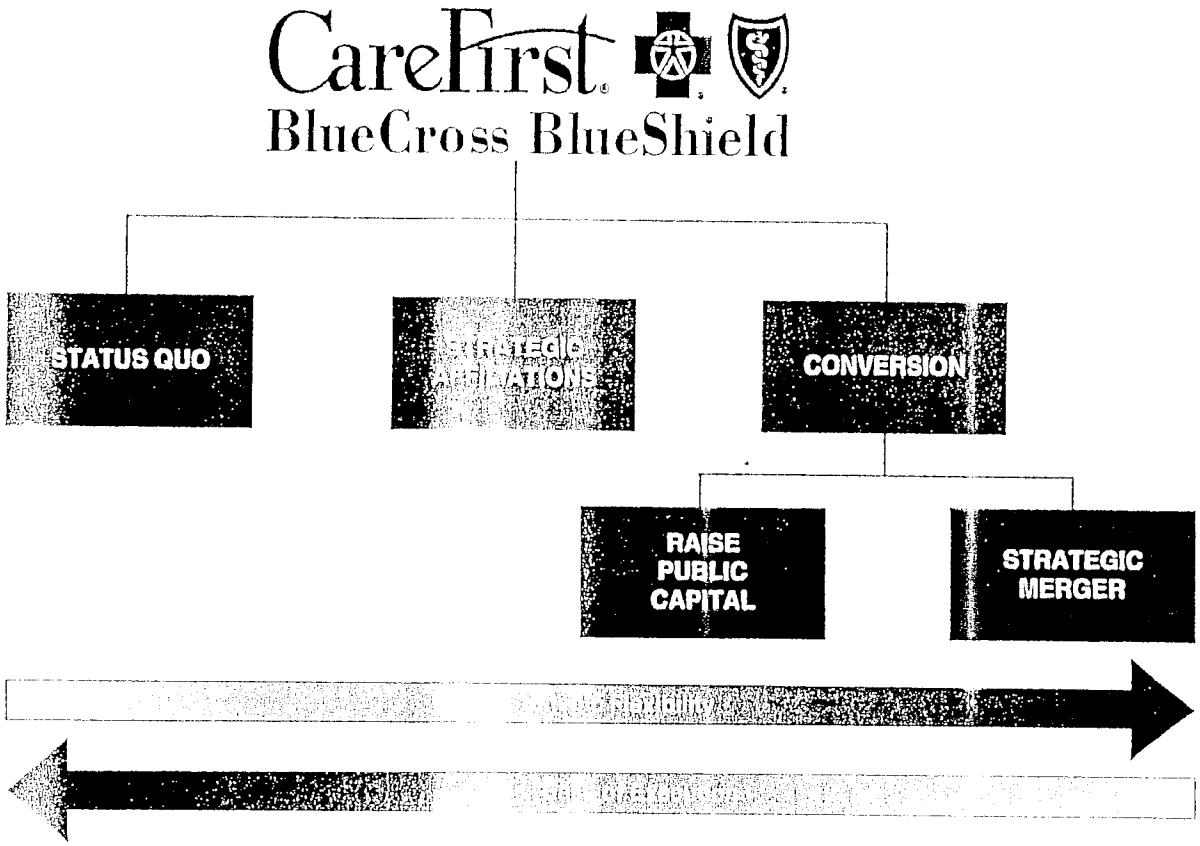
STRATEGIC ALTERNATIVES

CareFirst has a wide range of strategic alternatives available to it, each with a set of advantages and disadvantages. DLJ has detailed these alternatives in Appendix I, as well as next steps and considerations.



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APPENDIX I

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STRATEGIC ALTERNATIVES

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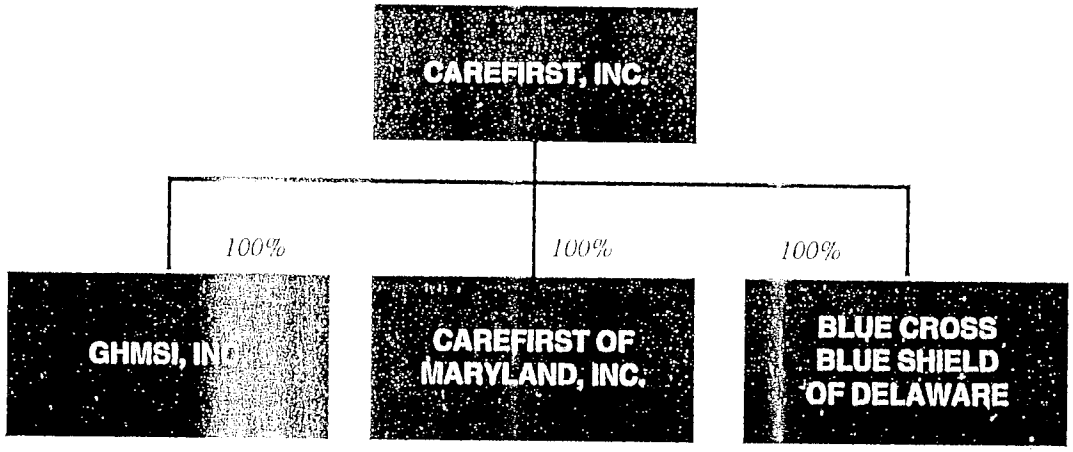
OPTION 1: STATUS QUO

Preserve the current affiliation agreement among the BCBS plans in Maryland, Delaware and Washington, DC.



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OPTION 1: STATUS QUO (CONT'D)

Continuing with the current corporate structure offers significantly less risk, but may impair the Company's long-term prospects.

Advantages

- ▲ No action required
- ▲ Avoid probability of significant media and political scrutiny

Disadvantages

- ▼ Limited access to capital markets
- ▼ Limited acquisition currency
- ▼ Limited ability to pursue strategic mergers or acquisitions
- ▼ Sub-optimal positioning for long-term plan growth
- ▼ Foregone first mover advantage during market consolidation
- ▼ Vulnerability to larger, better capitalized competitors
- ▼ Impaired ability to fund competitive technology improvements

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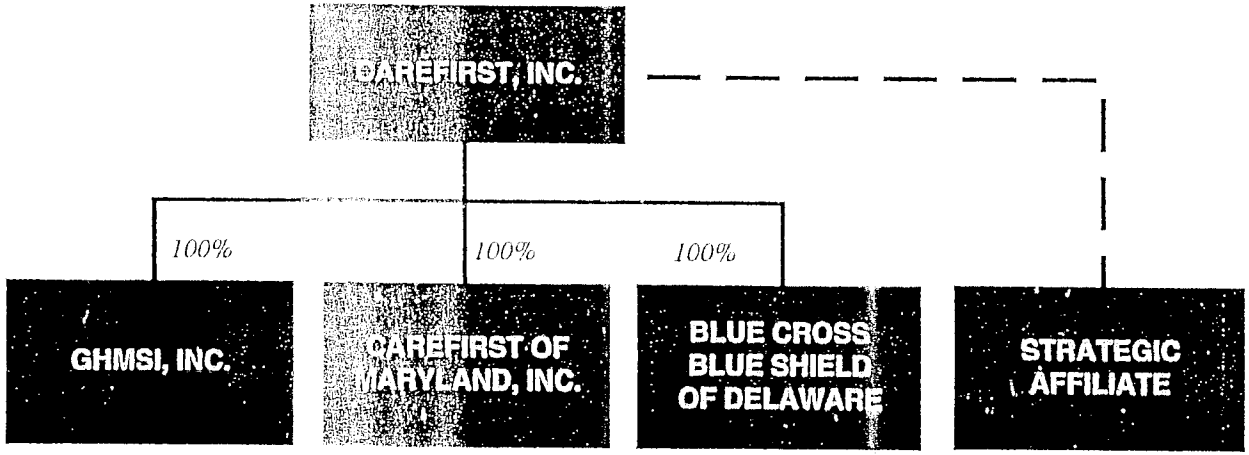
OPTION 2: STRATEGIC AFFILIATIONS

Replicate current affiliation structure with BCBS plans in adjacent markets.

Post-Affiliation



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OPTION 2: STRATEGIC AFFILIATIONS (CONT'D)

The strategic affiliations model has proven successful in the past, but may limit possibilities for future growth.

Advantages

- ▲ Successful precedent in BCBSD and GHMSI transactions
- ▲ Relatively inexpensive to implement

Disadvantages

- ▼ Limited access to capital markets
- ▼ Limited acquisition currency
- ▼ Complicated governance and management structure
- ▼ Strategic affiliation opportunities may be limited
- ▼ Limited ability to reap synergies typically associated with mergers and acquisitions transactions
- ▼ Probability of significant media and political scrutiny

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OPTION 3: CONVERSION

Conversion to a stockholder-owned corporation to facilitate strategic combinations and/or access to the public capital markets.

- **The term "conversion" often relates to a transaction in which:**

  A non-profit health plan transfers a substantial portion of its assets to a for-profit subsidiary;

  The for-profit subsidiary offers stock to the public, resulting in partial public ownership of the plan's assets; and,

  Most of the plan's insurance operations are carried out through the for-profit subsidiary, which continues to have the same management as the non-profit parent.

- **In recent years, a number of BCBS plans have undergone some form of a conversion.**

  The conversion of the BCBS plan in Missouri (RightCHOICE) was carried out in the manner described above and continues to be partially owned by a non-profit BCBS plan. BCBSMO is currently awaiting final approval for the conversion of the entire entity to for-profit status.

  The conversion of Blue Cross of California (WellPoint) was initially conducted in the manner described above. However, subsequently the entire Blue Cross plan converted to for-profit status.

  The conversion of BCBS Virginia (Trigon) was actually a demutualization in which policyholders received value and the BCBS plan took on for-profit status.

- **Since the elimination of the non-profit requirement for BCBS plans in 1994, three of the fifty-one BCBS plans (Georgia, California and Virginia) have fully converted to for-profit ownership.**

  Plans in Kansas, Massachusetts, New York, North Dakota, Ohio and Wisconsin, among others, are currently considering or have considered conversions.

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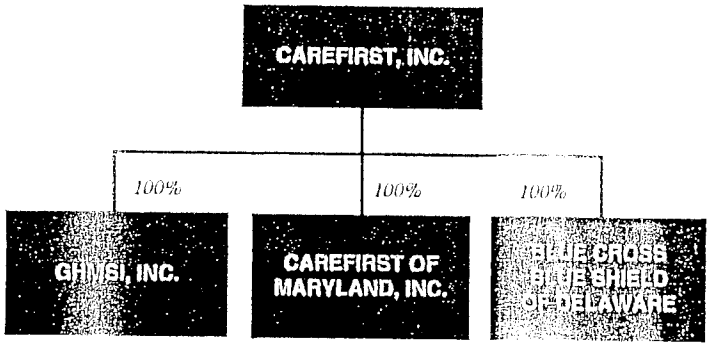
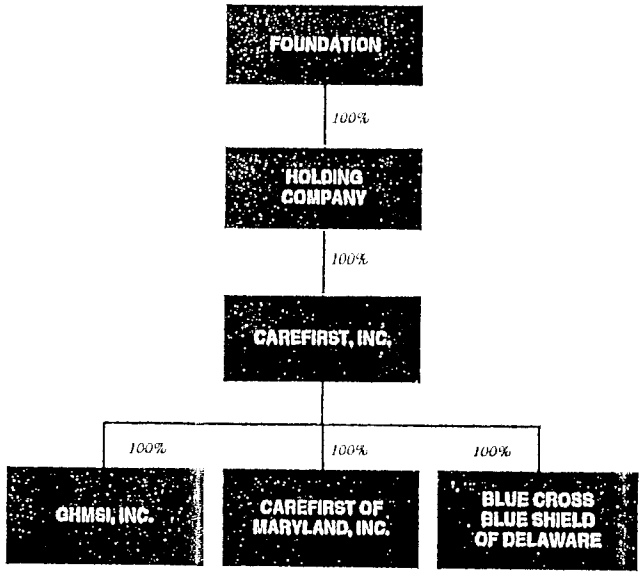
OPTION 3: CONVERSION (CONT'D)

A conversion to a stock insurance company structure would result in the following reorganization to CareFirst's corporate structure.

Pre-Conversion



Post-Conversion



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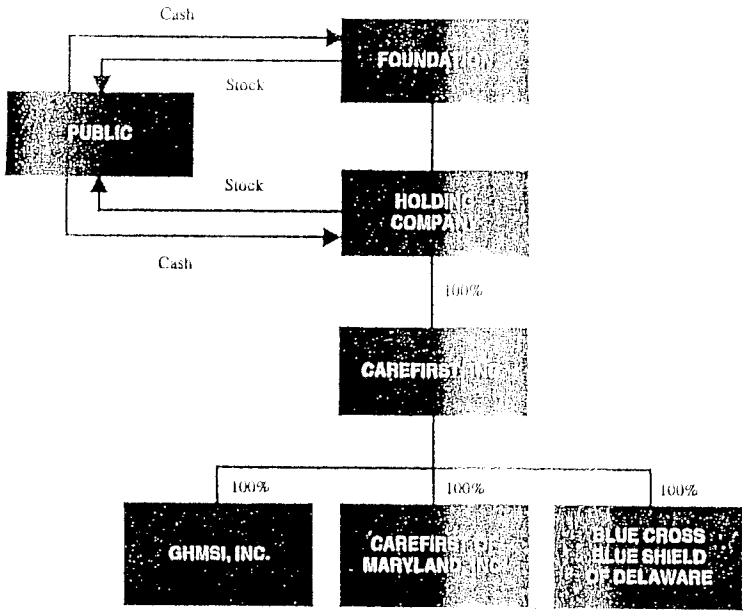
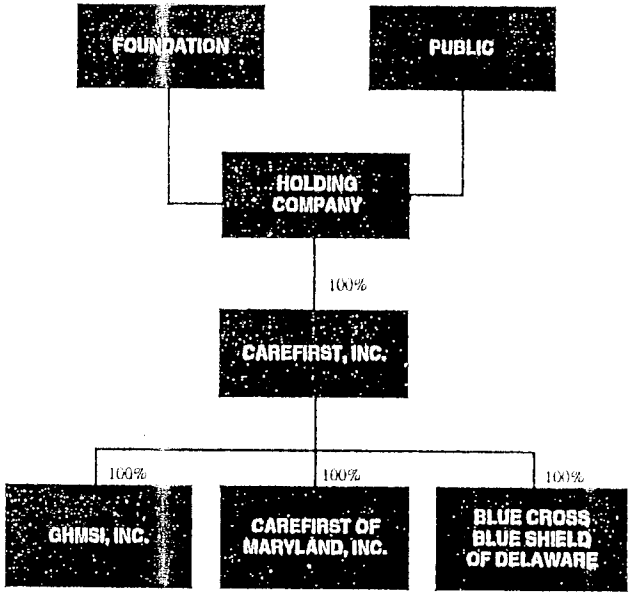
OPTION 3A: RAISE PUBLIC CAPITAL

Under this scenario, CareFirst would first convert to a stock-corporation and then raise new capital from the public markets to fund its operating plans.

Post-Conversion



Post-Capital Raise



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