

# ***Independence Blue Cross and Subsidiaries***

*Consolidated Financial Statements as of  
December 31, 2004 and 2003 and for the Years  
Ended December 31, 2004, 2003, and 2002,  
and Independent Auditors' Report*

## INDEPENDENT AUDITORS' REPORT

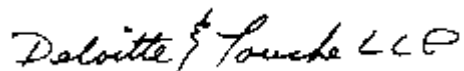
Members and the Board of Directors  
Independence Blue Cross  
Philadelphia, Pennsylvania

We have audited the accompanying consolidated balance sheets of Independence Blue Cross and subsidiaries (the "Company" or "IBC") as of December 31, 2004 and 2003, and the related consolidated statements of income and comprehensive income, changes in reserves, and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of IBC's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Independence Blue Cross and subsidiaries at December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the financial statements, in 2002 the Company changed its method of accounting for goodwill to conform to Statement of Financial Accounting Standards No. 142.



April 27, 2005

## INDEPENDENCE BLUE CROSS AND SUBSIDIARIES

### CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2004 AND 2003 (Dollars in thousands)

<b>ASSETS</b>	<b>2004</b>	<b>2003</b>	<b>LIABILITIES AND RESERVES</b>	<b>2004</b>	<b>2003</b>
CASH AND CASH EQUIVALENTS	\$ 466,361	\$ 766,363	CLAIMS LIABILITIES	\$ 1,459,277	\$ 1,537,597
INVESTMENTS AVAILABLE FOR SALE	1,912,163	1,618,365	ACCOUNTS PAYABLE AND ACCRUED EXPENSES:		
RECEIVABLES:			Merit rating refunds	21,353	18,433
Member and national account premiums	459,273	478,422	Accrued expenses	221,052	238,244
Federal Employee Health Benefits Program	55,056	54,882	Accrued postretirement benefits	37,715	32,104
BlueCard Program	122,656	86,302	Income taxes	-	96,461
Interest	17,252	17,719	Other	<u>119,310</u>	<u>156,508</u>
Other	<u>51,078</u>	<u>41,846</u>			
Total receivables	<u>705,315</u>	<u>679,171</u>	Total accounts payable and accrued expenses	<u>399,430</u>	<u>541,750</u>
Prepaid expenses	99,113	14,204	UNEARNED INCOME	425,753	384,984
Property and equipment—net	81,212	139,659	LONG-TERM DEBT	<u>64,900</u>	<u>70,172</u>
Other assets	111,535	144,662	Total liabilities	<u>2,349,360</u>	<u>2,534,503</u>
Investments in affiliates	50,317	46,493	COMMITMENTS AND CONTINGENCIES (Notes 9 and 14)		
Goodwill	208,183	208,183	RESERVES:		
			Unallocated	1,247,293	1,082,113
			Accumulated other comprehensive income— net of income taxes	<u>37,546</u>	<u>484</u>
			Total reserves	<u>1,284,839</u>	<u>1,082,597</u>
<b>TOTAL ASSETS</b>	<b><u>\$ 3,634,199</u></b>	<b><u>\$ 3,617,100</u></b>	<b>TOTAL LIABILITIES AND RESERVES</b>	<b><u>\$ 3,634,199</u></b>	<b><u>\$ 3,617,100</u></b>

See notes to consolidated financial statements.

# INDEPENDENCE BLUE CROSS AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME YEARS ENDED DECEMBER 31, 2004, 2003, AND 2002 (Dollars in thousands)

	2004	2003	2002
UNDERWRITING INCOME	<u>\$9,736,304</u>	<u>\$9,226,907</u>	<u>\$8,515,023</u>
UNDERWRITING COSTS:			
Claims incurred	8,655,543	8,077,661	7,453,585
Medical management	188,258	208,572	196,135
Operating expenses	<u>687,557</u>	<u>698,294</u>	<u>691,577</u>
Total underwriting costs	<u>9,531,358</u>	<u>8,984,527</u>	<u>8,341,297</u>
Net underwriting income	204,946	242,380	173,726
Investment income—net	82,823	70,790	38,006
Equity in net income of affiliates	13,617	10,657	12,670
Other expenses—net	<u>(26,506)</u>	<u>(13,054)</u>	<u>(11,296)</u>
Income before income taxes	274,880	310,773	213,106
PROVISION FOR INCOME TAXES	<u>109,700</u>	<u>121,900</u>	<u>84,100</u>
Income before cumulative effect of a change in accounting principle	165,180	188,873	129,006
Cumulative effect of a change in accounting principle in 2002, net of taxes of \$5,800 (Note 1)	<u>-</u>	<u>-</u>	<u>(8,835)</u>
NET INCOME	165,180	188,873	120,171
OTHER COMPREHENSIVE INCOME— NET OF INCOME TAXES:			
Unrealized holding gain (loss) on investments arising during the period, net of reclassification adjustment, and the change in additional minimum pension obligation	<u>37,062</u>	<u>6,337</u>	<u>3,986</u>
COMPREHENSIVE INCOME	<u>\$ 202,242</u>	<u>\$ 195,210</u>	<u>\$ 124,157</u>

See notes to consolidated financial statements.

# INDEPENDENCE BLUE CROSS AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CHANGES IN RESERVES YEARS ENDED DECEMBER 31, 2004, 2003, AND 2002

(Dollars in thousands)

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	2004	2003	2002
BEGINNING BALANCE	\$ 1,082,597	\$ 887,387	\$ 763,230
Comprehensive income	<u>202,242</u>	<u>195,210</u>	<u>124,157</u>
ENDING BALANCE	<u>\$ 1,284,839</u>	<u>\$ 1,082,597</u>	<u>\$ 887,387</u>

See notes to consolidated financial statements.

# INDEPENDENCE BLUE CROSS AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2004, 2003, AND 2002

(Dollars in thousands)

	2004	2003	2002
<b>OPERATING ACTIVITIES:</b>			
Net income	\$ 165,180	\$ 188,873	\$ 120,171
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	22,665	24,678	29,830
Equity in net income of affiliates—net of dividends received	(4,354)	3,743	(12,670)
(Gain) loss on sale of investments	(17,809)	(26,041)	35,237
Deferred income taxes	(18,196)	(6,643)	(5,549)
Change in assets and liabilities:			
Premiums receivable	18,975	2,378	(92,574)
Other receivables	(45,119)	(21,209)	9,939
Prepaid expenses and other	(51,782)	(49,191)	(10,921)
Claims liabilities	(78,320)	140,926	180,429
Accounts payable and accrued expenses	(142,320)	104,483	53,536
Unearned income	40,769	51,665	91,493
Net cash (used in) provided by operating activities	<u>(110,311)</u>	<u>413,662</u>	<u>398,921</u>
<b>INVESTING ACTIVITIES:</b>			
Purchase of investments available for sale	(1,571,677)	(2,086,608)	(1,642,419)
Sale or maturity of investments available for sale	1,347,779	1,938,901	1,440,915
Purchase of other invested assets	-	(1,400)	-
Purchase of property and equipment	(69,299)	(83,095)	(94,829)
Proceeds from sale of property and equipment	<u>108,778</u>	<u>100,693</u>	<u>41,837</u>
Net cash used in investing activities	<u>(184,419)</u>	<u>(131,509)</u>	<u>(254,496)</u>
<b>FINANCING ACTIVITIES:</b>			
Repayment of notes receivable	-	-	21
Payment on long-term debt	<u>(5,272)</u>	<u>(64,465)</u>	<u>(12,090)</u>
Net cash used in financing activities	<u>(5,272)</u>	<u>(64,465)</u>	<u>(12,069)</u>
(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(300,002)	217,688	132,356
CASH AND CASH EQUIVALENTS—Beginning of year	<u>766,363</u>	<u>548,675</u>	<u>416,319</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 466,361</u>	<u>\$ 766,363</u>	<u>\$ 548,675</u>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>			
Cash paid during year for:			
Interest	<u>\$ 5,812</u>	<u>\$ 8,869</u>	<u>\$ 10,056</u>
Income taxes	<u>\$ 221,180</u>	<u>\$ 123,799</u>	<u>\$ 79,330</u>

See notes to consolidated financial statements.

# INDEPENDENCE BLUE CROSS AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2004, 2003, AND 2002

(Dollars in thousands, except per share data)

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### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Business**—Independence Blue Cross (the “Company” or “IBC”) is a nonprofit corporation in the Commonwealth of Pennsylvania and is subject to regulation by the Commonwealth of Pennsylvania Insurance Department (“PID”). Health benefits are provided under contracts with members through hospitals, skilled nursing facilities and other organizations. The Company contracts with providers of health care to provide health services to members and also performs administrative services such as billing, collection, and marketing for Highmark Blue Shield (“HBS”) and processes claims for other Blue Cross plans’ members and for programs such as the Federal Employee Health Benefits Program and the BlueCard Program. The Company and HBS jointly participate in lines of business to provide Major Medical and Comprehensive Major Medical benefits. The Company offers its Preferred Provider Organization and Point-of-Service programs in Pennsylvania through its wholly owned subsidiary, QCC Insurance Company (“QCC”). The Company provides health insurance coverage to New Jersey residents through AmeriHealth Insurance Company of New Jersey and to Delaware residents through QCC d/b/a AmeriHealth Insurance Company. Health insurance is provided by the Company for Puerto Rico residents through its 82.7% owned subsidiary, La Cruz Azul de Puerto Rico, Inc. (“La Cruz Azul”). The Company provides workers’ compensation claims management services and third-party administrative services through CompServices, Inc. and AmeriHealth Administrators, Inc., respectively. In addition, the Company provides HMO coverage through its wholly owned subsidiaries, AmeriHealth HMO, Inc. and Keystone Health Plan East (“KHPE”). The Company and HBS provide hospitalization and medical/surgical coverages through Inter-County Hospitalization Plan, Inc. and Inter-County Health Plan, Inc., which are jointly owned subsidiaries. Through its 93% owned subsidiary, NewSeasons Assisted Living Communities, Inc. (“NewSeasons”), the Company acquires, constructs, owns, and operates assisted living facilities.

**Service Marks**—The Blue Cross and Blue Shield Association (the “Association”) licenses Independence Blue Cross to offer certain products and services under the BLUE CROSS® brand name. Independence Blue Cross is an independent organization governed by its own Board of Directors and is solely responsible for its own debts and other obligations. Neither the Association nor any other organization using the BLUE CROSS® or BLUE SHIELD® brand name acts as a guarantor of Independence Blue Cross’ obligations, except as discussed in Note 14.

**Principles of Consolidation**—The accompanying consolidated financial statements include the accounts of the Company and all of its majority-owned subsidiaries, hereafter referred to as IBC, and IBC’s share of assets, liabilities, reserves and operating results of the lines of business it participates in with HBS. All significant intercompany transactions have been eliminated in consolidation.

**Cash and Cash Equivalents**—IBC considers cash and cash equivalents to be all highly liquid investments with original issue maturities of three months or less.

***Investments Available for Sale***—IBC has categorized its investment portfolio as “available for sale” (“AFS”) and has reported the portfolio at fair value with unrealized gains and losses, net of tax, as a separate component of reserves. Gross realized gains and losses are calculated based upon the specific cost of the investments sold. The fair value of IBC’s AFS investment portfolio is estimated based on quoted market prices for the same or similar issues.

***National Accounts***—In order to provide service to employers with employees located in more than one geographical area, IBC participates in numerous syndicated contracts, known as National Accounts, with other Blue Cross plans throughout the country. On an interim basis, income, claims and administrative costs incurred in servicing National Account members are recorded in the consolidated statements of income and comprehensive income and changes in reserves. Underwriting gains and losses are recorded at settlement, which normally occurs within nine months following the end of the annual contract period.

***Member Premiums and Unearned Income***—Member premiums are billed in advance of their respective coverage periods. Receivables and income from such premiums are recorded during the coverage period. The unearned portion of premiums for a coverage period is recorded in the consolidated balance sheet as unearned income and later reported as underwriting income when earned.

***Property and Equipment***—Property and equipment are recorded at cost, which includes expenditures for significant improvements. Maintenance, repairs and minor improvements are expensed as incurred. When property or equipment is retired or otherwise disposed of, cost and accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in the consolidated statement of income. Depreciation is computed on the straight-line method over the estimated useful lives of the assets (three to ten years for office furniture and equipment, twelve to forty years for building and improvements).

In accordance with Statement of Position 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*, certain software costs are capitalized for purchased software including costs incurred to develop new systems. Developmental costs are accumulated until the software is put into use, at which time amortization commences. Amortization is computed on a straight-line basis over the expected useful life of the software (three to five years).

***Claims Liabilities***—Claims liabilities include the estimated amounts to be paid for member benefits based on accumulated financial and statistical data. Processing expenses related to such claims are accrued currently based on an estimate of expenses necessary to process such claims. Claims liabilities are presented net of advances to providers.

***Merit Rating Refunds***—Merit rating refunds are the estimated premiums refundable to eligible retrospectively rated groups based on accumulated financial and statistical data.

***Risk-Sharing Arrangements***—IBC’s HMO operations have certain arrangements for their Commercial and Medicare lines of business with independent physician and managed care groups to share in any deficit or surplus generated against established target medical budgets in the hospital, referral, and pharmacy service categories. A liability or a receivable is recorded based upon each arrangement’s estimated experience.

**Retirement Benefits**—Pension expense related to IBC’s pension plans is recorded based on actuarially determined net periodic pension costs using a year-end measurement date. The actuarial cost method used is the projected unit credit method.

Health care and life insurance benefits are also provided for retirees. IBC recognizes, as a liability, the actuarial present value of postretirement benefits expected to be paid to employees. The related expense reflects benefits attributed to services rendered by eligible employees during the period and interest on the liability.

**Medical Management**—Medical management activities include provider network creation and maintenance, credentialing and recredentialing, precertification and concurrent review, discharge planning and case management, claim payment review, medical cost analysis, medical information management, and quality management. Costs of these activities are expensed as incurred.

**Expense Reimbursement**—Operating expenses are allocated to various lines of business in order to determine the expense reimbursement due from other Blue Cross plans and other health programs for which IBC processed claims. Expense reimbursement is also calculated for operating expenses incurred on behalf of HBS. The method by which IBC is reimbursed is either actual cost or a predetermined amount.

**Income Taxes**—The Company is subject to federal income taxes under provisions of Section 1012.b of the Tax Reform Act of 1986. Since the Company is a nonprofit corporation, it is exempt from Pennsylvania corporate taxes. All of the Company’s subsidiaries are subject to federal and state income or premium taxes.

The Company files a consolidated federal income tax return including all of its wholly owned subsidiaries. Deferred income taxes are recognized for the expected tax consequences of temporary differences between the tax bases of assets and liabilities and their reported amounts.

**Comprehensive Income**—Total comprehensive income includes net income, unrealized gains (losses) on AFS investments arising during the period, net of reclassification adjustments, and the change in the additional minimum pension obligation.

**Goodwill**—IBC adopted Statement of Financial Accounting Standards (“SFAS”) No. 142, *Goodwill and Other Intangible Assets*, effective January 1, 2002. SFAS No. 142 addresses the initial recognition and measurement of intangible assets acquired outside of a business combination and the accounting for goodwill and other intangible assets subsequent to their acquisition. SFAS No. 142 provides that intangible assets with finite lives be amortized and that goodwill and intangible assets with indefinite lives will not be amortized, but will rather be tested at least annually for impairment.

In 2002, upon the adoption of SFAS No. 142, IBC recorded an impairment loss related to the goodwill recorded on its investments in NewSeasons and CorCell, Inc. in the amount of \$7,769 and \$1,066, net of tax, respectively. The impairment loss is presented on the consolidated statements of income and comprehensive income as a cumulative effect of a change in accounting principle. IBC concluded such impairment existed given the recent operating results of both NewSeasons and CorCell, Inc. In 2003, IBC recorded an impairment loss related to the goodwill recorded on its investment in NewSeasons in the amount of \$3,763. The impairment loss is presented on the consolidated statements of income and comprehensive income as a component of other expenses. IBC concluded such impairment existed given the recent operating results of NewSeasons. No such impairment was recorded in 2004. In 2004 and 2003, IBC used an income approach based on expected earnings to determine the fair value of each entity and to conclude on the impairment.

***Basis of Presentation***—The financial statements of the Company and certain subsidiaries are reported to their domiciliary State Insurance Departments on the basis of statutory accounting practices in a format established by the National Association of Insurance Commissioners (“NAIC”) and are presented herein in conformity with accounting principles generally accepted in the United States of America (“GAAP”).

The principal differences relate to certain assets and liabilities designated as nonadmitted (primarily capitalized software, office furniture, equipment, certain receivables, certain intangibles, certain accrued and prepaid expenses and certain deferred income taxes) that are excluded from the balance sheet and reserves for statutory reporting purposes. As a result of these differences, statutory reserves at December 31, 2004 and 2003 were \$1,038,534 and \$840,917, respectively. Statutory net income for 2004, 2003, and 2002 was \$22,282, \$53,189 and \$16,769, respectively.

***Fair Value of Financial Instruments***—In accordance with SFAS No. 107, *Disclosure about Fair Value of Financial Instruments*, IBC has calculated the fair values of its notes receivable and long-term debt at the discounted amount of future cash flows using IBC’s current incremental lending/borrowing rate for similar financial instruments. Such fair values approximate IBC’s carrying amounts. In addition, the carrying amount of cash and cash equivalents approximates its fair value due to the short-term nature of these financial instruments. See Note 3 for additional disclosures about the fair value of *Investments Available for Sale*.

***Use of Estimates***—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

***Reclassifications***—Certain prior-year amounts have been reclassified to conform to the current year’s presentation.

***Recent Accounting Pronouncements***—In November 2002, the FASB issued FASB Interpretation No. 45, *Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*. This Interpretation elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. This Interpretation also incorporates, without change, the guidance in FASB Interpretation No. 34, *Disclosure of Indirect Guarantees of Indebtedness of Others*, which was superseded. The initial recognition and initial measurement provisions of this Interpretation were applicable on a prospective basis to guarantees issued or modified after December 31, 2002, irrespective of the guarantor’s fiscal year-end. The disclosure requirements in this Interpretation were effective for financial statements of interim or annual periods ending after December 15, 2002. As of December 31, 2004 and 2003, IBC had a guarantee totaling \$0 and \$3,700, respectively, related to a debt agreement with DePaul, an affiliated entity. See Note 9 for disclosure of additional guarantees and commitments.

In January 2003, the FASB issued FASB Interpretation No. 46, *Consolidation of Variable Interest Entities*. The Interpretation clarifies the application of Accounting Research Bulletin No. 51, *Consolidated Financial Statements*, to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. In December 2003, FIN 46 was revised in FIN 46R. A nonpublic entity with an interest in an entity that is subject to this Interpretation and that is created after December 31, 2003, shall apply this Interpretation to that entity immediately. A nonpublic enterprise shall apply this Interpretation to all entities that are subject to this Interpretation by the beginning of the first annual period beginning after December 15, 2004. IBC is not a party to any variable interest entities covered by the Interpretation. In management's opinion, this Interpretation will have no impact on the Company's financial statements.

In July 2004, the Emerging Issues Task Force ("EITF") of the Financial Accounting Standards Board reached a consensus with respect to guidance to be used in determining whether an investment within the scope of EITF Issue No. 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*, is other than temporarily impaired. The guidance was to be applied in other than temporary impairment evaluations made in reporting periods beginning after June 15, 2004. In September 2004, the FASB issued, and the Company adopted, EITF Issue 03-1-1, which deferred the effective date of the impairment measurement and recognition provisions contained in EITF 03-1 until final guidance is adopted. The disclosure requirements of EITF 03-1 were previously adopted by the Company as of December 31, 2003 for investments accounted for under SFAS No. 115, *Accounting for Certain Investment in Debt and Equity Securities*. For all other investments within the scope of EITF 03-1, the disclosures are effective and have been adopted by the Company as of December 31, 2004. As this accounting guidance develops, the Company will continue to review it to assess any potential impact to the Company's portfolio and asset management policy. The Company has included the required disclosures in the Notes to Consolidated Financial Statements (see Note 3).

In December 2003, the FASB revised SFAS No. 132 *Employers' Disclosures about Pensions and Other Postretirement Benefits*. This revision is intended to improve financial statement disclosures for defined benefit plans. The standard requires that companies give more details about their plan assets, benefit obligations, cash flows, benefit costs and other relevant information. This standard is effective for fiscal years ending on or after June 15, 2004. The Company has included the additional disclosures in the Notes to Consolidated Financial Statements (see Note 4).

## **2. AGENCY CONTRACTS**

Claims processed for others and excluded from the consolidated financial statements amounted to \$397,887 in 2004, \$284,308 in 2003 and \$236,504 in 2002. Reimbursements for the administrative cost of services performed for HBS, governmental agencies, and other plans in the amount of \$34,564 in 2004, \$31,291 in 2003 and \$34,289 in 2002, respectively, have been offset against operating expenses.

### 3. INVESTMENTS

The cost or amortized cost and estimated fair value of investments at December 31, 2004 and 2003, are as follows:

	Available for Sale December 31, 2004			
	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. Treasury notes and federal agencies	\$ 180,065	\$ 544	\$ 973	\$ 179,636
Mortgage-backed securities	115,618	2,263	1,007	116,874
Asset-backed securities	129,740	1,936	1,289	130,387
Corporate debt securities	765,768	25,686	4,307	787,147
Other	<u>102,660</u>	<u>1,385</u>	<u>67</u>	<u>103,978</u>
Total debt securities	<u>1,293,851</u>	<u>31,814</u>	<u>7,643</u>	<u>1,318,022</u>
Common stock	358,043	60,937	9,946	409,034
Preferred stock	<u>181,067</u>	<u>5,858</u>	<u>1,818</u>	<u>185,107</u>
Total equity securities	<u>539,110</u>	<u>66,795</u>	<u>11,764</u>	<u>594,141</u>
Total investments	<u>\$ 1,832,961</u>	<u>\$ 98,609</u>	<u>\$ 19,407</u>	<u>\$ 1,912,163</u>

	Available for Sale December 31, 2003			
	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. Treasury notes and federal agencies	\$ 276,768	\$ 1,396	\$ 613	\$ 277,551
Mortgage-backed securities	167,911	3,466	990	170,387
Asset-backed securities	98,936	1,191	888	99,239
Corporate debt securities	652,132	33,463	1,354	684,241
Other	<u>89,246</u>	<u>1,890</u>	<u>285</u>	<u>90,851</u>
Total debt securities	<u>1,284,993</u>	<u>41,406</u>	<u>4,130</u>	<u>1,322,269</u>
Common stock	164,839	20,973	8,474	177,338
Preferred stock	<u>114,080</u>	<u>5,096</u>	<u>418</u>	<u>118,758</u>
Total equity securities	<u>278,919</u>	<u>26,069</u>	<u>8,892</u>	<u>296,096</u>
Total investments	<u>\$ 1,563,912</u>	<u>\$ 67,475</u>	<u>\$ 13,022</u>	<u>\$ 1,618,365</u>

The amortized cost and estimated fair value of debt securities by maturity date at December 31, 2004 are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	<b>Amortized Cost</b>	<b>Estimated Fair Value</b>
Due in one year or less	\$ 114,230	\$ 115,060
Due after one year through five years	252,987	257,088
Due after five years through ten years	536,092	550,537
Due after ten years	<u>145,184</u>	<u>148,076</u>
	1,048,493	1,070,761
Mortgage-backed securities	115,618	116,874
Asset-backed securities	<u>129,740</u>	<u>130,387</u>
Total debt securities	<u>\$1,293,851</u>	<u>\$1,318,022</u>

Gross realized gains and losses from sales of investments recorded in *Investment income – net* were as follows:

	<b>2004</b>	<b>2003</b>	<b>2002</b>
Realized gains	\$ 46,575	\$ 48,797	\$ 25,333
Realized losses	<u>(28,766)</u>	<u>(22,756)</u>	<u>(60,570)</u>
Net realized gains (losses)	<u>\$ 17,809</u>	<u>\$ 26,041</u>	<u>\$ (35,237)</u>

The net change in the unrealized appreciation (depreciation) on investments classified as AFS included as a component of other comprehensive income was \$24,749, \$38,634, and \$31,316 for the years ended December 31, 2004, 2003, and 2002, respectively. In addition, the Company's share of the unrealized gains (losses) included in the equity of its investment in affiliates accounted for under the equity method is included as a component of IBC's other comprehensive income.

In order to comply with statutory requirements, the Company has placed on deposit with various State Insurance Departments investments with an estimated fair value of \$66,396 and \$65,646 at December 31, 2004 and 2003, respectively. Deposits are included in *Investments available for sale* on the consolidated balance sheets.

The following table summarized the gross unrealized losses and fair value of fixed income and equity securities by the length of time that individual securities have been in a continuous unrealized loss position at December 31, 2004 and 2003:

	2004						Total Unrealized Losses
	Less than 12 months			12 months or more			
	Number of Issues	Estimated Fair Value	Unrealized Losses	Number of Issues	Estimated Fair Value	Unrealized Losses	
U.S. Treasury notes and federal agencies	97	\$ 141,542	\$ 711	18	\$ 10,736	\$ 262	\$ 973
Mortgage-backed securities	86	29,981	288	53	32,173	719	1,007
Asset-backed securities	84	44,812	492	22	19,435	797	1,289
Corporate debt securities	783	218,819	3,775	84	30,457	532	4,307
Other	<u>19</u>	<u>17,434</u>	<u>55</u>	<u>1</u>	<u>3,833</u>	<u>12</u>	<u>67</u>
Total debt securities	<u>1,069</u>	<u>452,588</u>	<u>5,321</u>	<u>178</u>	<u>96,634</u>	<u>2,322</u>	<u>7,643</u>
Common stock	604	55,508	6,981	140	6,728	2,965	9,946
Preferred stock	<u>132</u>	<u>41,169</u>	<u>1,326</u>	<u>11</u>	<u>10,692</u>	<u>492</u>	<u>1,818</u>
Total equity securities	<u>736</u>	<u>96,677</u>	<u>8,307</u>	<u>151</u>	<u>17,420</u>	<u>3,457</u>	<u>11,764</u>
Total investments	<u>1,805</u>	<u>\$ 549,265</u>	<u>\$ 13,628</u>	<u>329</u>	<u>\$ 114,054</u>	<u>\$ 5,779</u>	<u>\$ 19,407</u>

	2003						Total Unrealized Losses
	Less than 12 months			12 months or more			
	Number of Issues	Estimated Fair Value	Unrealized Losses	Number of Issues	Estimated Fair Value	Unrealized Losses	
U.S. Treasury notes and federal agencies	52	\$ 45,998	\$ 517	2	\$ 2,960	\$ 96	\$ 613
Mortgage-backed securities	103	73,391	936	8	1,517	54	990
Asset-backed securities	83	37,276	436	4	9,409	452	888
Corporate debt securities	300	77,284	963	57	8,424	391	1,354
Other	<u>5</u>	<u>25,131</u>	<u>285</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>285</u>
Total debt securities	<u>543</u>	<u>259,080</u>	<u>3,137</u>	<u>71</u>	<u>22,310</u>	<u>993</u>	<u>4,130</u>
Common stock	324	15,305	1,494	372	12,389	6,980	8,474
Preferred stock	<u>26</u>	<u>19,163</u>	<u>415</u>	<u>1</u>	<u>221</u>	<u>3</u>	<u>418</u>
Total equity securities	<u>350</u>	<u>34,468</u>	<u>1,909</u>	<u>373</u>	<u>12,610</u>	<u>6,983</u>	<u>8,892</u>
Total investments	<u>893</u>	<u>\$ 293,548</u>	<u>\$ 5,046</u>	<u>444</u>	<u>\$ 34,920</u>	<u>\$ 7,976</u>	<u>\$ 13,022</u>

The assessment of other than temporary impairments is performed on a case-by-case basis. Factors considered in determining whether an other than temporary impairment exists include: the financial condition, business prospects and creditworthiness of the issuer, the length of time and extent to which fair value has been less than cost for equity securities or amortized cost for fixed income securities, and the Company's intent and ability to hold such investments until the fair value recovers.

The Company recognizes other than temporary impairments on debt and equity securities when, in management's judgment, the decline in value is not temporary or when the Company has made a decision

to sell the security at an amount below its carrying value. When an other than temporary impairment is recognized, the security is written down to fair value as the new cost basis, and the amount of the write-down is recorded as a realized loss. The Company recognized \$3,211 and \$4,035, respectively, of other than temporary impairments on common stock during the years ended December 31, 2004 and 2003. No impairments were recorded on debt or preferred stock securities during the year ended December 31, 2004 or December 31, 2003.

#### **4. PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS**

IBC has a noncontributory defined benefit pension plan for the benefit of all its employees hired prior to January 1, 2000. For those employees hired on or after January 1, 2000, benefits are calculated on a cash balance formula. IBC's funding policy is to contribute annually the maximum amount that can be deducted for federal income tax purposes. Contributions are intended to provide for benefits attributed to service to date and for those expected to be earned in the future.

In addition to providing pension benefits, the Company provides certain health care and life insurance benefits for retirees. Under the current program, substantially all of IBC's employees may become eligible for these benefits if they are working for IBC when they reach age 55 and they have completed at least 10 years of service. Therefore, IBC begins accruing an obligation for active participants at the later of age 45 or date of hire.

A summary of assets, obligations and assumptions of the pension and health/life benefit plans are as follows at December 31, 2004 and 2003:

	Pension Benefits		Health/Life Benefits	
	2004	2003	2004	2003
Change in benefit obligation:				
Benefit obligation at beginning of year	\$ 350,243	\$ 242,259	\$ 50,012	\$ 38,715
Service cost	23,535	20,528	4,973	4,399
Interest cost	23,358	19,870	3,465	3,086
Actuarial loss	26,016	71,790	5,382	7,409
Benefits paid	(9,752)	(5,748)	(2,489)	(2,857)
Amendments	-	1,544	-	(740)
Benefit obligation at end of year	\$ 413,400	\$ 350,243	\$ 61,343	\$ 50,012
Change in plan assets:				
Fair value of plan assets at beginning of year	\$ 232,507	\$ 150,039	\$ 8,639	\$ 8,165
Actual return on plan assets	31,966	34,831	444	474
Employer contribution	67,470	53,385	2,489	2,857
Benefits paid	(9,752)	(5,748)	(2,489)	(2,857)
Fair value of plan assets at end of year	\$ 322,191	\$ 232,507	\$ 9,083	\$ 8,639
Funded status:				
Funded status	\$ (91,209)	\$(117,736)	\$(52,260)	\$(41,373)
Unrecognized net loss	149,227	135,062	15,060	9,897
Unamortized prior-service cost (benefit)	3,107	3,442	(515)	(628)
Prepaid asset (benefit obligation) for nonvested employees	\$ 61,125	\$ 20,768	\$ (37,715)	\$ (32,104)
Components of net periodic benefit cost:				
Service cost	\$ 23,535	\$ 20,528	\$ 4,973	\$ 4,399
Interest cost	23,358	19,870	3,465	3,086
Expected return on plan assets	(27,783)	(17,215)	(717)	(714)
Amortization of unrecognized:				
Prior-service cost (benefit)	335	335	(113)	(295)
Actuarial loss	7,667	6,926	492	100
Special termination benefit charge	-	212	-	-
Net periodic benefit cost	\$ 27,112	\$ 30,656	\$ 8,100	\$ 6,576

## Additional Information

	<u>Pension Benefits</u>		<u>Health/Life Benefits</u>	
	2004	2003	2004	2003
(Decrease) increase in minimum liability included in other comprehensive income, net of income tax	\$ (23,879)	\$ 16,978	N/A	N/A

The assumptions used in determining the actuarial present value of the projected benefit obligations were as follows:

<b>Weighted-average assumptions as of December 31</b>	<u>Pension Benefits</u>		<u>Health/Life Benefits</u>	
	2004	2003	2004	2003
Discount rate	6.0 %	6.5 %	6.0 %	6.5 %
Rate of compensation increase	4.0	4.0	4.0	4.0
Expected long-term rate of return on plan assets	9.5	10.0	9.5	10.0

The expected rate of return on plan assets was estimated utilizing a variety of factors including the historical investment return achieved over a long-term period, the targeted allocation of plan assets and expectation concerning future returns in the marketplace for both equity and debt securities.

In addition to providing pension benefits, the Company provides certain health care and life insurance benefits for retirees. The related trend rate information is as follows:

<b>Assumed health care cost trend rates at December 31</b>	<b>2004</b>	<b>2003</b>
Health care cost trend rate assumed for next year	10.0 %	9.0 %
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	5.0	5.0
Year that the rate reaches the ultimate trend rate	2010	2009

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would not significantly change results.

IBC's pension plan weighted-average asset allocations at December 31, 2004 and 2003, by asset category are as follows:

<b>Asset Category</b>	<b>Plan Assets at December 31</b>	
	<b>2004</b>	<b>2003</b>
	Equity securities	61 %
Debt securities	25	27
Money market	7	8
Other	<u>7</u>	<u>5</u>
Total	<u>100 %</u>	<u>100 %</u>

The investment strategy of the Company's funded defined benefits plans is to achieve consistent positive returns, after adjusting for inflation, and to maximize long-term total return within prudent levels of risk through a combination of income and capital appreciation. Risk to capital is minimized through the diversification of investments across and within various asset categories.

IBC's health/life benefit plan weighted-average asset allocations at December 31, 2004 and 2003, by asset category are as follows:

<b>Asset Category</b>	<b>Plan Assets at December 31</b>	
	<b>2004</b>	<b>2003</b>
	Debt securities	<u>100 %</u>
Total	<u>100 %</u>	<u>100 %</u>

**Contributions**—In 2005, the Company expects to contribute at least \$16,700 and \$5,900 to its pension plans and postretirement benefit plan, respectively. Expected future benefit payments are as follows:

<b>Year</b>	<b>Pension Benefits</b>	<b>Health/Life Benefits</b>
2005	\$ 29,077	\$ 2,976
2006	10,518	3,424
2007	13,863	4,077
2008	16,637	4,999
2009	20,642	6,017
2010-2014	151,537	49,684

The Company sponsors a qualified 401(k) Savings Plan available to all full-time employees of the Company and its subsidiaries and affiliates. The Company contributes an amount equal to 50% of the first 6% of salary deferral contributed by the employee, except for those employees at the Florida Operations Center. The Florida Operations Center employees, who are not covered under IBC's defined

benefit plan, receive a company matching contribution equal to 100% of the first 5% of salary deferral contributed by the employee. The Company's contribution for the plan was \$7,659 and \$7,780 for 2004 and 2003, respectively. The fair value of plan assets was \$268,393 and \$225,276 at December 31, 2004 and 2003, respectively.

## 5. COMPREHENSIVE INCOME

The components of IBC's other comprehensive income as of December 31, 2004, 2003, and 2002, are as follows:

	<b>2004</b>		
	<b>Before-Tax</b>	<b>Tax Expense</b>	<b>Net</b>
Change in additional minimum pension obligation	\$ 36,347	\$ (12,468)	\$ 23,879
Unrealized holding gains arising during the period	36,720	(12,852)	23,868
Less: reclassification adjustment for gains realized in net income	<u>17,809</u>	<u>(7,124)</u>	<u>10,685</u>
Other comprehensive income	<u>\$ 55,258</u>	<u>\$ (18,196)</u>	<u>\$ 37,062</u>
	<b>2003</b>		
	<b>Before-Tax</b>	<b>Tax Benefit (Expense)</b>	<b>Net</b>
Change in additional minimum pension obligation	\$ (26,120)	\$ 9,142	\$ (16,978)
Unrealized holding gains arising during the period	65,141	(26,298)	38,843
Less: reclassification adjustment for gains realized in net income	<u>26,041</u>	<u>(10,513)</u>	<u>15,528</u>
Other comprehensive income	<u>\$ 12,980</u>	<u>\$ (6,643)</u>	<u>\$ 6,337</u>
	<b>2002</b>		
	<b>Before-Tax</b>	<b>Tax Benefit</b>	<b>Net</b>
Change in additional minimum pension obligation	\$ (21,391)	\$ 7,487	\$ (13,904)
Unrealized holding losses arising during the period	(4,311)	1,817	(2,494)
Less: reclassification adjustment for losses realized in net income	<u>(35,237)</u>	<u>14,853</u>	<u>(20,384)</u>
Other comprehensive income	<u>\$ 9,535</u>	<u>\$ (5,549)</u>	<u>\$ 3,986</u>

## 6. INCOME TAXES

The components of the provision for income taxes are as follows:

	Years Ended December 31,		
	2004	2003	2002
Federal:			
Current	\$ 76,800	\$ 126,000	\$ 83,700
Deferred	9,100	(36,500)	(18,700)
State and local	<u>23,800</u>	<u>32,400</u>	<u>13,300</u>
	<u>\$ 109,700</u>	<u>\$ 121,900</u>	<u>\$ 78,300</u>

IBC paid \$187,165, \$104,600, and \$65,100 in federal income taxes in 2004, 2003, and 2002, respectively. The Company paid \$34,015, \$19,199, and \$14,230 in state and local income taxes in 2004, 2003, and 2002, respectively.

The net deferred taxes as of December 31, 2004 and 2003, included in other assets on the consolidated balance sheets, include the following amounts of deferred tax assets and liabilities:

	2004	2003
Deferred tax asset	\$ 143,400	\$ 131,800
Deferred tax asset—additional minimum pension obligation	4,200	16,600
Valuation allowance for deferred tax asset	<u>(6,600)</u>	<u>(4,800)</u>
	<u>141,000</u>	<u>143,600</u>
Deferred tax liability	(61,300)	(42,400)
Deferred tax liability—investments available for sale	<u>(28,400)</u>	<u>(20,700)</u>
	<u>(89,700)</u>	<u>(63,100)</u>
Net deferred tax asset	<u>\$ 51,300</u>	<u>\$ 80,500</u>

The deferred tax asset results primarily from nondeductible accruals for postretirement employee benefits, the discounting of claims liabilities and unearned income required for tax purposes, and an allowance for doubtful accounts that is not deductible for tax purposes until losses are identified, quantified and written off. The deferred tax liability results from the use of accelerated methods of depreciation for tax purposes and the required accounting for pension funding. The effective tax rates differed from the statutory tax rate of 35% primarily due to state and local income taxes.

In connection with the ownership increase in NewSeasons in 2001, IBC acquired \$13,500 of net operating loss carryforwards. As of December 31, 2004, the net operating loss carryforward will begin expiring in 2011. The net operating loss carryforward may only be utilized by NewSeasons.

SFAS No. 109, *Accounting for Income Taxes*, requires deferred tax assets to be reduced by a valuation allowance if it is more likely than not some portions or all of the deferred tax assets will not be realized. As of December 31, 2004 and 2003, IBC has recorded valuation allowances of \$6,600 and \$4,800, respectively. The amounts as of December 31, 2004 and 2003 relate to subsidiary net operating loss ("NOL") carryforwards which can only be utilized against that subsidiary's taxable income. The

valuation allowance increase in 2004 of \$1,800 is due to reinstating the full valuation allowance on the deferred tax asset of the net operating loss for NewSeasons.

## 7. PROPERTY AND EQUIPMENT—NET

Property and equipment at December 31, 2004 and 2003, is as follows:

	<b>2004</b>	<b>2003</b>
Land	\$ 2,532	\$ 3,091
Building and improvements	30,286	37,603
Office furniture and equipment	35,646	30,117
Capitalized software	<u>45,334</u>	<u>98,784</u>
Property and equipment—gross	113,798	169,595
Accumulated depreciation and amortization	<u>(32,586)</u>	<u>(29,936)</u>
Property and equipment—net	<u>\$ 81,212</u>	<u>\$ 139,659</u>

Depreciation and amortization expense related to property and equipment was \$18,914, \$15,998, and \$10,180 for the years ended December 31, 2004, 2003, and 2002, respectively.

## 8. INDEBTEDNESS

Indebtedness outstanding at December 31, 2004 and 2003 is as follows:

	<b>2004</b>	<b>2003</b>
Mortgage and construction loans and notes payable	\$ 24,704	\$ 29,962
Subordinated capital note	40,000	40,000
Capital lease obligation	<u>196</u>	<u>210</u>
	<u>\$ 64,900</u>	<u>\$ 70,172</u>

In June 1999, the Company, through its wholly owned subsidiary, KHPE, entered into a \$40,000 subordinated capital note agreement with a third party. Under the terms of the note, interest accrues at 9.6% per annum and is paid quarterly. The principal balance is payable on June 30, 2014.

The Company, through one of its subsidiaries, owns buildings pledged as collateral for related mortgage loans. The fair value of the buildings pledged as collateral approximates the amount of outstanding debt as of December 31, 2004 and 2003.

Industrial Revenue Bonds were issued to finance the purchase of the land and building of the Company's Puerto Rico affiliate, La Cruz Azul, and were secured by the land and building of the affiliate. On June 27, 2003, the affiliate sold the land and building and paid off all outstanding principal and interest related to these bonds.

Maturities of mortgage loans, bonds, notes payable, and capital lease obligations for each of the next five years and thereafter are as follows:

<b>Year</b>	<b>Amount</b>
2005	\$ 645
2006	640
2007	663
2008	15,729
2009	7,223
Thereafter	<u>40,000</u>
<b>Total</b>	<b><u>\$ 64,900</u></b>

Interest paid amounted to \$5,812 in 2004, \$8,869 in 2003, and \$10,056 in 2002.

IBC has an available line of credit with an area bank in the amount of \$10,000, which expires on June 30, 2005. Borrowings under the line of credit bear interest at LIBOR plus 60 basis points, and are payable upon demand. As of December 31, 2004 and 2003, no amounts were outstanding under this agreement.

IBC has established Reverse Repurchase Agreements with a financial institution with the amount not to exceed \$52,579 and \$49,727, which represent two percent of the statutory admitted assets of IBC and KHPE as of December 31, 2004 and 2003, respectively. Borrowings under these agreements bear interest at the prevailing repurchase rate. As of December 31, 2004 and 2003, no amounts were outstanding under these agreements.

## 9. COMMITMENTS

IBC leases certain facilities and equipment under long-term leases. As of December 31, 2004, future minimum rental payments required under operating leases that have initial or remaining noncancelable lease terms in excess of one year are as follows:

<b>Years Ended December 31</b>	<b>Facilities</b>	<b>Equipment</b>	<b>Total</b>
2005	\$ 35,123	\$ 47,044	\$ 82,167
2006	34,232	30,038	64,270
2007	34,096	23,038	57,134
2008	32,070	2,289	34,359
2009	30,429	2,212	32,641
Thereafter	<u>292,036</u>	<u>2,523</u>	<u>294,559</u>
<b>Total</b>	<b><u>\$ 457,986</u></b>	<b><u>\$ 107,144</u></b>	<b><u>\$ 565,130</u></b>

Total rental expense amounted to \$81,070, \$73,552, and \$71,773 for 2004, 2003, and 2002, respectively.

During 2003, IBC's subsidiary, NewSeasons, entered into agreements for the sale and leaseback of several of its buildings to a Maryland real estate investment trust (the "Trust"). The net proceeds from the sale were \$69,832. Deferred gains of \$8,527 are being amortized over 160 months, the life of the respective leases. NewSeasons provided a Guaranty on lease payments for certain properties leased from the Trust. Under the terms of the Guaranty, IBC will guarantee the rental payments and monetary

obligations of NewSeasons over the term of the lease up to a maximum of 16 years. As of December 31, 2004, no payments have been made by IBC in connection with this agreement.

During 2003, IBC's subsidiary, La Cruz Azul, entered into an agreement for the sale and leaseback of its building. The net proceeds from the sale were \$15,018. Deferred gains of \$1,627 are being amortized over 24 months, the life of the lease. La Cruz Azul provided a Guaranty on lease payments for the leased property. Under the terms of the Guaranty, IBC will guarantee the rental payments and monetary obligations of La Cruz Azul over the term of the lease. As of December 31, 2004, no payments have been made by IBC in connection with this agreement.

During 2004 and 2003 IBC entered into agreements for the sale and leaseback of a portion of the Company's office furniture, capitalized software and equipment. The leases have terms of 30 through 60 months. These leases are accounted for as operating leases. The book value and associated depreciation of the office furniture, capitalized software and equipment have been removed from the accounts for those operating leases. The proceeds from the 2004 and 2003 sales of \$99,791 and \$15,843, respectively, approximated the net book values of the disposed items; therefore, no gain or loss was realized on these sales. Annual payments under the 2004 and 2003 leases are \$22,880 and \$7,219, respectively.

In June of 1998, IBC entered into a \$10,000 surplus note agreement with Blue Cross and Blue Shield of Vermont ("BCBS of VT"). Under the terms of the agreement, if BCBS VT draws on an IBC letter of credit, such amounts will become a principal advance under the surplus note agreement. As of December 31, 2004 and 2003, there have not been any advances under this surplus note agreement.

#### 10. MEDICAID JOINT VENTURES

The Company, through its wholly owned subsidiaries KHPE, Vista Health Plan, Inc., and AmeriHealth HMO, Inc., is a 50-50 partner in two joint ventures with Mercy Health Plan, Keystone Mercy Health Plan ("KMHP") and AmeriHealth Mercy Health Plan ("AMHP") (the "Medicaid Joint Ventures") (see Note 11). The Medicaid Joint Ventures provide medical services to certain persons eligible for participation in the Pennsylvania and South Carolina Medical Assistance Programs pursuant to agreements with the States' Departments of Welfare. Under the terms of the current Pennsylvania agreements, the capitation payments received by KHPE and AmeriHealth HMO, Inc. are remitted to the Medicaid Joint Ventures; and it is the responsibility of the Medicaid Joint Ventures, through their providers, to provide defined program benefits. The South Carolina payments are received directly by Select Health, a licensed HMO in the state. The consolidated statements of income and comprehensive income include the following activity related to the agreements:

	<u>Years Ended December 31,</u>		
	<u>2004</u>	<u>2003</u>	<u>2002</u>
Underwriting income	\$ 1,355,737	\$ 1,165,130	\$ 1,008,722
Claims incurred	<u>(1,355,737)</u>	<u>(1,165,130)</u>	<u>(1,008,722)</u>
Net income	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

The accompanying consolidated financial statements do not include any liabilities for outstanding claims under this program.

## 11. INVESTMENTS IN AFFILIATES

The Company is a 50-50 partner in KMHP and records their portion of equity in KMHP earnings in accordance with the equity method of accounting.

Summary financial data for KMHP is as follows:

	2004	2003	2002
Revenues	\$ 1,202,000	\$ 1,022,404	\$ 915,042
Net income	8,728	20,140	22,164
Total assets	244,428	214,138	212,788
Partners' equity	58,696	63,154	56,514

The Company is a 50-50 partner in AMHP and records their portion of equity in AMHP earnings in accordance with the equity method of accounting.

Summary financial data for AMHP is as follows:

	2004	2003	2002
Revenues	\$ 337,016	\$ 297,619	\$ 258,784
Net income	17,174	5,898	4,924
Total assets	84,164	58,739	58,494
Partners' equity	32,986	20,334	22,784

## 12. ACQUISITIONS AND DISPOSITIONS

On December 31, 2003, the Company, through a wholly owned subsidiary, sold AmeriHealth Health Plan, Inc., a health maintenance organization that provides services to New York residents. IBC recorded a gain of \$265 related to this sale.

On November 25, 1998, the Company, through a wholly owned subsidiary, purchased 51% of the common stock of La Cruz Azul for \$18,000. The excess of acquisition cost over the fair value of net assets acquired of \$8,718 was fully amortized as of December 31, 2001. On October 29, 2003, \$55,500 of La Cruz Azul capital notes owned by the Company were converted to 365,132 shares of La Cruz Azul common stock. The conversion increased the Company's common stock ownership to 82.7%.

### 13. UNPAID CLAIMS AND CLAIMS ADJUSTMENT EXPENSES LIABILITY

	2004	2003
Balance, January 1	\$ 1,537,597	\$ 1,396,671
Incurred related to:		
Current year	9,072,858	8,453,713
Prior years	<u>(417,315)</u>	<u>(376,052)</u>
Total incurred	<u>8,655,543</u>	<u>8,077,661</u>
Paid related to:		
Current year	(7,765,876)	(7,019,241)
Prior years	<u>(967,987)</u>	<u>(917,494)</u>
Total paid	<u>(8,733,863)</u>	<u>(7,936,735)</u>
Balance, December 31	<u>\$ 1,459,277</u>	<u>\$ 1,537,597</u>

The claims and claims adjustment expenses for prior years decreased by a total of \$417,315 in 2004 and \$376,052 in 2003, respectively, because of lower than anticipated claims costs and favorable utilization trends.

### 14. CONTINGENCIES

**Trust Fund**—During 2000, the Company established an Insolvency Protection Trust Fund (the “Trust”) to comply with the Blue Cross and Blue Shield membership standards, which require plans to take steps to ensure the payment of claims liabilities and the continuation of coverage. As of December 31, 2004 and 2003, the funded amount required for the Trust was \$7,952 and \$9,881, respectively, and the estimated fair value of investments on deposit was \$15,324 and \$14,402, respectively.

**Litigation**—In the course of ordinary business, IBC is involved in and is subject to claims, contractual disputes, and other uncertainties. In the opinion of management, after consultation with legal counsel, the ultimate disposition of these matters will not have a material adverse effect on IBC’s financial condition or results of operations.

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