7 is a table
03:13:18 21 that encompasses three years of financial data from
03:13:26 22 the audited financial statements, correct?

03:13:29 23 A. This is commonly referred to as a

03:13:32 1 spreadsheet. It seeks to capture multiple entities,
03:13:36 2 multiple years, in a concise, easy-to-compare format.

03:13:42 3 Q. Is this called spreadsheeting?

03:13:45 4 A. Yes, it is.

03:13:46 5 Q. When did you start spreadsheeting financial
03:13:48 6 statements?

03:13:48 7 A. Well, in the case of HealthTrust, it goes
03:13:51 8 all the way back to 2010.

03:13:53 9 Q. No, when did you first start personally
03:13:56 10 developing the skills to spreadsheet?

03:13:58 11 A. Oh. Okay. I don't know if I want to admit
03:14:00 12 that. Probably '72.

03:14:03 13 Q. You've used the process of spreadsheeting
03:14:07 14 multiple financial statements basically throughout
03:14:10 15 your entire career?

03:14:11 16 A. I do.

03:14:12 17 Q. All right. So we have HealthTrust on this
03:14:15 18 particular chart, '08 to '10; Property-Liability
03:14:21 19 Trust, '08 to 10; and Workers' Compensation, '08 to
03:14:27 20 '10?

03:14:28 21 A. And LGC.

03:14:30 22 Q. LGC itself. That's the parent
03:14:32 23 organization, correct?

03:14:32 1 A. Yes. And let me clarify one point while
03:14:35 2 we're talking about it. These numbers here is the
03:14:37 3 holding company without the risk pools consolidating
03:14:45 4 into LGC. In accounting-speak, these numbers are
03:14:49 5 referred to as the consolidating financial numbers,
03:14:56 6 not the consolidated.

03:14:57 7 So what it does -- and this will
03:15:00 8 become more relevant as we move on through the
03:15:03 9 afternoon -- is that it gives us the opportunity to
03:15:04 10 look at LGC as a standalone entity.

03:15:08 11 Q. So if we go back to my handwritten chart
03:15:11 12 here, those last three columns deal with only the
03:15:17 13 parent's financial data?

03:15:18 14 A. That's correct. That's '08 through 2010,
03:15:25 15 LGC parent company standalone.

03:15:27 16 Q. I want to take you to the information about
03:15:31 17 HealthTrust. And in particular, information about
03:15:37 18 HealthTrust's net assets. Am I displaying the right
03:15:41 19 part of the Exhibit 7?

03:15:43 20 A. Well, why don't you just keep it there for
03:15:45 21 a second.

03:15:45 22 Q. Okay.

03:15:46 23 A. Obviously these nomenclatures apply to all

03:15:49 1 the numbers that go across the page. I did this in
03:15:53 2 essentially a couple buckets. This first piece is
03:15:56 3 the balance sheet of HealthTrust and the other
03:16:01 4 entities. The balance sheet is a snapshot of the
03:16:06 5 company's financial position as of the statement
03:16:11 6 date. In this case, 12/31/08, '09, and '10. And
03:16:19 7 below that is the income statement. It's the summary
03:16:21 8 of revenues and expenses in claims incurred that
03:16:28 9 happened over the 12-month period ending 12/31/08,
03:16:35 10 '09, or '10.

03:16:37 11 Now, to go back up to the balance
03:16:39 12 sheet -- right there -- you'll remember that I
03:16:41 13 described the word "net assets" as equivalent of
03:16:45 14 "surplus" or "members' balances."

03:16:48 15 So for '08, HealthTrust had net
03:16:53 16 assets of \$92.7 million. In '09 it had net assets of
03:16:59 17 \$79.5. And in 2010, it had net assets of \$86.8
03:17:07 18 million.

03:17:09 19 The significance of the statement is
03:17:13 20 if we're going to make a comment about surplus, I
03:17:15 21 think one needs to begin the journey by saying,
03:17:20 22 that's surplus. Now, within the net assets
03:17:23 23 structure, it also has a series of components.

03:17:28 1 Board-designated is what the board of LGC decides is
03:17:34 2 the appropriate level of surplus for this business.
03:17:41 3 And in 2008, the board-designated was \$68.3 million.
03:17:48 4 In '09, it was \$77.9 million. And in 2010, it was
03:17:54 5 \$84.4 million.

03:17:57 6 Mr. Volinsky in his opening comments
03:18:00 7 made the note or the observation that this number
03:18:05 8 here is not at the target rate that the board set of
03:18:11 9 an RBC of 4.2, but actually is higher than that
03:18:16 10 because LGC HealthTrust in years prior to 2010
03:18:23 11 capitalized the future administrative expenses and
03:18:28 12 used that capitalized figure to bolster the net asset
03:18:33 13 account.

03:18:34 14 That amount measured on an RBC basis
03:18:38 15 is .5. So if one wants to do a calculation of RBC
03:18:43 16 for '08, '09, and '10, this number here would be 4.7,
03:18:51 17 all right? 4.7. And here it's 4.2. Now, if we
03:18:59 18 would scroll down to the bottom, I have that
03:19:02 19 information. Okay. The administrative expenses in
03:19:04 20 2008 -- this is what was capitalized and included as
03:19:09 21 designated -- is \$7.229 million.

03:19:12 22 So in effect, what they did is, Let's
03:19:15 23 make an estimate of what our forward admin expenses

03:19:18 1 are. Let's make a provision for it. I'll use the
03:19:22 2 term "reserve." You know, it's just sort of rainy
03:19:27 3 day money. And we'll throw that into the capital
03:19:29 4 base as well. And that's 7.2.

03:19:32 5 And then in 2009, the capitalized
03:19:36 6 future admin expenses was \$8.7 million. And then all
03:19:40 7 of a sudden in 2010, it dropped to \$500,000.

03:19:48 8 Q. You have an RBC calculation overall right
03:19:53 9 underneath that line?

03:19:53 10 A. I do. But I need to go up and pick up a
03:19:56 11 data point first.

03:19:57 12 Q. Okay.

03:20:01 13 A. So one is the administrative expenses are
03:20:03 14 part of the capital calculation board-designated, and
03:20:09 15 I think it's noteworthy that what had been running at
03:20:14 16 \$7 or \$8 million a year dropped to \$500,000 in 2010.

03:20:17 17 The other thing I want to call
03:20:19 18 attention to is unrestricted. Now, the best way to
03:20:23 19 look at unrestricted is if the board of LGC says,
03:20:29 20 Gee, we need 4.2 RBC plus the .5 for admin expenses,
03:20:38 21 all right, what is that number? And that number is
03:20:41 22 \$68 million. Then as it turns out, HealthTrust had
03:20:46 23 another \$25.7 million, which was excess of what the

03:20:58 1 board said they needed. So that number, \$25.7
03:21:03 2 million, is above and beyond what the board claimed
03:21:07 3 it needed to support this balance sheet.

03:21:09 4 Now, if you'll scroll down. And let
03:21:11 5 me just show one thing. In 2009, that number
03:21:15 6 flipped, negative 757. So \$26 million was consumed
03:21:20 7 between '08 and '09. And I'll show you that.

03:21:25 8 Now, to Mr. Volinsky's comment
03:21:29 9 earlier, you have RBC, even though the board set as a
03:21:34 10 target an RBC of 4.2 and even though it has admin
03:21:37 11 expenses for another .5, you would say, Well, gee,
03:21:43 12 shouldn't that be 4.7? No. Because of the
03:21:46 13 unrestricted number that I showed you up above that's
03:21:51 14 just under \$26 million, when you take the
03:21:53 15 unrestricted and the board-designated and the
03:21:57 16 capitalized administrative expenses, the actual RBC,
03:22:02 17 the effective RBC for HealthTrust, is 6.4.

03:22:10 18 Same thing in 2009. It dropped. And
03:22:16 19 it dropped -- began -- that's the year in which the
03:22:19 20 loss occurred at almost \$9 million. And the loss
03:22:23 21 notwithstanding, \$4.4 million was distributed. But
03:22:27 22 because the admin expense, the capitalized admin
03:22:31 23 expense was still part of the mix in '09, that caused

03:22:36 1 the RBC to be 4.8.

03:22:38 2 And then in 2010, two things happened.
03:22:43 3 One, in '08, the unrestricted capital account was
03:22:48 4 wiped out. It was also negative in 2010. And the
03:22:52 5 admin capitalized arrangement dropped from \$8.7 million
03:23:00 6 to \$500,000. So as a result of that, since reaching
03:23:06 7 the target RBC that the board of LGC set back in '05,
03:23:11 8 they didn't get back to their target level of 4.2
03:23:15 9 until 12/31/10.

03:23:21 10 Q. I know we'll go into this in more detail
03:23:24 11 later, but is it your expert opinion that 4.2 is what
03:23:30 12 this organization needs --

03:23:31 13 MR. SATURLEY: Objection.

03:23:32 14 Q. BY MR. VOLINSKY: -- of this capital --

03:23:33 15 THE PRESIDING OFFICER: One moment,
03:23:35 16 Mr. Volinsky. There's an objection.

03:23:36 17 MR. VOLINSKY: I didn't finish the
03:23:37 18 question.

03:23:38 19 THE PRESIDING OFFICER: Well, it wasn't
03:23:39 20 going to get any better.

03:23:42 21 Mr. Saturley?

03:23:44 22 MR. SATURLEY: If I were to cross-examine
03:23:47 23 Mr. Coutu at this point -- and obviously I'm not

03:23:50 1 doing that -- but every part of his background and
03:23:58 2 every expression that he's given with regards to his
03:24:01 3 background and what he's done has to do with the
03:24:03 4 property and casualty side of the insurance business.

03:24:07 5 This is a health insurance business
03:24:09 6 that he's talking about. He's given you some glimpse
03:24:12 7 into the differences between those two lines of
03:24:15 8 business. Health is very different from property and
03:24:17 9 casualty. He's given you some glimpse of that.
03:24:19 10 I can give you some more and I will during his cross-
03:24:22 11 examination.

03:24:22 12 But he's not been established as
03:24:26 13 knowing what's an appropriate RBC for a health
03:24:30 14 insurance company. I know they're both in the health
03:24:32 15 insurance industry, your Honor -- or Mr. Mitchell.
03:24:35 16 But I dare say that if I were -- if I -- It's like
03:24:42 17 going to a dentist or an oral surgeon. They both
03:24:46 18 look in your mouth. But they do very different
03:24:49 19 things. It's like going to an internist or an
03:24:53 20 oncologist. They both are concerned about what's
03:24:56 21 inside you. They both have medical degrees. You
03:24:59 22 wouldn't want an opinion from one on the topic of the
03:25:03 23 other.

03:25:04 1 And you wouldn't want a lawyer who
03:25:06 2 worked in the securities area to be trying a case
03:25:10 3 about securities [sic]. And what I'm suggesting is
03:25:13 4 that this gentleman has not been qualified to offer
03:25:16 5 an opinion on the appropriate RBC for a company in
03:25:23 6 the health line of insurance. That's my objection.

03:25:32 7 THE PRESIDING OFFICER: Mr. Volinsky, do
03:25:33 8 you want to respond, sir?

03:25:34 9 MR. VOLINSKY: Yes, sir. You've heard a
03:25:36 10 long explanation of what short tail line is and how
03:25:39 11 you invest related to the maturities of your claims.

03:25:42 12 THE PRESIDING OFFICER: Correct.

03:25:44 13 MR. VOLINSKY: Mr. Coutu has an opinion,
03:25:48 14 looking at the short tail line nature of health
03:25:52 15 insurance, to which there is no objection, as to how
03:25:58 16 overcapitalized this company is.

03:26:02 17 So based on the durations of short
03:26:07 18 tail line insurance where you have a certain
03:26:10 19 short-term need for cash versus having investments
03:26:14 20 that go out three, five, ten years, he can tell us
03:26:21 21 how much capital should be in this balance sheet
03:26:26 22 based on all of their numbers. He's not going to
03:26:31 23 quarrel with how they run efficiently or inefficiently.

03:26:34 1 He's going to look at the maturity levels of the
03:26:37 2 claims versus the investments and offer an opinion.

03:26:43 3 THE PRESIDING OFFICER: Mr. Saturley, any
03:26:44 4 rebuttal to that? If necessary.

03:26:57 5 MR. SATURLEY: Mr. Coutu has talked at
03:26:59 6 great length about being a runoff guy. Mr. Coutu
03:27:03 7 will concede when asked in cross-examination that the
03:27:06 8 difference between the qualities that make you a
03:27:09 9 runoff guy where you are not involved in underwriting
03:27:14 10 and like tasks does not qualify you. They're
03:27:19 11 different tasks. They're different qualities.

03:27:22 12 And what I am suggesting is that with
03:27:24 13 regards to RBC, we've not heard anything that
03:27:28 14 qualifies him as an RBC expert with regards to
03:27:34 15 HealthTrust. And that's the opinion he's about to
03:27:35 16 offer. Thus, he will acknowledge, if asked, that the
03:27:40 17 RBC formulas that are run to determine those very
03:27:46 18 numbers he's put up are done by complex formula and
03:27:51 19 that they differ between the two industries, between
03:27:53 20 the property and casualty field, the life field, and
03:27:55 21 the health field. So that he -- and that he is not
03:28:00 22 familiar with them.

03:28:02 23 So for him to skip over that step

03:28:04 1 with no actuarial training at all and no tendered
03:28:09 2 qualifications in that field, for he has none, for
03:28:13 3 him --

03:28:14 4 THE PRESIDING OFFICER: In which field,
03:28:15 5 please?

03:28:16 6 MR. SATURLEY: The actuarial field.

03:28:17 7 THE PRESIDING OFFICER: Okay.

03:28:18 8 MR. SATURLEY: Which is what RBC concerns
03:28:19 9 and where it comes from. And for him to then skip
03:28:22 10 over that, that knowledge, that training, and that
03:28:26 11 experience that actuaries have, and just to say,
03:28:31 12 Well, from my lofty perch, I will say that this
03:28:34 13 company in the health insurance industry, where I
03:28:37 14 have never worked, it's appropriate for it to have
03:28:39 15 the following RBC and none other, that, I think, sir,
03:28:46 16 goes far beyond what our law permits with regards to
03:28:50 17 an expert.

03:28:51 18 THE PRESIDING OFFICER: Okay. Mr. Volinsky,
03:28:52 19 anything further?

03:28:54 20 MR. GORDON: Your Honor --

03:28:56 21 MR. VOLINSKY: I can --

03:28:58 22 THE PRESIDING OFFICER: Anything further in
03:28:59 23 response to Mr. Saturley?

03:29:00 1 MR. VOLINSKY: Yes. I'm glad to lay as
03:29:06 2 long a foundation as Mr. Saturley likes.

03:29:06 3 THE PRESIDING OFFICER: Well, then why
03:29:06 4 don't you hold on and I'll recognize Mr. Gordon.

03:29:06 5 Mr. Gordon, could you come forward
03:29:07 6 just a bit towards the microphone, sir. I'm sorry
03:29:09 7 for that inconvenience.

03:29:11 8 MR. GORDON: The only point I would like to
03:29:13 9 add --

03:29:13 10 THE PRESIDING OFFICER: You are objecting?

03:29:16 11 MR. GORDON: Yes. I am objecting. Because
03:29:17 12 I thought that the question was specifically to LGC.
03:29:21 13 I think the question was for this organization.

03:29:24 14 THE PRESIDING OFFICER: Um-hum.

03:29:28 15 MR. GORDON: And I think that the record
03:29:30 16 will demonstrate that while Mr. Coutu has looked at
03:29:33 17 the financials, he has not looked at any of the
03:29:35 18 minutes of the organization, has not looked at any of
03:29:38 19 the minutes that had the discussions as to why they
03:29:40 20 reached the levels that they reached.

03:29:43 21 He didn't listen to any of the
03:29:45 22 presentations by the actuaries and the consultants
03:29:49 23 who provided information with regard to the

03:29:53 1 establishment of the RBC. That is all part of the
03:29:57 2 minutes of the exhibits here that you will get an
03:30:01 3 opportunity sometime to be shown.

03:30:04 4 So I take objection to the
03:30:07 5 specificity of the question for this particular
03:30:10 6 organization because the record is that he has not
03:30:15 7 studied at all any of the decision-making process,
03:30:19 8 which is laid out in the minutes, as to why they got
03:30:21 9 to where they got.

03:30:24 10 Does that make sense?

03:30:26 11 THE PRESIDING OFFICER: Everything makes
03:30:26 12 sense, Mr. Gordon, but let me ask a question.

03:30:31 13 MR. GORDON: Sure.

03:30:31 14 THE PRESIDING OFFICER: Would that not go
03:30:32 15 to the weight of his testimony as opposed to his
03:30:38 16 ability to render the testimony, in that the minutes
03:30:40 17 and other documents that you've just referred to
03:30:42 18 would be specific to this particular operation and,
03:30:49 19 therefore, would bona fide, or if you will, diminish
03:30:54 20 the weight of his testimony?

03:30:56 21 MR. GORDON: I'm not foolish enough to say
03:30:58 22 that that approach is wrong. But I do believe if
03:31:01 23 you're going to be offering an expert opinion to a

03:31:05 1 particular organization, that you as a gatekeeper in
03:31:08 2 the first sense -- you could say, I'll let it in and
03:31:12 3 give it whatever weight is due -- I understand that
03:31:16 4 the gate can swing wide and open -- but I do think at
03:31:19 5 the preface, at the beginning of that, that there
03:31:21 6 should be a record demonstrated that he has looked at
03:31:24 7 the documents by which this formulation was decided
03:31:27 8 by a board.

03:31:28 9 It wasn't -- It was not that they
03:31:30 10 were just counting up these numbers and then making
03:31:33 11 that decision. There was a full discrete process by
03:31:37 12 which that was reached. And I think it's a little
03:31:40 13 misleading for him to just look at this chart and
03:31:42 14 then say, This is what I think the RBC should be for
03:31:46 15 this particular organization.

03:31:49 16 So I would say it is sufficiently off
03:31:51 17 that you are appropriate in denying the introduction
03:31:55 18 of that evidence or, as you suggested, understand
03:31:59 19 that it is a snapshot of information and give it
03:32:03 20 whatever weight it deserves.

03:32:04 21 THE PRESIDING OFFICER: These other
03:32:05 22 documents that you referred to -- I heard you refer
03:32:08 23 to minutes.

03:32:09 1 MR. GORDON: Yes.

03:32:10 2 THE PRESIDING OFFICER: What other
03:32:10 3 documents besides the financial documents were you
03:32:15 4 alluding to?

03:32:16 5 MR. GORDON: There would be calculations by
03:32:18 6 Mr. Riemer by which he gave information to the board
03:32:23 7 and then the board actually would have a dialogue as
03:32:27 8 to what would be the appropriate RBC and why.

03:32:30 9 What are the factors that go into
03:32:32 10 establishing the RBC. What are the needs of the
03:32:38 11 organization which need to be addressed. What are
03:32:41 12 the factors that they should be concerned about.
03:32:42 13 What are the risks that they are seeing. All those
03:32:45 14 discussions are taking place in documents that
03:32:48 15 Mr. Coutu has not reviewed.

03:32:50 16 THE PRESIDING OFFICER: Mr. Coutu, you
03:32:51 17 heard Attorney Gordon go down a list of documents.
03:32:54 18 Are those documents in the realm of your knowledge
03:32:58 19 that would be taken into consideration in calculating
03:33:01 20 an RBC?

03:33:03 21 THE WITNESS: I actually reviewed the
03:33:05 22 documents that are being alleged that I did not
03:33:08 23 review.

03:33:08 1 THE PRESIDING OFFICER: All right. Thank
03:33:10 2 you, Mr. Gordon.

03:33:11 3 Mr. Volinsky, before we -- Well, let
03:33:13 4 me hear some additional foundation from you with
03:33:16 5 respect to -- excuse me?

03:33:19 6 I'm sorry. Did you have something
03:33:20 7 else to say, Mr. Gordon?

03:33:22 8 MR. GORDON: No. I actually didn't hear --
03:33:24 9 did he say that he reviewed them?

03:33:26 10 THE PRESIDING OFFICER: That was his
03:33:26 11 representation.

03:33:27 12 MR. GORDON: It was not his deposition
03:33:29 13 testimony, but I'll -- I'll just leave it at that.

03:33:32 14 THE PRESIDING OFFICER: Well, all I'm going
03:33:33 15 to take for right now is what he's just said.

03:33:38 16 MR. GORDON: Okay.

03:33:39 17 THE PRESIDING OFFICER: All right. Was
03:33:42 18 there something -- Were your comments along the same
03:33:46 19 line Mr. Gordon was just reaching?

03:33:48 20 MR. SATURLEY: Yes. I couldn't understand
03:33:50 21 what his answer was.

03:33:51 22 THE PRESIDING OFFICER: So we're all
03:33:51 23 settled there then.

03:33:53 1 Back to you, Mr. Volinsky. Give me a
03:33:56 2 little more foundation, and then we'll take a break.
03:33:59 3 So give me about five minutes of foundation maximum
03:34:01 4 and we'll take a break.

03:34:04 5 MR. VOLINSKY: Okay.

03:34:05 6 THE PRESIDING OFFICER: Come to the
03:34:06 7 microphone, please.

03:34:08 8 Q. BY MR. VOLINSKY: Let's start here,
03:34:09 9 Mr. Coutu. You have a long series of experiences
03:34:12 10 working with RBCs in the companies that you ran; have
03:34:15 11 you not?

03:34:16 12 A. I do.

03:34:16 13 Q. Now, the RBCs that appear on the chart,
03:34:21 14 which is BSR 7, how are they determined?

03:34:29 15 A. The target RBC that is notionally 4.2, but
03:34:35 16 with the administrative expenses is 4.7, is a
03:34:38 17 calculation that's performed by the consulting
03:34:43 18 actuary, Peter Riemer.

03:34:46 19 Q. That's the LGC consulting actuary?

03:34:48 20 A. Right. The LGC consulting actuary. The
03:34:52 21 effective --

03:34:53 22 THE PRESIDING OFFICER: Could you please
03:34:53 23 address the difference between calculating the RBC

03:35:00 1 that you're familiar with and the point that's been
03:35:04 2 raised in the objection about to what extent that
03:35:08 3 might differ when considering a health insurance
03:35:13 4 company?

03:35:14 5 THE WITNESS: Let me -- one of the minutes
03:35:16 6 of the board -- Peter Riemer, who was, I'll use the
03:35:23 7 word, a sponsor of the risk-based capital and
03:35:28 8 benefits of using an RBC methodology -- Mr. Riemer
03:35:32 9 also suggested various levels that would be
03:35:38 10 appropriate for HealthTrust as respects of the amount
03:35:42 11 of capital or surplus in the business.

03:35:46 12 And one of the benchmarks that he
03:35:52 13 uses was that which is followed at that time -- this
03:35:57 14 is going back to 2002, I might note, all right? --
03:36:03 15 that was followed by Blue Cross Blue Shield, which
03:36:06 16 put the RBC calculation for his comments in the notes
03:36:15 17 or the minutes between 4 and 5 percent -- 400 or 500
03:36:20 18 percent or decimal notation 4 and 5, 4.0, 5.0.

03:36:26 19 There is a fair amount of discussion
03:36:30 20 at the board level over time, a lot of it in 2002,
03:36:35 21 that talks about the evolution of the RBC and
03:36:40 22 eventually gets to a recommendation made by Mr. Riemer
03:36:45 23 that the board adopt 4.2 as the appropriate RBC level

03:36:50 1 of surplus for the HealthTrust, which amount was
03:36:54 2 ratified by the board, I believe in, again, 2002,
03:37:00 3 maybe early 2003.

03:37:02 4 THE PRESIDING OFFICER: Mr. Coutu, my
03:37:06 5 question is directed to the point of the objection,
03:37:08 6 which I understand to be you are familiar with RBC
03:37:11 7 calculation in insurance and areas of insurance other
03:37:15 8 than health.

03:37:17 9 THE WITNESS: That is correct.

03:37:18 10 MR. VOLINSKY: May I --

03:37:19 11 THE PRESIDING OFFICER: Would you please
03:37:20 12 explain to me the differences that would come into
03:37:27 13 play from your experience with other lines of
03:37:31 14 insurance and health insurance in this instance.

03:37:35 15 THE WITNESS: I believe I testified a bit
03:37:37 16 earlier today in my testimony that --

03:37:38 17 THE PRESIDING OFFICER: Well, refresh my
03:37:40 18 memory, sir.

03:37:40 19 THE WITNESS: -- that the NAIC Model Act
03:37:46 20 promulgated different mathematical -- mathematical
03:37:51 21 calculations for different lines of insurance.

03:37:54 22 THE PRESIDING OFFICER: Okay.

03:37:55 23 THE WITNESS: So the mathematical

03:37:57 1 calculation of RBC for healthcare is different than
03:38:00 2 for property and casualty, and that both of them are
03:38:03 3 different than life.

03:38:04 4 This is not a one-size fits all.
03:38:07 5 Thought was given to what are the unique issues
03:38:12 6 associated with healthcare. And based on that, the
03:38:16 7 NAIC tailored the calculation of RBC for healthcare
03:38:22 8 companies, property and casualty companies, and life
03:38:26 9 insurance companies. Mike Coutu didn't. The NAIC
03:38:31 10 did.

03:38:31 11 Second is there were refinements that
03:38:34 12 were made in the healthcare calculations. And it
03:38:39 13 wasn't until 1998 that those calculations -- that is,
03:38:46 14 the healthcare calculation of RBCs -- were modified
03:38:50 15 based on input from the Casualty America -- Casualty
03:38:55 16 Society -- Actuarial Society and other professionals
03:38:59 17 that are in the business of actuarial practice.

03:39:01 18 When that got done, then from 1998 to
03:39:06 19 where we are today, that formulation for healthcare
03:39:10 20 companies has not changed, to the best of my knowledge,
03:39:15 21 other than one change. The one change that was made
03:39:17 22 in the healthcare calculation says this. There's a
03:39:22 23 ratio that's used to measure the profitability of

03:39:26 1 insurance companies. It's called a combined ratio.

03:39:29 2 THE PRESIDING OFFICER: Okay. But we're
03:39:30 3 not involved with that right now.

03:39:32 4 THE WITNESS: It does involve the RBC
03:39:33 5 calculation.

03:39:34 6 THE PRESIDING OFFICER: It does. But that
03:39:36 7 RBC calculation standard, if that term can be used,
03:39:41 8 set by NAIC, you are just referencing -- would it be
03:39:49 9 wrong to characterize it as an industry standard?

03:39:53 10 THE WITNESS: It is an industry standard.

03:39:54 11 THE PRESIDING OFFICER: Okay.

03:39:55 12 THE WITNESS: And so to close the comment,
03:39:57 13 the industry standard says, for healthcare, if it's
03:40:02 14 at an RBC of 2.0, or 200 percent, that the NAIC and
03:40:10 15 the regulators which have adopted the NAIC model deem
03:40:15 16 that insurer -- that healthcare insurer to be
03:40:19 17 satisfactorily capitalized.

03:40:21 18 THE PRESIDING OFFICER: Your testimony was
03:40:24 19 that the RBC was not an appropriate number. If I
03:40:29 20 rephrase that to say that the RBC for the --

03:40:36 21 MR. VOLINSKY: For the LGC.

03:40:38 22 THE PRESIDING OFFICER: Yes. For the LGC.
03:40:39 23 Thank you. -- HealthTrust -- or LGC.

03:40:46 1 MR. VOLINSKY: LGC HealthTrust.

03:40:49 2 THE PRESIDING OFFICER: If I'm to rephrase
03:40:51 3 that to say that the NAIC standard exceeds or is less
03:41:00 4 than what has been calculated, is that an accurate
03:41:05 5 statement?

03:41:08 6 THE WITNESS: Well, clearly at 4.2, the 4.2
03:41:12 7 that was adopted by the board of LGC exceeds the NAIC
03:41:19 8 presumption of capital adequacy at 2.0 by a factor of
03:41:23 9 2.2.

03:41:24 10 THE PRESIDING OFFICER: Okay. Thank you.
03:41:25 11 Anything further?

03:41:26 12 MR. VOLINSKY: I just -- with some risk,
03:41:29 13 let me just clarify what --

03:41:32 14 THE PRESIDING OFFICER: With some risk.

03:41:33 15 Q. BY MR. VOLINSKY: RBC in property/casualty
03:41:37 16 is calculated in a particular way. RBC in healthcare
03:41:41 17 is calculated in a different way.

03:41:44 18 A. Right.

03:41:44 19 Q. Do they both use the 2.0 or 200 percent
03:41:48 20 standard in the same way?

03:41:50 21 A. Including life companies, yes.

03:41:52 22 Q. So they all use 2.0 or 200 the same way?

03:41:58 23 A. The matrix of how measured is the same.

03:42:03 1 The mathematical formulation is different.

03:42:05 2 Q. Got it. So the internal. But the standard
03:42:09 3 is the same: property, liability, health --

03:42:12 4 A. Life.

03:42:13 5 Q. -- life? Okay.

03:42:15 6 THE PRESIDING OFFICER: He can testify. He
03:42:17 7 can testify as to the RBC either meeting, exceeding,
03:42:23 8 or being less than the NAIC standard.

03:42:30 9 Q. BY MR. VOLINSKY: In this case --

03:42:32 10 THE PRESIDING OFFICER: So it is denied.

03:42:33 11 MR. SATURLEY: May I --

03:42:34 12 THE PRESIDING OFFICER: Hold on. You know,
03:42:36 13 that is my ruling. So let's take a break.

03:42:38 14 MR. VOLINSKY: Okay.

03:42:44 15 THE PRESIDING OFFICER: I've heard you
03:42:47 16 both, you know, twice, twice. Take a break. Ten
03:42:52 17 minutes.

03:42:52 18 (Recess at 3:42 p.m.,
03:57:28 19 resumed at 3:57 p.m.)

03:57:46 20 THE PRESIDING OFFICER: Having returned
03:57:47 21 from the afternoon break, Mr. Volinsky, would you
03:57:49 22 please continue with your questioning.

03:57:50 23 MR. VOLINSKY: Thank you.

03:57:52 1 Q. BY MR. VOLINSKY: Mr. Coutu, there's one
03:57:53 2 other piece I wanted to ask you about with Exhibit 7
03:57:56 3 still up. We discussed that there was \$25 million in
03:58:04 4 unrestricted assets in 2008 and then you used the
03:58:08 5 term "flipped" in '09.

03:58:13 6 Are you able to tell from the
03:58:15 7 financial statements where the \$25 million went?

03:58:18 8 A. I actually have an exhibit which can pencil
03:58:20 9 out exactly those numbers. But to do rough justice --

03:58:25 10 Q. That's fine.

03:58:26 11 A. -- the \$25,723,000 was supplied against --
03:58:35 12 or used to fund the loss -- where am I? -- okay.
03:58:41 13 I'll give you another one. It -- \$9 million rounded
03:58:47 14 plus the 4.4, let's call that \$13 million. Go back
03:58:56 15 up the balance sheet. It also funded the increase
03:58:59 16 here, about \$9 million, and the board-designated
03:59:05 17 \$68 million to \$78 million. And the balance was used
03:59:11 18 in a combination of a decrease in assets -- excuse
03:59:18 19 me -- a decrease in liabilities and an increase --

03:59:22 20 There are four or five different
03:59:24 21 accounts which change from '09 to '10 -- excuse me --
03:59:30 22 from '08 to '09.

03:59:32 23 Q. Thank you. In the chart marked as BSR 7,

03:59:40 1 you looked at three years' worth of financial
03:59:45 2 statements and spreadsheeted them. Let me show you
03:59:50 3 Exhibit 6.

03:59:55 4 THE PRESIDING OFFICER: Mr. Coutu, did you
03:59:56 5 respond "yes"?

03:59:57 6 THE WITNESS: Yes. Excuse me.

04:00:00 7 Q. BY MR. VOLINSKY: Exhibit 6, would you do
04:00:01 8 the same thing for the prior three years for all of
04:00:05 9 the enterprises again?

04:00:08 10 A. Yes, but I would note just to be crisp, I
04:00:13 11 did not spread financials for the real estate
04:00:15 12 subsidiary. But they're spoken for as part of the
04:00:20 13 LGC consolidated.

04:00:21 14 Q. So with that one proviso, is Exhibit 6 your
04:00:26 15 spreadsheeting using the audited financial statements
04:00:30 16 for these entities for the period '05 to '07?

04:00:34 17 A. That is correct.

04:00:35 18 MR. VOLINSKY: I move to strike the ID on 6
04:00:40 19 and for its admission.

04:00:41 20 THE PRESIDING OFFICER: Any objection on
04:00:42 21 Exhibit 6?

04:00:42 22 MR. SATURLEY: No objection to the
04:00:43 23 characterization of what it is. I do not accept

04:00:46 1 necessarily the accuracy of the statements. But I
04:00:48 2 don't object to it as what it's intended as being his
04:00:53 3 summary.

04:00:53 4 THE PRESIDING OFFICER: Can I interpret
04:00:54 5 that to be a similar objection that you had to 7;
04:00:57 6 that is, you haven't been able to compare that with
04:01:02 7 yours, see if it is complete?

04:01:05 8 MR. SATURLEY: Yes, sir, thank you very
04:01:06 9 much.

04:01:06 10 THE PRESIDING OFFICER: Thank you. Just
04:01:07 11 for my understanding.

04:01:07 12 (BSR 6 admitted into evidence.)

04:01:08 13 Q. BY MR. VOLINSKY: One more question on 6,
04:01:10 14 the prior chart. Was that part of your expert report
04:01:13 15 turned over in this case months ago?

04:01:16 16 A. This chart and the prior chart?

04:01:18 17 Q. Yes.

04:01:18 18 A. Yes. They're included in my expert report.

04:01:20 19 Q. Actually, was it Exhibit C to your expert
04:01:24 20 report?

04:01:24 21 A. It was.

04:01:27 22 Q. Let's do one more just so I can get it into
04:01:29 23 evidence. BSR No. 5, same kind of spreadsheeting

04:01:34 1 based on the audited financials for all of the
04:01:38 2 enterprises from '02 to '04?

04:01:42 3 A. With the same exception, I did not spread
04:01:45 4 the numbers related to the real estate subsidiary.

04:01:47 5 MR. VOLINSKY: I move to strike the ID on 5
04:01:50 6 and for its admission.

04:01:52 7 THE PRESIDING OFFICER: With the same
04:01:53 8 condition, Mr. Saturley?

04:01:54 9 MR. SATURLEY: Yes, please. Thank you.

04:01:55 10 THE PRESIDING OFFICER: Very good. Okay.
04:01:56 11 Admitted with condition and we'll clear that up
04:01:58 12 tomorrow or later in the proceedings.

04:01:58 13 MR. VOLINSKY: Thank you.

04:02:00 14 (BSR 5 admitted into evidence.)

04:02:03 15 Q. BY MR. VOLINSKY: I want to ask you about
04:02:06 16 cash and noncash distributions. Did you create a
04:02:15 17 chart of cash and noncash distributions?

04:02:20 18 A. I created a chart of the cash
04:02:25 19 distributions. And in my expert report, I have a
04:02:27 20 narrative of the noncash transfers.

04:02:29 21 Q. So let's talk about the cash first, okay?

04:02:32 22 A. Yes.

04:02:33 23 Q. Let me show you what we've marked as BSR 8,

04:02:40 1 Exhibit E to your report from a couple of months ago.
04:02:43 2 Is this the chart that you prepared about cash
04:02:46 3 distributions?

04:02:47 4 A. It is.

04:02:49 5 MR. VOLINSKY: I'd move to strike the ID of
04:02:52 6 8 and for its admission.

04:02:54 7 THE PRESIDING OFFICER: And with the same
04:02:55 8 proviso, Mr. Saturley; is that correct?

04:02:57 9 MR. SATURLEY: Yes, sir.

04:02:57 10 THE PRESIDING OFFICER: Thank you.
04:02:59 11 Admitted.

04:03:00 12 (BSR 8 admitted into evidence.)

04:03:03 13 Q. BY MR. VOLINSKY: As we did with Exhibit 7
04:03:06 14 a moment ago, or an hour ago, let's have you explain
04:03:09 15 what this chart is. I'll get it over here. So the
04:03:13 16 title of it is "Intercompany transfers '03 to '10."

04:03:20 17 And what's displayed on this chart?

04:03:21 18 A. What I did is from the time of the
04:03:24 19 reorganization, which was done in '03, through and
04:03:29 20 including 2010, by risk pool and, in this case, real
04:03:38 21 estate as well, is to chart how much in the way of
04:03:44 22 cash was distributed from these entities, "these
04:03:49 23 entities" being HealthTrust, Property Trust, Workers'

04:03:54 1 Comp Trust, Real Estate. And then I have a total
04:03:56 2 distributions.

04:03:58 3 Q. And did you do that by year?

04:04:01 4 A. For each year '03 to 2010, inclusive.

04:04:04 5 Q. So the top line is distributions to LGC.

04:04:09 6 And then the next line is HealthTrust. So
04:04:14 7 distributions to LGC, I assume, means cash going to
04:04:18 8 LGC?

04:04:18 9 A. In this particular exhibit, what we're
04:04:20 10 looking at is only cash.

04:04:22 11 Q. And the line referring to HealthTrust, is
04:04:26 12 that money going into HealthTrust or out of
04:04:28 13 HealthTrust to --

04:04:30 14 A. Out of.

04:04:32 15 Q. So that we can remember, under the year,
04:04:36 16 it's the amount of money distributed to LGC first and
04:04:40 17 then the amount of money that came from HealthTrust
04:04:44 18 next, right?

04:04:45 19 A. Correct.

04:04:46 20 Q. Is that what this shows?

04:04:47 21 A. Correct.

04:04:47 22 Q. So in '03 there's a blank line to --

04:04:52 23 A. No. That's just the title.

04:04:54 1 Q. Oh, I'm sorry. I apologize.

04:04:59 2 A. Longer speak, it would be distributions
04:05:01 3 made by risk pools to holding companies.

04:05:06 4 Q. Got it. Okay. So in '03, what does that --
04:05:09 5 these are in thousands, so that's \$3,900,000 --

04:05:12 6 A. Right. So in '03, HealthTrust distributed
04:05:16 7 \$3.9 million to LGC Holding Company. Property-
04:05:22 8 Liability distributed one million four, rounded. And
04:05:27 9 Workers' Comp Trust, zero.

04:05:28 10 Q. '04?

04:05:30 11 A. In '04, HealthTrust just over a million,
04:05:36 12 \$34,000 from PLT, \$4,000 from Workers' Comp Trust.
04:05:44 13 '05 --

04:05:46 14 THE PRESIDING OFFICER: Excuse me. The
04:05:48 15 document can speak for itself with respect to those
04:05:50 16 two lines unless you have another question.

04:05:53 17 MR. VOLINSKY: Let's go to the last line
04:05:54 18 here.

04:05:55 19 THE PRESIDING OFFICER: Thank you.

04:05:55 20 Q. BY MR. VOLINSKY: The last column rather.
04:05:57 21 What are those totals?

04:05:59 22 A. For the years '03 to 2010 inclusive,
04:06:03 23 HealthTrust had distributed \$31 million -- I'm going

04:06:09 1 to round everything -- and PLT \$3 million and
04:06:15 2 Workers' Compensation Trust \$300,000.

04:06:20 3 Q. And then total distributions are \$34
04:06:24 4 million --

04:06:25 5 A. \$35 million rounded. There was an
04:06:30 6 intercompany transfer made that I picked up in the
04:06:32 7 consolidating financials for Local Government Center,
04:06:37 8 no details given. In the interest of erring on the
04:06:43 9 side of being conservative, I netted that unexplained
04:06:46 10 intercompany transfer from the total to get net
04:06:49 11 distributions as \$33 million.

04:06:52 12 Q. At the same time that these distributions
04:06:55 13 were coming out of the risk pools -- HealthTrust
04:07:01 14 primarily -- some from property, very small from
04:07:06 15 workers' comp -- did you also find that the Local
04:07:11 16 Government Center parent was contributing to any of
04:07:13 17 the risk pools?

04:07:14 18 A. Yes, I did.

04:07:15 19 Q. And what did you find on that score?

04:07:21 20 A. If it pleases your Honor, we can scroll to
04:07:25 21 the end results of all this, if you wish.

04:07:27 22 THE PRESIDING OFFICER: Whichever point
04:07:28 23 you'd like to make.

04:07:29 1 Q. BY MR. VOLINSKY: There you go.

04:07:31 2 A. This line here represents capital
04:07:34 3 contributions made by Local Government Center to the
04:07:40 4 Workers' Comp Trust. Over the years under review,
04:07:44 5 '03 to 2010, \$18.3 million was distributed out of
04:07:50 6 this pot monies as capital from LGC to Workers' Comp.

04:07:57 7 This second number, \$3,524,000, is
04:08:04 8 the capital contribution made by LGC in 2008 to its
04:08:08 9 real estate subsidiary, all right? And the total of
04:08:14 10 these distributions says that we can account for at
04:08:20 11 this point between the real estate subsidiary and
04:08:23 12 Workers' Comp of \$22 million, part of \$33 million
04:08:29 13 collected.

04:08:30 14 Q. And then that leaves the \$11 million figure.
04:08:34 15 Where did that come from?

04:08:35 16 A. To be explained. I need to go up more.

04:08:43 17 Q. Yes.

04:08:43 18 A. This here section of the chart tells you
04:08:45 19 where the remaining 11.7 went. And starting first
04:08:50 20 with '03, for reasons I do not know, there was no
04:08:57 21 income statement produced with respect to LGC on a
04:09:01 22 standalone basis.

04:09:02 23 The rest of the years, '04 to 2010,

04:09:06 1 are showing what LGC operating results were on a
04:09:13 2 standalone basis. These numbers here all indicate
04:09:18 3 losses.

04:09:21 4 So with the caveat that I don't know
04:09:23 5 what happened in 2003, I can tell you that LGC
04:09:29 6 Holding Company -- again, on an unconsolidated basis,
04:09:33 7 so this is a standalone -- has lost \$7.5 million. So
04:09:40 8 part of \$11 million that was unaccounted in the chart
04:09:46 9 immediately above went to finance the losses in LGC.

04:09:51 10 The remaining 3.955, call it
04:09:56 11 \$4 million, represents the increase in consolidated
04:10:00 12 assets between this ending point in 2010 of
04:10:04 13 \$9.2 million, and then if you go to '03, in this
04:10:09 14 starting point in '03 of \$5,246,000.

04:10:13 15 Q. So the term you used, "consolidated net
04:10:17 16 assets," this is what LGC parent --

04:10:22 17 A. I misspoke. I said "consolidated." This
04:10:30 18 is LGC's carried investment in the underlying
04:10:35 19 entities, not consolidated. Consolidated is a much
04:10:37 20 bigger number.

04:10:37 21 Q. And so to go from here to here --

04:10:40 22 A. Is the \$3.5 million -- \$3.955,000. Then I
04:10:49 23 had 275 that I just could not account for.

04:10:51 1 Q. So with the exception of the 275, you
04:10:54 2 accounted for all of the \$33 million contributed up
04:10:59 3 to the parent?

04:11:00 4 A. Yes. I mean, in summary, the lion's share
04:11:04 5 of this \$33 million did two things. It subsidized
04:11:08 6 the losing business model known as Workers' Comp
04:11:13 7 Trust.

04:11:14 8 And then secondly, it financed the
04:11:17 9 cost of having the holding company, which was created
04:11:20 10 as part of the '03 reorganization.

04:11:31 11 Q. You said that you had a chart earlier to
04:11:33 12 explain what happened to the \$25 million of
04:11:36 13 unrestricted net assets?

04:11:39 14 A. Again, this was the unrestricted net
04:11:42 15 assets. Think of it as excess surplus, or excess of
04:11:46 16 the targeted surplus. This was \$26 million. And the
04:11:52 17 application of that included, (a), funding the losses
04:11:58 18 in '09, which is the \$8.8 million; funding the
04:12:04 19 distribution made by HealthTrust in '09, which is
04:12:10 20 4.4. Then there was the remaining \$13.3 million,
04:12:17 21 \$9 million of which was used to bolster the net
04:12:20 22 assets board-designated in the year-to-year review.

04:12:37 23 MR. VOLINSKY: Thank you.

04:12:38 1 THE PRESIDING OFFICER: Mr. Volinsky, would
04:12:39 2 this be a good time?

04:12:43 3 MR. VOLINSKY: I was just going to suggest
04:12:45 4 that this was the time.

04:12:45 5 THE PRESIDING OFFICER: Very good. Thank
04:12:47 6 you, ladies and gentlemen. You're excused.

04:12:49 7 And the witness, as you may know,
04:12:50 8 you're excused, expected to return tomorrow to the
04:12:53 9 same place.

04:12:54 10 9:00 a.m. tomorrow, ladies and
04:12:57 11 gentlemen.

04:12:57 12 That concludes our hearing for this
04:12:59 13 afternoon. If counsel could remain for some
04:13:03 14 technical feedback, as I am told is their desire.

04:13:09 15 Thank you.

04:13:13 16 (Whereupon, at 4:13 p.m.,
04:13:24 17 the proceedings were recessed,
04:13:27 18 to reconvene on Tuesday, May 1,
04:13:38 19 2012, at 9:00 a.m.)

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C E R T I F I C A T E

1
2 I, KIMBERLY A. SMITH, Certified Shorthand
3 Reporter, Certified Realtime Reporter, and Registered
4 Diplomat Reporter in the State of New Hampshire,
5 do hereby certify that I reported in machine
6 shorthand the proceedings had at the taking of the
7 above-entitled hearing, held on the 30th day of April
8 2012, and that the foregoing is a true, complete,
9 and accurate transcript of said proceedings as appears
10 from my stenographic notes so taken to the best of my
11 ability, and transcribed under my personal direction.

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19 my Certified Shorthand Reporter seal this 13th day of
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22 _____
23 KIMBERLY A. SMITH, CSR, CRR, RDR