

# Uncovering a Multi-Million Dollar Pattern of Deception

Superior Court rules in favor of the  
school district in SAUSD vs. KMEBS

May 2, 2011

# The Judge's Ruling

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- After a 7-year legal battle, the courts ruled that the District's health benefits insurance consultant KMEBS unlawfully concealed millions of dollars in commissions it received from Blue Cross
- Kirk Montgomery and Bridget Sirkegian were ordered to repay \$2,481,399.96 plus interest to Santa Ana USD

# Three Phases Over a Decade

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## ➤ Bidding & Contracting

- 2000 to 2001

## ➤ Investigation & Disclosure

- 2002 to 2004

## ➤ Litigation & Restitution

- 2004 to 2011

# Background and History

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## ➤ In 2000

- District issues RFP seeking insurance consultant to manage/administer health benefit plan (July)
- Committee ranks KMEBS 5<sup>th</sup> out of six in competitive bidding and puts forward top three bidders to the school board (August)
- School Board decides to interview all six bidders (September)

# Background and History

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## ➤ In 2000

- On a 3-2 split vote, School Board selects KMEBS as its district consultant (October)
  - Nadia Davis, Nativo Lopez and John Palacio vote in favor
  - Rosie Avila and Audrey Yamagata-Noji vote to oppose
- KMEBS contract (11/01 to 10/03) drafted after two months of wrangling over commission language (December)

# Background and History

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## ➤ In 2000

Actual contract language:

- “All parties agree that certain carriers have as part of their underwriting process, built-in commissions that are not removed from the rating formula. In these cases, *the Consultant will remit any commissions, overrides or other carrier compensation to the District to One Hundred Percent (100%) of the total fee.*” (November)
- KMEBS begins receiving \$5,000 per month retainer to manage the District’s health benefit account

# Background and History

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## ➤ In 2001

- KMEBS seeks insurance bids and recommends moving from self-insurance to a covered plan (February)
  - KEY: This enables KMEBS to collect commissions
- Blue Cross plan quoted, but KMEBS fails to disclose 5% commission is included in the bid
  - KEY: First evidence that KMEBS was deceiving the district by failing to disclose its financial arrangement

# Background and History

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## ➤ In 2001

- School board approves, on consent, changing the PPO medical benefits from a self-funded program to a fully-insured program with Blue Cross. (July)
- Estimated annual premium: over \$19 million

# Background and History

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## ➤ In 2002

- KMEBS submits “doctored” renewal calculations to the District concealing commissions; then does so again in 2003 (Spring)
- KEY: Montgomery firm re-types Blue Cross calculation form by consolidating categories to hide commission figures

# Background and History

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## ➤ In 2003

- New school board members seated and start asking questions about commissions (December-February)
- During open bidding on contract renewal KMEBS refuses publicly to disclose if commissions are being paid when asked directly by the Health Benefits Committee (September)
- Blue Cross informs the district that it cannot provide commission information because of a threatened lawsuit by KMEBS over privacy rights (September)

# Background and History

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## ➤ In 2003

- School Board approves interim two-month contract extension for November-December since KMEBS contract expired October 30, 2003 and coverage renewal was in progress
- School Board interviews potential consultants and KMEBS refuses to answer a direct question about whether it had received commissions (December)

# Background and History

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## ➤ In 2004

- One-month interim contract extension granted to KMEBS as the District transitions to a new insurance consultant (January)
- School Board officially drops KMEBS as its benefits consultant and retains Mercer (January)
- With assurance of immunity, Blue Cross provides the District with evidence of non-disclosed commissions paid to KMEBS (February)

# Background and History

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## ➤ In 2004

- Blue Cross data show KMEBS was paid \$3,683,702.87 over a 39-month period (March)
- School District files lawsuit against KMEBS for breach of contract and non-disclosure of commissions (April)

## ➤ 2004 to 2011

- The school district spends seven years in a legal battle with KMEBS to get commissions paid back

# Getting Our Day in Court

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- KMEBS waged an aggressive defense filing numerous motions which dragged out the process
- The case was shifted to Riverside County at KMEBS' insistence using a technical rule that allows a lawsuit to be heard in a neutral location outside of a public entity's jurisdiction
- Case backlog in Riverside Superior Court and illnesses among the parties led to further delays

# Getting Our Day in Court

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- Phase I bench trial held on June 8, 2008 to determine whether breach of contract language occurred
  - Trial Judge Kraetzer concludes contract language is ambiguous enough to not lead to breach of contract ruling. So trial moves to second phase regarding KMEBS' non-disclosure and concealment tactics and whether they constituted a tort against the district

# Getting Our Day in Court

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- Phase II bench trial over eight days began on January 31, 2011. The ruling:
- The contract language may have been ambiguous enough to not establish a clear cut breach of contract, but the evidence was ample to show a tort was committed by concealment

# Facts in the Case Revealed

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- Blue Cross data show KMEBS was paid \$3,683,702.87 in commissions over a 39-month period
- In court documents, KMEBS revealed they paid former SAUSD trustee Sal Mendoza \$1,041,367 to be associated with the firm as its contract was being adopted by the SAUSD Board of Education

# During the Trial

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- The most compelling evidence was the refunding calculation worksheet intentionally altered by Kirk Montgomery before being submitted to the District
  - The August 7, 2002 form was re-typed in a similar format, but omitted any reference to commissions paid by Blue Cross
  - The court ruled that this was clearly an effort to “conceal” the true nature of KMEBS’ financial arrangement

# Concealing Commissions

Actual Blue Cross Table

KMEBS "Doctored" Table

REFUNDING CALCULATION  
Santa Ana USD  
Prudent Buyer  
EFFECTIVE DATE  
7/1/2002

CALCULATION COMPONENTS	MEDICAL	PHARMACY	TOTAL
MEDICAL PAID CLAIMS 01/01/01 TO 01/01/02	\$10,609,600	\$1,336,951	\$11,946,551
DRUG PAID CLAIMS 06/01/01 TO 01/01/02	\$0	\$0	\$0
ADJUSTMENT FOR BENEFIT MODIFICATION	(\$536,742)	\$0	(\$536,742)
CREDIT FOR LARGE CLAIMS	\$10,072,858	\$1,336,951	\$11,409,809
ADJUSTED PAID CLAIMS	\$2,007,400	\$0	\$2,007,400
BEGINNING RESERVE	\$2,330,659	\$241,445	\$2,572,104
ENDING RESERVE	\$10,396,117	\$1,578,396	\$11,974,513
ADJUSTED PAID CLAIMS	32,163	12,400	44,563
EXPOSURE (MEDI) 01/01/01 TO 01/01/02	\$323.23	\$117.53	\$440.76
EXPOSURE (PH) 06/01/01 TO 01/01/02	1.2236	1.2282	2.4518
CLAIMS COST PER CONTRACT	\$395.51	\$60.00	\$455.51
TREND:	\$0.00	\$143.99	\$143.99
PROJECTED CURRENT COST PER CONTRACT	\$395.51	\$143.99	\$539.50
ESTIMATED BCC DISCOUNT SAVINGS	\$7.12	\$0.00	\$7.12
PROJECTED BCC COST PER CONTRACT	\$402.63	\$143.99	\$546.62
ADJUSTMENT FOR PROPOSED BENEFIT MOD	21,892	31,982	53,874
ADJUSTED INCURRED COST PER CONTRACT	\$424,525	\$175,971	\$600,496
PROJECTED PARTICIPATION	\$12,880,939	\$4,606,528	\$17,487,467
ADJUSTED PROJECTED PAID CLAIMS	\$12,880,939	\$184,281	\$13,065,220
ADJUSTED PROJECTED PAID CLAIMS**	\$115,238	\$0	\$115,238
MARGIN 4.00%	\$490,784	\$0	\$490,784
LARGE CLAIMS	\$784,612	\$205,442	\$990,054
COMMISSION	\$0	\$0	\$0
PREMIUM TAXES	\$1,016,951	\$62,008	\$1,078,959
RETENTION	\$12,088,244	\$4,805,489	\$16,893,733
REQUIRED RENEWAL PREMIUM	\$13,828,508	\$4,805,489	\$18,633,997
REQUIRED PREMIUM	1,1345	1,0631	2,1976
REQUIRED RENEWAL ADJUSTMENT			

\*\*\*SEE ATTACHED CALCULATION NOTES PAGE.

Exhibit 96 Page 3  
BCC00188

KMEBS re-typed this worksheet and combined these two lines to hide its commission

BLUE CROSS OF CALIFORNIA  
REFUNDING CALCULATION  
PRUDENT BUYER  
SANTA ANA UNIFIED SCHOOL DISTRICT  
EFFECTIVE DATE JULY 1, 2002

CALCULATION COMPONENTS	MEDICAL	PHARMACY	TOTAL
MEDICAL PAID CLAIMS 01/01/01 TO 01/01/02	10,609,600	1,336,951	11,946,551
DRUG PAID CLAIMS 06/01/01 TO 01/01/02	0	0	0
ADJUSTMENT FOR BENEFIT MODIFICATION	0	0	0
CREDIT FOR LARGE CLAIMS	(536,742)	0	(536,742)
ADJUSTED PAID CLAIMS	10,072,858	1,336,951	11,409,809
BEGINNING RESERVE	2,330,659	241,445	2,572,104
ENDING RESERVE	10,396,117	1,578,396	11,974,513
ADJUSTED (INCURRED) PAID CLAIMS	32,163	12,400	44,563
EXPOSURE (MEDI) 01/01/01 TO 01/01/02	323.23	117.53	440.76
EXPOSURE (PH) 06/01/01 TO 01/01/02	1.2236	1.2282	2.4518
CLAIMS COST PER CONTRACT	\$395.51	\$60.00	\$455.51
TREND:	\$0.00	\$143.99	\$143.99
PROJECTED CURRENT PER CONTRACT	\$395.51	\$143.99	\$539.50
ESTIMATED BCC DISCOUNT SAVINGS	\$7.12	\$0.00	\$7.12
PROJECTED BCC COST PER CONTRACT	\$402.63	\$143.99	\$546.62
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ADJUSTED PROJECTED PAID CLAIMS	\$12,880,939	\$184,281	\$13,065,220
ADJUSTED PROJECTED PAID CLAIMS	\$115,238	\$0	\$115,238
MARGIN 4.00%	\$490,784	\$0	\$490,784
LARGE CLAIMS (LOOKING @ \$200,000)	\$784,612	\$205,442	\$990,054
COMMISSION	\$0	\$0	\$0
PREMIUM TAXES	\$1,016,951	\$62,008	\$1,078,959
RETENTION	\$12,088,244	\$4,805,489	\$16,893,733
REQUIRED RENEWAL PREMIUM	\$13,828,508	\$4,805,489	\$18,633,997
REQUIRED PREMIUM	1,1345	1,0631	2,1976
REQUIRED RENEWAL ADJUSTMENT			

Exhibit 74 Page 3  
SA 04281

This submission by KMEBS was re-typed to omit any reference to commissions paid by Blue Cross

# The Judgment

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In his ruling, Judge Dallas Holmes said Montgomery:

- “Snookered” the District when he got it to accept vague language in Section 3 of the contract
- “Lied” to SAUSD by revising tables from Blue Cross to hide commissions and then submitting those revisions to his client as if they were Blue Cross documents
- “Stonewalled” the District when it tried to find out what he was making as non-disclosed commissions
- “He may have tried to walk an ethical tightrope here, but the evidence shows he did not succeed.”

# The Judgment

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In his ruling, Judge Dallas Holmes said KMEBS:

- Committed the tort of concealment which entitles the district to damages
- Kirk Montgomery (dba KM Employee Benefits Services) has been ordered to re-pay the school district \$2 million
- Bridget Sirkegian, an employee of KMEBS, has been ordered to repay \$481,399.96.
- SAUSD may be awarded pre- and post-judgment interest dating from 2004 that could add more than \$1.2 million to the final penalty

# Where do we go from here?

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- KMEBS has not indicated whether they will appeal this decision
- SAUSD will seek interest and fees totaling more than \$1.2 million dating from 2004
- Collection process will commence
- For more information and background documents access the “KMEBS Lawsuit” link on the District web page ([www.sausd.us](http://www.sausd.us))