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Health Republic's Curious Liquidation: Part 5

Law360, New York (October 7, 2016, 8:29 PM EDT) -- For those readers just joining us, Part 1 addressed how Health Republic Insurance of New York Inc., New York's only not-for-profit health insurer formed under the Affordable Care Act, opened in January 2014 and was shut down in the Fall of 2015. Part 2 explained why Health Republic's liquidation cries out for committees of policyholders and service providers to participate in Health Republic's recently commenced liquidation proceedings.



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Part 3 reported on a July 2016 status conference requested by outside counsel representing Maria T. Vullo, superintendent of the New York Department of Financial Services, in her capacity as Health Republic's liquidator. Counsel asked for the conference to advise the court overseeing the liquidation about a proposed claims procedure for Health Republic's 206,000 former policyholders. During the July conference, Justice Carol Edmead, who oversees the liquidation pursuant to NYIL Article 74, directed that counsel post contracts entered into with Health Republic's third-party administrators, vendors and counsel and also post all expenses incurred by these third parties.

Part 4 set out more reasons why committees of policyholders and service providers are desperately needed to weigh in during Health Republic's liquidation, particularly given the amount of money now being spent on vendors, outside counsel and third-party administrators.

Court Directs that Contracts and Expenses be Posted

During the July conference, the court directed that Health Republic's "administrative costs and related agreements" be posted online in order that "interested parties ... can see * * * the [estate's] administrative costs, and to whom those costs are going ..."[1]

The court also directed that the liquidator's counsel return to court with a revised claims procedure for policyholders, one that would address how policyholder disputes over claims would be handled.[2]

On September 20, counsel filed a revised, proposed order to show cause with respect to claims procedures for policyholders. The proposed order to show cause is now returnable at 10:00 a.m. in Supreme Court, New York County, Part 35 (Room 438) on Tuesday, Oct. 11, 2016.

At about the same time that counsel filed the revised order to show cause, a one-page summary of \$1.6 million in expenses paid by the estate for the ten-week period from May 11, 2016, through July 31, 2015, appeared on a website operated by the Garden City Group (GCG), one of Health Republic's third-party service providers.[3] The paid expenses summary may be found on the site under the heading: "Key Documents." The website also included under the heading key documents copies of five contracts/engagement letters with vendors, third-party administrators and counsel.

After unsuccessfully seeking additional information about the contracts and paid expenses from the DFS, I wrote to Justice Edmead and set out the questions and concerns that committees of

policyholders and service providers would probably raise if such committees were recognized.[4] What follows is a synopsis of those questions, some of which may be addressed on the October 11 return date of the proposed order to show cause.

Third-Party Contracts

Since I wrote to the court, two more agreements have been posted. You can now find on the Health Republic website seven engagement agreements or contracts. Five of the seven agreements/contracts were entered into before Health Republic was liquidated on May 10, 2016.

Here are the firms or companies for which contracts have been posted:

- a. Alvarez & Marsal, engaged to "assist with" an examination of Health Republic and to "wind down ... its operations" (one contract executed on Nov. 24, 2015 and another on Sept. 27, 2016);
- b. GCG, hired to provide notices, collect information on claimants and their addresses, run a website and provide related administrative services (executed on Nov. 24, 2015);
- c. EisnerAmper, engaged to audit Health Republic's statutory financial statements and schedules of federal government loans (executed on May 11, 2016);
- d. POMCO Inc., hired to review and audit policyholder claims, essentially the same functions that POMCO performed pursuant to a 2013 contract entered into with Health Republic before Health Republic began issuing policies (no date of execution provided);
- e. Weil Gotshal & Manges, retained to provide legal advice to the superintendent in her role as Health Republic's liquidator (executed on Nov. 19, 2014) ; and
- f. Rackspace, hired to provide data-base "hosting services" for Health Republic (executed in Dec. 24, 2013, a week before Health Republic issued its first policies).[5]

You can read these contracts and review the paid expenses summary yourself on the Health Republic website (maintained by GCG), but here are a few questions that committees of policyholders and service providers might raise.

Questions About the Contracts

1. A&M Agreement/Fees. Three persons signed the November 2015 A&M agreement, which runs for 16 single-spaced pages with a couple of appendices: Barbara Davis, Health Republic's board chair; Cheryl Aini, the DFS director of administration; and Ronald Vance, a managing director at A&M. Pursuant to the A&M Agreement, Mr. Vance became (and until late September apparently remained as) Health Republic's Chief Restructuring Officer or "CRO." [6]

The November 2015 A&M Agreement states that, pursuant to an October 2015 Health Republic board resolution, the board had consented to "having [Mr. Vance and other A&M personnel] operate under the supervision of the Department," but describes Vance as Health Republic's "Chief Restructuring Officer (the 'CRO')." [7] The September 2016 A&M agreement that Vance and DFS special deputy superintendent Scott Fischer just signed appears to demote Vance to a "consultant" role, but his hourly fee remains at \$675.[8]

The November 2015 A&M Agreement provided that for the month of November 2015, A&M's total hourly fees billed would not exceed \$395,000 "without the express written agreement of the Department." Under the November 2015 agreement, subsequent monthly billings would not exceed \$750,000 unless the department agreed in writing. A&M also agreed to provide "weekly bills to the Department for review." [9] The September agreement appears to have eliminated these caps on billing.

In the November 2015 A&M Agreement, Health Republic, which was at that point subject to the superintendent's supervision, agreed to pay promptly a retainer of \$395,000.[10] The September 2016 agreement reduced the retainer to \$150,000.[11]

As discussed below, the paid expenses summary does not cover the period from the date of the board's consenting to liquidation until the Health Republic liquidation order was entered on May 11, 2016. Where is the accounting for the fees paid to A&M from October 2015 through mid-May 2016? With respect to the November 2015 A&M Agreement, it appears that Vance engaged Weil on Nov. 19, 2014, even though the November A&M Agreement was executed on Nov. 24, 2019.

Under what contract or authority did Vance engage Weil before A&M entered into its agreement? Is there another A&M agreement that predates the November agreement? More importantly, if the board stepped aside in October 2015, and it appears that it did, who was hiring third-party administrators, engaging counsel and spending Health Republic's money from October 27, 2015 to May 10, 2016?

2. Weil Engagement/Fees. Five days before Vance executed the November 2015 A&M Agreement in his capacity as a managing director of Alvarez & Marsal Healthcare Industry Group LLC, Vance was the addressee on a "Restructuring Engagement" letter with Weil (Weil Engagement).[12] Vance hired Weil to "advise and represent [Health Republic] in preparation for, and in connection with, the administration and prosecution of a potential proceeding involving [Health Republic] under Article 74 of the New York Insurance Law ... and such other matters, if any, as may be listed on Schedule 1." [13]

Health Republic agreed to Weil's regular hourly rates of up to \$1,215 an hour.[14] Health Republic also agreed to pay promptly all monthly billings and also agreed to pay a \$250,000 "initial fee advance." [15] The Weil agreement contains an advance conflict waiver. Within the advance conflict waiver provision, the agreement states that: "[Health Republic] hereby consents to the engagement of Weil in connection with an Article 74 Proceeding by (i) the Superintendent of Financial Services of the State of New York in his capacity as rehabilitator or liquidator of the Company, and (ii) the New York Liquidation Bureau." [16]

The paid expenses summary does not identify any fees paid to Weil from the date of entry of the liquidation order, May 11, 2016, through July 31, 2016. During the July 28 status conference, the court did not limit the period for an accounting of Health Republic expenses. When will Weil's fees be posted and what period will the fees cover?

The Weil engagement letters calls for a \$250,000 retainer.[17] Has that been paid? Will Weil's billings, when posted, describe the services rendered so that these services can be matched with the service provider and the provider's hourly rates?

3. GCG Agreement/Fees. On Feb. 1, 2016, more than three months after Health Republic's board consented to the entry of an order of liquidation, Vance, acting for Health Republic, entered into an agreement with the GCG to "perform certain noticing, claims processing, and other administrative services" for Health Republic.[18] This work would be done in connection with Health Republic's anticipated liquidation.[19] The services to be provided by GCG were set out in an attached pricing summary and included: printing and sending notices, "importing claimant data," posting legal notices, scanning and storing records, creating a claimant name and address database, supplying "Interactive Voice Responses" and customer services representatives.[20]

GCG now maintains a website for Health Republic that includes FAQs, summaries of the claims process for policyholders, service providers, and general creditors, a court docket, and copies of documents filed in the liquidation proceeding. GCG also operates a phone bank and provides recorded messages for policyholders who call with questions.

The paid expenses summary shows that GCG was paid \$304,580 in June for mailing court orders and operating a phone center, but the summary also shows GCG paid nothing in

May and July.[21] Are the GCG's bills still under review? How much was GCG paid from October 2015 until May 10, 2016, and who approved those payments? Most importantly, when will GCG's billing be made available with a description of services showing hourly rates and specific services rendered?

4. EisnerAmper (E&A) Agreement. The "scope of services" set out in the E&A agreement describes an audit of Health Republic's financial statements "as of December 31, 2015 ... "[22] On information and belief, Health Republic's last financial statement was its Second Quarter 2015 statement as of June 30, 2015. The E&A agreement presumably would cover the second half of 2015, but would not address the period from Jan. 1, 2016 through May 10, 2016. Will there be a further audit for this period?

The E&A agreement contains a \$295,000 estimate for the fees required to complete E&A's statutory audit.[23] The paid expenses summary states that E&A was paid \$150,000 in June and \$145,000 in July for a total of \$295,000, which is precisely the estimated statutory statement audit cost.[24] If so, is the "statutory" audit complete? When will it be produced? [25]

It also appears that E&A's assignment does not include the review or audit of policyholder claims. In other words, can it be confirmed that the \$295,000 paid to E&A is not for the "audit" of pending policyholder claims that counsel referred to during the July 18th status conference?[26]

During the status conference on July 18, counsel stated that the liquidator was "finalizing agreements" with a third-party administrator to audit Health Republic's claims inventory and that this claims audit would take three to four months.[27] Who is performing this audit? Is the auditor POMCO?

5. POMCO Agreement. The original POMCO agreement, entered into on Feb. 1, 2013, established POMCO as Health Republic's "agent for the payment of claims." In that capacity, POMCO administered and, on information and belief, adjusted health claims for Health Republic during its short life.[28] The amended POMCO agreement has POMCO providing "Run-Out Services" as defined in the amended "Attachment A - Fees and Run-out Services." These services cover all aspects of claim handling, including "[c]laim adjudication against benefits." [29] Presumably that entails preparation of the explanations of benefits (EOBs) that counsel referred to during the July status conference.

The amended POMCO agreement calls for the payment of \$4 million "contemporaneous" with the execution of the POMCO agreement.[30] The Health Republic website now displays an "execution copy" of the POMCO Agreement, but without an execution page. Will an execution page be posted? Was POMCO, in fact, paid \$4 million on the date the POMCO agreement was executed?

The POMCO agreement calls for a \$400,000 retainer. [31] Was that paid? The POMCO agreement also calls for the payment of \$181,818 per month for providing "Claims Centric Adjudication Services," including, but not limited to, providing "Eligible Person EOBs." Has the \$400,000 retainer been drawn down to pay the monthly billings or is the estate paying \$181,818 per month and the retainer remaining at \$400,000?

Paid Claims Summary

The one-page paid expenses summary shows that the New York Liquidation Bureau was paid \$166,665 in June and July, but without any description of services rendered. Who at the bureau worked on the Health Republic matter in June and July and what did they do? On information and belief, a portion of the charges levied by the bureau pays for a pro rata share of the bureau's rent, directors and officers liability coverage, and employee benefits, including retirement benefits. Will those charges be isolated and broken out?

The paid expenses summary shows the following additional entities paid during the 10 weeks

from May 11, 2015 through July 31, 2015: DAZ, MegaPath, BDO Seidman, Finsbury, Dentons and Transperfect. No contracts were posted with respect to these entities. Were the monies set out in the paid expenses summary paid pursuant to invoices without any contractual commitments?

Finsbury's website describes Finsbury, which has offices in London, Beijing, Moscow, Brussels, Hong Kong, Singapore, Dubai and Abu Dhabi and clients such as Starbucks, Charles Schwab, Nielsen, Shell Oil and The Royal Bank of Scotland, as a "global leader in strategic communications" and a "trusted adviser to boards, senior executives and legal counsel of many of the world's most successful companies, institutions and organizations." What services is Finsbury providing to Health Republic, a failed not-for-profit New York health insurer capitalized solely with loans from the federal government?

Missing Balance Sheet.

Policyholders and service providers have not been provided with a balance sheet of Health Republic's assets and liabilities. Health Republic's last quarterly statement revealed that as of June 30, 2015, Health Republic had assets of \$530 million and total liabilities of \$444 million, but, to my knowledge, these figures have not been updated in any published report. Nor have the EisnerAmper audit results discussed above been released.

It is also unclear where Health Republic stands with respect to the Health and Human Services' (HHS) risk adjustment program, as well as where matters stand with respect to the federal government's loans to Health Republic. If the federal government is Health Republic's largest creditor, what priority of payment will the federal government assert? Has the superintendent discussed with HHS the nature of any federal government claims?

A simple, but complete, balance sheet would help Health Republic's policyholders understand whether they should bother to pursue their claims. Regardless of how consumer-friendly the claims process may turn out to be, a balance sheet would allow policyholders to determine how much of their ultimately approved claims will be paid. 50 cents on the dollar? Five cents on the dollar?

Where are we going; how long will it take; how much will it cost?

This court's direction that the liquidator post Health Republic's third-party contracts and the estate's expenses has shed more light on the status of the Health Republic liquidation than has either the DFS or the New York Liquidation Bureau. At this point, however, Health Republic's liquidation moves forward with almost no input from its 206,000 former policyholders or the dozens of major hospitals and practice groups that provided health services for these former policyholders.

Counsel now seeks the court's approval of a claims settlement procedure without, to my knowledge, obtaining comments or suggestions from either Health Republic's policyholders or service providers and without advising the court with respect to how much money is available to pay any ultimately approved policyholder claims.

These circumstances, and the questions raised above, call out for committees of policyholders and service providers in Health Republic's liquidation. These committees would help the court fashion procedures that will allow Health Republic to be wound up quickly and economically.

The court's direction that third-party administrator contracts be posted along with the expenses that are being paid from the estate's dwindling assets is a great step forward, but it's unclear how much money was spent from October 2015 to date. The snapshot provided for the 10-week period after the entry of the liquidation order reveals that more than \$1.6 million was spent and that's without Weil's fees. At that rate, more than \$8 million will be spent during the first year of Health Republic's liquidation.

When will policyholders (and service providers who hold an assignment of policyholder claims) be paid? Is there a target date for a partial payment?[32] Has the liquidator a target date by

which to close the estate? And what role, if any, will federal regulators at the Department of Health and Human Services have to play in these proceedings? These are the types of issues and questions that committees of policyholders and service providers could and should address during Health Republic's liquidation proceedings.

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[1] July Trans. at 6-7.

[2] July Trans. at 34-48.

[3] <http://www.healthrepublicny.org/>

[4] The letter appears as docket number 31 on the New York State Unified Court System site under New York Supreme Court Docket No. 450500/2016 (Vullo v. Health Republic Insurance of New York Corp.: <https://iapps.courts.state.ny.us/nyscef/>)

Among other things, my letter to the court pointed out that the paid expense summary referred to companies that had been paid, but whose contracts or letters of engagement were not produced, including a firm named Rackspace. The Health Republic website now has posted a Rackspace contract and another contract with Alvarez & Marsal, a contract executed on Sept. 27, 2016.

[5] For a snapshot of Health Republic's short history within the context of the Affordable Care Act, see Crain's investigation into Health Republic's rise and fall, including the timeline on p. 7/19. M. Waldholz, The short and chaotic life of an Obamacare darling, Crain's New York, http://www.craainsnewyork.com/article/201604017/HEALTH_CARE/160419890/a-craains-insurance

With respect to the receivership process, note that by mid-September 2015, the DFS had directed Health Republic to stop issuing new policies. On Oct. 27, 2015, Health Republic's board of directors consented to the entry of an order of liquidation or rehabilitation. Three days later, then-acting Superintendent Albanese directed that all Health Republic policies be terminated effective Nov. 30, 2015. The Department of Health and other New York state agencies helped Health Republic's 206,000 policyholders find other health coverage.

[6] November 2015 A&M Agreement, p. 1

[7] November A & M Agreement, p. 3

[8] September 2016 A&M Agreement, pp. 1, 4. The September 2016 agreement purportedly operates "as of May 10, 2016." September 2016 A&M Agreement, p. 1.

[9] 2015 A&M Agreement, pp. 4-5. The 2015 A&M agreement also makes clear that for the period from November 2 through the date of execution of the agreement, A&M was entitled to fees and expenses incurred during the negotiations that led up to the November 2015 A&M Agreement.

[10] Id. A&M may, under the agreement, invoice Health Republic to replenish the retainer agreement and would supply a copy of such invoice to the director of the administration bureau at the DFS. While neither the DFS nor any state agency is obligated to pay A&M for services rendered to Health Republic, "the Department [will] reasonably assist A&M in assuring that A&M's monthly statements are paid by the Company in a timely manner." A&M Agreement, p.

6.

[11] September 2016 A&M Agreement, p. 4.

[12] The letter came from Joseph Verdesca, Jr. at Weil, was addressed to Mr. Vance, and was executed on Health Republic's behalf by Christine Testaverde, Health Republic's General Counsel.

[13] Weil Engagement, p. 1 Schedule 1 is not attached to the engagement letter posted.

[14] Weil Engagement, p. 1 Health Republic also agreed to pay for "Computerized Legal Research," "Document Production" (defined as word processing that involves "over two continuous hours of work"), photocopies, and "Secretarial Overtime." Weil Engagement, p. 2.

[15] Weil Engagement, p. 2 Health Republic agreed to add to this retainer if necessary.

[16] Weil Engagement, p. 3

[17] Weil Agreement, p. 2.

[18] GCG Agreement, p. 1.

[19] GCG Agreement, p. 1.

[20] GCG Agreement, Exhibit A.

[21] Paid Claims Summary.

[22] E&A Agreement, p. 1.

[23] E&A Agreement, p. 8.

[24] Paid Expenses Summary.

[25] It appears that the E&A Agreement will not extend to E&A's "auditing" or, more accurately, preparing a summary of the Health Republic estate, pursuant to NYIL 7405(g). Under this provision, the Liquidator must submit to the DFS "an annual report of the preceding calendar or fiscal year's activity" for every New York-domiciled insurer subject to rehabilitation or liquidation. Because Health Republic was not placed in liquidation until mid-2016, that report will not be due until 2017.

[26] July Trans. at 10-11.

[27] July Trans. at 10-11.

[28] POMCO Agreement, p. 1.

[29] POMCO Agreement, p. 11.

[30] POMCO Agreement, p. 4.

[31] POMCO Agreement, p. 4.

[32] During the July conference counsel stated: "We are not going to make any distributions until the claims are all resolved." July Trans. at 26. Counsel also stated that it will take "18 to 24 months" before an initial distribution could be arranged. July Trans. at 49-50. There are no guaranty fund monies available to pay approved claims. Unless approved claims are paid on a partial basis, policyholders may not see any payments until three or more years after Health Republic stopped paying claims.

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