# LOUISIANA HEALTHCARE CONNECTIONS, INC.

(A Wholly Owned Subsidiary of Centene Corporation)

Statutory Financial Statements and
Supplemental Information

December 31, 2012

(With Independent Auditors' Report Thereon)

**LOUISIANA HEALTHCARE CONNECTIONS, INC.**
(A Wholly Owned Subsidiary of Centene Corporation)

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**KPMG LLP**
Suite 900
10 South Broadway
St. Louis, MO 63102-1761

# Independent Auditors' Report

The Audit Committee of the Board of Directors
Louisiana Healthcare Connections, Inc.:

We have audited the accompanying financial statements of Louisiana Healthcare Connections, Inc. (the Company), which comprise the statutory statement of admitted assets, liabilities, and capital and surplus as of December 31, 2012, and the related statutory statement of revenue and expenses, changes in capital and surplus, and cash flow for the period from February 1, 2012 (initial date of operations) through December 31, 2012, and the related notes to the statutory 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 statutory accounting practices prescribed or permitted by the Louisiana Department of Insurance. Management is also responsible for 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 audit. We conducted our audit 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 statutory financial statements. The procedures selected depend on the auditors' 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 entity's preparation and fair presentation of the statutory 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 entity'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 opinions.

### *Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles*

As described in note 2 to the financial statements, the financial statements are prepared by the Company using statutory accounting practices prescribed or permitted by the Louisiana Department of Insurance, which is a basis of accounting other than U.S. generally accepted accounting principles. Accordingly, the financial statements are not intended to be presented in accordance with U.S. generally accepted accounting principles.

The effects on the financial statements of the variances between the statutory accounting practices described in note 2 and U.S. generally accepted accounting principles, although not reasonably determinable, are presumed to be material.

***Adverse Opinion on U.S. Generally Accepted Accounting Principles***

In our opinion, because of the significance of the variances between accounting principles and U.S. generally accepted accounting principles discussed in the Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles paragraph, the financial statements referred to above do not present fairly, in accordance with U.S. generally accepted accounting principles, the financial position of Louisiana Healthcare Connections, Inc. as of December 31, 2012, or the results of its operations or its cash flow for the period February 1, 2012 (initial date of operations) through December 31, 2012.

***Opinion on Statutory Basis of Accounting***

In our opinion, the financial statement referred to above present fairly, in all material respects, the admitted assets, liabilities, and capital and surplus of Louisiana Healthcare Connections, Inc. as of December 31, 2012, and the results of its operations and its cash flow for the period from February 1, 2012 (initial date of operations) through December 31, 2012, in accordance with statutory accounting practices prescribed or permitted by the Louisiana Department of Insurance described in note 2.

***Other Matter***

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary information included in the accompanying Supplemental Summary Investment Schedule – December 31, 2012 and Investment Risk Interrogatories – December 31, 2012, is presented for purposes of additional analysis and is not a required part of the financial statements but is supplementary information required by the National Association of Insurance Commissioners' *Accounting Practices and Procedures Manual*. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

KPMG LLP

St. Louis, Missouri
May 23, 2013

**LOUISIANA HEALTHCARE CONNECTIONS, INC.**
(A Wholly Owned Subsidiary of Centene Corporation)

Statutory Statement of Admitted Assets, Liabilities and Capital and Surplus

December 31, 2012

**Admitted Assets**

| | | |
|---|---|---|
| Bonds | $ | 15,259,841 |
| Cash and short-term investments | | 37,026,932 |
| Investment income due and accrued | | 27,764 |
| Premiums receivable | | 6,493,360 |
| Reinsurance receivable | | 451,613 |
| Federal income tax recoverable | | 5,887,646 |
| Amounts due from affiliates | | 24,000,101 |
| Healthcare receivables | | 56,710 |
| State income tax recoverable | | 125,541 |
| Total admitted assets | $ | 89,329,508 |

**Liabilities and Capital and Surplus**

| | | |
|---|---|---|
| Liabilities: | | |
| Claims payable | $ | 46,541,996 |
| Accrued medical incentive pool and bonus amounts | | 18,160 |
| Unpaid claims adjustment expenses | | 893,000 |
| General expenses due or accrued | | 119,825 |
| Premium taxes accrued | | 6,203,781 |
| Amounts due to affiliates | | 376,289 |
| Total liabilities | | 54,153,051 |
| Capital and surplus: | | |
| Common stock, no par value. Authorized 5,000 shares, issued and outstanding 1,000 shares | | — |
| Gross paid-in and contributed capital | | 51,900,000 |
| Unassigned deficit | | (16,723,543) |
| Total capital and surplus | | 35,176,457 |
| Total liabilities and capital and surplus | $ | 89,329,508 |

See accompanying notes to statutory financial statements.

**LOUISIANA HEALTHCARE CONNECTIONS, INC.**
(A Wholly Owned Subsidiary of Centene Corporation)

Statutory Statement of Revenue and Expenses

Period from February 1, 2012 (initial date of operations) to December 31, 2012

| | | |
|---|---|---|
| Revenue: | | |
| Premium income | $ | 271,118,625 |
| Expenses: | | |
| Medical and hospital benefits | | 191,943,889 |
| Other professional services | | 12,965,711 |
| Emergency room | | 30,887,011 |
| Prescription drugs | | 20,407,247 |
| Incentive pool and bonus amounts | | 18,160 |
| Reinsurance recoveries | | (2,429,532) |
| Total medical and hospital expenses | | 253,792,486 |
| Claims adjustment expenses | | 9,163,082 |
| General administrative expenses | | 30,566,560 |
| Total expenses | | 293,522,128 |
| Investment income: | | |
| Net investment income, including net realized loss of ($1,048) | | 107,222 |
| Loss before federal income taxes | | (22,296,281) |
| Federal income tax benefit | | (5,887,685) |
| Net loss | $ | (16,408,596) |

See accompanying notes to statutory financial statements.

**LOUISIANA HEALTHCARE CONNECTIONS, INC.**
(A Wholly Owned Subsidiary of Centene Corporation)

Statutory Statement of Changes in Capital and Surplus

Period from February 1, 2012 (initial date of operations) to December 31, 2012

| | Common stock | Gross paid-in and contributed surplus | Unassigned surplus (deficit) | Total |
|---|---|---|---|---|
| Balance, December 31, 2011 | $ — | 3,000,000 | 8,526 | 3,008,526 |
| Paid-in surplus | — | 48,900,000 | — | 48,900,000 |
| Net loss | — | — | (16,408,596) | (16,408,596) |
| Change in net deferred income tax | — | — | 2,029,152 | 2,029,152 |
| Change in nonadmitted assets | — | — | (2,352,625) | (2,352,625) |
| Balance, December 31, 2012 | $ — | 51,900,000 | (16,723,543) | 35,176,457 |

See accompanying notes to statutory financial statements.

**LOUISIANA HEALTHCARE CONNECTIONS, INC.**
(A Wholly Owned Subsidiary of Centene Corporation)

Statutory Statement of Cash Flow

Period from February 1, 2012 (initial date of operations) to December 31, 2012

| | | |
|---|---|---|
| Cash from operations: | | |
| Premiums collected net of reinsurance | $ | 264,625,266 |
| Net investment income | | 101,580 |
| Benefits and loss related payments | | (208,056,625) |
| General administrative and claims adjustment expenses paid | | (32,313,281) |
| Federal income taxes recovered | | 564 |
| Net cash from operations | | 24,357,504 |
| Cash from investments: | | |
| Proceeds from investments sold, matured, or repaid | | 725,000 |
| Cost of investments acquired | | (14,013,789) |
| Net cash from investments | | (13,288,789) |
| Cash from financing and miscellaneous sources: | | |
| Paid-in surplus | | 24,900,000 |
| Net cash from financing and miscellaneous sources | | 24,900,000 |
| Net change in cash and short-term investments | | 35,968,715 |
| Cash and short-term investments, beginning of period | | 1,058,217 |
| Cash and short-term investments, end of period | $ | 37,026,932 |

See accompanying notes to statutory financial statements.

## (1) Organization and Operations

Louisiana Healthcare Connections, Inc. (the Company) is wholly owned by Healthy Louisiana Holdings, LLC (HLH). HLH was formed as a joint venture between Centene Corporation and Louisiana Partnership for Choice and Access, LLC (LPC&A). Centene Corporation purchased LPC&A's interest in the joint venture on October 31, 2012, making Centene Corporation the sole owner of HLH and the Company wholly owned by Centene Corporation.

The Company, which is organized as a network model Health Maintenance Organization (HMO), was incorporated in October 2009. It is subject to regulation by the Federal Government and the Louisiana Department of Insurance (LDI). The Company began providing healthcare services to Medicaid enrollees participating in the Bayou Health program under the Company's contract with the Louisiana Department of Health and Hospitals on February 1, 2012. The Company completed its three-phase membership rollout for the statewide geographical service areas during the second quarter of 2012. The Company's contract with the Louisiana Department of Health and Hospitals accounts for 100% of the Company's revenue for the period from February 1, 2012 to December 31, 2012. The Company contracts directly with healthcare providers on fee-for-service, per diem, and capitation bases.

## (2) Basis of Presentation and Significant Accounting Policies

The statutory financial statements of the Company are presented on the basis of accounting practices prescribed or permitted by LDI for determining and reporting the financial condition and the results of operations of an insurance company and for determining its solvency under Louisiana insurance law.

The State of Louisiana has adopted accounting policies found in the revised National Association of Insurance Commissioners' (NAIC) *Accounting Practices and Procedures Manual* (NAIC SAP), subject to any deviations prescribed or permitted by LDI (SAP). In 2012, there were no differences between SAP and NAIC SAP that significantly impacted the Company. SAP differs in certain respects from U.S. generally accepted accounting principles (GAAP) followed by other types of enterprises in determining their financial position, results of operations, and cash flow. The most significant variances are as follows:

A. Under SAP, certain assets, designated as "nonadmitted assets" are excluded from the statutory statement of admitted assets, liabilities and capital and surplus and are charged to unassigned deficit as follows:

| | | |
|---|---|---|
| Deferred tax asset | $ | 2,029,152 |
| Healthcare receivables | | 315,973 |
| Prepaid expenses | | 7,500 |
| Total nonadmitted assets | $ | 2,352,625 |

Under GAAP, such assets are included in the balance sheets subject to impairment and allowances.

B. The statutory financial statements reflect certain assets and liabilities net of ceded reinsurance.

C. Under SAP, debt securities are carried at amortized cost. Under GAAP, debt securities are carried at amortized cost only if there is both a positive intent and ability to hold to maturity. Otherwise, they are carried at fair value with unrealized gains and losses recognized in operations or accumulated other comprehensive income according to prescribed rules.

D. Under SAP, the statement of cash flow reconciles to changes in cash and cash equivalents, certificates of deposit and short-term investments with original maturities of one year or less. Under GAAP, the statement of cash flows reconciles to changes in cash and cash equivalents with a maturity period of three months or less. The statutory statement of cash flow is presented in a specified format which differs from the format prescribed by GAAP.

E. Under SAP, net deferred income tax assets are admitted following the application of certain criteria with the resulting change in admitted deferred tax asset amount being credited directly to capital and surplus. Under GAAP, deferred income tax assets and liabilities are recorded for temporary differences between the reported amounts of assets and liabilities and those in the Company's income tax return. Changes to deferred income tax assets and liabilities are recorded in current operations under GAAP and directly to surplus under SAP.

F. Comprehensive income is not determined for statutory reporting purposes, and there is no statement reflecting accumulated other comprehensive income.

The aggregate effect of the foregoing differences between SAP and GAAP has not been determined, but is presumed to be material.

***(a) Management's Estimates***

The preparation of statutory financial statements in conformity with the accounting practices prescribed or permitted by the LDI requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the statutory financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

***(b) Fair Value Measurements***

In the normal course of business, the Company invests in various financial assets and incurs various financial liabilities. Fair values are disclosed for all financial instruments, whether or not such values are recognized in the statutory statement of admitted assets, liabilities and capital and surplus. Management obtains quoted market prices for these disclosures. The carrying amounts reported for premium and related receivables, accounts payable and accrued expenses, and certain other assets and liabilities approximate fair value because of their short-term nature.

***(c) Bonds***

Bonds, at amortized cost, are valued as prescribed by the NAIC. Bonds are generally carried at amortized cost with the accretion of discounts and amortization of premiums being computed under the scientific method. Realized gains and losses are calculated using the specific-identification method.

The Company evaluates all of its investments for impairment based on current market prices, economic conditions and the financial condition of the issuer. Investments that have declines in NAIC market value below cost, which are judged to be other-than-temporary, are written down to estimated NAIC market value. Factors considered in evaluating whether a decline in value is other-than-temporary include: (1) whether the decline is substantial, (2) the Company's ability and intent to retain the investment for a period of time sufficient to allow for an anticipated recovery in value, (3) the duration and extent to which the fair value has been less than cost, and (4) the financial condition and near-term prospects of the issuer in relation to the anticipated recovery period. There were no charges recorded in 2012 related to other-than-temporary impairments.

Investment securities are exposed to various risks, such as interest rate, market and credit. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risks in the near term would materially affect the amounts reported in the statutory statement of admitted assets, liabilities, and capital and surplus or the statutory statement of revenue and expense.

***(d) Restricted Assets***

Under the LDI regulations, the Company is required to maintain certain insolvency deposits of not less than $1,000,000 in a custodial account for the protection of enrollees. The Company is entitled to receive interest income on these deposits. At December 31, 2012, assets in the amount of $1,000,000 were on deposit with government authorities or trustees as required by law and are invested in certificates of deposit and presented within cash and short term investments.

***(e) Cash and Short-Term Investments***

Cash and short-term investments consist of cash on deposit and investments with an original maturity, upon acquisition, of less than one year. Such balances are carried at cost, which approximates fair value.

***(f) Investment Income Due and Accrued***

The Company recognizes investment income when earned. The Company records receivables for investment income earned as of the reporting date but collected in a subsequent period. The Company performs an evaluation of the receivables to determine whether an impairment exists. No impairment charges were recorded in 2012.

***(g) Premiums Receivable***

Premiums receivable consists of reimbursements receivable from the State of Louisiana. Amounts receivable under government insured plans, including amounts over 90 days due, that qualify as accident and health contracts are admitted assets under NAIC SAP. Amounts receivable under government insured plans include, but are not limited to, receivables under Medicare, Medicaid, and similarly funded government insured plans. As of December 31, 2012, the Company had no receivables greater than 90 days.

Premiums receivable are recorded at net realizable value, adjusted for estimated uncollectible amounts. As of December 31, 2012, no allowance for doubtful accounts was deemed necessary based on the Company's evaluation.

### *(h) Reinsurance Receivable*

The Company recognizes receivables for reinsurance recoveries on paid losses that remain outstanding as of the end of the year.

### *(i) Deferred Taxes*

The Company recognizes deferred tax assets and liabilities for the future tax consequences attributable to differences between statutory financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

### *(j) Healthcare Receivables*

Healthcare receivables consist primarily of pharmaceutical rebate receivables. The Company records pharmaceutical rebate receivables based on actual utilization and estimated rebate rates and admits those receivables recorded during the three months immediately preceding the reporting date.

### *(k) Claims Payable and Unpaid Claims Adjustment Expenses*

Claims expenses, related to medical services costs, include claims paid, claims adjudicated but not yet paid, estimates for claims received but not yet adjudicated, estimates for claims incurred but not yet received, and estimates for the costs necessary to process unpaid claims.

The Company estimates its medical claims liability using actuarial methods that are commonly used by health insurance actuaries and meet actuarial standards of practice. These actuarial methods consider factors such as historical data for payment patterns, cost trends, product mix, seasonality, utilization of healthcare services and other relevant factors. The Company's development of the medical claims liability estimate is a continuous process which it monitors and refines on a monthly basis as additional claims receipts and payment information becomes available. As more complete claim information becomes available, the Company adjusts the amount of the estimates, and includes the changes in estimates in medical costs in the period in which the changes are identified. In every reporting period, the operating results include the effects of more completely developed medical claims liability estimates associated with previously reported periods. The Company consistently applies its reserving methodology from period to period. As additional information becomes known, it adjusts the actuarial model accordingly to establish medical claims liability estimates. Management believes the amount of medical claims payable is reasonable and adequate to cover the Company's liability for unpaid claims as of December 31, 2012; however, actual claim payments may differ from established estimates.


(Continued)

***(l) General Expenses Due or Accrued***

The Company records general expenses due or accrued for those direct costs associated with operations incurred as of the reporting date but paid in a subsequent period. General expenses due or accrued as of December 31, 2012 were $119,825.

***(m) Premium Taxes Accrued***

During 2012, the Company incurred a premium tax equal to 2.25% of premium revenues. The premium tax accrual was $6,203,781 at December 31, 2012.

***(n) Premium Income***

Premiums are generally received in the month to which coverage applies and income from such premiums is recorded as earned during the period in which the Company is obligated to provide services to members. Substantially all premiums are based on a fixed amount per eligible enrolled member per month. Premiums collected in advance of the month for which coverage applies are deferred and recorded as unearned premium revenue.

During 2012, the Company earned premium revenues net of ceded reinsurance premiums of $271,118,625, under a contract with the State of Louisiana Department of Health and Hospitals (DHH). The current contract with DHH runs through January 31, 2015 with a two year option for renewal.

The Company records a premium tax revenue and expense within premium income and general administrative expenses, respectively. During 2012, the Company recorded premium tax income and expense of $6,203,781.

***(o) Medical and Hospital Expenses***

The Company contracts with various healthcare providers for the provision of certain related medical care to its members. Medical claims are submitted by providers and processed in accordance with the terms of the contract. Additionally, the Company compensates some providers on a capitation basis. The amount of the capitation payments and the frequency of the distributions to the provider are based on contractual arrangements.

The cost of other healthcare services provided or contracted for is accrued in the period in which it is provided to a member based in part on estimates, including an accrual for medical services provided but not reported.

***(p) Reinsurance***

Premium income is recorded net of ceded reinsurance premiums. Total medical and hospital expenses are recorded net of reinsurance recoveries. The Company is liable in the event its reinsurer is unable to meet its obligations.

### *(q) General Administrative Expenses*

The Company has a management services agreement with CMC, which was approved by the LDI. Under the agreement, the Company pays CMC a fee equal to 12% of its gross monthly revenues for which CMC provides the services necessary to manage the business operations of the Company and assumes responsibility for all associated costs. CMC assumes responsibility for program planning and development, management information systems, financial systems and services, facilities arrangement, claims administration, provider and enrollee services and records, case management, care coordination, utilization and peer review, and quality assurance/quality improvement. In addition, under the agreement, the Company also pays other direct costs associated with the business.

### *(r) Income Taxes*

For the period ended December 31, 2012, the Company filed a consolidated federal income tax return with Centene Corporation and its other subsidiaries. In accordance with the group's tax allocation agreement, the subsidiaries reimburse or recover from Centene Corporation their portion of the income taxes as calculated on a separate company basis.

### *(s) Dividend Restrictions*

The amount of dividends that can be paid by the Company to its shareholder is limited by statute and subject to prior approval from the Commissioner of the LDI. All dividends must be paid from surplus that is fully paid in cash, unimpaired, and beyond the minimum surplus required and all other liabilities equal to fifteen percent of its capital stock; this restriction does not apply to an issuer when its paid-in capital and surplus exceed the minimum required by 100%. No dividends were declared or paid by the Company during the period ended December 31, 2012.

## (3) Bonds

The amortized cost and estimated statutory fair values of investments in bonds at December 31, 2012 are as follows:

| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Statutory fair value |
|---|---|---|---|---|
| U.S. Treasury securities | $ 300,573 | 5,919 | — | 306,492 |
| U.S. government agency obligations | 14,709,268 | 102,172 | 162 | 14,811,278 |
| Unaffiliated domestic securities | 250,000 | — | — | 250,000 |
| Total | $ 15,259,841 | 108,091 | 162 | 15,367,770 |

The fair values of the Company's bonds are evaluated based on NAIC designations set forth by the Securities Valuation Office (SVO). The SVO does not provide fair market values for certain of the Company's bonds. As such, the Company utilizes independent pricing services to estimate fair value for bonds which are not actively traded on the measurement date or for which the SVO does not provide fair market values.

The following table illustrates the gross unrealized losses included in the Company's investment portfolio aggregated by investment category. The table also illustrates the length of time the securities have been in an unrealized loss position as of December 31, 2012.

| | | Decline for less than 12 months | | | Decline for greater than 12 months | | |
|---|---|---|---|---|---|---|---|
| | | Amortized cost | Statutory fair value | Difference | Amortized cost | Statutory fair value | Difference |
| U.S. government agency obligations | $ | 228,687 | 228,525 | 162 | — | — | — |
| Total | $ | 228,687 | 228,525 | 162 | — | — | — |

The Company views the decrease in value of all of the securities with unrealized capital losses at December 31, 2012 as temporary, expects recovery in fair value, anticipates continued payments under the terms of the securities, and has the intent and ability to hold these securities until maturity or a recovery in fair value occurs. Therefore, no impairment of these securities was recorded during 2012.

The amortized cost and statutory fair value of debt securities at December 31, 2012, by contractual maturity, are shown below. Actual maturities may differ due to call or prepayment options.

| | | Amortized cost | Statutory fair value |
|---|---|---|---|
| Due one year or less | $ | 2,951,582 | 2,956,470 |
| Due after one year through five years | | 12,308,259 | 12,411,300 |
| Due after five years through ten years | | — | — |
| Due after ten years | | — | — |
| Total | $ | 15,259,841 | 15,367,770 |

Proceeds from sales of investments in debt securities during 2012 were $250,000. Gross realized losses for the period ended December 31, 2012 were ($1,283). Gross realized gains for the period ended December 31, 2012 were $235.

Net investment income for the period ended December 31, 2012 was as follows:

| | | |
|---|---|---|
| Interest income: | | |
| Bonds | $ | 71,267 |
| Cash and short-term investments | | 37,003 |
| Net realized losses | | (1,048) |
| Net investment income | $ | 107,222 |

## (4) Reinsurance

During 2012, the Company obtained reinsurance coverage with an affiliated insurance entity equal to 90% of hospital inpatient services in excess of $200,000 per covered person per agreement term to a $2,000,000 maximum incurred during the period February 1, 2012 through January 1, 2013. Reimbursement for services provided at hospitals is subject to coinsurance provisions. Eligible hospital expenses are limited to an average daily maximum of $10,000.

The loss reinsurance agreement also provides for certain coverage in the event of the insolvency of the Company, as defined in the reinsurance agreement. The reinsurance company agrees to continue benefits to the Company’s members who are hospitalized at the time of the insolvency until the earlier of the member’s discharge from the hospital or the date the covered person becomes eligible for health insurance coverage or benefit under another group or blanket policy or plan or any federal state or local governmental plan or program. The reinsurance company will also continue benefits for any member for medical services incurred after the date of insolvency provided that premium was received. Coverage for such medical services will continue 30 days after the Company becomes insolvent. The reinsurance company’s aggregate maximum liability under this provision of the reinsurance agreement will not exceed $2,000,000.

Under this agreement, the Company recorded ceded premiums of $4,550,782 for the period ended December 31, 2012 and reinsurance recoveries of $2,429,532.

## (5) Income Taxes

The Company adopted SSAP No. 101, a replacement of SSAP No. 10R, upon commencement of operations. The December 31, 2012 balances and related disclosures are calculated and presented pursuant to SSAP No. 101.



(Continued)

The net deferred tax asset (liability) at December 31, 2012 is comprised of the following components:

| | | Ordinary | Capital | Total |
|---|---|---|---|---|
| Total gross deferred tax assets | $ | 2,060,736 | — | 2,060,736 |
| Valuation allowance adjustment | | — | — | — |
| Adjusted gross deferred tax assets | | 2,060,736 | — | 2,060,736 |
| Total gross deferred tax liabilities | | (31,584) | — | (31,584) |
| Net deferred tax assets | | 2,029,152 | — | 2,029,152 |
| Total deferred tax assets nonadmitted | | (2,029,152) | — | (2,029,152) |
| Net admitted deferred tax assets | $ | — | — | — |
| Net change in total deferred tax assets nonadmitted | $ | (2,029,152) | — | (2,029,152) |

The amount of adjusted gross deferred tax assets admitted is as follows:

| | | Ordinary | Capital | Total |
|---|---|---|---|---|
| FIT recoverable by loss carryback | $ | — | — | — |
| Expected to be realized | | — | — | — |
| Expected to be realized | | — | — | — |
| Surplus limitation | | — | — | — |
| Deferred tax liability offset 11.c. | | 31,584 | — | 31,584 |
| Total admitted under 11.a.-11.c. | | 31,584 | — | 31,584 |
| Deferred tax liabilities | | (31,584) | — | (31,584) |
| Total admitted from the application of paragraphs 11.a.-11.c. | $ | — | — | — |

The information used in the expected to be realized calculation consists of the following:

| | | |
|---|---|---|
| Authorized control level risk based capital ratio without net deferred tax assets | | 306% |
| Adjusted capital and surplus | $ | 35,176,457 |

The change in deferred income taxes reported in surplus before consideration of nonadmitted assets is comprised of the following components:

| | | |
|---|---|---|
| Total deferred tax assets | $ | 2,060,736 |
| Total deferred tax liabilities | | (31,584) |
| Net deferred tax assets | | 2,029,152 |
| Statutory valuation allowance adjustment | | — |
| Net deferred tax assets after statutory valuation allowance | $ | 2,029,152 |
| Change in deferred income tax | $ | — |

Current income taxes incurred consist of the following major components:

| | | |
|---|---|---|
| Current year tax benefit | $ | (5,887,685) |
| Current income taxes incurred | $ | (5,887,685) |

Deferred income tax assets and liabilities consist of the following major components:

| | Ordinary | Capital | Total |
|---|---|---|---|
| Deferred tax assets: | | | |
| Loss reserve discounting | $ 234,912 | — | 234,912 |
| Nonadmitted assets | 113,216 | — | 113,216 |
| Net operating loss carryforward | 1,712,608 | — | 1,712,608 |
| Total adjusted gross deferred tax assets | 2,060,736 | — | 2,060,736 |
| Valuation allowance adjustment | — | — | — |
| Total adjusted gross deferred tax assets | 2,060,736 | — | 2,060,736 |
| Nonadmitted deferred tax assets | (2,029,152) | — | (2,029,152) |
| Admitted deferred tax assets | 31,584 | — | 31,584 |
| Deferred tax liabilities: | | | |
| Investments | (84) | — | (84) |
| Prepaid expenses | (31,500) | — | (31,500) |
| Total deferred tax liabilities | (31,584) | — | (31,584) |
| Net admitted deferred tax asset | $ — | — | — |

The valuation allowance adjustment to gross deferred tax assets as of December 31, 2012 was $0. The net change in the total valuation allowance adjustments for the period ended December 31, 2012 was $0.



(Continued)

The Company's income tax incurred and change in deferred income tax differs from the amount obtained by applying the federal statutory rate of 35% to income before income taxes as follows:

| | | |
|---|---|---|
| Current income taxes incurred | $ | (5,887,685) |
| Change in deferred income tax (without tax on unrealized gains and losses) | | (2,029,152) |
| Total income tax reported | $ | (7,916,837) |
| Loss before taxes | $ | (22,296,281) |
| | | 35% |
| Expected income tax benefit at 35% statutory rate | | (7,803,698) |
| Increase (decrease) in actual tax reported resulting from: | | |
| a. Change in deferred taxes on nonadmittted assets | | (113,216) |
| b. Other | | 77 |
| Total income tax reported | $ | (7,916,837) |

As of December 31, 2012, the Company had net operating loss carryforwards expiring through the year 2032 of $1,712,608.

There are no Federal income taxes incurred that are available for recoupment in the event of future net losses.

The Company's federal income tax return is consolidated with:

Absolute Total Care, Inc.
AECC Total Vision Health Plan of Texas, Inc.
Bankers Reserve Life Insurance Company of Wisconsin, Inc.
Buckeye Community Health Plan, Inc.
Celtic Insurance Company
CeltiCare Health Plan of Massachusetts, Inc.
Coordinated Care Corporation
Hallmark Life Insurance Co.
Home State Health Plan, Inc.
IlliniCare Health Plan, Inc.
Kentucky Spirit Health Plan, Inc.
Sunshine State Health Plan, Inc.
Magnolia Health Plan, Inc.
Managed Health Services Insurance Corp.
Peach State Health Plan, Inc.
Superior HealthPlan, Inc.
University Health Plans, Inc.

The method of allocation among companies is subject to a written agreement whereby allocation is made primarily on a separate company basis using the percentage method pursuant to provisions of IRC Sections 1502 and 1552 and Treasury Regulations 1.1502 and 1.1552. This percentage method allocates a tax asset (i.e. intercompany receivable) for any benefit derived by the consolidated group for the member's losses or credits that offset consolidated taxable income. In accordance with the tax sharing agreement, each member shall pay to Parent or receive from the Parent the amount of tax liability or benefit reported on each member's proforma federal income tax return within 90 days of the date Parent files its consolidated federal income tax return.

## (6) Claims Payable

Following is a summary of claims-related expenses and payments during 2012:

| | | |
|---|---|---|
| Balance at February 1, net of reinsurance ceded of $0 | $ | — |
| Incurred related to current year | | 253,792,486 |
| Incurred related to prior year | | — |
| Total incurred | | 253,792,486 |
| Paid related to current year | | 207,232,330 |
| Paid related to prior year | | — |
| Total paid | | 207,232,330 |
| Balance at December 31, net of reinsurance ceded of $1,590,000 | | 46,560,156 |
| Less accrued medical incentive pool and bonus payment | | 18,160 |
| Net balance at December 31 | $ | 46,541,996 |

## (7) Related-Party Transactions

In addition to the reinsurance agreement in footnote 4 to the financial statements, the Company's transactions with and amounts due from (to) related parties in exchange for services provided for the period ended December 31 are as follows:

| Affiliate | | Expense | Amount due amounts from (to) | Services provided |
|---|---|---|---|---|
| Cenpatico Behavioral Health | $ | 564,477 | 101 | Behavioral health |
| CMC | | 33,080,329 | (376,289) | Data and claims processing general management |
| NurseWise LP | | 1,608,421 | (1,850) | *Nurse-line triage |
| Nurtur Health, Inc. | | 2,025,380 | (73) | *Life and health management |
| Opticare Vision Company, Inc. | | 3,894,633 | (118,051) | *Vision |
| US Script, Inc. | | 22,692,368 | — | Pharmacy |

* Amounts due from (to) affiliate reflected in claims payable in statutory statement of admitted assets, liabilities, and capital and surplus as of December 31, 2012

The Company received surplus contributions totaling $24,900,000 from HLH for the period ended December 31, 2012. In addition, included in the statutory statement of admitted assets, liabilities and capital and surplus at December 31, 2012 are amounts due from parent, subsidiaries and affiliates of $24,000,000 due to a contribution receivable from HLH.

## (8) Statutory Net Worth

Under the laws of the State of Louisiana, the Company is required to maintain a minimum statutory net worth. At December 31, 2012, the minimum requirement is $3,000,000.

## (9) Risk-Based Capital Requirements

The Company is required to report an assessment of its solvency based upon the NAIC Managed Care Organizations Risk-Based Capital (RBC) analysis formulas, as adopted by the State of Louisiana. As of December 31, 2012, the Company's adjusted capital and surplus exceeded the thresholds set forth by the NAIC RBC formula. At December 31, 2012, the Company's actual total adjusted capital was $35,176,457. The Company's action level equaling 200% of the authorized control level was $22,961,510.

## (10) Contingencies

From time to time, the Company may be involved in litigation arising in the ordinary course of operations. While the results of litigation cannot be predicted with certainty, management is of the opinion, after reviewing these matters with legal counsel, that the final outcome of such litigation, if any, will not have a material adverse effect on the Company's statutory financial position.

## (11) Fair Value of Financial Instruments

Assets and liabilities recorded at fair value in statutory statement of admitted assets, liabilities, and capital and surplus are categorized based upon the extent to which the fair value estimates are based upon observable or unobservable inputs. Level inputs are as follows:

| Level input | Input definition |
|---|---|
| Level I | Inputs are unadjusted, quoted prices for identical assets or liabilities in active markets at the measurement date. |
| Level II | Inputs other than quoted prices included in Level I that are observable for the asset or liability through corroboration with market data at the measurement date. |
| Level III | Unobservable inputs that reflect management's best estimate of what market participants would use in pricing the asset or liability at the measurement date. |

The following table summarizes fair value measurements by level at December 31, 2012 for admitted assets measured at fair value on a recurring basis:

| | Level I | Level II | Level III | Total |
|---|---|---|---|---|
| Cash and short-term investments | $ 37,026,932 | — | — | 37,026,932 |
| Total assets at fair value | $ 37,026,932 | — | — | 37,026,932 |

## (12) Risks and Uncertainties

The Company's profitability depends in large part on accurately predicting and effectively managing medical services costs. The Company continually reviews its premium and benefit structure to reflect its underlying claims experience and revised actuarial data; however, several factors could adversely affect the medical service costs. Certain of these factors, which include changes in healthcare practices, inflation, new technologies, major epidemics, natural disasters, and malpractice litigation, are beyond any health plan's control and could adversely affect the Company's ability to accurately predict and effectively control healthcare costs. Costs in excess of those anticipated could have a material adverse effect on the Company's results of operations.

## (13) Subsequent Events

In connection with the preparation of the statutory financial statements, the Company evaluated subsequent events after the statutory statement of admitted assets, liabilities, and capital and surplus date of December 31, 2012 through May 23, 2013, which was the date the statutory statements were issued. As of December 31, 2012, the Company recorded a contribution receivable of $24,000,000, which was satisfied prior to the date the statutory financial statements were issued.

**Schedule 1**

**LOUISIANA HEALTHCARE CONNECTIONS, INC.**
(A Wholly Owned Subsidiary of Centene Corporation)

Supplemental Summary Investment Schedule

December 31, 2012

| | Gross investment holdings | | Admitted assets | |
|---|---|---|---|---|
| Bonds: | | | | |
| U.S. Treasury securities | $ 300,573 | 0.6% | $ 300,573 | 0.6% |
| U.S. government agency obligations | 14,709,268 | 28.1 | 14,709,268 | 28.1 |
| Unaffiliated domestic securities | 250,000 | 0.5 | 250,000 | 0.5 |
| Cash and short-term investments | 37,026,932 | 70.8 | 37,026,932 | 70.8 |
| Total invested assets | $ 52,286,773 | 100.0% | $ 52,286,773 | 100.0% |

See accompanying independent auditors' report.

**Schedule 2**

**LOUISIANA HEALTHCARE CONNECTIONS, INC.**
(A Wholly Owned Subsidiary of Centene Corporation)

Supplemental Investment Risk Interrogatories

Period from February 1, 2012 (initial date of operations) to December 31, 2012

1. The Company's total admitted assets as of December 31, 2012 were: $ 89,329,508

2. The following are the ten largest exposures to a single issuer, excluding U.S. government, U.S. government agency securities and U.S. Government money market funds:

| | | | |
|---|---|---|---|
| 1. | JP Morgan Institutional | $ 10,000,000 | 11.19% |
| 2. | Invesco Liquid Assets | 2,000,000 | 2.24 |

3. The amounts and percentages of the Company's total admitted assets held in bonds and preferred stocks by NAIC rating is as follows:

| | Bonds | | | Preferred stocks | |
|---|---|---|---|---|---|
| **Rating** | **Amount** | **Percentage** | **Rating** | **Amount** | **Percentage** |
| NAIC-1 | $ 27,343,310 | 30.61% | | $ — | —% |

All other interrogatories in Section 2 of Appendix A-001 to the NAIC *Accounting Practices and Procedures Manual* have not been disclosed as they are not applicable.

See accompanying independent auditors' report.