

CENTENE CORP
Form 10-Q
April 23, 2019

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2019

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 (I.R.S. Employer
incorporation or organization) 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 every Interactive Data File required to be submitted 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 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, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer", "accelerated filer", "small reporting company", and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer o
Non-accelerated filer o 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.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

As of April 12, 2019, the registrant had 413,320,160 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 are forward-looking statements. Without limiting the foregoing, forward-looking statements often use words such as “believe,” “anticipate,” “plan,” “expect,” “estimate,” “intend,” “seek,” “target,” “goal,” “may,” “will,” “would,” “could,” “should,” “can,” “continue” and other words or expressions (and the negative thereof). 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. In particular, these statements include, without limitation, statements about our future operating or financial performance, market opportunity, growth strategy, competition, expected activities in completed and future acquisitions, including statements about the impact of our proposed acquisition (the WellCare Transaction) of WellCare Health Plans, Inc. (WellCare), our recent acquisition (the Fidelis Care Acquisition) of substantially all the assets of New York State Catholic Health Plan, Inc., d/b/a Fidelis Care New York (Fidelis Care), 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.”

These forward-looking statements reflect our current views with respect to future events and are based on numerous assumptions and assessments made by us in light of our experience and perception of historical trends, current conditions, business strategies, operating environments, future developments and other factors we believe appropriate. By their nature, forward-looking statements involve known and unknown risks and uncertainties and are subject to change because they relate to events and depend on circumstances that will occur in the future, 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, variables and events including but not limited to:

- the risk that regulatory or other approvals required for the WellCare Transaction may be delayed or not obtained or are obtained subject to conditions that are not anticipated that could require the exertion of management's time and our resources or otherwise have an adverse effect on us;
- the risk that our stockholders do not approve the issuance of shares of Centene common stock in the WellCare Transaction;
- the risk that WellCare's stockholders do not adopt the merger agreement (the Merger Agreement);
- the possibility that certain conditions to the consummation of the WellCare Transaction will not be satisfied or completed on a timely basis and, accordingly, the WellCare Transaction may not be consummated on a timely basis or at all;
- uncertainty as to the expected financial performance of the combined company following completion of the WellCare Transaction;
- the possibility that the expected synergies and value creation from the WellCare Transaction will not be realized, or will not be realized within the expected time period;
-

the exertion of management's time and the Company's resources, and other expenses incurred and business changes required, in connection with any regulatory, governmental or third party consents or approvals for the WellCare Transaction;

the risk that unexpected costs will be incurred in connection with the completion and/or integration of the WellCare Transaction or that the integration of WellCare will be more difficult or time consuming than expected;

the risk that potential litigation in connection with the WellCare Transaction may affect the timing of the WellCare Transaction, cause it not to close at all, or result in significant costs of defense, indemnification and liability;

unexpected costs, charges or expenses resulting from the WellCare Transaction;

- the possibility that competing offers will be made to acquire WellCare;

the inability to retain key personnel;

disruption from the announcement, pendency and/or completion of the WellCare Transaction, including potential adverse reactions or changes to business relationships with customers, employees, suppliers or regulators, making it more difficult to maintain business and operational relationships;

the risk that, following the WellCare Transaction, the combined company may not be able to effectively manage its expanded operations;

our ability to accurately predict and effectively manage health benefits and other operating expenses and reserves;

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•competition;

•membership and revenue declines or unexpected trends;

•changes in healthcare practices, new technologies, and advances in medicine;

•increased healthcare costs;

•changes in economic, political or market conditions;

•changes in federal or state laws or regulations, including changes with respect to income tax reform or government healthcare programs as well as changes with respect to the Patient Protection and Affordable Care Act and the Health Care and Education Affordability Reconciliation Act, collectively referred to as the Affordable Care Act (ACA) and any regulations enacted thereunder that may result from changing political conditions or judicial actions, including the ultimate outcome of the District Court decision in "Texas v. United States of America" regarding the constitutionality of the ACA;

•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, TRICARE or other customers);

•the difficulty of predicting the timing or outcome of pending or future litigation or government investigations;

•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 Fidelis Care Acquisition, will not be realized, or will not be realized within the expected time period;

•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 any regulatory, governmental or third party consents or approvals for acquisitions, including the Fidelis Care Acquisition;

•disruption caused by significant completed and pending acquisitions, including, among others, the Fidelis Care Acquisition, making it more difficult to maintain business and operational relationships;

•the risk that unexpected costs will be incurred in connection with the completion and/or integration of acquisition transactions, including among others, the Fidelis Care Acquisition;

•changes in expected closing dates, estimated purchase price and accretion for acquisitions;

•the risk that acquired businesses, including Fidelis Care, will not be integrated successfully;

•the risk that, following the Fidelis Care Acquisition, we may not be able to effectively manage our expanded operations;

•restrictions and limitations in connection with our indebtedness;

•our ability to maintain the Centers for Medicare and Medicaid Services (CMS) Star ratings and maintain or achieve improvement in other quality scores in each case that can impact revenue and future growth;

•availability of debt and equity financing, on terms that are favorable to us;

•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 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 report 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 and selling, general and administrative 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 and acquisition related expenses 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, 2019 2018	
GAAP net earnings	\$522	\$340
Amortization of acquired intangible assets	65	39
Acquisition related expenses	18	21
Income tax effects of adjustments ⁽¹⁾	(20)	(14)
Adjusted net earnings	\$585	\$386
GAAP diluted earnings per share (EPS)	\$ 1.24	\$ 0.96
Amortization of acquired intangible assets ⁽²⁾	0.12	0.09
Acquisition related expenses ⁽³⁾	0.03	0.04
Adjusted Diluted EPS	\$ 1.39	\$ 1.09

(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 is net of an income tax benefit of \$0.04 and \$0.02 for the three months ended March 31, 2019 and 2018, respectively.

(3) Acquisition related expenses per diluted share are net of an income tax benefit of \$0.01 and \$0.02 for the three months ended March 31, 2019 and 2018, respectively.

	Three Months Ended March 31, 2019 2018	
GAAP selling, general and administrative expenses	\$1,609	\$1,316
Acquisition related expenses	17	21
Adjusted selling, general and administrative expenses	\$1,592	\$1,295

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FINANCIAL INFORMATION

ITEM 1. Financial Statements.

CENTENE CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In millions, except shares in thousands and per share data in dollars)

	March 31, 2019 (Unaudited)	December 31, 2018
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 6,345	\$ 5,342
Premium and trade receivables	5,819	5,150
Short-term investments	697	722
Other current assets	755	784
Total current assets	13,616	11,998
Long-term investments	7,186	6,861
Restricted deposits	582	555
Property, software and equipment, net	1,800	1,706
Goodwill	6,981	7,015
Intangible assets, net	2,208	2,239
Other long-term assets	1,196	527
Total assets	\$ 33,569	\$ 30,901
LIABILITIES, REDEEMABLE NONCONTROLLING INTERESTS AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Medical claims liability	\$ 7,381	\$ 6,831
Accounts payable and accrued expenses	4,641	4,051
Return of premium payable	718	666
Unearned revenue	363	385
Current portion of long-term debt	40	38
Total current liabilities	13,143	11,971
Long-term debt	6,775	6,648
Other long-term liabilities	2,007	1,259
Total liabilities	21,925	19,878
Commitments and contingencies		
Redeemable noncontrolling interests	10	10
Stockholders' equity:		
Preferred stock, \$0.001 par value; authorized 10,000 shares; no shares issued or outstanding at March 31, 2019 and December 31, 2018	—	—
Common stock, \$0.001 par value; authorized 800,000 shares; 419,058 issued and 413,305 outstanding at March 31, 2019, and 417,695 issued and 412,478 outstanding at December 31, 2018	—	—
Additional paid-in capital	7,491	7,449
Accumulated other comprehensive earnings (loss)	38	(56)
Retained earnings	4,185	3,663
Treasury stock, at cost (5,753 and 5,217 shares, respectively)	(174)	(139)

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Total Centene stockholders' equity	11,540	10,917
Noncontrolling interest	94	96
Total stockholders' equity	11,634	11,013
Total liabilities, redeemable noncontrolling interests and stockholders' equity	\$ 33,569	\$ 30,901

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

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CONSOLIDATED STATEMENTS OF OPERATIONS

(In millions, except shares in thousands and per share data in dollars)

(Unaudited)

	Three Months Ended March 31,	
	2019	2018
Revenues:		
Premium	\$16,203	\$11,903
Service	635	653
Premium and service revenues	16,838	12,556
Premium tax and health insurer fee	1,606	638
Total revenues	18,444	13,194
Expenses:		
Medical costs	13,882	10,039
Cost of services	544	543
Selling, general and administrative expenses	1,609	1,316
Amortization of acquired intangible assets	65	39
Premium tax expense	1,659	546
Health insurer fee expense	—	171
Total operating expenses	17,759	12,654
Earnings from operations	685	540
Other income (expense):		
Investment and other income	99	41
Interest expense	(99) (68
Earnings from operations, before income tax expense	685	513
Income tax expense	166	175
Net earnings	519	338
Loss attributable to noncontrolling interests	3	2
Net earnings attributable to Centene Corporation	\$522	\$340
Net earnings per common share attributable to Centene Corporation:		
Basic earnings per common share	\$1.26	\$0.98
Diluted earnings per common share	\$1.24	\$0.96
Weighted average number of common shares outstanding:		
Basic	412,924	347,843
Diluted	419,752	355,380

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,	
	2019	2018
Net earnings	\$519	\$338
Change in unrealized gain (loss) on investments, net of tax	94	(52)
Foreign currency translation adjustments	—	1
Other comprehensive earnings (loss)	94	(51)
Comprehensive earnings	613	287
Comprehensive loss attributable to noncontrolling interests	3	2
Comprehensive earnings attributable to Centene Corporation	\$616	\$289

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 shares in thousands and per share data in dollars)
(Unaudited)

Three Months Ended March 31, 2019

	Centene Stockholders' Equity					Treasury Stock		Non-controlling Interest	Total
	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Earnings (Loss)	Retained Earnings	Par Value	Amt			
	\$0.001 Par Value Shares	Amt			\$0.001 Par Value Shares				
Balance, December 31, 2018	417,695	\$ —	\$ 7,449	\$ (56)	\$ 3,663	5,217	\$ (139)	\$ 96	\$ 11,013
Comprehensive Earnings:									
Net earnings (loss)	—	—	—	—	522	—	—	(2)	520
Other comprehensive earnings, net of \$30 tax	—	—	—	94	—	—	—	—	94
Common stock issued for employee benefit plans	1,363								