



Legal Division  
Lisa T. Murphy  
Director, Corporate Legal Services  
& Senior Associate General Counsel  
(503) 225-4879 Voice  
(503) 225-5431 Facsimile  
lisa.murphy@cambiahealth.com

Reply to:  
P.O. Box 1271 (M/S E12B)  
Portland, OR 97207-1271

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APR 29 2013

INSURANCE COMMISSIONER  
COMPANY SUPERVISION

Via Overnight Courier

April 26, 2013

Mr. Sukalyan Ghosh, CFE  
Insurance Financial Analyst  
Financial Regulation Section - 4  
Department of Consumer and  
Business Services  
350 Winter Street, N.E., Room 440  
Salem, OR 97309-0405

Mr. Cliff Larson  
Senior Financial Analyst Supervisor  
Idaho Department of Insurance  
700 W. State Street, 3rd Floor  
Boise, ID 83720

Mr. Daniel Applegarth  
Assistant Chief Examiner  
Utah State Insurance Department  
State Office Building, Room 3110  
Salt Lake City, UT 84114

Mr. Ronald J. Pastuch  
Holding Company Manager  
Company Supervision Division  
Office of Insurance Commissioner  
5000 Capitol Boulevard  
Tumwater, WA 98501

Re: 2012 Annual Holding Company Statement

Dear Mr. Ghosh, Mr. Larson, Mr. Applegarth, and Mr. Pastuch:

On behalf of Cambia Health Solutions, Inc. and the affiliated insurers within its holding company system, enclosed are two copies each of the consolidated Cambia annual holding company registration for 2012.

Please let me know if you have any questions.

Sincerely,

LISA T. MURPHY  
Director, Corporate Legal Services  
& Senior Associate General Counsel

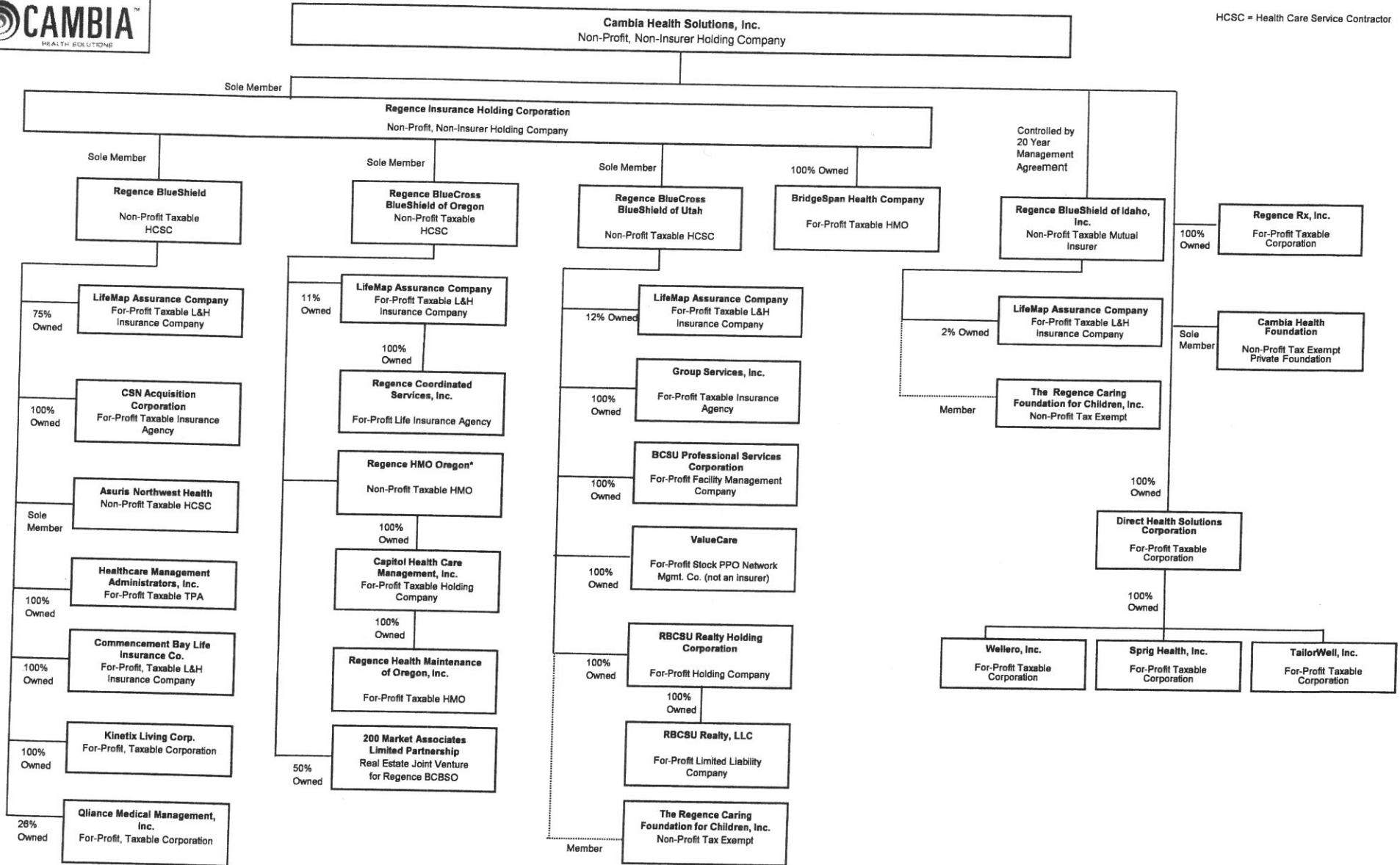
cc: Kerry E. Barnett

Enclosures

100 SW Market Street, P.O. Box 1271, Portland, OR 97207-1271



HCSC = Health Care Service Contractor



CAMBIA HEALTH SOLUTIONS, INC. – 2012  
Holding Company Annual Registration  
EXHIBIT B – Organizational Chart

**Exhibit C**

**Cambia Health Solutions, Inc. Officers**

**Mark B. Ganz**  
President & Chief Executive Officer

**Kerry E. Barnett**  
Corporate Secretary; Executive Vice  
President, Corporate Services &  
Chief Legal Officer

**Andreas B. Ellis**  
Vice President & Corporate Treasurer

**Lisa T. Murphy**  
Assistant Secretary

**Jared L. Short**  
Division President,  
Health Insurance Services

**Steven J. Gaspar**  
Senior Vice President &  
Chief Actuarial Officer

**Vince P. Price**  
Executive Vice President, Finance &  
Chief Financial Officer

**John J. Cimral**  
Senior Vice President,  
Chief Information Officer

**Margaret M. Maguire**  
Senior Vice President, Chief of Staff

**Mohandas Nair**  
Chief Innovation Officer

**Exhibit C**

**Cambia Health Solutions, Inc. Directors**

**Mark C. Adams, M.D.**

**Paula A. Jones**  
President & CEO,  
P.A. Banks Enterprises, Inc.

**S. Fred Beck**  
CFO, ICON Health & Fitness, Inc.

**Cynthia A. Bioteau, Ph.D.**  
President & CEO  
Salt Lake Community College

**Gregory L. Charlton**  
Senior Vice President  
Idaho Independent Bank

**William L. Chenevich**  
Vice Chairman, US Bank

**Peggy Y. Fowler**  
Retired, President & CEO  
Portland General Electric

**Mark B. Ganz**  
President & CEO  
Cambia Health Solutions, Inc.

**Mack L. Hogans, Vice Chair**  
CEO, M.L. Hogans, LLC Consulting  
Services & Executive Director Puget  
Sound BOLD Initiative

**Michael G. Koppel**  
EVP & CFO  
Nordstrom, Inc.

**Katharine G. Lindemann**  
SVP, Savers, Inc.

**Luis Machuca**  
CEO, Kryptiq Corporation

**D. Kurt Seppi, M.D.**  
St. Luke's Magic Valley Medical Center

**Jack G. Strother, Chair**  
Attorney-at-Law  
Graham & Dunn

**Elliott J. Hill**  
Vice President and General Manager,  
Nike North America, Nike, Inc.

**John W. Morgan**  
Chief Executive Officer  
Avamere Family of Companies



**Consolidated Financial Statements**

**December 31, 2012 and 2011**

(With Independent Auditors' Report)

An Independent Licensee of the Blue Cross and Blue Shield Association.

CAMBIA HEALTH SOLUTIONS, INC.

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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors of  
Cambia Health Solutions, Inc.  
Portland, Oregon

We have audited the accompanying consolidated financial statements of Cambia Health Solutions, Inc., its subsidiaries, and affiliates (the "Company"), which comprise the consolidated balance sheets as of December 31, 2012 and 2011, and the related consolidated statements of operations and comprehensive income, changes in surplus and accumulated other comprehensive income (loss), and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Cambia Health Solutions, Inc. and its subsidiaries and affiliates as of December 31, 2012 and 2011, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## Report on Supplemental Schedules

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary information listed in the table of contents is presented for the purpose of additional analysis and is not a required part of the consolidated financial statements. This supplementary information is the responsibility of the Company's management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. Such information has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, such information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

*Debitte Touche LLP*

April 4, 2013



**CAMBIA HEALTH SOLUTIONS, INC.**  
**Consolidated Balance Sheets**  
**December 31, 2012 and 2011**  
(In thousands)

<u>ASSETS</u>	<u>2012</u>	<u>2011</u>
Cash and Cash Equivalents	\$ 286,401	\$ 306,309
Receivables, net	800,380	907,704
Investments	2,842,661	2,639,753
Property, Buildings and Equipment, net	367,894	379,549
Other Assets	156,811	160,252
Deferred Compensation Assets	<u>48,289</u>	<u>48,276</u>
Total Assets	<u>\$ 4,502,436</u>	<u>\$ 4,441,843</u>

(Continued)

**CAMBIA HEALTH SOLUTIONS, INC.**

**Consolidated Balance Sheets**

**December 31, 2012 and 2011**

(In thousands)

<u>LIABILITIES AND SURPLUS</u>	<u>2012</u>	<u>2011</u>
Liabilities:		
Reserve for Unpaid Claims	\$ 846,075	\$ 993,509
Reserve for Adjusting Expenses on Unpaid Claims	25,547	27,205
Unearned Premiums	334,701	353,037
Debt and Other Obligations	107,932	119,303
Accrued Expenses and Other Liabilities	337,800	323,187
Experience Refunds Payable	36,753	32,578
Deferred Compensation	48,289	48,276
Pension and Postretirement Obligations	120,080	132,258
Deferred Income Taxes	32,367	12,079
Total Liabilities	<u>1,889,544</u>	<u>2,041,432</u>
Commitments and Contingencies (Note 14)		
Surplus:		
Accumulated Surplus	2,560,994	2,387,242
Accumulated Other Comprehensive Income	51,898	13,169
Total Surplus	<u>2,612,892</u>	<u>2,400,411</u>
Total Liabilities and Surplus	<u>\$ 4,502,436</u>	<u>\$ 4,441,843</u>

(Concluded)

See accompanying notes to consolidated financial statements.

**CAMBIA HEALTH SOLUTIONS, INC.**  
**Consolidated Statements of Operations and Comprehensive Income**  
**Years Ended December 31, 2012 and 2011**  
(In thousands)

	2012	2011*
Premium Revenue	\$ 5,761,435	\$ 5,861,869
Self-funded Revenue	1,957,093	1,952,935
Fee Revenue	98,383	100,355
Gross Revenue	7,816,911	7,915,159
Less Amounts Attributable to Claims Under Self-funded Arrangements	1,839,702	1,834,545
Commissions Expense	124,114	135,839
Premium Taxes	54,971	54,475
Net Premium, Self-funded, and Fee Revenue	5,798,124	5,890,300
Claims Expense	4,816,351	5,070,766
Operating Expense	875,519	824,213
Gain on Sale of Real Estate	(2,041)	(36,902)
Operating Income	108,295	32,223
Investment Income, net	151,519	120,327
Interest Expense	(4,891)	(5,363)
Other Expense, net	(4,924)	(6,759)
Uninsurable Pool Assessments	(32,026)	(26,854)
Income Before Income Taxes	217,973	113,574
Income Tax Expense	44,221	24,318
Net Income	173,752	89,256
Other Comprehensive Income, net of tax:		
Unrealized Gain (Loss) on Investments	47,735	(15,820)
Periodic Pension and Postretirement Cost	(9,006)	(57,544)
Other Comprehensive Income (Loss)	38,729	(73,364)
Comprehensive Income	\$ 212,481	\$ 15,892

\*See Note 18

See accompanying notes to consolidated financial statements

**CAMBIA HEALTH SOLUTIONS, INC.**  
**Consolidated Statements of Changes in Surplus and Accumulated Other Comprehensive Income**  
**Years Ended December 31, 2012 and 2011**

(In thousands)

	Accumulated Surplus	Accumulated Other Comprehensive Income	Total
Balance at January 1, 2011	\$ 2,297,986	\$ 86,533	\$ 2,384,519
Net Income	89,256	-	89,256
Other Comprehensive Loss	-	(73,364)	(73,364)
Balance at December 31, 2011	\$ 2,387,242	\$ 13,169	\$ 2,400,411
Net Income	173,752	-	173,752
Other Comprehensive Income	-	38,729	38,729
Balance at December 31, 2012	<u>\$ 2,560,994</u>	<u>\$ 51,898</u>	<u>\$ 2,612,892</u>

See accompanying notes to consolidated financial statements.

**CAMBIA HEALTH SOLUTIONS, INC.**  
**Consolidated Statements of Cash Flows**  
**Years Ended December 31, 2012 and 2011**  
(In thousands)

	2012	2011
<b>Cash Flows From Operating Activities:</b>		
Net Income	\$ 173,752	\$ 89,256
Adjustments to Reconcile Net Income to Net Cash		
Provided by Operating Activities:		
Depreciation and Amortization	71,491	78,247
Impairment of Long-Lived Assets	-	5,849
Deferred Income Taxes	11,185	8,222
Amortization of Bond Premium, net	14,121	10,073
Net Realized Gains on Investments	(68,941)	(31,442)
Net Losses (Gains) on Sales of Property, Buildings and Equipment	2,253	(34,868)
Changes In:		
Receivables, net	106,866	(105,234)
Other Assets	(788)	3,287
Reserve for Unpaid Claims	(147,434)	108,156
Reserve for Adjusting Expenses on Unpaid Claims	(1,658)	4,211
Unearned Premiums	(18,336)	71,229
Accrued Expenses and Other Liabilities	8,520	14,587
Experience Refunds Payable	4,175	(6,888)
Pension and Postretirement Obligations	(23,872)	(42,114)
Net Cash Provided by Operating Activities	\$ 131,334	\$ 172,571
<b>Cash Flows From Investing Activities:</b>		
Proceeds from Sales and Maturities of Investments	1,899,844	1,569,073
Purchases of Investments	(1,997,292)	(1,683,354)
Proceeds from Sales of Property, Buildings and Equipment	5,042	76,114
Purchases of Property, Buildings and Equipment	(32,626)	(59,845)
Net Cash Used in Investing Activities	\$ (125,032)	\$ (98,012)

(Continued)

**CAMBIA HEALTH SOLUTIONS, INC.**  
**Consolidated Statements of Cash Flows**  
**Years Ended December 31, 2012 and 2011**  
(In thousands)

	2012	2011
<b>Cash Flows From Financing Activities:</b>		
Proceeds from Debt and Other Obligations	\$ -	\$ 10,000
Repayments of Debt and Other Obligations	(26,210)	(36,264)
Net Cash Used in Financing Activities	\$ (26,210)	\$ (26,264)
Net (Decrease) Increase in Cash and Cash Equivalents	(19,908)	48,295
Cash and Cash Equivalents at Beginning of Year	306,309	258,014
Cash and Cash Equivalents at End of Year	\$ 286,401	\$ 306,309
<b>Non-Cash Investing and Financing Activities:</b>		
Purchases of Property, Buildings and Equipment Financed Through Capital Lease Obligations	\$ 14,839	\$ 5,390
Purchases of Property, Buildings and Equipment Financed Through Incurrence of Accounts Payable	\$ 547	\$ 922
<b>Cash Paid for Taxes and Interest:</b>		
Cash Paid During the Year for Taxes	\$ 21,873	\$ 20,809
Cash Paid During the Year for Interest	\$ 4,781	\$ 4,897

(Concluded)

See accompany notes to consolidated financial statements.

**CAMBIA HEALTH SOLUTIONS, INC.**  
**Notes to Consolidated Financial Statements**  
**Years Ended December 31, 2012 and 2011**

1. NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**A. Business Organization** – Cambia Health Solutions (CHS), formerly known as The Regence Group, is incorporated as a nonprofit corporation under the laws of the State of Oregon. CHS is the sole member of Regence Insurance Holding Corporation (RIHC) and Direct Health Solutions Corporation (DHS). RIHC is the sole member of Regence BlueShield, Regence BlueCross BlueShield of Oregon, and Regence BlueCross BlueShield of Utah. CHS has established a long-term management services contract with Regence BlueShield of Idaho, Inc. CHS has control over the operations and management of Regence BlueShield, Regence BlueCross BlueShield of Oregon, Regence BlueCross BlueShield of Utah and Regence BlueShield of Idaho, Inc. (collectively, the Plans). CHS, its subsidiaries RIHC, DHS, Regence Rx, Inc. (Regence Rx) and Cambia Health Foundation (Foundation), as well as the Plans and their subsidiaries are collectively referred to as Cambia or the Company. Cambia is a health care services company that primarily provides hospital, medical, dental, pharmaceutical drug, life, and disability coverage to groups and individuals through insurance policies. Each of the Plans is subject to federal regulation of health and life insurance entities, as well as, by the insurance commissioners in the states in which they are licensed to sell insurance.

**B. Principles of Consolidation** – The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) and include the accounts of Regence BlueShield and its wholly owned subsidiaries (Regence BlueShield), Regence BlueCross BlueShield of Oregon and its wholly owned subsidiaries (Regence BCBSO), Regence BlueShield of Idaho, Inc., Regence BlueCross BlueShield of Utah and its wholly owned subsidiaries (Regence BCBSU), Regence Rx, Foundation, DHS, RIHC and CHS. All intercompany accounts and transactions have been eliminated.

**C. Use of Estimates** – The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could vary from those estimates.

**D. Cash and Cash Equivalents** – Cash equivalents consist of short-term, highly liquid investments with original maturities of three months or less at the date of acquisition. Cash equivalents of \$99,305,000 and \$153,107,000 are included within Cash and Cash Equivalents at December 31, 2012 and 2011, respectively.

**E. Concentration of Risk** – Cambia invests its excess cash in deposits with major banks, commercial paper, money market funds and government securities. Investments principally include U.S. Treasury securities, obligations of U.S. Government-sponsored agencies, loan-backed securities, corporate and other debt and equity securities. Deposits in accounts with a single financial institution

may exceed FDIC insured limits of \$250,000. Cambia uses multiple financial institutions to limit exposure to these risks.

**F. Receivables, net** – Receivables, net includes premiums due and accrued, reinsurance, income taxes and other miscellaneous receivables. At December 31, 2012 and 2011, Receivables, net also includes allowances for premium retroactivity and doubtful accounts of \$5,176,000 and \$6,674,000, respectively.

**G. Investments** – Investments consist of debt and equity securities categorized as available-for-sale. These investments are carried at fair value with unrealized gains and losses (net of tax) recorded as a separate component of surplus. The amortized cost of debt securities not backed by loans is adjusted for amortization of premiums and accretion of discounts to maturity. For asset-backed and residential and commercial mortgage-backed securities (collectively, loan-backed securities), premiums and discounts are amortized or accreted over the estimated life of the security. Such amortization and accretion, as well as interest income, is included in Investment Income, net. Realized gains and losses on the sale of investments are determined using the first-in, first-out method and are included in Investment Income, net.

Management periodically reviews Cambia's investments to determine whether declines in fair value below amortized cost are other-than-temporary. Relevant factors considered in the analysis include, but are not limited to, changes in fair value relative to market volatility, the extent and/or duration of impairment, price recovery trend, credit risk and concentration within Cambia's total holdings. Other criteria that may indicate an other-than-temporary impairment include declarations of bankruptcy by the issuer, significant downgrades in credit ratings and delinquent dividends or interest payments.

Upon determination that equity securities are other-than-temporarily impaired or that Cambia does not have the intent and ability to hold the securities until the fair value is recovered, permanent adjustments are made to the cost basis of the investment to reflect the impairment. Adjustments are included in Investment Income, net.

For debt securities, Cambia assesses whether it has the intent to sell or will more likely than not be required to sell the security prior to recovery of the amortized cost basis. If either condition is met, the full impairment is included in other-than-temporary impairment losses recognized in Investment Income, net. Otherwise, only the impairment resulting from credit deterioration is included in Investment Income, net. Impairment caused by all other factors is included in Other Comprehensive Income (Loss) (OCI). The credit component is determined by comparing the amortized cost basis to the net present value of expected future cash flows. Cash flow estimates for loan-backed securities are based on assumptions regarding the credit quality of the underlying collateral and prepayment timing. Cash flow estimates of corporate and other debt securities are driven by the probability of default or risk of an issuer declaring bankruptcy. U.S. Treasury securities have no significant credit risk as these investments would not likely be settled for less than amortized cost.

**H. Property, Buildings and Equipment, net** – Property, Buildings, and Equipment, net, are recorded at cost less accumulated depreciation. Depreciation is recorded on the straight-line basis over estimated useful lives of three to ten years for furniture and equipment, three to twelve years for



capitalized software, and up to fifty years for buildings and improvements. Leasehold improvements are amortized over the estimated useful life of the asset, not to exceed the life of the lease.

**I. Other Assets** – Other Assets includes investments accounted for under the equity method. Annually, management reviews these investments to determine whether declines in fair value below carrying value are other-than-temporary. The carrying value of the investment, and net income, are adjusted for the Company's proportionate share of the investee's gains and losses. These adjustments are included in Investment Income, net, on the Consolidated Statements of Operations and Comprehensive Income.

Also included in Other Assets are certain costs incurred in the development of internally-customized software not yet placed into service, prepaid expenses and other miscellaneous assets.

**J. Long-Lived Assets** – Management reviews long-lived assets, including capitalized internally-customized software, for impairment whenever events or circumstances indicate the carrying amount of an asset may not be recoverable. If there is an indication of impairment, management prepares an estimate of future cash flows (undiscounted and without interest charges) expected to result from the use of the asset and its eventual disposition. If these cash flows are less than the carrying amount of the asset, an impairment loss is recognized to write down the asset to its fair value. All long-lived assets to be disposed of by sale are carried at the lower of carrying amount or fair value less costs to sell, and no depreciation is recorded on these specifically identified assets. No long-lived asset impairment was recorded during the year ended December 31, 2012. During the year ended December 31, 2011 an impairment of \$5,849,000 was recorded in Operating Expense. (See Note 5)

**K. Underwriting Reserves** – The Reserves for Unpaid Claims and the Reserve for Adjusting Expenses on Unpaid Claims represent Cambia's estimate of future payments for services rendered as of each year end and an estimate of future expenses to process such claims. The reserves are actuarial estimates based upon historical claims experience modified for current trends and changes in benefit coverage; however, subsequent actual claim payments may differ from established estimates. Adjustments are included in current period earnings.

Premium Deficiency Reserves are accrued for anticipated losses on existing health care contracts when estimated future health care costs will exceed expected future premiums and recoveries for those contracts. Management's review has determined no premium deficiency reserves were necessary at December 31, 2012 or 2011.

**L. Experience Refunds Payable** – For certain customer contracts, Cambia recognizes balances for any excess of premiums over claims expense and retention charged. The Experience Refunds Payable represents excess customer payments and deposits under these contracts. As specified in each customer contract, these balances may be refunded or applied toward future premiums or claims.

**M. Income Taxes** – CHS and its sole member affiliates including Regence Rx, file a consolidated federal income tax return. Under tax sharing agreements, the affiliates pay to, or receive from CHS amounts by which the affiliates' federal income tax liability is affected by virtue of inclusion in the consolidated federal return.

Cambia accounts for income taxes under the asset and liability method, which reflects the tax effect of temporary differences between carrying amounts of assets and liabilities for financial reporting purposes. A valuation allowance is established for deferred tax assets if it is more likely than not that all or some portion of the deferred tax asset will not be realized. The effect of changes in the expected tax rates is recognized in income in the period that includes the enactment date. Cambia records net deferred tax assets to the extent it believes these assets are more likely than not to be realized. In making this determination, Cambia considers all positive and negative evidence, including future reversals of existing taxable differences, projected future taxable income, tax planning strategies, existing inventory of Alternative Minimum Tax (AMT) credits, and recent financial operations.

**N. Comprehensive Income** – Comprehensive Income includes all changes in surplus (net of tax, where applicable) during the period, including Net Income, unrealized gains and losses on available-for-sale investments, and periodic pension and postretirement costs. OCI is reported net of reclassification adjustments for items included in net income, such as realized gains and losses on investments.

**O. Administrative Services Contracts** – Cambia has administrative services contracts with self-insured customers, under which the customers are at risk for all or a portion of their claims experience. Cambia charges these self-insured customers for administrative services rendered and for claims paid on behalf of the group. This administrative service charge and the claims reimbursement are recorded within Self-Funded Revenue and Amounts Attributable to Claims Under Self-Funded Arrangements, respectively, in the Consolidated Statements of Operations and Comprehensive Income.

Administrative Fee Deficiency Reserves are accrued for anticipated losses on existing health care contracts when estimated administrative fees will exceed expected future fees for those contracts. Administrative fee deficiency reserves included in accrued expenses and other liabilities were \$19,653,000 and \$2,234,000 at December 31, 2012 and 2011, respectively.

**P. Premium Revenue Recognition** – Premiums received for underwritten products are recognized as Premium Revenue over the period the insurance coverage is in effect. Premiums collected in advance of the period of coverage are recorded in Unearned Premiums on Cambia's Consolidated Balance Sheets.

Cambia also provides coverage for certain groups whose contracts provide for premiums based on group experience factors. Under these contracts, revenue is generally recorded on the basis of claims expense and retention charged. These contracts include maximum rates that may be charged, and losses can result if claims and retention exceed those rates. In certain instances, such losses may be collectible from specific groups, in which case the excess to be received is recognized in Premium Revenue, and included in Receivables, net. All other losses are recorded in the year incurred.

Cambia serves as a plan sponsor offering Medicare Advantage and Medicare Part D prescription drug insurance coverage under contracts with Centers for Medicare and Medicaid Services (CMS). CMS deploys a risk adjustment model that apportions premiums paid to all health plans according to health severity and certain demographic factors. The CMS risk adjustment model pays more for members whose medical history indicates they have certain medical conditions. Under this risk adjustment methodology, CMS calculates the risk adjusted premium payment using diagnosis data from hospital inpatient, hospital outpatient and physician treatment settings. Cambia and health care providers collect, capture, and submit

the necessary and available diagnosis data to CMS within prescribed deadlines. Cambia estimates risk adjustment revenues based upon the diagnosis data submitted to CMS.

In addition to premiums paid by CMS, all Medicare subscribers pay a fixed monthly premium to Cambia for the plan year. Premium revenues are recognized ratably over the period in which eligible subscribers are entitled to receive covered benefits. Cambia records premium payments received in advance of the applicable service period as Unearned Premiums.

**Q. Fee Revenue** – Cambia generates fee revenue by providing other administrative services to customers. These services may include claims and transaction processing and access to contracted provider networks. Under these contracts, Cambia recognizes revenue in the period the related services are performed.

**R. Commissions Expense and Other Insurance Contract Acquisition Costs** – Expenses incurred in connection with acquiring new insurance business, including acquisition costs such as sales commissions, are charged to expense as incurred due to the short term nature of Cambia's contracts.

**S. Fair Value of Financial Instruments** – Cambia reports all financial assets and liabilities and non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis in accordance with Accounting Standards Codification (ASC) 820 – *Fair Value Measurement*, which defines fair value as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 establishes a fair value hierarchy, which prioritizes the inputs and valuation techniques used to measure fair value into the following levels:

*Level 1.* Observable inputs that reflect quoted prices in active markets for identical assets or liabilities.

*Level 2.* Observable inputs other than quoted prices in active markets for identical assets and liabilities. These include quoted prices for similar assets or liabilities in less active or inactive markets or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

*Level 3.* Inputs that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability.

An instrument's classification is based on the lowest level of input that is significant to its measurement.

**T. New Accounting Pronouncements** –

In May 2011, the Financial Accounting Standards Board (FASB) issued new guidance on fair value measurement and disclosure requirements in order to achieve more commonality between GAAP and International Financial Reporting Standards. Effective for reporting years beginning after December 15, 2011, this guidance clarifies particular principles and requirements related to measuring fair value or disclosing information about fair value measurements and also provides clarification of the application of existing fair value measurement and disclosure requirements. Specifically, this guidance clarifies that the highest and best use concept only applies to the fair value of nonfinancial assets and updates certain principles related to the measuring of fair value of financial instruments managed in a portfolio and the

application of premiums and discounts in a fair value measurement. Adoption of these revisions for the year ended December 31, 2012 resulted in additional disclosures but did not have a material impact on Cambia's consolidated financial statements.

In June 2011, the FASB issued new guidance on the presentation of comprehensive income effective retrospectively for reporting periods ending after December 15, 2012 with an option to early adopt. Guidance requires that the components of comprehensive income be presented in either a single continuous statement of comprehensive income or two separate but consecutive statements. These revisions remove the previous option of presenting components of comprehensive income as part of Cambia's Consolidated Statements of Changes in Surplus and Accumulated Other Comprehensive Income. Cambia adopted the modifications for the year ended December 31, 2012.

In July 2011, the FASB issued new guidance for fees paid to the federal government by health insurers. This update affects health insurers subject to an annual fee imposed by the Patient Protection and Affordable Care Act as amended by the Health Care and Education Reconciliation Act (the Acts). Effective January 1, 2014, health insurers must pay an annual fee based on the ratio of the insurer's net premiums written to the total amount of health insurance written in the United States during the preceding year. This guidance requires a liability for the fee to be estimated and recorded at the beginning of the calendar year in which it is payable with a corresponding deferred cost that is subsequently amortized over the year. Cambia will include the fee incurred in its Consolidated Statements of Operations and Comprehensive Income beginning with the year ending December 31, 2014.

In February 2013, the FASB issued new guidance for reporting of reclassifications out of accumulated other comprehensive income. The guidance requires entities to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income. The guidance is effective prospectively for reporting periods beginning after December 15, 2013 with an option to early adopt. Cambia will report these reclassifications in its Consolidated Statements of Operations and Comprehensive Income beginning with the year ending December 31, 2014.

**U. Subsequent Events** – Cambia evaluated subsequent events for recognition or disclosure through April 4, 2013, which represents the date the consolidated financial statements were available to be issued. No events have occurred after December 31, 2012, but before April 4, 2013, the date the financial statements were available to be issued, that require consideration as adjustments to, or disclosures in, the financial statements.

**V. Reclassification** – Cambia has separately presented the amounts of Pension and Postretirement Obligations as of December 31, 2011, in the Consolidated Balance Sheets to conform to the December 31, 2012 presentation.

## 2. INVESTMENTS

### A. Available for Sale Investments

The following table sets forth the cost, or amortized cost, and fair values of investments held at December 31, 2012:

(In thousands)	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Equity securities:				
Communications	\$ 27,339	\$ 12,890	\$ 113	\$ 40,116
Consumer goods	104,183	36,625	537	140,271
Industrial goods	56,562	18,363	107	74,818
Utilities	52,231	18,244	60	70,415
Financial services	64,778	19,689	111	84,356
Technology	32,839	12,230	137	44,932
Foreign equity	109,057	20,510	419	129,148
Private placement	11,063	57,621	-	68,684
Other	17,083	2,667	-	19,750
Total equity securities	<u>475,135</u>	<u>198,839</u>	<u>1,484</u>	<u>672,490</u>
Debt securities:				
U.S. Treasury securities and				
U.S. Government-sponsored agencies	681,491	17,990	87	699,394
U.S. states and political				
subdivisions	30,899	785	89	31,595
Foreign government	13,473	480	-	13,953
Corporate				
Communications	54,292	4,730	9	59,013
Consumer goods	89,926	6,253	149	96,030
Industrial goods	57,448	3,405	148	60,705
Utilities	131,689	10,901	178	142,412
Financial services	228,960	14,831	52	243,739
Technology	7,192	125	5	7,312
Other and private placement	45,847	681	-	46,528
Loan-backed				
Residential mortgage-backed	553,709	31,241	21	584,929
Commercial mortgage-backed	90,080	3,715	94	93,701
Asset-backed	90,473	522	135	90,860
Total debt securities	<u>2,075,479</u>	<u>95,659</u>	<u>967</u>	<u>2,170,171</u>
Total investments	<u>\$ 2,550,614</u>	<u>\$ 294,498</u>	<u>\$ 2,451</u>	<u>\$ 2,842,661</u>

The following table sets forth the cost, or amortized cost, and fair values of investments held at December 31, 2011:

(In thousands)	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Equity securities:				
Communications	\$ 37,810	\$ 9,106	\$ 366	\$ 46,550
Consumer goods	97,500	31,695	847	128,348
Industrial goods	57,038	14,358	319	71,077
Utilities	45,208	17,795	411	62,592
Financial services	69,371	8,732	618	77,485
Technology	33,784	12,341	323	45,802
Foreign equity	104,010	6,252	1,936	108,326
Private placement	11,065	59,346	-	70,411
Other	17,342	1,354	342	18,354
Total equity securities	<u>473,128</u>	<u>160,979</u>	<u>5,162</u>	<u>628,945</u>
Debt securities:				
U.S. Treasury securities and				
U.S. Government-				
sponsored agencies	323,700	13,515	29	337,186
U.S. states and political				
subdivisions	91,186	6,308	105	97,389
Foreign government	12,588	401	2	12,987
Corporate				
Communications	67,011	5,673	427	72,257
Consumer goods	96,406	7,064	611	102,859
Industrial goods	55,295	2,346	750	56,891
Utilities	151,687	10,958	1,023	161,622
Financial services	304,497	9,163	5,535	308,125
Technology	20,105	515	237	20,383
Other	33,033	523	-	33,556
Loan-backed				
Residential mortgage-	631,496	27,145	461	658,180
backed				
Commercial mortgage-	93,794	2,506	263	96,037
backed				
Asset-backed	53,306	267	237	53,336
Total debt securities	<u>1,934,104</u>	<u>86,384</u>	<u>9,680</u>	<u>2,010,808</u>
Total investments	<u>\$ 2,407,232</u>	<u>\$ 247,363</u>	<u>\$ 14,842</u>	<u>\$ 2,639,753</u>

The following investments have been in a continuous unrealized loss position at December 31, 2012:

(In thousands)	<u>Less than Twelve Months</u>		<u>Twelve Months or More</u>	
	<u>Fair Value</u>	<u>Unrealized Loss</u>	<u>Fair Value</u>	<u>Unrealized Loss</u>
Equity securities:				
Communications	\$ 2,107	\$ 111	\$ 32	\$ 2
Consumer goods	8,832	536	31	1
Industrial goods	2,779	101	106	6
Utilities	1,728	49	174	11
Financial services	4,937	109	26	2
Technology	2,849	137	-	-
Foreign equity	7,637	351	573	68
Total equity securities	<u>30,869</u>	<u>1,394</u>	<u>942</u>	<u>90</u>
Debt securities:				
U.S. Treasury securities and U.S. Government-sponsored agencies	52,202	87	-	-
U.S. states and political subdivisions	-	-	2,116	89
Corporate				
Communications	2,943	9	-	-
Consumer goods	3,286	43	652	106
Industrial goods	3,958	119	172	29
Utilities	9,175	113	1,363	65
Financial services	8,465	41	1,436	11
Technology	1,795	5	-	-
Loan-backed				
Residential mortgage-backed	1,354	1	1,129	20
Commercial mortgage-backed	7,158	21	3,402	73
Asset-backed	21,396	58	3,052	77
Total debt securities	<u>111,732</u>	<u>497</u>	<u>13,322</u>	<u>470</u>
Total investments	<u>\$ 142,601</u>	<u>\$ 1,891</u>	<u>\$ 14,264</u>	<u>\$ 560</u>

The following investments have been in a continuous unrealized loss position at December 31, 2011:

(In thousands)	Less than Twelve Months		Twelve Months or More	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Equity securities:				
Communications	\$ 6,449	\$ 365	\$ 8	\$ 1
Consumer goods	10,861	847	-	-
Industrial goods	6,240	319	9	-
Utilities	3,701	411	-	-
Financial services	16,233	618	16	-
Technology	5,789	323	-	-
Other	26,207	1,936	-	-
Foreign equity	7,777	342	-	-
Total equity securities	<u>83,257</u>	<u>5,161</u>	<u>33</u>	<u>1</u>
Debt securities:				
U.S. Treasury securities and				
U.S. Government-				
sponsored agencies	63,504	29	-	-
U.S. states and political				
subdivisions	5,736	105	-	-
Foreign government	1,728	2	-	-
Corporate				
Communications	4,299	365	304	62
Consumer goods	9,764	483	699	128
Industrial goods	12,082	716	37	34
Utilities	17,001	763	751	260
Financial services	114,939	5,338	4,673	197
Technology	6,974	237	-	-
Loan-backed				
Residential mortgage-backed	22,095	427	415	34
Commercial mortgage-backed	17,312	257	130	6
Asset-backed	29,856	237	-	-
Total debt securities	<u>305,290</u>	<u>8,959</u>	<u>7,009</u>	<u>721</u>
Total investments	<u>\$ 388,547</u>	<u>\$ 14,120</u>	<u>\$ 7,042</u>	<u>\$ 722</u>



Cambia had 911 out of 9,624 securities in an unrealized loss position at December 31, 2012. The fair value of these investments is less than cost due to reasons including, but not limited to, changes in interest rates, economic conditions, and market outlook for various industries. Cambia has the intent and ability to hold equity securities until the market price recovers. Cambia neither intends to sell nor will likely be required to sell debt securities and expects to recover the entire amortized cost basis of these securities. As a result, Cambia concluded these investments were not other-than-temporarily impaired at December 31, 2012.

The amortized cost and fair value of debt securities held at December 31, 2012 other than those backed by loans, are shown below by contractual maturity:

(In thousands)	Amortized Cost	Fair Value
Due in one year or less	\$ 119,095	\$ 119,867
Due after one year through five years	738,740	765,598
Due after five years through ten years	454,143	483,755
Due after ten years	29,239	31,461
	<u>1,341,217</u>	<u>1,400,681</u>
Loan-backed securities	734,262	769,490
Total debt securities	<u>\$ 2,075,479</u>	<u>\$ 2,170,171</u>

The maturities of loan-backed securities differ from contractual maturities because borrowers may have the right to prepay obligations with or without call or prepayment penalties. The maturities of all other securities are contractually based.

Realized gains (losses), included in Investment Income, net, for the years ended December 31, 2012 and 2011 are as follows:

(In thousands)	2012	2011
Total other-than-temporary losses	\$ (6,271)	\$ (19,280)
Portion of losses in other comprehensive income	140	1,265
Other-than-temporary losses in net income	(6,131)	(18,015)
Gross realized gains from sales of investments	90,739	76,899
Gross realized losses from sales of investments	(15,667)	(27,442)
Total realized gains, net	<u>\$ 68,941</u>	<u>\$ 31,442</u>

The following represents the activity for the credit-related portion of other-than-temporary impairment losses recognized in net investment income:

(In thousands)	Credit-related Impairment
Cumulative losses at January 1, 2011	\$ (8,974)
Additions for credit impairments recognized on:	
Securities not previously impaired	(1,275)
Securities previously impaired	(796)
Reductions for credit impairments previously recognized on securities that matured or were sold during the year	<u>2,095</u>
Cumulative losses at December 31, 2011	\$ (8,950)
Additions for credit impairments recognized on:	
Securities not previously impaired	(1,227)
Securities previously impaired	(940)
Reductions for credit impairments previously recognized on securities that matured or were sold during the year	<u>1,679</u>
Cumulative losses at December 31, 2012	<u>\$ (9,438)</u>

The Plans are required to keep investments on deposit in certain states in which they are licensed. At December 31, 2012 and 2011, debt securities with a fair value of \$78,677,000 and \$77,928,000, respectively, were restricted to comply with these requirements.

#### **B. Equity Method Investments**

Cambia owns a 13.2 percent limited partnership interest in TZ Holdings, L.P. (TZ Holdings). While this represents a minority interest, Cambia holds a 6.7 percent voting interest on TZ Holdings' board of directors. Therefore, Cambia accounts for the investment under the equity method. The carrying value of the investment included in other assets was \$111,637,000 and \$113,725,000 as of December 31, 2012 and 2011, respectively. TZ Holdings' total assets and liabilities as of December 31, 2012 were \$1,871,062,000 and \$1,022,165,000, respectively. TZ Holdings' total assets and liabilities as of December 31, 2011 were \$1,759,994,000 and \$907,141,000, respectively. TZ Holdings experienced a net loss of \$4,019,000 and \$2,207,000 for the year ended December 31, 2012 and 2011, respectively.

Cambia has an agreement through 2016 with a subsidiary of TZ Holdings that provides data processing and related services for Cambia. Expenditures under this agreement represent \$24,967,000 and \$43,798,000 for the years ended December 31, 2012 and 2011, respectively. These costs are included in Operating Expense on the Consolidated Statement of Operations and Comprehensive Income and within Property, Buildings and Equipment, net, as capitalized software on the Consolidated Balance Sheets.

### C. Variable Interest Entities

Cambia periodically evaluates its variable interests on a quantitative and qualitative basis in order to determine whether it is the primary beneficiary and if it is required to consolidate those interests. The assessment considers the entity's structure and purpose, the risks and rewards created by and shared through the entity and Cambia's ability to direct the activities that most significantly impact the entity's economic performance. Additionally, the assessment considers benefits received and losses absorbed that could potentially be significant. Cambia has reviewed its investments, related party relationships and other applicable transactions and concluded that it does not have the ability to direct the activities that most significantly impact the economic performance for those entities determined to be variable interest entity's (VIE's) for the years ended December 31, 2012 and 2011 and, therefore, consolidation of those interests was not required.

Regence BCBSO holds a 50 percent limited partner interest in 200 Market Associates Limited Partnership (200 Market). The remaining partners are under either common ownership or management by a party not affiliated with Cambia. As a special purpose entity, the nature of 200 Market's activities is to own, manage, and lease property located in Portland, Oregon. At December 31, 2012, Cambia leased approximately 59 percent of the property's space available for lease. The business operations are managed by the general partner while the limited partners' ability to direct activities is contractually limited by the partnership agreement and debt covenants of a promissory note. Regence BCBSO guarantees the note held by 200 Market (see Note 14). Regence BCBSO does not have the power to direct the significant activities that affect 200 Market's economic performance and, therefore, is not the primary beneficiary and has not consolidated 200 Market. The carrying value of the investment, which is accounted for using the equity method, was in a negative position representing a \$10,623,000 and \$10,796,000 liability included in Accrued Expenses and Other Liabilities at December 31, 2012 and 2011, respectively. The total partnership deficit balance at December 31, 2012 and 2011 was \$21,609,000 and \$23,539,000, respectively.

### 3. FAIR VALUE MEASUREMENTS

The following summarizes fair value measurements by level for assets measured at fair value on a recurring basis as of December 31, 2012:

(In thousands)	Fair Value	Fair Value Measurement Using		
		Level 1	Level 2	Level 3
Cash equivalents	\$ 99,305	\$ 95,857	\$ 3,448	\$ -
Equity securities:				
Communications	40,116	40,116	-	-
Consumer goods	140,271	140,271	-	-
Industrial goods	74,818	74,818	-	-
Utilities	70,415	70,415	-	-
Financial services	84,356	84,356	-	-
Technology	44,932	44,932	-	-
Foreign equity	129,148	129,148	-	-
Private placement	68,684	-	-	68,684
Other	19,750	-	19,750	-
Total equity securities	<u>672,490</u>	<u>584,056</u>	<u>19,750</u>	<u>68,684</u>
Debt securities:				
U.S. Treasury securities and U.S. Government- sponsored agencies	699,394	465,155	234,239	-
U.S. states and political subdivisions	31,595	-	31,595	-
Foreign government	13,953	-	13,953	-
Corporate				
Communications	59,013	-	59,013	-
Consumer goods	96,030	-	96,030	-
Industrial goods	60,705	-	60,375	330
Utilities	142,412	-	141,992	420
Financial services	243,739	-	243,739	-
Technology	7,312	-	7,312	-
Other and private placement	46,528	-	39,028	7,500
Loan-backed				
Residential mortgage-backed	584,929	-	583,813	1,116
Commercial mortgage-backed	93,701	-	93,701	-
Asset-backed	90,860	-	90,860	-
Total debt securities	<u>2,170,171</u>	<u>465,155</u>	<u>1,695,650</u>	<u>9,366</u>
Total assets	<u>\$ 2,941,966</u>	<u>\$ 1,145,068</u>	<u>\$ 1,718,848</u>	<u>\$ 78,050</u>

The following summarizes fair value measurements by level for assets measured at fair value on a recurring basis as of December 31, 2011:

(In thousands)	Fair Value	Fair Value Measurement Using		
		Level 1	Level 2	Level 3
Cash equivalents	\$ 153,107	\$ 152,796	\$ 311	\$ -
Equity securities:				
Communications	46,550	46,550	-	-
Consumer goods	128,348	128,348	-	-
Industrial goods	71,077	71,077	-	-
Utilities	62,592	62,592	-	-
Financial services	77,485	77,485	-	-
Technology	45,802	45,802	-	-
Foreign equity	108,326	108,326	-	-
Private placement	70,411	-	-	70,411
Other	18,354	-	18,354	-
Total equity securities	628,945	540,180	18,354	70,411
Debt securities:				
U.S. Treasury securities and				
U.S. Government-				
sponsored agencies	337,186	241,547	95,639	-
U.S. states and political				
subdivisions	97,389	-	97,389	-
Foreign government	12,987	-	12,987	-
Corporate				
Communications	72,257	-	71,310	947
Consumer goods	102,859	-	102,859	-
Industrial goods	56,891	-	56,691	200
Utilities	161,622	-	160,588	1,034
Financial services	308,125	-	308,125	-
Technology	20,383	-	20,383	-
Other	33,556	-	33,556	-
Loan-backed				
Residential mortgage-backed	658,180	-	656,503	1,677
Commercial mortgage-backed	96,037	-	96,037	-
Asset-backed	53,336	-	53,336	-
Total debt securities	2,010,808	241,547	1,765,403	3,858
Total assets	\$ 2,792,860	\$ 934,523	\$ 1,784,068	\$ 74,269

Assets classified as Level 1 include actively-traded money market funds, equity securities, and U.S. Treasury securities. The fair values of these securities reflect quoted prices in active markets.

The fair value of cash equivalents is equal to the carrying value at the measurement date. Cash equivalents classified as Level 2 represent securities maturing within three months that do not trade on a regular basis.

Equity securities classified as Level 2 use other observable market inputs to estimate fair value. The fair value of these instruments is obtained from third-party pricing services which use quoted prices for similar securities or quoted prices for identical or similar securities in less active markets. Cambia evaluates prices received from the pricing services at least annually. If Cambia does not agree with the estimated price, the identified price will be verified by an independent pricing source or through performing independent valuations of inputs and assumptions similar to those used by pricing service in order to ensure prices represent a reasonable estimate of fair value. Although Cambia does identify differences as a result of these validation procedures, Cambia did not make any significant adjustments as of December 31, 2012 or 2011.

Private placement equity securities designated as Level 3 represent private placement investments for which no observable market data is available. Private placement equity securities are valued annually, or on an as needed basis. Values of private placement equity investments classified as Level 3 are derived from the underlying shareholders' equity per the investee's financial statements and adjusted to fair value. This valuation reflects reasonable and consistent assumptions for fair value measurement and uses the best information available. Fair value measurements may also be validated through the use of valuation models which incorporate both a quantitative and qualitative perspective.

The fair value of debt securities classified as Level 2 inputs are derived using pricing models that incorporate estimated market interest rates, benchmark yields, credit spreads, broker quotes and other observable market data.

Values of private placement debt investments classified as Level 3 are based on current market observable rates for debt instruments with similar terms, maturities and credit risk and may also incorporate broker quotes and assumptions for benchmark yields, credit spreads, default rates and prepayment speeds that are not observable in the markets.

Other debt securities classified as Level 3 includes certain securities in a default position or at-risk of entering default, and therefore, management judgment is a significant input in estimating fair value. These prices are provided by proprietary valuation models from the fund manager. Loan-backed securities incorporate prepayment speeds, default rates, and collateral values into the pricing models.

The following table represents a reconciliation of assets valued using Level 3 inputs on a recurring basis for the twelve months ended December 31:

(In thousands)	Level 3 Fair Value Measurements				Total
	Private Placement Equity Securities	US States / Political Subdivisions Debt Securities	Corporate Debt Securities	Loan-Backed Securities	
Balance at January 1, 2011	\$ 55,688	\$ 1,230	\$ 1,399	\$ 7,781	\$ 66,098
Total gains or losses (realized/unrealized):					
Included in investment income	-	-	(203)	(53)	(256)
Included in accumulated other comprehensive income	14,723	4	(140)	299	14,886
Purchases	-	-	54	-	54
Sales	-	(60)	(475)	(457)	(992)
Transfers into Level 3	-	-	1,843	1,677	3,520
Transfers out of Level 3	-	(1,174)	(297)	(7,570)	(9,041)
Balance at December 31, 2011	<u>70,411</u>	<u>-</u>	<u>2,181</u>	<u>1,677</u>	<u>74,269</u>
Total gains or losses (realized/unrealized):					
Included in investment income	-	-	(1,060)	92	(968)
Included in accumulated other comprehensive income	(1,725)	-	150	35	(1,540)
Purchases	-	-	7,522	-	7,522
Sales	-	-	-	(688)	(688)
Transfers into Level 3	-	-	604	-	604
Transfers out of Level 3	(2)	-	(1,147)	-	(1,149)
Balance at December 31, 2012	<u>\$ 68,684</u>	<u>\$ -</u>	<u>\$ 8,250</u>	<u>\$ 1,116</u>	<u>\$ 78,050</u>

Cambia recognizes transfers between levels at the end of the reporting period. There were no significant transfers between any fair value levels during the years ended December 31, 2012 and 2011, respectively.

#### 4. PROPERTY, BUILDINGS AND EQUIPMENT, NET

Property, Buildings and Equipment, net consisted of the following at December 31:

(In thousands)	2012	2011
Capitalized software	\$ 523,469	\$ 514,604
Buildings and improvements	130,081	160,353
Furniture and equipment	104,447	114,266
Leased equipment	55,802	41,777
Land	10,927	11,787
	<u>824,726</u>	<u>842,787</u>
Less: Accumulated depreciation and amortization	<u>477,458</u>	<u>470,590</u>
	347,268	372,197
Assets held for sale	<u>20,626</u>	<u>7,352</u>
Property, buildings and equipment, net	<u>\$ 367,894</u>	<u>\$ 379,549</u>

Assets held for sale as of December 31, 2012 include land and buildings, recorded at the lower of cost or fair value, less estimated costs to sell.

On December 20, 2011, the Company sold real estate located in Seattle, Washington, to an unrelated third party for \$76,540,000. Several floors of this property were subsequently leased back to the Company at market rates based on occupied square footage. The lease is classified as an operating lease. The net book value of the property sold was \$21,413,000 and the net cost to sell the property was \$3,770,000. The Company recognized \$51,357,000 of total gain from the sale, of which \$36,902,000 is included in gain from sale of real estate during the year ended December 31, 2011. In accordance with *ASC 840 – Leases*, the remaining gain amount of \$14,455,000, which represented the present value of future minimum lease payments, is deferred and amortized to earnings over the seven year term of the lease. Amortization of \$2,041,000 related to this sale was recognized during the year ended December 31, 2012.

Depreciation and amortization expense recorded in Operating Expense on the Consolidated Statements of Operations and Comprehensive Income was \$71,491,000 and \$78,247,000 for 2012 and 2011, respectively.

#### 5. CAPITALIZED SOFTWARE

Included in Property, Buildings and Equipment, net are costs related to internally-customized and purchased software that are capitalized and amortized over periods of between three and twelve years. Included in Other Assets are costs related to software currently being customized, but not amortized, as it has not yet been placed into service. Capitalized costs include direct costs of materials and services incurred in customizing or obtaining internal-use software and payroll and payroll-related costs for employees directly involved in the customization of internal-use software.

During 2011, the total accumulated capitalized costs of several software projects were reevaluated due to changes in project directions. As a result, the Company recognized \$5,849,000 in software impairments. There were no impairments in 2012.

Reclassifications from Other Assets to Property, Buildings and Equipment, net for internally-customized software placed into service during 2012 and 2011 was \$26,882,000 and \$32,202,000, respectively.

The following table sets forth the total amount of internally-customized and purchased software capitalized at December 31:

(In thousands)	2012	2011
Internally-customized and purchased software included in Property, Buildings and Equipment, net	\$ 523,469	\$ 514,604
Less: Accumulated amortization	(315,401)	(288,872)
	208,068	225,732
Capitalized Software in Process included in Other Assets	6,046	24,335
Net capitalized software	\$ 214,114	\$ 250,067



## 6. RESERVE FOR UNPAID CLAIMS AND ADJUSTING EXPENSES ON UNPAID CLAIMS

Activity in the reserves for unpaid health claims and the reserve for adjusting expenses on unpaid health claims are summarized as follows:

(In thousands)	<u>2012</u>	<u>2011</u>
Balance at January 1	\$ 1,003,081	\$ 885,108
Less: Reinsurance receivables	<u>(40,351)</u>	<u>(40,929)</u>
Net balance at January 1	<u>962,730</u>	<u>844,179</u>
Incurred related to:		
Current year	7,052,163	7,173,003
Prior year	<u>(185,148)</u>	<u>27,142</u>
Total incurred	<u>6,867,015</u>	<u>7,200,145</u>
Paid related to:		
Current year	6,241,559	6,203,540
Prior year	<u>777,140</u>	<u>878,054</u>
Total paid	<u>7,018,699</u>	<u>7,081,594</u>
Net balance at December 31	811,046	962,730
Add: Reinsurance receivables	<u>39,989</u>	<u>40,351</u>
Balance at December 31	<u>\$ 851,035</u>	<u>\$ 1,003,081</u>

Incurred related to prior year in the table represents the change in reserves attributable to the difference between the original estimate of incurred claims for prior years and the revised estimate. The redundancy in reserves for the year ended December 31, 2012 is primarily attributed to positive completion factor development related to fluctuations in claims processing patterns, as well as favorable claims trend relative to the prior year.

Cambia enters into reinsurance arrangements to transfer a portion of the risks associated with certain long-term disability contracts to reinsurers. As the primary liability to customers remains with Cambia, estimated reserves are recorded in Reserves for Unpaid Claims and Adjusting Expenses on Unpaid Claims. Corresponding reinsurance receivables are recorded in Receivables, net. The financial condition of reinsurers is evaluated, and Cambia only records reinsurance receivables to the extent recovery is probable.

The following illustrates the differences between total incurred claims (above) and Claims Expense as reported on the Consolidated Statements of Operations and Comprehensive Income:

(In thousands)	<u>2012</u>	<u>2011</u>
Incurred claims and adjusting expenses on unpaid claims	\$ 6,867,015	\$ 7,200,145
Less: Claims adjusting expenses included in operating expense	(228,157)	(302,076)
Add: Life claims incurred	17,195	13,418
Change in premium deficiency reserves	-	(6,176)
Less: Claims expense and amounts attributable to claims under self-funded arrangements	<u>(1,839,702)</u>	<u>(1,834,545)</u>
Claims expense	<u>\$ 4,816,351</u>	<u>\$ 5,070,766</u>

The following illustrates the difference between the Reserves for Unpaid Claims and Claims Adjusting Expenses (above) and the Reserve for Unpaid Claims and Adjusting Expenses on Unpaid Claims as reported on the Consolidated Balance Sheets:

(In thousands)	<u>2012</u>	<u>2011</u>
Reserves for unpaid claims and claims adjusting expenses	\$ 851,035	\$ 1,003,081
Add: Life claims reserves	<u>20,587</u>	<u>17,633</u>
Reported on Consolidated Balance Sheets	<u>\$ 871,622</u>	<u>\$ 1,020,714</u>

## 7. DEBT AND OTHER OBLIGATIONS

Debt and other obligations consist of the following at December 31:

(In thousands)	<u>2012</u>	<u>2011</u>
Debt secured by investments:		
Payable in monthly principle installments of \$200 with interest of 5.12%, due March 28, 2018	\$ 48,600	\$ 51,200
Debt secured by commercial property:		
Payable in monthly installments of \$216 including interest of 7.19%, due October 1, 2022	18,228	19,458
Payable in monthly installments of \$100 including interest of 5.94%, due August 1, 2018	9,442	10,101
Payable in monthly installments of \$54 including interest of 5.82%, due February 7, 2015	7,044	7,287
Payable in monthly installments of \$51 including interest of 5.94%, due August 1, 2016	6,911	7,125
Payable in monthly installments of \$9 including interest of 7.92%, due April 1, 2012	-	37
Total debt secured by investments and commercial property	<u>90,225</u>	<u>95,208</u>
Revolving line of credit	-	10,000
Capital lease obligations	<u>18,149</u>	<u>14,622</u>
	108,374	119,830
Less: Interest on capital lease obligations	<u>442</u>	<u>527</u>
Carrying value of debt and other obligations	<u>\$ 107,932</u>	<u>\$ 119,303</u>

As of December 31, 2012 and 2011, Cambia has debt secured by investments in debt securities. These assets are in the creditor's custody, however, Cambia retains control over the assets as it can withdraw or substitute the securities provided the balance of the collateral does not fall below a 94 percent loan-to-value ratio. The creditor may not sell, transfer, or re-pledge the assets unless Cambia defaults on its obligations. The collateral has a carrying value of \$55,727,000 and \$72,590,000 as of December 31, 2012 and 2011, respectively, and is included in Investments in the Consolidated Balance Sheets.

Commercial property and investments securing debt had a total carrying value of \$102,428,000 and \$120,985,000 as of December 31, 2012 and 2011, respectively. The fair value of debt was \$101,348,000 and \$104,797,000 at December 31, 2012 and 2011, respectively.

Cambia's capital lease obligations relate to software and other general office equipment.

Cambia maintains a revolving line of credit to supplement short-term cash flows. The maximum available line of credit is \$40,000,000 and renewable annually. The interest rate is based on LIBOR plus 130 basis points for the term of the agreement.

Cambia's future minimum principal payments for years ended December 31 are as follows:

(In thousands)	
2013	13,708
2014	11,639
2015	13,710
2016	11,418
2017	4,991
Thereafter	52,908
	<u>108,374</u>
Less: Interest on capital lease obligations	442
Carrying value of debt and other obligations	<u>\$ 107,932</u>

Cambia has financial debt covenants with certain loans secured by commercial property and investments requiring Cambia to maintain minimum debt service coverage ratios. Cambia is in compliance with these debt covenants as of December 31, 2012.

#### 8. ACCRUED EXPENSES AND OTHER LIABILITIES

Accrued expenses and other liabilities consisted of the following at December 31:

(In thousands)	2012	2011
Checks written in excess of bank balances	64,707	91,428
Payroll and employee benefits	88,483	73,491
Suspense accounts	21,117	24,902
Federal income taxes	23,410	22,782
Administrative deficiency reserve	19,653	2,234
Trade accounts payable	32,940	14,980
Deferred gain on sale of real estate	15,443	14,285
Commissions payable	15,789	14,129
Partnership interest	10,623	10,796
All other	45,635	54,160
Total accrued expenses and other liabilities	<u>\$ 337,800</u>	<u>\$ 323,187</u>

#### 9. RETIREMENT PLANS

The defined benefit pension plan which covered substantially all full-time employees having one or more years of service, provided benefits based on years of service and the employee's final average compensation was frozen effective December 31, 2009. As a result of the freeze, no new participants have entered the plan, no pension benefits have been earned, benefits-eligible employees who had not yet met plan eligibility criteria became immediately eligible and non-vested plan participants received accelerated vesting to 100 percent.

Cambia also provides a supplemental retirement plan to cover key employees meeting certain eligibility requirements. Cambia funds this plan as benefit obligations become due.

The following sets forth the defined benefit pension plan's funded status and amounts recognized in Cambia's Consolidated Balance Sheets at December 31, 2012 and 2011. The benefit obligations and plan assets are measured at December 31.

(In thousands)	Defined Benefit Pension Plan		Supplemental Retirement Plan	
	2012	2011	2012	2011
Projected benefit obligation	\$(531,475)	\$(494,586)	\$ (59,108)	\$ (55,430)
Fair value of plan assets	531,757	476,322	-	-
Funded status recognized	<u>\$ 282</u>	<u>\$ (18,264)</u>	<u>\$ (59,108)</u>	<u>\$ (55,430)</u>
Net actuarial loss	\$ 259,547	\$ 260,595	\$ 18,045	\$ 14,722
Prior service (credit) cost	<u>(67,611)</u>	<u>(72,731)</u>	<u>1,076</u>	<u>1,382</u>
Total recognized in Accumulated OCI	<u>\$ 191,936</u>	<u>\$ 187,864</u>	<u>\$ 19,121</u>	<u>\$ 16,104</u>
Accumulated benefit obligation	\$(531,475)	\$(494,586)	\$ (50,531)	\$ (47,466)
Employer contributions	\$ 30,000	\$ 30,000	\$ 4,909	\$ 3,635
Benefits paid	\$ 28,050	\$ 27,320	\$ 4,909	\$ 3,635

The following summarizes the components of net periodic benefit cost:

(In thousands)	Defined Benefit Pension Plan		Supplemental Retirement Plan	
	2012	2011	2012	2011
Service cost	\$ 1,071	\$ 1,074	\$ 1,730	\$ 1,465
Interest cost	23,672	23,859	2,486	2,703
Expected return on assets	(25,337)	(30,095)	-	-
Amortization:				
Prior service (credit)/cost	(5,120)	(5,120)	307	313
Actuarial (gain)/loss	<u>13,096</u>	<u>9,803</u>	<u>1,046</u>	<u>445</u>
Net periodic benefit cost	<u>\$ 7,382</u>	<u>\$ (479)</u>	<u>\$ 5,569</u>	<u>\$ 4,926</u>

The following weighted average assumptions were used in determining the actuarial present value of the projected benefit obligations at December 31:

	Defined Benefit Pension Plan		Supplemental Retirement Plan	
	2012	2011	2012	2011
Discount rate	4.40%	4.97%	3.68%	4.70%
Rate of increase in future compensation	N/A	N/A	5.00%	5.00%

The following weighted average assumptions were used in determining the actuarial present value of the net period benefit cost at December 31:

	Defined Benefit Pension Plan		Supplemental Retirement Plan	
	2012	2011	2012	2011
Discount rate	4.97%	5.85%	4.70%	5.85%
Rate of increase in future compensation	N/A	N/A	5.00%	5.00%
Expected long term rate of return on assets	5.50%	7.20%	N/A	N/A

The expected long-term rate of return on assets assumption was determined by using a combination of expected returns for each asset class within Cambia's portfolio plus inflation. The expected returns were based on past performance as well as projections for the next twelve months. Based on these considerations, Cambia believes the expected long-term rate of return on assets assumption is reasonable.

The following benefit payments are expected to be paid:

(In thousands)	Defined Benefit Pension Plan	Supplemental Retirement Plan
2013	33,165	3,675
2014	32,986	5,630
2015	34,553	4,474
2016	34,010	4,932
2017	36,959	4,967
Years 2018-2022	171,182	26,848

The following summarizes changes recognized in Accumulated OCI:

(In thousands)	Defined Benefit Pension Plan		Supplemental Retirement Plan	
	2012	2011	2012	2011
Net loss (gain) arising during period	\$ 12,049	\$ 62,619	\$ 4,370	\$ 6,876
Amortization:				
Prior service (cost) credit	5,120	5,120	(307)	(313)
Loss	(13,097)	(9,803)	(1,046)	(445)
Total recognized in other comprehensive loss	<u>\$ 4,072</u>	<u>\$ 57,936</u>	<u>\$ 3,017</u>	<u>\$ 6,118</u>

The estimated amounts that will be amortized from Accumulated OCI into net periodic benefit cost in 2013 are as follows:

(In thousands)	Defined Benefit Pension Plan	Supplemental Retirement Plan
Actuarial loss	\$ 13,136	\$ 1,455
Prior service cost (credit)	(5,120)	295
Total	<u>\$ 8,016</u>	<u>\$ 1,750</u>

Cambia follows a Retirement Trust Committee (RTC) approved investment policy that focuses on long-term investment performance. To manage the overall risk of the portfolio, the portfolio asset allocation and investment manager selection are continually monitored and approved by the RTC. An independent external investment consultant provides the RTC with a quarterly update on policy compliance and fund performance. Semi-annually, the overall performance and asset allocation are reported to Cambia's Board of Directors for review.

The target allocations for plan assets, including the underlying investments of common collective trusts, are 20 percent equity securities and 80 percent debt securities. The portfolio is rebalanced to the target asset allocations as necessary to ensure proper risk exposure.

Other investments consist of financial instruments without readily determined market values. These include limited partnerships, insurance contracts, hedge fund companies, and other pooled investments. The value of the investments has been determined by management based upon the estimates of fair value made by these entities. Estimates provided are reviewed for reasonableness by management, who considers the financial condition and operating results of each limited partnership and other pooled investment entity, as well as other factors deemed appropriate. Insurance contracts are valued at contract value. Shares of hedge fund companies are valued at estimated fair value which represents the net asset values of shares held by the defined benefit pension plan at year end.

The following summarizes the fair value measurements of Cambia's defined benefit plan assets by level of assets measured at fair value on a recurring basis, excluding net investment trade receivables of \$447,000 and cash of \$942,000 as of December 31, 2012:

(In thousands)	Fair Value	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
U.S. government securities	\$ 64,188	\$ 64,188	\$ -	\$ -
Corporate debt securities				
Banking and finance	70,539	-	70,539	-
Industrial	10,159	-	10,159	-
Non US bonds	48,728	-	48,717	11
Oil and gas	29,028	-	29,028	-
Private placements	31,215	-	31,215	-
Consumer goods	95,524	-	95,524	-
Utilities	50,701	-	50,701	-
Registered investment companies				
Money market	15,160	14,080	1,080	-
Small capital value	4,717	4,717	-	-
Common and collective trusts				
Small capital value	10,721	-	10,721	-
Large capital value	20,582	-	20,582	-
Large capital growth	20,911	-	20,911	-
International funds	25,471	-	25,471	-
Unallocated insurance contracts	1,510	-	-	1,510
Other pooled investment entities	13,032	-	13,032	-
Other investments	18,182	-	18,182	-
<b>Total</b>	<b>\$ 530,368</b>	<b>\$ 82,985</b>	<b>\$ 445,862</b>	<b>\$ 1,521</b>



The following summarizes fair value measurements of Cambia's defined benefit plan assets by level of assets measured at fair value on a recurring basis, excluding net investment income payables of \$7,596,000, as of December 31, 2011:

(In thousands)	Fair Value	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
U.S. government securities	\$ 99,174	\$ 99,174	\$ -	\$ -
Corporate debt securities				
Banking and finance	55,793	-	55,793	-
Industrial	9,476	-	9,476	-
Non US bonds	45,204	-	45,204	-
Oil and gas	16,428	-	16,428	-
Private placements	15,675	-	15,675	-
Consumer goods	70,488	-	70,488	-
Utilities	45,810	-	45,810	-
Other	15,000	-	15,000	-
Corporate stock - common				
Basic industries	1,959	1,959	-	-
Capital goods	35	35	-	-
Consumer goods	1,165	1,165	-	-
Energy	1,213	1,213	-	-
Financial services	549	549	-	-
Healthcare	612	612	-	-
Technology	258	258	-	-
Other	684	684	-	-
Registered investment companies				
Money market	10,316	10,316	-	-
Small capital value	4,257	4,257	-	-
Common and collective trusts				
Large capital value	17,760	-	17,760	-
Large capital growth	16,412	-	16,412	-
International funds	23,002	-	23,002	-
Partnership and joint venture interests	109	-	-	109
Unallocated insurance contracts	1,467	-	-	1,467
Other pooled investment entities	29,871	-	11,228	18,643
Other investments	1,201	160	-	1,041
Total	<u>\$ 483,918</u>	<u>\$ 120,382</u>	<u>\$ 342,276</u>	<u>\$ 21,260</u>

Certain 2011 corporate debt securities have been reclassified in the table above to conform with 2012 presentation.

The following table represents a reconciliation of assets valued using Level 3 inputs on a recurring basis for the twelve months ended December 31:

(In thousands)

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)							Total
	Corporate Debt	Partnership /		Unallocated Insurance Contracts	Hedge Fund Companies	Other Pooled		
		Venture Interests	Joint			Investment Entities	Other Investments	
Balance at January 1, 2011	\$ 608	\$ 109	\$ 1,572	\$ 18,477	\$ 19,086	\$ -	\$ 39,852	
Actual return on plan assets	-	-	-	173	(443)	(273)	(543)	
Purchases	-	-	-	-	-	1,314	1,314	
Sales	-	-	-	(18,650)	-	-	(18,650)	
Settlements	-	-	(105)	-	-	-	(105)	
Transfers out of Level 3	(608)	-	-	-	-	-	(608)	
Balance at December 31, 2011	-	109	1,467	-	18,643	1,041	21,260	
Actual return on plan assets	11	556	43	-	669	131	1,410	
Sales	-	(665)	-	-	(19,312)	(1,172)	(21,149)	
Balance at December 31, 2012	\$ 11	\$ -	\$ 1,510	\$ -	\$ -	\$ -	\$ 1,521	

#### 10. POSTRETIREMENT BENEFITS

Cambia provides certain health care and life insurance benefits through a postretirement health and welfare plan (retiree health and welfare plan) for retired employees, subject to certain eligibility rules based on age and years of service at retirement date. Employees hired after January 1, 2004 are not eligible for benefits. Cambia's contribution to the cost of coverage is based on the retiree's age and years of service at retirement and is limited to a maximum dollar amount. This amount is calculated based on the Cambia contribution percentage and applies to the Cambia-funded health plan. If a retiree elects a medical or dental option that is more expensive than the Cambia-funded health plan, the retiree must pay the additional cost for the more expensive plan.

Cambia funds a portion of the accumulated postretirement benefit obligation through the Voluntary Employees' Beneficiary Association Trust (the VEBA Trust). Contributions to the VEBA Trust are based on the present value of prospective benefits for retirees and their dependents, amortized over eleven years, plus the normal cost for active employees and their dependents (both components are adjusted for interest to the end of the year) determined by the entry age cost method. Under this method, the cost of each individual's benefits are allocated on a level percent of payroll between the time employment starts (entry age) and the assumed retirement date. Investments held by the VEBA Trust consist of U.S. governmental obligations, common stocks, preferred stocks, other equity securities, and registered investment funds. The fair values of these investments are measured at Level 1 as defined in Note 1. Cambia did not fund additional amounts in 2012 or 2011.

The following sets forth the postretirement health and welfare plan's funded status and amounts recognized in Cambia's Consolidated Balance Sheets at December 31, 2012 and 2011. The accumulated benefit obligation and plan assets are measured at December 31.

(In thousands)	2012	2011
Accumulated postretirement benefit obligation	\$ (63,373)	\$ (60,768)
Fair value of plan assets	2,401	2,204
Funded status recognized	\$ (60,972)	\$ (58,564)
Net actuarial loss	\$ 23,044	\$ 22,290
Prior service credit	(17,652)	(21,503)
Total recognized in Accumulated OCI	\$ 5,392	\$ 787
Benefits paid	\$ 3,740	\$ 4,380

The following summarizes the components of the net periodic benefit cost:

(In thousands)	2012	2011
Service cost	\$ 729	\$ 612
Interest cost	2,672	2,697
Expected return on assets	(119)	(136)
Amortization:		
Actuarial (gain)/loss	1,789	1,043
Prior service (credit)/cost	(3,852)	(3,909)
Net periodic benefit cost	\$ 1,219	\$ 307

The following weighted average assumptions were used in determining the actuarial present value of the accumulated postretirement benefit obligation at December 31:

	2012	2011
Discount rate	3.66%	4.44%

The following weighted average assumptions were used in determining the actuarial present value of the accumulated postretirement net periodic benefit cost at December 31:

	2012	2011
Discount rate	4.44%	5.11%
Expected long-term rate of return on assets	5.43%	6.09%

The expected long-term rate of return on assets assumption was determined by using a combination of expected returns for each asset class within Cambia's portfolio plus inflation. The expected returns were

based on past performance as well as projections for the next twelve months. Based on these considerations, Cambia believes the expected long-term rate of return on assets assumption is reasonable.

The assumed healthcare cost trend used in measuring the health-care portion of the postretirement cost for 2013 is 7.0 percent, gradually declining to 5.0 percent by the year 2017 and remaining at that level thereafter. The assumed rates for health-care cost trend have a significant effect on the amounts reported for postretirement benefits.

The following benefit payments are expected to be paid:

(In thousands)	<u>Gross</u>	<u>Expected Federal Subsidy</u>	<u>Net</u>
2013	4,158	(324)	3,834
2014	4,180	(363)	3,817
2015	4,167	(399)	3,768
2016	4,501	(151)	4,350
2017	4,520	(151)	4,369
Years 2018-2022	21,890	(708)	21,182

The following summarizes changes recognized in Accumulated OCI:

(In thousands)	<u>2012</u>	<u>2011</u>
Net loss arising during period	\$ 2,542	\$ 7,813
Amortization:		
Prior service credit	3,852	3,908
Actuarial loss	(1,789)	(1,043)
Total recognized in other comprehensive loss (income)	<u>\$ 4,605</u>	<u>\$ 10,678</u>

The estimated amounts that will be amortized from Accumulated OCI into net periodic benefit cost in 2013 are as follows:

(In thousands)	
Actuarial loss	\$ 1,883
Prior service credit	(3,565)
Total	<u>\$ (1,682)</u>

## 11. EMPLOYEE SAVINGS PLAN

Under the provisions of The Regence Group 401(k) Savings Plan (the 401(k) plan), Cambia matches employee contributions up to 100 percent of the first six percent of salary for each pay period in which employees make an Internal Revenue Code (IRC) Section 401(k) contribution. Employees working at least 20 hours per week may contribute to the 401(k) plan. The IRC permitted employees to contribute up to \$17,000 and \$16,500 in 2012 and 2011, respectively, or 70 percent of eligible earnings, whichever was lower. Employer contributions are fully vested when an employee starts participating in the program. An additional employer contribution of up to five percent of eligible earnings for participating employees can also be made, subject to annual review and Board approval. Employer contributions totaled \$33,679,000 and \$34,687,000 for the years ended December 31, 2012 and 2011, respectively.

## 12. PHYSICIAN DEFERRED COMPENSATION

Regence BCBSO and Regence BlueShield maintain separate nonqualified physician deferred compensation plans covering certain member physicians who voluntarily defer payment of their billings. The plans are no longer accepting contributions; however, prior contributions are still being held in investments and paid out. Until the physicians retire and give instructions for lump payout or annuity purchase, the funds are treated as a defined contribution plan. Plans fund the obligations primarily through the purchase of group flexible paid-up life insurance contracts for active participants and annuity contracts for retired participants. As Regence BCBSO and Regence BlueShield are the owners and named beneficiaries of these contracts, in order to reflect policies to pay benefits equal to accumulations, both the assets and liabilities under the physician deferred compensation plans are reflected in Cambia's Consolidated Balance Sheets. As of December 31, 2012 and 2011, the balances were \$21,468,000 and \$22,842,000, respectively.

## 13. DEFERRED COMPENSATION

Cambia also offers The Regence Group Deferred Income Program for Executives and The Regence Group Deferred Income Program for Directors (collectively, the Programs). The purpose of the Programs is to provide an unfunded, nonqualified deferred compensation arrangement to eligible key employees and eligible directors. Benefits are based on the amounts contributed to these accounts plus any investment earnings, which equals the assets, and liabilities in the Consolidated Balance Sheets. Cambia made payments totaling \$953,000 and \$1,013,000 to the programs in the years ended December 31, 2012 and 2011, respectively. Assets are invested in publicly traded mutual funds consisting of equity and fixed income securities. The fair value of these publicly traded investments is determined using Level 1 inputs and was \$26,821,000 and \$25,383,000 as of December 31, 2012 and 2011, respectively.

## 14. COMMITMENTS AND CONTINGENCIES

Cambia is committed under various operating leases and agreements for office space, equipment (primarily computers and peripheral equipment) and professional services for remaining terms of up to eleven years. Some of these lease agreements contain escalation clauses for increases over base payment amounts. These leases expire on various dates with renewal options available on many of the leases. In the normal course of business, operating leases are generally renewed or replaced by other leases.

Minimum payment obligations under non-cancellable operating leases and agreements for the years ended December 31 are as follows:

(In thousands)	
2013	35,463
2014	30,623
2015	25,394
2016	20,306
2017	8,198
Thereafter	43,028
	<u>\$ 163,012</u>

Cambia's total rent expense for leases and agreements for 2012 and 2011 amounted to \$26,906,000 and \$31,816,000, respectively.

Cambia leases office space from 200 Market, a related party. The payments for this lease activity were \$5,110,000 and \$5,079,000 for the years ended December 31, 2012 and 2011, respectively (see Note 2C).

Regence BCBSO is a guarantor for a \$61,000,000 promissory note for 200 Market. The note bears an interest rate of 5.26 percent. Principal and interest payments of \$337,000 are due in monthly installments until the note reaches maturity in December 2015, at which point the remaining principal and interest balance is due. The probability that Regence BCBSO will be required to perform under this guarantee is considered remote. The outstanding balance was \$58,283,000 at December 31, 2012.

Cambia is involved in various legal actions arising in the ordinary course of business and accrues a liability for such matters when it is probable that a liability has been incurred and the amount can be reasonably estimated. When only a range of possible loss can be established, the most probable amount in the range is accrued. If no amount within this range is a better estimate than any other amount within the range, the minimum amount in the range is accrued. It is management's opinion that the resolution of these matters will not have a material effect on Cambia's consolidated financial statements.

15. OTHER COMPREHENSIVE INCOME (LOSS)

Changes in Other Comprehensive Income (Loss) at December 31, 2012 and 2011, consist of the following:

(In thousands)	<u>2012</u>	<u>2011</u>
Unrealized holding gains on investments arising during the period	\$ 128,607	\$ 13,850
Reclassification adjustment for gain included in net income	(68,941)	(31,442)
Other-than-temporary impairment	(140)	(1,265)
Tax (expense) benefit	<u>(11,791)</u>	<u>3,037</u>
Unrealized gain (loss) on investments, net of tax	<u>47,735</u>	<u>(15,820)</u>
Periodic pension and postretirement cost	(11,694)	(74,732)
Tax benefit	<u>2,688</u>	<u>17,188</u>
Periodic pension and postretirement cost, net of tax	<u>(9,006)</u>	<u>(57,544)</u>
Total changes in other comprehensive loss (income)	<u>\$ 38,729</u>	<u>\$ (73,364)</u>

Accumulated Other Comprehensive Income at December 31, 2012 and 2011 is as follows:

(In thousands)	<u>2012</u>	<u>2011</u>
Unrealized holding gains on Investments	\$ 217,546	\$ 169,811
Unrecognized pension and postretirement liabilities	<u>(165,648)</u>	<u>(156,642)</u>
Total Accumulated Other Comprehensive Income	<u>\$ 51,898</u>	<u>\$ 13,169</u>

16. INCOME TAXES

Certain activities of Cambia are subject to federal and state income taxes.

Components of Cambia's income tax provision for the years ended December 31 are as follows:

(In thousands):	<u>2012</u>	<u>2011</u>
Current:		
Federal	\$29,148	\$13,386
State	3,888	2,710
	<u>33,036</u>	<u>16,096</u>
Deferred:		
Federal	9,774	7,225
State	1,411	997
	<u>11,185</u>	<u>8,222</u>
Income tax expense	<u>\$44,221</u>	<u>\$24,318</u>



Components of Cambia's net deferred income tax liabilities for the years ended December 31 are as follows:

(In thousands):	2012	2011
Deferred income tax assets:		
Alternative minimum tax (AMT) credits	\$ 93,468	\$ 94,390
Reserve discount	22,208	28,459
Investments/other basis adjustment	13,766	22,057
Postretirement benefits	20,482	21,337
Accrued liabilities	28,753	20,141
Other	25,986	32,299
	204,663	218,683
Valuation allowance	(87,394)	(89,299)
Deferred income tax assets, net of valuation allowance	117,269	129,384
Deferred income tax liabilities:		
Accumulated depreciation and amortization	(76,973)	(86,243)
Pension	(59,485)	(51,145)
	(136,458)	(137,388)
Net deferred tax liabilities, before OCI items	(19,189)	(8,004)
Deferred tax on OCI:		
Deferred tax on unrealized gains and losses on investments	(103,798)	(80,711)
Deferred tax on unrealized benefit costs	84,468	80,024
Valuation allowance on OCI items	6,152	(3,388)
	(13,178)	(4,075)
Net deferred income tax liabilities	\$ (32,367)	\$ (12,079)

A valuation allowance is recorded to reduce the deferred tax assets associated with the Company's AMT credits to the amount that is more likely than not to be realized. Since the Company expects to be an AMT taxpayer for the foreseeable future, the deferred taxes are valued at the AMT tax rate. Cambia's valuation allowance on net deferred tax assets excluding amounts recorded in OCI decreased by \$1,905,000 and \$16,045,000 during the years ended December 31, 2012 and 2011, respectively.

Cambia has AMT credits of \$93,468,000 and \$94,390,000 in 2012 and 2011, respectively. These credits do not expire. Regence BlueShield of Idaho, Inc., which files a separate company tax return, has a capital loss carry forward of \$1,842,000. The capital loss carry forward expires in 2014.

Cambia's effective rate on pretax income from operations differed from the federal regular tax rate due to application of the AMT system and the Company's expectation that it will be an AMT taxpayer for the foreseeable future, as well as the net result of permanent differences including the IRC §833(b) deduction, dividend received deduction, investment in subsidiaries, the inclusion of state taxes (net of federal tax benefit), and adjustments for prior year tax expense.

At December 31, 2012, the years 2010 and 2011 were open for audit by the Internal Revenue Service and the years 2009 through 2011 were open for audit for the states of Oregon, Utah and Idaho under the three year statute of limitations rule. During 2012, an audit by the IRS was concluded for the year 2009.

As of December 31, 2012 and 2011, there were no material uncertain tax positions for which the Company believes it is reasonably possible that the total amount of tax contingencies will significantly increase or decrease within twelve months of the reporting date. Any interest or penalties associated with these uncertain tax positions would be recorded as part of Income Tax Expense. For the years ended December 31, 2012 and 2011, respectively, there were no material interest or penalties recorded related to uncertain tax positions.

17. MAJOR CUSTOMERS

Revenues related to contracts with CMS in the aggregate constitute more than ten percent of gross revenue. During the years ended December 31, 2012 and 2011, total revenue earned under the contracts were \$1,141,863,000 and \$1,166,222,000, respectively. Related claims were \$1,003,699,000 and \$1,038,829,000 for the years ended December 31, 2012 and 2011, respectively.

18. PRESENTATION OF SELF-FUNDED REVENUE AND AMOUNTS  
ATTRIBUTABLE TO CLAIMS UNDER SELF-FUNDED ARRANGEMENTS

Subsequent to the issuance of the Company's December 31, 2011 consolidated financial statements, management determined that certain amounts historically presented as Underwritten Premium Revenue and Claims Expense, should be disclosed separately in the Consolidated Statements of Operations and Comprehensive Income. The current presentation improves transparency and comparability to other health care services companies. This change had no impact on net income or accumulated surplus for 2012 and 2011. The accompanying financial statements were adjusted as follows:

(In thousands):

	2011	
	As Currently Reported	As Previously Reported
Underwritten Premium Revenue	\$ 5,861,869	\$ 7,814,804
Self-Funded Revenue	1,952,935	-
Less Amounts attributable to claims		
Under Self-Funded Arrangements	1,834,545	-
Net Premium, Self-funded Revenue, and Fee Revenue	5,890,300	7,724,845
Claims Expense	5,070,766	6,905,311

**CAMBIA HEALTH SOLUTIONS, INC.**  
**Consolidating Balance Sheet Information**  
**December 31, 2012**  
 (In thousands)

	Regence BlueShield	Regence BCBSO	Regence BlueShield of Idaho, Inc.	Regence BCBSU	CHS, RIHC & DHS	Regence Rx	Cambia Health Foundation	Reclass/ Eliminations	Total
ASSETS									
Cash and Cash Equivalents	\$ 83,551	\$ 43,479	\$ 40,281	\$ 41,475	\$ 72,007	\$ 4,260	\$ 1,348	\$ -	\$ 286,401
Receivables, net	334,712	261,262	30,081	181,772	42,922	26,193	2	(76,564)	800,380
Investments	1,397,613	684,491	194,510	355,940	164,082	-	66,195	(20,170)	2,842,661
Property, Buildings and Equipment, net	112,853	105,836	40,019	73,464	34,526	6	-	1,190	367,894
Other Assets	137,305	138,344	16,893	20,941	27,296	10	-	(183,978)	156,811
Deferred Compensation Assets	22,892	4,494	1,850	420	18,633	-	-	-	48,289
Deferred Income Taxes	-	-	-	-	52,877	-	-	(52,877)	-
<b>Total Assets</b>	<b>\$ 2,088,926</b>	<b>\$ 1,237,906</b>	<b>\$ 323,634</b>	<b>\$ 674,012</b>	<b>\$ 412,343</b>	<b>\$ 30,469</b>	<b>\$ 67,545</b>	<b>\$ (332,399)</b>	<b>\$ 4,502,436</b>

(Continued)

**CAMBIA HEALTH SOLUTIONS, INC.**  
**Consolidating Balance Sheet Information**  
**December 31, 2012**  
 (In thousands)

	Regence BlueShield	Regence BCBSO	Regence BlueShield of Idaho, Inc.	Regence BCBSU	CHS, RIHC & DHS	Regence Rx	Cambia Health Foundation	Reclass/ Eliminations	Total
<b>LIABILITIES AND SURPLUS</b>									
<b>Liabilities:</b>									
Reserve for Unpaid Claims	\$ 402,843	\$ 253,918	\$ 57,364	\$ 145,846	\$ 3	\$ -	\$ -	\$ (13,899)	\$ 846,075
Reserve for Adjusting Expenses on Unpaid Claims	12,310	7,160	1,833	4,244	-	-	-	-	25,547
Unearned Premiums	120,444	114,936	21,395	77,908	18	-	-	-	334,701
Debt and Other Obligations	56,024	-	16,353	18,227	22,453	-	-	(5,125)	107,932
Accrued Expenses and Other Liabilities	156,413	76,741	24,018	43,151	259,514	21,058	2,013	(245,108)	337,800
Experience Refunds Payable	15,470	2,659	13,187	5,437	-	-	-	-	36,753
Deferred Compensation	22,892	4,494	1,850	420	18,633	-	-	-	48,289
Pension and Postretirement Obligations	-	-	-	-	120,080	-	-	-	120,080
Deferred Income Taxes	39,668	19,150	12,831	13,613	-	(58)	40	(52,877)	32,367
<b>Total Liabilities</b>	<b>826,064</b>	<b>479,058</b>	<b>148,831</b>	<b>308,846</b>	<b>420,701</b>	<b>21,000</b>	<b>2,053</b>	<b>(317,009)</b>	<b>1,889,544</b>
<b>Surplus:</b>									
Accumulated Surplus	1,166,059	707,558	154,228	335,577	141,925	9,469	61,568	(15,390)	2,560,994
Accumulated Other Comprehensive Income (Loss)	96,803	51,290	20,575	29,589	(150,283)	-	3,924	-	51,898
<b>Total Surplus</b>	<b>1,262,862</b>	<b>758,848</b>	<b>174,803</b>	<b>365,166</b>	<b>(8,358)</b>	<b>9,469</b>	<b>65,492</b>	<b>(15,390)</b>	<b>2,612,892</b>
<b>Total Liabilities and Surplus</b>	<b>\$ 2,088,926</b>	<b>\$ 1,237,906</b>	<b>\$ 323,634</b>	<b>\$ 674,012</b>	<b>\$ 412,343</b>	<b>\$ 30,469</b>	<b>\$ 67,545</b>	<b>\$ (332,399)</b>	<b>\$ 4,502,436</b>

(Concluded)

CAMBIA HEALTH SOLUTIONS, INC.  
 Consolidating Balance Sheet Information  
 December 31, 2011  
 (In thousands)

	Regence BlueShield	Regence BCBSO	Regence BlueShield of Idaho, Inc.	Regence BCBSU	CHS, RIHC & DHS	Regence Rx	Cambia Health Foundation	Reclass/ Eliminations	Total
ASSETS									
Cash and Cash Equivalents	\$ 116,832	\$ 44,813	\$ 11,396	\$ 36,644	\$ 96,339	\$ -	\$ 285	\$ -	\$ 306,309
Receivables, net	383,965	285,350	36,176	203,238	77,159	13,447	-	(91,631)	907,704
Investments	1,311,512	656,944	200,673	330,349	94,862	-	57,915	(12,502)	2,639,753
Property, Buildings and Equipment, net	116,843	127,337	42,881	76,098	16,390	-	-	-	379,549
Other Assets	132,385	133,521	15,892	20,969	14,919	-	-	(157,434)	160,252
Deferred Compensation Assets	23,908	4,409	1,941	374	17,644	-	-	-	48,276
Deferred Income Taxes	-	-	-	-	50,317	-	-	(50,317)	-
Total Assets	<u>\$ 2,085,445</u>	<u>\$ 1,252,374</u>	<u>\$ 308,959</u>	<u>\$ 667,672</u>	<u>\$ 367,630</u>	<u>\$ 13,447</u>	<u>\$ 58,200</u>	<u>\$ (311,884)</u>	<u>\$ 4,441,843</u>

(Continued)

**CAMBIA HEALTH SOLUTIONS, INC.**  
**Consolidating Balance Sheet Information**  
**December 31, 2011**  
 (In thousands)

LIABILITIES AND SURPLUS	Regence BlueShield	Regence BCBSO	Regence BlueShield of Idaho, Inc.	Regence BCBSU	CHS, RIHC & DHS	Regence Rx	Cambia Health Foundation	Reclass/ Eliminations	Total
<b>Liabilities:</b>									
Reserve for Unpaid Claims	\$ 488,220	\$ 281,399	\$ 64,398	\$ 170,770	\$ -	\$ -	\$ -	\$ (11,278)	\$ 993,509
Reserve for Adjusting Expenses on Unpaid Claims	12,456	7,814	2,213	4,722	-	-	-	-	27,205
Unearned Premiums	121,836	122,819	21,038	87,344	-	-	-	-	353,037
Debt and Other Obligations	59,222	619	17,227	29,460	17,900	-	-	(5,125)	119,303
Accrued Expenses and Other Liabilities	157,195	99,690	23,628	40,491	226,103	12,149	686	(236,755)	323,187
Experience Refunds Payable	15,043	3,517	12,018	2,000	-	-	-	-	32,578
Deferred Compensation	23,908	4,409	1,941	374	17,644	-	-	-	48,276
Pension and Postretirement Obligations	-	-	-	-	132,258	-	-	-	132,258
Deferred Income Taxes	28,239	14,316	9,213	10,608	-	-	20	(50,317)	12,079
<b>Total Liabilities</b>	<b>906,119</b>	<b>534,583</b>	<b>151,676</b>	<b>345,769</b>	<b>393,905</b>	<b>12,149</b>	<b>706</b>	<b>(303,475)</b>	<b>2,041,432</b>
<b>Surplus:</b>									
Accumulated Surplus	1,104,560	679,332	138,192	294,407	122,324	1,298	55,538	(8,409)	2,387,242
Accumulated Other Comprehensive Income (Loss)	74,766	38,459	19,091	27,496	(148,599)	-	1,956	-	13,169
<b>Total Surplus</b>	<b>1,179,326</b>	<b>717,791</b>	<b>157,283</b>	<b>321,903</b>	<b>(26,275)</b>	<b>1,298</b>	<b>57,494</b>	<b>(8,409)</b>	<b>2,400,411</b>
<b>Total Liabilities and Surplus</b>	<b>\$ 2,085,445</b>	<b>\$ 1,252,374</b>	<b>\$ 308,959</b>	<b>\$ 667,672</b>	<b>\$ 367,630</b>	<b>\$ 13,447</b>	<b>\$ 58,200</b>	<b>\$ (311,884)</b>	<b>\$ 4,441,843</b>

(Concluded)

**CAMBIA HEALTH SOLUTIONS, INC.**  
**Consolidating Statements of Operations and Comprehensive Income Information**  
**Year Ended December 31, 2012**  
(In thousands)

	Regence BlueShield	Regence BCBSO	Regence BlueShield of Idaho, Inc.	Regence BCBSU	CHS, RIHC & DHS	Regence Rx	Cambia Health Foundation	Reclass/ Eliminations	Total
Premium Revenue	\$ 2,451,812	\$ 1,850,098	\$ 459,919	\$ 999,606	\$ -	\$ -	\$ -	\$ -	\$ 5,761,435
Self-funded Revenue	1,019,090	569,215	62,367	306,421	-	-	-	-	1,957,093
Fee Revenue	45,843	23,829	5,248	14,978	133	50,130	-	(41,778)	98,383
Gross Revenue	3,516,745	2,443,142	527,534	1,321,005	133	50,130	-	(41,778)	7,816,911
Less amounts Attributable to Claims Under Self-funded Arrangements	966,916	532,130	57,962	282,694	-	-	-	-	1,839,702
Commissions Expense	61,555	25,778	14,059	22,722	-	-	-	-	124,114
Premium Taxes	38,680	10,001	6,083	207	-	-	-	-	54,971
Net Premium, Self-funded Revenue, and Fee Revenue	2,449,594	1,875,233	449,430	1,015,382	133	50,130	-	(41,778)	5,798,124
Claims Expense	2,029,264	1,573,008	367,097	846,982	-	-	-	-	4,816,351
Operating Expense	408,990	247,470	68,004	129,533	25,375	37,435	-	(41,288)	875,519
Gain on Sale of Real Estate	(2,041)	-	-	-	-	-	-	-	(2,041)
Operating Income	13,381	54,755	14,329	38,867	(25,242)	12,695	-	(490)	108,295
Investment Income, net	76,018	35,059	14,386	23,403	86	-	2,567	-	151,519
Interest Expense	(3,057)	(21)	(1,009)	(17)	(787)	-	-	-	(4,891)
Other Expense, net	(4,030)	(2,781)	(1,143)	(4,177)	9,950	277	3,471	(6,491)	(4,924)
Uninsurable Pool Assessments	(12,294)	(17,237)	(2,386)	(109)	-	-	-	-	(32,026)
Income Before Income Taxes	70,018	69,775	24,177	57,967	(15,993)	12,972	6,038	(6,981)	217,973
Income Tax Expense	8,519	16,549	8,141	10,797	(4,594)	4,801	8	-	44,221
Net Income	61,499	53,226	16,036	47,170	(11,399)	8,171	6,030	(6,981)	173,752
Other Comprehensive Income, net of tax:									
Unrealized Gain on Investments	22,037	12,831	1,484	2,093	7,322	-	1,968	-	47,735
Periodic Pension and Postretirement Cost	-	-	-	-	(9,006)	-	-	-	(9,006)
Other Comprehensive Income (Loss)	22,037	12,831	1,484	2,093	(1,684)	-	1,968	-	38,729
Comprehensive Income (Loss)	\$ 83,536	\$ 66,057	\$ 17,520	\$ 49,263	\$ (13,083)	\$ 8,171	\$ 7,998	\$ (6,981)	\$ 212,481

**CAMBIA HEALTH SOLUTIONS, INC.**  
**Consolidating Statements of Operations and Comprehensive Income Information**  
**Year Ended December 31, 2011**  
 (In thousands)

	Regence BlueShield	Regence BCBSO	Regence BlueShield of Idaho, Inc.	Regence BCBSU	CHS, RIHC & DHS	Regence Rx	Cambia Health Foundation	Reclass/ Eliminations	Total
Premium Revenue	\$ 2,517,950	\$ 1,865,115	\$ 465,870	\$ 1,012,934	\$ -	\$ -	\$ -	\$ -	\$ 5,861,869
Self-funded Revenue	1,018,352	550,223	63,172	321,188	-	-	-	-	1,952,935
Fee Revenue	49,437	27,935	5,568	15,510	1,207	698	-	-	100,355
Gross Revenue	3,585,739	2,443,273	534,610	1,349,632	1,207	698	-	-	7,915,159
Less amounts Attributable to Claims Under Self-funded Arrangements	958,937	517,499	59,238	298,871	-	-	-	-	1,834,545
Commissions Expense	66,262	27,093	15,655	26,829	-	-	-	-	135,839
Premium Taxes	40,006	8,535	5,934	-	-	-	-	-	54,475
Net Premium, Self-funded Revenue, and Fee Revenue	2,520,534	1,890,146	453,783	1,023,932	1,207	698	-	-	5,890,300
Claims Expense	2,154,092	1,621,180	389,859	905,635	-	-	-	-	5,070,766
Operating Expense	367,972	246,340	65,142	130,104	14,655	-	-	-	824,213
Gain on Sale of Real Estate	(36,902)	-	-	-	-	-	-	-	(36,902)
Operating Income	35,372	22,626	(1,218)	(11,807)	(13,448)	698	-	-	32,223
Investment Income, net	59,922	34,008	9,040	13,485	823	-	3,049	-	120,327
Interest Expense	(3,185)	(142)	(1,070)	(26)	(940)	-	-	-	(5,363)
Other Expense, net	(7,503)	(6,187)	(1,239)	(4,222)	6,683	(8)	6,151	(434)	(6,759)
Uninsurable Pool Assessments	(12,268)	(12,416)	(2,081)	(89)	-	-	-	-	(26,854)
Income Before Income Taxes	72,338	37,889	3,432	(2,659)	(6,882)	690	9,200	(434)	113,574
Income Tax Expense	20,878	1,399	2,085	(1,024)	803	256	(79)	-	24,318
Net Income	51,460	36,490	1,347	(1,635)	(7,685)	434	9,279	(434)	89,256
Other Comprehensive Income, net of tax:									
Unrealized Gain on Investments	(9,944)	(6,834)	2,739	1,472	(3,253)	-	-	-	(15,820)
Periodic Pension and Postretirement Cost	-	-	-	-	(57,544)	-	-	-	(57,544)
Other Comprehensive Income (Loss)	(9,944)	(6,834)	2,739	1,472	(60,797)	-	-	-	(73,364)
Comprehensive Income (Loss)	\$ 41,516	\$ 29,656	\$ 4,086	\$ (163)	\$ (68,482)	\$ 434	\$ 9,279	\$ (434)	\$ 15,892