

# Consolidated Statements of Earnings

Aflac Incorporated and Subsidiaries

(In millions, except for share and per-share amounts) Years Ended December 31,

|   | 2004      | 2003     | 2002     |
|---|-----------|----------|----------|
| <b>Revenues:</b>  |           |          |          |
| Premiums, principally supplemental health insurance                       | \$ 11,302 | \$ 9,921 | \$ 8,595 |
| Net investment income   | 1,957     | 1,787    | 1,614    |
| Realized investment gains (losses)  | (12)      | (301)    | (14)     |
| Other income  | 34        | 40       | 62       |
| Total revenues  | 13,281    | 11,447   | 10,257   |
| <b>Benefits and expenses:</b>   |           |          |          |
| Benefits and claims   | 8,482     | 7,529    | 6,589    |
| Acquisition and operating expenses:                                       |           |          |          |
| Amortization of deferred policy acquisition costs                         | 519       | 464      | 385      |
| Insurance commissions   | 1,252     | 1,146    | 1,037    |
| Insurance expenses  | 1,098     | 982      | 842      |
| Interest expense  | 23        | 22       | 20       |
| Japanese policyholder protection fund provision                           | —         | —        | 40       |
| Other operating expenses  | 100       | 79       | 85       |
| Total acquisition and operating expenses                                  | 2,992     | 2,693    | 2,409    |
| Total benefits and expenses   | 11,474    | 10,222   | 8,998    |
| Earnings before income taxes  | 1,807     | 1,225    | 1,259    |
| <b>Income tax expense:</b>  |           |          |          |
| Current   | 391       | 212      | 353      |
| Deferred  | 245       | 218      | 85       |
| Release of valuation allowance on deferred tax assets                     | (128)     | —        | —        |
| Total income taxes  | 508       | 430      | 438      |
| Net earnings  | \$ 1,299  | \$ 795   | \$ 821   |
| <b>Net earnings per share:</b>  |           |          |          |
| Basic   | \$ 2.56   | \$ 1.55  | \$ 1.59  |
| Diluted   | 2.52      | 1.52     | 1.55     |
| <b>Common shares used in computing earnings per share (In thousands):</b> |           |          |          |
| Basic   | 507,333   | 513,220  | 517,541  |
| Diluted   | 516,421   | 522,138  | 528,326  |

See the accompanying Notes to the Consolidated Financial Statements.

# Consolidated Balance Sheets

(In millions, except for share and per-share amounts) December 31,

Aflac Incorporated and Subsidiaries

2004

2003

## Assets:

Investments and cash:

Securities available for sale, at fair value:

Fixed maturities (amortized cost \$26,138 in 2004 and \$23,686 in 2003)

\$ 29,166 \$ 26,495

Perpetual debentures (amortized cost \$3,952 in 2004 and \$3,280 in 2003)

4,019 3,349

Equity securities (cost \$34 in 2004 and \$33 in 2003)

77 73

Securities held to maturity, at amortized cost:

Fixed maturities (fair value \$10,522 in 2004 and \$9,263 in 2003)

10,080 8,752

Perpetual debentures (fair value \$4,924 in 2004 and \$4,412 in 2003)

4,759 4,297

Other investments

41 32

Cash and cash equivalents

3,813 1,052

Total investments and cash

51,955 44,050

Receivables, primarily premiums

417 547

Accrued investment income

495 456

Deferred policy acquisition costs

5,595 5,044

Property and equipment, at cost less accumulated depreciation

515 518

Other

349 349

Total assets

\$ 59,326 \$ 50,964

## Liabilities and shareholders' equity:

Liabilities:

Policy liabilities:

Future policy benefits

\$ 39,360 \$ 35,588

Unpaid policy claims

2,355 2,115

Unearned premiums

593 516

Other policyholders' funds

1,248 1,021

Total policy liabilities

43,556 39,240

Notes payable

1,429 1,409

Income taxes

2,583 2,189

Payables for return of cash collateral on loaned securities

2,887 374

Other

1,298 1,106

Commitments and contingent liabilities (Notes 10 and 11)

Total liabilities

51,753 44,318

Shareholders' equity:

Common stock of \$.10 par value. In thousands: authorized 1,000,000 shares;

issued 652,628 shares in 2004 and 651,554 shares in 2003

65 65

Additional paid-in capital

468 417

Retained earnings

6,992 5,885

Accumulated other comprehensive income:

Unrealized foreign currency translation gains

220 213

Unrealized gains on investment securities

2,417 2,316

Minimum pension liability adjustment

(28) (36)

Treasury stock, at average cost

(2,561) (2,214)

Total shareholders' equity

7,573 6,646

Total liabilities and shareholders' equity

\$ 59,326 \$ 50,964

See the accompanying Notes to the Consolidated Financial Statements.

# Consolidated Statements of Shareholders' Equity

Aflac Incorporated and Subsidiaries

(In millions, except for per-share amounts) Years Ended December 31,

2004

2003

2002

## Common stock:

|                                    |       |       |       |
|------------------------------------|-------|-------|-------|
| Balance, beginning and end of year | \$ 65 | \$ 65 | \$ 65 |
|------------------------------------|-------|-------|-------|

## Additional paid-in capital:

|  |     |     |     |
|--|-----|-----|-----|
| Balance, beginning of year                               | 417 | 371 | 338 |
| Exercise of stock options, including income tax benefits | 15  | 19  | 11  |
| Gain on treasury stock reissued                          | 36  | 27  | 22  |
| Balance, end of year                                     | 468 | 417 | 371 |

## Retained earnings:

|   |       |       |       |
|---|-------|-------|-------|
| Balance, beginning of year  | 5,885 | 5,244 | 4,542 |
| Net earnings  | 1,299 | 795   | 821   |
| Dividends to shareholders (\$.38 per share in 2004, \$.30 per share in 2003, and \$.23 per share in 2002) | (192) | (154) | (119) |
| Balance, end of year  | 6,992 | 5,885 | 5,244 |

## Accumulated other comprehensive income:

|   |       |       |       |
|---|-------|-------|-------|
| Balance, beginning of year  | 2,493 | 2,630 | 2,091 |
| Change in unrealized foreign currency translation gains (losses) during year, net of income taxes | 7     | (9)   | 9     |
| Change in unrealized gains (losses) on investment securities during year, net of income taxes     | 101   | (100) | 538   |
| Minimum pension liability adjustment during year, net of income taxes                             | 8     | (28)  | (8)   |
| Balance, end of year  | 2,609 | 2,493 | 2,630 |

## Treasury stock:

|                             |          |          |          |
|-----------------------------|----------|----------|----------|
| Balance, beginning of year  | (2,214)  | (1,916)  | (1,611)  |
| Purchases of treasury stock | (392)    | (343)    | (346)    |
| Cost of shares issued       | 45       | 45       | 41       |
| Balance, end of year        | (2,561)  | (2,214)  | (1,916)  |
| Total shareholders' equity  | \$ 7,573 | \$ 6,646 | \$ 6,394 |

See the accompanying Notes to the Consolidated Financial Statements.

# Consolidated Statements of Cash Flows

Aflac Incorporated and Subsidiaries

(In millions) Years Ended December 31,

|   | 2004     | 2003     | 2002     |
|---|----------|----------|----------|
| <b>Cash flows from operating activities:</b>  |          |          |          |
| Net earnings  | \$ 1,299 | \$ 795   | \$ 821   |
| Adjustments to reconcile net earnings to net cash provided by operating activities: |          |          |          |
| Change in receivables and advance premiums  | 159      | (86)     | (11)     |
| Increase in deferred policy acquisition costs                                       | (443)    | (408)    | (372)    |
| Increase in policy liabilities  | 3,023    | 2,641    | 2,385    |
| Change in income tax liabilities  | 347      | 83       | 67       |
| Realized investment losses  | 12       | 301      | 14       |
| Japanese policyholder protection fund provision                                     | —        | —        | 40       |
| Other, net  | 89       | 63       | 94       |
| Net cash provided by operating activities   | 4,486    | 3,389    | 3,038    |
| <b>Cash flows from investing activities:</b>  |          |          |          |
| Proceeds from investments sold or matured:  |          |          |          |
| Securities available for sale:  |          |          |          |
| Fixed maturities sold   | 1,481    | 1,908    | 1,729    |
| Fixed maturities matured  | 820      | 1,458    | 1,188    |
| Perpetual debentures sold   | —        | 131      | —        |
| Equity securities   | —        | 223      | 69       |
| Securities held to maturity:  |          |          |          |
| Fixed maturities matured or called  | 1        | 1        | 240      |
| Costs of investments acquired:  |          |          |          |
| Securities available for sale:  |          |          |          |
| Fixed maturities  | (3,914)  | (5,059)  | (3,057)  |
| Perpetual debentures  | (464)    | (288)    | —        |
| Equity securities   | (1)      | (3)      | (130)    |
| Securities held to maturity:  |          |          |          |
| Fixed maturities  | (1,468)  | (947)    | (2,619)  |
| Perpetual debentures  | (358)    | (170)    | (136)    |
| Cash received as collateral on loaned securities, net                               | 2,512    | (727)    | 485      |
| Additions to property and equipment, net  | (21)     | (21)     | (25)     |
| Other, net  | (6)      | (6)      | (18)     |
| Net cash used by investing activities   | (1,418)  | (3,500)  | (2,274)  |
| <b>Cash flows from financing activities:</b>  |          |          |          |
| Proceeds from borrowings  | —        | —        | 254      |
| Principal payments under debt obligations   | (12)     | (20)     | (234)    |
| Change in investment-type contracts, net  | 220      | 159      | 74       |
| Dividends paid to shareholders  | (182)    | (146)    | (112)    |
| Purchases of treasury stock   | (392)    | (343)    | (346)    |
| Treasury stock reissued   | 39       | 33       | 35       |
| Other, net  | 14       | 19       | 9        |
| Net cash used by financing activities   | (313)    | (298)    | (320)    |
| Effect of exchange rate changes on cash and cash equivalents                        | 6        | 82       | 83       |
| Net change in cash and cash equivalents   | 2,761    | (327)    | 527      |
| Cash and cash equivalents, beginning of year  | 1,052    | 1,379    | 852      |
| Cash and cash equivalents, end of year  | \$ 3,813 | \$ 1,052 | \$ 1,379 |

## Supplemental disclosures of cash flow information - See Note 12

See the accompanying Notes to the Consolidated Financial Statements.

# Consolidated Statements of Comprehensive Income

Aflac Incorporated and Subsidiaries

(In millions) Years Ended December 31,

|  | 2004     | 2003   | 2002     |
|--|----------|--------|----------|
| Net earnings   | \$ 1,299 | \$ 795 | \$ 821   |
| Other comprehensive income (loss) before income taxes:                             |          |        |          |
| Foreign currency translation adjustments:  |          |        |          |
| Change in unrealized foreign currency translation gains (losses) during year       | (24)     | (121)  | (72)     |
| Unrealized gains (losses) on investment securities:                                |          |        |          |
| Unrealized holding gains (losses) arising during year                              | 143      | (604)  | 763      |
| Reclassification adjustment for realized (gains) losses included in net earnings   | 13       | 301    | 13       |
| Minimum pension liability adjustment during year                                   | 13       | (40)   | (8)      |
| Total other comprehensive income (loss) before income taxes                        | 145      | (464)  | 696      |
| Income tax expense (benefit) related to items of other comprehensive income (loss) | 28       | (327)  | 157      |
| Other comprehensive income (loss) net of income taxes                              | 117      | (137)  | 539      |
| Total comprehensive income   | \$ 1,416 | \$ 658 | \$ 1,360 |

See the accompanying Notes to the Consolidated Financial Statements.

## Notes to the Consolidated Financial Statements

### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Description of Business:** Aflac Incorporated (the Parent Company) and its subsidiaries (the Company) primarily sell supplemental health and life insurance in the United States and Japan. The Company's insurance operations are conducted through American Family Life Assurance Company of Columbus (Aflac), which operates in the United States (Aflac U.S.) and as a branch in Japan (Aflac Japan). Most of Aflac's policies are individually underwritten and marketed through independent agents. Aflac Japan, which conducts its insurance operations in Japanese yen, accounted for 75% of the Company's total revenues in 2004, 74% in 2003 and 75% in 2002, and 80% of total assets at December 31, 2004, and 84% in 2003.

**Basis of Presentation:** We prepare our financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP). These principles are established primarily by the Financial Accounting Standards Board (FASB) and the American Institute of Certified Public Accountants. The preparation of financial statements in conformity with GAAP requires us to make estimates when recording transactions resulting from business operations based on currently available information. The most significant

items on our balance sheet that involve a greater degree of accounting estimates and actuarial determinations subject to changes in the future are the valuation of investments, deferred policy acquisition costs, and liabilities for future policy benefits and unpaid policy claims. These accounting estimates and actuarial determinations are sensitive to market conditions, investment yields, mortality, morbidity, commission and other acquisition expenses, and terminations by policyholders. As additional information becomes available, or actual amounts are determinable, the recorded estimates will be revised and reflected in operating results. Although some variability is inherent in these estimates, we believe the amounts provided are adequate.

The consolidated financial statements include the accounts of the Parent Company, its majority owned subsidiaries and those entities required to be consolidated under applicable accounting standards. All material intercompany accounts and transactions have been eliminated.

**Translation of Foreign Currencies:** The functional currency of Aflac Japan's insurance operations is the Japanese yen. We translate financial statement accounts that are maintained in foreign currencies into U.S. dollars as follows. Assets and liabilities denominated in foreign currencies are translated at end-of-period exchange rates. Realized gains and losses on