JOINT PUBLIC HEARING

before

ASSEMBLY INSURANCE COMMITTEE

AND THE

ASSEMBLY HEALTH AND HUMAN SERVICES COMMITTEE

"On the issue of the financial condition of health maintenance organizations (HMOs) in the State and recent HMO insolvencies, including Omnicare/The HMO"

January 22, 1991
Cunningham Center
Cumberland County College
Vineland, New Jersey

MEMBERS OF ASSEMBLY HEALTH AND HUMAN SERVICES COMMITTEE PRESENT:

Assemblyman George J. Otlowski, Chairman
Assemblywoman Ann A. Mullen

ALSO PRESENT:

Assemblyman Fred Scerni
District 2

Assemblyman Anthony J. "Skip" Cimino
District 14

Thomas K. Musick
Office of Legislative Services
Aide, Assembly Insurance Committee

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Hearing Recorded and Transcribed by
Office of Legislative Services
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Hearing Unit
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MICHAEL F. ADUBATO
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New Jersey State Legislature
ASSEMBLY INSURANCE COMMITTEE
STATE HOUSE ANNEX, CN-068
TRENTON, NEW JERSEY 08625-0068
(609) 984-0445

NOTICE OF JOINT PUBLIC HEARING

The Assembly Insurance Committee and the Assembly Health and Human Services Committee will hold a joint public hearing on the issue of the financial condition of health maintenance organizations (HMO's) in the State and recent HMO insolvencies, including Omnicare/The HMO.

The hearing will be held on **Tuesday, January 22, 1991 at 10:30 a.m. in the Cunningham Center of Cumberland County College, Vineland, New Jersey.**

The public may address comments and questions to Thomas K. Musick or Carolyn S. Mealing, Committee Aides, and persons wishing to testify should contact Cynthia D. Petty, secretary, at (609) 984-0445.

Those persons presenting written testimony should provide 20 copies to the committees on the day of the hearing.

Directions to Cumberland County College:

FROM NORTH JERSEY:
New Jersey Turnpike to Exit 7 (Bordentown).
295 South to Rt. 42 South Atlantic City Exit.
Rt. 42 South 1 Mile to Rt. 55 South.
Rt. 55 South to Exit 29 Rt. 552 East (Sherman Avenue).
Sherman Avenue to Blinker Light.
***RIGHT** at Blinker Light - Cumberland County College on the Right.

FROM SOUTH JERSEY:
Garden State Parkway Exit 36 to Rt. 40 West.
Rt. 40 West to Mays Landing.
1 Mile Past Mays Landing, Make Left at Light and Fork in the Road on to Rt. 552 (Mays Landing Road).
Take Rt. 552 (Mays Landing Road) to Sherman Avenue.
Right on Sherman Avenue (Rt. 552) Through Two Lights.
At the First Blinker Light Make a Left on College Drive.
Cumberland County College on the Right.

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ASSEMBLYMAN GEORGE J. OTLOWSKI (Chairman): First of all, let me apologize for being late. We had a flat tire. Would you believe it? I'm terribly sorry. I just realized now that we are running a half-an-hour behind schedule. (brief discussion here regarding microphones)

This hearing, of course, is intended primarily to fulfill a legislative function; namely, we want to determine what kind of legislation, if any, is needed to cope with the problems you have had in this area with HMO organizations. As a matter of fact, the 20 HMOs we have in the State-- The record has been pretty good over the years. It is my understanding that only four out of the 20 wound up with a problem. There are close to a million people participating in this system.

The unfortunate thing that has happened in this area, of course, is what concerns us primarily. We are going to be dealing with our testimony on the basis of what happened, how it happened, and what is needed to correct it or to avoid it. I particularly want to express my thanks to Mayor Ed Salmon, who arranged for this hearing so we could get the benefit of what happened firsthand, how it happened, and how it can be avoided.

Frankly, with that I would like to conclude, unless-- What we are going to do later on is call on Assemblyman Cimino, who is proposing legislation. But first what we are going to do, of course, is call upon Assemblyman Salmon, who is from this district. Ed, we're ready for you, if you will? All right?

A S S E M B L Y M A N E D W A R D H. S A L M O N: Thank you very much, Mr. Chairman and members of both Committees. I think I would like to start off first on behalf of the 18,000 subscribers of Omnicare HMO, which is no longer in existence. My thanks to you for coming here to the district, and for accepting my request that an investigative hearing be held to

try to determine why this HMO no longer exists, where the problems were, who is really at fault, and, just as important, where do we go from here to make sure it never happens again.

Mr. Chairman and members of the Committees, I called for this hearing back in October. I know there have been a lot of pressing needs in the State of New Jersey, and that the nation is facing a major crisis as we are all engaged in what is happening in the Gulf. But I do appreciate the Assemblywoman and the Assemblymen coming here and giving this their attention today, because I think this has been a major problem in our district, and also a major problem to be addressed in the State to make sure it does not occur again.

I would like to let you know that I have literally hundreds of letters on file in my district office with reference to Omnicare; questions being raised that you will hear today. I think our hearts go out to those 18,000 subscribers, and also to the employees who were very dedicated in giving health care services through Omnicare HMO. I have a short statement to make, but before I do that I would like to again thank you for coming to the district and for holding this hearing and giving people the opportunity to have input in the process. Hopefully, legislation will result.

The issue before these Committees today is not one of why health maintenance organizations go into bankruptcy, but more, whose responsibility is it to oversee the financial health of Omnicare and other such HMOs?

It is important that we, as State legislators, understand why some 18,000 people from the South Jersey area had their continuity of care interrupted. It is important to understand why New Jersey's regulatory system -- with all of its failsafes -- was unable to foresee the problems before they occurred.

We need to know if Omnicare was mismanaged and why it was allowed to happen. And we need to know if the intervention

and promised rehabilitation of Omnicare by the Department of Insurance of the State of New Jersey helped the situation, or actually made the situation worse.

More importantly, we owe an explanation not only to the 18,000 subscribers to Omnicare, but also to all the people of New Jersey who put their faith and lives in State-sanctioned HMOs.

The tension and burden have been great on employers, employees, and their families, and especially on senior citizens who depend on HMOs for their health care. Their faith in our regulatory system has been shaken.

Today's hearing provides them with the opportunity to communicate directly with you as you investigate the causes of the Omnicare failure and look for ways to prevent such causes in the future. This is their right, and our obligation as legislators.

I thank you for your time and interest, and certainly would be willing to answer any questions the Committees might have.

ASSEMBLYMAN OTLOWSKI: Assemblyman, before we go any further -- I should have done this at the outset -- may we introduce the people who are sitting here so that everybody will be acquainted with them? May we start over on the extreme left?

MR. MUSICK: Yes. My name is Tom Musick. I am the aide to the Assembly Insurance Committee.

ASSEMBLYMAN SCERNI: Fred Scerni. I am the Assemblyman from the Second District.

ASSEMBLYWOMAN MULLEN: Ann Mullen. I am the Assemblywoman from the Fourth District.

ASSEMBLYMAN OTLOWSKI: George Otlowski, the Nineteenth District.

MR. TAFFET: Gary Taffet, the Democratic staff to the Insurance Committee.

ASSEMBLYMAN CIMINO: Skip Cimino, Assemblyman from the Fourteenth District.

MS. ZITA: Patricia Zita, Assembly aide to the Health and Insurance Committees.

ASSEMBLYMAN OTLOWSKI: Do you want to speak a little louder? I think we ought to know who you are. I don't think they heard you.

MS. ZITA: I'm sorry. My name is Patricia Zita. I am an aide to the Assembly Health and Insurance Committees.

ASSEMBLYMAN OTLOWSKI: Thank you very, very much.

Assemblyman, for the record, the HMO you make reference to is now in bankruptcy and under the umbrella of the Federal Bankruptcy Court. Is that correct?

ASSEMBLYMAN SALMON: My understanding is that it is not only in bankruptcy, but it is no longer in existence.

ASSEMBLYMAN OTLOWSKI: We'll get into that.

ASSEMBLYMAN SALMON: I believe there are some law cases pending which I know the Department of Insurance will be able to go into further, Mr. Chairman, with reference to the final dispensation of the Omnicare HMO.

ASSEMBLYMAN OTLOWSKI: It is my understanding, too, that the Attorney General's Office is conducting its own investigation. Am I correct about that?

ASSEMBLYMAN SALMON: That is correct.

ASSEMBLYMAN OTLOWSKI: Is there any other agency conducting an investigation, other than the Attorney General's Office?

ASSEMBLYMAN SALMON: I do not know of any.

ASSEMBLYMAN OTLOWSKI: This HMO was organized when?

ASSEMBLYMAN SALMON: I do not know the exact date, Mr. Chairman, but I know there are people here who were right from the beginning of the Omnicare, and they would have that information. I know they are going to present that in their testimony.

ASSEMBLYMAN OTLOWSKI: When did they go out of business, when they were no longer meeting their obligations?

ASSEMBLYMAN SALMON: It happened just this past year -- 1990.

ASSEMBLYMAN OTLOWSKI: It is my understanding -- and we will probably get into this in greater depth with Assemblyman Cimino-- Let me ask you this: Do you have any recommendations that you want to make at this point on what you think should be done to better monitor these organizations?

ASSEMBLYMAN SALMON: I am anxious to hear the testimony in today's joint public hearing. I am going to stay for the entire thing for that reason. I think the testimony will give us some insight. At least that is what I am hopeful of. I feel strongly that there are major questions to be asked on exactly the handling of the State's end of it from the Department of Insurance. I'm glad we have people here representing the Department of Insurance today to look at that angle.

I must have had numerous requests, and telephone conversations with people involved, who felt that at one time or another the agency could have been sold privately, and could still be operating today. I think that is a real question to be asked: Did the State handle its obligations correctly, or could this have been sold privately to another organization and still be functioning today? Not only the original management of the HMO has to be looked at, but also I think you have to raise some questions about exactly what the State did. We would think, with what is in place now, that regulations would be there to make sure that something like this did not occur. I had people say to me that it wouldn't occur, but the actuality is, it did.

So that says something needs to be put into legislation. That would be what I would hope would be the final outcome of today's hearing.

ASSEMBLYMAN OTLOWSKI: How many people have been affected by this particular incident?

ASSEMBLYMAN SALMON: Eighteen thousand subscribers. Mr. Chairman, those subscribers live in South Jersey.

ASSEMBLYMAN OTLOWSKI: And, how many of those would be in your district, roughly?

ASSEMBLYMAN SALMON: I think the majority would be in Cumberland County and in Cape May County. There are quite a number in Atlantic County, also, and I think there are some in Salem.

ASSEMBLYMAN OTLOWSKI: About four counties have been affected, roughly?

ASSEMBLYMAN SALMON: Yes.

ASSEMBLYMAN OTLOWSKI: Let me ask you this-- We are going to get into this in more detail with the Department of Insurance later on. I'm sure Assemblyman Cimino, who is proposing legislation, is going to talk about some of the measures that he has in mind to, you know, help prevent anything like this from happening again. But, let me ask you this: Do you have anything you want to suggest particularly to the Insurance Commissioner's Office, or would you rather hold back on that?

ASSEMBLYMAN SALMON: I think I am going to reserve that, Mr. Chairman, until the end of the hearing today. There may be some real particular questions that we may want to offer at that time. I think we also have to understand that there were-- Most of what occurred during Omnicare's demise happened in the previous administration. Many of those who were brought on near the end with the new administration did not really have sufficient time to get up to speed in order to be able to make decisions. Some of those decisions may have been already too late to save Omnicare.

ASSEMBLYMAN OTLOWSKI: We're talking about a big number -- 18,000.

ASSEMBLYMAN SALMON: Yes, we are.

ASSEMBLYMAN OTLOWSKI: I am going to ask Assemblywoman Mullen if she has any questions she would like to ask.

ASSEMBLYWOMAN MULLEN: No. I am interested, as is the Assemblyman. What I would like to suggest, Mr. Chairman, is, it might be better for him, in order to hear better and get the most information, to come up and join us at the Committee table. I would certainly be glad to move over to help to make space for him.

ASSEMBLYMAN OTLOWSKI: Well, that goes without saying.

ASSEMBLYMAN SALMON: I think it's true. You just wanted to get closer to the Chairman, right? (laughter)

ASSEMBLYMAN OTLOWSKI: Supposing we hold back, as far as you are concerned, so you can hear some of the testimony. Then we will get into it later. In the meantime, I think it is important for us -- Fred, unless you want to ask a question at this point, or do you want to--

ASSEMBLYMAN SCERNI: Just by way of background, Ed, where are these 18,000 people now, with regard to the status of their insurance? Do you have any feel for that?

ASSEMBLYMAN SALMON: Yes. Most of those people went into other health care organizations. It became a competitive market to try to go after the 18,000 subscribers. My understanding -- and I could be wrong in this -- is that most of those were taken care of, of course at a much higher cost.

ASSEMBLYMAN SCERNI: I think there is a collateral problem that goes along with this. Assuming they have been picked up by other insurers, that's good. But we all know that we are dealing with this Uncompensated Care Trust Fund problem right now. One of my concerns would be that these folks have not found themselves in that position, both for their own personal benefit and for the overall operation of the system. If this puts a greater strain on the Trust Fund, that is a dual concern we have to address and be aware of.

ASSEMBLYMAN SALMON: I don't have the exact numbers. I think the Department of Insurance has them. I think that would be a good question to ask the Assistant Commissioner: Exactly how many of the 18,000 have been placed, and approximately where are they? I think they have been part of the overseeing process in that regard.

ASSEMBLYMAN OTLOWSKI: Ed, do you want to come up and join us now, please? All right? Do you mind bringing up a chair?

ASSEMBLYWOMAN MULLEN: I think there is an extra chair here.

ASSEMBLYMAN OTLOWSKI: May we hear from Assemblyman Cimino now, please? (brief consultation with other members of Committee) It has been suggested that rather than hearing from the Assemblyman, we hear from the Deputy Commissioner of Insurance, Jasper Jackson. Mr. Jackson, please? Does he have written testimony? The copy we have here-- Is this the testimony from the Insurance Department?

MR. MUSICK: I'm sorry, Mr. Chairman. I apologize. Someone who just came in, someone who didn't get in here early enough to give them to us, just dropped these off -- Dale Florio, from the HMO Association.

ASSEMBLYMAN OTLOWSKI: How about the Insurance Department? Do they have any written testimony?

MR. MUSICK: You didn't have any written testimony, did you, Mr. Jackson?

D E P U T Y C O M M. J A S P E R J. J A C K S O N: No, we do not have any written testimony.

ASSEMBLYMAN OTLOWSKI: Mr. Jackson, without further ado, will you introduce the big crew you have with you, please, for the record?

DEPUTY COMMISSIONER JACKSON: Yes, I will. I have, to my far right, Mr. Leon Moscowitz, who is a Special Deputy Commissioner within the Department of Insurance. He has--

ASSEMBLYMAN OTLOWSKI: Excuse me. We are going to have a problem here being heard. Would you please speak up louder?

DEPUTY COMMISSIONER JACKSON: Okay. To my far right, I have with me Leon Moscowitz, who is a Special Deputy Commissioner within the Department of Insurance. One of his responsibilities at this time would include the Omnicare liquidation process. Adjacent to me is Denise Linton, who is an Administrator within the HMO Unit within the Department of Insurance. She is directly involved with the Omnicare liquidation also.

ASSEMBLYMAN OTLOWSKI: Thank you very much. Before we do any kind of a questioning gig here, one of the things I would hope you would do, is to outline what you see -- what you have seen here and what you know about this, to make it easier for us. That way, when we get into the questioning program we will have some sense of direction.

Now, here is a company that had 18,000 members. Suddenly they found themselves without coverage, and suddenly, from what Assemblyman Salmon said, this company evidently went bankrupt. Are they, in fact, bankrupt?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: They are bankrupt?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: Do you want to pick it up from there and just develop your statement from that point of view, and from your Department's point of view?

DEPUTY COMMISSIONER JACKSON: Well, I think it would be difficult for me to pick it up from the point that Omnicare is bankrupt. In light of some of the statements that Assemblyman Salmon made earlier, and also in order to really understand the problems with Omnicare, it may-- I think it is necessary to give some of the background regarding HMO regulations within the State.

I am currently a Deputy Commissioner within the Department of Insurance for the Florio administration, but I was also a Deputy Commissioner for the Department of Insurance during the Kean administration. About three to four years prior to the demise of the Kean administration, the Department began to focus on the solvency of all types of insurers or health care systems that it had the responsibility for regulating. When I first became the Deputy Commissioner for Insurance, the entire State was in a crisis; in fact, the entire country was in a crisis with respect to the property casualty insurers. Those are the insurers who write automobile insurance, homeowners' insurance, and who also cover different professionals with their liability coverage, such as doctors and lawyers. They provide general liability to businessmen in the operations of their businesses.

As we went through that crisis, we discovered that the greatest reason that system was in trouble had to do with the financial weakness of a lot of the insurers involved. What had happened was, when the country went through the last economic crisis and interest rates began to spiral, a lot of insurers, in their haste to make more money on their investments, began to reduce their premiums to a level where the premiums were not sufficient to cover the actual risk they were taking on. But, by reducing the premiums, it increased the cash flow in terms of money they could hold for investment. Most of them believed that they would make so much money off the increased investments that it would more than offset the reduced premiums they were writing the coverage at, which was not sufficient to cover the actual losses.

As we became aware of that problem, we became concerned about to what extent those practices went beyond the property/casualty industry; whether those practices were also taking place within the life industry or the health industry. As we moved from the property/casualty area and began to focus

on other areas, we began to also look at the HMO system. From the very beginning there, we discovered that we had a very big problem, because although we had something to do with the HMOs, we were not the primary regulators of the HMOs. The Department of Health had the primary responsibility for regulating HMOs.

Well, the Department of Health, as it turned out, had the primary responsibility. We began to talk with the Department of Health to see what information we could glean, or learn, to see what type of shape the HMO system within the State was in, and what their understanding was with respect to it.

To make a long story short, we were not very successful in getting that much information out of the Department of Health with respect to the financial status of the HMO system. So, as a result of that, we conducted our own survey of the HMO system. We discovered at that time that out of 21 systems doing business in this State, 19 of them were financially impaired or, in fact, insolvent; that only two of those systems were healthy systems.

As we tried to come to grips with the reason for the HMO industry being in that type of shape within the State, the conclusion we came to was that although the Department of Health had the primary responsibility for regulating the HMOs, they did not have the expertise nor the experience required to regulate the HMOs; that all they could really do was evaluate an HMO system with respect to the quality of care that would be offered the subscribers or members of the HMO. But they did not have the capability of reviewing and evaluating the contract forms between the HMO and its providers, the physicians and/or hospitals. They did not have the capability of evaluating whether or not the fees or the premiums that would be charged to members or subscribers would be sufficient to, in fact, cover the costs; nor did they have the ability to

monitor the financial safety and soundness of any HMO system as it went about doing its business.

What we did at that point was-- We entered into a set of discussions with the Health Commissioner, who was at the time a lady by the name of Molly Coye. We entered into an agreement whereby the Department of Insurance undertook the de facto regulation of HMOs away from the Department of Health. The Department of Health would still be responsible for reviewing the system with respect to quality of care, but the--

ASSEMBLYMAN OTLOWSKI: Excuse me. You took it away without legislation, but by way of regulation, or by way of what you thought was absolutely necessary at that point?

DEPUTY COMMISSIONER JACKSON: Yes, by--

ASSEMBLYMAN OTLOWSKI: What you thought was necessary?

DEPUTY COMMISSIONER JACKSON: Yes, by agreement between the two Departments. See, I think if you look at the current HMO legislation, or the current statutes that control the regulation of HMOs, it is the Department of Health that has the primary responsibility, in that they evaluate the plans and they issue the certificates of authority.

ASSEMBLYMAN OTLOWSKI: Excuse me. You, as the Department of Insurance, had no idea of the approaching disaster of this particular HMO, did you?

DEPUTY COMMISSIONER JACKSON: Well, we did after we undertook the survey; when we looked at the 21 systems and we found 19 of the systems financially impaired, which included Omnicare.

ASSEMBLYMAN OTLOWSKI: When you looked at the 21 systems, how far down the road of the disaster was this particular one -- the Omnicare? Was it already taking place at that point, when you got into it?

DEPUTY COMMISSIONER JACKSON: Yes. I don't know--

ASSEMBLYMAN OTLOWSKI: It was already on the skids?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: So, at that point, there wasn't a thing you could do, with the exception, of course, of being a pallbearer at the funeral?

DEPUTY COMMISSIONER JACKSON: Well, we attempted to be more than a pallbearer at the funeral. At the time we looked at it, it was insolvent, but we believed that there was a chance that perhaps we could rehabilitate it. What we thought of by way of rehabilitation was not being able to repair its ills and troubles and return it to the same management it had. We thought that perhaps we would be able to attract a buyer, some other entity that already had an existing HMO network, or health care delivery system, that wanted -- that saw some benefit and opportunity for it by acquiring the Omnicare system with all of its problems.

ASSEMBLYMAN OTLOWSKI: When the Department of Insurance made this survey of the 21, this particular one was on the brink of disaster? Am I correct about that? I just want to get this into--

DEPUTY COMMISSIONER JACKSON: It wasn't on the brink of disaster. The disaster had occurred, but no one knew it.

ASSEMBLYMAN OTLOWSKI: It had occurred. That's when you got into it?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: That's when you got into surveying the 21 other--

DEPUTY COMMISSIONER JACKSON: No, we did not focus on Omnicare. The idea was to focus on -- was to try to discover to what extent the HMO system within the State was financially healthy, or not. In order to accomplish that, we had to evaluate every HMO system -- the financial soundness of every HMO system doing business in this State. There were 21 of them.

ASSEMBLYMAN OTLOWSKI: So you were looking at the others?

DEPUTY COMMISSIONER JACKSON: We were looking at them all.

ASSEMBLYMAN OTLOWSKI: The remaining survivors, or those that were operating?

DEPUTY COMMISSIONER JACKSON: No, we were looking at all of them. When we commenced--

ASSEMBLYMAN OTLOWSKI: You had a total of 21, right?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: There were 20 left, right?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: Those were the ones you were looking at -- the 20 remaining?

DEPUTY COMMISSIONER JACKSON: No, we were looking at all of them.

ASSEMBLYMAN OTLOWSKI: Including Omnicare?

DEPUTY COMMISSIONER JACKSON: Including Omnicare.

ASSEMBLYMAN OTLOWSKI: Let me ask you this, at this point: In looking at Omnicare, did you see any signs of mismanagement?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: You did. That mismanagement, if you had tighter controls under the Insurance Department-- Could that have been corrected by regulation, or would it have taken legislation?

DEPUTY COMMISSIONER JACKSON: We believe it could have been corrected by regulation.

ASSEMBLYMAN OTLOWSKI: It could have been corrected by regulation. From where you sit now, and from what you have seen, do you think that legislation is necessary to put this into the Department of Insurance, and giving the Department of Insurance the necessary sinews and muscles to deal with this?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: In your looking at Omnicare, did you see anything you think would be helpful to this

Committee and to the people who are working and proposing legislation? When you talk of mismanagement, was there mismanagement that included giveaways on the top between management, loose standards for paying salaries, loose standards in meeting obligations such as contracts, and whatnot? Is that what you saw?

Forgive me for asking that leading question. I want you to put it in your own words. What did you see when you looked at it?

DEPUTY COMMISSIONER JACKSON: I am going to let Ms. Linton answer that question. I think she is the one most competent to answer that among us.

ASSEMBLYMAN OTLOWSKI: Would you just hold it for one minute? (pause here to set up P.A. equipment) I think this will be better for the people who are testifying. I don't think these people want to hide from us. Probably the HMOs would want to hide from us, wouldn't they? (no response)

D E N I S E L I N T O N: Omnicare went into rehabilitation in April -- April 22, 1988. I got involved with Omnicare in June--

DEPUTY COMMISSIONER JACKSON: Distinguish between rehabilitation and liquidation.

MS. LINTON: Rehabilitation was our effort to bring the entity back into financial health. We were not, at that point, attempting to liquidate it or terminate the operations of the organization. Again, it went into rehab in 1988. What we attempted to do was restore its financial health and hopefully find a buyer for it.

But what we found, when we looked into the management of the organization, was that it had only three specialties in-house. It had: family practitioners, pediatrics, and internal medicine. Omnicare was a staff model HMO, which meant that it should have most of its care delivered within the context of the system. We found that people were going outside

the system in very large proportions, to the tune of $13 million. This was at the point of rehab.

The other problem with Omnicare was that its rates were not structured properly. In order to attract membership, Omnicare lowered its rates, seemingly, and attracted the membership they wanted to bring in the numbers. In terms of the Medicare situation, they had a risk contract, as opposed to a cost contract, which meant that they were taking a risk on the people they insured in the Medicare category. So those particular things contributed to its ultimate demise.

DEPUTY COMMISSIONER JACKSON: Talk about their relationship to CompAAS, how it was actually managed, how they set that up.

MS. LINTON: Also, we had a problem with the way CompAAS, which was the parent company, organized Omnicare. They organized Omnicare to the extent where Omnicare was responsible for its purchase and also responsible for paying CompAAS a management fee on them. We found that CompAAS' Board did not have the expertise to run a managed care system, as well.

ASSEMBLYMAN OTLOWSKI: They did not have the expertise--

MS. LINTON: To run an HMO--

ASSEMBLYMAN OTLOWSKI: --to run the management system, in your opinion?

MS. LINTON: In our opinion, yes.

ASSEMBLYMAN OTLOWSKI: Let me ask you this: In looking at it, what percentage of the moneys that were handled by them went for administration and went for management? Would you know that off the top of your head?

MS. LINTON: No, I wouldn't.

ASSEMBLYMAN OTLOWSKI: You wouldn't know that?

MS. LINTON: No. We have the numbers back at the Department, but I don't have that particular number.

ASSEMBLYMAN OTLOWSKI: Assemblyman Cimino?

ASSEMBLYMAN CIMINO: Ms. Linton, excuse me. You have defined several of the deficiencies that, in fact, you found when the Department investigated Omnicare. What mechanism was in place to have provided the Certificate of Authority for Omnicare to have operated in the first place?

MS. LINTON: That would have come from the Department of Health.

ASSEMBLYMAN CIMINO: To what extent, in your examination as a Department, had there been a failure to live within that mechanism where Omnicare was concerned, as well as the other HMOs?

MS. LINTON: I'm not quite sure I understand the question.

ASSEMBLYMAN CIMINO: Well, obviously, I mean, if we are talking about a regulatory scheme, there was a regulatory scheme, or a mechanism which should have been followed. Is that a fair-- That is a fair assumption, I would take it.

MS. LINTON: Right.

ASSEMBLYMAN CIMINO: All right. To what extent did you find in your investigation with regard to Omnicare-- In other words, I guess what I am trying to ask you is, who dropped the ball here? If there was a mechanism in place, why is it that we failed to see those deficiencies prior to the Department becoming involved?

DEPUTY COMMISSIONER JACKSON: Let me answer that. I would say that the State dropped the ball with respect to the regulatory system. The statute that provides for the regulation of HMOs straddles the responsibility for them between two Departments. If you review the legislation, I think it is clear that the Department of Health, or the Health Commissioner, is the primary mover with respect to what is right and what is wrong with respect to regulating HMOs. It provides some responsibility for the Department of Insurance in

consulting with the Department of Health, or the Health Commissioner, with respect to forms, rates, everything that has nothing to do with the quality of care.

But the problem is, when you review the statute, it is not clear just what the Department of Insurance is supposed to do and when the Department is supposed to do it, if the Department of Health does not request the Department of Insurance's aid. The reality is, once the statute was enacted, various entities made application to the Department of Health for Certificates of Authority to operate as HMOs, and those certificates were granted, primarily with the Department of Health undertaking a review with respect to the quality of care aspect.

In other words, the Department of Health is expert at evaluating whether or not the medical care that is proposed to be provided is adequate or not and up to standards, but it is not qualified to do hardly anything else. The system was set up in a way in which the Department of Insurance was never tied in. Therefore, I cannot speak to what it was the Department of Health reviewed when they issued Certificates of Authority. They don't have life or health actuaries at the Department of Health. They do not have financial examiners; they do not have financial analysts; they do not have people who are familiar with the business operations of an HMO.

So, I would say that the regulatory system, as it existed then, and as it exists by statute now, is defective and ill-designed. That was the primary problem.

ASSEMBLYMAN CIMINO: Okay. Then effectively, in the past, HMOs have neither been fish nor fowl in the regulatory scheme?

DEPUTY COMMISSIONER JACKSON: Exactly.

ASSEMBLYMAN CIMINO: And effectively then, what we really have is a failure of the regulatory scheme, because the articulation of who should effectively be in charge, really is what has failed here?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN CIMINO: Thank you, Mr. Chairman.

ASSEMBLYMAN OTLOWSKI: Assemblywoman Mullen?

ASSEMBLYWOMAN MULLEN: Thank you, Mr. Chairman.

S P E C I A L D E P. C O M M. L E O N M O S C O W I T Z: I think one other point should be made. I think the standards as to what constitutes solvency and stability in terms of being able to deliver on your promise are not well defined in the law as it stands today. One of the things we feel is quite pressing and should be addressed is, what standards should be exercised by the regulatory authority to make sure that the deliverer of the service will, in fact, be there to deliver it when the claim -- or when the service must, in fact, be delivered?

ASSEMBLYMAN CIMINO: Mr. Moscowitz, let me ask you a question: How is it that the Department, absent-- I mean, there has been a clear declaration by my good friend Mr. Jackson -- and we have shared other opportunities with auto insurance, and what have you-- How is it that the Department, de facto, without a legislative scheme in place, took control?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: Jasper, do you want to talk to that issue?

DEPUTY COMMISSIONER JACKSON: We did it de facto because after conducting the survey and discovering that out of 21 HMO systems 19 of them were-- Or, for all intents and purposes the way we looked at it, the industry was financially impaired, and recognizing that although the statute was unclear as to what the Department of Insurance's role was and how it should be played out, in the discussions we had with the Department of Health about the condition of the HMO industry, it became clear to the then Commissioner of Health that the ability to regulate that industry resided within the Department of Insurance, and not within the Department of Health.

So, since we did have some responsibility by statute, both Commissioners -- the Commissioner of Health, who was then Molly Coye, and the Commissioner of Insurance, Kenneth Merin -- agreed that the Department would take over the primary responsibility for regulating the HMOs, and then would seek a piece of legislation to endorse that particular scenario.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: And at the same time set standards that would be meaningful in terms of determining the solvency of units or organizations that came into the State to do the business of running an HMO. That is critical. There is also the critical issue of, even if you set solvency standards that are pertinent, what happens if one of them does go into a bad financial situation and comes belly-up? What are you going to do about protecting the insureds in that kind of a situation? The whole issue of a guarantee fund gets to be quite pertinent here. No matter how good your solvency standards may be, one of them, sooner or later, is going to run into trouble, and you are going to have to establish a means of protecting the insureds against the financial disaster that might befall any HMO.

ASSEMBLYMAN CIMINO: When you say that the Departments of Insurance and Health came together-- I think Ms. Linton said-- Ms. Linton, when was it that you came into play here with Omnicare, once again?

MS. LINTON: It went into rehab in '88.

ASSEMBLYMAN CIMINO: In '88?

MS. LINTON: Yes.

ASSEMBLYMAN CIMINO: You say you moved forward and realized that effectively what both Departments were doing, was walking down the middle of the street getting hit by the truck on both sides. Was this brought to the attention of the Governor of the State of New Jersey?

DEPUTY COMMISSIONER JACKSON: Yes, it was.

ASSEMBLYMAN CIMINO: Did that become, at that point -- knowing the insolvency that, in effect, was being created-- Did that become a priority of the administration, to get this issue resolved?

DEPUTY COMMISSIONER JACKSON: I don't know. I have no knowledge of that. I don't know what priority it was given within the administration at that time.

ASSEMBLYMAN CIMINO: Let me go back and ask: As members of the Department of Insurance, knowing that the regulatory scheme had failed -- as we have already indicated -- was there any direction back down through the chain to those in the Department who were most knowledgeable about this issue to prioritize this issue back up to the Legislature?

DEPUTY COMMISSIONER JACKSON: Yes, I would say there was. In fact, I believe a bill was drafted. I do not recall who participated in the drafting of it. Commissioner Merin found a sponsor and the bill was, in fact, introduced, but nothing happened to it.

ASSEMBLYMAN CIMINO: Okay. Thank you very much, Mr. Chairman.

ASSEMBLYMAN OTLOWSKI: Who introduced the bill, if there was a bill at that time? We're talking what, '88?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: No, it was later than that.

MS. LINTON: The bill was--

ASSEMBLYMAN OTLOWSKI: Do we know who introduced the bill at that point?

DEPUTY COMMISSIONER JACKSON: I don't know.

UNIDENTIFIED MEMBER OF COMMITTEE: It was Van Wagner, in the Senate.

ASSEMBLYMAN OTLOWSKI: Oh, it was in the Senate. The bill was introduced in the Senate by Senator Van Wagner. That bill never saw the light of day, evidently. Is that correct?

DEPUTY COMMISSIONER JACKSON: That's correct.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: It has not been enacted.

DEPUTY COMMISSIONER JACKSON: So it didn't see the light of day.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: That's right.

ASSEMBLYMAN OTLOWSKI: I'm sorry, Assemblywoman Mullen.

ASSEMBLYWOMAN MULLEN: Folks, I'm coming to a conclusion and, please, after I state what I am thinking, would you tell me whether I am on the right track or the wrong track?

Over the years, in dealing with the State as a local Mayor, I have found that so many functions of the State government are duplicated in various departments. I'll give you an example: I understand Treasury reviews development plans. The Department of Education reviews development plans, and the Department of Community Affairs has an entire section where they review development plans. Okay?

I guess what I am hearing here is, we have two Departments reviewing insurance regulation plans. I cannot, for the life of me, fathom why the Department of Health would be even vaguely responsible for regulating insurance matters. Do you feel that if this was made clear, that should never have been in the Department of Health in the first place? (no response)

Now, I can understand their need to review whether the care that is going to be given by this plan is proper care, but I have no idea what they would be doing regulating the cost or the premiums, or whatever. Am I on the right track here?

DEPUTY COMMISSIONER JACKSON: Yes, I believe so. I believe -- as you have stated -- that oftentimes you will find that there are different agencies or boards or subdivisions of the State that have responsibility for the same thing, or something that is close to the same thing.

I believe part of the problem here is that the HMO systems-- There are some people who argue that HMO systems

are, in fact, not insurance systems; that they are health care delivery systems. Therefore, the jurisdiction for them should not be within the Department of Insurance--

ASSEMBLYWOMAN MULLEN: It makes no sense. People are paying premiums.

DEPUTY COMMISSIONER JACKSON: --but within the department of the State that would regulate health care delivery systems, which would be the Department of Health.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: You've got to consider the historical development of this phenomenon, this HMO pattern. It is a post World War II development. It does not have as traditional a background as health insurance, as evidenced by either the Blue Cross/Blue Shield mechanism or the commercial insurance companies. There were some, I think, decisions to be made early on which might have made sense at that point in time, but as the mechanism developed and as it grew, insuring as it does, or covering as it does a million people in the State of New Jersey, it became apparent that the regulatory system as initially visualized and enacted just wasn't responsive to the needs.

I think we may have come to that realization in the State of New Jersey late, or too late. There were clearly any number of plans which got in trouble, and are still in trouble, and something has to be done to react, or respond to that situation. I think the time for new legislation clearly is here, recognizing the essence of a solvency issue, a financial stability problem. What do you do when an HMO gets in trouble? Those are critical issues which were not at the top of everybody's mind when HMOs first started developing in the State of New Jersey some 25 or 30 years ago.

ASSEMBLYMAN OTLOWSKI: Actually, you got into this in 1988?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: Into this particular HMO.

ASSEMBLYMAN OTLOWSKI: Into this particular HMO. But at that point, you took a look at the total picture, at the 21 HMOs and, as a matter of fact, you immediately -- from your testimony -- saw that there was trouble ahead. When you saw that, from 1988 until Omnicare went down the tube, there wasn't any positive or immediate action that was taken to try to stem that?

DEPUTY COMMISSIONER JACKSON: Oh, yes, there was.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: Oh, yes.

ASSEMBLYMAN OTLOWSKI: Yes?

DEPUTY COMMISSIONER JACKSON: Yes, there was. Aside from the legislation that Senator Van Wagner introduced, once the Department of Insurance took de facto responsibility for the HMO system, and at that time having--

ASSEMBLYMAN OTLOWSKI: Excuse me. Again what Assemblyman Cimino said: You took over the regulation by de facto means and, as a matter of fact, I suppose, too, by the fact that there was some implied-- Aside from some of the positive powers that the Department of Insurance had, there were some implied powers you had, and on the basis of that you got into it.

DEPUTY COMMISSIONER JACKSON: Yes. We built a unit-- We commenced building and establishing a unit within the Department that could effectively oversee HMOs with respect to every aspect of their operation. But, most importantly, in recognizing that 19 out of the 21 systems were in trouble, we began to-- We opened discussions. Most of the systems had parents that were-- For instance, the Aetna Life and Casualty Insurance system owns an HMO system within the State of New Jersey. Prudential Life Insurance Company owns an HMO network within the State of New Jersey. Most of the systems -- and Mr. Moscowitz can correct me if I am wrong, because I am apt to be; it is within their arena, not mine--

We commenced discussions with all of the entities that were responsible for the HMO networks operating within the State. We demanded that they make significant capital infusions into the systems, and we put a lot of other regulatory demands upon them. As a result, we have been successful in bringing most of the systems to a state of financial solvency.

ASSEMBLYMAN OTLOWSKI: On all 21 of them at that time, with the exception, of course-- It was already too late to deal with Omnicare. Was it already too late to save them?

DEPUTY COMMISSIONER JACKSON: Well, it was too late to deal with Omnicare in that fashion. First of all, Omnicare had a parent, but it did not have a parent with the type of financial resources that a Prudential Life Insurance Company would have, or Aetna Casualty would have, or another major national HMO network would have.

ASSEMBLYMAN OTLOWSKI: But there was nothing at that point, from your point of view, now, you know, that you got into it, that you could have done to save Omnicare? There wasn't a thing that you could do?

DEPUTY COMMISSIONER JACKSON: Well, the thing that we could do, we were trying to do. That was, we moved Omnicare into rehabilitation. We did that so that we could take management control--

ASSEMBLYMAN OTLOWSKI: But you moved them into rehabilitation -- just so that we get this--

DEPUTY COMMISSIONER JACKSON: May I finish my answer?

ASSEMBLYMAN OTLOWSKI: Yes, all right.

DEPUTY COMMISSIONER JACKSON: We moved them into rehabilitation so that we could effectively take control of the management. The question you asked earlier was whether or not it was mismanaged, and we believe it was.

ASSEMBLYMAN OTLOWSKI: So you stepped in? You stepped in totally?

DEPUTY COMMISSIONER JACKSON: Yes, we stepped in totally.

ASSEMBLYMAN OTLOWSKI: Let me ask you this: In the time frame when you stepped in, where was the Federal Court and where were the bankruptcy proceedings at that point?

DEPUTY COMMISSIONER JACKSON: I'm not sure.

ASSEMBLYMAN OTLOWSKI: This company had gone bankrupt, as I understand it.

MS. LINTON: Yes. We had not applied for bankruptcy at that point. We were trying to reestablish them in terms of getting them financially sound again. At that point, we had not petitioned the Court to put them into liquidation.

ASSEMBLYMAN OTLOWSKI: Who petitioned for bankruptcy?

DEPUTY COMMISSIONER JACKSON: Well, I believe the management of Omnicare petitioned for bankruptcy.

ASSEMBLYMAN OTLOWSKI: Oh, they petitioned for bankruptcy.

DEPUTY COMMISSIONER JACKSON: The Commissioner would never have petitioned for bankruptcy. If the Commissioner believes that an entity is not operating correctly and is insolvent, then the Commissioner will either take it over and place it in rehabilitation -- if he believes there is a chance of saving it -- or he will ask the Court to give him the power to liquidate it.

ASSEMBLYMAN OTLOWSKI: Yes. Let me ask you this--

DEPUTY COMMISSIONER JACKSON: The management placed it into bankruptcy in an attempt to have the bankruptcy court stop the Commissioner of Insurance from putting it into rehabilitation.

ASSEMBLYMAN OTLOWSKI: Oh, I see. Let me ask you this: In the bankruptcy proceedings, were you subpoenaed as a party in interest?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: And, as a matter of fact, the bankruptcy record will show that you testified in the bankruptcy proceedings?

DEPUTY COMMISSIONER JACKSON: Well, I think what the record will show is that we intervened in the bankruptcy proceedings to--

ASSEMBLYMAN OTLOWSKI: That what?

DEPUTY COMMISSIONER JACKSON: I think the record will show that we intervened in the bankruptcy proceedings, requesting that the Federal judge not take any action that would be adverse to the Commissioner's interest and powers and authorities over placing it in rehabilitation.

ASSEMBLYMAN OTLOWSKI: Did the bankruptcy court agree with that position?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: They agreed?

DEPUTY COMMISSIONER JACKSON: Yes.

ASSEMBLYMAN OTLOWSKI: Assemblyman Cimino, did you have a question?

ASSEMBLYMAN CIMINO: Yes. Ms. Linton, when you went into Omnicare, was there any interruption of a continuum of coverage for the individuals who were in that HMO?

MS. LINTON: At the time of rehabilitation?

ASSEMBLYMAN CIMINO: Yes.

MS. LINTON: No.

ASSEMBLYMAN CIMINO: There was not?

MS. LINTON: There was not.

ASSEMBLYMAN CIMINO: Was there, at any given point in time thereafter, an interruption of continuum of coverage?

MS. LINTON: No.

ASSEMBLYMAN CIMINO: How did the people maintain coverage with an insolvent HMO? How did they continue to get their coverage?

MS. LINTON: If you are talking about the time of liquidation, we made arrangements for--

DEPUTY COMMISSIONER JACKSON: No, no, he is talking about the whole process; what we did once we placed it in rehabilitation, and how we insured that the coverage be made available after we moved it into liquidation.

MS. LINTON: Okay. Well, at the point of being put into rehabilitation, it was just business as usual, as far as the subscriber population was concerned. There was never an interruption of coverage; there was never any gap in coverage. They went on continuously as though nothing had taken place.

ASSEMBLYMAN CIMINO: Did you, as the Department, in the regulatory scheme, then mandate that other HMOs pick them up?

MS. LINTON: In the time of rehabilitation, that wasn't an issue, no.

ASSEMBLYMAN CIMINO: I'm sorry, maybe I am confusing you. Once we had gotten past the point of rehabilitation, and rehabilitation did not succeed, at that point, did the Department then mandate that other HMOs in the surrounding service delivery area pick them up?

MS. LINTON: Well, we didn't mandate it; we negotiated with the other HMOs to come in and pick up that subscriber base. We were successful in our negotiations with them.

ASSEMBLYMAN CIMINO: Thank you.

ASSEMBLYMAN OTLOWSKI: Excuse me. If you had the power at that time, if there were legislation, you could have mandated it?

MS. LINTON: That's right.

DEPUTY COMMISSIONER JACKSON: Yes, but we did not have clear--

ASSEMBLYMAN OTLOWSKI: Excuse me. Are you considering this?

ASSEMBLYMAN CIMINO: Yes. We have legislation that is companion to Senator Van Wagner's legislation that, in fact, deals with net worth implications, minimum deposit requirements, a guarantee fund, and placing this legislatively by statute, housing -- Assemblyman Scerni and I have that legislation; we are both prime sponsors of that -- the regulatory scheme Certificate of Authority clearly within the province of the Department of Insurance. That is the first priority, and then establishing minimum net worths, as well as minimum deposit requirements, prior to the issuance of the Certificates of Authority.

ASSEMBLYMAN OTLOWSKI: Excuse me. At this point, I just want to deviate for a moment. Assemblyman Salmon, do you want to introduce the class that is here with Dr. Reinard, which is going to solve this whole problem? (laughter) Would you, please?

ASSEMBLYMAN SALMON: The Chairman has asked me to introduce Dr. John Reinard who is here with his class -- his class in government. Dr. Reinard also happens to be the Director of our Board of Freeholders here in Cumberland County. John, do you and your class want to stand up so you can be recognized by the Committee?

D R. J O H N R. R E I N A R D: Thank you, Mr. Assemblyman. I think the class should stand up. I am very proud that they have the interest to come here, and I am very grateful that we have the opportunity here in South Jersey to come to this type of a hearing. Assemblyman Salmon, over the past few years, has provided this sort of thing for us, and I think it is a great experience. And, Mr. Chairman, we thank you for recognizing us.

ASSEMBLYMAN OTLOWSKI: Would you mind if we applauded your class?

DR. REINARD: Not at all. I'll do that, too. (applause)

ASSEMBLYMAN SALMON: May I ask a question, Mr. Chairman?

ASSEMBLYMAN OTLOWSKI: Yes.

ASSEMBLYMAN SALMON: First of all, John, I will provide you with the test questions to be asked of your class, as they take notes here. (laughter)

Here is the number one question I get: First of all, what was the month, Leon, that you took over in 1988? Do you know the month?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: Yes. We took over on April 22, 1988.

ASSEMBLYMAN SALMON: Okay. And the objective--

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: That's in rehabilitation.

ASSEMBLYMAN SALMON: Right. The objective of the Insurance Department was to rehabilitate and sell Omnicare. Am I correct in making that statement?

MS. LINTON: Yes.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: Rehabilitate, which means getting it to be a going concern in some form or fashion. Selling is an obvious, possible solution.

ASSEMBLYMAN SALMON: Why were you not able to sell it? The number one question I get is-- Many people felt that you had a bona fide buyer in Graduate Hospital, and that there was a bona fide offer, but there was not the cooperation of the State to finalize the sale of Omnicare at that time. I think the question that many people in my district want to know is, what happened in that sale to Graduate Hospital?

MS. LINTON: We negotiated with the Graduate a number of times and we came to the understanding that there was going to be a stock purchase of Omnicare. That means all assets and all liabilities. The Graduate sent us through a number of communications attesting to that fact.

Later on, back in December, I would say, of 1989 -- going into January of 1990 -- the Graduate came back and decided that they were going to do an "asset only" sale. When we spoke about asset only purchases, we suggested to them that they needed some particular criteria in place which they did not have. At that point, negotiations began to break down. The Graduate did not have a Certificate of Authority to operate within New Jersey. They would have had to apply for one. It would have taken some time. They were interested in continuing with certain operational things that were already in place, and we didn't necessarily agree with those things either. Therefore, the negotiations and the discussions ultimately broke down around August.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: It should be pointed out that in the interim, the situation was that Omnicare itself had deteriorated significantly, and continued to deteriorate. When liquidation-- Well, let me put it this way: When it went into rehab, Omnicare had a net worth -- a negative net worth -- of slightly in excess of $2 million. That had gotten to the point where it was between $5 million and $6 million, and I think Graduate kind of lost their anxiety and desire to pick up an operation which I think they recognized as being in difficulty and with real troubles.

DEPUTY COMMISSIONER JACKSON: I think, so that you can better understand--

ASSEMBLYMAN OTLOWSKI: Excuse me. If you don't mind, the Assemblyman here has a follow-up question. I will come back to you, Ed.

ASSEMBLYMAN SALMON: I may have a follow-up on his follow-up.

ASSEMBLYMAN CIMINO: I think it dovetails with what Assemblyman Salmon has suggested. There has been a good deal of discussion about rehabilitation, and thereafter insolvency. At what point does the Department determine that-- Where do

you cross the line between rehab and insolvency in the asset to liability ratio here?

You talked about a negative net worth as you moved in. At what point do you then determine-- You said, "Well, we went into rehabilitation." You went through the process of rehabilitation, and that went on for a period of time. At what point did you reach-- What is your criteria to determine that rehab is no longer an issue and you must now move-- You know, what number in negative net worth, or in negative asset to liability ratio says -- where the Department says, "Fold the cards. It is done"?

DEPUTY COMMISSIONER JACKSON: There is no such number. When you are dealing with these types of entities and these types of issues, the solution in each case is particular to the circumstances of each case. A decision to take an entity out of rehabilitation and either return it to the marketplace or to, in fact, liquidate it, would depend upon the circumstances and evaluation that is undertaken at particular points in time. For instance, Mr. Moscowitz said that at the time we placed Omnicare into rehabilitation, they had a negative net worth of $2 million. Its management alleged that the negative net worth was only $500,000, but we found it to be, in fact, in excess of $2 million.

It is possible to remove an entity from rehabilitation and return it back to the marketplace while it still has a negative net worth. But the decisions that would lead to that type-- The circumstances that would lead to that type of a decision would involve one of whatever the problems were when we took it over. If we saw that the problems had been substantially cured or were about to be cured, although there was still a negative net worth, we would be able to predict, in some zone of reasonableness, that the entity would be able to operate as it was intended to do, providing the services that it was intended to provide, while at the same time moving

itself out of a negative cash position, or liability position, into a positive one.

But, under the circumstances attendant to the Omnicare situation, there was no opportunity to work out such a plan. As we indicated, the management and the parent of Omnicare were resourced for itself, both in terms of their financial capability, as well as their experience and expertise capabilities. So the only way that we saw of affecting a rehabilitation with respect to Omnicare, would be if some "white knight" company came along; some other entity that had the financial resources and the experience and expertise in operating an HMO, and for some reason saw Omnicare as an opportunity and would be willing, able, and capable of taking it over.

The type of problems that Omnicare had-- Ms. Linton explained what they were, but she didn't really go into that much detail. For instance, when you looked at Omnicare as an operating entity-- Usually when you look at an HMO, the idea behind an HMO is that-- The reason you do it, as opposed to going to what you would call a "traditional health care insurer," is that for the premium you pay to the HMO you can get all of your medical services taken care of within the system. Usually the price for that if you go to a traditional insurer-- They are only going to pay so much on the dollar for whatever care is provided, and they are not going to cover every type of medical care you may need. Putting an HMO in the marketplace, then when you review them, you have to be -- you should be sure that there is sufficient, what they call "provided participation" by contract to be able to deliver those comprehensive services at the fee that is charged, and still have someone making money doing it.

When you look at Omnicare, of all of the physicians who worked the Omnicare system, only 95 of them had contracts, and 495 of them were what you call-- (witness consults with

his associates sitting with him) Four-hundred and seventy-five of them were what you would call "noncontract providers." What that means is, Omnicare, in delivering its medical services, could only control the costs with respect to about maybe 16% to 20% of the medical care it was providing. It had absolutely no control over the bulk of it. That is one of the reasons the system went under. They had a Medicare contract that provided a few hundred thousand dollars a month in income, but the entity was losing $60,000 per month on the contract. It was losing something like $25 to $30 per subscriber.

When we first commenced discussions with Graduate, Ms. Linton indicated that the deal was supposed to be for what she characterized as a "stock transfer." What that means is, in order for Graduate to take over Omnicare, they would have had to buy the whole of Omnicare, assets and liabilities. After they became aware of the type of problems that Omnicare had, they became disinterested in a stock only transfer and only wanted to purchase the assets. They made proposals to the Department that we sell them all of the assets and make an application to the court to wipe out what began as a $2 million liability, but had grown to a $5.5 million liability. We simply said to them: "If you can provide a rationale that will have a court accept such a deal, give it to us and we will be only too happy to do that." But, of course, they couldn't do that.

Aside from that, other problems began to emerge with respect to Graduate as a potential buyer of Omnicare also. We did a financial evaluation and analysis of Graduate's system, and it appeared that Graduate itself was financially weak. So another problem we would have had was, if we had sold Omnicare to Graduate, it would have only been about a year or two before we would have to move in and take the Graduate system over. That was another reason for us not to go with that deal.

Then another problem emerged that if we had sold the system to Graduate, Graduate would not have had a sufficient network for servicing the client base that Omnicare had, and would not have had the experience, nor the expertise to get a Certificate of Authority at that time.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: Then, when you take a look at the bottom line of this, with no real option in terms of selling, no real option of continuing Omnicare on a profitable basis, and the ability to place the 18,000 subscribers with viable, ongoing, successful HMOs, it became apparent ultimately that a liquidation was the appropriate step to take. We negotiated with the three acquiring HMOs so that they would have continuity of coverage, and all of the insureds were able to replace their Omnicare coverage, in fact, with HMO coverage with three other reputable companies.

ASSEMBLYMAN OTLOWSKI: Excuse me. I want to return to Assemblyman Salmon.

ASSEMBLYMAN SALMON: I would like to follow-up with just a couple of quick questions to put this Graduate question to an issue on the record. When was the first Graduate offer?

MS. LINTON: I believe it came sometime early '88.

ASSEMBLYMAN SALMON: Early '88. You took over on April 22, 1988.

MS. LINTON: That's true. Maybe it was late '87; either late '87 or early '88.

ASSEMBLYMAN SALMON: It was before you took over?

MS. LINTON: There was some--

ASSEMBLYMAN SALMON: There was an interest by Graduate Hospital before you took over?

MS. LINTON: I believe it was early '88.

ASSEMBLYMAN SALMON: Okay. I am not so sure that we have the exact date on that, but-- Here is what -- and I want to say this for the record -- people felt. I think you should know as far as the Department of Insurance is concerned what

subscribers and employees and people who were dealing with the system felt.

I will have to be honest with you, Commissioner Jackson. This is the first time I heard Graduate being described as weak. I have not heard that from anybody before. No one mentioned that to me. No one said that they weren't-- All I heard was that they were a very good HMO and delivered excellent service.

DEPUTY COMMISSIONER JACKSON: You didn't hear that from the Department of Insurance.

ASSEMBLYMAN SALMON: Okay. Well, I did not hear that they were weak. This is the first I have heard that on testimony. I am not here to argue that with you, because I am sure you can provide this Committee with substantiation of that statement. And I would like to have that substantiation of that statement.

The feeling of individuals is that when the State originally took over Omnicare here in this district and was trying to rehabilitate it, you had a very substantial group that wanted to take over, it being Graduate Hospital -- the Graduate Program -- and that Graduate was making a good offer. But there was a lot of time that lapsed, and a lot of frustration dealing with the bureaucracy, and as time went on then, a situation occurred-- The situation went from as you described it, $2 million, to $5.5 million. It makes sense why no one would want to take it over when it got to be $5.5 million.

The frustration of a lot of people who have talked to me on the street and in my office, is the fact that they feel the State did not move efficiently and effectively to consummate a sale of Omnicare so it could be alive today. That is the feeling. Whether that is correct or not, that is the feeling of the people within this district.

DEPUTY COMMISSIONER JACKSON: Well, let me correct the record with respect to one item, so we don't misunderstand each other.

Graduate did not withdraw its offer. We refused to sell Omnicare to Graduate--

ASSEMBLYMAN SALMON: Right.

DEPUTY COMMISSIONER JACKSON: --because Graduate did not have the financial capability of operating an HMO, nor did it have a sufficient network within the State. Also, the reason the deal, or the negotiations dragged, or lagged, however one wants to characterize it, is because Omnicare -- because Graduate changed in midstream the nature of its offer. When we placed Omnicare in rehabilitation and sought prospective buyers for Omnicare, we did it through a competitive bidding process. That bidding process was for the sale of the whole of Omnicare; everything that Omnicare entailed, its assets, its liabilities, and whatever else it may have had.

Graduate submitted a proposal along those lines. Other entities submitted proposals for asset only purchases, but because of the nature of the bid we rejected those offers. Omnicare (sic), after we got down the road in negotiations, began to, while still characterizing its offer as a stock purchase-- Really, it had effectively changed it to an asset only purchase. At the time, we were between administrations. I had become the Acting Commissioner, and in my mind that sort of an offer smacked of a liquidation. In light of the circumstances and the facts as I knew them, I thought that it would be unfair at that point to continue negotiations with Graduate, which had significantly altered its proposal to something else, and that we had an obligation and a duty to give others which may have been interested in the assets an opportunity also.

But, the biggest problem was, the Department had discovered that Graduate, itself, was financially weak, and

there was no way -- or at least there was a significant question, in the opinion of the staff that had evaluated Graduate, and the consulting firm that we had gotten to undertake the evaluation of Graduate, that without a substantial capital infusion from its parent, there was no way that Graduate could safely carry out the acquisition and ultimately nonhazardous operation of Omnicare. Aside from that, Graduate had no Certificate of Authority to operate within the State. It had proposed, in fact, that the Omnicare Certificate of Authority be sold to them as an asset. We would never do that. The statute sets forth how one gets a Certificate of Authority to operate within this State. They are not assets to be transferred or to be bought and sold as one would buy a car. There are all sorts of things that you have to look into before you issue a Certificate of Authority.

Then the other problem was, Graduate, itself, did not have a sufficient network for servicing the Omnicare subscribers, if it had gotten control of the system.

ASSEMBLYMAN SALMON: One of the reasons I am really appreciative of having a hearing on this whole issue is, I would like to have for the Committee some validation as far as the ability of Graduate Hospital is concerned -- for the Committee to review. That puts it on record. It is information that I have never heard, which I am glad to hear if it is true, but I would like to have some substantiation of it.

MS. LINTON: If I may just add something-- It wasn't just the Department of Insurance that evaluated Graduate's position. We sent it out to Tillinghouse, which is a very qualified consulting actuarial firm.

ASSEMBLYMAN SALMON: Okay.

MS. LINTON: They primarily set the tone of the direction for us to take with respect to the Graduate's Health System's financial solvency.

DEPUTY COMMISSIONER JACKSON: In any event, we will make the reports available.

ASSEMBLYMAN SALMON: We can have a copy of that report?

DEPUTY COMMISSIONER JACKSON: We will make that available to you.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: The facts are, they did not deliver on their initial promise to buy. Their promise to buy was to buy the company in toto and they changed that into an asset purchase arrangement, which would have been unfair to everyone; which would only have delayed the day of reckoning, and would have probably created an even bigger crisis.

ASSEMBLYMAN OTLOWSKI: Excuse me, at this point. Assemblyman Scerni had some questions, and I delayed getting him into this. Assemblyman, do you want to question the witnesses now?

ASSEMBLYMAN SCERNI: Thank you, Mr. Chairman. Let me pose a couple of questions from the subscribers' point of view: You began rehabilitation with Omnicare in April of '88, and sometime after that they went into bankruptcy. Is that correct?

DEPUTY COMMISSIONER JACKSON: They applied to the court for bankruptcy protection before we placed them into rehabilitation. Their attempt at seeking bankruptcy was to try to cut off the Commissioner's power to take them over.

ASSEMBLYMAN SCERNI: During that period of time, how were the subscribers served, by Omnicare or by the other agencies?

DEPUTY COMMISSIONER JACKSON: They were served through Omnicare.

ASSEMBLYMAN SCERNI: And that continued up until the time that these subscribers were transferred into other programs?

DEPUTY COMMISSIONER JACKSON: Yes. That continued up until the time we decided to place them into liquidation.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: That date was October 1, 1990, roughly.

ASSEMBLYMAN SCERNI: Okay. We have been provided by staff with four different areas where transfers occurred, and that information is correct. Are you familiar with what I am talking about? (no response) We have 2200 members going into Medicare; 7400 members into the State Health Benefits Program; 7700 members going into traditional Blue Cross/Blue Shield or other HMOs; and just over 1200 members going into the Federal program. I believe that was supplied by you guys. Is that correct?

MS. LINTON: We put that information together, but I don't believe you are understanding it properly. The 7400 people in the State Health Benefits Program were receiving their benefits through Omnicare. However, at the time we decided it would be liquidated, we talked to the three HMOs who gave us assistance, and we placed those people within those other programs, such as U.S. Health Care. Healthways, and PruCare, yes.

ASSEMBLYMAN SCERNI: Was there ever, at any time, a window of time where these subscribers were not served either by Omnicare or by the new carriers?

MS. LINTON: Not that we are aware of, no.

ASSEMBLYMAN SCERNI: Okay. So, the subscribers did not actually suffer any loss through this?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: That was one of our principal conditions in negotiating with the other acquiring HMOs; that there be continuity of coverage.

ASSEMBLYMAN SCERNI: And that was accomplished, so there was no window?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: To the best of our knowledge.

DEPUTY COMMISSIONER JACKSON: We haven't said it, but there is another thing here that needs to be said: One of the reasons no one was interested in acquiring this entity was that not only was it running amuck in terms of having 600-and-some physicians, with only 95 having contracts with the system where you could control the prices, but the other reality is, every subscriber within the Omnicare system got the best buy in town. Those rates that the Omnicare management had been charging for the services delivered by Omnicare were grossly inadequate. One of the reasons no other entity was interested in assuming that entity was because they were not willing to take the bath that they would have to take at the rates that Omnicare had approved.

ASSEMBLYMAN SCERNI: Let me leave Omnicare for a minute. We said there were 21 HMOs that you reviewed at one time. Are the other 20 still functioning in the State now?

MS. LINTON: No. One is the Foundation Health Plan, which was placed in liquidation also.

ASSEMBLYMAN SCERNI: Okay. So we have 19 functioning now?

MS. LINTON: I would say there are 19, yes.

ASSEMBLYMAN SCERNI: And, are they financially solvent at this point in time? I mean, are we going to see a rerun of Omnicare? From where you are sitting, are we going to see a rerun of Omnicare someplace else in the not-too-distant future?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: Obviously, our hope is that that not be the case. But if you are asking me, "Is everybody in a financially sound position at this point in time?" I would have to be honest and say I do not believe they are all operating with the kind of stability -- financial stability -- and solvency that we would like to see.

One of the points of the proposed legislation is to establish criteria and standards that will allow us to get all of the HMOs up to that level. I fear for some of them, to be perfectly honest.

ASSEMBLYMAN SCERNI: When we are talking about HMOs, from some of the information, again, that we have been provided by staff, I am concerned that we may be dealing with a definitional problem, because we are talking also about preferred provider organizations and exclusive provider organizations. Are they dealt with in the same fashion as HMOs, or do we, in fact, have a subtle problem here that we haven't raised yet in terms of calling different providers by different names and holding them to different standards?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: It's not so subtle; it's quite real. There are multiple organizations that we have to be concerned about in terms of solvency. There are specialist operations, dental operations, and other types of specialized providers. There is the overall problem of all health care providers in the State of New Jersey. We operate in the State of New Jersey without a guarantee fund, either as it relates to HMOs or any of the other types of organizations. The Department has expressed serious concern on this issue. It was a matter of concern that found itself in the Governor's Health Care Commission, which had its report completed several months ago, as I assume you are aware.

One of the issues is the matter of solvency and guarantee funds as they relate to any and all health care providers in the State. This has to be faced up to. It presumably is being faced up to, and we would expect to see legislation at some point in time to respond to the need. This is not unique to HMOs.

DEPUTY COMMISSIONER JACKSON: The other problem is -- and I think you are on the verge of it -- we need legislation that enables us to regulate health care entities but not by their alphabet acronyms only. There is an existing alphabet soup, and that alphabet soup is going to grow. We need a piece of legislation -- an omnibus type of legislation -- that would enable us to regulate managed health care units, or managed

health care entities, whether they call themselves HMOs, PPOs, or ABCs.

ASSEMBLYMAN SCERNI: That, Commissioner, is precisely the point I am getting at, because if we pursue legislation that establishes standards for HMOs, and the day after that someone comes along and creates an EPO, that permits that new organizer to avoid the standards we have just imposed on HMOs, and we have missed the point.

DEPUTY COMMISSIONER JACKSON: Exactly.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: Absolutely. We are in total agreement with you.

ASSEMBLYMAN SCERNI: If we had in place the kinds of requirements that are currently proposed in A-4333 -- which is the companion to Senator Van Wagner's bill-- Do you believe that what is contained in that bill, in that proposal, would have solved, or greatly reduced the situation we had in the current case?

DEPUTY COMMISSIONER JACKSON: I am going to let Mr. Moscowitz address that.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: We think it contains a structure within which appropriate regulation is possible. To be perfectly blunt about it, that legislation was drafted by people in the Department before I arrived, and before the present Commissioner was appointed. We are reviewing the legislation in terms of its standards concerning financial stability and solvency. We may have some suggestions to make concerning its actual wording. We should have our own thinking completed within the very near future, and we would expect to try to respond to that question a little bit more positively, or even have some suggestions as to further amendments.

DEPUTY COMMISSIONER JACKSON: The answer is, "Yes," but we believe that that bill can be improved.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: With certain modification, it would do the job.

ASSEMBLYMAN SCERNI: Let me just share my perspective on that: If we are going to do this, I think we would like to do it right. The legislation sponsored by Assemblyman Cimino and myself-- If you have substantive changes -- and admittedly this Committee is not hearing that bill today; it will hear that bill at some point in the future -- I know I would like to be aware of them. I don't want to see the bill go through, and then a year or 18 months from now find ourselves in a situation where we have another problem because that bill did not do something that it should have done. You are in the position of regulating. So if you anticipate a problem, please let us know about it so we can begin to address it now, as we move forward to begin solving this problem.

DEPUTY COMMISSIONER JACKSON: We will do that.

ASSEMBLYMAN SCERNI: Thank you. Mr. Chairman, thank you, too.

ASSEMBLYMAN OTLOWSKI: Thank you. Before we do anything else, I just want to point out that I understand there are people here from the Health Department. Am I correct?

J O H N J. K I R C H N E R: (speaking from audience) John Kirchner, Department of Health. I am not in a position to testify today. It was our impression that from the solvency standpoint, the Department of Insurance would be the more appropriate Department to deal with that issue.

I will get you any information the Committee finds necessary.

ASSEMBLYMAN OTLOWSKI: No, I just wanted to know if you were here. We'll get back to you, all right?

MR. KIRCHNER: Okay.

ASSEMBLYMAN OTLOWSKI: I just wanted to know if you were here.

I would like to ask Assemblyman Cimino, who is one of the sponsors of a pretty comprehensive bill now, if there is any more help they need from the Department of Insurance at this moment?

ASSEMBLYMAN CIMINO: One other thing, if I may, Mr. Chairman, and I thank you for indulging me. Under the HMO scheme, you expressed that there were "X" number of people who were contracted for service. There were "X" number of people -- 400-and-some -- who were effectively noncontract providers.

MS. LINTON: Right.

ASSEMBLYMAN CIMINO: In the HMO scheme, if you are contracted to provide service, the individual -- the enrollee receives that service for a set fee. Is that accurate?

MS. LINTON: Yes.

ASSEMBLYMAN CIMINO: Okay. What happens to the enrollee who has received service from a noncontract provider? Are they as protected under the umbrella of the HMO as the individuals who receive the service from a contracted provider?

MS. LINTON: No. They will probably be responsible for copayments, because what the HMO will do, is pay up to the amount they would have paid their contracted provider.

ASSEMBLYMAN CIMINO: Was there any, in your looking at rates and in looking at fees-- I would assume you look at fees for noncontract providers as well. Was there any examination of that?

MS. LINTON: I would not have done that, but the management of Omnicare would have done it. When we sent our deputy rehabilitators in, that is one area they looked at. They attempted to go out and contract with more providers within the community. But the providers did not want a contract with Omnicare.

ASSEMBLYMAN CIMINO: Who would have determined if those fees to an enrollee-- Who would have determined if, in fact, the enrollee was told about the fee, and who would determine if the fee had been excessive?

S I D B R O D Y: The enrollee wouldn't even know it. I'm sitting here and listening to all this--

ASSEMBLYMAN OTLOWSKI: Excuse me. We are going to take this-- We will get to you. Assemblyman Cimino, do you want to continue?

ASSEMBLYMAN CIMINO: Yes. Could you--

MS. LINTON: Normally there is supposed to be an educational process between the enrollee and the enrollee's employer, meaning that the employer group will try to relate to the enrollee what kind of obligations they are responsible for, what kind of responsibilities the HMO is responsible for, and why they should use a primary physician -- a contracting physician, and so forth. Most of these people are working and they have HMO assistance through their employer.

However, when that communication level breaks down, the enrollee is not really aware of what kinds of financial ramifications come from going outside the system.

ASSEMBLYMAN OTLOWSKI: In that connection, in the bankruptcy proceedings, have they been concluded? The bankruptcy proceedings -- have they been concluded?

DEPUTY COMMISSIONER JACKSON: Not to our knowledge.

ASSEMBLYMAN OTLOWSKI: Then I suppose you won't know the answer to the question I am going to ask you now: To your knowledge, has the bankruptcy court made any effort to return any moneys to the enrollees, at this point?

DEPUTY COMMISSIONER JACKSON: No.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: I don't think that is in the woods, so to speak. Do you mean, return to the enrollees, in the form of subscription premiums?

ASSEMBLYMAN OTLOWSKI: Right.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: No, I doubt if that will ever come to pass.

MR. BRODY: Mr. Chairman, I've got to interject myself just for a moment.

ASSEMBLYMAN OTLOWSKI: If there are no more questions, gentlemen, would you do me the kindness to stay in the room? We do not have any more questions here at this point, but would you just do me the kindness, because there is a Ms. Marilyn Henry-- Is Ms. Henry still in the room? (affirmative response from audience) It is my understanding that you have asked the Chair to deviate from our set schedule so you can be heard, because you have to leave and you will not be able to return.

M A R I L Y N H E N R Y: (speaking from audience) No, I will not. I know that Mr. Brody wants to speak about something. I would be willing to--

ASSEMBLYMAN OTLOWSKI: Is it important for you to go on now? That is the question.

MS. HENRY: No, I just have to get going.

ASSEMBLYMAN OTLOWSKI: Can you wait?

MR. BRODY: I'll let her go.

MS. HENRY: I cannot wait.

ASSEMBLYMAN OTLOWSKI: Do you want to stand by, and let me hear Ms. Henry?

MR. BRODY: No problem.

MS. HENRY: I think I am the only subscriber here.

ASSEMBLYMAN OTLOWSKI: Do you want to sit down, please?

MS. HENRY: I think I am the only former subscriber in this room.

ASSEMBLYMAN OTLOWSKI: Excuse me. Let me run the hearing, and then you just testify. All right?

MS. HENRY: Okay, go ahead. I'm sorry.

ASSEMBLYMAN OTLOWSKI: First of all, will you please give us your name and your address and your connection with this whole business?

MS. HENRY: My name is Marilyn Henry. I live in the City of Vineland.

ASSEMBLYMAN OTLOWSKI: You live where?

MS. HENRY: I live in the City of Vineland.

ASSEMBLYMAN OTLOWSKI: Will you please give us your address for the record?

MS. HENRY: It's 582 Sarah Place, Vineland.

ASSEMBLYMAN OTLOWSKI: And you are a subscriber to--

MS. HENRY: I am a former subscriber. That is correct.

ASSEMBLYMAN OTLOWSKI: You have a formal statement you want to make?

MS. HENRY: I did want to say something. I mean, I realize this is the first time I have ever done this, so if I break a procedural rule you will please forgive me. Okay?

ASSEMBLYMAN OTLOWSKI: Let me just say this: We are as informal as we possibly can be and yet be orderly, because we are making a record here. The purpose of this hearing is to be helpful to the two Assemblymen who are preparing legislation.

MS. HENRY: Okay. I think the things I have to say are going to be very helpful. I recognize some former employees in the room, but I, personally, do not recognize any other subscriber in the room. I am being told now that I am incorrect.

I really believe that both the State of New Jersey and Omnicare, as it existed during the 1980s, are clearly at fault for what happened. My situation clearly shows that process. I was an Omnicare subscriber since I began my employment with the State of New Jersey in 1981. I was promoted within the same department of the State of New Jersey, but promoted from one division to another in 1987. Okay? Last August of 1990, I received a written notification from Omnicare that I was "terminated." Excuse me! I'm terminated? What exactly does terminated mean? I mean, in my line of work that means something totally different than what--

ASSEMBLYMAN OTLOWSKI: Let's not talk about that.

MS. HENRY: I was terminated. Omnicare had not received payment from the State of New Jersey for any health care that they had provided for me since August 1987 through August of 1990. They were--

ASSEMBLYMAN OTLOWSKI: From when?

MS. HENRY: From August of 1987, when I was promoted, through August of 1990. That is why they took the drastic step of "terminating" me. They -- Omnicare -- had not been--

ASSEMBLYMAN OTLOWSKI: Omnicare terminated you?

MS. HENRY: Right, because they had not been paid by my employer, who happens to be the State of New Jersey.

ASSEMBLYMAN OTLOWSKI: With whom you are still employed?

MS. HENRY: Yes. Please, let's-- I love my job, thank you very much. (laughter) Very, very much, I love my job. Okay?

ASSEMBLYMAN OTLOWSKI: All right. That's on the record now. Do you want to continue?

MS. HENRY: Yes. From 1987, when I was promoted, through August of 1990, Omnicare, the HMO in the City of Vineland, did not receive one single, solitary penny for any of the health care that they had provided me. In two years time--

ASSEMBLYMAN OTLOWSKI: When were you told that?

MS. HENRY: I was told that when I was terminated, because, of course, I went in for my weekly allergy shot-- I went in and they said, "I'm sorry. Unless you give us 40 bucks, we are not giving you the shot." And I went, "Excuse me, but I have never paid you a cent for these shots in 11 years. What do you mean?" They said, "You have been terminated." I said--

ASSEMBLYMAN OTLOWSKI: Did you find out why they weren't being paid?

MS. HENRY: Yes, I did. In all of that time, it was a very simple and easy-to-correct, on the State of New Jersey's part, computer error. And the State, from what I was able to learn had--

ASSEMBLYMAN OTLOWSKI: Was that just in your case, or was it generally prevalent?

MS. HENRY: I understand there were 15 other individuals terminated at the same time because of nonpayment from the State. They didn't pay them. They didn't pay them for my C-section; they didn't pay them for me having my gall bladder out. I walked into that place every Monday for the last 11 years to get an allergy shot. They did not pay them.

Now, my point is, both sides are at fault. Why did Omnicare continue to provide me services for two years when they never got paid, and why didn't the State respond to "requests for payment" from Omnicare? Omnicare took the position with me that they terminated me because they knew it would force me to go into my office and scream all the way up the chain of command, until finally someone realized that the individual who completed the paperwork on my promotion, instead of punching in "transfer," punched in "terminate." All right?

Now, it was a very simple-to-correct problem, but my point--

ASSEMBLYMAN OTLOWSKI: The computer showed that you were terminated, and they cut out the payments?

MS. HENRY: Right. I had--

ASSEMBLYMAN OTLOWSKI: And the truth of the matter is, you weren't terminated. You were transferred.

MS. HENRY: I was transferred. Omnicare continued to provide the services--

ASSEMBLYMAN OTLOWSKI: Was that peculiar only in your case?

MS. HENRY: I don't know. I am just one individual. My point is, why did the people at Omnicare continue to provide me services when they weren't being paid? They knew they weren't being paid. They had told me that they had requested-- You know, they kept sending up these little form letters. They said, "Oh, Marilyn, there is a form letter. We sent it up and we asked and we asked and we asked, and 'they'" -- the State of New Jersey -- "never responded." And why didn't the State of New Jersey ever respond?

Can you imagine the hundreds and hundreds and thousands of dollars over two-and-a-half years? I had a baby. I had nine months' prenatal care. I had a very difficult C-section and the baby involved, who was immediately covered, was in the neonatal intensive care unit for a week. Then, four months after that, I had to have emergency surgery to save my life, not to mention over all that period of time the colds, the bruises, the eye doctor, you know, all the other-- Can you imagine how much money that was? If I am one person-- I know that in August of 1990 they terminated at least 15 other people.

ASSEMBLYMAN OTLOWSKI: Excuse me. When this was happening, did you notify your department head that you weren't covered?

MS. HENRY: Oh, yeah, yeah. I screamed--

ASSEMBLYMAN OTLOWSKI: And nothing happened?

MS. HENRY: Yeah, within 48 hours of my screaming at the assistant director of my department--

ASSEMBLYMAN OTLOWSKI: When did you start screaming?

MS. HENRY: Within 48 hours of getting that letter. I wasn't even notified for two years. As soon as they told me I was terminated-- As soon as Omnicare terminated me-- They said, "Listen, you're terminated. You go talk to your boss." As soon as they contacted me, the subscriber--

ASSEMBLYMAN OTLOWSKI: It took them two years to correct the record?

MS. HENRY: It took both sides -- what happened on both sides-- Omnicare: Why did they continue to provide to me? If they realized they weren't getting paid, why did it take them two years to do something? And why did the State of New Jersey, after receiving two years of requests for payment notices for myself and other people-- Why didn't they do it?

ASSEMBLYMAN OTLOWSKI: Wait a minute. Excuse me. I think you heard the testimony here by the Insurance Department.

MS. HENRY: Oh, yeah. I think nobody was right.

ASSEMBLYMAN OTLOWSKI: I think they made it very clear that at least the record is going to show that there was mismanagement there. You are a single case of that mismanagement.

MS. HENRY: I also want to know, because I have been sitting here listening and paying very close attention the entire time-- I would not be wrong in my guessing, in my estimate that a full 80% of the subscribers, of the people who joined Omnicare HMO, were State, county, and city employees. Does that factor into the equation at all, the fact that most of us worked for the local school district, worked at the local developmental centers, worked at the local DYFS offices, and most of our husbands and most of our friends worked at the Department of Corrections?

ASSEMBLYMAN OTLOWSKI: Excuse me. Ms. Henry, I think you have made it very clear, but the testimony already shows -- the record already shows -- that this particular HMO was mismanaged. Now, you come in and you say they had a partner. The State was also involved in that mismanagement. That is all you've shown. As a matter of fact, that is very, very important, and collaborates what has already been said.

MS. HENRY: That is all I wanted to do.

ASSEMBLYMAN OTLOWSKI: So, now you can go on your way, so we don't detain you any longer.

MS. HENRY: Thank you very much. I have to get back to the office.

ASSEMBLYMAN OTLOWSKI: Thank you very much.

I just want the record to show that-- Who is here from the Health Department? May we just have your name? Let's get this in the record, all right? May we have your name, please?

MR. KIRCHNER: Yes, Mr. Chairman. My name is John Kirchner. I am in the Government Relations area of the Department of Health.

ASSEMBLYMAN OTLOWSKI: You are here representing the Health Department as an auditor?

MR. KIRCHNER: Essentially, yes. Our expertise in the area of solvency, we felt, was probably better left to the Department of Insurance.

ASSEMBLYMAN OTLOWSKI: I have been informed -- this is the information I have -- that the Health Department was notified of this hearing and was asked to appear and was asked to testify. And, as a matter of fact, they asked to be excused from testifying. Is that correct?

MR. KIRCHNER: We received notification last Wednesday that there would be a hearing. Unfortunately, there is one person in the Department who I think could probably have at least spoken for the Department in terms of what we saw. Again, it would not have been particularly the solvency issue. I don't think the Department has the expertise to handle that. Unfortunately, that person was not available. I wanted to be here to provide -- or, to inform you that I can get you answers to any of the questions that may come up.

ASSEMBLYMAN OTLOWSKI: So you are here, but you are not authorized to speak for the Department? You are primarily here as an auditor?

MR. KIRCHNER: Correct; exactly.

ASSEMBLYMAN OTLOWSKI: I just wanted the record to show that.

Skip, do you have any questions at this moment?

ASSEMBLYMAN CIMINO: I don't know that I really have any questions of the Department of Health. Mr. Chairman, let me ask if, in fact, based on the testimony we have just heard, Omnicare was given the opportunity to come forward and testify, as well?

ASSEMBLYMAN OTLOWSKI: I understand they were given the opportunity. As a matter of fact, my memory has just been refreshed. Yes, they were, but they declined. Obviously they

would decline because of the fact that they are involved in litigation. I suppose they would not want to expose themselves to this hearing because of the litigation. But they were invited and, of course, they made the choice of not testifying for this particular record. The truth of the matter is, they could be helpful to you, and to Assemblyman Scerni, with this legislation, but this is a decision they have made and, as far as I am concerned, I am going to respect it.

ASSEMBLYMAN CIMINO: Mr. Chairman, also let me indicate that I've got to get back to my district. I will not be able to stay for the balance of the hearing today, but I do want to thank you.

ASSEMBLYMAN OTLOWSKI: There are so many people who are taking advantage of the generosity of the Chair, supposing we hear from you now.

ASSEMBLYMAN CIMINO: It is not that I want to take advantage of your generosity -- although I appreciate it -- but I do have to get back.

ASSEMBLYMAN OTLOWSKI: No, I knew you wouldn't want to do that.

ASSEMBLYMAN CIMINO: However, I think there is clear evidence from the legislation that Assemblyman Scerni and I have prime sponsored in the Assembly, as well as Senator Van Wagner's legislation, based upon the testimony -- the very articulate testimony, I might add -- of the Department of Insurance, that, in fact, a statutory scheme needs to be established. Let me echo Assemblyman Scerni's comments that we want to work with the Department to ensure that when this legislation goes into place as law that, in fact, we are not going to revisit this problem when we deal with the issue of net worth and deal with the issue of minimum deposits and a guarantee fund, as well as making sure who has the statutory authority to regulate and to implement Certificates of Authority.

Thank you very much, Mr. Chairman.

ASSEMBLYMAN OTLOWSKI: Do you have anything else you want to add?

ASSEMBLYMAN CIMINO: No, that's all.

ASSEMBLYMAN OTLOWSKI: And you're leaving now?

ASSEMBLYMAN CIMINO: Yes. Thank you.

ASSEMBLYMAN OTLOWSKI: Thank you very, very much. Will I get back home?

ASSEMBLYMAN CIMINO: You'll get back home. We wouldn't leave you in these southern climes, Mr. Chairman.

ASSEMBLYMAN OTLOWSKI: May we hear from Dale Florio? Is he here?

UNIDENTIFIED SPEAKER AT COMMITTEE TABLE: He stepped out, but he will be back.

ASSEMBLYMAN OTLOWSKI: The gentleman there who was asking to be heard-- Do you want to take a seat up here, please? May we have your name and your address, and if you are representing anyone in particular?

MR. BRODY: Actually, I am representing myself, Mr. Chairman. I am Mr. Sid Brody. I am the former Executive Vice President of Omnicare, which was known as the Cumberland Health Systems at the time.

I would like to just make a few corrections of things that have happened. Number one, there were approximately 22,000 subscribers, not 18,000. Omnicare, as we know it today by that name-- Its concept was total HMO, nonprofit. You are looking for input into legislation. One of the things that I looked at for the failure of Omnicare today, was that it was permitted by the State to be converted from a nonprofit organization to a profit organization with the same set of directors.

ASSEMBLYMAN OTLOWSKI: Did they convert?

MR. BRODY: They did convert. As of today, Omnicare is not in bankruptcy. CompAAS is, which is the alleged parent of Omnicare. There is a big difference. Omnicare is in liquidation as a result--

ASSEMBLYMAN OTLOWSKI: Omnicare is not in bankruptcy?

MR. BRODY: No, CompAAS is.

ASSEMBLYMAN OTLOWSKI: Who is it that is in bankruptcy?

MR. BRODY: CompAAS, the alleged parent of Omnicare. There is a big difference. And I think the Department of Insurance should have that fully outlined and in their minds. Is there any question, Commissioner Jackson, on that?

ASSEMBLYMAN OTLOWSKI: Wait a minute. (as Commissioner Jackson starts to answer from audience) Just a moment, please. Do you want to continue your testimony, please?

MR. BRODY: Yes.

ASSEMBLYMAN OTLOWSKI: Continue your testimony.

MR. BRODY: Oh, okay. I thought you had a question for me.

Also, the disparity of a half-a-million dollars in debt to possibly $2 million in debt-- There is a definite disparity there, because many of the providers-- There were two sets of fees. If a doctor or a provider group was under contract, they billed Omnicare at one fee. If their contract had expired and was not renegotiated, they billed at a higher fee. So there is always a question as to how much was really owed by Omnicare to the providers. I think, and assume, even to this day, that that exists.

In my opinion, the logical buyer of Omnicare, after Graduate, and during the period of Graduate's offer, would have been Newcomb Medical Center. Newcomb Medical Center locally made a valid bid for the organization and, as far as I am concerned, the Department of Insurance, which I interceded with many times, went up there and dragged their feet until finally Omnicare had to be put into liquidation. It could have been salvaged, in my opinion, with a very, very competent staff, and could have been really working today.

Unfortunately, Mr. Chairman, a lot of the testimony I would like to give is limited, because I am also involved in

litigation, which the Attorney General is now-- I am part of the Attorney General's suit, and I cannot testify to some of the things that I would like to testify to. But these are some of the matters that I think your Committee should be well aware of, and the fact that there is a difference between a bottom-line profit organization and a nonprofit organization.

This was patterned after a nonprofit organization. The concept was good. It worked. I was Executive Vice President for eight years, and a nonpaid member of the Board, and one of the founders. We were looking to deliver complete medical services to the public at reduced costs. This is the way to go. As far as the Department of Insurance of the State of New Jersey is concerned, I do feel it is an insurance program. I do feel that the Department of Health of New Jersey must be involved also. It is a dual capacity. One cannot operate without the other. I don't think the Department of Insurance has the expertise to see that medical services are delivered properly, nor do I think the Department of Health has the expertise to see that the insureds' premiums are kept -- that the organization is solvent. So it is a dual capacity, and a very, very fine line to walk.

I would imagine now that all of the HMOs in New Jersey have been converted to profit organizations. The minute you say "profit," you know the premiums are going up, and that is exactly what happened here.

ASSEMBLYMAN OTLOWSKI: Thank you very, very much.

ASSEMBLYWOMAN MULLEN: Mr. Chairman, one question?

ASSEMBLYMAN OTLOWSKI: Assemblywoman Mullen has a question.

ASSEMBLYWOMAN MULLEN: Mr. Brody, the former testifier who had to leave -- Ms. Henry -- said that 80% of the makeup of Omnicare were State employees, or school boards, or whatever.

MR. BRODY: I don't think it was that high. Frankly, she said something that, well, I guess it wouldn't disturb me,

but I think you should be made aware of-- She was on a group plan, so it is very simple. In the bookkeeping, she may have gotten lost in the plan. I think Omnicare was very good to continue her coverage through all of those years.

ASSEMBLYWOMAN MULLEN: Yes, it was very kind of them.

MR. BRODY: Right, very kind of them.

Another thing I feel also, in the liquidation, is that the Department of Insurance contributed to the insolvency because they brought in outside people, which was necessary, but they left them in place too long. They just dragged their feet too long. As they dragged their feet, it deteriorated more because it lost the confidence of the providers. It lost the confidence of subscribers, and many were disenrolled as a result of that.

This is a real tragedy for Cumberland County and for Omnicare.

ASSEMBLYMAN OTLOWSKI: That is why we are here.

ASSEMBLYWOMAN MULLEN: Mr. Brody, for the record, when did you leave the company?

MR. BRODY: Well, I didn't leave the company, I left the Board. It was a nonprofit Board, and it was a completely volunteer Board.

ASSEMBLYWOMAN MULLEN: I understand.

ASSEMBLYMAN OTLOWSKI: What year?

MR. BRODY: I left in 1987 or 1988; 1980, I'm sorry.

ASSEMBLYMAN OTLOWSKI: In 1980?

MR. BRODY: Right.

ASSEMBLYMAN OTLOWSKI: When did they transfer from nonprofit to profit, in your opinion?

MR. BRODY: Sometime, I believe, in 1987.

ASSEMBLYMAN OTLOWSKI: In '87?

MR. BRODY: Right.

ASSEMBLYWOMAN MULLEN: Your testimony has been very helpful to me.

ASSEMBLYMAN OTLOWSKI: Thank you for being so patient, Mr. Brody.

ASSEMBLYWOMAN MULLEN: Thank you, Mr. Brody.

MR. BRODY: Thank you. I am going to stay for a while, and if I see something else in testimony, please, if I get excited and interject myself-- Please bear with me.

ASSEMBLYMAN OTLOWSKI: We'll let you interject yourself, but don't get excited. All right? Thank you very, very much.

Now we want to hear from Dale Florio. Dale, are you here with your partner in crime?

D A L E F L O R I O: No crime, but I am here with my partner.

ASSEMBLYMAN OTLOWSKI: Dale, do you want to identify yourself for the record, please?

MR. FLORIO: Mr. Chairman and members of the Committee: My name is Dale Florio. I am a partner with the Princeton Public Affairs Group. We are a legislative counsel to the New Jersey HMO Association. With me is Glenn Klink, who is Director of Administrative Services--

ASSEMBLYMAN OTLOWSKI: You are representing the Association?

MR. FLORIO: That is correct. With me is Glenn Klink, who is the Director of Administrative Services for Aetna Health Plans of New Jersey, which is a wholly owned subsidiary of Aetna Life and Casualty Company.

We had the opportunity to hear the people who went before us. When you have that opportunity, it is also an opportunity to try to rehabilitate the image of your client. I think that is certainly the case here. While we cannot deny the problems associated with Omnicare -- and I think the Department of Insurance pointed out some management practices that are not standard in the industry -- I think it is fair to say that the HMO industry is very vibrant in this State. It is a necessary component of the health care industry. By and

large, the HMOs in this State are doing very well, both financially and in meeting the needs of the consumers. So I want to put that on the record, and indicate that Omnicare, hopefully, is an anomaly, and will never happen again.

Another point I wanted to make is that the HMO is an industry not unlike any other industry. And, since most of the HMOs are owned now by insurance companies, I think we all understand the problems insurance companies have had in the '80s in terms of their investments. Well so, too, the HMO industry, in the early '80s, was made up of many regional plans, and through the '80s there was fierce competition, because the HMO industry in New Jersey, although it has been here since the '60s, really began to bloom in the '80s. Through the '80s, there was a tremendous amount of shake-out, and I think what you see today is a much stronger industry, both financially and from an efficiency standpoint.

I think the Committee should factor into their considerations that there was a lot of competition within the industry, and premiums maybe should not have been as low as they were. But you also have to keep in mind that one of the bases of an HMO is that it is prepaid. HMOs had to deal in the '80s with rising hospital costs and rising health care costs, and at all times they were charging prepaid fees. In other words, the enrollee had to pay up-front before he or she received services. So, if the HMO did not make an accurate prediction, it was going to have some problems in terms of providing services based on the fees it had collected.

As I said before, all HMOs now in New Jersey are affiliated with major insurance companies, except for two -- two of the largest -- U.S. Health Care and HIP Rutgers Community Health Plan. This fact, combined with rising enrollment, suggests that the industry shake-out has run its course. I don't have the figures that the Insurance Department cited, but as I said, I think today, compared to two years ago, the industry is in a much stronger position financially.

We cannot comment specifically about the Omnicare situation. A lot of the facts that were brought out today, we heard for the first time. In fact, the Association was formulated in June 1987. Omnicare was one of the founding members of the Association, but left several months later when their financial problems became obvious.

Part of today's hearing is to address the financial problems with Omnicare, but obviously the Committee has the much larger purpose of figuring out how to deal with the HMO industry. I would suggest that as the Committee pursues solutions to the Omnicare situation, that you look at HMOs both from a financial perspective and the ability of the HMOs to compete into the 1990s and into the 21st century with traditional indemnity carriers.

If you decide to move in a direction whereby you want to strengthen financial requirements, I think it is a perfect opportunity for the Committee, and the Legislature, to make HMOs an equal partner in providing health care, and I will discuss that a little bit further.

Let's talk first about the financial issue. No regulatory structure should keep a failing business artificially afloat, and we are not suggesting that that be the case today. There certainly should be appropriate parameters for operation and transition if an entity needs to leave the market. That is why the Association does support Assemblyman Cimino's legislation and Senator Van Wagner's legislation in concept. As the Department well knows, we spent over a year-and-a-half working with various members of the Department on developing a bill which is basically what you see today.

The bills that have been introduced contain many of the principles that we discussed and we agreed to. Although there are several first tier issues, like transplants for example, the Department of Health would like the final say on what transplants an HMO should perform -- or pay for. That is

fine, except that traditional indemnity insurers are not subject to the same regulations. So I think on that kind of an issue, it should be something that is across-the-board, not just specific to HMOs, or you are going to have a lot of adverse selection. That is the kind of issue we think is still undeveloped in this legislation.

More importantly to these discussions here today, we do support the net worth and minimum deposit requirements contained in the legislation. These financial requirements will preclude future Omnicare situations. It is worth pointing out that the net worth and minimum deposit requirements in this bill -- in these bills -- are the same levels contained in the model legislation by the National Association of Insurance Commissioners. So this is standard model language that has been adopted nationally by the NAIC.

The Association also supports the provision in these bills that would allow the Commissioner of Insurance to require HMOs and health insurance companies to offer coverage to affected consumers in the event of an HMO insolvency. This provision will provide consumers with continuity in their health care coverage. I think it was mentioned in earlier testimony that HMOs did participate in the transition of affected enrollees, so it has been a policy of the industry to cooperate with the Insurance Department in making sure that there was coverage if somebody chose to remain with an HMO. But this legislation would put it into statute.

As I mentioned earlier, any reform with how the State deals with HMOs should also include authority that will keep HMOs competitive in the marketplace. These bills are a perfect opportunity for this to occur. Without this flexibility, HMOs will not be able to compete with commercial insurers. I think it is important to point out that we are addressing HMOs today, but we are really talking about the entire health care system. And, if you want HMOs to compete, any statutory structure that

is developed, any regulatory structure that is developed, should be looked at in that context: What part can HMOs play in the health care delivery system?

Specifically, the Association supports increasing the flexibility and competitive position of the HMOs by permitting them to offer integrated in- and out-of-network services now being marketed to employers by other health benefits organizations. Similarly, the health care legislation dealing with small group coverage now under consideration by the Assembly Health Committee presents a dilemma for HMOs. Although the Van Wagner and Cimino legislation would issue a stronger -- would ensure a stronger HMO industry, legislation by Assemblyman Deverin and Senator Codey would make it difficult for HMOs to compete in the small group market with commercial health insurers.

ASSEMBLYMAN OTLOWSKI: Do you want to stop there for just a moment? Why would the legislation by Assemblyman Deverin and Senator Codey make it difficult for HMOs to compete?

MR. FLORIO: Primarily, Assemblyman, most of the HMOs in New Jersey are federally qualified, except for two of them: Medigroup, which is a Blue Cross plan and Metropolitan Life. Federally qualified HMOs have to maintain certain benefit levels. In other words, they have to offer certain benefit levels to their enrollees in order to maintain their Federal qualification. The Codey bill would require a substantially lower benefit level. Therefore, an HMO would lose its Federal qualification if it complied with the Codey legislation.

Now, Senator Codey understood that and allowed for an exemption in his bill that said no federally qualified HMO need not -- is exempted basically. The problem with that is that I think the State wants HMOs in the system. They want HMOs dealing with small groups. Therefore, an HMO could compete, but it would have to offer a higher quality benefit package, and it is going to cost more. So the HMO will not be able to

compete cost-effectively with an indemnity insurer which can meet the requirements of the Codey bill. If an HMO does want to compete in the small group market and wants to offer a benefit package that costs more, it cannot offer deductibles. They cannot contain any preexisting exclusions in their contracts. So if someone, for example, needed a heart transplant and was switching jobs and was excluded from an insurance carrier's policy, they would automatically want to switch over to an HMO, because they would know that the HMO does not have any preexisting exclusions and could have the procedure performed. So you run the risk of adverse selection.

I think the State wants HMOs to be part of the small group market. There are just problems in those bills which will make it difficult for HMOs to compete. The Association has a dilemma in discussing that legislation, in that most of the HMOs are owned by insurance companies.

ASSEMBLYMAN OTLOWSKI: I'm sorry to do this to you. In the situation that the State finds itself in now, you know, with uncompensated care and with insurance generally, one million and some people who are not covered-- You're saying that Deverin's legislation and Codey's legislation would further damage this whole situation. Is that what you're saying?

MR. FLORIO: Thank you for bringing me back to the main point of this hearing, and that is to say that when you look at the small group issue, when you look at the rising costs of hospital care and the uncompensated care issue, yes, the HMOs have been subject to the same problems that other health care entities have been. All these things need to be looked at in the broad context, if you are going to come up with a regulatory scheme to deal with HMOs.

ASSEMBLYMAN OTLOWSKI: Let me ask you this question: In that bill we have now -- that the Health Committee has now -- and for the moment we are calling it an omnibus bill, and a

lot of other people are calling it, you know, worse things than that-- But, in any event, is that covered in that bill? Do we do anything in that bill with HMOs?

MR. FLORIO: It is my understanding that the Deverin legislation would leave up--

ASSEMBLYMAN OTLOWSKI: It is in that omnibus thing?

MR. FLORIO: You have included in the Deverin bill some components of the Codey legislation. There is an exclusion for federally qualified HMOs. Again, the problem is that if the State wants HMOs involved in the small group market, which I think they do, the bill makes it difficult for them to compete.

ASSEMBLYMAN OTLOWSKI: Did you make that known when we were holding hearings on the Uncompensated Care? Did you make this known to us?

MR. FLORIO: I was at the hearing and I was reading the bill for the first time, like everybody else was that morning. We were prepared to--

ASSEMBLYMAN OTLOWSKI: I'm sorry about that.

MR. FLORIO: No, I understand. I was in touch with staff so, you know, I knew--

ASSEMBLYMAN OTLOWSKI: And they are familiar with it?

MR. FLORIO: Yes, they are. The problem I have from an Association standpoint--

ASSEMBLYMAN OTLOWSKI: Are you going to be available tomorrow when we are going to be holding a hearing on that?

MR. FLORIO: Yes, sir.

ASSEMBLYMAN OTLOWSKI: We want to make sure that we get to you, because what you are saying here is important.

MR. FLORIO: It is. The problem I have with representing the Association in this matter, is that most of the members of the Association are also part of the larger insurance companies. And, as you know, the health insurance companies like the Deverin legislation. So the Association is

able to take a position per se, but only to point out the diverse problems they face, because the insurance companies like the preexisting exclusions. If your HMO is owned by that insurance company, it is going to be difficult, from a corporate policy standpoint, to develop a position. So the Association has been unable to come up with--

ASSEMBLYMAN OTLOWSKI: You're not saying that the large insurance companies shouldn't have any ownership or influence over the HMOs, are you?

MR. FLORIO: I am not saying that at all. HMOs just find themselves in a difficult position. The HMOs are not subject to Federal qualification, and can work within the Codey and Deverin legislation. So the HMO industry is split as it deals with those two bills.

ASSEMBLYMAN OTLOWSKI: I needed that for my own information. I didn't want to, you know, push you to the wall on that.

MR. FLORIO: Oh, I appreciate your letting me make some comments on those two bills, because I think it addresses the issue we are facing today. There is a concern that HMOs are not properly regulated. The Association recognizes that the Cimino and Van Wagner bills--

ASSEMBLYMAN OTLOWSKI: Excuse me. Getting to this bill -- Skip's and Fred's bill-- Did you look at their bill?

MR. FLORIO: Yes, I did.

ASSEMBLYMAN OTLOWSKI: Have you any suggestions about that bill particularly?

MR. FLORIO: Well, one of the main issues that remains outstanding is how you deal with transplants. As I said, the bill would give the Department of Health broad authority to determine what transplants an HMO would have to pay for. The HMOs are concerned that if that is going to be a new policy, the Department of Health also have the same authority in dealing with traditional health insurance companies, or not at all.

In other words, what I have argued here for, sir, is that there be parity in the industry; that the HMOs be subject to similar standards as the insurance companies, or not at all

ASSEMBLYMAN OTLOWSKI: Is that in their bill? It is in their bill.

MR. FLORIO: Yes, it is.

ASSEMBLYMAN OTLOWSKI: For all of them to be treated equally?

MR. FLORIO: No.

ASSEMBLYMAN OTLOWSKI: It is not?

MR. FLORIO: The Cimino and Van Wagner bills deal specifically with HMOs.

ASSEMBLYMAN OTLOWSKI: All right, I'm sorry.

MR. FLORIO: But, as I have said, we have had over a year-and-a-half of discussions with the Department on this legislation. I have been in touch with Leon Moscowitz about this. I know we are about to sit down and renew those discussions on some of the new issues the Department has on this legislation. So we have been working very closely with them in an effort to prepare the industry to deal with the next decade. As I said, I think there has been a tremendous shake-out of the industry in the 1980s, and I believe the HMOs are--

ASSEMBLYMAN OTLOWSKI: I think what the two Assemblymen are doing with this bill-- This is just the beginning because, as you say, there will be big changes coming along with time here in dealing with this whole health problem.

Fred, do you have a question?

ASSEMBLYMAN SCERNI: One that I raised before. This is on the EPOs and the PPOs and like that. Do you consider that type of an organization an HMO?

MR. FLORIO: I would call them hybrids. I am going to defer to my expert, and he says, "No."

G L E N N K L I N K: I would say, "No." PPOs are not allowed to be sold in the State as they are not regulated at the current time.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: (speaking from audience) There is legislation that has been introduced that would, in fact, permit that kind of an organization to operate-- (remainder of sentence lost to transcriber; speaker not near microphone)

ASSEMBLYMAN OTLOWSKI: Did you get those remarks for the record, that came from the Insurance Department? (negative response from hearing reporter)

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: It is legislation that has not been heard by the Senate committee where it was introduced because of the illness of its sponsor, but at some point in time we believe that will come to a vote.

ASSEMBLYMAN OTLOWSKI: Oh, I have just been told by our staff people here that that bill is in the hopper, introduced by Assemblyman Joe Charles.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: That is the counterpart of the Jackman bill.

MR. FLORIO: And we have commented on that bill, Mr. Chairman. The bill does not now include the opportunity for an HMO to set up a PPO, and really when you are looking at the HMO industry today, since all of the HMOs are owned by insurance companies except for two, you are only talking about two additional HMOs that are precluded under that legislation. So, we have followed that legislation as well, and have asked to be part of that. I think the Department agrees with us on that issue.

ASSEMBLYMAN OTLOWSKI: I just want to ask Assemblywoman Mullen if she has a question before we go to Assemblyman Scerni.

ASSEMBLYWOMAN MULLEN: No, thank you, I don't.

ASSEMBLYMAN OTLOWSKI: Assemblyman Scerni, do you want to--

ASSEMBLYMAN SCERNI: No, I think I understand Mr. Florio's position on these. I don't need anything further from him today.

ASSEMBLYMAN OTLOWSKI: Assemblyman Salmon?

ASSEMBLYMAN SALMON: Just a couple of questions. Mr. Florio, are your HMOs in the State of New Jersey all profit organizations, or are some nonprofit?

MR. FLORIO: I believe they are all for-profit.

ASSEMBLYMAN SALMON: You said they are in a stronger position financially now than ever before, and I saw a few smiles from the Department of Insurance.

MR. FLORIO: Well, whether it is the Kean administration or the Florio administration, I think the attitude about HMOs has remained the same with regard to their financial stability. I think I could argue the difference with them. The difference between two years ago and today is that it is much better. Quite frankly, a lot of them-- There have been some mergers and some acquisitions. As I said, only two are freestanding HMOs and not stepchildren, if you will, of the insurance companies, so there is a lot of financial support there. From my peripheral vision they are nodding their heads yes, that the industry is in much better shape, but that doesn't mean that it shouldn't be in better shape.

UNIDENTIFIED SPEAKER FROM AUDIENCE: The industry is in better shape, Mr. Chairman, but is the consumer?

ASSEMBLYMAN OTLOWSKI: We are going to say "Amen" to that. What I would like to do now is-- There are people here from the public who wish to be heard, and I am going to open the hearing up to them. I am just going to ask the Insurance Department to stay for a moment, because I want them to wrap this up from their perspective.

ASSEMBLYMAN SCERNI: I am going to get out of here.

ASSEMBLYMAN OTLOWSKI: You're going to leave?

ASSEMBLYMAN SCERNI: I am going to be leaving, okay?

ASSEMBLYMAN OTLOWSKI: Yes. As soon as I get pneumonia, make sure that my insurance is paid. All right?

ASSEMBLYMAN SCERNI: Basically, I am going outside to get warm. I am going to go outside to get warm. (referring to room temperature)

ASSEMBLYMAN OTLOWSKI: Bring some heat back, will you?

ASSEMBLYMAN SALMON: I was going to tell you, Mr. Chairman, the County College has experienced tremendous cuts from State government. They're saving on heat.

ASSEMBLYMAN OTLOWSKI: They brought that to our attention very well.

Let me just go to the public here, all right? Listen, thanks. Make sure you are there Wednesday. I want to talk to you Wednesday -- all right? -- when you come in Wednesday morning.

MR. FLORIO: I will be there, Mr. Chairman.

ASSEMBLYMAN OTLOWSKI: We start at 10:00, don't we, on Wednesday? (affirmative response from aide) All right?

MR. FLORIO: Fine, thank you.

ASSEMBLYMAN OTLOWSKI: Good, thank you. You have been very helpful. Thank you very much.

MR. FLORIO: Thank you for listening.

MR. KLINK: Thank you very much.

ASSEMBLYMAN OTLOWSKI: Now, is there anyone from the public who wants to be heard? (no response) Mr. Brody, do you want to be heard?

MR. BRODY: Well, all I can say, in my closing remarks--

ASSEMBLYMAN OTLOWSKI: No, no, we are not making speeches. We're testifying for the record.

MR. BRODY: All right. I just feel strongly that unless legislation is really enacted, we are going to have a

debacle the same as you had in the insurance industry. Frankly, I got on the Board originally and helped to found the Omnicare HMO for the protection of the consumer. As we all know, medical costs are running rampant. We now have all the HMOs -- which I just heard in testimony -- for-profit. The original concept for an HMO was for a nonprofit organization to deliver medical services to protect the consumer. This is now out the window. So whatever you have left-- I would strongly urge that you, with as much rapidity as possible, expedite legislation to protect the consumer from any further debacles, the same as you had in the insurance industry with the auto.

That is all I have to say, Mr. Chairman.

ASSEMBLYMAN OTLOWSKI: Thank you very, very much. Thank you for your contribution and, as a matter of fact, thank you for your patience with me.

The Insurance people now-- I think we have this pretty well wrapped up from your point of view, don't you think so? Do you want to say anything else in conclusion?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: (speaking from audience) I guess the only thing I would like to say is, Omnicare's experience shakes us up something awful. It is the second major liquidation that has taken place in the State of New Jersey.

ASSEMBLYMAN OTLOWSKI: Excuse me. Will you speak into the microphone for the record, please?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: I just want to make it very clear on the record that the Omnicare experience is one of two major liquidations that have taken place in the HMO industry in the last several years in the State of New Jersey. It really is of great concern to us in the Department, and I am sure to anybody who is interested in the quality of care in the entire medical care delivery system in the State of New Jersey.

It should be noted that in the Governor's Health Care Commission Study and Report, managed care systems, in which HMOs clearly play a major role, are conceived as being a critical key to the development of effective cost controls and more effective delivery systems going forward. If this is the pattern of the future -- and, to a very large extent, it clearly is part of the pattern of the future -- we have to make sure that the operations -- the organizations themselves are effectively delivering what they promise. They are custodians of the public interest in a real sense and, as such, need to be effectively regulated by the appropriate agency within State operations.

I think there is agreement between all parties that new legislation is appropriate and required. We look forward to working with the Assembly Committee to make sure that the legislation does, in fact, encompass all of the various ifs, ands, and buts, and dotted "i's," that have been indicated by the various Assemblymen who were here this morning.

We have appreciated the opportunity to come here to tell you what our feelings on this issue are.

ASSEMBLYMAN OTLOWSKI: I just want to tell you this: You have been very, very helpful, and very patient with us. As a matter of fact, I want to express a deep appreciation from the Committee for your cooperation and, as a matter of fact, for some of your pointed testimony.

What is the status of the litigation with Omnicare?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: There are motions currently before the court which would, in fact, reduce, or at least the last I saw it -- I have been away for 10 days, so I am not quite sure what has happened in those last 10 days -- but which would, in fact, remove some of the issues at litigation between the State and the principals of Omnicare/CompAAS which would hopefully operate to the benefit of the state of the Omnicare organization.

At this point in time, we are looking for the liquidation stage to come to a close by -- what, roughly the end of the second quarter of this year, Denise?

MS. LINTON: Or, no later than the fourth quarter.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: Sometime during 1991, we would like to see the liquidation, in fact, terminated, and all of the assets distributed, so that the Omnicare issue will be behind us once and for all. That is our hope.

ASSEMBLYMAN OTLOWSKI: Thank you. Assemblyman Salmon, do you want to wrap this up, please?

ASSEMBLYMAN SALMON: Thank you very much, Mr. Chairman.

MR. BRODY: (speaking from audience) Mr. Chairman, one thing I would like to ask, and I think it should be part of your considerations--

ASSEMBLYMAN OTLOWSKI: Wait a minute, excuse me.

MR. BRODY: It just came to me. What about the subscribers who may be possibly sued for nonpayment? I think this ought to be--

ASSEMBLYMAN OTLOWSKI: Do you want to sit down and ask that question?

MR. BRODY: I'm sorry, but this just occurred to me.

ASSEMBLYMAN OTLOWSKI: Just for the record, do you want to repeat the question?

MR. BRODY: I think your Committee -- or whoever has the legislation, or is in charge of it -- should protect the consumer who may be sued for nonpayment of a bill by one of the providers in this liquidation. This could be a very serious situation and have an adverse effect upon the consumer. I don't think there has been any provision for this.

ASSEMBLYMAN OTLOWSKI: That's the question? All right.

MR. BRODY: Right.

ASSEMBLYMAN OTLOWSKI: Do you want to answer that question, please?

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: This is a major concern of ours. Unfortunately, it has to be handled in the courts in such a fashion that there is a residual potential problem in this area. There will be a hearing on this issue on February 10 before the courts.

The Department's position, of course, would be to protect the subscribers, if at all possible. I am not sure how the courts are going to come out on this issue.

ASSEMBLYMAN OTLOWSKI: But that is a matter for the courts to deal with on February 10.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: At this point--

MR. BRODY: No, I think there ought to be State legislation to help the consumers.

SPECIAL DEPUTY COMMISSIONER MOSCOWITZ: Well, but that is ex post facto.

ASSEMBLYMAN OTLOWSKI: As a matter of fact, we are going to deal with that in the total legislative approach to this.

Ed, do you want to wrap this up, please?

ASSEMBLYMAN SALMON: Thank you very much, Mr. Chairman. First of all, I again would like to thank you and the members of the Committees and the staff for coming here and holding this hearing, so that those who wished to come to testify on the tragedy of the demise of Omnicare in our district would have the opportunity to do so.

I cannot state it enough that it was a tragedy -- what occurred with Omnicare HMO here in the district. It was a tragedy to the subscribers, those many thousands of individuals had came to know their doctors and know the people giving health care services, and who had great confidence in the kinds of services being given. It was a tragedy to the employees. It is something that has occurred. I would hope, if we could have one wish, that legislation will be brought forward and passed and signed by the Governor so that this will never happen again in the State of New Jersey.

ASSEMBLYMAN OTLOWSKI: Thank you very much. Again, I just want to express my appreciation to you, as the Chairman of this Committee, because you have been very, very helpful to us. Some of the testimony that came out here today, obviously we are going to be dealing with in the uncompensated care question and with some of the legislation that is going to follow.

To all of you here, thank you very, very much. You have been very kind, with the exception of whoever the custodian of this building is. He is a very cruel man -- heat-wise. Thank you again very, very much.

(HEARING CONCLUDED)

APPENDIX

NEW JERSEY HMO ASSOCIATION
TESTIMONY BEFORE THE
ASSEMBLY INSURANCE COMMITTEE
ASSEMBLY HEALTH AND HUMAN SERVICES

JANUARY 22, 1991

My name is Dale Florio, legislative counsel for the New Jersey HMO Association (the "Association"). With me today is Glenn Klink, Director of Administrative Services for Aetna Health Plans of New Jersey which is a wholly owned subsidiary of Aetna Life & Casualty Company and is the third largest HMO in New Jersey. Mr. Klink is a member of the Association's Executive Committee.

Health Maintenance Organizations (HMOs) provide comprehensive health care services to enrolled members on a prepaid basis. HMOs provide virtually all required services through organized provider networks for one monthly premium, with few if any copayments. Typically, members enroll in HMOs under arrangements where they select from among traditional insurance and HMO plans offered by their employer or other third party (e.g., Medicare). HMOs have enjoyed a rapid rate of growth in New Jersey over the past 15 years, now serving approximately one million members, or 14 percent of the state's insured population. (See attached census.) Nationally, 35 million Americans belong to HMOs, double

the number of only five years ago, with substantial growth projected in future years as a result of healthcare cost concerns.

Government policymakers as well as industry and labor leaders have shown widespread interest in HMOs because of their demonstrated ability to provide quality, coordinated health care on a cost-effective basis. In contrast to traditional health care arrangements that separate financing and delivery, HMOs provide comprehensive care directly to enrolled members through organized and integrated health care financing and delivery systems. Offering virtually complete coverage for a wide range of physician and hospital care, with an emphasis on preventive, diagnostic and therapeutic services provided outside of the hospital, HMO benefits lower barriers to early detection and treatment. Fixed, prospective premiums paid by or on behalf of enrollees encourage the HMO physician to use the most medically appropriate and cost-effective resources in meeting patient needs.

The HMO industry is not unlike any growing industry -- at some point in the growth cycle, adjustments occur. Two years ago, the HMO industry in New Jersey was comprised of many regional plans. Today, however, due to mergers and acquisitions, the industry has experienced a healthy consolidation which has resulted in a more efficient HMO industry.

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All of New Jersey's HMOs are affiliated with national insurance companies except for the State's two largest HMOs -- U.S. Healthcare and HIP/Rutgers Health Plan. This fact combined with rising enrollments suggests that the industry shake-out has run its course. As a result, the State's HMOs are stronger financially and better equipped to participate in the development of health care solutions.

Today, New Jersey's HMOs are stronger financially than at any time in recent history. The HMO potential for growth in New Jersey is significant. State policymakers have recognized that a managed care component is essential to providing greater access and stabilizing the rising costs associated with health.

The Association cannot comment specifically about the Omnicare situation because we are not privy to the intimate facts. Although Omnicare was a member of the Association prior to its demise, they left the Association several months after the inception of our organization because of their financial problems.

Although I am pleased to be able to say that the industry is stronger today than yesterday, the Association recognizes that revisions to the State's HMO laws will ensure the long term viability of the industry. The Association urges, however, that as the Legislature and the Administration review policy changes in regulating

HMOs, it should include solutions to the Omnicare situation as part of an overall proposal that requires HMOs to meet minimum financial requirements and allows HMOs to compete with traditional indemnity insurers. The former without the latter will cause chaos within the HMO industry.

Let us address the financial issue first. Present statutory and regulatory authority requires the Departments of Insurance and Health to make a finding that the HMO "is financially sound and may reasonably be expected to meet its obligations to enrollees and prospective enrollees" before the HMO can begin to operate. The HMO must also demonstrate to the satisfaction of the Departments that its contracts for health care services and scale of charges to enrollees are financially sound.

No regulatory scheme should keep a business afloat artificially. However, appropriate parameters for operation and transition from the market make sense. The Association supports many of the concepts in S-393 sponsored by Senator Richard Van Wagner (D-Monmouth) and A-4333 sponsored by Assemblyman Skip Cimino (D-Mercer) which would revise the law governing HMOs. The Association has worked closely with the Insurance Department for over 1 year. These bills include many of the principles discussed in those meetings. In fact, the Association

and the Department of Insurance are about to renew those discussions in order to refine the legislation.

Although there are a few first tier and numerous second tier issues of concern to the Association, we do support the net worth and minimum deposit requirements contained in the legislation. These financial requirements will preclude future Omnicare-type problems. The net worth and deposit requirements in the legislation are the same levels contained in the model legislation developed by the National Association of Insurance Commissioners.

The Association also supports a provision in the bill that would allow the Commissioners of Insurance to require HMOs and health insurance companies to offer coverage to affected consumers in the event of an HMO insolvency. This provision will provide consumers with continuity in their health care coverage. Please be aware that HMOs already participate in transition strategies as a general policy.

This hearing and a significant part of the Van Wagner/Cimino bills are focused on the financial stability of HMOs. As I mentioned earlier, any reform in how the State deals with HMOs also should include authority that will keep HMOs

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competitive in the marketplace. This legislation is an appropriate vehicle to give HMOs the flexibility to compete with commercial health insurers. Without this flexibility, HMOs will not be able to compete with indemnity insurers. Specifically, the Association supports increasing the flexibility and competitive position of HMOs by permitting HMOs to offer integrated in-and-out-of-network services now being marketed to employers by other health benefits organizations.

Similarly, the health care legislation dealing with small group coverage now under consideration by the Assembly Health Committee presents a dilemma for HMOs. Although the Van Wagner/Cimino legislation would insure a stronger HMO industry, legislation by Assemblyman Deverin and Senator Codey would make it difficult for HMOs to compete in the small group market with commercial health insurers. The playing field must be balanced if the State expects to have financially viable HMOs to continue to operate in New Jersey.

Any consideration of a bare bones program for small groups must recognize that federally qualified HMOs must provide a minimum benefit level, cannot charge deductibles and cannot include preexisting conditions in their policies. The minimum federal requirements exceed the benefit levels in the Codey bill. The Deverin bill provides that the Departments of Insurance and Health will establish

minimum requirements.

There are federally qualified HMOs that want to compete in the small group market. However, they are concerned that first, their product will not be cost competitive. Second, because HMOs cannot use preexisting conditions as exclusions, they would experience adverse selection that could cripple them financially. Finally, HMOs cannot experience rate their employer groups which also places them at a distinct disadvantage.

The Association looks forward to working with the members of the Legislature and the Administration on developing a policy that allows HMOs to continue to offer healthcare services to consumers in an efficient and cost effective manner. The consumer will be the ultimate beneficiary of these objectives.

Thank you for the opportunity to participate in this Joint Hearing.