

STATE OF WISCONSIN

BEFORE THE OFFICE OF THE COMMISSIONER OF INSURANCE

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In the Matter of:

Proposed Acquisition of Control of  
Physicians Insurance Company of Wisconsin, Inc., by  
American Physicians Capital, Inc. and  
American Physicians Assurance Corporation ("Applicants")

RECEIVED  
WISCONSIN COMMISSIONER  
OF INSURANCE

Case No. 04-C29283

**REPLY BRIEF IN SUPPORT OF APPLICANTS' REQUESTED DISCOVERY**

The Applicants' discovery requests target the issues identified by the Commissioner at the prehearing conference, and by Physicians Insurance Company of Wisconsin, Inc. ("PIC") in its various assertions as to why the Form A should be disapproved. After PIC spent months disparaging the Applicants to PIC's shareholders, the Wisconsin Medical Society, the press, and to the Commissioner, it is now apparent that PIC had no good faith basis for its assertions, as it sidesteps every question in which it is asked to identify the factual basis for its assertions, the witnesses it will call if admitted as a party and the exhibits it intends to offer. One need only read through PIC's proposed responses to interrogatories # 6-21 to verify that PIC does not identify any factual basis for its assertions, other than a generic reference to Applicants' "public filings" and mysterious "other sources."

PIC has made repeated, vigorous statements to the OCI and the world in opposition to the transaction. Yet a generic reference to the "public filings" is the best that it comes up with as support for the vicious attacks that it has launched. It is difficult to know whether to characterize PIC's conduct as deceptive or irresponsible, or both. If PIC has no facts to support its claims, it should say so, and spare everyone the expense of proving facts that should be obvious – such as the fact that the proposed transaction will not create a monopoly or substantially lessen

competition in Wisconsin. If PIC has a basis for its wild assertions, it should be compelled to disclose it now.

Moreover, while professing its eagerness to move the proceeding along and bragging about the responses it is willing to give, a careful review of those responses indicates that PIC is not providing any meaningful information regarding its positions. On the one hand PIC states that it needs “full and probing” discovery, but yet attempts to limit all discovery pertaining to PIC through a partial, self-serving stipulation. If the Commissioner buys into this approach, it places PIC in the best position possible: PIC can avoid discovery on an issue it identified, without restraining PIC from introducing testimony at the hearing regarding the history of PIC and what the “intentions” were surrounding PIC’s formation and historical development. It is easy to see why PIC wants to proceed in this fashion, but it is difficult to conceive a more one-sided approach. The issues beyond the statutory tests (the history and purpose of PIC, whether the shares can be transferred) were introduced into this proceeding by PIC’s outcries. Unless PIC is willing to fully stipulate that these are not issues in this proceeding, it should not now be permitted to forego the results of its efforts to have the Commissioner consider these arguments.

In fact, PIC’s “responses” provide compelling support for the Applicants’ position that the Commissioner and his Staff do not need PIC’s presence as a party to assist them in determining the facts. PIC basically admits that it has no facts to support the arguments that it has been making for months. After having advanced these arguments without support and convinced the Commissioner that the issues should be considered seriously, PIC cannot now run for cover and say that it has no facts, but wants to look for some. If the Commissioner or his Staff want to pursue any of the issues identified by PIC, they are more than capable of doing so

in a professional, balanced method that sets aside the grandstanding, and allows for an appropriate discussion of the merits.<sup>1</sup>

PIC also berates the Applicants for “building delay” into the discovery process, as the Applicants objected to PIC’s purported “service” of discovery responses before it is admitted as a party, and before the Commissioner has decided whether to permit any discovery in this proceeding. The Applicants’ letter to PIC’s counsel was an appropriate response to PIC’s attempt to end-run the procedure spelled out during the prehearing conference. Non-admitted parties do not have the right to serve discovery, and the Commissioner has not determined what, if any, discovery will be permitted. Furthermore, the Applicants will not be the source of any delay in this matter. If the Commissioner permits discovery along the lines outlined in the Applicants’ brief in opposition to PIC’s discovery requests, the Applicants will be prepared to provide the information that they have identified within a week of the Commissioner’s Order.

With these issues in view, this reply brief analyzes the responses offered by PIC using the same categories identified at page 9 of Applicants’ original brief in support of the discovery requests.<sup>2</sup>

#### **Discovery Regarding Transferability Of PIC Stock**

At the prehearing conference, and in the subsequent prehearing memorandum, the Commissioner stated that he would evaluate “the effect of the proposed plan on the history and purpose of PIC of Wisconsin, including the extent to which the stock is or was intended or expected to be transferable and the contribution of PIC of Wisconsin to the Wisconsin insurance

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<sup>1</sup> The only purported “facts” identified as supporting PIC’s position are the Applicants’ public filings and AM Best reports, both of which are fully available to the Commissioner without PIC’s assistance.

<sup>2</sup> This reply does not address those requests where PIC has indicated it is willing to respond, as those are presumably not contested.

marketplace.” (Transcript, pp. 28-29.) The Commissioner also stated that he wanted to understand the “bigger picture” in order to evaluate whether the stock is transferable and what the market may be like in the future. (Transcript, p. 30.) The majority of the discovery requests proposed by the Applicants were designed to elicit information responsive to this statement by the Commissioner. (Interrogatories #1-4, Document Request #1-16, and Request to Admit #1-11.)

PIC proposes to respond to these requests by a stipulation that “PIC stock is transferable, subject to certain limitations, as stated.” (PIC Exhibit C, p. 1.) This proposal is woefully inadequate for several reasons.

Initially, the proposed stipulation addresses only part of the issues identified by the Commissioner. PIC has been arguing for months that it is a unique entity that is somehow not bound by the usual rules that apply to stock corporations, fostering the impression that its shareholders should expect to be treated poorly because the original prospectus advised purchasers of the risk that the stock would not be publicly traded, and would be subject to restrictions for nine months following the purchase.

PIC has also made clear that it intends to argue that its unique history means that the Commissioner should treat this transaction differently than any other stock transaction. For example, in its Memorandum in Support of Its Request to Be Admitted as A Party, PIC makes the following statements:

- “The Wisconsin market has come a long way since PIC was founded, and PIC has played a significant role in bringing stability to this crucial segment.”

(Memorandum, p. 1.)

- “Respectfully, there is no way that these issues [the history and contribution of PIC and whether its shares were intended or expected to be transferable] can be considered – much less “contested” – without PIC’s participation as a party.”  
(Memorandum, p. 8.)
- “No other person or entity has a greater interest regarding whether APC’s acquisition of control is likely to ... (c) affect PIC’s history or purpose...”  
(Memorandum, p. 8.)
- “PIC is not a publicly traded stock corporation, and its business structure was designed to further PIC’s core philosophy and mission (i.e., providing quality, stable, and affordable medical malpractice insurance in the Wisconsin market.)”  
(Memorandum, p. 9.)
- “Because PIC shares are not publicly traded, the company is insulated from the customary pressure to maximize shareholders’ investments, which may work to the detriment of public companies’ financial stability and long-term goals.”  
(Memorandum, p. 9.)

The stipulations offered by PIC address only a fraction of these issues. They do not delve into all the issues surrounding the formation of PIC. The stipulations do not provide information regarding the multiple efforts that PIC has made to provide its shareholders with a more ready opportunity to sell their PIC stock or to otherwise realize a reasonable economic return on their investment in PIC, telling them repeatedly (and as recently as this year’s proxy statement) that it is attempting to bring value to its shareholders. They do not address the fact that PIC long ago abandoned any original “intentions” that PIC would be writing business only in Wisconsin for Wisconsin policyholders. Unless PIC is willing to retract its statements outlined above, or the

Commissioner determines that the substance of such statements is irrelevant to these proceedings, the Applicants should be permitted to discover the documents that will show how PIC has changed over the years, how the stock has been transferred repeatedly, how PIC has responded to other proposals to acquire shares, how PIC's insiders routinely receive stock as compensation and view it as a valuable asset, and how its policyholder and shareholder bases are no longer the same. This information is vital to the evaluation of the credibility of PIC's positions.

At PIC's urging, the Commissioner identified the issues of transferability and PIC's "history and purpose" as relevant to the hearing. If PIC will stipulate that the stock at issue in the transaction is transferable, and that the "history and purpose" of PIC are not issues for the hearing, then the Applicants can withdraw their discovery on these issues. The proposed stipulation does not come close to agreeing to these points, although it does confirm that the whole issue of "transferability" has been a red-herring since the beginning. If the proposed stipulation does not completely convince the Commissioner that the "issues" raised by PIC are spurious, then the Commissioner should grant the discovery requested.

Finally, it is unclear from the proposed stipulation whether PIC is claiming that the transaction outlined in the Form A violates any of the "restrictions" it identifies in the proposed Stipulation, ¶¶ 4-7. If PIC is claiming that the proposed purchase will violate one of more of these restrictions, then PIC should be required to state which restriction(s) it is claiming are violated and the basis for this contention. It is inappropriate for PIC to lead everyone to believe that it has agreed that the stock is transferable, and then attempt to argue at the hearing that it is not transferable because of one of the "restrictions" it mentions in the stipulation. The

Commissioner should require PIC to clarify this issue and, if any of the “restrictions” are at issue, provide the Applicants with discovery regarding that issue(s).

#### **Discovery Regarding the Issue of Control**

The Applicants have requested documents sufficient to show shareholder votes on three particular issues (Document Request #19). PIC gives an ambiguous response, stating that it will produce documents reflecting “voting participation in various contexts during relevant periods.” It is impossible to tell from this response whether PIC will provide information regarding voting participation in the three votes identified by the Applicants, all of which raised issues of importance to the shareholders. Given that PIC has the information readily at hand for these three votes, it should be required to produce it.

The Applicants also request documents relating to the Rights Agreement (Document Request #18). PIC refuses to produce such documents, claiming that it is not relevant, and the request is “burdensome and oppressive.” The information sought is relevant to the issue of whether the Applicants will acquire control following the transaction. The Applicants believe that the requested documents will demonstrate that PIC adopted the Rights Plan specifically to (1) prevent Applicants from acquiring any additional shares without triggering the poison pill, and (2) to put in “shark repellants” that make it difficult for any shareholder to exercise its shareholder rights. The request is narrowly drafted, and seeks documents that pertain specifically to an issue in this proceeding. As such, the Commissioner should order PIC to comply with the request.

#### **Issues Advanced By PIC In Opposition To The Form A**

The final category of information sought by the Applicants pertains to issues that have been raised by PIC in its public statements and its pitches to the Wisconsin Medical Society in

opposition to the Form A filing. The most blatant attempt by PIC to avoid discovery on these issues is evidenced by its responses to interrogatories 8 through 18. These are standard contention interrogatories, designed to elicit the factual basis for PIC's many unfounded assertions made throughout the last nine months. PIC refuses to answer any of these interrogatories at this point, sometimes alluding only to unspecified "public filings," "other sources" and "A.M. Best" reports. An example of PIC's evasiveness is its response to the interrogatory asking whether PIC contends that it will be unable to satisfy the requirements for the issuance of a license if the sale is approved, and the basis for that contention. (Interrogatory #8.) PIC gives a non-responsive answer, claiming it needs discovery on this issue. How can PIC not know whether it satisfies the licensure requirements in the State of Wisconsin?

The Applicants are entitled to understand the full factual basis for the disparaging comments made by PIC, and the witnesses and exhibits it intends to use in support of them. If, as the Applicants suspect, the allegations were made without any support, PIC should be required to simply admit that fact.

If PIC intends to attempt to prove any of these contentions, the Applicants are not able to prepare fully for the proceeding without knowing the factual basis for them. Under PIC's approach, it will not be disclosing the basis for any of its positions until after discovery is completed. This is classic sand-bagging, and should not be permitted by the Commissioner. For example, it is simply incredible that PIC intends to assert that this transaction creates a monopoly or "substantially lessens competition" under Wis. Stats. § 611.72, but yet claims not to know what facts support this contention. (See response to Request to Admit # 9).

PIC also seeks to avoid providing information regarding its exodus from a number of states after it acquired Century American Casualty Company and Century American Insurance

Company. The Applicants provided PIC with an opportunity to agree that a history of acquiring companies and exiting various insurance markets is not relevant to these proceedings. In particular, interrogatory #15 sought the basis for PIC's assertion that "there are serious questions about Petitioner's history of acquisitions and dispositions of companies." Rather than conceding that the issue is irrelevant, PIC states that its contentions are based on "publicly disclosed (by APC) information and other sources, including A.M. Best Reports." It is clear that PIC is not abandoning this argument, although it has refused to describe any specific facts that it believes support its position in the proceeding. Pointing to an unspecified portion of the Applicants' voluminous public filings and to unspecified "other sources" discloses nothing.

If the Commissioner agrees with PIC that whether APA exited certain crisis markets like Nevada and Florida is relevant to these proceedings, then APA should be permitted to introduce evidence that it acted like any prudent insurance company would in the face of ineffective tort reform and a poor loss ratio. Indeed, PIC has reacted to the same kind of information by doing the exact same things that it is criticizing the Applicants for doing. The Applicants are entitled to establish this for the Commissioner so that PIC's arguments can be viewed in context. PIC should be required to respond to Document Request 21.

Document Request #24 seeks documents reflecting the negotiations between PIC and the Wisconsin Medical Society regarding the terms of their financial relationship. PIC has objected to this request on the ground that the documents "are not relevant" to these proceedings. As stated in the Applicants' brief seeking the discovery, the Applicants believe that PIC may be placing inappropriate pressure on the Medical Society to support its position in these proceedings through the negotiations regarding their continuing business relationship. In the event that PIC offers testimony from Medical Society members in opposition to the Form A, the Applicants are

entitled to demonstrate a bias that may exist in PIC's favor as a result of the ongoing negotiations. Evidence seeking to demonstrate the bias of a witness is discoverable.

Document Request #25 seeks all documents addressing the proposed sale or acquisition of PIC stock from or to any person, including the Applicants. The Applicants have been advised that the PIC Board planned to pass a resolution stating that they intended to oppose any acquisition of PIC stock, regardless of the party seeking to purchase the stock. This document would demonstrate a bias and perspective on the manner in which PIC treats its shareholders, which in turn will demonstrate that it is motivated by the entrenchment of management, not protection of the policyholders or shareholders.

#### **PIC's Argument Regarding Depositions**

PIC has never identified who it intends to depose in this matter, generically stating that it envisions taking 10-15 depositions. Depositions are unnecessary in a Form A proceeding. If the Commissioner disagrees and authorizes fact witness depositions, then both sides should be permitted to take depositions. The Applicants should be permitted to depose, at a minimum, Mr. Montei, Dr. Roberts, Dr. Listwan and any other witnesses that PIC seeks to call at the hearing.

#### **Conclusion**

Unless the Commissioner is satisfied that the stock is transferable, and PIC's "history and purpose" are no longer issues in this proceeding, the requested discovery should go forward so that Applicants can present appropriate proofs. The Applicants are also entitled to refute the positions taken by PIC, and demonstrate that they have no basis in fact, and that the business practices it criticizes are the same practices PIC itself has used over the years. Alternatively, the Commissioner can recognize that PIC offers nothing original or unique to these proceedings, and it can proceed without PIC as a party.

Respectfully submitted this 22nd day of June, 2005:

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