THE STATE OF NEW HAMPSHIRE
SUPREME COURT

2012 TERM

CASE NO. 2012-0729

APPEAL OF THE LOCAL GOVERNMENT CENTER, INC., et al.

RULE 10 APPEAL FROM AN ADMINISTRATIVE DECISION OF THE STATE OF NEW HAMPSHIRE, BUREAU OF SECURITIES REGULATION

APPELLEE'S BRIEF

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STATEMENT OF THE CASE AND FACTS

This appeal arises from a staff petition issued by the Bureau of Securities Regulation (the "Bureau") on September 2, 2011 against the Local Government Center, Inc. and a number of related corporate entities (collectively "LGC"), as well as several individual LGC officers and board members (collectively the "Individual Respondents"). Appellants' Appendix (hereafter "LGC App.") at 53. Pursuant to an Order to Cease and Desist; Order to Show Cause; and Hearing Order issued by the New Hampshire Secretary of State on September 2, 2011 and corrected on September 6, 2011, an administrative proceeding was initiated against LGC and the Individual Respondents. Appellee's Appendix (hereafter "BSR App.") at 1, 6. An Amended Petition was filed, pursuant to RSA ch. 5-B, by the Bureau on February 17, 2012 after discovery was completed. LGC App. at 107.

Risk pools function in a fashion similar to mutual insurance programs for the benefit of municipal participants ("members"). August 16, 2012 Final Order ("Order") at 26. Risk pool members pay annual premiums to obtain coverage for certain risks as permitted by statute. *Id.*; RSA 5-B:3, III. Although New Hampshire's risk pools existed before the authorizing statute was adopted in 1987, the legislature confirmed the authority of risk pools to operate in conformity with prescribed standards, but exempted them from regulatory oversight and allowed them to avoid taxation. Order at 20; RSA ch. 5-B. Amendments to RSA ch. 5-B began to implement regulatory oversight by the Secretary of State in 2009. RSA 5-B:4. Effective June 14, 2010, the Secretary of State was given his current oversight authority which is exercised through the Bureau. RSA 5-B:4-a; *see* Order at 9. Risk pools exist to serve a three-fold function. RSA 5-B:1. They provide alternatives to traditional private market insurers for sub-divisions of the State. Risk pools allow New Hampshire's political sub-divisions to be rated based upon their

own risk experience. Finally, risk pools exist to allow political subdivisions to insure against risk at a very modest cost. *See id.*; Order at 8-9. At times relevant to this proceeding, New Hampshire had two risk pools that competed with the LGC related pools; Primex and SchoolCare. Hearing Transcript ("Tr."), Vol. III (Andrews) at 433 (BSR App. 92).

Prior to 2003, when it re-organized, LGC provided coverage to its members in three areas through three separate risk pools, respectively referred to as HealthTrust (for health and dental coverage), PLT (for property and liability coverage) and WorkersComp (for workers' compensation coverage). Each risk pool had its own members and was directly beholden only to them. *See* Order at 12. The membership of each risk pool was not the same (*e.g.*, a town that bought health coverage did not also necessarily buy workers compensation coverage). *Id.* None of the risk pools had a parent corporation that it supported financially or to which it reported. *Id.* Each risk pool charged premiums based on its own claims experience and administrative costs. This all changed in 2003.

According to contemporaneous board committee meeting minutes and hearing testimony, the ostensibly independent HealthTrust risk pool began to respond to a perceived threat posed by another New Hampshire risk pool, known as Primex, by looking for a way to subsidize workers compensation offerings. *See e.g.,* BSR App. at 42 (Bureau Exhibit 42 at 56-58) and Tr., Vol. III (Andrews) at 492, 493 (BSR App. 105-06). ("The purpose of choosing workers comp as your beneficiary of...subsidy...was so that Primex would have to compete with your subsidized rates...[?] That was certainly a consideration.").[1] The then existing LGC risk pools undertook a convoluted set of corporate transfers, including use of Delaware shell companies, in an attempt to consolidate control of the LGC risk pools under a single corporate parent company with a

[1] As well, a former lieutenant of executive director John Andrews, Paul Genovese, left the LGC risk pool to run Primex. Tr. Vol. III (Andrews) at 451-52 (BSR App. 94-95).

single board of directors (the "LGC Board"). Order at 13-15. LGC "decided that they were going to operate in a manner that would allow the [LGC Board] to have complete control and dominion, by fiat, over what had been separately governed RSA 5-B pooled risk management programs."[2] *Id.* at 15. After considering the evidence and testimony presented, the Hearing Officer determined LGC's corporate re-organization violated RSA 5-B:5, I(b) and (e), and created inherent conflicts of interest with the single resulting LGC Board controlling multiple subsidiary risk pools that often had conflicting interests (*e.g.*, operating as both "landlord and tenant" or "borrower and lender"). *Id.* at 21-23. LGC did not appeal this portion of the Order. Appellants' Brief ("LGC Brief") at 1.

The resulting parent-subsidiary corporate structure facilitated the transfer of monies from HealthTrust to subsidize WorkersComp. Order at 22, 40-41. The subsidy was effected without member authorization and through opaque transfers from HealthTrust to the parent, termed "parent contributions," and then from the parent to WorkersComp. *Id.* at 40. These transfers were made each year from 2003 ($3,930,000) through 2010 ($3,875,000) and ultimately totaled $17.1 million. *Id.* at 41. On June 2, 2011, while LGC was under investigation by the Bureau, the LGC Board voted to execute a note documenting WorkersComp's responsibility to re-pay HealthTrust, but the note did not include any schedule for re-payment or interest.[3] *Id.* at 78. *See also* Tr., Vol. VIII (Carroll) at 1800-1802 (BSR App. 156-58); LGC Exhibits 279, 281 (BSR

[2] At the time of the "alleged separate votes of the boards" to consolidate into a single parent-subsidiary structure, each entity involved was "provided advice and counsel, served or staffed by the same [core group of] individuals" (*i.e.*, senior staff, consultants, actuaries, and legal counsel). Order at 20-21.

[3] The promissory note executed by the LGC board requiring WorkersComp to repay HealthTrust the sum of $17,111,804.35 states: "On June 2, 2011, the Board determined that it was in the organization's collective best interest to choose, at this time, to re-characterize the original inter-organizational transfers as a loan, and thereby provide for the repayment to HealthTrust of the previous transfers that were used to support the operation of WCT as and when WCT experiences net surplus in operations...." BSR App. 62 (LGC Exhibit 279 at ¶ C).

App. 62, 64). PLT made similar transfers in smaller amounts ranging from $34,000 to $1,398,000. Order at 41. The LGC Board made no effort to re-characterize the PLT transfers as a loan.

At the same time that the LGC parent instituted the subsidy payments, the parent also made efforts to substantially increase the net capital held by the risk pools despite the RSA 5-B:5(c) requirement that risk pools return "all earnings and surplus in excess of any amounts required for administration, claims, reserves, and purchase of excess insurance to the participating political subdivisions." *Id.* at 35. The LGC Board set publicly stated "targets" for retained capital and then commonly exceeded those targets allowing capital to grow in Health Trust from approximately $25 million in 2003 to a high of $92.7 million in 2008 to $86.8 million in 2010, the last year in which audited financial reports were provided to the hearing officer. *See* Order at 50-51, and Table 2, at 35. LGC's HealthTrust became one of the largest municipal risk pools in the nation and controlled 85% of the New Hampshire market. Tr., Vol. III (Andrews) at 426 (BSR App. 91).

Surpluses are grown by increasing the premiums charged to members.[4] *See, e.g.*, BSR App. at 53 (Bureau Exhibit 66 at 239) (According to LGC retained actuary Peter Reimer, "[t]he 5% risk charge [applied in compiling the 2003 rates] is intended to cover normal experience fluctuations and to grow Member Balance to target levels").[5] LGC built large surpluses to compete with other risk pools organized in New Hampshire. *See* Tr., Vol. III (Andrews) at 490 (BSR App. 103). Although LGC claimed to return surpluses to members in the form of rate

[4] Surplus is sometime referred to as "member balance." Order at 33.

[5] Mr. Reimer also acknowledged that net assets, or surplus, belongs to members, and members are participating cities, towns, school districts, and counties. Tr., Vol. VI (Reimer) at 1337-38 (BSR App. 129-30).

credits applied over multiple years,[6] Mr. Andrews admitted that the rate crediting was subject to manipulation in that multi-year promised reductions would be discontinued and announced decreases could be offset by other factors. *See* Tr., Vol. III (Andrews) at 420-21 (BSR App. 89-90). The Hearing Officer also found that HealthTrust overcharged members who participated in their calendar year pool by "inflating the premium rate charged to political subdivisions." Order at 54.

Ultimately, the Hearing Officer found that LGC "improperly accrued and retained unnecessary surplus funds, improperly transferred assets and improperly expended funds for purposes beyond those permitted in the statute, and fail[ed] to return excess funds to political subdivisions which are members of each individual pooled risk management program." *Id.* at 6. Further, after hearing extremely detailed, but conflicting testimony from the parties' experts and judging their credibility, the Hearing Officer made factual findings that HealthTrust held $33.2 million in surplus as of June 30, 2010 that it is required to return to HealthTrust members. *Id.* at 74-75. Similarly, the smaller PLT held $3.1 million in surplus that it is required to return to members. *Id.* at 77. The Hearing Officer also determined that the WorkersComp subsidy was not permitted under the statute and ordered the return to Health Trust of $17.1 million which is, in turn, to be returned to HealthTrust members. *Id.* at 78.

SUMMARY OF ARGUMENT

LGC cannot overcome the presumption of correctness of the Hearing Officer's detailed factual findings and identifies no reversible legal error in the Hearing Officer's Order applying RSA ch. 5-B to LGC's specific conduct. The legislature expressly authorized the Bureau to conduct adjudicatory proceedings for violations of RSA ch. 5-B, and LGC received substantial

[6] Between 2003 and 2010 LGC collected approximately $1.1 billion in premiums, but returned only $30.2 million (2.7%) to its members. Order at 46.

notice and a full opportunity to be heard through an adjudicatory proceeding that included "over 2,437 pages of transcribed dialogue and the submission of approximately 8,000 pages of exhibit documents." Order at 3. The Bureau was not required to promulgate rules prior to adjudicating LGC's violations of the evident purpose and specific standards of RSA ch. 5-B. Nor does the business judgment rule operate to protect LGC from the obligation to comply with the requirements of RSA ch. 5-B in order to maintain LGC's beneficial status as a tax-exempt statutory risk pool.

In consideration of the extensive evidence and testimony presented, and having weighed the credibility of the witnesses, the Hearing Officer reasonably interpreted and applied RSA ch. 5-B to LGC consistently with the statute's central purpose to provide low cost risk coverage to participating political subdivisions and return any excess funds not required to pay claims and administer the risk pools. The Hearing Officer made detailed factual findings related to the maximum level of capital reserves LGC could maintain and determined certain uses of member funds, such as to subsidize a separate and distinct pool, were improper and contrary to the statutory purpose. Moreover, the Hearing Officer's Order requiring LGC to currently come into compliance with the statute, in part, by returning excess surplus currently maintained by LGC did not constitute an unconstitutional retrospective application.

Finally, LGC failed to demonstrate an improper pecuniary interest in the Hearing Officer's method of payment where the Hearing Officer was paid a flat bi-weekly fee and the duration of the proceedings was driven primarily by LGC's own conduct. Further, LGC waived any argument that the Hearing Officer should have been recused by failing to raise the issue until the final day of the ten-day evidentiary hearing. LGC's dissatisfaction with the Hearing Officer's extensive and detailed factual findings is insufficient to warrant reversal.

ARGUMENT

I. Standard of Review

Pursuant to RSA 541:13, LGC bears the burden of proof to demonstrate that the Hearing Officer's order "is clearly unreasonable or unlawful." *See also* RSA 5-B:4-a, VIII. Appellate review of administrative decisions is limited, and the Court "is not free to substitute its judgment on the wisdom of an administrative decision for that of the agency making the decision." *In re Laconia Patrolman Ass'n*, 164 N.H. 552, 555 (2013) (citations omitted). "The agency's findings of fact are deemed *prima facie* lawful and reasonable. This presumption may be overcome only by a showing that there was no evidence from which the agency could conclude as it did." *Appeal of Basani,* 149 N.H. 259, 262 (2003) (citations omitted). "As a fact-finder, the hearing officer was at liberty to accept or reject the testimony before him as he saw fit and his conclusions are entitled to great weight." *Appeal of Regenesis Corp.*, 156 N.H. 445, 451 (2007).

It is "well established in [this Court's] case law that an interpretation of a statute by the agency charged with its administration is entitled to deference." *Appeal of Morrissey*, __ N.H. __, 70 A.3d 465, 470 (2013). "The deference afforded, however, is not absolute." *In re Town of Seabrook*, 163 N.H. 635, 644 (2012). This Court is "the final arbiter of the legislature's intent as expressed in the words of the statute considered as a whole," and the Court "review[s] an agency's interpretation of a statute *de novo*." *Appeal of Morrissey*, 70 A.3d at 470.

II. The Bureau's Enforcement of RSA 5-B Through a Fully-Contested Adjudicatory Proceeding Provided LGC with the Full Process Legally Due.

The consideration of due process claims requires the Court to consider two prongs: 1) "whether a legally protected interest has been implicated;" and 2) "whether the procedures provided afford adequate safeguards against a wrongful deprivation of the protected interest." *Appeal of School Administrative Unit # 44*, 162 N.H. 79, 83-84 (2011). *See also Mathews v.*

Eldridge, 424 U.S. 319, 334-35 (1976). LGC has failed to articulate a legally protected interest or an absence of safeguards to protect those interests. Instead, LGC attempts to transform an argument in favor of rulemaking into a claim that it was denied the due process of law by claiming "the Presiding Officer violated LGC's right to due process and fair notice when he imposed standards of which LGC was not afforded notice." LGC Brief at 14. As explained further *infra,* RSA 5-B:5 ("Standards of Organization and Operation") provided LGC with notice of the standards in question. The Hearing Officer made factual findings about LGC's lack of compliance with these standards. Order at 73-80. LGC also fails to establish it was denied due process at the hearing, having been provided with months of notice of the issues and having been provided with a contested ten-day hearing at which it was fully heard.[7] LGC does not demonstrate reversible error.

A. The Bureau Was Not Required to Promulgate Rules to Enforce RSA Ch. 5-B.

LGC claims the Bureau was prohibited from sanctioning LGC in an adjudicatory proceeding in the absence of administrative rules regarding the scope and intent of RSA 5-B. LGC Brief at 14. However, the authorities relied on by LGC demonstrate that the Bureau is not required to promulgate rules in order to enforce the standards set out in RSA 5-B:5. *See, e.g.*, *Nevins v. Dep't of Resources and Econ. Dev.*, 147 N.H. 484, 487 (2002) ("[P]romulgation of a rule pursuant to RSA chapter 541-A is not necessary to carry out what a statute demands on its face.") (citations omitted); *Appeal of Blizzard*, 163 N.H. 326, 330 (2012) (same) (quoting *Nevins*).

In fact, the statutory enforcement regimen that established the Secretary of State's authority to oversee risk pools also directly provides for enforcement of the statutory standards

[7] LGC's due process arguments related to recusal of the Hearing Officer are addressed separately in Section V, *infra.*

for risk pool operations through the issuance of cease and desist orders, with the opportunity for contested hearings pursuant to RSA 421-B:26-a. RSA 5-B:4-a, VI. Here, the standards of RSA 5-B:5 were factually applied by the Hearing Officer to LGC and an order issued that required LGC to comply with RSA ch. 5-B based upon the then current state of LGC's corporate organization and based on its then current audited finances.[8]

Setting aside the specific statutory grant of authority to proceed by way of adjudications, RSA 5-B:4-a, VII, LGC's arguments fail to establish the lack of statutory detail required to trigger a requirement to promulgate administrative rules. *See Blizzard*, 163 N.H. at 330 ("If the statute lacks sufficient detail on its face, then the agency must adopt rules supplying the necessary detail."). Instead, LGC extrapolates from legislative inaction to support a claim that the governing statutes lack sufficient detail, ignoring that the "legislature expresses its will by enacting laws, not by failing to do so." *Merrill v. Manchester*, 114 N.H. 722, 728 (1974). *See also Corson v. Thomson*, 116 N.H. 344, 350 (1976) ("Defendants' argument that proposed amendments to the section which failed to be enacted are indicative of the legislative intent that the director should be removed by the fish and game commission is not persuasive.").

RSA ch. 5-B contains more than sufficient clarity and specificity to support the Hearing Officer's rulings, and LGC's claims of due process violations are unpersuasive. Interpretation of RSA ch. 5-B must be informed by its statutory purpose, which is to relieve municipal overburden caused by reliance on traditional insurance that is subject to regulation and taxation. RSA 5-B:1. Risk pools are intended to be a particularly cost-efficient alternative to traditional insurance. Thus, the standards for risk pool operations require that they "[r]eturn all earnings and surplus in excess of any amounts required for administration, claims, reserves, and purchase of excess

[8] The parties agreed to rely on the 2010 audited financial statements of LGC and its affiliates as the financial reporting through June 30, 2010 was the most recent available. Order at 74. Thus, all references to LGC's "current" finances are references to the LGC's audited finances as of June 30, 2010.

insurance to the participating political subdivisions." RSA 5-B:5, I(c). Risk pools are also established to benefit New Hampshire's political subdivisions. RSA 5-B:1. Thus they are required to exist as "entit[ies] organized under New Hampshire law" and be governed by boards of a certain composition. RSA 5-B:5, I(a) and (b). These standards of operation are not unclear.

The Delaware LLCs that LGC used to affect their 2003 reorganization, for example, cannot be construed as "entit[ies] organized under New Hampshire law." Order at 13-14. No further notice of a violation of this 5-B:5, I(a) standard is necessary to comport with due process. Also, LGC was particularly aware of the 5-B standards as LGC's former executive director, John Andrews, helped draft them in 1987. *Id.* at 9-10.

Ultimately, the Hearing Officer applied the statutory standards and found LGC was out of compliance. His order enforces the Secretary's cease and desist order and describes the actions that LGC must undertake to comply with the governing statutes. In doing so, the Hearing Officer gave LGC full opportunity to contest the application of these standards, and, the true nature of LGC's complaint is simply dissatisfaction with the Hearing Officer's findings of current violations of the 5-B standards by LGC.

1. The Bureau properly applied RSA 5-B through adjudication.

The core of LGC's due process argument is that the Bureau is prohibited from interpreting or enforcing RSA ch. 5-B without first formally promulgating rules. LGC fails to recognize the Bureau's authority to interpret the meaning of RSA ch. 5-B and to develop new policy through adjudicatory actions. It is well established that administrative agencies may act through rule-making *or* adjudication. *See New Hampshire-Vermont Physician Service v. Durkin*, 113 N.H. 717, 722-23 (1973) ("The fact that [the Insurance Commissioner] proceeded in an adjudicatory rather than rule making context is irrelevant to the validity of the order in that the

Supreme Court has endorsed an agency's choice of the former ad hoc approach under circumstances where it 'may not have had sufficient experience with a particular problem to warrant rigidifying its tentative judgment into a hard and fast rule.") (quoting *SEC v. Chenery Corp.*, 332 U.S. 194, 202 (1947)). Indeed, the U.S. Supreme Court has stated that in "performing its important functions...an administrative agency must be equipped to act either by general rule or by individual order. To insist upon one form of action to the exclusion of the other is to exalt form over necessity." *SEC v. Chenery Corp.*, 332 U.S. 194, 202 (1947).

In *Chenery Corp.*, the U.S. Supreme Court established unequivocally that:

> [an] agency must retain power to deal with the problems on a case-by-case basis if the administrative process is to be effective. There is thus a very definite place for the case-by-case evolution of statutory standards. And the choice made between proceeding by general rule or by individual, ad hoc litigation is one that lies *primarily in the informed discretion of the administrative agency.*

Id. at 203 (emphasis supplied). In the context of the Bureau's regulatory authority over RSA ch. 5-B, it is within the Bureau's sound discretion to proceed through an adjudicatory action before engaging in formal rule making. The legislature's 2009 and 2010 amendments expressly gave the Secretary of State the authority to proceed by way of cease and desist orders coupled with the right to contested adjudicatory hearings pursuant to RSA 421-B:26-a. RSA 5-B:4-a, VI.

As a starting point, prior to June 29, 2009, the Secretary and the Bureau were expressly prohibited from promulgating rules with regard to RSA ch. 5-B. RSA 5-B:4 (2008) ("Nothing contained in this chapter shall be construed as enabling the department to exercise any rulemaking, regulatory or enforcement authority over any pooled risk management program formed or affirmed in accordance with this chapter."). By amendments effective June 29, 2009 and June 14, 2010, the General Court stripped this language from the statute and added section 4-

a, which granted the Bureau express enforcement authority,[9] but with a sunset provision after three years, that also was later removed from the statute.[10] RSA 5-B:4 & 4-a.

In light of the immediacy and significance of LGC's violations of the statute, it was well within the Bureau's discretion to address LGC's violations of RSA ch. 5-B through adjudication rather than a rule-making process. *Chenery Corp.*, 332 U.S. at 203. The Secretary's statutory authority afforded him this option as well. RSA 5-B:4-a, VI.

2. LGC failed to demonstrate any prejudice arising from the absence of administrative rules.

Even assuming LGC has a protected interest deserving of safeguards,[11] LGC fails to establish any prejudice from the lack of administrative rules or from the Bureau's decision to proceed via an administrative hearing. *See Blizzard*, 163 N.H. at 330 ("[W]e determine whether the result was unfair by examining whether the complaining party suffered harm as a result of the lack of required rules."). Here, the Order enforces the Bureau's cease and desist order and requires LGC to come into compliance with the standards set out in its authorizing statute in order to remain a statutory risk pool under RSA ch. 5-B. The provisions of the Order require LGC to comply with the RSA 5-B:5 standards and, depending upon the violation, gave the LGC from 90 days to over 15 months to do so. Order at 73-80. Indeed, the bulk of the relief granted by the Hearing Officer was to require LGC to return excess or surplus funds to LGC's members,

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[9] RSA 5-B:4-a authorizes the Secretary of State to conduct investigations, bring administrative actions, issue cease and desist orders, and impose penalties for violations of the statute; it does not expressly authorize or mandate rule making. References to rules in the context of violations of "this chapter or any rule or order under this chapter" imply the Secretary has general rulemaking authority, RSA 5-B:4-a, V & VI.

[10] RSA 5-B:4-a was originally set to expire effective July 1, 2013. Ch. 149:9, Laws of 2010 (LGC App. at 51-52). This sunset provision was later repealed effective June 18, 2012, Ch. 230:1, Laws of 2012 (BSR App. at 168), well *after* the Bureau initiated its administrative action against the LGC.

[11] Here, the Bureau can discern no claimed protected interest by LGC other than perhaps an assertion that LGC has a right to require the Bureau to proceed via rulemaking instead of adjudication. However, there is no such right protected by law, particularly where, as here, the legislature expressly granted to the Secretary the option of proceeding by adjudication. RSA 5-B:4-a.

the very entities who entrusted the funds to LGC. *Id.*; *See* RSA 5-B:5, I(c). It also ordered that LGC re-organize under New Hampshire law with entities directly supervised by boards, rather than employing a parent subsidiary model. *See* RSA 5-B:5, I(a) and (b).[12]

In fact, LGC received a great deal more due process through the statutorily authorized administrative hearing than it would have received through rulemaking. As a result, the Hearing Officer had a great deal more information upon which to base his factual findings. In rulemaking, the Bureau would have been required to provide LGC with reasonable written notice of a proposed rule. RSA 541-A:11, I(a). Reasonable notice may not be less than five days. *Id.* LGC would then have been permitted to submit written comments for consideration at a public hearing. *See generally* RSA 541-A:11. Publicly presented oral testimony and the opportunity to cross examine witnesses is not required at administrative rules proceedings. At most, the Bureau may have been required to provide a written rational for its proposed rule. RSA 541-A:11, VII.

By contrast, LGC enjoyed the full panoply of rights provided for by RSA 421-B:26-a. LGC had months of notice of the Bureau's intended ruling through the issuance of its complaint on September 2, 2011, more than seven months before the administrative hearing was convened. LGC App. at 53. LGC was permitted to introduce thousands of pages of hearing exhibits and elicited volumes of testimony from its witnesses at a hearing that was open to the public and live streamed on the Internet. Order at 3. LGC also fully confronted the entirety of the Bureau's case through the cross examination of each and every Bureau witness, as well as through pre-hearing depositions of each expert designated by the Bureau.[13] Indeed, it is difficult to imagine any greater level of process that could have been afforded to the LGC. Given the substantial advance notice provided to LGC of the claims raised by the Bureau and the Bureau's interpretation of the

[12] The LGC has not appealed the portions of the Order that required corporate re-organization.

[13] The LGC was further provided with extensive reports compiled by the Bureau's experts months before the hearing. *See* Bureau Exhibit 68.

statute, LGC's claimed prejudice from the "disruption and expense of an enforcement action" was not caused by lack of notice. Indeed, LGC had ample opportunity to settle the dispute with the Bureau as did the two other risk pools then in existence. *See* LGC App. at 258, 276.

Given the extensive process provided to the LGC, even assuming the LGC had demonstrated a legally protected interest that was substantial, "the risk of an erroneous deprivation...is minimal." *Appeal of School Administrative Unit # 44*, 162 N.H. 79, 84-85 (2011). Avoiding an erroneous determination is the crux of a due process analysis. *See id.*

> The purpose of notice under the Due Process Clause is to apprise the affected individual of, and permit adequate preparation for, an impending "hearing." To satisfy due process, the notice must be of such nature as reasonably to convey the required information and must be more than a mere gesture. Due process, however, does not require perfect notice, but only notice reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections.

Id. 162 N.H. at 87 (citations and quotations omitted). However, LGC does not, and indeed could not, claim a lack of notice of the matters to be contested at the adjudicatory hearing. Instead, it suggests that the statute was too vague to allow it to comply with its terms.[14] This argument misses the mark as far as due process is concerned because LGC did not receive any additional penalty for its failure to comply with the standards set out in RSA 5-B:5. Instead, its arguments were heard and its evidence considered by the Hearing Officer and it was then ordered to comply with the statutory standards, no more and no less. Further, LGC was fully permitted to make its case. LGC, therefore, has failed to demonstrate any prejudice arising from the absence of administrative rules and this Court should not find a violation of due process.

B. The Protections of the Business Judgment Rule Do Not Apply to an Administrative Action Enforcing a Statute Against a Corporate Entity.

LGC argues that the "business judgment rule" insulates LGC from an order requiring

[14] Nevertheless, LGC does not challenge the constitutionality of RSA ch. 5-B on vagueness grounds.

compliance with the standards of RSA ch. 5-B. This unsupported assertion is based on a misapplication of the business judgment rule. Because the business judgment rule is designed to protect individual board members from liability and provides no protection or excuse for LGC's violation of RSA ch. 5-B, LGC's reliance thereon is without merit.

The "business judgment rule" is a common law precept incorporated into many state statutory schemes,[15] that "creates a presumption that in making a business decision, the directors of a corporation acted on an informed basis (i.e., with due care), in good faith and in the honest belief that the action taken was in the best interest of the company." *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 360 (Del. 1994) (citations omitted). The purpose of the rule is to "shield directors from personal liability arising out of completed actions involving operational issues." *Unitrin, Inc. v. American General Corp.*, 651 A.2d 1361, 1374 (Del. 1995). *See also McMullin v. Beran*, 765 A.2d 910, 917 (Del. 2000) ("[T]he business judgment rule...operates to protect the individual director-defendants from personal liability for making the board decision at issue.").

Critically, the focus of the business judgment rule is on *individual liability* of directors and officers. While the business judgment rule "shields directors and officers from liability," *Black's Law Dictionary* at 192 (7th ed. 1999), it has no applicability to questions of corporate statutory compliance. The instant appeal addresses the Hearing Officer's findings that LGC, as a group of corporate entities, violated the standards of RSA ch. 5-B. The Hearing Officer found no individual board member liable and did not impose sanctions beyond those necessary to affect compliance (i.e., no fines were imposed and restitution and disgorgement were only alternative

[15] In New Hampshire the business judgment rule is codified in RSA 293-A:8.30, which provides that a "director is not liable for any action taken as a director, or any failure to take any action, if he performed the duties of his office" in "good faith," with "the care an ordinarily prudent person in a like position would exercise under similar circumstances," and in "a manner her reasonable believed to be in the best interests of the corporation." RSA 293-A:8.30(a) & (d).

forms of relief).[16] Order at 73-80. As such, a rule protecting directors from individual liability has no place in either the Hearing Officer's or this Court's analysis.

The LGC's argument twists the concept of the business judgment rule into an alleged grant of nearly complete discretion to the LGC Board to take any action the Board in "good faith" believes is in the company's best interests. Even setting aside whether the LGC Board's decisions were made in good faith,[17] no amount of good intentions can remedy a statutory violation. For example, where a "good faith" decision to avoid payment of taxes might absolve corporate directors from individual liability, it would not exempt the corporation from its legal obligation to pay taxes that were due. Similarly, LGC's violations of RSA 5-B are not excused by any alleged good faith business discretion exercised by the LGC Board.

Indeed, even in cases of a director's individual liability, a director's decision to violate a statute is not protected by the business judgment rule. *See, e.g., Miller v. American Telephone & Telegraph Co.*, 507 F.2d 759, 762 (3d Cir. 1974) ("Where...the decision...is itself alleged to have been an illegal act...the business judgment rule cannot insulate the defendant directors from liability if they did in fact breach [the statute] as plaintiffs have charged."); Fletcher's Cyclopedia of the Law of Corporations, § 1040 ("There are a number of other situations where the business judgment rule will not be applied," including "where the directors committed...an illegal act...."). Here, the LGC made decisions to violate RSA 5-B:5 by, for example, registering as a Delaware LLC and by not returning surplus to its members.

Finally, even assuming that the business judgment rule might apply in this context, LGC derives no protection from the rule because the business judgment rule does not apply where the

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[16] The Hearing Officer declined to "Order the Respondents to pay administrative fines for each violation of RSA ch. 5-B and RSA ch. 421-B" as requested by the Bureau. LGC App. at 143 (Prayer H).

[17] The Hearing Officer found the evidence "weigh[ed] heavily against and diminish[ed] both the weight and the credibility of the evidence offered by the witnesses called by LGC" that LGC "always 'acted in the members' interests.'" Order at 58.

directors are "interested" in the transaction. RSA 293-A:8.31 ("A conflict of interest transaction is a transaction with the corporation in which a director of the corporation has a direct or indirect interest."). Here, all of the members of the LGC Board had an indirect interest in any transaction involving two or more of the LGC entities governed by the single board of the parent.[18] *Id.* ("[A] director of the corporation has an indirect interest in a transaction if...(2) another entity of which he is a director...is a party to the transaction and the transaction is or should be considered by the board of directors of the corporation.").

Where directors are interested in a transaction, the business judgment rule is rebutted and "the burden shifts to the defendant directors, the proponents of the challenged transaction, to prove to the trier of fact the 'entire fairness' of the transaction to the shareholder plaintiff." *Cede & Co.*, 634 A.2d at 361. Thus, even if the business judgment rule were applicable here, which it is not, the rule does not apply to decisions of the inherently conflicted LGC Board.

III. The Hearing Officer's Order is Consistent with the Purpose and Language of RSA Ch. 5-B and the Remedies Imposed Do Not Exceed the Scope of His Authority.

LGC argues that the Hearing Officer impermissibly exceeded his authority by imposing requirements that are not expressly spelled out in RSA ch. 5-B. LGC demonstrates no error by the Hearing Officer. At the outset, LGC erroneously relies on a line of cases regarding promulgation of administrative rules that are in conflict with, or add requirements that are inconsistent with, the statute administered by the administrative agency. LGC Brief at 16-18. *See Appeal of Anderson*, 147 N.H. 181, 183 (2001) (finding rule requiring application for disability within 60 days of termination of employment "arbitrary and unreasonable as applied" to individual whose disability became permanent more than 60 days after termination); *Appeal of*

[18] The Hearing Officer found "an immediate conflict of interest problem" following consolidation of governance of all three risk pools under a single LGC Board, resulting in the LGC Board acting as both landlord and tenant or lender and borrower in single transactions. Order at 21-22.

Mays, 161 N.H. 470, 476 (2011) (finding rule requiring applicant for CPA license to have experience in a licensed public accounting firm invalid where statute required only experience under the supervision of a licensed CPA). These cases do not involve adjudicative proceedings.

In any event, LGC misconstrues the applicable limit on administrative authority to promulgate rules. As set forth in *Appeal of Anderson*, "[i]f an administrative rule reasonably and effectively carries out the legislative purpose, it will be upheld." *Appeal of Anderson*, 147 N.H. at 183. Thus, even in the rulemaking context, the central question is consistency with clear legislative purpose. Here, the Bureau reasonably interpreted the requirements of RSA ch. 5-B consistently with the stated purpose of the statute, and enforced the statute through an adjudicatory proceeding.

On appeal, LGC must do more than present an alternative interpretation of the statute in order to overcome the Hearing Officer's ruling. RSA 541:13 (administrative decision "shall not be set aside or vacated except for errors of law, unless the...order is unjust or unreasonable"); *In re Laconia Patrolman Ass'n*, 164 N.H. 552, 555 (2013) (the Court shall not "substitute its judgment on the wisdom of an administrative decision for that of the agency making the decision") (citations omitted). Moreover, as the agency expressly charged with administering and enforcing Chapter 5-B, the Bureau's interpretation of the statute is entitled to deference. *Appeal of Morrissey*, __ N.H. __, 70 A.3d 465, 470 (2013). In the absence of a showing that the Hearing Officer's ruling applying the Bureau's statutory interpretation directly conflicts with RSA ch. 5-B or is inconsistent with the statute's express purpose, this Court should uphold the Hearing Officer's Order. Here, the Hearing Officer's Order is based on reasonable interpretations of RSA ch. 5-B that are rooted firmly in effectuating the express purpose of the statute.

A. The Central Purpose of RSA ch. 5-B is to Benefit Member Political Subdivisions.

The purpose of RSA ch. 5-B was set forth by the legislature at RSA 5-B:1:

> The purpose of this chapter is to provide for the establishment of pooled risk management programs and to affirm the status of such programs *established for the benefit of political subdivisions of the state*. The legislature finds and determines that insurance and risk management is essential to the proper functioning of political subdivisions; that risk management can be achieved through purchase of traditional insurance or by participation in pooled risk management programs *established for the benefit of political subdivisions*; that pooled risk management is an essential governmental function by providing focused public sector loss prevention programs, *accrual of interest and dividend earnings which may be returned to the public benefit* and establishment of costs predicated solely on the actual experience of political subdivisions within the state; that the resources of political subdivisions are presently burdened by the securing of insurance protection through standard carriers; and that pooled risk management programs which meet the standards established by this chapter should not be subject to insurance regulation and taxation by the state.

RSA 5-B:1 (emphasis supplied). The legislature's repetition of the phrase "established for the benefit of political subdivisions" leaves no doubt that the purpose of authorizing pooled risk management programs is to benefit municipalities and other political subdivisions of the state that make up the Members of a risk pool.[19] Moreover, the statute specifically expresses the intent to reduce the costs of obtaining insurance coverage and to return surplus funds to the Members for the public benefit. *See* RSA 5-B:5, I(c).

Consequently, it is through the lens of the clear legislative intent and evident purpose that the Hearing Officer's application of RSA ch. 5-B must be reviewed. *Doggett v. Town of North Hampton Zoning Bd. of Adjustment*, 138 N.H. 744, 746 (1994) (holding statutes must be construed "so as to effectuate their evident purpose"). The Hearing Officer's findings that LGC's actions were in violation of RSA ch. 5-B were consistent with and rooted in this statutory purpose and should not be disturbed. *See* Order at 10 (citing purpose of RSA ch. 5-B).

[19] Indeed, this phrase is repeated two additional times in the statute. *See* RSA 5-B:3, III; RSA 5-B:4.

B. LGC's Preferred Interpretations of RSA Ch. 5-B Fail to Demonstrate Any Reversible Legal Errors by the Hearing Officer

LGC enumerates six areas where it claims the Hearing Officer committed legal error by failing to defer to the LGC Board's business judgment and by imposing requirements not specifically set forth in the statue. LGC's claims are actually challenges to the Hearing Officer's factual findings and enforcement of the Bureau's reasonable interpretation of RSA ch. 5-B. LGC fails to demonstrate reversible legal error by the Hearing Officer on any of the issues raised. All of the factual findings enjoy support in the record. *See Appeal of Basani,* 149 N.H. 259, 262 (2003) ("presumption [of correctness] may be overcome only by a showing that there was no evidence from which the agency could conclude as it did.") (citations omitted).

1. The Hearing Officer's reserve requirements are reasonable and appropriate factual findings.

It is undisputed that RSA 5-B:5, I(c) is unique among statutes authorizing pooled risk management programs in that it specifically requires the return of all excess surplus funds to the Members of risk pools.[20] RSA 5-B:5, I(c) (mandating that each pooled risk management program shall: "[r]eturn *all* earnings and surplus in excess of any amounts *required* for administration, claims, reserves, and purchase of excess insurance to the participating political subdivisions") (emphasis supplied). Similarly, LGC does not dispute that this mandate functionally sets a limit on the amount of excess reserves LGC may accumulate. *See* Order at 55-56 (discussing interplay between return of surplus and reasonable "target" for permissible reserves).

Accordingly, the Hearing Officer was required by the adjudicative process to factually determine the amounts required "for administration, claims, reserves, and purchase of excess

[20] The Hearing Officer appropriately discounted the relevance of reports on the reserve levels allowed in other states, and in some instances related to insurance companies as opposed to risk pools, finding that there was no evidence any of the other jurisdictions "are subject to a statute like ours that mandates a return of funds to political subdivisions in excess of the costs of administration, claims, reserves and purchase of reinsurance." Order at 36.

insurance" and, having done so, he properly ordered the return of funds held in excess of the required amounts by each pool.[21] The parties offered very different perspectives of what amounts were required to be held by the pools. Each presented factual and expert testimony on this point. *Compare, e.g.*, Testimony of Bureau's expert Michael Coutu, Tr., Vol. I at 160 (BSR App. 72) ("So again, the indication of investing...in longer than... 24 [months] to 10-plus years tells me that...Health Trust is over capitalized...mean[ing] that there's more surplus on the balance sheet than what is necessary...."), *with* testimony of LGC's expert, Peter Reimer, Tr., Vol. VI at 1289-91 (BSR App. 120-22). The Hearing Officer was required to factually determine the proper amount to be held. After reviewing the evidence and testimony, the Hearing Officer chose to permit amounts similar to those amounts retained by the two other risk pools, Primex and SchoolCare, after they negotiated risk pool practices agreements with the Bureau. *See* Order at 75, and LGC App. at 258 and 276 (the risk pool practices agreements).

The required amounts found by the Hearing Officer were more than those recommended by the Bureau. *See* Tr., Vol. IV (Atkinson) at 668 (BSR App. 112); Order at 29-30. The required amounts were determined by the Hearing Officer after consideration of multiple ways of analyzing the issue. The Bureau presented the testimony of Atkinson, a qualified actuary, who used computer modeling to determine that a lesser quantity of reserves was required for risk pool operations and that more excess or surplus could be returned. Order at 30-31. A second expert called by the Bureau, Michael Coutu, determined that health care is a "short tail line" of insurance.[22] *Id.* at 53. A "short tail line" means that claims are generally determined in less than three years and the insurer or risk pool must only reserve funds with that short time frame in

[21] "[T]he statute's formula for returns is straightforward, *i.e.* Earnings + Surplus – (costs of administration + costs of claims + reserves + cost of reinsurance) = Amount returned to member political subdivisions." Order at 45.

[22] LGC's actuarial expert agreed. Tr., Vol. VI (Reimer) at 1341 (BSR App. 133).

mind. *Id.* Yet, over half of LGC Health Trust's investments exceeded five years in length in 2010. *Id.* Based on this, Mr. Coutu concluded that the LGC's Health Trust was grossly overcapitalized and retained surplus that should have been returned to members.[23] Tr., Vol. II at 220 (BSR App. 82) ("2008 the excess surplus would be [64,648,000]. In 2009 the excess surplus would be 44,991,000, and in 2010 the excess surplus would be 43,706,000.").

Based on the evidence and testimony presented, the Hearing Officer reasonably determined that investments maturing over periods longer than dictated by the short tail nature of health coverage are excess surplus not required to pay claims. Order at 53. Finally, in factually concluding that 15% of claims or an RBC of 3.0 was an appropriate upper limit of capital for LGC's Health Trust to maintain, the Hearing Officer considered the LGC's past practices and statements, including:

- testimony by LGC's CFO, Sandal O'Keefe that in 1997 Health Trust was financially sound when its excess surplus dropped to only 7.6% of claims (or approximately an RBC of 1.22). Order at 33;
- the historic capital levels near 15% of claims between 1998 and 2003, before LGC improperly altered its corporate structuring. *Id.* at 34; and
- HealthTrust's ability to rapidly increase its excess capital when desired. *Id.* at 35.

Contrary to the LGC's claims, the Hearing Officer's Order does not assert that RSA ch. 5-B requires a specific level of reserves in all cases. Rather, the Hearing Officer made findings based on the facts adduced before him and a strong part of the factual predicate involved credibility findings. In particular, the Hearing Officer relied on figures that showed the LGC Health Trust often overshot its stated target for capital, sometimes by as much as over 50%.

> These hard figures weigh heavily against and diminish both the weight and the credibility of evidence offered by witnesses called by the LGC, Inc., and its

[23] The Hearing Officer ordered the return by Health Trust of $33.2 million in surplus, approximately $12 million less than the more than $45 million Health Trust held in long term investments with five years or more to maturity. *See* Order at 53.

> entities and the sole witness called by respondent Carroll that the LGC, Inc. and its entities always "acted in the members' interests." These figures also contribute to my determination that the LGC, Inc. and its entities paid little attention, if any, to the requirement that funds in excess be returned to members of pooled risk management programs. Therefore by reasons of the actions and practices undertaken by the LGC, Inc. and its entities detailed above, the hearing officer finds that those entities have violated the provisions of RSA 5-B:5, I (c).

Id. at 58. Based on these factual findings, as well as other evidence and testimony related to LGC's practices of arbitrarily increasing its excess capital, the Hearing Officer properly established a threshold level of reserves above which additional funds would necessarily be deemed excess surplus that must be returned to Members pursuant to RSA 5-B:5, I(c). Moreover, the parties are given discretion to vary from the foregoing limits in future years, if, in their good faith exercise of their responsibilities, it is concluded that a variation is merited. *See Id.* at 77-78.

Finally, LGC argues that agreements entered into between the Bureau and the two other risk pools in the state, PRIMEX and SchoolCare, are inconsistent with the Hearing Officer's ruling. LGC Brief at 10.[24] The three risk pools are not treated differently. The reserve threshold of RBC 3.0 established by the Order is not a target imposed by statute, but a factual determination, based on the facts particular to LGC and its health coverage, of when the reserve level becomes unreasonable and contrary to the intent and meaning of RSA 5-B:5's requirement to return excess surplus to the members. The Bureau engaged in a similar effort with Primex and SchoolCare during the negotiating process, in which LGC participated. *See* LGC App. 259-60,

[24] LGC has not, as it suggests, been handicapped by being afforded less discretion to control its operations than Primex and SchoolCare Boards through their respective negotiations with the Bureau. LGC Brief at 10. The Primex Board, pursuant to its negotiated agreement, agreed to adopt the same Risk Based Capital formula to compute reserves and surplus (RBC of 3.0) that the Hearing Officer imposed on LGC. *Compare* LGC App. at 263, §3.4 *with* Order at 77. Primex has further agreed that it will only increase this RBC value with 30 days prior notice to the Bureau and a published statement of all reasons supporting an increased amount of retained surplus. LGC App. At 262, §3.1. SchoolCare has agreed to a similar level of retained earnings, but calculated using the Stochastic method. LGC App. at 281, §3.2. SchoolCare also agreed to the 30 day advance notice provision. *Id*

§1.7 (Primex) and 277-78, §1.8 (SchoolCare). LGC fails to establish that the Hearing Officer's Order with regard to reserves is "unjust or unlawful," and the Order should be upheld.

2. Return of excess surplus annually as cash or cash equivalents is consistent with the purpose and language of RSA ch. 5-B.

LGC next argues that the Presiding Officer erred by requiring return of excess surplus as cash rather than through LGC's complex and opaque rate stabilization method. LGC Brief at 23-24. LGC supports its argument, in part, by stating that its members "wanted surplus returned by rate stabilization." RSA 5-B:5, I(c) unequivocally requires the return of excess earnings and surplus to members. The statute should be read in conjunction with the statutes that concern municipal budgeting, which is to be done annually, absent a specific municipal vote to approve non-lapsing funds.[25] LGC's rate stabilization system is discretionary by the LGC (*i.e.*, the targeted return of surplus may not be carried out) and takes place over multiple years. Tr., Vol. III (Andrews) at 420-21 (BSR App. 82-83). Further, the proof elicited established that LGC's rate stabilization is illusory because LGC, at the same time it claims to return surplus as a credit, arbitrarily raises other risk factors used to calculate premiums that serve to offset its return of surplus. *Id.* The testimony also established that the LGC held other additional amounts of capital as a result of having added margins to its calculations of reserves required to pay claims. *See* Tr., Vol. VI (Reimer) at 1359-61 (BSR App. 151-53). Therefore, the Hearing Officer's requirement that excess earnings and surplus be returned annually is both reasonable and prudent, and forms no basis for reversal of the Order.

[25] *See, e.g.*, RSA 32 and 35. Under New Hampshire municipal budget laws, municipalities budget in gross, which means the municipalities generally account for all sources of revenues each year, RSA 32:5, III, without off-book revenue sources. These same laws contemplate that municipal appropriations will lapse at the end of each year. RSA 32:7. This means that municipalities, absent special circumstances, do not maintain surpluses. *Id.* These municipal budgeting concepts are completely consistent with the prohibition against pools maintaining surpluses year to year as pools are no more than associations of municipalities. LGC also budgets annually. *See* RSA 5-B:5, I(d).

Similarly, RSA 5-B:5's mandate that pooled risk management programs return "*all* earnings and surplus in excess of any amounts *required* for administration, claims, reserves, and purchase of excess insurance to the participating political subdivisions" must be read to effectuate the overall statutory purpose of providing low-cost risk management coverage. RSA 5-B:5, I(c). LGC's rate-stabilization method of "returning" surplus funds is statutorily inadequate because it fails to return "all" earnings and surplus to Members. By its plain language, the term "return" contemplates the repayment of surplus funds to Members, not an actuarial estimation that functionally results in LGC retaining a portion or all of annual surplus funds.

3. LGC's subsidization of WorkersComp was properly found to violate RSA 5-B

LGC claims that "[n]othing in RSA 5-B supports the Presiding Officer's conclusion that HealthTrust's strategic support for Workers' Compensation risk pool from 2000 forward was unlawful." LGC Brief at 26. The Hearing Officer made the following factual findings:

1. LGC diminished otherwise available surplus that could have been returned to members by "taking funds from the health and property liability programs to subsidize the operation of a workers compensation pooled risk program," Order at 40;

2. WorkersComp was "financially deficient, *i.e.*, insufficient premiums were paid to cover all claims and administration of claims costs," *Id.*;

3. The members of WorkersComp were different than the members of the health and property liability programs; *Id.;*

4. The payments to subsidize WorkersComp "were done in violation of a specific inter-entity loan policy that existed . . . within LGC . . . and without compensation to health trust and property liability trust," *Id.*; and

5. "Further, the LGC, Inc.'s manner of reporting these transfers...on the financial statements...made it unnecessarily difficult...for a member reviewing the financial statements to discern the actual purpose of the transfer as a subsidy...for a separate risk management program to which that member did not subscribe." *Id.*

In short, the Hearing Officer made factual findings, with support in the record, that the LGC-controlled entities propped up a financially deficient program by transferring funds from successful programs in violation of its own policies. Nothing in RSA ch. 5-B supports the claim that these transfers were permitted.

Ultimately, the Hearing Officer concluded that the $17.1 million subsidy paid to WorkersComp must be repaid to Health Trust. The Hearing Officer's conclusion was rooted in the statutory requirement that all surplus funds be returned to members. RSA 5-B:5, I(c). Because a subsidy to WorkersComp was not "administration, claims, reserves, [or] purchase of excess insurance," RSA 5-B:5, I(c), the funds used to subsidize WorkersComp were necessarily excess surplus required to be returned to the members of HealthTrust. Moreover, the LGC Board did not disclose or obtain member consent for the transfer of HealthTrust member funds to subsidize a separate program with non-identical membership. LGC's argument that its actions were made in good faith and in the best interest of the company was soundly rejected by the Hearing Officer, Order at 21-22, and LGC presents no legal error warranting reversal of the Hearing Officer's factual findings.

4. The Order properly requires LGC to purchase reinsurance.

RSA ch. 5-B contemplates the purchase of reinsurance as a reasonable and prudent administrative cost of operating a 5-B pool. LGC, however, chose to amass excessive net assets in order to "self-insure" for catastrophic claims. Order at 47-48. The Hearing Officer reasonably found this decision to violate RSA 5-B:5, I(c) in that it resulted in the retention of excess surplus that should have been returned to members. *Id.* at 48-49. The expense of reinsurance is more than offset by the tens of millions of dollars in excess net assets retained by LGC to self-insure for catastrophic events, and the Hearing Officer's findings are reasonable. Further, LGC charged

members higher premiums to build up its capital by replacing the risk factor that represented a charge for the cost of reinsurance with a risk factor for "pooling risk." Tr. Vol. VI (Reimer) at 1344-45 (BSR App. 136-37) ("stop loss" reinsurance charge at 4% of premiums in 2011 replaced with "pooling fee" at 4.2% in 2012).

5. The Hearing Officer did not take any action related to LGC's administrative expenses

LGC also argues that the Hearing Officer erred in finding LGC's defined benefits retirement program and no-work consulting agreement with Mr. Andrews unreasonable expenditures in violation of RSA ch. 5-B. LGC Brief at 26. The Hearing Officer properly determined that these expenses are not reasonable administrative costs, but did not order their return as separate instances of improperly retained excess surplus. Order at 43-44. Thus, the Hearing Officer's factual findings, which are presumed to be reasonable and lawful, do not present a legal error.

6. LGC waived any claim to exclude its alleged capital assets from excess surplus.

Finally, LGC briefly argues that approximately $2.2 million of the $33.2 million in excess surplus ordered to be returned to members of the HealthTrust should be exempt because it represents capital assets such as furniture and computers. LGC waived this argument by failing to raise it at the hearing. LGC Brief at 24-25 (omitting reference to any argument at hearing). Moreover, the Hearing Officer's calculation of a threshold reserve level does not implicate specific administrative expenses or capital assets.

IV. The Hearing Officer's Order Was Not an Unconstitutional Retrospective Application of RSA 5-B:4-a.

LGC next misconstrues the Order and argues that the requirement to repay the $17.1 million WorkersComp subsidy constitutes an unconstitutional retrospective enforcement of

R.S.A ch. 5-B because the bulk of the transfers that make up the $17.1 million subsidy occurred before the Bureau was given full enforcement powers in 2010. LGC, however, overlooks the express language of the Order and LGC's acts to ratify its obligation to repay the $17.1 million subsidy that occurred in June 2011, after RSA 5-B:4-a was enacted.

In reference to the $17.1 million subsidy to WorkersComp, the Hearing Officer wrote, "These represent funds that, if not transferred as improper subsidy payments, could have been returned to the members of the health trust and members of the property liability program, in whole or in part, during the years in which they were transferred, *or can be returned presently as excess earnings and surplus*." Order at 41 (emphasis supplied). The fact that the transfers occurred at a time before the Secretary of State had enforcement powers does not make these subsidies legal.

The question is, may the Bureau currently enforce the law, and, on this point, the emphasized phrase above is critical to establish that the Order is based on the currently existing state of affairs. WorkersComp has not been dissolved or discontinued. It currently exists. It was combined with PLT in 2007. *Id.* at 41, n. 28. As it currently exists today, WorkersComp is $17.1 million to the better for having received the improper subsidy.

As well, the language of the very note executed in June 2011 with respect to the $17.1 million subsidy is instructive. The promissory note executed by the LGC Board requiring WorkersComp to repay HealthTrust the sum of $17,111,804.35 states:

> [O]n June 2, 2011, the Board determined that it was in the organization's collective best interest to choose, *at this time*, to re-characterize the original inter-organizational transfers as a loan, and thereby provide for the repayment to HealthTrust of the previous transfers that were used to support the operation of WCT as and when WCT experiences net surplus in operations...."

LGC Exhibit 279 at ¶ C (emphasis supplied). The LGC Board refused to establish a schedule for repayment or impose interest. *Id. See also* LGC Exhibit 281 (associated LGC Board vote). The LGC Board thus acted to HealthTrust's detriment by not requiring prompt repayment or imposing interest. *See* Order at 40, n. 27. The Order requires repayment by December 1, 2013 and permits WorkersComp to borrow the necessary funds from a commercial lender, presumably at market rates and terms. *Id.* at 78.

LGC's failure to repay the subsidy is a current and ongoing violation of RSA 5-B:5, and the Hearing Officer properly ordered its reimbursement to HealthTrust. The Hearing Officer's interpretation of the statute presents no reversible legal error. 2A Norman J. Singer & J.D. Shambie Singer, *Sutherland Statutory Construction* § 45:12 (7th ed. 2007) ("When one of several possible interpretations produces an unreasonable result, that is a reason for rejecting that interpretation in favor of another which would produce a reasonable result.").

Moreover, that the Bureau's enforcement action "might have a retroactive effect [is] not necessarily fatal to its validity." *Chenery Corp.*, 332 U.S. at 203. The United State Supreme Court in the *Chenery* case held that:

> Every case of first impression has a retroactive effect, whether the new principle is announced by a court or by an administrative agency. But such retroactivity must be balanced against the mischief of producing a result which is contrary to a statutory design or to legal and equitable principles. If that mischief is greater than the ill effect of the retroactive application of a new standard, it is not the type of retroactivity which is condemned by law.

Id. Once again, allowing WorkersComp to retain millions of dollars of surplus funds that were required to be returned to HealthTrust members far outweighs any ill effect of alleged retroactive application of a finding against LGC. The standards set out in RSA 5-B:5 were in place and were violated by the payments of the subsidy when those payments were made. It is only the particular means of enforcing these operational standards that changed in 2010 with the adoption

of R.S.A. 5-B:4-a. Where LGC has no right to retain surplus member funds, there can be no prejudice to enforcing the standards of the statute.

V. The Court Should Reject LGC's Claim that It Was Denied Due Process Based on an Alleged Pecuniary Interest of the Hearing Officer.

A. LGC Waived Any Due Process Claim With Respect To The Presiding Officer By Waiting Until the Final Day of the Evidentiary Proceeding to Raise the Issue.

LGC waived any claim concerning the Hearing Officer's alleged pecuniary interest in the proceeding because it did not raise the issue until the final day of the parties' ten-day evidentiary hearing and the Hearing Officer had disclosed his pay arrangement to LGC more than six months prior. Tr., Vol. X at 2305 (BSR App. 160).[26] "[W]hen a cause of recusation or exception to a judge exists," it is waived "by a defendant who, knowing the existence of just grounds of recusation, appears, and, without objecting, makes defense." *Stearns Adm'r v. Wright Adm'r*, 51 N.H. 600, 1872 WL 4342, at *8 (1872); *see also In re Abijoe Realty Corp.*, 943 F.2d 121, 126 (1st Cir. 1991) ("In general, one must raise the disqualification of the...[judge] at the *earliest* moment after [acquiring] knowledge of the [relevant] facts.") (emphasis in original) (internal quotations and brackets omitted). LGC waited more than six months between learning of the Hearing Officer's pay arrangement and raising objection, and the Court should deem their due process argument waived.

At a hearing on October 4, 2011, the Hearing Officer responded to an inquiry from LGC's lead counsel concerning his pay arrangement. BSR App. at 32. He disclosed that he had a contract with the State of New Hampshire that was equivalent to what he earned in his prior

[26] The Appendix citation refers to a transcript that Kristina Mann, assistant to undersigned counsel, prepared of an audio-recording of an October 4, 2011 hearing at which the LGC's counsel inquired as to the pay arrangement of the Hearing Office. LGC did not object to the accuracy of Ms. Mann's transcript, so it should be taken as a true and accurate record of the hearing. The audio recording of the hearing is available at http://sos.nh.gov/nhsos_content.aspx?id=43884.

position with the State and paid him in increments of $5,000.00. *Id.* at 34.[27] He further disclosed that his contract ran through approximately December 22, 2011, but that it had been represented to him that the contract would be extended if the dispute was not resolved by that time. *Id.* The Hearing Officer advised counsel for LGC to file a "Right to Know" request under RSA Ch. 91-A if he wanted more information. *Id.* at 33.[28] LGC did not raise the issue of the Hearing Officer's compensation again until May 11, 2012—the final day of the parties' ten-day evidentiary hearing. Tr., Vol. X at 2305 (BSR App. 160). By that time, LGC had an opportunity to make a judgment about how its case was fairing in front of the Hearing Officer. Preventing a litigant from determining the favorability of the adjudicator to its case before it raises grounds for recusal is the reason courts require parties to raise the grounds at the earliest possible time. *See In re Cargill, Inc.*, 66 F.3d 1256, 1263 (1st Cir. 1995). That is precisely what LGC has tried to do here, and the Court should find it has waived its claim.

B. LGC Has Failed to Identify Any Pecuniary Interest that the Hearing Officer Had in the Proceedings.

LGC argues that it was denied due process because the Hearing Officer had a pecuniary interest in the proceedings. "Administrative officials that must serve in an adjudicatory capacity are presumed to be of conscience and capable of reaching a fair and just result." *Appeal of Maddox a/k/a Cookish*, 133 N.H. 180, 182 (1990). The LGC attempts to overcome this presumption of fairness by arguing that the Hearing Officer had a pecuniary interest in the duration and outcome of the proceedings. With respect to the length of the proceedings, LGC claims that the Hearing Officer increased his compensation by denying LGC's dispositive

[27] LGC has suggested that the Hearing Officer actually earned more than he did when he was a State employee. It is notable, however, that the Hearing Officer received no benefits in connection with his contract, *see* LGC App. at 166-73, whereas he received benefits when the State employed him.

[28] There is no evidence that LGC filed a Right to Know request prior to requesting the Hearing Officer's recusal on the last day of the evidentiary hearing.

motions because the denials meant that he would continue to be paid to conduct the rest of the proceedings. This argument necessarily assumes that there was merit to the dispositive motions, because if the motions were without merit, the Hearing Officer had no choice but to deny them. LGC did not appeal the Hearing Officer's rulings on the dispositive motions, meaning that this Court may assume that all matters that the motions challenged were well-pled and that LGC perceives no substantive error in the denial of the motions. *See also* RSA 421-B:26-a, XIX (providing that participants in adjudicatory proceedings pursuant to this chapter do not have the right to a pre-hearing ruling on dispositive motions). Moreover, the length of the proceedings was the result of the actions of LGC and not the Hearing Officer. LGC requested continuances and extra time throughout the proceedings, including requesting a briefing schedule that specifically ran through the end of the Hearing Officer's then-current contract, and a continuance of the trial in order to accommodate the schedule of its lead counsel. *See* BSR App. at 13-15. LGC sought these extensions after the Hearing Officer had disclosed to it that he expected his contract would be renewed if the parties could not resolve their dispute during its initial term, so it cannot claim that it did not know what effect its requests would have. Thus, although LGC seeks to create a pecuniary interest via the duration of the proceedings, it cannot show that the Hearing Officer took any action that prolonged the proceedings other than deny its dispositive motions—rulings that LGC did not appeal.

Similarly, LGC cannot show its rights were violated because the Hearings Officer had any pecuniary interest in the outcome of the proceedings. It attempts to make this showing by citing to two cases from California. A crucial difference between this case and the California matters (other than the fact that both California parties raised the recusal issue at their first opportunity) is that both California cases involved serialized proceedings, whereas the

proceeding below was the first of its kind. *See Lucky Dogs, LLC v. City of Santa Rosa*, 913 F. Supp. 2d 853, 860 (N.D. Cal. 2012) ("The City is a repeat player."); *Haas v. County of San Bernardino*, 45 P.3d 280, 289 (Cal. 2002). The serialized nature of the California hearings matters because both California courts were concerned that the adjudicator's prospect of future employment with the government conducting similar hearings could result in government favoritism. *See Lucky Dogs*, 913 F. Supp. 2d at 861; *Haas* at 289. There is no evidence in the appellate record of any such prospect here, nor is it likely that such evidence exists. All parties acknowledge that this hearing was the first of its kind, and the fact that the Bureau settled with LGC's two competitors makes it unlikely that another such hearing would occur. *See* LGC App. at 258, 276. As such, the prospect that the Secretary would re-hire the Hearing Officer to conduct an adjudicatory hearing involving another insurance risk pool if he ruled in its favor in this proceeding is too remote to create any pecuniary interest in the outcome.

In the absence of evidence of actual impropriety, LGC has attempted to imply that the Hearing Officer acted improperly by stating that he was paid on a "flat fee" basis. LGC claims that this statement did not adequately put it on notice of the total amount of compensation the Hearing Officer might receive. This assertion is unsupported in the record. The Hearing Officer advised LGC in October 2011 that he was paid in $5,000.00 bi-weekly increments, that his agreement ended in late December 2011, and that it had been represented to him that his contract would be renewed if the proceedings had not concluded by that time. *See* BSR App. at 34. The most LGC can say is that the Hearing Officer's agreement was, in fact, renewed. It cannot show that the Hearing Officer ever "renegotiated" his contract because it cannot show that the incremental rate of $5,000.00 ever changed. That is, the fee for two weeks of service remained "flat" regardless of the amount of time spent or the results of the hearing. Moreover, if LGC had

further questions about the Hearing Officer's compensation arrangement, it could have filed a Right-to-Know request under RSA ch. 91-A as the Hearing Officer advised it to do in October 2011. *See* BSR App. at 33.

Thus, where LGC cannot identify any improper conduct on the part of the Hearing Officer, where it fails to point to any record evidence showing that the Hearing Officer had an interest in future employment with the State, and where it cannot show that the Hearing Officer's conduct had any effect on the duration of the proceedings save his pre-hearing rulings, which LGC did not appeal, it has demonstrated no pecuniary interest on the part of the Hearing Officer that would have warranted recusal.

C. LGC's Approach to Recusal Is at Odds with Public Policy.

LGC has asserted that the appropriate way to conduct a hearing under RSA ch. 421-B is to employ a full-time adjudicatory officer in order to eliminate the prospect that a hearings officer would be influenced by future re-employment or the duration of the proceedings. Thus, LGC would have the Bureau pay a hearings officer to have him or her available to conduct future proceedings that LGC has provided no reason to believe will occur with any regularity in order to eliminate the possibility, however remote, that such officer would have a pecuniary interest in the proceeding. This approach would forbid the course the Secretary has chosen, consistent with statute, to employ a hearings officer only as needed. *See* RSA 421-B:26-a (allowing the Secretary of State to appoint a hearings officer to adjudicate proceedings under the chapter). The Bureau is not required to engage in likely wasteful spending in order to eliminate the remote contingency of which LGC complains. Accordingly, the Court should reject LGC's approach.

VI. The Award of the Bureau's Reasonable Costs and Attorneys' Fees Was Proper.

After failing to acknowledge the Bureau's good faith effort to comply with the Order's

requirement that the Bureau and LGC confer to reach agreement on the amount of fees and costs due to the Bureau, LGC now attempts to find fault in an aspect of the Order that does not exist. LGC claims that the Order requires LGC to repay "all of the Bureau's costs," LGC Brief at 34, yet the costs submitted by the Bureau did not include fees for those claims on which the Bureau did not prevail. In any case, even if LGC's claims were true, they would at most constitute grounds for a reduction in the fee award; they do not justify reversal of the Order.

CONCLUSION

For all of the foregoing reasons, the Bureau respectfully requests that this Honorable Court uphold the Hearing Officer's August 16, 2012 Final Order.

ORAL ARGUMENT

Appellee requests 15 minutes for oral argument by Andru Volinsky.

Dated this 26th day of September, 2013

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that two copies of the foregoing Appellee's Brief and the accompanying Appendix were provided to counsel of record for the Local Government Center, Inc. and its affiliates, Preti Flaherty and Ramsdell Law Office, and for the *Amicus Curiae*, Howard & Ruoff, P.L.L.C., by U.S. Mail, postage prepaid, this 26th day of September, 2013.

Andru H. Volinsky, Esq.