CoverColorado

Statutory Financial Statements
December 31, 2004 and 2003

ACM
Anton Collins Mitchell LLP

AN INDEPENDENT MEMBER OF
BDO SEIDMAN
ALLIANCE

CoverColorado

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Contents

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Independent Auditors' Report

The Board of Directors
CoverColorado
Glendale, Colorado

We have audited the accompanying statutory statements of admitted assets, liabilities and surplus of CoverColorado (the "Program"), a component unit of the State of Colorado, as of December 31, 2004 and 2003 and the related statutory statements of operations, surplus and cash flows for the years then ended. These financial statements are the responsibility of the Program's management. Our responsibility is to express an opinion on these 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing 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 over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

The Program presents its statutory financial statements in conformity with the accounting practices prescribed or permitted by the Division of Insurance of the State of Colorado. The effects on the financial statements of the variances between such practices and accounting principles generally accepted in the United States of America are described in the Summary of Accounting Policies.

In our opinion, because of the effects of the matter discussed in the preceding paragraph, the statutory financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the Program as of December 31, 2004 and 2003 and the results of its operations and its cash flows for the years then ended.

Anton Collins Mitchell LLP

May 11, 2005

Accountants & Consultants

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CoverColorado

Statutory Statements of Admitted Assets, Liabilities and Surplus

December 31,	**2004**	2003
Admitted Assets		
Cash and cash equivalents (Note 1)	**$ 3,537,414**	$ 6,760
Investments (Note 3)	**39,066,372**	20,213,163
Accounts receivable	**1,145,081**	138,905
Accrued interest receivable	**239,086**	56,136
Restricted cash held by the State Treasurer (Note 4)	**1,556,982**	11,179,936
Total admitted assets	**$ 45,544,935**	$ 31,594,900
Liabilities and Surplus		
Reserve for health policy claims (Note 2)	**$ 11,295,079**	$ 8,797,545
Advance premiums	**1,177,936**	642,636
Assessment overpayments and appeals	**1,089,484**	-
Deferred revenue	**8,600,632**	5,634,952
Accrued expenses	**297,746**	456,002
Total liabilities	**22,460,877**	15,531,135
Commitments and contingencies (Notes 2, 4, 5, 6 and 7)		
Surplus	**23,084,058**	16,063,765
Total liabilities and surplus	**$ 45,544,935**	$ 31,594,900

See accompanying independent auditors' report, summary of accounting policies and notes to financial statements.

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Statutory Statements of Operations

Year Ended December 31,	**2004**	2003
Revenues:		
Premiums earned	**$ 21,930,259**	$20,559,263
Federal TAA grant	**2,026,974**	-
State of Colorado (Note 4)	**836,007**	5,944,682
Assessments	**21,454,868**	3,709,199
Total revenues	**46,248,108**	30,213,144
Expenses:		
Health policy benefits (Note 2)	**36,619,970**	28,782,284
General and administrative expenses (Notes 5, 6 and 7)	**3,148,686**	3,007,299
Total expenses	**39,768,656**	31,789,583
Gain (loss) from operations	**6,479,452**	(1,576,439)
Investment income:		
State of Colorado (Note 4)	**248,720**	381,113
Net increase in fair value of investments	**290,700**	103,829
Total investment income	**539,420**	484,942
Net gain (loss)	**$ 7,018,872**	$(1,091,497)

See accompanying independent auditors' report, summary of accounting policies and notes to financial statements.

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Statutory Statements of Surplus

Years Ended December 31, 2003 and 2004

Balance at January 1, 2003	$ 17,147,954
Net loss	1,091,497
Change in non-admitted assets	7,308
Balance at December 31, 2003	16,063,765
Net gain	7,018,872
Change in non-admitted assets	1,421
Balance at December 31, 2004	$ 23,084,058

See accompanying independent auditors' report, summary of accounting policies and notes to financial statements.

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Statutory Statements of Cash Flows

Year Ended December 31,	**2004**	2003
Cash provided by operating activities:		
Premiums received	**$ 22,287,443**	$ 20,369,773
Assessments received	**24,681,972**	8,512,023
State of Colorado	**10,707,681**	11,634,457
Federal TAA grant	**2,026,974**	-
Health policy claims paid (Note 2)	**(34,122,436)**	(27,577,931)
General insurance expenses paid	**(3,296,932)**	(2,902,785)
Cash provided by underwriting operations	**22,284,702**	10,035,537
Investment income received	**107,749**	55,903
Net cash provided by operating activities	**22,392,451**	10,091,440
Cash used in investing activities:		
Proceeds from maturity of investments	**20,213,163**	652,611
Purchase of investments	**(39,066,372)**	(20,213,163)
Purchase of furniture and equipment	**(8,588)**	(2,073)
Cash used in investing activities	**(18,861,797)**	(19,562,625)
Increase (decrease) in cash and cash equivalent	**3,530,654**	(9,471,185)
Cash and cash equivalents, beginning of year	**6,760**	9,477,945
Cash and cash equivalents, end of year	**$ 3,537,414**	$ 6,760

See accompanying independent auditors' report, summary of accounting policies and notes to financial statements.

Statutory Statements of Cash Flows (Continued)

Year Ended December 31,	**2004**	2003
Reconciliation of net gain (loss) to net cash provided by operating activities:		
Net gain (loss)	**$ 7,018,872**	$ (1,091,497)
Adjustments to reconcile net gain (loss) to net cash provided by operating activities:		
Depreciation	**10,009**	9,381
Changes in operating assets and liabilities:		
(Increase) in accounts receivable	**(828,060)**	(138,905)
(Increase) in premium receivable	**(178,116)**	-
(Increase) in accrued interest receivable	**(182,950)**	(47,926)
Increase in reserve for health policy claims	**2,497,534**	1,204,354
Increase (decrease) in advance premiums	**535,300**	(189,491)
Increase in assessment overpayments and appeals	**1,089,484**	-
Increase in deferred revenue	**2,965,680**	4,941,730
Increase (decrease) in accrued expenses	**(158,256)**	95,132
Decrease in restricted cash held by the State Treasurer	**9,622,954**	5,308,662
Net cash provided by operating activities	**$ 22,392,451**	$ 10,091,440

See accompanying independent auditors' report, summary of accounting policies and notes to financial statements.

Summary of Accounting Policies

Organization and Nature of Business

CoverColorado (the "Program") is a non-profit unincorporated public entity created pursuant to Colorado Revised Statute 10-8-501. The purpose of the statute is to provide access to health insurance for those Colorado residents who are unable to obtain health insurance, or who are unable to obtain health insurance except at prohibitive rates or with restrictive exclusions.

The statute had a sunset provision provided that, if not otherwise extended, the statute would be repealed effective July 1, 1993. On June 2, 1993, the sunset provision was repealed by Senate Bill 93-55.

On June 5, 2001, the General Assembly of the State of Colorado approved House Bill 01-1319 (the "Bill"), which amended the Colorado Revised Statute 10-8-501. The Bill changed the plan name from "Colorado Uninsurable Health Insurance Plan" to "CoverColorado". In addition, the Bill designated the Program as the state alternative mechanism for health care coverage under federal "Health Insurance Portability and Accountability Act of 1996" and allowed the board of directors of the Program to assess a special fee against insurers for the financial solvency of the Program. The Bill also redefined certain program eligibility, coverage terms and the board of directors' powers and duties.

The Program is an instrumentality of the State of Colorado (the "State") and is considered to be a component unit of the State only for the purpose of the State's annual financial reporting.

Summary of Accounting Policies

Basis of Presentation

The statutory financial statements have been prepared in conformity with accounting practices prescribed or permitted by the Division of Insurance of the State of Colorado (the "Division"), which vary in some respects from accounting principles generally accepted in the United States of America. The most significant of these variances resulting from prescribed practices is that certain assets designed as "non-admitted assets" have been excluded from the statements of admitted assets and liabilities and recorded as a charge to surplus and assessments paid by the insurance carriers are recorded as deferred revenue at the assessment date and amortized ratably over the period in which the assessment revenue was forecasted to match expenses. The only variance resulting from a permitted practice is that restricted cash held by the State Treasurer is included as an admitted asset. The Program has obtained permission from the Division to use this practice.

Colorado has adopted the National Association of Insurance Commissioners' ("NAIC") statutory accounting practices as the basis for its statutory accounting practices. In 1999, the NAIC completed a process to codify statutory accounting practices for certain insurance enterprises, resulting in a revised Accounting Practices and Procedures Manual (the revised "Manual"), effective January 1, 2001. Colorado requires insurers to comply with the provisions of the revised Manual and the Program prepared its December 31, 2004 and 2003 financial statement and footnotes in accordance with the revised Manual. There was no effect on the Program's surplus due to the adoption of the revised Manual. There are no material differences between codified NAIC statutory accounting practices and those prescribed by Colorado.

The impact of differences between reported and prescribed statutory accounting practices is as follows:

Year Ended December 31,	**2004**	2003
Statutory net gain (loss)-reported	**$ 7,018,872**	$ (1,091,497)
Permitted accounting practice	**9,622,954**	5,308,662
Statutory net income prescribed	**$ 16,641,826**	$ 4,217,165
Statutory surplus-reported	**$ 23,084,058**	$ 16,063,765
Restricted cash held by the State Treasurer	**(1,556,982)**	(11,179,936)
Statutory surplus – prescribed	**$ 21,527,076**	$ 4,883,829

The impact of the differences between statutory and generally accepted accounting principle ("GAAP") basic accounting practices is as follows:

Year Ended December 31,	**2004**	2003
Statutory net gain (loss)-reported	**$ 7,018,872**	$ (1,091,497)
Statutory to GAAP adjustments	**12,588,634**	10,250,392
Net income – GAAP	**$ 19,607,506**	$ 9,158,895

December 31,	**2004**	2003
Statutory surplus reported	**$ 23,084,058**	$ 16,063,765
Restricted cash held by the State Treasurer	**(1,556,982)**	(11,179,936)
Deferred revenue	**8,600,632**	5,634,952
Furniture and equipment	**12,503**	13,924
Surplus – GAAP	**$ 30,140,211**	$ 10,532,705

Use of Estimates

The preparation of statutory financial statements in conformity with accounting principles prescribed or permitted by the Division requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the statutory financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates included the reserve for health policy claims. Actual results could differ from those estimates.

Cash and Cash Equivalents

For purposes of the statutory statements of cash flow, the Program considers all highly liquid debt security investments with original maturities of three months or less to be cash investments.

Investments

Investments are carried at fair value in the accompanying balance sheet. Fair value is determined using current market value. Investment income, including interest, dividends and realized and unrealized gains and losses, are included in the accompanying statements of revenues and expenses and change in fund net assets in the period in which they occur.

Reserve for Health Policy Claims

The reserve for health policy claims provides for reported claims and incurred but not reported claims, and loss expenses to administer the claims. The actuarial projections of ultimate losses on reported claims and claims incurred but not reported are based on a composite of the Program's experience. Adjustments to the probable ultimate liability for claims are made continually, based on subsequent developments and experience, and are included in operations as incurred. However, the actual cost of settling all claims may be more or less than the reserve as of December 31, 2004.

Income Taxes

The Internal Revenue Service issued a favorable determination letter dated February 4, 1992 exempting the Program from income taxes pursuant to Section 115 of the Internal Revenue Code. Management believes that the Program continues to operate in accordance with tax-exempt requirements.

Advance Premiums

Advance premiums consist of premiums received prior to their policy effective date.

Summary of Accounting Policies

Revenues

The Program is funded by premiums charged to insureds, an allocated portion of the Unclaimed Insurance Moneys Fund and up to $2.5 million annually from the Business Associations Unclaimed Moneys Funds ("BAUMF"). Moneys other than premiums charged to insureds are subject to annual appropriation by the General Assembly of the State of Colorado. The Program began receiving funds from the Unclaimed Insurance Moneys Fund in 1995. House Bill 93-1336, which was effective July 1, 1993, entitled the Program to receive amounts from the BAUMF, reduced for amounts required to pay claims as determined by the Administrator of the BAUMF. House Bill 93-1336 contained a sunset provision whereby the funds received by the Program from the BAUMF were to terminate on July 1, 1997. In early 1997, however, Senate Bill 97-041 was passed and signed by the Governor, whereby the allocations received by the Program from the BAUMF were extended indefinitely, effective July 1, 1997.

In November 1992, the Colorado electorate approved Article X, Section 20 of the Colorado Constitution, which restricts the State's ability to increase existing taxes or impose new taxes. The effect of this Article on the future funding of the Program, if any, is uncertain.

Premiums collected and amounts appropriated which exceed net premiums required for the year are held primarily in highly liquid investments and can be used to offset future losses or reduce plan premiums for subsequent years as determined by the board of directors of the Program.

Effective July 1, 2001, in accordance with Senate Bill 00-057, the Program no longer receives an allocated portion of the Unclaimed Insurance Monies Fund and the BAUMF. These amounts are put into the Unclaimed Property Trust Fund (the "Fund"). The Program receives all interest derived from the fund.

Premiums are prepaid primarily monthly and are recognized as revenue during the month earned. Revenue from the State of Colorado is recognized when the funds are received by the State Treasurer.

Effective March 2002, the balance in the Fund and related interest income will decrease significantly due to a decision made by the Joint Budget Committee to borrow money from the Fund to cover state budget shortfalls. Management has determined that the change of funding will create a significant decrease in program revenues, resulting in a need to assess Colorado insurers for excess losses in order to maintain the financial solvency of the Program. As discussed in the above paragraph, the Program was granted authority under House Bill 01-1319 to assess a special fee against insurers.

In accordance with House Bill 01-1319, prior to the notice of the first assessment to be paid by the insurers, CoverColorado has obtained two actuarial evaluations of the amount of the assessment. As a result of such actuarial evaluations, which were obtained in May 2002, CoverColorado notified insurers of its first assessment of approximately $9.3 million in July 2002, which was due in August 2003. CoverColorado notified insurers of another assessment of approximately $29.8 million in July 2003, which was collected beginning in May 2004.

The Program records deferred revenue as amounts are received for the annual assessments. On August 1, 2003, the beginning period of benefit for the first annual assessment, the Program recorded receivable relating to the assessments and deferred revenue for the portion of the assessment due but not yet received as of August 1. Subsequent to August 1 of each year, the Program will amortize the annual assessments deferred revenue ratably over the period from August 1 through July 31.

Management believes the Program will be able to meet its claim obligations as they become due. At December 31, 2004, $1,556,982 of restricted cash held by the State Treasurer is available to pay claims, if necessary.

Credit Risk Concentration

The Program maintains cash and cash equivalents at financial institutions. The Program maintains balances in excess of federally insured limits at financial institutions.

1. Cash and Invested Cash

At December 31, 2004 and 2003, all cash and invested cash were maintained in money market accounts and highly liquid obligations of the United States and certain U.S. government agencies with maturities of three months or less.

2. Reserve for Health Policy Claims

The activity in the reserve for health policy claims is summarized as follows:

	2004	2003
Balance at December 31,	**$ 8,797,545**	$ 7,593,191
Incurred related to:		
Current year	**33,446,476**	28,440,390
Prior years	**3,173,494**	341,895
Total incurred	**36,619,970**	28,782,285
Paid related to:		
Current year	**24,617,244**	21,518,582
Prior years	**9,505,192**	6,059,349
Total paid	**34,122,436**	27,577,931
Balance at December 31,	**$ 11,295,079**	$ 8,797,545

As a result of changes in estimates of insured events in prior years and as increase in the number of insureds, the provision for health policy claims increased by $2,497,534 and $1,204,354 in 2004 and 2003.

3. Investments

The Program's cash equivalents include highly liquid investments with maturities of three months or less. Colorado statutes specify investment instruments meeting defined rating and risk criteria in which Colorado governmental units may invest.

The Program's investments are recorded at fair value and are categorized to give an indication of the level of credit risk assumed by the Program at year-end. Category one includes investments that are insured or registered or for which the securities are held by the entity or its agent in the Program's name. Category two includes uninsured and unregistered investments for which the securities are held by the broker's or dealer's trust department or agent in the Program's name. Category three includes uninsured and unregistered investments for which the securities are held by the broker or dealer, or by its trust department or agent, but not in the Program's name. All investments held in the Program are classified as Category one.

December 31, 2004	**Amortized Cost**	**Estimated Fair Value**
U.S. Government agency bonds	**$ 39,271,794**	**$ 39,066,372**

December 31, 2003	Amortized Cost	Estimated Fair Value
U.S. Treasury securities	$ 20,213,163	$ 20,213,163

The following represents the maturities of investments as of December 31, 2004:

	Amortized Cost	Estimated Fair Value
Within one year	$ 23,768,154	$ 23,669,802
After one year through five years	15,503,640	15,396,570
	$ 39,271,794	$ 39,066,372

4. Funds Held by the State Treasurer

Restricted cash held by the State Treasurer was as follows:

December 31,	**2004**	2003
Restricted cash held by the State Treasurer at beginning of year	**$ 11,179,936**	$ 16,488,598
Special grant from Governor's office	-	5,000,000
Unclaimed Insurance Moneys Fund	**836,007**	944,682
Interest income, net of investment fees	**248,720**	381,113
	12,264,663	22,814,393
Less amounts transferred to the Program	**10,707,681**	11,634,457
Funds held by the State Treasurer	**$ 1,556,982**	$ 11,179,936

Funds of $1,556,982 and $11,179,936 represent the unused amounts allocated to the Program by the General Assembly of the State of Colorado totaling $1,556,982 and $6,179,936 as of December 31, 2004 and 2003 and a special grant from the Governor's office of the State of Colorado totaling $5,000,000 as of December 31, 2003.

Restricted cash held by the State Treasurer is invested by the State with the related interest income being allocated net of investment fees to the Program's account.

5. Administrative Agreement

The Program has entered into multi-year agreements with third-party administrators for its general administration, including processing of claims and collection of premiums. Fees for such services were $1,644,943 and $1,530,026 for the years ended December 31, 2004 and 2003.

6. Public Employees' Retirement Association of Colorado

The Program participates in the State Division Trust Fund (the "Trust"), a cost-sharing multiple-employer defined benefit pension plan administered by the Public Employees' Retirement Association of Colorado ("PERA"). The Trust provides retirement and disability and death benefits for its members or their beneficiaries. All employees and board members of the Program are members of the Trust. State statutes have assigned the Colorado Legislature the authority to establish benefit provisions of the Trust.

Plan members and the Program are required to contribute at rates set by State statutes. The current contribution rate for members is 8% of covered salary. The Program's contributions to the Trust for the years ended December 31, 2004 and 2003 were $27,601 and $22,866, respectively, which was equal to the Program's required contributions for year-end.

7. Commitments and Contingencies

Operating Lease

The Program leases office facilities under an operating lease, which expires in 2007. Total rental expense for the year ended December 31, 2004 and 2003 was $23,473 and $20,908, respectively.

The future minimum annual rental commitment under this lease is as follows:

Year Ending December 31,	
2005	$ 28,300
2006	29,200
2007	30,100
	$ 87,600

Litigation

The Program is involved in litigation incurred in the normal settlement of claims liabilities.

In addition, the Program, the State of Colorado, the Colorado Division of Insurance and the Commissioner of Insurance ("the Parties") were involved in litigation with a stop-loss insurance carrier relating to the assessments. The carrier asserted, among other things, that the assessment is a violation of Taxpayer Bills of Rights ("TABOR") and that the funding mechanism under Insurance Regulation 4-2-22 violates Colorado Revenue Statue Section 10-8-530. The carrier alleged that the assessment scheme generally violates TABOR because the assessment is really a tax and, under TABOR, such a tax must be approved in advance by the voters. The parties reached a mediated settlement in 2004, and the Program has no liability to the carrier with regard to this action.

Line of Credit Agreement

In September, 2003, the Program entered into a line of credit agreement with a bank for a $4,000,000 revolving line of credit. The agreement requires monthly interest only payments at the prime rate (4.0% at December 31, 2004), matures in November 2005 and is secured by short term investments held by the Program. No amounts were borrowed against the line of credit during the year ended December 31, 2004 or 2003.