

# **Maricopa Health Plan (A Contract of Maricopa Integrated Health System)**

Financial Statements  
With Independent Auditor's Report Thereon  
June 30, 2015 and 2014

## Contents

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Independent Auditor's Report	1-2
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Required Supplementary Information (Unaudited)	
Management's discussion and analysis	3-6
Financial Statements	
Statements of net position	7
Statements of revenues, expenses and changes in net position	8-9
Statements of cash flows	10
Notes to financial statements	11-16

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## Independent Auditor's Report

To the Board of Directors  
Maricopa Integrated Health System  
Phoenix, Arizona

### Report on the Financial Statements

We have audited the accompanying financial statements of Maricopa Health Plan (a contract of Maricopa Integrated Health System) (MHP) as of and for the years ended June 30, 2015 and 2014, and the related notes to the financial statements, which collectively comprise MHP's financial statements, as listed in the table of contents.

### 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.

### Auditor's 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 of 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 entity'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 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 opinion.

### Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Maricopa Health Plan (a contract of Maricopa Integrated Health System) as of June 30, 2015 and 2014, and its changes in net position and its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

**Emphasis of Matter**

As described more fully in Note 1, MHP is a contract of Maricopa County Special Health Care District, d/b/a Maricopa Integrated Health System (MIHS), a statutory Special Health Care District and political subdivision of the State of Arizona. The financial statements present only MHP and do not purport to, and do not, present fairly the financial position of MIHS and its changes in net position and its cash flows, in conformity with accounting principles generally accepted in the United States of America.

**Other Matters**

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board (GASB), who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.



Minneapolis, Minnesota  
October 21, 2015

## **Maricopa Health Plan (A Contract of Maricopa Integrated Health System)**

### **Management's Discussion and Analysis**

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#### **Introduction**

Maricopa Health Plan (MHP), a contract of Maricopa Integrated Health System (MIHS), offers readers of its financial statements this narrative overview of the current financial position, results of operations, and cash flows for MHP for the years ended June 30, 2015 and 2014. The narrative within contains required supplemental information, which should be read in conjunction with MHP's audited financial statements, including the notes thereto.

#### **Overview of the Financial Statements**

This discussion and analysis is intended to serve as an introduction to MHP's audited financial statements. The financial statements are composed of the statement of net position, the statement of revenues, expenses and changes in net position, and the statement of cash flows. The financial statements also include notes to the financial statements that explain in more detail some of the information in the financial statements. The financial statements are designed to provide readers with a broad overview of MHP's finances.

These statements offer short- and long-term information about MHP's activities. The statement of net position includes all of MHP's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to MHP's creditors (liabilities). The statement of net position also provides the basis for evaluating the capital structure of MHP and assessing the liquidity and financial flexibility of MHP.

All of the current year's revenues and expenses are accounted for in the statement of revenues, expenses and changes in net position. This statement measures the financial performance of MHP's operations and can be used to determine whether MHP has successfully recovered all of its costs through its revenue sources. Revenues and expenses are reported on an accrual basis, which means the related cash could be received or paid in a subsequent period.

The final required statement is the statement of cash flows. This statement reports the cash receipts, cash payments, and net changes in cash resulting from operations, investing and financing activities. It also provides answers to where cash came from, what cash was used for, and what the change in cash balance was during the reporting period.

#### **Overview of MHP**

Maricopa Health Plan is a contract of Maricopa Integrated Health System and provides health plan services to enrollees under a contract, through September 2018, with the Arizona Health Care Cost Containment System (AHCCCS) in Maricopa County, Arizona.

In addition to the AHCCCS contract, MIHS holds a contract with the Centers for Medicare & Medicaid Services (CMS) for the operation of a Medicare Advantage Prescription Drug (MAPD) health plan through Maricopa Care Advantage. AHCCCS requires all acute care contractors to hold a MAPD contract with CMS to encourage coordination of care between primary and secondary payors. The financial results of this contract are not included in MHP's financial statements, but rather are reported elsewhere.

## Maricopa Health Plan (A Contract of Maricopa Integrated Health System)

### Management's Discussion and Analysis

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#### Financial Analysis of MHP

The statements of net position and the statements of revenues, expenses and changes in net position report the net position of MHP and the related changes. MHP's net position (the difference between total assets and total liabilities) is a way to measure the financial health, or financial position. Over time, sustained increases or decreases in MHP's net position is one indicator of whether its financial health is improving or deteriorating. However, other nonfinancial factors, such as changes in economic conditions, population growth and new governmental legislation, should also be considered.

#### Statements of Net Position

**Liquidity:** As of June 30, 2015 and 2014, MHP has cash and cash equivalents of \$27,635,879 and \$22,446,697, respectively. Cash and cash equivalents consist of cash held in depository accounts in the name of MHP. The carrying amount approximates fair value because of the highly liquid nature of these accounts.

In addition, MHP maintains excess cash and cash equivalents with MIHS, which are available on demand and are presented in the accompanying statements of net position as due from affiliate. MHP expects to adequately generate cash to meet the day-to-day requirements.

MHP is required to make estimates and assumptions that affect the reported amounts of assets and liabilities. Actual results may differ from those estimates.

**Assets:** MHP's total assets are \$65,866,503 and \$60,030,267 as of June 30, 2015 and 2014, respectively. MHP has no assets held in bonds and money market mutual funds. MHP has no assets held in foreign investments, investments with contractual sales restrictions, equity interests, or in nonaffiliated, privately placed equities. MHP has neither mortgage loans nor any assets held in real estate.

At June 30, 2015 and 2014, respectively, MHP reported a receivable of \$92,408 and \$257,692 for supplemental revenue and \$2,723,772 and \$10,208,702 for reconciliation receivable due from AHCCCS.

MHP receives reinsurance coverage from the State of Arizona to reduce the risk of catastrophic loss on services provided under the AHCCCS program. The gross capitation rates were reduced by the reinsurance cost. Under the state program, risk of loss for inpatient claims is generally limited to an annual deductible of \$25,000 for 2015 and 2014 per member, per policy year. Eligible claims in excess of the deductible are generally paid by the state at 75 percent to 85 percent, with no maximum annual benefit. MHP's reinsurance receivable reported at June 30, 2015 and 2014, was \$3,507,042 and \$3,616,696, respectively.

**Liabilities:** MHP reported total liabilities of \$47,190,374 and \$40,207,933 as of June 30, 2015 and 2014, respectively. As of June 30, 2015 and 2014, respectively, MHP reported \$16,444,655 and \$3,870,089 for reconciliation payable due to AHCCCS.

At June 30, 2015 and 2014, MHP reported \$25,678,037 and \$26,905,059, respectively, for medical claims payable. The costs of hospital and medical services provided to enrollees served under contract are recognized in the period that the services are rendered. A provision has been made for claims in process of review and for claims incurred but not reported at year-end. The amount of this liability is computed using historical claims payment experience coupled with a review of experience for similar plans. Estimates are adjusted based upon changes in experience, and such adjustments are reflected in current operations. Although considerable variability is inherent in such estimates, there is a possibility that recorded estimates will change by a material amount in the near term.

Management believes that the medical claims payable is adequate.

## Maricopa Health Plan (A Contract of Maricopa Integrated Health System)

### Management's Discussion and Analysis

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**Net position:** MHP had ending net position of \$18,676,129 and \$19,822,334 at June 30, 2015 and 2014, respectively. The decrease of \$1,146,205 is the result of operating gain of \$8,853,795 in fiscal year 2015 as reported within the statement of revenues, expenses and changes in net position, offset by a capital distribution to MIHS of \$10,000,000.

### Statements of Revenues, Expenses and Changes in Net Position

MHP reported a net operating gain of \$8,853,795 and \$616,265 for the fiscal years ended June 30, 2015 and 2014, respectively. MHP reported revenues and gains, net, of \$262,062,603 and \$202,765,440 for fiscal years ended June 30, 2015 and 2014, respectively. Prospective Tiered and PPC capitation received from AHCCCS for MHP members totaled \$261,958,360 and \$190,820,015 for fiscal years ended June 30, 2015 and 2014, respectively. MHP receives delivery supplemental revenue upon the delivery of a child by a member during a prospective enrollment period. This supplemental payment does not include payment for deliveries of those members who deliver in a prior coverage period. Delivery supplemental revenue for fiscal years 2015 and 2014 totaled \$10,877,210 and \$9,440,655, respectively.

PCP Parity (Primary Care Provider Parity) cost settlement revenues represent reimbursement of eligible enhanced payment expenses incurred by MHP and reimbursable by the State of Arizona. Section 1202 of the Affordable Care Act requires minimum levels of payment for certain primary care services (Primary Care Provider Parity or PCP Parity) provided by certain physicians. The enhanced reimbursement requirements for MHP are subject to reimbursement by the State of Arizona. MHP incurred PCP Parity enhanced payment expenses of \$2,517,808 and \$5,480,481 for the years ended June 30, 2015 and 2014, respectively. MHP has also recorded PCP Parity cost settlement revenues of \$2,517,808 and \$5,480,481, respectively, as these enhanced payment expenses are reimbursable by the State of Arizona. This temporary program was established by the Affordable Care Act to exist from January 1, 2013, through December 31, 2014.

Total health care expenses, net of reinsurance and third-party liability, were \$226,028,143 and \$180,796,095 for the years ended June 30, 2015 and 2014, respectively.

Administrative expenses for 2015 and 2014 consist of the management fee paid to the administrator of MHP. Until February 28, 2015, University Physicians Healthcare (UPH) was the administrator of MHP. Effective February 28, 2015, UPH merged with Banner Health (Banner), and Banner became successor to UPH in this management contract. The total management fees incurred were \$21,157,297 and \$17,029,404, and other administrative expenses of \$306,172 and \$220,078 were incurred for the years ended June 30, 2015 and 2014, respectively. For fiscal year 2015, the management fee payable to the administrator of MHP represents 8 percent of collected revenues for the period July through September 2014, 8.25 percent for the period October through December 2014, and 8 percent for the period January through June 2015. For fiscal year 2014, the management fee payable to the administrator of MHP is calculated at 8 percent of the revenue collected by MHP for 2014. Premium tax expense of \$5,717,196 and \$4,103,598 was reported for 2015 and 2014, respectively.

MHP performs periodic analysis of its expected future health care costs and maintenance costs to determine whether such costs will exceed anticipated future revenues under its contracts. Should expected costs exceed anticipated revenues, a premium deficiency reserve is accrued. At June 30, 2015 and 2014, MHP did not record a premium deficiency reserve.

**Federal income tax:** As a governmental unit or a political subdivision thereof, MIHS is exempt from federal income tax under section 115(1) of the Internal Revenue Code. MIHS is also exempt from state income taxes.

## **Maricopa Health Plan (A Contract of Maricopa Integrated Health System)**

### **Management's Discussion and Analysis**

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**Premium tax:** The State of Arizona imposes a premium tax on capitation payments paid to MHP by AHCCCS. MHP receives the premium tax from AHCCCS and remits the entire amount to the appropriate taxing authority. MHP includes the taxes collected as revenues and taxes remitted as an expense in the accompanying statements of revenues, expenses and changes in net position.

#### **Economic and Other Factors and Next Year's Forecast**

MHP's management considers many factors when setting the fiscal year 2016 forecast. Of primary importance is the status of the economy, which takes into account market forces and environmental factors such as the following:

- Health care reform
- Changes in revenue rates under the AHCCCS contract
- Changes in enrollment/market share under the AHCCCS contract
- Effectiveness in managing care and population health for enrolled members
- Changes in provider costs affecting MHP's total health care expenses

Enrollment at June 30, 2014, was 75,791 and has increased by 3,892 to 79,683 at June 30, 2015.

As all of MHP's revenues were earned under its AHCCCS contract, continuation of the AHCCCS programs is dependent on governmental policies. With the award of the new AHCCCS contract beginning October 1, 2013, and effective through September 30, 2018, MHP will continue to provide health plan services to its members for the foreseeable future.

#### **Contacting Maricopa Health Plan**

MHP's financial statements are designed to present readers with a general overview of MHP's finances and attempt to demonstrate MHP's accountability and transparency. If you have questions about the report or need additional financial information, please contact Administration at Maricopa Integrated Health System, 2601 East Roosevelt Street, Phoenix, AZ 85008.



**Maricopa Health Plan (A Contract of Maricopa Integrated Health System)**

**Statements of Net Position  
June 30, 2015 and 2014**

<b>Assets</b>	<b>2015</b>	<b>2014</b>
Current Assets		
Cash	\$ 27,635,879	\$ 22,446,697
Reinsurance receivable	3,507,042	3,616,696
Capitation and supplemental revenue receivable	92,408	257,692
Reconciliation receivable	2,723,772	4,728,221
Premium tax receivable	-	181,539
Due from affiliates	31,428,586	23,024,911
Other current assets	478,816	294,030
<b>Total current assets</b>	<b>65,866,503</b>	<b>54,549,786</b>
Reconciliation Receivable	-	5,480,481
<b>Total assets</b>	<b>\$ 65,866,503</b>	<b>\$ 60,030,267</b>
<b>Liabilities and Net Position</b>		
Current Liabilities		
Accounts payable	\$ 685,660	\$ 691,450
Accrued administrative costs	2,123,232	1,468,000
Medical claims payable	25,678,037	26,905,059
Payment reform/shared savings payable	1,913,622	-
Reconciliation payable	7,387,515	978,360
Other current liabilities	345,168	7,273,335
<b>Total current liabilities</b>	<b>38,133,234</b>	<b>37,316,204</b>
Reconciliation Payable	9,057,140	2,891,729
<b>Total liabilities</b>	<b>47,190,374</b>	<b>40,207,933</b>
Unrestricted Net Position	18,676,129	19,822,334
<b>Total liabilities and net position</b>	<b>\$ 65,866,503</b>	<b>\$ 60,030,267</b>

See Notes to Financial Statements.

**Maricopa Health Plan (A Contract of Maricopa Integrated Health System)**

**Statements of Revenues, Expenses and Changes in Net Position  
Years Ended June 30, 2015 and 2014**

	2015	2014
Revenues and gains, net:		
Capitation	\$ 239,455,543	\$ 163,185,313
PPC capitation	22,502,817	27,634,702
Delivery supplement	10,877,210	9,440,655
Adults <=/=106 reconciliation settlement	90,838	234,516
PPC reconciliation settlement	(9,690,425)	(2,427,800)
Prospective Tiered reconciliation settlement	(4,838,089)	(694,212)
Adults > 106 reconciliation settlement	1,098,627	(120,023)
PCP Parity cost settlement	2,517,808	5,480,481
Investment income	48,274	31,808
<b>Total revenues and gains, net</b>	<b>262,062,603</b>	<b>202,765,440</b>
Health care expenses:		
Hospitalization expenses:		
Hospital inpatient	48,588,012	38,128,198
PPC—hospital inpatient	5,925,455	14,567,413
<b>Total hospitalization expenses</b>	<b>54,513,467</b>	<b>52,695,611</b>
Medical compensation:		
Primary care physician services	10,499,463	9,247,502
Referral physician services	32,276,007	21,571,330
Other professional services	10,106,502	6,736,038
PPC—physician services	1,155,261	2,847,755
PCP Parity enhanced payment	2,517,808	5,480,481
<b>Total medical compensation expenses</b>	<b>56,555,041</b>	<b>45,883,106</b>
Other medical expenses:		
Emergency facility services	26,229,720	18,499,311
Pharmacy	35,821,539	20,069,366
Lab, X-ray and medical imaging	11,105,028	7,734,103
Outpatient facility	25,315,426	18,372,605
Durable medical equipment	2,391,850	1,752,278
Dental	9,248,387	7,501,098
Transportation	6,257,303	5,934,809
Nursing facility, home health care	4,599,156	3,743,298
Physical therapy	892	(3,941)
Shared savings arrangements	73,513	-
PPC—other	2,474,431	4,979,412
<b>Total other medical expenses</b>	<b>123,517,245</b>	<b>88,582,339</b>
<b>Total health care expenses</b>	<b>234,585,753</b>	<b>187,161,056</b>
Less:		
Reinsurance recoveries	7,105,346	5,493,834
Third-party liability, net of collection fees	1,452,264	871,127
<b>Total net health care expenses</b>	<b>226,028,143</b>	<b>180,796,095</b>

(Continued)

**Maricopa Health Plan (A Contract of Maricopa Integrated Health System)**

**Statements of Revenues, Expenses and Changes in Net Position (Continued)**  
**Years Ended June 30, 2015 and 2014**

	<b>2015</b>	2014
Administrative expenses:		
Management fees	<b>21,157,297</b>	17,029,404
Other	<b>306,172</b>	220,078
<b>Total administrative expenses</b>	<b>21,463,469</b>	17,249,482
Premium taxes	<b>5,717,196</b>	4,103,598
<b>Total operating expenses</b>	<b>253,208,808</b>	202,149,175
<b>Operating gain</b>	<b>8,853,795</b>	616,265
Capital distribution to Maricopa Integrated Health Systems	<b>(10,000,000)</b>	-
<b>Increase (decrease) in unrestricted net position</b>	<b>(1,146,205)</b>	616,265
Unrestricted net position, beginning	<b>19,822,334</b>	19,206,069
Unrestricted net position, ending	<b>\$ 18,676,129</b>	<b>\$ 19,822,334</b>

See Notes to Financial Statements.

**Maricopa Health Plan (A Contract of Maricopa Integrated Health System)**

**Statements of Cash Flows**  
**Years Ended June 30, 2015 and 2014**

	2015	2014
Cash Flows From Operating Activities		
Cash received for capitation and other operating receipts	\$ 286,079,848	\$ 215,235,945
Cash paid to providers and facilities	(235,812,775)	(173,700,987)
Cash paid for supplies, purchased services and other	(26,674,216)	(20,556,652)
<b>Net cash provided by operating activities</b>	<b>23,592,857</b>	<b>20,978,306</b>
Cash Flows From Investing Activities		
Change in due from affiliate	(8,403,675)	(23,024,911)
<b>Net cash used in investing activities</b>	<b>(8,403,675)</b>	<b>(23,024,911)</b>
Cash Flows From Noncapital Financing Activities		
Capital distribution to Maricopa Integrated Health Systems	(10,000,000)	-
<b>Net cash used in noncapital financing activities</b>	<b>(10,000,000)</b>	<b>-</b>
<b>Net increase (decrease) in cash</b>	<b>5,189,182</b>	<b>(2,046,605)</b>
Cash, beginning	22,446,697	24,493,302
Cash, ending	<b>\$ 27,635,879</b>	<b>\$ 22,446,697</b>
Reconciliation of Operating Gain to Net Cash Provided by Operating Activities		
Operating gain	\$ 8,853,795	\$ 616,265
Adjustments to reconcile operating gain to net cash provided by operating activities:		
Changes in assets and liabilities:		
Reinsurance receivable	109,654	(298,298)
Capitation and supplemental revenue receivable	165,284	6,954,213
Other current assets	(184,786)	268,335
Reconciliation receivable	7,484,930	(4,312,380)
Premium tax receivable	181,539	(181,539)
Accounts payable and accrued administrative costs	649,442	945,195
Medical claims payable	(1,227,022)	13,460,069
Reconciliation payable	12,574,566	3,585,940
Payment reform/shared savings payable	1,913,622	-
Other current liabilities	(6,928,167)	(59,494)
<b>Total adjustments</b>	<b>14,739,062</b>	<b>20,362,041</b>
<b>Net cash provided by operating activities</b>	<b>\$ 23,592,857</b>	<b>\$ 20,978,306</b>

See Notes to Financial Statements.

## Maricopa Health Plan (A Contract of Maricopa Integrated Health System)

### Notes to Financial Statements

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#### Note 1. Organization and Operations

**Organizational structure:** Maricopa Health Plan (MHP) provides health plan services to enrollees under a contract with the Arizona Health Care Cost Containment System (AHCCCS) in Maricopa County, Arizona. Effective October 1, 2005, Maricopa County Special Health Care District, d/b/a Maricopa Integrated Health System (MIHS), a statutory Special Health Care District and political subdivision of the State of Arizona, assumed the operations and financial responsibility for MHP, which was previously operated by Maricopa County. MHP is governed by MIHS. The financial statements present only MHP and do not purport to, and do not, present fairly the net position of MIHS and its changes in net position and its cash flows, in conformity with accounting principles generally accepted in the United States of America.

All of MHP's revenues were earned under its AHCCCS contract. Continuation of the AHCCCS programs is dependent upon governmental policies. This contract is subject to renewal. In March 2013, MHP was awarded a new five-year contract with AHCCCS to operate MHP through September 30, 2018. The loss of this contract would have an adverse effect on MHP's future operations. MHP has a contract with University Physicians Healthcare (UPH) to provide comprehensive management and administrative services necessary for the operation of MHP. UPH merged with Banner Health on February 28, 2015, and Banner Health became successor to UPH in this management contract.

#### Note 2. Summary of Significant Accounting Policies

**Basis of accounting:** MHP is a health care organization, as defined in the American Institute of Certified Public Accountants' (AICPA) *Audit and Accounting Guide, Health Care Entities*, and follows accounting principles generally accepted in the United States of America. MHP follows applicable Governmental Accounting Standards Board (GASB) principles and has prepared MHP's financial statements on the accrual basis of accounting using the economic resources measurement focus.

**Use of estimates:** The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Cash:** During 2015 and 2014, cash consists of cash held in depository accounts in the name of MHP. The carrying amount approximates fair value because of the highly liquid nature of these accounts. MHP maintains cash in a bank account that frequently exceeds federally insured limits. To date, MHP has not experienced any losses in such accounts. The depository insurance related to these bank balances at June 30, 2015 and 2014, was \$250,000. At June 30, 2015 and 2014, MHP had a book balance of cash of \$27,635,879 and \$22,446,697, respectively, and a bank balance of \$33,543,194 and \$28,217,433, respectively. As MHP operates as a department of MIHS, MIHS assumes any custodial credit risk related to MHP cash balances.

MHP also maintains excess cash and cash equivalents with MIHS, which are presented in the accompanying statements of net position as due from affiliate. These balances maintained with MIHS are available on demand. As a result, MIHS assumes any credit risk associated with the cash and cash equivalents held on behalf of MHP. These cash equivalents are limited to commercial paper.

## Maricopa Health Plan (A Contract of Maricopa Integrated Health System)

### Notes to Financial Statements

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#### Note 2. Summary of Significant Accounting Policies (Continued)

**Reinsurance receivable:** Reinsurance receivable represents management's best estimate and is calculated based on the identification of qualifying incurred inpatient expenses and a percentage of estimated inpatient and certain pharmaceutical costs incurred but not yet reported. As a result, there is at least a possibility that recorded estimates will change by a material amount in the near term. MHP recorded increased reinsurance recoveries of approximately \$46,000 during 2015 that relate to services provided in 2014, and an increase of approximately \$11,000 during 2014 that relates to services provided in 2013.

**Medical claims payable:** The costs of hospital and medical services provided to enrollees served under contract are recognized in the period that the services are rendered. A provision has been made for claims in process of review and for claims incurred but not reported at year-end. The amount of this liability is computed using historical claims payment experience coupled with a review of experience for similar plans. Estimates are adjusted based upon changes in experience, and such adjustments are reflected in current operations. Although considerable variability is inherent in such estimates, there is a possibility that recorded estimates will change by a material amount in the near term. Management believes that the medical claims payable recorded is adequate. See also Note 3.

**Other current liabilities:** Other current liabilities include a risk adjustment payable to AHCCCS of \$-0- and \$7,113,225 for the years ended June 30, 2015 and 2014, respectively. This liability represents management's best estimate of capitation overpayments by AHCCCS based upon the risk profile of MHP's membership.

**Premium deficiency reserve:** MHP performs periodic analysis of its expected future health care costs and maintenance costs to determine whether such costs will exceed anticipated future revenues under its contracts. Should expected costs exceed anticipated revenues, a premium deficiency reserve is recognized. Investment income is not included in the calculation of premium deficiency reserves. At June 30, 2015 and 2014, contracted rates and anticipated expenses did not warrant a premium deficiency reserve.

**Unrestricted net position:** Unrestricted net position is the remaining net position that does not meet the definition of restricted or invested in capital assets in accordance with GASB Statement No 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*.

**Capitation revenues:** Capitation revenues include premiums earned under contracts that require MHP to provide health care services to subscribers of AHCCCS for monthly capitation fees as agreed upon by MHP and AHCCCS. Capitation revenues are recognized as revenue in the period to which health care coverage relates. Amounts receivable under these contracts are recorded as capitation and supplemental revenue receivable. Capitation rates are subject to adjustment based on national episodic/diagnostic risk. As such, there is a possibility that recorded amounts will change by a material amount in the near term.

**Supplemental revenue:** Delivery supplemental revenue is recognized upon the delivery of a child by a member assigned to MHP during a prospective enrollment period. This supplemental payment does not include payment for deliveries of those members who deliver in a prior coverage period.

**Reconciliation settlement revenue (contra-revenue):** Amounts due to (from) the State of Arizona for prior-period coverage (PPC) reconciliation settlement revenue (contra-revenue) represents MHP's profit or loss in excess of 2 percent of capitation received for the population and is estimated based on the state's applicable policy. Because the reconciliation settlement is subject to change based on claims experience, there is a possibility that recorded reconciliation settlements will change by a material amount in the near term.

## Maricopa Health Plan (A Contract of Maricopa Integrated Health System)

### Notes to Financial Statements

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#### Note 2. Summary of Significant Accounting Policies (Continued)

Amounts due to (from) the State of Arizona for the Adults  $\leq$  106 percent of the Federal Poverty Level (Adults  $\leq$  106, formerly known as TWG) reconciliation settlement represents MHP's profit or loss for these members in excess of 2 percent for the population. For the contract years ended September 30, 2014 and 2015, MHP is no longer subject to reconciliation settlement on this population. For the contract year ended September 30, 2013, the Adults  $\leq$  106 reconciliation settlement represents MHP's profit or loss for these members in excess of 2 percent of capitation received for the nonmedical expense deduction (nonmed) population. Because the Adults  $\leq$  106 reconciliation settlement is subject to change based on claims experience, there is a possibility that recorded reconciliation settlements will change by a material amount in the near term.

Amounts due to (from) the State of Arizona for the Prospective Tiered reconciliation settlement represents MHP's profit or loss for the prospective members. For the contract years ended September 30, 2015 and 2014, this tiered reconciliation settlement represents 50 percent of MHP's profit for these members in excess of 3 percent to 6 percent and 100 percent of MHP's profit over 6 percent, or loss for these members in excess of 3 percent. Because the reconciliation settlement is subject to change based on claims experience, there is a possibility that recorded reconciliation settlements will change by a material amount in the near term.

Amounts due to (from) the State of Arizona for the Adults  $>$  106 percent of the Federal Poverty Level (Adults  $>$  106, formerly known as Newly Eligible Adults) reconciliation settlement represents MHP's profit or loss for the newly eligible adult members. For the contract years ended September 30, 2015 and 2014, the Adults  $>$  106 reconciliation settlement represents MHP's profit or loss for these members in excess of 1 percent of capitation. Because the Adults  $>$  106 reconciliation settlement is subject to change based on claims experience, there is a possibility that recorded reconciliation settlements will change by a material amount in the near term.

**PCP Parity cost settlement:** Section 1202 of the Affordable Care Act requires minimum levels of payment for certain primary care services (Primary Care Provider Parity or PCP Parity) provided by certain physicians for dates of service beginning January 1, 2013, through December 31, 2014. The enhanced reimbursement requirements for MHP are subject to reimbursement by the State of Arizona. PCP Parity cost settlement revenue represents reimbursement of eligible enhanced payment expenses incurred by MHP and reimbursable by the State of Arizona.

**Payment reform/shared savings program settlement:** AHCCCS has developed the payment reform policy with the intent to drive innovative arrangements that will further enhance cost control and result in quality improvements, while also offering providers incentive to participate in these arrangements. MHP is required to participate in these payment reform efforts as delineated by AHCCCS. For 2015, MHP has a payable to AHCCCS for approximately \$1,914,000 related to this policy.

**Administrative expenses:** Administrative expenses are recognized as incurred and consist of the management fee paid to the administrator of MHP (see Note 5). Up to February 28, 2015, UPH was the administrator of MHP. UPH merged with Banner Health on February 28, 2015, and Banner Health became successor to UPH in this management contract.

**Premium tax:** The State of Arizona imposes a premium tax on capitation payments paid to MHP by AHCCCS. MHP receives the premium tax from AHCCCS and remits the entire amount to the appropriate taxing authority. MHP includes the taxes collected as revenues and taxes remitted as an expense in the accompanying statements of revenues, expenses and changes in net position.

## Maricopa Health Plan (A Contract of Maricopa Integrated Health System)

### Notes to Financial Statements

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#### Note 2. Summary of Significant Accounting Policies (Continued)

**Income taxes:** As a governmental unit or a political subdivision thereof, MIHS is exempt from federal income tax under section 115(1) of the Internal Revenue Code. MIHS is also exempt from state income taxes. Accordingly, no provision is made for income taxes in the accompanying financial statements.

**Risk management:** MHP is exposed to various risks of loss from torts, business interruption, errors and omissions, and natural disasters. Commercial insurance coverage is purchased by MIHS for MHP for claims arising from such matters.

MHP receives reinsurance coverage from the State of Arizona to reduce the risk of catastrophic loss on services provided under the AHCCCS program. The gross capitation rates were reduced by the reinsurance cost. Under the state program, risk of loss for inpatient claims is generally limited to an annual deductible of \$25,000 per member, per policy year. Eligible claims in excess of the deductible are generally paid by the State at 75 percent to 85 percent, with no maximum annual benefit. Eligible reinsurance claims are reported in the accompanying financial statements as a reduction of health care expenses at the amount expected to be collected from AHCCCS.

**Subsequent events:** All of the effects of subsequent events that provide additional evidence about conditions that existed at the financial statement date, including the estimates inherent in the process of preparing the financial statements, are recognized in the financial statements. MHP does not recognize subsequent events that provide evidence about conditions that did not exist at the financial statement date but arose after, but before the financial statements are available to be issued. In some cases, nonrecognized subsequent events are disclosed to keep the financial statements from being misleading.

MHP made a \$3,500,000 capital contribution on behalf of MIHS in July 2015 to Maricopa Care Advantage (A Contract of Maricopa Integrated Health System).

MHP has evaluated events and transactions occurring subsequent to June 30, 2015, through October 21, 2015, the date of issuance of the financial statements. During this period, there were no events requiring recognition in the financial statements. Additionally, there were no nonrecognized subsequent events requiring disclosure, with the exception of the disclosure in the preceding paragraph.

#### Note 3. Medical Claims Payable

Medical claims liability consists of the following at June 30, 2015 and 2014:

	2015	2014
Claims payable or pending approval	\$ 13,967,153	\$ 14,480,970
Provisions for claims incurred but not yet reported	11,710,884	12,424,089
	<u>\$ 25,678,037</u>	<u>\$ 26,905,059</u>



## Maricopa Health Plan (A Contract of Maricopa Integrated Health System)

### Notes to Financial Statements

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#### Note 3. Medical Claims Payable (Continued)

The cost of health care services is recognized in the period in which care is provided and includes an estimate of the cost of services that has been incurred but not yet reported. MHP estimates accrued claims payable based on historical claims payments and other relevant information. Unpaid claims adjustment expenses are an estimate of the cost to process the incurred but not reported claims and are included in medical claims payable. Estimates are continually monitored and reviewed, and as settlements are made or estimates adjusted, differences are reflected in current operations. Such estimates are subject to the impact of changes in the regulatory environment and economic conditions. Given the inherent variability of such estimates, the actual liability could differ significantly from the amounts provided. While the ultimate amount of claims paid is dependent on future developments, management is of the opinion that the accrued medical claims payable is adequate.

The following is a reconciliation of the accrued claims liability for the years ended June 30, 2015 and 2014:

	2015	2014
Beginning balance	\$ 26,905,059	\$ 13,444,990
Incurred:		
Current	235,282,517	185,168,150
Prior	(696,764)	1,992,906
Total	<u>234,585,753</u>	<u>187,161,056</u>
Paid:		
Current	209,604,480	158,263,090
Prior	26,208,295	15,437,897
Total	<u>235,812,775</u>	<u>173,700,987</u>
Ending balance	<u>\$ 25,678,037</u>	<u>\$ 26,905,059</u>

Amounts incurred related to prior years vary from previously estimated liabilities as the claims are ultimately adjudicated and paid. Liabilities at any year-end are continually reviewed and re-estimated as information regarding actual claim payments becomes known. This information is compared to the originally established year-end liability. Negative amounts reported for incurred, related to prior years, result from claims being adjudicated and paid for amounts less than originally estimated. Positive amounts reported for incurred, related to prior years, result from claims being adjudicated and paid for amounts greater than originally estimated.

#### Note 4. Related-Party Transactions

MHP purchased hospitalization and medical compensation services from MIHS. During 2015 and 2014, MHP incurred claims to MIHS totaling approximately \$26,600,000 and \$25,000,000, respectively.

#### Note 5. Commitments and Contingencies

**Litigation:** MHP is party to various legal actions and is subject to various claims arising in the ordinary course of business. Management believes that the disposition of these matters will not have a material adverse effect on MHP's financial position or results of operations.

## Maricopa Health Plan (A Contract of Maricopa Integrated Health System)

### Notes to Financial Statements

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#### Note 5. Commitments and Contingencies (Continued)

**AHCCCS performance measures:** MHP's contract with AHCCCS requires MHP to be in compliance with certain financial and quality performance measures, as defined. During fiscal 2015, for the contract year ended September 30, 2014, and during fiscal year 2014, for the contract year ended September 30, 2013, management determined that MHP did not meet certain quality AHCCCS performance measures. In response to these violations, AHCCCS may require MHP to submit corrective action plans and subject MHP to sanctions. At June 30, 2015 and 2014, MHP has recognized a liability of \$176,000 and \$150,000, respectively, related to this contingency within other current liabilities. Due to the uncertainty of the outcome of AHCCCS' review, it is reasonably possible that recorded estimates will change by a material amount in the near term.

**Performance bond:** MIHS secured an annual performance bond on behalf of MHP in the amount of \$25,000,000 with an unrelated third-party insurance company to satisfy the performance bond requirement of MHP's AHCCCS contract. The bond satisfies MHP's contractual obligation as prescribed by AHCCCS. The current performance bond expires on September 30, 2016.

**Contract with Banner Health:** MHP has a management agreement with Banner Health through September 30, 2018, that provides for payments to Banner Health based on a percent of revenue, per month (as defined) as consideration for services rendered. Management fees to Banner Health are classified under administrative expenses in the statement of revenues, expenses and changes in net position.

**Health care regulatory environment:** The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, and reimbursement for patient services. Government activity has continued with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that MHP is in compliance with fraud and abuse, as well as other applicable government laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.