

**MANAGED CARE
MERGERS AND ACQUISITIONS**

**REVIEW OF ACTIVITIES
OVER THE LAST 2 YEARS
AND CERTAIN OBSERVATIONS**

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Introduction

- The national managed care index has outperformed the S&P 500 by 500% over the last five years up to the end of 2005
- Managed care industry consolidation has accelerated over the last 30 months

Introduction

- The overall recent merger and acquisition transaction mix reflects certain trends impacting the health care market, including:
 - Strong profits
 - Positive commercial and governmental reimbursement environment
 - Excellent prospects for new growth opportunities (Medicare, Consumer Driven Health Plans)
 - Rising health care costs

Introduction

- The overall recent merger and acquisition transaction mix reflects certain trends impacting the health care market, including:
 - Interest in Medicare plans as a result of the Medicare Modernization Act of 2003
 - The competitive threat of the two leaders of the managed care industry, “United HealthCare” and “WellPoint”

NOTABLE RECENT DENTAL PLAN TRANSACTIONS

■ Mergers & Acquisitions

- **Safeguard** has completed three acquisitions over the past three years
 - GE Dental & Vision in 2005
 - Health Net Dental & Vision in 2004
 - Ameritas Dental in 2003

NOTABLE RECENT DENTAL PLAN TRANSACTIONS

- Mergers & Acquisitions
 - **BrightNow! Dental** has completed three acquisitions in the past three years
 - Castle Dental Centers in 2004
 - Newport Dental in 2004
 - Monarch Dental in 2003

NOTABLE RECENT DENTAL PLAN TRANSACTIONS

- Mergers & Acquisitions

- United HealthCare completed two acquisitions in 2005
 - Pacific Union Dental/Pacific Dental Benefits
 - PacifiCare Dental

NOTABLE RECENT DENTAL PLAN TRANSACTIONS

- Mergers & Acquisitions
 - **WellPoint** completed one acquisition in 2003
 - Golden West Dental in 2003

NOTABLE RECENT DENTAL PLAN TRANSACTIONS

■ Affiliations Arrangements

- **Safeguard** has entered into four affiliation arrangements over the past three years
 - Nevada Care—Medical/Dental Joint Marketing in 2005
 - MetLife—Dental PPO/HMO Joint Marketing in 2005
 - Horizon Behavioral Services—Mental Health/Dental Joint Marketing in 2004
 - Humana Dental—Dental Service Area Expansion Joint Marketing in 2003

NOTABLE FULL-SERVICE MANAGED CARE PLAN TRANSACTIONS

- Mergers & Acquisitions
 - **United HealthCare** has completed over \$16 billion in acquisitions over the past 3½ years
 - QualChoice for undisclosed amount in April 2006
 - John Deere for \$500M
 - Pacificare for \$8.2B
 - Neighborhood Health for an undisclosed price
 - Definity for \$300M

NOTABLE FULL-SERVICE MANAGED CARE PLAN TRANSACTIONS

- Mergers & Acquisitions
 - **United HealthCare** has completed over \$16 billion in acquisitions over the past 3½ years
 - Oxford for \$4.9B
 - Golden Rule for \$500M
 - Touchpoint for \$40M
 - Great Lakes for \$37M
 - MAMSI for \$2.6B

NOTABLE FULL-SERVICE MANAGED CARE PLAN TRANSACTIONS

- Mergers & Acquisitions
 - **Wellpoint** has completed three major acquisitions in the past three years
 - WellChoice for \$6.5B in 2005
 - Lumenos for \$185M in 2005
 - Anthem for \$14B in 2004

NOTABLE FULL-SERVICE MANAGED CARE PLAN TRANSACTIONS

■ Mergers & Acquisitions

- Aetna has completed four acquisitions in the past two years
 - HMS HealthCare for \$390M in 2005
 - Strategic Resource Co. for \$250M in 2005
 - Active Health Management for \$400M in 2005
 - Magellan Health Services in 2004

NOTABLE FULL-SERVICE MANAGED CARE PLAN TRANSACTIONS

- Mergers & Acquisitions
 - **PacifiCare** has completed three acquisitions in the past three years (prior to merger with United Health)
 - Pacific Life Insurance Company in 2005
 - American Medical Security Group for \$515M in 2004

NOTABLE FULL-SERVICE MANAGED CARE PLAN TRANSACTIONS

- Mergers & Acquisitions
 - **Coventry Health** completed two acquisitions
 - First Health Group for \$1.8B in 2005
 - Omnicare for \$36.2M in 2004

NOTABLE FULL-SERVICE MANAGED CARE PLAN TRANSACTIONS

- Mergers & Acquisitions
 - **Humana** completed two acquisitions
 - CarePlus Health Plan-Florida for \$444M in 2005
 - Ochsner Health Plan in 2004

NOTABLE FULL-SERVICE MANAGED CARE PLAN TRANSACTIONS

- Affiliations

- Aetna entered into a strategic alliance

- BenefitPoint in 2005 (Customer relationship management company)

REASONS FOR ACQUIRERS IN MANAGED CARE PLAN MERGERS & ACQUISITIONS

- Mergers and Acquisitions activity has been strong and has been fueled by positive sector outlooks, strategic positioning, and growth objectives
 - Reduced ability by managed care plans to achieve membership growth through marketing or organic growth
 - Economies of scale – ability to spread administrative costs over a large membership base in order to compete/grow earnings

REASONS FOR ACQUIRERS IN MANAGED CARE PLAN MERGERS & ACQUISITIONS

- Mergers and Acquisitions activity has been strong and has been fueled by positive sector outlooks, strategic positioning, and growth objectives
 - Eliminate Competitors
 - Product Expansion: Provide access to new products (e.g. Medicare or Consumer Directed Plans) to secure higher earnings and stability e.g. dental
 - Maintain Position: To maintain position in certain market segments (e.g. Commercial or Medicare)

REASONS FOR ACQUIRERS IN MANAGED CARE PLAN MERGERS & ACQUISITIONS

- Mergers and Acquisitions activity has been strong and has been fueled by positive sector outlooks, strategic positioning, and growth objectives
 - Provide access to new geographic service areas for medical and specialized products
 - Cross-Selling Opportunities (includes use of alliances)
 - Availability of Acquisition capital at relatively low interest rates and high stock valuations – significant motivating factor. Many acquirers use their stock as currency

ACQUISITION CONSIDERATION

- **05 Wellchoice / Wellpoint:**
 - 50% cash / 50% stock
- **05 Pacificare / United Health:**
 - 27% cash / 73% stock
- **04 Oxford / United Health:**
 - 28% cash / 72% stock
- **03 Wellpoint / Anthem:**
 - 24% cash / 76% stock
- **03 MidAtlantic / United Health:**
 - 29% cash / 71% stock

RATIONALE FOR SELLERS IN MANAGED CARE PLAN MERGERS & ACQUISITIONS

- Provider sponsored plans may be motivated to be sellers because they cannot support the growth and capital investment required to operate a competitive managed care company in today's environment
- High valuation

MARKET TRENDS

- General Public Company Merger and Acquisition Trends
 - The annual transaction value of mergers and acquisitions are increasing, however the volume is decreasing due to the lack of available companies for acquisition
 - 1995 (18 public managed care companies)
 - 2000 (15 public managed care companies)
 - 2005 (8 public managed care companies) plus IPO's of 2 additional companies in 2005 – total is 10

MARKET TRENDS

- General Public Company Merger and Acquisition Trends
 - Strong consolidation trend
 - Dominance of 2 major players
 - Rising scale of enterprises

MARKET TRENDS

■	<u>Market Cap -- May 2006</u>	
■	1. United Health	59.2 B
■	2. Wellpoint	45.6 B
■	3. Aetna	21.8 B
■	4. Cigna	11.1 B
■	5. Coventry	8.4 B
■	6. Humana	8.3 B
■	7. Healthnet	5.0 B
■	8. Sierra	2.3 B
■	9. Healthspring	900M
■	10. Universal American	817M

MARKET TRENDS

- Public Market Valuation Trends
 - Following continued profitability, valuation multiples for public companies had been rapidly increasing until the end of 2005 Strong consolidation trend

MARKET TRENDS

- Private Equity Trends

- During the first quarter of 2006, increased activity in the health care venture capital market pushed both dollar total and deal volume to levels that rival the late nineties

GROWTH OPPORTUNITIES

- Medicare Advantage Opportunity
 - Medicare Advantage together with the Prescription Drug Plan are estimated to be a \$100B revenue opportunity

GROWTH OPPORTUNITIES

- Medicare Managed Care
 - Medicare beneficiary participation in managed care is only 13% compared to 95% in the commercial market
 - Aging of baby boomers will make Medicare an even more attractive market
 - Competition between Medicare managed care plans will result in the provision of "supplemental benefits" by the plans to attract members.

GROWTH OPPORTUNITIES

- Medicare Managed Care
 - Commercial Market – lower opportunity for organic growth
 - 70% in PPO's or POS Plans
 - 25% in HMO's (Calif. 49%)
 - 5% fee for service

GROWTH OPPORTUNITIES

- Medicare Managed Care Mergers, Acquisitions and other Transactions
 - CareMore Medical Group located in Los Angeles (approximately 20,000 Medicare lives for \$260 million in 2006)
 - HealthSpring (50% equity interest in approximately 80,000 Medicare lives for \$170 million in 2005, company subsequently went public and raised \$300 million in 2005)
 - Stratus Capital, a private equity firm that is focused on the Medicare sector, paid \$200 million for a controlling interest in **MMM**, a Medicare Advantage Plan with 77,000 members in Puerto Rico in 2005

GROWTH OPPORTUNITIES

- Medicare Managed Care Mergers, Acquisitions and other Transactions
 - Universal American Financial acquired Heritage Health Systems, a Medicare Plan with 15,700 members in Texas for \$98 million in 2004
 - IPO completed in June 2005

GROWTH OPPORTUNITIES

- Consumer Driven Health Care/Healthcare Savings Accounts
 - Healthcare savings account enrollment is expected to grow to six million in 2008 and 18 million in 2012
 - Universal American Financial acquired Heritage Health Systems, a Medicare Plan with 15,700 members in Texas for \$98 million in 2004

GROWTH OPPORTUNITIES

- Consumer Driven Health Care/Healthcare Savings Accounts
 - **United HealthCare**
 - Definity Health for \$300M in 2005.
 - **WellPoint**
 - Luminous for \$185M in 2005.

GROWTH OPPORTUNITIES

- Impact of Consumer Driven Healthcare on Dental
 - Workers can deposit funds for dental plan premiums and routine dental care

STATE LAW REGULATORY ISSUES

- In California, the Department of Insurance and California Department of Managed Health Care reviews all mergers and acquisitions, and may impose conditions on approval of the transaction

STATE LAW REGULATORY ISSUES

- Steps in California DMHC Regulatory Review Process
 - Waiver of Statutory Review Time Period (fast track review process waiver of 20 day time frame to respond to filings)
 - Schedule Public Hearings
 - Review Filing and Documents

STATE LAW REGULATORY ISSUES

- Steps in California DMHC Regulatory Review Process
 - Complete Undertakings
 - Work with Department of Insurance to Ensure Consistency
 - Decision-Making Process (Approve or Deny)

STATE LAW REGULATORY ISSUES

- Issues Raised in Recent Mergers & Acquisitions
 - A plan must maintain organizational and administrative capacity to timely provide health care services
 - DMHC reviews proposed merger's effect on the California Health Care Market, including market consolidation and anti-competitive effects, commitment to the community

STATE LAW REGULATORY ISSUES

- Issues Raised in Recent Mergers & Acquisitions
 - Change in control severance payments and retention bonus payments payable by reason of the Merger not payable by the California licensed entity
 - Prohibition on declaration of dividends or other distributions unless the plan maintains up to 150% of tangible net equity, sufficient working capital, and 79% of net income from the year prior to the calendar year

STATE LAW REGULATORY ISSUES

- Issues Raised in Recent Mergers & Acquisitions
 - No affiliate company distributions unless the Plan maintains 150% of average monthly total expenses based on the two most recent quarterly financial reports
 - Must obtain state approval to assume, co-sign or guarantee affiliate loans, pledge assets or capital for loans, or borrow funds for affiliate company distributions

STATE LAW REGULATORY ISSUES

- Issues Raised in Recent Mergers & Acquisitions
 - Must provide the state with annual certifications that methodology for premium rates, plan benefit designs, and other practices have not changed post-merger
 - Plan prohibited from terminating any group or individual health plan contracts prior to expiration of its term, except as otherwise permitted by law

STATE LAW REGULATORY ISSUES

- Issues Raised in Recent Mergers & Acquisitions
 - Plan required to participate in a Healthy California by committing substantial amounts to provide social benefits for underserved communities to promote community health projects

FUTURE TRENDS

- Continuing consolidation of full service platforms and specialized plans to fill gaps within geographic areas of expansion and broaden product offerings to create differentiation in order to compete more effectively

FUTURE TRENDS

- Growth in the Development of Medicaid Advantage managed care plans
- Increasing consolidation of newly developed Medicare Advantage managed care plans as they begin yielding earnings

FUTURE TRENDS

- Alliances, Mergers or Acquisitions between Medicare Advantage managed care plans and dental plans that provide the dental plan product as a supplemental Medicare benefit to attract fee-for-service Medicare beneficiaries who do not have dental coverage
- Stiffening regulatory challenges to consolidation as financial pressure is placed upon providers and employee groups

CASE STUDIES

- **UnitedHealth Group Acquisition of Pacificare Health Systems**

- *Announced July 2005; Closed December 2005*

- **Transaction Highlights**

- Valued on announcement at over \$9 billion, the sale of PacifiCare represents the second largest acquisition ever in the managed care industry

CASE STUDIES

■ Strategic Rationale

- UnitedHealth attains a significant membership base and network in California and the Northwest, augmenting its national network
- As PacifiCare is the nation's largest Medicare Advantage provider, the transaction allows UnitedHealth to gain a significant foothold in this business segment
- UnitedHealth gains access to PacifiCare's internal Pharmacy Benefit Manager

CASE STUDIES

- **WellPoint Acquisition of WellChoice**

- *Announced September 2005*

- **Transaction Highlights**

- WellChoice provides a variety of health benefits and managed care plans to over five million members, primarily in New York state and the New York city metropolitan area
 - Transaction value: \$5.9 billion

CASE STUDIES

■ Strategic Rationale

- Strengthens WellPoint's position in providing health benefits to national accounts with multi-state operations; New York City is the headquarters of more Fortune 500 companies than any other U.S. city, providing WellPoint with a strategic presence in this important market
- Consistent with WellPoint's goals toward consumer-driven health plans
- Ability to spread administrative costs over a larger membership base