

UNITEDHEALTH GROUP INC
Form 10-Q
November 08, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2016

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: 1-10864

UnitedHealth Group Incorporated
(Exact name of registrant as specified in its charter)

Delaware 41-1321939
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

UnitedHealth Group Center
9900 Bren Road East 55343
Minnetonka, Minnesota
(Address of principal executive offices) (Zip Code)
(952) 936-1300
(Registrant's telephone number, including area code)

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. Yes 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). Yes 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 "smaller reporting company" in Rule 12b-2 of the Exchange Act:

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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

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As of October 31, 2016, there were 951,816,220 shares of the registrant's Common Stock, \$.01 par value per share, issued and outstanding.

UNITEDHEALTH GROUP

Table of Contents

	Page
<u>Part I. Financial Information</u>	
<u>Item 1. Financial Statements (unaudited)</u>	<u>1</u>
<u>Condensed Consolidated Balance Sheets as of September 30, 2016 and December 31, 2015</u>	<u>1</u>
<u>Condensed Consolidated Statements of Operations for the Three and Nine Months Ended September 30, 2016 and 2015</u>	<u>2</u>
<u>Condensed Consolidated Statements of Comprehensive Income for the Three and Nine Months Ended September 30, 2016 and 2015</u>	<u>3</u>
<u>Condensed Consolidated Statements of Changes in Equity for the Nine Months Ended September 30, 2016 and 2015</u>	<u>4</u>
<u>Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2016 and 2015</u>	<u>5</u>
<u>Notes to the Condensed Consolidated Financial Statements</u>	<u>6</u>
<u>1. Basis of Presentation</u>	<u>6</u>
<u>2. Investments</u>	<u>8</u>
<u>3. Fair Value</u>	<u>9</u>
<u>4. Medicare Part D Pharmacy Benefits</u>	<u>12</u>
<u>5. Other Current Receivables</u>	<u>12</u>
<u>6. Medical Costs Reserve Development</u>	<u>12</u>
<u>7. Commercial Paper and Long-Term Debt</u>	<u>13</u>
<u>8. Shareholders' Equity</u>	<u>14</u>
<u>9. Commitments and Contingencies</u>	<u>14</u>
<u>10. Segment Financial Information</u>	<u>15</u>
<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>17</u>
<u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>25</u>
<u>Item 4. Controls and Procedures</u>	<u>26</u>
<u>Part II. Other Information</u>	
<u>Item 1. Legal Proceedings</u>	<u>26</u>
<u>Item 1. Risk Factors</u>	<u>26</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>27</u>
<u>Item 6. Exhibits</u>	<u>27</u>
<u>Signatures</u>	<u>28</u>

PART I

ITEM 1. FINANCIAL STATEMENTS

UnitedHealth Group

Condensed Consolidated Balance Sheets

(Unaudited)

(in millions, except per share data)	September 30, 2016	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 12,796	\$ 10,923
Short-term investments	2,871	1,988
Accounts receivable, net	7,347	6,523
Other current receivables, net	7,502	6,801
Assets under management	2,952	2,998
Prepaid expenses and other current assets	2,300	2,406
Total current assets	35,768	31,639
Long-term investments	23,324	18,792
Property, equipment and capitalized software, net	5,524	4,861
Goodwill	47,183	44,453
Other intangible assets, net	8,719	8,391
Other assets	3,124	3,118
Total assets	\$ 123,642	\$ 111,254
Liabilities, redeemable noncontrolling interests and equity		
Current liabilities:		
Medical costs payable	\$ 16,500	\$ 14,330
Accounts payable and accrued liabilities	12,994	11,994
Other policy liabilities	8,670	7,798
Commercial paper and current maturities of long-term debt	7,202	6,634
Unearned revenues	5,730	2,142
Total current liabilities	51,096	42,898
Long-term debt, less current maturities	26,022	25,331
Future policy benefits	2,509	2,496
Deferred income taxes	2,492	3,587
Other liabilities	2,032	1,481
Total liabilities	84,151	75,793
Commitments and contingencies (Note 9)		
Redeemable noncontrolling interests	1,937	1,736
Equity:		
Preferred stock, \$0.001 par value - 10 shares authorized; no shares issued or outstanding	—	—
Common stock, \$0.01 par value - 3,000 shares authorized; 952 and 953 issued and outstanding	10	10
Additional paid-in capital	—	29
Retained earnings	39,945	37,125
Accumulated other comprehensive loss	(2,303)	(3,334)
Nonredeemable noncontrolling interest	(98)	(105)
Total equity	37,554	33,725
Total liabilities, redeemable noncontrolling interests and equity	\$ 123,642	\$ 111,254

See Notes to the Condensed Consolidated Financial Statements

Table of Contents

UnitedHealth Group
Condensed Consolidated Statements of Operations
(Unaudited)

(in millions, except per share data)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenues:				
Premiums	\$36,142	\$31,801	\$107,366	\$95,436
Products	6,696	6,482	19,699	8,935
Services	3,264	3,036	9,673	8,607
Investment and other income	191	170	567	530
Total revenues	46,293	41,489	137,305	113,508
Operating costs:				
Medical costs	29,040	25,729	87,342	77,646
Operating costs	7,033	6,178	20,584	17,750
Cost of products sold	6,125	6,112	18,108	8,350
Depreciation and amortization	515	452	1,528	1,209
Total operating costs	42,713	38,471	127,562	104,955
Earnings from operations	3,580	3,018	9,743	8,553
Interest expense	(269)	(229)	(799)	(530)
Earnings before income taxes	3,311	2,789	8,944	8,023
Provision for income taxes	(1,333)	(1,171)	(3,579)	(3,407)
Net earnings	1,978	1,618	5,365	4,616
Earnings attributable to noncontrolling interests	(10)	(21)	(32)	(21)
Net earnings attributable to UnitedHealth Group common shareholders	\$1,968	\$1,597	\$5,333	\$4,595
Earnings per share attributable to UnitedHealth Group common shareholders:				
Basic	\$2.07	\$1.68	\$5.60	\$4.82
Diluted	\$2.03	\$1.65	\$5.51	\$4.75
Basic weighted-average number of common shares outstanding	952	953	952	953
Dilutive effect of common share equivalents	17	14	16	14
Diluted weighted-average number of common shares outstanding	969	967	968	967
Anti-dilutive shares excluded from the calculation of dilutive effect of common share equivalents	1	8	3	8
Cash dividends declared per common share	\$0.625	\$0.500	\$1.750	\$1.375

See Notes to the Condensed Consolidated Financial Statements

Table of Contents

UnitedHealth Group
Condensed Consolidated Statements of Comprehensive Income
(Unaudited)

(in millions)	Three Months		Nine Months	
	Ended		Ended	
	September 30,	September 30,	September 30,	September 30,
	2016	2015	2016	2015
Net earnings	\$1,978	\$1,618	\$5,365	\$4,616
Other comprehensive (loss) income:				
Gross unrealized (losses) gains on investment securities during the period	(21)	66	473	(51)
Income tax effect	7	(26)	(173)	17
Total unrealized (losses) gains, net of tax	(14)	40	300	(34)
Gross reclassification adjustment for net realized gains included in net earnings	(26)	(28)	(97)	(99)
Income tax effect	9	11	35	37
Total reclassification adjustment, net of tax	(17)	(17)	(62)	(62)
Total foreign currency translation (losses) gains	(69)	(1,063)	793	(1,859)
Other comprehensive (loss) income	(100)	(1,040)	1,031	(1,955)
Comprehensive income	1,878	578	6,396	2,661
Comprehensive income attributable to noncontrolling interests	(10)	(21)	(32)	(21)
Comprehensive income attributable to UnitedHealth Group common shareholders	\$1,868	\$557	\$6,364	\$2,640

See Notes to the Condensed Consolidated Financial Statements

Table of Contents

UnitedHealth Group
Condensed Consolidated Statements of Changes in Equity
(Unaudited)

(in millions)	Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)			Nonredeemable Noncontrolling Interest	Total Equity
	Shares	Amount			Net Unrealized Gains (Losses) on Investments	Foreign Currency Translation (Losses) Gains			
Balance at January 1, 2016	953	\$ 10	\$ 29	\$37,125	\$56	\$ (3,390)	\$ (105)	\$33,725	
Adjustment to adopt ASU 2016-09				28				28	
Net earnings				5,333			31	5,364	
Other comprehensive income					238	793		1,031	
Issuances of common stock, and related tax effects	8	—	187					187	
Share-based compensation			350					350	
Common share repurchases	(9)	—	(242)	(875)				(1,117)	
Cash dividends paid on common shares				(1,666)				(1,666)	
Acquisition of redeemable noncontrolling interest shares			(143)					(143)	
Redeemable noncontrolling interests fair value and other adjustments			(181)					(181)	
Distribution to nonredeemable noncontrolling interest							(24)	(24)	
Balance at September 30, 2016	952	\$ 10	\$ —	\$39,945	\$294	\$ (2,597)	\$ (98)	\$37,554	
Balance at January 1, 2015	954	\$ 10	\$ —	\$33,836	\$223	\$ (1,615)	\$ —	\$32,454	
Net earnings				4,595			11	4,606	
Other comprehensive loss					(96)	(1,859)		(1,955)	
Issuances of common stock, and related tax effects	9	—	112					112	
Share-based compensation, and related tax benefits			477					477	
Common share repurchases	(10)	—	(391)	(739)				(1,130)	
Cash dividends paid on common shares				(1,310)				(1,310)	
Redeemable noncontrolling interests fair value and other adjustments			(129)					(129)	
Acquisition of nonredeemable noncontrolling interests							9	9	
Distribution to nonredeemable noncontrolling interest							(12)	(12)	
Balance at September 30, 2015	953	\$ 10	\$ 69	\$36,382	\$127	\$ (3,474)	\$ 8	\$33,122	

See Notes to the Condensed Consolidated Financial Statements

4

Table of Contents

UnitedHealth Group

Condensed Consolidated Statements of Cash Flows

(Unaudited)

	Nine Months Ended September 30,	
(in millions)	2016	2015
Operating activities		
Net earnings	\$5,365	\$4,616
Noncash items:		
Depreciation and amortization	1,528	1,209
Deferred income taxes	(405)	(49)
Share-based compensation	369	306
Other, net	(68)	(208)
Net change in other operating items, net of effects from acquisitions and changes in AARP balances:		
Accounts receivable	(580)	(907)
Other assets	(1,835)	(1,686)
Medical costs payable	1,984	2,137
Accounts payable and other liabilities	1,004	616
Other policy liabilities	276	374
Unearned revenues	3,566	(179)
Cash flows from operating activities	11,204	6,229
Investing activities		
Purchases of investments	(12,231)	(6,712)
Sales of investments	4,422	4,041
Maturities of investments	3,040	2,557
Cash paid for acquisitions, net of cash assumed	(2,727)	(16,183)
Purchases of property, equipment and capitalized software	(1,220)	(1,072)
Other, net	(25)	(51)
Cash flows used for investing activities	(8,741)	(17,420)
Financing activities		
Common share repurchases	(1,117)	(1,130)
Acquisition of redeemable noncontrolling interest shares	(257)	(113)
Cash dividends paid	(1,666)	(1,310)
Proceeds from common stock issuances	387	366
Proceeds from issuance of long-term debt	2,485	11,982
Repayments of long-term debt	(2,101)	(416)
Proceeds from commercial paper, net	693	2,665
Customer funds administered	1,249	119
Other, net	(333)	(333)
Cash flows (used for) from financing activities	(660)	11,830
Effect of exchange rate changes on cash and cash equivalents	70	(151)
Increase in cash and cash equivalents	1,873	488
Cash and cash equivalents, beginning of period	10,923	7,495
Cash and cash equivalents, end of period	\$12,796	\$7,983

See Notes to the Condensed Consolidated Financial Statements

Table of Contents

UnitedHealth Group

Notes to the Condensed Consolidated Financial Statements
(Unaudited)

1. Basis of Presentation

UnitedHealth Group Incorporated (individually and together with its subsidiaries, “UnitedHealth Group” and “the Company”) is a diversified health and well-being company dedicated to helping people live healthier lives and making the health system work better for everyone. Through its diversified family of businesses, the Company leverages core competencies in advanced, enabling technology; health care data, information and intelligence; and clinical care management and coordination to help meet the demands of the health system. The Company offers a broad spectrum of products and services through two distinct platforms: UnitedHealthcare, which provides health care coverage and benefits services; and Optum, which provides pharmacy care services and information and technology-enabled health services.

The Company has prepared the Condensed Consolidated Financial Statements according to U.S. Generally Accepted Accounting Principles (GAAP) and has included the accounts of UnitedHealth Group and its subsidiaries. The year-end condensed consolidated balance sheet was derived from audited financial statements, but does not include all disclosures required by GAAP. In accordance with the rules and regulations of the U.S. Securities and Exchange Commission (SEC), the Company has omitted certain footnote disclosures that would substantially duplicate the disclosures contained in its annual audited Consolidated Financial Statements. Therefore, these Condensed Consolidated Financial Statements should be read together with the Consolidated Financial Statements and the Notes included in Part II, Item 8, “Financial Statements” of the Company’s Annual Report on Form 10-K for the year ended December 31, 2015 as filed with the SEC (2015 10-K). The accompanying Condensed Consolidated Financial Statements include all normal recurring adjustments necessary to present the interim financial statements fairly.

Use of Estimates

These Condensed Consolidated Financial Statements include certain amounts based on the Company’s best estimates and judgments. The Company’s most significant estimates relate to estimates and judgments for medical costs payable and revenues, valuation and impairment analysis of goodwill and other intangible assets and valuations of certain investments. Certain of these estimates require the application of complex assumptions and judgments, often because they involve matters that are inherently uncertain and will likely change in subsequent periods. The impact of any change in estimates is included in earnings in the period in which the estimate is adjusted.

The accounting policies disclosed in Note 2 of Notes to the Consolidated Financial Statements in Part II, Item 8, “Financial Statements” in the 2015 10-K remain unchanged.

Reclassification

During the fourth quarter of 2015, the Company aligned its accounting policy to conform the presentation of certain pharmacy fulfillment costs related to an acquired OptumRx business. These costs are now included in medical costs and cost of products sold, whereas they were previously included in operating costs. Prior periods have been reclassified to conform to the current period presentation. The reclassification increased medical expenses by \$111 million and \$313 million, decreased operating costs by \$123 million and \$352 million and increased cost of products sold by \$12 million and \$39 million for the three and nine months ended September 30, 2015, respectively. The reclassification had no impact on total operating costs, earnings from operations, net earnings, earnings per share or total equity.

Recently Issued Accounting Standards

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standard Update (ASU) No. 2016-02, “Leases (Topic 842)” (ASU 2016-02). Under ASU 2016-02, an entity will be required to recognize assets and liabilities for the rights and obligations created by leases on the entity’s balance sheet for both finance and operating leases. For leases with a term of 12 months or less, an entity can elect to not recognize lease assets and lease liabilities and expense the lease over a straight-line basis for the term of the lease. ASU 2016-02 will require new disclosures that depict the amount, timing, and uncertainty of cash flows pertaining to an entity’s leases. Companies are required to adopt the new standard using a modified retrospective approach for annual and interim periods beginning after December 15, 2018. Early adoption of ASU 2016-02 is permitted. The Company is currently evaluating the effect of

the new leasing guidance.

In January 2016, the FASB issued ASU 2016-01, “Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities” (ASU 2016-01). The new guidance changes the current accounting related to (i) the classification and measurement of certain equity investments, (ii) the presentation of changes in the fair value of financial liabilities measured under the fair value option that are due to instrument-specific credit risk, and (iii) certain disclosures associated with the fair value of financial instruments. Most notably, ASU 2016-01 requires that equity investments, with certain exemptions, be measured at fair value with changes in fair value recognized in net income as opposed to other

Table of Contents

comprehensive income. The new guidance is effective for annual and interim reporting periods beginning after December 15, 2017. The Company is currently evaluating the effect of the new financial instruments guidance. In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)" (ASU 2014-09) as modified by ASU No. 2015-14, "Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date," ASU 2016-08, "Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)," ASU No. 2016-10, "Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing," and ASU No. 2016-12, "Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients." ASU 2014-09 will supersede 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). The revenue recognition principle in ASU 2014-09 is that an entity should recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In addition, new and enhanced disclosures will be required. Companies may adopt the new standard either using the full retrospective approach, a modified retrospective approach with practical expedients, or a cumulative effect upon adoption approach. The Company will early adopt the new standard effective January 1, 2017, as allowed by the standard, using the modified retrospective approach. The adoption of ASU 2014-09 will not have a material impact on the Company's consolidated financial position, results of operations, equity or cash flows.

Recently Adopted Accounting Standards

In March 2016, the FASB issued ASU No. 2016-09, "Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting" (ASU 2016-09). ASU 2016-09 modifies several aspects of the accounting for share-based payment awards, including income tax consequences, and classification on the statement of cash flows. The Company early adopted ASU 2016-09 in the first quarter of 2016. The provisions of ASU 2016-09 related to the timing of when excess tax benefits are recognized, minimum statutory withholding requirements and forfeitures were adopted using a modified retrospective transition method by means of a cumulative-effect adjustment to equity as of January 1, 2016. The provisions of ASU 2016-09 related to the recognition of excess tax benefits in the income statement and classification in the statement of cash flows were adopted prospectively and the prior periods were not retrospectively adjusted. The adoption of ASU 2016-09 did not materially impact the Company's consolidated financial position, results of operations, equity or cash flows.

In November 2015, the FASB issued ASU No. 2015-17, "Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes" (ASU 2015-17). ASU 2015-17 requires entities to present deferred tax assets and deferred tax liabilities as noncurrent on the balance sheet. Prior to the issuance of ASU 2015-17, deferred taxes were required to be presented as a net current asset or liability and a net noncurrent asset or liability. The Company adopted ASU 2015-17 on a prospective basis in the first quarter of 2016 and the prior period was not retrospectively adjusted. The adoption of ASU 2015-17 did not impact the Company's consolidated financial position, results of operations, equity or cash flows.

In April 2015, the FASB issued ASU No. 2015-03, "Interest-Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs" (ASU 2015-03). ASU 2015-03 requires debt issuance costs to be presented as a reduction of the carrying amount of the related debt liability. Prior to the issuance of ASU 2015-03, debt issuance costs were required to be presented as an asset in the balance sheet. The Company adopted ASU 2015-03 on a retrospective basis, as required, in the first quarter of 2016. The Company reclassified \$129 million in debt issuance costs that were recorded in other assets on the Consolidated Balance Sheet as of December 31, 2015 to long-term debt, less current maturities.

The Company has determined that there have been no other recently adopted or issued accounting standards that had, or will have, a material impact on its Condensed Consolidated Financial Statements.

Table of Contents

2. Investments

A summary of short-term and long-term investments by major security type is as follows:

(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2016				
Debt securities - available-for-sale:				
U.S. government and agency obligations	\$ 2,301	\$ 12	\$ (2)	\$2,311
State and municipal obligations	7,207	213	(3)	7,417
Corporate obligations	10,292	176	(6)	10,462
U.S. agency mortgage-backed securities	2,571	42	(1)	2,612
Non-U.S. agency mortgage-backed securities	931	24	(3)	952
Total debt securities - available-for-sale	23,302	467	(15)	23,754
Equity securities - available-for-sale	1,919	58	(41)	1,936
Debt securities - held-to-maturity:				
U.S. government and agency obligations	174	2	—	176
State and municipal obligations	8	—	—	8
Corporate obligations	323	—	—	323
Total debt securities - held-to-maturity	505	2	—	507
Total investments	\$ 25,726	\$ 527	\$ (56)	\$26,197
December 31, 2015				
Debt securities - available-for-sale:				
U.S. government and agency obligations	\$ 1,982			