

Statutory Basis Financial Statements and Supplementary
Information with Report of Independent Certified
Public Accountants

Maryland Health Insurance Plan

June 30, 2012 and 2011

Contents

| | Page |
|--|-------------|
| Report of Independent Certified Public Accountants | 1 |
| Statutory Financial Statements: | |
| Statutory Statements of Admitted Assets, Liabilities and Net Assets | 3 |
| Statutory Statements of Operations and Changes in Net Assets | 4 |
| Statutory Statements of Cash Flows | 5 |
| Notes to Statutory Financial Statements | 6 |
| Supplementary Information: | |
| Schedule 1 – Statutory Statement of Admitted Assets, Liabilities and Net Assets by Program as of June 30, 2012 | 17 |
| Schedule 2 – Statutory Statement of Operations and Changes in Net Assets by Program for the fiscal year ended June 30, 2012 | 18 |
| Schedule 3 – Statutory Statement of Admitted Assets, Liabilities and Net Assets by Program as of June 30, 2011 | 19 |
| Schedule 4 – Statutory Statement of Operations and Changes in Net Assets by Program for the fiscal year ended June 30, 2011 | 20 |



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Report of Independent Certified Public Accountants

Board of Directors of
Maryland Health Insurance Plan

We have audited the accompanying statutory statement of admitted assets, liabilities and net assets of Maryland Health Insurance Plan (the "Plan") as of June 30, 2012 and the related statutory statements of operations and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audit. The statutory financial statements of Maryland Health Insurance Plan as of and for the year ended June 30, 2011 were audited by other auditors. Those auditors expressed an unqualified opinion on those statutory financial statements in their report dated October 3, 2011, which were prepared in conformity with the accounting practices prescribed or permitted by the Maryland Insurance Administration.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America as established by the American Institute of Certified Public Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Plan's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note B, these financial statements were prepared in conformity with the accounting practices prescribed or permitted by the Maryland Insurance Administration, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities and net assets of Maryland Health Insurance Plan as of June 30, 2012, and the results of its operations and its cash flows for the year then ended, on the basis of accounting described in Note B.

Our audit was conducted for the purpose of forming an opinion on the statutory financial statements as a whole. The supplementary information starting on page 17 is presented for purposes of additional analysis and is not a required part of the statutory financial statements. Such supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the statutory financial statements. The supplementary information has been subjected to the auditing procedures applied in the audit of the statutory financial statements and certain additional procedures. These additional procedures included comparing and reconciling the information directly to the underlying accounting and other records used to prepare the statutory financial statements or to the statutory financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America established by the American Institute of Certified Public Accountants. In our opinion, the supplementary information is fairly stated in all material respects, in relation to the statutory financial statements as a whole.



It is inappropriate to, and we do not, express an opinion on the supplementary information relative to accounting principles generally accepted in the United States of America.

This report is intended solely for the information and use of the Board of Directors and management of Maryland Health Insurance Plan, the Maryland Insurance Administration and the State of Maryland and is not intended to be and should not be used by anyone other than these specified parties.

Grant Thornton LLP

October 1, 2012
Glastonbury, Connecticut

MARYLAND HEALTH INSURANCE PLAN

Statutory Statements of Admitted Assets, Liabilities and Net Assets

June 30, 2012 and 2011

ADMITTED ASSETS

| | <u>2012</u> | <u>2011</u> |
|---|-----------------------|-----------------------|
| Cash and cash equivalents | \$ 182,594,870 | \$ 171,989,709 |
| Receivables: | | |
| Assessments | 20,839,977 | 19,267,652 |
| Contract - U.S. Department of Health and Human Services | 1,636,508 | 1,148,143 |
| Federal grants | 1,974,465 | 2,374,230 |
| Premiums | 1,588,996 | 5,182,323 |
| Pharmaceutical rebates | 456,900 | 450,000 |
| Other current assets | 138,418 | 379,880 |
| | <u>\$ 209,230,134</u> | <u>\$ 200,791,937</u> |

LIABILITIES AND NET ASSETS**LIABILITIES**

| | | |
|--|-------------------|-------------------|
| Loss reserves and loss adjustment expenses | \$ 22,372,000 | \$ 20,468,000 |
| Deferred premium tax revenue | 4,500,000 | 4,500,000 |
| Premium subsidies payable | 8,706,769 | 6,078,081 |
| Premiums received in advance | 6,326,739 | 4,830,027 |
| Accounts payable and accrued expenses | 1,920,046 | 2,774,257 |
| Due to CareFirst BlueCross BlueShield | 5,683,304 | 1,042,242 |
| Other liabilities | 10,000 | 10,000 |
| Due to State of Maryland | 2,265,355 | 1,233,163 |
| | <u>51,784,213</u> | <u>40,935,770</u> |

NET ASSETS

| | | |
|---|-----------------------|-----------------------|
| Unreserved and undesignated | 147,945,921 | 154,606,167 |
| Reserved pending legislative authority - State of Maryland Special Fund <i>(Note H)</i> | - | 5,250,000 |
| Designated - State of Maryland Kidney Disease Program <i>(Note H)</i> | 5,000,000 | - |
| Designated - State of Maryland Medical Assistance Program <i>(Note H)</i> | 4,500,000 | - |
| | <u>157,445,921</u> | <u>159,856,167</u> |
| | <u>\$ 209,230,134</u> | <u>\$ 200,791,937</u> |

The accompanying notes are an integral part of these statutory financial statements.

MARYLAND HEALTH INSURANCE PLAN

Statutory Statements of Operations and Changes in Net Assets

For the Years Ended June 30, 2012 and 2011

| | 2012 | 2011 |
|---|-----------------------|-----------------------|
| PREMIUMS AND OTHER REVENUES | | |
| Premiums | \$ 101,942,284 | \$ 86,861,796 |
| Contract revenues - U.S. Department of Health and Human Services | 13,747,104 | 3,764,824 |
| Interest income | 2,033,740 | 3,304,726 |
| Federal grants | 2,454,495 | 2,856,550 |
| | <u>120,177,623</u> | <u>96,787,896</u> |
| BENEFITS PAID OR PROVIDED | | |
| Loss and loss adjustment expenses | 228,888,936 | 179,540,758 |
| Premium subsidy expense | 14,675,649 | 13,347,135 |
| | <u>243,564,585</u> | <u>192,887,893</u> |
| INSURANCE EXPENSES AND OTHER DEDUCTIONS | | |
| Program administration expenses | 13,370,867 | 12,468,373 |
| Professional and other expenses | 1,915,038 | 2,688,315 |
| Write-off of uncollectible premiums | 3,267,939 | 2,154,139 |
| | <u>18,553,844</u> | <u>17,310,827</u> |
| Loss from operations | <u>(141,940,806)</u> | <u>(113,410,824)</u> |
| NON-OPERATING REVENUES | | |
| Assessments <i>(Note B)</i> | 122,296,039 | 116,368,118 |
| Premium taxes <i>(Note B)</i> | 18,000,000 | 18,000,000 |
| | <u>140,296,039</u> | <u>134,368,118</u> |
| Change in net assets | (1,644,767) | 20,957,294 |
| NET ASSETS, beginning of year | 159,856,167 | 140,825,003 |
| TRANSFER FROM STATE OF MARYLAND DEPARTMENT OF HEALTH AND MENTAL HYGIENE | 2,928,255 | - |
| TRANSFERS FROM RESERVED AND DESIGNATED NET ASSETS: | | |
| State of Maryland General Fund <i>(Note H)</i> | (1,500,000) | - |
| State of Maryland Kidney Disease Program <i>(Note H)</i> | (3,000,000) | (1,500,000) |
| CHANGE IN NON-ADMITTED ASSETS | <u>806,266</u> | <u>(426,130)</u> |
| NET ASSETS, end of year | <u>\$ 157,445,921</u> | <u>\$ 159,856,167</u> |

The accompanying notes are an integral part of these statutory financial statements.

MARYLAND HEALTH INSURANCE PLAN

Statutory Statements of Cash Flows

For the Years Ended June 30, 2012 and 2011

| | <u>2012</u> | <u>2011</u> |
|---|-----------------------|-----------------------|
| OPERATIONS | | |
| Premiums received | \$ 103,770,401 | \$ 82,527,976 |
| Contract revenues received - U.S. Department of Health and Human Services | 13,258,739 | 2,616,681 |
| Federal grant funds received | 2,854,260 | 2,317,410 |
| Interest income received | 2,275,202 | 2,935,104 |
| Premiums subsidy paid | (12,046,961) | (9,639,908) |
| Program administration, professional and other | (11,499,054) | (13,153,373) |
| Benefits paid | <u>(227,005,636)</u> | <u>(176,120,430)</u> |
| Net cash used in operations | <u>(128,393,049)</u> | <u>(108,516,540)</u> |
| FINANCING AND MISCELLANEOUS ACTIVITIES | | |
| Other cash provided (applied): | | |
| Assessments received | 121,537,763 | 116,084,559 |
| Premium taxes received | 18,000,000 | 18,000,000 |
| Advance funding provided by the State of Maryland | 1,032,192 | 1,233,163 |
| Net transfers from net assets | <u>(1,571,745)</u> | <u>(1,500,000)</u> |
| Net cash provided by financing and miscellaneous activities | <u>138,998,210</u> | <u>133,817,722</u> |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 10,605,161 | 25,301,182 |
| CASH AND CASH EQUIVALENTS, beginning of year | <u>171,989,709</u> | <u>146,688,527</u> |
| CASH AND CASH EQUIVALENTS, end of year | <u>\$ 182,594,870</u> | <u>\$ 171,989,709</u> |

The accompanying notes are an integral part of these statutory financial statements.

MARYLAND HEALTH INSURANCE PLAN

Notes to Statutory Financial Statements

June 30, 2012 and 2011

NOTE A – NATURE OF OPERATIONS

Maryland Health Insurance Plan (MHIP or the Plan) was established by the Maryland General Assembly in 2002 under Chapter 153 of the Acts of 2002, the Health Insurance Safety Net Act. Chapter 259, Acts of 2008, *“Maryland Health Insurance Plan – Status, Operation & Regulation,”* transferred MHIP from the Maryland Insurance Administration (the “Administration”) and established MHIP as an independent unit of the State Government, effective October 1, 2008.

MHIP is a full-risk, state sponsored health plan created to decrease uncompensated health costs by providing access to affordable, comprehensive health benefits for medically uninsurable residents, as defined by Maryland law. MHIP superseded the Substantial Available and Affordable Coverage (SAAC) open enrollment program operated by commercial insurance carriers in Maryland and also functions as a state alternative mechanism in accordance with federal requirements under the Health Insurance Portability and Accountability Act (HIPAA). Policyholders currently pay premiums that are no more than 150% of the standard risk rate for individual health insurance sold in Maryland. MHIP also derives funding from annual assessments on net patient revenue of Maryland hospitals.

MHIP oversees the operation of the State’s Senior Prescription Drug Assistance Program (SPDAP). The purpose of SPDAP is to subsidize the costs associated with participating in Medicare Part D for eligible individuals. The subsidy provided to Medicare Part D enrollees by SPDAP qualifies it as a State Pharmaceutical Assistance Program (SPAP) pursuant to federal law. SPDAP assists individuals with incomes below 300 percent of the federal poverty level who enroll in Medicare Part D by subsidizing member premiums. SPDAP also subsidizes coinsurance costs incurred in the Medicare Part D coverage gap, or so-called “donut hole.”

On March 23, 2010, the President of the United States of America signed into law H.R. 3590, the Patient Protection and Affordable Care Act, Public Law 111-148 (the “ACA”) as amended by the Health Care and Education Recovery Act of 2010. Section 1101 of the ACA established a temporary high risk health insurance pool program to provide health insurance coverage to currently uninsured individuals with pre-existing conditions as a transition to the broader market and health care reforms scheduled to take effect in January 2014. The ACA authorized the United States Department of Health and Human Services (HHS) to carry out the program directly, or through contracts with States or private, non-profit entities.

On July 1, 2010, MHIP entered into a contract with HHS to implement, in the State of Maryland, the temporary federal high risk pool program established by Section 1101 of the ACA, thus creating the Temporary Federal High Risk Health Insurance Pool Program of Maryland Health Insurance Plan (the “Federal Pool”). Under the contract, MHIP is using its existing arrangements with third parties, internal staffing and ongoing governance by its Board of Directors. In connection with this contract, HHS allocated \$85 million to Maryland to fund all costs of the federal pool through December 31, 2013, when it will cease operation by law. These funds are anticipated to be sufficient to cover the costs of the Federal Pool through its scheduled termination on December 31, 2013.

MARYLAND HEALTH INSURANCE PLAN

Notes to Statutory Financial Statements

June 30, 2012 and 2011

NOTE A – NATURE OF OPERATIONS - Continued

The laws governing MHIP are codified at Title 14, Subtitle 5 of the Insurance Article of the Maryland Annotated Code (the “Code”). Section 14-504 of the Code establishes the MHIP Fund. Member premiums, premium tax revenue for the SPDAP, the annual assessment on hospitals, and amounts deposited pursuant to Section 14-513, among other sources of revenue specified under Section 14-504(b), constitute the MHIP fund.

Under the Code, upon termination of MHIP, the Maryland General Assembly will legislate what is to be done with any funds held by MHIP after payment of all claims and expenses of MHIP.

NOTE B – SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

The preparation of statutory financial statements in conformity with accounting practices prescribed or permitted by the Administration requires management to make estimates and assumptions that affect the reported amounts and disclosures in the statutory financial statements. These estimates and assumptions by management could change in the future as more information becomes available. Actual results could differ from the estimates and assumptions used by management.

Basis of Presentation

The accompanying financial statements have been prepared in conformity with accounting practices prescribed or permitted by the Administration (Note C), which practices differ from accounting principles generally accepted in the United States of America (GAAP). The more significant variances from GAAP are:

Non-admitted Assets: Certain assets designated as “non-admitted,” principally receivables over ninety days, if any, are excluded from the statements of admitted assets, liabilities and net assets and directly charged or credited to net assets. Under GAAP, such assets may be included in the balance sheet, net of specific reserves. The Plan holds non-admitted assessments receivable over ninety days totaling \$-0- and \$814,049, premiums receivable over ninety days totaling \$47,991 and \$54,008, and pharmaceutical rebates receivable over ninety days totaling \$913,800 and \$900,000 as of June 30, 2012 and 2011, respectively. Net non-admitted assets credited (charged) to net assets totaled \$806,266 and \$(426,130) for the years ended June 30, 2012 and 2011, respectively.

Statements of Cash Flows: Cash and cash equivalents in the statements of cash flows represent cash deposits, savings accounts and certificates of deposit in banks or other similar financial institutions with initial maturities of one year or less. Under GAAP, the corresponding caption of cash and cash equivalents includes cash balances and investments with initial maturities of three months or less.

The effects of the foregoing variances from GAAP on the accompanying statutory financial statements have not been determined. Other significant accounting practices are as follows:

Assets

Assets are stated at admitted asset value, which is the value prescribed or permitted by the Administration.

MARYLAND HEALTH INSURANCE PLAN

Notes to Statutory Financial Statements

June 30, 2012 and 2011

NOTE B - SIGNIFICANT ACCOUNTING POLICIES - Continued

Cash and Cash Equivalents

All highly liquid investments with original maturities of one year or less at acquisition are considered to be cash equivalents and cost approximates fair value.

Premiums Receivable

Premiums are paid monthly and are recognized as revenue over the policy period. Premiums received in advance represent the portion of premiums received that relate to future policy periods.

Contract Receivable – U.S. Department of Health and Human Services

The Federal Pool is funded by an \$85 million allocation included in a contract between MHIP and HHS. Amounts are available to be requisitioned on a continuous basis to fund the difference between premiums collected and claims paid plus allowable administrative costs incurred, as defined in the contract. Revenue is recognized to the extent that eligible expenditures have been paid by the Federal Pool.

Pharmaceutical Rebates Receivable

Pharmaceutical rebates receivable represent an estimate of pharmaceutical rebates earned but not yet received for the three month periods ended June 30, 2012 and 2011, respectively, based on historical information including contractual changes in rebate amounts, seasonality differences, changes in premium revenue and changes in utilization of drugs with varying rebate levels. Income from pharmaceutical rebates is recognized by MHIP as earned and is reported as a reduction to claims expense.

Federal Grants Receivable

Grants are generally considered to be exchange transactions in which the grantor requires the performance of specified activities. Entitlement to these grants is based on the expenditure of funds in accordance with grant restrictions and, therefore, revenue is recognized once MHIP is notified it has been approved to receive the grant to the extent of grant expenditures for those grants. During fiscal year 2012, MHIP reported revenues from a federal bonus grant award of \$960,760 for the low income premium subsidy program and of \$1,493,735 related to a federal grant received for operating losses incurred during fiscal year 2011. During fiscal year 2011, MHIP reported revenues from a federal bonus grant award of \$965,340 for the low income premium subsidy program and of \$1,891,210 related to a federal grant received for operating losses incurred during fiscal year 2010. These federal grant awards are included in federal grant revenues for those respective fiscal years.

MHIP has also been notified that it was approved to receive a federal bonus grant award of \$785,565 that will be available to MHIP during fiscal year 2013 for the low income premium subsidy program.

MARYLAND HEALTH INSURANCE PLAN

Notes to Statutory Financial Statements

June 30, 2012 and 2011

NOTE B - SIGNIFICANT ACCOUNTING POLICIES - Continued

Assessments Receivable

Chapter 244, Acts of 2008, *"Health Services Cost Review Commission – Averted Uncompensated Care – Assessment,"* amended subsection 19-219 of the Health – General Article to authorize the Health Service Cost Review Commission to assess a uniform, broad-based, and reasonable amount in hospital rates to a) reflect the aggregate reduction in hospital uncompensated care realized from the expansion of health care coverage under Chapter 7 of the Acts of the General Assembly of 2007, and b) operate and administer MHIP. Hospitals would pay a portion of the assessment reflecting the aggregated reduction in hospital uncompensated care into the Health Care Coverage Fund and the portion of the assessment for operating and administering MHIP assessment funding. The act also sets an assessment floor of 0.8128% of net patient revenue. The overall hospital assessment may not exceed 3% in the aggregate of any hospital's total net regulated patient revenue. Assessments are recognized as non-operating income by MHIP as earned. Assessments receivable represent assessments earned but not yet received as of June 30, 2012 and 2011.

Premium Taxes

Pursuant to Section 14-106(e)(2) of the Insurance Article, CareFirst BlueCross BlueShield ("CareFirst") is required to deposit in the MHIP Fund an amount from its premium tax exemption to administer SPDAP. Pursuant to Chapter 27, Acts of 2012, *"Senior Prescription Drug Program – Sunset Extension,"* and Chapter 119, Acts of 2010, *"Senior Prescription Drug Program – Sunset Extension,"* amounts deposited into the MHIP Fund by CareFirst for the administration of SPDAP totaled \$14,000,000 for each of the years ended June 30, 2012 and 2011. Chapter 557, Acts of 2008, *"Senior Prescription Drug Assistance Program – Subsidy for Medicare Part D Coverage Gap and Sunset Extension"* provides that, among other things, beginning January 1, 2009 and for each calendar year thereafter that if CareFirst has a surplus that exceeds 800% of the consolidated risk-based capital requirements applicable to the corporation in the immediate preceding calendar year, CareFirst shall transfer \$4,000,000 to subsidize a Medicare D benefits gap for costs incurred by SPDAP members.

Chapter 734, Acts of 2009, *"Health Insurance – Senior Prescription Drug Assistance Program – Funding,"* provides that the \$4,000,000 in new funding from CareFirst, pursuant to Chapter 557, Acts of 2008, is a sum to be paid in addition to the \$14,000,000 subsidy that CareFirst already provides to SPDAP. The enactment also makes the following technical and procedural changes to the funding process to address the timing of the transfer of funds: the enactment requires CareFirst to notify SPDAP by September 1 of each year whether CareFirst will provide the additional funding to the program during the calendar year that starts on the immediately following January 1. It also requires CareFirst to pay the additional funding in quarterly installments of \$1,000,000, beginning not later than October 1 for the calendar year that starts on the immediately following January 1.

Chapter 27, Acts of 2012, *"Senior Prescription Drug Program – Sunset Extension,"* requires a premium tax subsidy of \$14,000,000 to be provided to SPDAP through fiscal year 2015.

MARYLAND HEALTH INSURANCE PLAN

Notes to Statutory Financial Statements

June 30, 2012 and 2011

NOTE B - SIGNIFICANT ACCOUNTING POLICIES - Continued

Premium Taxes (Continued)

Amounts deposited into the MHIP fund by CareFirst to fund the administration of SPDAP totaled \$14,000,000 in each of the years ended June 30, 2012 and 2011. Amounts deposited into the MHIP fund to subsidize the Medicare Part D coverage gap subsidy totaled \$4,000,000 in each of the years ended June 30, 2012 and 2011.

Losses, Loss Adjustment Expenses and Loss Reserves

The liability for losses, loss adjustment expenses and loss reserves consists of an aggregation of the estimated liability for incurred losses on claims that are known to the Plan as of the reporting date (claims payable) and an aggregate estimate of the liability for losses incurred (loss reserves) and loss adjustment expenses (LAE) incurred, but not reported, as of the same date. While information is available for the known losses, the liability for which has been established on a case-by-case basis, the unknown losses are based on the best estimate of such liabilities. Although MHIP considers its experience and industry data in determining such reserves, assumptions and projections as to future events are necessary in making these determinations, and ultimate losses may differ significantly in the near term from amounts projected. The effects of changes in reserve estimates are included in results of operations in the period in which estimates are changed. Reserves are not discounted.

Net Assets

Net assets represent the resources available and may be used to fund the liability for unreported losses and LAE, future operating deficiencies, or other specific uses designated by the Board of Directors or the Legislature of the State of Maryland. Net assets can be reserved or designated for specific purposes pursuant to legislative authority.

Coordination of Benefits

Funds obtained through the coordination of benefits with other providers of health care services are included as a reduction of operating losses.

Income Tax Status

MHIP meets the definition of a 501(c)(26) entity under the Internal Revenue Code and is, therefore, exempt from federal income taxes. MHIP is not subject to Maryland state income taxes. Accordingly, the accompanying financial statements do not include a provision or a liability for income taxes.

NOTE C - PERMITTED STATUTORY ACCOUNTING PRACTICES

The Plan, domiciled in Maryland, prepares statutory financial statements in accordance with the accounting practices prescribed or permitted by the insurance administration of that state. Prescribed statutory accounting practices include a variety of publications of the National Association of Insurance Commissioners (NAIC), as well as state laws, regulations and general administrative rules. Permitted statutory accounting practices encompass all accounting practices not so proscribed.

MARYLAND HEALTH INSURANCE PLAN

Notes to Statutory Financial Statements

June 30, 2012 and 2011

NOTE D - CONCENTRATIONS OF CREDIT RISK

The Plan's financial instruments that are exposed to concentrations of credit risk consist primarily of the following:

Cash and cash equivalents – The Plan has cash balances in certain financial institutions in amounts which occasionally exceed federal deposit insurance limits. The financial stability of these institutions is continually reviewed by management. Effective December 31, 2010 and extending through December 31, 2012, all non-interest-bearing transaction accounts are fully insured by the Federal Deposit Insurance Corporation (FDIC) regardless of the balance of the account. Generally, the Plan's cash and cash equivalents in interest-bearing accounts exceed FDIC insurance limits. However, the Plan has not experienced any losses in such accounts and believes that its cash and cash equivalents are not exposed to significant credit risk.

Assessments receivable – Assessments are receivable from multiple hospitals. Included in assessments receivable is an amount from one hospital accounting for approximately twelve and thirteen percent of total assessments receivable at June 30, 2012 and 2011, respectively. Potential credit losses are considered minimal by management.

Contract receivable – The contract receivable is due from a single agency of the U.S. Government at June 30, 2012 and 2011. Potential credit losses are considered minimal by management. Consequently, management has not recorded an allowance for potential credit losses.

Premiums receivable – Premiums are receivable from insured individuals and from one governmental agency of the State of Maryland. At June 30, 2012 and 2011, premiums receivable from a governmental agency of the State of Maryland were \$410,257 and \$1,041,455, respectively. Potential credit losses are considered minimal by management.

NOTE E - ADMINISTRATIVE SERVICE PROVIDERS

MHIP is required by law to contract with a third-party administrator. As of July 1, 2007, CareFirst has been MHIP's third-party administrator, and is currently obligated to continue in that capacity through June 30, 2014. Under the terms of the contract, CareFirst is responsible for all operational functions of the MHIP Plan, including marketing, receiving applications, determining eligibility, enrollment, issuance of certificates, collection of premiums, administering the provider network, data collection, case management, financial tracking and reporting, payment of claims, reporting to the MHIP Board, and premium billing. In exchange for those services, CareFirst is paid a monthly administrative fee for each member, a monthly disease management fee for members in the disease management program, and a monthly producer referral fee for each accepted application assisted by a producer. When claims exceed premiums, CareFirst is reimbursed by MHIP.

MHIP is also required by law to contract with a third-party administrator to administer SPDAP. The MHIP Board contracted with Pool Administrators, Inc. (PAI) as contract administrator of SPDAP effective January 1, 2008 and is currently obligated to continue in that capacity through December 31, 2012. Under the terms of the agreement, PAI is responsible for implementing and administering SPDAP in accordance with Title 14, Subtitle 5, Part II of the Maryland Insurance Article, and in a manner that ensures that SPDAP remains a federally-qualified SPAP. In exchange for these services, PAI is paid administrative fees.

MARYLAND HEALTH INSURANCE PLAN

Notes to Statutory Financial Statements

June 30, 2012 and 2011

NOTE E - ADMINISTRATIVE SERVICE PROVIDERS - Continued

CareFirst is MHIP's third party administrator, and accordingly, they carry out substantially all operational functions of the Federal Pool including marketing, receiving applications, determining eligibility, enrollment, issuance of certificates, billing and collection of premiums, administering the provider network, data collection, case management, financial tracking and reporting, payment of claims and reporting to the MHIP Board. In exchange for those services, CareFirst is paid a monthly administrative fee for each member, a monthly disease management fee for each member in the disease management program, and a monthly producer referral fee for each accepted application assisted by a producer.

NOTE F - PHARMACEUTICAL REBATES RECEIVABLE

| Quarter Ended | Estimated Pharmacy Rebates as Reported on Financial Statements | Pharmacy Rebates as Invoiced/Confirmed | Actual Rebates Collected Within 90 Days of Invoicing/Confirmation | Actual Rebates Collected Within 91 to 180 Days of Invoicing/Confirmation | Actual Rebates Collected More Than 180 Days After Invoicing/Confirmation |
|---------------|--|--|---|--|--|
| 6/30/2012 | \$ 456,900 | \$ - | \$ - | \$ - | \$ - |
| 3/31/2012 | 468,470 | 7,313 | 7,313 | - | - |
| 12/31/2011 | 465,130 | 12,487 | 4,130 | 8,357 | - |
| 9/30/2011 | 487,920 | 487,920 | - | 487,920 | - |
| 6/30/2011 | 450,000 | 537,304 | - | 537,304 | - |
| 3/31/2011 | 450,000 | 489,214 | - | 489,214 | - |
| 12/31/2010 | 450,000 | 457,270 | - | 457,270 | - |
| 9/30/2010 | 415,038 | 415,038 | - | 415,038 | - |
| 6/30/2010 | 450,000 | 452,096 | - | 452,096 | - |
| 3/31/2010 | 450,000 | 378,372 | - | 378,372 | - |
| 12/31/2009 | 452,689 | 452,689 | - | 452,689 | - |
| 9/30/2009 | 543,970 | 543,970 | - | - | 543,970 |

MARYLAND HEALTH INSURANCE PLAN

Notes to Statutory Financial Statements

June 30, 2012 and 2011

NOTE G - LOSSES, LOSS ADJUSTMENT EXPENSES AND LOSS RESERVES

The Plan's liability for losses, loss adjustment expenses and loss reserves consists of an aggregation of the estimated liability for incurred losses on claims that are known to the Plan as of the reporting date (claims payable) and an aggregate estimate of the liability for losses incurred (loss reserves) and loss adjustment expenses (LAE) incurred, but not reported to the Plan, as of the same date. The following is a summary of activity losses, loss adjustment expenses and loss reserves:

| | <u>2012</u> | <u>2011</u> |
|---|----------------------|----------------------|
| Beginning of year | \$ 20,018,000 | \$ 16,147,672 |
| Incurred (recovered) related to: | | |
| Current year | 229,134,746 | 182,841,240 |
| Prior years | <u>(245,810)</u> | <u>(3,300,482)</u> |
| | <u>228,888,936</u> | <u>179,540,758</u> |
| Change in non-admitted assets – pharmaceutical rebates | 13,800 | 450,000 |
| Paid related to: | | |
| Current year | (207,386,446) | (163,095,240) |
| Prior years | <u>(19,619,190)</u> | <u>(13,025,190)</u> |
| | <u>(227,005,636)</u> | <u>(176,120,430)</u> |
| Balance, end of year | <u>\$ 21,915,100</u> | <u>\$ 20,018,000</u> |

The provision for loss and loss adjustment expenses decreased by approximately \$245,000 and \$3,300,000 in fiscal years 2012 and 2011, respectively, as a result of changes in estimates and due to lower than anticipated losses incurred in prior years. Incurred losses are presented net of pharmaceutical rebates of approximately \$2,012,000 and \$1,695,000 for the fiscal years ended June 30, 2012 and 2011, respectively. Paid losses are presented net of pharmaceutical rebates of approximately \$1,993,000 and \$1,245,000 for the fiscal years ended June 30, 2012 and 2011, respectively.

MARYLAND HEALTH INSURANCE PLAN

Notes to Statutory Financial Statements

June 30, 2012 and 2011

NOTE H - NET ASSETS

Section 11 of Chapter 397, Acts of 2011, "*Budget Reconciliation and Financing Act of 2011*," provides that, among other things, and notwithstanding any other provision of the law, the Governor may transfer by budget amendment from the SPDAP account of the MHIP Fund established under Section 14-504 of the Insurance Article to the Kidney Disease Program established under Title 13, Subtitle 3 of the Health – General Article up to \$1,500,000 in fiscal year 2012, and up to \$3,000,000 in fiscal year 2013. Chapter 1 of the "*Budget Reconciliation and Financing Act of 2012*" signed on May 22, 2012, repealed and reenacted, with amendments, Section 11 of Chapter 397, Acts of 2011 and now provides, among other things, and notwithstanding any other provision of the law, the Governor may transfer by budget amendment from the SPDAP account of the MHIP Fund to the Kidney Disease Program up to \$3,000,000 in fiscal year 2012 and up to \$5,000,000 million in fiscal year 2013. Pursuant to this legislation, during fiscal year 2012 designated net assets of SPDAP totaling \$3,000,000 were transferred to the Kidney Disease Program. In addition, \$5,000,000 of SPDAP net assets is classified as "Designated – State of Maryland Kidney Disease Program" in the accompanying June 30, 2012 statutory statement of admitted assets, liabilities and net assets.

Section 5 of Chapter 397, Acts of 2011, "*Budget Reconciliation and Financing Act of 2011*" provides that, among other things, and notwithstanding any other provision of the law, the Governor may transfer by budget amendment from the SPDAP account of the MHIP Fund to the Maryland General Fund up to \$1,500,000 in fiscal year 2012. Pursuant to this legislation, during fiscal year 2012 designated net assets of SPDAP totaling \$1,500,000 were transferred to the Maryland General Fund.

Section 16 of Chapter 1, Acts of 2012, "*Budget Reconciliation and Financing Act of 2012*", approved by the governor on May 22, 2012, provides that, among other things, and notwithstanding any other provisions of the law, the Governor may transfer from the SPDAP account of the MHIP fund to the Medical Assistance Program up to \$4,500,000 in fiscal year 2013. Accordingly, such amounts are classified as "Designated – Medical Assistance Program" in the accompanying statutory statements of admitted assets, liabilities and net assets.

Section 70 of Chapter 395, Acts of 2012, "*Budget Bill of 2012*," signed on May 10, 2011, provides that, among other things, and notwithstanding any other provisions of the law, \$5,000,000 of MHIP net assets are to become available immediately upon passage of the State of Maryland 2012 budget to reduce MHIP's appropriation for fiscal year 2011 due to lower-than-budgeted estimates of actual spending. In addition, this act provides that \$250,000 of SPDAP net assets are to become available immediately upon passage of the State of Maryland 2012 budget to reduce appropriation for fiscal year 2011 due to lower than budgeted estimates of actual spending. Accordingly, such amounts are classified as "Reserved pending legislative authority – Maryland Special Fund" in the accompanying June 30, 2011 statutory statements of admitted assets, liabilities and net assets. During 2012, this provision lapsed and such funds were returned to unreserved and undesignated assets.

Section 24 of Chapter 484, Acts of 2010, "*Budget Reconciliation and Financing Act of 2010*," provided that, among other things, and notwithstanding any other provision of the law, the Governor may transfer by budget amendment from the SPDAP account of the MHIP Fund to the Kidney Disease Program up to \$10,500,000 in fiscal year 2010 and up to \$1,500,000 in fiscal year 2011 and up to \$5,000,000 to the Medical Assistance Program during fiscal year 2010. Pursuant to this legislation, during fiscal year 2011 designated net assets of SPDAP totaling \$1,500,000 were transferred to the Kidney Disease Program and during 2010 designated net assets of SPDAP totaling \$10,500,000 were transferred to the Kidney Disease Program and \$5,000,000 were transferred to the Medical Assistance Program. During fiscal year 2012, unused funds related to these appropriations totaling \$2,928,255 were returned to the SPDAP account of the MHIP Fund and are reflected as a transfer from the Department of Health and Mental Hygiene in the accompanying June 30, 2012 statutory statement of operations and changed in net assets.

MARYLAND HEALTH INSURANCE PLAN

Notes to Statutory Financial Statements
June 30, 2012 and 2011

NOTE I - RELATED PARTY TRANSACTIONS

The State of Maryland receives and disburses cash on behalf of MHIP. The balance of MHIP's cash maintained by the State of Maryland as of June 30, 2012 and 2011 totaled approximately \$167,890,000 and \$164,802,000, respectively.

NOTE J - OPERATING LEASE

MHIP leases office space under an operating lease, which was renewed effective June 12, 2011 and expires in June 2016. Future minimum lease payments under this operating lease total \$67,350 for fiscal years 2013 through 2016. Rent expense under this lease totaled \$66,708 and \$66,866 for the fiscal years ended June 30, 2012 and 2011, respectively.

NOTE K - CONTINGENCIES

MHIP acknowledges that certain claims and legal actions can arise in the ordinary course of business. Management is currently unaware of any such actions against MHIP.

NOTE L - SUBSEQUENT EVENTS

Subsequent events were evaluated through October 1, 2012, which is the date the statutory financial statements were available to be issued.

SUPPLEMENTARY INFORMATION

MARYLAND HEALTH INSURANCE PLAN

Schedule 1 - Statutory Statement of Admitted Assets, Liabilities and Net Assets by Program

June 30, 2012

| | MHIP | Federal Pool | SPDAP | Eliminations | Total |
|--|-----------------------|---------------------|----------------------|--------------------|-----------------------|
| ADMITTED ASSETS | | | | | |
| Cash and cash equivalents | \$ 157,508,284 | \$ 1,823,826 | \$ 23,262,760 | \$ - | \$ 182,594,870 |
| Receivables: | | | | | |
| Assessments | 20,839,977 | - | - | - | 20,839,977 |
| Contract - U.S. Department of Health and Human Services | - | 1,636,508 | - | - | 1,636,508 |
| Federal grants | 1,974,465 | - | - | - | 1,974,465 |
| Premiums | 1,499,864 | 89,132 | - | - | 1,588,996 |
| Pharmaceutical rebates | 450,000 | 6,900 | - | - | 456,900 |
| Due from MHIP Federal | 61,660 | - | - | (61,660) | - |
| Other current assets | 23,762 | - | 114,656 | - | 138,418 |
| | <u>\$ 182,358,012</u> | <u>\$ 3,556,366</u> | <u>\$ 23,377,416</u> | <u>\$ (61,660)</u> | <u>\$ 209,230,134</u> |
| LIABILITIES AND NET ASSETS | | | | | |
| LIABILITIES | | | | | |
| Loss reserves and loss adjustment expenses | \$ 20,502,000 | \$ 1,870,000 | \$ - | \$ - | \$ 22,372,000 |
| Deferred premium tax revenue | - | - | 4,500,000 | - | 4,500,000 |
| Premium subsidies payable | - | - | 8,706,769 | - | 8,706,769 |
| Premiums received in advance | 6,162,987 | 163,752 | - | - | 6,326,739 |
| Accounts payable and accrued expenses | 993,205 | 89,627 | 837,214 | - | 1,920,046 |
| Due to CareFirst BlueCross BlueShield | 4,452,259 | 1,231,045 | - | - | 5,683,304 |
| Other liabilities | 10,000 | - | - | - | 10,000 |
| Due to State of Maryland | - | 2,265,355 | - | - | 2,265,355 |
| Due to MHIP | - | 61,660 | - | (61,660) | - |
| | <u>32,120,451</u> | <u>5,681,439</u> | <u>14,043,983</u> | <u>(61,660)</u> | <u>51,784,213</u> |
| NET ASSETS | | | | | |
| Unreserved and undesignated | 150,237,561 | (2,125,073) | (166,567) | - | 147,945,921 |
| Designated - | | | | | |
| State of Maryland Kidney Disease Program | - | - | 5,000,000 | - | 5,000,000 |
| State of Maryland Medical Assistance Program | - | - | 4,500,000 | - | 4,500,000 |
| | <u>150,237,561</u> | <u>(2,125,073)</u> | <u>9,333,433</u> | <u>-</u> | <u>157,445,921</u> |
| | <u>\$ 182,358,012</u> | <u>\$ 3,556,366</u> | <u>\$ 23,377,416</u> | <u>\$ (61,660)</u> | <u>\$ 209,230,134</u> |

See report of independent certified public accountant.

MARYLAND HEALTH INSURANCE PLAN

Schedule 2 - Statutory Statement of Operations and Changes in Net Assets by Program
For the Year Ended June 30, 2012

| | MHIP | Federal Pool | SPDAP | Total |
|--|-----------------------|-----------------------|---------------------|-----------------------|
| PREMIUMS AND OTHER REVENUES | | | | |
| Premiums | \$ 99,383,158 | \$ 2,559,126 | \$ - | \$ 101,942,284 |
| Contract revenues - U.S. Department of Health and Human Services | - | 13,747,104 | - | 13,747,104 |
| Interest income | 1,790,868 | 292 | 242,580 | 2,033,740 |
| Federal grants | 2,454,495 | - | - | 2,454,495 |
| | <u>103,628,521</u> | <u>16,306,522</u> | <u>242,580</u> | <u>120,177,623</u> |
| BENEFITS PAID OR PROVIDED | | | | |
| Loss and loss adjustment expense | 213,632,921 | 15,256,015 | - | 228,888,936 |
| Premium subsidy expense | - | - | 14,675,649 | 14,675,649 |
| | <u>213,632,921</u> | <u>15,256,015</u> | <u>14,675,649</u> | <u>243,564,585</u> |
| INSURANCE EXPENSES AND OTHER DEDUCTIONS | | | | |
| Program administration expenses | 10,653,593 | 725,660 | 1,991,614 | 13,370,867 |
| Professional and other expenses | 616,168 | 819,567 | 479,303 | 1,915,038 |
| Write-off of uncollectible premiums | 3,177,405 | 90,534 | - | 3,267,939 |
| | <u>14,447,166</u> | <u>1,635,761</u> | <u>2,470,917</u> | <u>18,553,844</u> |
| Loss from operations | <u>(124,451,566)</u> | <u>(585,254)</u> | <u>(16,903,986)</u> | <u>(141,940,806)</u> |
| NON-OPERATING REVENUES | | | | |
| Assessments | 122,296,039 | - | - | 122,296,039 |
| Premium taxes | - | - | 18,000,000 | 18,000,000 |
| | <u>122,296,039</u> | <u>-</u> | <u>18,000,000</u> | <u>140,296,039</u> |
| Change in net assets | (2,155,527) | (585,254) | 1,096,014 | (1,644,767) |
| NET ASSETS, beginning of year | 151,572,822 | (1,525,819) | 9,809,164 | 159,856,167 |
| TRANSFER FROM STATE OF MARYLAND DEPARTMENT OF HEALTH AND MENTAL HYGIENE | | | | |
| | - | - | 2,928,255 | 2,928,255 |
| TRANSFERS FROM RESERVED AND DESIGNATED NET ASSETS | | | | |
| State of Maryland General Fund | - | - | (1,500,000) | (1,500,000) |
| State of Maryland Kidney Disease Program | - | - | (3,000,000) | (3,000,000) |
| CHANGE IN NON-ADMITTED ASSETS | <u>820,266</u> | <u>(14,000)</u> | <u>-</u> | <u>806,266</u> |
| NET ASSETS, end of year | <u>\$ 150,237,561</u> | <u>\$ (2,125,073)</u> | <u>\$ 9,333,433</u> | <u>\$ 157,445,921</u> |

See report of independent certified public accountant.

MARYLAND HEALTH INSURANCE PLAN

Schedule 3 - Statutory Statement of Admitted Assets, Liabilities and Net Assets by Program

June 30, 2011

| | MHIP | Federal Pool | SPDAP | Eliminations | Total |
|---|-----------------------|---------------------|----------------------|--------------------|-----------------------|
| ADMITTED ASSETS | | | | | |
| Cash and cash equivalents | \$ 150,904,593 | \$ 313,998 | \$ 20,771,118 | \$ - | \$ 171,989,709 |
| Receivables: | | | | | |
| Assessments | 19,267,652 | - | - | - | 19,267,652 |
| Contract - U.S. Department of Health and Human Services | - | 1,148,143 | - | - | 1,148,143 |
| Federal grant | 2,374,230 | - | - | - | 2,374,230 |
| Premiums | 5,138,990 | 43,333 | - | - | 5,182,323 |
| Pharmaceutical rebates | 450,000 | - | - | - | 450,000 |
| Due from MHIP Federal | 61,660 | - | - | (61,660) | - |
| Other current assets | 30,599 | - | 349,281 | - | 379,880 |
| | <u>\$ 178,227,724</u> | <u>\$ 1,505,474</u> | <u>\$ 21,120,399</u> | <u>\$ (61,660)</u> | <u>\$ 200,791,937</u> |
| LIABILITIES AND NET ASSETS | | | | | |
| LIABILITIES | | | | | |
| Loss reserves and loss adjustment expenses | \$ 19,048,000 | \$ 1,420,000 | \$ - | \$ - | \$ 20,468,000 |
| Deferred premium tax revenue | - | - | 4,500,000 | - | 4,500,000 |
| Premium subsidies payable | - | - | 6,078,081 | - | 6,078,081 |
| Premiums received in advance | 4,757,086 | 72,941 | - | - | 4,830,027 |
| Accounts payable and accrued expenses | 1,964,822 | 76,281 | 733,154 | - | 2,774,257 |
| Due to CareFirst BlueCross BlueShield | 874,994 | 167,248 | - | - | 1,042,242 |
| Other liabilities | 10,000 | - | - | - | 10,000 |
| Due to State of Maryland | - | 1,233,163 | - | - | 1,233,163 |
| Due to MHIP | - | 61,660 | - | (61,660) | - |
| | <u>26,654,902</u> | <u>3,031,293</u> | <u>11,311,235</u> | <u>(61,660)</u> | <u>40,935,770</u> |
| NET ASSETS | | | | | |
| Unreserved and undesignated | 146,572,822 | (1,525,819) | 9,559,164 | - | 154,606,167 |
| Reserved pending legislative authority - Maryland Special Fund | 5,000,000 | - | 250,000 | - | 5,250,000 |
| | <u>151,572,822</u> | <u>(1,525,819)</u> | <u>9,809,164</u> | <u>-</u> | <u>159,856,167</u> |
| | <u>\$ 178,227,724</u> | <u>\$ 1,505,474</u> | <u>\$ 21,120,399</u> | <u>\$ (61,660)</u> | <u>\$ 200,791,937</u> |

See report of independent certified public accountant.

MARYLAND HEALTH INSURANCE PLAN

Schedule 4 - Statutory Statement of Operations and Changes in Net Assets by Program
For the Year Ended June 30, 2011

| | MHIP | Federal Pool | SPDAP | Total |
|---|-----------------------|-----------------------|---------------------|-----------------------|
| PREMIUMS AND OTHER REVENUES | | | | |
| Premiums | \$ 86,286,946 | \$ 574,850 | \$ - | \$ 86,861,796 |
| Contract revenues - U.S. Department of Health and Human Services | - | 3,764,824 | - | 3,764,824 |
| Interest income | 2,981,344 | 38 | 323,344 | 3,304,726 |
| Federal grants | 2,856,550 | - | - | 2,856,550 |
| | <u>92,124,840</u> | <u>4,339,712</u> | <u>323,344</u> | <u>96,787,896</u> |
| BENEFITS PAID OR PROVIDED | | | | |
| Loss and loss adjustment expenses | 174,382,712 | 5,158,046 | - | 179,540,758 |
| Premium subsidy expense | - | - | 13,347,135 | 13,347,135 |
| | <u>174,382,712</u> | <u>5,158,046</u> | <u>13,347,135</u> | <u>192,887,893</u> |
| INSURANCE EXPENSES AND OTHER DEDUCTIONS | | | | |
| Program administration expenses | 10,416,540 | 388,038 | 1,663,795 | 12,468,373 |
| Professional and other expenses | 1,558,216 | 305,803 | 824,296 | 2,688,315 |
| Write-off of uncollectible premiums | 2,140,495 | 13,644 | - | 2,154,139 |
| | <u>14,115,251</u> | <u>707,485</u> | <u>2,488,091</u> | <u>17,310,827</u> |
| Loss from operations | <u>(96,373,123)</u> | <u>(1,525,819)</u> | <u>(15,511,882)</u> | <u>(113,410,824)</u> |
| NON-OPERATING REVENUES | | | | |
| Assessments | 116,368,118 | - | - | 116,368,118 |
| Premium taxes | - | - | 18,000,000 | 18,000,000 |
| | <u>116,368,118</u> | <u>-</u> | <u>18,000,000</u> | <u>134,368,118</u> |
| Change in net assets | 19,994,995 | (1,525,819) | 2,488,118 | 20,957,294 |
| NET ASSETS, beginning of year | 132,003,957 | - | 8,821,046 | 140,825,003 |
| TRANSFERS FROM RESERVED AND DESIGNATED NET ASSETS | | | | |
| State of Maryland Kidney Disease Program | - | - | (1,500,000) | (1,500,000) |
| CHANGE IN NON-ADMITTED ASSETS | <u>(426,130)</u> | <u>-</u> | <u>-</u> | <u>(426,130)</u> |
| NET ASSETS, end of year | <u>\$ 151,572,822</u> | <u>\$ (1,525,819)</u> | <u>\$ 9,809,164</u> | <u>\$ 159,856,167</u> |

See report of independent certified public accountant.