CENTENE CORP
Form 10-Q
April 25, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2017
OR
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number: 001-31826

CENTENE CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	42-1406317
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

7700 Forsyth Boulevard	
St. Louis, Missouri	63105
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code:
(314) 725-4477

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: x Yes o No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x Yes o No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer”, “accelerated filer” and “small reporting company” in Rule 12b-2 of the Exchange Act. Large accelerated filer x Accelerated filer o Non-accelerated filer o (do not check if a smaller reporting company) Smaller reporting company o Emerging growth company o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes o No x

As of April 14, 2017, the registrant had 172,277,703 shares of common stock outstanding.

CENTENE CORPORATION
QUARTERLY REPORT ON FORM 10-Q
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CAUTIONARY STATEMENT ON FORWARD-LOOKING STATEMENTS

All statements, other than statements of current or historical fact, contained in this filing or incorporated by reference herein are forward-looking statements. We intend such forward looking statements to be covered by the safe-harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and we are including this statement for purposes of complying with these safe-harbor provisions. We have attempted to identify these statements by terminology including “believe,” “anticipate,” “plan,” “expect,” “estimate,” “intend,” “seek,” “targ “may,” “will,” “would,” “could,” “should,” “can,” “continue” and other similar words or expressions (and the negative thereof) connection with, among other things, any discussion of future operating or financial performance. In particular, these statements include without limitation statements about our market opportunity, our growth strategy, competition, expected activities and future acquisitions, investments and the adequacy of our available cash resources. These statements may be found in the various sections of this filing, such as Part I, Item 2. “Management's Discussion and Analysis of Financial Condition and Results of Operations,” Part II, Item 1. “Legal Proceedings,” and Part II, Item 1A. “Risk Factors.” Readers are cautioned that matters subject to forward-looking statements involve known and unknown risks and uncertainties, including economic, regulatory, competitive and other factors that may cause our or our industry’s actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. These statements are not guarantees of future performance and are subject to risks, uncertainties and assumptions.

All forward-looking statements included in this filing are based on information available to us on the date of this filing. Except as may be otherwise required by law, we undertake no obligation to update or revise the forward-looking statements included in this filing, whether as a result of new information, future events or otherwise, after the date of this filing. You should not place undue reliance on any forward looking statements, as actual results may differ materially from projections, estimates, or other forward-looking statements due to a variety of important factors, including but not limited to:

- our ability to accurately predict and effectively manage health benefits and other operating expenses and reserves;
- competition;
- membership and revenue declines or unexpected trends;
- changes in healthcare practices, new technologies, and advances in medicine;
- increased health care costs;
- changes in economic, political or market conditions;
- changes in federal or state laws or regulations, including changes with respect to government health care programs as well as changes with respect to the Patient Protection and Affordable Care Act and the Health Care and Education Affordability Reconciliation Act and any regulations enacted thereunder that may result from changing political conditions;
- rate cuts or other payment reductions or delays by governmental payors and other risks and uncertainties affecting our government businesses;
- our ability to adequately price products on federally facilitated and state based Health Insurance Marketplaces;
- tax matters;
- disasters or major epidemics;
- the outcome of legal and regulatory proceedings;
- changes in expected contract start dates;
- provider, state, federal and other contract changes and timing of regulatory approval of contracts;
- the expiration, suspension, or termination of our contracts with federal or state governments (including but not limited to Medicaid, Medicare, and TRICARE);
- challenges to our contract awards;
- cyber-attacks or other privacy or data security incidents;

- the possibility that the expected synergies and value creation from acquired businesses, including, without limitation, the acquisition of Health Net, Inc. (Health Net), will not be realized, or will not be realized within the expected time period, including, but not limited to, as a result of conditions, terms, obligations or restrictions imposed by regulators in connection with their approval of, or consent to, the acquisition;
- the exertion of management's time and our resources, and other expenses incurred and business changes required in connection with complying with the undertakings in connection with certain regulatory approvals;
- disruption from the acquisition making it more difficult to maintain business and operational relationships;
- the risk that unexpected costs will be incurred in connection with, among other things, the acquisition and/or the integration;
- changes in expected closing dates, estimated purchase price and accretion for acquisitions;
- the risk that acquired businesses will not be integrated successfully;
- our ability to maintain or achieve improvement in the Centers for Medicare and Medicaid Services (CMS) Star ratings and other quality scores that impact revenue;
- availability of debt and equity financing, on terms that are favorable to us;

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- inflation; and
- foreign currency fluctuations.

This list of important factors is not intended to be exhaustive. We discuss certain of these matters more fully, as well as certain other risk factors that may affect our business operations, financial condition and results of operations, in our filings with the Securities and Exchange Commission, including our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K. Item 1A. “Risk Factors” of Part II of this filing contains a further discussion of these and other important factors that could cause actual results to differ from expectations. Due to these important factors and risks, we cannot give assurances with respect to our future performance, including without limitation our ability to maintain adequate premium levels or our ability to control our future medical costs.

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Non-GAAP Financial Presentation

The Company is providing certain non-GAAP financial measures in this report as the Company believes that these figures are helpful in allowing investors to more accurately assess the ongoing nature of the Company's operations and measure the Company's performance more consistently across periods. The Company uses the presented non-GAAP financial measures internally to allow management to focus on period-to-period changes in the Company's core business operations. Therefore, the Company believes that this information is meaningful in addition to the information contained in the GAAP presentation of financial information. The presentation of this additional non-GAAP financial information is not intended to be considered in isolation or as a substitute for the financial information prepared and presented in accordance with GAAP.

Specifically, the Company believes the presentation of non-GAAP financial information that excludes amortization of acquired intangible assets, Health Net acquisition related expenses, as well as other items, allows investors to develop a more meaningful understanding of the Company's performance over time. The tables below provide reconciliations of non-GAAP items ($ in millions, except per share data):

	Three Months Ended March 31,	
	2017	2016
GAAP net earnings (loss) from continuing operations	$139	$(15)
Amortization of acquired intangible assets	40	9
Health Net acquisition related expenses	5	189
Penn Treaty assessment expense	47	—
Income tax effects of adjustments [1]	(34)	(87)
Adjusted net earnings from continuing operations	$197	$96
GAAP diluted earnings (loss) per share (EPS)	$0.79	$(0.12)
Amortization of acquired intangible assets [2]	0.14	0.04
Health Net acquisition related expenses [3]	0.02	0.82
Penn Treaty assessment expense [4]	0.17	—
Adjusted Diluted EPS from continuing operations	$1.12	$0.74

(1) The income tax effects of adjustments are based on the effective income tax rates applicable to adjusted (non-GAAP) results.

(2) The amortization of acquired intangible assets per diluted share are net of an income tax benefit of $0.09 and $0.03 for the three months ended March 31, 2017 and 2016, respectively.

(3) The Health Net acquisition related expenses per diluted share are net of an income tax benefit of $0.01 and $0.64 for the three months ended March 31, 2017 and 2016, respectively.

(4) The Penn Treaty assessment expense per diluted share is net of an income tax benefit of $0.09 for the three months ended March 31, 2017. For a further discussion of the Penn Treaty assessment, see Note 9, Contingencies.

	Three Months Ended March 31,	
	2017	2016
GAAP selling, general and administrative expenses	$1,091	$722
Health Net acquisition related expenses	5	189

Penn Treaty assessment expense	47	—
Adjusted selling, general and administrative expenses	$1,039	$533

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PART I
FINANCIAL INFORMATION

ITEM 1. Financial Statements.
CENTENE CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In millions, except share data)

	March 31, 2017 (Unaudited)	December 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	$ 4,839	$ 3,930
Premium and related receivables	3,121	3,098
Short-term investments	725	505
Other current assets	723	832
Total current assets	9,408	8,365
Long-term investments	4,636	4,545
Restricted deposits	140	138
Property, software and equipment, net	841	797
Goodwill	4,712	4,712
Intangible assets, net	1,504	1,545
Other long-term assets	121	95
Total assets	$ 21,362	$ 20,197
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Medical claims liability	$ 4,290	$ 3,929
Accounts payable and accrued expenses	4,275	4,377
Unearned revenue	633	313
Current portion of long-term debt	4	4
Total current liabilities	9,202	8,623
Long-term debt	4,643	4,651
Other long-term liabilities	1,295	869
Total liabilities	15,140	14,143
Commitments and contingencies		
Redeemable noncontrolling interests	138	145
Stockholders' equity:		
Preferred stock, $0.001 par value; authorized 10,000,000 shares; no shares issued or outstanding at March 31, 2017 and December 31, 2016	—	—
Common stock, $0.001 par value; authorized 400,000,000 shares; 178,669,935 issued and 172,271,202 outstanding at March 31, 2017, and 178,134,306 issued and 171,919,071 outstanding at December 31, 2016	—	—
Additional paid-in capital	4,224	4,190
Accumulated other comprehensive loss	(21)	(36)
Retained earnings	2,059	1,920
Treasury stock, at cost (6,398,733 and 6,215,235 shares, respectively)	(192)	(179)
Total Centene stockholders' equity	6,070	5,895
Noncontrolling interest	14	14

Total stockholders' equity	6,084	5,909
Total liabilities and stockholders' equity	$ 21,362	$ 20,197

The accompanying notes to the consolidated financial statements are an integral part of these statements.

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CENTENE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In millions, except share data)
(Unaudited)

	Three Months Ended March 31, 2017	Three Months Ended March 31, 2016
Revenues:		
Premium	$10,638	$ 5,986
Service	527	425
Premium and service revenues	11,165	6,411
Premium tax and health insurer fee	559	542
Total revenues	11,724	6,953
Expenses:		
Medical costs	9,322	5,311
Cost of services	441	367
Selling, general and administrative expenses	1,091	722
Amortization of acquired intangible assets	40	9
Premium tax expense	590	450
Health insurer fee expense	—	74
Total operating expenses	11,484	6,933
Earnings from operations	240	20
Other income (expense):		
Investment and other income	41	15
Interest expense	(62)	(33)
Earnings from continuing operations, before income tax expense	219	2
Income tax expense	87	16
Earnings (loss) from continuing operations, net of income tax expense	132	(14)
Discontinued operations, net of income tax (benefit)	—	(1)
Net earnings (loss)	132	(15)
(Earnings) loss attributable to noncontrolling interests	7	(1)
Net earnings (loss) attributable to Centene Corporation	$139	$ (16)
Amounts attributable to Centene Corporation common shareholders:		
Earnings (loss) from continuing operations, net of income tax expense	$139	$ (15)
Discontinued operations, net of income tax (benefit)	—	(1)
Net earnings (loss)	$139	$ (16)
Net earnings (loss) per common share attributable to Centene Corporation:		
Basic:		
Continuing operations	$0.81	$ (0.12)
Discontinued operations	—	(0.01)
Basic earnings (loss) per common share	$0.81	$ (0.13)
Diluted:		
Continuing operations	$0.79	$ (0.12)
Discontinued operations	—	(0.01)
Diluted earnings (loss) per common share	$0.79	$ (0.13)

Weighted average number of common shares outstanding:		
Basic	172,073,968	125,543,076
Diluted	175,836,290	125,543,076

The accompanying notes to the consolidated financial statements are an integral part of these statements.

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CENTENE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS
(In millions)
(Unaudited)

	Three Months Ended March 31,	
	2017	2016
Net earnings (loss)	$132	$(15)
Reclassification adjustment, net of tax	—	1
Change in unrealized gain on investments, net of tax	14	18
Foreign currency translation adjustments	1	1
Other comprehensive earnings	15	20
Comprehensive earnings	147	5
Comprehensive (earnings) loss attributable to noncontrolling interests	7	(1)
Comprehensive earnings attributable to Centene Corporation	$154	$4

The accompanying notes to the consolidated financial statements are an integral part of these statements.

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CENTENE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS’ EQUITY
(In millions, except share data)
(Unaudited)

Three Months Ended March 31, 2017

	Centene Stockholders’ Equity								
	Common Stock					Treasury Stock			
	$.001 Par Value Shares	Amt	Additional Paid-in Capital	Accumulated Other Comprehensive Earnings (Loss)	Retained Earnings	$.001 Par Value Shares	Amt	Non-controlling Interest	Total
Balance, December 31, 2016	178,134,306	$ —	$ 4,190	$ (36)	$ 1,920	6,215,235	$ (179)	$ 14	$ 5,909
Comprehensive Earnings:									
Net earnings	—	—	—	—	139	—	—	—	139
Other comprehensive earnings, net of $8 tax	—	—	—	15	—	—	—	—	15
Common stock issued for employee benefit plans	535,629	—	2	—	—	—	—	—	2
Common stock repurchases	—	—	—	—	—	183,498	(13)	—	(13)
Stock compensation expense	—	—	32	—	—	—	—	—	32
Balance, March 31, 2017	178,669,935	$ —	$ 4,224	$ (21)	$ 2,059	6,398,733	$ (192)	$ 14	$ 6,084

The accompanying notes to the consolidated financial statements are an integral part of this statement.

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CENTENE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions)
(Unaudited)

	Three Months Ended March 31,	
	2017	2016
Cash flows from operating activities:		
Net earnings (loss)	$132	$(15)
Adjustments to reconcile net earnings (loss) to net cash provided by operating activities		
Depreciation and amortization	86	35
Stock compensation expense	32	51
Deferred income taxes	(51)	(17)
Gain on contingent consideration	—	(1)
Changes in assets and liabilities		
Premium and related receivables	59	(174)
Other assets	89	(46)
Medical claims liabilities	358	196
Unearned revenue	320	(64)
Accounts payable and accrued expenses	(237)	35
Other long-term liabilities	459	192
Other operating activities, net	1	4
Net cash provided by operating activities	1,248	196
Cash flows from investing activities:		
Capital expenditures	(83)	(45)
Purchases of investments	(594)	(212)
Sales and maturities of investments	349	203
Investments in acquisitions, net of cash acquired	—	(782)
Other investing activities, net	(1)	—
Net cash used in investing activities	(329)	(836)
Cash flows from financing activities:		
Proceeds from long-term debt	560	3,790
Payments of long-term debt	(560)	(1,388)
Common stock repurchases	(13)	(22)
Debt issuance costs	—	(51)
Other financing activities, net	3	(13)
Net cash (used in) provided by financing activities	(10)	2,316
Net increase in cash and cash equivalents	909	1,676
Cash and cash equivalents, beginning of period	3,930	1,760
Cash and cash equivalents, end of period	$4,839	$3,436
Supplemental disclosures of cash flow information:		
Interest paid	$72	$3
Income taxes paid	$2	$33
Equity issued in connection with acquisitions	$—	$3,105

The accompanying notes to the consolidated financial statements are an integral part of these statements.

CENTENE CORPORATION AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in millions, except share data)
(Unaudited)

1. Organization and Operations

Basis of Presentation

The accompanying interim financial statements have been prepared under the presumption that users of the interim financial information have either read or have access to the audited financial statements included in the Form 10-K for the fiscal year ended December 31, 2016. The unaudited interim financial statements herein have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, footnote disclosures which would substantially duplicate the disclosures contained in the December 31, 2016 audited financial statements have been omitted from these interim financial statements where appropriate. In the opinion of management, these financial statements reflect all adjustments, consisting only of normal recurring adjustments, which are necessary for a fair presentation of the results of the interim periods presented.

Certain 2016 amounts in the consolidated financial statements and notes to the consolidated financial statements have been reclassified to conform to the 2017 presentation. The Company adopted Accounting Standards Update (ASU) 2016-09, Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting during the fourth quarter of 2016. The ASU simplifies several aspects of the accounting for employee share-based payment transactions. Among other elements, the ASU requires an entity to recognize all excess tax benefits and deficiencies related to stock-based compensation expense as income tax expense or benefit in the statements of operations. The ASU requires adjustments be reflected as of the beginning of the fiscal year of adoption and as a result, prior periods have been restated accordingly. The adoption resulted in a decrease to income tax expense of $1 million for the three months ended March 31, 2016.

In January 2017, the Company reclassified Cenpatico Behavioral Health of Arizona, LLC and the related Cenpatico Integrated Care health plan from the Specialty Services segment to the Managed Care segment due to a reorganization of the Arizona management structure following the Health Net integration. As a result, the financial results of Cenpatico Behavioral Health of Arizona, LLC and the related Cenpatico Integrated Care health plan have been reclassified from the Specialty Services segment to the Managed Care segment for all periods presented.

On March 24, 2016, the Company completed the acquisition of Health Net, Inc. (Health Net) for $6.0 billion, including the assumption of debt. The acquisition was accounted for as a business combination, which requires that assets acquired and liabilities assumed be recognized at their fair values as of the acquisition date. The valuation of all the assets acquired and liabilities assumed was finalized in the fourth quarter of 2016. As a result of the completion of the Health Net acquisition, the Company's results of operations for the three months ended March 31, 2016 include the results of operations of Health Net from March 24, 2016 to March 31, 2016.

Accounting Guidance Not Yet Adopted

In March 2017, the Financial Accounting Standards Board (FASB) issued an ASU which changes the period over which premiums on callable debt securities are amortized. The new standard requires the premiums on callable debt securities to be amortized to the earliest call date rather than to the contractual maturity date of the instrument. The new guidance more closely aligns the amortization period of premiums to expectations incorporated in the market pricing on the underlying securities. The new guidance is effective for annual and interim periods beginning after December 15, 2018. Early adoption is permitted. The new guidance is not expected to have a material impact on the

Company's consolidated financial position, results of operations or cash flows.

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In May 2014, the FASB issued an ASU which supersedes existing revenue recognition standards with a single model unless those contracts are within the scope of other standards (e.g., an insurance entity's insurance contracts). Under the new standard, recognition of revenue occurs when a customer obtains control of promised goods or services in an amount that reflects the consideration which the entity expects to receive in exchange for those goods or services. In addition, the standard requires disclosure of the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The new effective date is for annual and interim periods beginning after December 15, 2017. Early adoption is permitted. The Company is currently analyzing selected contracts to determine the impact of the new guidance and anticipates adopting the new guidance in the first quarter of 2018 using the modified retrospective approach with a cumulative-effect adjustment to retained earnings in the period of initial application. The Company also plans to elect the practical expedient of applying the new guidance only to contracts that are not completed as of the date of initial application. The majority of the Company's revenues are derived from insurance contracts and are excluded from the new standard; therefore, the new guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

2. Short-term and Long-term Investments, Restricted Deposits

Short-term and long-term investments and restricted deposits by investment type consist of the following ($ in millions):

	March 31, 2017				December 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$365	$ —	$ (1)	$364	$364	$ —	$ (1)	$363
Corporate securities	2,034	14	(9)	2,039	1,933	12	(13)	1,932
Restricted certificates of deposit	5	—	—	5	5	—	—	5
Restricted cash equivalents	12	—	—	12	6	—	—	6
Municipal securities	1,908	3	(22)	1,889	1,767	1	(35)	1,733
Asset-backed securities	331	1	(1)	331	317	1	(1)	317
Residential mortgage-backed securities	231	1	(5)	227	219	1	(5)	215
Commercial mortgage-backed securities	347	1	(5)	343	343	—	(5)	338
Cost and equity method investments	169	—	—	169	163	—	—	163
Life insurance contracts	122	—	—	122	116	—	—	116
Total	$5,524	$ 20	$ (43)	$5,501	$5,233	$ 15	$ (60)	$5,188

The Company’s investments are classified as available-for-sale with the exception of life insurance contracts and certain cost and equity method investments. The Company’s investment policies are designed to provide liquidity, preserve capital and maximize total return on invested assets with the focus on high credit quality securities. The Company limits the size of investment in any single issuer other than U.S. treasury securities and obligations of U.S. government corporations and agencies. As of March 31, 2017, 96% of the Company’s investments in rated securities carry an investment grade rating by S&P and Moody’s. At March 31, 2017, the Company held certificates of deposit, life insurance contracts and cost and equity method investments which did not carry a credit rating.

The Company's residential mortgage-backed securities are primarily issued by the Federal National Mortgage Association, Government National Mortgage Association or Federal Home Loan Mortgage Corporation, which carry implicit or explicit guarantees of the U.S. government. The Company's commercial mortgage-backed securities are primarily senior tranches with a weighted average rating of AA+ and a weighted average duration of 4.0 years at March 31, 2017.

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The fair value of available-for-sale investments with gross unrealized losses by investment type and length of time that individual securities have been in a continuous unrealized loss position were as follows ($ in millions):

	March 31, 2017				December 31, 2016			
	Less Than 12 Months		12 Months or More		Less Than 12 Months		12 Months or More	
	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$(1)	$311	$—	$3	$(1)	$215	$—	$2
Corporate securities	(9)	806	—	30	(12)	1,020	(1)	39
Municipal securities	(22)	1,177	—	39	(35)	1,423	—	30
Asset-backed securities	(1)	127	—	14	(1)	101	—	18
Residential mortgage-backed securities	(4)	175	(1)	16	(5)	188	—	—
Commercial mortgage-backed securities	(4)	258	(1)	15	(5)	271	—	—
Total	$(41)	$2,854	$(2)	$117	$(59)	$3,218	$(1)	$89

As of March 31, 2017, the gross unrealized losses were generated from 1,682 positions out of a total of 2,985 positions. The change in fair value of fixed income securities is primarily a result of movement in interest rates subsequent to the purchase of the security.

For each security in an unrealized loss position, the Company assesses whether it intends to sell the security or if it is more likely than not the Company will be required to sell the security before recovery of the amortized cost basis for reasons such as liquidity, contractual or regulatory purposes. If the security meets this criterion, the decline in fair value is other-than-temporary and is recorded in earnings. The Company does not intend to sell these securities prior to maturity and it is not likely that the Company will be required to sell these securities prior to maturity; therefore, there is no indication of other-than-temporary impairment for these securities.

The contractual maturities of short-term and long-term investments and restricted deposits are as follows ($ in millions):

	March 31, 2017				December 31, 2016			
	Investments		Restricted Deposits		Investments		Restricted Deposits	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
One year or less	$656	$656	$92	$92	$500	$500	$91	$91
One year through five years	1,967	1,967	48	48	1,982	1,974	47	47
Five years through ten years	1,636	1,621	—	—	1,101	1,089	—	—
Greater than ten years	216	216	—	—	633	617	—	—
Asset-backed securities	909	901	—	—	879	870	—	—
Total	$5,384	$5,361	$140	$140	$5,095	$5,050	$138	$138

Actual maturities may differ from contractual maturities due to call or prepayment options. Cost and equity method investments and life insurance contracts are included in the five years through ten years category. The Company has an option to redeem at amortized cost substantially all of the securities included in the greater than ten years category listed above.

The Company continuously monitors investments for other-than-temporary impairment. Certain investments have experienced a decline in fair value due to changes in credit quality, market interest rates and/or general economic conditions. The Company recognizes an impairment loss for cost and equity method investments when evidence demonstrates that it is other-than-temporarily impaired. Evidence of a loss in value that is other-than-temporary may include the absence of an ability to recover the carrying amount of the investment or the inability of the investee to sustain a level of earnings that would justify the carrying amount of the investment.

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3. Fair Value Measurements

Assets and liabilities recorded at fair value in the Consolidated Balance Sheets are categorized based upon observable or unobservable inputs used to estimate fair value. Level inputs are as follows:

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

The following table summarizes fair value measurements by level at March 31, 2017, for assets and liabilities measured at fair value on a recurring basis ($ in millions):

	Level I	Level II	Level III	Total
Assets				
Cash and cash equivalents	$4,839	$—	$—	$4,839
Investments available for sale:				
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$237	$4	$—	$241
Corporate securities	—	2,039	—	2,039
Municipal securities	—	1,889	—	1,889
Asset-backed securities	—	331	—	331
Residential mortgage-backed securities	—	227	—	227
Commercial mortgage-backed securities	—	343	—	343
Total investments	$237	$4,833	$—	$5,070
Restricted deposits available for sale:				
Cash and cash equivalents	$12	$—	$—	$12
Certificates of deposit	5	—	—	5
U.S. Treasury securities and obligations of U.S. government corporations and agencies	123	—	—	123
Total restricted deposits	$140	$—	$—	$140
Other long-term assets: Interest rate swap agreements	$—	$3	$—	$3
Total assets at fair value	$5,216	$4,836	$—	$10,052
Liabilities				
Other long term liabilities:				
Interest rate swap agreements	$—	$72	$—	$72
Total liabilities at fair value	$—	$72	$—	$72

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The following table summarizes fair value measurements by level at December 31, 2016, for assets and liabilities measured at fair value on a recurring basis ($ in millions):

	Level I	Level II	Level III	Total
Assets				
Cash and cash equivalents	$3,930	$—	$ —	$3,930
Investments available for sale:				
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$221	$15	$ —	$236
Corporate securities	—	1,932	—	1,932
Municipal securities	—	1,733	—	1,733
Asset-backed securities	—	317	—	317
Residential mortgage-backed securities	—	215	—	215
Commercial mortgage-backed securities	—	338	—	338
Total investments	$221	$4,550	$ —	$4,771
Restricted deposits available for sale:				
Cash and cash equivalents	$6	$—	$ —	$6
Certificates of deposit	5	—	—	5
U.S. Treasury securities and obligations of U.S. government corporations and agencies	127	—	—	127
Total restricted deposits	$138	$—	$ —	$138
Other long-term assets:				
Interest rate swap agreements	$—	$4	$ —	$4
Total assets at fair value	$4,289	$4,554	$ —	$8,843
Liabilities				
Other long-term liabilities:				
Interest rate swap agreements	$—	$62	$ —	$62
Total liabilities at fair value	$—	$62	$ —	$62

The Company periodically transfers U.S. Treasury securities and obligations of U.S. government corporations and agencies between Level I and Level II fair value measurements dependent upon the level of trading activity for the specific securities at the measurement date. The Company's policy regarding the timing of transfers between Level I and Level II is to measure and record the transfers at the end of the reporting period. At March 31, 2017, there were $4 million of transfers from Level I to Level II and $15 million of transfers from Level II to Level I. The Company utilizes matrix pricing services to estimate fair value for securities which are not actively traded on the measurement date. The Company designates these securities as Level II fair value measurements. The aggregate carrying amount of the Company's life insurance contracts and other non-majority owned investments, which approximates fair value, was $291 million and $279 million as of March 31, 2017 and December 31, 2016, respectively.

4. Medical Claims Liability

In January 2017, the Company reclassified Cenpatico Behavioral Health of Arizona, LLC and the related Cenpatico Integrated Care health plan from the Specialty Services segment to the Managed Care segment due to a reorganization of the Arizona management structure following the Health Net integration. As a result, the financial results of Cenpatico Behavioral Health of Arizona, LLC and the related Cenpatico Integrated Care health plan have been reclassified from the Specialty Services segment to the Managed Care segment for all periods presented. Due to this change in segment reporting, the Specialty Services segment now has an insignificant amount of medical claims liability and therefore disclosures related to medical claims liabilities have been aggregated and are presented on a consolidated basis.

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The following table summarizes the change in medical claims liability ($ in millions):

	Three Months Ended March 31,	
	2017	2016
Balance, January 1	$3,929	$2,298
Less: Reinsurance Recoverable	5	—
Balance, January 1, net	3,924	2,298
Acquisitions	—	1,370
Incurred related to:		
Current year	9,557	5,478
Prior years	(235)	(167)
Total incurred	9,322	5,311
Paid related to:		
Current year	5,973	3,391
Prior years	2,991	1,725
Total paid	8,964	5,116
Balance at March 31, net	4,282	3,863
Plus: Reinsurance Recoverable	8	—
Balance, March 31	$4,290	$3,863

Reinsurance recoverables related to medical claims are included in premium and related receivables. Changes in estimates of incurred claims for prior years are primarily attributable to reserving under moderately adverse conditions. Additionally, as a result of minimum HBR and other return of premium programs, approximately $3 million and $17 million of the "Incurred related to: Prior years" was recorded as a reduction to premium revenues in the three months ended March 31, 2017 and 2016, respectively.

Incurred but not reported (IBNR) plus expected development on reported claims as of March 31, 2017 was $3,288 million. Total IBNR plus expected development on reported claims represents estimates for claims incurred but not reported, development on reported claims, and estimates for the costs necessary to process unpaid claims at the end of each period. We estimate our liability using actuarial methods that are commonly used by health insurance actuaries and meet Actuarial Standards of Practice. These actuarial methods consider factors such as historical data for payment patterns, cost trends, product mix, seasonality, utilization of healthcare services and other relevant factors.

5. Affordable Care Act

The Affordable Care Act (ACA) established risk spreading premium stabilization programs effective January 1, 2014. These programs, commonly referred to as the “three Rs,” include a permanent risk adjustment program, a transitional reinsurance program, and a temporary risk corridor program. Additionally, the ACA established a minimum annual medical loss ratio (MLR) and cost sharing reductions. Each of the three R programs are taken into consideration to determine if the Company’s estimated annual medical costs are less than the minimum loss ratio and require an adjustment to Premium revenue to meet the minimum MLR. The 2016 benefit year was the final year for transitional reinsurance and risk corridor. No additional balances were recorded for the 2017 benefit year for these programs.

The Company's receivables (payables) for each of these programs are as follows ($ in millions):

	March 31, 2017	December 31, 2016
Risk adjustment	$ (735)	$ (425)
Reinsurance	90	122

Risk corridor	(5)	(3)
Minimum MLR	(13)	(18)
Cost sharing reductions	(199)	(147)

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6. Debt

Debt consists of the following ($ in millions):

	March 31, 2017	December 31, 2016
$1,400 million 5.625% Senior notes, due February 15, 2021	$ 1,400	$ 1,400
$1,000 million 4.75% Senior notes, due May 15, 2022	1,008	1,008
$1,000 million 6.125% Senior notes, due February 15, 2024	1,000	1,000
$1,200 million 4.75% Senior notes, due January 15, 2025	1,200	1,200
Fair value of interest rate swap agreements	(69)	(58)
Total senior notes	4,539	4,550
Revolving credit agreement	100	100
Mortgage notes payable	63	64
Capital leases and other	18	18
Debt issuance costs	(73)	(77)
Total debt	4,647	4,655
Less current portion	(4)	(4)
Long-term debt	$ 4,643	$ 4,651

Senior Notes

The indentures governing the senior notes listed in the table above, contain non-financial and financial covenants of Centene Corporation, including requirements of a minimum fixed charge coverage ratio. At March 31, 2017, the Company was in compliance with all covenants.

Interest Rate Swaps

In February 2017 and in connection with the November 2016 issuance of $1,200 million of 4.75% Senior Notes, due January 15, 2025 ($1,200 Million Notes), the Company entered into interest rate swap agreements for a notional amount of $600 million, at floating rates of interest based on the one month LIBOR plus 2.53%. Gains and losses due to the changes in the fair value of the interest rate swaps completely offset changes in the fair value of the hedged portion of the underlying debt and are recorded as an adjustment to the $1,200 Million Notes.

The Company uses interest rate swap agreements to convert a portion of its interest rate exposure from fixed rates to floating rates to more closely align interest expense with interest income received on its cash equivalent and variable rate investment balances. The Company has $2,700 million of notional amount of interest rate swap agreements consisting of:

- $600 million expiring on February 15, 2021;
- $500 million expiring on May 15, 2022;
- $1,000 million expiring on February 15, 2024; and
- $600 million expiring on January 15, 2025.

Under the Swap Agreements, the Company receives a fixed rate of interest and pays an average variable rate of either the three or one month LIBOR plus 3.61% adjusted monthly or quarterly, based on the terms of the individual swap agreements. At March 31, 2017, the weighted average rate was 4.62%.

The Swap Agreements are formally designated and qualify as fair value hedges and are recorded at fair value in the Consolidated Balance Sheets in other assets or other liabilities. Gains and losses due to changes in fair value of the interest rate swap agreements completely offset changes in the fair value of the hedged portion of the underlying debt. Therefore, no gain or loss has been recognized due to hedge ineffectiveness. Offsetting changes in fair value of both the interest rate swaps and the hedged portion of the underlying debt both were recognized in interest expense in the Consolidated Statements of Operations. The Company does not hold or issue any derivative instrument for trading or speculative purposes.

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Revolving Credit Agreement

The Company has an unsecured $1,000 million revolving credit facility. Borrowings under the agreement bear interest based upon LIBOR rates, the Federal Funds Rate or the Prime Rate. The agreement has a maturity date of March 24, 2021. As of March 31, 2017, the Company had $100 million of borrowings outstanding under the agreement with a weighted average interest rate of 4.5%.

The revolving credit facility contains non-financial and financial covenants, including requirements of minimum fixed charge coverage ratios and maximum debt-to-EBITDA ratios. The Company is required to not exceed a maximum debt-to-EBITDA ratio of 3.0 to 1.0 on and subsequent to December 31, 2016. As of March 31, 2017, there were no limitations on the availability under the revolving credit agreement as a result of the debt-to-EBITDA ratio, and the Company was in compliance with all covenants.

Letters of Credit & Surety Bonds

The Company had outstanding letters of credit of $71 million as of March 31, 2017, which were not part of the revolving credit facility. The Company also had letters of credit for $45 million (valued at March 31, 2017 conversion rate), or €42 million, representing its proportional share of the letters of credit issued to support Ribera Salud's outstanding debt, which are a part of the revolving credit facility. Collectively, the letters of credit bore interest at 1.42% as of March 31, 2017. The Company had outstanding surety bonds of $397 million as of March 31, 2017.

7. Earnings Per Share

The following table sets forth the calculation of basic and diluted net earnings (loss) per common share ($ in millions, except per share data):

	Three Months Ended March 31,	
	2017	2016
Earnings (loss) attributable to Centene Corporation:		
Earnings (loss) from continuing operations, net of tax	$139	$ (15)
Discontinued operations, net of tax	—	(1)
Net earnings (loss)	$139	$ (16)
Shares used in computing per share amounts:		
Weighted average number of common shares outstanding	172,073,268	129,543,076
Common stock equivalents (as determined by applying the treasury stock method)	3,762,322	—
Weighted average number of common shares and potential dilutive common shares outstanding	175,835,590	129,543,076
Net earnings (loss) per common share attributable to Centene Corporation:		
Basic:		
Continuing operations	$0.81	$ (0.12)
Discontinued operations	—	(0.01)
Basic earnings (loss) per common share	$0.81	$ (0.13)
Diluted:		
Continuing operations	$0.79	$ (0.12)
Discontinued operations	—	(0.01)
Diluted earnings (loss) per common share	$0.79	$ (0.13)

The calculation of diluted earnings (loss) per common share for the three months ended March 31, 2017 and 2016 excludes the impact of 55,170 and 6,742,714 shares (before application of the treasury stock method), respectively, related to anti-dilutive stock options, restricted stock and restricted stock units.

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8. Segment Information

Centene operates in two segments: Managed Care and Specialty Services. The Managed Care segment consists of Centene’s health plans including all of the functions needed to operate them. The Specialty Services segment consists of Centene’s specialty companies offering auxiliary healthcare services and products.

In January 2017, the Company reclassified Cenpatico Behavioral Health of Arizona, LLC and the related Cenpatico Integrated Care health plan from the Specialty Services segment to the Managed Care segment due to a reorganization of the Arizona management structure following the Health Net integration. As a result, the financial results of Cenpatico Behavioral Health of Arizona, LLC and the related Cenpatico Integrated Care health plan have been reclassified from the Specialty Services segment to the Managed Care segment for all periods presented.

Segment information for the three months ended March 31, 2017, follows ($ in millions):

	Managed Care	Specialty Services	Eliminations	Consolidated Total
Total revenues from external customers	$ 11,115	$ 609	$ —	$ 11,724
Total revenues from internal customers	11	2,333	(2,344)	—
Total revenues	$ 11,126	$ 2,942	$ (2,344)	$ 11,724
Earnings from operations	$ 187	$ 53	$ —	$ 240

Segment information for the three months ended March 31, 2016, follows ($ in millions):

	Managed Care	Specialty Services	Eliminations	Consolidated Total
Total revenues from external customers	$ 6,517	$ 436	$ —	$ 6,953
Total revenues from internal customers	34	1,448	(1,482)	—
Total revenues	$ 6,551	$ 1,884	$ (1,482)	$ 6,953
Earnings (loss) from operations	$ (19)	$ 39	$ —	$ 20

9. Contingencies

Overview

The Company records reserves and accrues costs for certain legal proceedings and regulatory matters to the extent that it determines an unfavorable outcome is probable and the amount of the loss can be reasonably estimated. While such reserves and accrued costs reflect the Company's best estimate of the probable loss for such matters, the recorded amounts may differ materially from the actual amount of any such losses. In some cases, no estimate of the possible loss or range of loss in excess of amounts accrued, if any, can be made because of the inherently unpredictable nature of legal and regulatory proceedings, which may be exacerbated by various factors, including but not limited to, they may involve indeterminate claims for monetary damages or may involve fines, penalties or punitive damages; present novel legal theories or legal uncertainties; involve disputed facts; represent a shift in regulatory policy; involve a large number of parties, claimants or regulatory bodies; are in the early stages of the proceedings; involve a number of separate proceedings and/or a wide range of potential outcomes; or result in a change of business practices.

As of the date of this report, amounts accrued for legal proceedings and regulatory matters were not material. However, it is possible that in a particular quarter or annual period the Company’s financial condition, results of operations, cash flow and/or liquidity could be materially adversely affected by an ultimate unfavorable resolution of or development in legal and/or regulatory proceedings, including as described below. Except for the proceedings discussed below, the Company believes that the ultimate outcome of any of the regulatory and legal proceedings that are currently pending against it should not have a material adverse effect on financial condition, results of operations, cash flow or liquidity.

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California

The Company's California subsidiary, Health Net of California, Inc. (Health Net California), has been named as a defendant in a California taxpayer action filed in Los Angeles County Superior Court, captioned as Michael D. Myers v. State Board of Equalization, et al., Los Angeles Superior Court Case No. BS158655. This action is brought under a California statute that permits an individual taxpayer to sue a governmental agency when the taxpayer believes the agency has failed to enforce governing law. Plaintiff contends that Health Net California, a California licensed Health Care Service Plan (HCSP), is an “insurer” for purposes of taxation despite acknowledging it is not an “insurer” under regulatory law. Under California law, “insurers” must pay a gross premiums tax (GPT), calculated as 2.35% on gross premiums. As a licensed HCSP, Health Net California has paid the California Corporate Franchise Tax (CFT), the tax generally paid by California businesses. Plaintiff contends that Health Net California must pay the GPT rather than the CFT. Plaintiff seeks a writ of mandate directing the California taxing agencies to collect the GPT, and seeks an order requiring Health Net California to pay GPT, interest and penalties for a period dating to eight years prior to the October 20, 2015 filing of the complaint. This lawsuit is being coordinated with similar lawsuits filed against other entities. The Company expects an initial status conference shortly. The Company intends to vigorously defend itself against these claims; however, this matter is subject to many uncertainties, and an adverse outcome in this matter could potentially have a materially adverse impact on our financial position and results of operations.

Federal Securities Class Action

On November 14, 2016, a putative federal securities class action was filed against the Company and certain of its executives in the U.S. District Court for the Central District of California. On March 1, 2017, the court entered an order transferring the matter to the U.S. District Court for the Eastern District of Missouri. The plaintiffs in the lawsuit allege that the Company's accounting and related disclosures for certain liabilities acquired in the acquisition of Health Net violated federal securities laws. The Company denies any wrongdoing and is vigorously defending itself against these claims. Nevertheless, this matter is subject to many uncertainties and the Company cannot predict how long this litigation will last or what the ultimate outcome will be, and an adverse outcome in this matter could potentially have a materially adverse impact on our financial position and results of operations.

Civil Investigative Demand

On December 15, 2016, a Civil Investigative Demand (CID) was issued to Health Net by the United States Department of Justice regarding Health Net’s submission of risk adjustment claims to the CMS under Parts C and D of Medicare. The CID may be related to a federal qui tam lawsuit filed under seal in 2011 naming more than a dozen health insurers including Health Net. The lawsuit was recently unsealed when the Department of Justice intervened in the case with respect to one of the insurers (not Health Net). The Company is complying with the CID and will vigorously defend any lawsuits. At this point, it is not possible to determine what level of liability, if any, the Company may face as a result of this matter.

Guaranty Fund Assessment

Under state guaranty association laws, certain insurance companies can be assessed for certain obligations to the policyholders and claimants of impaired or insolvent insurance companies that write the same line or similar lines of business. In 2009, the Pennsylvania Insurance Commissioner placed long-term care insurer Penn Treaty Network America Insurance Company and its subsidiary (Penn Treaty), neither of which is affiliated with the Company, in rehabilitation and petitioned a state court for approval to liquidate Penn Treaty. In March 2017, the court issued the final liquidation order, and as a result, in the three months ended March 31, 2017, the Company recognized $47 million representing its undiscounted estimated share of the guaranty association assessment as selling, general and administrative expenses.

Miscellaneous Proceedings

Excluding the matters discussed above, the Company is also routinely subjected to legal and regulatory proceedings in the normal course of business. These matters can include, without limitation:

- periodic compliance and other reviews and investigations by various federal and state regulatory agencies with respect to requirements applicable to the Company's business, including, without limitation, those related to payment of out-of-network claims, submissions to CMS for risk adjustment payments or the False Claims Act, pre-authorization penalties, timely review of grievances and appeals, timely and accurate payment of claims, and the Health Insurance Portability and Accountability Act of 1996;

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- litigation arising out of general business activities, such as tax matters, disputes related to health care benefits coverage or reimbursement, putative securities class actions and medical malpractice, privacy, real estate, intellectual property and employment-related claims;

- disputes regarding reinsurance arrangements, claims arising out of the acquisition or divestiture of various assets, class actions and claims relating to the performance of contractual and non-contractual obligations to providers, members, employer groups and others, including, but not limited to, the alleged failure to properly pay claims and challenges to the manner in which the Company processes claims, and claims alleging that the Company has engaged in unfair business practices.

Among other things, these matters may result in awards of damages, fines or penalties, which could be substantial, and/or could require changes to the Company's business. The Company intends to vigorously defend itself against the miscellaneous legal and regulatory proceedings to which it is currently a party; however, these proceedings are subject to many uncertainties. In some of the cases pending against the Company, substantial non-economic or punitive damages are being sought.

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ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and the related notes included elsewhere in this filing. The discussion contains forward-looking statements that involve known and unknown risks and uncertainties, including those set forth under Part II, Item 1A. "Risk Factors" of this Form 10-Q. The following discussion and analysis, with the exception of cash flow information, is presented in the context of continuing operations unless otherwise identified.

EXECUTIVE OVERVIEW

General

We are a diversified, multi-national healthcare enterprise that provides services to government sponsored and commercial healthcare programs, focusing on under-insured and uninsured individuals. We provide member-focused services through locally based staff by assisting in accessing care, coordinating referrals to related health and social services and addressing member concerns and questions.

Results of operations depend on our ability to manage expenses associated with health benefits (including estimated costs incurred) and selling, general and administrative (SG&A) costs. We measure operating performance based upon two key ratios. The health benefits ratio (HBR) represents medical costs as a percentage of premium revenues, excluding premium tax and health insurer fee revenues that are separately billed, and reflects the direct relationship between the premium received and the medical services provided. The SG&A expense ratio represents SG&A costs as a percentage of premium and service revenues, excluding premium tax and health insurer fee revenues that are separately billed.

Health Net Acquisition

On March 24, 2016, the Company acquired all of the issued and outstanding shares of Health Net, a publicly traded managed care organization that delivers healthcare services through health plans and government-sponsored managed care plans. The transaction was valued at $6.0 billion, including the assumption of debt. The acquisition allows the Company to offer a more comprehensive and scalable portfolio of solutions and provides opportunity for additional growth across the combined company's markets. Due to the size of this acquisition, the primary drivers of the quarter over quarter variances discussed throughout this section are related to the acquisition of Health Net.

Regulatory Trends and Uncertainties

The U.S. Presidential administration and certain members of Congress had affirmatively indicated that they will pursue full repeal of or significant amendment to the Affordable Care Act (ACA). However, in the first quarter of 2017, the House Republican leaders retracted the legislation to repeal the ACA from consideration by the House of Representatives due to concerns that the bill would not pass. Overall, the impact of the new U.S. Presidential administration is not yet clear. There are various contingents within Congress with varying agendas, and it will take time to see if any resolution can be reached. There are still discussions of a repeal and replace bill, but the ultimate outcome remains uncertain. Even if the ACA is not amended or repealed, the new administration could propose changes impacting implementation of the ACA. We continue to believe we have both the capacity and capability to successfully navigate industry changes to the benefit of our members, customers and shareholders.

For additional information regarding regulatory trends and uncertainties, see Part II, Item 1A, "Risk Factors."

First Quarter 2017 Highlights

Our financial performance for the first quarter of 2017 are summarized as follows:

- Managed care membership of 12.1 million, an increase of 605,000 members, or 5% year over year.
- Total revenues of $11.7 billion, representing 69% growth year over year.
- Health benefits ratio of 87.6%, compared to 88.7% in 2016.
- SG&A expense ratio of 9.8%, or 9.3% excluding the Penn Treaty assessment and Health Net acquisition related expenses, for the first quarter of 2017, compared to 11.3%, or 8.3% excluding Health Net acquisition related expenses, in the first quarter of 2016.
- Operating cash flows of $1,248 million.

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- Diluted earnings (loss) per share (EPS) for the first quarter of 2017 of $0.79, compared to $(0.12) for the first quarter of 2016.
- Adjusted Diluted EPS for the first quarter of 2017 of $1.12, compared to $0.74 for the first quarter of 2016.

Adjusted Diluted EPS is highlighted below and additional detail is provided above under the heading "Non-GAAP Financial Presentation":

	Three Months Ended March 31,	
	2017	2016
GAAP diluted EPS	$0.79	$(0.12)
Amortization of acquired intangible assets	0.14	0.04
Health Net acquisition related expenses	0.02	0.82
Penn Treaty assessment expense	0.17	—
Adjusted Diluted EPS from continuing operations	$1.12	$0.74

In the three months ended March 31, 2017, we recognized $47 million for our estimated share of the undiscounted guaranty association assessment resulting from a court ordered liquidation of the Pennsylvania based Penn Treaty Network America Insurance Company and its subsidiary (Penn Treaty) as SG&A expenses.

The following items contributed to our revenue and membership growth over the last year:

- Arizona. In January 2017, we continued our participation as a qualified health plan issuer in the Arizona Health Insurance Marketplace and exited the Health Net preferred provider organization offerings in Arizona.

- Centurion. In April 2016, Centurion began providing correctional healthcare services for the Florida Department of Corrections in Regions 1, 2 and 3. In June 2016, Centurion began operating under two new contracts with the State of New Mexico Corrections Department to provide correctional medical healthcare services and pharmacy services.

- Health Insurance Marketplace. In January 2017, we added over 500,000 new members across our Health Insurance Marketplace service areas.

- Health Net. On March 24, 2016, we acquired all of the issued and outstanding shares of Health Net for approximately $6.0 billion, including the assumption of debt. This strategic acquisition broadened our service offerings, providing expansion in both Medicaid and Medicare programs. This acquisition provided further diversification across our markets and products through the addition of commercial products and government sponsored care under federal contracts with the Department of Defense (DoD) and the U.S. Department of Veteran's Affairs (VA), as well as Medicare Advantage. Health Net's operations are primarily concentrated in the states of California, Arizona, Oregon, and Washington.

- Indiana. In January 2017, our Indiana subsidiary, Managed Health Services, began operating under a contract with the Indiana Family & Social Services Administration to provide risk-based managed care services for enrollees in the Healthy Indiana Plan and Hoosier Healthwise programs.

- Louisiana. In July 2016, our Louisiana subsidiary, Louisiana Healthcare Connections began serving Medicaid expansion members.

- Nebraska. In January 2017, our Nebraska subsidiary, Nebraska Total Care, began operating under a contract with the Nebraska Department of Health and Human Services' Division of Medicaid and Long Term Care as one of three managed care organizations to administer its new Heritage Health Program for Medicaid, ABD, CHIP, Foster Care and LTC enrollees.

- Texas. In November 2016, our Texas subsidiary, Superior HealthPlan, Inc., began operating under a new contract with the Texas HHSC to serve STAR Kids Medicaid population in seven delivery areas, more than any other successful bidder.

- Washington. In April 2016, our Washington subsidiary, Coordinated Care of Washington, began operating as the sole contractor with the Washington State Health Care Authority to provide foster care services through the Apple Health Foster Care contract.

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We expect the following items to contribute to our future growth potential:

- We expect to realize the full year benefit in 2017 from the Health Net acquisition completed on March 24, 2016.

- We expect to realize the full year benefit in 2017 of business commenced during 2016 in Florida, Louisiana, New Mexico, Texas and Washington, and Health Insurance Marketplace membership growth in January 2017, as discussed above.

- In January 2017, we signed a joint venture agreement with the North Carolina Medical Society, working in conjunction with the North Carolina Community Health Center, to collaborate on a patient-focused approach to Medicaid under the reform plan enacted in the State of North Carolina. The newly created health plan, Carolina Complete Health, was created to establish, organize and operate a physician-led health plan to provide Medicaid managed care services in North Carolina.

- In January 2017, our Pennsylvania subsidiary, Pennsylvania Health & Wellness, was selected by the Pennsylvania Department of Human Services to serve Medicaid recipients enrolled in the HealthChoices program in three zones. Expected contract commencement dates vary by zone, starting January 2018, and will be fully implemented by January 2019, pending regulatory approval and successful completion of a readiness review.

- In November 2016, our Georgia subsidiary, Peach State Health Plan, was awarded a statewide managed care contract to continue serving members enrolled in the Georgia Families managed care program, including PeachCare for Kids and Planning for Healthy Babies. Through the new contract, Peach State Health Plan will be one of four managed care organizations providing medical, behavioral, dental and vision health benefits for its members. The contract is expected to become effective July 1, 2017.

- In November 2016, our Nevada subsidiary, Silver Summit Health Plan, was selected to serve Medicaid recipients enrolled in Nevada's Medicaid managed care program. The contract is expected to commence on July 1, 2017, pending regulatory approval and successful completion of a readiness review.

- In October 2016, our Missouri subsidiary, Home State Health, was selected to provide managed care services to MO HealthNet Managed Care beneficiaries. Under the new contract, Home State Health expects to serve MO HealthNet Managed Care beneficiaries in each of the state's 114 counties and the city of St. Louis. The contract is expected to commence May 1, 2017.

- In August 2016, our Pennsylvania subsidiary, Pennsylvania Health & Wellness, was selected by the Pennsylvania Department of Human Services to serve enrollees in the Community HealthChoices program statewide. Expected contract commencement dates vary by zone, starting January 2018, and will be fully implemented by January 2019, pending regulatory approval and successful completion of a readiness review.

- In July 2016, it was announced that the Department of Defense awarded our wholly-owned subsidiary, Health Net Federal Services, the TRICARE West Region contract. We currently administer services for the TRICARE program in the North Region. In connection with this latest generation of TRICARE contracts, the Department of Defense has consolidated the prior North, South and West TRICARE regions into two: the West and East Regions (the East combining the current North and South Regions). We expect health care delivery for this new contract to begin on January 1, 2018.

- In May 2016, our specialty solutions subsidiary, Envolve, Inc., was selected by Maryland Care Inc. d/b/a Maryland Physicians Care MCO to provide health plan management services for its Medicaid operations in Maryland effective

July 1, 2017.

In February 2017, our Alabama subsidiary withdrew our contracts with five nonprofit regional care organizations in Alabama to provide management services due to uncertainty in the political environment. Subsequent to our withdrawal, the governor of Alabama resigned.

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MEMBERSHIP

From March 31, 2016 to March 31, 2017, we increased our managed care membership by 605,000, or 5%. The following table sets forth the Company's membership by state for its managed care organizations:

	March 31, 2017	December 31, 2016	March 31, 2016
Arizona	684,300	598,300	607,000
Arkansas	98,100	58,600	50,700
California	2,980,100	2,973,500	3,125,400
Florida	872,000	716,100	660,800
Georgia	568,300	488,000	495,500
Illinois	253,800	237,700	239,100
Indiana	335,800	285,800	290,300
Kansas	133,100	139,700	141,100
Louisiana	484,100	472,800	381,200
Massachusetts	44,200	48,300	52,400
Michigan	2,100	2,000	2,600
Minnesota	9,500	9,400	9,500
Mississippi	349,500	310,200	328,300
Missouri	106,100	105,700	100,000
Nebraska	79,200	—	—
New Hampshire	77,800	77,400	81,500
New Mexico	7,100	7,100	—
Ohio	328,900	316,000	