Vhi Healthcare Annual Report & Accounts 2004

HEALTHCARE

IT'S ALL ABOUT LIVING

CONTENTS

BOARD OF DIRECTORS

Mr. Bernard Collins
Chairman
Bernard Collins is Chief Executive Officer of Lifemed Consulting Limited. Mr. Collins received a B.A. Honours in Applied Industrial Psychology/Business from University College Cork, Ireland. Mr. Collins maintains positions at board level on many other associations, the American Chamber of Commerce, Irish Medical Devices Association and other government appointed bodies. (*)

Ms Patricia Ennis B.Arch. F.R.I.A.I.
Managing Director,
Kildare Architects Ltd. (#)

Mr Kevin Moynihan F.C.A.
Principal, Kevin G. Moynihan & Co. Chartered Accountants, Chairman, Killarney Technology Innovation Centre 2003/2004 , Chairman, Chambers of Commerce of Ireland - Taxation Committee 1993/95 . Chairman, Southern Region Chambers of Commerce of Ireland 1992/93, President, Killarney Chamber of Commerce 1991/93.

Mr Pat Farrell M.M.I.I.
Chief Executive, Irish Bankers Federation
Chairperson, Audit Committee. (#)

Mr Humphrey Murphy
Managing Director, Global Stainless Ltd., Member of Governing Body, University College Cork 1997-2000, 2000-2003, 2004 to date. Chairman of UCC Audit Committee 2000-2003, Chair of Risk Management Group. Member of Cork Chamber of Commerce, Former Member of National Trade Advisory Board, Former Cork Regional Chairman of SFA. (*)

Ms Gillian Bowler F.M.I.I., F.Mgt.I.
Chairman, Budget Travel Ltd., Chairman, Failte Ireland, Chairperson, Irish Life & Permanent, Plc., Non-Executive Director, Grafton Group, Non-Executive Director, Clear Channel Ireland, Board Member, Michael Smurfit Graduate School of Business, UCD, Board Member, Social Innovations Ireland, Member,Executive Committee Institute of Directors. (*)

(#) denotes Member of Audit Committee
(*) denotes Member of Remuneration Committee

Mr Liam Twohig B.Comm. F.C.A.
Managing Partner, Baker, Tilly O'Hare, Chartered Accountants and Business Advisors. Past President, German-Irish Chamber of Industry and Commerce. Member, Institute of Chartered Accountants in Ireland, Disciplinary Appeals Committee. (#)

Mr Joseph O'Leary F.C.C.A.
Partner – Patrick McNamara & Associates – (Cork) Auditors, Accountants and Taxation Consultants. Past Member of the National Council for Education Awards (N.C.E.A.), Irish Region President of the Chartered Association of Certified Accountants (A.C.C.A.) 1994/95, Past Member of the Irish Region Executive of the Chartered Association of Certified Accountants.

Mr Phil Flynn
Chairman ICC Investment Bank Limited; Chairman, Bank of Scotland (Irl.), Chairman, Ballyfermot Partnership Company Ltd.,Director, National College of Ireland, Director, Harcourt Developments Ltd, Director, P. Elliott & Company Ltd., Director, Capital Route Private Hire Ltd.

Mr Christy Cooney
Master of Education,
Assistant Director General FÁS, Director, Pairc an Chrocaigh Teoranta, Member, Broadcasting Complaints Commission, Chairman GAA Council 2001-2003.

COMPARATIVE RESULTS AND GRAPHS

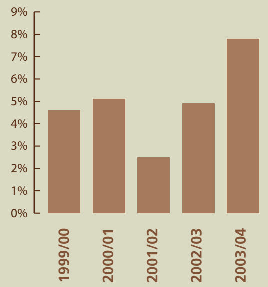
COMPARATIVE RESULTS

	2000 €'000s	2001 €'000s	2002 €'000s	2003 €'000s	**2004** **€'000s**
Earned premium	489,257	548,059	596,594	687,583	**802,992**
Claims incurred	422,532	471,370	520,502	595,169	**663,324**
Unexpired risks reserve	-	-	15,279	19,871	**15,641**
Operating expenses	36,683	64,904	57,782	58,095	**66,322**
Investment return	(133)	24,931	15,864	24,684	**13,980**
Taxation charge	7,506	8,557	4,189	5,308	**9,379**
Surplus for the year	22,403	28,159	14,706	33,824	**62,306**
Surplus / income ratio	4.6%	5.1%	2.5%	4.9%	**7.8%**
Reserves	139,038	167,200	181,907	215,732	**278,038**
Minimum solvency	91,688	98,901	107,240	120,860	**135,053**
Financial Ratios	%	%	%	%	**%**
*Solvency margin level	28.4	30.5	30.5	31.4	**34.6**
Claims as a % of earned premium	86.4	86.0	89.8	89.4	**84.6**
Operating expenses as % of earned premium	7.5	11.8	9.7	8.4	**8.3**

*Minimum solvency margin as shown above is calculated in accordance with the provisions of the 1976 EU Non-Life Regulations, which Vhi Healthcare is not currently required to comply with.

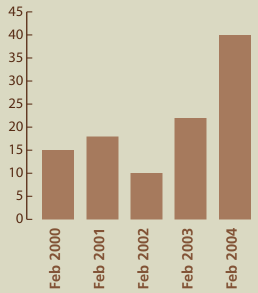
The Board strives to achieve a solvency margin level equivalent to 40% of earned premium, which is considered by commercial insurance companies to be the appropriate level.

SURPLUS AS % OF EARNED PREMIUM

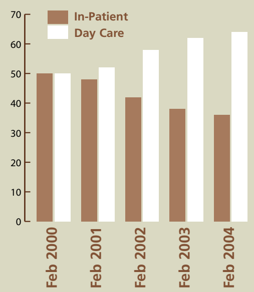


The surplus over 5% has been allocated to reduce the rate of premium increase at 1st September 2004.

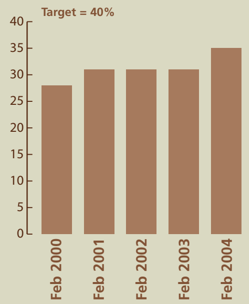
NET SURPLUS PER MEMBER = €40



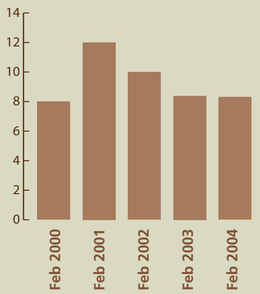
CLAIMS MIX



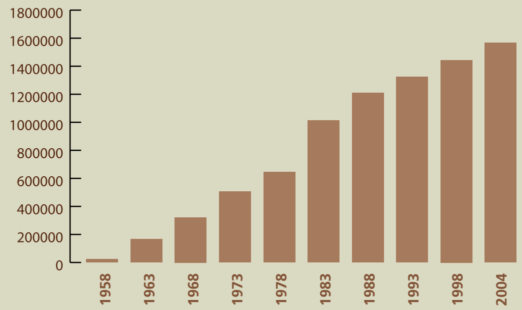
RESERVES RATIO



OPERATING EXPENSES AS % OF EARNED PREMIUM



MEMBERSHIP GROWTH: 46 YEARS HISTORY



CHAIRMAN'S REVIEW

INTRODUCTION

The year ended 29th February 2004 was bittersweet in many respects. On the positive side Vhi Healthcare performed extremely effectively. For the third year in a row the operating cost ratio was reduced; claims costs came in well below budget; new innovative products were launched and a small increase in membership numbers was recorded. All of these factors contributed to an improved surplus over the previous year.

Notwithstanding this performance, the long-term viability of the business remains in doubt. Seven years after the arrival of competition in the market the Government finally delivered on their long-standing policy decision and introduced Risk Equalisation regulations with effect from 1st July 2003. However, Government has delegated responsibility for recommending the activation of Risk Equalisation payments to the Health Insurance Authority (HIA). Following their first review of returns for the six months to 31st December 2003, the HIA decided not to recommend the commencement of Risk Equalisation.

In the absence of Risk Equalisation in this competitive community rated market there is nothing that the Board or management can do to guarantee the long-term viability of this business. It is not only Vhi that is at risk, but the system of Community Rating, which has served the Irish public so well over the past 47 years. I have chosen these words with care and thus I feel obliged to deal initially and in some detail with this crucial issue of Risk Equalisation.

RISK EQUALISATION

At the heart of the issue of Risk Equalisation is the inherent conflict between the social policy of Community Rating and the economic policy of competition. Community Rating is the funding system for health insurance in Ireland. It means that everyone pays the same premium regardless of age, gender or health. Ireland's Community Rated health insurance system is envied around the world for its fairness. Unlike other systems where your premium goes up if you are older or if you get sick, Community Rating means that everyone pays the same regardless of age, gender or health. Premiums are affordable throughout a lifetime due to the pooling of resources between the old and the young, the sick and the healthy.

Successive Irish governments have always supported the principle of Community Rating as being in the interests of the general public. In it's White Paper on Private Health Insurance (1999) the Minister for Health and Children at the time stated that:

"*In particular, the inter-generational solidarity which is at the very core of community rating in Ireland has made insurance accessible to those (i.e. the elderly and the chronically ill) who might otherwise not be able to afford the cost of cover.*"

However, on its own, Community Rating is inherently anti-competitive and can only work perfectly in a monopoly market. Competition, on the other hand, is an important economic objective. It should deliver to customers better prices, more choice and greater efficiency.

The challenge lies in ensuring that the conflicting ideals of Community Rating and competition can both operate effectively in the same market. The mechanism that allows this to happen is called Risk Equalisation. In the absence of Risk Equalisation over the past seven years the following has resulted in the Irish health insurance market:

- Community Rating cannot be applied across the market.
- Competition does not exist across the market i.e. it is currently focused only on the younger age groups.
- The price of health insurance is higher than it should be.
- One company is generating large windfall profits and as a result Irish consumers are subsidising the cost of health insurance in the UK.
- Product development has been handicapped.

Since the arrival of competition into the community rated Health Insurance market in Ireland in 1996, Vhi Healthcare has had to make a critical decision at each pricing point, i.e. whether to charge a true community rated premium to its members, or to price premiums to secure the financial stability of the business and, by implication, the market. On each occasion over the past seven years Vhi Healthcare has decided to price for stability thereby depriving its members of the full benefits of Community Rating. To date, this decision has only been justified on the basis that Government policy has been consistently in favour of Risk Equalisation throughout this period and it was expected that it would only be a matter of time before bureaucratic and regulatory problems in Dublin and Brussels would be resolved, allowing regularisation of the market place.

However, the HIA decision changes the future outlook entirely. It can no longer be defensible to charge Vhi Healthcare members more than a true community rated price. Without Risk Equalisation, the consequences in cash flow terms for Vhi Healthcare of charging such a price would be a net outflow of cash in the year to 28 February 2006 and subsequent years, until the total cash reserves are wiped out in relatively few years.

The Board has been confronted with a conflict that cannot be reconciled. Do we protect the stability of the business (and the market) and deprive our members of a true community rated premium or do we charge our members the price to which they are entitled in a community rated market? We have decided that at our next price review on 1st September 2004 we will change the pricing policy we have pursued to date and establish a premium based on a true community rate.

A further consequence of a community rated market without Risk Equalisation is that competition is entirely directed at the younger age profile within the market. Vhi Healthcare does not encounter competition in the older, unprofitable section of the market. There is much evidence to suggest that our competitor's strategy is to gain 100% of 25% of the market i.e. the highly profitable young groups, rather than achieve 25% of the total market. The absence of Risk Equalisation encourages and hugely rewards this discriminatory strategy.

It is an irrefutable fact (borne out by our competitor's profit margins and hugely inflated costs) that the way in which competition has been allowed to develop within the health insurance market in Ireland has added to the cost of the product for consumers. The huge price advantages that accrue to the company with the lower age profile provides no incentive for them to achieve cost or other efficiencies. On the contrary a strategy of pitching prices at just below the Vhi Healthcare price level has allowed our competitor to generate enormous windfall profits at the expense of the Irish consumer and the Irish health insurance market.

To put it into perspective it is estimated that our competitor made more money in Ireland in 2002 from 282,000 customers than Vhi did on 1.5 million customers! This was not due to greater efficiency, indeed the opposite was the case. It was due purely and simply to the disproportionately younger age profile of its membership who, naturally, have fewer and smaller claims.

It is our deeply held conviction that by not activating Risk Equalisation, the Authority has failed in its duty to ensure a sustainable and competitive community rated market in Ireland.

Finally, under this heading, I find it most alarming but perhaps not surprising that in their report dated 28th April 2004, the HIA noted that not all insurers completed the returns on the basis sought by them and that this resulted in inconsistencies in the returns filed. In their pursuit of windfall profits from the Irish health insurance market our competitor has now opposed the Irish Government at European Commission level, is currently taking a case against the European Commission in the European Court of First Appeal and is apparently refusing to co-operate with the Health Insurance Authority in Ireland. While this is going on health insurance costs in Ireland remain higher than they should be and our long established and trusted system of Community Rating is being put at a risk.

It is impossible to overstate the fundamental importance of Risk Equalisation to the future of Vhi Healthcare and indeed the future of the Community Rating system in Ireland. Our auditors make specific reference in their audit opinion to the likelihood of deficits being incurred by Vhi Healthcare in future years. This would have a severe impact on the stability of the entire market.

I now turn to other issues of importance to our business.

DIVERSIFICATION

All indications from our market research show that traditional health insurance, with a market penetration of 50%, has become a mature market where future growth prospects are far more limited than heretofore. The likely arrival of more competitors to the market will have a further impact on our ability to materially increase our current market share. The need to diversify our product range is a key element of our business strategy.

A number of initiatives have previously been undertaken as part of this strategy e.g.:

- Vhi Global – the health insurance product for those staying for extensive periods abroad;
- Vhi HealthSteps – the health insurance product providing cover for primary care providers e.g. GPs, physiotherapists etc; and
- Vhi Corporate Solutions – services directed at the Corporate market including Occupational Health (during the year we opened an Occupational Health centre on the Naas Road in Dublin), Employee Assistance Programmes and Staff Survey schemes.

I am pleased to report continued growth in all of these products and services during the year.

In February 2004, we launched Multi Trip from Vhi Healthcare, our first venture into the non-medical area. This innovative product has brought huge cost savings to the growing annual travel insurance market. The product has been a tremendous success and is attracting customers at the rate of 500 per day. In the first three months we had exceeded our best sales projections for the initial year!

As I write this review we have just launched Vhi Decare Dental insurance. This is a range of three dental insurance plans which we are bringing to market in Ireland in a joint venture with a major US dental insurer, DeCare International.

We have a number of other products and services in course of development or undergoing detailed analysis. Further launches are planned for 2005 and subsequent years. However, a major constraint on our diversification strategy continues to be our corporate status.

COMMERCIAL FREEDOM

As a statutory body operating in the state sector, the current corporate status of Vhi Healthcare impedes our progress in both our core business and our diversification strategy. All pricing changes, product enhancements, new product innovations and developments etc. require the prior approval of the Minister for Health and Children. This lack of flexibility places Vhi Healthcare at a distinct disadvantage when compared to our competitors who are free to interpret the regulations and act without delay. During the year Vhi Healthcare met with the Minister to discuss the future corporate structure of Vhi Healthcare. I am delighted to report that the Minister has agreed to bring proposals to Government to incorporate Vhi Healthcare. This will involve Vhi moving from a Statutory Body to a company owned by the State. The legislation required to do this is not complicated but other pressing legislative demands within the Department means that this legislation is unlikely to be enacted until Spring 2005.

While we understand the pressures facing the Department, Vhi Healthcare is extremely concerned at the delay envisaged for the passing of the necessary legislation. The lack of commercial freedom under our current corporate structure is seriously hindering the strategic management of the business.

COST CONTAINMENT INITIATIVES

Vhi Healthcare is very conscious of the need to control costs and works with providers to bring costs down. We have kept fee increases to medical consultants in line with national wage agreements over the past ten years. Fixed Price Packages ensure that a growing number of procedures are carried out in the most appropriate settings, in line with best practice. Last year alone this saved our members in excess of €128 million, which equates to 16% of annual premium. The global trend of providing more services on a daycare basis is increasing and Ireland is no exception. During 2003/04 almost 63% of all claims paid by Vhi Healthcare were provided in a daycare setting. We continue to work with providers to reduce the average length of in-patient stays and increase the number of procedures carried out on a daycare basis. Last Autumn, Shandon Street Hospital, Cork became the first Vhi approved stand-alone Day Care Centre to provide surgical/diagnostic treatment for Vhi members in the greater Cork area. The provision of more daycare facilities such as this represents significant cost saving to Vhi Healthcare and ensures that our members receive quality modern healthcare in the most appropriate way.

Another cost saving initiative announced during the year was a new agreement to provide daycare Radiotherapy treatment for cancer patients. This initiative will save patients from €150 to €2,000 depending on the location of the tumour and the type of treatment which can involve between 15 and 35 radiotherapy sessions. This represents a significant cost saving to Vhi members as eight in ten patients already attend on a daycare basis. We are currently examining further ways in which we can achieve more cost savings by working closely with our many service providers.

BOARD

My appointment as Chairman of the Voluntary Health Insurance Board during the middle of the year came as a result of the decision by my predecessor Mr Derry Hussey to step down from the position he occupied with such diligence and skill since March 1997. Mr Hussey presided over a period of strong growth for Vhi including a membership increase of 134,000 persons since his appointment. During that period Mr Hussey proved to be a very effective Chairman of a company in transition and oversaw the development of Vhi into a company well equipped operationally to face the challenges posed by a competitive environment. His contribution to the success of Vhi Healthcare has been immense.

I would like to express too my appreciation to former Board member Ms Suzanne Kelly for her outstanding contribution over two terms in office. Ms Kelly was first appointed in May 1993 for five years and was re-appointed in September 1998 for a further five-year term.

Finally I would like to thank my colleagues on the Board for their valued support and input over the period under review and I would like to especially welcome our newest Board Member, Mr Christopher Cooney who commenced office from February 2004.

ADVISORY GROUPS

Vhi Healthcare benefits greatly from the support provided by two unpaid committees, namely the Members Advisory Council and the Medical Advisory Group. These two groups provide expert advice and communication on matters that directly influence how we provide for, and improve our service to members. Their input to the running of our business is significant and I would like to thank them for their help during the year.

MANAGEMENT AND STAFF

I would like to pay tribute to the professionalism and commitment of all Vhi employees based throughout Ireland. Their role in the delivery of quality service to our customers is pivotal to the success of our business both now and in the future. I have no doubt that our management and staff will continue to provide members with the excellent level of service and support synonymous with the name Vhi Healthcare. I would like to record the appreciation and thanks of the Board of Directors for this.

TRIBUTES

I would especially like to acknowledge the contribution made by our esteemed staff members Mr John O'Dowd and Mr Greg Foley both of whom passed away during the year. Our sincere sympathy goes to their families, friends, and colleagues in Vhi Healthcare. May they rest in peace.

THE FUTURE

Operationally, 2003/04 was a big success due in large part to the skill, vision and tenacity of the Board, Management and Staff of Vhi Healthcare. Even less than a year into my tenure as Chairman of the Board I can see that the company is well positioned to deal with the difficult operating conditions which lie ahead.

However, the long term future of Vhi rests with those charged to bring about the implementation of Risk Equalisation. Without Risk Equalisation it is difficult to be optimistic about the financial future of the organisation or the prospects for Community Rating in Ireland.

As I have mentioned earlier, the next premium increase in September 2004 will be funded largely out of reserves as Vhi considers it unfair that its members be asked to continually subsidise the windfall profits of competitors. In the longer term this reduction can only be maintained if the Health Insurance Authority reverses its decision, is forced to do so by the Courts, or if the Government meets the cost of financing community rating.

It is the view of the Board, Management and Staff of Vhi Healthcare that we operate primarily to serve the interests of our members. Operating on a not for profit basis we are mindful of the fact that the resources of the business have been entirely provided by the members and in the entire history of the organisation we have been totally self financing. It goes without saying that all of our thinking and all of our actions are dictated by, and dedicated to, the needs of our members.

Bernard Collins
Chairman

OPERATIONS REVIEW

INTRODUCTION

From the point of view of business activities, the year ended February 2004 was a very successful one for Vhi Healthcare with the introduction of a range of new and diverse products, improvements in the number and quality of services to members, increased surplus, a further reduction of our operating cost ratio, and a significant strengthening of reserves.

However, major risks attach to our business under two headings:

1. **Community Rating and Risk Equalisation**
   Vhi Healthcare cannot apply a true community rated price to its members and retain financial stability in the absence of Risk Equalisation. The risks resulting from this situation are so great that the Auditors have drawn attention to them in the course of their Report to the Directors on the accounts.

2. **Corporate Status and Commercial Freedom**
   The health insurance market in Ireland has grown to the point where it can now be termed a mature market. It is thus a strategic imperative for Vhi Healthcare to diversify. Under our current corporate status as a Statutory Body it is not possible to develop this strategy to any appreciable extent. The business needs to be incorporated.

Both of these issues have been covered in the Chairman's Review.

HIGHLIGHTS OF YEAR TO 29TH FEBRUARY 2004

- Total Membership now stands at more than 1.55 million people.
- €638 million paid out on behalf of claims for our members or more than €2.4 million paid out every working day.
- Launch of new products *Plan B with Excess*, HealthSteps *Silver*, and *Multi Trip* Travel Insurance for Vhi Healthcare members.
- 485,000 claims and 1.22 million doctor invoices processed.
- 3.1 million Customer contacts.
- Significant benefit enhancements for members of Plans A-E and Options.
- Launch of our Dental Insurance product in May in conjunction with our partners, DeCare International.

MEMBERSHIP, SALES AND SERVICES

MEMBERSHIP RESULTS 2003/2004

During the year 63,395 new members selected Vhi Healthcare as their insurer contributing €36.6 million to premium income. Some members left because of their inability to continue to make premium payments. This is a major concern for us in our objective of providing quality health cover at affordable prices. With the launch of Lifestage products later in the year we intend to offer our members a greater range of products which can be tailored to suit their individual needs.

With more than 1.55 million people insured (A-E, Options plus Plan P), Vhi Healthcare generated a total premium income of more than €840 million by year-end with the majority of members insured through more than 8,300 group schemes, operated either by their employer or an organisation to which they belong.

Sales of non-core products during 2003/04 were particularly encouraging. Our primary care product HealthSteps experienced a 77% increase in turnover compared to the previous year helped by the introduction of HealthSteps *Silver* – a stablemate to the original HealthSteps *Gold* product, providing a cost effective option for members needing basic cover for everyday primary medical expenses. By year end more than 15,000 new members had taken out HealthSteps cover bringing total membership of HealthSteps to 35,610. In the Corporate Solutions area revenue generated by our Occupational Health service and other product/services designed for employers increased more than four fold during 2003/04, while sales of Global, our travel health offering, also substantially exceeded target driven by strong individual sales coupled with the winning of significant corporate business from competitors.

February 2004 saw the launch of Multi Trip from Vhi Healthcare, representing the company's first product launch outside of the strictly medical sphere. In its first two weeks the product attracted almost 5,000 members and at the time of writing we have sold over 30,000 policies. The product is continuing to be very popular and looks set to dominate the travel insurance market in 2004. In response to requests from our members we have reviewed and improved the product offering for people aged over 65.

In May we launched our Dental Insurance product - Vhi DeCare Dental, the first such product in the country. This is a joint venture with DeCare International, the largest dental insurance provider in the US.

We intend to launch Lifestage products later in the year with the specific objective of having quality plans tailored to meet the individual needs of our members.

Vhi Healthcare has built a reputation for excellence in customer service. In September, Vhi Healthcare's Maurice Whelan became the first manager of an Irish company to be awarded European Call Centre People Manager at Call Centre Expo UK 2003. The award was in recognition of excellent customer experience delivery through people management and reflects the high standard of customer care associated with the Vhi Healthcare brand. In practice, more than 90% of telephone calls to our customer service line were answered within ten seconds and in the vast majority of cases the staff member who answered the phone was in a position to provide the information requested.

Contact with our customers is extremely important to Vhi Healthcare and its members. During the year we had more than 3.1 million contacts with our members through telephone, e-mail, mail, text message or by calling to one of our offices in Dublin, Dun Laoghaire, Cork, Limerick, Galway or Kilkenny.

HEALTH SERVICES

Ensuring that our members have access to modern, best practice medical care has always been a primary objective of Vhi Healthcare. At the same time we work hard to ensure that the cost of providing such services is rigorously contained.

During 2003/04 Vhi Healthcare paid out almost €640 million in claims benefit to its members – on average more than €2.4 million per working day. No other health insurer in Ireland comes near to providing this level of benefit to its members.

Vhi Healthcare works with providers to bring costs down through agreed fixed prices for accommodation and professional services. Fixed prices are the recommended international approach as they assist cost management, limit exposure to open ended costs, incentivise hospitals to be efficient, transfer the risk of increasing costs to the hospitals, cut down on claims administration and reduce lengths of stay.

In addition to agreeing full cover payment structures with hospitals and consultants for their services Vhi Healthcare is committed to the principle of ensuring that procedures are carried out in the most appropriate setting as based on best medical practice. The global trend of providing more medical services on a daycare basis is increasing and Ireland is no exception. Last year almost 63% of all claims paid by Vhi Healthcare were provided in a daycare setting. This figure has increased from 38% in 1996. Last year alone this saved our members more than €128 million, or up to 16% of the premium.

Such cost containment measures have helped Vhi Healthcare to improve the efficiency and productivity within the private medicine sector over the past ten years to the point that although the number of claims has risen by 85% we have not had to increase overall private bed capacity. Given that the addition of even one new private facility will add upwards of €40 million to our costs this is a significant achievement.

During 2003/04, a total of 104 medical facilities had agreements with Vhi Healthcare on fees, of which 35 were private hospitals. In addition, over 99% of all hospital consultants agreed to accept Vhi Healthcare payment structures in full settlement for services provided to members. A further 150 convalescent homes, 21 MRI centres,14 laboratory and diagnostic radiology centres, six ambulance companies and a PET Scanning facility all had agreements with us.

New facilities approved by Vhi Healthcare included three new MRI centres in Dublin, Kilkenny and Tralee together with Shandon Street Hospital in Cork which became the first Vhi approved Day Care Centre to provide surgical/diagnostic treatment for Vhi members in the greater Cork area.

During the year we increased the choice and quality of new products and services available to our members. In summary, these enhancements included:

- New product - Plan B with Excess - a further innovation in our most popular product;
- New Product – HealthSteps *Silver* – providing even more choice for members needing cover for everyday medical expenses;
- New product – Multi Trip Travel Insurance for members going abroad;
- Approval of Shandon Street Hospital, Cork for members requiring day care surgery / diagnostic treatment;
- Maternity benefits - Public Hospital charges for normal delivery extended to 3 days fully covered. The maximum monetary amount no longer applies;
- Newborn infants included free of charge until next renewal;
- Significantly enhanced Repatriation and Assist benefits;
- NurseLine 24/7 telephone advice line services enhanced
- Direct payment of members' claims agreed with Rotunda Hospital, Dublin;
- Additional number of approved MRI scanners for members needing scans on an in-patient or out-patient basis;
- MRI benefit increases for in-patient and out-patient scans at selected Centres; and
- Full cover provided for members needing daycare Radiotherapy for cancer.

Vhi Healthcare is committed to providing access to quality private healthcare services for its members and uses member feedback to monitor the quality of the services provided by Vhi and its providers. Regular patient satisfaction research is collected by Vhi to ensure that high levels of satisfaction with services are enjoyed by members. Research gathered during 2003/04 shows extremely high levels of member satisfaction within important areas such as the standard of accommodation, medical and nursing care received, levels of general comfort and efficiency of claims handling. With the growing trend towards utilisation of day care services, it is worth noting that more than seven in ten members requiring day surgery in a private hospital were admitted within four weeks of referral.

The vigilance of our members has a vital role to play in the control we seek to exercise over the cost of health services. The vast bulk of hospital and consultant services performed for members is paid for in full by Vhi Healthcare. Subsequent to every payment, full details of the claim are sent to members. We have made major improvements in the manner in which these claim costs are reported. The precise details of what has been paid are now easier to read and understand. We are committed to taking appropriate action if members bring to our attention any errors in claims discharged by us on their behalf e.g. procedures billed but not carried out; queries on medical consultant charges etc.. This audit by members can make a significant contribution to the control of premium costs.

FINANCIAL RESULTS

Vhi Healthcare operates as a not-for-profit business. This means that it is not the objective of the business to make profit so that a return can be paid to the owners of the business. However, we do need to generate a surplus so that the free reserves within the business grow in line with Premium Income and provide security for members. Our surplus in 2003/04 exceeded our target and the excess surplus will be applied to reduce the rate of premium increase that would otherwise be required at the next review on 1st September 2004.

The key elements of the financial results were:

- Surplus after tax increased by 84% from €33.8m to €62.3m. This increase represents a return of 7.8% of premium income and has served to increase the reserve ratio from 31.4% at 28 February 2003 to 34.6% at 29 February 2004. Profitability during the year was influenced by the following factors:
  - The effects of a premium increase from September 2002;
  - A small increase in core plan membership;
  - Lower than expected Claims costs;
  - Delay in the opening of new hospital facilities;
  - Further reduction in the operating cost ratio; and
  - Strong sales of non-core products.

- Earned premium of almost €803m was generated during the year, representing growth of 16.8% over the previous 12 month period. Membership of core plans increased slightly over the previous year with strong sales also recorded for HealthSteps, Global and Corporate Solutions products.

- Claims costs increased by just 11.5%, which was lower than expected. This was less than budgeted mainly due to lower claims volumes, expected new provider facilities not coming on stream, and the encouragement of more efficient use of medical facilities leading to more day cases and shorter lengths of stay.

- Operating Expenses grew by 14.2% on the previous year and reflected Vhi's investment in additional employees, marketing, and systems development required to support the launch of new products and services. Despite this, the ratio of operating expenses to earned premium has fallen to just 8.3% - significantly less than the industry norm. Our competitor in the Irish market, for instance, reported an operating cost ratio of 16% in 2003! This is the third successive year that we have recorded a reduction in our operating cost ratio.

- At €14m, income from investment returns was down 43% on the previous year's performance. We pursue a conservative investment policy due to the fact that the level of our free reserves remains below our long term target level. Thus investment returns are dependent on interest rates (which are at historically low levels) and movements in interest rates. It was recognised in last year's report that the return generated in 2002/03 was exceptional and was 'unlikely to be repeated'.

- Unexpired Risk Reserve has increased by €15.6m from €35m to €51m. This reserve arises from the decision of the Board to provide for losses anticipated on contracts renewed, or to be renewed, up to September 2005. This decision takes into account the fact that the premium increase in September 2004 will not be sufficient to provide a surplus in 2005/06 in the absence of risk equalisation.

HUMAN RESOURCES AND FACILITIES DEVELOPMENT

- In order to support the increased demand for new and innovative products and services from Vhi Healthcare, the average number of employees (whole-time equivalent) increased by 5% during the year. The additional staff members have been deployed in areas involving systems development, quality assurance, claims processing, and new product delivery.

Training and Development of our work force continues to be a priority with no less than 6% of employees currently completing modules of study on a range of programmes including Human Resource Management, General Management, Project Management, Law, Accountancy, Selling, IT, E-commerce, Quality. We believe that investing time and money into lifelong learning for employees is crucial to our business success in the long term and our employee retention rate demonstrates that this investment is very worthwhile.

To cater for the increased numbers of employees we have embarked on a facilities development programme which during the year has seen the complete modernisation and refurbishment of our office in Dun Laoghaire as well as the provision of a dedicated Training Centre, extra workstation capacity, and postal facilities at Vhi Kilkenny. Further upgrading of facilities is planned for the coming year to improve capacity and functionality at our Abbey Street, Dublin office.

Early 2004, Vhi Healthcare officially opened a purpose built, state-of-the-art Corporate Solutions Centre on the Old Naas Road in Dublin, specially equipped and designed to deliver our suite of Occupational Health services to the corporate sector.

TECHNOLOGY DEVELOPMENT

Vhi Healthcare is committed to investment in technology in order to improve the quality and efficiency of service to members and to continuously reduce our operating cost ratio. Over the past 18 months work has been progressing to replace our core policy administration system which we call the renewal and billing system (RAB). The core of the existing system was developed in the 1970s and has served the business exceedingly well over three decades. Not surprisingly it has now become inflexible and not responsive to product changes or new developments. The new system at a total cost of approximately €25 million is one of the largest systems currently under development in Ireland and is on target to go live in July 2004. There has been enormous commitment from staff during the course of this development. Our partners in the development of the system, CGI, will market the system as a software solution package to the health insurance industry worldwide. One sale has already been finalised for which Vhi Healthcare has received a share of the sale proceeds.

Work has commenced on the specification of a new claims system which will go into development when the new RAB system is fully operational.

PROVIDING PRODUCTS FOR PEOPLE AT EVERY LIFESTAGE

Vhi Healthcare, with an 80% share of the private health insurance market has been providing Irish people with acute hospital plans since 1957. With more than 1.55 million members it is estimated that in excess of 40% of the population is covered by Vhi Healthcare. With the health insurance market open to competition since 1996, there is now evidence to suggest that the market for providing hospital insurance is now close to saturation.

Our market research shows that change in customer demand in Ireland is having an impact on the health insurance dynamic. In this respect Vhi Healthcare has responded to this change by extending its product suite to include a new array of insurance products and services that reflect what people need and want.

Vhi Healthcare has now made it possible for members to mix and match product offerings to suit their lifestage requirements.

During 2003/04 Vhi Healthcare brought to the marketplace a diverse range of exciting new products including:

- *Plan B with Excess* – a product which offers all the benefits of Plan B but at an even more affordable price;
- *HealthSteps Gold and Silver* – our everyday expenses plan now comes in two versions, offering customers more choice in terms of cover and price; and
- *Multi Trip Travel Insurance* – offers full travel insurance covering all trips taken by Vhi Healthcare members for an entire year for a single payment – at prices which are among the most competitive in the market.

Further innovative development of our core plans (including development of the Lifestage approach) together with exciting new products and services will be launched in 2004/05.

BRAND DEVELOPMENT AND PRODUCT AWARENESS

In 2003/04 our brand awareness activities continued to focus on wellness and lifestyle themes to support our proposition 'Its All About Living'.

- **'It's All About Living' Magazine:** Full of articles on healthy living and lifestyles together with special offers for members, this magazine is published quarterly and is circulated to members at renewal date.
- **'Fit for Fun' :** Launched in association with the Irish Rugby Football Union, this unique programme is

designed to assist primary schools in encouraging children to be more active and to embrace healthier lifestyles by benchmarking fitness and monitoring progress achieved after six weeks. The programme commenced in Dublin on a phased basis and will spread to schools in other counties around the country over a three-year period. To date 50 primary schools and over 3,000 children have participated in the programme.

- **'Where in the World':** a high profile campaign delivered to corporate clients to highlight the benefits available on Assist and the newly introduced *Multi Trip Travel Insurance* product.

- **Sponsorships:** These included children's arts activities at Kilkenny Arts Festival and Hullabaloo Children's Festival in Waterford; Vhi Dance Blitz - an exciting dance convention offering Irish people an opportunity to learn dance steps from leading international choreographers.
  Sports sponsorships included the successful Irish 49er sailing team of Tom Fitzpatrick and Fraser Brown who have qualified to represent Ireland at the Olympics in Athens 2004, the Children of Ireland Award for Outstanding Achievement in Sport and international canoeist and staff member, Sarah Lang.

- **Advertising:** a very successful series of new media advertisements was launched featuring Vhi Healthcare products and services, including NurseLine 24/7 and Child Home Nursing.

During the year our health portal www.vhi.ie was redesigned and enhanced to include a host of new features for members including 'Ask a Nurse', free personalised diet and e-fitness plans, appointment reminders sent by text to mobile phones and a week-by-week pregnancy information service. In addition there are monthly competitions, discounts on weekend breaks and a comprehensive online programme to help people quit smoking.

Vhi Healthcare wants to encourage its members to get even more value and benefits from its services by providing the most modern and informed health and medical information available online as well as policy management facilities.

People can also join Vhi on-line and revenue generated through online sales increased by 140% in 2003/04. With almost 70,000 registered members, and receiving on average more than 200,000 site visits per month, www.vhi.ie is considered to be the most popular health information portal in Ireland and was recognised for its excellence in 2003 by winning the Golden Spider and Excellence in e-Government awards.

SOCIAL RESPONSIBILITY

Vhi Healthcare is committed to its Vision Statement 'Working together for the wellbeing of customers' and in keeping with our Corporate Values we recognise the importance of sharing responsibility for the continued good health of the people and environment of Ireland. Over the course of more than four decades we have built a reputation for supporting our members throughout their life stages in a proactive way to encourage healthy living, prevent illness, and in the event of illness, ensure access to best quality and most appropriate care available. Our support for the principle of inter-generational solidarity is best illustrated by the fact that today we cover the grandchildren of members who joined over forty years ago.

We recycle all of our paper, bottles, drink cans, print cartridges, used batteries and discarded mobile phones.

During the year we sent more than 126,360 kgs of paper to be recycled which is enough to save more than 1,404 trees.

The necessary upgrading of computer equipment during 2003/04 provided us with an opportunity to recycle our old equipment and put it back into use for the benefit of the community. More than 30 redundant computers were donated to CANDO (Carlow Area Network Development Organisation) a government sponsored organisation group which arranged for these machines to be reconfigured and redistributed to identified Community Groups, Charitable Organisations and individuals who would be unable to source computer equipment in any other way.

In 2003/04 Vhi Healthcare continued to support communities through its involvement with Junior Achievement/Young Enterprise primary and secondary school programmes designed to help young people develop the skills needed to succeed in school, the future workplace and in life. In practical terms this support involved Vhi employees coaching young people on subjects including Personal Banking, Economics, and Resources. Students also learned to identify their own skills, participate in mock interviews, improve interview techniques and curriculum vitae preparations. Through association with Junior Achievement, we hope to encourage students to appreciate the importance of staying in full time education and the concept of lifelong learning.

The employees of Vhi Healthcare last year raised a total of €13,000 in charitable donations through voluntary salary deduction. These funds were distributed to 45 different registered charities operating nationally and internationally. In addition a corporate charitable donation of €20,000 was given to the Irish Heart Foundation. This donation was used to promote Sli na Slainte in corporate group schemes.

OUTLOOK

The past year has demonstrated yet again that Vhi Healthcare as an organisation has the vision, skills, innovation and commitment to members to continue to lead the way in the Irish private health insurance market and provide Irish consumers with variety, quality and value for money. With the launch of more new products in 2004 catering for Dental care and Lifestages the organisation is setting the pace in a market which is likely to see the introduction of more competition before year end.

The Operations Review last year emphasised that to survive in a competitive market Vhi Healthcare needed two particular issues to be addressed to enable it to compete on a level playing field, firstly the commercial freedom to operate without rigid statutory controls and secondly the immediate establishment of a Risk Equalisation fund. During the early part of 2004 Minister Michael Martin has indicated that work has started on the Bill to enable change to the Corporate Status of Vhi and that this would likely come before Dail Eireann in 2005. This is certainly very welcome news. However, despite the passing of Risk Equalisation regulations in July 2003, Vhi Healthcare is dismayed by the decision of the Health Insurance Authority not to recommend the activation of Risk Equalisation following their first review. Vhi Healthcare takes the view that this inaction by the HIA is distorting a vital service by denying the benefits of Community Rating to the majority of the market and delivering huge windfall profits to a single insurer.

Vhi Healthcare exists to serve its members. In the coming year we will continue to provide the highest level of service to which members are entitled and we will bring new and exciting products and services to the market.

Vincent Sheridan
Chief Executive

EXECUTIVE MANAGEMENT TEAM

Vincent Sheridan BComm FCA
Chief Executive
Vincent Sheridan joined Vhi Healthcare in April 2001, with 28 years experience in the insurance industry. He obtained a B.Comm from UCD and is a chartered accountant by profession. He is a past president of the Irish Insurance Federation, the Insurance Institute of Ireland and the Irish Association of Investment Managers. He is a director of the Irish Stock Exchange and a council member of the Institute of Chartered Accountants in Ireland, the International Federation of Health Plans and the Financial Reporting Council in the UK.

Dr. Bernadette Carr MD, FRCPI, MPH, LFOM
Director - Medical and Claims
Bernadette Carr is an epidemiologist with extensive clinical and research experience. A graduate of UCC, her qualifications include: Fellowship in UCLA 1989, Doctorate in Medicine TCD 1992, Licentiate of Faculty of Occupational Medicine 1991, and Masters Public Health 1994. She was elected to Fellowship of the Royal College of Physicians in Ireland 1996. Bernadette joined Vhi in 1994 and her responsibilities include provider relations, contract negotiations and claims.

John Creedon
Director - Information Technology
John Creedon has a BSc in Computer Applications from Dublin City University and a Diploma in Systems Analysis from Trinity College, Dublin. He held a number of senior positions in Vhi prior to his current appointment in 1996 and is responsible for all Information Technology services.

Declan Moran
Director - Marketing and Business Development
Declan Moran has a BSc in Computer Science and is a Fellow of the Institute of Actuaries since 1994. He joined Vhi in 1997 from the life and pensions Industry and is responsible for the expansion of Vhi's product line, development of new markets and the provision of actuarial expertise within the organisation.

Michael Owens
Director - Human Resources
Michael Owens has a BA in industrial relations and is a Chartered Fellow of CIPD. He joined Vhi in August 1999 and has over 25 years experience in human resources management in light engineering,paper and print, commercial retailing and insurance.

Tony McSweeney
Director - Individual and Corporate Business
Tony McSweeney, a member of the Marketing Institute of Ireland, joined Vhi from the life and pensions industry in 1996. He is responsible for Customer Services, Customer Administration, Sales and our Corporate Solutions business.

Willie Shannon BBS FCA
Director - Finance
Willie Shannon is a graduate of TCD, having obtained the BBS in 1974. He qualified as a chartered accountant in 1977 with Arthur Andersen and joined the Coyle Hamilton Group, insurance and re-insurance brokers in 1987 as group financial controller. He was subsequently appointed Group Finance Director in 1989. He joined Vhi Healthcare as Director of Finance in 2002. He serves on several committees in the Institute of Chartered Accountants. He is also a past Chairman of the Finance Committee of the Insurance Institute of Ireland and Past President of the Financial Executives Association.

Report of the Directors

The Directors have pleasure in submitting their 47th Annual Report in accordance with Section 20 (1) of the Voluntary Health Insurance Act 1957. The Accounts of the Board and the related notes which form part of the Accounts are included in this report, and have been prepared in accordance with accounting standards generally accepted in Ireland and comply with the European Communities (Insurance Undertakings: Accounts) Regulations, 1996.

1. Principal Activities

The Voluntary Health Insurance Board is a statutory corporation established by the Voluntary Health Insurance Act 1957 and has as its objective the provision of a financing system for private health care, carried out on a mutual assistance basis.

2. Results

The results for the year are set out in the Income and Expenditure Account.

3. Business Review and Future Developments

A review of business transacted during the year, together with the Board's views of likely future developments is contained in the Chairman's Statement.

4. Directors' Responsibilities

The directors are required to prepare accounts for each financial period, which give a true and fair view of the state of affairs of the Board and of the surplus or deficit of the Board for that period.

In preparing those accounts, the Directors are required to:

- Select suitable accounting policies and then apply them consistently.
- Make judgements and estimates that are reasonable and prudent.
- Prepare the accounts on the going concern basis unless it is inappropriate to presume that the Board will continue in business.

The Directors are responsible for keeping proper books of account, which disclose with reasonable accuracy at any time the financial position of the organisation and to enable them to ensure that the accounts are prepared in accordance with accounting standards generally accepted in Ireland and comply with the European Communities (Insurance Undertakings: Accounts) Regulations 1996. They are also responsible for safeguarding the assets of the organisation and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

5. Corporate Governance

The Directors support the principles of Corporate Governance outlined in the Combined Code of the Committee on Corporate Governance. While not itself a listed company, the Board has sought to comply with the provisions of the Code that are applicable having regard to the Constitution of Voluntary Health Insurance Board, and hence reports below on compliance throughout the year with the Code published by the Irish Stock Exchange.

The Directors consider that it has in place the procedures to comply with the provisions laid out in section 1 of the Combined Code: Principles of Good Governance and Code of Best Practice, except in respect of the appointment and terms of office of Directors, which are the responsibility of the Minister for Health and Children. For this reason, the Board does not have a Nomination Committee or a Senior Independent Director. Directors of the Board are independent non-Executive Directors.

Board of Directors

The roles of Chairman and Chief Executive are separate and the Board is entirely comprised of non-Executive Directors. All Directors are appointed by the Minister for Health and Children for 5 year terms of office.

The Board has appointed an Audit Committee which is comprised of three non-Executive Directors. The Audit Committee reviews the annual accounts, internal control and compliance matters and the effectiveness of internal and external audit. The members of the Audit Committee also address the issue of risk, the purpose of which is to ensure that appropriate risk management procedures and reporting protocols are in place.

The Board has also appointed a Remuneration Committee comprising of three non-Executive Directors. This committee is responsible for recommending candidates for senior management appointments and remuneration policies.

The Board has also drawn up procedures for Directors to take independent professional advice and adopted a schedule of matters specifically reserved for decision by the Board. All Directors have access to the advice and services of the Secretary. The Board meets on a monthly basis throughout the year.

Internal Control

The Board has given effect to the recommendations of Internal Control: Guidance for Directors on the Combined Code (The Turnbull Guidance) which was published in September 1999.

The Directors are responsible for the Board's system of internal control and for reviewing its effectiveness. They have assigned responsibility for the implementation of this system to Executive Management. Such a system can only provide reasonable and not absolute assurance against material misstatement or loss. The key elements of the system are:

- Formal policies, procedures and organisational structures are in place which support the maintenance of a strong control environment.
- The business strategy, planning and budgetary process includes analysis of the major business risks which affect the organisation. Risk assessment is a continuous process on which the Board places significant emphasis.

- A comprehensive set of management information and performance indicators is produced promptly on a monthly basis using a series of interrelated balanced scorecards. This enables progress against longer term objectives and annual budgets to be monitored, trends to be evaluated and variances to be acted upon. Detailed budgets are prepared annually in the context of longer term strategic plans and are updated regularly.

- Accounting procedures are documented, transaction cycles are defined, accounting timetables are detailed, automated interfaces are controlled, review and reconciliation processes are carried out, duties are segregated and authorisation limits are checked. Experienced and qualified staff have been allocated responsibility for all major business functions.

On behalf of the Board, the audit committee has reviewed the effectiveness of the systems of internal control in existence for the year ended 29 February 2004 and up to the date of this report.

Going Concern

The accounts have been prepared on the going concern basis and, in accordance with the requirements of the Combined Code, the Directors report that they have satisfied themselves that the Board is a going concern, having adequate resources to continue in operational existence for the foreseeable future. In forming this view the Directors have reviewed the Board's budget for 2004/2005 and the medium term plans as set out in the corporate strategy of the Board. In this regard, attention is directed to Note 9 of the Accounts.

6. Directors' Remuneration

Annual remuneration levels for the Chairman and each Director have been set by Government at €15,237 and €10,158 respectively. The Directors do not receive any other remuneration nor do they have any service agreements or contracts with the Board.

7. Safety, Health & Welfare at Work Act, 1989

The Board has a health and safety policy in existence which is fully in accordance with the specific requirements of the above Act. The Board recognises the value of consultation with staff on matters of health, safety and welfare.

The Directors are pleased to report that no serious accidents occurred to any members of staff or visitors to its premises during the year.

8. Prompt Payment of Accounts Act, 1997

Voluntary Health Insurance Board is included as a listed purchaser of goods and services in the schedule to the Prompt Payments of Accounts Act, 1997. The Directors acknowledge their responsibility for ensuring compliance, in all material respects, with the provisions of the Act. The Board's payment practice is one of ensuring that properly completed and agreed invoices for goods and services supplied to the Board will be discharged within the prescribed payment period. Procedures have been implemented which provide reasonable assurance against material non-compliance with the Act.

9. Books of Account

The Directors are responsible for ensuring that proper books of account are maintained by the Board and this has been achieved by the employment of appropriately qualified accounting personnel and by maintaining appropriate accounting systems. The books of account are located at the head office of the Board at VHI House, Lower Abbey Street, Dublin 1.

10. Auditors

The auditors Deloitte, Chartered Accountants, continue in office in accordance with Section 19 (2) of the Voluntary Health Insurance Act 1957.

On behalf of the Board:

Bernard Collins
Chairman

Pat Farrell
Director

8 June 2004

Report of the Auditors

Independent Auditors' report to the Directors of the Board of the Voluntary Health Insurance Board.

We have audited the accounts of Voluntary Health Insurance Board for the year ended 29 February 2004 which comprise of the Income and Expenditure Account, the Balance Sheet, the Cash Flow Statement, the statement of Accounting Policies and the related notes 1 to 18. These accounts have been prepared under the accounting policies set out therein.

This report is made solely to the Directors of the Board of Voluntary Health Insurance Board in accordance with Section 19 of the Voluntary Health Insurance Act 1957. Our audit work has been undertaken so that we might state to the Directors those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Board and the Directors as a body for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Board and Auditors

The directors are responsible for preparing the Annual Report including, as set out in the Statement of Directors' Responsibilities, the preparation of the accounts in accordance with applicable Irish law and accounting standards. Our responsibilities, as independent auditors, are established in Ireland by statute, the auditing standards as promulgated by the Auditing Practices Board in Ireland and by our profession's ethical guidance.

We report to you our opinion as to whether the accounts give a true and fair view.

We review whether the corporate governance statement reflects the Board's compliance with the seven provisions of the Combined Code specified for our review by those rules and we report if it does not. We are not required to form an opinion on the effectiveness of the Board's corporate governance procedures or its internal controls.

We read the other information contained in the Annual Report and consider whether it is consistent with the audited accounts. The other information comprises only the Directors' Report, which includes the Corporate Governance statement, the Chairman's Statement, the Review of Operations and the Comparative Results table. We consider the implications for our report if we become aware of any apparent misstatement or material inconsistencies with the accounts. Our responsibilities do not extend to other information.

Basis of audit opinion

We conducted our audit in accordance with the auditing standards issued by the Auditing Practice Board and generally accepted in Ireland. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgments made by the Board in the preparation of the accounts and of whether the accounting policies are appropriate to the circumstances of the Board, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we evaluated the overall adequacy of the presentation of information in the accounts.

Other Technical Provisions – Unexpired Risk Reserve

In forming our opinion, we have examined the amount of €50.8m included in other technical provisions, and the assumptions on which the provision is based. We have also considered the disclosures made in note 9 to the accounts with regard to the provision and with regard to the likelihood of deficits being incurred in future years, with consequent severe impact on the financial position of the Board. In view of the significance of the uncertainties inherent in both the provision and the likelihood of further significant deficits, we consider that these matters should be drawn to your attention. Our opinion is not qualified in this respect.

Opinion

In our opinion the accounts give a true and fair view of the state of the affairs of the Board as at 29 February 2004 and of the surplus of the Board for the year then ended.

Deloitte & Touche
Chartered Accountants and Registered Auditors
Dublin
8 June 2004

Accounting Policies

Basis of Preparation
The accounts are prepared in accordance with accounting standards generally accepted in Ireland, the European Communities (Insurance Undertakings:Accounts) Regulations, 1996 and the Statement of Recommended Practice on Accounting for Insurance Business (SORP) as adopted by the Association of British Insurers.

The following are the principal accounting policies adopted:

Basis of Accounting
The accounts are prepared under the historical cost convention modified by the revaluation of investments.

Premiums Written
Gross premiums written consist of the premium income receivable from members in respect of policies commencing in the financial year.

Unearned premiums represent the proportion of premiums written in the year that relate to the un-expired term of policies in force at the Balance Sheet date, calculated on a time apportionment basis.

Claims Incurred
Claims incurred comprise claims and related expenses paid in the year and changes in provisions for outstanding claims, including provisions for the estimated cost of claims incurred but not reported and related handling expenses. The provisions for outstanding claims are based on actuarial methods of calculation approved by the Board's consulting actuaries, Watson Wyatt LLP.

Unexpired Risks
Provision is made, based on information available at the balance sheet date, for any estimated underwriting deficits related to unexpired risks after taking into account relevant investment return.

Tangible Assets
Tangible fixed assets are stated at cost less accumulated depreciation. Depreciation is calculated so as to write off the cost of the assets over their estimated useful lives on a straight line basis as follows:

Motor vehicles	4 years
Computer equipment and software	4 years
Furniture, fittings and office equipment	5 years

Expenditure incurred on the development of computer systems which is substantial in amount and is considered to have an economic benefit to the Board lasting more than one year into the future is capitalised and depreciated over the period in which the economic benefits are expected to arise. This period is subject to a maximum of four years. In the event of uncertainty regarding its future economic benefit, the expenditure is charged to Income and Expenditure account.

Accounting Policies

Investments

Investments in listed securities, including investments in government and government guaranteed stocks, are stated at market value. Market value represents the middle market price less accrued interest at the Balance Sheet date. Realised gains/losses on investment transactions are determined on an average cost basis and recorded in the Income and Expenditure account.

Land and buildings are valued annually on an open market value basis. Valuations are made by independent professionally qualified valuers. All properties occupied by the Board are maintained in a continual state of sound repair. As a result, the Directors consider that the economic lives and residual values of these properties are such that any depreciation is insignificant and is therefore not provided.

Investment Income

Interest on fixed interest stocks and bank deposits is taken to include income as earned on a day-to-day basis. Income from equities is included on the basis of dividends received during the financial year.

Investment Return

Operating surplus is reported on the basis of longer term investment return. The longer term investment return is calculated based on rates which are reviewed annually and reflect both historical experience and the Directors' current expectations for investment returns. The short term fluctuation in investment return, representing the difference between the longer term return and the actual return, is incorporated in arriving at surplus before taxation.

The allocation of investment return from the non-technical account to the technical account is based on the longer term return on investments attributable to the insurance business.

Pension Costs

The expected cost of providing pensions to employees is charged to the Income and Expenditure account, at a substantially level percentage of payroll, over the employees expected service lives. Any difference between the amount so charged and the amount contributed to pension funds is included as a provision in the accounts.

The disclosures required under the transitional arrangements of FRS 17: Retirement Benefits, for the year ended 29 February 2004 are shown in note 18.

Deferred Taxation

Deferred taxation is provided on timing differences between the taxable surplus of the Board and its surplus as stated in the accounts. The provisions are made at the tax rates that are expected to apply in the periods in which the timing differences are expected to reverse.

Income and Expenditure Account

Year to end of February

Technical Account: Health Insurance

Continuing Activities	Notes	**2004 €'000s**	2003 €'000s
Earned Premium:	1		
Gross premiums written		840,493	735,433
Change in the provision for unearned premiums		(37,501)	(47,850)
		802,992	687,583
Allocated investment return transferred from the non-technical account		**24,890**	21,737
		827,882	709,320
Claims incurred:			
Claims paid		638,381	559,043
Change in the provision for claims		24,943	36,126
		663,324	595,169
Other technical provisions:			
Unexpired risk reserve	9	**15,641**	19,871
Net operating expenses	2	**66,322**	58,095
Balance on the health insurance technical account		**82,595**	36,185

Non-Technical Account: Health Insurance

Continuing Activities	Notes	**2004 €'000s**	2003 €'000s
Balance on the health insurance technical account		**82,595**	36,185
Longer term investment return	3	24,890	21,737
Allocated investment return transferred to the health insurance technical account		(24,890)	(21,737)
Operating surplus		82,595	36,185
Short term fluctuations in investment return	3	(10,910)	2,947
Surplus on ordinary activities before taxation		**71,685**	39,132
Taxation on surplus on ordinary activities	4	(9,379)	(5,308)
Surplus on ordinary activities after taxation carried to reserves	5	**62,306**	33,824

The accounts were approved by the Board on 8th June 2004, and signed on its behalf by:

Bernard Collins
Chairman

Pat Farrell
Director

Balance Sheet

As at 29th February

	Notes	2004 €'000s	2003 €'000s
Assets			
Investments			
Land and buildings	6	31,850	31,050
Other financial investments	7	604,202	481,637
Debtors			
Debtors from members arising out of insurance operations		332,269	309,018
Other debtors		521	1,503
Other Assets			
Tangible assets	8	18,173	16,041
Cash at bank and in hand		1,596	2,172
Prepayments and accrued income			
Accrued interest		5,651	8,982
Total Assets		**994,262**	850,403
Liabilities			
Reserves			
General reserve		278,038	215,732
Technical provisions			
Provision for unearned premiums		395,414	357,913
Claims outstanding		248,196	223,253
Other technical provisions	9	50,791	35,150
Deferred taxation	10	1,041	1,703
Creditors			
Bank overdraft		4,860	2,970
Creditors and accruals	11	15,922	13,682
Total Liabilities		**994,262**	850,403

The accounts were approved by the Board on 8th June 2004, and signed on its behalf by:

Bernard Collins
Chairman

Pat Farrell
Director

Cash Flow Statement

Year to end of February

	Notes	**2004 €'000s**	2003 €'000s
Net cash inflow from operating activities	12	143,289	103,600
Taxation paid		(10,513)	(5,825)
Capital expenditure		(8,387)	(9,989)
		124,389	87,786
Cash flows were invested as follows:			
Decrease in cash holdings		(2,466)	(22,088)
Net portfolio investment	13&15	126,855	109,874
Net investment of cash flows	14	**124,389**	87,786

Notes to the Accounts

1 Earned premium

The insurance business of the Board is substantially health insurance and earned premium relates mainly to this class of business. Amounts from ancilliary products are minimal. All business written is in the Republic of Ireland.

2 Net operating expenses

	2004	2003
	€'000s	€'000s
Administrative expenses	52,636	47,199
Acquisition costs	13,686	10,896
	66,322	58,095

Employee Information	**2004**	2003
The average number of persons, including part time employees, employed by the Board was:	763	727

Staff costs were:	**2004**	2003
	€'000s	€'000s
Wages and salaries	32,086	30,109
Social security costs	3,521	3,286
Pension costs	3,322	2,825

3 Investment return

(a) Longer term investment return

The rates of investment return underlying the calculation of the longer term investment return are set out below.	**2004**	2003
	%	%
Land and buildings	6.0	8.0
Shares in listed securities	7.5	7.5
Debt securities/fixed interest securities	4.5	5.0
Deposits with credit institutions	3.0	3.5

(b) Comparison of longer term investment return with actual return	**2004**	2003
	€'000s	€'000s
Actual return: Income from land and buildings	169	214
Income from other investments	18,383	17,571
Gains on realisation of investments	234	2,797
Unrealised (losses)/gains on investments	(3,964)	4,720
Investment management expenses	(842)	(618)
	13,980	24,684
Longer term investment return	24,890	21,737
Short term fluctuations	(10,910)	2,947

A transfer of the full amount of the longer term investment return has been made from the non-technical account to the technical account on the basis that the reserves of the Board are lower than the solvency margin level considered desirable within the health insurance industry and therefore all reserves are deemed to be in support of the technical provisions.

Notes to the Accounts

4 Taxation

	2004 €'000s	2003 €'000s
The taxation charge in the income and expenditure account comprises:		
Corporation taxation - charge	10,041	2,533
Deferred taxation - (credit)/charge	(662)	2,775
	9,379	5,308

Factors affecting the current taxation charge for the period

The tax assessed for the period is higher than the standard rate of corporation tax in Ireland of 12.5% (2003: 15.47%) for the year ended 29 February 2004.
The differences are explained below:

	2004 €'000s	2003 €'000s
Surplus on ordinary activities before tax	71,685	39,132
Surplus on ordinary activities multiplied by standard rate of corporation tax of 12.5% (2003, 15.47%)	8,961	6,054
Effects of:		
Expenses not deductible/(deductible) for tax purposes	697	(514)
Depreciation in excess of capital allowances for period	81	90
Adjustments to tax charge in respect of previous periods	302	(3,097)
Current tax charge for period	**10,041**	2,533

5 Surplus for year

	2004 €'000s	2003 €'000s
The surplus for the year is stated after charging:		
Depreciation of tangible fixed assets	5,780	5,950
Board remuneration	110	110
Audit fee	120	102

6 Investments: land and buildings

	2004 €'000s	2003 €'000s
Valuation:		
At 1 March	31,050	30,822
Additions	474	713
Gain/(loss) on revaluation	326	(485)
At end of year	**31,850**	31,050

Land and buildings included above are occupied by the Board for its own activities and are mainly freehold.

Land and buildings were valued at 29th February 2004 at open market value. These valuations were made by Thornton & Partners, Hamilton Osborne King, Cunningham Auctioneers and O'Keeffe Auctioneers.

If the land and buildings had not been revalued they would have been included at the following amounts which represent the lower of cost or net realisable value:

	2004 €'000s	2003 €'000s
At 1 March	15,763	15,049
At 29 February	**16,237**	15,763

Notes to the Accounts

7 Other financial investments

	2004 Market Value €'000s	**2004 Cost €'000s**	2003 Market Value €'000s	2003 Cost €'000s
Shares in listed securities	3,277	3,000	2,622	3,000
Debt securities/fixed interest securities	591,078	591,239	468,329	463,546
Loans secured by mortgages	165	165	188	188
Deposits with credit institutions	9,682	9,682	10,498	10,498
	604,202	**604,086**	481,637	477,232

8 Tangible Assets

	Motor vehicles €'000s	**Fixtures, furnishings and fittings €'000s**	**Computer equip/software & office equipment €'000s**	**Total €'000s**
Cost				
At 1 March 2003	2,070	4,284	33,854	40,208
Additions	825	527	6,858	8,210
Disposals	(557)	(25)	(326)	(908)
At 29 February 2004	**2,338**	**4,786**	**40,386**	**47,510**
Depreciation				
At 1 March 2003	(1,048)	(2,942)	(20,177)	(24,167)
Charge for the year	(572)	(656)	(4,552)	(5,780)
Eliminated in respect of disposals	393	22	195	610
At 29 February 2004	**(1,227)**	**(3,576)**	**(24,534)**	**(29,337)**
Net book value at 29 February 2004	**1,111**	**1,210**	**15,852**	**18,173**
Net book value at 28 February 2003	1,022	1,342	13,677	16,041

Computer equipment includes expenditure on computer systems in the amount of €10.96m (2003: €5.89m) which will be depreciated when the assets come into use.

Notes to the Accounts

9 Other technical provisions

The amount of €50,791,000 provided for at 29 February 2004 is in respect of losses anticipated on contracts that the Board will be obliged to incept or renew arising from the commitment of the Board to a certain level of price increase effective from 1 September 2004 and anticipated increases in the cost of providing healthcare benefits. These losses are expected to be incurred in the period between September 2004 and August 2006. The charge of €15,641,000 represents the change in the provision over the amount of €35,150,000 which was included in the Balance Sheet at 28 February 2003.

The decision with regard to the price increase reflects the current healthcare insurance environment, and specifically the decision in April 2004 of the Health Insurance Authority not to recommend the activation of Risk Equalisation following their review of the first returns from market participants for the six months to 31 December 2003. Projected cost increases arise from certain changes expected in the healthcare environment in Ireland, notably the anticipated opening of a number of significant new facilities.

The Board's consulting actuaries Watson Wyatt LLP have confirmed that the amount of the provision is a reasonable estimate of these expected losses.

Provision has not been made for further losses anticipated to be incurred in future periods as it is not considered practicable to reliably estimate such losses. However, such losses will arise in an environment where the community rated funding system is applied across the market in the absence of Risk Equalisation. Such losses would have a severe impact on the financial position of the Board, and urgent consideration is being given by the Board to the implications of this position.

10 Deferred Taxation

Provision has been made in respect of deferred taxation for the following timing differences:

	2004	2003
	€'000s	€'000s
Unrealised gain on investment valuation	(14)	(651)
Other timing differences	(1,027)	(1,052)
Total provision	**(1,041)**	(1,703)

11 Creditors and accruals

	2004	2003
	€'000s	€'000s
Corporation tax	1,836	2,308
PAYE and PRSI	911	751
Other creditors	2,245	1,058
Accruals	10,930	9,565
	15,922	13,682

12 Reconciliation of operating surplus to net cash flow from operating activities

	2004	2003
	€'000s	€'000s
Surplus on ordinary activities before taxation	**71,685**	39,132
Depreciation charges	5,780	5,950
Unrealised losses/(gains) on investments	3,964	(4,720)
Increase in health insurance technical provisions	78,085	103,847
Increase in debtors from members arising out of insurance operations	(23,251)	(38,863)
Decrease/(increase) in debtors and prepayments	4,313	(4,776)
Increase in creditors and accruals	2,713	3,030
Net cash inflow from operating activities	**143,289**	103,600

Notes to the Accounts

13 Movement in opening and closing portfolio investments

	2004 €'000s	2003 €'000s
Net cash outflow for the period	**(2,466)**	(22,088)
Portfolio investments	126,855	109,874
Movement arising from cash flows	124,389	87,786
Changes in market values	(4,289)	5,205
Total movement in portfolio	120,100	92,991
Portfolio investments and cash in hand at 1 March	480,839	387,848
Portfolio investments and cash in hand at 29 February	**600,939**	480,839

14 Movement in cash and portfolio investments

	At 1 March 2003 €'000s	Cash flow €'000s	Changes to market value €'000s	**At 29 February 2004 €'000s**
Cash at bank and in hand	(798)	(2,466)	-	(3,264)
Shares in listed securities	2,622	-	655	3,277
Debt securities and other fixed interest securities	468,329	127,693	(4,944)	591,078
Loans secured by mortgages	188	(22)	-	166
Deposits with credit institutions	10,498	(816)	-	9,682
	480,839	**124,389**	**(4,289)**	**600,939**

15 Analysis of cash flows for headings netted in the cash flow statement

	2004 €'000s	2003 €'000s
Portfolio investments		
Purchase of shares in listed securities	-	3,000
Purchase of fixed interest securities	1,603,530	1,165,895
Purchase of deposits with credit institutions	822,342	561,794
Sale of shares in listed securities	-	(428)
Sale of fixed interest securities	(1,475,837)	(1,050,906)
Sale of deposits with credit institutions	(823,158)	(569,440)
	126,877	109,915
Repayment of mortgage loans	(22)	(41)
Net cash outflow on portfolio investments	**126,855**	109,874

16 Capital Commitments

	2004 €'000s	2003 €'000s
Capital expenditure contracted for	2,974	6,500
Capital expenditure approved but not contracted for	3,000	850

17 Related Party Disclosures

There have been no transactions with related parties which require disclosure under Financial Reporting Standard 8.

18 Retirement benefits

The Board operates a defined benefit pension scheme. The assets of the scheme are held in a separate trustee administered fund. Contributions to the scheme are charged to the income and expenditure account so as to spread the cost of pensions over employees working lives with the Board.

The pension charge for the year was €3,322,000 (2003: €2,825,000). The pension cost is determined by an independent qualified actuary, using the projected unit credit method of funding. The most recent actuarial valuation was at 28 February 2003. The principal assumptions used in the actuarial valuation were that investment returns will exceed salary increases by 1.75% and pensioner increases by 2.75%.

At the date of the latest actuarial valuation, 28 February 2003 the market value of the scheme's assets was €49,600,000 and the actuarial value of these assets represented 81% of the benefits that had accrued to members after allowing for expected future increases in earnings and pensions. The funding rate was increased with effect from 1 May 2003 to reflect changed investment conditions and actuarial advice confirms that the current levels of contributions payable to the scheme, together with existing assets, are adequate to secure members benefits over the expected remaining service lives of the participating employees.

The actuarial reports are available for inspection by members of the scheme but not for public inspection. An accrual of €79,000 (2003: prepayment €859,000) is included in the Balance Sheet at year end.

FRS 17 disclosure

The disclosures required under the transitional arrangements of FRS 17 'Retirement Benefits' have been calculated by qualified independent actuaries. In addition to pension entitlements, the Board also provides certain benefits to retirees in respect of health insurance cover. The disclosures in relation to the pension scheme are based on the most recent full actuarial valuation at 28 February 2003 updated to 29 February 2004.

The major assumptions used in respect of the pension scheme are:	**2004**	2003
	%	%
Rate of increase in salaries	4.00	4.00
Rate of increase in pensions in payment	3.25	3.25
Discount rate	5.25	5.50
Inflation assumption	2.25	2.50

Long-term expected rates of return at 29 February were:	**2004**	2003
	%	%
Equities	7.50	8.00
Fixed interest securities	4.50	5.00
Property	6.00	6.50
Other	3.00	3.00

18 Retirement benefits (continued)

The assets in the pension scheme at market value were:	**2004**	2003
	€'000s	€'000s
Equities	49,400	32,500
Fixed interest securities	11,600	11,800
Property	4,100	3,600
Other	1,100	1,700
Total market value of assets	66,200	49,600
Present value of scheme liabilities	(86,800)	(62,600)
Deficit in the scheme	(20,600)	(13,000)
Unfunded health insurance premium provision	(5,700)	(4,500)
Net retirement benefits deficit	(26,300)	(17,500)
Related deferred tax asset	3,288	2,188
Net retirement benefit liability	**(23,012)**	(15,312)

	2004	2003
Total assets	**€'000s**	€'000s
Total assets excluding retirement benefits liability	994,262	850,403
Retirement benefits liability	(23,012)	(15,312)
Total assets including retirement benefits liability	**971,250**	835,091
Reserves		
Reserves excluding retirement benefits liability	278,038	215,732
Retirement benefits liability	(23,012)	(15,312)
Reserves including retirement benefits liability	**255,026**	200,420

Notes to the Accounts

18 Retirement benefits (continued)

If FRS 17 had been fully adopted, the following amounts would have been reflected in the financial statements

	2004	2003
Income and Expenditure account	**€'000s**	€'000s
Charged to net operating expenses		
Current service cost	1,500	1,300
Past service cost	-	-
Death in service cost	-	-
Other retirement benefits	1,200	700
Total operating charge	**2,700**	2,000
Credited to other income		
Interest in scheme liabilities	(3,800)	(3,400)
Expected return on scheme assets	3,600	4,800
	(200)	1,400
Net reduction in operating surplus	**(2,900)**	(600)
Statement of total recognised gains and losses		
Actual return less expected return on scheme assets	8,800	(19,900)
Experience gains and losses on scheme liabilities	(7,300)	4,500
Changes in demographic and financial assumptions	(10,800)	(6,600)
Actuarial loss	(9,300)	(22,000)
Deferred tax credit	1,100	2,401
Total actuarial loss	**(8,200)**	(19,599)
History of experience gains and losses		
Difference between expected and actual return on assets	8,800	(19,900)
% of scheme assets	13%	(40%)
Experience gains and losses on scheme liabilities	(7,300)	4,500
% of scheme liabilities	(8%)	7%
Total actuarial loss	(9,300)	(22,000)
% of scheme liabilities	(11%)	(35%)
Movement in net surplus during the year		
Net (deficit)/surplus in scheme at start of year	(15,312)	1,487
Current service cost	(1,500)	(1,300)
Contributions	3,400	3,400
Past service cost	-	-
Interest on scheme liabilities	(3,800)	(3,400)
Expected return on scheme assets	3,600	4,800
Actuarial loss	(9,300)	(22,000)
Deferred tax credit	1,100	2,401
Other retirement benefits	(1,200)	(700)
Net deficit at end of year	**(23,012)**	(15,312)

COMPANY DETAILS

Main Bankers
AIB Bank plc
Bank of Ireland

Auditors
Deloitte & Touche

Solicitors
McCann FitzGerald

Consulting Actuaries
Watson Wyatt LLP

Voluntary Health Insurance Board
An Bord Árachais Sláinte Shaorálaigh

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