PREFILED WRITTEN TESTIMONY
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This written testimony is submitted to the Maryland Insurance Administration (the "Administration") on behalf of Evergreen Health, Inc. ("Evergreen Health") in connection with an independent valuation provided by Moss Adams LLP ("Moss Adams") to the Board of Directors of Evergreen Health. Moss Adams was first engaged by Evergreen Health in September of 2016 and provided an independent valuation to the Board of Directors at its meeting on October 3, 2016. After Evergreen Health pursued a different transaction, Moss Adams was asked to update its independent valuation as of January 31, 2017. That independent valuation was presented to the Board at its meeting on April 4, 2017. The Valuation Analysis report as of January 31, 2017 (the "Valuation Analysis") was submitted to the Administration on May 1, 2017 as part of Evergreen Health's application to convert from a nonprofit entity to a for-profit entity. Moss Adams has been asked by Evergreen Health to discuss how events and financial results have impacted value from January 31, 2017 to a more current date. The purpose of this testimony is to both describe the valuation methodologies employed by Moss Adams in its analysis as well as to discuss the value of Evergreen Health as of March 31, 2017 and taking into account the surplus notes issued in April and May of 2017.

Background and Qualifications of Calvin Swartley and of Moss Adams

Moss Adams provides accounting, tax, and consulting services to public and private middle-market enterprises in many different industries and with clients in every state across the nation. With 2,500 employees, Moss Adams is one of the 15 largest accounting and consulting firms in the United States. Moss Adams provides consulting and advisory services for mergers and acquisitions, corporate finance, valuations, business owner succession, business planning, litigation and forensic accounting, information technology integration and reviews, and compensation.

I am a member of the Valuation & Litigation Services Group of Moss Adams. I have a BS degree in Business Administration from Lewis & Clark College and an MBA from Washington University. I have received the Chartered Financial Analyst (CFA) designation from the CFA Institute and the Accredited Senior Appraiser (ASA) designation from the American Society of Appraisers. I joined Moss Adams in 1998 and focus my practice on business valuations, including the analysis and valuation of health care-related operating companies like Evergreen Health. Relevant experience in this area includes determining the fair market value of the total surplus of Blue Cross Blue Shield of Montana, Inc. and providing expert testimony before the State of Montana Department of Securities and Insurance and the Department of Justice.

Significant Subsequent Events

As noted on page 2 of the Valuation Analysis, significant events subsequent to the appraisal date were not considered as part of the analysis. The Valuation Analysis was performed as of January 31, 2017 and was based on an appraisal investigation that occurred in February and early March of 2017.

We have been advised by Evergreen Health that there have been significant events subsequent to our Valuation Analysis and we understand that the Administration wishes us to discuss how these subsequent events and financial results would impact our Valuation Analysis as of January 31, 2017.

Since early March of 2017, Evergreen Health has made certain adjustments to its 2016 year-end statutory financial statements, both because of items it identified in the course of its own diligence as well as items identified in the course of the audit of the 2016 financial statements. One effect of these adjustments is that the surplus as of December 31, 2016 was adjusted from ($5,421,970) to ($11,355,979), on a statutory basis.

In addition, Evergreen Health has experienced net operating losses in each month of January[1] through March 2017, which reduces surplus month over month. Mitigating this loss of surplus are the additional surplus notes issued to the three entities that have applied to acquire control of Evergreen Health. Evergreen Health's surplus as of March 31, 2017 was ($11,672,248).[2]

In this testimony, we will describe the valuation methodologies employed in the original analysis and comment on the impact of the subsequent events and financial results to the Valuation Analysis.

Overview of Valuation Methodologies

In determining the value of Evergreen Health, we considered the income approach, the market approach, and the asset-based approach. We then considered the appropriate weight to apply to each approach given the specific facts and circumstances of Evergreen Health. The premise of value generally used in the Valuation Analysis is going concern value which is based on the concept that a business enterprise is expected to continue operations into the future. Therefore, the valuation approaches we analyzed give consideration to the factor that the Administration may consider in § 6.5-301(d)(2) of the State Government Article (the value as a going concern).

In addition, Section 6.5-301(d)(1) permits the Administration to consider the value of Evergreen Health determined as if Evergreen Health has voting stock outstanding and 100 percent of its stock is freely transferable and available for purchase without restriction. The valuation was performed on a 100 percent controlling interest basis. This assumes that 100 percent of the Company's stock is included in any transfer and the transfer occurs in an open market. If the interest had been less than 100 percent or non-controlling, we may have considered discounts such as lack of control.

1 The January 2017 net loss is after removing the imputed gain from the repayment of the CMS Surplus Note at a discount.

2 This surplus reflects the issuance of $6 million in surplus notes in January 2017. An additional $6 million in surplus notes were issued in the second quarter of 2017.

The Income Approach

Income approach valuation methods include discounted cash flow and capitalization of cash flow analyses. In the discounted cash flow analysis, future cash flows are discounted to present value using an appropriate discount rate or rate of return for the investment. Cash flows are forecasted for a discrete period of years (here, five years) and then projected to grow at a constant rate in perpetuity (the residual period). The capitalization of cash flow analysis uses forecasted cash flow for the next period, which is converted to present value using an appropriate capitalization rate, equal to the discount rate less the expected growth rate in perpetuity. The capitalization of cash flow analysis was not used in this valuation as it requires a normalized level of earnings and cash flow, which the Company is not expected to report for several years. The income approach valuation methodology is one that the Administration may consider pursuant to § 6.5-301(d)(4) of the State Government Article (the investment or earnings value). In essence, this method projects the future income potential of Evergreen Health and provides a value based on the future earnings and cash flows of Evergreen Health at a specific point in time.

We considered the income approach for Evergreen Health under a scenario in which Evergreen Health is able to find an investor and continue normal operations (scenario #1) and a wind-down scenario (scenario #2). I will address only scenario #1 in this testimony as it is the more relevant scenario for valuing Evergreen Health for purposes of the proposed acquisition.

A variety of factors are used to determine the discount rate to apply in the income approach. In determining Evergreen Health's discount or return rate we considered market based factors, such as required return rates based on risk free rates, market return rates, and industry characteristics. Further, in assessing specific or subject company risk within our return rate, we considered the Company's history, its position in the marketplace, its historical operating and financial results, and its projected future results. Based on our evaluation of the risks associated with Evergreen Health, we concluded an appropriate discount rate for scenario #1 is 22%.

The residual capitalization rate utilized in the residual period is equal to the discount rate minus the expected long-term growth rate of cash flows. Based on historical results, the economic climate, the outlook for the industry, and management's expectations, we estimated a long-term growth rate of 2.5%.

In this approach, we used a 2017 budget that was prepared in early 2017, and a five-year projection prepared by management in late 2016 to determine the Company's free cash flow (debt free). We then calculated the present value of the free cash flows over a discrete five year period. To this value we added the present value of the residual period to reach an indicated total enterprise value of $5,047,000. From this value we subtracted the $6 million surplus notes issued by Evergreen Health on January 17, 2017 (interest-bearing debt) to reach an indicated equity or surplus value of ($953,000) under scenario #1. The concluded equity or surplus value from the income approach, therefore, was $0.[3]

[3] Scenario #2 produced an indicated equity value of ($11,867,000) which also resulted in a concluded value of $0.

We note that the three-year pro formas attached to the Form A Statement of JARS Health Investments, LLC, Anne Arundel Health System, Inc. and LBH Evergreen Holdings, LLC (the "Purchasers") project lower revenue as compared to the projections we were provided in late 2016 and early 2017. Overall we noted that in the new projections the Company's member and revenue growth expectations had been lowered. Further, cash flow (EBITDA) was also projected to be lower than the levels included in our valuation analysis. Even with these modifications, there is still significant risk of the Company meeting those projections. For the value of Evergreen Health to increase in this approach either cash flow (EBITDA) would have to increase or the discount rate would have to decline (or both of these events would have to occur). The three-year pro formas do not result in higher cash flows and there is not enough evidence to lower the discount rate from the level included in our January 31, 2017 valuation. Therefore, it appears that the income approach would not increase from the levels we concluded in our January 31, 2017 valuation.

In addition, since January 31, 2017, Evergreen Health has issued an additional $6 million in surplus notes to the Purchasers. Although the initial impact of this debt would increase cash holding of the Company, it has most likely been used to offset the Company's continuing losses. Any update of the valuation would consider a debt balance of $12 million. Thus the income approach results in a $0 equity or surplus value for Evergreen Health.

The Market Approach

In a market approach, valuation approaches include the consideration of a public company analysis, a merger and acquisition analysis, and a prior transaction analysis. In this case, we did not consider a prior transaction analysis (of either the entire Company or any interest in the Company) because there were no arm's length sales transactions involving ownership interests in Evergreen Health. The focus, rather, was on the public company analysis and the merger and acquisition analysis. We note that this valuation methodology is one that the Administration may consider pursuant to § 6.5-301(d)(3) of the State Government Article (the market value).

In this approach, we considered publicly-traded companies in similar lines of business to Evergreen Health. These companies are influenced by comparable business and economic conditions as Evergreen Health. We used the SEC filings for these companies to derive a number of valuation ratios, including total equity. Each of these valuation ratios was applied to Evergreen Health's financials to produce an indication of equity or surplus value. The results of this analysis were not meaningful because of the negative equity/surplus position of the Company.

We also considered merger and acquisition transactions involving companies that are similar in nature to Evergreen Health. Valuation ratios were derived from the merger and acquisition transactions studied, and these valuation ratios were then applied to Evergreen Health's financials. As in the publicly-traded company analysis, the results of this analysis were not meaningful.

Section 6.5-301(d)(6) permits the Administration to consider whether a control premium should be applied to the proposed conversion of Evergreen Health. To address this consideration, we searched ten years of transactions in the Control Premium Study database to find comparable transactions in the healthcare insurance industry and the reported control premium for those transactions. The most recent transactions in the database reflected a small control premium of 3.4%. These transactions involved public companies acquiring other public companies. It is our opinion that a control premium should not be applied to the value of Evergreen Health because the Company is small, does not have a long history, has poor financial results, and has not garnered acquisition interest from other insurance companies in the health insurance industry.

The Asset-Based Approach

In the asset-based approach, net asset value is estimated by restating the value of assets and liabilities from historical cost to fair market value. This valuation methodology is one that the Administration may consider pursuant to § 6.5-301(d)(5) of the State Government Article (the net asset value).

In this approach, we restated the value of Evergreen Health's assets and liabilities from historical cost to fair market value as of December 31, 2016 and adjusted the values to January 31, 2017. We also considered and included assets that are not reported on a statutory basis. We then subtracted total liabilities from total assets to determine a net asset value. The net asset value was ($2,319,000) as of December 31, 2016 and ($730,000) as of January 31, 2017. We further adjusted the net asset value as of January 31, 2017 by reclassifying the surplus notes as debt, resulting in an adjusted net asset value of ($6,730,000) as of January 31, 2017.

The negative adjustments to surplus as of December 31, 2016 booked in the first and second quarters of 2017 would further reduce the Company's net asset value, as would the additional $6 million in surplus notes issued to the Purchasers in April and May of 2017. Thus, the net asset value analysis results in a concluded equity or surplus value of $0.

Conclusion

As described more fully in the Valuation Analysis, we considered the income approach, market approach, and asset-based approach in determining the fair value of Evergreen Health. The final step in a valuation analysis is to reconcile and weight each valuation methodology in order to reach a final, concluded equity or surplus value.

Of the three methods, we gave the most weight to the market approach. In this instance, the publicly-traded company multiples and merger and acquisition transaction multiples provide the best indication of value of the subject Company. Although the results of this valuation methodology are reported as "not meaningful" due to the negative equity/surplus position of Evergreen Health, they indicate that there is no equity or surplus value for the Company.

We gave some weight to the income approach, as this approach represents the amount a prudent investor would pay for a company's expected future cash flows based on market rates of return and the company's specific risks. We believe this approach results in a valid value for a company like Evergreen Health.

We gave little weight to the asset-based approach because, although it provides a value at a specific point in time, investors tend to focus more on earnings and cash flow than on the value of the underlying assets.

As of January 31, 2017, our opinion of the range of fair market value of the equity or surplus of Evergreen Health on a going concern basis was $0 to $379,000. We concluded that the value of the public or charitable assets of Evergreen Health was $0 based on our determination that the value of the public or charitable assets is the excess value of Evergreen Health's assets above the value of its liabilities.[4]

We determined a range of fair market value of the equity or surplus of Evergreen Health as of January 31, 2017 of less than $0 to $379,000 by determining a high value and low value under the approaches described above. The new investor, high value (Scenario #1) under the income approach produced the only positive equity or surplus value for Evergreen Health. The new investor, low value (Scenario #2) under the income approach and all other valuation approaches we applied concluded an equity or surplus value of $0, or less than $0. In light of the adjustments to surplus as of December 31, 2016 made since the time of our Valuation Analysis and the additional surplus notes that have been issued to the Purchasers, all valuation approaches, including the new investor, high value (Scenario #1) under the income approach, would produce values of $0 or less than $0. Thus, although we found some potential value as of January 31, 2017 using the income approach, our opinion as of March 31, 2017, and taking into account the surplus notes issued by Evergreen Health, is that the concluded value of Evergreen Health under all valuation approaches is $0 or less than $0. Further, it is our opinion that the value of the public or charitable assets of Evergreen Health remains $0 as of March 31, 2017.

Respectfully submitted,

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[4] We assumed for purposes of the Valuation Analysis and this testimony that Evergreen Health's assets are public assets and, therefore, did not address whether the assets would qualify as charitable assets.