GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Consolidated Financial Statements

Federal Uniform Guidance Reports

Year ended December 31, 2016 (Restated)

(With Independent Auditors' Reports Thereon)

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

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KPMG LLP
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

Independent Auditors' Report

The Board of Directors
Kaiser Foundation Health Plan of Washington
Seattle, Washington

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Group Health Cooperative and Subsidiaries (the Group), which comprise the consolidated balance sheets as of December 31, 2016 and 2015, and the related consolidated statements of operations and changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from 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 auditors' 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.

Emphasis of Matter

As discussed in note 17 to the consolidated financial statements, the 2016 consolidated financial statements have been restated to correct a misstatement. Our opinion is not modified with respect to this matter.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Group Health Cooperative and Subsidiaries as of December 31, 2016 and 2015 and the changes in their net assets and their cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.

Other Matter

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis, as required by Title 2 U.S. Code of Federal Regulations, Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards,* and is 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 consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the 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 consolidated financial statements or to the 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 schedule of expenditure of federal awards is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 24, 2017, except for the effects of the restatement described in Note 17 and subsequent events in Note 18, as to which the date is June 1, 2017, on our consideration of the Group's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Group's internal control over financial reporting and compliance.

KPMG LLP

Seattle, Washington
March 24, 2017, except for
the effects of the restatement
described in Note 17 and subsequent
events in Note 18, as to which
the date is June 1, 2017

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2016 and 2015

(In thousands)

Assets		**2016 (Restated)**	**2015**
Current assets:			
Cash and cash equivalents	$	87,413	183,325
Short-term marketable securities		52,513	23,094
Accounts receivable – net		211,707	147,752
Inventories		27,724	18,072
Other		36,827	24,690
Total current assets		416,184	396,933
Long-term marketable securities		1,001,640	1,065,977
Long-term investments – other		117,038	69,055
Restricted assets		—	32,522
Land, buildings, and equipment:			
Land		30,574	30,835
Buildings and improvements		636,008	603,169
Equipment		391,104	411,772
Construction in progress		29,046	31,656
Total land, buildings, and equipment		1,086,732	1,077,432
Less accumulated depreciation		(662,264)	(680,800)
Land, buildings, and equipment – net		424,468	396,632
Other assets		36,034	58,186
Total	$	1,995,364	2,019,305

(Continued)

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2016 and 2015

(In thousands)

Liabilities and Net Assets		2016 (Restated)	2015
Current liabilities:			
Accounts payable and accrued expenses	$	212,876	115,662
External delivery services payable		254,372	253,605
Unearned premiums and deposits		89,468	81,546
Accrued employee compensation		64,882	61,169
Accrued taxes and interest		38,687	46,613
Current portion of long-term debt		—	6,003
Current portion of reserve for self-insurance		15,567	16,945
Current portion of retiree medical benefits		3,870	4,369
Total current liabilities		679,722	585,912
Noncurrent liabilities:			
Long-term debt		—	116,898
Self-insurance		42,449	40,646
Retiree medical benefits		33,488	40,544
Pension		164,781	185,622
Other		14,663	16,089
Total noncurrent liabilities		255,381	399,799
Total liabilities		935,103	985,711
Commitments and contingencies (note 11)			
Net assets:			
Unrestricted		1,044,228	1,017,767
Temporarily restricted		6,393	6,218
Permanently restricted		9,640	9,609
Total net assets		1,060,261	1,033,594
Total	$	1,995,364	2,019,305

See accompanying notes to consolidated financial statements.

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Consolidated Statements of Operations and Changes in Net Assets

Years ended December 31, 2016 and 2015

(In thousands)

		2016 (Restated)	2015
Revenues:			
Premiums	$	3,366,056	3,222,452
Clinical services – net		361,745	325,431
Other		122,055	109,720
Total operating revenues		3,849,856	3,657,603
Expenses:			
External delivery services		1,971,900	1,846,401
Employee compensation		607,793	572,841
Medical and operating supplies		421,413	358,573
Group Health Physicians expense		409,340	352,194
Other expenses		180,497	169,437
Services purchased		119,090	119,733
Business taxes and insurance		121,514	107,011
Depreciation and amortization		61,859	56,737
Total operating expenses		3,893,406	3,582,927
Operating (loss) income		(43,550)	74,676
Nonoperating income (expense):			
Investment income – net		60,591	42,579
Interest expense		(10,963)	(3,652)
Total nonoperating income		49,628	38,927
Excess of revenues over expenses		6,078	113,603
Change in net unrealized investment gains and losses		2,256	(29,189)
Change in defined benefit pension and other postretirement plans		18,227	(3,982)
Other		(100)	(117)
Change in unrestricted net assets		26,461	80,315
Change in temporarily restricted net assets		175	(990)
Change in permanently restricted net assets		31	161
Change in net assets		26,667	79,486
Net assets:			
Beginning of year		1,033,594	954,108
End of period	$	1,060,261	1,033,594

See accompanying notes to consolidated financial statements.

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended December 31, 2016 and 2015

(In thousands)

	2016 (Restated)	2015
Cash flows from operating activities:		
Change in net assets	$ 26,667	79,486
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	61,859	56,737
Pension actuarial adjustment	19,159	34,979
Provision for self-insurance	8,906	11,770
Realized and change in unrealized investments (gains) and losses, net	(34,062)	20,064
Change in fair value of interest rate swap	5,388	(1,069)
Gain on sale of land, buildings, and equipment	(9)	(790)
Equity loss (income) of equity method investees	521	(3,939)
Other	8,328	3,141
Cash provided by operating assets and liabilities:		
Accounts receivable – net	(63,955)	2,793
Inventories	(9,652)	(1,308)
Other current and noncurrent assets	1,366	(3,635)
Accounts payable and accrued expenses	88,267	(21,354)
External delivery services payable	767	24,685
Unearned premiums and deposits	9,624	9,209
Accrued employee compensation	3,713	(25,190)
Accrued taxes and interest	(7,926)	(7,147)
Self-insurance	(8,481)	(21,158)
Retiree medical benefits	(7,555)	(6,962)
Pension	(40,000)	(40,000)
Other noncurrent liabilities	(1,425)	(6,367)
Net cash provided by operating assets and liabilities	61,500	103,945
Cash flows from investing activities:		
Payments for land, buildings, and equipment	(80,706)	(39,294)
Proceeds from disposal of land, buildings, and equipment	37	1,120
Proceeds from sale of marketable securities	521,876	408,471
Purchases of marketable securities	(459,636)	(464,003)
Distribution from equity investments	1,496	1,476
Purchases of long-term investments – other	(50,000)	(8,227)
Release of restricted assets	32,522	5,918
Collateralized security	—	22,700
Net cash used in investing activities	(34,411)	(71,839)
Cash flows from financing activities:		
Repayment of long-term debt	(122,901)	(5,918)
Other	(100)	(117)
Net cash used in financing activities	(123,001)	(6,035)
Net (decrease) increase in cash and cash equivalents	(95,912)	26,071
Cash and cash equivalents:		
Beginning of year	183,325	157,254
End of period	$ 87,413	183,325
Supplemental disclosure of cash flow information:		
Cash paid during the year for:		
Interest	$ 3,798	2,009
Income taxes	14,750	13,397

See accompanying notes to consolidated financial statements.

(1) Organization

The accompanying consolidated financial statements include the accounts of Group Health Cooperative (GHC), GHC's wholly owned subsidiary, Group Health Options, Inc. (GHO), and controlled affiliates, Columbia Medical Associates, LLC (CMA) and Group Health Foundation (the Foundation), (collectively, the Group).

GHC is a Washington nonprofit corporation registered as a health maintenance organization headquartered in Seattle, Washington. GHC offers comprehensive, coordinated health care to an enrolled membership for a fixed fee through its owned and leased facilities, employed providers, and contracted providers, in addition to providing certain health care services on a fee-for-service basis to both enrollees and nonenrollees.

GHO is a Washington for-profit corporation registered and operating as a health care service contractor headquartered in Seattle, Washington. GHO provides health care coverage products that feature increased customer choice, including point of service and preferred provider organization plan benefits. It is also registered in Idaho as a Disability, Including Managed Care Carrier, operating in two counties.

CMA is a Washington limited liability company headquartered in Spokane, Washington. CMA provides medical services to families and individuals within the greater Spokane area.

The Foundation is a Washington nonprofit corporation. It is organized exclusively to benefit, perform the functions of, and carry out the purposes of GHC and other affiliated tax-exempt organizations. It supports research, health careers, training, health education, GHC programs, and other projects that promote high quality health care. Grants are awarded to qualified health-related community organizations, extending the internal resources of GHC to the community. The Foundation's operations are largely a function of the level of donations it receives.

In 2015, a formal plan of reorganization was entered into by GHC, GHO, and KPS Health Plans (KPS), a controlled affiliate of GHC. The plan of reorganization set forth that GHC was to contribute its sole membership interest in KPS to GHO with a subsequent voluntary wind up of KPS, effective December 31, 2015. GHC contributed its sole membership interest in KPS to GHO on December 1, 2015. Assets and liabilities of KPS were transferred to GHO as of December 31, 2015. KPS's Certificate of Registration as a health care service contractor was surrendered by KPS and cancelled by the Washington State Office of the Insurance Commissioner effective December 31, 2015. KPS filed the Articles of Dissolution with the Washington Secretary of State and was dissolved on March 3, 2016.

In December 2015, GHC signed an agreement to be acquired by Kaiser Foundation Health Plan of Washington (KFHPW). Closing of the acquisition was subject to certain conditions, including approval by GHC's eligible voting members, filings with, and approval by, state and federal regulators, and just prior to closing, separation of the Foundation as a controlled affiliate of GHC. On March 12, 2016, GHC's eligible voting members approved the Plan of Member Substitution, the resolution supporting KFHPW's acquisition of GHC. The federal antitrust regulatory review pursuant to the Hart-Scott-Rodino Act was complete on March 10, 2016.

On January 13, 2017, the Washington State Office of Insurance Commissioner approved the acquisition. On January 31, 2017, the Foundation separated from GHC. KFHPW acquired and became the sole corporate member of GHC on February 1, 2017.

(Continued)

Following the acquisition, KFHPW was renamed “KFHPW Holdings” (Holdings), GHC was renamed “Kaiser Foundation Health Plan of Washington,” and GHO was renamed “Kaiser Foundation Health Plan of Washington Options, Inc.”

(2) Summary of Significant Accounting Policies

(a) Principles of Consolidation

The consolidated financial statements include those of GHC, its wholly owned subsidiary, and controlled affiliates. All significant intercompany accounts and transactions have been eliminated in these consolidated financial statements.

The Group has prepared the accompanying consolidated financial statements in accordance with U.S. generally accepted accounting principles (GAAP).

(b) Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements. Significant estimates and assumptions are used in the recording of external delivery services payable, fair value of financial instruments, allowances for uncollectible accounts, reinsurance, risk adjustment, risk corridor, self-insurance reserves, pension liabilities, retiree medical liabilities, and the evaluation of contingencies and litigation. Changes in these estimates and assumptions may have a material impact on the consolidated financial statements.

(c) Cash and Cash Equivalents

Cash and cash equivalents consist of liquid investments with original or remaining maturities of three months or less at the date of purchase and approximate fair value. Cash equivalents generally consist of money market funds, U.S. Treasury bills, and commercial paper.

The Group is potentially subject to a concentration of credit risk related to financial instruments such as funds held at high credit quality financial institutions, and at times, such balances with any one financial institution may exceed the Federal Deposit Insurance Corporation’s (FDIC) insured limits.

(d) Marketable Securities

Marketable securities are readily convertible to cash, are carried at fair value, and are classified as available-for-sale securities. The Group considers securities that will mature within one year as short-term investments. The change in unrealized gains and losses is recorded as a separate component of the change in net assets for GHC and GHO. The Foundation records the change in unrealized gains and losses in investment income. The cost of debt securities is adjusted for amortization of premiums and accretion of discounts to maturity or, in the case of mortgage-backed securities, over the estimated life of the security. The discount or premium is amortized using the effective-yield method. Such amortization and accretion is included in investment income. Realized gains or losses on sale are calculated using the first-in, first-out (FIFO) method and are recorded in investment income. The Group’s investment transactions are recorded on a trade-date basis.

(e) Repurchase Agreements

Repurchase agreements are used to obtain short-term use of funds. Under the terms of a repurchase agreement, the transferor (borrower) transfers a security to a transferee (lender) in exchange for cash and concurrently agrees to reacquire the security at a future date. If the transferor does not surrender control of the underlying security, the transaction is accounted for as a secured borrowing and reported as a receivable by the transferee. When the transferor does surrender control, the transaction is accounted for as a sale.

The Group enters into tri-party repurchase agreements where it lends cash and receives highly liquid, high quality securities, such as U.S. Treasuries, and are accounted for as secured borrowings. The Group requires a minimum of 102% of the fair value of securities purchased under repurchase agreements to be maintained as collateral and has accepted collateral that is permitted by contract or custom to sell or repledge. There were no repurchase agreements held as of December 31, 2016 and 2015.

(f) Other-than-Temporary Impairment (OTTI)

An investment is impaired if the fair value of the investment is less than its book value or amortized cost, resulting in an unrealized loss position. Impaired securities are assessed to determine if the impairment is other-than-temporary. The Group evaluates investment securities for OTTI based on qualitative and quantitative factors. If the Group has the intent to sell, or it is more likely than not that it will sell the security before recovery, OTTI is recorded in income equal to the entire difference between the security’s book or amortized cost basis and its fair value at the consolidated balance sheet date.

For debt securities, if the Group does not intend to sell or it is more likely than not it will be required to sell the security before recovery, OTTI is separated into the amount representing the credit loss and the amount related to all other factors. The credit component of the OTTI is recognized in income and the noncredit component is recognized as a component of the changes in net assets. The credit component of OTTI is determined by comparing the present value of projected future cash flows with the amortized cost basis of the fixed income security. The present value is calculated by discounting the projected future cash flows at the effective interest rate implicit in the fixed income maturity at the date of acquisition. For mortgage-backed and asset-backed securities, cash flow estimates are based on assumptions regarding the underlying collateral including prepayment speeds, type of underlying assets, geographic concentrations, default rates, recoveries, and changes in value. For all other debt securities, cash flow estimates are driven by assumptions regarding probability of default, including changes in credit ratings, and estimates regarding timing and amount of recoveries associated with a default. Unrealized losses caused by noncredit related factors related to debt securities, for which the Group expects to fully recover the amortized cost basis, continue to be recognized as a component of net assets.

(g) Accounts Receivable

Accounts receivable are primarily comprised of premiums, receivables for noncovered health care services, copays and deductibles, receivables for fee-for-service clinical services provided to nonenrollees, and reinsurance. The Group records a reduction in the related premium revenues for an estimate of amounts related to retroactive enrollment changes. Provisions for contractual adjustments and bad debts related to clinical services revenues are recorded on the accrual basis and deducted from gross revenues.

(h) Provision for Uncollectible Accounts and Retroactivity

The Group provides an allowance for potential uncollectible accounts receivable whereby such receivables are reduced to their estimated net realizable value. There are various factors that can impact the collection trends and the estimation process, such as changes in the economy, the increased burden of copays and deductibles to be made by enrollees, and business practices related to collection efforts.

The Group estimates the allowance for receivables of noncovered health care services, fee-for-service clinical services, and other receivables based on the aging of accounts receivable, historical collection experience, and other relevant factors. The allowance for uncollectible accounts was $3,787,000 and $2,403,000 at December 31, 2016 and 2015, respectively.

Due to lack of collectibility, an allowance for Affordable Care Act Risk Corridor receivable was $15,327,000 as of December 31, 2016 for benefit year 2016 and benefit year 2015. The net receivable balance is zero.

The allowance for receivables of premiums is based on aging of accounts receivable and historical experience of enrollment retroactive changes. The allowance for retroactivity was $9,364,000 and $15,120,000 as of December 31, 2016 and 2015, respectively.

(i) Inventories

Inventories consist of pharmaceuticals and are stated at the lower of weighted average cost or market.

(j) Long-Term Investments – Other

Long-term investments – other consists of equity and cost method investments.

(k) Fair Value Measurement for Alternative Investments

The Group may elect to measure the fair value of alternative instruments using the net asset value (NAV) or its equivalent as a practical expedient if there is no readily determinable fair value. No further adjustment is made unless it is probable that the investment fund will be sold at a value significantly less than NAV. The election will occur at inception and on an instrument-by-instrument basis.

(l) Charitable Gift Annuities

As of December 31, 2016 and 2015, the Foundation had a charitable gift annuities liability of $773,000 and $1,211,000, respectively, which is recorded as a component of other noncurrent liabilities in the accompanying consolidated balance sheets. Investments held for the charitable gift annuities are $1,684,000 and $1,751,000 as of December 31, 2016 and 2015, respectively, and are recorded as a component of noncurrent other assets in the accompanying consolidated balance sheets.

(m) Land, Buildings, and Equipment

In accounting for its long-lived assets, the Group makes estimates about the expected useful lives of the assets, the expected residual values of the assets, and the potential for impairment based on the fair value of the assets and the cash flows they generate. Factors indicating potential impairment include, but are not limited to, significant decreases in the market value of the long-lived assets, a significant change in the long-lived assets' condition, and operating cash flow losses associated with the use of the long-lived assets.

There is inherent risk in estimating the future cash flows used in the impairment test. If cash flows do not materialize as estimated, there is a risk the impairment charges recognized to date may be inaccurate, or further impairment charges may be necessary in the future.

Land, buildings, and equipment are recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets or, for leasehold improvements, over the term of the related lease, whichever is shorter. When assets are sold or retired, their cost and related accumulated depreciation are removed from the accounts and any related gain or loss is reflected in operations. The estimated useful lives of buildings, improvements, and leasehold improvements are 5 to 40 years, and the estimated useful life of equipment is 2 to 20 years.

(n) Construction in Progress (CIP)

CIP projects include costs incurred while preparing assets for their intended use. CIP projects consist of major computer system installations, the construction or remodel of buildings, or the installation of major equipment. The Group capitalizes interest costs on borrowings incurred during construction or development of qualifying assets. Capitalized interest is added to the cost of the underlying assets during construction and is depreciated or amortized over the useful lives of the assets.

(o) Notes Receivable

Notes receivable relate to long-term financing arrangements that exceed one year and bear interest at a market rate based on negotiated terms and are recorded at face value. Interest is recognized over the life of the note. The Group requires collateral for notes for real estate transactions. The Group does not intend to sell these receivables. Amounts collected on notes receivable are included in net cash provided by operating activities in the consolidated statements of cash flows. Notes receivable balance was $14,008,000 and $22,596,000 at December 31, 2016 and 2015, respectively, and is a component of noncurrent other assets. At December 31, 2016, future annual payments on notes receivable due within one year is zero and due in full by March 2020 is $14,008,000.

(p) Current Other Assets and Noncurrent Other Assets

Current other assets and noncurrent other assets consist of interest receivable, note receivable, interest rate swap, deposits, prepaid assets, insurance recovery receivable, deferred tax assets, and federal tax receivable.

(q) Self-Insurance

The Group is self-insured for industrial accident claims and GHC is self-insured for professional liability claims and unemployment benefits. GHC purchases excess insurance coverage to limit its exposure for professional liability claims and industrial accident claims and maintains excess insurance on a claims-made basis. Retention levels for professional liability are $7,000,000 per claim with annual aggregates of $22,000,000 in 2016 and 2015. Retention levels for industrial accident claims are $750,000 per claim in 2016 and 2015. Professional liability and industrial accident claims liability are determined using case-based estimates for reported claims and actuarial estimates for incurred but not reported claims. These estimates are based on historical information along with certain assumptions about future events. Changes in assumptions related to expected claims development as well as changes in actual experience could cause these estimates to change. At December 31, 2016 and 2015, the estimated liability for professional liability claims was $47,547,000 and $46,730,000, respectively. At December 31, 2016 and 2015, the estimated liability for industrial accident claims was $7,292,000 and $7,014,000, respectively. At December 31, 2016 and 2015, the estimated liability for unemployment claims was $3,177,000 and $3,847,000, respectively. Insurance recovery receivables for 2016 and 2015 are $1,946,000 and $2,049,000, respectively, and are a component of noncurrent other assets. GHC is a subscriber of and purchases its professional liability excess insurance coverage from a Risk Retention Group (RRG). As a subscriber of the RRG, GHC is also an owner granting it rights to its subscriber’s equity in the RRG. GHC’s portion of the RRG’s subscriber equity was $17,588,000 and $22,036,000 as of December 31, 2016 and 2015, respectively, and is included as a component of long-term investments – other.

(r) Revenues

Revenues are derived principally from health care premiums and clinical service billings. Premiums received in advance of the coverage period are deferred, and revenues are recognized in the period in which services are covered. Group contracts cover employee groups and are entered into with employers or union trusts. Clinical service revenues are generated through the provision of certain medical and pharmacy services not fully covered under existing benefit policies and from services provided to nonenrollees who receive care at the Group’s facilities.

GHC participates in the Medicare Advantage program and offers both Medicare Advantage (MA) and Medicare Advantage Prescription Drug (MA-PD) plans. MA plans offer Part C Medicare benefits to members and GHC receives capitated revenue from the Centers for Medicare and Medicaid Services (CMS), as well as supplemental premiums from the member. MA-PD plans offer Part C and Part D Medicare benefits to members and GHC receives capitated revenue from CMS, as well as supplemental premiums from the member. The capitated revenue from CMS for Part C and Part D is based on a risk adjustment model, where the demographic and health status (i.e., risk score) of the member is a factor used in determining payment. The other major factors of the capitated payment are the member’s county of residence and the plan/product in which the member is enrolled. Capitated payments from CMS are received monthly and are prospective. Adjustments for enrollment and certain member status updates are made to the payments retrospectively. Various accruals related to Part C and Part D revenue as a result of the risk-sharing arrangement, as well as federal reinsurance, and low-income cost-sharing subsidies are recognized as well. Retrospective settlements of payment are made after the end of the calendar year.

The table below presents the balances of the significant operating revenue types for the years ended December 31 (in thousands):

		2016	2015
Premiums:			
Group	$	2,117,463	2,081,551
Medicare		1,024,981	955,535
Individual and family		223,612	185,366
Total premiums		3,366,056	3,222,452
Clinical services revenue, net of contractual allowances and discounts		371,528	335,057
Less provision for bad debt		(9,783)	(9,626)
Clinical services – net		361,745	325,431
Other revenue:			
Grants		53,094	47,671
Self-funded administrative service fees		33,014	28,581
Other		19,744	17,786
Sales		16,203	15,682
Total other		122,055	109,720
Total operating revenues	$	3,849,856	3,657,603

The Group has agreements with third-party payors that provide for payments of amounts different from established charges. The Group's clinical services revenue, net of contractual allowances and discounts, came from the following major payor sources:

	2016	2015
Commercial	64 %	57 %
Private	32	38
Medicare	3	4
Medicaid	1	1
Total	100 %	100 %

There is a corresponding significant concentration of credit risk in net accounts receivable balances at December 31:

	2016	2015
Commercial	58 %	52 %
Private	38	44
Medicare	3	3
Medicaid	1	1
Total	100 %	100 %

Commercial represents receivables from other insurance companies. The private accounts receivable represents noncovered health care services, copays, and deductibles from enrollees as well as nonenrollees receiving fee-for-service clinical services.

The Group has entered into payment agreements with certain commercial insurance carriers including employer groups under self-funded plans. The basis for payment to the Group under these agreements includes prospectively determined rates per unit of service and discounts from established charges. Most arrangements provide for payment or reimbursement to the Group at amounts different from established rates. Contractual discounts represent the difference between established rates for services and amounts paid or reimbursed by these third-party payors.

The Group has estimated payments for services rendered to Medicare and Medicaid fee-for-service patients during the year by applying the payment principles of the applicable governmental agencies and believes that an adequate provision has been made in the accompanying consolidated financial statements for final settlement.

Most outpatient services provided to Medicare patients are reimbursed based on prospectively determined rates. Medicaid patients are also reimbursed based on a combination of prospectively determined rates and cost reimbursement methodology. Continuation of these reimbursement programs at the present level, and on the present basis, is dependent upon future policies of the federal and state governmental agencies.

Other revenue includes grants awarded to the Group Health Research Institute, a division of GHC, optical sales, and self-funded administrative service fees. Also included in other revenue are unconditional promises to donate cash and other assets to the Foundation, which are reported at fair value at the date the promise is received. The Foundation reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the time and purpose of the donated assets. When a donor restriction expires (when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets.

(s) Premium Deficiency Reserves

A premium deficiency reserve is recognized when the expected future claims payments and administrative costs of a grouping of existing contracts exceed the premiums to be collected for the remainder of a contract period. Deficiencies in one grouping of contracts are not offset by anticipated surpluses in other groupings. The Group considers anticipated investment income in determining if a premium deficiency exists. Reserves are regularly reviewed and adjusted as experience develops or new information becomes known. Such adjustments would be included in current operations. No reserve was considered necessary at December 31, 2016 and 2015.

(t) Charity Care

Charity care represents medically necessary hospital-based care to patients who have demonstrated an inability to pay and receive care at a Group facility. Patients must have income at or less than 200% of the Federal Poverty Level. Only the portion of a patient's account that meets the Group's criteria is recognized as charity care. The method to estimate costs associated with charity care involves a ratio of gross charges. The cost of charity care was estimated at $482,000 and $398,000 for the years ended December 31, 2016 and 2015, respectively.

(u) External Delivery Services

External delivery services represent health care expenses incurred by the Group for care provided to their respective members by contracted and noncontracted health care facilities and practitioners, other than Group Health Physicians (note 2v). The liability reflected on the consolidated balance sheets is determined using actuarial estimates. These estimates are based on historical information along with certain assumptions about future events. Changes in assumptions related to expected claims development as well as changes in actual experience could cause these estimates to change.

(v) Group Health Physicians (GHP) Expense

Group Health Permanente P.C., doing business as Group Health Physicians, is an independent medical group with an exclusive contract to provide medical services that includes primary, specialty, and inpatient care. The Group's net liability to GHP was $93,811,000 and $36,924,000 as of December 31, 2016 and 2015, respectively, which is a component of accounts payable and accrued expenses in the accompanying consolidated balance sheets.

(w) Advertising

Advertising costs are expensed as incurred and are recorded within services purchased in the consolidated statements of operations and changes in net assets. The Group recorded advertising expense of $2,860,000 and $5,435,000 for the years ended December 31, 2016 and 2015, respectively.

(x) Leases

Rent revenue and expense is recorded on a straight-line basis over the term of the respective leases. Lease incentives are amortized ratably over the lease term (note 11a).

The Group was obligated under capital leases covering certain equipment that expired in 2016. Amortization of assets held under capital leases is included with depreciation.

(y) Income Taxes

GHO is subject to federal income taxes and is not subject to any state income tax filing requirements. GHC is exempt from federal income taxes under Section 501(a) of the Internal Revenue Code (the Code) as a charitable organization under Section 501(c)(3) of the Code, except for unrelated

(Continued)

business income tax. The Foundation has received a determination letter from the Internal Revenue Service (IRS) that it is a tax-exempt public foundation in accordance with Section 501(c)(3) and a public charity in accordance with Section 170(b)(1)(A)(vi) of the Code. CMA is considered a disregarded entity for federal tax purposes and would be included with any GHC federal income tax filing.

Deferred income taxes are recognized for the tax consequences in future years of the differences between the tax basis of assets and liabilities and the financial reporting amounts at each year end based on enacted tax laws and statutory tax rates applicable to the periods in which the differences are expected to reverse. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities (including the impact of available carryback and carryforward periods), projected future taxable income, and tax planning strategies in making this assessment. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized. Interest and penalties, if any, are recognized as other expense in the period in which the interest would be accruing according to tax law or in the period the tax position is initially taken.

(z) Net Assets

Changes in unrestricted net assets result from the excess (deficit) of revenues over expenses and the changes in net unrealized investment gains (losses) as well as pension and other postretirement plan changes. Temporarily and permanently restricted net assets are accounted for within the Foundation. Temporarily restricted net assets account for funds restricted by donors for specific time and purposes, unappropriated earnings on permanent endowments, and are available to support the Foundation in carrying out its mission.

Temporarily restricted net assets are available for the following purposes as of December 31 (in thousands):

		2016	2015
Health care services	$	4,058	4,076
Health care education		1,798	1,574
Health care research and development		480	515
Time restricted		57	53
Total temporarily restricted net assets	$	6,393	6,218

When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets. Permanently restricted net assets as of December 31, 2016 and 2015 are contributions restricted by the donor to be invested in perpetuity.

The change in temporarily restricted net assets was comprised of $1,307,000 and $1,160,000 of contributions, $(2,271,000) and $(1,629,000) of release from restrictions, and investment income (loss) of $1,138,000 and $(521,000), for the years ended December 31, 2016 and 2015, respectively.

(aa) Accounting Changes

In May 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2015-07, *Fair Value Measurement (Topic 820) Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent)*. ASU 2015-07 eliminates the requirement to categorize investments valued using the net asset value per share expedient from the fair value (FV) hierarchy of financial instruments. This standard was effective for the Group's 2016 consolidated financial statements. The adoption of this standard did not have a material impact on the Group's consolidated financial statements.

(3) Marketable Securities

Marketable securities as of December 31, 2016 and 2015 consist of the following (in thousands):

	2016			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Total fair value
Debt securities:				
U.S. government	$ 106,728	191	(3,567)	103,352
U.S. government agency	19,634	194	(114)	19,714
Municipal debt	41,152	1,072	(278)	41,946
International government	3,967	50	(39)	3,978
Corporate debt	380,703	4,686	(2,859)	382,530
Mortgage-backed	193,422	996	(3,081)	191,337
Asset-backed	54,330	299	(261)	54,368
Collateralized mortgage obligations	9,985	288	(30)	10,243
Domestic equity securities:				
Mutual funds:				
Large blend	20,501	9,625	(272)	29,854
Large value	13,927	1,390	(604)	14,713
Large growth	2,400	1,219	(22)	3,597
Small value	22,556	5,959	—	28,515
Small growth	5,544	880	—	6,424
Intermediate term	3,469	32	(63)	3,438
Short term	2,245	—	(31)	2,214
Emerging market bond fund	50,000	98	—	50,098
Other	2,139	2	(706)	1,435

	2016			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Total fair value
Common stock:				
Communications	$ 6,726	857	(258)	7,325
Consumer	30,956	4,552	(1,266)	34,242
Energy	6,003	539	(30)	6,512
Financial	19,177	4,740	(404)	23,513
Industrial	10,597	2,646	(96)	13,147
Technology	9,985	3,053	(42)	12,996
Utilities	4,366	735	(226)	4,875
Other	3,068	830	(111)	3,787
Total	$ 1,023,580	44,933	(14,360)	1,054,153

	2015			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Total fair value
Debt securities:				
U.S. government	$ 72,156	194	(876)	71,474
U.S. government agency	39,180	493	(35)	39,638
Municipal debt	53,538	1,465	(181)	54,822
International government	7,706	75	(14)	7,767
Corporate debt	412,860	3,032	(7,513)	408,379
Mortgage-backed	161,104	1,417	(1,221)	161,300
Asset-backed	29,933	158	(292)	29,799
Collateralized mortgage obligations	8,998	70	(94)	8,974
Domestic equity securities:				
Mutual funds:				
Large blend	69,591	27,661	(337)	96,915
Large value	10,570	3,423	(870)	13,123
Large growth	2,344	1,206	(20)	3,530
Small value	37,726	3,927	(1,417)	40,236
Small growth	6,367	278	(892)	5,753
Intermediate term	53,358	6	(4,229)	49,135
Short term	1,917	—	(21)	1,896
Other	2,107	—	(787)	1,320

	2015			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Total fair value
Common stock:				
Communications	$ 6,335	501	(748)	6,088
Consumer	30,918	4,022	(1,566)	33,374
Energy	6,033	89	(1,003)	5,119
Financial	19,231	2,271	(1,414)	20,088
Industrial	9,115	1,958	(425)	10,648
Technology	10,514	1,366	(544)	11,336
Utilities	5,181	488	(281)	5,388
Other	2,873	329	(233)	2,969
Total	$ 1,059,655	54,429	(25,013)	1,089,071

Contractual maturities of debt securities held as of December 31, 2016 include the following (in thousands):

	Fair value				
	Within 1 year	After 1 year through 5 years	After 5 years through 10 years	After 10 years	Total fair value
Debt securities:					
U.S. government	$ 9,012	29,752	48,886	15,702	103,352
U.S. government agency	4,002	11,944	3,768	—	19,714
Municipal debt	1,218	11,744	10,779	18,205	41,946
International government	—	2,028	1,950	—	3,978
Corporate debt	38,229	221,880	100,078	22,343	382,530
Mortgage-backed	6	1,920	12,904	176,507	191,337
Asset-backed	—	12,954	30,267	11,147	54,368
Collateralized mortgage obligations	46	381	1,000	8,816	10,243
Total	$ 52,513	292,603	209,632	252,720	807,468

Securities not due at a single maturity date are reflected in the table above by its final maturity date.

The Group records investment income net of related expenses and consists of the following as of December 31 (in thousands):

		2016	2015
Interest	$	29,275	28,602
Realized gains on sale		35,654	14,996
Realized losses on sale		(2,544)	(2,330)
Dividends and capital gain		8,961	11,271
Amortization, accretion, and other		(4,462)	(5,942)
OTTI		(6,293)	(4,018)
Total investment income	$	60,591	42,579

The following tables show the fair value and gross unrealized losses of the Group's marketable securities with unrealized losses. These securities are aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2016 and 2015 (in thousands):

		Less than 12 months		12 months or greater		Total	
2016		Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Debt securities:							
U.S. government	$	81,678	(3,567)	—	—	81,678	(3,567)
U.S. government agency		5,540	(114)	—	—	5,540	(114)
Municipal debt		12,515	(246)	521	(32)	13,036	(278)
International government		948	(39)	—	—	948	(39)
Corporate debt		157,035	(2,272)	14,884	(587)	171,919	(2,859)
Mortgage-backed		132,595	(2,760)	7,576	(321)	140,171	(3,081)
Asset-backed		21,080	(233)	1,766	(28)	22,846	(261)
Collateralized mortgage obligations		805	(4)	1,005	(26)	1,810	(30)
Domestic equity securities:							
Mutual funds:							
Large blend		71	—	923	(272)	994	(272)
Large value		206	(3)	1,742	(601)	1,948	(604)
Large growth		131	(4)	137	(18)	268	(22)
Intermediate term		2,128	(63)	2	—	2,130	(63)
Short term		2,007	(27)	204	(4)	2,211	(31)
Other		723	(8)	659	(698)	1,382	(706)

2016	Less than 12 months Fair value	Less than 12 months Unrealized losses	12 months or greater Fair value	12 months or greater Unrealized losses	Total Fair value	Total Unrealized losses
Common stock:						
Communications	$ 1,430	(169)	308	(89)	1,738	(258)
Consumer	9,438	(1,010)	1,146	(256)	10,584	(1,266)
Energy	50	(5)	327	(25)	377	(30)
Financial	2,872	(271)	1,288	(133)	4,160	(404)
Industrial	967	(79)	186	(17)	1,153	(96)
Technology	346	(14)	273	(28)	619	(42)
Utilities	1,652	(203)	89	(23)	1,741	(226)
Other	278	(108)	27	(3)	305	(111)
Total	$ 434,495	(11,199)	33,063	(3,161)	467,558	(14,360)

2015	Less than 12 months Fair value	Less than 12 months Unrealized losses	12 months or greater Fair value	12 months or greater Unrealized losses	Total Fair value	Total Unrealized losses
Debt securities:						
U.S. government	$ 52,446	(876)	—	—	52,446	(876)
U.S. government agency	8,298	(35)	—	—	8,298	(35)
Municipal debt	6,592	(164)	541	(17)	7,133	(181)
International government	2,529	(14)	—	—	2,529	(14)
Corporate debt	229,201	(5,704)	14,083	(1,809)	243,284	(7,513)
Mortgage-backed	77,236	(742)	13,703	(479)	90,939	(1,221)
Asset-backed	19,510	(256)	1,668	(36)	21,178	(292)
Collateralized mortgage obligations	2,426	(15)	2,411	(79)	4,837	(94)
Domestic equity securities:						
Mutual funds:						
Large blend	416	(48)	784	(289)	1,200	(337)
Large value	337	(86)	1,252	(784)	1,589	(870)
Large growth	320	(20)	—	—	320	(20)
Small value	23,661	(1,417)	—	—	23,661	(1,417)
Small growth	—	—	2,109	(892)	2,109	(892)
Intermediate term	48,036	(4,229)	—	—	48,036	(4,229)
Short term	1,648	(16)	246	(5)	1,894	(21)
Other	751	(20)	568	(767)	1,319	(787)
Common stock:						
Communications	3,062	(747)	1	(1)	3,063	(748)
Consumer	11,580	(1,482)	285	(84)	11,865	(1,566)
Energy	4,008	(772)	509	(231)	4,517	(1,003)
Financial	8,009	(1,376)	106	(38)	8,115	(1,414)
Industrial	2,764	(298)	393	(127)	3,157	(425)
Technology	3,190	(468)	169	(76)	3,359	(544)
Utilities	1,564	(126)	494	(155)	2,058	(281)
Other	1,213	(175)	201	(58)	1,414	(233)
Total	$ 508,797	(19,086)	39,523	(5,927)	548,320	(25,013)

The unrealized losses in the Group's marketable securities in 2016 were due primarily to changes in interest rates and, in the case of equities, market price movements. The majority of debt security positions are investment grade and rated high quality, AA, or higher by Standard & Poor's rating agency. Securities with contractual payments are current and no payments were missed in 2016. For investments other than those determined to be other-than–temporarily impaired, the Group has the ability and intent to hold these investments until a recovery of fair value, which may be maturity, and considers these investments to be temporarily impaired.

(4) External Delivery Services Payable

Activity in the external delivery services payable for unpaid claims and claim adjustment expenses is summarized as follows (in thousands):

		2016	2015
Balances at January 1	$	253,605	228,920
Incurred related to:			
Current year		2,006,281	1,891,047
Prior years		(3,394)	(14,535)
Total incurred		2,002,887	1,876,512
Paid related to:			
Current year		1,789,384	1,653,374
Prior years		212,736	198,453
Total paid		2,002,120	1,851,827
Balances at December 31	$	254,372	253,605

Amounts incurred related to prior years vary from previously estimated liabilities as the claims are ultimately adjudicated and paid. Liabilities at any year end are continually reviewed and re-estimated as information regarding actual claims payments becomes known. This information is compared to the originally established year end liability. Amounts reported for incurred related to prior years result from claims being adjudicated and paid for amounts different from originally estimated.

(5) Medical Loss Ratio (MLR)

Effective January 1, 2011, as part of the Patient Protection and Affordable Care Act (Health Care Reform), minimum medical loss ratios were mandated for all commercial fully insured medical plans with annual rebates owed to policyholders if the actual loss ratios, calculated in a manner prescribed by the U.S. Department of Health and Human Services (HHS), fall below certain targets (85% for large employer groups and 80% for small employer groups and individuals). In the 2014 contract year, MA and MA-PD became subject to MLR requirements similar to the commercial fully insured medical plans. The target medical loss ratios for the Medicare plans is 85%. HHS issued guidance specifying the types of costs that should be included in benefit expense for purposes of calculating medical loss ratios. The Group’s medical loss ratios were above the minimum target levels and no liability for rebates was recorded in 2016 and 2015.

(6) Borrowing Arrangements

GHC has a commercial paper financing program under which notes may be issued from time to time up to the aggregate face amount of $75,000,000. The notes may be sold at a discount from the par amount to reflect an interest component to the maturity date. The maturity date of the notes will be 1 to 270 days and

(Continued)

the notes are not subject to redemption prior to the maturity date. The notes are secured by GHC's gross receivables, certain equipment, and a lien on certain real property.

Revenue bonds were issued through the Washington Health Care Facilities Authority (the Authority). As security for the repayment of the bonds, GHC granted the Authority a security interest in its gross receivables, bond funds, and liens against certain facilities and equipment. The loan agreements for the revenue bonds required, among other restrictions, that GHC achieve certain minimum debt service coverage ratios. The 2006 revenue bond series was redeemed December 1, 2016.

In 2014, GHC entered into a bank loan agreement for $30,085,000 with an interest rate of London Interbank Offered Rate (LIBOR) plus 0.80. The account is a component of restricted assets for 2015 only. The bank loan was paid in full in 2016 and the cash collateral account was closed.

Long-term debt at December 31 consists of the following (in thousands):

	Year(s) of maturity	2016	2015
Revenue bonds:			
Series 2006, 4 – 1/2% to 5%, plus bond premium of $1,263 in 2015.	2022–2036	$ —	99,227
Bank Loan, LIBOR plus 0.80%.	2019	—	23,674
Subtotal		—	122,901
Less current portion		—	(6,003)
Total long-term debt		$ —	116,898

Interest paid during 2016 and 2015 was $3,798,000 and $2,009,000, respectively. Interest expense was $10,963,000 and $3,652,000 during 2016 and 2015, respectively, and the amount of interest capitalized was $10,000 and $106,000 in 2016 and 2015, respectively. The effect of the interest rate swap increased interest expense by $2,850,000 in 2016 and decreased interest expense by $1,966,000 in 2015.

(7) Derivative Financial Instruments

GHC is exposed to the effects of changing interest rates. This exposure is managed, in part, with the use of derivatives. In January 2007, GHC entered into an interest rate swap with Citigroup on the 2006 Series bonds as part of the effort to rebalance the mix of variable and fixed rate exposure. The swap entitles GHC to receive payments based on a fixed rate and pay a variable rate based on the Securities Industry and Financial Markets Association Municipal Swap Index. The terms include a provision to cap the market value of the swap at $22,500,000, and a par termination option with a term to match the call provision of the 2006 Series bonds. GHC elected to account for the swap as a free standing derivative; therefore, changes in the fair value are recorded in interest expense. The notional amount of this derivative is $75,000,000. The swap was called by the Citigroup in 2016.

(8) Disclosure about Fair Value of Financial Instruments

Assets and liabilities that are recorded at fair value are required to be grouped in three levels, based on the markets in which the assets and liabilities are traded and the observability of the inputs used to determine fair value. The three levels are:

- Level 1 – Valuation is based upon quoted prices for identical instruments traded in active markets.
- Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and a model-based valuation approach for which all significant assumptions are observable in the market.
- Level 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Group's estimates of assumptions that market participants would use in pricing the asset or liability. Valuation approach includes use of discounted cash flow models and similar approaches, which included unobservable inputs of discount factor, forward rate, and credit risk of counterparty and GHC.

Fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Group maximizes the use of observable inputs and minimizes the use of unobservable inputs when developing fair value measurements. Fair value measurements for assets and liabilities where there is limited or no observable market data and, therefore, are based primarily upon estimates calculated by the Group, are based on the economic and competitive environment, the characteristics of the asset or liability, and other factors. Therefore, the results cannot be determined with precision and may not be realized upon an actual settlement of the asset or liability. There may be inherent weaknesses in any calculation approach, and changes in the underlying assumptions used, including discount rates and estimates of future cash flows, that could significantly affect the results of the current or future values.

Following is a description of valuation methods and assumptions used for assets and liabilities recorded at fair value and for estimating fair value for financial instruments not recorded at fair value but required to be disclosed:

(a) Assets and Liabilities

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, accounts receivable – net, accounts payable, external delivery services payable, accrued employee compensation, and accrued taxes and interest approximate fair value.

(b) Notes Receivable

Long-term notes receivable are carried at face value; however, accounting standards require the Group to disclose the fair value. The fair value of the Group's long-term notes receivable is determined as the present value of future contractual cash flows discounted at an interest rate that reflects the risk inherent in those cash flows. The discount rate is 5% and approximates rates currently observed in publicly traded debt markets for debt of similar terms with companies with comparable credit risk. The fair value of the long-term notes receivable was $11,979,000 and $16,862,000 as of December 31, 2016 and 2015, respectively.

(c) Long-Term Debt

Long-term debt is carried at amortized cost; however, accounting standards require the Group to disclose the fair value. The fair value of the Group's revenue bonds is based on quoted market prices in markets that are not active, which are Level 2 inputs. The fair value of the revenue bonds was $100,724,000 as of December 31, 2015. The bonds were redeemed in 2016.

The fair value of the Group's bank loan is determined as the present value of future contractual cash flows discounted at an interest rate that reflects the risk inherent in those cash flows. This discount rate was 1.2275% at December 31, 2015 and approximates rates observed in publicly traded debt markets for debt of similar terms. The fair value of the bank loan was $22,295,000 as of December 31 2015. The loan was paid in full in 2016.

(d) Marketable Securities, Restricted Assets, Commingled Securities Trust, and Interest Rate Swap

The table below presents the balances of assets and liabilities measured at fair value on a recurring basis as of December 31, 2016 and 2015 (in thousands):

	Fair value at December 31, 2016	Fair value measurements at December 31, 2016 using	
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)
Marketable securities:			
Debt securities:			
U.S. government	$ 103,352	103,352	—
U.S. government agency	19,714	—	19,714
Municipal debt	41,946	—	41,946
International government	3,978	—	3,978
Corporate debt	382,530	—	382,530
Mortgage-backed	191,337	—	191,337
Asset-backed	54,368	—	54,368
Collateralized mortgage obligations	10,243	—	10,243
Domestic equity securities:			
Mutual funds:			
Large blend	29,854	29,854	—
Large value	14,713	14,713	—
Large growth	3,597	3,597	—
Small value	28,515	28,515	—
Small growth	6,424	6,424	—
Intermediate term	3,438	3,438	—
Short term	2,214	2,214	—
Emerging market bond fund	50,098	50,098	—
Other	1,435	1,435	—

	Fair value at December 31, 2016	Fair value measurements at December 31, 2016 using: Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)
Common stock:			
Communications	$ 7,325	7,325	—
Consumer	34,242	34,242	—
Energy	6,512	6,512	—
Financial	23,513	23,513	—
Industrial	13,147	13,147	—
Technology	12,996	12,996	—
Utilities	4,875	4,875	—
Other	3,787	3,787	—
Total marketable securities	$ 1,054,153	350,037	704,116

	Fair value at December 31, 2015	Fair value measurements at December 31, 2015 using: Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Marketable securities:				
Debt securities:				
U.S. government	$ 71,474	71,474	—	—
U.S. government agency	39,638	—	39,638	—
Municipal debt	54,822	—	54,822	—
International government	7,767	—	7,767	—
Corporate debt	408,379	—	408,379	—
Mortgage-backed	161,300	—	161,300	—
Asset-backed	29,799	—	29,799	—
Collateralized mortgage obligations	8,974	—	8,974	—
Domestic equity securities:				
Mutual funds:				
Large blend	96,915	96,915	—	—
Large value	13,123	13,123	—	—
Large growth	3,530	3,530	—	—

		Fair value at December 31, 2015	Fair value measurements at December 31, 2015 using: Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Small value	$	40,236	40,236	—	—
Small growth		5,753	5,753	—	—
Intermediate term		49,135	49,135	—	—
Short term		1,896	1,896	—	—
Other		1,320	1,320	—	—
Common stock:				—	—
Communications		6,088	6,088	—	—
Consumer		33,374	33,374	—	—
Energy		5,119	5,119	—	—
Financial		20,088	20,088	—	—
Industrial		10,648	10,648	—	—
Technology		11,336	11,336	—	—
Utilities		5,388	5,388	—	—
Other		2,969	2,969	—	—
Total marketable securities	$	1,089,071	378,392	710,679	—
Restricted assets:					
Guaranteed investment contract	$	8,848	—	—	8,848
Other assets:					
Interest rate swap	$	5,388	—	—	5,388

(e) Net Asset Valuation

Investments recorded in long-term investments – other that are reported at net asset value as a practical expedient for fair value are presented by major category (in thousands):

		Fair value at December 31, 2016	Redemption frequency	Redemption notice period
a. Commingled securities trust	$	33,916	Daily	30 days
b. Real estate commingled trust		51,909	Quarterly	90 days
	$	85,825		

a. This category is comprised of a long-term strategy to maximize returns by investing in high yield bank loan fund. This investment is reported at NAV as a practical expedient with the fair value option elected.

b. This category is comprised of a long-term strategy to maximize returns by investing in a real estate trust. This investment is reported at NAV as a practical expedient with the fair value option elected. After GHC has been in the fund one full year, all shares acquired are permitted to be redeemed on a quarterly basis. As of December 31, 2016, GHC has not been in the fund a full year.

At December 31, 2016 there were no outstanding funding commitments.

(9) Defined Benefit Pension Plans

The Group sponsors two defined benefit plans (the DB Plans), a defined contribution plan (the DC Plan), two 401(k) plans, a 403(b) plan, and contributes to a union sponsored multiemployer trust defined benefit plan for certain employees. Collectively, these plans cover substantially all of its employees. The Group's policy is to fund pension costs for the DB Plans based on actuarially determined funding requirements, thereby accumulating funds adequate to provide for all accrued benefits. Contributions for the DC Plan are based on a percentage of covered employees' salaries according to the plan document. Matching contributions to the 401(k) and 403(b) plans are based on a percentage of participants' contributions as set forth in the plan document. The total expense for the DB Plans was $31,680,000 and $25,557,000 in 2016 and 2015, respectively, and the total expense for the other plans was $30,568,000 and $28,951,000 in 2016 and 2015, respectively.

GHC amended its defined benefit pension plan (the Plan), effective January 1, 2014, to freeze the accrued benefits of eligible employees whose terms of employment are not covered by a collective bargaining agreement (nonunion employees) and exclude nonunion employees from actively participating in the Plan. As a result of this amendment, effective January 1, 2014, these participants stopped accruing benefits under the Plan and will not earn additional benefits under the Plan based on hours of service earned or pay received after December 31, 2013. Participants were automatically enrolled in the DC Plan as of January 1, 2014 and earn contributions on pay received after January 1, 2014 subject to terms of the DC Plan.

The Plan was amended on December 10, 2015 to limit benefit accrual in the Plan to those union represented participants enrolled in the plan as of the following dates for the respective bargaining groups: United Food and Commercial Workers International Union (UFCW), January 29, 2016; Office and Professional Employees International Union (OPEIU), February 1, 2016; and Service Employees International Union (SEIU), February 9, 2016. With this action, the Plan has been closed to new entry.

In 2015, pursuant to the plan of reorganization, GHO became the sponsor of the Kitsap Physicians Service Employees' Retirement Plan, a qualified defined benefit pension plan. On January 15, 2009, this defined benefit pension plan was amended to curtail benefits effective March 1, 2009. As a result, each active participant's pension benefit was determined based on the participant's compensation and duration of employment as of March 1, 2009. Thus, no new benefits are being accrued after the date of the curtailment. The amended plan covers employees who had one year of service at the date of curtailment.

(Continued)

For the DB Plans, the actuarial cost method used in determining the net periodic pension cost is the projected unit credit cost method. At December 31, 2016 and 2015, net periodic pension expense related to the Group's participation in the DB Plans for 2016 and 2015 included the following components (in thousands):

		2016	2015
Service cost	$	15,824	18,037
Interest cost on projected benefits		35,202	32,522
Expected return on plan assets		(46,866)	(49,385)
Amortization of net loss		28,151	24,383
Amortization of prior service cost		(1,714)	—
Special termination benefit recognized		1,083	—
Net periodic benefit cost	$	31,680	25,557

	2016	2015
Discount rate (preretirement)	4.75%–4.80%	4.25%–4.30%
Rate of increase in compensation levels	3.00–4.50	3.00–4.50
Expected return on plan assets	5.25–8.00	5.25–8.00

The DB Plans' funded status and amounts included in unrestricted net assets to be recognized as a component of net periodic pension cost as of December 31, 2016 and 2015 are shown in the following table (in thousands):

		2016	2015
Change in projected benefit obligation:			
Projected benefit obligation at beginning of year	$	762,909	796,719
Service cost		15,824	18,037
Interest cost		35,202	32,522
Plan amendments		—	(14,069)
Actuarial loss (gain)		22,342	(25,073)
Expenses paid		(448)	—
Special termination benefits		1,083	—
Benefits paid		(37,119)	(45,227)
Projected benefit obligation at end of year		799,793	762,909

		2016	2015
Fair value of plan assets – beginning of year	$	577,287	606,076
Actual return on plan assets		55,292	(23,562)
Employer contributions		40,000	40,000
Expenses paid		(448)	—
Benefits paid		(37,119)	(45,227)
Fair value of plan assets – end of year		635,012	577,287
Funded status	$	(164,781)	(185,622)
Items recognized in unrestricted net assets:			
Prior service cost	$	(12,355)	(14,069)
Actuarial net loss		286,012	300,246
	$	273,657	286,177
Accumulated benefit obligation – end of year	$	776,526	739,824

The funded status is recorded as a component of noncurrent liabilities as of December 31, 2016 and 2015 in the consolidated balance sheets.

	2016	2015
Actuarial assumptions used were as follows:		
Discount rate	4.55%–4.60%	4.75%–4.80%
Rate of increase in compensation levels	3.00–4.50	3.00–4.50

Expected amounts to be recognized as components of 2017 net periodic pension cost are as follows (in thousands):

Service cost	$	17,629
Interest cost on projected benefits		35,186
Expected return on plan assets		(58,510)
Amortization of net loss		25,775
Amortization of prior service cost		(1,714)
Net periodic pension cost	$	18,366

The estimated net loss amount will be amortized from unrestricted net assets into net periodic benefit cost.

The benefits expected to be paid in each of the next five years, and in the aggregate for the five fiscal years thereafter, as of December 31, 2016 are as follows (in thousands):

Years ending December 31:		
2017	$	53,561
2018		56,130
2019		57,083
2020		58,575
2021		57,022
2022–2026		272,710
Total	$	555,081

The Group participates in a multiemployer defined benefit pension plan under the terms of collective-bargaining agreements that cover its union-represented employees. The risk of participating in this multiemployer plan is different from single-employer plans in the following aspects:

a. Assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of participating employers.

b. If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.

c. If the Group chooses to stop participating in its multiemployer plan, the Group may be required to pay these plans an amount based on the underfunded status of the plan referred to as a withdrawal of money.

The Group participates in the Sound Retirement Trust, formerly Retail Clerks Pension Trust (Federal Identification Number 91-6069306), which includes Pharmacy and Optical employees under the UFCW union. The collective bargaining agreement with Pharmacy employees expires October 31, 2020 and the Optical employees expires April 30, 2018. The most recent Pension Protection Act (PPA) status available is for the plan's year end of September 30, 2016. The status has been designated critical status. The status is based on information that the Group received from the plan and is certified by the plan's actuary. Among other factors, plans in critical status are generally less than 65% funded, plans in the endangered status are between 65% and 79% funded, and plans in the critical and declining status are projected to become insolvent within 15 years. The Plan has a financial improvement plan (FIP) or rehabilitation plan that has been implemented. The contributions to the plan were $1,280,000 and $1,079,000 for the years ended December 31, 2016 and 2015, respectively. The Group's contributions represent less than 5% of total contributions to the plan. The Group paid rehabilitation surcharges in 2016 and 2015.

(a) Investment Policies and Strategies

The Group has adopted investment policies for its DB plans that incorporate a strategic, long-term asset allocation mix designed to best meet its long-term pension obligations. Plan fiduciaries set the investment policies and strategies for the pension trust. This includes the following:

- Selecting investment managers

- Setting long-term and short-term target asset allocations
- Periodic review of the target asset allocations, and, if necessary, to make adjustments based on changing economic and market conditions
- Monitoring the actual asset allocations, and, when necessary, rebalancing to the current target allocation

As of December 31, 2016 and 2015, the following table summarizes the target allocation range defined in the investment policies compared to the actual allocations of the Group's plan assets:

	2016		2015	
	Target allocation	Actual allocation	Target allocation	Actual allocation
Equity securities	32%–67%	46 %	32%–67%	45 %
Debt securities	14–41	31	14–41	37
Cash equivalents	0–5	—	0–5	—
Other investments	4–44	23	4–44	18

The investment policy emphasizes the following key objectives:

- Maintain a diversified portfolio among various asset classes and investment managers
- Invest in a prudent manner for the exclusive benefit of plan participants
- Preserve the funded status of the plan
- Balance between acceptable level of risk and maximizing returns
- Maintain adequate control over administrative costs
- Maintain adequate liquidity to meet expected benefit payments

(b) Expected Long-Term Rate of Return on Assets

The Group uses a "building block" approach to determine the expected rate of return on plan assets assumption for the DB plans. This approach analyzes historical long-term rates of return for various investment categories, as measured by appropriate indices. The rates of return on these indices are then weighted based upon the percentage of plan assets in each applicable category to determine a composite expected return. The Group reviews its expected rate of return assumption annually. However, this is considered to be a long-term assumption and hence not anticipated to change annually, unless there are significant changes in economic and market conditions.

Employer contributions made to the plan in 2017 were $143,000,000.

(c) Fair Value of Defined Benefit Pension Assets

The Group’s pension assets are reported at fair value and are required to be grouped in three levels, based on the markets in which they are traded and the observability of the inputs used to determine fair value. The three levels are:

- Level 1 – Valuation is based upon quoted prices for identical instruments traded in active markets.
- Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation approach for which all significant assumptions are observable in the market.
- Level 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Group’s estimates of assumptions that market participants would use in pricing the asset. Valuation approach includes use of discounted cash flow models and similar approaches.

The table below presents the balances of plan assets measured at fair value on a recurring basis as of December 31, 2016 and 2015 (in thousands):

		Fair value measurements at December 31, 2016 using
	Fair value at December 31, 2016	**Quoted prices in active markets for identical assets (Level 1)**
Plan assets:		
Cash and cash equivalents	$ 9,044	9,044
Commingled funds	103,771	103,771
Common stocks	137,900	137,900
Limited partnership	5,692	5,692
Mutual funds:		
Domestic equities:		
Large blend	2,689	2,689
Long term bond	21,623	21,623
Intermediate term bond	30,701	30,701
Foreign equities:		
Large blend	1,267	1,267
	312,687	312,687
Investments measured at net asset value	322,325	
Total plan assets	$ 635,012	

		Fair value at December 31, 2015	Fair value measurements at December 31, 2015 using — Quoted prices in active markets for identical assets (Level 1)
Plan assets:			
Cash and cash equivalents	$	5,537	5,537
Commingled funds		102,581	102,581
Common stocks		129,666	129,666
Limited partnership		5,362	5,362
Mutual funds:			
Domestic equities:			
Large blend		2,528	2,528
Long term bond		21,422	21,422
Intermediate term bond		29,660	29,660
Foreign equities:			
Large blend		1,062	1,062
Total plan assets		297,818	297,818
Investments measured at net asset value		279,469	
Total plan assets	$	577,287	

(d) Defined Benefit Pension Net Asset Valuation

Alternative investments held in the DB Plans that are reported at net asset value as a practical expedient for fair value are presented by major category (in thousands):

		Fair value at December 31, 2016	Redemption frequency	Redemption notice period
Commingled trust (a)	$	53,719	Monthly	1–10 days
Limited partnership (b)		139,780	Monthly, Quarterly	1–30 days
Private equity (c)		119,781	—	—
Trust index fund (d)		9,045	Monthly	10 days
Total	$	322,325		

(Continued)

a. This category is comprised of two different fund strategies: 1) An index fund that invests in non-U.S. global equities; and 2) An actively managed fund that invests in emerging market local and U.S. dollar debt employing a long-term strategy focused on income and capital appreciation.

b. This category is comprised of five fund strategies: 1) An index fund that invests in Russell 3000 equities that meet a defined criteria related to quality, stability, and income; 2) Two actively managed funds that invest in noninvestment grade bonds employing a long-term strategy focused on income and capital appreciation; 3) An actively managed fund that invests in non-U.S. developed market equities (Europe, Australia, Asia and Far East) employing a long-term value approach to stock selection; 4) An actively managed fund that invests in frontier market equities employing strategies that take advantage of mispriced high quality stocks for long-term capital appreciation; and 5) An actively managed fund that invests in secured loans and other debt instruments of below investment grade companies.

c. Private equity investments include both U.S. and foreign investments with strategies that can include debt, venture capital, buyout, real estate, natural resources, and infrastructure. Fair values have been estimated by using either the net asset value per share or the net asset value of the Group’s ownership interest in the partners’ capital. These funds do not allow the Group to submit redemption requests. Distributions from these funds will be received as the underlying investments are liquidated. Based on the expiration dates of the funds, it is estimated that the underlying assets will be liquidated over the next 3 to 10 years.

d. This category is comprised of an index fund that invests in commodity futures.

At December 31, 2016 and 2015 the private equity investments have outstanding funding commitments totaling $94,155,000 and $95,949,000, respectively.

(10) Retiree Medical Plan

GHC provides certain medical benefits for eligible retired employees. Employees became eligible for these benefits upon retirement, attainment of a specified age, and upon completion of a certain number of years of service.

In 2009, GHC completed the curtailment of this benefit. The contribution to the premiums for collective bargaining active employees was discontinued. This resulted in the final phase out of the benefit. In 2008, the phase out of the benefit occurred for the nonunion active employees.

At December 31, 2016 and 2015, net periodic postretirement benefit cost is comprised of interest costs on accumulated benefit obligation of $1,884,000 and $2,826,000, respectively.

Amounts recognized in unrestricted net assets consisted of net actuarial losses of $5,995,000 and $11,472,000 at December 31, 2016 and 2015, respectively.

GHC's accumulated postretirement benefit obligation (APBO) is unfunded. The APBO is included in the components of the retiree medical benefits liability on the consolidated balance sheets at December 31, and comprises the following components (in thousands):

		2016	2015
Change in accumulated postretirement benefit obligation:			
Accumulated postretirement benefit obligation – beginning of year	$	44,913	51,875
Interest cost		1,678	1,926
Actuarial loss		(5,270)	(4,449)
Benefits paid		(3,963)	(4,439)
Accumulated postretirement benefit obligation – end of year	$	37,358	44,913
Change in plan assets:			
Employer contributions	$	3,963	4,439
Benefits paid		(3,963)	(4,439)

Future benefit costs were estimated assuming medical costs would increase at a 7.30% annual rate. A 1% increase in this annual trend rate would have increased the APBO at December 31, 2016, by $1,812,000 and the sum of service cost and interest cost for 2016 by $79,000. A 1% decrease in this annual trend rate would have decreased the APBO at December 31, 2016 by $1,634,000 and the sum of service cost and interest cost for 2016 by $71,000.

The weighted average discount rate used in determining the APBO was 4.4% in 2016 and 3.85% in 2015. The assumptions used to determine the APBO are measured at year end. The weighted average discount rate used in determining the net periodic postretirement benefit cost was 4.1% in 2016 and 4.40% in 2015, and is based on beginning of year assumptions.

Expected amounts to be recognized as components of 2017 net periodic postretirement benefit cost are interest cost on projected benefits of $1,453,000 and amortization of net loss of $193,000.

GHC funds the plan as benefit payments are required. The expected benefit payments to be paid, and contributions to be made, in each of the next five years, and in the aggregate for the five fiscal years thereafter, as of December 31, 2016, are as follows (in thousands):

Years ending December 31:		
2017	$	3,870
2018		3,753
2019		3,620
2020		3,466
2021		3,350
2022–2026		14,457
	$	32,516

(11) Commitments and Contingencies

(a) Leases

The Group was obligated under capital leases covering certain equipment that expired in 2016. At December 31, the gross amount of equipment and related accumulated amortization recorded under capital leases were as follows (in thousands):

		2016	2015
Equipment	$	6,420	6,420
Less accumulated amortization		(6,420)	(4,380)
Net equipment under capital lease	$	—	2,040

The Group has various operating leases for land, buildings, and equipment. Total rent expense was $24,832,000 and $23,428,000 on these leases in 2016 and 2015, respectively. Total sublease rental revenue was $3,983,000 and $3,746,000 in 2016 and 2015, respectively, and is recorded as a component of other revenue. Future minimum operating lease rental payments and future minimum operating sublease rental receipts under noncancelable operating lease and sublease agreements as of December 31, 2016 are as follows (in thousands):

		Operating lease rental payments	Operating sublease rental receipts
Years ending December 31:			
2017	$	25,722	2,198
2018		18,474	544
2019		16,628	306
2020		16,040	197
2021		15,037	21
Thereafter		110,958	—
Total	$	202,859	3,266

GHC entered into a sale-leaseback transaction in 2006 involving the sale of its administrative main building located in Tukwila, Washington, and then entered into a 10-year operating lease with the purchaser. The gain on sale was deferred and amortized over 120 months with the amortization recorded in other expense in the consolidated statements of operations and changes in net assets. The deferred gain is a component of unearned premiums and deposits in the consolidated balance sheets in the amount of zero and $1,702,000 as of December 31, 2016 and 2015, respectively.

(b) Labor

Approximately 62% of GHC’s employees are covered under collective bargaining agreements. These employees provide nursing and other technical services to GHC. Bargaining disputes could adversely affect GHC.

(Continued)

(c) Litigation

The Group is involved in litigation and regulatory investigations arising in the normal course of business. After consultation with legal counsel, management estimates accruals, if any, that are necessary related to these matters. Management believes the recorded amounts are adequate and the ultimate outcome of the matters will not have a material adverse effect on the Group's consolidated financial position or results of operations.

(d) Joint Partnerships and New Administrative Buildings

In 2015, GHC signed two separate joint venture agreements with Ryan Companies US, Inc., a national commercial real estate firm, to form Ryan-GHC One, LLC and Ryan-GHC Two, LLC. GHC has a 50 percent ownership in Ryan-GHC One, LLC in the amount of $3,663,000 and a 50% ownership in Ryan-GHC Two, LLC in the amount of $4,834,000 as of December 31, 2016 and 2015, respectively. Under the agreements, the joint ventures plan to develop an operations and administrative campus involving four adjacent buildings located in Renton, Washington. GHC will become the major tenant of the new campus with two 15-year operating lease agreements. GHC moved certain administrative, lab and pharmacy operations in 2016. GHC will move additional administrative operations in 2017.

(e) Government Contracts

In February 2013, the Group received a subpoena from the United States Attorney's Office, Western District of New York, requesting information related to the Group's Medicare Advantage Risk Adjustment submissions made for payment years 2008 through 2012. The Group is continuing to respond to intermittent requests for additional information subject to the subpoena. No amounts have been accrued in the accompanying consolidated financial statements related to this matter because the investigation remains in a preliminary stage and it is not possible to estimate a probable loss or provide a range of loss, if any.

(12) Federal Income Taxes

The components of income tax expense for the Group related to continuing operations and the change in unrestricted net assets for the years ended December 31, 2016 and 2015 are summarized as follows (in thousands):

		2016	2015
Federal income tax expense on operations	$	3,891	8,623
Federal income tax (benefit) expense included in the change in unrestricted net assets		(491)	973
Federal income tax expense	$	3,400	9,596

Federal income tax expense on operations is recognized as a component of other expenses in the consolidated statements of operations and changes in net assets. Federal income tax expense (benefit) included in the change in unrestricted net assets is recognized as a component of changes in net unrealized investment gains and losses and the change in defined benefit pension and other postretirement plans in the consolidated statements of operations and changes in net assets.

The deferred tax asset is recorded within current other assets and noncurrent other assets and the deferred tax liability is recorded as a component of accrued taxes and interest and in other noncurrent liabilities in the accompanying consolidated balance sheets in the following amounts (in thousands):

		2016	2015
Deferred tax asset	$	3,032	4,457
Deferred tax liability		(690)	(827)
		2,342	3,630
Valuation allowance		(316)	—
Net deferred tax asset	$	2,026	3,630

Deferred tax assets primarily relate to the tax effects of temporary differences associated with pension liabilities, buildings and improvements, postretirement accruals and capital and net operating loss carryforwards. The deferred tax liability results primarily from temporary differences in unrealized investment gains and pension accruals.

A valuation allowance of $316,000 was recorded in 2016 for unrealized losses in excess of unrealized gains and for the tax effect of impaired investments. As of December 31, 2015, the Group had net operating loss carryforwards for federal income tax purposes of $5,991,000, which were fully utilized in 2016.

(13) Endowment

Endowment funds held at the Foundation consist of approximately 36 individual funds established for a variety of purposes and all are donor-restricted. The change in net assets associated with the endowment funds is classified and reported based on the existence or absence of donor-imposed restrictions. Donor-restricted endowment assets were $14,823,000 and $14,002,000 at December 31, 2016 and 2015, respectively, and are recorded in temporarily and permanently restricted net assets.

The State of Washington Uniform Prudent Management of Institutional Funds Act of 2009 (the Act) requires the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result, the Foundation classifies as permanently restricted net assets, the original value of gifts donated to the permanent endowment funds, the original value of subsequent gifts to the permanent endowment fund, and accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation was added to the fund.

The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Foundation in a manner consistent with the standard of prudence prescribed by the Act, unless otherwise stipulated by the donor. In accordance with the Act, the Foundation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- The duration and preservation of the endowment funds
- The purposes of the Foundation and the endowment funds
- General economic conditions
- The possible effect of inflation or deflation
- The expected total return from income and the appreciation of investments
- Other resources of GHC and the Foundation
- The investment policy of the Foundation

The Foundation has adopted spending and investment policies for endowment assets that are consistent with the provisions of the Act.

Foundation policy limits spending in any calendar year to 5% of the prior year end fair market value of endowment balances. The Foundation may in any year choose to spend less than 5%. In times of low inflation or possible deflation, in the interests of preserving the endowment balances, the Foundation is more likely to keep spending under 5%. The Foundation may also choose to charge up to 1% of the endowment market value as an annual management fee. Total annual spending, including both management fee and spending allocations, cannot exceed the 5% limit. Newly received and named endowment funds are invested for one year before disbursements are made.

Under the investment policy, a diversified asset allocation is used consisting of fixed income and equity securities, and cash equivalents.

(14) Statutory Net Worth

GHC and GHO (insurance entities) are required to periodically file financial statements with regulatory agencies in accordance with statutory accounting and reporting practices. The insurance entities must comply with the minimum regulatory net worth requirements under the regulations of the Washington State Office of the Insurance Commissioner (OIC). Such requirements are generally based on 100% risk-based capital. The regulatory net worth as filed with the OIC and regulatory net worth in excess of minimum regulatory requirements as of December 31, 2016 and 2015 are shown in the following table (in thousands):

		2016	2015
GHC regulatory net worth	$	970,479	879,326
GHO regulatory net worth		130,994	142,283
GHC regulatory net worth in excess of minimum regulatory requirements		944,472	854,138
GHO regulatory net worth in excess of minimum regulatory requirements		120,455	132,362

(15) Patient Protection and Affordable Care Act

The Patient Protection and Affordable Care Act, as well as the Health Care and Education Reconciliation Act of 2010, or collectively, Health Care Reform, significantly changed the current U.S. health care system. Health Care Reform includes numerous provisions affecting the delivery of health care services, the financing of health care costs, payments to health care providers and the legal obligation of health insurers, providers and employers. Health Care Reform is intended to expand access to health insurance coverage over time by increasing the eligibility thresholds for most state Medicaid programs and providing certain other individuals and small businesses with tax credits to subsidize a portion of the cost of health insurance coverage.

Health Care Reform requires public health exchanges be available in every state by January 1, 2014. GHC offered individual products in the Washington State Health Benefit Exchange (WSHBE) starting in 2014. GHC and GHO also offered products in the outside, non-Exchange market for both individuals and small groups. Because individuals seeking to purchase health insurance coverage are guaranteed to be issued a policy, Health Care Reform provides three programs designed to reduce the risk for participating health insurance companies. Those three programs are as follows:

- A three-year temporary reinsurance program for the years 2014 through 2016. The program is designed to provide reimbursement for high cost individual enrollees and is funded by the per-customer reinsurance fee assessed against insurers and self-insured group health plans. The Group recorded $1,247,000 and $1,561,000 in ceded reinsurance premium payments in 2016 and 2015, respectively, which is an expense component of external delivery services and had $16,082,000 and $19,961,000 in reinsurance recoveries on paid losses in 2016 and 2015, respectively, which is an expense reduction of external delivery services and accounts receivable. Transitional reinsurance fees, recorded as an expense component of business taxes and insurance, was $10,394,000 and $16,302,000 for 2016 and 2015, respectively.

- A three-year temporary risk corridor program for the years 2014 through 2016. The program limits the insurer gains and losses and protects against inaccurate rate setting at the outset of the new program. The program creates a mechanism for sharing risk for allowable costs between the federal government and the insurer. In 2016, the Group recorded total risk corridor premium revenue of $15,327,000 for both benefit year 2016 and benefit year 2015 which had a full valuation allowance due to lack of collectibility. In 2015, a risk corridor revenue reduction for the 2014 benefit year was recorded of $6,386,000.
- A permanent risk adjustment program that transfers funds from lower risk to higher risk plans within similar plans in the same state in order to adjust premiums for adverse selection among carriers. The program provides payments to health insurance carriers that disproportionately attract higher-risk populations and transfers funds from plans with lower risk enrollees to plans with higher-risk enrollees. The Group recorded receivables of $869,000 and $1,134,000 and payables of $33,381,000 and $8,242,000 resulting in net premium revenue reductions of $38,248,000 and $2,584,000 in 2016 and 2015, respectively. In 2016, a risk adjustment net premium revenue reduction for the 2015 benefit year was recorded of $5,728,000.

In 2014, Health Care Reform imposed an annual carrier fee on the health insurance sector of $8 billion, and growing to $14.3 billion in 2018, that will be allocated to health insurers based on the written premium. The Group incurred fees of $35,252,000 and $37,430,000 for the years ended December 31, 2016 and 2015, respectively. This fee is temporarily suspended for the 2017 fee year only and, unless the moratorium is extended through future legislation, the fee would again become effective after 2017.

(16) Correction of Error

During the year ended December 31, 2016, the Group identified an error in the recording of a liability related to unrelated business taxes prior to January 1, 2015. As a result, the consolidated financial statements, including beginning net assets as of January 1, 2015, have been revised from amounts previously reported as follows (in thousands):

		As previously reported	2015 As revised	Change
At December 31:				
Accrued taxes and interest	$	41,482	46,613	5,131
Unrestricted net assets		1,022,898	1,017,767	(5,131)
For the year ended December 31:				
Interest expense	$	(3,506)	(3,652)	(146)
Excess of revenues over expenses		113,749	113,603	(146)
Change in unrestricted net assets		80,461	80,315	(146)
Change in net assets		79,632	79,486	(146)
Net assets, end of year		1,038,725	1,033,594	(5,131)

The impact of opening net assets for January 1, 2015 was a decrease of $4,985,000.

(17) Restatement

Subsequent to the issuance of the Group's December 31, 2016 consolidated financial statements, management identified an understatement in liabilities. In connection with the acquisition disclosed in note 1, certain contingent liabilities were recognized for $53,000,000 that were required to be recorded at December 31, 2016 as a subsequent event. As a result, the December 31, 2016 consolidated financial statements have been revised from amounts previously reported, as follows (in thousands):

		As previously reported	As restated	Change
At December 31, 2016:				
Accounts payable and accrued expenses	$	159,876	212,876	53,000
Unrestricted net assets		1,097,228	1,044,228	(53,000)
For the year ended December 31:				
Group Health Physicians expense	$	356,340	409,340	53,000
Excess of revenues over expenses		59,078	6,078	(53,000)
Change in unrestricted net assets		79,461	26,461	(53,000)
Change in net assets		79,667	26,667	(53,000)
Net assets, end of period		1,113,261	1,060,261	(53,000)

(18) Subsequent Events

Subsequent events are events or transactions that occur after the consolidated balance sheet date but before consolidated financial statements are issued that provide additional evidence about conditions that existed at the date of the consolidated balance sheet.

The Group has evaluated subsequent events for recognition or disclosure through June 1, 2017, the date these consolidated financial statements were issued.

KPMG LLP
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

The Board of Directors
Kaiser Foundation Health Plan of Washington

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the consolidated financial statements of Group Health Cooperative and Subsidiaries (the Group), which comprise the consolidated balance sheets as of December 31, 2016 and 2015 and the related consolidated statements of operations and changes in net assets and cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated March 24, 2017, except for the effects of the restatement described in Note 17 to the consolidated financial statements and subsequent events described in Note 18 to the consolidated financial statements, as to which the date is June 1, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered the Group's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control. Accordingly, we do not express an opinion on the effectiveness of the Group's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identified a deficiency in internal control that we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying schedule of findings and questioned costs as item 2016-01 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Group's consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The Group's Response to Findings

The Group's response to the finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The Group's response was not subjected to the auditing procedures applied in the audit of the consolidated financial statements and, accordingly, we express no opinion on the response.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Group's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Group's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Seattle, Washington
March 24, 2017, except for
the effects of the restatement
described in Note 17 to the
consolidated financial statements
and subsequent events described
in Note 18 to the consolidated
financial statements, as to which
the date is June 1, 2017

KPMG LLP
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

Independent Auditors' Report on Compliance for Each Major Federal Program; Report on Internal Control Over Compliance; and Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

The Board of Trustees
Group Health Cooperative and Subsidiaries:

Report on Compliance for Each Major Federal Program

We have audited Group Health Cooperative and Subsidiaries' (the Group) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Group's major federal programs for the year ended December 31, 2016. The Group's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for each of the Group's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance)*. Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Group's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Group's compliance.

Opinion on Each Major Federal Program

In our opinion, the Group complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2016.

Report on Internal Control over Compliance

Management of the Group is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Group's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Group's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

We have audited the consolidated financial statements of the Group as of and for the year ended December 31, 2016, and have issued our report thereon dated March 24, 2017, which contained an unmodified opinion on those financial statements. Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is 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 consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the 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 consolidated financial statements or to the 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 schedule of expenditures of federal awards is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

Seattle, Washington
March 24, 2017

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Schedule of Expenditures of Federal Awards

Year ended December 31, 2016

CFDA	Federal Grantor / Pass-Through Grantor / Program Title	Pass-through Grantor's number (only for pass-through awards)	Expenditures to Subrecipients	Total SEFA Expenditures
	Research and Development Cluster:			
	US Department of Health and Human Services:			
93.226	Agency For Healthcare Research		$ 3,259,990	6,190,198
93.185	Centers For Disease Control		58,366	846,105
93.RD	Centers For Disease Control		—	702,635
93.510	Health Resources & Serv Admin		—	86,001
93.866	National Institutes Of Health		—	29,057
93.121	National Institutes Of Health		168,902	549,141
93.172	National Institutes Of Health		403,829	1,001,952
93.213	National Institutes Of Health		121,614	390,347
93.242	National Institutes Of Health		2,855,011	4,587,687
93.273	National Institutes Of Health		91,834	605,015
93.279	National Institutes Of Health		24,911	98,839
93.307	National Institutes Of Health		106,326	188,152
93.393	National Institutes Of Health		1,989,507	3,891,267
93.395	National Institutes Of Health		4,644	12,712
93.397	National Institutes Of Health		28,861	974,156
93.837	National Institutes Of Health		411,191	728,195
93.847	National Institutes Of Health		487,588	798,841
93.865	National Institutes Of Health		959,979	1,667,726
93.866	National Institutes Of Health		1,230,622	3,065,416
93.879	National Institutes Of Health		13,479	44,818
93.RD	National Institutes Of Health		364,298	2,018,640
	Prime Subtotal		12,580,952	28,476,900
	Pass-through awards from:			
93.RD	Abt Associates Inc.	HHSA2901000004I / HHSA29032009T	—	111,439
93.RD	Abt Associates Inc.	GS-10F-0086K/BPA 200-2013-M-53	—	3,050

(Continued)

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Schedule of Expenditures of Federal Awards

Year ended December 31, 2016

CFDA	Federal Grantor / Pass-Through Grantor / Program Title	Pass-through Grantor's number (only for pass-through awards)	Expenditures to Subrecipients	Total SEFA Expenditures
93.RD	Abt Associates Inc.	HHSM-500-2014-00026I / HHSM-50	$ —	43,115
93.RD	Abt Associates Inc.	HHSM-500-2014-00026I	—	18,859
93.RD	Abt Associates Inc.	GS00F252CA/200-2016-F-92356	—	2,308
93.393	Center For Health Research, Kaiser Foundation Hospitals	5UH3CA188640-03	—	(63)
93.393	Center For Health Research, Kaiser Foundation Hospitals	5UH3CA188640-04	—	133,489
93.853	Center For Health Research, Kaiser Foundation Hospitals	UH3NS088731-S1	—	1,099
93.RD	Center For Health Research, Kaiser Foundation Hospitals	HHSA290201200015I	—	15,897
93.RD	Center For Health Research, Kaiser Foundation Hospitals	HHSA290201200015I	—	41,279
93.RD	Center For Health Research, Kaiser Foundation Hospitals	HHSA290201200015I	—	117,507
93.RD	Center For Health Research, Kaiser Foundation Hospitals	HHSA290201200015I	—	88,207
93.RD	Center For Health Research, Kaiser Foundation Hospitals	HHSA290201200015I	—	158,533
93.RD	Center For Health Research, Kaiser Foundation Hospitals	HHSA290201200015I	—	29,630
93.RD	Center For Health Research, Kaiser Foundation Hospitals	HHSA290201500007I	—	119,350
93.RD	Center For Health Research, Kaiser Foundation Hospitals	HHSA290201200015I	—	11,001
93.RD	Center For Health Research, Kaiser Foundation Hospitals	HHSA290201500007I	—	28,014
93.RD	Center For Health Research, Kaiser Foundation Hospitals	GS-10F0086K/BPA 200-2013M53890	—	3,840
93.RD	Crosby Marketing	HHSA2990201200019I	—	116,418
93.RD	Crosby Marketing	HHSA2990201200019I	—	65,246
93.393	Dana Farber Cancer Institute	5R01CA172143-03	—	1,831
93.393	Dana Farber Cancer Institute	4R01CA172143-04	—	37,291
93.393	Dartmouth College	5R01CA149365-05	—	111,042
93.213	Duke University	5U54AT007748-04	—	128,291
93.213	Duke University	4U54AT007748-05	—	60,248
93.279	Duke University	1R01DA040056-01	—	5,497
93.393	Fred Hutchinson Cancer Research Center	R01CA168758	—	2,537
93.393	Fred Hutchinson Cancer Research Center	5R01CA151251-05	—	25,502
93.393	Fred Hutchinson Cancer Research Center	5R01CA166646-03	—	517
93.393	Fred Hutchinson Cancer Research Center	4R01CA166646-04	—	40,715

(Continued)

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Schedule of Expenditures of Federal Awards

Year ended December 31, 2016

CFDA	Federal Grantor / Pass-Through Grantor / Program Title	Pass-through Grantor's number (only for pass-through awards)	Expenditures to Subrecipients	Total SEFA Expenditures
93.393	Fred Hutchinson Cancer Research Center	5R01CA168338-03	$ —	124,163
93.393	Fred Hutchinson Cancer Research Center	4R01CA168338-04	—	156,439
93.393	Fred Hutchinson Cancer Research Center	1R01CA192402-01A1	—	24,406
93.393	Fred Hutchinson Cancer Research Center	5R01CA192402-02	—	36,647
93.866	Fred Hutchinson Cancer Research Center	1R01AG048209-01A1	—	34,777
93.866	Fred Hutchinson Cancer Research Center	5R01AG048209-02	—	481,941
93.393	Georgetown University	1R01CA190221-01A1	—	88,649
93.393	Georgetown University	1R01CA190221-01A1	—	93,824
93.393	Georgetown University	1U01CA199218-01	—	21,818
93.393	Georgetown University	5U01CA199218-02	—	17,309
93.113	Harvard Chan School of Public Health	5R01ES024332-02	—	19,213
93.393	Harvard Medical School	5R01CA168959-05	—	21,456
93.RD	Harvard Pilgrim Health Care	HHSF223201000009I	—	5,636
93.RD	Harvard Pilgrim Health Care	HHSF223200910006I	—	1,336
93.RD	Harvard Pilgrim Health Care	HHSF223201000009I	—	35,915
93.RD	Harvard Pilgrim Health Care	HHSF223200910006I	21,182	241,669
93.RD	Harvard Pilgrim Health Care	HHSF22320140030I	—	36,173
93.RD	Harvard Pilgrim Health Care	HHSF223200910006I	—	16,169
93.RD	Harvard Pilgrim Health Care	HHSF223201400030I	—	89,539
93.RD	Harvard Pilgrim Health Care	HHSF223201400030I	—	2,371
93.RD	Harvard Pilgrim Health Care	HHSF223201400030I	—	110,205
93.RD	Harvard Pilgrim Health Care	HHSF223201400030I	—	31,990
93.RD	Harvard Pilgrim Health Care	HHSF223201400030I	—	42,732
93.RD	Harvard Pilgrim Health Care	HHSF223201400030I	—	13,291
93.RD	Harvard Pilgrim Health Care	HHSF223201400030I	—	106,805
93.RD	Harvard Pilgrim Health Care	HHSF223201400030I	—	27,404

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Schedule of Expenditures of Federal Awards

Year ended December 31, 2016

CFDA	Federal Grantor / Pass-Through Grantor / Program Title	Pass-through Grantor's number (only for pass-through awards)	Expenditures to Subrecipients	Total SEFA Expenditures
93.RD	Harvard Pilgrim Health Care	HHSF223200910006I	$ —	104,297
93.RD	Harvard Pilgrim Health Care	HHSF22320140030I	—	52,058
93.RD	Harvard Pilgrim Health Care	HHSF223200910006I	—	13,053
93.RD	Harvard Pilgrim Health Care	HHSF223201400030I	—	27,434
93.RD	Harvard Pilgrim Health Care	HHSF223201400042I	—	1,577
93.RD	Harvard Pilgrim Health Care	HHSF223201400030I	—	10,275
93.RD	Harvard Pilgrim Health Care	HHSF22301002T	—	20,674
93.837	Healthpartners, Inc	5R01HL090965-06	—	5,630
93.242	Henry Ford Health System	1R01MH103530-01A1	—	67,803
93.853	Icahn School Of Medicine at Mount Sinai	5U01NS086625-02	—	3,142
93.853	Icahn School Of Medicine at Mount Sinai	5U01NS086625-03	—	212,604
93.855	Id Genomics Inc	2R42AI116114-02	—	59,592
93.242	Indiana University	5R01MH103310-03	—	33,599
93.837	Kaiser Foundation Health Plan Of Co	R01HL113550	—	12,081
93.837	Kaiser Foundation Health Plan Of Co	R01HL113550	—	12,978
93.837	Kaiser Foundation Health Plan, Oakland, CA	1R01HL130462-01A1	—	26,082
93.847	Kaiser Foundation Health Plan, Oakland, CA	1R01DK108522-01	—	20,146
93.847	Kaiser Permanente, Pasadena, CA	5R01DK108522-02	—	13,317
93.RD	Kaiser Permanente, Oakland, CA	HHSF223201400132C	—	6,087
93.279	Kaiser Permanente Division of Research	1UG1DA040314-01	—	112,317
93.279	Kaiser Permanente Division of Research	5UG1DA040314-02	—	121,441
93.279	Kaiser Permanente Division of Research	3UG1DA040314-01S1	—	103,641
93.279	Kaiser Permanente Division of Research	3UG1DA040314-02S2	—	127,746
93.279	Kaiser Permanente Division of Research	3UG1DA040314-02S1	—	15,532
93.279	Kaiser Permanente Division of Research	3UG1DA040314-02S1	14,208	135,923
93.393	Kaiser Permanente Division of Research	5U24CA171524-04	—	21,513
93.393	Kaiser Permanente Division of Research	5U24CA171524-04	—	283,645
93.393	Kaiser Permanente Division of Research	4U24CA171524-05	—	138,309

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Schedule of Expenditures of Federal Awards

Year ended December 31, 2016

CFDA	Federal Grantor / Pass-Through Grantor / Program Title	Pass-through Grantor's number (only for pass-through awards)	Expenditures to Subrecipients	Total SEFA Expenditures
93.393	Kaiser Permanente Division of Research	5U24CA171524-04	$ —	23,757
93.RD	Mathematica Policy Research	HHSM-500-2010-00026I	—	92,077
93.RD	Mathematica Policy Research	HHSM-500-2010-00026I	—	57,184
93.331	Merced County Dept Public Health	5U58DP005710-02	—	51,336
93.331	Merced County Dept Public Health	5U58DP005710-03	—	8,214
93.393	Memorial Sloan Kettering Cancer Center	5U01CA152959-05	—	1,961
93.RD	National Committee For Quality Assurance	HHSN316201200139W	—	5,565
93.242	Northwestern University	5R01MH095753-04	—	46,795
93.393	Nyu School Of Medicine	1R01CA188353-01A1	—	40,922
93.393	Nyu School Of Medicine	5R01CA188353-02	—	136,970
93.226	Oregon Health & Science University	1R01HS023940-01	—	3,696
93.226	Oregon Health & Science University	5R01HS023940-02	—	7,104
93.270	Public Health – Seattle & King	5U51PS004601-02	—	123,457
93.270	Public Health – Seattle & King	5NU51OS004601-03	—	31,912
93.424	Public Health Institute	NNPHI/EBOLA: 05315-01-01	—	21,199
93.424	Public Health Institute	NNPHI/USVI: 05348-01-01	—	5,479
93.424	Public Health Institute	NNPHI/GHWIC: 05316-01-01	—	14,917
93.424	Public Health Institute	NNPHI/APPALACHIA: 05413-01-01	—	14,981
93.RD	Puget Sound Blood Center	H30MC24049	—	7,644
93.393	Rand	1U01CA199335-01	—	67,202
93.279	Research Triangle Institute	5R01DA034627-02	—	43,582
93.865	Seattle Children'S Hospital	5K23HD069467-03	—	1,694
93.865	Seattle Children'S Hospital	1R21HD083770-01A1	—	78,353
93.945	Seattle Children'S Hospital	1U18DP006136-01	—	11,362
93.945	Seattle Children'S Hospital	5U18DP006136-02	—	4,570

(Continued)

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Schedule of Expenditures of Federal Awards

Year ended December 31, 2016

CFDA	Federal Grantor / Pass-Through Grantor / Program Title	Pass-through Grantor's number (only for pass-through awards)	Expenditures to Subrecipients	Total SEFA Expenditures
93.933	Southcentral Foundation	U261IHS0079-01-00	$ —	34,383
93.866	Stanford University	1RF1AG053959-01	—	1,733
93.RD	Takeda Vaccines, Inc	HHSN272201000034C	—	16,848
93.RD	The Emmes Corporation	HHSN271201400028C	—	15,536
93.393	Ucsf Controller'S Office	1R01CA185687-01A1 REVISED	—	42,116
93.393	Ucsf Controller'S Office	1R01CA185687-01A1	—	33,435
93.393	Ucsf Controller'S Office	5R01CA185687-02	—	119,992
93.846	University Of Alabama	5R01AR060240-05	—	54,125
93.393	University Of Cincinnati	5R01CA175346-02	—	6,136
93.393	University Of Cincinnati	5R01CA175346-03	—	22,747
93.866	University Of Massachussetts	5R24AG045050-02	—	33,697
93.866	University Of Massachussetts	5R24AG045050-03	—	10,879
93.866	University Of Massachussetts	3R24AG045050-03S1	—	34,435
93.866	University Of Michigan	1K08AG048321-01	—	96
93.866	University Of Utah	5R01AG023801-10	—	46,353
93.113	University Of Washington	1R01ES026187-01A1	—	8,732
93.866	University Of Washington	1 R01AG053221-01	—	70,675
93.135	University Of Washington	3U48DP005013-01S1	—	6,031
93.135	University Of Washington	5U48DP005013-03	—	1,940
93.135	University Of Washington	5U48DP005013-02	—	51,769
93.135	University Of Washington	5U48DP005013-03	—	7,907
93.213	University Of Washington	1T90AT008544-01	—	20,283
93.213	University Of Washington	5T90AT008544-02	—	45,746
93.226	University Of Washington	4R01HS022106-03	—	17,795
93.226	University Of Washington	1R01HS023785-01	—	5,373
93.226	University Of Washington	5R01HS022106-04	—	8,266
93.226	University Of Washington	1K12HS022982-01	—	169
93.226	University Of Washington	5K12HS022982-02	—	4,838

(Continued)

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Schedule of Expenditures of Federal Awards

Year ended December 31, 2016

CFDA	Federal Grantor / Pass-Through Grantor / Program Title	Pass-through Grantor's number (only for pass-through awards)	Expenditures to Subrecipients	Total SEFA Expenditures
93.226	University Of Washington	1K12HS022982-01	$ —	4,924
93.226	University Of Washington	5R01HS023785-02	—	7,851
93.226	University Of Washington	5K12HS022982-03	—	746
93.226	University Of Washington	5K12HS022982-03	—	1,561
93.226	University Of Washington	5K12HS022982-03	—	2,561
93.279	University Of Washington	5R01DA015183-14	—	5,300
93.310	University Of Washington	5UH3AR066795-03	—	2,393
93.310	University Of Washington	5UH3AR066795-04	—	126,788
93.350	University Of Washington	4UL1TR000423-10	—	93,830
93.350	University Of Washington	5UL1TR000423-09	—	89,303
93.350	University Of Washington	5TL1TR000422-09	—	248
93.393	University Of Washington	5R01CA168598-03	—	142,349
93.393	University Of Washington	5R01CA168598-04	—	255,576
93.837	University Of Washington	4K08HL116640-04	—	7,688
93.847	University Of Washington	2R01DK076608-08A1	—	26,438
93.847	University Of Washington	1U34DK107917-01	—	9,189
93.847	University Of Washington	5U35DK107917-02	—	4,395
93.847	University Of Washington	5U01DK102150-03	—	22,161
93.855	University Of Washington	5R01AI106007-04	—	160,308
93.859	University Of Washington	5U01GM092676-05	—	54,568
93.866	University Of Washington	2P50AG005136-32	—	30,935
93.866	University Of Washington	5P50AG005136-33	—	68,685
93.866	University Of Washington	5R01AG049815-02	—	94,927
93.866	University Of Washington	1R21AG049196-01	—	18,160
93.RD	University Of Washington	HHSN276201100008C	—	2,334
93.624	Wa State Health Care Authority	1G1CMS331406-01-00	—	239,569
93.RD	Westat	HHSN261201300016C	—	44,746
	Pass-through Subtotal		35,390	8,307,563
	Total US Department of Health and Human Services		12,616,342	36,784,463

(Continued)

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Schedule of Expenditures of Federal Awards

Year ended December 31, 2016

CFDA	Federal Grantor / Pass-Through Grantor / Program Title	Pass-through Grantor's number (only for pass-through awards)	Expenditures to Subrecipients	Total SEFA Expenditures
	US Department of Defense			
64.RD	Department Of Veterans Affairs		$ —	12,950
	Prime Subtotal		—	12,950
	Pass-through awards from:			
64.RD	Dept Of Veterans Affairs Med	523D62004	—	6,045
12.RD	Tasso Inc	W31P4Q-14-C-0006	—	96,121
	Pass-through Subtotal		—	102,166
	Total US Department of Health and Human Services		—	115,116
	Total Research and Development Cluster		$ 12,616,342	36,899,579

(1) Basis of Presentation

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal grant activity of Group Health Cooperative and Subsidiaries (the Group) under programs of the federal government for the year ended December 31, 2016. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*. Because the Schedule presents only a selected portion of the operations of the Group, it is not intended to and does not present the financial position, changes in net assets, or cash flows of the Group.

(2) Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the *Uniform Guidance, Cost Principles for Non-profit Organizations*, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Negative amounts shown on the Schedule represent adjustments or credits made in the normal course of business to amounts reported as expenditures in prior years. Pass-through entity identifying numbers are presented where available.

(3) Indirect Cost Rate

The Group has negotiated Facilities & Administration rates from the Division of Cost Allocation. The Group has elected not to use the 10% de minimis cost rate.

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Restated Schedule of Findings and Questioned Costs

December 31, 2016

(1) Summary of Auditors' Results

Financial Statements

Type of auditors' report issued:	Unmodified			
Internal control over financial reporting:				
Material weaknesses identified?	X	Yes		No
Significant deficiencies identified that are not considered to be material weaknesses		Yes	X	None reported
Noncompliance material to the financial statements noted?		Yes	X	No

Federal Awards

Internal control over major programs:				
Material weaknesses identified?		Yes	X	No
Significant deficiencies identified that are not considered to be material weaknesses		Yes	X	None reported
Type of auditors' report issued on compliance for major programs:	Unmodified			
Any audit findings disclosed that are required to be reported in accordance with CFR section 200.516 of the Uniform Guidance?		Yes	X	No

Identification of Major Programs

CFDA number	Name of federal program
Cluster	Research and Development

Dollar threshold used to distinguish between Type A and Type B programs:	$1,106,987			
Auditee qualified as low-risk auditee?	X	Yes		No

(2) Financial Statement Findings Section

Finding 2016-001

Federal Program:

NA

Federal Agency:

NA

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Restated Schedule of Findings and Questioned Costs

December 31, 2016

Federal Award Year:

January 1, 2016 to December 31, 2016

Criteria

The Group's review over subsequent events related to business acquisitions should be designed at a proper level of precision to identify misstatements.

Statement of Condition

There was a deficiency in internal control around the consideration of subsequent events giving rise to disclosure or recognition in the financial statements. Subsequent to the issuance of the consolidated financial statements as of and for the year ended December 31, 2016, an error in the recognition of a liability resulting from the acquisition of the Group by KFHPW Holdings was identified. As a result, the December 31, 2016 consolidated financial statements have been restated from the amounts previously reported.

Cause and Effect

This error is the result of the Group's controls not designed at an appropriate level of precision to detect subsequent events related to business acquisition activity. As a result of the material misstatement, financial statements were restated for fiscal year 2016.

Questioned Costs

None

Was the sampling statistically valid?

The error was not found as a part of a sampled population.

Repeat Finding?

No

Recommendation

We recommend that the Group refine controls over financial reporting, specifically over the review of subsequent events related to business acquisitions.

View of Responsible Officials and Corrective Action Plan:

Management agrees with the finding. Management will enhance its documentation of its consideration of subsequent events, through the date of issuance, for each annual audited financial statement. Management is committed to remediating the internal control deficiency in 2018.

(3) Federal Award Findings and Questioned Costs

No matters reported.