

THE UNIVERSITY OF MICHIGAN
REGENTS COMMUNICATION

Approved by the Regents
September 22, 2006

ACTION REQUEST

Subject: M-CARE

Action

Requested: Authorization to sell M-CARE and its subsidiaries

Background:

We are requesting authorization to sell M-CARE and its subsidiary M-CAID to Blue Care Network (a subsidiary of Blue Cross Blue Shield of Michigan), and sell M-CARE's subsidiary Michigan Health Insurance Company to Blue Cross Blue Shield of Michigan for a combined price of \$240 million. The pursuit of this transaction will help to ensure that the University of Michigan Health System remains sharply focused on our critical missions of education, patient care, and research.

M-CARE was started by the University in 1986 in response to the ascendancy of managed care in the healthcare marketplace, in order to provide patient activity for UMHS in an era of hospital overcapacity, as well as provide the University flexibility and experience owning and managing a primary health insurance benefit. However, in the past 20 years the healthcare marketplace has changed. Increasing patient volumes have created a situation of under capacity in the hospital market, as well as within UMHS. The managed care industry has also changed. There has been significant consolidation, as larger plans buy smaller plans. In addition, the demands for significant capital investment in information technology in response to market and governmental demands has made it difficult for smaller health plans to compete. We anticipate that this need for capital will accelerate in the future as the managed care marketplace becomes increasingly complex and competitive.

The University is committed to providing our faculty and staff excellent healthcare benefits. We have carefully considered the impact of this transaction on employees, dependents, retirees, and graduate students who are currently enrolled in M-CARE. The University remains fully committed to continuing to offer a variety of high quality, affordable, and market-competitive health benefits to our employees, retirees and their dependents following this transaction.

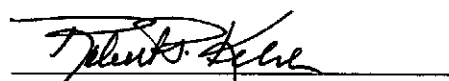
In 2005, M-CARE served approximately 200,000 members across Southeastern Michigan, with revenue of \$536 million and operating income of \$4.8 million.

We have engaged Cain Brothers, a Wall Street investment banking firm with deep expertise in the sale of provider-owned health plans, to assist the University with this transaction. They have performed a valuation of M-CARE, using a number of valuation techniques. Cain Brothers believes that \$240 million represents a fair and appropriate price for M-CARE.

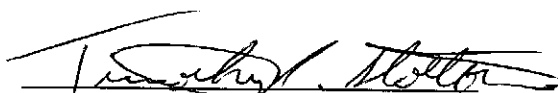
In addition to the sale of M-CARE, the University and Blue Cross will enter into a joint venture to build upon our history of successful collaboration in multiple quality and efficiency initiatives. The goal of the joint venture is to improve healthcare delivery and public health. The venture will initially be focused on improving quality, safety, efficiency, and appropriateness of healthcare delivery through research, demonstration projects, and quality improvement programs.

We therefore recommend that the Board of Regents authorize the sale of M-CARE and its subsidiary M-CAID to Blue Care Network and the sale of M-CARE's subsidiary Michigan Health Insurance Corporation to Blue Cross Blue Shield of Michigan for a total negotiated price of \$240 million, subject to final due diligence and review by relevant government authorities; acknowledge the authority of the executive vice president and chief financial officer to negotiate and execute a final purchase agreement and all related documents; and authorize the EVPCFO to take all appropriate actions required of the University under the purchase agreement and such other actions as may be necessary to complete the transaction including, but not limited to, revising the M-CARE bylaws and articles of incorporation to convert to a stock corporation to facilitate this transaction, all in close collaboration with the executive vice president for medical affairs.

Respectfully submitted,



Robert P. Kelch
Executive Vice President for
Medical Affairs



Timothy P. Slottow
Executive Vice President and
Chief Financial Officer

September 2006