

BEFORE THE INSURANCE COMMISSIONER AND THE
ATTORNEY GENERAL OF THE STATE OF IOWA

In the matter of the joint application)	
of WORLD MUTUAL HOLDING)	
COMPANY and AMERICAN REPUBLIC)	FINDINGS OF FACT,
MUTUAL HOLDING COMPANY for)	CONCLUSIONS OF LAW
approval of a plan to merge WORLD)	AND ORDER
MUTUAL HOLDING COMPANY with)	
and into AMERICAN REPUBLIC)	(Iowa Code ch. 521)
MUTUAL HOLDING COMPANY)	
)	

I. INTRODUCTION

WORLD MUTUAL HOLDING COMPANY (“World”) is a Nebraska domestic mutual insurance holding company. AMERICAN REPUBLIC MUTUAL HOLDING COMPANY (“American Republic”) is a mutual insurance holding company organized and licensed under Iowa law.

Iowa Code chapter 521 provides that both the Iowa insurance commissioner and the Iowa attorney general (“the Commission”) must approve proposed plans of merger for mutual insurance holding companies. World and American Republic (“Applicants”) jointly applied to the Commission for approval of a proposed plan to merge World with and into American Republic.

Notice of hearing was issued on December 19th, 2003. Notice was also posted on the Iowa Insurance Division’s (“the Division”) website.

Pursuant to Iowa Code section 521.4 (2003), and at Applicants’ request, the Commission held a public hearing regarding the proposed merger on Monday, December 29th, 2003 at the Division for the purpose of determining whether authorization of the merger is appropriate under the requirements of Iowa Code section 521.8 (2003).

II. JURISDICTION

The Commission has jurisdiction over this proceeding under Iowa Code sections 521.3, 521.4, 521.5 and 521.8 (2003).

III. EVIDENCE PRESENTED

Both American Republic and World presented evidence at the hearing. American Republic’s evidence included the testimony of Michael E. Abbott, its president and chief executive officer. World presented the testimony of Tom D. Eilers, its president. Also submitted in support of the proposed merger were several exhibits, including the

November 7, 2003 order of the Nebraska director of insurance approving the proposed merger and the actuarial opinion and testimony of Milliman USA principal and consulting actuary Daniel J. McCarthy, M.A.A.A., submitted on behalf of American Republic.

All submitted evidence was admitted without objection and is part of the record considered by the Commission in issuing the following findings, conclusions and order.

No one appeared at the hearing to oppose Applicants' requests or otherwise offer evidence to contradict or question Applicants' submission of evidence required under Iowa Code chapter 521.

IV. FINDINGS OF FACT

The filings of record, other documentary evidence and witness testimony comprising the record in this matter support the following findings:

Iowa Code section 521.8 (2003) permits the Commission to authorize a proposed merger if (1) satisfied that the interests of the affected members are properly protected, and (2) no reasonable objection to the proposed merger exists.

A. Whether the interests of American Republic's members are properly protected by the plan of merger.¹

Iowa Code section 521.8 (2003) requires a finding by the Commission as to whether the interests of American Republic's members are properly protected by the plan of merger.

World owns World Insurance Company ("World Insurance"). World Insurance's principal insurance product is major medical insurance. (Trans. at 18.) It also writes Medicare supplement policies, other accident and health products and some life insurance products. (*Id.*) Mr. Abbott stated that World Insurance's products complement American Republic's. (*Id.*; Ex. 6 at 2.)

Mr. Abbott characterized growth as "critical" to the immediate and long-term needs of American Republic. (Trans. at 60.) If approved, the proposed merger is a significant move forward for American Republic financially. (*Id.* at 21.) Combined capital and surplus will exceed \$250 million, with American Republic being roughly 35 percent larger in terms of capital and surplus and 30 percent larger in terms of members. (*Id.* at 21, 53; Ex. 6 at 3.) American Republic will enjoy a combined block of major medical

¹ Iowa Code section 521.8 directs the Commission to assess whether the interests of affected "policyholders" are properly protected under a proposed merger plan. Because American Republic is a mutual insurance holding company, it has no policyholders. Rather, it has "members" whose interests will be affected by the proposed merger of World with and into American Republic. For the purposes of this proceeding, the Commission will construe section 521.8 as requiring an assessment of whether American Republic's member interests are properly protected by the proposed merger. This construction is consistent with the statutory intent of chapter 521, which seeks to protect the interests of policyholders/members of mutual companies.

business that will be twice as large as the individual blocks currently managed by both companies. (Trans. at 21.) American Republic will also be approximately 48 percent larger as a company in terms of assets and 53 percent larger in terms of net premiums written by its insurance company subsidiaries. (*Id.* at 53; Ex. 6 at 3.) The post-merger company will be able use World's surplus in excess of its liabilities for the growth American Republic is seeking. (Trans. at 84.)

In Mr. Abbott's opinion, the proposed merger does not dilute existing American Republic members' interests in any measure. (Trans. at 53; Ex. 6 at 3.) These existing interests will be virtually unchanged after the proposed merger if approval is granted. (*Id.*; Ex. 6 at 4.)

It appears that the proposed merger will be beneficial to American Republic members in other ways. American Republic will enjoy increased brand and product flexibility. (Trans. at 24.) Its viability and financial stability will be enhanced through the addition of World Insurance's established independent distribution system of marketing and broker relationships as another channel through which American Republic can sell major medical and dental insurance and other medical insurance products. (Trans. at 23; Ex. 2 at 2.)

American Republic's long-term ability to compete in the ever-consolidating insurance and financial services marketplace will be enhanced by the proposed merger, which will allow American Republic to continue offering quality products and services to its members. (Ex. 2 at 2.) As a larger holding company, American Republic will be better able to monitor health care trends, analyze experience, negotiate discounts with providers, and weather volatility in the marketplace. (Trans. at 25, 62, 113.)

The proposed merger will also afford American Republic synergies and efficiencies from economies of scale through integration of services. (Trans. at 56; Ex. 2 at 3; Ex. 6 at 5.) Redundancies will be eliminated. (Trans. at 23.) Some functions now performed by World Insurance will be relocated to and integrated within American Republic's home office in Des Moines. (*Id.* at 56; Ex. 6 at 5.) Integration will allow American Republic to take advantage of World Insurance's more efficient technology platform, allowing it to migrate from a mainframe to PC-based system. (Trans. at 21-22, 85-86.) This will reduce the cost of American Republic's support technology, particularly in the claims processing area, and result in significant savings. (*Id.* at 22.)

All of the positive changes resulting from the merger will mean a better overall delivery of services by American Republic and a better-positioned merged company in the long term. Better delivery of services by a better-positioned merged company translates into better value for American Republic's existing members now and into the future.

These findings are confirmed by the testimony of Mr. McCarthy and supporting exhibits. As noted above in Section III, Mr. McCarthy is a principal and consulting actuary with Milliman USA. He has extensive experience evaluating changes in corporate form, including mutual insurance holding company merger transactions. (Trans. at 30.) He

reviewed the proposed merger plan for fairness to American Republic members from an actuarial point of view. (*Id.* at 31.) His conclusions are in evidence. (*Id.* at 30-34; Ex. 8, Ex. 9 at 1-2, Ex. 23.)

Among other things, Mr. McCarthy determined that the proposed merger will not change the nature of American Republic members' membership rights nor their previously held dividend expectations. (Trans. at 31.) The proposed merger poses "a very modest risk," and "the long term prospects for the merged entity are excellent," providing American Republic with the size and resources needed to successfully compete in the health care insurance field today. (*Id.* at 44, 32.) He stated that, after transaction costs are accounted for, the proposed merger has approximately \$82 million of value to American Republic. (*Id.* at 34.) All of these factors translate into better value for American Republic members in the future. (*Id.*) In Mr. McCarthy's expert opinion, the proposed merger is fair to American Republic members from an actuarial point of view. (*Id.* at 31; Ex. 9 at 2.)

The Commission also notes that American Republic conducted an extensive due diligence examination of World. (Ex. 6 at 6.)

The Commission finds that American Republic's member interests are properly protected by the proposed merger of World with and into American Republic.

B. Whether any reasonable objection to the plan of merger exists.

Iowa Code section 521.8 (2003) also requires a finding by the Commission as to whether any reasonable objection to the plan of merger exists.

The benefits of the proposed merger articulated in Section IV (A) above need not be repeated here except to underscore the lack of any reasonable objection to the plan of merger in the record presented. Taken as a whole, the record establishes that the proposed merger ultimately will benefit American Republic, its existing members, potential members, and ultimately the public at large.

The Commission finds that no reasonable objection to the plan of merger of World with and into American Republic exists.

The record collectively establishes that the proposed merger meets the requirements of Iowa Code section 521.8 (2003). The Commission finds that American Republic member interests are properly protected by the proposed merger and no reasonable objection to approval of the proposed merger exists.²

² Much cross examination testimony at the hearing was devoted to Applicants answering the Commission's questions about the executive compensation package three current World senior executives will receive. This compensation package is an integral part of the transaction, was approved by World's board, and will be paid by World.

In justifying this package, witnesses placed great weight upon a Towers Perrin report summarizing its conclusions "regarding the competitiveness of compensation paid to the senior executives of World

V. CONCLUSIONS OF LAW

The legislature has vested discretion in the Commission not only to hold hearings and make factual findings, but also to interpret and apply the law. Iowa Code sections 521.3 and 521.8 permit the Commission to approve a proposed plan of merger if it determines that the Applicants sufficiently demonstrate the two criteria listed within section 521.8 to the Commission.

All evidence in the record relevant to chapter 521 requirements was considered by the Commission, whether or not specifically referenced herein. After a careful review of the record, the Commission concludes, upon substantial evidence, that the proposed plan of merger meets the two requirements of Iowa Code section 521.8 (2003).

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Insurance during the period 1991-2002.” (Ex. 11, at 1.) (Towers Perrin is a nationally recognized New York actuarial and consulting firm.) The gist of the report, issued during the pendency of merger negotiations between World and American Republic, is that these three executives collectively are owed approximately \$7.5 million in additional compensation from World for services rendered over the last twelve years. The Towers Perrin author of this report was unavailable for examination at the hearing.

Mr. Abbott testified that American Republic is the guarantor of two of World’s financial obligations associated with the compensation package. (Trans. at 57-59.) He further testified that these guarantees were negotiated, and that each guarantee “carr[ies] very little risk” to American Republic due to World’s “very significant strong financial capabilities.” (Trans. at 67.) Even in the very unlikely event that American Republic would become obligated to pay under both of these guarantees, Mr. Abbott affirmed that “the merger is still a good deal for American Republic.” (Trans. at 90.)

As noted above, World is the primary obligor for the compensation package. Whether this compensation package is fair to World or its members is a question reserved for the Nebraska Department of Insurance (“the Nebraska Department”)—the sister state agency possessing regulatory authority over World as its domestic licensee. The Nebraska Department has already answered this question affirmatively. Its November 7, 2003 order approving World’s participation in the proposed merger was issued with the knowledge of World’s concomitant obligation to pay this compensation package.

The Commission thus takes no position on this question. American Republic’s contingent and secondary obligation attendant to this compensation package does not change the Commission’s finding that American Republic and its members will collectively benefit from the merger and the Commission’s conclusion that the requirements of Iowa Code section 521.8 have been met under the record presented.

ORDER

IT IS THEREFORE ORDERED that:

Applicants' application for approval of a plan to merge World Mutual Holding Company with and into American Republic Mutual Holding Company is **APPROVED**.

This Order shall be considered final agency action for the purposes of Iowa Code chapter 17A (2003). Any action challenging this Order shall comply with the requirements of Iowa Code chapter 17A.

Any application for rehearing shall comply with the requirements of Iowa Code section 17A.16.

DATED this 8th day of January, 2004.

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Iowa Insurance Commissioner

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