WHEN YOU EVALUATE YOUR ORGANIZATION THROUGH THE EYES OF YOUR CUSTOMERS, GREAT THINGS HAPPEN.

Workers Compensation Fund 2004 Annual Report

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At WCF, we realize customer feedback is vital to progress. By listening to our policyholders we have been able to refine how to take workers’ compensation matters off the minds of employers and injured workers.

Workers Compensation Fund, listening to those who matter most.

LANE A. SUMMERHAYS, President & CEO, **ROBERT D. MYRICK,** Chair, Board of Directors

Dear Policyholders and Friends,

We are pleased to report that 2004 was an excellent year for Workers Compensation Fund (WCF). We began the year with proposed legislation and a $50 million offer to the State of Utah to settle litigation over who owns WCF—the State or WCF's policyholders. While legislative efforts failed, Third District Court Judge Timothy R. Hanson ruled in WCF's favor, expressing that, "the State has no ownership in WCF or its assets other than as a policyholder." The State has appealed this ruling to the Utah Supreme Court, and the appeal will be heard in April of 2005. We are confident that the Utah Supreme Court will uphold Judge Hanson's ruling.

With this ruling in hand, WCF resolved licensing challenges facing Advantage Workers Compensation Insurance Company (Advantage). Working with Advantage, we are now able to move forward and offer workers' compensation insurance coverage outside the state of Utah for customers who operate in multiple states. This capability is essential to the long-term success of WCF. It also influences our ability to provide low, competitive premium rates to Utah businesses.

WCF had an excellent year financially, recording net income of $38 million on $246 million of premiums earned. We were pleased to return a dividend of $20 million to our policyholders/owners. WCF has now returned a total $190 million in dividends to policyholders since 1992. During this same period of time, policyholders' surplus has grown from $63 million to $327 million. The average rate charged to employers per $100 of payroll for workers' compensation insurance was $2.30 in 1992 and only $1.77 in 2004. Rates for manufacturing companies were the 3rd lowest in the United States in 2002, the most recent year for which data is available. WCF received 41,100 claims in 1992 and 30,600 claims in 2004—an amazing decrease considering the expansion in the economy and the increase in WCF's market share.

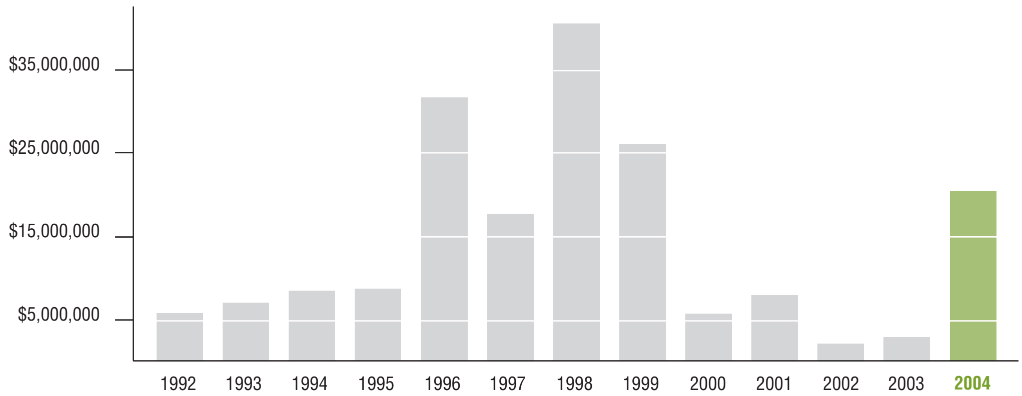
At the end of 2004, WCF bid farewell to long time Board Chair, Melvin C. Green. Mr. Green joined the board in 1992 and has played a major role in WCF's improvements and progress over the last 12 years. We express our gratitude to Mr. Green for his tireless efforts and wish him well.

Looking to the future we are concerned about the increase in claims costs, particularly medical costs. If the cost of workers' compensation insurance is going to remain low in Utah, we must be vigilant in finding ways to control medical expenses. While the frequency of accidents continues to decline, severity is on the rise. Employers must focus on protecting their employees from serious injury by providing adequate training, implementing effective safety procedures, and eliminating drugs and alcohol from the workplace. Success depends upon employers' top management focusing on these issues.

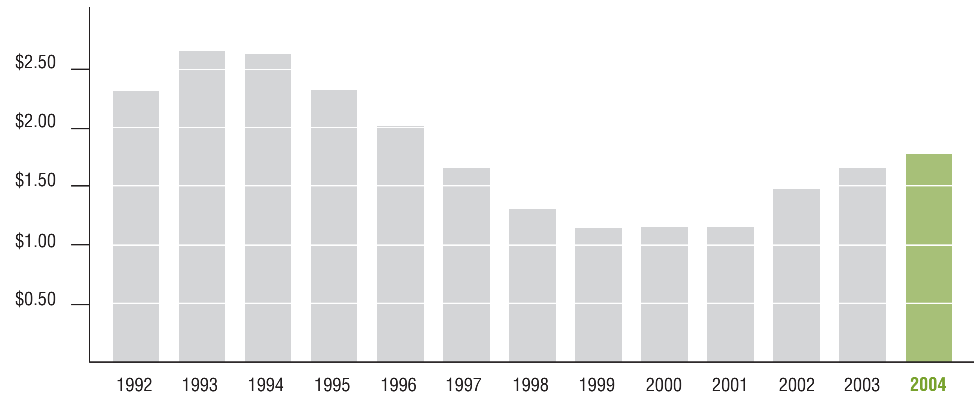
We appreciate the loyalty of our customers, and we will continue to work diligently to deserve your business.

Lane A. Summerhays
President & CEO

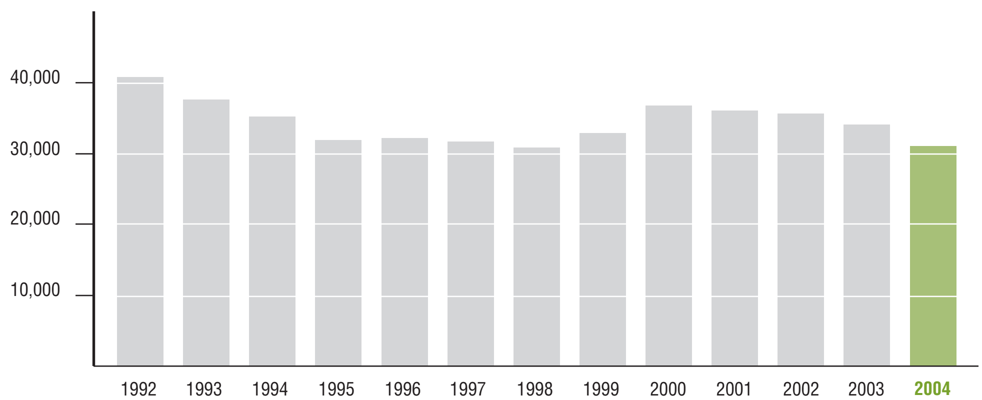
Robert D. Myrick
Chair, Board of Directors



WORKERS COMPENSATION FUND DIVIDENDS FROM 1992–2004



AVERAGE RATE PER $100 OF PAYROLL FROM 1992–2004



NUMBER OF WORKERS COMPENSATION FUND CLAIMS REPORTED FROM 1992–2004

FINANCIAL HIGHLIGHTS

Year ended December 31	2004	2003
(in thousands)		
Revenues	$ 289,870	$ 271,773
Premiums earned, net of reinsurance	245,558	227,382
Net investment income	44,312	44,391
Realized gains on investments	11,272	7,935
Underwriting gain	3,798	2,084
Policyholder dividends	19,889	3,000
Net income	38,475	48,959

Year ended December 31,	2004	2003
Loss and loss adjustment expense ratio	74.9	75.1
Expense ratio (excluding dividends)	23.6	24.0
Combined ratio (excluding dividends)	98.5	99.1

December 31,	2004	2003
(in thousands)		
Admitted assets	$ 1,037,669	$ 953,967
Cash and invested assets	1,001,398	921,464
Reserve for losses and loss adjustment expenses	648,878	600,598
Policyholders’ surplus	326,651	293,447

CHRIS ROYBAL President & CEO, Economic Development Corporation of Utah

FAIR & ACCURATE PRICING

At Workers Compensation Fund, we understand the importance of providing reliable workers' compensation insurance at a fair and accurate price. We work hard to offer the lowest rates possible while still keeping the market stable.

Currently Utah has the third lowest workers’ compensation rates in the nation, which the Economic Development Corporation of Utah has recognized as a key economic incentive for bringing business to Utah.

“Serving our policyholders has always been Workers Compensation Fund’s first priority. Our staff emphasizes efficiency and accountability so we can pass cost-savings on to customers. We are pleased to be part of the reason Utah is a smart place to do business.” Lane A. Summerhays, CEO and president of WCF.

“When courting businesses to relocate or expand in Utah, we provide comparative economic data that demonstrates the cost-effectiveness of doing business in Utah. Invariably, workers’ compensation insurance is one of the deciding factors, and rates provided by the region’s largest provider, Workers Compensation Fund, are part of the state’s appeal.”

– CHRIS ROYBAL, President & CEO, Economic Development Corporation of Utah

898
workplace safety visits

112
free safety classes

"At WCF, we partner with our policyholders to find solutions that will protect their employees. We offer a number of safety resources such as seminars and publications, but since no two companies are alike, we also offer additional customized services to meet a variety of organizations' safety needs."

— **STEVE ERICKSON**, WCF Vice President of Safety

SAFETY RESOURCES

Everyone wants to prevent workplace injuries, and to help avoid accidents we provide an assortment of safety services and educational resources. WCF's Safety and Loss Prevention Department has certified safety professionals who offer a variety of loss prevention services, including safety and health audits, program assistance including general safety, substance abuse prevention, safe driving practices and all OSHA required programs.

Last year, WCF's safety specialists traveled throughout the state of Utah to assist policyholders with their safety concerns and needs. In 2004, the Safety team performed 898 workplace safety visits and taught 112 free safety classes.

"The safety professionals at WCF have helped our company implement procedures that have improved our safety record and helped our bottom line. Safety pays, and in a measurable way."

– **W.W. CLYDE** Safety Director, Bruce Dallin

CRAIG ALLEN WCF Safety Specialist, **BRUCE DALLIN,** W.W. Clyde Safety Director

QUICK, EXPERIENCED CLAIMS SERVICE

There are usually many questions and concerns when an injury occurs. We know that during this worrisome time information and answers need to be communicated clearly and claims processed quickly and accurately to help injured workers get on with life.

In 2004, WCF processed 30,600 claims, with each claimant being contacted in 2 days or less.

To Whom It May Concern:

I wanted to write a quick note to compliment Alaris Johnson, one of your claims adjusters, for the fantastic service that she provided. She was not even assigned to my claim; however, she responded quickly, helped set me up with a new doctor in a new area that I recently moved to, called ahead to let them know that I would be calling and pointed me in the direction that I needed to go. I don't have enough kind words to explain the great job that she is doing.

Sincerely,
Barry L. Henline
[Injured Worker]

ALARIS JOHNSON, Claims Adjuster

RESPONSIVE CUSTOMER SERVICE

When you have a question or a problem, we recognize your need to have it resolved quickly. At WCF, we have developed internal systems to deliver responsive customer service in every department, from every individual.

We have also focused on developing a friendly and accessible phone system and providing useful Internet services to get you the information you need quickly. During 2004, WCF developed an online payment program based on the requests of our customers.

"Everything we develop is created with the policyholder in mind. We strive to provide programs and services to help our customers and employees handle workers' compensation matters easily and efficiently. With policyholders' needs as our first priority, we use strategic planning and constant evaluation to exceed expectations and maintain the correct course." Debi Mofford, Acting Chief Information Officer.

TIM DAFFERN, Systems Analyst

LAURA STIREMAN, Account Manager

BRENT ISAACSON, Underwriter

GEORGE LUPANOW, IT Specialist

SILVIA JENSEN, Customer Service Rep.

PAOLA STAUFFER, Claims Manager

AARON SALAZAR, Help Desk Technician

CATHY WILKEY, Customer Service Rep.

JULIO RODRIGUEZ, Vocational Rehabilitation

ERIC TORGERSEN, Senior Account Executive

REGAN MOTT, Business Analyst

CHARLES PUGH, Safety Specialist

At Workers Compensation Fund, we have developed internal systems to deliver responsive customer service in every department, from every individual.

The Pleasant Grove Police Department

At WCF, our goal is to do everything possible to help prevent on-the-job injuries, but when one does occur, we're right there to help in anyway we can.

Dear Mr. Summerhays:

On Friday July 9, 2004, I learned that I, along with 11 other members of the Pleasant Grove Police Department, had been exposed to a potentially deadly bacterial infection during our investigation into an unattended death in our city. I contacted the Utah County Health Department and then made my next call to your office.

To be honest, I expected to run into red tape. Instead, I received instant cooperation and help. The woman that I spoke with dropped everything, helped us through the forms and made things happen. Within an hour of talking with your office, my officers had started taking their preventive medication.

I just wanted you to know that you have exceptional, caring people working for you. I cannot explain the sense of relief and peace of mind that was made possible for my officers, their families, and for the whole extended family of Utah law enforcement by their actions.

Sincerely,
Captain Cody Cullimore
Pleasant Grove Police Department


NEXTEL

VOCATIONAL REHABILITATION & MEDICAL MANAGEMENT

Being injured is painful, frustrating and challenging. WCF's medical management and vocational rehabilitation teams understand the problems injured workers encounter and are available for support, guidance and vocational direction to get injured workers back to work. Returning to productive work in a timely manner boosts morale for the employee and is cost effective for the employer.

OPPOSITE PAGE: SHELLY STEPHENS, Claims Manager & Volunteer Return to Work Coordinator, **BOBBY COLVIN,** Salvation Army Volunteer Supervisor
THIS PAGE:CAROLYN MONTGOMERY, Injured Worker, **CAROL ANN WEBB,** WCF Medical Case Manager

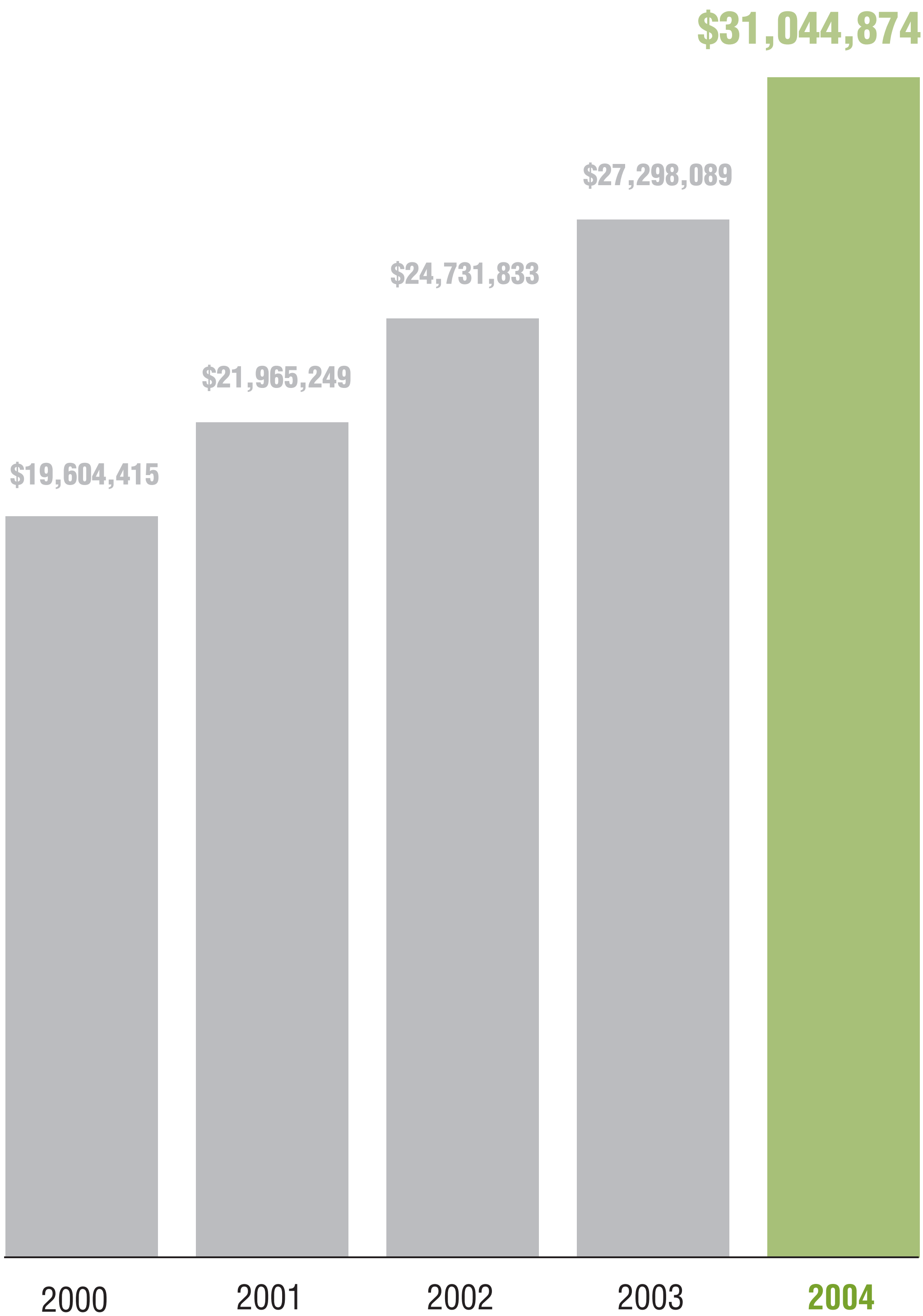
Dear Carol Ann [Webb]:

I just wanted to send you a quick note to thank you for meeting with me to review my case. I have been a bit frustrated trying to move things along with the doctor's office, but all of you at Workers Compensation Fund have done an amazing job at getting everything approved very quickly. It's comforting to know I have someone with your knowledge and expertise working on my behalf, and I am looking forward to working with you over the next couple of months. Thank you again for your time, and it was a pleasure meeting you!

Sincerely,
Carolyn Montgomery, RN, BSN
[Injured Worker]

In order to continue to find ways to control costs and keep premiums low, WCF introduced the Volunteer Return to Work Program to assist both injured workers and their employers with the rehabilitation process.

In 2004, this program along with other WCF managed care programs, such as the Preferred Provider Network, and Vocational Rehabilitation, saved $31,044,874.



WCF MANAGED CARE SAVINGS FROM 2000 – 2004

AN OPEN DOOR AND A LISTENING EAR

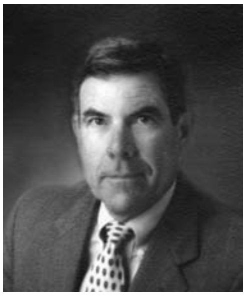
At WCF, we seek out feedback by asking 35 to 40 policyholders to be members of our Customer Advisory Council. Twice a year the council meets with senior management and others to help us stay connected with our customers' needs. At each session, policyholders spend time helping us identify important issues and set priorities. The dialogue between the council and WCF is just the beginning. Once we establish priorities, our team puts together an action plan and mobilizes employees to turn our mutual goals into achievements.

"Creating and convening the Customer Advisory Council, and then acting upon its suggestions on how to improve our service, is an important element of our Company-wide effort to address quality service." Lane A. Summerhays

"I've been part of the council for three years and have appreciated the opportunity to voice my concerns to an attentive ear. It's also been gratifying to watch WCF employees work on providing solutions to resolve the matters I've suggested."

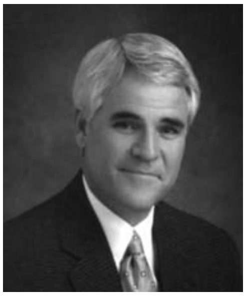
– DARRELL STEVENSON, Nature's Way Products, Customer Advisory Council Member

BOARD OF DIRECTORS



Robert D. Myrick
BOARD CHAIR

Mr. Myrick chairs WCF's Board of Directors. He was president and chief operating officer of Morgan Stanley Bank and has more than 30 years experience in the banking and financial industry. He holds a bachelor's degree and a master of business administration from the University of Utah. He serves on the Investment and Compensation committees. His term expires in 2006.



Judd A. Turner
VICE CHAIR

Mr. Turner serves as vice chair of WCF's Board of Directors. He is an insurance broker and vice president at Fred A. Moreton & Company. He holds a bachelor's degree from Brigham Young University and a master of business administration from the University of Utah. Mr. Turner is also a Certified Property Casualty Underwriter. He serves on the Compensation and Marketing committees.
His term expires in 2006.

Dallas H. Bradford

Mr. Bradford is a retired certified public accountant. He spent 33 years with Arthur Andersen. In the Salt Lake office, he was head of the tax division and managing partner. Mr. Bradford is a graduate of Brigham Young University. He serves on the Audit, Investment and Compensation committees. His term expires in 2006.

Alan F. Edwards

Mr. Edwards is Director of the Utah Division of Risk Management and represents the State of Utah as a policyholder. Mr. Edwards sits on the Audit and Marketing committees. He holds a bachelor's degree and a master of business administration from the University of Utah.

Ruth Lybbert

Ms. Lybbert is an attorney at Salt Lake City-based law firm Dewsnup, King & Olsen, where she has an interest in personal injury law. She earned her juris doctorate from the University of Maryland and her bachelor's degree from the University of Utah. She is on the Marketing and Audit Committees. Her term will expire in 2008.

Robert B. Murray

Mr. Murray is the owner of Alpine Confections. Mr. Murray was also an instructor at Brigham Young University College of Business for more than 15 years. He earned his master's degree at Harvard Business School and his bachelor's degree from Utah State University. Mr. Murray is on the Audit and Investment Committees. His term will expire in 2008.

Lane A. Summerhays

Mr. Summerhays is president and chief executive officer of WCF. He is a certified public accountant and holds a bachelor's degree and a master of business administration from the University of Utah. He serves on the Investment, Marketing and Compensation committees. Mr. Summerhays will remain on the Board for the duration of his tenure as WCF's CEO.

CORPORATE OFFICERS

Lane A. Summerhays
PRESIDENT, CHIEF EXECUTIVE OFFICER,
WCF BOARD MEMBER

Mr. Summerhays joined WCF in 1992 as president, chief executive officer and director. Prior to WCF, he was senior vice president and chief financial officer of ALTA Health Strategies. He also worked in public accounting for Deloitte Haskins & Sells and Arthur Andersen. A certified public accountant, Mr. Summerhays holds a bachelor's degree in accounting and a master of business administration from the University of Utah.

Dennis V. Lloyd
SENIOR VICE PRESIDENT,
CHIEF LEGAL COUNSEL

Mr. Lloyd joined WCF in 1981 and is responsible for adjudication, subrogation, insurance regulation, business operation and government relations. Prior to WCF, he worked for the Utah Legislative Auditor General. Mr. Lloyd holds a bachelor's degree in finance, a juris doctorate and master of business administration from the University of Utah.

Ray D. Pickup
SENIOR VICE PRESIDENT,
CHIEF FINANCIAL OFFICER

Mr. Pickup joined WCF in 1993 and is responsible for investments, financial operations, human resources and information technology. Prior to WCF, he was vice president of finance at First Health Strategies and a senior audit manager for Ernst & Young and Touche Ross & Co. Mr. Pickup holds a bachelor's and master's degree from Brigham Young University and is a certified public accountant.

Robert H. Short
SENIOR VICE PRESIDENT,
CHIEF OPERATIONS OFFICER

Mr. Short joined WCF in 1993 and is responsible for claims administration, medical management and special investigations. In addition, he is president of WCF's subsidiary Pinnacle Risk Management Services, a third-party administrator. Prior to WCF, he was senior vice president of administration at First Health Strategies. Mr. Short is a graduate of the University of Utah.

STATUTORY BASIS FINANCIAL STATEMENTS

WORKERS COMPENSATION FUND YEAR ENDED DECEMBER 31, 2004 AND 2003 THE WITH REPORT OF INDEPENDENT AUDITORS

Management's Discussion and Analysis of Financial Condition and Results of Operations

Year ended December 31, 2004

DESCRIPTION OF BUSINESS

Workers Compensation Fund (the Company) is a statutorily created corporation owned by its policyholders. The Company provides disability and medical insurance coverage within the state of Utah's (the State) mandatory workers' compensation system. The Company is governed by a seven-member Board of Directors, which consists of five public directors, the executive director of the State's administrative services department representing the State as a policyholder, and the Company's president. Three of the five public directors represent policyholders other than the State. Two of the five public directors are from the public in general. Four of the five public directors must have experience in the actuarial, accounting, investments, risk management, occupational safety, casualty insurance or legal professions. The plan for selecting the five public directors is outlined in the Company's bylaws and comports with the Company's enabling statute as well as Insurance Code requirements for the selection of directors of mutual insurance companies. The five public directors are appointed by the Governor of the State with the advice and consent of the Senate. The Company's Board of Directors, not the Governor or the State, has ultimate control of the Company, maintaining managerial, financial, and operational responsibility. The Company is subject to regulation and examination by the Utah Insurance Department. The Company functions as an autonomous mutual insurance company supported solely from its own revenues. All assets, debts and obligations of the Company are separate and distinct from the assets, debts and obligations of the State. Upon dissolution of the Company, any monies not needed to liquidate Company obligations would be returned to its policyholders.

Through July 19, 2004, the Company was the sole shareholder of Advantage Workers Compensation Insurance Company (Advantage), a property and casualty insurance company domiciled in the state of Indiana and licensed in 42 jurisdictions. The Company's investment in Advantage through July 19, 2004, was accounted for as affiliated common stock. On March 24, 2004, the Company's Board of Directors approved an additional capital investment of $25 million into Advantage. Effective July 19, 2004, the Company transferred its investment in common stock into a voting trust held by The National Bank of Indianapolis (Trustee). The voting control of Advantage stock rests with the Trustee, who is obligated to vote the shares in the trust based on voting guidance received from Company policyholders who are also policyholders of Advantage. The Company maintains beneficial economic interest in Advantage. The Company's investment in Advantage subsequent to the transfer is classified as an unaffiliated common stock. The aforementioned change fully resolved a dispute with the Idaho Department of Insurance over issues related to the ownership and control of Advantage. Advantage writes workers' compensation coverage in 26 states.

Effective July 1, 2004, the Company restructured its reinsurance agreement with Advantage. Prior to July 1, 2004, the Company assumed 80% of earned premium and losses equal to that amount from Advantage. Beginning July 1, 2004, the Company assumed 100% of premium and losses on policies providing coverage for Utah-based policyholders from Advantage and assumed no premium or losses on coverage unrelated to Utah-based risks.

Pinnacle Risk Management Services, Inc. (Pinnacle), a wholly owned subsidiary, provides third-party administration of claims to self-insured clients. The Company's investment in Pinnacle is carried at a zero book value for statutory purposes as it currently has negative retained earnings.

Advantage WorkComp Services, Inc. (Advantage Services), a wholly-owned subsidiary, provides bill review, utilization review, medical case management and other services to the Company, to companies that self-insure, and to workers compensation insurers. The investment in Advantage Services is carried at a zero book value for statutory purposes as the entity is not audited on a stand-alone basis.

Univantage Insurance Company (UIC), a wholly-owned subsidiary, licensed in Utah to write life and health and accident insurance, is currently inactive and has no policyholders. Assets of UIC consist entirely of investments and cash. The Company's investment in Univantage is carried at a book value of $1.6 million.

OVERVIEW

Workers Compensation Fund had net income for the year ended December 31, 2004 of $38.5 million. For 2004, the Company recorded an underwriting gain of $3.8 million and a combined ratio of 98.5%.

The $18.2 million or 8.0% growth in net earned premium in 2004 resulted from increases in insured payroll and aggregate premium rates for direct business, partially offset by decreases in premiums assumed. Net earned premium for assumed business decreased by $7.6 million, or 22.0% as the Company discontinued its assumption of non-Utah related out-of-state business.

The Utah Insurance Department approved loss-cost premium rate increases of 11.2% and 7.4% for 2004 and 2003, respectively, as recommened by the National Council on Compensation Insurance.

Net investment income was down slightly to $44.3 million in 2004 compared to $44.4 million in 2003 as the average weighted yield of the Company's bond portfolio continues to decline due to reinvestment at current low interest rates.

Overall, policyholders' surplus increased $33.2 million or 11.3% from December 31, 2003 to December 31, 2004.

FINANCIAL POSITION

Total cash and invested assets at December 31, 2004 were $1.0 billion, an increase of $79.9 million, or 8.7%, since December 31, 2003. The increase resulted primarily from investment of $74.7 million in cash provided by underwriting and operations, net realized capital gains of $11.3 million, and an increase in unrealized capital gains of $2.6 million. These increases were partially offset by the purchase of $7.8 million of non-admitted investments, equipment, and software and $0.9 million in other cash applications.

Net cash generated from operations was principally the result of $45.6 million of cash received from net investment income and $30.3 million of cash provided by underwriting during the year. Cash and short-term investment balances decreased $26.4 million during 2004. The $74.7 million of cash provided from operations and the $26.4 million decrease in cash, was used to invest in bonds ($40.7 million), Advantage ($25.0 million), first lien mortgage loans ($17.6 million), publicly-traded common stocks ($10.3 million), real estate ($4.9 million), other invested assets ($1.7 million) and other applications of cash ($0.9 million).

The components of cash and invested assets consisted of the following:

December 31,	**2004**	2003
Bonds	**70.5%**	72.4%
Stocks	**20.4%**	16.6%
Mortgage Loans	**2.5%**	0.8%
Real Estate	**2.8%**	3.2%
Cash and short-term investments	**3.8%**	7.0%
Total cash and invested assets	**100.0%**	100.0%

The Company's investments in Advantage Services, Pinnacle, non-income producing land ($8.6 million), and private equity ($3.0 million) are currently stated at zero book value for statutory reporting purposes.

The quality of the Company's investment portfolio remains excellent. At December 31, 2004, investments in bonds totaled $705.9 million. All of the Company's long-term bonds are investment grade quality, with 100% rated NAIC Class 1 investments. Short-term investments consisted of two NAIC exempt dollar valued mutual funds, for which the underlying securities are primarily U.S. government obligations, and one NAIC Class 1 dollar valued mutual fund.

The book value of investments in non-affiliated common stocks increased from $131.1 million at December 31, 2003 to $197.9 million at December 31, 2004 due to transfer of the Company's $40.3 million investment in Advantage from affiliated stock investments, realized gains of $13.6 million, net additional investment of $10.3 million in publicly-traded common stocks, and unrealized gains of $2.8 million. During the same period, the book value of investments in affiliated common stocks decreased from $16.9 million to $1.6 million due to the transfer of the Company's investment in Advantage to a voting trust, net of the Company's additional $25 million capital contribution made prior to the transfer.

The two office buildings owned by the Company were fully occupied in 2004. The Company occupies 95% of one of the buildings with the remaining 5% leased to a tenant. The other building was fully leased to a tenant under an eight-year contract effective August 1, 2000.

The Company participates in first lien mortgage loans in cooperation with local community banks and is the sole lender on an $11.6 million 20-year office building loan. Mortgage loan balances increased from $7.3 million to $24.9 million, on various loans including a $10.2 million net increase in construction loans and an additional $7.5 million for the aforementioned 20 year office building loan.

At December 31, 2004, uncollected premiums totaled $17.9 million, an increase of $3.4 million or 23.3% from December 31, 2003, due primarily to increases in written premium.

The Company is periodically assessed by the Utah Property and Casualty Insurance Guaranty Association to cover the deficits of insolvent insurance companies. These mandatory assessments may be recovered through reduction in future premium taxes in the five years following payment. As of December 31, 2004 and 2003, the Company has accrued $2.0 million for guaranty fund assessments. At December 31, 2004 and 2003, deferred assets of $2.8 million and $3.1 million, respectively, were recorded for future premium tax deductions related to these assessments. In 2004 and 2003, $0.4 million was offset each year against premium tax payments and a corresponding reduction was made to the deferred premium tax asset.

During 2004, receivables from subsidiaries increased $0.3 million. The increase was primarily due to a $0.5 million loan to Pinnacle under a line of credit agreement, partially offset by a $0.2 million reduction in amounts due from affiliates under management and service agreements.

The reserve for losses and loss adjustment expenses is based on an actuarial determination and represents a reasonable estimate of the ultimate net cost of all medical benefit losses, compensation losses, and loss adjustment expenses that are unpaid at year end. The reserve includes an estimate for unallocated operating costs to process, and ultimately settle, incurred but unpaid claims. The reserve is not discounted to its present value. Included in the reserve are amounts for estimated losses and loss adjustment expenses relating to claims incurred but not reported at the end of the year. The reserve is estimated using individual case-basis valuations and the Company's claims payments and statistical experience and is subject to the outcome of future events, including changes in the medical condition of the claimants, medical inflation, medical care technology, legislative changes, court interpretations, and other factors. Although variability is inherent in such estimates, management believes that the reserve is adequate. The reserve estimate is reviewed by an independent consulting actuary and adjusted as necessary as experience develops or new information becomes known. The impact of such adjustments is included in current year operations.

The reserve for losses and loss adjustment expenses is recorded net of amounts recoverable under reinsurance contracts. Recoverables were $15.1 million and $17.5 million at December 31, 2004 and 2003, respectively. Should any of the reinsurers fail to perform under the reinsurance agreements, the Company remains ultimately liable for payment of the claims.

At December 31, 2004, the reserve for losses and loss adjustment expenses totaled $648.9 million, an increase of $48.3 million, or 8.0% since December 31, 2003. The increase consisted of a loss and loss adjustment expense provision for the current year of $183.8 million, less benefit payments (net of subrogation) of $135.5 million.

The Company typically receives premiums in advance of the period in which they are earned. Unearned and advance premiums of $38.7 million and $3.1 million are recorded as a liability at December 31, 2004, compared to $39.8 million of unearned premium and $2.6 million of advance premium at December 31, 2003.

Dividends payable to policyholders decreased $1.4 million between December 31, 2003 and December 31, 2004 as payment of all dividends declared by the Board of Directors were completed by December 31, 2004. At December 31, 2004, amounts held for others totaled $1.6 million, an increase of $0.3 million from December 31, 2003, due primarily to an increase in the payroll tax and escheatable funds liabilities.

Unrealized gains and losses on common stocks are recorded as direct credits or charges to policyholders' surplus. The change in net unrealized gains on common stocks included as a component of policyholders' surplus at December 31, 2004 was $2.6 million. This included gains of $2.8 million on unaffiliated common stocks, partially offset by an unrealized loss of $0.2 million on the common stock of affiliates.

The Company is required to file a risk-based capital report with the NAIC and with state regulatory authorities. The risk-based capital report is a standardized analysis for measuring the solvency of an insurer. The NAIC risk-based capital formula is used to calculate the Company's authorized control level, the capital level below which regulatory authorities may take control of the Company. The Company's total adjusted capital at December 31, 2004, was $326.6 million, or 5.0 times the authorized control level of $64.7 million. This measurement is indicative of the exceptional financial strength of the Company.

RESULTS OF OPERATIONS

Net premium earned for the year ended December 31, 2004, was $245.6 million, which represents an increase of $18.2 million, or 8.0%, from 2003. $25.5 million of the increase was due to increased direct premium and $0.3 million was due to a decrease in ceded reinsurance. These increases were partially offset by a $7.7 million decrease in premium assumed. Increases in direct premiums were primarily due to gains in market share and price increases based on policyholders' loss experience, but also included changes in economic factors such as wage levels and changes in the mix of the labor force among classifications of risk.

The Company currently contracts with both Advantage and Alea North America Insurance Company to provide workers' compensation insurance for out-of-state operations of Utah businesses. The Company assumes the majority of risk associated with these arrangements. Earned premium assumed decreased to $27.0 million in 2004 compared to $34.7 million in 2003 due to Advantage increasing its overall retention of risk.

The amount of premiums ceded decreased primarily as the result of a decrease in reinsurance rates from 2003 to 2004.

Net investment income earned for 2004 was $44.3 million, which represents a decrease of $0.1 million or 0.2% from the prior year due primarily to the decrease in bond portfolio yields resulting from continuing low interest rates.

The Company realized net capital gains on the sale of common stocks totaling $13.6 million during the year, partially offset by realized losses of $2.0 million from the sale of bonds. Net realized gains on the sale of investments during 2004 were $3.3 million more than during 2003 due primarily to market gains on equity investments. There was a $0.3 million impairment loss on a private equity investment in 2004 compared to $1.5 million in 2003.

Losses and loss adjustment expenses incurred for the year ended December 31, 2004, were $183.8 million, an increase of $13.1 million or 7.7% over the previous year; an increase approximately equal to the 8.0% growth in net earned premium. The Company continues its efforts to reduce workers' compensation costs for its policyholders through its loss control and claims management programs. For direct business, the number of accidents reported by Utah policyholders during 2004 increased by 2.1%; however, increases in the severity of accidents and increased utilization of medical services, combined with medical inflation and increases in claimant litigation, resulted in a 6.2% increase in net loss and loss adjustment expense payments for Utah policyholders during 2004 in comparison to 2003. Paid losses and loss adjustment expenses for all business during 2004 (cash basis) totaled $135.6 million, up from 2003 payments of $119.1 million.

Underwriting expenses incurred were approximately $3.3 million or 6.1% higher for 2004 than for 2003, including a $3.5 million increase in taxes, licenses and fees, which resulted from an increase in direct written premium. Business development expenses increased $0.8 million due primarily to $0.5 million additional expense for market development programs. Professional service expenses were up $0.7 million due primarily to costs associated with transferring ownership interests in Advantage to a voting trust. Labor costs including salaries, payroll taxes, and employee relations and welfare increased $0.5 million compared to 2003 due primarily to higher employee benefit costs and performance-related salary increases during 2004. These increases were partially offset by commission and brokerage expenses which decreased $2.0 million since 2003, commensurate with the decrease in business assumed from Advantage.

CASH FLOW AND LIQUIDITY

The Company's sources of cash include policyholder premiums, investment income, and proceeds from the sales, maturities, calls, and pay-downs of investments. The Company anticipates that future revenue collections will be adequate to fund current period expenditures for benefits, operating expenses, and dividends.

The timing of bond maturities for a portion of the investment portfolio is generally coordinated with the estimated timing of benefit expenditures. The Company retains sufficient cash reserves and readily marketable securities to provide for unexpected variances in the timing of benefits paid.

Report of Independent Auditors

Board of Directors
Workers Compensation Fund

We have audited the accompanying statutory-basis statements of admitted assets, liabilities and policyholders' surplus of Workers Compensation Fund as of December 31, 2004 and 2003, and the related statutory-basis statements of operations and changes in policyholders' surplus and cash flows for the years then ended. These financial statements are the responsibility of Workers Compensation Fund'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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. Our audit included 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, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 1 to the financial statements, the Workers Compensation Fund presents its financial statements in conformity with accounting practices prescribed or permitted by the Utah Insurance Department, which practices differ from accounting principles generally accepted in the United States. The variances between such practices and accounting principles generally accepted in the United States and the effects on the accompanying financial statements are described in Note 1.

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

However, in our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Workers Compensation Fund at December 31, 2004 and 2003, and the results of its operations and its cash flows for the years then ended in conformity with accounting practices prescribed or permitted by the Utah Insurance Department.

Ernst + Young LLP

February 18, 2005
Salt Lake City, Utah

Statements of Admitted Assets, Liabilities and Policyholders' Surplus – Statutory Basis

December 31,	**2004**	2003
(In thousands)		
ADMITTED ASSETS		
Cash and invested assets *(Note 2)*:		
Bonds	**$ 705,881**	$ 667,396
Common stocks	**199,499**	147,985
Preferred stocks	**5,000**	5,000
Mortgage loans on real estate	**24,926**	7,278
Real estate	**28,124**	29,415
Short-term investments	**23,522**	34,753
Cash and cash equivalents	**14,446**	29,637
	1,001,398	921,464
Uncollected premiums, net	**17,858**	14,482
Receivable from subsidiaries	**3,967**	3,691
Deferred premium tax asset *(Note 8)*	**2,745**	3,137
Data processing equipment, net	**619**	405
Accrued investment income	**11,028**	10,788
Other admitted assets	**54**	–
	$ 1,037,669	$ 953,967
LIABILITIES AND POLICYHOLDERS' SURPLUS		
Liabilities:		
Reserve for losses *(Note 3)*	**$ 586,140**	$ 536,663
Reserve for loss adjustment expenses *(Note 3)*	**62,738**	63,935
	648,878	600,598
Amounts held for others	**1,627**	1,292
Unearned premiums	**41,871**	42,462
Dividends payable	–	1,441
Guaranty fund assessment payable *(Note 8)*	**1,961**	1,961
Premium taxes payable	**6,421**	5,044
Accounts payable and accrued expenses	**9,970**	7,484
Other liabilities	**290**	238
	711,018	660,520
Policyholders' surplus	**326,651**	293,447
	$ 1,037,669	$ 953,967

See accompanying notes.

Statements of Operations and Changes in Policyholders' Surplus – Statutory Basis

Year Ended December 31,	2004	2003
(In thousands)		
Premiums earned *(Note 4)*	**$ 245,558**	$ 227,382
Losses incurred *(Note 3)*	**163,935**	150,135
Loss adjustment expenses incurred *(Note 3)*	**19,870**	20,562
	183,805	170,697
Other underwriting expenses	**57,955**	54,601
	241,760	225,298
Underwriting gain	**3,798**	2,084
Net investment income *(Note 2)*	**44,312**	44,391
Realized capital gains on investments *(Note 2)*)	**11,592**	9,450
Loss on impairment of investments *(Note 2)*	**(320)**	(1,515)
Other expenses	**(1,018)**	(2,451)
Net income before policyholder dividends	**58,364**	51,959
Policyholder dividends	**19,889**	3,000
Net income	**38,475**	48,959
Change in net unrealized capital gains or losses *(Note 2)*)	**2,617**	24,363
Change in non-admitted assets	**(7,888)**	309
Policyholders' surplus at beginning of year	**293,447**	219,816
Policyholders' surplus at end of year	**$ 326,651**	$ 293,447

See accompanying notes.

Statements of Cash Flows – Statutory Basis

Year Ended December 31,	2004	2003
(In thousands)		
OPERATIONS		
Premiums collected, net of reinsurance	$ 241,062	$ 224,538
Losses and loss adjustment expenses paid, net of salvage and subrogation	(135,525)	(119,057)
Underwriting expenses paid	(53,942)	(51,565)
Net investment income received	45,553	46,433
Dividends paid to policyholders	(21,330)	(2,563)
Other cash applied	(1,072)	(2,451)
Net cash provided by operations	74,746	95,335
INVESTING ACTIVITIES		
Proceeds from sale, repayment or maturity of investments	342,369	346,353
Purchase of investments	(442,655)	(402,389)
Net cash used in investing activities	(100,286)	(56,036)
FINANCING AND OTHER SOURCES		
Other cash applied	(882)	(1,543)
Increase (decrease) in cash, cash equivalents and short-term investments	(26,422)	37,756
Cash, cash equivalents and short-term investments		
Beginning of year	64,390	26,634
End of year	$ 37,968	$ 64,390

See accompanying notes.

Notes to Statutory Basis Financial Statements December 31, 2004

1. SIGNIFICANT ACCOUNTING POLICIES

Description of Business

Workers Compensation Fund (the Company) is a statutorily created corporation owned by its policyholders. The Company provides disability and medical insurance coverages within the state of Utah's mandatory workers' compensation system. The Company is governed by a seven-member Board of Directors, which consists of five members appointed by the Governor of the state of Utah (the State), the Company's president and chief executive officer and the executive director of the State's administrative services department (or his/her designee).

The Company functions as an autonomous mutual insurance company supported solely from its own revenues. All assets, debts and obligations of the Company are separate and distinct from the assets, debts and obligations of the State. Upon dissolution of the Company, any monies not needed to liquidate Company obligations would be returned to its policyholders.

At December 31, 2004, the Company was the sole shareholder in the following for-profit subsidiaries:

- Pinnacle Risk Management Services, Inc. (Pinnacle), a third-party claims administrator serving self-insured entities and other insurance companies.
- Advantage WorkComp Services, Inc., a company providing risk management services to the Company, self-insured entities and other insurance companies.
- Univantage Insurance Company, an inactive life and health subsidiary domiciled in the state of Utah.

Through July 19, 2004, the Company was the sole shareholder of Advantage Workers Compensation Insurance Company (Advantage), a property and casualty insurance company domiciled in the state of Indiana and licensed in 42 jurisdictions. The Company's investment in Advantage through July 19, 2004, was accounted for as affiliated common stock. On March 24, 2004, the Company's Board of Directors approved an additional capital investment of $25 million into Advantage. Effective July 19, 2004, the Company transferred its investment in common stock into a voting trust held by The National Bank of Indianapolis (Trustee). The voting control of Advantage stock rests with the Trustee, who is obligated to vote the shares in the trust based on voting guidance received from Company policyholders who are also policyholders of Advantage. The Company maintains beneficial economic interest in Advantage. The Company's investment in Advantage subsequent to the transfer is classified as an unaffiliated common stock. The aforementioned change fully resolved a dispute with the Idaho Department of Insurance over issues related to the ownership and control of Advantage.

On December 22, 2004, the Company acquired a residual minority interest in Pinnacle and became the sole shareholder.

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Presentation

The accompanying financial statements are presented in accordance with accounting practices prescribed or permitted by the Utah Insurance Department. Such practices vary from accounting principles generally accepted in the United States (GAAP); the more significant variances are as follows:

- Policyholder Dividends: For statutory purposes, dividends are recorded when declared by the Company's Board of Directors. GAAP requires that dividends be accrued at the balance sheet date, based upon an estimate of the amount to be paid.

- Investments: Investments in bonds and redeemable preferred stocks are reported at amortized cost or market value based on their National Association of Insurance Commissioners (NAIC) rating. Under GAAP, such fixed maturity investments are reported at fair value with unrealized gains and losses reported in operations.

- Real Estate: Real estate owned and occupied by the Company is included in investments. Under GAAP, real estate owned and occupied by the Company is reported as an operating asset.

- Nonadmitted Assets: Certain assets designated as "nonadmitted," principally the Company's investments in Pinnacle, Advantage Services, private equity funds, non-income producing land, as well as furniture and equipment and overdue premium receivables, are excluded from the statement of admitted assets and are charged directly to policyholders' surplus. These assets are included in the balance sheet under GAAP.

- Reserve for Losses and Loss Adjustment Expenses: The reserve for losses and loss adjustment expenses is stated net of reinsurance recoverables. Under GAAP, the reserve is shown gross of reinsurance recoverables, which are classified as assets.

- Investments in Subsidiaries: The accounts and operations of the Company's subsidiaries are not consolidated, but are included in investments. Under GAAP, accounts and operations of the subsidiaries would be consolidated.

- Investments in Advantage: The accounts and operations of Advantage are not consolidated, but are included in investments. Under GAAP, accounts and operations of Advantage would be consolidated.

- Policy Acquisition Costs: The costs of acquiring and renewing business are expensed when incurred. Under GAAP, such costs, to the extent recoverable, would be deferred and amortized over the effective coverage period of the related insurance policies.

- Guaranty Fund Assessments: A liability for guaranty fund assessments is accrued after an insolvency has occurred regardless of whether the assessment is based on premiums written before or after the insolvency. Under GAAP, the liability is accrued when premiums upon which the assessment is based are written.

- Statements of Cash Flows: Cash, cash equivalents, and short-term investments represent cash balances and investments with initial maturities of one year or less. Under GAAP, the corre sponding caption of cash and cash equivalents include cash balances and investments with initial maturities of three months or less.

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- Goodwill: In connection with the Company's initial acquisition of Advantage in 1998 for $12,334,000, the Company recorded goodwill of $5,656,000 representing the excess of the purchase price over net assets acquired. The goodwill is being amortized straight-line over 10 years. The unamortized goodwill of $2,027,000 is included in the fair value of the Company's investment in Advantage. Under GAAP, goodwill would not be amortized but would be reviewed for impairment.

A reconciliation of net income and policyholders' surplus as determined in accordance with statutory accounting practices to amounts determined in accordance with GAAP is as follows:

	NET INCOME YEAR ENDER DECEMBER 31,		POLICYHOLDERS' SURPLUS DECEMBER 31,	
	2004	2003	**2004**	2003
(In thousands)				
Statutory-basis	**$ 38,475**	$ 48,959	**$ 326,651**	$ 293,447
Add (deduct) adjustments for:				
Investments:				
Bonds	**(13,869)**	(23,875)	**28,445**	42,314
Common stocks	**3,627**	24,229	**–**	–
Preferred stock	**26**	218	**480**	454
Subsidiaries	**(263)**	(2,577)	**(1,100)**	224
Advantage	**(840)**	–	**1,100**	–
Nonadmitted assets	**–**	–	**16,547**	8,658
Deferred acquisition costs	**(386)**	1,088	**5,809**	6,195
Dividend	**19,889**	(17,250)	**–**	(20,000)
Other	**–**	(585)	**–**	–
GAAP-basis	**$ 46,659**	$ 30,207	**$ 377,932**	$ 331,292

Investments

Investments in bonds are stated at cost, adjusted for amortization of premium or accretion of discount using the effective interest method. Changes in amortization due to prepayments are accounted for retrospectively for fixed rate securities and prospectively for variable rate securities.

Investments in redeemable preferred stocks, which have characteristics of debt securities and are rated as high quality by the NAIC, are stated at lower of cost or market. Common stocks are stated at values specified by the NAIC, which approximate fair values. The investment in Advantage, pending valuation by the NAIC, represents a reasonable fair value determined by the Company. Unrealized gains or losses on common stocks are included as direct credits or debits to policyholders' surplus. If it is determined that a decline in fair value is other than temporary, the cost basis of the security is written down to the fair value and a realized capital loss is recognized. Realized capital gains and losses are determined on a specific identification basis for bonds and weighted average basis for common stocks. There are no restrictions on common or preferred stocks.

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investments in insurance subsidiaries are reported at their underlying statutory equity. Investments in non-insurance subsidiaries are reported at equity values determined under GAAP or admitted asset equivalents. The net change in subsidiary equity is included in changes in net unrealized capital gains or losses in the accompanying statements of operations and changes in policyholders' surplus.

Mortgage loans on real estate are reported at unpaid principal balance, less allowance for impairment, if any.

Land is reported at cost and building and improvements are reported at depreciated cost, with depreciation calculated on a straight-line basis over the estimated useful life of the property (30 years). Leasehold improvements are depreciated over the term of the lease.

Short-term investments include investments with maturities of one year or less at the date of acquisition, excluding cash equivalents. The carrying value of short-term investments are at cost or amortized cost and approximate fair value.

Cash and Cash Equivalents
Cash consists of demand deposits with financial institutions, repurchase agreements and certificates of deposit with original maturities of one year or less. Cash equivalents consist of highly liquid investments with original maturities of three months or less with an insignificant risk of change in value due to changes in interest rates. The carrying amounts for cash approximate their fair values. The carrying values of cash equivalents are at cost.

Premiums
Premium rates are approved by the Utah Insurance Commissioner and are based on rates recommended by the National Council on Compensation Insurance (NCCI), adjusted for loss experience and various other factors. Premiums are earned ratably over the terms of the policies. Premiums are estimated and accrued based on the dollar amount of payroll underlying the policy contract. Uncollected premiums are stated net of an allowance for uncollectible amounts of $5,091,000 and $5,310,000 at December 31, 2004 and 2003, respectively.

Premiums on retrospectively rated policies have been determined based on loss experience on individual policyholder accounts. Net written premiums subject to retrospective rating features for the year ended December 31, 2004 were $8,715,000, or 3.6%, of total net written premium of $244,470,000. Net written premiums subject to retrospective rating features for the year ended December 31, 2003 were $9,040,000, or 3.9%, of total net written premium of $229,906,000.

Furniture and Equipment
The Company's data processing equipment and operating software is reported at cost, less accumulated depreciation of $1,937,000 and $2,033,000 at December 31, 2004 and 2003, respectively. Depreciation expense for data processing equipment, operating software and nonadmitted furniture and equipment is computed on a straight-line basis over estimated useful lives of 3 years for data processing equipment and operating software and 5 to 10 years for furniture and other equipment. Total depreciation expense for data processing equipment,

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

operating software, nonadmitted furniture and equipment and property was $1,149,000 and $1,023,000 for the years ended December 31, 2004 and 2003, respectively.

Reserve for Losses and Loss Adjustment Expenses
The reserve for losses and loss adjustment expenses is based on an actuarial determination and represents a reasonable estimate of the ultimate net cost of all medical benefit losses, compensation losses, and loss adjustment expenses that are unpaid at year end. The reserve includes an estimate for unallocated operating costs to process, and ultimately settle, incurred but unpaid claims. The reserve is not discounted to its present value. Included in the reserve are amounts for estimated losses and loss adjustment expenses relating to claims incurred but not reported at the end of the year. The reserve is estimated using individual case-basis valuations and the Company's claims payments and statistical experience and is subject to the outcome of future events including changes in the medical condition of the claimants, medical inflation, medical care technology, legislative changes, court interpretations and other factors. Although variability is inherent in such estimates, management believes that the reserve is adequate. The reserve estimate is reviewed by an independent consulting actuary and adjusted as necessary as experience develops or new information becomes known. The impact of such adjustments is included in current year operations.

Unearned Premiums
Premium is recognized ratably over the coverage period. The portion of premiums paid that will be earned in the future is deferred and reported as unearned premiums.

Policyholder Dividends
Certain policies are eligible for dividends based on loss experience and other factors. Policyholder dividends are subject to restrictions relating to surplus and approval by the Utah Insurance Department. Policyholder dividends are accrued and expensed when declared by the Company's Board of Directors.

Use of Estimates
The preparation of financial statements in conformity with accounting practices prescribed or permitted by the Utah Insurance Department requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Permitted Statutory Accounting Practices
The Company prepares its financial statements in conformity with accounting practices prescribed or permitted by the Utah Insurance Department. Effective January 1, 2001, the state of Utah adopted the NAIC's Accounting Practices and Procedures Manual (NAIC SAP) as a component of prescribed or permitted practice. The Utah Insurance Department adopted certain prescribed accounting practices that differ from those found in NAIC SAP. Specifically, the Utah Insurance Department prohibits the recording of a liability to the state of Utah for second injury fund claims for years 1994 and prior. The second injury fund is administered by the State and the liability of the second injury fund is recorded as a liability on the state of Utah's Comprehensive Annual Financial Report. The liability is funded on a pay-as-you-go basis by a tax on workers' compensation premiums. Under NAIC SAP, a liability to the state of Utah (contingent upon

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

receipt of future premiums) would be recorded for second injury fund claims for years 1994 and prior.

Had the Company followed NAIC SAP for the recording of the liability of second injury fund claims for years 1994 and prior, the policyholders' surplus of the Company would have been $74,123,000 and $85,486,000 lower at December 31, 2004 and 2003, respectively, and net income would have been $11,363,000 and $18,397,000 greater, respectively, for the years then ended.

2. INVESTMENTS

The amortized cost, gross unrealized gains, gross unrealized losses and fair value of long-term investments in bonds are as follows:

December 31, 2004	AMORIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	FAIR VALUE
(In thousands)				
U.S. Treasury securities and obligations of U.S. Government authorities and agencies	$ 453,015	$ 23,696	$ (606)	$ 476,105
Obligations of states and political subdivisions	156,971	4,251	(944)	160,278
Corporate debt securities	59,184	1,223	(19)	60,388
Mortgage-backed securities	36,711	157	(216)	36,652
	$ 705,881	$ 29,327	$ (1,785)	$ 733,423

2. INVESTMENTS (CONTINUED)

The amortized cost and fair value or statement value of bonds at December 31, 2004, by contractual maturity, are as follows. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations, with or without penalties.

(In thousands)	Amortized Cost	Fair Value
Due in one year or less	$ 71,624	$ 72,691
Due after one year but before five years	231,839	245,927
Due after five years but before ten years	335,532	342,061
Due after ten years	30,175	36,092
	669,170	696,771
Mortgage-backed securities	36,711	36,652
	$ 705,881	$ 733,423

At December 31, 2004 and 2003, bonds with admitted asset values of $56,538,000 and $56,412,000, respectively, were on deposit to satisfy regulatory and contractual requirements.

Realized gains and losses on sales of bonds are computed using amortized cost. Proceeds, gross realized gains and gross realized losses from sales, maturities, calls and paydowns of bonds in 2004 were $211,852,000, $141,000 and $2,163,000, respectively. Proceeds, gross realized gains and gross realized losses from sales, maturities, calls and paydowns of bonds in 2003 were $250,026,000 and $5,304,000 and $1,527,000, respectively.

The cost, gross unrealized gains, gross unrealized losses and fair value of preferred stocks are as follows:

December 31, 2004	COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	FAIR VALUE
(In thousands)				
Preferred stocks	$ 5,000	$ 480	–	$ 5,480

December 31, 2003	COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	FAIR VALUE
(In thousands)				
Preferred stocks	$ 5,000	$ 454	–	$ 5,454

2. INVESTMENTS (CONTINUED)

The cost, gross unrealized gains, gross unrealized losses and fair value of unaffiliated common stocks and affiliated common stocks are as follows:

December 31, 2004	**COST**	**GROSS UNREALIZED GAINS**	**GROSS UNREALIZED LOSSES**	**FAIR VALUE**
(In thousands)				
Unaffiliated common stocks	**$ 176,567**	**$ 25,660**	**$ (4,316)**	**$ 197,911**
Affiliated common stocks	**2,602**	**654**	**(1,668)**	**1,588**
	$ 179,169	**$ 26,314**	**$ (5,984)**	**$ 199,499**

December 31, 2003	COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	FAIR VALUE
(In thousands)				
Unaffiliated common stocks	$ 112,087	$ 20,002	$ (978)	$ 131,111
Affiliated common stocks	18,185	611	(1,922)	16,874
	$ 130,272	$ 20,613	$ (2,900)	$ 147,985

As of December 31, 2004, no goodwill was included in the statement values of affiliated common stocks. As of December 31, 2003, the statement values of affiliated common stocks included unamortized goodwill of $2,593,000.

The Company reviews common stocks for impairment on an annual basis. For common stocks valued at less than 80% of cost, the Company evaluates several qualitative factors in determining if the decline in fair value is other than temporary, including the opinion of the Company's outside equity managers, past and projected earnings growth, analysts' recommendations, industry or segment performance, and number of months the stock's fair value has been below cost. Common stocks valued at less than 50% of cost at the measurement date are deemed impaired, unless there are significant mitigating factors that indicate the decline in value is temporary. For the year ended December 31, 2003, the Company recorded an impairment loss on common stock of $78,000. For the year ended December 31, 2004, the Company did not record any impairment on common stocks.

The Company recognized impairment losses on other invested assets of $320,000 and $1,437,000 for the years ended December 31, 2004 and 2003, respectively, due to adjustments to carrying values where declines in fair value were deemed other than temporary.

Realized gains and losses on sales of equity securities are computed using historical cost. The Company realized gains of $16,854,000 and losses of $3,241,000 on sales of common stocks

2. INVESTMENTS (CONTINUED)

in 2004. The Company realized gains of $9,869,000 and losses of $4,196,000 on sales of common stocks in 2003.

As of December 31, 2004, the gross unrealized losses in unaffiliated and affiliated common stocks and the fair value of the related investments that have been in an unrealized loss position over 12 months and under 12 months are as follows:

	OVER 12 MONTHS		UNDER 12 MONTHS	
	FAIR VALUE	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	FAIR VALUE
(In thousands)				
Unaffiliated common stocks	$ 45,804	$ (2,274)	$ 18,340	$ (2,042)
Affiliated common stocks	–	(1,418)	–	(250)
	$ 45,804	$ (3,692)	$ 18,340	$ (2,292)

The fair value of affiliated common stocks with unrealized losses is zero at December 31, 2004, as the investments were non-admitted.

All of the Company's bond investments have received a Class 1 NAIC rating. As such, the Company has determined that any fluctuation in market value is a result of interest rate risk and not as a result of credit risk. For the years ended December 31, 2004 and 2003, the Company did not record any impairment on bonds.

As of December 31, 2004, the gross unrealized losses in bonds and the fair value of the related investments that have been in an unrealized loss position over 12 months and under 12 months are as follows:

	OVER 12 MONTHS		UNDER 12 MONTHS	
	FAIR VALUE	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	FAIR VALUE
(In thousands)				
Bonds	$ 58,338	$ (751)	$ 93,745	$ (1,034)

At December 31, 2004, the Company's investments in mortgage loans consist of first mortgage liens for construction and permenant financing of commercial and multi-family residential real estate of $24,926,000. The mortgaged properties are located in the state of Utah. The Company participates with banks on all mortgage loans except for an $11,639,000 commercial loan. During 2004, the respective maximum and minimum lending rates for the mortgage loans

2. INVESTMENTS (CONTINUED)

were 7.1% and 4.0% and the maximum loan to value ratio as of December 31, 2004, was 76.7%. During 2003, the respective maximum and minimum lending rates for the mortgage loans were 7.1% and 5.0% and the maximum loan to value ratio as of December 31, 2003, was 77.7%.

The Company's investments in real estate are as follows:

December 31,	**2004**	2003
(In thousands)		
Occupied by the Company:		
Land	**$ 2,062**	$ 2,062
Building	**7,076**	7,053
Less accumulated depreciation	**(2,690)**	(2,440)
Net real estate occupied by the Company	**6,448**	6,675
Held for the production of income:		
Land	**3,172**	3,172
Building	**22,697**	22,758
Less accumulated depreciation	**(4,193)**	(3,190)
Net held for the production of income	**21,676**	22,740
Net investment in real estate	**$ 28,124**	$ 29,415

Investment in real estate held for the production of income consists of a six-story Class A office building. The building was fully leased in April 2000 for eight years under a noncancelable lease and is carried at cost less accumulated depreciation. Rental income was $3,410,000 and $3,433,000 for the years ended December 31, 2004 and 2003, respectively. Future minimum rental income under noncancelable leases consist of the following:

2005	$ 2,463,000
2006	2,513,000
2007	2,588,000
2008	2,440,000
2009	–
	$ 10,004,000

Non-income producing real estate of $8,627,000 and $3,620,000 was excluded from admitted assets and reflected in unrealized capital losses at December 31, 2004 and 2003, respectively.

3. RESERVE FOR LOSSES AND LOSS ADJUSTMENT EXPENSES

Income from investments is reported net of investment related expenses of $4,301,000 and $3,915,000 for the years ended December 31, 2004 and 2003, respectively.The reserve for losses and loss adjustment expenses, net of reinsurance recoverable, consist of the following components:

December 31,	2004	2003
(In thousands)		
Medical	$ 460,078	$ 413,420
Compensation	126,062	123,243
Defense and cost containment expenses	27,832	27,840
Adjusting and other expenses	34,906	36,095
	$ 648,878	$ 600,598

Activity in the reserve for losses and loss adjustment expenses is as follows:

December 31,	2004	2003
(In thousands)		
Reserve at beginning of year, net of reinsurance recoverable of $17,497 and $20,290, respectively	$ 600,598	$ 548,958
Provision for current year	179,916	165,302
Increase in provision for prior years	3,889	5,395
	183,805	170,697
Payments for current year, net of subrogation and recoveries	53,283	46,649
Payments for prior years, net of subrogation and recoveries	82,242	72,408
	135,525	119,057
Reserve at end of year, net of reinsurance recoverable of $15,058 and $17,497, respectively	$ 648,878	$ 600,598

The 2004 and 2003 provision for prior years' losses increased due to unfavorable development on prior year claims. No single event was the cause of the changes in prior year provisions, and no additional premiums have been accrued as a result of the increases to prior-year loss reserves. The reserve is recorded net of anticipated future subrogation and reinsurance recoveries. Actual subrogation and recoveries of $3,660,000 and $5,285,000 in 2004 and 2003, respectively, have been offset against losses and loss adjustment expenses in the statement of operations and changes in policyholders' surplus and against loss and loss adjustment expenses paid in the statement of cash flows.

4. REINSURANCE

The Company cedes a portion of its premium to other insurance companies to limit its exposure arising from large losses. These ceding arrangements consist of excess of loss contracts that protect the Company against losses over stipulated amounts. For 2004 and 2003, the Company retained liability on the first $20 million of each loss while reinsurers are liable for losses from $20 million up to $100 million on occurrences involving multiple claimants (up to a maximum of $5 million for any one life). The Company also cedes premium to other insurance companies under excess of loss arrangements on a policy specific basis.

Reinsurance recoverables from individual reinsurers are as follows:

December 31,	**2004**	2003
(In thousands)		
SCOR Reinsurance Company	**$ 3,512**	$ 3,626
Pinehurst Accident Reinsurance Group	**2,651**	2,922
ReliaStar Life Insurance Company	**2,047**	2,694
St. Paul Fire and Marine Insurance Company	**1,778**	1,925
Northwestern National	**1,457**	1,898
UNUM Life Insurance Company	**852**	890
Continental Assurance Company	**704**	918
Connecticut General Life Insurance Company	**670**	651
XL Re America	**622**	788
American United Life Insurance Company	**348**	732
American National Insurance Company	**139**	151
Canada Life Insurance Company	**139**	151
Clarica Life Insurance Company	**139**	151
	$ 15,058	$ 17,497

In the event the reinsurers are unable to meet their obligations, the Company is liable for all losses, as the reinsurance agreements do not discharge the Company from its primary liability to the policyholders. In 2004 and 2003, the Company did not commute any ceded reinsurance.

Through June 30, 2004, Company assumed 80% of earned premium and losses and loss adjustement expenses in excess of Advantage's premium retention. Effective July 1, 2004, the Company assumes 100% of earned premium from Advantage for policies written for policyholders of the Company, and the Company is liable for all losses and loss adjustment expenses related to those policies.

As part of the reinsurance agreement, the Company paid a ceding commission to Advantage on earned premium subject to the reinsurance agreement of 20% to 25%. The ceding commission serves as a reimbursement to Advantage for premium taxes and other assessments, agent commissions and administrative services.

4. REINSURANCE (CONTINUED)

The Company also assumes premium for coverages written through other insurance companies under excess of loss arrangements.

The effect of reinsurance on the reserve for losses and loss adjustment expenses at December 31, 2004 and 2003 and on reserves and premiums earned and losses and loss adjustment expenses incurred for the years then ended is as follows:

	2004			2003		
	Premium	**Losses and Loss Adjustment Expenses**	**Reserve for Losses and Loss Adjustment Expenses**	Premium	Losses and Loss Adjustment Expenses	Reserve for Losses and Loss Adjustment Expenses
(in thousands)						
Direct	**$ 221,894**	**$ 166,883**	**$ 616,353**	$ 196,353	$ 149,038	$ 571,345
Assumed:						
from affiliates	**15,181**	**10,204**	**34,260**	28,046	11,252	29,8777
from non-affiliates	**11,864**	**4,588**	**13,323**	6,634	7,964	16,873
Ceded	**(3,381)**	**2,130**	**(15,058)**	(3,651)	2,443	(17,497)
	$ 245,558	**$ 183,805**	**$ 648,878**	$ 227,382	$ 170,697	$ 600,598

5. RETIREMENT PLANS

The Company contributes to the State and School Contributory Retirement System and State and School Noncontributory Retirement System, cost-sharing multi-employer defined benefit pension plans administered by the Utah Retirement System (Systems). The Systems provide refunds, retirement benefits, annual cost of living adjustments and death benefits to plan members and beneficiaries in accordance with retirement statutes.

The Systems are established and governed by Utah State law. The Systems issue a financial report that includes financial statements and required supplementary information for the State and School Contributory Retirement System and State and School Noncontributory Retirement System. A copy of the report may be obtained by writing to Utah Retirement Systems, 540 East 200 South, Salt Lake City, Utah 84102.

Plan members in the State and School Contributory Retirement System are required to contribute 6.00% of their salaries and the Company is required to contribute 8.89% of their salaries. In the State and School Noncontributory Retirement System, the Company is required to contribute 13.38% of plan members' salaries. The contribution rates are the actuarially determined rates. The contribution requirements of the Systems are authorized by statute.

5. RETIREMENT (CONTINUED)

Employees participating in the contributory or noncontributory plans are also eligible to participate in a 401(k) salary deferral program. The Company contributes 1.5% of eligible noncontributory plan participant earnings to the 401(k) salary deferral program and each individual employee may elect to contribute additional amounts.

Company contributions to the State and School Contributory Retirement System for the years ended December 31, 2004, 2003 and 2002 were $64,000, $47,000 and $53,000, respectively; Company contributions to the State and School Noncontributory Retirement System for the years ended December 31, 2004, 2003 and 2002 were $2,436,000, $1,969,000 and $1,732,000, respectively; and Company contributions to the 401(k) salary deferral program for the years ended December 31, 2004, 2003 and 2002 were $321,000, $296,000 and $276,000, respectively.

An executive of Workers Compensation Fund participates in an unfunded retirement plan administered by the Company. Plan expenses were approximately $30,000 and $157,000 for the years ended December 31, 2004 and 2003, respectively.

6. POLICYHOLDERS' SURPLUS

Property and casualty insurance companies are subject to certain Risk-Based Capital ("RBC") requirements as specified by the NAIC. Under those requirements, the adequacy of policyholders' surplus maintained by a property and casualty insurance company is determined based on various related risk factors. At December 31, 2004, the Company meets the RBC requirements.

7. INCOME TAXES

The Company has received determination from the Internal Revenue Service that it is exempt from Federal taxes under Internal Revenue Code Section 501(a).

8. GUARANTY FUND ASSESSMENT

The Company is assessed amounts by the Utah Property and Casualty Insurance Guaranty Association to cover deficits of insolvent insurance companies. These mandatory assessments may be recovered through a reduction in future premium taxes in the five years following payment. In 2004 and 2003, $392,000 was offset against premium tax payments in each year and a corresponding reduction was made to the deferred premium tax asset.

9. RELATED PARTIES

The Company shares office facilities and personnel with subsidiaries and Advantage. Shared costs and expenses are allocated to the subsidiaries and Advantage based on estimates of time and usage and those allocations may vary depending on the assumptions underlying those estimates. The amount of operating expenses allocated to subsidiaries and Advantage during 2004 and 2003 were $1,677,000 and $2,075,000, respectively. At December 31, 2004 and 2003, uncollected premiums included $1,102,000, and $30,500 in premiums due from Advantage

9. RELATED PARTIES (CONTINUED)

under reinsurance agreements. At December 31, 2004, premiums due to Advantage under reinsurance agreements of $3,070,000 were included in accounts payable and accrued liabilities. The Company incurred loss adjustment expenses of $109,000 and $93,000 for the years ended December 31, 2004 and 2003, respectively for claims administration services provided by Pinnacle.

The Company has extended a line of credit to Pinnacle at interest rates based on the prime rate plus one percent (decreasing to prime effective January 1, 2005). The Company suspended the accrual of interest under the agreement from October 1, 2004 through June 30, 2005. At December 31, 2004 and 2003, $3,843,000 and $3,376,000, respectively, were outstanding under this agreement at an interest rate of 6.25% and 5.00%, respectively. During 2004 and 2003, the Company recognized $120,000 and $117,000, respectively, of interest income related to this agreement.

10. COMMITMENTS AND CONTINGENCIES

The Company leases computer equipment and office space under noncancelable operating leases that expire in various years through 2008. These leases may be renewed for periods of up to five years. Rental expenses were approximately $1,002,000 and $1,129,000 for the years ended December 31, 2004 and 2003, respectively.

Future minimum payments under noncancelable operating leases with initial terms of one year or more consist of the following:

2005	$ 1,005,000
2006	851,000
2007	286,000
2008	67,000
2009	–
	$ 2,209,000

The Company is subject to legal proceedings arising from the normal conduct of its business. In the opinion of management, any ultimate liability that may arise from these proceedings will not have a material effect on the Company's financial position.

11. SUBSEQUENT EVENT

Effective January 1, 2005, The Company contributed its ownership interest in Advantage Services to Pinnacle.

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