FINAL TRANSCRIPT

Thomson StreetEvents℠

WLP - Q3 2008 WellPoint, Inc. Earnings Conference Call

Event Date/Time: Oct. 22. 2008 / 8:30AM ET

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PRESENTATION

Operator

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Ladies and gentlemen, thank you for standing by, and welcome to the WellPoint Inc. quarterly results conference call. (Operator Instructions). As a reminder, this conference is being recorded. I would now like to turn the conference over to the Company's management. Please go ahead.

Michael Kleinman - *WellPoint, Inc. - VP, IR*

Good morning and welcome to WellPoint's third-quarter earnings conference call. I'm Michael Kleinman, Vice President of Investor Relations. With me this morning are Angela Braly, our President and Chief Executive Officer; Wayne DeVeydt, Executive Vice President and Chief Financial Officer; Ken Goulet, Executive Vice President and President of our Commercial business, and Brian Sassi, Executive Vice President and President of our Consumer business. Angela will begin this morning's call with an overview of our third-quarter results, actions and accomplishments. Wayne will then offer a detailed review of our third-quarter financial performance and current guidance, which will be followed by a question-and-answer session in which Ken and Brian will also participate.

We will be making some forward-looking statements on this call. Listeners are cautioned that these statements are subject to certain risks and uncertainties, many of which are difficult to predict and generally beyond the control of WellPoint. These risks and uncertainties can cause actual results to differ materially from our current expectations. We advise listeners to review the risk factors discussed in our press release this morning and other periodic filings we make with the SEC.

I will now turn the call over to Angela.

Angela Braly - *WellPoint, Inc. - President & CEO*

Thank you, Michael, and good morning. Today we announced third-quarter 2008 net income of $821 million, or a record $1.60 per share. On a per-share basis, this is an increase of 10% over the third quarter of 2007 and an 11% increase over the second quarter of 2008. Our third-quarter 2008 results included net realized investment losses of $563 million pretax or $0.71 per share, consisting primarily of other than temporary impairment charges on equity security investments, an impairment charge related to the fair value of certain intangible assets in our State Sponsored business which totaled $141 million pretax or $0.17 per share, and income tax benefits totaling $461 million or $0.90 per share resulting from the favorable resolution of certain federal and state tax matters. These three items substantially offset each other and had a minimal net impact on our earnings per share and operating cash flow.

Net income in the third quarter of 2007 was $868 million or $1.45 per share, which included $0.01 per share in net realized investment gains. Overall WellPoint delivered a solid third quarter amidst a challenging economic environment. We are seeing the corrective action plans we initiated earlier this year positively impact our business.

Our commercial segment is performing well as we continue to grow commercial membership while maintaining strong operating margins that improved 70 basis points sequentially from the second quarter.

We're also seeing improvements in our consumer segment where we achieved the highest level of operating gain in seven quarters. Despite the challenging economic environment and state budgetary issues impacting our State Sponsored business, operating margins in the consumer segment improved by 40 basis points sequentially.

Our Blue operations remains strong, and we now expect our 2008 full-year earnings to be in the range of $5.43 to $5.49 per share. This guidance assumes no additional net realized investment gains or losses in 2008.

Wayne will discuss our investment portfolio in greater detail later on the call, but it is very possible there could be additional realized investment losses in 2008 subject to market conditions.

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We maintain a diverse investment portfolio and strong liquidity. Our insurance subsidiaries are very well capitalized and, on a combined basis at September 30, 2008, have statutory capital levels approximately $6.3 billion higher than what the state regulators require and $3.3 billion above the Blue Cross and Blue Shield Association's minimum required level. We have no needs or plans to inject capital into our insurance subsidiaries.

In the third quarter of 2008, premiums were $14.2 billion, an increase of over $325 million or 2% over the third quarter of 2007 due to premium rate increases for all medical lines of business, growth in our Medicare Advantage business and increased reimbursement in the Federal Employee Program. These increases were partially offset by the loss of the very low margin New York State prescription drug contract, a $1.3 billion annual contract that had $1.3 billion in benefit expense; our exit from Ohio Medicaid; the conversion of Connecticut Medicaid to a self-funded program; and fully insured membership declines.

At September 30, 2008, our medical enrollment totaled approximately 35.3 million members, an increase of more than 500,000 members or 2% from 34.8 million at September 30, 2007. Enrollment in our national business increased by 643,000, including 420,000 new National Accounts members and 223,000 BlueCard members. National Accounts continued to appreciate our strong value proposition, including broad networks and excellent discounts.

Local Group membership in our Blue states increased by 272,000 members over the past 12 months, while our non-Blue UniCare and HealthLink group business declined by 238,000.

As of September 30, 2008, 53% of our medical enrollment was self-funded and 47% was fully insured. At September 30, 2007, our membership was almost equally split with self-funded and fully insured each comprising 50%. Our membership base is growing faster in the self-funded market as our National Accounts business continues to grow, and we have lost more than 300,000 fully insured State Sponsored members mostly from programs where we were unable to receive actuarially sound rates. We have added 188,000 State Sponsored members on a self-funded basis over the past 12 months, predominately due to Connecticut changing from an insured contract to a self-funded contract in the fourth quarter of 2007.

Membership increased sequentially by 63,000 members in the third quarter of 2008, which included Blue branded commercial and individual membership growth of 150,000 offset by declines in our non-Blue business of 50,000 members. Our State Sponsored business declined by 46,000 members. All other sequential membership changes resulted in a gain of 9000 members.

We are seeing growth from a number of new products that we've introduced across several states. These products offer customers choice with varying price points and alternative benefit designs.

For example, the introduction of our SmartSense product for individuals in California has been successful and is generating over half of our new sales. We plan to expand SmartSense to more states over the next few quarters.

In New York the Prism product we launched earlier this year for small group business has been well-received and is generating membership growth in that region. For group business in Georgia, we expect to launch Blue Essential, which is a low price point product, in the fourth quarter of this year, and California regulators recently approved four new small group plan designs that will offer lower-cost options to employers beginning in the first quarter of 2009.

As we look ahead to 2009, I would like to give you an early glimpse into aspects of our membership outlook. We have just concluded a successful 2009 National Accounts selling season, and with in-group growth, we expect more than 400,000 net new national members in 2009. We have 40 new group sales and 17 clients where we have significant in-group growth booked for January 1, 2009.

As we have previously announced in January of 2009, we will be exiting from the Nevada State Sponsored business program. This will impact approximately 49,000 members. In addition, we currently provide administrative services to 203,000 Medicaid members in Connecticut, and we expect these members to transition to other carriers by January 1, 2009.

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As we noted earlier this year, our senior business profitability in 2008 has been constrained by a poorly designed benefit plan in certain Medicare Advantage private fee-for-service offerings that resulted in adverse collections. We will continue to experience higher than expected medical costs on this block of business through the end of 2008. However, we are addressing this problem by eliminating this product design and through our pricing filed for 2009. There are approximately 64,000 members in this plan design.

With respect to Part D, as we bid over the benchmark in five regions, we will lose approximately 48,000 low income subsidy members next year. We will not be receiving new Medicare Part D level income subsidy members during the January 2009 enrollment process due to certain administrative issues impacting low income subsidy members. This will leave us with more than 700,000 low income subsidy members in 2009.

To improve performance in our senior business, we recently named Krista Bowers as Senior Vice President and President of Senior Business and Consumer Marketing. Krista is an outstanding talent who returned to WellPoint after working for a competitor. Under Krista's leadership, we are developing new network-based products in most of our Blue states as a result of recent federal legislation setting the stage for network-based product growth. The Blue brand is a highly trusted brand for senior consumers, and we believe we are well-positioned to capitalize on the coming changes to the Medicare Advantage marketplace.

One of the questions we are often asked is about our expectations for commercial membership in 2009. Since we're still pricing business for the first part of next year and in light of current economic conditions, I'm going to defer providing guidance on commercial membership for 2009 until early next year. We're planning an Investor Day for February 24, 2009, and we will provide detailed guidance for you at that time.

Overall the competitive situation we are facing is rational. Through the recently completed national accounts selling season, we have seen very competitive pricing and more guarantees offered by competitors in response to our superior value proposition.

Heading into 2009, our significant national competitors are all talking about being disciplined in their pricing for fully insured business, and we're seeing some early signs of firmer pricings. We enjoy an advantage that most of our large competitors do not enjoy in that with one exception, namely California, we do not have to compete against non-public Blue plans in our Blue branded service areas.

While we continue to see certain smaller competitors pricing very aggressively in limited geographic areas, we will remain disciplined by pricing our business in an actuarially sound fashion.

We are also implementing strategies to improve our industry-leading competitive position. For example, in Georgia we're recontracting our point of service network. We're receiving a good response from our providers, reflecting that our number one market share is attractive to hospitals who will participate in our new network with favorable pricing for our customers.

Turning now to one of our performance improvement items, claims inventories continue to trend downward, and we believe we have good visibility into our fully insured claim. We're still resolving issues with one system migration that impacted self-funded claims in certain geographies, and we are currently working with our providers to minimize the impact of this issue. We have provided advances to some of the providers who were most affected by this issue and expect to recoup these advances by early next year. We strive to provide excellent service to both our providers and members, and we recently received an award for some services we provide to our members.

Last month we were awarded the Recognizing Innovation in Multicultural Health Care Award by the National Committee for Quality Assurance or NCQA for efforts to reach across cultural and language barriers and provide African-American and Latino members with services that meet their unique needs. The NCQA called our innovative efforts to improve the lives of ethnically and racially diverse members a model for health plans across the country. Efforts like this are just one way that we continue to deliver on our commitments to our customers. While we continue to face business challenges, including weak economic conditions, we believe we have the right team in place to deliver on our commitments to our customers and enhance shareholder

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value. We are executing on our performance improvement plans. We have improved our claims processing and customer service capabilities, reduced our claims inventory, set out our new strategy, re-evaluated our IT migration plans and are turning our ability to act locally while achieving scale into a competitive advantage. While we all have challenges predicting the economy and all of its potential effects, we believe that we can bring the best brand and opportunities to the marketplace, together with a renewed focus on executing and creating health care value.

We are in the process of finalizing our 2009 plans and currently expect single digit EPS growth in 2009. We plan to provide more details about our 2009 outlook in our fourth quarter 2008 earnings conference call and at our Investor Day in Indianapolis scheduled for February 24, 2009. Please contact our Investor Relations to register.

I will now turn the call over to Wayne DeVeydt for a detailed discussion of our third-quarter '08 financials and updated guidance points.

Wayne?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Thank you, Angela, and good morning. I also want to open my comments by noting that our underlying operations are doing quite well. We're making good progress in our performance improvement plans, and this is reflected in our Q3 '08 results.

Operating revenue was $15.3 billion in the third quarter of 2008, an increase of 2% from $15 billion in the third quarter of 2007. The increase was driven by premium rate increases across our medical lines of business and growth in our Medicare Advantage products.

As Angela noted, these revenue increases were partially offset by the loss of the New York State prescription drug contract and lower commercial and State Sponsored fully insured membership.

Administrative fees were $926 million in the third quarter of '08, an increase of $14 million or 2%, primarily due to increased revenue from medical management programs offered by our comprehensive health solutions business unit and self-funded membership growth in National Accounts, including BlueCard and Local Group.

We continue to attract large self-funded customers through our network breadth, our leading discounts, customer service and increased capabilities in medical management and health improvement programs. Our benefit expense ratio was 82.5% in the third quarter of 2008, an increase of 70 basis points from 81.8% in the third quarter of 2007. The increase resulted primarily from higher medical costs and membership mix changes in Local Group business. This was partially offset by the loss of the New York State prescription drug contract, which had a benefit expense ratio higher than the overall Company average.

The benefit expense ratio declined by 80 basis points sequentially as expected due to seasonality in our Medicare Part D drug benefit design and a decline in Local Group as we are implementing actuarially sound rate increases. The impact of our disciplined pricing is becoming very evident. We are pricing business so that our expected premium yield exceeds total cost trends where total cost trend includes medical costs and selling, general and administrative expense.

Based on results through the first nine months, we continue to expect the underlying medical cost trends for full-year 2008 will be in the range of 8% plus or minus 50 basis points. Although we have recently seen some trend mitigation, our pricing for 2009 assumes a small increase in underlying trend.

For the 12-month period ended September 30, 2008, unit cost increases continue to be the primary drivers of medical cost trends. In-patient hospital trend is in the very high single digit range and is all related to unit cost increases. Admissions per thousand have slightly decreased. Our enhanced 360 degree care management programs, more focused review of neonatal

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intensive care cases, spinal injury cases and enhanced clinical management of kidney disease are helping manage in-patient trend.

Outpatient trend is in the upper single digit range and is about 90% related to unit cost increases and 10% utilization-related. We are expanding our American Imaging Management platform to specialty pharmacy reviews to favorably impact this trend.

Physician services trend is in the mid single digit range and is 55% unit cost and 45% utilization. Pharmacy trend is in the mid single digit range and is approximately 70% unit cost and 30% utilization-driven. Unit cost is impacted by our programs to increase use of generic drugs, planned design changes and improved pharmaceutical contracting.

Selling, general and administrative expense was $2.2 billion in the third quarter of 2008, an increase of $30 million or 1% over the third quarter of 2007, primarily due to normal salary increases and higher outside services partially offset by lower incentive compensation. We continue to aggressively manage our administrative costs while investing money to enhance our service.

Our SG&A expense ratio decreased 10 basis points to 14.5% in the third quarter of '08 from the third quarter of '07. The decrease in our selling, general and administrative expense ratio was primarily due to lower incentive compensation this year and our spreading of general and administrative costs over a larger revenue base.

Net investment income in the third quarter of '08 was $214 million, a decrease of $44 million or 17% due to lower investment balances from our share repurchases and lower yields on short-term investments during 2008. There has been significant volatility in the investment markets during the past few weeks. What I would like to do is just take a few minutes to discuss our investment portfolio and our impairment policies.

Our investment accounting is very conservative. We mark our securities that are available for sale to market each quarter. Any unrealized gains and losses are recognized in the shareholders equity section of our balance sheet as accumulated other comprehensive income and loss. We evaluate our investment securities for other than temporary declines based on quantitative and qualitative factors.

For equity securities, if a security is underwater by any amount, even a $1.00 versus cost after 12 months, we recognize that loss through the income statement as an other than temporary impairment. If a equity security is underwater by 20% or more after six months, we similarly recognize that loss as an other than temporary impairment.

We recognized realized losses from other than temporary impairments of $564 million in the third quarter of 2008 compared to $42 million for the third quarter of 2007. Significant other than temporary impairments recognized during the three months ended September 30, 2008 included write-downs for our investments in Fannie Mae, Freddie Mac and Lehman Brothers.

We continue to have a high-quality and well-diversified investment portfolio, which totaled $17.5 billion as of September 30, 2008. The portfolio was comprised of 78% fixed maturity securities, 9% equities including 1% of alternatives, and $2.3 billion of cash and cash equivalents which represents 13% of our portfolio. The average credit rating of fixed maturity securities across our entire portfolio was AA at September 30, 2008, and the portfolio has an average duration of 3.7 years. Our fixed maturity portfolio contains primarily corporate securities, mortgage-backed investments and tax-exempt state and municipal bonds. The corporate securities totaled $5 billion at September 30, 2008. These investments are spread across a diverse array of issuers and industries and carry an average credit rating of A minus.

Our mortgage-backed securities totaled $4.1 billion at September 30, 2008, of which about $3.8 billion was in residential mortgage-backed securities and approximately $300 million were in commercial mortgage and other asset-backed securities. Approximately 73% of our mortgage-backed securities are agency-backed. Of the remaining 27% that are not agency-backed, 24% are rated AAA. Included in these numbers are $188 million of subprime mortgage exposure at quarter-end. All mortgage securities are current on principle and interest.

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Our allocation to tax-exempt munis was $3.7 billion at September 30, 2008 and carried an average credit rating of AA.

Our equity portfolio is diversified across industries and comprised of large-cap and small cap domestic equities, foreign equities and indexed mutual funds. At September 30, 2008, we had fixed maturity and equity securities that were in a net unrealized loss position of $619 million and $157 million respectively. We continue to review our investment portfolios under our impairment review policy. Given the current market conditions and the significant judgments involved, there is continuing risk that further declines in the fair value may occur and additional material other than temporary impairments may be recorded in future periods, driven primarily by the equity portfolio.

Turning now to our intangible asset write-down. During the third quarter of 2008, due to ongoing state budgetary challenges and changes in the regulatory environment in our State Sponsored business, we revised our performance outlook for this business in California and certain other states. This new information triggered an impairment review of our indefinite lived intangible assets related to certain State Sponsored licenses, and we identified and recorded an impairment of $141 million during the third quarter of 2008. The intangible asset impairments and investment losses we recognized during the third quarter of 2008, were substantially offset by the settlement of certain tax matters in the quarter. We settled with the IRS and state taxing authorities disputes related to certain tax years and industry issues, which we had previously disclosed in our SEC filing. This settlement and deductions resulted in a tax benefit of $461 million in the quarter. We're pleased that we satisfactorily resolved these tax matters dating from 1987 to 2002.

Please note that this tax benefit, the realized investment losses due to other than temporary impairments and the impairment charge related to the State Sponsored business had minimal operating cash flow impact.

Turning now to our claims reserves, medical claims payable were $6.3 billion at the end of the third quarter, an increase of $485 million or 8% from year-end 2007, while fully insured members have declined 2%. Medical claims payable were approximately flat with the second quarter of 2008, while days in claims payable increased.

As of September 30, 2008, days in claims payable was 49.1 days, an increase of 1.4 days from 47.7 days as of June 30, 2008. The increase in DCP was driven by medical benefit seasonality and our continued practice of establishing reserves for medical claims in a consistent and conservative manner.

We have included in our press release a reconciliation and roll forward of our medical claims payable reserves. This disclosure is comparable to the reconciliation provided in our 2Q '08 press release. We report prior year redundancies in order to demonstrate the adequacy and consistency of prior year reserves.

For the nine months ended September 30, 2008, we again had significant positive prior year reserve development of $264 million. This level of positive reserve development is lower than the $336 million we experienced for the nine months ended September 30, 2007, primarily due to the medical cost trend visibility issues we experienced near the end of 2007 following certain system migrations.

We continue to establish reserves in a consistent and conservative manner and believe that our September 30, 2008, reserves are appropriately stated.

In the third quarter of 2008, operating cash flow totaled $893 million or 1.1 times net income. We now expect full-year operating cash flow to be $2.6 billion. This is lower than prior expectations, due principally to advances we made to some of the providers who are most affected by the system migration Angela discussed earlier. We expect to recoup these advances by early next year.

We also have one large state customer drawing down from their premium rate stabilization reserve this year. As of September 30, 2008, cash and investments held at the parent company and available for general corporate use was $646 million.

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Approximately $1.5 billion in ordinary dividends are scheduled to be received by the parent company from our subsidiaries in the fourth quarter of 2008.

We also maintain a commercial paper program that is supported by a $2.4 billion senior credit facility. As of September 30, 2008, we have $1.3 billion outstanding under the commercial paper program, down from $2 billion outstanding at June 30, 2008. No amounts were outstanding under the senior credit facility.

At September 30, 2008, our debt to capitalization ratio was 29.8%, up from 28.2% at December 30, 2007, but down from 31.5% at June 30, 2008. We have slowed down our share repurchases in light of the turmoil in the credit markets. While we are very well capitalized, we do think this action has been prudent and reflects that liquidity and the strength of our brand are important.

During the third quarter of 2008, we repurchased 3.6 million shares of common stock for $172 million. For the nine months ended September 30, 2008, we repurchased 50 million shares or 9% of the shares outstanding at December 31, 2007 for approximately $3 billion.

At quarter-end the remaining board approved share repurchase authorization was approximately $1.3 billion. We will continue to monitor financial markets as we evaluate future share repurchase activity subject to market conditions.

Turning to our 2008 guidance, we now expect net income to be in the range of $5.43 to $5.49 per share. This updated outlook includes the following three items that Angela discussed at the beginning of this call.

First, net realized investment losses of $0.78 per share which included no realized investment gains or losses beyond those recorded at September 30, 2008, expenses of $0.17 per share related to the third-quarter impairment of State Sponsored intangible assets, and finally, income tax benefits totaling $0.90 per share resulting from the favorable resolution of certain income tax matters in the third quarter.

Year-end medical enrollment is now expected to be approximately 35.2 million members. Operating revenue is now expected to total approximately $61.7 billion. The benefit expense ratio is now expected to be in the range of 83.5% to 83.6%. The SG&A expense ratio is now expected to be approximately 14.6%. As Angela noted, we currently expect single digit earnings per share growth in 2009. We will provide additional details about our 2009 outlook on our fourth-quarter 2008 earnings conference call and at our Investor Day scheduled for February 24, 2009.

I will now turn the call back to Angela to lead the question and answer session.

Angela Braly - *WellPoint, Inc. - President & CEO*

Thank you, Wayne. Operator, we can open the call for questions and answers.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). John Rex, JPMorgan.

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John Rex - *JPMorgan - Analyst*

Thanks for providing some color on '09. I just wanted to get a sense, so what do you envision and when you talk about single digit EPS growth -- I guess maybe a little more precision -- is that high or low? And really importantly, does that envision share repurchase?

I guess what I'm trying to get out here is, do you believe you can grow operating earnings in '09?

Angela Braly - *WellPoint, Inc. - President & CEO*

John, we thought you might ask that question. We are not going to really narrow the range beyond single digit. But I will say we do expect growth in '09, and the guidance that we give on a more detailed basis will include obviously the operating gain growth, as well as share repurchase expectations for 2009.

We really wanted to be in a position to do a couple of things. One is, as we get through the fourth quarter, you have really great clarity in terms of what '09 will be, and we want to provide you with that great clarity, particularly in light of all the external circumstances that all of us face in terms of the economy and understanding that as best we can. And then we also present our annual plan to our Board in December, at which time we will get final approval and be in a better position so that when we are on the call for the year-end, we can give you a lot more clarity, and we will follow-up with that on Investor Day.

But we're feeling good about our opportunities right now even with the uncertain environment because we have a great brand. We're really executing well in terms of our operations, and our leadership team is really clicking. And so I'm looking forward to being able to give you more guidance on 2009.

John Rex - *JPMorgan - Analyst*

But it is fair to assume that your bias is to something in the way of operating earnings growth, not flat or down just in terms of a general direction on operating earnings for '09?

Angela Braly - *WellPoint, Inc. - President & CEO*

We will be able to give you a lot more granularity as we move forward and look forward to that.

John Rex - *JPMorgan - Analyst*

Okay. Could you just quantify the unrealized losses also and realized/unrealized losses through October kind of given what the markets have done?

Angela Braly - *WellPoint, Inc. - President & CEO*

I'm going to ask Wayne to address that. Wayne?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Just real quick, I want to clarify this. I think this is a question many people have. As we disclosed in our press release, the gross unrealized investment losses at 9/30/08, and I will update in a minute, were about $925 million. But I want to emphasize the fact that well over 70% of that, over $700 million of that, is in fixed maturities.

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So just as a reminder, fixed maturities while mark-to-market, we do not have to take other than temporary impairment charges on. So for statutory purposes, those are carried at amortized cost. There is no impact. And even for GAAP purposes, because we have the intent and ability to hold to recovery, because the average duration on this is just around three and a half years, we do not see that being a significant exposure for us as a Company.

So the real exposure we talk about then is the equities. Because on the equities, our policy is very conservative, about 12 months and even $1.00 under water or 20% in six months. And, as you know, the market is down substantially just since 9/30/08 as well.

So if you were to look at 9/30/08 on a gross basis, it was about $221 million, and not all of that would have necessarily represented a mark-to-market adjustment through the P&L. So to size it, John, I cannot predict the future in terms of where the market will finish between now and the end of the year. Clearly if the markets recover, we may have no writedown. If the markets stay where they were at at 9/30/08, that number would have been closer to, say, about $150 million. That number obviously is going to grow.

The other thing I would like to add is that recognizing of the impairment charge we took this quarter, 40% of that was at the parent company. So our statutory subs took no impact for 40%, yet the full tax benefit is in the statutory sub. So on a net net basis, our statutory equity actually grew for the quarter.

More importantly, it grew enough because of the tax benefit, we believe, to offset even future declines in the fourth quarter in the equity impairment.

John Rex - *JPMorgan - Analyst*

So what was this through October unrealized/realized loss?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

It depends what day you're looking at, John. (multiple speakers)

John Rex - *JPMorgan - Analyst*

I will take as current as you have, I guess.

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

If I looked at last Friday, I'm going to be north of that $162 million, and I will be closer to $250 million. If I look at where we were at two days ago, that number came back down. If I look at where we were at yesterday, it went back up. So literally it is varying by day, my friend.

John Rex - *JPMorgan - Analyst*

So I just want to make sure I understand it correctly, though, in terms of, if I take the $925 million at 9/30/08, I am only adding $150 million to that?

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Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Again, what I would say is, of the $925 million, $700 million plus of that is in fixed maturities, which is a non-issue. So what you really need to focus on is the $221 million of gross unrealized losses on equities. I'm saying that that balance, even if you were to use last Friday, might have been closer to $250 million to $275 million. So you are adding about $50 million to it. And again, that has recovered since last Friday.

John Rex - *JPMorgan - Analyst*

Okay. But that does not include kind of the 70% fixed maturities when you're giving that number. That is just the equity piece, right?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

That is correct, John, but we're not expecting any impairments on the fixed maturities.

John Rex - *JPMorgan - Analyst*

Do you just know what it would have been? I know it is not an impairment. Do you know what it would have been on the full portfolio so I can just get a straight comp to the $925 million?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

I don't have that in front of me, John, and I apologize. We will have to follow-up. I just don't have the full impairment. I have the equity piece.

Operator

Matthew Borsch, Goldman Sachs.

Matthew Borsch - *Goldman Sachs - Analyst*

I have heard a number of references from other companies and from you guys to the economy. I'm just -- if you can put it in historical context for us, and what I'm looking back to is the 2001 recession.

From my numbers your predecessor companies, WellPoint Health Networks, grew earnings by 23% during that recession year; Anthem grew earnings by 57%. So I mean could you just juxtapose where we are now and how that impacts the outlook versus how the industry conditions have changed over that time period and maybe so we can better understand the swing factors going into next year?

Angela Braly - *WellPoint, Inc. - President & CEO*

You know, I think that when you look back at those time periods, there were opportunities at that point where there were major consolidations happening in the industry that benefited the synergies we were seeing and some of the growth expectations as well. And while we think there will be opportunities, particularly during tough economic times for new consolidation opportunities, we're not essentially going to count on those on a prospective basis.

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So I think we have to distinguish it probably from those periods of time. So it is probably not apples-to-apples comparison.

That said, we're looking in terms of the potential impact from the economy on issues like in-group growth for our existing large group customers. We're looking at the levels of buydowns that we might expect. And then, of course, we are always looking at trends and cost of care. And it is more important for us now than ever to really be effective in reducing costs appropriately and improving quality because that is the value that our customers are looking for, and they are looking for affordable products during this time period, so a lot of activity we have around producing those results and delivering products.

I'm going to ask Wayne -- I have Ken and Brian here as well, if they want to add to that response, (inaudible).

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

I would just add real quick that clearly this is a different economy than I think any of us have experienced in most of our lives compared to any other previous recession. I would also say that the number of small group employers that are offering coverage, especially in the one to nine employee range, has dropped at really an unbelievable rate over the last several years, especially when compared to previous recession periods.

So I think it is clearly affordability, but it is also affordability in an environment where people are making choices, hard choices, about making a house payment, making a car payment or buying their insurance, and they are seeing their life-time savings being wiped out.

So there is a lot more happening now than I think a typical recession, and I think as Angela said, there was much more consolidation in 2001, and we had decelerating trend occurring in 2001 up through the last five years until the most recent period where trends have flattened out. So people also benefited from the higher pricing with the decelerating trend.

Angela Braly - *WellPoint, Inc. - President & CEO*

And while we want to take a number of questions, I would like to give Ken and Brian just a minute to talk about how we're responding to those economic challenges in terms of the market activity.

Ken Goulet - *WellPoint, Inc. - EVP & President, Commercial*

This is Ken. A couple of things. First, as we're looking at the economy going into next year, as Angela noted, there will probably be more benefit buydowns. There will probably be some clients that will not -- that will have in-group growth going down, and there will be some that may not be able to afford coverage unless we expand our product portfolio. We're expanding our product portfolio to include more lower-cost products to be able to offer opportunities to continue coverage or to win coverage from other carriers.

And then on just running a Company basis, we have a variety of different scenarios planned where our G&A can be -- we're looking at different ways to impact G&A so that if the membership does go in different directions, we can respond appropriately and have our action plans in place already.

Brian Sassi - *WellPoint, Inc. - EVP & President, Consumer*

To supplement what Ken just said, we're very focused in the individual market on delivering individuals a wide variety of products at different price points, particularly focused on lower-cost options.

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For example, this year in California we introduced SmartSense, which has been very successful from a sales standpoint. It is a lower end PPO option with multiple deductible options. We rolled that out in Georgia in Q3 and just this week in Colorado. We will be also looking to introduce new lower-cost options across our footprint.

Angela Braly - *WellPoint, Inc. - President & CEO*

And let me add one more fact, too, when you look back into the 2001/2002 timeframe, there were two very major competitors who really stumbled at that point and were really shrinking their membership, had really worked on that, and I think we benefited by that.

But the symbol for that is our brand is very strong, and we will benefit by the strength of our brand and our focus on execution in a tough economic environment.

So with that, can we go to the next question?

Operator

Josh Raskin, Barclays.

Josh Raskin - *Barclays - Analyst*

I guess just a question about growth versus margin. It sounds like a lot of the initiatives Angela you spoke about and included in the press release talked about growth whether that was retention programs, higher broker incentives and new product. I'm just curious how do you juxtapose that with what are sort of down margins this year? Should we think about sort of this 8% operating margin run-rate as the appropriate margin that you would expect over the long term, say, three to five years?

Angela Braly - *WellPoint, Inc. - President & CEO*

I think what we're focused on is growth and margins in a sense that we do think we have product and capabilities to bring to the marketplace that can grow in terms of top-line growth.

In terms of margin, we do think it is appropriate to be focused on disciplined pricing. In terms of our expectations around the operating margin, we will be more specific at Investor Day in terms of our expectations for 2009.

Josh Raskin - *Barclays - Analyst*

I guess not so much '09, but as you think about three to five years out, do you think 8% operating margins are adequate, or do you think you would get back to previous levels?

Angela Braly - *WellPoint, Inc. - President & CEO*

I think Wayne was going to speak to this point just a minute ago.

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Again, what is the right margin three to five years out? Obviously we will have to see how the economy continues to progress in the markets.

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When I look at the commercial book, you look at the same period a quarter ago, and we're talking double-digit margins. This year while we're sitting at 9% plus margin, that is with significant reserve strengthening and re-establishing our balance sheet.

And our pricing is holding firm. So I don't know that margins have to shrink over the next three to five years. But again, that will be dependent on a number of factors, including consolidation in this industry and the general economic conditions.

Where I do think you have to look for margin compression over time is going to be in programs such as State Sponsored. I think more and more states are feeling the crunch of budgetary constraints, and I think California was a good example of that, even while they rescinded most of the 10% cut, they did not rescind all of it. I think also when you look at Medicare, I think all of us would agree that many companies in this industry have benefited from good margins in the Medicare business. Obviously who knows where the elections will go and what we will draw from there.

So in certain lines from a consolidated basis, I think you can see things that would put some margin pressure, but I think on the commercial time will tell.

Josh Raskin - *Barclays - Analyst*

That is helpful. Then I think you mentioned in your prepared remarks that cost trends were mitigating recently. So I was curious what areas have you seen that mitigation? I did not notice in the components. And then how do you juxtapose that with we're still expecting an uptick in '09?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Yes, while we're still expecting an uptick, I would say that it is slightly mitigated from the level we thought it would be at at this point. So we're still expecting trends to move upward. We're seeing some things that are giving us some positive signs. Again, our admissions per thousand are slightly down again this quarter. So remember, we saw those starting to pick up in the second quarter, and that was the first time we saw them pick up in a while. But they are actually down slightly in the third quarter.

So it is ever so slightly. We use the word slightly intentionally, but nonetheless we're not seeing what I would say continuous upward movement beyond what we had thought, and I would say at this point it seems to be mitigating slightly below where we would thought it would be at.

Angela Braly - *WellPoint, Inc. - President & CEO*

And to that point, part of our performance improvement was to get the kind of clarity we feel we have now around the trends, around the elements, the drivers of cost of care, and we feel comfortable that we have had better clarity now than we have had and so are giving you the slight uptick as a reflection of that.

Josh Raskin - *Barclays - Analyst*

Okay. So you would have said sort of at least 50 bps last quarter, you had sort of agreed with that number. So is it fair to say it is coming in maybe less than 50 bps, but the pricing was still geared towards the higher than 50 bps for '09?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Yes, I think in the last quarter we said 50 bps was a reasonable approximation. I would say it still is.

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Operator

Justin Lake, UBS.

Justin Lake - *UBS - Analyst*

Just a follow-up on the cost trend side. You are talking about cost trend maybe mitigating a little bit, and yet the days claims payable were up. I'm just curious if you can walk us through any kind of metrics on the reserve side, specifically maybe IBNR and IBNR per member?

Angela Braly - *WellPoint, Inc. - President & CEO*

You know, we are consistent and conservative in terms of overall reserves. I will ask Wayne to talk about the cost trend in terms of where the DCP is in particular.

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

We have seen in the year positive intrayear development on our reserves. But I would also tell you as we continue to drive our inventories down, we want to ensure that there is sustainability with that. So we continue, as Angela said, to be conservative and consistent in our methodology. Our DCP is up, quite honestly, because we have maintained a strong balance sheet because our average claim costs per day are down slightly in the quarter.

So at this point I would just say we feel very comfortable with the strength of our reserves and our balance sheet, and we do not expect to have to re-establish a shortfall like we did in the previous year.

Justin Lake - *UBS - Analyst*

That is helpful. And then just on the pricing side, I think in the second quarter you outlined for us a strategy of going literally market by market, county by county and looking at your competitive positioning to try to figure out how much of that 90 basis points shortfall you can get back. I'm just curious I know it is too early to talk about where the market is from a competitive standpoint, whether employers are going to push back or what other players are doing, but when you look at your competitive position right now from a strategic standpoint, how do you feel like that review came out? Do you feel like you're looking to get back 50 basis points of that or 20 or 70?

Angela Braly - *WellPoint, Inc. - President & CEO*

I'm going to let Ken, who has led the efforts around these deep dives on market by market, respond to that.

Ken Goulet - *WellPoint, Inc. - EVP & President, Commercial*

We completed our deep dives in the best majority of our Blue states, and it was good more detailed information than we have had in the past and our positioning in terms of product pricing and our offerings in all areas down to the county and small MSA levels.

I cannot give you a specific number because it really does vary across the board of what we're using in terms of being able to recover what was underpricing last year. I would say that we have fully recovered, of course, medical costs moving forward. We're able to get some additional trends, meaning our MLR improved year-over-year in many and, in fact, most of our small

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case markets. But it is -- we're not going to get anything back in one fell swoop. Because you have to when you are managing the business, you are also managing what a customer's trend expectation is versus trend across the board. And if you try to get it all back in one area, you're going to force cases to bid, which is not the best position to be in.

So we're able to find where we are competitively. We're gathering it back, but I am not able to give you a specific in terms of what percentage of the 90 bps.

Justin Lake - *UBS - Analyst*

Okay. Can I just ask one numbers question before I jump off? You mentioned that the membership losses have been on the non-Blue side on the commercial book and at UniCare. Can you just tell us how many UniCare members you have as of the third quarter and break that out by risk and non-risk, and then compare that to a year ago or maybe at the beginning of the year?

Angela Braly - *WellPoint, Inc. - President & CEO*

Wayne, do you have that number?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

That is what I'm looking at, to make sure I have it here. I'm sorry, just give me a second, please. I want to say the membership is about 1.4 million members, and about 800,000 of that is ASO with about 600,000 of that being fully insured.

Justin Lake - *UBS - Analyst*

And where was that at the beginning of the year?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Well, it is down almost 236,000 from the beginning of the year.

Justin Lake - *UBS - Analyst*

That is helpful. Thanks a lot, guys.

Angela Braly - *WellPoint, Inc. - President & CEO*

What I would say in that one regard is we had some significant strengthening of pricing, especially in Texas and Illinois, and we recognized and planned that our membership would go down. We felt that in the individual and small group we were not priced right, and we wanted to position our pricing appropriately. So we understood our membership would go down; however, it is down 236 year-to-date.

Justin Lake - *UBS - Analyst*

Great. Thanks. I wanted to make sure I was not overthinking that. Appreciate it.

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Operator

Doug Simpson, Merrill Lynch.

Doug Simpson - *Merrill Lynch - Analyst*

I was wondering if you could just talk about changes in the players market to market? Specifically are you seeing any new entrants disproportionally targeting some of your higher margin markets? I'm just trying to understand if you have a situation where you guys have a -- you are earning $25 to $30 PMPM and someone comes in and says they are willing to write it for $20 to $25, how do you deal with that competitively? What you do with products, and how do you deal with that in negotiations with customers?

Angela Braly - *WellPoint, Inc. - President & CEO*

Ken, do you want to take that?

Ken Goulet - *WellPoint, Inc. - EVP & President, Commercial*

There is always a balance, of course, of pricing where we are in recognizing the competitive market. What I would first say is we're fortunate that we don't compete against not-for-profits in most of our areas except for in one state. And then in a few other areas, I think we mentioned in the last call Virginia, and then in Northeast, we do have some smaller not-for-profits that we run into.

It is a case-by-case position on the larger cases. We do not want to give up a margin price when there is a competitive position. But we're pricing to expand margin in all of our businesses across the area. So we do make case-by-case decisions if it is appropriate, and we feel comfortable with the level of stability of the pricing that we have seen in a certain case. So by that, I mean a larger case. Whereas on a smaller case, we're pricing against our pool, and we are going to get our full margins going forward.

Doug Simpson - *Merrill Lynch - Analyst*

Okay. And then could you just sort of -- I want to make sure we understand your comments about customer pushback that you're seeing sort of between large group, small group and individual. Can you just give us a sense which of those markets have you seen the greatest change in price sensitivity over the last 12 months? Just any sort of historical perspective on that would be helpful.

Angela Braly - *WellPoint, Inc. - President & CEO*

I'm going to have Ken and Brian talk a little bit about what is happening. Of course, we're sensitive to the opportunity to continue to pursue our strategies without telling the marketplace all of the issues that we're facing. But I'm going to ask Ken and Brian to speak to that.

Brian Sassi - *WellPoint, Inc. - EVP & President, Consumer*

This is Brian. I will address individual and senior first. Individual, we continue to see a very competitive but rational market. We are addressing the challenges of that by holding our pricing firm but developing a wider variety of products for individuals to choose. In the individual market, one size does not fit all. So we want to offer products across a variety of price and affordability

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spectrums, and the same really holds true in the senior market. We continue to attack both the individual and senior market at a very granular level, taking a look at pricing of each of our competitors in each of our geographies.

Ken Goulet - *WellPoint, Inc. - EVP & President, Commercial*

I do not see a specific focus on a large group or small group as to where the push is any more significant than the past. But because of the economy, and it really has been just because health care is a big portion of spend, there is always a pretty good focus on it. But our job and the way that we drive the better earnings for our Company and the growth is we need to offer price points at our spreads so that if the client is receiving a certain rate increase, they can choose different price points and different products and services from that level. So it really is no different than it has been. Historically we're doing a better job I think of providing different products at different price points to meet their needs.

Operator

Charles Boorady, Citigroup.

Charles Boorady - *Citigroup - Analyst*

In terms of bringing down a high-end of the range of guidance, if I understand you right, this assumes no additional investment losses. So I'm wondering what would the additional reduction be to your EPS guidance if you assume the markets do not recover from where they are here?

Angela Braly - *WellPoint, Inc. - President & CEO*

It does not include potential additional realized losses. We wanted to just create more clarity. As you know, we did not provide quarterly guidance this year. We thought that by narrowing the guidance we're giving you more clarity in terms of the fourth quarter and then obviously be in a position in terms of '09 to give you the best clarity for '09.

Charles Boorady - *Citigroup - Analyst*

Yes, my question was on the investment loss specifically that it sounds like bringing it down was not related to your expectation for potential additional investment losses. So I'm just wondering if you just assume the debt and credit market, the debt and equity markets do not recover from where they are now, what would the impact be to your EPS guidance?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

This is Wayne. Again, not knowing where the markets will finish, but if you look at it 9/30/08, you applied our very strict policy of anything under water by a $1.00 for 12 months or 20% after six, and because we've had more than a 20% drop in the recent period, you would be looking at pretax based on 9/30/08 of about $160 million pretax. So that could be the impact.

Again, the flipside is last Friday that number grew. As of this past Tuesday, that number went back down -- I mean it is all over the board. So it is very difficult to predict what the broader markets will do, whether they will stay where they are at today or whether they will grow. But that is why we wanted to really spike out that, and from our perspective core operations are solid. So what will happen is based on the broader markets and how we treat it from an accounting prospective.

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Charles Boorady - *Citigroup - Analyst*

Got it. So we would just reduce your guidance by $160 million pretax if we assumed that that is where the markets ended the year?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Yes, if you assume that that is where the market would end, if 9/30/08 held through the end of the year, that would be a reasonable proxy.

Charles Boorady - *Citigroup - Analyst*

Got it. And then the newswires had quoted Angela -- Angela, I don't know if they were accurate or not -- on appetite for acquisitions. I'm wondering what size health plan do you feel ready operationally to acquire and integrate at this point?

Angela Braly - *WellPoint, Inc. - President & CEO*

Well, you know the newswires are always accurate when they report. I did have a conversation, and I'm happy to continue to talk about, there will be opportunities for acquisitions I think in these environments in particular, and we find ourselves always in an interesting place with a unique opportunity to consider Blue acquisitions at times.

So historically if we look to the past, there were opportunities that arose out of difficult economic circumstances because there are tremendous benefits to having scale and having the Blue brands and having the ability to make investments around technology and innovation for our customers. So we look forward to having those opportunities. While we don't speak to any particular transaction or really, frankly, the size of the transactions, because they tend to be, as you know, Charles, very opportunistic. And so we would look at the opportunities that arose and pursue them.

In terms of non-Blue transactions, I think we always prioritize transactions that would be in our markets. So we had some successful ones over the last couple of years where we essentially did endorsement deals, one here in Indiana and we also looked at other places. And so those tend to be fortunate events for us when those opportunities arise.

And then as you know, we have looked at some capabilities. We want to look carefully at those and work on those capabilities that we think would be best owned by WellPoint. But our strategy is not to have to own all capabilities. We can vendor those. We can own some. We can build some. And so what we're bringing together is the best portfolio of what meets our customers' needs.

So we look forward to those opportunities that might arise, and we're going to consider them carefully as those opportunities come up.

Charles Boorady - *Citigroup - Analyst*

So you and the board feel operationally ready, Angela, to make another big acquisition?

Angela Braly - *WellPoint, Inc. - President & CEO*

You know, I think we're feeling operationally ready. I hope that you see in terms of the performance improvement plan, what we believe is our better visibility into claims. We have reevaluated our IT migration plan. We have organized in a way with a

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disciplined management process within the Company to produce better execution. And so I'm confident that we could acquire and integrate a sizable Company.

Operator

Scott Fidel, Deutsche Bank.

Scott Fidel - *Deutsche Bank - Analyst*

Just sticking on the Blues for a moment, I'm just interested, as you've been talking with your Blues brethren whether you are seeing any interest in any of the nonprofits trying to give another go here, trying to convert to for profit status just as we think about some of the significant budget issues that the states are going to be facing. So I'm wondering whether you think the Horizon conversion application here is more of a one-off, or do you think this could be followed up if there is other interest out there among other Blues?

Angela Braly - *WellPoint, Inc. - President & CEO*

Yes, we are always reluctant to speak to any specific Blue plan and their plans for conversion. I do have great confidence, though, in the relationships within the Blue system. I think there's a renewed interest in Blue plans to make sure we are effectively executing around the BlueCard program, delivering the most value there. We're doing some great things together like Centers of Blue Distinction around quality, hospitals that provide the most effective care. There's lots of great discussions. You know, our companies, AIM and Resolution Health, have a number of Blue customers.

So we do think there are new opportunities for Blue plans to work together collaboratively. And we do think that Blue plans across the country consider what their strategic opportunities might be whether it is through sharing capabilities and remaining independent or considering opportunities to combine.

Scott Fidel - *Deutsche Bank - Analyst*

I just had a follow-up question around out of network hospital costs. I know in the first half you had cited seeing some pressure there. I'm just interested in sort of an update on the third quarter, whether you have seen any change in that?

And then just more conceptually whether as we think about the economy continuing to deteriorate, do you think that we're going to start seeing the members be more interested in looking at in-network options as a way to reduce their expenses compared to out of network?

Angela Braly - *WellPoint, Inc. - President & CEO*

You know, I'm going to have Brian and Ken speak to it. In terms of the product choices that we're making available and whether the draw towards products with maybe more specific networks are really seen as being very attractive.

Ken Goulet - *WellPoint, Inc. - EVP & President, Commercial*

I will start off, and then Brian I think can chime in.

First, in terms of out of network hospital costs or out of network costs in general, it still remains a very, very small part of our overall cost because we have such a broad network overall. We have actually introduced some cost control in those areas. We

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have always had our -- Blue products have some discounts in place for nonnetworked hospitals for prompt pay to those hospitals, and we have expanded that through some additional relationships where we will even on an out of network basis through prompt pay agreements receive discounts from out of network providers. So that gets passed through to our customers and to ourselves.

I would say in response to your question, is there more of a focus on network-based? In our product areas, I think it is fair to say that our clients are looking and continue to look for good cost alternatives. And one of those things that we then look at is whether the entire network or other approaches that would best meet their needs. So our product development slate is looking at different product alternatives regarding alternative networks or tighter networks. And that has to go through the whole process of vetting it with consumers, vetting it with employers, but it is one area that we're looking at to see a tighter network, which was not acceptable a decade ago, becomes more acceptable given the tighter cost climate right now.

Brian Sassi - *WellPoint, Inc. - EVP & President, Consumer*

As Ken noted, a small percentage of our costs are related to out of network expenses. I think as costs and price transparency becomes greater, consumers are going to be more focused on their out-of-pocket expenses and probably more focused on staying in network.

Certainly in certain segments of our business like in the senior market, there is going to be a migration towards more network-based products, particularly as private fee-for-service fades out. And I think WellPoint is in an excellent position to take advantage of that since building networks is one of our core competencies.

Angela Braly - *WellPoint, Inc. - President & CEO*

Yes, Scott, when you think about our value proposition, it is that we have had the broadest network. We have had 80% of the doctors, 95% of the hospitals. And so within those networks, though, we have opportunities because we are so deep in our market to make a meaningful difference in terms of the products and the way that we offer the networks to our members. So we think that is going to be to our advantage as well going forward.

Operator

Tom Carroll, Stifel Nicolaus.

Tom Carroll - *Stifel Nicolaus - Analyst*

Just quickly on a couple of things here. On the Medicare private fee-for-service business, what service lines are driving the higher than expected costs here? And Angela, did you say you have 64,000 private fee-for-service members?

Angela Braly - *WellPoint, Inc. - President & CEO*

I'm going to let Brian speak to this. He runs our senior business since this January and is doing a great job of really focusing on that for 2009. So Brian, in terms of overall membership for senior, we have about 213,000 Medicare private fee-for-service members, including 64,000 that are in these enhanced products where we have seen adverse selection, and we're not going to carry those through to 2009.

So Brian, do you want to address that?

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Brian Sassi - *WellPoint, Inc. - EVP & President, Consumer*

Okay. The 64,000 members in our enhanced plans, those are the plans that we have seen some of the deteriorating experience. And it is primarily around Part B drugs, as well as increased in-patient and outpatient costs.

But again, during the 2009 bid process, we did not refile those plans, so we do expect a good portion of that membership to either transition back to traditional Medicare or to potentially one of our other private fee-for-service or network-based plans.

Tom Carroll - *Stifel Nicolaus - Analyst*

Great. I had missed that point. And then one second short question, what would you suggest is driving the potential uptick in cost trends in 2009? Can you maybe point to something that we can start thinking about?

Angela Braly - *WellPoint, Inc. - President & CEO*

In terms of 2009, in terms of what we think is driving it, in-patient costs have been in the high single digits. While we have seen utilization relatively flat, most of the increase is related to unit cost increases. We have some very specific contracting initiatives and management programs in the NICU area around spinal surgery cases, chronic kidney disease and end-stage renal to really focus on really the intensity that we're seeing in terms of in-patient. Outpatient we're seeing come in at upper single digits, up a little bit from mid to upper last quarter and mostly unit cost driven. And we do have radiology management programs that we think were having an impact on that.

We also are working on that from a transparency perspective, too. We have Anthem CareCompare, which is our transparency tool showing our members on episode treatment grouping, what the cost of a procedure would be to our members and giving some levels of quality data. We are expanding that. We are in 10 states, and we're expanding that further.

So we think between the management programs that we have, as well as some of the transparency tools that we have, that we can address those trends.

Tom Carroll - *Stifel Nicolaus - Analyst*

Right. And if I could sneak one last one in here, Wayne, for you, on the tax benefit that you talked about today, what is your discretion on when to show us that or when not to show us that?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Well, I don't think there is very much discretion. I think the accounting rules are very clear on that. Keep in mind that this was a disputed tax that goes all the way back to 1987. So obviously you can imagine we have been in dispute over this for an extended period of time. It was actually during this quarter that we got signed settlement agreement from the IRS, and it was only within the quarter that we were able to eventually release those reserves because of that. So there is no discretion from my perspective.

Operator

Greg Nersessian, Credit Suisse.

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Greg Nersessian - *Credit Suisse - Analyst*

Three quick questions for you. First, your guidance for '08 implies a stepdown in the fourth quarter. I guess it has been historically the pattern. Could you just speak to the drivers of that?

Second, on your Medicare it sounds like you're looking to take advantage of the elimination of deeming. Is it fair to say your strategy is going to be exclusively organic, or would you consider doing some M&A to accelerate that process on the M&A book?

And then finally, on Medicaid do you feel like the markets where you will remain in 2009 have sort of stabilized? Is there a potential for further exits on any of your Medicaid markets? And I guess on that front, this medical write-down, should we interpret that as a signal of a change in your thought process with respect to that program?

Angela Braly - *WellPoint, Inc. - President & CEO*

Let me divide your questions up. In terms of guidance for 2008, we did try to show some back at our Investor Day conference for 2008 the seasonality. And so the seasonality is coming in as we expected. So I will let Wayne speak to that a little bit more.

And then in terms of both Medicare and Medicaid, Brian Sassi runs those businesses, and he can speak to both your question about deeming in terms of where we expect growth there, as well as in the Medicaid business. When you look at them, the Medicaid impairment charge that we took, we look at that every year. We also have an external validation in terms of valuation. So it was the appropriate timing for us to look at whether or not our expectations in terms of the margins and the growth for that business were appropriate in terms of the impairment issue. So that is something we do on kind of a regular scheduled basis.

But with that, I will ask Wayne to answer the first part of that question and then Brian to cover the other two.

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Well, again, Angela, I think you addressed a lot of this, Greg. But, as we said, if you actually go back to the original IR day, while we have not achieved that original guidance, you will see that we showed a significant seasonality switch from what you have seen historically and actually showed that there was actually a stepdown in the fourth quarter.

So again, I would just reiterate what Angela said that this is not out of line with what our expectations were and not out of line with what we were trying to communicate back in December, including showing a slide that showed that seasonality of the quarterly earnings per share progressions.

I think if you look at that, you will see that even with the stepdown in guidance from our original guidance, I think you'll find that that pattern is holding very true at this point. Again, it is driven primarily by Part D doughnut holes being eliminated, and that starts running through more, and there is the commercial MCR creep that happens in the fourth quarter. So again, I think if you look at that, I think you'll find that is pretty consistent.

In terms of the M&A, I will just simply say that one of the biggest opportunities we see within the Medicare right now, though, is really the network-based program in our Blue states. So I think there is going to be a lot of organic building within our existing networks within our existing Blue states versus going out right now and necessarily trying to acquire that skillset.

But nonetheless, we're always open to thoughts, but we never like to talk about those specific M&A deals.

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Angela Braly - *WellPoint, Inc. - President & CEO*

Okay. Brian, do you want to take those questions?

Brian Sassi - *WellPoint, Inc. - EVP & President, Consumer*

Okay. With respect to growth in Medicare Advantage, we do anticipate a conversion from our private fee-for-service to our network-based products, so a lot of that would be organic growth. As well as we have really built-up the infrastructure to capitalize on WellPoint's age-in opportunity. As our under 65 members within our commercial and other consumer books of business turn 65, we're very focused on converting those to senior lines of business. But, as Wayne said, the door remains open for potential acquisition opportunities as they present themselves.

With respect to SSB, our Medicaid business, we have taken a very close look at that business this year, the business model. We put some new leadership in place. Other than the announced exits that we previously talked about in Nevada - we're leaving the Nevada market at the end of January and leaving Connecticut, which is on an ASO basis, by the end of the year, we're not anticipating any additional state exits for the coming year.

With that said, with 30 states being in budget deficits, we continue to monitor the performance of this business unit very closely and will make the appropriate business calls at that time.

Operator

(Operator Instructions). Carl McDonald, Oppenheimer.

Carl McDonald - *Oppenheimer - Analyst*

In the past you have given us some broad puts and takes as you think about '09 versus '08 in terms of costs that were incurred this year really related to '07, the benefit of getting out of some unprofitable Medicaid and, at the end of this year, Medicare markets, the onset of higher incentive comps. Could you update us just sort of broadly on how you are thinking about those now?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Yes, I think a lot of those will stay the same. So again, if you were to look at some of the tailwinds, one was we said, if we got reserves right, we would not need to restrengthen reserves then you would expect somewhere in the $200 million plus range for a tailwind.

What I would say is we're feeling very comfortable with our reserves. So I think that is one that at this point in time I'm feeling very good about, I think Angela is feeling very good about it, and that is one I think we would all expect to materialize as long as we continue to maintain the conservative and consistent approach that we have.

Two is we talked about the fact that in the senior business we thought there would be approximately $100 million tailwind there. Clearly by eliminating the products as Brian had mentioned that were causing us some of our most difficult results, again we made the decision to exit them completely versus trying to modify benefits. So again, I think that tailwind is something we feel very comfortable with at this point in time as well.

And then, of course, we said that in the commercial and individual that we ought to be able to try to price up for some of this and see if we could recover some of, this year's pricing shortfall, coupled with just pricing for trend and getting the leverage of the G&A off that as well. And that was the number that we talked about historically being in the $200 million range. And again,

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that is a number that I don't feel uncomfortable with, but I think, as Angela said, it is one of the reasons we are also postponing guidance and wanting to really give better clarity between how this year finishes out and where the fully insured pricing comes in for next year. We know where our pricing is going to be in the general market.

When you look at some of the headwinds, obviously the most significant headwind is the fact that we had to maintain a workforce that is at a market-based compensation. We do believe in being a performance-based company, and we wiped out the vast majority of our incentive compensation program for all of our associates.

And so that is one item that we have said is in the $200 million to $300 million range and is closer to $300 million than it is to $200 million.

The other thing that we want to emphasize is that clearly there will be lower investment income. Obviously with our buyback program and with rates where they are at today, that is going to drive lower investment income. But that gets offset by the fact that your buybacks ought to have some accretion for you. So there is not a complete offset, but again there are some give and takes there.

The only other one that I would throw out that we have not talked about in the past is that with our disciplined pricing this year and as we're working through this, we do have a lot of fully insured membership, though, that is going away at this point. Obviously there is op gain on that membership throughout this year that does not repeat next year.

But when you take those headwinds/tailwinds, you are still able to come up with some positives in terms of having positive growth next year. And that is why at this point we are still comfortable saying single digit growth.

Carl McDonald - *Oppenheimer - Analyst*

Thank you for that. Then the second question is just on UniCare profitability this year. If we look at the overall operating earnings being down low double digits for the consolidated book, how does the UniCare profitability compare to that?

Angela Braly - *WellPoint, Inc. - President & CEO*

We do not specifically spike that out in terms of overall. As Ken said, there were some specific initiatives within UniCare to make sure that the pricing was right there. It is a challenging environment for UniCare and it does not necessarily have all the same advantages that we have in our Blue states. So we're looking strategically at targeting the opportunities that exist for UniCare and being very focused on how we do that.

Carl McDonald - *Oppenheimer - Analyst*

Do you think at the end, the UniCare needs to be a much smaller business than it is today?

Angela Braly - *WellPoint, Inc. - President & CEO*

I think that Ken and his team are looking at the way that UniCare can operate in the most strategic and effective way. So Ken, do you want to --?

Ken Goulet - *WellPoint, Inc. - EVP & President, Commercial*

I would just say, as we go forward, we're looking at a lot of different strategies and assessing everything. But UniCare will be a different business than it is today. Our licenses are valuable. We can use UniCare in a lot of different ways for everything from

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doing on a green license. A question came up earlier about tighter networks, using a tighter network around some of our UniCare products and selling it in that way. Or if we look towards Internet business in the future, we can use UniCare.

Now I'm just using that as two of many examples of things we're looking at. But it is fair to say it will be a different business as we go forward.

Operator

Anu Gupta, Sanford Bernstein.

Anu Gupta - *Sanford Bernstein - Analyst*

I had a couple of questions. One is on the senior market and specifically related to the pipeline for Medicare Advantage. Are you seeing in your National Accounts business that employers -- are you seeing traction on group retiree conversions, and is that being accelerated by the economy? Are they showing concern around the recent cuts and potential future cuts to private fee?

Angela Braly - *WellPoint, Inc. - President & CEO*

Brian, would you take that one?

Brian Sassi - *WellPoint, Inc. - EVP & President, Consumer*

Yes, I will take that. Since the passage of the most recent Medicare law, what we have seen is actually less interest in moving towards a private fee-for-service based employer group retiree strategy. We see that as a temporary situation.

Beginning in 2010 and 2011, as more network- based products get into the market, I think there will be renewed interest in that. We think that we're very well-positioned again to capitalize on our national and our commercial segment and offer employer group retiree plans, as well as the Blue Medicare Advantage kind of BlueCard network gets up and running, we will be very well-positioned to handle national business.

Anu Gupta - *Sanford Bernstein - Analyst*

Should we be thinking about that for '09, or is this more long-term in terms of larger groups moving --?

Brian Sassi - *WellPoint, Inc. - EVP & President, Consumer*

I think '09 we're seeing less interest given the changes in the Medicare because if an employer moved to a private fee-for-service based employer group retiree product they would have to move in 2010, 2011 to another network-based product. So our outlook is that many employers are questioning the movement in '09 and probably going to be deferring that to later years.

Anu Gupta - *Sanford Bernstein - Analyst*

One more question. Can you comment on the outlook for states regulating and putting in the lower caps in context of what happened recently in California with the MLR requirement?

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Angela Braly - *WellPoint, Inc. - President & CEO*

Yes, I'm going to speak to that. We want to have a dialogue about responsible reform. One of the concerns we had around minimum medical loss ratios is that it really creates the wrong policy incentive because the focus needs to be on the cost and quality of health care and delivering the right results there. And from a policy perspective, we thought there were better ways to address health care reform.

So we do have a focus on responsible health care reform. We think we need to have access. We think it is best delivered through public/private partnerships. We need to have coverage for all children in America. We do think there are public programs that need to expanded and be effective and strong, particularly in economic situations, particularly those programs that address the most needy. We do think there are opportunities where there could be subsidization - where we could subsidize premiums for some of the working poor where we have tough issues. And we do think we need, though, to have a strong private market that, as it does today, delivers affordable products with a wide choice of products for our customers.

So when we look at options like minimum medical loss ratio issues, we think while well-intentioned, we think that there are more effective ways to address the underlying issue in health care, which is that the cost and quality are not where they need to be.

Operator

Brian Wright, Bank of America.

Brian Wright - *Bannk of America - Analyst*

On the sequential decline in other noncurrent liabilities in the quarter, did that run through operating cash flow this quarter?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Brian, I would have to go back to the specific details, but essentially we use an indirect method cash flow approach. So essentially any changes in the balance sheet are going to run through operating cash flow to the extent that they are operationally related. So the short answer is yes. I just don't have all the pieces in front of me.

Brian Wright - *Bannk of America - Analyst*

So that $400 million could largely be the reduction in the cash flow outlook for the year then?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Most of the cash flow reduction in guidance is really related to two items. It is just north of $200 million of advances to some providers that we expect to recoup in the early part of next year. And the other part is that we have one very large state customer that is drawing down their premium rate stabilization reserve this year.

Brian Wright - *Bannk of America - Analyst*

Okay. And then would it be fair to assume that you are using the current share authorization in your '09 outlook?

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Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Well, again, we will provide more specific guidance on '09 once we get board approval on the plan. But we would expect obviously to get some of that share repurchase done between now and the end of the year.

But, at the same time, I want you to know we're being cautious in light of the current market conditions. So obviously whatever we get done this year does impact next year at the same time. Even if we do not get it done this year, if we get it done early next year, it has virtually the same impact on the year.

Brian Wright - *Bannk of America - Analyst*

Okay. And one last quick one. What was the effective tax rate in the quarter, excluding the tax settlement?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

I don't have that in front of me. I want to say it was -- excuse me one second. For the year-to-date -- sorry, Brian, I am just trying to make sure I get you -- about 35.75%, 36%.

Angela Braly - *WellPoint, Inc. - President & CEO*

Operator, unfortunately we're not going to be able to take everyone's call in the queue, but if we could have one last question.

Operator

Peter Costa, FTN Midwest.

Peter Costa - *FTN Midwest - Analyst*

A couple of questions actually. First, the higher MLR guidance at the bottom and the lower EPS guidance at the top end of the ranges, what product specifically caused you to change your views there? Was that all of the State Sponsored business, or were there other products that contributed to your changing view?

Angela Braly - *WellPoint, Inc. - President & CEO*

You know, Peter, you're right that the State Sponsored business we're looking at very carefully in terms of the impact on MLR.

Wayne, do we have anything to add?

Wayne DeVeydt - *WellPoint, Inc. - EVP & CFO*

Yes, most of the increase on the low-end is around State Sponsored. As you know, they came out in California obviously with the 10% not being rescinded in full. More importantly, even when that happened, it's not until March 1 of next year.

So while we had baked in some of that, because it extends into next year, you are forced to pull some of that forward under a PDR calculation, which we have done. So, first of all, that is driving the low-end. That is timing, as you know, because the PDR will unwind itself throughout part of next year, early next year. So that is the big driver there.

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In terms of the top end of the range, at this point from our perspective there's obviously a number of factors. We are maintaining a very strong, conservative balance sheet, and we plan to continue to do that between now and obviously the end of the year. Our reserves are very strong at this point. But I would not say it is driven by any underlying core operation that puts us at a concern or risk. Trend is not coming down, and we really thought on the higher end, we saw flat to mitigating trends coming downward, and that is not the case.

Peter Costa - *FTN Midwest - Analyst*

Okay. And then on the system conversion problems that you had where you paid out advances to some of the hospitals and providers, did you also have any problems with customer service on those system conversions with your customers?

Angela Braly - *WellPoint, Inc. - President & CEO*

Let me talk about that, Peter, because in terms of that conversion, that was really in the Midwest. We are now at pre-migration claims inventory levels. And so I think we have produced the right results in terms of the remediation efforts there. This is a self-funded part of the system. We are now working through the reconciliation with the providers. Often they leave their A/Rs open while we go through the reconciliation processes, and as we complete the reconciliations, we will see the return of those advances in terms of cash flow and how we have done that.

In terms of impacting the member, most of the issues that we face and the reconciliations that we're working on are with our providers and our provider service. And we want them to be good partners and us to be good partners to them. So we are very focused on remediating those issues. For the most part, our members were not directly impacted by that.

Peter Costa - *FTN Midwest - Analyst*

You don't expect any membership rollback the next year from that?

Angela Braly - *WellPoint, Inc. - President & CEO*

No, we don't. We do not see that happening in terms of membership overall as a result of that specific activity.

Peter Costa - *FTN Midwest - Analyst*

Okay. And then you talked about -- just to follow-up on the first question -- on the State Sponsored business, you talked about not leaving any other states. Are you leaving any counties in California?

Angela Braly - *WellPoint, Inc. - President & CEO*

Brian, do you want to speak to California in particular?

Brian Sassi - *WellPoint, Inc. - EVP & President, Consumer*

Yes, with respect to California, we do not anticipate leaving any Medicaid counties. We will be exiting some of the healthy families counties for next year, although we continue to have the largest footprint in California of any Medicaid provider. We will do so even after exiting a couple of counties within California for healthy families.

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Peter Costa - *FTN Midwest - Analyst*

How much membership is that?

Brian Sassi - *WellPoint, Inc. - EVP & President, Consumer*

It is give or take about 60,000.

Angela Braly - *WellPoint, Inc. - President & CEO*

Okay, Peter. Well, thank you for that last question or questions, and I'm sorry that we are not able to get to everyone's questions today. We got to as many as we possibly could. But let me close here.

Let me reiterate that our core operations remain strong as we continue to execute on our performance improvement plan. We're striving to create the best health care value for our customers. We're excelling at day to day execution, and we continue to expand by capitalizing on our unique value proposition and distinctive competitive advantages. By doing this, we intend to provide an appropriate return for our shareholders and drive sustainable long-term results.

I want to thank you all for participating in this call this morning, and operator, will you please provide the call replay information. Thank you.

Operator

Thank you. Ladies and gentlemen, this conference will be available for replay after 11:00 AM Eastern time today through November 5. You may access the AT&T Teleconference Replay System at any time by dialing 1-800-475-6701 and entering the access code 908944. International participants dial 320-365-3844.

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