Lehman Brothers Health Benefits Broker Call

SECTOR VIEW

Rating: 1 - POSITIVE

Joshua R. Raskin, CFA
1.212.526.2279
jraskin@lehman.com

Gregory K. Nersessian, CFA
1.212.526.5298
gnersess@lehman.com

Sarah James
1.212.526.2217
sajames@lehman.com

Review of November 2005 Call

On November 14, we hosted our quarterly conference call with two regional health insurance brokers, one in Texas and the other in New York.

- Competitive landscapes are remarkably similar in Texas (mostly Houston) and the tri-state area.
- While both brokers saw double-digit cost-trend increases for 2006, the particularities behind the trend varied significantly.
- When discussions turned toward carrier differentiation, the usual items such as price, network, service and of course, relations with brokers came up.
- Comparing technological platforms, both Fleder and Watt agreed that United was head and shoulders above the competition, although Aetna was catching up.
- Employers remain on the sideline for consumer-driven products, according to these two brokers.
- Self funding remains the preferred funding method in Houston, but continues to shrink in New York.
- The movement to insure the uninsured continues through cheaper product introductions.

Analyst Certification

I, Joshua R. Raskin, CFA, hereby certify (1) that the views expressed in this research Industry Report accurately reflect my personal views about any or all of the subject securities or issuers referred to in this Industry Report and (2) no part of my compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this Industry Report.

Lehman Brothers does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report.

Customers of Lehman Brothers in the United States can receive independent, third-party research on the company or companies covered in this report, at no cost to them, where such research is available. Customers can access this independent research at www.lehmanlive.com or can call 1-800-2LEHMAN to request a copy of this research.

Investors should consider this report as only a single factor in making their investment decision.

PLEASE SEE IMPORTANT DISCLOSURES BEGINNING ON PAGE 19

December 13, 2005

Table of Contents

Introduction 3
Broker Participants 3
Observations 4
Cautionary Statement 6
Health Benefits Broker Call Transcript 6
Valuation 18

Introduction

New York City and Texas markets.

On November 14, we hosted our quarterly conference call with two regional health insurance brokers. On the call, we were fortunate enough be joined by prominent brokers that service the New York City and Texas markets, two of the largest health insurance markets in the country where several of our covered companies have meaningful presences including Oxford, WellChoice, UnitedHealth, Humana, Aetna and others. Richard Fleder is the CEO of Thesco Benefits, LLC an employee benefits agency in New York City where he serves corporate clients ranging from below 50 employees to large group, multi-location accounts. James Watt is the president, CEO and a director of Employee Benefit Solutions, Inc. As we have done for the past few years, we touched on a number of key issues pertaining to the managed care industry as well as trends specific to the New York and Texas markets for some true color in the marketplace.

Broker Participants

Richard Fleder, Thesco Benefits, LLC

Richard Fleder has more than 25 years experience in the employee benefits industry and is the CEO of Thesco Benefits, LLC. After receiving his CLU designation in 1976, Richard helped found Comprehensive Benefits Service Company (CBSC) a third-party claims administrator. He was named president of CBSC in 1986 prior to the company's being sold to Employee Benefits Plans, Inc. (EBP), the largest third party administrator in the country. In 1992, Richard became president of the largest health plan of EBP. In 1996, EBP was sold to First Data Corporation after which Richard founded Thesco Benefits. Richard is a member of the advisory councils of Oxford Health Plans, Aetna, Health Net, and United Healthcare.

James D. Watt, Employee Benefit Solutions, Inc.

James D. Watt is the president, CEO and a director of EBS. Jim joined EBS at its founding in 1995 and has 19 years of experience in the design, communication, administration, and the funding of employee benefit plans. During his career, he has completed numerous strategy design projects and consulting on group health and welfare plans, self-funded and VEBA trust funded plans, various forms of managed care health plans, ERISA and regulatory compliance, post retirement and post employment benefits, employee communications and plan administration. Previously, Jim was a senior account executive of CIGNA Healthcare in sales and marketing in Los Angeles, California. In October 1993, he was instrumental in engineering the development of the first market based Health Insurance Purchasing Cooperative (HIPC). Jim is also the former director of the Employee Benefit Planning Association of Los Angeles.

Observations

In Houston, Texas, Mr. Watt noted that United is the dominant provider, attaining its position through acquisitions over the past ten years.

Mr. Watt is seeing CIGNA gain the most market share in Houston, followed by Aetna, and BCBS of Texas.

Competitive landscapes are remarkably similar in Texas (mostly Houston) and the tri-state area. In Houston, Texas, Mr. Watt noted that United is the dominant provider, attaining its position through acquisitions over the past ten years. Prior to this consolidation phase there were many small plans in the market, and the market leaders were Prudential/Aetna. Mr. Watt believes that the membership gains by United have pushed its operating system to its fullest capacity, and Mr. Watt has in fact noted certain cases of service and reporting issues that have led some clients to switch to other providers. Specifically, Mr. Watt is seeing CIGNA gain the most market share in Houston, followed by Aetna, and BCBS of Texas. Aside from service levels, Mr. Watt cites pricing as the main driver of market share change.

In the tri-state area Mr. Fleder noted that United (including Oxford) held the top market share, followed again by CIGNA, Aetna, Health Net and WellChoice.

In the tri-state area Mr. Fleder noted that United (including Oxford) held the top market share, followed again by CIGNA, Aetna, Health Net, and WellChoice. Mr. Felder notes that United/Oxford has approximately a 40% market share in the area, with that share likely higher in the "white collar" segment. The most notable shift in New York market share has been from Aetna (as a reminder the company has been expanding its national account presence following its 2003 turnaround). Turning to New Jersey, Mr. Felder notes Horizon BCBS has the largest market share, followed by United, Aetna, CIGNA, then Health Net. In Connecticut, Mr. Felder sees Anthem (now WellPoint) as having the top market share by a large margin, followed by Oxford/United, Health Net, and then ConnectiCare. As far as drivers of market share, Mr. Fleder reiterated the same drivers that he spoke about two years ago on a previous broker call. He noted broker relationships both with carriers and with employers. Unique to the New York market, Mr. Fleder notes that the networks of various carriers are very similar, mirroring the Oxford network, which had been viewed as the superior network in New York. In addition, Mr. Fleder cites the ease of price negotiation as the reason why rates across various carriers are virtually the same. With little pricing and network differentiation, the market relies on relationships and brand loyalty to drive the decision making process.

While both brokers saw double-digit cost-trend increases for 2006, the particularities behind the trend varied significantly. In the Texas region, Watt discussed an annual survey of 150-200 companies which showed healthcare cost increases of between 11% and 13% for 2005 and he expected to see the continuation of similar trends into 2006. With regard to cost shifting to employees in the form of buydowns, Watt implied that the Texas market was an exception in that the booming energy markets in Texas have led to benefit increases.

Fleder noted in New York a marked increase in pricing flexibility and that it was possible to negotiate the original insurance bid downwards significantly.

Turning to the New York market, Fleder noted cost trends in the 10% range, a decline of between 2% and 3% over the prior year. We note that this figure excludes pharmaceutical cost trends of 15% and dental costs increasing at 6%. During the contracting process, Fleder noted in New York a marked increase in pricing flexibility and that it was possible to negotiate the original insurance bid downwards significantly.

The service side seemed to be an after-thought for most as New York benefit designs tend to force large amounts of in network usage which makes claims payment smoother.

When discussions turned toward carrier differentiation, the usual items such as price, network, service and of course, relations with brokers came up. Watt noted that there were a number of important variables and that while pricing and relative discounts are important, networks play a key role as well. In contrast to Watt's comments, Fleder noted that relationships between the employer, the broker, and the carrier have been the most important factor in selecting carriers for that past 30 years in the large-group segment. In the New York market, many networks have significant overlap (with most carriers chasing the best in class Oxford network) and because pricing has become flexible, you can work toward any price. Lastly, the service side seemed to be an after-thought for most as New York benefit designs tend to force large amounts of in network usage which makes claims payment smoother. For the small-group market, however, Fleder noted that price differentiation was much more important.

Comparing technological platforms, both Fleder and Watt agreed that United was head and shoulders above the competition, although Aetna was catching up. Specifically, Fleder noted that the proof of strength in United's systems were the ease in integrating new acquisitions into the existing platform as well as providing easy access to claims for employers and simple billing processes for providers.

Employers remain on the sideline for consumer driven products, according to these two brokers. This comes as no surprise to us, as we have seen employers be slow adopters of any new initiative in healthcare. In the New York market, Mr. Fleder points to the large disparity between current rich benefits and an HSA style benefit as the main reason employers are unwilling to adopt the plan. Fleder suggested that the marketplace is one with such rich benefits that the switch to lower benefit plans (through cost shifting) would be less palatable. In the Houston market, Mr. Watt is seeing employer skepticism of the value of HSAs. One caveat we make is that these brokers tend to focus on less national large group accounts which we believe have been more willing to move to CDHP plans.

TPAs are unable to negotiate as deep of a discount as larger carrier, creating a market for TPAs to rent managed care network, Aetna is renting its network to local TPAs.

In New York, Mr. Fleder notes little interest from employers in the blue card product, as it is consistently priced over other available product, specifically, Aetna, United, and CIGNA.

Self -funding remains the preferred funding method in Houston, but continues to shrink in New York. In the Houston market self-funded accounts remain the preferred method of healthcare insurance. Mr. Watt notes that TPAs are maintaining market share. However, the TPAs are unable to negotiate as deep of a discount as larger carriers. This has created a market for TPAs to rent managed care networks. One case of this is Aetna, which has entered into what he termed "leaseback arrangements" with its network, where it has leased its network to TPAs, but required them to purchase stop loss insurance through Aetna in New York. Mr. Fleder has seen the self funded accounts shrinking over the past few years, giving way to risk contracts. With respect to the National offering from the BCBS association, Blue Card sales are not seeing much traction with employers. In New York, Mr. Fleder notes little interest from employers in the blue card product, as it is consistently priced over other available products. Specifically, Aetna, United, and CIGNA national products are priced below the Blue card offerings. In addition, Mr. Fleder notes again that the benefit design in New York is not consistent with the core BlueCard National offering. In Houston, Mr. Watt notes that with the exception of Halliburton, Mr. Watt has not seen the Bluecard network have a large appeal in the market.

The movement to insure the uninsured continues through cheaper product introductions. Both Mr. Watt and Mr. Fleder have seen Aetna increase its membership of previously uninsured members following its acquisition of SRC. United introduced lateral products after its Golden Rule acquisition that increased its coverage of the uninsured.

Cautionary Statement

As always, we acknowledge that extrapolating trends based on localized, anecdotal evidence can be a risky strategy. Nevertheless, we note that the evidence of slowing but still double-digit rate increases, disciplined underwriting, and continued cost shifting to the employee are consistent with what we have found to be the case in other areas of the country.

Health Benefits Broker Call Transcript

Joshua Raskin: Thank you and good morning and welcome to everyone. We really appreciate everyone dialing in early on a Monday and apologize for switching the time as well. We are excited again to host the next installment of our Lehman Brothers Benefits Brokers conference call series. We've been doing this for several years and try and check in about every quarter or so, with the local markets and trying to gauge market trends. I'm going to turn it over to Greg Nersessian who everyone knows from my team to introduce today's brokers and then I'll update everyone on the format.

Greg Nersessian: Thanks Josh and good morning everyone. We're very excited to be joined today by two top producing health insurance agents. Richard Fleder has more than 25 years experience in the employee benefit industry and is the CEO of Thesco Benefits. Thesco is the largest independent employee benefits broker in the Northeast and one of the ten largest employee benefit firms in the country. Richard is a member of the Advisories Councils of Oxford, Aetna, HealthNet and United Healthcare.

Jim Watt is the president and CEO and the director of Employee Benefit Solutions and has 19 years of experience in the design, communication, administration and funding of its employee benefit plans. Prior to joining EBS Jim, was a senior account executive at Cigna Healthcare in Los Angeles. Josh.

Joshua Raskin: Thanks Greg. The purpose of the call is to gauge what certain brokers are seeing in their local markets in terms of trends. We're going to touch on all of the topical areas; pricing, benefit design, the economy, technology, et cetera.

In terms of format I'll turn it over to Richard first, he'll give us a brief introduction and background. Some of you may remember Richard. He joined us about two years ago on this call and gave an introduction and overview of his market. I'll then turn it over to Jim to do the same in his market. And then we'll ask a couple of questions and of course leave time at the end to have the audience participate.

In all we'll try and wrap this up hopefully in about 40 minutes. So with that let me turn it over to Richard for a brief introduction.

Richard Fleder: Thanks Josh. Thesco Benefits is an employee benefits brokerage firm located in New York City. We have offices in Long Island and in New Jersey. We've been in business for ten years. Before that I was involved in running a company called EBP Health Plans out of Minneapolis which was a public corporation and very involved in the self-funded sector.

Joshua Raskin: That's a good intro Richard, we'll start with that. And Jim if you want to give a quick background—anything we didn't mention.

Jim Watt: Actually I think Greg covered it fairly well.

Joshua Raskin: Okay. And you've been in Texas for I think you said a little over ten years?

Jim Watt: Ten years now yes.

Joshua Raskin: Great. So, Jim why don't we start with you. Just generally speaking could you give us a sense of the market. Who are the biggest players in your market and maybe how has that competition changed over the last three to five years or so?

Jim Watt: There's been significant change in this market. With United Healthcare being the most dominant player and historically prior to that, Prudential and Aetna were the dominant players. But through acquisition United Healthcare has really remained on top.

Cigna Healthcare has been the recipient of some of that market loss from United Healthcare.

What's changed in the last year that has been interesting is their market share has begun to erode largely to Cigna Healthcare which has been the recipient of some of that market loss from United Healthcare. Aetna as well has seen significant growth in its operation. And to a lesser extent Blue Cross has also regained a footprint after many years of declining market share.

Joshua Raskin: Jim just while we're there you mentioned significant change and I think you said United's remained on top through acquisitions. I know obviously, you know, Prudential Aetna. Maybe you could give us a little history of some of the M&A that's gone on in your markets.

And also if you could just help us define where your Texas market; is that Dallas or is that Houston or the Austin area? Where exactly are you specifically talking about?

Jim Watt: We're headquartered here in Houston and the largest – our largest share of business comes from Houston and Texas but we also work across the country and internationally for their clients as well.

On the subject of market share and changes in market share what's interesting when I first came to this market is most of the smaller health plans had either been acquired or were being acquired as I entered the market for the first time. So the bigger, more dominant national footprint carriers had initially started with smaller acquisitions. And of course Prudential was the largest acquisition here that changed the whole dynamic for the market, certainly for Aetna.

And so it's been an interesting tug of war to watch the four largest players compete for market share with changes in pricing and plan design certainly in the insured market. And to a lesser extent packaging with networks and stop loss at the larger end of the self-funded market.

Joshua Raskin: Thank you. Richard why don't we move over – I have a feeling we're going to hear some similar comments but maybe you could give us an update on who the local competitors are there. And I have a feeling you'll have a few comments on the M&A landscape as well.

Richard Fleder: Sure. Things have not changed greatly in five years but they are different from the way they were. Five years ago Oxford certainly was the prime player especially with white collar type employers; Empire was the big player in the blue collar market. United, Aetna, Cigna and Healthnet followed behind those two carriers.

There has been tremendous growth though for Aetna; Aetna has really gotten a much stronger position than they had a few years ago.

Now with Oxford and United merged they probably represent about 40% of the marketplace and certainly from a white collar perspective even more than that. There has been tremendous growth though for Aetna; Aetna has really gotten a much stronger position than they had a few years ago.

Other carriers are GHI and HIP. They're now combined in addition to Vitra all being one entity. They're very much in the blue collar marketplace. They don't really compete with the Oxfords and the Aetnas and the Healthnets. That's really the way it is in New York.

HealthNet is losing some market share in New Jersey.

In New Jersey, Horizon is still the main player with Oxford United probably second along with Aetna, Cigna and Healthnet again, Healthnet losing some market share there. In Connecticut, Anthem is certainly the largest player followed by Oxford, Healthnet and ConnectiCare.

We're in a marketplace where self-funding continues to shrink.

We're in a marketplace where self-funding continues to shrink. Small group being a little different than large group but Oxford and Empire are certainly the largest players in New York even in the small group area.

Joshua Raskin: Thank you but I want to make sure I got everything you said right. It sounded like with the combination of Oxford and United you sort of see them at maybe 40% type of market share.

Richard Fleder: Right.

Joshua Raskin: Certainly higher in the white collar area as you define it. After that is it sort of the Empire or WellChoice Blues after that or?

Empire is certainly going after the Oxford United business and there still is a differential Aetna, Cigna and Healthnet behind them.

Richard Fleder: Certainly Empire would be right behind them although it's a slightly different market although Empire is certainly going after the Oxford United business and there still is a differential Aetna, Cigna and Healthnet behind them.

Joshua Raskin: And just curious on the Oxford United are you seeing an integration there or are they still sort of…

They've added the United providers to the Oxford base so it's really one network. But systems are still separate and they're not integrated at all.

Richard Fleder: Not yet. I mean, you know, Oxford has taken over all the United small group business. Management is basically Oxford management but the network themselves have become basically one network—they've added the United providers to the Oxford base so it's really one network. But systems are still separate and they're not integrated at all.

Joshua Raskin: So it sounds like they've integrated the networks and some of the product base, but maybe from branding and the processing standpoint they are not as integrated as they could be.

Richard Fleder: Well actually you can get two separate proposals and the proposals will vary from Oxford and United. They have different rating mechanisms.

Joshua Raskin: Interesting. And then you talked about HIP and GHI combining. You mentioned ConnectiCare which has also been acquired. Curious over the last couple of years we've seen some of these big mergers. How has that changed from a consumer standpoint or from the customer's standpoint? Would you argue there are fewer options or do you think that there's still plenty of competition in New York?

Aetna has gotten so much stronger that they've become quite a viable player.

Richard Fleder: Well there's still plenty of competition in New York certainly in the white collar arena. Aetna has gotten so much stronger that they've become quite a viable player. And Empire is going to be stronger than they were.

Cigna is very aggressive for business.

We think that the WellPoint acquisition is going to have positive ramifications for them. Cigna is very aggressive for business so there still are a decent number of alternatives in New York. Obviously the Oxford United merger doesn't help because they were two very viable carriers and now they're one.

The GHI HIP certainly will cut down a lot of choice, you know, in that now looking for that type of business is really Empire or the GHI HIP combination when it gets merged.

Joshua Raskin: Sure, makes sense. Switching gears a little bit Jim why don't we go back to the Houston or Texas area and I'm wondering if you could talk a little bit about premium rates and what your customers are seeing in terms of cost trend or on the self-

funded business or premium growth on the risk business as we move into 2006 and maybe how that compares to 2005.

Jim Watt: Sure. As part of the work that we do we perform an analysis for the Houston business group on health. When we look at health plans and pricing of cost profiles roughly 150 to 200 companies every year, year over year, and we've been conducting a survey for the last four years heading now into our fifth year. And we've seen a very consistent trend across that roughly a billion and a half of healthcare spending that low double-digit healthcare cost changes year over year have been fairly typical.

We had a spike in those costs about five years ago but it's been relatively consistent in the 11%, 12%, 13% range and our preliminary forecast for 2006 suggests that it's going to look like that again when we finalize the data.

Joshua Raskin: So would you suggest that if it was 11% to 13% in 2005 it sounds like 11% to 13% is probably a good number for 2006?

On the self-funded side of things we're doing monthly forecasts on a rolling 12 month basis and it's suggesting to us that we'll probably end up at 11% to 13% again.

Jim Watt: Yes. Our early evidence suggests that and we get a lot of that data obviously from the January 1 renewals that are being presented by the carriers on the insured side of things. And on the self-funded side we're doing monthly forecasts on a rolling 12 month basis and it's suggesting to us that we'll probably end up at 11% to 13% again.

Joshua Raskin: And then just while we're there Jim any change in benefit design or benefit buy downs as we call them from your consumer base? Do you see more or less or is there sort of a constant level there as well?

Jim Watt: Well that's what's been so interesting. Even though we have been seeing these kinds of cost increases year over year, in this market what we've seen is moderate reluctance to making significant plan design changes. Recognizing that the energy sector is booming right now we're likely to see little or no change and in some cases we'll see employers actually improve benefits to support holding onto their talent.

Joshua Raskin: So with regard to the energy sector, would you argue that the economy is actually probably doing better locally and that's actually leading to more generous benefits?

Jim Watt: Yes, it's roaring here. In fact, the constant theme with not only the E&P companies but also the service companies in the sector is not being able to acquire the talent that they need to support the growth that they're seeing in their businesses.

Joshua Raskin: Okay that's helpful. And then Richard in New York maybe you could talk a little bit about rates and increases versus the last couple of years and then also maybe on the benefit buy down side.

Richard Fleder: Sure. We certainly aren't seeing benefit improvements here but then again, you know, the New York area probably has the richest benefits anywhere in the country where other places in the country you're infrequently seeing 100% benefits we're still seeing an awful lot of 100% in network benefits here.

Medical trend certainly has slowed as we're seeing (excluding buy downs) numbers net of Rx of about 10%, Rx being at about 15% and dental being about 6%. We're seeing much more flexibility in rates than we've ever seen – not ever but we've seen in the last couple of years meaning that the rate is far different after we've negotiated renewals and looked at alternative carriers than the rate that's initially proposed by the insurance company. They're generally coming out with higher trend numbers and then coming down to with, you know, a more realistic trend number by the time we get through the process.

Benefit buy downs have slowed a little bit in a sense that because the trend has come down there's been a little less urgency. On the other hand, with all the discussion I'm sure we'll talk about it a lot toward consumer driven healthcare.

There has been some movement or at least discussion of eliminating some of the 100% benefits maybe as almost a preparation moving towards an HSA or an HRA.

Because the benefits are so rich there's such a large gap between the plan designs that employers have today and where the consumer driven plan designs are going to take them. There has been some movement or at least discussion of eliminating some of the 100% benefits maybe as almost a preparation moving towards an HSA or an HRA.

Joshua Raskin: Interesting. Just want to make sure I got that all right; you said the trend has sort of slowed to maybe 10%, Richard, Rx is still 15% and dental did you say 6%?

Richard Fleder: Right, the 10% is net of Rx just pure medical.

Joshua Raskin: Right, and how does that 10% compare to, you know, maybe what you were seeing as we entered 2005?

Richard Fleder: Oh, I'd say it's a good two to three points less than we were seeing a year ago.

Joshua Raskin: Okay that's helpful.

We'll stay with you Richard; you had mentioned some products – potential product changes. It sounds like and when we spoke two years ago I think you said that New York still had the richest benefits in the country. It doesn't sound like that's changed a lot.

You mentioned some of the HSA or HRA what we'll call generally consumer directed health plans. Any uptake in that? Are you starting to see interest there or are there any products that have gained any traction?

Richard Fleder: Well I mean certainly the movement to consumer driven is very slow. I mean even though the great majority of our clients are in the New York area our largest

clients are outside of New York. Actually Florida, Illinois, California, Minneapolis and the HSA claims that we have are the ones that are outside of this area. And as I kind of stated it was an easier movement for them because they were not providing 100% benefits before so the move to a consumer driven healthcare plan was easier for them.

Here, we'll start the discussion with a client and more often than not we won't get through the second or third sentence before they look at us and say no we're not ready for that yet.

Joshua Raskin: Yes.

Richard Fleder: So it's real slow here compared to what we're seeing other places in the country.

There are different things though happening in plan design. Certainly there's a great movement and has been a great movement toward open access point of service plans as opposed to PPOs. We keep reading about the movement from HMOs to PPOs. We certainly do not see it here.

A great majority of our clients have core buy up plans meaning they'll provide a low plan and a high plan. More often than not the lesser benefit will be an HMO based plan, either an HMO or a point of service either as a gatekeeper or open access. And then the buy up plan will be a PPO or an open access point of service plan.

Joshua Raskin: And Richard I don't want to put words in your mouth but it sounded like New York's got some very generous benefit packages and so the movement to consumerism is tougher. Is that to say that the market perception or your perception of consumer directed health plans is a low benefit product, it's a cut in benefits?

Richard Fleder: Well, it's certainly moving a lot of the responsibility to the employee. It's a cost shift to the employee and I don't see any other way of looking at it. It's packaged nicely and it's certainly a cost shift to the employee.

Joshua Raskin: Fair enough. And Jim maybe we could talk a little bit about new products or change in product design including consumerism in the Texas market.

Jim Watt: I would echo Richard's comments, Josh. We're seeing very, very slow adoption of a consumer based approach in this market. And you'll have to realize also this is a market that never really took to HMO's either.

So there's a healthy dose of skepticism in most of the buyer's minds around really the value of HSAs and certainly from what we've seen pricing wise from the carriers essentially we're looking at a decrement in costs only related to plan design. And when you scratch beneath the surface with the carriers too, they will tell you that they're not giving any credibility yet to consumers being better consumers inside of these plans either.

Joshua Raskin: Yes, that's helpful. I guess switching topics a little bit, Jim maybe we'll start with you. What attracts a broker, a sales agent in the market to a specific carrier? Is it just simply, this is where I can get the best price for my specific customer or is product important, brand name, costumer service. Just trying to figure out what attracts you to a specific carrier?

Jim Watt: Well I think really in different segments of the market Josh the buyers will value different things. Pricing certainly is important. In this market there's the prevalence of self-funded plans, employers essentially realize that it's their claims, it's their employees uses that's driving costs.

United Healthcare having some slippage in this market has more to do with the fact that they've grown so quickly they're having not only service issues but reporting challenges as well that are very, very important to a self-funded customer.

So what we're seeing is really plan selection or I should say carrier selection really driven by networks and relative discounts in those networks, access, and then to certainly around service capability. And my prior comments on United Healthcare having some slippage in this market has more to do with the fact that they've grown so quickly they're having not only service issues but reporting challenges as well that are very, very important to a self-funded customer.

Joshua Raskin: So in the larger group you'd argue that's where it's more impactful to them?

Jim Watt: Yes.

Joshua Raskin: Interesting. And any other points of differentiation among the carriers? Is anyone seen as the best service or worst service or is anyone seen as having typically the best price points or is it more – or the most broad product selection?

Certainly at the lower end of the market in the insured market here we see Humana as a viable player. They've got exceptional network coverage, their pricing tends to be more aggressive but then again that's at the lower end of the market.

Jim Watt: Again that varies by market. Certainly at the lower end of the market in the insured market here we see Humana as a viable player. They've got exceptional network coverage, their pricing tends to be more aggressive but then again that's at the lower end of the market.

Joshua Raskin: Yes. And then Richard in terms of what you're seeing from carriers sort of differentiation what draws you to place a specific customer with a carrier and how does that differ?

Richard Fleder: Well, this year is my 30th year of doing this and I don't think this has varied in the 30 years that I've done it. That relationships between the broker and the client but the broker and the insurance carrier still are the most important factor.

The networks have certainly been important but all the carriers have pretty much gravitated to the Oxford network and duplicated them so when we do disruption analysis reports for clients there's very little difference between the carriers. Price as I said, more now than before, it's fairly negotiable. You'll get movement so you'll get to the price that you want with any of the main carriers.

Service has become less of an issue in that since such a high percentage of the claims are in network claims anyway, there's very few claims that are going to create problems for the insurance companies.

Joshua Raskin: Okay.

Richard Fleder: So reputation and relationships are still the most important category. Now in small group that is a differentiation because price is far more important in small group than it is in large group. And the network, I mean probably the carrier with the strongest reputation certainly in New York more than Jersey and Connecticut is Oxford. I mean it has seemed to have the best network although I'd say the differentiation is becoming less and less.

Empire does have one huge advantage in that they're the only carrier that has the Sloan-Kettering, the local cancer hospital and the cancer hospital here in their network. And that has seemed to be a differentiator for Empire.

Joshua Raskin: Interesting, I thought actually United went out with Oxford and actually had Sloan-Kettering but…

Richard Fleder: They have an arrangement that basically and I won't get this exactly as precise as they would probably want me to but in situations where care cannot be provided in any other hospital and they feel that care has to be provided in Sloan they do have an arrangement and they will consider it an in network provider. But in general if there are other alternatives it will still be out of network which is a huge problem for the participants.

Joshua Raskin: While we're sort of on the topic of service and differentiation I'm wondering if you can talk a little bit about technology. Which carriers are seen as having sort of the best systems whether that means the ability for brokers to get quotes online or even for their customers to check benefit check claims or providers to check eligibility, et cetera. Who in your market, maybe we'll start with Richard, seems to lead from a technology standpoint?

Richard Fleder: Well United is still heads and tails above all the other carriers. Aetna is catching up but United has a tremendous capacity for consolidation. They've taken in other carriers and it's gone very smoothly and I think that that will be an issue with some of the other consolidations.

They're as far as just easy access for the participants to get into the system, for the employer to do billing and other things, United is still heads and tails above all the other carriers.

Joshua Raskin: Yes. And Jim in your market any comments on technology?

Jim Watt: I would echo Richard's comment, United probably the leader with Aetna certainly a close second.

Joshua Raskin: Okay, that's helpful. Just want to talk a little bit about the self-funded market. We still see plenty of accounts placed with TPAs and sort of less maybe managed care arrangements and wondering two questions I guess one, have the dynamics in the self-funded market changed, i.e., are you seeing more and more volume go to the larger national carriers or is the TPA still maintaining a decent share?

And second, any comments on the Blue Card program specifically? Obviously completely different markets Jim with the not-for-profit Blue Cross Blue Shield of Texas as part of a relatively big organization and obviously WellChoice for profit merging with WellPoint. Maybe we'll start with Jim.

Jim Watt: Well, it's the self-funded market here and really in all of Texas is the biggest market of all. We see TPAs maintaining share although we've seen also some interesting changes. For example, lease back arrangements and networks that Aetna has contracted to various TPAs tying – allowing network penetration that TPA is using Aetna's network but also requiring that Aetna stop loss be purchased at the same time.

The TPAs have typically not been able to negotiate as deep a discount in their networks so with Aetna relinquishing its network to for TPA use but also requiring the purchase of stop loss on it, it allows Aetna to penetrate a market in an entirely different way.

And I think that's a very, very interesting approach that Aetna is taking. The TPAs have typically not been able to negotiate as deep a discount in their networks so with Aetna relinquishing its network to for TPA use but also requiring the purchase of stop loss on it, it allows Aetna to penetrate a market in an entirely different way.

The Blue Card has not been a big hit here with a couple of exceptions, Halliburton, obviously has taken a national approach with a consortium. That's the most notable of their clients but they're not seeing significant growth in this market certainly.

Joshua Raskin: And Richard in terms of the TP – the self-funded market and the Blue Card?

Richard Fleder: Well, self-funding itself is certainly shrinking and has been shrinking in the last few years just the ability to get very aggressive fully insured rates plus the fact that the – I hate using the word discount but the discounts that are available through the carriers was always better.

And yes, now Aetna has been made available to some of the TPAs locally. Also the fact that Empire didn't do self-funding business under I think was 1,000 lives certainly took them out of the equation.

The TPA market itself has never been large here. In the 1980s I owned the largest TPA in the area and we were based out of Pennsylvania. There really was no large TPA in the New York area; it was never a big TPA environment.

As far as the Blue Card is concerned it's always been one of the mysteries to us, we've seen how the big consultants have used it, the Hewitt's etc, I believe in it very much so. It never really made sense for our largest clients.

As I talked about before almost all of our clients utilize this core buy up concept of a low plan and a high plan and the Blue Card itself never made sense for that in that if you're going to be multi-state you were going to have use a PPO product for the core benefit.

And a PPO product could never get to a price level where an HMO product could and therefore whether it was United or Cigna or an Aetna you were always going to be able to find a more competitive based product which would also make the pricing of the buy up more expensive for the participants. So we've never been high utilizers of the Blue Card.

Joshua Raskin: Interesting. Approaching sort of 35 minutes here so want to maybe ask one more question and then we'll turn it over to the audience to see if they have questions. We'll stick with Richard; anything from a legislative standpoint, on the horizon anything being talked about in the market that you think is either, an opportunity or a potential worrisome issue?

Richard Fleder: Nothing significant I mean obviously the whole Spitzer thing has certainly been a discussion point. I don't know that it's had a real effect on us. I mean we've always been about disclosing compensation anyway so it really hasn't had a huge effect but I think that the most discussion is about that.

The only thing that we see is if at some point Horizon is able to become a for-profit concern, and whether that leads to a merger with WellPoint but I don't think that's going to happen anytime in the near future. But that would probably be the most significant next event around here.

Joshua Raskin: Got you, so it's not likely though. And Jim maybe from your standpoint anything from a regulatory standpoint that jumps out?

Jim Watt: Echoing Richard's comments again, Elliot Spitzer has really been the dominant point of discussion certainly in all of our client meetings, it's had a very significant impact on both Aeon and Marsh in this market. They suffered as a result of his investigation and ultimately the settlement. But it's something that employers are very, very cognizant of here and it is discussion point number one in a new or prospect kind of meeting.

Joshua Raskin: Thanks. We're at the 35 minute mark so we'll turn it over to the audience and see if there's any Q&A. Operator do you want to see if anyone has a question?

Operator: At this time I would like to remind everyone if you'd like to ask a question please press star then the number one on your telephone keypad. We'll pause for just a moment to compile the Q&A roster.

Joshua Raskin: And maybe I'll just ask one more question, while we're waiting, I'll start with Richard. In terms of the individual and small group market we've seen new product introduced sort of nationally around and the opportunity in the uninsured or maybe even the underinsured. I was wondering are any of the carriers sort of targeting the lower end of the market there, trying to produce maybe products that are less expensive and more attractive to those that aren't currently buying insurance?

Richard Fleder: Well certainly Aetna and United are, Aetna with its acquisition of SRC certainly showed a tremendous commitment to that whole sector. United has created its own internal products and they're also very focused on buying the Golden Rule which is an individual product and then buying – creating these products for the discount cards so they also are very committed in that environment.

Joshua Raskin: Okay, anything Jim in Texas?

Jim Watt: I see nothing different than what Richard's already offered.

Joshua Raskin: Okay so Aetna still – those are the two that are there?

Jim Watt: Yes.

Joshua Raskin: Okay that's helpful. Operator, do we have any questions?

Operator: No, sir, we have no questions from the telephone.

Joshua Raskin: There's a transcript available and there will be a replay as well. I want to thank Richard and Jim again for their participation and great insights. If anyone's got any follow up definitely don't hesitate giving me a call here in the office, 212-526-2279 and with that any parting last minute words Richard or Jim?

Jim Watt: No.

Richard Fleder: Thank you Josh.

Jim Watt: Thanks for the opportunity.

Joshua Raskin: Okay, thank you.

Valuation

Figure 1: Valuation

Joshua Raskin, CFA **Jraskin@lehman.com**
(212) 526-2279

COMPARABLE ANALYSIS

		Price at	Market	EPS			P/E			EBITDA/Share			EV/EBITDA			Val. Methodology	
		12/9/2005	Cap. (Mil)	2004	2005E	2006E	2004	2005E	2006E	2004	2005E	2006E	2004	2005E	2006E	Target	2006 EPS Mult.
National Companies																	
Aetna	**AET**	$98.68	$29,675.54	$3.51	$4.60	$5.30	28.1x	21.4x	18.6x	$5.95	$7.76	$8.80	17.1x	13.2x	11.7x	$95.00	17.9x
1 Overweight	$ 95.00			35%	31%	15%				32%	31%	13%					
CIGNA	**CI**	$112.40	$14,763.29	$7.79	$7.75	$7.15	14.4x	14.5x	15.7x	$13.78	$13.43	$12.75	8.9x	9.1x	9.6x	$120.00	16.8x
2 Equal Weight	$ 120.00			37%	-1%	-8%				35%	-3%	-5%					
UnitedHealth	**UNH**	$63.67	$83,980.73	$1.97	$2.48	$2.75	32.4x	25.7x	23.1x	$3.42	$4.31	$4.94	19.5x	15.4x	13.5x	$63.00	22.9x
1 Overweight	$ 63.00			33%	26%	11%				31%	26%	15%					
WellPoint	**WLP**	$79.40	$49,355.04	$3.31	$3.99	$4.55	24.0x	19.9x	17.5x	$5.77	$7.11	$7.99	15.0x	12.2x	10.8x	$86.00	18.9x
1 Overweight	$ 86.00			26%	21%	14%				21%	23%	12%					
Regional																	
Coventry	**CVH**	$59.65	$9,741.77	$2.48	$3.13	$3.45	24.0x	19.1x	17.3x	$3.78	$5.46	$5.74	17.2x	11.9x	11.3x	$58.00	16.8x
2 Equal Weight	$ 58.00			35%	26%	10%				34%	44%	5%					
Health Net	**HNT**	$52.58	$5,825.86	$2.15	$2.40	$2.95	24.5x	21.9x	17.8x	$4.23	$4.65	$5.35	13.3x	12.1x	10.5x	$46.00	15.6x
3 Underweight	$ 46.00			-21%	12%	23%				-18%	10%	15%					
Humana	**HUM**	$49.33	$8,134.91	$1.66	$2.09	$2.65	29.7x	23.6x	18.6x	$3.39	$4.15	$5.30	16.1x	13.2x	10.3x	$47.00	17.7x
2 Equal Weight	$ 47.00			14%	26%	27%				12%	22%	28%					
Pacificare	**PHS**	$90.12	$8,822.39	$3.19	$3.97	$4.86	28.3x	22.7x	18.5x	$6.42	$7.26	$9.80	15.7x	13.9x	10.3x	$85.00	17.5x
1 Overweight	$ 85.00			11%	24%	22%				2%	13%	35%					
Sierra Health	**SIE**	$79.83	$2,724.20	$3.28	$3.38	$3.95	24.3x	23.6x	20.2x	$5.71	$6.04	$6.77	14.6x	13.8x	12.3x	$78.00	19.7x
2 Equal Weight	$ 78.00			21%	3%	17%				17%	6%	12%					
Universal American	**UHCO**	$15.37	$891.31	$1.01	$0.96	$1.30	15.2x	16.0x	11.8x	$1.84	$1.78	$2.25	9.1x	9.4x	7.4x	$ 18.00	13.8x
1 Overweight	$ 18.00			33%	-5%	36%				42%	-3%	26%					
WellChoice	**WC**	$79.02	$6,687.78	$2.86	$3.43	$3.88	27.6x	23.0x	20.4x	$5.06	$5.93	$6.69	15.6x	13.3x	11.8x	$ 77.00	19.8x
2 Equal Weight	$ 77.00			19%	20%	13%				10%	17%	13%					
Medicaid Plans																	
AMERIGROUP	**AGP**	$19.19	$1,016.34	$1.66	$0.89	$1.15	11.5x	21.6x	16.7x	$3.14	$2.03	$2.54	6.1x	9.5x	7.6x	$ 19.00	16.5x
2 Equal Weight	$ 19.00			12%	-46%	29%				3%	-35%	25%					
Centene	**CNC**	$25.49	$1,154.14	$1.02	$1.30	$1.75	25.0x	19.6x	14.6x	$1.86	$2.39	$3.26	14.3x	11.1x	8.2x	$ 27.00	15.4x
2 Equal Weight	$ 27.00			19%	27%	35%				-47%	28%	36%					
Molina Healthcare	**MOH**	$28.06	$787.62	$2.00	$0.80	$1.20	14.0x	35.1x	23.5x	$3.53	$1.90	$2.61	8.0x	14.9x	10.8x	$ 21.00	17.6x
3 Underweight	$ 21.00			9%	-60%	49%				8%	-46%	37%					
WellCare	**WCG**	$42.11	$1,670.46	$1.29	$1.67	$2.50	32.6x	25.2x	16.8x	$2.56	$3.32	$4.92	18.0x	13.9x	9.4x	$ 39.00	15.6x
2 Equal Weight	$ 39.00			70%	29%	50%				35%	30%	48%					
Specialty																	
Magellan	**MGLN**	$29.82	$1,121.53	$2.33	$2.65	$1.60	12.8x	11.2x	18.6x	$6.41	$6.52	$4.35	5.8x	5.7x	8.6x	$ 35.00	21.8x
2 Equal Weight	$ 35.00			N/A	14%	-40%				28%	2%	-33%					
Averages																	
National				33%	19%	8%	24.7x	20.4x	18.7x	30%	19%	9%	15.1x	12.5x	11.4x		
Regional				16%	15%	21%	24.8x	21.4x	17.8x	14%	16%	19%	14.5x	12.5x	10.6x		
Medicaid				28%	-12%	41%	20.8x	25.4x	17.9x	0%	-6%	37%	11.6x	12.3x	9.0x		
Specialty				N/A	14%	-40%	12.8x	11.2x	18.6x	28%	2%	-33%	5.8x	5.7x	8.6x		
Overall				**24%**	**9%**	**19%**	**23.0x**	**21.5x**	**18.1x**	**15%**	**10%**	**18%**	**13.4x**	**12.0x**	**10.3x**		
Overall (ex Medicaid)				**22%**	**17%**	**16%**	**24.8x**	**21.0x**	**18.1x**	**20%**	**17%**	**15%**	**14.7x**	**12.5x**	**10.9x**		
S&P 500	**SPX**	**1,259.37**		**20%**	**12%**	**8%**	**18.8x**	**16.8x**	**15.5x**	**$142.28**	**$152.24**	**$164.42**	**10.4x**	**8.3x**	**7.7x**		

Price targets are based on a multiple of CY06 EPS. Material discussing our valuation methodology is available upon request.
Source: Company documents and Lehman Brothers estimates

Source: Lehman Brothers estimates

Important Disclosures:

Sector Coverage Universe

Below is the list of companies that constitute the sector coverage universe:

Aetna Inc (AET)
Coventry Health Care (CVH)
Humana Inc (HUM)
PacifiCare Health Systems (PHS)
UnitedHealth Group (UNH)
WellChoice Inc (WC)
CIGNA Corp (CI)
Health Net (HNT)
Magellan Health Services (MGLN)
Sierra Health Services (SIE)
Universal American Financial Corp. (UHCO)
WellPoint, Inc. (WLP)

FOR CURRENT IMPORTANT DISCLOSURES REGARDING COMPANIES THAT ARE
THE SUBJECT OF THIS RESEARCH REPORT, PLEASE SEND A WRITTEN REQUEST TO:
LEHMAN BROTHERS CONTROL ROOM
745 SEVENTH AVENUE, 19TH FLOOR
NEW YORK, NY 10019
OR
REFER TO THE FIRM'S DISCLOSURE WEBSITE AT www.lehman.com/disclosures

Important Disclosures:

The analysts responsible for preparing this report have received compensation based upon various factors including the firm's total revenues, a portion of which is generated by investment banking activities

Guide to the Lehman Brothers Equity Research Rating System:

Our coverage analysts use a relative rating system in which they rate stocks as 1-Overweight, 2-Equal weight or 3-Underweight (see definitions below) relative to other companies covered by the analyst or a team of analysts that are deemed to be in the same industry sector ("the sector coverage universe"). To see a list of companies that comprise a particular sector coverage universe, please go to www.lehman.com/disclosures.

In addition to the stock rating, we provide sector views which rate the outlook for the sector coverage universe as 1-Positive, 2-Neutral or 3-Negative (see definitions below). A rating system using terms such as buy, hold and sell is not the equivalent of our rating system. Investors should carefully read the entire research report including the definitions of all ratings and not infer its contents from ratings alone.

Stock Ratings:

1-Overweight - the stock is expected to outperform the unweighted expected total return of the sector coverage universe over a 12-month investment horizon.

2-Equal weight - the stock is expected to perform in line with the unweighted expected total return of the sector coverage universe over a 12-month investment horizon.

3-Underweight - the stock is expected to underperform the unweighted expected total return of the sector coverage universe over a 12-month investment horizon.

RS-Rating Suspended - The rating and target price have been suspended temporarily to comply with applicable regulations and/or firm policies in certain circumstances including when Lehman Brothers is acting in an advisory capacity in a merger or strategic transaction involving the company.

Sector View:

1-Positive - sector coverage universe fundamentals/valuations are improving.

2-Neutral - sector coverage universe fundamentals/valuations are steady, neither improving nor deteriorating.

3-Negative - sector coverage universe fundamentals/valuations are deteriorating.

New York
745 Seventh Avenue
New York, NY 10019 USA
1.212.526.7000

London
25 Bank Street
London E14 5LE UK
44.20.7102.1000

Tokyo
Roppongi Hills Mori Tower, 31st Floor
6-10-1 Roppongi, Minato-ku
Tokyo 106-6131 Japan
813.6440.3000

Hong Kong
Two International Finance Centre
8 Finance Street Central Hong Kong
852.2252.6000

This material has been prepared and/or issued by Lehman Brothers Inc., member SIPC, and/or one of its affiliates ("Lehman Brothers") and has been approved by Lehman Brothers International (Europe), authorized and regulated by the Financial Services Authority, in connection with its distribution in the European Economic Area. This material is distributed in Japan by Lehman Brothers Japan Inc., and in Hong Kong by Lehman Brothers Asia Limited. This material is distributed in Australia by Lehman Brothers Australia Pty Limited, and in Singapore by Lehman Brothers Inc., Singapore Branch ("LBIS"). Where this material is distributed by LBIS, please note that it is intended for general circulation only and the recommendations contained herein does not take into account the specific investment objectives, financial situation or particular needs of any particular person. An investor should consult his Lehman Brothers' representative regarding the suitability of the product and take into account his specific investment objectives, financial situation or particular needs before he makes a commitment to purchase the investment product.. This material is distributed in Korea by Lehman Brothers International (Europe) Seoul Branch. This document is for information purposes only and it should not be regarded as an offer to sell or as a solicitation of an offer to buy the securities or other instruments mentioned in it. No part of this document may be reproduced in any manner without the written permission of Lehman Brothers. With the exception of disclosures relating to Lehman Brothers, this research report is based on current public information that Lehman Brothers considers reliable, but we make no representation that it is accurate or complete, and it should not be relied on as such. In the case of any disclosure to the effect that Lehman Brothers Inc. or its affiliates beneficially own 1% or more of any class of common equity securities of the subject company, the computation of beneficial ownership of securities is based upon the methodology used to compute ownership under Section 13(d) of the United States' Securities Exchange Act of 1934. In the case of any disclosure to the effect that Lehman Brothers Inc. and/or its affiliates hold a short position of at least 1% of the outstanding share capital of a particular company, such disclosure relates solely to the ordinary share capital of the company. Accordingly, while such calculation represents Lehman Brothers' holdings net of any long position in the ordinary share capital of the company, such calculation excludes any rights or obligations that Lehman Brothers may otherwise have, or which may accrue in the future, with respect to such ordinary share capital. Similarly such calculation does not include any shares held or owned by Lehman Brothers where such shares are held under a wider agreement or arrangement (be it with a client or a counterparty) concerning the shares of such company (e.g. prime broking and/or stock lending activity). Any such disclosure represents the position of Lehman Brothers as of the last business day of the calendar month preceding the date of this report. This material is provided with the understanding that Lehman Brothers is not acting in a fiduciary capacity. Opinions expressed herein reflect the opinion of Lehman Brothers and are subject to change without notice. The products mentioned in this document may not be eligible for sale in some states or countries, and they may not be suitable for all types of investors. If an investor has any doubts about product suitability, he should consult his Lehman Brothers representative. The value of and the income produced by products may fluctuate, so that an investor may get back less than he invested. Value and income may be adversely affected by exchange rates, interest rates, or other factors. Past performance is not necessarily indicative of future results. If a product is income producing, part of the capital invested may be used to pay that income. © 2005 Lehman Brothers. All rights reserved. Additional information is available on request. Please contact a Lehman Brothers entity in your home jurisdiction.

Lehman Brothers policy for managing conflicts of interest in connection with investment research is available at www.lehman.com/researchconflictspolicy. Ratings, earnings per share forecasts and price targets contained in the Firm's equity research reports covering U.S. companies are available at www.lehman.com/disclosures.

Complete disclosure information on companies covered by Lehman Brothers Equity Research is available at www.lehman.com/disclosures.