Audited Financial Statements and Other Supplementary Information

VHS Phoenix Health Plan, LLC
Year Ended June 30, 2013
With Report of Independent Auditors

Ernst & Young LLP

Ernst & Young

Ernst & Young LLP
One Nashville Place
Suite 1400
150 Fourth Avenue North
Nashville, TN 37219

Tel: +1 615 252 2000
Fax: +1 615 242 9128
www.ey.com

Report of Independent Auditors

The Board of Directors
VHS Phoenix Health Plan, LLC

We have audited the accompanying financial statements of VHS Phoenix Health Plan, LLC, a subsidiary of Vanguard Health Systems, Inc., which comprise the balance sheet as of June 30, 2013, and the related statement of earnings, member's equity, and cash flows for the year 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 conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of 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. 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.

Ernst & Young

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of VHS Phoenix Health Plan, LLC at June 30, 2013, and the results of its operations and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The details of the attached schedules (pages 20 through 28) of other supplementary information are presented for purposes of additional analysis and are not a required part of the financial statements. 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 not been subjected to the auditing procedures applied in our audit of the financial statements and, accordingly, we express no opinion on it.

Ernst + Young LLP

October 24, 2013

VHS Phoenix Health Plan, LLC

Balance Sheet

June 30, 2013

Assets	
Current assets:	
Cash and cash equivalents	$ 50,447,818
AHCCCS receivables	22,304,477
Prepaid expenses and other current assets	1,590,458
Due from affiliates, net	286,731,239
Total current assets	361,073,992
Property and equipment:	
Furniture and equipment	5,319,696
Software	2,874,379
Less: accumulated depreciation and amortization	(7,057,023)
Net property and equipment	1,137,052
Goodwill	79,402,908
Intangible assets, net	4,075,000
Total assets	$ 445,688,952
Liabilities and member's equity	
Current liabilities:	
Accounts payable	$ 4,920,100
Medical claims payable	66,810,700
Other accrued expenses	1,744,623
Total current liabilities	73,475,423
Other long-term liabilities	538,839
Member's equity:	
Member's capital	157,035,173
Retained earnings	214,639,517
Total member's equity	371,674,690
Total liabilities and member's equity	$ 445,688,952

See accompanying notes.

VHS Phoenix Health Plan, LLC

Statement of Earnings

Year Ended June 30, 2013

Revenues:	
Capitation	$ 522,255,662
Supplemental revenues	40,265,236
Other revenues	982,315
Total revenues	563,503,213
Expenses and losses:	
Hospital	114,687,981
Medical compensation	118,723,135
Other medical	258,334,238
	491,745,354
Less: reinsurance and third party liability	14,572,124
Total medical expenses	477,173,230
Administrative expenses	43,053,295
Realized loss on equity method investment	1,321,613
Total expenses and losses	521,548,138
Earnings before premium and income taxes	41,955,075
Premium taxes	11,340,994
Income taxes	10,716,118
Net earnings	$ 19,897,963

See accompanying notes

VHS Phoenix Health Plan, LLC

Statement of Member's Equity

Year Ended June 30, 2013

	Member's Capital	Retained Earnings	Total Member's Equity
Balance at July 1, 2012	$ 157,035,173	$ 194,741,554	$ 351,776,727
Net earnings	–	19,897,963	19,897,963
Balance at June 30, 2013	$ 157,035,173	$ 214,639,517	$ 371,674,690

See accompanying notes.

VHS Phoenix Health Plan, LLC

Statement of Cash Flows

Year Ended June 30, 2013

Operating activities	
Net earnings	$ 19,897,963
Adjustments to reconcile net earnings to net cash provided by operating activities:	
Depreciation and amortization	4,102,964
Deferred income taxes	(1,372,119)
Realized loss on investment	1,321,613
Changes in assets and liabilities:	
Increase in AHCCCS receivables	(11,818,968)
Decrease in prepaid expenses and other current assets	83,019
Increase in medical claims payable	4,831,106
Decrease in accounts payable	(176,467)
Decrease in other accrued expenses	(1,188,455)
Increase in other long-term liabilities	517,561
Net cash provided by operating activities	16,198,217
Investing activity	
Capital expenditures	(608,605)
Increase in equity method investment	(1,321,613)
Net cash used in investing activities	(1,930,218)
Financing activity	
Increase in due from affiliates	(25,313,585)
Decrease in cash and cash equivalents	(11,045,586)
Cash and cash equivalents, beginning of year	61,493,404
Cash and cash equivalents, end of year	$ 50,447,818

See accompanying notes.

1. Organization and Operations

VHS Phoenix Health Plan, LLC (the Company) is a wholly owned subsidiary of Abrazo Advantage Health Plan, Inc. (AAHP) and an indirect wholly owned subsidiary of Vanguard Health Systems, Inc. (Vanguard). Vanguard's subsidiaries and affiliates owned and operated 28 acute care hospitals with 7,081 licensed beds and related outpatient service locations complementary to the hospitals providing healthcare services in six states. Vanguard also owns or maintains an interest in certain outpatient diagnostic imaging and surgery centers, clinics, managed health plans, laboratory processing companies and billing companies affiliated with the hospitals. See Note 7 *Subsequent Events* for recent developments in regards to Vanguard's acquisition by Tenet Healthcare Corporation (Tenet).

The Company is a prepaid Medicaid managed health plan that derives substantially all of its revenues through a contract with the Arizona Health Care Cost Containment System (AHCCCS) to provide specified health services to qualified Medicaid enrollees through contracts with providers. AHCCCS is the state agency that administers Arizona's Medicaid program. The contract requires the Company to arrange for healthcare services for enrolled Medicaid patients in exchange for fixed monthly premiums, based on negotiated per capita member rates, reinsurance and other supplemental payments from AHCCCS.

The Company subcontracts with hospitals, physicians and other medical providers in Arizona to provide services to its enrollees in Apache, Coconino, Gila, Maricopa, Mohave, Navajo, Pima, Pinal, and Yavapai counties. These services are provided regardless of the actual costs incurred to provide the services. The Company receives reinsurance and other supplemental payments from AHCCCS to cover certain costs of healthcare services that exceed defined thresholds.

AHCCCS Contract

On March 22, 2013, the Company was notified that it was not awarded an acute care program contract with AHCCCS for the three-year period commencing October 1, 2013. However, on April 1, 2013, the Company agreed with AHCCCS on the general terms of a capped contract for Maricopa County for the three-year period commencing October 1, 2013. Enrollment would be limited to existing members (capped) effective October 1, 2013 and the enrollment cap will not be lifted at any time during the contract period, unless AHCCCS deems additional plan capacity necessary based upon growth in covered lives or other reasons as outlined in a letter provided by AHCCCS that clarifies certain terms of the capped contract.

1. Organization and Operations (continued)

Approximately 98,000 of the Company's members resided in Maricopa County as of June 30, 2013. Pursuant to the terms of the Company's agreement with AHCCCS, the Company will not file a protest of any of AHCCCS' decisions. AHCCCS has indicated that it intends to hold an open enrollment for the Company's members in Maricopa County sometime in calendar year 2014.

In determining the capitation rates for the contract period ending September 30, 2013, AHCCCS has utilized a national episodic/diagnostic risk adjustment model (RAM) that has been applied to all health plan specific capitation rates for prospective risk groups. Risk adjustment factors for the contract year ended September 30, 2012, were also used for the contract year ending September 30, 2013. The Company's management estimated that no RAM settlement was due for the contract year ended September 30, 2012.

The Company's contract is terminable without cause on 90 days' written notice from AHCCCS or for cause upon written notice from AHCCCS if the Company fails to comply with any term or condition of the contract or fails to take corrective action as required to comply with the terms of the contract. AHCCCS may also terminate the contract with the Company in the event of unavailability of state or federal funding. PHP can terminate the contract without cause. If the Company elected to terminate, the Company would be subject to various administrative guidelines which require the Company to assist AHCCCS in transitioning enrollees to coverage under a new health plan. Should AHCCCS terminate its contract with the Company, the Company would cease operations.

Member months, by geographic service area (GSA), covered by the Company during the month of June 2013, were as follows:

Maricopa	98,688
Gila/Pinal	31,159
Yavapai	23,362
Pima	15,422
Apache, Coconino, Mohave, and Navajo	18,129
	186,760

2. Summary of Significant Accounting Policies

Cash and Cash Equivalents

Cash equivalents include all highly liquid investments with an initial maturity of three months or less when purchased. At various times during the year, the Company's cash and cash equivalents balances exceeded the federally insured limit. Cash and cash equivalents are maintained at high quality financial institutions, and management believes exposure to credit risk is not significant.

AHCCCS Receivables

The Company had approximately $22,304,000 of receivables due from AHCCCS as of June 30, 2013, including reinsurance reimbursement receivable for amounts paid by the Company for enrollee healthcare services that exceeded maximum limits set forth in its contract with AHCCCS and other supplemental reimbursement receivables. The reinsurance reimbursement receivables are determined on an enrollee-specific basis and are stated at net realizable value. The Company writes off 100% of reinsurance receivables related to completed AHCCCS contract years that exceed the AHCCCS reinsurance timely filing limits.

Property and Equipment

Property and equipment are recorded at cost and depreciated using the straight-line method over the estimated useful life of the assets. The estimated useful lives of the Company's property and equipment range from three to eight years. Routine maintenance and repairs are charged to expense as incurred. Expenditures that increase values, change capacities or extend useful lives are capitalized. The Company recorded a non-cash increase to property and equipment for approximately $531,000 during the fiscal year ended June 30, 2013, related to an allocation of internal use software from a Vanguard affiliate.

Depreciation expense for property and equipment was approximately $80,000 for the year ended June 30, 2013, which is included in administrative expenses in the accompanying Statement of Earnings. The unamortized net book value of capitalized internal use software included in net property and equipment was approximately $981,000 as of June 30, 2013. Amortization expense for internal use software, included in depreciation and amortization expense, was approximately $763,000 for the fiscal year ended June 30, 2013.

2. Summary of Significant Accounting Policies (continued)

Revenues

The Company receives monthly capitation payments under the AHCCCS contract based on the number of enrollees and type of enrollee coverage. Capitation premiums are recognized as revenues in the month in which the Company is notified that a member is eligible for healthcare coverage provided by the Company. Included in these monthly payments are capitation amounts applicable to Title XIX Waiver Group (TWG) Members. The TWG Medical Expense Deduction (MED) population includes TWG members whose income exceeds the limits of all other Title XIX categories and have medical expenses that reduce income to at or below 40% of the federal poverty level. The TWG non-Medical Expense Deduction (Non-Med) population includes adults or childless couples at or below 100% of the federal poverty level (Non-Med) that do not meet the requirements of another categorically linked Title XIX program. For the year ended June 30, 2013, the Company recognized prospective capitation revenues of approximately $66,700,000 related to Title XIX Waiver Member enrollees. AHCCCS limits the profitability and loss that health plans may recognize for both the TWG prospective MED population and the TWG prospective Non-Med population.

The MED reconciliation limits the Company's profits or losses related to this population to 3% of related capitation revenues (net of reinsurance, administrative expenses, and premium taxes) as defined in the applicable AHCCCS contract. During the fiscal year ended June 30, 2013, the Company decreased its estimated MED settlement payable related to prior AHCCCS contract year's reconciliations by approximately $972,000 ($632,000, net of taxes). Additionally, during the fiscal year ended June 30, 2013, AHCCCS collected approximately $1,369,000 from the Company related to the MED reconciliation for contract year ended September 30, 2011.

The Non-Med reconciliation limits the Company's profits or losses related to this population to 2% of related capitation revenues (net of reinsurance, administrative expenses and premium taxes) as defined in the applicable AHCCCS contract for specific contract years. As of June 30, 2013, the Company had an estimated net TWG settlement payable of approximately $416,000, which is included in AHCCCS receivables on the accompanying Balance Sheet and relates to the contract years ending September 30, 2013 and prior.

2. Summary of Significant Accounting Policies (continued)

The Company is subject to a tiered prospective reconciliation for certain groups related to the contract year ending September 30, 2013, based upon prospective expenses and prospective net capitation. Populations subject to this tiered reconciliation are limited to Temporary Assistance to Needy Families (TANF), eligible pregnant women under Section 9401 of the Sixth Omnibus Budget and Reconciliation Act of 1986 (SOBRA), Supplemental Security Income (SSI) with Medicare, SSI without Medicare, and SOBRA Family Planning. Expenses incurred and revenues received for covered services with dates of service during Prior Period Coverage (PPC) are excluded from this reconciliation. As of June 30, 2013, PHP had no settlement payable or reconciliation for the tiered prospective reconciliation group.

The Company receives capitation payments for Prior Period Coverage (PPC) separately from its prospective capitation payments. PPC capitation payments are applicable to all types of enrollee coverages in the Company and are intended to cover those healthcare costs incurred by individuals while they are awaiting enrollment in the Company and prior to the Company's ability to manage the healthcare of those enrollees. PPC revenues are recognized in the month in which the Company is notified that a member is eligible for coverage provided by the Company. AHCCCS limits the profitability and loss that health plans may recognize during the PPC eligibility period to 2% of related capitation revenues (net of administrative expenses and premium taxes) and reconciles the PPC member costs incurred by the Company. For the year ended June 30, 2013, the Company recognized approximately $15,549,533 of PPC revenues, excluding PPC settlement estimates. As of June 30, 2013, the Company had a net settlement receivable for PPC costs incurred in excess of PPC payments received of approximately $11,281,000 for contract years ending September 30, 2013 and prior, which is included in AHCCCS receivables on the accompanying Balance Sheet.

The Company also receives supplemental payments for delivery premiums to cover the cost of maternity care for qualified members under the federally funded Sixth Omnibus Budget Reconciliation Act (SOBRA) program. The Company recognizes supplemental revenues during the month in which AHCCCS notifies the Company of payment.

Goodwill and Intangible Assets

As of June 30, 2013, the Company's intangible assets included the AHCCCS contract of $31,370,000 ($3,921,000 net of accumulated amortization) and provider network of $1,230,000 ($154,000 net of accumulated amortization). These intangible assets are reviewed for impairment as management becomes aware of impairment indicators.

2. Summary of Significant Accounting Policies (continued)

The AHCCCS contract and the provider network intangibles are being amortized over a period of 120 months. Amortization expense of intangible assets, excluding the amortization of internal use software, was $3,260,000 for the fiscal year ended June 30, 2013, and the estimated amortization expense during the subsequent fiscal years follows: 2014 – $3,260,000 and; 2015 – $815,000.

As of June 30, 2013, the Company had approximately $79,403,000 of goodwill. Goodwill and indefinite-lived intangible assets are evaluated annually for impairment during the fourth quarter or earlier upon the occurrence of certain events or substantive changes in circumstances. Goodwill is tested for impairment at a level referred to as a reporting unit. In assessing goodwill for impairment, the Company has the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the Company determines that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment review process is unnecessary. However, if the Company concludes otherwise or elects not to perform the qualitative assessment, then it is required to perform the first step of the two-step impairment review process.

In 2013, the Company elected not to perform a qualitative impairment assessment for goodwill but instead to complete the quantitative analysis. The first step of the quantitative two-step process involves a comparison of the Company's estimated fair value to its carrying amount, including goodwill. In performing the first step, the Company determines the fair value using a discounted cash flow (DCF) analysis. Determining fair value requires the exercise of significant judgment, including judgments about appropriate discount rates, perpetual growth rates and the amount, and timing of expected future cash flows. The significant judgments are typically based upon Level 3 inputs, generally defined as unobservable inputs representing the Company's own assumptions. The cash flows employed in the DCF analysis are based on the Company's most recent budgets and business plans and, when applicable, various growth rates are assumed for years beyond the current business plan period. Discount rate assumptions are based on an assessment of the risks inherent in the Company's future cash flows. If the Company's estimated fair value exceeds its carrying amount, the goodwill is not impaired and the second step of the impairment test is not necessary. The Company's 2013 annual impairment analysis did not result in any impairments of the Company's goodwill. Approximately $17,213,000 of the Company's goodwill is deductible for tax purposes.

2. Summary of Significant Accounting Policies (continued)

Due From Affiliates

Due from affiliates primarily represents the net excess of funds transferred to the centralized cash management account of Vanguard Health Management, Inc. (VHM), a wholly owned subsidiary of Vanguard, over funds transferred to or paid on behalf of the Company by VHM. Due from affiliates balances are readily available to the Company for settlement of its current liabilities as they become due.

Generally, this balance is decreased by automatic cash transfers from VHM's centralized cash management account to reimburse the Company's bank accounts for operating expenses and capital expenditures and to pay the Company's fees and services provided by VHM, including information systems services and other operating expenses, such as payroll, interest and insurance. Generally, the due from affiliates balance is increased through daily cash deposits by the Company to VHM's centralized cash management account. As of June 30, 2013, due from affiliates was reduced by approximately $3,065,000 related to cash overdrafts for disbursements from a bank account in which the Company does not have the right of offset.

Interest income of approximately $660,000 was earned by the Company on outstanding due from affiliates balances during the year ended June 30, 2013, which is included in other revenues in the accompanying Statement of Earnings. The Company earned interest income on amounts due from affiliates at a rate of less than 1.0% during the year ended June 30, 2013. The interest rate earned approximates the variable portion of the total interest rate paid by Vanguard under LIBOR contracts for its outstanding term loan debt. The Company also earned approximately $2,000 of interest income on its outstanding cash balances during the year ended June 30, 2013, which is included in other revenues in the accompanying Statement of Earnings.

Medical Expenses and Reinsurance Proceeds

Monthly capitation payments to primary care physicians and other healthcare providers are expensed in the month services are contracted to be performed. Claims expense for non-capitated arrangements are accrued as services are rendered by hospitals, physicians and other healthcare providers during the year. The Company is at risk for hospitalization and medical service claims, including medical compensation and other medical expenses, which exceed its capitation payments from AHCCCS. Medical compensation includes primary care and specialty physician services. Other medical expenses include hospital outpatient services and other ancillary services such as radiology and lab.

2. Summary of Significant Accounting Policies (continued)

The Company is reimbursed by AHCCCS for costs incurred for those enrollees with severe illnesses to the extent such costs exceed $35,000 per enrollee, including for Title XIX Waiver Group members for the contract year end September 30, 2013. The Company estimates reinsurance recoveries monthly based on reported claims by member and the provisions of the AHCCCS contract. Reinsurance recoveries are deducted from gross medical expenses on the accompanying Statement of Earnings. The Company is at risk for excess medical costs under reinsurance claims that are disputed and not honored by AHCCCS. As of June 30, 2013, the Company had an estimated reinsurance receivable of approximately $10,781,000, which is included in AHCCCS receivables on the accompanying Balance Sheet.

Medical claims payable includes claims received but not paid as well as estimated claims incurred but not reported (IBNR). During the fiscal year ended June 30, 2013, the Company reduced medical claims payable related to prior fiscal year health claims experience by approximately $2,121,000 ($1,300,000 net of taxes). Medical claims payable is estimated using a combination of historical claims payment data and current cost per member estimates. In order to test the reasonableness of its June 30, 2013, medical claims payable estimate, the Company engaged an actuary to provide an independent estimate of medical claims payable. While management believes that its estimation methodology captures trends in medical claims costs in a timely manner, actual payments could differ significantly from its estimates given changes in the healthcare cost structure or adverse experience.

Income Taxes

Vanguard files consolidated Federal and state income tax returns that include the operating results of the Company. Vanguard allocates taxes to the Company pursuant to the asset and liability method, as if the Company was a separate taxpayer. For balance sheet purposes, such allocations are deducted from due from affiliates in the accompanying Balance Sheet.

Fair Value of Financial Instruments

The carrying amounts of cash and cash equivalents, receivables, amounts due from affiliates and payables approximate fair value because of the short maturity of these financial instruments.

2. Summary of Significant Accounting Policies (continued)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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. Financial statement areas involving significant estimation include reinsurance receivables, PPC, MED, and Non-Med settlements, and medical claims IBNR. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and are accounted for in the period identified.

3. Realized Loss on Equity Method Investment

During the year ended June 30, 2013, the Company entered into a partnership agreement with Magellan Health Services of Arizona (Magellan) to serve the behavioral health population of Maricopa County. The Company had a 20% interest and utilized the equity method of accounting to record its share of the financial activity related to the partnership. The partnership was not awarded a contract for the behavioral health services in Maricopa County, and the partnership was terminated. Upon termination of the partnership, the Company realized a $1,322,000 loss on its equity method investment during the year ended June 30, 2013.

4. Transactions With Affiliates

Effective October 1, 2010, the Company entered into a management agreement with Advantage Health Care Management Company, Inc. (AHCMC), a wholly owned subsidiary of Vanguard, to manage the general and administrative functions related to the Company inclusive of payroll services, lease agreements and expenses, general and professional liability insurance coverages, advertising and related expenses. The Company has recorded expenses of approximately $40,269,000 for services provided by AHCMC. Expenses for AHCMC services are included in administrative expenses on the accompanying Statement of Earnings. At June 30, 2013, approximately $3,273,000 payable to AHCMC for services provided is included within the net amount due from affiliates on the accompanying Balance Sheet.

4. Transactions With Affiliates (continued)

Affiliates of the Company include healthcare service providers for eligible PHP members that are also affiliated with Vanguard. Medical services provided by these affiliates to eligible PHP members totaled approximately $23,457,000 during the year ended June 30, 2013. At June 30, 2013, medical claims payable included approximately $3,284,000 payable to these affiliates for medical services provided to the Company's enrollees.

5. Commitments and Contingencies

Operating Leases

As a result of the Company's management agreement with AHCMC, AHCMC assumed the remaining facility and equipment leases. The related rent expenses are included within the management fee charged by AHCMC, which is included in administrative expenses in the accompanying Statement of Earnings.

Professional, General, and Other Liability Insurance

In the normal course of business, the Company is subject to claims and lawsuits relating to injuries arising from patient treatment and denials thereof. The Company believes that its liability for damages resulting from such claims and lawsuits is adequately covered by insurance and is adequately provided for in its financial statements. The Company's contract with AHCCCS requires that it maintain professional liability insurance, comprehensive general insurance, and automobile liability insurance coverage of at least $1,000,000 for each occurrence. The Company is covered under Vanguard's wholly-owned captive insurance subsidiary or Vanguard's self-insurance program for professional and general liability claims. For professional and general liability claims incurred from June 1, 2002 through June 30, 2013, Vanguard's wholly owned captive subsidiary or other Vanguard subsidiaries insures the Company's professional and general liability risks at a $10,000,000 retention level. Vanguard carries professional and general liability insurance in excess of its self-insured retention and the captive insurance subsidiary's retention through unrelated commercial insurance carriers for aggregate claims up to $75,000,000, but limited to annual payments of $65,000,000 in the aggregate. There is no guarantee that existing coverage will be sufficient for professional and general liability claims either individually or in the aggregate. Professional and general liability insurance expense is no longer allocated from Vanguard and is included in the management fee charged by AHCMC. For the year ended June 30, 2013, the management fee is included in administrative expenses in the accompanying Statement of Earnings.

5. Commitments and Contingencies (continued)

The Company is covered under Vanguard's self-insurance program for workers' compensation claims. Vanguard maintains coverage for workers' compensation claims exceeding retention levels ranging from $1,000,000 to $1,250,000, which amounts the Company believes to be adequate. Workers' compensation insurance expense is included in the management fee charged by AHCMC for the year ended June 30, 2013, which is included in administrative expenses in the accompanying Statement of Earnings.

Vanguard maintains reserves for general and professional liability and workers' compensation risks and makes any necessary claims payments on the Company's behalf. Accordingly, no reserve for liability risks is recorded on the accompanying Balance Sheet. The Company is currently not a party to any such proceedings that, in management's opinion, would have a material adverse effect on the Company's business, results of operations or financial position.

Other Claims

The Company is subject to claims and suits arising in the ordinary course of business. Plaintiffs in these matters may request punitive or other damages that may not be covered by insurance. The Company is not aware that it is currently a party to any such proceeding that, in management's opinion, if adversely decided, would have a material effect on the Company's results of operations or financial position.

Subcontracted Services

The Company subcontracts with physician specialists, affiliated hospitals, and unaffiliated hospitals to provide covered services to certain patients enrolled in or assigned to the Company on either a capitated or fee-for-service basis.

AHCCCS Plan Compliance

Under the Company's contract with AHCCCS, the Company is required to maintain a performance guaranty. As of June 30, 2013, the Company maintained performance bonds totaling $40.0 million to meet this performance guaranty.

5. Commitments and Contingencies (continued)

The AHCCCS contract contains certain financial viability standards that the Company reports on a quarterly and annual basis. These standards enable AHCCCS to monitor the financial health of its contracted health plans. The Company must meet the financial viability standards, which include a current ratio requirement of at least one (1.0), equity per member requirement of at least $100, a medical expense ratio as defined in the AHCCCS contract (at least 84% for the contract year ended September 30, 2012, and 85% for the contract year ending September 30, 2013), and an administrative cost percentage ratio as defined in the AHCCCS contract (no more than 10%). AHCCCS does not automatically penalize or sanction health plans that do not meet these standards but, utilizes these guidelines in combination with other measures to determine the overall operational health and compliance of its contracted health plans. As of June 30, 2013, the Company met these financial viability standards.

The Company is also subject to minimum performance standards for certain clinical quality performance measures under its contract with AHCCCS. The Company accrues for potential sanctions based upon its estimated rate of non-compliance as reported by AHCCCS until such time that the Company is able to document compliance within the timeline to remedy the non-compliance established by AHCCCS. Management believes that possible additional sanctions beyond those already accrued related to contract years ending September 30, 2011, 2012, and 2013 as of June 30, 2013, would not be material to the financial position, results of operations or cash flows of the Company.

Compliance With Laws and Regulations

The healthcare 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 healthcare program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse regulations. Management believes that the Company is in compliance with fraud and abuse regulations as well as other applicable government laws and regulations. While no regulatory inquiries have been made, 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.

6. Income Taxes

Income tax expense allocated to the Company by Vanguard on a separate return basis for the year ended June 30, 2013, consisted of the following:

Current:	
Federal	$ 12,088,237
State	–
	12,088,237
Deferred:	
Federal	(1,372,119)
State	–
	(1,372,119)
	$ 10,716,118

The tax effects of temporary differences which give rise to deferred tax assets and liabilities at June 30, 2013, are as follows:

Depreciation, amortization and fixed asset basis differences	$ (5,176,170)
Excess book basis over tax basis of prepaid expenses	769,825
Discounted unpaid losses	325,314
Net deferred tax asset (liability)	$ (4,081,031)

Income tax expense allocated to the Company by Vanguard approximated the federal statutory rate for the year ended June 30, 2013. The tax effects of temporary differences that give rise to deferred tax assets and liabilities are included in due from affiliates in the accompanying Balance Sheet.

7. Subsequent Events

The Company has evaluated subsequent events for the year ended June 30, 2013 through October 24, 2013, the date these financial statements were available to be issued. On October 1, 2013, the Company's parent, Vanguard, completed a merger with Tenet. Pursuant to the merger, Vanguard became a wholly-owned subsidiary of Tenet and Vanguard's shares ceased to be traded on the New York Stock Exchange.