SOUTHWEST CATHOLIC
HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

CONSOLIDATED FINANCIAL STATEMENTS, ADDITIONAL INFORMATION AND UNIFORM GUIDANCE SUPPLEMENTAL REPORTS

Years Ended June 30, 2018 and 2017

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION dba MERCY CARE PLAN AND AFFILIATE

CONSOLIDATED FINANCIAL STATEMENTS, ADDITIONAL INFORMATION AND UNIFORM GUIDANCE SUPPLEMENTAL REPORTS

Years Ended June 30, 2018 and 2017

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

We have audited the accompanying consolidated financial statements of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate***, which comprise the consolidated statements of financial position as of June 30, 2018 and 2017, and the related consolidated statements of activities and changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate*** as of June 30, 2018 and 2017, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Supplemental Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate*** as a whole. The accompanying schedule of expenditures of federal awards, as required by Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principals and Audit Requirements for Federal Awards*, is presented for purposes of additional analysis and is not a required part of the consolidated 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 consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated 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 consolidated financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 5, 2018, on our consideration of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** internal control over financial reporting and on our tests of their compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** internal control over financial reporting and compliance.

Mayer Hoffman McCann P.C.

November 5, 2018

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

June 30, 2018 and 2017
(In thousands)

ASSETS

	2018	2017
CURRENT ASSETS		
Cash and cash equivalents	$ 258,945	$ 455,947
Short-term investments	47,312	31,775
Receivables:		
Reinsurance receivables, net of allowance for doubtful accounts of $13,017 and $19,142, respectively	14,392	21,239
Reconciliation receivables	46,347	8,821
Capitation and supplemental receivables	1,817	1,745
Pharmacy rebate receivable	26,478	16,030
Third-party liability receivable	4,824	4,685
Interest receivable	696	512
Provider advances, net of allowance for doubtful accounts of $1,313 and $1,334, respectively	8,191	6,538
Other receivables, net of allowance for doubtful accounts of $64 and $47, respectively	3,321	1,464
Risk share settlement, current portion	10,069	9,477
Due from AHCCCS	26,179	285
Due from Aetna	9,777	49
Prepaid assets	1,702	1,973
TOTAL CURRENT ASSETS	460,050	560,540
RESTRICTED SECURITIES	437	438
CAPITALIZED SOFTWARE COSTS, net	577	1,346
RISK SHARE SETTLEMENT, less current portion	2,309	2,309
LONG-TERM INVESTMENTS	241,683	183,738
TOTAL ASSETS	$ 705,056	$ 748,371

LIABILITIES AND NET ASSETS

	2018	2017
CURRENT LIABILITIES		
Claims payable	$ 271,940	$ 265,668
Payable to providers	28,034	28,823
Reconciliation payable	15,045	42,643
Due to AHCCCS	2	15,690
Due to Aetna	321	2,397
Deferred revenue	36,590	37,561
Risk share settlement payable	21,301	25,720
Other current liabilities	4,405	4,836
TOTAL CURRENT LIABILITIES	377,638	423,338
RISK SHARE SETTLEMENT PAYABLE, net of current portion	2,345	10,793
TOTAL LIABILITIES	379,983	434,131
UNRESTRICTED NET ASSETS		
Controlling interest	308,277	295,390
Noncontrolling interest - District	16,796	18,850
TOTAL UNRESTRICTED NET ASSETS	325,073	314,240
TOTAL LIABILITIES AND NET ASSETS	$ 705,056	$ 748,371

See Notes to Consolidated Financial Statements

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

CONSOLIDATED STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS

Years Ended June 30, 2018 and 2017
(In thousands)

	2018	2017
OPERATING REVENUES		
Capitation premiums	$ 3,809,443	$ 3,505,094
Delivery supplement	58,879	62,021
Other	8,446	8,583
TOTAL OPERATING REVENUES	3,876,768	3,575,698
HEALTH CARE EXPENSES		
Hospitalization	421,368	378,523
Medical compensation	374,905	350,394
Ancillary and other medical services	2,397,937	2,191,911
Institutional	207,371	182,891
Home and community based services	211,264	173,533
Less: reinsurance recoveries	(78,940)	(82,179)
TOTAL HEALTH CARE EXPENSES	3,533,905	3,195,073
GENERAL AND ADMINISTRATIVE EXPENSES	280,190	270,181
PREMIUM TAX EXPENSE	65,439	62,466
TOTAL EXPENSES	3,879,534	3,527,720
OPERATING INCOME (LOSS)	(2,766)	47,978
NONOPERATING INCOME (EXPENSE)		
Investment income	15,216	6,162
Investment fees	(1,171)	(772)
TOTAL NONOPERATING INCOME	14,045	5,390
CHANGE IN NET ASSETS PRIOR TO UNREALIZED GAINS (LOSSES) AND CHANGE IN NET ASSETS ATTRIBUTABLE TO DISTRICT	11,279	53,368
UNREALIZED GAINS (LOSSES) ON INVESTMENTS	(446)	4,839
CHANGE IN NET ASSETS PRIOR TO CHANGE IN NET ASSETS ATTRIBUTABLE TO DISTRICT	10,833	58,207
CHANGE IN NET ASSETS ATTRIBUTABLE TO DISTRICT	1,972	(1,449)
CHANGE IN NET ASSETS ATTRIBUTABLE TO CONTROLLING INTEREST	12,805	56,758
NET ASSETS, BEGINNING OF YEAR	314,240	256,033
NET ASSETS, END OF YEAR	$ 325,073	$ 314,240

See Notes to Consolidated Financial Statements

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended June 30, 2018 and 2017
(In thousands)

	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets prior to change in net assets attributed to District	$ 10,833	$ 58,207
Adjustments to reconcile change in net assets prior to change in net assets attributable to District to net cash (used in) provided by operating activities:		
Bad debt expense	3,647	8,266
Amortization expense	769	769
Net unrealized (gains) losses on investments	445	(4,841)
Net realized gains on investments	(6,838)	(2,930)
Net unrealized losses on restricted securities	1	2
Change in operating assets and liabilities:		
Decrease (increase) in:		
Reinsurance receivables	3,207	(12,391)
Reconciliation receivables	(37,526)	(1,041)
Capitation and supplemental receivables	(72)	1,506
Pharmacy rebate receivable	(10,448)	1,121
Third-party liability receivable	(139)	10
Interest receivable	(184)	(198)
Provider advances	(1,660)	383
Other receivables	(1,857)	(1,049)
Risk share settlement, net	(13,459)	13,457
Due from AHCCCS	(25,894)	9,019
Due from Aetna	(9,728)	1,377
Prepaid assets	271	6,291
Increase (decrease) in:		
Claims payable	6,272	18,783
Payable to providers	(789)	2,519
Reconciliation payable	(27,598)	(2,186)
Due to AHCCCS	(15,688)	(20,467)
Due to Aetna	(2,076)	(277)
Deferred revenue	(971)	31,893
Other current liabilities	(431)	23,925
Net cash (used in) provided by operating activities	(129,913)	132,148
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale of restricted securities	-	520
Purchase of restricted securities	-	(440)
Purchases of investments	(162,354)	(158,851)
Proceeds from sale of investments	95,265	76,552
Net cash used in investing activities	(67,089)	(82,219)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(197,002)	49,929
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	455,947	406,018
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 258,945	$ 455,947

See Notes to Consolidated Financial Statements

(1) Company operations and significant accounting policies

Company operations - Southwest Catholic Health Network Corporation dba Mercy Care Plan (SCHN, or the Plan) is a nonprofit corporation, whose sponsor organizations are Dignity Health (Dignity) and Carondelet Health Network (Carondelet), collectively the “sponsors.” SCHN provides medical care under various contracts with the Arizona Health Care Cost Containment System (AHCCCS), a department of the state of Arizona charged with administering health care for the state’s indigent population. SCHN provides medical coverage under the AHCCCS contract for the following populations:

- AHCCCS Acute - Members eligible under Title XIX Medicaid and Title XXI program requirements
- Arizona Long Term Care System (ALTCS) - Provide institutional care, home and community based services and behavioral health services to long term care members
- Arizona Department of Economic Security, Division of Developmental Disabilities (DES/DDD) - provide medical services to eligible members

Effective January 22, 2013, Mercy Maricopa Integrated Care (Mercy Maricopa), was incorporated in the State of Arizona with a dissolution date of the later of December 31, 2021 or six months after the expiration of the Regional Behavioral Health Authority (RBHA) contract. The initial members of Mercy Maricopa are SCHN, its two sponsor organizations Dignity and Carondelet, and Maricopa County Special Health Care District (District). The by-laws provide that Mercy Maricopa shall have one class of members initially; however, the current members may decide to create additional classes of membership or to add new members with unanimous consent of existing members. Relative interests of the members of Mercy Maricopa and the formula for distributions to members effective September 9, 2013 are as follows:

SCHN	85%
District	15%

The agreements also provide that SCHN serve as the managing member of Mercy Maricopa.

Mercy Maricopa was formed to provide physical and behavioral health care services on an integrated basis to Medicaid eligible adults with serious mental illness, and to operate as the RBHA to coordinate the delivery of health care services to eligible persons in Maricopa County, Arizona. Mercy Maricopa was initially funded through a $30 million capital contribution from SCHN and a $10 million capital contribution from District. SCHN contributed additional capital totaling $25 million during each of the years ended June 30, 2015 and 2014. No additional capital contributions were made during the years ended June 30, 2016, 2017 or 2018.

On March 25, 2013, Mercy Maricopa was awarded a $3 billion three year contract with the Arizona Department of Health Services (ADHS) to serve as the designated RBHA for the geographical service area (GSA) of Maricopa County. This new contract was to take effect October 1, 2013; however, the prior contract holder filed a legal challenge and requested and received a stay order requiring the contract to remain with the prior contract holder until the legal challenge had been decided. On December 3, 2013, the Deputy Director of the Arizona Department of Administration issued an Order affirming the Arizona Department of Health Services award of the GSA 6 Integrated Care RBHA contract to Mercy Maricopa effective April 1, 2014. Effective July 1, 2016 the contract with ADHS was transferred to AHCCCS. Mercy Maricopa’s contract with AHCCCS has been renewed through September 30, 2020. Subsequent to June 30, 2018, in connection with the merger described in Note 10, Mercy Maricopa’s AHCCCS contract was assumed by SCHN.

Mercy Maricopa is responsible for managing and maintaining an organized, comprehensive integrated healthcare delivery system for the benefit of eligible members within its assigned geographical service area.

(1) Company operations and significant accounting policies (continued)

SCHN operates a Medicare Advantage plan with the Centers for Medicare and Medicaid Services (CMS), offering medical and prescription drug benefits to qualified members. Medicare Advantage operates as a special needs plan under CMS guidelines. The populations covered under Medicare Advantage are members who are eligible for both Medicare and Medicaid coverage.

Mercy Maricopa also operated a Medicare Advantage Plan with CMS. Mercy Maricopa did not renew its Medicare Advantage Plan with CMS and discontinued the plan effective December 31, 2015. The results of the Mercy Maricopa Medicare Advantage Plan were minimal during fiscal year 2017 through the closure of the claims window on June 30, 2017.

SCHN has had a management agreement with Aetna since 2007, which is a continuation of the agreement held with Schaller Anderson, L.L.C. since 2001. The new contract became effective August 15, 2017 and continues through the expiration or termination of the Acute contract with AHCCCS effective October 1, 2018 and will automatically renew for a second five year term. Mercy Maricopa entered into a five year management agreement with Aetna effective May 1, 2013. The Mercy Maricopa agreement automatically renews for a second five year term and thereafter for successive one-year periods. Under the terms of the agreements, SCHN and Mercy Maricopa pay a monthly fee to Aetna, as defined in the agreement, to cover the employee salary and benefit costs and general and administrative expenses incurred to operate the organizations. SCHN and Mercy Maricopa incurred management fees per the management agreements of approximately $280,151,000 and $258,522,000 for the years ended June 30, 2018 and 2017, respectively. These amounts are included in general and administrative expenses in the accompanying consolidated statements of activities and changes in net assets. At June 30, 2018 and 2017, net unpaid management fees due to Aetna for SCHN and Mercy Maricopa totaled approximately $703,000 and $308,000, respectively, and are included in the net Due to Aetna in the accompanying consolidated statements of financial position.

SCHN's management agreement provides for a share of risk of the results of operations. Subject to certain performance measures, amounts will either be due from or due to Aetna. Additionally, the management agreement provides for supplemental compensation to be paid to Aetna upon meeting certain performance measures. At June 30, 2018, the amount due from Aetna includes $10,000,000 for the share of risk related to the Plan's performance. At June 30, 2017, Due to Aetna included $2,000,000 of supplemental compensation measured based on the performance of the Plan. Mercy Maricopa's management agreement does not provide for a share of the risk of the results from operations.

The significant accounting policies followed by SCHN and Mercy Maricopa, collectively referred to in these consolidated financial statements as the "Company", are summarized below:

Consolidation policy - The consolidated financial statements include the accounts of SCHN and Mercy Maricopa. The Company reports noncontrolling interests in consolidated entities as a component of unrestricted net assets. For purposes of consolidation, all significant intercompany balances and transactions have been eliminated in consolidation.

Basis of presentation - The accompanying consolidated financial statements have been prepared in accordance with Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) 954-205, *Health Care Entities - Presentation of Financial Statements*. The Company's consolidated financial statements are also presented in accordance with FASB ASC 958-205, *Not-for-Profit Entities - Presentation of Financial Statements.* Under FASB ASC 958-205, the Company is required to report information regarding their consolidated financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. As of June 30, 2018 and 2017, there were no temporarily restricted or permanently restricted net assets.

(1) Company operations and significant accounting policies (continued)

Management's use of estimates - The preparation of the consolidated 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 disclosures of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. A material estimate potentially susceptible to change in the near term relates to the claims payable liability.

Cash and cash equivalents - Cash includes cash deposits in banks and cash equivalents. The Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents. Amounts at each institution are insured in limited amounts by the Federal Deposit Insurance Corporation (FDIC).

Capitation premiums - The Plan receives from AHCCCS, DES/DDD and CMS fixed capitation payments, generally in advance, based on certain rates for each member enrolled with the Plan. The Plan is required to provide all covered health care services to their members, regardless of the cost of care. If there are funds remaining, the Plan retains the funds as profit; if the costs are higher than the amount of capitation payments, the Plan absorbs the loss. Capitation premiums are recognized in the month that enrollees are entitled to health care services. Certain provisions of the AHCCCS Acute, DES/DDD and ALTCS contracts include a risk band whereby SCHN and the AHCCCS programs share in the profits and losses of the contract, as defined in the respective contracts (reconciliation revenue). SCHN has recorded an estimate of the reconciliation revenue, within capitation premiums, based on the operational performance of the AHCCCS Acute, DES/DDD and ALTCS lines of business. The Plan may recover certain losses for those cases eligible for reinsurance payments. Premiums received prior to the month of service included in deferred revenue as of June 30, 2018 and 2017 totaled $36,127,000 and $33,765,000, respectively.

Capitation is paid prospectively as well as for prior period coverage (PPC) under the AHCCCS Acute and ALTCS contracts. The PPC period is the period of time prior to the member's enrollment, during which a member is eligible for covered services. The timeframe is from the effective date of eligibility to the day a member is enrolled with a contractor. The risk under PPC is shared by both the Plan and AHCCCS for the contract years ended September 30, 2018 and 2017. AHCCCS reconciles the actual PPC medical costs to the PPC capitation paid during the contract year.

The Plan shares risk with AHCCCS and DES/DDD for specific populations as follows:

- Acute Prospective
- Acute Prior Period Coverage
- Adult Group above 106% Federal Poverty Level (formerly known as the Newly Eligible Adults Prospective and Prior Period Coverage)
- ALTCS Prior Period Coverage
- Home and Community Based Services
- Share of Cost

(1) Company operations and significant accounting policies (continued)

Profits in excess of the percentages set forth by the contract will be recouped by AHCCCS. Losses in excess of the percentages set forth by the contract will be paid to the contractor. As of June 30, 2018, the Company has recorded an estimated receivable from AHCCCS of approximately $46,347,000 and an estimated payable to AHCCCS of approximately $15,045,000 which is included in reconciliation receivables and reconciliation payable, respectively. Additionally, as of June 30, 2017, the Company recorded an estimated receivable from AHCCCS of approximately $8,821,000 and an estimated payable of approximately $42,643,000 to AHCCCS which is included in reconciliation receivables and reconciliation payable, respectively. Reconciliation receivable and payable amounts pertaining to separate contracts cannot be offset against reconciliation receivable and payable balances of a different contract, and as such, amounts have been presented separately as a payable and receivable balance on the accompanying consolidated statements of financial position.

AHCCCS subjects 1% of gross prospective capitation of Acute contractors in Arizona to measurements based on each contractor’s performance on selected Quality Management Performance Measures as determined by AHCCCS. The program is an effort to encourage activity for AHCCCS contractors in the area of quality improvement, particularly those initiatives that are conducive to improved health outcomes and cost savings. As of June 30, 2018 and 2017, the Plan anticipates achieving the required targets and accordingly, has not recorded a liability for the performance measures.

Capitation and supplemental and reconciliation receivables are stated at the amount management expects to collect. Management provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual balances. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to capitation and supplemental and reconciliation receivables. Capitation and supplemental and reconciliation receivables at June 30, 2018 and 2017 are considered by management to be fully collectible and, accordingly, an allowance for doubtful accounts has not been provided.

Mercy Maricopa receives substantially all of its revenue from its contract with AHCCCS. Operating revenue includes funding in the form of capitation revenue, which is recognized over the applicable coverage period on a per member basis for covered members. Under this arrangement, Mercy Maricopa is paid a per member fee for all enrolled members, and this fee is recorded as revenue in the month in which members are entitled to services. Any fees received prior to the month of service are recorded as deferred revenue. Capitation and other revenues from AHCCCS totaled approximately $1,276,173,000 and $1,171,836,000 for the years ended June 30, 2018 and 2017, respectively.

The AHCCCS contract is partially funded by state, county and block grants (non-title revenue), which represent annual appropriations. Mercy Maricopa recognizes revenue from this funding ratably over the period to which the funding applies. Non-Title revenues, including block grants, totaled approximately $148,396,000 and $141,213,000 for the years ended June 30, 2018 and 2017, respectively.

Deferred revenue consists of grant payments from multiple grantors which exceeded the amounts earned by Mercy Maricopa. Deferred revenue for Mercy Maricopa totaled approximately $463,000 and $3,795,000 at June 30, 2018 and 2017, respectively.

(1) Company operations and significant accounting policies (continued)

Mercy Maricopa's AHCCCS contract revenue is limited by the terms of the AHCCCS contract to a maximum profit/loss percentage. Profits and losses related to capitation payments from AHCCCS have a maximum percentage able to be recognized under the contract, and as a result any profits or losses greater than this limit will result in a Due to AHCCCS or a Due from AHCCCS, respectively. The Title XIX/XXI capitation profits and losses are considered on a contract year which runs from October through September. For the contract periods April 1, 2014 through September 30, 2015 and October 1, 2015 through September 30, 2016, the maximum profit/loss limit was four percent. For the contract period October 1, 2016 through September 30, 2017, the maximum profit/loss percentage was decreased to one percent. For the contract period October 1, 2017 through September 30, 2018, the maximum profit percentage was increased to four percent and the maximum loss was decreased to one half of one percent. Any contract periods not described below had results which were within the allowable profit/loss percentages within the respective contract period and no amounts were recorded as Due to or Due from AHCCCS. Under Title XIX/XXI, Mercy Maricopa also makes payments to providers upon completion of contracted goals/measures in accordance with the Value Based Purchasing ("VBP") strategy selected for the contract. This is a non-encounterable payment and does not reflect payment for direct medical service to a member. Payment is reimbursed by AHCCCS after the completion of the contract period in recognition of successful performance measurement. These expected reimbursements were recorded within Due from AHCCCS. The Non-Title profits and losses are considered on a state fiscal year which runs from July through June. Profits related to non-title revenue have a maximum percentage able to be recognized, and as a result any profits greater than this limit will result in a Due to AHCCCS. Losses under the non-title portion of the contract will not be reimbursed by AHCCCS.

At June 30, Mercy Maricopa's Due to AHCCCS included the following amounts related to the applicable profit/loss corridor:

	2018	2017
Contract Year:		
Title XIX/XXI - April 1, 2014 through September 30, 2015	$ -	$ 12,412,226
Non-Title - October 1, 2016 through September 30, 2017	-	3,278,328
Balance at June 30	$ -	$ 15,690,554

At June 30, the Due from AHCCCS included the following amounts related to the applicable profit/loss corridor:

	2018	2017
Contract Year:		
Title XIX/XXI – October 1, 2016 through September 30, 2017	$ (1,473,725)	$ -
Title XIX/XXI – October 1, 2017 through September 30, 2018	5,725,681	-
Balance at June 30	$ 4,251,956	$ -

At June 30, the Due from AHCCCS also included the following amounts related to the applicable VBP Strategy:

	2018	2017
Contract Year:		
Title XIX/XXI – October 1, 2016 through September 30, 2017	$ 2,600,911	$ -
Title XIX/XXI – October 1, 2017 through September 30, 2018	9,673,835	-
Balance at June 30	$ 12,274,746	$ -

(1) Company operations and significant accounting policies (continued)

Mercy Maricopa's Due to AHCCCS related to the contract year ended September 30, 2015 was dismissed by AHCCCS in fiscal year 2018 and was recognized as revenue. The Due to AHCCCS related to the contract year ended June 30, 2017 was eliminated in fiscal year 2018 as a result of further runout of claims which resulted in the contract year no longer having a profit greater than the applicable limit. As of June 30, 2018, for the contract year ended September 30, 2017, as a result of further runout of claims, Mercy Maricopa recorded an estimated Due from AHCCCS of $1,127,186.

At June 30, 2018, in addition to the amounts noted above, Mercy Maricopa's Due from AHCCCS included approximately $9.65 million due for the provision of housing and other services, reimbursement payments related to the Arizona Opioid State Targeted Response grant and capitation payments under Mercy Maricopa's contract. At June 30, 2017, due from AHCCCS consisted primarily of amounts due for the provision of housing and other services. The receivables are stated at the amount management expects to collect. Mercy Maricopa establishes an allowance for doubtful accounts, if necessary, based upon factors including credit risk, historical trends, and other information. As of June 30, 2018 and 2017, amounts due from AHCCCS are considered by management to be fully collectible and, accordingly, an allowance for doubtful accounts has not been provided.

Due from AHCCCS - At June 30, 2018, due from AHCCCS consists of approximately $16,631,000 of amounts due for the profit/loss reconciliations described above, as well as $9,474,000 related to the provisions of housing and other services and for capitation payments under Mercy Maricopa's contract. At June 30, 2017, Due from AHCCCS consists of $285,000 related to the provision of housing and other services. The receivables are stated at the amount management expects to collect. Mercy Maricopa establishes an allowance for doubtful accounts, if necessary, based upon factors including credit risk, historical trends, and other information. As of June 30, 2018 and 2017, amounts Due from AHCCCS are considered by management to be fully collectible and, accordingly, an allowance for doubtful accounts has not been provided.

Delivery supplement - As part of the AHCCCS Acute Care contract, AHCCCS supplements capitation premiums with lump-sum payments for births by women eligible under the Medicaid program. This delivery supplement represents childbirth delivery reimbursement which is recorded when the delivery occurs. Delivery revenue of approximately $58,879,000 and $62,021,000 was recognized for the years ended June 30, 2018 and 2017, respectively. As of June 30, 2018 and 2017, approximately $593,000 and $462,000 was due from AHCCCS related to delivery supplement, respectively, which is included in capitation and supplemental receivables in the accompanying consolidated statements of financial position.

Premium taxes - SCHN is subject to a 2% tax on all payments received from AHCCCS for premiums, reinsurance, and reconciliations. Mercy Maricopa is subject to a 2% premium tax on all payments received from AHCCCS for premiums, reinsurance, and reconciliations which are remitted by Mercy Maricopa directly to the Arizona Department of Insurance (ADOI).

Reinsurance - AHCCCS and DES/DDD provide a stop-loss reinsurance program for the Plan for partial reimbursement of reinsurable covered medical services incurred for members. The program includes a deductible, which varies based on the Plan's enrollment and the eligibility category of the members. AHCCCS and DES/DDD reimburse the Plan based on a coinsurance amount for reinsurable covered services incurred above the deductible. SCHN contracts with commercial reinsurers to provide reinsurance for the Medicare Advantage Plan. Reinsurance recoveries are stated at the actual and estimated amounts due to SCHN and Mercy Maricopa pursuant to the AHCCCS Acute, DES/DDD, ALTCS and Medicare Advantage Plan contracts. Reinsurance recoveries have been offset against health care expenses in the accompanying consolidated statements of activities and changes in net assets.

(1) Company operations and significant accounting policies (continued)

Below are the reinsurance thresholds by line of business:

Line of Business	Annual Deductible Effective October 1, 2017	Annual Deductible Effective October 1, 2016	Coinsurance
AHCCCS Acute – Prospective Only	$ 25,000	$ 25,000	75%
DES/DDD	50,000	50,000	75%
ALTCS w/Medicare	20,000	20,000	75%
ALTCS w/o Medicare	30,000	30,000	75%

Line of Business	Annual Deductible Effective January 1, 2018	Annual Deductible Effective January 1, 2017	Coinsurance
SCHN Medicare Advantage	$ 700,000	$ 700,000	90%

Line of Business	Annual Deductible Effective April 1, 2015	Coinsurance
Mercy Maricopa Medicare Advantage and certain SMI membership– effective April 1, 2015 through September 30, 2018	$ 500,000	90%

To be eligible for reinsurance billing, qualified healthcare expenses must be incurred during the contract year. Reinsurance is recorded based on actual billed reinsurance claims adjusted for medical cost completion factors and historical collection experience. Reinsurance is subject to review by AHCCCS, DES/DDD, and the Medicare Advantage Plan's commercial reinsurer, and as a result, there is at least a reasonable possibility that recorded reinsurance will change by a material amount in the near future.

Reinsurance receivables represent the expected payment from AHCCCS, DES/DDD, and the Medicare Advantage Plan's commercial insurer to the Company for certain enrollees whose qualifying medical expenses paid by the Company were in excess of specified deductible limits. Reinsurance receivables are stated at the amount management expects to collect. Management provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual balances. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to reinsurance receivables. At June 30, 2018 and 2017, gross reinsurance receivables totaled approximately $27,350,000 and $40,381,000, for SCHN and $59,000 and $0 for Mercy Maricopa, respectively. SCHN also had an allowance for doubtful accounts of approximately $13,017,000 and $19,142,000 at June 30, 2018 and 2017, respectively.

(1) Company operations and significant accounting policies (continued)

Pharmacy rebate receivable - The Company receives rebates from pharmaceutical companies based on the volume of drugs purchased. The Company records a receivable and a reduction of health care expenses for estimated rebates due based on purchase information. During the years ended June 30, 2018 and 2017, health care expenses were reduced by approximately $31,565,000 and $26,444,000 for rebates, respectively. At June 30, 2018 and 2017, management believes the pharmacy rebate receivable is fully collectible and accordingly, an allowance has not been established.

Third-party liability receivable - In cases such as motor vehicle accidents and worker's compensation claims, a third-party insurer may be liable for a claim. When SCHN pays claims on behalf of its members and determines a third-party insurance company is ultimately responsible for that claim, it estimates a receivable and recoups the claim cost from the third-party insurer. SCHN has hired an asset recovery company to manage the third-party receivable collections. Third-party liability receivables are stated at the amount management expects to collect and is compared to the annual recoveries received. Recovery rates are updated periodically and confirmed by the vendor. At June 30, 2018 and 2017, gross third-party liability receivables totaled approximately $4,824,000 and $4,685,000, respectively. Third-party liability receivables at June 30, 2018 and 2017 are considered by management to be fully collectible, accordingly, an allowance for doubtful accounts has not been provided.

Provider advances - Upon request, SCHN and Mercy Maricopa may advance monies to high-volume providers based on cash flow needs and timing of claims payments. Advances are stated at the amount management expects to collect or offset against future claims. Advances are non-interest bearing and are expected to be settled within 12 months. Management provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual balances. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowances and a credit to provider advances receivable. At June 30, 2018 and 2017, SCHN gross provider advances receivable totaled approximately $7,284,000 and $5,838,000, respectively. SCHN had an allowance for doubtful provider advances of approximately $343,000 and $1,127,000 at June 30, 2018 and 2017, respectively. Mercy Maricopa's gross provider advance receivable balances were approximately $2,220,000 and $2,034,000 at June 30, 2018 and 2017, respectively. Mercy Maricopa had an allowance for doubtful accounts of approximately $970,000 at June 30, 2018 and $207,000 for 2017.

Risk share settlement - The risk share settlement receivable represents the CMS risk adjustment for the Medicare Advantage, Medicare Part C, enrollees. CMS performs a risk adjustment each year using health status indicators to correlate payment to the health acuity of the member and consequently establish incentives for plans to enroll and treat less healthy Medicare beneficiaries. Management estimates the expected impact from the CMS rate risk adjustment on the Plan's enrolled population for each contract year. As of June 30, 2018 and 2017, the Plan has recorded an estimated current receivable from CMS of approximately $10,069,000 and $9,477,000, respectively. Risk share settlement receivables at June 30, 2018 and 2017 are considered by management to be fully collectible, accordingly, an allowance for doubtful accounts has not been provided.

(1) Company operations and significant accounting policies (continued)

Management estimates expected risk share settlements to be paid to or received from CMS in connection with the pharmacy component of Medicare Advantage, Medicare Part D. This balance is reviewed and monitored by management and adjusted as necessary as experience develops or new information becomes available. Such adjustments are netted against the capitation premiums on the consolidated statements of activities and changes in net assets. Amounts recorded under this program totaled approximately $9,881,000 and $9,032,000 for the years ended June 30, 2018 and 2017, respectively, which are included as capitation premiums in the accompanying consolidated statements of activities and changes in net assets. As of June 30, 2018, the Plan recorded $12,171,000 for Medicare Part D settlements relating to contract years 2018 and 2017. The pharmacy risk share settlements for calendar years 2018 and 2017 are expected to be finalized in late 2018. As of June 30, 2017, the Plan recorded $10,739,000 for Medicare Part D settlements due to CMS relating to contract years 2017 and 2016. The estimate for contract year 2016 was settled in November 2017 for $8,278,000. The risk share settlements for Medicare Part D are included in risk share payable in the accompanying consolidated statements of financial position. As of June 30, 2017, $8,448,000 of the Medicare Part D estimated settlements were presented as a long term risk share settlement payable based on the expected timing of final settlement.

The pharmacy risk share settlement for calendar year 2013 remains open and is presented as a long-term receivable totaling $2,309,000 as of June 30, 2018 and 2017. The risk share settlement receivable balance is considered by management to be fully collectible and, accordingly, an allowance for doubtful accounts has not been provided. Collection of the balance is anticipated in 2019. A corresponding long-term risk share settlement payable of $2,345,000 has been recorded by the Plan as of June 30, 2018 and 2017, representing the amount to be paid to Aetna once collection of the 2013 contract year settlement is received by the Plan.

AHCCCS at times performs a review of the Medicaid program rates for its enrollees and assesses the appropriateness of rates applied to services for those enrollees. The risk adjustment of capitation payments modifies revenue to contractors based on the health status of their covered population relative to the average health status of the population. To estimate the impact to its capitation rates for the open contract years, the Plan performed an analysis of the impact of the published rate change for its enrolled populations based on member months during those years. As of June 30, 2017, the Plan recorded estimated amounts payable to AHCCCS for the risk adjustment of $10,158,000 for contract year 2017 and $13,271,000 for contract year 2016 which were included in risk share settlement payable in the accompanying consolidated statement of financial position. AHCCCS recouped $13,271,000 for contract year 2016 in August 2017 and recouped $22,570,000 for contract year 2017 in June 2018. As of June 30, 2018, the Plan has recorded an estimated payable to AHCCCS for risk adjustment of $9,130,000 for contract year 2018 which is included in risk share settlement payable in the accompanying consolidated statement of financial position.

Premium deficiency reserve - The Company evaluates possible losses on its contracts through the end of each contract year. If necessary, a premium deficiency reserve is recorded within claims payable on the consolidated statements of financial position. For the years ended June 30, 2018 and 2017, SCHN recorded no premium deficiency reserve for probable losses within its contracts. Mercy Maricopa had no estimated amounts recorded for premium deficiency reserves as of June 30, 2018 and 2017.

Healthcare service cost recognition - The costs of providing hospitalization, medical compensation, ancillary and other medical services, institutional, and home and community based services are accrued in the period in which the service is provided to eligible recipients based in part on estimates, including an accrual for services incurred but not yet reported.

(1) Company operations and significant accounting policies (continued)

Mercy Maricopa contracts with various providers for the provision of a full range of integrated healthcare services to eligible adults and children for Title XIX, Title XXI, and Non-Title programs, and physical healthcare services to Seriously Mental Ill Title XIX eligible adults. Healthcare services are purchased under fee-for-service or block purchase arrangements. Fee-for-service contract expenses are accrued as incurred. Healthcare services provided under block purchase arrangements are accrued based upon contract terms. From time to time, Mercy Maricopa amends the provider contracts. The effects of these amendments are recorded in the period in which the amendment was executed.

The Company's estimates for unreported claims payable is developed using actuarial methods based on historical experience and are continually reviewed by management and adjusted as necessary based on current claims data, and medical cost completion factors. Such adjustments are included in health care expenses in the consolidated statements of activities and changes in net assets in each period when necessary. While management believes the amount is adequate, the ultimate liability may be in excess of or less than the amount provided. There is at least a reasonable possibility that the recorded estimates will change by a material amount, in the near future.

As part of AHCCCS' Alternative Payment Model (APM) (formerly Value-Based Purchasing Initiative), and in accordance with the AHCCCS contract, Mercy Maricopa has agreements with certain providers that provide for the establishment of a pool into which Mercy Maricopa places funds based on the performance of the provider as defined in the contract. Mercy Maricopa manages the disbursement of the funds from this account as well as reviews the utilization and designated quality scores based on members assigned to the provider. Mercy Maricopa APM expense totaled approximately $5,920,000 and $16,054,000 for the years ended June 30, 2018 and 2017, respectively, and are included within health care expenses in the accompanying consolidated statements of activities and changes in net assets. Mercy Maricopa accrued approximately $13,686,000 and $10,743,000 as of June 30, 2018 and 2017, respectively, which is included in payable to providers in the accompanying consolidated statements of financial position for this program. Similar APM requirements are included in SCHN's contracts with AHCCCS, CMS and DES/DDD. SCHN APM expense totaled $15,743,000 and $9,439,000 for the years ended June 30, 2018 and 2017, respectively, and are included within health care expenses in the accompanying consolidated statements of activities and changes in net assets. SCHN has accrued approximately $8,622,000 and $7,981,000 as of June 30, 2018 and 2017, respectively, which is included in payable to providers in the accompanying consolidated statements of financial position for these incentives.

Payable to providers - Mercy Maricopa compensates providers for authorized healthcare and substance abuse services to covered beneficiaries. Mercy Maricopa used a variety of methods to estimate the amount payable to providers including authorization for services to be provided, payments to be made under contract arrangements currently in force, and correspondence with significant providers to ascertain the level of care being provided to beneficiaries for which a claim has not yet been submitted.

Investments and restricted securities - Investments and restricted securities are recorded in accordance with FASB ASC 958-320, *Investments-Debt and Equity Securities*. Under FASB ASC 958-320, the Company reports investments in equity securities that have readily determinable fair values, and all investments in debt securities at fair value based on quoted market prices. Investment securities without quoted market prices are valued at estimated fair value using appropriate valuation methods that consider the underlying assets. The Company's investment portfolio is managed by professional investment managers within guidelines established by the Company's Board of Directors which, as a matter of policy, limits the amounts which may be invested in any one issuer or type of investment.

(1) Company operations and significant accounting policies (continued)

Investment securities in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the near term could materially affect account balances and the amounts reported in the accompanying consolidated financial statements.

At July 1, 2016, restricted securities consisted of U.S. Treasury notes held by a bank required to remain in trust by the State of Arizona, Department of Insurance (ADOI) for the duration of Mercy Maricopa's contract with AHCCCS. As of March 2017, this security was no longer required due to the surrender of Mercy Maricopa's Health Care Services Organization license with ADOI. The ADOI did require a security deposit for remaining claims on the Medicare Advantage Plan. At June 30, 2018 and 2017, the security deposit consists of a U.S. Treasury note held by a bank in trust by the State of Arizona. Mercy Maricopa may not make withdrawals on the account without prior approval from the ADOI. The purchases and sales of restricted securities are recorded on a trade-date basis. Interest is recognized on the accrual basis.

Fair value measurements - FASB ASC 820, *Fair Value Measurements*, establishes a common definition for fair value to be applied to accounting principles generally accepted in the United States of America requiring use of fair value, establishes a framework for measuring fair value, and expands disclosures about such fair value measurements. FASB ASC 820 also establishes a hierarchy for ranking the quality and reliability of the information used to determine fair values by requiring that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

Level 1: Unadjusted quoted market prices in active markets for identical assets or liabilities.

Level 2: Unadjusted quoted prices in active markets for similar assets or liabilities, unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices that are observable for the asset or liability.

Level 3: Unobservable inputs for the asset or liability.

Investment income - Investment income consists of interest, dividends, and realized gains and losses on investments. Interest is recognized on the accrual basis, and dividends are recorded as earned on the ex-dividend date. Interest income on mortgage-backed and asset-backed securities is determined on the effective yield method based on estimated principal repayments. Accrual of income is suspended for bonds and mortgage loans that are in default or when the receipt of interest payments is in doubt. Accrual of income has not been suspended for any bonds or mortgage loans during the years ended June 30, 2018 and 2017. The Company has a policy to review and identify investments with declines in value that would be considered to be other-than-temporary. Such other-than-temporary declines, if significant, are accounted for as realized losses (See Note 3).

Capitalized software costs - Research and development costs are charged to expense as incurred. However, the costs incurred for the development or purchase of computer software that relate to the implementation of the claims processing system are capitalized when technological feasibility has been established. These capitalized costs are subject to an ongoing assessment of recoverability based on anticipated useful lives and changes in hardware and software technologies. Costs that are capitalized include direct labor and related overhead.

(1) Company operations and significant accounting policies (continued)

Amortization of capitalized software development costs begins when the product is available for release and installation. Amortization is provided on a straight-line method over periods not exceeding five to seven years. Unamortized capitalized software development costs determined to be in excess of net realizable value of the product is expensed immediately. Capitalized software cost totaled approximately $3,845,000 at June 30, 2018 and 2017. Effective April 1, 2014, the software was completed and placed into service, at which time Mercy Maricopa commenced amortization. Amortization expense totaled approximately $769,000 for each of the years ended June 30, 2018 and 2017. Accumulated amortization was approximately $3,268,000 and $2,499,000 as of June 30, 2018 and 2017, respectively.

Income taxes - SCHN and Mercy Maricopa qualify as tax exempt organizations under Section 501(c)(3) of the Internal Revenue Code (the Code) and, therefore, there is no provision for income taxes included in the accompanying consolidated financial statements. Income determined to be unrelated business taxable income would be taxable.

FASB ASC 740-10, *Income Taxes*, relates to the accounting for uncertainty in income taxes which requires the application of a “more likely than not” threshold recognition and de-recognition of uncertain tax positions in operations in the year of such change. The Company evaluates their uncertain tax positions, if any, on a continual basis through review of their policies and procedures, review of their regular tax flings, and discussions with outside experts. At June 30, 2018 and 2017, the Company did not have any uncertain tax positions.

SCHN and Mercy Maricopa’s Federal Exempt Organization Business Income Tax Returns (Form 990) for 2015, 2016, and 2017 are subject to examination by the IRS, generally for the three years after they were filed. As of the date of this report, the fiscal 2018 tax returns for either organization had not yet been filed.

Performance indicator - The consolidated statements of activities and changes in net assets include the performance indicator operating income (loss). The performance indicator excludes investment income and fees and net unrealized investment gains/losses, which is consistent with industry practice.

Recent accounting pronouncements - In May 2014, the FASB issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* that will supersede most current revenue recognition guidance, including industry-specific guidance. The core principle of the new guidance is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard provides a five-step analysis of transactions to determine when and how revenue is recognized. Other major provisions include the capitalization and amortization of certain contract costs, ensuring the time value of money is considered in the transaction price, and allowing estimates of variable consideration to be recognized before contingencies are resolved in certain circumstances. Additionally, the guidance requires disclosures related to the nature, amount, timing, and uncertainty of revenue that is recognized.

(1) Company operations and significant accounting policies (continued)

In August 2015, the FASB issued FASB ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606)*, which changed the effective date of the provisions of FASB ASU No. 2014-09. As a result, the new effective dates for public business entities, certain not-for-profit entities, and certain employee benefit plans to apply the guidance in FASB ASU No. 2014-09 is for annual reporting periods beginning after December 15, 2017. All other entities should apply the guidance in FASB ASU No. 2014-09 to annual reporting periods beginning after December 15, 2018. Earlier application is permitted only as of annual reporting periods beginning after December 15, 2016. Transition to the new guidance may be done using either a full or modified retrospective method. The Company is currently evaluating the full effect that the adoption of this standard will have on the consolidated financial statements.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows* (*Topic 230*). This ASU requires that a statement of cash flows explain the change during the period in the total cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the consolidated statement of cash flows. The amendments in the ASU do not provide a definition of restricted cash or restricted cash equivalents. The ASU is effective for all nonpublic business entities for fiscal years beginning after December 15, 2018. Early adoption is permitted. The Company is evaluating the full effect that the adoption of this standard will have on the consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958), Presentation of Financial Statements of Not-for-Profit Entities*. ASU 2016-14 improves the current net asset classification requirements and the information presented in financial statements and notes about a not-for-profit entity's liquidity, financial performance, and cash flows. ASU 2016-14 is effective for annual financial statements issued for fiscal years beginning after December 15, 2017. Early adoption is permitted. The amendments of this ASU are to be applied on a retrospective basis in the year that the ASU is first applied. The Company is currently evaluating the full effect that the adoption of this standard will have on the consolidated financial statements.

Reclassifications - Certain prior year amounts have been reclassified for consistency with the current year presentation in the consolidated financial statements. The reclassifications had no net effect on the reported consolidated statements of activities and changes in net assets.

Subsequent events - The Company has evaluated subsequent events through November 5, 2018, which is the date the consolidated financial statements were available to be issued.

(2) Reconciliation

Reconciliation balances are recorded as a net receivable or payable on the consolidated statements of financial position by line of business. A summary of the balances by line of business for the years ended June 30 is as follows (in thousands):

	2018		2017	
	Reconciliation Receivable	Reconciliation Payable	Reconciliation Receivable	Reconciliation Payable
Acute	$ 35,854	$ 14,361	$ 6,363	$ 42,643
ALTCS	10,493	684	2,458	-
Total	46,347	15,045	8,821	42,643
Less current portion	(46,347)	(15,045)	(8,821)	(42,643)
Non-current portion	$ -	$ -	$ -	$ -

(3) Investments

The cost and fair value of the Company's investments by type at June 30 are as follows (in thousands):

	2018		2017	
	Cost	Fair Value	Cost	Fair Value
Short-term:				
Marketable equity securities	$ 35,972	$ 35,972	$ 28,279	$ 28,279
Corporate bonds	6,914	6,836	3,499	3,496
U.S. Government securities	4,479	4,504	-	-
	47,365	47,312	31,778	31,775
Long-term:				
Marketable equity securities	98,599	111,507	70,228	81,542
U.S. Government securities	76,723	76,057	40,076	40,010
Corporate bonds	45,283	44,278	50,564	50,671
Mortgage-backed securities	9,941	9,646	10,845	10,763
Preferred securities	197	195	688	752
	230,743	241,683	172,401	183,738
	$ 278,108	$ 288,995	$ 204,179	$ 215,513
Restricted securities	$ 438	$ 437	$ 440	$ 438

Investment income for the years ended June 30 is comprised of the following (in thousands):

	2018	2017
Interest and dividend income	$ 8,378	$ 3,232
Realized gains on investments	6,838	2,930
	$ 15,216	$ 6,162

Management continually reviews their investment portfolio and evaluates whether declines in the fair value of securities should be considered other-than-temporary. Factored into this evaluation are the general market conditions, the issuer's financial condition and near-term prospects, conditions in the issuer's industry, the recommendation of advisors and the length of time and extent to which the market value has been less than cost. During the years ended June 30, 2018 and 2017, the Company recorded no losses for other-than-temporary declines in the fair value of investments.

(3) Investments (continued)

The following table summarizes the unrealized losses on investments held at June 30, 2018 (in thousands):

Description of securities	Less than twelve months		Twelve months or longer		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
U.S. Government securities	$ -	$ -	$ 60,963	$ 718	$ 60,963	$ 718
Marketable equity securities	-	-	26,440	1,855	26,440	1,855
Corporate bonds	6,836	78	40,813	1,047	47,649	1,125
Mortgage-backed securities	-	-	9,624	295	9,624	295
Preferred securities	-	-	195	2	195	2
Total	$ 6,836	$ 78	$ 138,035	$ 3,917	$ 144,871	$ 3,995

The following table summarizes the unrealized losses on investments held at June 30, 2017 (in thousands):

Description of securities	Less than twelve months		Twelve months or longer		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
U.S. Government securities	$ -	$ -	$ 25,909	$ 147	$ 25,909	$ 147
Marketable equity securities	-	-	14,878	1,647	14,878	1,647
Corporate bonds	2,251	10	32,493	277	34,744	287
Mortgage-backed securities	-	-	9,469	96	9,469	96
Preferred securities	-	-	-	-	-	-
Total	$ 2,251	$ 10	$ 82,749	$ 2,167	$ 85,000	$ 2,177

Investments classified as long-term are based on management's intent to hold such investments. Long-term investments can be liquidated without significant penalty typically within twenty-four hours, and are considered short-term for purposes of calculating current ratios under AHCCCS reporting guidelines.

(4) Fair value measurements

The following table sets forth by level, within the fair value hierarchy, the Company's investments at fair value as of June 30, 2018 (in thousands):

	Level 1	Level 2	Level 3	Total
Investments:				
U.S. Government securities	$ -	$ 80,561	$ -	$ 80,561
Marketable equity securities				
U.S. large cap	111,508	-	-	111,508
Money market mutual funds	29,096	-	-	29,096
Other	6,875	-	-	6,875
Total marketable equity securities	147,479	-	-	147,479
Corporate bonds	-	51,114	-	51,114
Mortgage-backed securities	-	9,646	-	9,646
Preferred securities	195	-	-	195
Total Investments	$ 147,674	$ 141,321	$ -	$ 288,995
Restricted securities	$ -	$ 437	$ -	$ 437

The following table sets forth by level, within the fair value hierarchy, the Company's investments at fair value as of June 30, 2017 (in thousands):

	Level 1	Level 2	Level 3	Total
Investments:				
U.S. Government securities	$ -	$ 40,010	$ -	$ 40,010
Marketable equity securities				
U.S. large cap	81,542	-	-	81,542
Money market mutual funds	19,841	-	-	19,841
Other	8,438	-	-	8,438
Total marketable equity securities	109,821	-	-	109,821
Corporate bonds	-	54,167	-	54,167
Mortgage-backed securities	-	10,763	-	10,763
Preferred securities	752	-	-	752
Total Investments	$ 110,573	$ 104,940	$ -	$ 215,513
Restricted securities	$ -	$ 438	$ -	$ 438

Restricted securities, which consist of U.S. Treasury notes, are valued using proprietary models incorporating live data from active market makers and inter-dealer brokers as reported on electronic communication networks. The valuation models incorporate benchmark yields, reported trades, broker/dealer quotes, bids, offers and other data.

(5) Claims payable

On a consolidated basis at June 30, 2018 and 2017, claims outstanding to third parties for health care services provided to members, including estimates for incurred but not reported claims, were approximately $272 million and $266 million (SCHN $208 and $200 million and Mercy Maricopa $64 and $66 million), respectively. The balances at June 30, 2018 and 2017 were certified by an actuary. Activity in the liability for claims payable and health care expense for the years ended June 30, 2018 and 2017 is as follows (in thousands):

	2018	2017
Claims unpaid at beginning of year prior to reinsurance recoverable	$ 286,907	$ 246,885
Reinsurance recoverable, beginning of year	(21,239)	(17,634)
Claims unpaid, beginning of year	265,668	229,251
Incurred related to:		
Current year	2,757,557	2,491,774
Prior years	(960)	(6,813)
Total incurred	2,756,597	2,484,961
Paid related to:		
Current year	(2,471,685)	(2,194,310)
Prior years	(264,248)	(232,995)
Total paid	(2,735,933)	(2,427,305)
Claims unpaid at end of year prior to reinsurance recoverable	286,332	286,907
Reinsurance recoverable, end of year	(14,392)	(21,239)
Claims unpaid, end of year	$ 271,940	$ 265,668

Estimates for incurred claims are based on historical enrollment, cost trends, and consider operational changes. Future actual results will typically differ from the estimates. Differences could be due to factors such as an overall change in medical expenses per member or a change in client mix affecting medical costs due to the addition of new members.

The liability for SCHN claims unpaid at June 30, 2017 was more than the actual claims incurred related to fiscal year 2017 and prior by approximately $5.2 million or 2.6% of SCHN claims unpaid. The liability for SCHN claims unpaid at June 30, 2016 was more than the actual claims incurred related to fiscal year 2016 and prior by approximately $2.4 million or 1.4% of SCHN claims unpaid. The primary drivers for the claim development variations include member mix changes, active cost and encounter management, changes in anticipated member utilization, a shift in inpatient costs and re-admittance utilization to physician office visits, inpatient unit cost variations related to state-mandated outlier reform, speed of claims processing, and initiative levels to recoup provider overpayments.

The claims payable liability for Mercy Maricopa claims payable at June 30, 2017 was less than the actual claims incurred related to fiscal year 2017 and prior by approximately $2.2 million or 3.2%. The primary drivers for unfavorable claim development include member mix changes, higher than anticipated member utilization and enrollment growth. Mercy Maricopa continues to incur claims for prior periods. The claims payable liability for Mercy Maricopa at June 30, 2016 was less than the actual claims incurred related to fiscal year 2016 and prior by approximately $6.8 million or 12%. The primary drivers for unfavorable claim development include member mix changes and higher than anticipated member utilization. The claims payable is adjusted each period end as more information becomes available.

(5) Claims payable (continued)

Estimated third-party subrogation included as a reduction to medical and hospital expenses in the accompanying consolidated statements of activities and changes in net assets at June 30, 2018 and 2017 totaled approximately $6,599,000 and $5,894,000 respectively.

(6) District noncontrolling interest

During the period from formation (January 22, 2013) through June 30, 2015, District contributed $10 million towards the funding of Mercy Maricopa.

In accordance with the membership agreement, any time after three years from the commencement of the RBHA contract (April 1, 2014), District may require that Mercy Maricopa purchase the membership interest of District. The purchase price of District's membership interest under the District put option shall be the sum of District's capital contributions to Mercy Maricopa, without interest, and any remaining accrued or deferred distributions to District (a 15% relative interest), plus interest, if any. As a result, $16,877,275 (the $10 million, plus District's share of the changes in Mercy Maricopa's net assets since formation of $6,877,275) and $18,849,539 was included as a noncontrolling interest within unrestricted net assets, in the accompanying consolidated statements of financial position at June 30, 2018 and 2017, respectively.

On March 30, 2018, District notified Mercy Maricopa that District elected to exercise the $10 million put option effective July 1, 2018. Subsequent to June 30, 2018 the $10 million was paid to District. At that time, the remaining noncontrolling interest totaling $6,877,275 at June 30, 2018 was reclassified from noncontrolling to controlling unrestricted net assets.

(7) Related party transactions

In September 2015, Tenet Healthcare Corporation, Dignity Health and Ascension Health finalized a joint venture to own and operate Carondelet Health Network in Tucson, Arizona. Tenet Healthcare Corporation is the majority partner at 60% ownership share and Dignity Health and Ascension Health each having a 20% ownership share. The Company paid approximately $223,799,000 in 2018 and $192,364,000 in 2017 to Dignity Health and its affiliates, and paid approximately $18,622,000 in 2018 and $20,560,000 in 2017 to Ascension Health and its affiliates, and paid approximately $61,654,000 in 2018 and $51,316,000 in 2017 to District for hospitalization, behavioral health and other medical services provided to its members. These balances include net prospective provider advance payments made to Dignity. Provider advances to Dignity amounted to approximately $5,816,000 and $3,929,000 at June 30, 2018 and June 30, 2017, respectively. During the years ended June 30, 2018 and 2017 SCHN made no asset distributions to either Dignity or Carondelet Health Network, respectively.

(8) Commitments and contingencies

Performance bonds - SCHN obtains unsecured surety bonds to satisfy the AHCCCS Acute, ALTCS, DES/DDD and Medicare performance bond requirements. The following table sets forth the SCHN contract requirement and the Performance Bond amounts at June 30, 2018:

Line of Business	AHCCCS Minimum Requirement	Performance Bond Amount		Effective Date
Acute	90% of Capitation Revenue	$	116,000,000	10/1/2017
ALTCS	90% of Capitation Revenue	$	48,000,000	10/1/2017
DDD	70% of Capitation Revenue	$	4,200,000	10/1/2017
Medicare	$1,050 PMPM	$	20,500,000	1/1/2018

In accordance with the terms of its contract with AHCCCS, Mercy Maricopa is required to post a performance bond with AHCCCS equal to 80% of the expected monthly Title capitation and Non-Title payments, as specified in the contract. The performance bond must be maintained to guarantee payment of Mercy Maricopa's obligations under the contract. The following table sets forth the Mercy Maricopa performance bond amount at June 30, 2018.

Line of Business	AHCCCS Minimum Requirement	Performance Bond Amount		Effective Date
Title/Non-Title	80% of Capitation Revenue	$	90,000,000	10/1/2017

Litigation - Periodically, the Company is involved in litigation and claims arising in the normal course of operations. In the opinion of management based on consultation with legal counsel, losses, if any, from these matters are covered by insurance or are immaterial. Management believes that any resulting liability will not materially affect the Company's consolidated financial position.

Liability insurance - SCHN and Mercy Maricopa each maintain directors and officers, errors and omissions, and cyber liability insurance coverage under claims-made policies. Each policyholder is insured for losses up to $20 million per claim and in the aggregate under each of its directors and officers liability policy and $10 million per claim and in the aggregate under each of its errors and omissions and cyber liability policies. Claims reported endorsement (tail) coverage is available if the policy is not renewed to cover claims incurred but not reported. SCHN and Mercy Maricopa anticipate that renewal coverage will be available at expiration of the current policy. Aetna maintains the general liability coverage for the Company, and is insured for losses up to $2 million per claim and $6 million in the aggregate under its general liability policy.

Healthcare regulation - 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, and government healthcare program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Company is in compliance with fraud and abuse laws and regulations, as well as other applicable government laws and regulations. Compliance with such laws and regulations can be subject to future reviews and interpretation as well as regulatory actions unknown or unasserted at this time.

(8) Commitments and contingencies (continued)

Health reform legislation at both the federal and state levels continues to evolve. Changes continue to impact existing and future laws and rules. Such changes may impact the way the Company does business, restrict revenue and enrollment growth in certain products and market segments, restrict growth rates for certain products and market segments, increase medical, administrative and capital costs, and expose the Company to increased risk of loss or further liabilities. The Company's consolidated operating results, financial position and cash flows could be adversely impacted by such changes.

Community reinvestment program - In accordance with the AHCCCS contract, Mercy Maricopa has approved a Community Reinvestment program. Under the program, Mercy Maricopa will demonstrate a commitment to the local communities in which it operates through community reinvestment activities including contributing 6% of its annual profits to community reinvestment. The program funds community projects that enhance the lives of people in the communities in Mercy Maricopa's geographic service area. These funds are for projects and services not eligible for service or prevention dollars from Mercy Maricopa.

For the years ended June 30, 2018 and 2017, Mercy Maricopa approved amounts that resulted in grants to providers of approximately $1,655,000 and $482,000, respectively, to be spent on various healthcare community projects. These amounts are included in general and administrative expenses in the accompanying consolidated statements of activities and changes in net assets. At June 30, 2018 and 2017, Mercy Maricopa had not yet spent all of the funds appropriated. Accordingly, at June 30, 2018 and 2017, Mercy Maricopa has recorded a liability for unspent Community Reinvestment program funds of approximately $827,000 and $2,517,000, respectively, which is included in other current liabilities in the accompanying consolidated statements of financial position.

Contract compliance - Under the terms of the AHCCCS and Medicare Advantage contracts, SCHN is required to meet certain financial covenants for both AHCCCS and CMS products, as applicable.

In accordance with the AHCCCS Contract, Mercy Maricopa is required to maintain certain minimum financial reporting and viability measures.

Mercy Maricopa must maintain unrestricted minimum capitalization of at least 90% of the monthly capitation and block payments received under the AHCCCS contract. As of June 30, 2018 and 2017, Mercy Maricopa was in compliance with this requirement.

Mercy Maricopa's contract contains various quarterly financial performance requirements, including a required minimum liquidity ratio, an administrative cost percentage, and service expense percentages. As of June 30, 2018 and 2017 Mercy Maricopa was in compliance with these requirements.

As discussed in Note 1, Mercy Maricopa is limited by the terms of its contract with AHCCCS to profit that can be earned under the various programs.

Should Mercy Maricopa be in default of any material obligations under the AHCCCS contract, AHCCCS may, at its discretion, in addition to other remedies, either adjust the amount of future payments or withhold future payment until satisfactory resolution of the default or exception. Further, if monies are not appropriated by the State or are not otherwise available, the AHCCCS contract may be cancelled upon written notice until such monies are so appropriated or available.

(8) Commitments and contingencies (continued)

Mercy Maricopa is required to meet quarterly and contract year end minimum encounter submission percentages, or be subject to sanction by AHCCCS. Typically, Mercy Maricopa has up to eight months after the contract period end to meet the minimum number of encounters. For the year ended June 30, 2017, Mercy Maricopa anticipated meeting the required encounter threshold for the contract period from October 1, 2016 through September 30, 2017. Accordingly as of June 30, 2017, Mercy Maricopa did not record a liability associated with an encounter sanction. Through the date of this report, AHCCCS has not yet completed its encounter evaluation assessment for the contract year ended September 30, 2017. However, management continues to anticipate meeting the required encounter threshold. As of June 30, 2018, Mercy Maricopa anticipates meeting the required encounter threshold for the contract year from October 1, 2017 through September 30, 2018. Accordingly, as of June 30, 2018, Mercy Maricopa has not recorded a liability associated with an encounter sanction.

AHCCCS has a right to sanction Mercy Maricopa for other matters of non-compliance of the AHCCCS contract, as determined by AHCCCS. Mercy Maricopa received no sanctions for the years ended June 30, 2018 and 2017.

(9) Concentration of credit risk

SCHN's future contract awards are contingent upon the continuation of the AHCCCS Acute, DES/DDD, and ALTCS programs by the State of Arizona and SCHN's ability and desire to retain its status as a Contractor under these programs. The AHCCCS Acute contract is effective through September 30, 2018 with no additional renewal options.

The current ALTCS contract expired on September 30, 2018. SCHN was awarded a new ALTCS contract effective October 1, 2018, for an initial period of three years with three renewal periods: one renewal of two years, and two renewals of one year each. The DES/DDD contract was renewed through September 30, 2019. SCHN's Medicare Advantage contract is renewed annually by CMS. Mercy Maricopa's contract with AHCCCS has been renewed through September 30, 2020. Subsequent to June 30, 2018, in connection with the merger described in Note 10, Mercy Maricopa's AHCCCS contract was assumed by SCHN.

Failure to renew these contracts could have a significant impact on consolidated operations.

(10) Subsequent events

On November, 2, 2017, AHCCCS released the AHCCCS Complete Care Request for Proposal (RFP) which will integrate physical and behavioral health care contacts under managed care plans for the majority of the 1.9 million AHCCCS members. The integrated delivery model will offer a more cohesive health care system for members incentivizing quality health care outcomes with alternative payment models, and leverage health information technology for improved care coordination. Additionally, integrating physical health and behavioral healthcare contracts will drive strategic, innovative health care initiatives forward. SCHN submitted a bid as an integrated plan in response to the RFP in January 2018. In March 2018, SCHN was selected to provide physical and behavioral healthcare services through the AHCCCS Complete Care program in the Central and South regions. The three year contract agreement, with the possibility of two two-year extensions, is expected to commence on October 1, 2018.

In conjunction with Mercy Maricopa's acquisition of District's noncontrolling interest (see Note 6), Mercy Maricopa merged into SCHN effective July 1, 2018 to form a combined Organization operating as Mercy Care. Mercy Care will operate the Complete Care contract effective October 1, 2018 as well as the remainder of the Mercy Maricopa contract with AHCCCS to provide physical and behavioral health services to the seriously mentally ill and other defined populations within Maricopa County through September 30, 2020.

ADDITIONAL INFORMATION

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INDEPENDENT AUDITORS' REPORT ON ADDITIONAL INFORMATION

To the Board of Directors of

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

We have audited the consolidated financial statements of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate*** as of and for the years ended June 30, 2018 and 2017, and our report thereon dated November 5, 2018, which contained an unmodified opinion on those consolidated financial statements, appears on pages 1 - 2. Our audits were performed for the purpose of forming an opinion on the consolidated financial statements as a whole. The additional information on pages 30 and 31 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. The consolidating statements on pages 28 and 29 are presented for purposes of additional analysis of the 2018 consolidated financial statements rather than to present the financial position, activities and changes in net assets of the individual entities and are not a required part of the consolidated financial statements. The Sub-Capitated Expenses Report on page 32 is required in accordance with the Arizona Health Care Cost Containment System contract. The additional information on pages 28 to 32 is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the additional information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Mayer Hoffman McCann P.C.

November 5, 2018

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

ADDITIONAL INFORMATION

CONSOLIDATING STATEMENT OF FINANCIAL POSITION

June 30, 2018
(In thousands)

A S S E T S

	SCHN	Mercy Maricopa	Eliminations	Consolidated
CURRENT ASSETS				
Cash and cash equivalents	$ 71,263	$ 187,682	$ -	$ 258,945
Short-term investments	47,312	-	-	47,312
Receivables:				
Reinsurance receivables, net of allowance for doubtful accounts of $13,017	14,333	59	-	14,392
Reconciliation receivables	46,347	-	-	46,347
Capitation and supplemental receivables	1,817	-	-	1,817
Pharmacy rebate receivable	25,734	744	-	26,478
Third-party liability receivable	4,824	-	-	4,824
Interest receivable	696	-	-	696
Provider advances, net of allowance for doubtful accounts of $1,313	6,941	1,250	-	8,191
Other receivables, net of allowance for doubtful accounts of $64	567	2,754	-	3,321
Risk share settlement, current portion	10,069	-	-	10,069
Due from AHCCCS	-	26,179	-	26,179
Due from Aetna	9,777	-	-	9,777
Prepaid assets	361	1,341	-	1,702
TOTAL CURRENT ASSETS	240,041	220,009	-	460,050
RESTRICTED SECURITIES	-	437	-	437
CAPITALIZED SOFTWARE COSTS, net	-	577	-	577
RISK SHARE SETTLEMENT, less current portion	2,309	-	-	2,309
INVESTMENT IN MMIC	118,971	-	(118,971)	-
LONG-TERM INVESTMENTS	241,683	-	-	241,683
TOTAL ASSETS	$ 603,004	$ 221,023	$ (118,971)	705,056

L I A B I L I T I E S A N D N E T A S S E T S

	SCHN	Mercy Maricopa	Eliminations	Consolidated
CURRENT LIABILITIES				
Claims payable	$ 208,212	$ 63,728	$ -	$ 271,940
Payable to providers	8,654	19,380	-	28,034
Reconciliation payable	15,045	-	-	15,045
Due to AHCCCS	-	2	-	2
Due to Aetna	-	321	-	321
Deferred revenue	36,127	463	-	36,590
Risk share settlement payable	21,301	-	-	21,301
Other current liabilities	3,124	1,281	-	4,405
TOTAL CURRENT LIABILITIES	292,463	85,175	-	377,638
RISK SHARE SETTLEMENT PAYABLE, net of current portion	2,345	-	-	2,345
TOTAL LIABILITIES	294,808	85,175	-	379,983
UNRESTRICTED NET ASSETS	308,196	135,848	(118,971)	325,073
TOTAL LIABILITIES AND NET ASSETS	$ 603,004	$ 221,023	$ (118,971)	$ 705,056

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

ADDITIONAL INFORMATION

CONSOLIDATING STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

Year Ended June 30, 2018
(In thousands)

	SCHN	Mercy Maricopa	Eliminations	Consolidated
OPERATING REVENUES				
Capitation premiums	$ 2,384,875	$ 1,424,568	$ -	$ 3,809,443
Delivery supplement	58,879	-	-	58,879
Other	8,446	-	-	8,446
TOTAL OPERATING REVENUES	2,452,200	1,424,568	-	3,876,768
HEALTH CARE EXPENSES				
Hospitalization	421,368	-	-	421,368
Medical compensation	374,905	-	-	374,905
Ancillary and other medical services	1,093,789	1,304,148	-	2,397,937
Institutional	207,371	-	-	207,371
Home and community based services	211,264	-	-	211,264
Less: reinsurance recoveries	(77,996)	(944)	-	(78,940)
TOTAL HEALTH CARE EXPENSES	2,230,701	1,303,204	-	3,533,905
GENERAL AND ADMINISTRATIVE EXPENSES	170,711	109,479	-	280,190
PREMIUM TAX EXPENSE	40,403	25,036	-	65,439
TOTAL EXPENSES	2,441,815	1,437,719	-	3,879,534
OPERATING INCOME (LOSS)	10,385	(13,151)	-	(2,766)
NONOPERATING INCOME (EXPENSE)				
Investment income	15,212	4	-	15,216
Investment fees	(1,171)	-	-	(1,171)
Loss on investment in MMIC	(11,176)	-	11,176	-
TOTAL NONOPERATING INCOME	2,865	4	11,176	14,045
CHANGE IN NET ASSETS PRIOR TO UNREALIZED GAINS (LOSSES) AND CHANGE IN NET ASSETS ATTRIBUTABLE TO DISTRICT	13,250	(13,147)	11,176	11,279
UNREALIZED GAINS (LOSSES) ON INVESTMENTS	(445)	(1)	-	(446)
CHANGE IN NET ASSETS PRIOR CHANGE IN NET ASSETS ATTRIBUTABLE TO DISTRICT	12,805	(13,148)	11,176	10,833
CHANGE IN NET ASSETS ATTRIBUTABLE TO DISTRICT	-	1,972	-	1,972
CHANGE IN NET ASSETS ATTRIBUTABLE TO CONTROLLING INTEREST	12,805	(11,176)	11,176	12,805
NET ASSETS, BEGINNING OF YEAR	295,391	148,996	(130,147)	314,240
NET ASSETS, END OF YEAR	$ 308,196	$ 135,848	$ (118,971)	$ 325,073

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

ADDITIONAL INFORMATION

STATEMENT OF FINANCIAL POSITION - SCHN

June 30, 2018
(In thousands)

A S S E T S

	Acute	DES/DDD	ALTCS	Medicare	Total
CURRENT ASSETS					
Cash and cash equivalents	$ (27,839)	$ 6,801	$ 23,755	$ 68,546	$ 71,263
Short-term investments	25,174	3,105	17,015	2,018	47,312
Receivables:					
Reinsurance receivables, net	9,316	327	4,690	-	14,333
Reconciliation receivables	35,854	-	10,493	-	46,347
Capitation and supplemental receivables	2,933	-	(461)	(655)	1,817
Pharmacy rebate receivable	2,693	200	462	22,379	25,734
Third-party liability receivable	3,328	-	579	917	4,824
Interest receivable	370	46	250	30	696
Provider advances, net	6,213	25	432	271	6,941
Other receivables	574	-	(7)	-	567
Risk share settlement, current portion	-	-	-	10,069	10,069
Due from Aetna	5,478	242	2,164	1,893	9,777
Prepaid assets	222	6	72	61	361
TOTAL CURRENT ASSETS	64,316	10,752	59,444	105,529	240,041
RISK SHARE SETTLEMENT, less current portion	-	-	-	2,309	2,309
INVESTMENT IN MMIC	72,488	-	33,783	12,700	118,971
LONG-TERM INVESTMENTS	128,595	15,863	86,916	10,309	241,683
TOTAL ASSETS	$ 265,399	$ 26,615	$ 180,143	$ 130,847	$ 603,004

L I A B I L I T I E S A N D N E T A S S E T S

	Acute	DES/DDD	ALTCS	Medicare	Total
CURRENT LIABILITIES					
Claims payable	$ 108,814	$ 4,430	$ 63,705	$ 31,263	$ 208,212
Payable to providers	8,654	-	-	-	8,654
Reconciliation payable	14,361	-	684	-	15,045
Deferred revenue	-	-	-	36,127	36,127
Risk share settlement payable	9,130	-	-	12,171	21,301
Other current liabilities	596	64	1,505	959	3,124
TOTAL CURRENT LIABILITIES	141,555	4,494	65,894	80,520	292,463
RISK SHARE SETTLEMENT PAYABLE, net of current portion	-	-	-	2,345	2,345
TOTAL LIABILITIES	141,555	4,494	65,894	82,865	294,808
UNRESTRICTED NET ASSETS	123,844	22,121	114,249	47,982	308,196
TOTAL LIABILITIES AND NET ASSETS	$ 265,399	$ 26,615	$ 180,143	$ 130,847	$ 603,004

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

ADDITIONAL INFORMATION

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS - SCHN

Year Ended June 30, 2018
(In thousands)

	Acute	DES/DDD	ALTCS	Medicare	Total
OPERATING REVENUES					
Capitation premiums	$ 1,313,429	$ 61,858	$ 580,863	$ 428,725	$ 2,384,875
Delivery supplement	58,879	-	-	-	58,879
Other	7,847	27	239	333	8,446
TOTAL OPERATING REVENUES	1,380,155	61,885	581,102	429,058	2,452,200
HEALTH CARE EXPENSES					
Hospitalization	270,056	9,316	26,512	115,484	421,368
Medical compensation	309,388	7,014	14,219	44,284	374,905
Ancillary and other medical services	749,887	38,289	92,898	212,715	1,093,789
Institutional	-	-	207,371	-	207,371
Home and community based services	-	-	211,264	-	211,264
Less: reinsurance recoveries	(49,538)	(1,381)	(27,077)	-	(77,996)
TOTAL HEALTH CARE EXPENSES	1,279,793	53,238	525,187	372,483	2,230,701
GENERAL AND ADMINISTRATIVE EXPENSES	97,036	4,261	32,015	37,399	170,711
PREMIUM TAX EXPENSE	27,361	-	13,042	-	40,403
TOTAL EXPENSES	1,404,190	57,499	570,244	409,882	2,441,815
OPERATING INCOME (LOSS)	(24,035)	4,386	10,858	19,176	10,385
NONOPERATING INCOME (EXPENSE)					
Investment income	8,094	998	5,471	649	15,212
Investment fees	(623)	(77)	(421)	(50)	(1,171)
Investment in MMIC	(6,707)	-	(3,318)	(1,151)	(11,176)
TOTAL NONOPERATING INCOME (EXPENSE)	764	921	1,732	(552)	2,865
CHANGE IN NET ASSETS PRIOR TO UNREALIZED GAINS (LOSSES) ON INVESTMENTS	(23,271)	5,307	12,590	18,624	13,250
UNREALIZED GAINS (LOSSES) ON INVESTMENTS	(581)	(16)	184	(32)	(445)
CHANGE IN NET ASSETS	(23,852)	5,291	12,774	18,592	12,805
NET ASSETS, BEGINNING OF YEAR	147,696	16,830	101,475	29,390	295,391
NET ASSETS END OF YEAR	$ 123,844	$ 22,121	$ 114,249	$ 47,982	$ 308,196

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

ADDITIONAL INFORMATION

SUB-CAPITATED EXPENSES REPORT

Year Ended June 30, 2018

Account	Account Description	YTD ACUTE	YTD MCA	YTD DDD	YTD ALTCS
Sub-Capitated Hospitalization Expenses:					
402	Hospital Inpatient	$ -	$ -	$ -	$ 2,394,857
404	Hospital Inpatient -Behavioral Health Services	-	-	-	-
406	PPC-Hospital Inpatient	-	-	-	-
	Total Sub-Capitated Hospitalization Expense:	-	-	-	2,394,857
Sub-Capitated Medical Compensation Expenses:					
408	Primary Care Physician Services	-	-	-	-
409	Behavioral Health Physician Services	-	-	-	-
410	Referral Physician Services	-	-	-	-
411	FQHC/RHC Services	-	-	-	-
412	Other Professional Services	-	-	-	-
416	PPC-Physician Services	-	-	-	-
	Total Sub-Capitated Medical Compensation Expenses:	-	-	-	-
Sub-Capitated Other Medical Expenses:					
416	Emergency Facility Services	-	-	-	-
417	Pharmacy	-	-	-	-
418	Laboratory, Radiology and Medical Imaging	11,597,484	923,757	370,021	234,711
419	Outpatient Facility	-	-	-	-
420	Durable Medical Equipment	380,845	-	3,696,466	548,742
421	Dental	41,980,426	2,653,404	1,219,513	129,585
422	Transportation	-	-	-	-
423	Nursing Facility, Home Health Care	-	8,388,552	1,820	-
424	Physical Therapy	-	-	-	-
434	Value Based Purchasing Initiatives Provider Expenses	-	-	-	-
425	Miscellaneous Med Exp	-	-	-	-
426	Behavioral Health Day Program	-	-	-	-
427	Behavioral Health Case Management Services	-	-	-	-
428	Behavioral Health Crisis Intervention Services	-	-	-	-
429	Behavioral Health Rehabilitation Services	-	-	-	-
430	Behavioral Health Residential Services	-	-	-	-
431	All Other Behavioral Health Services	-	-	-	-
438	PPC-Other Medical Expenses	4,442,682	-	153,654	11,386
	Total Sub-Capitated Other Medical Expenses:	$ 58,401,437	$ 11,965,713	$ 5,441,474	$ 924,424
	Total Sub-Capitated Expenses:	$ 58,401,437	$ 11,965,713	$ 5,441,474	$ 3,319,281

UNIFORM GUIDANCE
SUPPLEMENTAL REPORTS

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended June 30, 2018

Federal Grantor / Pass-Through Agency / Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Grant Number	Federal Expenditures
U.S. Department of Health and Human Services Pass Through Program From:				
Centers for Medicare and Medicaid Services (CMS) and Arizona Health-e Connection:				
ACA - Transforming Clinical Practice Initiative: Practice Transformation Networks (PTNs)	93.638	68660047917631	1L1CMS331563-02-00	1,829,246
Total U.S. Department of Health and Human Services				1,829,246
TOTAL EXPENDITURES OF FEDERAL AWARDS				1,829,246

See Independent Auditors' Report
See Accompanying Notes to the Schedule of Expenditures of Federal Awards

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended June 30, 2018

(1) Basis of presentation

The accompanying Schedule of Expenditures of Federal Awards (the "Schedule") includes the federal award activity of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate*** under programs of the federal government for the year ended June 30, 2018. The information in the Schedule is presented in accordance with the requirements of *Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (the "Uniform Guidance"). Because the Schedule presents only a selected portion of the operations of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate***, it is not intended to and does not present the consolidated financial position, changes in net assets or cash flows of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate***. ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate*** did not provide federal awards to sub-recipients during the year ended June 30, 2018.

(2) Summary of significant accounting policies

Expenditures reported on the Schedule of Expenditures of Federal Awards are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement. ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate*** has not elected to use the ten percent de minimis indirect cost rate allowed under the Uniform Guidance.

(3) Additional federal financial assistance

Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliates' consolidated financial statements include the operations of Mercy Maricopa Integrated Care, which received $27,484,666 in federal awards from the U.S. Department of Health and Human Services which is not included in the accompanying Schedule of Expenditures of Federal Awards for the year ended June 30, 2018. Our audit did not include the operations of Mercy Maricopa Integrated Care as management has engaged us to conduct a separate audit of compliance under the Uniform Guidance on the federal awards of Mercy Maricopa Integrated Care.

(4) Catalog of Federal Domestic Assistance (CFDA) numbers

The program titles and CFDA numbers were obtained from the 2018 Catalog of Federal Domestic Assistance.

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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Directors of

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate*** (the "Organization"), which comprise the consolidated statements of financial position as of June 30, 2018 and 2017, and the related consolidated statements of activities and changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated November 5, 2018. ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** consolidated financial statements includes the operations of Mercy Maricopa Integrated Care which received $27,484,666 in federal awards from the U.S. Department of Health and Human Services which is not included in the accompanying schedule of expenditures of federal awards for the year ended June 30, 2018. Our audit, described below, did not include the operations of Mercy Maricopa Integrated Care, as management has engaged us to perform a separate audit of compliance of Mercy Maricopa Integrated Care in accordance with the requirements of the Uniform Guidance.

Internal Control Over Financial Reporting

In planning and performing our audits of the consolidated financial statements, we considered ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** internal control. Accordingly, we do not express an opinion on the effectiveness of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's consolidated financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of consolidated financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Mayer Hoffman McCann P.C.

November 5, 2018

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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

To the Board of Directors of

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

Report on Compliance for Each Major Federal Program

We have audited ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** compliance with the types of compliance requirements described in the U.S. Office of Management and Budget ("OMB") Compliance Supplement that could have a direct and material effect on ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** major federal program for the year ended June 30, 2018. ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliates'*** consolidated financial statements includes the operations of Mercy Maricopa Integrated Care which received $27,484,666 in federal awards from the U.S. Department of Health and Human Services which is not included in the accompanying schedule of expenditures of federal awards for the year ended June 30, 2018. Our audit, described below, did not include the operations of Mercy Maricopa Integrated Care, as management has engaged us to perform a separate audit of compliance of Mercy Maricopa Integrated Care in accordance the requirements of the Uniform Guidance.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations and the terms and conditions of its federal awards applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (the "Uniform Guidance"). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** compliance.

Opinion on Major Federal Program

In our opinion, ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate*** complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the major federal program for the year ended June 30, 2018.

Report on Internal Control Over Compliance

Management of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate*** is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of ***Southwest Catholic Health Network Corporation dba Mercy Care Plan and Affiliate's*** internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over* compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Mayer Hoffman McCann P.C.

November 5, 2018

SOUTHWEST CATHOLIC HEALTH NETWORK CORPORATION
dba MERCY CARE PLAN AND AFFILIATE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year Ended June 30, 2018

Section I – Summary of Auditors' Results

Financial Statements

1. Type of report the auditor issued on whether the consolidated financial statements audited were prepared in accordance with GAAP:	Unmodified
2. Internal control over financial reporting:	
a. Material weakness(es) identified?	No
b. Significant deficiency(ies) identified?	None reported
3. Noncompliance material to consolidated financial statements noted?	No

Federal Awards

1. Internal control over major federal program:	
a. Material weakness(es) identified?	No
b. Significant deficiency(ies) identified?	None reported
2. Type of Auditor's report issued on compliance for major federal program:	Unmodified
3. Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?	No
4. Identification of major federal programs:	

CFDA Number	Name of Federal Program or Cluster
93.638	ACA - Transforming Clinical Practices Initiative: Practice Transformation Networks (PTNs)

5. Dollar threshold used to distinguish between type A and type B programs:	$750,000
6. Auditee qualified as a low-risk auditee?	No

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year Ended June 30, 2018

Section II – Financial Statement Findings

None noted

Section III – Federal Award Findings

None noted

Section IV – Prior Audit Findings

None