CIGNA CORP
Form 10-Q
May 03, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

[x] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended **March 31, 2006**

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

for the transition period from _____ to _____

Commission file number 1-8323

CIGNA Corporation
(Exact name of registrant as specified in its charter)

Delaware	**06-1059331**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

Two Liberty Place, 1601 Chestnut Street
Philadelphia, Pennsylvania 19192
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code **(215) 761-1000**

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No _

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes x No _

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes _ No x

As of March 31, 2006 119,758,787 shares of the issuer's common stock were outstanding.

CIGNA CORPORATION

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As used herein, CIGNA refers to one or more of CIGNA Corporation and its consolidated subsidiaries.

Part I. FINANCIAL INFORMATION
Item 1. Financial Statements

CIGNA CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(In millions, except per share amounts)

	Three Months Ended March 31, 2006		Three Months Ended March 31, 2005	
REVENUES				
Premiums and fees	$	3,268	$	3,362
Net investment income		329		330
Other revenues		366		636
Realized investment gains		144		17
Total revenues		4,107		4,345
BENEFITS AND EXPENSES				
Health Care medical claims expense		1,448		1,456
Other benefit expenses		788		868
Other operating expenses		1,343		1,356
Total benefits and expenses		3,579		3,680
INCOME BEFORE INCOME TAXES		528		665
Income taxes (benefits):				
Current		254		59
Deferred		(78)		170
Total taxes		176		229
NET INCOME	$	352	$	436
EARNINGS PER SHARE - BASIC	$	2.93	$	3.34
EARNINGS PER SHARE - DILUTED	$	2.87	$	3.28
DIVIDENDS DECLARED PER SHARE	$	0.025	$	0.025

The accompanying Notes to the Financial Statements are an integral part of these statements.

CIGNA CORPORATION
CONSOLIDATED BALANCE SHEETS
(In millions, except per share amounts)

	As of March 31, 2006	As of December 31, 2005
ASSETS		
Investments:		
Fixed maturities, at fair value (amortized cost, $13,612; $13,873)	$ 14,328	$ 14,947
Equity securities, at fair value (cost, $146; $113)	163	135
Mortgage loans	4,206	3,934
Policy loans	1,341	1,337
Real estate	95	80
Other long-term investments	449	504
Short-term investments	105	439
Total investments	20,687	21,376
Cash and cash equivalents	1,904	1,709
Accrued investment income	289	282
Premiums, accounts and notes receivable	1,482	1,598
Reinsurance recoverables	6,719	7,018
Deferred policy acquisition costs	644	618
Property and equipment	626	638
Deferred income taxes	1,215	1,087
Goodwill	1,622	1,622
Other assets, including other intangibles	285	306
Separate account assets	8,555	8,609
Total assets	$ 44,028	$ 44,863
LIABILITIES		
Contractholder deposit funds	$ 9,423	$ 9,676
Future policy benefits	8,405	8,626
Unpaid claims and claim expenses	4,272	4,281
Health Care medical claims payable	1,065	1,165
Unearned premiums and fees	523	515
Total insurance and contractholder liabilities	23,688	24,263
Accounts payable, accrued expenses and other liabilities	5,029	5,127
Short-term debt	85	100
Long-term debt	1,253	1,338
Nonrecourse obligations	66	66
Separate account liabilities	8,555	8,609
Total liabilities	38,676	39,503

CONTINGENCIES - NOTE 12

SHAREHOLDERS' EQUITY				
Common stock (par value per share, $0.25; shares issued, 160; 160)		40		40
Additional paid-in capital		2,419		2,385
Net unrealized appreciation, fixed maturities	$ 100		$ 195	
Net unrealized appreciation, equity securities	20		24	
Net unrealized depreciation, derivatives	(15)		(14)	
Net translation of foreign currencies	9		2	
Minimum pension liability adjustment	(716)		(716)	
Accumulated other comprehensive loss		(602)		(509)
Retained earnings		5,425		5,162
Less treasury stock, at cost		(1,930)		(1,718)
Total shareholders' equity		5,352		5,360
Total liabilities and shareholders' equity		$ 44,028		$ 44,863
SHAREHOLDERS' EQUITY PER SHARE		$ 44.69		$ 44.23

The accompanying Notes to the Financial Statements are an integral part of these statements.

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CIGNA CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME AND CHANGES IN SHAREHOLDERS' EQUITY
(In millions)

Three Months Ended March 31,		2006		2005
Common stock		$ 40		$ 40
Additional paid-in capital, January 1		2,385		2,360
Effect of issuance of stock for employee benefits plans		34		(21)
Additional paid-in capital, March 31		2,419		2,339
Accumulated other comprehensive loss, January 1		(509)		(336)
Net unrealized depreciation, fixed maturities	$ (95)	(95)	$ (146)	(146)
Net unrealized depreciation, equity securities	(4)	(4)	(2)	(2)
Net unrealized depreciation on securities	(99)		(148)	
Net unrealized depreciation, derivatives	(1)	(1)	(2)	(2)
Net translation of foreign currencies	7	7	3	3
Other comprehensive loss	(93)		(147)	
Accumulated other comprehensive loss, March 31		(602)		(483)
Retained earnings, January 1		5,162		3,679
Net income	352	352	436	436
Effects of issuance of stock for employee benefits plans		(86)		(42)
Common dividends declared		(3)		(3)
Retained earnings, March 31		5,425		4,070
Treasury stock, January 1		(1,718)		(540)
Repurchase of common stock		(419)		(240)
Other, primarily issuance of treasury stock for employee benefit plans		207		123
Treasury stock, March 31		(1,930)		(657)
TOTAL COMPREHENSIVE INCOME AND SHAREHOLDERS' EQUITY	$ 259	$ 5,352	$ 289	$ 5,309

The accompanying Notes to the Financial Statements are an integral part of these statements.

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CIGNA CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions)

	Three Months Ended March 31, 2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	$ 352	$ 436
Adjustments to reconcile net income to net cash provided by operating activities:		
Insurance liabilities	(132)	(216)
Reinsurance recoverables	31	(52)
Deferred policy acquisition costs	(21)	(17)
Premiums, accounts and notes receivable	68	146
Accounts payable, accrued expenses and other liabilities	(165)	113
Current income taxes	222	(42)
Deferred income taxes	(78)	170
Realized investment (gains)	(144)	(17)
Depreciation and amortization	54	62
Gains on sales of businesses	(17)	(286)
Mortgage loans originated and held for sale	(240)	-
Other, net	(17)	(26)
Net cash provided by (used in) operating activities	(87)	271
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from investments sold:		
Fixed maturities	535	594
Equity securities	5	4
Mortgage loans	136	151
Other (primarily short-term investments)	611	25
Investment maturities and repayments:		
Fixed maturities	518	194
Mortgage loans	69	76
Investments purchased:		
Fixed maturities	(755)	(904)
Equity securities	(30)	(5)
Mortgage loans	(252)	(53)
Other (primarily short-term investments)	(150)	(113)
Property and equipment, net	(30)	(23)
Net cash provided by (used in) investing activities	657	(54)
CASH FLOWS FROM FINANCING ACTIVITIES		
Deposits and interest credited to contractholder deposit funds	141	176

Withdrawals and benefit payments from contractholder deposit funds		(179)		(168)
Change in cash overdraft position		4		(193)
Repayment of long-term debt		(100)		-
Repurchase common stock		(400)		(242)
Issuance of common stock		162		94
Common dividends paid		(3)		(3)
Net cash used in financing activities		(375)		(336)
Net increase (decrease) in cash and cash equivalents		195		(119)
Cash and cash equivalents, beginning of period		1,709		2,519
Cash and cash equivalents, end of period	$	1,904	$	2,400
Supplemental Disclosure of Cash Information:				
Income taxes paid (received), net	$	8	$	91
Interest paid	$	22	$	22

The accompanying Notes to the Financial Statements are an integral part of these statements.

CIGNA CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

The consolidated financial statements include the accounts of CIGNA Corporation, its significant subsidiaries, and variable interest entities of which CIGNA is the primary beneficiary, which are referred to collectively as "CIGNA." Intercompany transactions and accounts have been eliminated in consolidation. These consolidated financial statements were prepared in conformity with accounting principles generally accepted in the United States of America.

The interim financial statements are unaudited but include all adjustments (including normal recurring adjustments) necessary, in the opinion of management, for a fair statement of financial position and results of operations for the period reported. The interim consolidated financial statements and notes should be read in conjunction with the Consolidated Financial Statements and Notes in CIGNA's Annual Report to Shareholders and Form 10-K for the year ended December 31, 2005.

The preparation of interim financial statements necessarily relies heavily on estimates. This and certain other factors, such as the seasonal nature of portions of the insurance business as well as competitive and other market conditions, call for caution in estimating full year results based on interim results of operations.

Certain reclassifications have been made to prior period amounts to conform to the 2006 presentation, including the elimination of certain intercompany purchases and sales of short-term investments in the investing activities section of the statement of cash flows. This reclassification had no net impact on the prior year net purchases and sales of short-term investments or the total cash flows from investing activities.

NOTE 2 - RECENT ACCOUNTING PRONOUNCEMENTS

Other-than-temporary impairment. Effective January 1, 2006, CIGNA implemented guidance provided by the staff of the Financial Accounting Standards Board (FASB) on evaluating fixed maturities and equity securities for other-than-temporary impairment. Because this guidance is largely a summary of existing accounting principles generally accepted in the United States of America, there was no material effect in accounting for fixed maturities and equity securities with other-than-temporary impairments at implementation on January 1, 2006. See Note 9 for a review of declines in fair value of fixed maturities and equity securities.

Deferred acquisition costs. In 2005, the American Institute of Certified Public Accountants issued a Statement of Position (SOP), "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection With Modifications or Exchanges of Insurance Contracts," for implementation in the first quarter of 2007. The SOP requires that deferred acquisition costs be expensed in full when the original contract is substantially changed by election or amendment of an existing contract feature or by replacement with a new contract. CIGNA expects to implement the SOP for contract changes beginning in the first quarter of 2007 with no material effects to the financial statements at implementation. Although substantial contract changes are not expected to occur, the effect of this SOP in future periods may vary based on the nature and volume of any such contract changes.

Certain financial instruments. In 2006, the FASB issued an amendment related to Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivatives and Hedging Activities," for implementation in the first quarter of 2007. The amendment clarifies when certain financial instruments and features of financial instruments must be treated as derivatives and reported on the balance sheet at fair value with changes in fair value reported in net income. CIGNA will implement the amendment beginning with financial instruments acquired in the first quarter of

2007, with no material effects to the financial statements expected at adoption. However, this amendment may affect future income recognition for certain financial instruments if additional derivatives are identified because any changes in their fair values will be recognized in net income each period.

Stock compensation. SFAS No. 123 (as revised in 2004 and referred to as SFAS 123R,) "Share-Based Payment" was effective January 1, 2006. This standard, which CIGNA early adopted effective October 1, 2004, requires companies to recognize in net income an estimate of expense for stock awards and options over their vesting periods typically determined as of the date of grant. CIGNA records compensation expense for stock options over their vesting periods based on the estimated fair value of the stock options, which is calculated using an option-pricing model. Compensation expense is recorded for restricted stock grants and deferred stock units over their vesting periods based on fair value, which is equal to the market price of CIGNA common stock on the date of grant. Compensation expense for stock options, restricted stock grants and deferred stock units are recorded in Corporate.

Compensation cost and related tax benefits for stock options, restricted stock and deferred stock units were as follows:

	Three Months Ended March 31,	
(In millions)	2006	2005
Compensation cost	$ 12	$ 6
Tax benefits	$ 4	$ 2

CIGNA calculated the average fair value using the Black-Scholes option pricing model. The following assumptions were used for the periods indicated:

	Three Months Ended March 31,	
(Options in thousands)	2006	2005
Dividend yield	0.1%	0.1%
Expected volatility	35.0%	35.0%
Risk-free interest rate	4.6%	3.9%
Expected option life	4.5 years	5.25 years
Options granted	524	781
Weighted average fair value of options granted	$43.97	$33.88

The expected volatility reflects CIGNA's past daily stock price volatility. Volatility implied in the market prices of traded options was not considered a good indicator of future volatility because remaining maturities of traded options are less than one year. CIGNA developed the expected option life by considering certain factors, including assumptions used by other companies with comparable stock option plan features and CIGNA's cancellation of a replacement option feature in June 2004.

Restricted stock granted and the average fair value at the date of grant were as follows:

	Three Months Ended March 31,	
(Grants in thousands)	2006	2005

Restricted stock granted	193	282
Weighted average fair value	$122.50	$ 91.36

NOTE 3 - ACQUISITIONS AND DISPOSITIONS

CIGNA may from time to time acquire or dispose of assets, subsidiaries or lines of business. Significant transactions are described below.

Sale of Retirement Benefits Business. On April 1, 2004, CIGNA sold its retirement benefits business, excluding the corporate life insurance business, for cash proceeds of $2.1 billion. The sale resulted in an after-tax gain of $804 million, of which $267 million after-tax was recognized immediately.

As this transaction was primarily in the form of a reinsurance arrangement under which CIGNA retains the contractual obligation to pay these liabilities, $537 million of the after-tax gain was deferred. Subsequent to the original reinsurance transaction, the buyer of the retirement benefits business has entered into agreements with most of the insured parties relieving CIGNA of any remaining contractual obligation to those parties (novation). Additional such agreements are expected.

The deferred gain is amortized at the rate at which earnings from the sold business would have been expected to emerge (primarily 15 years on a declining basis) until CIGNA is relieved of any remaining contractual obligation. At the time of novation, CIGNA accelerates amortization of a portion of the deferred gain and also reduces the associated contractholder deposit funds, future policy benefits, reinsurance recoverables and separate account balances. See Note 6 to the Financial Statements for additional information on reinsurance recoverables associated with the sale of the retirement benefits business.

CIGNA recognized deferred gain amortization in other revenues in the Run-off Retirement segment as follows:

(In millions)	Pre-Tax	After-Tax
Three Months Ended March 31,		
2006		
Accelerated deferred gain amortization	$ 4	$ 1
Normal deferred gain amortization	$ 2	$ 1
2005		
Accelerated deferred gain amortization	$ 260	$ 169
Normal deferred gain amortization	$ 14	$ 9

The remaining pre-tax deferred gain as of March 31, 2006 was $60 million.

In 2005, in connection with a modified coinsurance arrangement, CIGNA received units of the buyer's separate accounts and continues to carry those units as separate account assets on its balance sheet for the business not yet directly assumed by the buyer. At March 31, 2006, there were approximately $3.5 billion of separate account assets and liabilities associated with this business not yet directly assumed by the buyer.

At March 31, 2006, CIGNA had approximately $1.7 billion of invested assets, primarily fixed maturities and mortgage loans, supporting a modified coinsurance arrangement relating to the single premium annuity business sold to the buyer. These invested assets were held in a business trust established by CIGNA. CIGNA pays or receives cash quarterly to settle the results of the reinsured business, including the investment results of the assets underlying the modified coinsurance arrangement.

Effective April 1, 2006, the buyer converted this modified coinsurance arrangement to an indemnity reinsurance structure and took ownership of the trust assets. As a result, CIGNA will decrease invested assets and will increase reinsurance recoverables in the second quarter of 2006.

NOTE 4 - EARNINGS PER SHARE

Basic and diluted earnings per share were computed as follows:

(Dollars in millions, except per share amounts)	Basic	Effect of Dilution	Diluted
Three Months Ended March 31,			
2006			
Net Income	$ 352	—	$ 352
Shares *(in thousands)*:			
Weighted average			