Evercare of Arizona, Inc.

Financial Statements as of and for the
Years Ended December 31, 2013 and 2012,
Independent Auditors' Report

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INDEPENDENT AUDITORS' REPORT

To the Audit Committee of
Evercare of Arizona, Inc.
9701 Data Park Drive
Minnetonka, MN 55343

We have audited the accompanying financial statements of Evercare of Arizona, Inc. (the "Company"), which comprise the balance sheets as of December 31, 2013 and 2012, and the related statement of operations, comprehensive income, changes in stockholder's equity and accumulated other comprehensive income, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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 of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design 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. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2013 and 2012, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

April 29, 2014

EVERCARE OF ARIZONA, INC.

BALANCE SHEETS
AS OF DECEMBER 31, 2013 AND 2012
(In thousands, except share and per share data)

	2013	2012
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 12,450	$ 4,183
Short-term investments	2,594	1,806
Receivables — net	16,933	14,804
Current income taxes receivable	-	1,396
Investment receivables	362	371
Related-party receivable — net	-	146
Deferred income taxes — net	219	218
Other current assets	-	21
Total current assets	32,558	22,945
LONG-TERM INVESTMENTS	38,753	39,521
TOTAL	$ 71,311	$ 62,466
LIABILITIES AND STOCKHOLDER'S EQUITY		
CURRENT LIABILITIES:		
Medical services payable	$ 42,446	$ 37,615
Payable to AHCCCS	643	2,556
Related-party payable — net	1,524	-
Current income taxes payable	813	-
Other current liabilities	1,035	1,084
Total current liabilities	46,461	41,255
LONG-TERM DEFERRED INCOME TAXES — Net	41	741
Total liabilities	46,502	41,996
CONTINGENCIES (Note 7)		
STOCKHOLDER'S EQUITY:		
Common stock, no par value — 2,000,000 shares authorized; 2 shares issued and outstanding	-	-
Additional paid-in capital	10,999	10,999
Retained earnings	13,733	8,323
Accumulated other comprehensive income	77	1,148
Total stockholder's equity	24,809	20,470
TOTAL	$ 71,311	$ 62,466

See notes to financial statements.

EVERCARE OF ARIZONA, INC.

STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012
(In thousands)

	2013	2012
REVENUES:		
Capitation Revenue	$295,118	$283,125
Investment income — net	1,528	1,259
Total revenues	296,646	284,384
MEDICAL SERVICES EXPENSES:		
Institutional care	125,477	127,829
Home-based and community-based services	92,032	87,443
Acute care	41,238	40,266
Recoveries from AHCCCS	(3,684)	(11,666)
Total medical services expenses	255,063	243,872
MANAGEMENT FEES	26,261	30,313
OPERATING EXPENSES	6,653	6,478
INCOME BEFORE INCOME TAXES	8,669	3,721
PROVISION FOR INCOME TAXES	3,259	1,307
NET INCOME	$ 5,410	$ 2,414

See notes to financial statements.

EVERCARE OF ARIZONA, INC.

STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012
(In thousands)

	2013	2012
NET INCOME	$ 5,410	$ 2,414
OTHER COMPREHENSIVE (LOSS) INCOME:		
Gross unrealized holding (losses) gains on investment securities during the period	(1,473)	368
Income tax effect	701	(146)
Total unrealized (losses) gains — net of tax	(772)	222
Gross reclassification adjustment for net realized gains included in net earnings	(495)	(200)
Income tax effect	196	79
Total reclassification adjustment — net of tax	(299)	(121)
Other comprehensive (loss) income	(1,071)	101
COMPREHENSIVE INCOME	$ 4,339	$ 2,515

See notes to the financial statements.

EVERCARE OF ARIZONA, INC.

STATEMENTS OF CHANGES IN STOCKHOLDER'S EQUITY AND ACCUMULATED OTHER COMPREHENSIVE INCOME FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

(In thousands, except share data)

	Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
	Shares	Amount				
BALANCE — January 1, 2012	2	$ -	$ 10,999	$ 10,909	$ 1,047	$ 22,955
Comprehensive income:						
Net income	-	-	-	2,414	-	2,414
Change in net unrealized gains on investments available-for-sale — net of tax effects and reclassification adjustments	-	-	-	-	222	222
Reclassification adjustments for net realized gains included in net income — net of tax effects	-	-	-	-	(121)	(121)
Total comprehensive income						2,515
Dividend paid	-	-	-	(5,000)	-	(5,000)
BALANCE — December 31, 2012	2	-	10,999	8,323	1,148	20,470
Comprehensive income:						
Net income	-	-	-	5,410	-	5,410
Change in net unrealized losses on investments available-for-sale — net of tax effects and reclassification adjustments	-	-	-	-	(772)	(772)
Reclassification adjustments for net realized gains included in net income — net of tax effects	-	-	-	-	(299)	(299)
Total comprehensive income						4,339
Dividend paid	-	-	-	-	-	-
BALANCE — December 31, 2013	2	$ -	$ 10,999	$ 13,733	$ 77	$ 24,809

See notes to financial statements.

EVERCARE OF ARIZONA, INC.

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012
(In thousands)

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 5,410	$ 2,414
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of investment premium — net	442	257
Gain on short term investments	(2)	-
Gain on long-term investments	(493)	(200)
Deferred income taxes	(1)	1
Changes in operating assets and liabilities:		
Receivables	2,892	(8,153)
Investment receivables	9	-
Other current assets	21	-
Other current liabilities	(388)	(209)
Current income taxes	2,209	35
Medical services payable	(2,985)	3,659
Payable to AHCCCS	(1,913)	2,335
Related-party receivable/payable — net	1,670	(2,645)
Net cash provided by (used in) operating activities	6,871	(2,506)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments available-for-sale	(15,067)	(17,804)
Proceeds from maturities/sales of investments available-for-sale	13,329	7,506
Net cash used in investing activities	(1,738)	(10,298)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Dividends paid	-	(5,000)
AHCCCS funds administered	3,199	-
Checks outstanding	(65)	(28)
Net cash provided by (used in) financing activities	3,134	(5,028)
NET CHANGE IN CASH AND CASH EQUIVALENTS	8,267	(17,832)
CASH AND CASH EQUIVALENTS — Beginning of year	4,183	22,015
CASH AND CASH EQUIVALENTS — End of year	$ 12,450	$ 4,183
SUPPLEMENTAL CASH FLOW DISCLOSURE — Cash paid for income taxes	$ 1,052	$ 1,272

See notes to financial statements.

1. ORGANIZATIONAL STRUCTURE

Organization — Evercare of Arizona, Inc. (the "Company") was incorporated on September 15, 1988. The Company is a wholly owned subsidiary of Ovations, Inc. ("Ovations"), which is a wholly owned subsidiary of United HealthCare Services, Inc. ("UHS"), which is a wholly owned subsidiary of UnitedHealth Group Incorporated ("UHG"). UHS provides management services to managed care companies and is a wholly owned subsidiary of UHG. UHG is a publicly held company trading on the New York Stock Exchange. The headquarters of the Company is located in Phoenix, Arizona.

Operation — The Company is a prepaid health plan that derives all of its revenue through an Arizona Long Term Care System ("ALTCS") contract with the Arizona Health Care Cost Containment System ("AHCCCS") to provide specified long-term health care services to qualified members. A prepaid health plan is a plan that assumes the financial risk associated with providing medical services in return for a fixed prepaid fee. The Company contracts for fixed monthly premiums based on negotiated per-capita enrollee rates. The Company subcontracts with hospitals, physicians, and other medical providers within Arizona and surrounding states to care for AHCCCS members in various counties.

2. BASIS OF PRESENTATION, USE OF ESTIMATES, AND SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation — The Company has prepared the financial statements according to United States of America (U.S.) Generally Accepted Accounting Principles (GAAP).

Use of Estimates — These financial statements include certain amounts based on the Company's best estimates and judgments. The Company's most significant estimates relate to medical services expenses, estimates of receivables (including AHCCCS stop loss reinsurance recoverable), medical services payable, payable to AHCCCS, valuation of certain investments, and estimates and judgments related to income taxes. These estimates require the application of complex assumptions and judgments, often because they involve matters that are inherently uncertain, and will likely change in subsequent periods. The impact of any changes in estimates is included in earnings in the period in which the estimate is adjusted.

Cash, Cash Equivalents, and Investments — Cash and cash equivalents are highly liquid investments with original maturity of three months or less. The fair value of cash and cash equivalents approximates their carrying value because of the short maturity of the instruments.

Cash and cash equivalents primarily represent the Company's share of an investment pool sponsored and administered by UHS. The investment pool consists principally of investments with original maturities of less than one year, with the average life of the individual investments being less than 60 days. The Company's share of the pool represents an undivided ownership interest in the pool and is immediately convertible to cash at no cost or penalty. The participants within the pool have an individual fund number to track those investments owned by the Company. In addition, the Company is listed as a participant in the executed custodial agreement between UHS and the custodian whereby the Company's share in the investment pool is segregated and separately maintained. The pool is primarily

invested in government obligations, commercial paper, certificates of deposit, and short term agency notes and is recorded at cost or amortized cost. Interest income from the pool accrues daily to participating members based upon ownership percentage.

The Company had checks outstanding of $0 and $65 at December 31, 2013 and 2012, respectively, which were classified as other current liabilities in the balance sheets. The change in this balance has been reflected as checks outstanding within financing activities in the statements of cash flows. The outstanding checks are related to zero balance accounts. The Company does not net checks outstanding with deposits in other accounts.

Investments with maturities of less than one year are classified as short-term. All investments are classified as available-for-sale and reported at fair value based on quoted market prices, where available.

The Company excludes unrealized gains and losses on investments in available-for-sale securities from earnings, and reports them as other comprehensive income, net of income tax effects, as a separate component of stockholder's equity. To calculate realized gains and losses on the sale of investments, the Company specifically identifies the cost of each investment sold.

The Company evaluates an investment for impairment by considering the length of time and extent to which market value has been less than cost or amortized cost, the financial condition and near-term prospects of the issuer as well as specific events or circumstances that may influence the operations of the issuer, and the Company's intent to sell the security or the likelihood that it will be required to sell the security before recovery of the entire amortized cost.

- For debt securities, if the Company intends to either sell, or determines that it will be more likely than not required to sell a security before recovery of the entire amortized cost basis or maturity of the security, the Company recognizes the entire impairment in investment income. If the Company does not intend to sell the debt security, and it determines that it will not be more likely than not required to sell the security, but it does not expect to recover the entire amortized cost basis, the impairment is bifurcated into the amount attributed to the credit loss, which is recognized in earnings, and all other causes, which are recognized in other comprehensive income.

New information and the passage of time can change these judgments. The Company manages its investment portfolio to limit its exposure to any one issuer or market sector, and largely limits its investments to U.S. government and agency securities; state and municipal securities; mortgage-backed securities; and corporate debt obligations, substantially all of which are investment grade quality. Securities downgraded below policy minimums after purchase will be disposed of in accordance with the investment policy.

Long term investments include U.S. agency and non-U.S. agency mortgage backed securities, which are valued using the retrospective adjustment methodology. Prepayment assumptions for the determination of the amortized cost of mortgage backed securities are based on a three month constant prepayment rate history obtained from external data source vendors. The Company's investment policy limits investments in non-agency residential mortgage-backed securities, including home equity and sub-prime mortgages, to 10% of total cash and invested assets and total investments in mortgage backed securities to 30% of total cash and invested assets.

Investment income earned and due as of the reporting date, in addition to investment income earned but not paid or collected until subsequent periods, is reported as investment receivables in the balance sheets. The Company evaluates the collectability of the amounts due and amounts determined to be uncollectible are written off in the period in which the determination is made.

Investment income — net includes investment income collected during the period, as well as the change in investment income due and accrued on the Company's holdings. Amortization of premium or discount on bonds and certain external investment management costs are also included in investment income — net.

Minimum Net Worth — Under the laws of the state of Arizona, AHCCCS requires the Company to maintain a minimum net worth of $2 per member. As of December 31, 2013 and 2012, the Company had $3 and $2 of equity per member, respectively, meeting this requirement.

Revenues — The Company receives its revenues from AHCCCS on a monthly basis for the ALTCS population as prospective capitation, prior period coverage ("PPC") capitation, and acute only capitation. The Company recognized $295,118 and $283,125 in revenues for the periods ended December 31, 2013 and 2012, respectively.

Prospective capitation is paid for those members who are receiving long-term care services and reside in a nursing facility, a certified home and community based setting or in their own home. The prospective capitation rate is a blended rate that uses an institutional rate and a Home and Community Based Services ("HCBS") rate based on an assumed placement ratio of HCBS member months to total member months for each geographic service area. Additionally, the prospective capitation incorporates an assumed deduction for the Share of Cost ("SOC"), which members contribute to the cost of care based on their income and type of placement. The Company and its contracted providers collect members' SOC directly from members.

At the end of the contract year, AHCCCS compares the actual HCBS member months to the assumed HCBS percentage that was used to determine the full long-term care capitation rate for that year. If the Company's actual HCBS percentage is different than the assumed percentage, AHCCCS will recoup (or reimburse) the difference between the institutional capitation rate and the HCBS capitation rate for the number of member months, which exceeded (or was less than) the assumed percentage. The Company recorded $643 and $2,556 related to HCBS redetermination as payable to AHCCCS in the balance sheets at December 31, 2013 and 2012, respectively.

After the end of the contract year, AHCCCS compares actual SOC assignment to the SOC assignment assumed in the calculation of the prospective capitation rate. Assumed SOC will be fully reconciled to actual SOC assignment, and AHCCCS will either recoup or refund the total difference, as applicable. The Company recorded $4,570 and $1,787 related to member SOC redetermination as receivables in the balance sheets at December 31, 2013 and 2012, respectively.

PPC capitation premiums pertain to service dates prior to notification of enrollment. Due to the uncertainty regarding actual utilization and medical cost experience during the PPC period, AHCCCS limits the financial risk to the Company through risk share. Effective October 1, 2012, AHCCCS reconciles ALTCS PPC capitation and refunds to or recovers from the Company all costs or profits in excess a 5% risk corridor band. Prior to October 1, 2012, AHCCCS reconciled ALTCS PPC capitation and refunded or recouped all costs or profits in excess of a 10% risk corridor band. The Company recorded $387 and $0 for the estimated risk share receivable as of December 31, 2013 and 2012 respectively, which was recorded in receivables — net in the balance sheets. The company recouped $159 and $0 related to the risk share in 2013 and 2012, respectively, which was recorded in capitation revenue in the statements of comprehensive income.

Acute care only capitation is paid for those members who are residing in an uncertified facility, refusing long-term care services, awaiting disenrollment from the program, or have not received long-term care services for more than 30 days.

Medical Services Expenses and Medical Services Payables — Medical services expenses and medical services payable include estimates of the Company's obligations for medical care services that have been rendered on behalf of insured consumers, but for which claims have either not yet been received or processed, and for liabilities for physician, hospital and other medical cost disputes. The Company develops estimates for medical services expenses incurred but not reported using an actuarial process that is consistently applied, centrally controlled and automated. The actuarial models consider factors such as historical submission and payment data, cost trends, customer and product mix, seasonality, utilization of health care services, contracted service rates, and other relevant factors. The Company estimates liabilities for physician, hospital and other medical services payable disputes based upon an analysis of potential outcomes, assuming a combination of litigation and settlement strategies. Each period, the Company re-examines previously established medical services payable estimates based on actual claim submissions and other changes in facts and circumstances. As the medical services payable estimates recorded in prior periods develop, the Company adjusts the amount of the estimates and includes the changes in estimates in medical services expenses in the period in which the change is identified.

The Company contracts for nursing home services at negotiated per diem rates. Hospital services are generally contracted at per-diem rates or adjusted total charges, as defined by AHCCCS, less any applicable discounts. Home-based and community-based services, physicians' services, and other medical services are contracted on a capitated or fee-for-service basis.

AHCCCS Reinsurance — Reinsurance is a stop-loss program provided by AHCCCS for the partial reimbursement of covered medical services and those costs incurred beyond an annual deductible per member. AHCCCS provides regular reinsurance so long as the member incurred an inpatient stay, catastrophic reinsurance for those members receiving certain drugs or diagnosed with specific disorders, transplant reinsurance and other reinsurance. The Company recorded recoveries from AHCCCS related to the above reinsurance types, of $3,684 and $11,666 during 2013 and 2012, respectively, which are included as a reduction to medical services expenses in the accompanying statements of operations. Recoveries from AHCCCS of $4,410 and $11,513 have been included in receivables in the balance sheets as of December 31 2013 and 2012, respectively. Recoveries from AHCCCS are stated at actual and estimated amounts due to the Company pursuant to the AHCCCS contract. These recoveries are recognized as a percentage of eligible expenses in which medical costs exceed the stated deductible per member for the contract year.

Loss Adjustment Expenses — Loss adjustment expenses are those costs expected to be incurred in connection with the adjustment and recording of health claims. Management believes the amount of the liability for unpaid loss adjustment expenses as of December 31, 2013, is adequate to cover the Company's cost for the adjustment of unpaid claims; however, actual expenses may differ from those established estimates. It is the responsibility of UHS to pay loss adjustment expenses in the event the Company ceases operations. As of December 31, 2013 and 2012, the unpaid loss adjustment expenses included in the accompanying balance sheets in the other current liabilities are $363 and $941, respectively.

Administration of AHCCCS Funds — The Company has two contracts with AHCCCS which became effective during 2013 to administer funds from AHCCCS to specific provider populations and are accounted for as deposits as a component of receivables — net and medical services payable on the balance sheets, with no impact to net income. The funds transferred during 2013 are reported as AHCCCS funds administered under cash flows from financing on the statements of cash flows.

Primary Care Physician Enhancement Payments — Effective for calendar years 2013 and 2014 the Patient Protection and Affordable Care Act ("ACA") has mandated that certain practicing primary care physicians ("PCPs") are eligible to receive increased payments for specified primary care services provided to Medicaid eligible individuals. This is to encourage PCPs to serve the Medicaid population in advance of the Medicaid expansion in 2014.

The state has elected to administer the additional PCP funds through non-risk reconciled payments for enhanced rates model. Under this model, the state's capitation rate is not inclusive of the enhanced rate. The Company is reimbursed at agreed upon intervals for all of the enhanced payment amounts in the determined period. There is no risk to the Company because any excess or shortfall is 100% remitted to or reimbursed from the state. The Company recorded a receivable from AHCCCS in receivables — net of $1,192 and a payable to providers in medical services payable of $866 in the balance sheets as of December 31, 2013.

Nursing Facilities — Beginning in 2013, the Company is required to include quarterly enhancement payments to qualifying nursing facilities. AHCCCS retroactively adjusts its capitation rates paid to the Company on a quarterly basis to fund these enhancement payments. A reconciliation is performed at the end of the contract year to true up the enhancement payments. The Company included $3,830 for amounts to be received from AHCCCS in receivables — net and $6,951 for amounts due to qualifying nursing facilities in medical services payable in the accompanying balance sheets as of December 31, 2013.

Income Taxes — The Company's operations are included in the consolidated federal income tax return of UHG. Federal and state income taxes are paid to, or refunded by, UHG pursuant to the terms of a tax sharing agreement ("TSA"), under which taxes approximate the amount that would have been computed on a separate company basis. Under the terms of the TSA, the Company's share based compensation related tax benefits are reimbursed to UHG upon realization (see Note 20).

Premium Deficiency Reserve — The Company assesses the profitability of its contract for providing health care services to its members when current operating results or forecasts indicate possible future losses. The Company compares anticipated premiums to health care related costs, including estimated payments for physicians and hospitals, commissions, and costs of collecting premiums and processing claims. If the anticipated future costs exceed the premiums, a loss contract accrual is recognized. The Company has no amounts recorded for premium deficiency reserves as of December 31, 2013 and 2012.

Concentration of Business and Credit Risks — The Company's only source of revenue is its contract with AHCCCS, which provides the Company the right to offer services in Apache, Coconino, La Paz, Maricopa, Mohave, Navajo, Pima, Santa Cruz, Yavapai, and Yuma counties. The Company's contract with AHCCCS to serve members in all contracted counties is up for renewal in September 2016.

Concentration of credit risk with respect to receivables is limited due to the fact that AHCCCS, the Company's sole customer, is a governmental agency. As of December 31, 2013 and 2012, the Company had cash and cash equivalents on deposit with a major financial institution that were in excess of Federal Deposit Insurance Corporation insured limits.

Recently Adopted Accounting Standards

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Updated (ASU) No. 2013-02, "*Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*" (ASU 2013-02). ASU 2013-02 requires companies to report the effect of significant reclassifications out of accumulated other comprehensive income, by

component, either on the face of the financial statements or in the notes to the financial statements and is intended to help entities improve the transparency of changes in other comprehensive income. ASU 2013-02 does not amend any existing requirements for reporting net income or other comprehensive income in the financial statements. ASU 2013-02 became effective for the Company's fiscal year 2013 and the new disclosures have been included with the Company's investment disclosures in Note 8 of Notes to the Consolidated Financial Statements.

ASU No. 2011-06, "*Other Expenses (Topic 720): Fees Paid to the Federal Government by Health Insurers (a consensus of the FASB Emerging Issues Task Force)*" (ASU 2011-06) addresses the recognition and classification of an entity's share of the annual health insurance industry assessment (the industry fee) mandated by Health Reform Legislation. The industry fee is levied on health insurers for each calendar year beginning on or after January 1, 2014, and is not deductible for income tax purposes. The amount of the industry fee for each health insurer is based on a ratio of the insurer's net health insurance premiums written for the previous calendar year compared to the U.S. health insurance industry total net premiums. Because long term care insurance is excluded from the industry fee calculation, the Company's ALTCS contract is exempt and the Company will not have a liability at January 1, 2014.

The Company has determined that there have been no other recently adopted or issued accounting standards that had or will have a material impact on its financial statements.

3. OTHER AMOUNTS

There are no material amounts included in other as a component of current assets or current liabilities not addressed in Note 2 included in the balance sheets or included as other in the statements of operations for the years ended December 31, 2013 or 2012.

4. PLEDGES/ASSIGNMENTS AND GUARANTEES

The Company has no pledges, assignments, collateralized assets, or guaranteed liabilities not disclosed on the balance sheet as of December 31, 2013 and 2012.

5. PERFORMANCE BOND

Pursuant to the contracts with the AHCCCS, the Company is required to provide either a performance bond or a designated substitute security to guarantee performance of the Company's obligations under the contracts. To satisfy this requirement, the Company maintained a surety bond in 2013 and 2012 in the amount of $20,000 and $18,000, respectively. The bond is unsecured and requires no Company assets to secure this obligation.

6. MEDICAL SERVICES PAYABLE ANALYSIS

Changes in estimates related to the prior year incurred claims are included in medical services expenses in the current year in the statements of operations. The following tables disclose paid claims, incurred claims, and the balance in medical services payable and claim overpayments less allowances and stop-loss recoveries within receivables, and pharmacy rebates receivables within related party-net on the balance sheets for 2013 and 2012 (in thousands):

	2013		
	Current Year Incurred Claims	Prior Years Incurred Claims	Total
Beginning of year medical services payable	$ -	$ (37,615)	$ (37,615)
Paid claims, net of stop loss recoveries, pharmacy rebates and claim overpayments collected	216,608	27,523	244,131
End of year medical services payable	42,270	176	42,446
Incurred claims excluding the change in stop loss recoveries, pharmacy rebates and claim overpayment receivables as presented below	258,878	(9,916)	248,962
Beginning of year stop loss recoveries, pharmacy rebates and claim overpayment receivables	-	13,190	13,190
End of year stop loss recoveries, pharmacy rebates and claim overpayment receivables	(6,249)	(840)	(7,089)
Total medical services expenses	$252,629	$ 2,434	$255,063

	2012		
	Current Year Incurred Claims	Prior Years Incurred Claims	Total
Beginning of year medical services payable	$ -	$ (33,956)	$ (33,956)
Paid claims, net of stop loss recoveries and claim overpayments collected	219,488	28,385	247,873
End of year medical services payable	37,209	406	37,615
Incurred claims excluding stop loss recoveries and claim overpayment receivables as presented below	256,697	(5,165)	251,532
Beginning of year stop loss recoveries and claim overpayment receivables	-	5,357	5,357
End of year stop loss recoveries and claim overpayment receivables	(11,324)	(1,693)	(13,017)
Total medical services expenses	$245,373	$ (1,501)	$243,872

In 2013 the table above includes pharmacy rebates as they are a component of total medical services expenses and the change in receivables are a direct adjustment to incurred expenses. The beginning balance of stop loss recoveries, pharmacy rebates, and claim overpayment receivables has been modified in the 2013 table to include the pharmacy rebate estimates as of December 31, 2012.

The liability for medical services payable net of stop loss recoveries, claims overpayment receivables and pharmacy rebates as of December 31, 2012 were $24,425. As of December 31, 2013, $27,523 has been paid for incurred claims attributable to insured events of prior years. Reserves remaining for prior years, net of stop loss recoveries, pharmacy rebates receivable and claim overpayment receivables of ($840), are now ($664) as a result of re-estimation of unpaid claims. Therefore, there has been $2,434 unfavorable prior year development since December 31, 2012 to December 31, 2013. The primary drivers consist of unfavorable development of $5,297 in stop loss, offset by favorable development as a result of a change in the provision for adverse deviations in experience of $2,558. At December 31, 2012, the Company recorded $1,501 of favorable development as a result of a change in the provision for adverse deviations in experience of $3,048, favorable development of $2,475 in stop loss, and offset by unfavorable development of $4,127 in retroactivity for inpatient, outpatient, physician and pharmacy claims.

7. CONTINGENT LIABILITIES AND GOVERNMENT REGULATIONS

Because of the nature of its businesses, the Company is frequently made party to a variety of legal actions and regulatory inquiries, including class actions and suits brought by members, care providers, consumer advocacy organizations, customers and regulators, relating to the Company's businesses, including management and administration of health benefit plans and other services.

The Company records liabilities for its estimates of probable costs resulting from these matters where appropriate. Estimates of costs resulting from legal and regulatory matters involving the Company are inherently difficult to predict, particularly where the matters: involve indeterminate claims for monetary damages or may involve fines, penalties or punitive damages; present novel legal theories or represent a shift in regulatory policy; involve a large number of claimants or regulatory bodies; are in the early stages of the proceedings; or could result in a change in business practices. Accordingly, the Company is often unable to estimate the losses or ranges of losses for those matters where there is a reasonable possibility or it is probable that a loss may be incurred. Although the outcomes of any such legal actions cannot be predicted, in the opinion of management, the resolution of any currently pending or threatened actions will not have a material adverse effect on the accompanying balance sheets or statements of operations of the Company.

The Company's business is regulated at the federal, state, and local levels. The laws and rules governing the Company's business and interpretations of those laws and rules are subject to frequent change. Broad latitude is given to the agencies administering those regulations. Further, the Company must obtain and maintain regulatory approvals to market and sell many of its products.

Health Reform Legislation and the related federal and state regulations will continue to impact how the Company does business and could restrict revenue and enrollment growth in certain products and market segments, restrict premium growth rates for certain products and market segments, increase the Company's medical and administrative costs, expose the Company to an increased risk of liability (including increasing our liability in federal and state courts for coverage determinations and contract interpretation), or put the Company at risk for loss of business. In addition, the Company's results of operations, financial condition and cash flows could be materially adversely affected by such changes. The Health Reform Legislation may create new or expand existing opportunities for business growth, but due to its complexity, the impact of the Health Reform Legislation remains difficult to predict and is not yet fully known.

8. INVESTMENTS

A summary of short-term and long-term investments by major security type is as follows:

December 31, 2013	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Debt securities — available-for-sale:				
U.S. government and agency obligations	$ 2,856	$ -	$ (81)	$ 2,775
State and municipal obligations	23,288	511	(166)	23,633
Corporate obligations	8,133	99	(68)	8,164
U.S. agency mortgage-backed securities	4,933	20	(203)	4,750
Non-U.S. agency mortgage-backed securities	2,010	40	(25)	2,025
Total debt securities — available-for-sale	41,220	670	(543)	41,347
Total investments	$41,220	$ 670	$(543)	$41,347
December 31, 2012				
Debt securities — available-for-sale:				
U.S. government and agency obligations	$ 4,736	$ 355	$-	$ 5,091
State and municipal obligations	21,718	1,079	(12)	22,785
Corporate obligations	8,660	274	-	8,934
U.S. agency mortgage-backed securities	2,026	56	-	2,082
Non-U.S. agency mortgage-backed securities	2,288	148	(1)	2,435
Total debt securities — available-for-sale	39,428	1,912	(13)	41,327
Total investments	$39,428	$1,912	$ (13)	$41,327

The fair value of the Company's mortgage-backed securities by credit rating (when multiple credit ratings are available for an individual security, the average of the available ratings is used) and origination as of December 31, 2013, were as follows:

	AAA	Non-Investment Grade	Total Fair Value
2005	$ 781	$ -	$ 781
2006	433	-	433
2012	811	-	811
U.S. agency mortgage-backed securities	4,750	-	4,750
Total	$6,775	$ -	$6,775

The amortized cost and fair value of available-for-sale debt securities as of December 31, 2013 and 2012, by contractual maturity, were as follows:

	2013	
	Amortized Cost	Fair Value
Due in one year or less	$ 2,570	$ 2,594
Due after one year through five years	12,921	13,156
Due after five years through ten years	13,753	13,824
Due after ten years	5,033	4,998
U.S. agency mortgage-backed securities	4,933	4,750
Non-U.S. agency mortgage-backed securities	2,010	2,025
Total debt securities — available-for-sale	$41,220	$41,347

	2012	
	Amortized Cost	Fair Value
Due in one year or less	$ 1,781	$ 1,806
Due after one year through five years	17,504	18,191
Due after five years through ten years	11,734	12,606
Due after ten years	4,095	4,207
U.S. agency mortgage-backed securities	2,026	2,082
Non-U.S. agency mortgage-backed securities	2,288	2,435
Total debt securities — available-for-sale	$39,428	$41,327

The fair value of available-for-sale investments with gross unrealized losses by major security type and length of time that individual securities have been in a continuous unrealized loss position, were as follows:

	Less Than 12 Months		12 Months or Greater		Total	
December 31, 2013	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Debt securities — available-for-sale:						
U.S government and agency obligations	$ 2,774	$ (81)	$ -	$ -	$ 2,774	$ (81)
State and municipal obligations	6,547	(166)	-	-	6,547	(166)
Corporate obligations	2,833	(68)	-	-	2,833	(68)
U.S. agency mortgage-backed securities	3,794	(203)	-	-	3,794	(203)
U.S. non-agency mortgage-backed securities	599	(13)	376	(12)	975	(25)
Total debt securities — available-for-sale	$16,547	$(531)	$376	$(12)	$16,923	$(543)
December 31, 2012						
Debt securities — available-for-sale:						
State and municipal obligations	$ 4,127	$ (12)	$ -	$ -	$ 4,127	$ (12)
U.S. non-agency mortgage-backed securities	388	(1)	-	-	388	(1)
Total debt securities — available-for-sale	$ 4,515	$ (13)	$ -	$ -	$ 4,515	$ (13)

The unrealized losses from all securities as of December 31, 2013, were generated from 94 positions out of a total of 239 positions. The Company believes that it will collect all principal and interest due on its investments that have an amortized cost in excess of fair value. The unrealized losses on investments were primarily caused by interest rate increases and not by unfavorable changes in the credit ratings associated with these securities. The Company evaluates impairment at each reporting period for each of the securities whereby the fair value of the investment is less than its amortized cost. The contractual cash flows of the U.S. government and agency obligations are either guaranteed by the U.S. government or an agency of the U.S. government. It is expected that the securities would not be settled at a price less than the cost of the investment, and the Company does not intend to sell the investment until the unrealized loss is fully recovered. The Company evaluated the underlying credit quality and credit ratings of the issuers, noting whether a significant deterioration since purchase or other factors that may indicate an other-than temporary impairment ("OTTI"), such as the length of time and extent to which fair value has been less than cost, the financial condition, and near term prospects of the issuer as well as specific events or circumstances that may influence the operations of the issuer and the Company's intent to sell the investment. As of December 31, 2013, the Company did not have the intent to sell any of the securities in an unrealized loss position.

Net realized gains reclassified out of accumulated other comprehensive income were from the following sources:

	Years Ended December 31,	
	2013	2012
Total OTTI	$ -	$ (1)
Net OTTI recognized in earnings	-	(1)
Gross realized losses from sales	(3)	-
Gross realized gains from sales	498	201
Net realized gains (included in investment income — net on the statements of operations)	495	200
Income tax effect (included in provision for income taxes on the statement of operations)	(196)	(79)
Realized gains — net of taxes	$ 299	$ 121

9. FAIR VALUE

Certain assets and liabilities are measured at fair value in the consolidated financial statements, or have fair values disclosed in the Notes to the Financial Statements. These assets and liabilities are classified into one of three levels of a hierarchy defined by GAAP. In instances in which the inputs used to measure fair value fall into different levels of the fair value hierarchy, the fair value measurement is categorized in its entirety based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular item to the fair value measurement in its entirety requires judgment, including the consideration of inputs specific to the asset or liability.

The fair value hierarchy is summarized as follows:

Level 1 — Quoted prices (unadjusted) for identical assets/liabilities in active markets.

Level 2 — Other observable inputs, either directly or indirectly, including:

Quoted prices for similar assets/liabilities in active markets;

Quoted prices for identical or similar assets/liabilities in non active markets (e.g., few transactions, limited information, non current prices, high variability over time, etc.);

Inputs other than quoted prices that are observable for the asset/liability (e.g., interest rates, yield curves, implied volatilities, credit spreads); and

Inputs that are corroborated by other observable market data.

Level 3 — Unobservable inputs that cannot be corroborated by observable market data.

Non-financial assets and liabilities, or financial assets and liabilities that are measured at fair value on a nonrecurring basis, are subject to fair value adjustments only in certain circumstances, such as when the Company records an impairment. There were no significant fair value adjustments for these assets and liabilities recorded during the years ended December 31, 2013 and 2012.

The following table presents a summary of fair value measurements by level, and carrying values for items measured at fair value on a recurring basis in the balance sheets:

December 31, 2013	Quoted Prices in Active Markets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Total Fair and Carrying Value
Cash and cash equivalents	$ 12,450	$ -	$ -	$ 12,450
Debt securities — available-for-sale:				
U.S. government and agency obligations	2,775	-	-	2,775
State and municipal obligations	-	23,633	-	23,633
Corporate obligations	-	8,164	-	8,164
U.S. agency mortgage-backed securities	-	4,750	-	4,750
Non-U.S. agency mortgage-backed securities	-	2,025	-	2,025
Total debt securities — available-for-sale	2,775	38,572	-	41,347
Total cash, cash equivalents, and investments at fair value	$ 15,225	$ 38,572	$ -	$ 53,797
December 31, 2012				
Cash and cash equivalents	$ 4,183	$ -	$ -	$ 4,183
Debt securities — available-for-sale:				
U.S. government and agency obligations	5,091	-	-	5,091
State and municipal obligations	-	22,785	-	22,785
Corporate obligations	-	8,934	-	8,934
U.S. agency mortgage-backed securities	-	2,082	-	2,082
Non-U.S. agency mortgage-backed securities	-	2,435	-	2,435
Total debt securities — available-for-sale	5,091	36,236	-	41,327
Total cash, cash equivalents, and investments at fair value	$ 9,274	$ 36,236	$ -	$ 45,510

Transfers between levels, if any, are recorded as of the beginning of the reporting period in which the transfer occurs. There were no transfers between Levels 1, 2 or 3 of any financial assets or liabilities during 2013 or 2012.

The Company does not have financial assets with a fair value hierarchy of Level 3.

The following methods and assumptions were used to estimate the fair value and determine the fair value hierarchy classification of each class of financial instrument:

Cash and Cash Equivalents — The carrying value of cash and cash equivalents approximates fair value, as maturities are less than three months. Fair values of cash equivalent instruments that do not trade on a regular basis in active markets are classified as Level 2.

Debt Securities — Fair values of debt and equity securities are based on quoted market prices, where available. The Company obtains one price for each security, primarily from a third-party pricing service (pricing service), which generally uses quoted or other observable inputs for the determination of fair value. The pricing service normally derives the security prices through recently reported trades for identical or similar securities and, if necessary, makes adjustments through the reporting date based upon available observable market information. For securities not actively traded, the pricing service may use quoted market prices of comparable instruments or discounted cash flow analyses, incorporating inputs that are currently observable in the markets for similar securities. Inputs that are often used in the valuation methodologies include, but are not limited to, benchmark yields, credit spreads, default rates, prepayment speeds and non-binding broker quotes.

As the Company is responsible for the determination of fair value, it performs quarterly analyses on the prices received from the pricing service to determine whether the prices are reasonable estimates of fair value. Specifically, the Company compares the prices received from the pricing service to prices reported by a secondary pricing source such as its custodian, its investment consultant, and third-party investment advisors. Additionally, the Company compares changes in the reported market values and returns to relevant market indices to test the reasonableness of the reported prices. The Company's internal price verification procedures, and review of fair value methodology documentation provided by independent pricing services, have not historically resulted in adjustment to the prices obtained from the pricing service.

Fair values of debt securities that do not trade on a regular basis in active markets, but are priced using other observable inputs, are classified as Level 2.

The carrying amounts reported in the balance sheets for cash and cash equivalents, receivables, and other assets and liabilities approximate fair value because of their short-term nature.

10. RELATED-PARTY TRANSACTIONS

Effective July 1, 2012, the Company entered into a revised Management Agreement ("Agreement") with UHS. This Agreement has been approved by AHCCCS. UHS will continue to provide management services to the Company under a revised fee structure which changed from a percentage of capitation revenue basis to a direct charge based on UHS's expenses for services or use of assets provided to the Company. Management fees under this arrangement totaled $26,261 and $30,313 in 2013 and 2012, respectively. Direct expenses not included in the management agreement, such as premium taxes are paid by UHS on behalf of the Company. UHS is reimbursed by the Company for these direct expenses.

The Company expensed as medical services expenses and operating expenses $319 and $131 in capitation fees to related parties during 2013 and 2012, respectively. UHS' subsidiaries and divisions provide various services to enrollees of the Company during the year. OptumHealth, a division of UHS, provides services including, but not limited to, integrated personal health management solutions, such as disease management, treatment decision support, health care delivery systems access and wellness services, including a 24-hour call-in service, as well as, access to a network of transplant providers. The Company entered into a new agreement, effective January 1, 2012 with OptumHealth Care Solutions, Inc. providing chiropractic, physical therapy and complex medical conditions services. Dental Benefit Providers, Inc. provides dental care assistance.

The capitation expenses, administrative services, and access fees paid to related parties, that are included as medical services expenses and operating expenses in the accompanying statements of operations for the years ended December 31, 2013 and 2012, are shown below:

	2013	2012
UHS	$ 226	$ 6
Dental Benefit Providers, Inc.	83	115
OptumHealth Care Solutions, Inc.	10	10
Total	$ 319	$ 131

The Company has entered into a tax-sharing agreement with UHG (see Note 20).

The Company has an agreement with OptumRx to provide administrative services related to pharmacy management and pharmacy claims processing for its enrollees. Fees related to these agreements, which are calculated on a per-claim basis, of $208 and $196 in 2013 and 2012, respectively, are included in operating expenses in the accompanying statements of operations. Additionally, OptumRx collects rebates on certain pharmaceutical products based on member utilization. Rebate receivables of $134 and $174 as of December 31, 2013 and 2012, respectively, are included as related-party receivable — net or an offset to related-party payable — net on the balance sheets.

The Company holds a $10,000 subordinated revolving credit agreement with UHG, at an interest rate of London InterBank Offered Rate, plus a margin of 0.50%. The credit agreement is for a one-year term and automatically renews annually, unless terminated by either party. The credit agreement was renewed effective June 1, 2012. No amounts were outstanding under the line of credit as of December 31, 2013 and 2012.

The remaining related-party payable — net, as reflected in the accompanying balance sheets, represents costs incurred in the ordinary course of business by, or on behalf of, the Company.

11. STOCKHOLDER'S EQUITY

As a result of the change in net unrealized gains and losses on investments available-for-sale, the Company had other comprehensive income of $1,071 and $101 for the years ended December 31, 2013 and 2012, respectively.

The Company paid a dividend of $5,000 on December 28, 2012, to Ovations, which was approved by AHCCCS and recorded as a reduction to retained earnings.

12. COMPLIANCE WITH FINANCIAL VIABILITY STANDARDS AND PERFORMANCE GUIDELINES

As of December 31, 2013 and 2012, the Company was in compliance with the Financial Viability Standards and Performance Guidelines.

13. PRIOR PERIOD ADJUSTMENTS

As of and for the years ended December 31, 2013 and 2012, there were no adjustments made to previously submitted or current financial statements.

14. DRUG REBATES/DISCOUNTS

The Company recorded $167 and $331 in pharmacy rebates in 2013 and 2012, respectively. The pharmacy rebates are recorded as a reduction to medical services expenses in the statements of operations (see Note 10).

15. INTEREST ON LATE CLAIMS

The Company paid $280 and $150 in interest on late claims for all members in 2013 and 2012, respectively. The interest on late claims is included in operating expenses in statements of operations.

16. ACCRUED SANCTIONS

As of December 31, 2013 the Company accrued sanctions of $50 for not meeting AHCCCS standards for the timely resolution of pended encounters. The Company did not have accrued sanctions as of December 31, 2012.

17. PROVIDER INCENTIVES AND SHARED SAVINGS ARRANGEMENTS

The Company does not currently offer any provider incentives and shared savings arrangements.

18. NON-COVERED SERVICES

The Company does not have any non-covered services.

19. RECEIVABLES

Receivables from third parties at December 31, 2013 and 2012, consist of the following:

	2013	2012
AHCCCS receivables:		
Capitated premiums and reconciliations	$ 4,957	$ 1,787
Stop loss recoveries receivable	4,409	11,513
Enhanced nursing facility payments	3,830	-
PCP enhanced rate payments	1,192	-
Total AHCCCS receivables	14,388	13,300
Claim overpayment receivable — net	2,545	1,504
Total	$ 16,933	$ 14,804

20. INCOME TAXES

The Company's operations are included in the consolidated federal income tax return of UHG. Federal income taxes are paid to or refunded by UHG pursuant to the terms of a TSA, approved by the Board of Directors, under which taxes approximate the amount that would have been computed on a separate company basis. The Company receives a benefit at the federal rate in the current year for net losses incurred in that year to the extent losses can be utilized in the consolidated federal income tax return of UHG.

The components of the provision for income taxes for the years ended December 31, 2013 and 2012, are as follows:

	2013	2012
Current provision:		
Federal	$2,665	$1,057
State	595	250
Total current provision	3,260	1,307
Deferred benefit:		
Federal	(1)	-
State	-	-
Total deferred benefit	(1)	-
Total provision for income taxes	$3,259	$1,307

The reconciliation of the tax provision at the U.S. Federal Statutory Rate to the provision for income taxes for the years ended December 31, 2013 and 2012, is as follows:

	2013	2012
Tax provision at the U.S. federal statutory rate	$3,034	$1,302
State income taxes — net of federal benefit	387	163
Tax-exempt investment income	(162)	(158)
Total provision for income taxes	$3,259	$1,307

The Company had federal income taxes payable of $607 included in current income taxes payable and federal income taxes recoverable of $1,396 included in current income taxes receivable in the balance sheets as of December 31, 2013 and 2012, respectively.

Deferred income tax assets and liabilities are recognized for the differences between the financial and income tax reporting bases of assets and liabilities, based on enacted tax rates and laws. The deferred income tax provision or benefit generally reflects the net change in deferred income tax assets and liabilities during the year. The current income tax provision reflects the tax consequence of revenues and expenses currently taxable or deductible on various income tax returns for the year reported.

As of December 31, 2013 and 2012, the components of deferred income tax assets and liabilities are as follows:

	2013	2012
Deferred income tax assets:		
Bad debt reserve	$ 55	$ 27
Medical services payable and loss adjustment expense	179	216
Total deferred tax assets	234	243
Deferred income tax liabilities:		
Investments	(6)	(16)
Unrealized gain on investments	(50)	(750)
Total deferred tax liabilities	(56)	(766)
Net deferred income tax assets (liabilities)	$ 178	$ (523)

Valuation allowances are provided when it is considered more likely than not that deferred tax assets will not be realized. There were no valuation allowances as of December 31, 2013 or 2012.

UHG currently files income tax returns in the United States federal jurisdiction, various states, and foreign jurisdictions. The U.S. Internal Revenue Service ("IRS") has completed exams on UHG's consolidated income tax returns for fiscal years 2012 and prior. UHG's 2013 tax return is under advance review by the IRS under its Compliance Assurance Program. With the exception of a few states, UHG is no longer subject to income tax examinations prior to 2008 in major state and foreign jurisdictions. The Company does not believe any adjustments that may result from these examinations will be material to the Company.

The Company has not included a reconciliation of the beginning and ending amount of unrecognized tax benefits, as it does not have any uncertain tax positions as of December 31, 2013 and 2012.

Federal and state income taxes paid, net of refunds, in 2013 and 2012 was $1,052 and $1,272, respectively.

21. RETIREMENT PLANS, DEFERRED COMPENSATION, POSTEMPLOYMENT BENEFITS AND COMPENSATED ABSENCES, AND OTHER POSTRETIREMENT BENEFIT PLANS

The Company has no retirement plan, deferred compensation, and other benefit plans, since all personnel are employees of UHS, which provides services to the Company under the terms of a management agreement (see Note 10).

22. SUBSEQUENT EVENTS

The Company has evaluated subsequent events through April 29, 2014, which is the date these financial statements were issued.

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