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Conference Call Transcript

WLP - Q3 2005 WellPoint, Inc. Earnings Conference Call

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SAFE HARBOR STATEMENT UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This transcript contains certain forward-looking information about WellPoint, Inc. ("WellPoint"), WellChoice, Inc. ("WellChoice") and the combined company after completion of the transactions that are intended to be covered by the safe harbor for "forward-looking statements" provided by the Private Securities Litigation Reform Act of 1995. Forward-looking statements are statements that are not historical facts. Words such as "expect(s)", "feel(s)", "believe(s)", "will", "may", "anticipate(s)" and similar expressions are intended to identify forward-looking statements. These statements include, but are not limited to, financial projections and estimates and their underlying assumptions; statements regarding plans, objectives and expectations with respect to future operations, products and services; and statements regarding future performance. Such statements are subject to certain risks and uncertainties, many of which are difficult to predict and generally beyond the control of WellPoint and WellChoice, that could cause actual results to differ materially from those expressed in, or implied or projected by, the forward-looking information and statements. These risks and uncertainties include: those discussed and identified in public filings with the U.S. Securities and Exchange Commission ("SEC") made by WellPoint (formerly Anthem, Inc.), WellPoint Health Networks Inc. ("WellPoint Health") and WellChoice; trends in health care costs and utilization rates; our ability to secure sufficient premium rate increases; competitor pricing below market trends of increasing costs; increased government regulation of health benefits and managed care; significant acquisitions or divestitures by major competitors; introduction and utilization of new prescription drugs and technology; a downgrade in our financial strength ratings; litigation targeted at health benefits companies; our ability to contract with providers consistent with past practice; other potential uses of cash in the future that present attractive alternatives to share repurchases; our ability to achieve expected synergies and operating efficiencies in the WellPoint Health merger within the expected time-frames or at all and to successfully integrate our operations; such integration may be more difficult, time-consuming or costly than expected; revenues following the transaction may be lower than expected; operating costs, customer loss and business disruption, including, without limitation, difficulties in maintaining relationships with employees, customers, clients or suppliers, may be greater than expected following the transaction; our ability to consummate WellPoint's merger with WellChoice, to achieve expected synergies and operating efficiencies in the merger within the expected time-frames or at all; to meet expectations regarding repurchases of shares of our common stock and to successfully integrate our operations; such integration may be more difficult, time-consuming or costly than expected; revenues following the transaction may be lower than expected; operating costs, customer loss and business disruption, including, without limitation, difficulties in maintaining relationships with employees, customers, clients or suppliers, may be greater than expected following the transaction; the regulatory approvals required for the transaction may not be obtained on the terms expected or on the anticipated schedule; our ability to meet expectations regarding the timing, completion and accounting and tax treatments of the transaction and the value of the transaction consideration; future bio-terrorist activity or other potential public health epidemics; and general economic downturns. Readers are cautioned not to place undue reliance on these forward-looking statements that speak only as of the date hereof. Neither WellPoint nor WellChoice undertakes any obligation to republish revised forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. Readers are also urged to carefully review and consider the various disclosures in WellPoint's and WellChoice's various SEC reports, including but not limited to Annual Reports on Form 10-K for the year ended December 31, 2004 and Quarterly Reports on Form 10-Q for the reporting periods of 2005.

ADDITIONAL INFORMATION AND WHERE TO FIND IT

This communication is being made in respect of the proposed merger transaction involving WellPoint and WellChoice. In connection with the proposed transaction, WellPoint and WellChoice will prepare a registration statement on Form S-4, containing a proxy statement/prospectus for the stockholders of WellChoice to be filed with the SEC and each will be filing other documents regarding the proposed transaction with the SEC as well. BEFORE MAKING ANY VOTING OR INVESTMENT DECISION, INVESTORS ARE URGED TO READ THE PROXY STATEMENT/PROSPECTUS REGARDING THE PROPOSED TRANSACTION AND ANY OTHER RELEVANT DOCUMENTS CAREFULLY IN THEIR ENTIRETY WHEN THEY BECOME AVAILABLE BECAUSE THEY WILL CONTAIN IMPORTANT INFORMATION ABOUT THE PROPOSED TRANSACTION. The final proxy statement/prospectus will be mailed to WellChoice's stockholders. Investors and security holders will be able to receive the registration statement containing the proxy statement/prospectus and other documents free of charge at the SEC's web site, www.sec.gov, from WellPoint Investor Relations at 120 Monument Circle, Indianapolis, Indiana 46204, or from WellChoice Investor Relations at 11 West 42nd Street, New York, New York 10036.

PARTICIPANTS IN SOLICITATION

WellPoint, WellChoice and their directors and executive officers and other members of management and employees may be deemed to be participants in the solicitation of proxies in respect of the proposed transaction. Information regarding WellPoint's directors and executive officers is available in WellPoint's proxy statement for its 2005 annual meeting of shareholders, which was filed with the SEC on April 8, 2005, and information regarding WellChoice's directors and executive officers is available in WellChoice's proxy statement for its 2005 annual meeting of stockholders, which was filed with SEC on March 28, 2005. Information regarding the persons who may, under the rules of the SEC, be considered participants in the solicitation of WellChoice stockholders in connection with the proposed transaction will be set forth in the proxy statement/prospectus when it is filed with the SEC.

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PLEASE NOTE: THIS TRANSCRIPT HAS BEEN EDITED FOR ACCURACY**CORPORATE PARTICIPANTS****Tami Durle***WellPoint, Inc. - VP IR***Larry Glasscock***WellPoint, Inc. - President and CEO, Director***John Watts***WellPoint, Inc. - President and CEO, National Accounts***Dave Colby***WellPoint, Inc. - EVP and CFO***Joan Herman***WellPoint, Inc. - President and CEO, Specialty, Senior and State-Sponsored Business***CONFERENCE CALL PARTICIPANTS****Charles Boorady***Citigroup - Analyst***Matthew Borsch***Goldman Sachs - Analyst***John Rex***Bear Stearns - Analyst***Josh Raskin***Lehman Brothers - Analyst***Doug Simpson***Merrill Lynch - Analyst***Ellen Wilson***Sanford Bernstein - Analyst***Christine Arnold***Morgan Stanley - Analyst***Patrick Hojlo***Credit Suisse First Boston - Analyst***Scott Fidel***J.P. Morgan - Analyst***Michael Baker***Raymond James - Analyst***Carl McDonald***CIBC World Markets - Analyst***Joe France***Banc of America Securities - Analyst***PRESENTATION****Operator**

Ladies and gentlemen, thank you for standing by and welcome to the WellPoint conference call. [OPERATOR INSTRUCTIONS] At this time, I would like to turn the conference over to the Company's management. Please go ahead.

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Tami Durle - WellPoint, Inc. - VP IR

Thank you. Good morning and welcome to WellPoint's third quarter earnings conference call. I'm Tami Durle, Vice President of Investor Relations, and with me are Larry Glasscock, our President and Chief Executive Officer, Dave Colby, Chief Financial Officer, and John Watts, President of our National Accounts Unit. Larry will begin this morning's call with an overview of our third quarter performance and other recent developments, followed by John Watts who will provide details of our National Accounts progress for 2006. Then Dave will review our financials and discuss our financial outlook for the rest of 2005.

Before we take your questions, Larry will provide a brief update on the status of our recently announced plan to merge with WellChoice. I would also like to note that Joan Herman, our President and CEO of Specialty, Senior and State-Sponsored Business will be available to respond to questions you may have regarding our activities in Medicare. I would like to point out that both John and Joan will be providing additional information on their businesses at our Investor Day on December 6. We may defer some questions to be addressed at that time.

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 in periodic filings we make with the SEC.

In connection with the merger, WellPoint and WellChoice expect that a registration statement, which will include a proxy statement/prospectus, will be filed with the SEC. We urge listeners to review the registration statement, if and when it becomes available, because it will contain important information about the merger. Information regarding the persons who may, under rules of the SEC, be considered participants in the solicitation will be set forth in the proxy statement/prospectus, when it is filed with the SEC. You can obtain free of charge documents filed with the SEC, by WellPoint or WellChoice by visiting the SEC's Website at www.sec.gov or by contacting the Investors Relations departments of WellPoint or WellChoice.

In addition, our discussion will include non-GAAP financial measures, such as comparable basis information, as defined under the SEC rules. As required by the rules, a reconciliation of those measures to the most comparable GAAP measure is available on our Website at www.wellpoint.com. I will now turn the call over to Larry Glasscock.

Larry Glasscock - WellPoint, Inc. - President and CEO, Director

Good morning and thank you Tami. We are very pleased to report an outstanding and very busy third quarter of 2005. Our earnings momentum continued, pretax margins reached a record 9.1%, medical costs continue to moderate and we are growing membership. In addition, we recently announced our intent to merge with WellChoice. We remain very excited that the combination of WellPoint and WellChoice, will further strengthen our ability to provide customers with innovative and cost effective solutions that will meet their healthcare needs.

During the quarter, WellPoint reported GAAP net income of \$1.02 per diluted share, or 20% growth over the prior year period. These earnings exceeded our prior guidance of \$1.00 per share. Our operating revenue exceeded \$11.1 billion, a 136% increase year-over-year, and a 5.6% increase on a comparable basis. Comparable basis information throughout our discussions today have been calculated by adding the historical information for former Anthem Inc. and the former WellPoint Health Networks Inc. Comparable revenue increases were driven by membership growth and disciplined pricing.

Our enrollment is now almost 29 million medical members, as we added 145,000 members in the third quarter. Every single region reported membership growth in the third quarter and our sequential growth continued in each customer type. Our membership has increased by over 1.5 million members on a comparable basis since September 2004, a 5.6% increase. Year-to-date organic growth, excluding the Lumenos acquisition, was 4%. At 9/30/2005 our business was almost evenly split between fully insured and self-funded. On a comparable basis at 9/30/2004, about 47% of our business was self-funded.

On July 1, 2005, the Georgia State HMO account converted about 140,000 members from a fully insured plan, to self-funded. We currently offer both HMO and PPO products to the Georgia State account but we'll lose the PPO portion on January 1, 2006. Currently about 300,000 members are covered under the PPO plan. Now, we expect some employees will want to stay with the BlueCross BlueShield product and switch during open enrollment from the PPO to the HMO option. We had some early signs of this, since during the Georgia Teachers open enrollment in September, we added about 3,500 HMO members.

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Our 2006 National Account selling season is essentially complete for January 1 effective dates. And we expect good growth in 2006. John Watts will discuss this later on the call. In addition to National Accounts, we've also had a nice pipeline of local large group account wins for 1/1/06.

We are continuing to develop and expand new products to attract and retain business. Our centers of business excellence, about which I have spoken in the past, have been formed to spread best products and practices across our enterprise. We have placed senior leaders in charge of each CBE to ensure that we leverage strengths across the entire Company. As an example, in the third quarter, we launched EmployeeElect in Colorado. EmployeeElect is a small group program that has been successful in California. It allows small group employers and employees product choices similar to those afforded to large businesses.

We continue to offer innovative products targeted to attract membership from the uninsured in our country. In the first nine months of this year, we have provided new individual policies to more than 282,000 people who had previously been uninsured. We are continuing our efforts to reach uninsured Americans with affordable healthcare coverage, like our innovative Tonik product that now accounts for about 17% of individual sales in California.

Beginning 1/1/2006, we will offer Medicare Part D prescription drug benefits to seniors in all 50 states. Our actuarially sound bids were below the benchmark in each region, meaning that we expect to receive about 600,000 auto enrollees. We continue to be optimistic about the Part D program and will provide updates on our progress. Beginning in 2006, Medicare Part D members will be reported on a new line item in the Specialty Metrics section of our Medical Membership and Specialty Metrics Summary that many of you see, obviously.

In addition to growing our business, we are also focusing on our administrative expenses. Our year-to-date SG&A ratio was 16.3%, through 9/30/2005, 20 basis points lower than the comparable period of 2004. Please note, however, that this 2005 year-to-date, SG&A ratio included expenses for the multi district litigation settlement from the second quarter. We will continue to work to improve our ratio of administrative costs as a percentage of revenue, while improving service to our customers through innovative tools like Employer Access. Employer Access enables small employers to have an easy and accessible way to administer health benefits for their employees.

We now have thousands of groups enrolled in this service. By allowing groups to have access to their account to order ID cards, perform eligibility and billing changes and other administrative tasks, we are able to put employers in control of their membership, resulting in lower administrative expenses as well as improved quality.

Service quality is important to our customers and obviously to us. Anthem Health Plans of Virginia and Nevada were recognized during the quarter by the Federal Employees Plan Director's Office as low-cost, high-performing plans. This was the 13th time in the last 14 years that the Virginia plan received this very prestigious award, which recognizes, again, the achievement of a superior level of service to federal employees at a low administrative cost.

We have additional opportunities to reduce our admin costs by continuing to execute our merger integration plans, and work towards achieving our expected synergies. We achieved our goal of recognizing at least \$40 million in synergies during the third quarter. We continue to expect synergies to accelerate, totaling at least \$150 million in 2005. We also continue to expect net savings of at least \$250 million in 2006 and are well on our way to achieving this run rate.

We have been able to integrate two large companies, achieve synergies and maintain the quality of our services. We have been recognized for our efforts in providing quality care to our members. Our core values include putting the customer first as well as personal accountability for excellence, and I'm pleased to report that the U.S. News and World Report, along with the National Committee For Quality Assurance, or NCQA, announced earlier this month that our Anthem BlueCross BlueShield plans in Connecticut and New Hampshire were ranked among the top commercial health plans in the nation. Recently, BlueCross of California won two BlueCross BlueShield Associations Best of Blue Awards. The first award was for "Out of the ER: The Tulare Project". This study demonstrated how unnecessary emergency room visits could be decreased by partnering with providers and providing educational tools to members who frequently use the emergency room for primary care.

The second award was for "Community Help: A Health Plan's Contribution." This award was in the "Innovation in Partnership" category. In partnership with local healthcare leaders, this project examined the effects of air pollution on members with asthma. The goal of the project was to develop strategies to mitigate the effects of identified asthma triggers. We are very proud of our efforts and work every day to improve the quality of care delivered to our members.

As you may have seen this morning, we also announced a few organizational changes that I thought I would spend just a few moments on. Let me begin with Tom Snead who plans to leave the Company early next year, in order to spend time with his family, and more time serving his

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community in Virginia. Tom, as you know, currently heads up our Southeast region, and has been with WellPoint or its legacy companies for over 20 years. He's been a tremendous partner and a friend to me over the years, and he will be greatly missed.

After the close of the pending merger with WellChoice, we also believe we can make our organization even more efficient by consolidating the existing Southeast and Northeast regions of WellPoint, as well as WellChoice, into a new East region that will be more comparable in size and scale to our current Central and West regions. Our plan is for Mike Stocker, who is currently the CEO of WellChoice, to assume the leadership responsibility for this new region. Ron Ponder who is currently our Chief Information Officer, also plans to leave the Company at the end of the year. Mark Boxer who is currently President and Chief Executive Officer of Consumer Driven Health Plans Enterprise Services as well as, Administar Federal and United Government Services, will assume Ron Ponder's role, as Chief Information Officer. Mark's current responsibilities will be assigned to other members of our existing leadership team, including John Watts who will assume responsibility for consumer-driven health plans.

Both Tom and Ron have been very instrumental in the growth and the operational success we have realized. And both have made a number of very important contributions to the formation of our strategy going forward. We are fortunate to have such a strong talent pool in place that we are able to make organizational changes, such as these, with confidence that our strategies will continue to be executed in a manner that produces exceptional results. I believe we have assembled one of the most outstanding and experienced leadership teams in the country and certainly in our industry. And I believe we have the right team in place to continue our significant progress in transforming the industry.

What I will do now is turn the call over to John Watts, President and CEO of our National Accounts Business to provide details about our National Account activity for January 1. John?

John Watts - WellPoint, Inc. - President and CEO National Accounts

Thank you, Larry and good morning. I'm pleased to be here this morning to share what we view to be some exciting results of our 2006 selling season. In January, we will begin serving 16 new groups and are projecting a net gain approximately 200,000 members, excluding Blue Card host members. The increase is comprised of members from these 16 new National Accounts, from known net growth within existing national account relationships. Key new sales include our first joint sales with Lumenos, following the acquisition of Lumenos earlier this year. We won this business from a variety of competitors nationwide, and are continuing to see the trend of national customers consolidating the number of carriers they offer.

Our major competitors in the national segment are working hard to keep their business from going out to market. And though we had an active quoting season this year, we expect to see more robust bidding for 1/1/07 effective dates. We think proposal activity will increasingly be driven by interest in consumer driven health solutions, where Lumenos gives us a competitive advantage. In general, pricing remains rational. While total costs, including fees and discounts, continues to be the clear driver in terms awarding business there's growing interest in sophisticated care management program, high performance networks and consumer-directed products and tools.

As we review our results for 1/1/06, it's clear that national account customers are using WellPoint for a number of reasons. First, we offer superior customer service and financial value across all of our geographies. We refer to ourselves as being a mile wide and a mile deep. A mile wide in that we offer our customers the ability to access America's largest provider network. And a mile deep in that customers accessing our provider network are availing themselves of the industry's deepest provider discount. All told, our network is one-third larger than our next nearest competitor, an advantage we believe will be difficult to duplicate.

National Accounts are also choosing WellPoint to access the innovative products and services we offer, a strength that's been greatly bolstered this year with the acquisition of Lumenos. As we continue to integrate Lumenos, it's important to note that select Lumenos clients will have access to Blue Networks effective January 1. And we're working very hard to make Blue Networks available to all Lumenos clients headquartered in our Blue states during 2006. Another reason we are attracted to National Accounts has to do with the broad set of consumer tools we have available for our members. We will broaden this capability as evidenced by our recent partnership with WebMD. This relationship greatly enhances our members' ability to access online medical information, providing our members with help in improving their health status over time.

Next, we continue to deploy our primary nurse advocate model, which provides members with a concierge type of resource to help them navigate and better access the healthcare system. And last but not least, we have the number one consumer brand in healthcare. One in three Americans carry a BlueCross BlueShield card. And eight in ten of the largest corporations offer BlueCross BlueShield coverage. This is a tremendous advantage for us.

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All that being said, we are not resting on our laurels. We have several major initiatives lined up for 2006. Including rollout of high performance networks in select geographies, significantly improved customer reporting and additional care management programs that focus on improving the health of our members through better quality care. And as we have said before, we strongly believe that higher quality will lead to lower healthcare costs over time. We expect these initiatives to result in a consumer focused healthcare suite of products second to none in terms of ease-of-use, transparency and overall financial value.

All considered, we believe we have a sustainable advantage over our competitors. And now I will turn the call over to Dave Colby for a detailed review of our third quarter 2005 financial results.

Dave Colby - WellPoint, Inc. - EVP and CFO

Thank you, John, and I do want to apologize up front for my voice. I'm recovering from a cold over this weekend. So, hopefully you won't read anything into my tone other than I'm recovering. We are very pleased with our third quarter 2005 earnings per diluted share of \$1.02. This is \$0.02 cents higher than our previous guidance, primarily due to lower than expected medical costs, resulting from a moderating trend and our effective medical cost management programs. On third quarter earnings per share of \$1.02, represents a 20% increase between the third quarter of '04, and this quarter. The most significant driver of the third quarter year-over-year changes relates to the inclusion of legacy WellPoint Health Networks operations following the November 2004 merger.

As in our prior earnings call, my financial commentary this morning will compare current results to three full months of legacy Anthem and three full months of legacy WellPoint on a combined basis for the third quarter of 2004 where appropriate. I will refer to this historical data as comparable basis information. As more fully described in our press release, reconciliations of comparable basis information to the historical GAAP information of the legacy companies is available on our Website.

Turning to premium revenues, it was \$10.3 billion in the third quarter, an increase \$517 million or 5.3% on a comparable basis over the third quarter of 2004, primarily due to disciplined pricing. On a comparable basis, fully insured membership increased by 85,000 members, or 0.6%. The marketplace continues to be very competitive, but generally rational and we remain very disciplined in our underwriting and pricing. Administrative fees were \$691 million in the third quarter, an increase of \$62 million or 9.8% on a comparable basis over the third quarter of last year, due primarily to Large Group and National Account membership growth, including the 140,000 State of Georgia employees that shifted from a fully insured HMO product to a self-funded one on July 1. On a comparable basis self-funded increased by 1.5 million members or 11.3%.

Our benefit expense ratio was 79.9% in the third quarter. 170 basis points favorable to the third quarter of last year and slightly lower than our prior guidance. During the third quarter, medical trends continued to moderate, and we now expect medical trend in 2005 to be less than 8.5%. The primary drivers of medical trend are outpatient and inpatient expenses. Our contracting of medical cost management programs continued to be successful and certain of the synergies related to the merger have reduced medical costs.

In terms of the components of medical trends, outpatient services trend is approximately 75% cost related and 25% utilization related. Our radiology management program continues to be very successful. In the Central region, where it was recently introduced, our trend for advanced imaging services has fallen dramatically. We are expanding our national contracting initiative, such as our contract with LabCorp, that offer lower cost and provides clinical data that we can then use to improve the quality of medical services provided to our members.

Inpatient medical trend is mostly unit cost driven. Admission rates were relatively stable. And days of care per thousand were actually down slightly. Contracting initiatives include implementation of quality incentive programs and a continued emphasis on fixed per diem rates, or DRG contracts as opposed to discounted fee for service arrangements. Approximately, 88% of our admissions are to facilities with fixed rate with DRG contracts. We are also adjusting our benefit designs for certain procedures, such as gastric bypass.

The pharmacy cost trend continues to moderate and is about 65% unit cost driven, as pharmaceutical companies raise pricing on popular drugs. We continue to encourage their usage through programs such as our Generic Select and we believe we have a significant opportunity for increasing generic utilization over the next year as some popular drugs such as Zocor lose patent protection. Our new Specialty pharmacy capabilities are favorably impacted by the medical trends. Certain Specialty drugs like some of those used for oncology can be provided by our Specialty pharmacy. This lowers our costs of providing these drugs to our members. Physician trend is about evenly split between cost and utilization and has remained relatively stable.

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The SG&A ratio in the third quarter of 2005, was 16.6%, 70 basis points higher than the third quarter of 2004. This increase reflects higher merger related stay bonuses included in the quarter, and the growth in our ASO membership, which is a higher SG&A ratio. Also impacting the ratio were the costs associated with the transition of our information technology infrastructure services to an external vendor, which is designed to reduce future operating costs.

Sequentially, the SG&A ratio was up by 10 basis points for essentially the same items. But, remember, that the second quarter, a portion of the charges associated with the multi district litigation settlement, or \$68 million, was booked to SG&A expenses. On a year-to-date basis our SG&A ratio of 16.3% was 20 basis points lower than the 16.5% for the comparable period of 2004. And this includes the additional expenses we incurred in 2005 that we expect will benefit our financial operations in the coming year. This improvement is primarily due to continuing expense management, spreading administrative expenses over a larger membership base, productivity increases and achieving our merger synergies.

Turning to our segments, the healthcare segment consists of our four health insurance geographic regions, plus National Accounts as well as the Senior and the State-Sponsored business. In the third quarter, our operating revenue in our healthcare segment was almost 10.7 billion, an increase of 6% on a comparable basis over the third quarter 2004, led by Individual and Small Group business. Our operating gain was \$917 million, an increase of \$157 million or 21% on a comparable basis over the third quarter of last year. The operating gain improvement was driven by our Large Group in ISG businesses, reflecting moderating medical costs and disciplined pricing. The healthcare segment operating margin improved to 8.6%, 110 basis point increase when compared to the third quarter of last year.

The Specialty segment includes our dental, pharmacy, vision, life, disability, behavioral health and workers' compensation businesses. In the third quarter operating revenue in that segment was \$723 million, an increase of \$56 million, or 8% on a comparable basis over the last year. Our operating gain was \$89 million, an increase of \$4 million or 4% on a comparable basis over last year, primarily due to margin expansion in the pharmacy benefit management operation. But these results were partly offset by higher mortality claims in our group life business.

Our largest Specialty business is our PBM. And our PBM prescription volume increased to 84.7 million scripts in 3Q05, 3% higher than the third quarter of last year and an increase of 274,000 prescriptions sequentially. As a reminder, on July 1, we lost the State of Connecticut, PBM inductor contract. That is why our dental membership declined in the quarter. Our Specialty business continued to generate higher margins on our healthcare businesses and we expect continued growth in our Specialty businesses.

Now moving to the balance sheet, our cash and investments were \$16.7 billion at September 30, 2005, an increase of \$1.7 billion from year end 2004, primarily due to strong cash flow and an effective investment portfolio management. Our total assets were \$41.9 billion, at quarter end, up \$2.1 billion from year end. Our medical claims payable were \$4.2 billion at the end of the third quarter, a \$20 million decrease from year end 2004, as our fully insured membership has declined in 2005. In the third quarter, as noted earlier approximately 140,000 members in the State of Georgia account converted from a fully insured HMO product to one that is self funded.

Days claims payable, remained flat in the quarter at 46.7 days when compared to June 2005. This is the first quarter in a couple of years where we were not able to improve the claim cycle time. In fact, claim cycle time increased by 0.3 day, offset by a 0.3 day reduction due to timing of our PBM claims payments. We have included in our press release a reconciliation and roll forward of our medical claims payable reserves and there were no surprises. It continues to demonstrate the adequacy and consistency of our reserving practices.

I do want to highlight that if you included legacy WellPoint Health Networks operations for all of 2004, the line item "prior year redundancies in the current period as a percent of prior year net incurred medical claims" would be 1.9%, which is very consistent with prior years. The schedule also demonstrates that we are paying claims at a faster rate. The amount of claims paid in the current year resulting from claims incurred in the current year has increased from 83.5% at September 30, 2004, to 84.6% at September 30 of this year. The increase is primarily attributable to our systems auto-adjudication and improved electronic connectivity with our provider networks. The result is our ability to pay claims quicker and have more current data for actuarial analysis.

The long-term debt of \$3.9 billion, at the quarter end, declined by 8% from year end. Our total debt-to-capital ratio declined to 17.1% at September 30, compared to 18.5 at year end 2004. Our operating cash flow was very strong at \$928 million in the third quarter of 2005, over 1.4 times our net income during the quarter, and indicates the strong quality of our earnings.

During the quarter, we did not repurchase any shares, due to the trading restrictions based on the Company during our negotiations with WellChoice. In August, our Board of Directors raised our share repurchase authority to \$1 billion. We expect to resume our share buyback program after the WellChoice transaction closes. In addition, our Board has approved increasing our share buyback authorization by an additional \$1 billion when the WellChoice transaction closes.

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In terms of 2005 guidance, we continue to expect fourth quarter earnings per share of \$1.03, and 2005 earnings per share of \$3.93. This guidance includes the higher synergy levels we expect to achieve in the fourth quarter and almost \$40 million in Medicare Part D start-up costs. In terms of 2006 guidance, we remain committed to our goal of achieving 15% growth in our net income per share, not taking into account the \$100 million of additional synergies from the WellPoint Health Networks merger expected to be realized in 2006, the impact of expensing stock options or the potential accretion from the pending merger with WellChoice, Inc.

As we have said in the past, our 15% growth rate does include the impact of Medicare Part D. We are currently finalizing our 2006 annual plan, and we'll share our 2006 formal guidance in great detail during our investor day, coming up December 6, 2005 in New York City. I will now turn the call back over to Larry.

Larry Glasscock - WellPoint, Inc. - President and CEO, Director

Thank you, Dave and your voice held up pretty well, actually. Before I turn it over for questions, we thought we would give you a brief update on where we are in the approval process for the WellChoice merger. We filed our application for license transfer with the BlueCross BlueShield Association on October 4. Last week, we received approval from the Plan Performance and Financial Standards Committee, and this Committee recommended that the full Board approve the transaction, and that will be taken up at the full Board meeting next month. We made filings with the Department of Justice under the Hart-Scott-Rodino Act. We did that on October 12. And we made our Form A change-in-control filings with the New York and New Jersey Departments of Insurance on October 18. So, we expect to receive all necessary approvals, including approval by the WellChoice shareholders. And we plan to close this transaction in the first quarter of 2006. That said let's open the call for questions. I'll turn it back to the AT&T operator.

QUESTION AND ANSWER

Operator

[OPERATOR INSTRUCTIONS] And our first question comes from the line of Charles Boorady with Citigroup.

Charles Boorady - Citigroup - Analyst

My first question is on yield that we actually would measure on the income statement year over year. I'm wondering if you could help reconcile what we would measure as an average premium yield on a model, versus what you are actually pricing on sort of a same product, same customer basis? So for example, how much was mix related from selling the lower priced products and how much was buy down, et cetera?

Dave Colby - WellPoint, Inc. - EVP and CFO

Well, I think the biggest change in this quarter really was 140,000 life Georgia account, which had a fairly significant benefit level, the HMO moving from fully insured to ASO. That had a pretty big impact. In terms of actual buydowns, they continue to be what we had said before, running at about 200 basis points. I think the key is, as you saw in the healthcare segment, our margins actually increased 110 basis points. Some of that is obviously because we have seen more growth in ASO, which runs a better margin. But it also demonstrates that, obviously with the medical care ratio being flat or slightly down that we are able to price ahead of the medical trends.

Charles Boorady - Citigroup - Analyst

Okay and what if I looked at it sort of same product, same customer basis for renewal, on average, what is the price increase that I would be seeing?

Dave Colby - WellPoint, Inc. - EVP and CFO

If you took out all the mix, our trend now is running just slightly less than 8.5%. And the medical care ratio is coming down slightly, so the pricing will be slightly above that.

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Operator

And we do have a question then from the line of Matthew Borsch with Goldman Sachs. Please go ahead.

Matthew Borsch - Goldman Sachs - Analyst

Thank you, good morning. Question on the outlook for National Accounts in January enrollment. The 200,000 that you talked about, can you comment - is that then going to be a net 100,000 loss with the impact of the Georgia, assuming 300,000 will all go away? How should we think about that for January? I know you have other large local groups coming in. Can you comment on Blue Card at all, as well?

Dave Colby - WellPoint, Inc. - EVP and CFO

Well, I turn it over to John to talk about National Accounts. You will remember that the State of Georgia PPO account is in our large group segment. It's not a National Account. But it is true that we will add 200,000 National Accounts and we will lose 300,000 State of Georgia. That's a negative 100,000 to start.

John Watts - WellPoint, Inc. - President and CEO National Accounts

And I just add on the Blue Card piece. It's a little early to tell in terms of Blue Card growth for 2006, although we do expect growth. It's just a little bit early to come up with a projection on that.

Larry Glasscock - WellPoint, Inc. - President and CEO, Director

I'm sorry Matt, Larry. We'll also provide more detailed guidance on enrollment at our investor day. So, again, you are taking sort of pieces of this. We'll try to put it all together for you when we meet in early December.

Dave Colby - WellPoint, Inc. - EVP and CFO

We still expect membership growth.

Matthew Borsch - Goldman Sachs - Analyst

Okay. Great. And just a related question on that for John, could you characterize the level of competition versus the level of employer account switching? Obviously 200,000 national account wise and 16 new accounts is very impressive. But just noting that it's somewhat less than the 250,000 you brought in last year, and the 20 accounts there. And I'm just wondering if you could sort of characterize what changed in the environment that led to a somewhat lower result?

John Watts - WellPoint, Inc. - President and CEO National Accounts

Well, it is a competitive environment. I think it is safe to say that the competitors we compete against are all primarily healthy at this stage of the game. And everyone, including WellPoint, is working very hard to keep our business from going out to business. So from a quoting season standpoint, we didn't see much of an uptick over 2005 levels. And as I said earlier, we do expect as people - as employers begin to focus - move from being interested in consumer driven health plans to actually thinking about truly adopting them. We expect a more robust bidding season in 2007. So it's a highly competitive market. Pricing is rational. But we do believe there's a lot of opportunity going forward.

Operator

Thank you. And we do have a question now from the line of John Rex with Bear Stearns. Please go ahead.

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John Rex - Bear Stearns - Analyst

Good morning. I was wondering if you could just give us a little more color on the subcomponent trends, perhaps maybe updating off the last quarter, as you provide that guidance?

Dave Colby - WellPoint, Inc. - EVP and CFO

Sure, John. Where we have had probably the best success, given the sort of below expectation trend, is on the outpatient side. I think a lot of the programs that Dr. Nussbaum and our regions have put in place around national contracting for things like lab, the radiology imaging program, which we are now rolling out nationwide, have been effective. I think, by the end of the year, we may see outpatient trend get below double digits.

John Rex - Bear Stearns - Analyst

And last quarter I think you characterized that as about 10% or low doubles; is that right?

Dave Colby - WellPoint, Inc. - EVP and CFO

Yes.

John Rex - Bear Stearns - Analyst

So we have edged down - it's fair to say we've edged down 100 bps or so from there.

Dave Colby - WellPoint, Inc. - EVP and CFO

That's correct and that's been the major driver of the overall. The other ones have been relatively stable. Our inpatient hospital is still in the mid to upper single digits. Pharmacy now down into single digits from double digits. And we have physician services in the mid single digits.

John Rex - Bear Stearns - Analyst

Okay. Would you expect any of those components to show acceleration next year? In pharmacy, do you think that rebases and ticks up a bit? And kind of what are your early thoughts about this trend?

Dave Colby - WellPoint, Inc. - EVP and CFO

We will give you more detailed guidance in December of what we expect. Because we still have some cases out being priced. I'd prefer to assume not tip our hand on what our expectation is. Although, I think we have been fairly consistent in saying that we don't see a whole lot that's going to drive trend either way up or way down in 2006.

Operator

Thank you very much. And we do have a question from the line of Josh Raskin with Lehman Brothers. Please go ahead.

Josh Raskin - Lehman Brothers - Analyst

Thanks. Good morning. Could you just give us a little bit more clarity? I know you're not going to give specifics on the 2006 guidance. But could you just help quantify? We know what the additional synergy number is. Could you let us know: what is the embedded Part D earnings that you guys are expecting in 2006? And what is your expectation maybe or just a range around the stock option expense impact?

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Dave Colby - WellPoint, Inc. - EVP and CFO

Well, let me address the stock option expense because we have been pretty clear there and it's actually disclosed in the footnotes to our financial statements in the quarterly. We have said somewhere in the 3% to 5% dilution range. If you use the midpoint there, it's probably a reasonable estimate. In terms of Part D, we will go into that a little bit more detail on December 6. I think the one thing you have to realize: while we have some benefit in Part D, we have a very large Medicare supplement book that we expect will have some cannibalization. So what we have to look at is really what the net increase is.

Josh Raskin - Lehman Brothers - Analyst

Okay. And then is it safe to assume that in terms of the membership numbers, and we have a sort of premium from CMS, and a sort of a mid single digit margin, is that just sort of a fair rough number to use for now?

Dave Colby - WellPoint, Inc. - EVP and CFO

Well, I think, we have said that we expect the opportunity to be about \$1 billion plus revenue opportunity. And it would run to comparable margins to government business.

Larry Glasscock - WellPoint, Inc. - President and CEO, Director

As you know, Josh, we do not discuss margins on specific products. But there have been a lot of discussions around this, certainly estimates appearing from various plan sponsors. And we think those rates are very much in the range of what you could expect from us.

Operator

Thank you and we are showing a question now from the line of Doug Simpson with Merrill Lynch. Please go ahead.

Doug Simpson - Merrill Lynch - Analyst

Hi. Good morning, everyone. I was just wondering if you could maybe talk a little bit longer term about your strategy? Looking out past the completion of the WellChoice deal, and just give us a sense of how you are thinking about potential Blue plan pipeline, and the propensity to maybe look at Specialty businesses as well? And maybe Dave if you could comment, debt-to-cap right now, we calculate about 17%. What kind of level would you be comfortable taking this up to over the next couple of years?

Larry Glasscock - WellPoint, Inc. - President and CEO, Director

Well, I will let Dave talk about the debt-to-cap here in a minute. I think in terms of strategy for the future, we are very focused, obviously, on integrating Anthem and WellPoint. And I think that's going very well. But remember, we're 11 months into this. So that's receiving a good bit of our focus. And when you add WellChoice, the reason we feel so very good about that is that integration really is not being dramatically affected by the Anthem/WellPoint integration, because we haven't added any state up in the Northeast region. So we feel very good about the timing of all of this.

I think as we look to the future, we're going to have 33 million members. And we've demonstrated an ability to grow same store at a very competitive level. Acquisitions have always been a part of our strategy. They will continue to be part of our strategy. And we will always make people aware of where it is we are trying to go into the future. And as other companies decide that their strategies align with ours, we'll make sure that we pursue those discussions. But right now, Doug, we are really focused on getting these done well.

In terms of Specialty acquisitions, we look at those from time to time. We believe we have a very good portfolio of Specialty products. As you know, when we put Anthem and WellPoint together, we had two of everything. So, we're in the process of having one of everything and that takes a little bit of time. So right now, our energies are focused on that.

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Dave Colby - WellPoint, Inc. - EVP and CFO

In terms of the cap ratio, Doug, you are right. Your computation is the same as mine at 17%. We are well below what our target level is, which is around the mid-20, range, which we think supports our current credit ratings. Obviously, we had made the decision earlier on to increase our share buyback program. Unfortunately, as a result of WellChoice negotiations during the third quarter, under advice of counsel, we were locked out from being in the market. But we will be back in the market with the share buyback programs that we have. \$1 billion without the WellChoice and an additional \$1 billion when that deal closes. And actually our expectation is even with that share buyback program, we will still be slightly below our targeted debt-to-cap.

Operator

Thank you and we have a question now from the line of Ellen Wilson with Sanford Bernstein. Go ahead.

Ellen Wilson - Sanford Bernstein - Analyst

Yes, thanks. Excuse me. A question on the SG&A front. You raised your full year SG&A ratio guidance a bit even though your deal related synergies are on track. Could you kind of explain what's changed there from the second quarter?

Dave Colby - WellPoint, Inc. - EVP and CFO

Well, probably the biggest change is we've had a number of costs: we announced the transition of our IT infrastructure, primarily data center, mainframes and servers from in-house to an IBM outsourced contract. There are a number of up front costs that we are incurring this year, things like severance for some of our employees. And that was not anticipated.

Ellen Wilson - Sanford Bernstein - Analyst

Okay. And then a follow on to that, thinking about the '06 guidance or the 15% growth off of '05; is that off of \$3.93, or is that actually off of something higher, given that there were a number of things that in my mind were kind of one-time this year, that would have pulled down the number to \$3.93, the core being something higher?

Dave Colby - WellPoint, Inc. - EVP and CFO

We will go through the more detailed guidance at our investor day. But we have spiked out, clearly some one-time items like a favorable tax benefit that we incurred earlier in the year, the multi district litigation, and realized gains and losses, which we normally exclude from our 15% target.

Operator

Thank you. And we do have a question then from the line of Christine Arnold with Morgan Stanley. Please go ahead.

Christine Arnold - WellPoint, Inc. - Morgan Stanley

Good morning. Two questions. First, could you give us a sense for the impact of kind of the one-time costs this year that you are bearing with incentive compensations and the merger stay bonuses that will gone next year. And then secondly, can you give us a sense for your Med Supp HIJ membership and drug card membership that will be impacted by the PDP? Thanks.

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Dave Colby - WellPoint, Inc. - EVP and CFO

I guess to answer the first question, we have talked a little bit about over \$100 million in 2005 in merger related, one-time costs, although, I hate to call them one-time because some of them will continue on into 2006. And, again, we'll go through that in our Investor Day in December. The expenses associated with the IBM contracting, was a little bit over \$20 million in the quarter. Plus, don't forget, we did incur year-to-date, as part of the multi district litigation, about \$68 million of G&A costs are included in 2005. In terms of the Medicare Part D, I think Joan can respond.

Joan Herman - WellPoint, Inc. - President and CEO of Specialty, Senior and State-Sponsored Business

Sure. Hi. About 25% of our Med Supp block, it's about 230,000 members, have drug benefits. About 16% of those are actually HI&J. The rest is prestandardization. And actually a lot of that prestandardization block is what would be considered credible coverage. So, the Med Supp members actually have the option with those plans to just stay with what they've got and not have to worry about a late entrance penalty. So, there are a chunk that have HI&J. Obviously, some of those may stay with what they've got. We think that those who do choose to make the change are likely to stay with us. And we will give them that choice.

Operator

Thank you. And we do have a question from the line of Patrick Hojlo with CSFB.

Patrick Hojlo - Credit Suisse First Boston - Analyst

Following up on the G&A issue. It sounds like if I'm reading my notes right you slightly upped our Part D spending. Is that a reaction to the amount of traffic you are seeing at your call centers for this product? That's my first question.

Joan Herman - WellPoint, Inc. - President and CEO of Specialty, Senior and State-Sponsored Business

Yes. Part of that is that the number of auto enrolls that we now expect to get. We have a better handle on that because we know we were below the benchmark in every region, which is different than where we were in second quarter. So, we've got all of the enrollment materials that have to go out to those people in the fourth quarter, in advance of the 1/1 effective date. In addition, obviously, yes, there's probably more phone traffic than we might have originally thought, just given everything that's going on in the marketplace. There's even more call volume, so yes, there is that increase in cost.

Patrick Hojlo - Credit Suisse First Boston - Analyst

Any comment on what you expect to see in terms of switching among the dual eligibles and how you're going to deal with that?

Joan Herman - WellPoint, Inc. - President and CEO of Specialty, Senior and State-Sponsored Business

I think actually, we think that because we have such a strong brand and we think that coupled with a good offering, that we would expect that we have very good persistency among those auto assigns because they will get a brand that they know and they trust and I think that will make them very comfortable. So, we would expect a high retention rate on that.

Larry Glasscock - WellPoint, Inc. - President and CEO, Director

And we just follow up with the guidance now, having about \$40 million of Medicare Part D start-up as opposed to 30 million. So about a \$10 million increase from last quarter.

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Operator

Thank you very much. And we do have a question now from the line of Scott Fidel with J.P. Morgan. Please go ahead.

Scott Fidel - J.P. Morgan - Analyst

Thank you. The question just had to do with your consumer-driven plans. And first if you could give us an update of how much enrollment you had there? And then also maybe discuss some of the relative differential and the cost trends you might be seeing in the Lumenos book as compared to your aggregate cost trends? And maybe some differences in terms of specific utilization areas?

John Watts - WellPoint, Inc. - President and CEO National Accounts

We currently have approximately 434,000 members in CDHP products. That's as of September 30 of this year. And we obviously continue to see significant interest in CDHP. About 60% to 70% of our bid activity for National Accounts for 1/1/06 was driven by CDHP interests. We still, though, continue to see the uptick, or the adoption of CDHP business at the employer level, trail the interest by a significant amount. We expect that gap to close next year and beyond. But at this point, we will still see a gap between the interest and the adoption. The second part of your question again was?

Scott Fidel - J.P. Morgan - Analyst

Relating to relative variations in cost trends between consumer driven products and conventional products?

John Watts - WellPoint, Inc. - President and CEO National Accounts

We don't have a specific number for you on this call. But we do, in fact, believe that bringing consumers more into the process, bringing more consumer skin to the game will, in fact, drive reduced utilization over time. I think that's something that we can spike out a little bit more at the Investor Day in December. But we do believe that giving consumer tools and information will, in fact, lower healthcare costs over time.

Larry Glasscock - WellPoint, Inc. - President and CEO, Director

Scott, we'll have quite a lot of detail on consumer-directed when we get together on the Investor Day. So hopefully we'll see you there.

Operator

Thank you. And we do have a question from the line of Michael Baker with Raymond James. Please go ahead.

Michael Baker - Raymond James - Analyst

Yes, John, I was wondering if you could provide us a sense of the uptake this selling season in Specialty services?

John Watts - WellPoint, Inc. - President and CEO National Accounts

Yes, we actually had a pretty strong uptake, especially among our pharmacy business. We had in excess of 50% of our new national account business purchased pharmacy from our PBM. So that's -- we think that's a pretty strong indicator of the competitiveness and product offerings out of the WellPoint Pharmacy Benefit Manager. We also had pretty strong activity in our dental lines of business. And I expect to see that trend continue in the future.

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Michael Baker - Raymond James - Analyst

And then secondly, are you seeing any shift in terms of what's important to the customer - - the prospect when making a selection. I know you mentioned expecting consumer-directed to be more important in 2006. Any other factors?

John Watts - WellPoint, Inc. - President and CEO National Accounts

Well, I think first and foremost, the overriding concern on the part of the employer is the continued escalation in cost. So, it really all comes down to costs at the employer level. But certainly consumer-directed products and services is driving a lot of the activity. Care management programs like our concierge product and other products that help members when they are accessing the healthcare system. And then I think we continue to see growing interest at the National Account level in programs that actually are focused on keeping people healthy. So, these are wellness programs, the traditional wellness programs along with products like our In-Tune product that really help, through incentives, drive healthier behaviors on the part of our members.

Operator

We do have a question then from the line of Carl McDonald with CIBC.

Carl McDonald - CIBC World Markets - Analyst

Could you give us an update on the Medicaid business and a sense in terms of how medical loss ratio looked sequentially and year-over-year?

Dave Colby - WellPoint, Inc. - EVP and CFO

Our Medicaid or state-sponsored program business has been very consistent. We have not seen much fluctuation in terms of the profitability there, as we see with some of the more standalone companies. I think it's part of the fact that we have been doing it for a long time in state-sponsored programs.

Larry Glasscock - WellPoint, Inc. - President and CEO, Director

I think just to add to that, we are - - as you know we don't report cost trends by business type. So that's not information that we have out there. But the trends we are seeing for this line of business are very much in line with what we are experiencing in our commercial line. So there isn't a big difference there. Remember, Medicaid is about 6% of our total membership. We're a very diversified Company, we think that's important. So our performance here, we have been pleased with.

Operator

Great thank you very much and we do have a question from the line of Joseph France with Bank of America Securities.

Joe France - Bank of America Securities - Analyst

Thank you, David. If I understand you are picking up the Magellan business in October 1 and that's like 1.8 million lives. What is the revenue impact for this year and next year and what is the impact on earnings?

Dave Colby - WellPoint, Inc. - EVP and CFO

I don't have that exact number, Joe. We can see if we can get it. In terms of the membership number, you have the correct number. And we have other members that continue to be outsourced. Our goal over time is obviously to bring those into our in-house operation as well. But I do not have that number available.

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Joe France - Bank of America Securities - Analyst

But it is okay for me to circle back and get it later with Tami or someone?

Dave Colby - WellPoint, Inc. - EVP and CFO

No, I don't know that we can - -.

Joe France - Bank of America Securities - Analyst

You are not going to release it.

Dave Colby - WellPoint, Inc. - EVP and CFO

We will try to provide maybe a little bit more clarity at our Investor Day.

Joe France - Bank of America Securities - Analyst

Thanks, Larry.

Operator

Thank you and our final question comes from the line of James Lane with North Star Investments. Please go ahead. Sir, your line is open. We are unable to hear your question if you are speaking. And hearing no question then, I would now like to turn the conference back to Larry Glasscock with the Company for closing comments.

Larry Glasscock - WellPoint, Inc. - President and CEO, Director

Okay. Thank you very much. And it's been almost 11 months since we merged Anthem and WellPoint Health networks, forming sort of the new WellPoint. And during this period, we have truly become one Company, one team. We're achieving our strong results by really putting our customer first, by providing high value products, delivering quality service and then remaining very focused on reducing our administrative costs. We're obviously pleased with our performance to date and we remain very optimistic about our future.

As we noted earlier, we're going to hold our annual Investor Day in New York City on Tuesday, December 6. We're going to do that at Gotham Hall. We hope we'll see many of you there. For those of you that cannot attend in person, it will be Webcast. So we'll look forward very much to that day. Again, I want to thank you all for your interest. And as always, I hope you have a great day.

Operator

Thank you. And ladies and gentlemen, this conference will be available for replay starting today, Wednesday, October 26 at 1:45 p.m. Central Time and it will be available through Wednesday November 9 at midnight Central Time. And you may access the AT&T executive playback service by dialing 1-800-475-6701 from within the United States or Canada. Or from outside the United States or Canada, please dial 320-365-3844 and then enter the access of 779659. Those numbers once again, are 1-800-475-6701 from within the United States or Canada, or 320-365-3844 from outside the U.S. or Canada. And, again, enter the access code of 779659. And that does conclude our conference for today. Thank you for your participation and for using AT&T's executive teleconference. You may now disconnect.

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