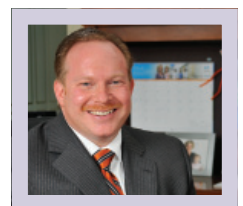


BLUE CROSS BLUE SHIELD OF MASSACHUSETTS

... Working for You



MASSACHUSETTS
ANNUAL REPORT 2008



Working for You is the 2008 annual report for Blue Cross and Blue Shield of Massachusetts, Inc. and its subsidiary, Blue Cross and Blue Shield of Massachusetts HMO Blue, Inc.

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**Letter from Cleve L. Killingsworth
Chairman, President, and Chief Executive Officer**

Massachusetts has done more than any state in the nation to provide residents with access to health care. Now we need to improve the quality and affordability of that care.

Years of independent research makes clear that as much as 30 percent of all health care spending may be unnecessary. A recent report by the New England Healthcare Institute identified hundreds of specific examples of the overuse, underuse, and misuse of health care services. The inappropriate use of care jeopardizes health care quality and patient safety and adds billions of dollars to health care costs.

Given these facts, it is no wonder that health care costs continue to rise significantly faster than the rate of inflation. The status quo is both unsustainable and unacceptable.

At Blue Cross Blue Shield of Massachusetts, we believe the most effective way to improve quality and affordability is by changing the way doctors and hospitals are paid. The current fee-for-service model rewards providers for the volume and complexity of services provided, not clinical outcomes.

We have developed an alternative Quality Contract that rewards doctors and hospitals based on the quality and clinical outcomes of the care they provide to our members. This innovative contract allows doctors and hospitals to earn more when they demonstrate high levels of performance on nationally accepted quality measures. Going forward, unless our contracts with providers address health care quality, we cannot offer payment increases that exceed the rate of inflation.



Reactions to the Quality Contract have been positive. Several physician groups and hospitals have signed the contract, and we are confident more will participate. The contract has also received national attention and is cited as a breakthrough model for much-needed payment reform.

The Quality Contract is just one of the ways that Blue Cross Blue Shield of Massachusetts is working to improve both the quality and affordability of health care. In this report, you will meet some of our leaders who are developing new and innovative ways to help the people of Massachusetts receive high-quality, patient-centered, affordable care. They—like all of our associates—work every day to keep our corporate promise: “To always put our members’ health first.”

Cleve L. Killingsworth
Chairman, President, and
Chief Executive Officer

“There’s a real soul to this company...”

Carole Waite

Senior Vice President, New Business Model

- Carole joined the company 40 years ago as a Member Service Representative
- Led the company’s effort to design and implement our award-winning concierge service model
- Promoted to Senior Vice President for Service and Operations, 2003
- Served as Chair of Board of Directors of the Resource Partnership, a non-profit organization partnering with the business community and individuals with disabilities to provide employment opportunities

In 1968, while attending night school at Northeastern University, Carole Waite landed an \$89.00 per week job as a Member Service Representative at Blue Cross of Massachusetts.

“I loved that job *so much*,” she recalls. “People depended on me to help them through a difficult situation. They would call about their health or the health of somebody they loved and you could hear the worry in their voice. To be able to ease some of their concerns—to help them get what they needed—what an incredible feeling!”



In each of her roles, Carole has always identified innovative ways to enhance the company’s performance. Last fall, when the company decided to do a comprehensive assessment of how we run our business, Carole was the perfect person to lead the corporate-wide effort because of her knowledge of the company, sharp business acumen, and proven commitment to our members.

At Blue Cross Blue Shield of Massachusetts, we are constantly looking for more efficient and economical ways to fulfill our mission. “We would be letting our members, accounts, and each other down if we did not constantly strive to become a leaner, more nimble organization,” Carole says.

And that is why Carole and her team are working to move our organization to a new business model that will position us for greater efficiency and, ultimately, to be even more competitive with an improved ability to deliver affordable products to our members and employers.

To be sure, her role and responsibilities have changed dramatically in the four decades since she joined the company. But Carole says her mission remains the same as the day she started: “The essence

“There’s a real soul to this company and you can feel it and see it in the way we treat our members. So much has changed over the years, especially with technology, but we have never lost the sense of why we are here, of our mission and the community we serve. There’s a person behind every identification card, and we try never, ever to forget it.” | **Carole Waite, Senior Vice President, New Business Model** |

of what I do has not changed,” she explains. “It’s still about people who need our help at a crucial time in their lives, and we can never, ever forget that. When you help people the way we do, it’s real, it *matters*.”

Ever since her earliest days at Blue Cross of Massachusetts, Carole understood that “behind every number on a member’s ID card is a real human being who needs our help, and that’s what our job is all about.” In her many years at the company she has assumed increasing levels of responsibility, but through it all she has never forgotten that we are here for the members.



Carole Waite surrounded by her team. L-R: Kelly Fanning, David Arbuckle, Andreas Mang, Ryan Boxill, Carole Waite, Bob Mallon, Susan Birdsey, Meredith Baumann

“...well cared for, at an affordable price.”

Audrey Shelto, MMHS

Senior Vice President, Health Care Services

Prior to joining Blue Cross Blue Shield of Massachusetts, Audrey's roles included:

- Associate Commissioner, Department of Mental Health, Commonwealth of Massachusetts
- Executive Director, Mayor's Advisory Committee on Health Care, Boston
- Assistant Director, Mental Health Services, Harvard Community Health Plan
- Chief Operating Officer, Neighborhood Health Plan

Elected to the Board of Directors of the Justice Resource Institute

Masters Degree in Management of Human Services, Heller Graduate School, Brandeis University



Audrey Shelto flanked by team members, Juan Lopera and Kristina Chung

In one way or another, Audrey Shelto has spent the last 25 years making sure people in Massachusetts have access to the health care they need. Whether it was as Associate Commissioner at the State Department of Mental Health, the Executive Director of the Boston Mayor's Advisory Committee on Health Care, or in her role as the Chief Operating Officer at Neighborhood Health Plan, Audrey has worked constantly to eliminate barriers to care.

For Audrey, access is about far more than having health insurance. It's about making sure that the care people receive is safe, effective, and affordable. Today, in her position as Senior Vice President of Health and Wellness, Audrey and her team are dedicated to helping our members with chronic illnesses manage their conditions and live the healthiest lives possible. And she is leading a corporate-wide effort to make sure that we leave no stone unturned in our efforts to provide all our members with access to higher quality, more affordable health care.

At Blue Cross Blue Shield of Massachusetts, we are determined to make health care more affordable. Since 2002, our trend management programs, including disease management programs and enhancements to our pharmacy formulary, have saved our customers more than \$1.5 billion. There is still much more to do.

Audrey knows that quality and affordability are inextricably linked. There is a significant opportunity to lower costs by removing the overuse, misuse, and underuse of care from the system. A RAND study concluded that only 60 percent of patients with chronic conditions received the care they need. And the FDA estimates that half of all antibiotics prescribed are unnecessary—a practice that increases costs and contributes to the rise of antibiotic-resistant infections.

“Audrey is working in close partnership with the Medical Directors to ensure that all our efforts are consistent with evidence-based guidelines and clinical best practices. By making health care safer and more effective, we can slow the growth in health care costs.”

| John A. Fallon, M.D., Chief Physician Executive, Senior Vice President |

There is also enormous variation in the cost of some services, with no measurable difference in quality or health outcomes. For example, tests done in hospital-based labs cost, on average, 80 percent more than work done in free-standing facilities or office settings.

Reversing these trends—changing how care is accessed and delivered, and motivating people to live healthier lives—is an enormous challenge. Audrey is working with leaders from all areas of the company to meet this challenge and help lower the medical cost trend. “We have an obligation,” says Audrey, “to make sure our members get the best care in the most cost-effective setting.”

At Blue Cross Blue Shield of Massachusetts, all of us take our role as stewards of our customers’ premium dollars very seriously. Audrey explains, “When people entrust us with their health and their dollars, they expect us to do everything within our power to make sure they are well cared for, at an affordable price. I think about that responsibility every day.”

“...transforming how care is delivered...”

Dana Gelb Safran, Sc.D.

*Senior Vice President
Performance Measurement and Improvement*

- Associate Professor, Department of Medicine, Tufts University School of Medicine
- Research Scientist, Institute for Clinical Research and Health Policy Studies, Tufts Medical Center
- Author of more than 50 peer-reviewed articles on health care quality and health policy in the scientific literature, including *JAMA*, *Health Affairs*, *Annals of Internal Medicine*
- Governor's appointee, Advisory Committee to the Massachusetts Health Care Quality and Cost Council
- Member, Board of Directors, Massachusetts Health Quality Partners (MHQP)
- Member, Board of Directors, Partnership for Healthcare Excellence
- Sc.D., Health Policy and Management, Harvard School of Public Health



There is a growing consensus that the way we pay for health care fuels rising costs and jeopardizes quality. Today, most health care payments are based on the quantity and complexity of the services provided.

Karen Davis, President of the Commonwealth Fund, observes: “Fee-for-service payments create incentives to provide more and more services, even when there may be better, lower-cost ways to treat a condition.” She also recognizes that “it’s not realistic to tell hospitals and doctors that they must improve quality if by doing so they are likely to lose money.”

At Blue Cross Blue Shield of Massachusetts, we were determined to create a payment system based on quality, outcomes, and efficiency. Simply put—what would we need to do to ensure that our members get the best results from the most appropriate treatment by the right kind of provider at the right time?

A team of Blue Cross Blue Shield of Massachusetts physicians, finance experts, and measurement scientists designed a model that would give hospitals and physicians meaningful incentives to improve the quality of care while conserving precious health care resources. Throughout the development process, the team continuously tested the concept with key hospital and physician leaders, local and national policy experts, employers, and other health care purchasers.

After months of work, the team developed the Quality Contract. The Quality Contract combines two forms of payment: a global, or fixed, payment per patient adjusted for health status that increases annually in line with inflation, and substantial performance incentives tied to the latest nationally accepted measures of quality, effectiveness, and patient experience of care. The Quality Contract values the primacy of the personal physician and recognizes the importance of coordinating patient care across the full continuum of health care services.

Dana Gelb Safran, Sc.D., Senior Vice President of Performance Measurement and Improvement, was a member of the team that designed the Quality Contract. “It is a privilege and deeply meaningful professionally to be part of something that will contribute to transforming

“Signing the Quality Contract was a great day for us, and more importantly, for our patients. The new contract aligns the incentives of patients, physicians, hospitals, employers, and health plans. Working with Blue Cross allows us to advance our long-standing commitment to high-quality, patient-centered care.” | **Dr. Barbara Spivak, President of MACIPA** |

how care is delivered,” Dr. Safran says. “To succeed under this model of care, physicians and health care organizations must focus on the patient as a whole human being—attending to the full continuum of care and on how that patient is managing his or her health in the complex day-to-day of life, not just in the confines of the medical encounter. It fundamentally changes the delivery system from one dedicated to producing visits and procedures to one dedicated to producing health.”

Mount Auburn Cambridge IPA (MACIPA) was one of the first physician groups to sign the contract. Dr. Barbara Spivak, President of MACIPA, says that “signing the Quality Contract was a great day for us, and more importantly, for our patients. The new contract aligns the incentives of patients, physicians, hospitals, employers, and health plans. Working with Blue Cross allows us to advance our long-standing commitment to high-quality, patient-centered care.”

“With data and evidence-based care, we can help populations get healthier.”

Thomas C. Hawkins, M.D., M.S.

Medical Director of Health Informatics

“A Physician for Employers”

Board Certified Internist

- M.D., University of Colorado Medical School
- Completed Medical Internship and Residency at UMass Memorial Hospital
- Practiced primary care for 11 years in Peabody and at Beverly Hospital

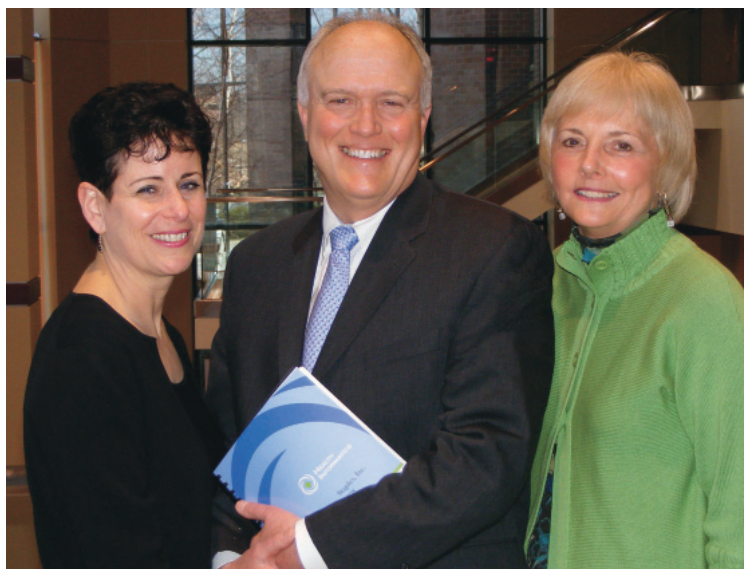
M.S., Health Policy and Management,
Harvard School of Public Health

- Clinical Instructor at Harvard Medical School in Population Health and Clinical Epidemiology

Twenty years at Harvard Pilgrim Health Care

- Associate Medical Director for Employer Health Programs
- Director of eHealth Strategy

Formerly served as Medical Director, New England Federal Reserve Bank



L-R: Account Executive Andrea Foxe Solomon; Tom Hawkins, M.D.; Nancy Lazgin, Director of Global Benefits, Staples

What is a primary care physician with 30 years experience—who also happens to be an instructor at Harvard Medical School—doing working for Blue Cross Blue Shield of Massachusetts?

“I’m doing what I’ve always done,” says Dr. Tom Hawkins, with a smile. “I’m taking care of patients, but instead of one at a time, I’m working with our employers to care for thousands of patients. I spend my time with employers figuring out how to improve the health of their employees and save money at the same time. I have no doubt that quality care means affordable care.”

As a leading specialist in the science of health informatics, Dr. Hawkins, in partnership with the Sales Account Management Teams, uses data in combination with ever evolving evidence-based guidelines to identify opportunities to improve the health of employees while simultaneously reducing the overall cost of care.

By analyzing a company’s aggregate health claims data, Dr. Hawkins can evaluate what percentage of employees are getting appropriate screenings and preventive care, and how the incidence of disease compares to the overall population.

Dr. Hawkins has found company CEOs and executives to be among his strongest allies. “When company leaders learn the facts—for example, their employees’ screening rates for various diseases are below average while the incidence of cancers, heart disease, and chronic illnesses are above average—they often feel an immediate sense of urgency to act!”

Just as every patient is different, every account is different. “Sometimes,” he says, “when there is a higher prevalence of a condition, we find that a large number of patients are not filling their prescriptions and, as a result, they may not be achieving the outcomes their physician expects, and may even be getting worse. We know from the literature that a more generous pharmacy benefit in targeted conditions can be one of the factors resulting in people taking their medicine, improving their health, and, in the long run, reducing expensive admissions. It’s a case where a little bit more of an investment up front yields tangible benefits later on.”

In other cases the data compels Dr. Hawkins to work with employers to create incentives for employees to get mammograms and colorectal screenings. Admittedly, no one enjoys these tests, but they detect diseases early when they are easier to treat, and far less costly as well.

“The Blue Cross team makes it easy to understand the health status of our associates and to do something about it. Dr. Hawkins’ analysis helps us design and target solutions unique to our workforce, which improve our associates’ health status efficiently and effectively.”

| Nancy Lazgin, Director of Global Benefits, Staples |

Using data and evidence-based guidelines, together with his colleagues at Blue Cross Blue Shield of Massachusetts, Dr. Hawkins joins forces with employers to create a “culture of health.” A culture of health increases screening rates and reduces disease, promotes participation in our disease management programs, and encourages preventive care and the adoption of healthy habits that make a huge difference.

Nancy Lazgin, the Director of Global Benefits at Staples says, “The Blue Cross team makes it easy to understand the health status of our associates and to do something about it. Dr. Hawkins’ analysis helps us design and target solutions unique to our workforce, which improve our associates’ health status efficiently and effectively.”

Dr. Hawkins and his colleagues at Blue Cross Blue Shield of Massachusetts are all about helping employers pursue the health care Holy Grail: scientific evidence that produces better health outcomes and translates to more affordable care.

“The simple choices we make every day profoundly affect our lives.”

Bryce Williams, M.S.

Director of Prevention and Wellness

Prior to joining Blue Cross Blue Shield of Massachusetts, Bryce worked as:

- Executive Director, Preventive Medicine Research Institute
- Director, Preventive Health Services, Highmark Blue Cross Blue Shield, Pennsylvania
- Chief Financial Officer and Chief Operating Officer of Lifestyle Advantage, a California wellness company

M.S., Exercise Physiology, University of Wisconsin



L-R: Account Executive Adrienne McGrath; Bryce Williams, M.S.; Donald E. Mullen, Director of Benefits, Putnam Investments

Working together, Blue Cross Blue Shield of Massachusetts and Putnam Investments, a financial services company, created Invest in Yourself, a program that fosters a “culture of health.” Invest in Yourself improved the health of Putnam associates and lowered health care costs.

Bryce Williams, Director of Prevention and Wellness, understands the components of successful prevention and wellness programs; a key component is making sure the program fits into the company’s culture. Invest in Yourself promotes the idea that “you can’t spend your wealth without your health.”

Putnam sent powerful signals throughout the firm that wellness was a priority and an important element of the company’s culture. In addition to personal health assessments (PHAs) and biometric screenings, Putnam offered workplace lectures, walking programs, yoga, Pilates, education on managing chronic diseases, Weight Watchers® at Work, and online tools as a way to surround employees with opportunities to improve their health.

“Health assessment tools are central to a successful wellness program,” says Bryce. “The challenge is finding ways to encourage employees to participate. Donald Mullen, Putnam’s Director of Benefits, worked with us every step of the way to design incentives their employees valued.”

A powerful combination of intensive promotion, on-site biometric screenings, and financial incentives helped foster a culture of health at Putnam. As a result, Putnam achieved best-in-class results; more than 70 percent of associates completed the PHA. This provided the team at Blue Cross Blue Shield of Massachusetts with the information needed to help Putnam associates live healthier lives. Blue Advisors and health coaches—nurses, dietitians, exercise physiologists—partnered with participating associates to design programs that empowered them to achieve their respective health goals.

Employees who chose to enroll in these programs saw measurable improvements. For example, in one year, Putnam experienced a 10 percent reduction in the prevalence of high blood pressure and a 40 percent increase in physical activity.

“The simple choices we make every day profoundly affect our lives—in the short term and the long term,” says Bryce. “The beauty of Invest in Yourself is that it gets more and more people to appreciate this and to act upon it now.”

“We measured many aspects of our program and found that as a result of our partnership with Blue Cross on wellness initiatives, we saved \$400,000, avoided potential claims of an additional \$1.4 million, and made a positive impact on our employees’ lives. Our cost trend is significantly lower than other companies our size.”

| Donald E. Mullen, Director of Benefits, Putnam Investments |

The costs savings are real. “We measured many aspects of our program and found that as a result of our partnership with Blue Cross on wellness initiatives, we saved \$400,000, avoided potential claims of an additional \$1.4 million, and made a positive impact on our employees’ lives,” says Donald Mullen. “Our cost trend is significantly lower than other companies our size.”

Bryce and his team collaborate with our Sales Account Management Teams and a wide range of employers—national accounts, municipalities, and mid-size accounts—to deliver results. Their work draws upon his expertise in behavioral change and exercise physiology as well as his business and financial acumen. “Each employer is different,” explains Bryce, “their cultures are different, and their values are different, but they share a common goal—improving health status and lowering the medical cost trend. We have a proven track record helping employers and their employees achieve results.”

“...from boardroom to bedside...”

Deanna Fulp, M.B.A.

Senior Director, Corporate Relations

Deanna joined Blue Cross Blue Shield of Massachusetts in 2003 as the Senior Director of Business Relations and Supplier Diversity.

- Previously, she was the Senior Director of Resource Development at Accion International, a microfinance economic development organization
- Prior to Accion, Deanna worked in International Finance with the Bank of America.
- M.B.A., Simmons School of Management



In 2001, the Institute of Medicine published its groundbreaking report stating that as many as 100,000 people die in hospitals each year from *preventable* medical errors. The errors—the deaths—are rarely the result of malfeasance or carelessness, but from systemic failures and faulty processes that prevent dedicated medical professionals from delivering high-quality care.

Deanna Fulp, Senior Director of Corporate Relations, is a member of a Blue Cross Blue Shield of Massachusetts team dedicated to doing whatever it can to help hospital trustees improve patient safety and health care quality. The trustees bear a profound fiduciary responsibility, which includes the quality and the safety of care delivered. The question was not whether to help the trustees meet the challenge, but how.

“Trustees define the hospital’s mission, articulate its vision, and set its strategy,” observes Deanna. “They are a powerful factor in driving quality. There is a direct link between the boardroom and the bedside.”

“We thought carefully about what an appropriate role for a health plan would be,” she says. “We reached out to the Massachusetts Hospital Association (MHA) for input and guidance. In partnership with the MHA, we spoke with many hospital trustees and CEOs. After a series of conversations, the answer emerged. They wanted us to be an educational collaborator and resource.”

So Deanna and her colleagues have worked closely with the American Medical Association Center for Healthcare Governance and the Massachusetts Hospital Association to develop a curriculum for hospital boards. The curriculum underscores that the trustees' responsibility for quality is an integral component of their fiduciary role. It offers guidance for trustee governance that can lead to improved health care quality—making their institutions stronger and safer.

John Lowe, Chairman of the Board at Emerson Hospital in Concord, says, “The educational program focuses our efforts as a board on what we can do, specifically, to provide higher quality and safer care for patients. We recognize, as does Blue Cross, that this is a journey boards must begin now, and commit to for the long term.”

“The educational program focuses our efforts as a board on what we can do, specifically, to provide higher quality and safer care for patients. We recognize, as does Blue Cross, that this is a journey boards must begin now, and commit to for the long term.”

| John Lowe, Chairman of the Board, Emerson Hospital |

Following the initial education programs, board members told Deanna and her colleagues that they wanted even more education and support. They were eager to hear what trustees and clinicians from other hospitals around the country were doing in the realm of quality and safety. As a result, she helped create the Trustee Insight program, which brings leading quality experts from around the country to share their ideas and successes with trustees and hospital executives in Massachusetts.

A new grant program from Blue Cross Blue Shield of Massachusetts is enabling selected hospitals to engage a coach to identify and implement specific ways to strengthen the link between trustee governance and enhanced clinical quality. In addition, hospital trustees and executives are coming together to share ideas, learn from each other's efforts, and explore new questions.

To be sure, improving health care quality is a complex task. But the work is well underway. “The trustees are enthusiastic and committed,” says Deanna. “Working together, I am absolutely convinced that we are making health care safer and better for everyone.”

“We have a tradition of technological innovation.”

Steven J. Fox, B.S., PAHM

Vice President, Provider Network Management

- Steve joined Blue Cross Blue Shield of Massachusetts in 1991
- Sets the strategic direction and oversees provider relations, education, and communications
- Heads up Blue Cross Blue Shield of Massachusetts eHealth initiatives
- Appointed to the Health Information Exchange Economic Sustainability Panel, an advisory group reporting to the U.S. Department of Health and Human Services
- Nationally recognized expert on eHealth and ePrescribing
- Board member of the Massachusetts eHealth Collaborative
- B.S., Communication, University of Miami
- Earned professional designation in the Academy for Healthcare Management (PAHM)

When it comes to health information technology, Blue Cross Blue Shield of Massachusetts is a pioneer.

Almost 20 years ago, we were one of the first plans to provide physicians' offices with technology that allowed them to check patients' eligibility and coverage at the point of service. Building upon the success of this effort, we introduced technology that enabled providers to submit claims electronically, significantly increasing efficiency and accuracy. More recently, we've been working with providers to perform these functions over the Internet so that we can achieve the same types of efficiencies and cost-savings experienced by the banking industry.



Through innovative pilots and seed money, Blue Cross Blue Shield of Massachusetts has taken a leadership role in the adoption of innovative medical information technologies, including e-prescribing and electronic health records. We were instrumental in building the Massachusetts eRx Collaborative. As a result of the eRx Collaborative's success, Massachusetts leads the nation in e-prescribing, and for three consecutive years, our state has received the prestigious Safe-Rx Award.

We also provided \$50 million dollars to launch the Massachusetts eHealth Collaborative, which funded the implementation of comprehensive electronic health records in three communities. These communities are now models and learning laboratories for Massachusetts as well as the nation.

Steve Fox, who joined Blue Cross Blue Shield of Massachusetts in 1991, has been a key player in each of these initiatives. His teams have led efforts to develop partnerships with vendors, providers, and other players in the Massachusetts health care market to ensure the success of these ventures. “Health care has a lot of moving parts and complicated information. We have an obligation to make it easier and

safer for everyone—the people who provide care and the people who receive it,” Steve notes.

In 2008, Steve led Blue Cross Blue Shield of Massachusetts’ efforts to join with Google™ as the first health plan in the nation to integrate with Google Health, a free online personal health record (PHR). The Google Health PHR enables our members, who choose to do so, to create a secure, password protected online PHR that collects their health history—conditions, procedures, prescriptions—in a single record. Our members can now manage and maintain their own health information by downloading up to two years of their Blue Cross Blue Shield of Massachusetts claims history and importing health information from other integrated providers on the Google Health platform, such as labs, hospitals, and retail pharmacies. Members can also add additional personal information to the Google Health PHR as they choose. Member information is never sent to Google without explicit consent from the member.

“Our members tell us they want easier and more portable access to their health care information,” said Steve. “Having this information in one place can help our members and their doctors make health care decisions that can improve the quality of care they receive.”

“Our partnership with Blue Cross is groundbreaking. Google offers a unique ability to store and synthesize information in a way that is easily viewable for patients. Blue Cross is committed to helping their members be informed health care decision-makers. Together, we can empower patients to become more knowledgeable about their health status and even more engaged in their health care.”

| Sameer Samat, Director of Product Management, Google Health |

Giving our members access to a Google Health account that integrates with Blue Cross Blue Shield of Massachusetts puts them in control of their medical information. It also enables members to learn about potential drug-to-drug interactions or a health issue pertinent to their health status. The Google PHR lets members access their complete health record via the Internet anytime and anywhere—while traveling, at home, in a doctor’s office—all that’s needed is an Internet connection.

“Our partnership with Blue Cross is groundbreaking. Google offers a unique ability to store and synthesize information in a way that is easily viewable for patients. Blue Cross is committed to helping their members be informed health care decision-makers,” said Sameer Samat, Director of Product Management for Google Health. “Together, we can empower patients to become more knowledgeable about their health status and even more engaged in their health care.”

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Seated L-R: Wiley, Guzzi, Larson, Aspinall, Lunt, Lavelle
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*Chairman, President,
and Chief Executive Officer*
Blue Cross and Blue Shield of MA
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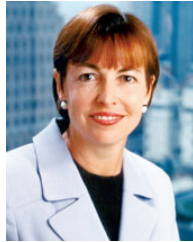
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Dean
Boston University School of Public Health
Boston, MA

Benaree P. Wiley

Principal
The Wiley Group
Brookline, MA

Letter from Gloria C. Larson
Lead Director



For more than 70 years, Blue Cross Blue Shield of Massachusetts has been a leading health plan and a valued corporate citizen. The company is more committed than ever to providing affordable health care solutions to employers and individuals. As part of this commitment, the corporation deliberately keeps its margin small—less than one percent in 2008. It spends just over ten cents of each dollar on administrative expenses, such as investments in technology, salary and benefits, advertising, taxes, and office facilities. Blue Cross Blue Shield of Massachusetts returns almost 90 cents of every premium dollar to members in the form of payments to health care providers. Never complacent, the leadership team continuously seeks to deliver new products and services to the market and to operate even more efficiently.

It is a privilege to serve on the Board of Directors with prominent physicians and business and community leaders. Together with his first-rate leadership team, Cleve Killingsworth continues to strengthen Blue Cross Blue Shield of Massachusetts' long-standing position as the market leader. The Board shares Cleve Killingsworth's commitment to improving the health care system, not just for the members of Blue Cross Blue Shield of Massachusetts, but for everyone in the Commonwealth.

Gloria C. Larson
Lead Director

Executive Team



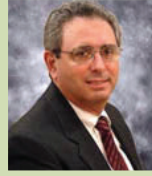
Cleve L. Killingsworth
*Chairman, President, and
Chief Executive Officer*



Sandra L. Jesse
*Executive Vice President
Chief Legal Officer*



Ann S. Anderson
*Senior Vice President
Chief Human Resources
Officer*



Allen P. Maltz
*Executive Vice President
Chief Financial Officer*



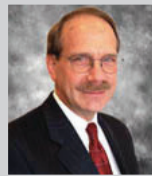
Stephen R. Booma
*Executive Vice President
Sales, Marketing,
Service, and Information
Technology*



Vinod K. Sahney, Ph.D.
*Senior Vice President
Chief Strategy Officer*



John J. Curley, Jr.
*Senior Vice President
Chief Government and
Public Affairs Officer*



John Schoenbaum
*Senior Vice President
and Chief of Staff
Executive Office and
Communications*



Andrew Dreyfus
*Executive Vice President
Health Care Services*



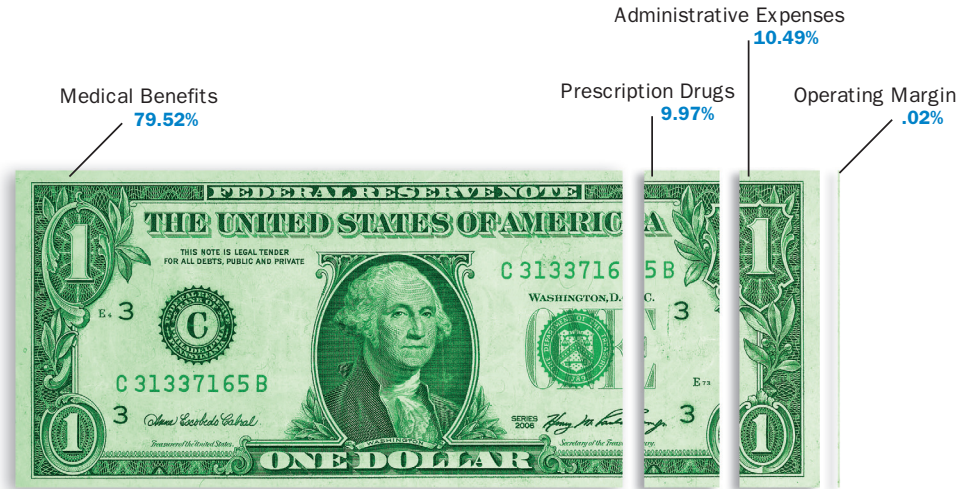
Fredi Shonkoff
*Senior Vice President
Corporate Relations*



John A. Fallon, M.D.
*Senior Vice President
Chief Physician Executive*

A Careful Steward of the Premium Dollar

Blue Cross Blue Shield of Massachusetts is committed to being a careful steward of the premium dollars entrusted to us by employers and members. We deliberately keep our profit margin small—.02% in 2008—so we can maximize what we return to our members in the form of payments to health care providers and pharmacies. The corporation consistently returns almost 90 cents of each dollar to our members and retains, on average, about ten cents to run the business. This includes compensation, investments in information technology, advertising, taxes, and office facilities. Our reserves protect members, providers, and employers, as they help to ensure that we can meet our financial obligations, even in the midst of market disruptions.



Blue Cross Blue Shield of Massachusetts consistently strives to lower the health care cost trend while improving the quality of health care for all citizens of Massachusetts.

Competitive Compensation Assessment

Blue Cross Blue Shield of Massachusetts conducts regular annual reviews of competitive compensation levels for associates and leaders. Watson Wyatt Worldwide conducted the 2008 review of the compensation programs for the Human Resources Committee (HRC) of the Board of Directors, which is responsible for ensuring that Blue Cross Blue Shield of Massachusetts' total compensation programs are reasonable, reflect best-practices, and are comparable to the median levels in the market. As part of their work, Watson Wyatt Worldwide evaluates all broad-based associate compensation programs as well as those that apply to the Chairman and CEO, all executive and senior vice presidents, and the Board of Directors.

Watson Wyatt Worldwide is a global consulting firm focused on human capital and financial management, specializing in compensation, benefits, human-capital strategies, technology solutions, and insurance and financial services. The HRC has engaged Watson Wyatt Worldwide directly. Watson Wyatt Worldwide is an independent firm and is hired by the HRC for the single purpose of informing and assessing our compensation practices and programs. Watson Wyatt Worldwide has no other engagement with Blue Cross Blue Shield of Massachusetts.

The 2008 review was designed to determine whether current Blue Cross Blue Shield of Massachusetts programs continue to be reasonable given the company's business direction and current market practice. To the greatest extent possible, the methodology for Wyatt's review has been consistently applied, focusing on similar data sources as in prior years. The review focused on:

- Compensation philosophy, which reflects Blue Cross Blue Shield of Massachusetts' dual commitment to our members and to achieving the solid financial performance required to fulfill our nonprofit mission and obligations to our members and the providers who serve them;
- Base-salary structure and administrative guidelines;
- Incentive pay provided through the Associate Performance Plan, Leadership Performance Plan, and Long-Term Incentive Plan (short-term and long-term incentive programs);
- Executive benefits.

Watson Wyatt Worldwide concluded that the current philosophy and programs are consistent with competitive market practices. Blue Cross Blue Shield of Massachusetts' programs are effectively designed to provide sufficient flexibility to respond to market trends over time. Continued consideration will be given to the short-term and long-term incentive performance measures to ensure that the programs continue to support the company's business needs and are aligned with current strategic objectives. The HRC and the Board of Directors will continue to evaluate programs on at least an annual basis relative to market trends and business needs.

Compensation Philosophy and Programs

Blue Cross Blue Shield of Massachusetts' 2008 compensation philosophy was most recently reviewed and approved by the HRC in November 2007. The review indicated that the philosophy continues to effectively support business needs and reflects market practice. The HRC understands and appreciates the cost and cash flow components of all the compensation and benefits programs.

Key elements of the philosophy are:

- Provide competitive compensation opportunities (salary and incentives) sufficient to attract and retain high-quality associates and to motivate them to achieve superior performance.
- Place a significant portion of compensation at reasonable risk through incentive plans for associates in leadership positions.
- Provide *all* associates with the opportunity to supplement competitive base salaries with performance incentives.
- Support business plans and strategies with effective compensation arrangements.
- Ensure compensation results that are reasonable and consistent with sound business practices found in other large, multi-product, billion-dollar organizations.
- Ensure that no-more-than-reasonable compensation is paid by linking incentive payments first to overall corporate performance and second to individual performance as assessed by each individual's leader. For the Chairman and CEO and his direct reports, the HRC reviews each individual's respective performance assessment and total compensation annually.

Competitive Compensation Assessment

Our Philosophy	Program
Provide competitive compensation opportunities sufficient to attract and retain high-quality associates.	The base-pay program targets median compensation levels based on industry and/or local market practice.
Place a significant portion of compensation at reasonable risk through incentive plans for associates in leadership positions.	The Leadership Performance Plan provides leaders with an incentive opportunity targeted at 10% to 100% of base salary. In combination with the Long-Term Incentive Plan, with its incentive opportunity targeted at 10% to 125%, the programs encourage a balance between short-term business goals and long-term organization objectives.
Provide all associates with the opportunity to supplement base salaries through an incentive plan.	The Associate Performance Plan provides all associates in non-leadership positions with an incentive opportunity targeted at 5% of base salary. Blue Cross Blue Shield of Massachusetts also provides a wide range of additional recognition programs targeted at specific business groups and recognizing key accomplishments within those groups.
Support business plans and strategies with effective compensation arrangements.	The incentive plans provide a platform for communicating the company's goals and rewarding their achievement. The plans are designed to focus associates on desired behaviors and link overall compensation with demonstrated results.
Ensure compensation results that are reasonable and consistent with sound business practices.	Blue Cross Blue Shield of Massachusetts uses flexible compensation policies and procedures that permit the organization to compete effectively for essential talent. The elements employed in the current compensation program are consistent with prevalent market practice.

How Current Programs Support the Philosophy

Blue Cross Blue Shield of Massachusetts' current programs effectively support the compensation philosophy as summarized above:

- **Base Salary Structure**

Blue Cross Blue Shield of Massachusetts targets base salary at median market levels, which is consistent with market practice. The base-pay structure and administrative practices generally align well with those of other organizations.

- **Annual Incentive Plans**

As part of fulfilling its compensation philosophy, Blue Cross Blue Shield of Massachusetts provides annual incentive opportunities to all associates, through a combination of the Leadership Performance Plan and the Associate Performance Plan. The 2008 plan focused on financial performance and membership.

- **Long-Term Incentive Plan**

In addition to the short-term incentive plans, the Long-Term Incentive Plan (for senior leaders) bases awards on company performance and provides a key element in the attraction and retention of talented executives. The performance measure for the 2006 through 2008 performance cycle was membership growth combined with a minimum level of statutory reserves. Rewarding increased membership through the Long-Term Incentive Plan focuses senior leaders on the delivery of cost-effective products that provide access to high-quality health care. No award was paid under this cycle.

- **Recognition Programs**

In addition to annual and long-term incentives, Blue Cross Blue Shield of Massachusetts sponsors a wide range of recognition programs that can effectively motivate and reward individual or team accomplishments and ideas. All associates are eligible for at least one form of recognition award, with the nature of awards varying based on individual department success criteria.

Competitive Compensation Assessment

Competitive Assessment of Compensation for Associates and Board of Directors

The HRC, on behalf of Blue Cross Blue Shield of Massachusetts, conducts regular annual reviews of compensation for all associates and the Board of Directors. This year's analysis and report were prepared by Watson Wyatt Worldwide. To ensure consistency, to the greatest extent possible, the methodology for the review has remained unchanged year-to-year, focusing on similar data sources as in prior years, and presented in a similar format.

The comparator organizations used in the analysis continue to reflect a mix of large Blue Cross Blue Shield organizations, the broader health care industry, and public health insurance companies. Watson Wyatt Worldwide and the HRC believe this

mix of comparators (which includes a mix of stock versus non-stock organizations) continues to be appropriate given the nature of Blue Cross Blue Shield of Massachusetts' competition for senior executive talent. The greatest competition for executive talent is found within other large health insurers and managed care companies.

Based on the analysis prepared by Watson Wyatt Worldwide, the HRC reviews proposed compensation levels for all associates as well as the Board of Directors and presents a final recommendation to the full board for its review and approval.

Key findings of the 2008 analysis suggest that current senior associate compensation levels are generally consistent with median market practice, as summarized below.

Compensation Element	Findings
Base Salaries	Overall, base salaries are within a competitive range (+/-15%) of median industry market practice, including the CEO position.
Total Cash Compensation (TCC—base salary plus target annual bonus)	Target total cash compensation is generally competitive with median market practice.
Total Direct Compensation (TDC—base salary plus target annual bonus and target long-term incentives)	Blue Cross Blue Shield of Massachusetts' target total direct compensation levels are generally within a competitive range of the market median. Total direct compensation levels are more conservative (lower) when compared to public peer organizations of similar size due to the prevalent use of equity compensation among those organizations.
Supplemental Retirement Program (SRP)	The SRP remains a common market practice and is limited to select participants approved by the Board. Key features of the SRP are above median market practice; however, retirement benefits at not-for-profit organizations tend to be greater than those provided at public organizations that rely more heavily on stock-based pay. This program has been closed to new participants.
Executive Benefits	The type and level are consistent with median market practice.

Financial Statements

Combined Balance Sheets

(In thousands)

	December 31	
	2008	2007
Admitted assets		
Bonds	\$ 862,585	\$ 907,476
Preferred stock	5,327	23,181
Common stock	380,475	387,074
Properties occupied by the company	231,857	236,410
Cash, cash equivalents, and short-term investments	166,427	59,736
Receivable for securities	4,402	3,816
Other invested assets	717,932	944,362
Total cash and invested assets	2,369,005	2,562,055
Accrued investment income	7,789	7,833
Premiums receivable	34,422	55,020
Reinsurance receivables	6,197	—
Receivables related to uninsured plans	537,705	395,873
Income tax recoverable	282	47,047
Net deferred tax asset	16,707	12,961
Data processing equipment	6,760	11,094
Receivable from affiliates	344	20
Health care and other receivables	33,099	32,778
Due from Federal Employees Program	33,908	40,502
Other assets	44,890	43,349
Total admitted assets	\$3,091,108	\$3,208,532
Liabilities and surplus		
Health care claim reserves	\$ 557,442	\$ 518,625
Accrued medical incentive pool and bonus payments	50,343	40,431
Aggregate policy reserves	27,117	41,904
Premiums received in advance	170,641	141,675
Federal income taxes payable	10,372	4,550
Accounts payable and accrued liabilities	294,242	355,002
Ceded reinsurance payable	6,842	29
Payable to affiliates	2,354	9,849
Payable for securities	6,930	4,522
Liability for amounts held under uninsured plans	585,985	454,672
Liability for post-retirement benefits	57,633	50,932
Total liabilities	1,769,901	1,622,191
Surplus	1,321,207	1,586,341
Total liabilities and surplus	\$3,091,108	\$3,208,532

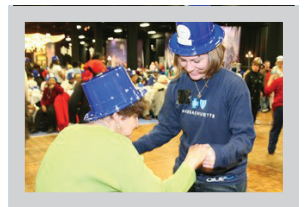
Audited financial reports are available at www.bluecrossma.com/2008AuditedFinancials

Combined Statements of Income

(In thousands)

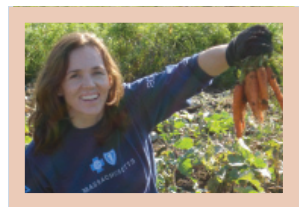
	Year Ended December 31	
	2008	2007
Premiums earned	\$6,670,849	\$6,729,373
Health care benefits	5,969,687	5,970,577
Claim adjustment expenses	370,242	383,320
General and administrative expenses	329,281	322,048
Total expenses	6,669,210	6,675,945
Underwriting gain	1,639	53,428
Net investment income	105,935	100,505
Net realized capital gains, less capital gains tax of \$1,142 and \$4,846 in 2008 and 2007, respectively	5,944	55,272
Total investment gains	111,879	155,777
Other income	1,396	190
Net income before federal income tax expense	114,914	209,395
Federal income tax expense	9,526	670
Net income	\$ 105,388	\$ 208,725

Audited financial reports are available at www.bluecrossma.com/2008AuditedFinancials



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... Working for You





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