FAMILYCARE, INC.
AND
SUBSIDIARY

Consolidated Financial Statements
December 31, 2012 and 2011
With Independent Auditor's Report

PERKINS & CO

5/17/13

FAMILYCARE, INC. AND SUBSIDIARY
YEARS ENDED DECEMBER 31, 2012 AND 2011
CONTENTS

PERKINS & CO

+ 1211 SW Fifth Avenue, Suite 1000
+ Portland, Oregon 97204-3710

+ Telephone: 503.221.0336
+ Fax: 503.294.4378
+ www.perkinsaccounting.com

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
FamilyCare, Inc.

We have audited the accompanying consolidated financial statements of FamilyCare, Inc. and Subsidiary (an Oregon nonprofit corporation) which comprise the consolidated statements of financial position as of December 31, 2012 and 2011, and the related consolidated statements of activities, changes in unrestricted net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of FamilyCare, Inc. and Subsidiary as of December 31, 2012 and 2011, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Perkins & Company, P.C.

May 13, 2013

FAMILYCARE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
DECEMBER 31, 2012 AND 2011

	2012	2011
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 14,061,132	$ 20,487,486
Restricted cash and cash equivalents	648,070	334,656
Short-term investments	3,401,736	4,873,404
Restricted short-term investments	3,383,232	894,584
Premiums receivable from DMAP	4,596,505	2,789,740
Reinsurance receivables	28,366	341,149
Receivable from CMS	312,981	757,111
Other current assets, net	1,913,115	3,146,995
Total current assets	28,345,137	33,625,125
LONG-TERM INVESTMENTS	25,126,769	7,609,423
RESTRICTED LONG-TERM INVESTMENTS	2,570,755	5,326,033
PROPERTY AND EQUIPMENT	1,803,097	3,034,135
OTHER ASSETS	450,653	167,654
Total assets	$ 58,296,411	$ 49,762,370

FAMILYCARE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION (continued)
DECEMBER 31, 2012 AND 2011

	2012	2011
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Checks in excess of deposits	$ 777,845	$ -
Claims payable and unpaid claims adjudication expenses	24,022,361	27,719,989
Savings pool and quality bonus payable	1,824,212	1,504,583
Other policy liabilities	1,489,135	1,044,167
Accounts payable	1,438,600	977,841
Accrued liabilities	2,912,736	823,480
Provider taxes payable	423,715	448,717
Current portion of capital lease obligation	111,236	107,621
Total current liabilities	32,999,840	32,626,398
CAPITAL LEASE OBLIGATION, LESS CURRENT PORTION	353,247	464,484
Total liabilities	33,353,087	33,090,882
COMMITMENTS AND CONTINGENCIES (NOTES 7, 8 AND 11)		
NET ASSETS:		
Unrestricted net assets:		
Designated reserve related to DMAP contract	4,797,272	4,797,272
Designated reserve related to the Insurance Division	2,500,000	2,500,000
Designated for OPSO	100,000	100,000
Undesignated	17,546,052	9,274,216
Total unrestricted net assets	24,943,324	16,671,488
Total liabilities and unrestricted net assets	$ 58,296,411	$ 49,762,370

FAMILYCARE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF ACTIVITIES
YEARS ENDED DECEMBER 31, 2012 AND 2011

	2012	2011
UNRESTRICTED NET ASSETS		
REVENUE		
Medicaid premiums, net	$ 138,268,595	$ 144,886,780
Medicare premiums, net	28,606,524	31,785,996
Other revenue	106,256	173,477
Total revenue	166,981,375	176,846,253
EXPENSES		
Medical and hospital	138,205,072	149,216,774
Administrative	21,139,562	18,836,088
Total expenses	159,344,634	168,052,862
CHANGE IN UNRESTRICTED NET ASSETS FROM OPERATIONS	7,636,741	8,793,391
INVESTMENT INCOME	635,095	152,867
INCREASE IN UNRESTRICTED NET ASSETS	$ 8,271,836	$ 8,946,258

FAMILYCARE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN UNRESTRICTED NET ASSETS
YEARS ENDED DECEMBER 31, 2012 AND 2011

	Designated Reserve Related to DMAP Contract	Designated Reserve Related to the Insurance Division	Designated for OPSO	Undesignated	Total Unrestricted Net Assets
BALANCE AT JANUARY 1, 2011	$ 5,125,230	$ 2,500,000	$ 100,000	$ -	$ 7,725,230
Increase in unrestricted net assets	-	-	-	8,946,258	8,946,258
Transfers	(327,958)	-	-	327,958	-
BALANCE AT DECEMBER 31, 2011	4,797,272	2,500,000	100,000	9,274,216	16,671,488
Increase in unrestricted net assets	-	-	-	8,271,836	8,271,836
BALANCE AT DECEMBER 31, 2012	$ 4,797,272	$ 2,500,000	$ 100,000	$ 17,546,052	$ 24,943,324

FAMILYCARE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2012 AND 2011

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES:		
Increase in unrestricted net assets	$ 8,271,836	$ 8,946,258
Adjustments to reconcile increase in unrestricted net assets to net cash provided by operating activities:		
Depreciation and amortization	1,039,158	948,392
Net realized and unrealized (gain) loss on investments	(108,867)	163,886
Impairment of software assets	400,000	-
Loss on sales of property and equipment	2,067	-
Changes in certain operating assets and liabilities:		
Restricted cash and cash equivalents	(313,414)	31,150
Premiums receivable from DMAP	(1,806,765)	1,183,764
Reinsurance receivables	312,783	(228,607)
Receivable from CMS	444,130	(10,347)
Other current and long-term assets, net	950,881	(1,254,581)
Checks in excess of deposits	777,845	(496,920)
Claims payable and unpaid claims adjudication expenses	(3,697,628)	(1,012,697)
Savings pool and quality bonus payable	319,629	1,379,696
Other policy liabilities	444,968	988,623
Accounts payable	460,759	99,004
Accrued liabilities	2,089,256	24,697
Provider taxes payable	(25,002)	70,229
Net cash provided by operating activities	9,561,636	10,832,547
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of investments	7,067,574	4,637,235
Proceeds from sale of restricted investments	890,000	1,795,000
Purchases of investments	(22,939,801)	(3,392,937)
Purchases of restricted investments	(687,954)	(3,830,345)
Purchases of property and equipment	(210,187)	(535,427)
Net cash used in investing activities	(15,880,368)	(1,326,474)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayment of capital lease obligation	(107,622)	(96,143)
Net cash used in financing activities	(107,622)	(96,143)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(6,426,354)	9,409,930
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	20,487,486	11,077,556
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 14,061,132	$ 20,487,486

FAMILYCARE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
YEARS ENDED DECEMBER 31, 2012 AND 2011

	2012	2011
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Noncash investing and financing activities:		
Equipment financed by capital lease	$ -	$ 393,573

FAMILYCARE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

NOTE 1 - ORGANIZATION

Organization and Basis of Presentation - The accompanying consolidated financial statements include the accounts and activities of FamilyCare, Inc. (FamilyCare) and its subsidiary, FamilyCare Health Plans, Inc. (Health Plans) (collectively, the Company). All significant intercompany balances and activities have been eliminated in consolidation.

Description of Business - The Company provides cooperative and comprehensive healthcare programs to the communities it serves. The Company contracts with individual primary care providers and hospitals to provide medical services to its members.

FamilyCare is under contract with the Oregon Department of Human Services (DHS) Division of Medical Assistance Programs (DMAP) and with the DHS Addictions and Mental Health Division (AMHD) as a fully capitated health plan for Medicaid benefits in the Oregon counties of Multnomah, Clackamas, Josephine, Umatilla, Jackson, Washington, Clatsop, and Morrow. Effective October 1, 2005, FamilyCare began contracting directly with providers for medical services under the AMHD contract. FamilyCare's present service contracts with DHS expire on December 31, 2013.

Health Plans also provides Medicare and Medicare Part D insurance coverage. Health Plans is certified by the Centers for Medicare and Medicaid Services (CMS) to provide Medicare insurance coverage in the Oregon counties of Multnomah, Clackamas, Umatilla, Washington, Clatsop and Morrow. Effective January 1, 2013, the contract with CMS has been renewed for the year ending December 31, 2013. In conjunction with Health Plans entering into the contracts with CMS, Health Plans is required to comply with certain additional regulatory requirements (see Note 7).

Basis of Accounting - The accompanying consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) using the accrual method of accounting, which recognizes revenue and income when earned and expenses when incurred.

Cash and Cash Equivalents - The Company considers all cash on hand, amounts deposited with banks, money market instruments, and short-term, highly liquid investments with maturities at acquisition of three months or less to be cash and cash equivalents.

Restricted Cash, Cash Equivalents and Investments - FamilyCare's restricted cash, cash equivalents and investment requirements are governed by DMAP and the State of Oregon Department of Consumer and Business Services, Insurance Division (the Insurance Division). In addition, FamilyCare investments in the amount of $881,575 collateralize a standby letter of credit issued to secure the Company's performance under its facility lease, and are restricted as to use. Health Plans' restricted cash, cash equivalents and investment requirements are governed by the Insurance Division. Restricted cash, cash equivalents and investments consist of cash, money market funds, certificates of deposit and U.S. Treasury securities.

Investments - Investments in all equity and debt securities are measured at fair value in the accompanying consolidated statements of financial position. Investments with remaining maturities of one year or less at the consolidated statement of financial position date and that do not otherwise meet the definition of a cash equivalent are reported as short-term investments in the consolidated statements of financial position. Investments with remaining maturities of greater than one year at the consolidated statement of financial position date are reported as long-term investments in the consolidated statements of financial position. Realized and unrealized gains and losses and interest and dividend income are included in investment income in the accompanying consolidated statements of activities. Realized gains and losses on sales of investments are recognized on a trade-date basis and determined using the specific-identification method.

Concentrations of Credit Risk - The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of cash, cash equivalents, investments, and accounts and other receivables. All of its non-interest bearing cash balances were fully insured at December 31, 2012 due to a temporary federal program in effect from December 31, 2010 through December 31, 2012. Under the program, there is no limit to the amount of insurance for eligible accounts. Beginning 2013, insurance coverage will revert to $250,000 per depositor at each financial institution, and the Company's non-interest bearing cash balances may, again, exceed federally insured limits. Cash and cash equivalents other than non-interest bearing cash balances may not be insured. Management believes that its credit risk with respect to cash and cash equivalents is minimal due to the relative financial strength of the financial institutions which maintain the Company's bank balances and the short-term nature of its other cash equivalents.

Credit risk related to investments varies depending on the nature of the investments. Management believes that its credit risk related to debt securities is limited due to the financial strength of the U.S. Government and supporting corporations securing such investments. Investment risk related to equity securities can vary depending on a variety of economic factors affecting the companies issuing such securities. Management believes that its investment risk related to equity securities is limited due to the diversity of such investments. Due to changes in economic conditions, interest rates, and common stock prices, the fair value of the Company's debt and equity securities can be volatile. Consequently, the fair value of such investments can significantly change in the near term as a result of such volatility.

Credit risk related to accounts and other receivables, which total $6,443,882 and $6,522,983 at December 31, 2012 and 2011, respectively, is limited due to the nature of significant receivables. Premiums receivable from DMAP represented 71% and 43% of accounts and other receivables at December 31, 2012 and 2011, respectively. Pharmacy rebates receivable represented 10% and 4% of accounts and other receivables at December 31, 2012 and 2011, respectively. Amounts receivable from CMS represented 5% and 12% of accounts and other receivables at December 31, 2012 and 2011, respectively. Receivables from medical service providers in connection with overpayments of claims represented 2% and 25% of accounts and other receivables at December 31, 2012 and 2011, respectively.

During 2012, the Company generated 17% and 83% of its total revenues from Medicare and DMAP government contracts, respectively. During 2011, the Company generated 18% and 82% of its total revenues from Medicare and DMAP government contracts, respectively. If these contracts are not renewed, the Company's future results of operations and financial position could be materially affected.

Premiums Receivable from DMAP - Premiums receivable from DMAP consist of uncollateralized amounts due from DMAP for maternity services performed (which are reimbursed at a fixed fee per-delivery) and for which reimbursement had not yet been received from DMAP as of December 31, 2012 and 2011. The Company believes that its credit risk related to the premiums receivable from DMAP is minimal due to the nature of the receivable.

Reinsurance - In the normal course of business, and as required by DMAP, the Company seeks to limit its loss on any single insured risk and to recover a portion of benefits paid by ceding reinsurance to its reinsurers, Physicians Insurance, HCC Life Insurance Company and ACE American Insurance Company (collectively, the reinsurers), under excess coverage agreements. The Company cedes reinsurance premiums to the reinsurers on a per-member per-month basis. In return, the reinsurers generally assume 90% to 100% of the risk in excess of $250,000 per-member per-year for hospital and physician services. The reinsurers assume no risk on claims in excess of $675,000 per-member per-policy year for Medicaid members, and $750,000 per-member per-policy year for Medicare members. Reinsurance agreements do not relieve the Company from its primary obligation to its members.

Amounts recoverable under reinsurance agreements are estimated in a manner consistent with the claim liability associated with each reinsurance policy. Reinsurance premiums are netted against premiums earned, and reinsurance recoveries are offset against claims incurred. Reinsurance premiums were approximately $2,562,000 and $3,992,000 for the years ended December 31, 2012 and 2011, respectively, and recoveries net of write-offs were approximately $612,000 and $842,000 for the years ended December 31, 2012 and 2011, respectively. Amounts receivable under reinsurance policies were $28,366 and $341,149 at December 31, 2012 and 2011, respectively. The Company believes that its credit risk related to estimated amounts receivable under reinsurance policies is minimal due to the financial strength of the reinsurers.

Receivable from CMS - Amounts receivable from CMS consist primarily of Part D low-income cost sharing and reinsurance subsidies based on higher than estimated Part D utilization and expected risk sharing adjustments based on the health condition of members.

Property and Equipment - Property and equipment acquisitions are recorded at cost and are depreciated over the estimated useful lives of the related assets, which is generally three to ten years, using the straight-line method. Expenditures for additions, major replacements, and improvements are capitalized. Routine maintenance and repairs are charged to expense as incurred.

Property and equipment financed under capital leases are recorded at the present value of future minimum lease payments and amortized using the straight-line method over the shorter of their related lease terms or their estimated useful lives.

In 2012 and 2011, the Company incurred costs for an internal-use software project. Such costs have been either capitalized or expensed in accordance with Financial Accounting Standards Board (FASB) Accounting Standards (ASC) Topic 350-40, *Internal-Use Software*. The primary component of the internal-use software asset was placed in service in 2009 and is being amortized over five years.

In accordance with ASC Topic 360-10-35 *Property, Plant and Equipment – Subsequent Measurement*, the Company periodically reviews the carrying value of its property and equipment to determine if impairment exists. If facts or circumstances support the possibility of impairment, the Company will prepare a projection of the undiscounted future operating cash flows. In cases when the Company does not expect to recover its carrying value, an impairment loss will be recognized.

Certain internal-use software assets as of December 31, 2012 were considered impaired by the Company and an impairment loss of $400,000 was recognized in 2012 related to those assets. No impairment losses were recorded in 2011.

Claims Payable and Unpaid Claims Adjudication Expenses - Claims incurred represent capitation and noncapitation payments to physicians, hospitals, and other healthcare providers for healthcare services rendered.

The liability for claims payable includes payments to be made on claims reported as of year-end and a provision for estimated incurred but not reported (IBNR) claims. IBNR claims represent the estimated liability for members who have received service from healthcare providers, but for which the invoices for services rendered have not yet been received as of year-end. Such invoices are generally paid within one year of the consolidated statement of financial position date and, therefore, the obligation is classified as a current liability in the consolidated statements of financial position. IBNR claims are actuarially determined based on historical claims payment experience and other statistics related to the Company's current business nature and volume.

The Company believes that its claims payable is adequate to satisfy its ultimate claims liabilities; however, the IBNR claims liability included in the accompanying consolidated statements of financial position may vary significantly from actual claims amounts, either negatively or positively, and as such adjustments are deemed necessary, they are included in current activities. The establishment of a liability for estimated IBNR claims is an inherently uncertain process, and there can be no assurance that currently established reserves will prove adequate to cover actual ultimate expenses. Subsequent actual experience could result in reserves being too high or too low, which could negatively or positively impact the Company's activities in future periods.

The liability for unpaid claims adjudication expenses is accrued based on management's estimate of expenses necessary to process the claims payable described above.

Savings Pool and Quality Bonus Payable - FamilyCare contracts directly with physicians, hospitals, and other healthcare providers to provide healthcare services to members. Under the terms of the Company's contracts with certain capitated providers, FamilyCare retains a calculated percentage of fees in a savings pool reserve. Following the end of the Company's fiscal year, FamilyCare distributes funds from the savings pool reserve to qualifying providers in accordance with the terms of their provider contracts. Payments from the savings pool reserve are limited by payment of healthcare costs to providers and hospitals in excess of agreed-upon medical loss ratios, as stipulated in the contracts. Payments from the savings pool reserve are also limited by certain CMS and DMAP regulations.

Certain provider contracts include a quality bonus incentive program, which allows the contract provider to receive incentive payments that are based on various quality measures outlined in those contracts. Data related to quality measure performance is supplied by the provider group, which is evaluated by the Company to determine the final payment related to the contract year.

Net Assets - The Company is required to report its consolidated financial position and activities according to three classes of net assets: unrestricted, temporarily restricted, and permanently restricted. As of December 31, 2012 and 2011, all of the Company's net assets are unrestricted. However, in accordance with the Company's DHS contracts, the Company has designated certain amounts consisting of a primary reserve of $250,000 for each DHS contract, and an additional reserve calculated based on a percentage of the average fee for services and expenses during the period of the DHS contracts. Also, the Company has designated a reserve in accordance with the requirements of the Insurance Division. In addition, the Company has designated certain amounts for future contributions to the Osteopathic Physicians and Surgeons of Oregon, Inc. (OPSO). The Company may redesignate these net assets at its discretion.

Loss Contracts - The Company monitors its provider contracts and its contracts with DHS and CMS for the provision of medical care and recognizes losses on the contracts when it is probable that expected future healthcare and maintenance costs will exceed anticipated future premiums. The estimation of future healthcare medical costs includes all costs related to the provision of healthcare to members covered by the contracts. As of December 31, 2012, management does not anticipate that future costs will exceed premiums related to such contracts.

Revenue Recognition - Premiums from DMAP for maternity services are recognized as revenue during the period that such services are provided, whereas all other premiums from DMAP and all premiums from Medicare are recognized as revenue during the period in which the Company is obligated to provide healthcare services to its members.

Other revenue primarily consists of amounts received from the State of Oregon relating to the Adult Mental Health Initiative designed to promote more effective utilization of facility based treatment centers.

Advertising - The Company expenses advertising costs as incurred. Advertising expense amounted to approximately $224,000 and $328,000 in 2012 and 2011, respectively.

Income Taxes - FamilyCare, and Health Plans are tax-exempt organizations pursuant to Internal Revenue Code (IRC) Section 501(c)(4). Only the Company's unrelated business income is subject to federal or state income taxes. It is management's belief that none of the Company's activities have generated material unrelated business income; therefore, no provision for income taxes has been made in the accompanying consolidated financial statements.

Generally, the Company is subject to examination by federal, state and local income tax authorities for three years from the filing of a tax return. With few exceptions, the Company is no longer subject to such examinations for years ended before December 31, 2009.

Subsequent Events - The Company has performed an evaluation of subsequent events in accordance with ASC 855, *Subsequent Events*, through May 13, 2013, which is the date these consolidated financial statements were available to be issued.

Estimates - The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue, income, and expenses during the reporting period. Actual results could differ from those estimates.

Significant estimates and assumptions are used to calculate certain receivables, claims payable and unpaid claims adjudication expenses and the savings pool and quality bonus payables. If future experience differs from these estimates and assumptions, the financial statements could be materially affected. Changes in such estimates are reflected in the consolidated financial statements in the year in which such estimates are updated.

Reclassifications - Certain reclassifications have been made to the 2011 financial statements to conform to the 2012 presentation.

NOTE 2 - INVESTMENTS AND RESTRICTED INVESTMENTS

Investments and restricted investments consisted of the following at December 31:

	2012		2011	
	Cost	Fair Value	Cost	Fair Value
Common stocks	$ 2,083,226	$ 2,588,446	$ 2,035,691	$2,283,956
U.S. Treasury Securities	24,860,936	24,768,328	15,942,420	15,757,075
Corporate Bonds	7,137,212	7,125,718	647,349	662,413
	$34,081,374	34,482,492	$18,625,460	18,703,444
Less short-term investments		3,401,736		4,873,404
Less short-term restricted investments		3,383,232		894,584
Less long-term restricted investments		2,570,755		5,326,033
Long-term investments		$25,126,769		$7,609,423

Investment income consisted of the following for the years ended December 31:

	2012	2011
Interest and dividend income	$ 526,228	$ 316,753
Change in net unrealized gain (loss) on investments	349,772	(232,177)
Net realized gain (loss) on sales of investments	(240,905)	68,291
	$ 635,095	$ 152,867

NOTE 3 - FAIR VALUE MEASUREMENTS

Assets and liabilities recorded at fair value in the statements of financial position are categorized based upon the level of judgment associated with the inputs used to measure their fair value. Level inputs, as defined by ASC 820, *Fair Value Measurements and Disclosures*, are as follows:

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

Level 2: Observable inputs other than those included in Level 1. For example, quoted market prices for similar assets or liabilities in active markets, or quoted market prices for identical assets or liabilities in inactive markets.

Level 3: Unobservable inputs reflecting management's own assumptions about the inputs used in pricing the asset or liability. Level 3 assets and liabilities include investments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair values requires significant management judgment or estimation.

Fair values of assets measured on a recurring basis were as follows:

	Fair Value as of December 31, 2012			
	Total	Level 1	Level 2	Level 3
Cash and cash equivalents:				
Money Market Mutual Fund	$ 1,081,575	$ 1,081,575	$ -	$ -
Restricted cash equivalents and investments:				
Money Market Mutual Fund	648,070	648,070	-	-
US Treasury Securities	5,953,987	5,953,987	-	-
	6,602,057	6,602,057	-	-
Investments:				
Corporate Bonds	7,125,718	-	7,125,718	-
US Treasury Securities	18,814,341	18,814,341	-	-
Common Stocks:				
Large Div Value	592,973	592,973	-	-
Large Value	445,471	445,471	-	-
Large Focus Growth	864,047	864,047	-	-
Large Growth	685,955	685,955	-	-
	28,528,505	21,402,787	7,125,718	-
Total at fair value	$ 36,212,137	$ 29,086,419	$ 7,125,718	$ -

	Fair Value as of December 31, 2011			
	Total	Level 1	Level 2	Level 3
Cash and cash equivalents:				
Money Market Mutual Fund	$ 247,177	$ 247,177	$ -	$ -
Restricted cash equivalents and investments:				
Money Market Mutual Fund	334,561	334,561	-	-
US Treasury Securities	6,220,617	6,220,617	-	-
	6,555,178	6,555,178	-	-
Investments:				
Corporate Bonds	662,413	-	662,413	-
US Treasury Securities	9,536,458	9,536,458	-	-
Common Stocks:				
Large Div Value	526,320	526,320	-	-
Large Value	411,637	411,637	-	-
Large Focus Growth	724,162	724,162	-	-
Large Growth	621,837	621,837	-	-
	12,482,827	11,820,414	662,413	-
Total at fair value	$ 19,285,182	$ 18,622,769	$ 662,413	$ -

The Company's level 2 investments in corporate bonds are valued using observable market inputs obtained from pricing services. The pricing services prepare estimates of fair value measurements based on either trades executed for similar bonds or on implied yield curves using observable inputs.

The availability of observable inputs can vary from instrument to instrument and is affected by a variety of factors including the availability of published dealer quotations and interest rates on similar assets. The level of a fair value measurement within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement in its entirety. The categorization of a fair value measurement within the hierarchy is based upon the pricing transparency of the instrument and does not necessarily correspond to the Company's perceived risk of that instrument.

NOTE 4 - OTHER ASSETS

Other assets consist of the following at December 31:

	2012	2011
Reinsurance experience refund receivable	$ 398,685	$ -
Prepaid expenses	691,862	521,923
Pharmacy rebates receivable	826,815	290,394
Cash surrender value of life insurance	166,446	157,804
Claims overpayments receivable	98,700	1,637,850
Accrued interest receivable	125,141	-
Accounts receivable, net	20,922	22,607
Other receivables	35,197	684,071
	2,363,768	3,314,649
Less other current assets	1,913,115	3,146,995
Other assets	$ 450,653	$ 167,654

NOTE 5 - PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at December 31:

	2012	2011
Computer software asset	$ 2,991,877	$ 3,103,813
Computer equipment	922,854	756,033
Office furniture and equipment	876,414	865,490
Leasehold improvements	68,312	68,312
Equipment under capital leases	620,810	620,810
	5,480,267	5,414,458
Less accumulated depreciation and amortization	3,291,905	2,396,858
Less impairment of software	400,000	-
	1,788,362	3,017,600
Construction in progress	14,735	16,535
	$ 1,803,097	$ 3,034,135

Depreciation and amortization expense amounted to $1,039,159 and $948,392 in 2012 and 2011, respectively. Construction in progress as of December 31, 2012 consisted of costs incurred to implement a disaster recovery program and software upgrades and enhancements. Construction in progress as of December 31, 2011 consisted primarily of costs incurred in connection with the project to implement a disaster recovery program.

NOTE 6 - CLAIMS PAYABLE, UNPAID CLAIMS ADJUDICATION EXPENSES, AND SAVINGS POOL PAYABLE

Claims payable at December 31, 2012 and 2011 includes estimates for IBNR claims based on actuarial analyses prepared by independent actuarial firms. Activity related to claims payable, unpaid claims adjudication expenses, and savings pool payable liabilities for the years ended December 31, 2012 and 2011 was as follows:

	2012	2011
Balance at beginning of year	$ 29,224,572	$ 28,857,573
Claims incurred related to:		
Current year	143,543,738	159,455,130
Prior year	(5,338,666)	(10,238,356)
Total incurred	138,205,072	149,216,774
Claims paid related to:		
Current year	118,606,649	131,296,580
Prior year	22,976,422	17,553,195
Total paid	141,583,071	148,849,775
Balance at end of year	$ 25,846,573	$ 29,224,572

Amounts incurred related to prior years vary from previously estimated liabilities as the claims are ultimately settled.

Amounts included in the consolidated statements of financial position at December 31, 2012 and 2011 were as follows:

	2012	2011
Reported on the consolidated statements of financial position as:		
Claims payable and unpaid claims adjudication expenses	$ 24,022,361	$ 27,719,989
Savings pool and quality bonus payable	1,824,212	1,504,583
	$ 25,846,573	$ 29,224,572

NOTE 7 - LEASE COMMITMENTS

The Company leases office equipment under various lease arrangements classified as capital leases, which expire on various dates through December 2016. The total cost of the equipment under the arrangement was $620,810. The related accumulated amortization at December 31, 2012 was $183,662. Amortization of assets held under capital leases is included within administrative expenses in the accompanying consolidated statements of activities.

The Company leases equipment and office facilities under noncancelable operating lease agreements which expire on various dates through April 2019. The lease agreements include escalation provisions based on the consumer price index. Under terms of one of the lease agreements, the Company is also required to pay its proportionate share of certain operating expenses and property taxes. Total rent expense under all these agreements was approximately $649,000 and $650,000 for the years ended December 31, 2012 and 2011, respectively.

As of December 31, 2012, the future minimum lease payments owed under such noncancelable lease agreements are as follows:

Years ending December 31:

	Capital Lease Obligation	Operating Leases
2013	$ 136,080	$ 612,413
2014	136,080	636,585
2015	136,080	642,791
2016	113,022	647,308
2017	-	666,797
Thereafter	-	921,942
Total minimum lease payments	521,262	$ 4,127,836
Less amount representing interest	56,779	
Present value of net minimum lease payments	$ 464,483	

NOTE 8 - REGULATION

Health Plans is subject to various additional regulatory requirements as administered by the Insurance Division. Failure to meet minimum premium-to-surplus requirements as prescribed by the Insurance Division can initiate certain mandatory and possibly additional discretionary actions that, if undertaken, could have a direct material effect on the Company's consolidated financial statements. As of December 31, 2012 and 2011, management believes that Health Plans was in compliance with the Insurance Division's requirements.

Health Plans is licensed with the Insurance Division to operate as a commercial health insurance plan in the State of Oregon. Such plans are generally required to file audited statutory basis financial statements with the Insurance Division within five months of each calendar year-end. These statutory basis financial statements are prepared in conformity with accounting practices prescribed or permitted by the Insurance Division. Prescribed statutory accounting practices are those practices mandated by the National Association of Insurance Commissioners (NAIC), as well as state laws, regulations, and general administrative rules. In contrast, permitted statutory accounting practices are those practices for which a company has applied for and received specific permission from its state of domicile. Health Plans' statutory surplus as of December 31, 2012 is approximately $582,000 less than its total unrestricted net assets as reported in the accompanying 2012 consolidating statement of financial position. The difference is primarily due to differences in accounting for investments, certain receivables, and prepaid expenses.

The NAIC requires insurance companies to calculate risk-based capital (RBC) ratios, which serve as a benchmark for the regulation of insurance companies' solvency by state insurance regulators. The formulas for determining the amount of RBC specify various weighting factors that are applied to financial balances or various levels of activity based on a perceived degree of risk. Regulatory compliance is determined by a ratio of the enterprise's regulatory total adjusted capital to its authorized control level RBC. Enterprises below specific trigger points or ratios are classified within certain levels, each of which require specified corrective action, or may cause state regulators to take certain actions.

NOTE 9 - RETIREMENT PLAN

The Company has a safe harbor 401(k) retirement plan (the Retirement Plan) which covers substantially all employees of the Company and its subsidiaries who are at least 21 years of age and have completed six months of service.

The Retirement Plan requires the Company (including its subsidiaries) to make a contribution equal to 3% of each employee's compensation. This contribution is immediately 100% vested. The Company may also make additional discretionary contributions.

Total expense related to the retirement and profit sharing plans was approximately $241,000 and $153,000 for the years ended December 31, 2012 and 2011, respectively.

NOTE 10 - RELATED PARTY TRANSACTIONS

In 2002, the Board approved a motion to contribute an annual fixed amount of $100,000 to OPSO (a nonprofit corporation whose chief executive officer also serves as president of the Company), with the amount by which 0.5% of annual net premiums from DMAP exceeds $100,000 to be classified as designated net assets for future contributions to OPSO, subject to a maximum designated amount of $100,000. The Company contributed approximately $100,000 to OPSO under this arrangement during both 2012 and 2011, which is included in administrative expenses in the accompanying consolidated statements of activities.

During 2012 and 2011, the Company transacted business with a professional service firm whose owner is also a member of the Company's Board of Directors. Amounts paid to this firm were approximately $192,000 and $135,000 during the years ended December 31, 2012 and 2011, respectively.

The Company holds an insurance policy on the life of a key officer of the Company. The cash surrender value of the life insurance policy is $166,446 and $157,804 at December 31, 2012 and 2011, respectively.

During 2012 and 2011, the Company transacted business with providers who are also members of the company's Board of Directors. Amounts paid to these providers were approximately $4,019,000 and $2,288,000 during the years ended December 31, 2012 and 2011, respectively.

NOTE 11 - CONTINGENCIES

In the normal course of business, the Company is party to various legal proceedings, many of which involve claims related to healthcare coverage. The Company, like health maintenance organizations and other health insurers, generally excludes the coverage of certain healthcare services under its contracts. The Company, in the ordinary course of business, is subject to the claims of its enrollees arising out of decisions to restrict treatment or reimbursement for certain services. The loss of even one such claim, if it results in a significant punitive damage award, could have a material adverse effect on the Company. In addition, the risk of potential liability under punitive damage theories may significantly increase the difficulty of obtaining reasonable settlements of coverage claims. However, the financial and operating impact that such evolving theories of recovery will have on the managed care industry and the Company is presently unknown.

In 2009, a contracted medical service provider (provider) asserted that the Company underpaid the provider in the amount of $350,000 for services to enrollees in 2008. In 2009, the Company recorded an accrued loss contingency of $250,000 based on its estimate of possible loss upon settlement with the provider. In 2010, the Company made a payment to the provider in connection with its claim in the amount of $13,239, reducing the accrued loss contingency to $236,761. Also in 2010, the provider filed additional claims in arbitration based on allegations that the Company underpaid the provider for services to enrollees in 2008, 2009 and 2010. The dispute was settled in August 2011 and the Company was required to make a settlement payment in the amount of $102,083.

NOTE 12 - FUNCTIONAL EXPENSES

Expenses by major functional classification consist of the following at December 31:

	2012	2011
Medical and hospital:		
Inpatient hospital	$ 40,526,095	$ 54,311,057
Physicians services	31,318,439	31,227,323
Emergency room and out-of-area services	12,282,642	15,258,981
Other medical and hospital expenses	54,077,896	48,419,413
Total medical and hospital	138,205,072	149,216,774
Administrative:		
Compensation and benefits	9,631,713	9,857,055
Professional services	3,094,509	2,936,029
Occupancy, depreciation and amortization	2,036,565	1,561,624
Repairs and maintenance	1,058,707	574,797
Contributions to others	1,969,003	263,707
Other administrative expenses	3,349,065	3,642,876
Total administrative	21,139,562	18,836,088
Total expenses	$ 159,344,634	$ 168,052,862

NOTE 13 - CONTRIBUTIONS TO OTHERS

The Company makes donations for research, education, and other projects in the field of workforce development and utilization. The minimum amount for which the Company is obligated is recorded upon the Board of Directors' approval. Donations payable beyond one year are reported at the present value of their estimated future cash flows using a discount rate of 3.25%, and totaled $1,477,993 and $0 at December 31, 2012 and 2011, respectively.

SUPPLEMENTARY INFORMATION

PERKINS & CO

+ 1211 SW Fifth Avenue, Suite 1000
+ Portland, Oregon 97204-3710

+ Telephone: 503.221.0336
+ Fax: 503.294.4378
+ www.perkinsaccounting.com

REPORT OF INDEPENDENT AUDITOR'S ON CONSOLIDATING INFORMATION

To the Board of Directors of
FamilyCare, Inc.

We have audited the consolidated financial statements of FamilyCare, Inc. and Subsidiary (the Company) as of and for the years ended December 31, 2012 and 2011, and our report thereon dated May 13, 2013, which expressed an unqualified opinion on those financial statements, appears on page 1. Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidating statement of financial position and consolidating statement of activities are presented for purposes of additional analysis of the 2012 consolidated financial statements, rather than to present the financial position and change in unrestricted net assets of the individual companies, and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the 2012 consolidated financial statements. The consolidating information has been subjected to the auditing procedures applied in the audit of the 2012 consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the 2012 consolidated financial statements or to the 2012 consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidating information is fairly stated in all material respects in relation to the 2012 consolidated financial statements as a whole.

Perkins & Company, P.C.

May 13, 2013

FAMILIYCARE, INC. AND SUBSIDIARY
CONSOLIDATING STATEMENT OF FINANCIAL POSITION
DECEMBER 31, 2012
(see report of independent auditor's on consolidating information)

	FamilyCare, Inc.	FamilyCare Health Plans, Inc.	Consolidating Entries	Consolidated
ASSETS				
CURRENT ASSETS:				
Cash and cash equivalents	$ 11,375,340	$ 2,685,792	$ -	$ 14,061,132
Restricted cash and cash equivalents	388,070	260,000	-	648,070
Short-term investments	-	3,401,736	-	3,401,736
Restricted short-term investments	3,383,232	-	-	3,383,232
Premiums receivable from DMAP	4,596,505	-	-	4,596,505
Reinsurance receivables	1,441	26,925	-	28,366
Receivable from CMS	-	312,981	-	312,981
Due from affiliates	353,235	-	(353,235)	-
Other current assets, net	1,399,466	513,649	-	1,913,115
Total current assets	21,497,289	7,201,083	(353,235)	28,345,137
Long-term investments	21,418,421	3,708,348	-	25,126,769
Restricted long-term investments	2,570,755	-	-	2,570,755
Investment in FamilyCare Health Plans, Inc.	4,486,685	-	(4,486,685)	-
Property and equipment	1,803,097	-	-	1,803,097
Other assets	167,643	283,010	-	450,653
Total assets	$ 51,943,890	$ 11,192,441	$ (4,839,920)	$ 58,296,411
LIABILITIES AND NET ASSETS				
CURRENT LIABILITIES:				
Checks in excess of deposits	$ 446,610	$ 331,235	$ -	$ 777,845
Claims payable and unpaid claims adjudication expenses	19,594,796	4,427,565	-	24,022,361
Savings pool and quality bonus payable	1,824,212	-	-	1,824,212
Other policy liabilities	50,658	1,438,477	-	1,489,135
Due to affiliates	-	353,235	(353,235)	-
Accounts payable	1,332,081	106,519	-	1,438,600
Accrued liabilities	2,864,011	48,725	-	2,912,736
Provider taxes payable	423,715	-	-	423,715
Current portion of capital lease obligation	111,236	-	-	111,236
Total current liabilities	26,647,319	6,705,756	(353,235)	32,999,840
CAPITAL LEASE OBLIGATION, LESS CURRENT PORTION	353,247	-	-	353,247
Total liabilities	27,000,566	6,705,756	(353,235)	33,353,087
NET ASSETS:				
Unrestricted net assets:				
Designated reserve related to DMAP contract	4,797,272	-	-	4,797,272
Designated reserve related to the Insurance Division	2,500,000	2,500,000	(2,500,000)	2,500,000
Designated for OPSO	100,000	-	-	100,000
Undesignated	17,546,052	1,986,685	(1,986,685)	17,546,052
Total unrestricted net assets	24,943,324	4,486,685	(4,486,685)	24,943,324
Total liabilities and unrestricted net assets	$ 51,943,890	$ 11,192,441	$ (4,839,920)	$ 58,296,411

9/17/13

FAMILIYCARE, INC. AND SUBSIDIARY
CONSOLIDATING STATEMENT OF ACTIVITIES
YEAR ENDED DECEMBER 31, 2012
(see report of independent auditor's on consolidating information)

	FamilyCare, Inc.	FamilyCare, Health Plans, Inc.	Consolidating Entries	Consolidated
UNRESTRICTED NET ASSETS				
REVENUE				
Medicaid premiums, net	$ 138,268,595	$ -	$ -	$ 138,268,595
Medicare premiums, net	-	28,606,524	-	28,606,524
Other revenue	106,256	-	-	106,256
Total revenue	138,374,851	28,606,524	-	166,981,375
EXPENSES				
Medical and hospital	113,076,514	25,128,558	-	138,205,072
Administrative	17,299,773	3,839,789	-	21,139,562
Total expenses	130,376,287	28,968,347	-	159,344,634
CHANGE IN UNRESTRICTED NET ASSETS FROM OPERATIONS	7,998,564	(361,823)	-	7,636,741
INVESTMENT INCOME	526,525	108,570	-	635,095
LOSS FROM SUBSIDIARY	(253,253)	-	253,253	-
INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS	$ 8,271,836	$ (253,253)	$ 253,253	$ 8,271,836