KAISER FOUNDATION HEALTH PLAN, INC. AND SUBSIDIARIES AND KAISER FOUNDATION HOSPITALS AND SUBSIDIARIES

Combined Financial Statements

December 31, 2015 and 2014

(With Independent Auditors' Reports Thereon)

KAISER FOUNDATION HEALTH PLAN, INC. AND SUBSIDIARIES AND KAISER FOUNDATION HOSPITALS AND SUBSIDIARIES

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KPMG LLP
Suite 1400
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San Francisco, CA 94105

Independent Auditors' Report

The Boards of Directors
Kaiser Foundation Health Plan, Inc.
and Kaiser Foundation Hospitals:

We have audited the accompanying combined financial statements of Kaiser Foundation Health Plan, Inc. and Subsidiaries (Health Plans) and Kaiser Foundation Hospitals and Subsidiaries (Hospitals), which comprise the combined balance sheets as of December 31, 2015 and 2014, and the related combined statements of operations and changes in net worth, and cash flows for the years then ended, and the related notes to the combined financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these combined 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 combined 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 combined financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the combined 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 combined 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 combined financial statements.

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

Opinion

In our opinion, the combined financial statements referred to above present fairly in all material respects, the combined financial position of Health Plans and Hospitals as of December 31, 2015 and 2014, and the results of their operations and their cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

KPMG LLP

San Francisco, California
February 12, 2016

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("KPMG International"), a Swiss entity.

KAISER FOUNDATION HEALTH PLAN, INC. AND SUBSIDIARIES AND KAISER FOUNDATION HOSPITALS AND SUBSIDIARIES

Combined Balance Sheets

December 31, 2015 and 2014

(In millions)

Assets	**2015**	**2014**
Current assets:		
Cash and cash equivalents	$ 210	$ 288
Current investments	6,554	6,390
Securities lending collateral	1,068	1,528
Broker receivables	816	495
Accounts receivable - net	1,966	1,841
Inventories and other current assets	1,427	1,208
Total current assets	12,041	11,750
Noncurrent investments	26,189	26,081
Land, buildings, equipment, and software - net	23,782	23,484
Other long-term assets	614	600
Total assets	$ 62,626	$ 61,915

Liabilities and Net Worth	**2015**	**2014**
Current liabilities:		
Accounts payable and accrued expenses	$ 2,977	$ 3,139
Medical claims payable	1,750	1,393
Due to associated medical groups	784	983
Payroll and related charges	1,694	1,832
Securities lending payable	1,068	1,528
Broker payables	1,160	819
Long-term debt subject to short-term remarketing arrangements - net	732	1,445
Other current debt	775	672
Other current liabilities	2,027	1,759
Total current liabilities	12,967	13,570
Long-term debt	6,089	5,505
Physicians' retirement plan liability	5,730	5,923
Pension and other retirement liabilities	10,525	13,700
Other long-term liabilities	2,418	2,390
Total liabilities	37,729	41,088
Net worth	24,897	20,827
Total liabilities and net worth	$ 62,626	$ 61,915

See accompanying notes to combined financial statements.

KAISER FOUNDATION HEALTH PLAN, INC. AND SUBSIDIARIES AND KAISER FOUNDATION HOSPITALS AND SUBSIDIARIES

Combined Statements of Operations and Changes in Net Worth

Years ended December 31, 2015 and 2014

(In millions)

	2015	2014
Revenues:		
Members' dues	$ 40,956	$ 38,587
Medicare	14,436	13,347
Copays, deductibles, fees, and other	5,357	4,506
Total operating revenues	60,749	56,440
Expenses:		
Medical services	27,732	26,410
Hospital services	16,364	14,619
Outpatient pharmacy and optical services	7,059	6,069
Other benefit costs	3,900	3,468
Total medical and hospital services	55,055	50,566
Health Plan administration	3,928	3,697
Total operating expenses	58,983	54,263
Operating income	1,766	2,177
Other income and expense:		
Investment income - net	300	1,101
Interest expense	(198)	(205)
Total other income and expense	102	896
Net income	1,868	3,073
Change in pension and other retirement liability charges	2,997	(5,196)
Change in net unrealized gains on investments	(793)	(110)
Change in restricted donations	(2)	15
Change in noncontrolling interest	—	(4)
Change in net worth	4,070	(2,222)
Net worth at beginning of year	20,827	23,049
Net worth at end of year	$ 24,897	$ 20,827

See accompanying notes to combined financial statements.

KAISER FOUNDATION HEALTH PLAN, INC. AND SUBSIDIARIES AND KAISER FOUNDATION HOSPITALS AND SUBSIDIARIES

Combined Statements of Cash Flows

Years ended December 31, 2015 and 2014

(In millions)

	2015	2014
Cash flows from operating activities:		
Net income	$ 1,868	$ 3,073
Adjustments to reconcile net income to net cash provided from operating activities:		
Depreciation and software amortization	2,158	2,006
Other amortization	(6)	(4)
Loss (gain) recognized on investments - net	175	(739)
Loss on land, buildings, equipment, and software - net	60	17
Changes in assets and liabilities:		
Accounts receivable - net	(125)	(339)
Other assets	(216)	(110)
Accounts payable and accrued expenses	11	833
Medical claims payable	357	133
Due to associated medical groups	(204)	186
Payroll and related charges	(138)	178
Pension and other retirement liabilities	(959)	(146)
Other liabilities	338	300
Net cash provided from operating activities	3,319	5,388
Cash flows from investing activities:		
Additions to land, buildings, equipment, and software	(2,698)	(2,793)
Proceeds from sales of land, buildings, and equipment	5	17
Proceeds from investments	38,930	33,562
Investment purchases	(40,169)	(36,394)
Decrease (increase) in securities lending collateral	460	(110)
Broker receivables / payables	20	(4)
Issuance of notes receivable	(161)	(217)
Prepayment and repayment of notes receivable	144	164
Other investing	28	103
Physicians' retirement plan liability	524	342
Net cash used in investing activities	(2,917)	(5,330)
Cash flows from financing activities:		
Issuance of debt	1,454	520
Prepayment and repayment of debt	(1,472)	(550)
Increase (decrease) in securities lending payable	(460)	110
Change in restricted donations	(2)	3
Change in noncontrolling interest	—	(4)
Net cash provided from (used in) financing activities	(480)	79
Net change in cash and cash equivalents	(78)	137
Cash and cash equivalents at beginning of year	288	151
Cash and cash equivalents at end of year	$ 210	$ 288
Supplemental cash flows disclosure:		
Cash paid for interest - net of capitalized amounts	$ 212	$ 200
Noncash investment transactions	$ —	$ (47)

See accompanying notes to combined financial statements.

(1) Description of Business

The accompanying combined financial statements include Kaiser Foundation Health Plan, Inc. and Subsidiaries (Health Plans) and Kaiser Foundation Hospitals and Subsidiaries (Hospitals). Health Plans and Hospitals are primarily not-for-profit corporations whose capital is available for charitable, educational, research, and related purposes. Health Plans are primarily health maintenance organizations and are generally exempt from federal and state income taxes. Membership at December 31, 2015 and 2014 was 10.2 million and 9.6 million, respectively. At both December 31, 2015 and 2014, the percentage of enrolled membership in California was approximately 78%. The principal operating subsidiary of Kaiser Foundation Hospitals is Kaiser Hospital Asset Management, Inc. (KHAM). The principal operating subsidiaries of Kaiser Foundation Health Plan, Inc. (Health Plan, Inc.) are:

Kaiser Foundation Health Plan of Colorado
Kaiser Foundation Health Plan of Georgia, Inc.
Kaiser Foundation Health Plan of the Mid-Atlantic States, Inc.
Kaiser Foundation Health Plan of the Northwest
Kaiser Health Plan Asset Management, Inc. (KHPAM)

Independent Medical Groups (Medical Groups) cooperate with Health Plans and Hospitals in conducting the Kaiser Permanente Medical Care Program. Health Plans contracts with Hospitals and the Medical Groups to provide or arrange hospital and medical services for members. Hospitals also contracts with the Medical Groups for certain professional services. Contract payments to the Medical Groups represent a substantial portion of the expenses for medical services reported in these combined financial statements. Payments from Health Plans and Hospitals constitute substantially all of the revenues for the Medical Groups. Because the Medical Groups are independent and not controlled by Health Plans and Hospitals, their financial statements are not combined or consolidated with Health Plans and Hospitals.

At December 31, 2015 and 2014, the percentages of Health Plans' and Hospitals' total labor force covered under collective bargaining agreements were approximately 70% and 69%, respectively. At December 31, 2015, less than 1% of the workforce was covered under collective bargaining agreements that are scheduled to expire within one year. At December 31, 2015, none of the workforce was working under an expired agreement, and approximately 1% of the workforce is in a new bargaining unit that is currently negotiating an agreement.

Health Plans and Hospitals strive to improve the health and welfare of the communities they serve through their Community Benefit investment programs. Community Benefit expenditures provide funding for programs that serve communities through research, community-based health partnerships, direct health coverage for low-income families, and collaboration with community clinics, health departments, and public hospitals.

For the year ended December 31, 2015, Community Benefit expenditures (at cost, net of approximately $2.6 billion of related revenues) were $2.1 billion, representing 3.5% of operating revenue. In comparison, for the year ended December 31, 2014, Community Benefit expenditures (at cost, net of $1.4 billion of

related revenues) were $2.2 billion, representing 3.9% of operating revenue. The calculation of Community Benefit expenditures is based on Health Plans' and Hospitals' direct and indirect costs and the services provided by Health Plans and Hospitals under Community Benefit programs.

(2) Summary of Significant Accounting Policies

(a) Basis of Presentation

The financial statements of Health Plans and Hospitals are presented on a combined basis due to the operational interdependence of these organizations and because their governing boards and management are substantially the same. These combined financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). All material intercompany balances and transactions have been eliminated. Management has evaluated subsequent events through February 12, 2016, which is the date that these combined financial statements were issued.

(b) Cash and Cash Equivalents

Cash and cash equivalents include interest-bearing deposits purchased with an original or remaining maturity of three months or less. Cash and investments that are restricted per contractual or regulatory requirements are classified as noncurrent investments and excluded from cash and cash equivalents.

(c) Investments

Investments include equity, U.S. Treasury, government agencies, money market funds, and other marketable debt securities and are reported at fair value. Investments are categorized as current assets if they are intended to be available to satisfy current liabilities. Alternative investments are reported under the equity method. Certain investments are illiquid and are valued based on the most current information available. Other-than-temporary impairment and recognized gains and losses, which are recorded on the specific identification basis, and interest, dividend income, and income from equity method alternative investments are included in investment income - net. Health Plans and Hospitals have designated a portion of their investments for the physicians' retirement plan liability related to defined retirement benefits provided for physicians associated with certain Medical Groups. These investments are unrestricted assets of Health Plans and Hospitals. A portion of investment income that represents the expected return on the investments designated for the physicians' retirement plan has been recorded as a reduction in the provision for physicians' retirement plan benefits and is excluded from investment income - net, as described in the *Physicians' Retirement Plan* note.

Investments are regularly reviewed for impairment and a charge is recognized when the fair value is below cost basis and is judged to be other-than-temporary. In its review of assets for impairment that is deemed other-than-temporary, management generally follows the following guidelines:

- Substantially all investments are managed by outside investment managers who do not need Health Plans' or Hospitals' management preapproval for sales; therefore, substantially all declines in value below cost are recognized as impairment that is other-than-temporary.
- For other securities, losses are recognized for known matters, such as bankruptcies, regardless of ownership period, and investments that have been continuously below book value for an extended period of time are evaluated for impairment that is other-than-temporary.

All other unrealized losses and all unrealized gains on investments are included as other changes in net worth.

Interest income is calculated under the effective interest method and included in investment income - net. Dividends are included in investment income - net on the ex-dividend date, which immediately follows the record date.

Health Plans' and Hospitals' investment transactions are recorded on a trade date basis.

(d) Securities Lending Collateral and Payable

Health Plans and Hospitals enter into securities lending agreements whereby certain securities from their portfolios are loaned to other institutions. Securities lent under such agreements remain in the portfolios of Health Plans and Hospitals. Health Plans and Hospitals receive a fee from the borrower under these agreements, which is recognized ratably over the period that the securities are lent. Collateral, primarily cash, is required at a rate of 102% of the fair value of securities lent and is carried as securities lending collateral. The obligation of Health Plans and Hospitals to return the cash collateral is carried as securities lending payable. The fair value of securities lending collateral is determined using level 1 or 2 inputs as appropriate, as defined in the *Fair Value Estimates* note. The fair value of the loaned securities is monitored on a daily basis, with additional collateral obtained or refunded as the fair value of the loaned securities fluctuates.

(e) Broker Receivables and Payables

Broker receivables and payables represent current amounts for unsettled securities sales or purchases.

(f) Inventory

Inventories, consisting primarily of pharmaceuticals and supplies, are carried at the lower of cost (generally first-in, first-out or average price) or market.

(g) Land, Buildings, Equipment, and Software

Land, buildings, equipment, and software are stated at cost less accumulated depreciation and amortization. Interest is capitalized on facilities construction and internally developed software work in progress and is added to the cost of the underlying asset. Software, which includes internal and external costs incurred in developing or obtaining computer software for internal use, is capitalized. Qualifying costs incurred during the application development stage are capitalized. Depreciation and amortization begin when the project is substantially complete and ready for its intended use. Software is amortized on a straight-line basis over the estimated useful lives, generally ranging from 3 to 7 years. Buildings and equipment are depreciated on a straight-line basis over the estimated useful lives of the various classes of assets, generally ranging from 3 to 33 years.

Management evaluates alternatives for delivering services that may affect the current and future utilization of existing and planned assets and could result in an adjustment to the carrying values or remaining lives of such land, buildings, equipment, and software in the future. Management evaluates and records impairment losses or adjusts remaining lives, where applicable, based on expected utilization, projected cash flows, and recoverable values.

Maintenance and repairs are expensed as incurred. Major improvements that increase the estimated useful life of an asset are capitalized. Upon the sale or retirement of assets, recorded cost and related accumulated depreciation are removed from the accounts, and any gain or loss on disposal is reflected in operations.

Management estimates the fair value of asset retirement obligations that are conditional on a future event if the amount can be reasonably estimated. Estimates are developed through the identification of applicable legal requirements, identification of specific conditions requiring incremental cost at time of asset disposal, estimation of costs to remediate conditions, and estimation of remaining useful lives or date of asset disposal.

(h) Medical Claims Payable

The cost of health care services is recognized in the period in which services are provided. Medical claims payable consists of unpaid health care expenses to third party providers, which include an estimate of the cost of services provided to Health Plans' members by the third party providers that have been incurred but not reported. The estimate for incurred but not reported claims is based on actuarial projections of costs using historical paid claims and other relevant data. Estimates are monitored and reviewed and, as settlements are made or estimates are revised, adjustments are reflected in current operations. Such estimates are subject to the impact of changes in the regulatory environment and economic conditions, actual utilization of medical services, changes in membership and product mix, claim submission and processing patterns, and other relevant factors. Given the inherent variability of such estimates, the actual liability could differ significantly from the amounts provided. While the ultimate amount of paid claims is dependent on future developments, management is of the opinion that the reserves for claims are adequate to cover such claims.

Health Plans and Hospitals record anticipated reinsurance recoveries for high cost claims eligible for reimbursement under the Patient Protection and Affordable Care Act (PPACA) as described in *The PPACA Health Insurance Providers Fee, Reinsurance, Risk Adjustment, and Risk Corridors Programs* note. The amount recorded is an estimate as the ultimate adjudication of these claims is conducted by the government.

(i) Due to Associated Medical Groups

Due to associated medical groups consists primarily of unpaid medical expenses owed to the Medical Groups for medical services provided to members under medical services agreements with Health Plans. The cost of medical services is recognized by Health Plans in the period in which services are provided and is reflected as a component of medical and hospital services expenses.

(j) Self-Insured Risks

Costs associated with self-insured risks, primarily for professional, general, and workers' compensation liabilities, are charged to operations based upon actual and estimated claims. The portion estimated to be paid during the next year is included in current liabilities. The estimate for incurred but not reported self-insured claims is based on actuarial projections of costs using historical claims and other relevant data. Estimates are monitored and reviewed and, as settlements are made or estimates are revised, adjustments are reflected in current operations. Given the inherent variability of such estimates, the actual liability could differ significantly from the amounts provided. While the ultimate payments for self-insured claims are dependent on future developments, management is of the opinion that the reserve for self-insured risks is adequate. Insurance coverage, in excess of the per occurrence self-insured retention, has been secured with insurers or reinsurers for specified amounts for professional, general, and workers' compensation liabilities. Decisions relating to the limit and scope of the self-insured layer and the amounts of excess insurance purchased are reviewed each year, subject to management's analysis of actuarial loss projections and the price and availability of acceptable commercial insurance.

(k) Premium Deficiency Reserves

Premium deficiency reserves and the related expense are recognized when it is probable that expected future health care and maintenance costs under a group of existing contracts will exceed anticipated future premiums and reinsurance recoveries over the contract period. If applicable, premium deficiency reserves extending beyond one year are shown as a long-term liability. Expected investment income and interest expense are included in the calculation of premium deficiency reserves, as appropriate. The level at which contracts are grouped for evaluation purposes is generally by geographic region. The methods for making such estimates and for establishing the resulting reserves are reviewed and updated, and any resulting adjustments are reflected in current operations. At December 31, 2015 and 2014, premium deficiency reserves were $45 million and $87 million, respectively. Given the inherent variability of such estimates, the actual liability could differ significantly from the calculated amount.

(l) Derivative Financial Instruments

Derivative financial instruments are utilized primarily to manage the interest costs and the risk associated with changing interest rates. Health Plans and Hospitals enter into interest rate swaps with investment or commercial banks with significant experience with such instruments. In addition, certain investments include derivative products. The changes in the fair value of these derivative instruments are included in investment income - net and settlement costs are recorded as interest expense or investment income - net.

Derivative financial instruments are also utilized to manage the risk of holding equity investments, primarily to hedge downside volatility risk. Heath Plans and Hospitals enter into derivatives such as put-spread collars with similar investment or commercial banks noted above. The changes in fair value for these derivatives are included in investment income - net.

Derivative financial instruments are utilized by Health Plans' and Hospitals' investment portfolio managers. These instruments include futures, forwards, options, and swaps. The changes in fair value for these derivative financial instruments are included in investment income - net.

(m) Revenue Recognition

Members' dues revenue includes premiums from employer groups and individuals. Members' dues revenue is recognized over the period in which the members are entitled to health care services.

Health Plans estimates accrued retrospective premium adjustments for certain group health insurance contracts based on claims experience and the provisions of the contract. Health Plans records accrued retrospective premiums as an adjustment to members' dues. For the years ended December 31, 2015 and 2014, the amount of premiums written by Health Plans subject to the retrospective rating feature were $786 million and $234 million, respectively. During 2015 and 2014, revenue derived under these contracts was 1.9% and 0.6%, respectively, of total members' dues. During 2015 and 2014, retrospective dues adjustments were $(15) million and $(16) million, respectively.

Health Plans participates in certain commercial contracts, which include provisions for risk adjustment of dues premiums, based on comparative data provided by Health Plans as well as other health plan vendors participating in these same arrangements. Settlements are typically calculated and paid according to the contract provisions and final settlements are made after the contract terms expire. For both the years ended December 31, 2015 and 2014, dues subject to these private risk adjustment arrangements comprise approximately 9% of total dues premiums. For the years ended December 31, 2015 and 2014, $39 million and $9 million, respectively, have been recorded as reductions to revenue for these private risk adjustment arrangements.

The majority of Health Plans' and Hospitals' Medicare revenue is received from the Medicare Advantage Program (Part C). Revenues for Part C include capitated payments, which vary based on health status, demographic status, and other factors. Medicare revenues also include accruals for estimates resulting from changes in health risk factor scores. Such accruals are recognized when the

amounts become determinable and collection is reasonably assured. Part C revenue is finalized after all data is submitted to Medicare and the final settlement is made after the end of the year.

In addition, Medicare benefits include a voluntary prescription drug benefit (Part D). Revenues for Part D include capitated payments made from Medicare adjusted for health risk factor scores. Revenues also include amounts to reflect a portion of the health care costs for low-income Medicare beneficiaries and a risk-sharing arrangement to limit the exposure to unexpected expenses. Related accruals are recognized monthly based on cumulative experience and membership data. Part D revenue is finalized after all data is submitted to Medicare and the final settlement is made after the end of the year.

Medicare Part C and D revenue is subject to governmental audits and potential payment adjustments. The Centers for Medicare & Medicaid Services (CMS) performs coding audits to validate the supporting documentation maintained by Health Plans and its care providers.

Certain Medicare revenues are paid under cost reimbursement plans based on pre-established rates, and the final settlement is made after the end of the year. Estimates of final settlements of the cost reports are recorded by the Health Plans in current operations.

Estimates of retrospective adjustments resulting from coding audits, cost reports, and other contractual adjustments are recorded in the time period in which members are entitled to health care services. Actual retrospective adjustments may differ from initial estimates.

Premiums collected in advance are deferred and recorded as dues collected in advance or Medicare payments received in advance. Revenue is adjusted to reflect estimates of collectability, including retrospective membership adjustment trends and economic conditions. Revenue and related receivables are exclusive of charity care. A portion of revenues derived under contracts with the United States Office of Personnel Management is subject to audit and potential retrospective adjustments.

Patient services revenue is included in copays, deductibles, fees, and other revenue in the statement of operations and is recognized as services are rendered. Bad debt expense related to patient services revenue is calculated based on historical bad debt experience and recorded as an offset to patient services revenue (net of contractual allowances, charity care, and discounts).

Health Plans provides coverage to certain Medicaid members through capitated contracts with third parties. Third party Medicaid revenue is included in copays, deductibles, fees, and other revenue in the statement of operations. For the years ended December 31, 2015 and 2014, revenues related to these arrangements were $1,353 million and $730 million, respectively.

(n) Pension and Other Postretirement Benefits

Health Plans' and Hospitals' defined benefit pension and other postretirement benefit plans are actuarially evaluated and involve various assumptions. Critical assumptions include the discount rate

and the expected rate of return on plan assets, and the rate of increase for health care costs (for postretirement benefit plans other than pension), which are important elements of expense and/or liability measurement. Other assumptions involve demographic factors such as retirement age, mortality, turnover, and the rate of compensation increases. Health Plans and Hospitals evaluate assumptions annually, or when significant plan amendments occur, and modify them as appropriate. Pension and other postretirement costs are allocated over the service period of the employees in the plans.

Health Plans and Hospitals use a discount rate to determine the present value of the future benefit obligations. The discount rate is established based on rates available for high-quality fixed-income debt securities at the measurement date whose maturity dates match the expected cash flows of the retirement plans.

Differences between actual and expected plan experience and changes in actuarial assumptions, in excess of a 10% corridor around the larger of plan assets or plan liabilities, are recognized into benefits expense over the expected average future service of active participants. Prior service costs and credits arise from plan amendments and are amortized into postretirement benefits expense over the expected average future service to full eligibility of active participants.

(o) Donations and Grants Made or Received

Donations and grants made are recognized at fair value in the period in which a commitment is made, provided the payment of the donation or grant is probable and the amount is determinable. Donations or grants received, including research grants, are recognized at fair value in the period the donation or grant was committed unconditionally by the grantor or in the period the donation or grant requirements are met, if later.

(p) Use of Estimates

The preparation of these combined financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts. Allowance for uncollectible accounts receivable; estimated fair value of investments; Medicare revenue accruals; Medicare reserves; incurred but not reported medical claims payable; physicians' retirement plan liabilities; pension and other retirement liabilities; premium deficiency reserves; self-insured professional liabilities; self-insured general and workers' compensation liabilities; land, buildings, equipment, and software impairment and useful lives; investment impairment; and certain amounts accrued related to the PPACA Reinsurance, Risk Adjustment, and Risk Corridors Programs represent significant estimates. Actual results could differ materially from those estimates. As occurs from time to time, negotiations with labor partners may result in changes to compensation and benefits. These changes are reflected in the financial statements as appropriate when agreements are finalized.

(q) Reclassifications

Certain reclassifications have been made in these combined financial statements to conform 2014 information to the 2015 presentation.

(r) The PPACA Health Insurance Providers Fee, Reinsurance, Risk Adjustment, and Risk Corridors Programs

The PPACA requires Health Plans to pay a Health Insurance Providers fee that is assessed based on Health Plans' prior year net premiums as a percentage of total premiums for all U.S. health plans. The Internal Revenue Service (IRS) has provided Health Plans its final assessment of $497 million for 2015, and the amount was paid and expensed in 2015. Management has estimated the 2016 assessment on Health Plans to be approximately $500 million, which will be expensed throughout 2016.

The PPACA also includes three programs designed to mitigate health plan risk. Two are temporary and one is permanent.

The Reinsurance Program is temporary, and provides for partial reimbursement of certain high cost claims for non-grandfathered individual members, beginning in 2014 and continuing through 2016. As described in the *Medical Claims Payable* note, certain amounts have been recorded in 2015 and 2014 as expected claims reimbursements under this program. For the years ended December 31, 2015 and 2014, Health Plans has recorded $301 million and $228 million, respectively, for estimated recoveries from the Reinsurance Program. For the years ended December 31, 2015 and 2014, Health Plans has recorded $342 million and $464 million, respectively, of Reinsurance fees.

The Risk Adjustment Program is permanent, and provides for retrospective adjustment of revenue for non-grandfathered individual and small group market plans, whether inside or outside PPACA exchanges. The Risk Adjustment Program is designed such that payments to plans with higher relative risk are funded by transfers from plans with lower relative risk. For the years ended December 31, 2015 and 2014, Health Plans has recorded $11 million and $0 million, respectively, as net revenue reductions related to the Risk Adjustment Program.

The Risk Corridors Program is temporary, beginning in 2014 and continuing through 2016. This program provides for gains and losses on the individual and small group market plans to be shared with the government. For the years ended December 31, 2015 and 2014, Health Plans has recorded $66 million and $0 million, respectively, as net revenue reductions related to the Risk Corridors Program.

At December 31, the net receivables (payables) for Reinsurance recoveries, Risk Adjustment settlements, and Risk Corridor settlements were as follows (in millions):

	2015	2014
Reinsurance recoveries	$ 229	$ 228
Risk Adjustment settlements	(39)	—
Risk Corridor settlements	(5)	—
Total	$ 185	$ 228

At December 31, 2015, net receivables (payables) for Reinsurance recoveries, Risk Adjustment settlements, and Risk Corridor settlements of $229 million, $(50) million, and $(6) million, respectively, were related to the 2015 Programs. At December 31, 2015, net receivables for Reinsurance recoveries, Risk Adjustment settlements, and Risk Corridor settlements of $0 million, $11 million, and $1 million, respectively, were related to the 2014 Programs.

(s) Recently Issued Accounting Standards

During 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2013-06 *Not-for-Profit Entities (Topic 958) Services Received from Personnel of an Affiliate* (a consensus of the FASB Emerging Issues Task Force). This guidance was adopted by Health Plans and Hospitals in 2015. Management has evaluated this accounting standard and it did not have a significant effect on the combined financial statements.

In May 2014, the FASB issued ASU No. 2014-09 *Revenue from Contracts with Customers (Topic 606)*. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for Health Plans and Hospitals on January 1, 2018, as amended by ASU No. 2015-14 *Revenue from Contracts with Customers (Topic 606)*. Early application is permitted but not earlier than the original effective date of January 1, 2017. The standard permits the use of either the retrospective or cumulative effect transition method. Management is evaluating the effect that ASU No. 2014-09 will have on its combined financial statements and related disclosures. Management has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

In June 2014, the FASB issued ASU No. 2014-11 *Transfers and Servicing (Topic 860)*. The ASU changes the accounting for certain repurchase transactions and requires additional disclosures for repurchase agreements, securities lending transactions and repurchase to maturity transactions that are accounted for as secured borrowings, and certain transfers of financial assets accounted for as a sale. The new standard was adopted by Health Plans and Hospitals in 2015. Management has evaluated this accounting standard and it did not have a significant effect on the combined financial statements.

In February 2015, the FASB issued ASU No. 2015-02 *Consolidation (Topic 810)*. The amendments in this update affect reporting entities that are required to evaluate whether they should consolidate certain legal entities. The new standard is effective for Health Plans and Hospitals on January 1, 2017. Early application is permitted. The standard permits the use of either the retrospective or cumulative effect transition method. Management is evaluating the effect that ASU No. 2015-02 will have on its combined financial statements and related disclosures. Management has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

In April 2015, the FASB issued ASU No. 2015-03 *Interest - Imputation of Interest (Subtopic 835-30)*. The amendments in this update require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The new standard is effective for Health Plans and Hospitals on January 1, 2016. Early application is permitted. The standard requires the application of the retrospective transition method. Management has evaluated this accounting standard and it is not expected to have a significant effect on the combined financial statements and related disclosures.

In April 2015, the FASB issued ASU No. 2015-05 *Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40)*. The amendments in this update provide guidance to customers about whether a cloud computing arrangement includes a software license. The new standard is effective for Health Plans and Hospitals on January 1, 2016. Early application is permitted. The standard permits the use of either the prospective or retrospective transition method. Management has evaluated this accounting standard and it is not expected to have a significant effect on the combined financial statements and related disclosures. Management has selected the prospective transition method.

In July 2015, the FASB issued ASU No. 2015-11 *Inventory - Simplifying the Measurement of Inventory (Topic 330)*. The amendments in this update change the measurement principle for inventory from the lower of cost or market to lower of cost and net realizable value. The new standard is effective for Health Plans and Hospitals on January 1, 2017. Early application is permitted. The standard requires the application of the prospective transition method. Management is evaluating the effect that ASU No. 2015-11 will have on its combined financial statements and related disclosures. Management has not determined the effect of the standard on its ongoing financial reporting.

In January 2016, the FASB issued ASU No. 2016-01 *Financial Instruments - Overall (Subtopic 825-10)*. The standard requires entities to measure equity investments that are not accounted for under the equity method or do not result in consolidation to be recorded at fair value and recognize any changes in fair value to net income. Investments that qualify for a practicability exception would not require a change in accounting. The disclosure of fair value of investments held at amortized cost will no longer be required. The new standard is effective for Health Plans and Hospitals on January 1, 2019. Early application is permitted but not earlier than January 1, 2018. The standard requires the use of the cumulative effect transition method, except for equity securities without readily

determinable fair values, for which the standard requires the application of the prospective transition method. The impact of adoption will result in the change in fair value of available for sale equity securities being reflected in net income and a reduction in the fair value disclosures for certain securities carried at amortized cost.

(3) Group Health Cooperative Agreement

In December 2015, Kaiser Foundation Health Plan of Washington (KFHPW), a subsidiary of Health Plan Inc., entered into a definitive agreement to acquire and become the sole member of Group Health Cooperative (Group Health), a Washington nonprofit corporation and licensed health maintenance organization, for $1.8 billion. The agreement also requires $1 billion of capital spending and key investments in infrastructure and other improvements, subject to review and approval under KFHPW's standard capital approval process; and KFHPW expects to make $800 million of community benefit contributions over a ten year period. Group Health and Group Health Permanente, P.C. (GHP), a Washington professional services corporation, have an existing exclusive arrangement for the provision of physician and certain other medical services to Group Health enrollees. As part of the Group Health transaction, KFHPW and GHP have reached an agreement, contingent on the successful completion of the Group Health transaction, providing the terms and conditions under which GHP will continue to provide such services to Group Health enrollees after the close of the Group Health transaction, including payments to GHP of up to $200 million. The transactions are expected to close in either 2016 or 2017. Cash of $2 billion has been transferred from Hospitals to KFHPW and is restricted for purposes of completing the transactions. At December 31, 2015, this restricted asset is included in noncurrent investments in the combined financial statements.

(4) Fair Value Estimates

The carrying amounts reported in the balance sheets for cash and cash equivalents, securities lending collateral, broker receivables, accounts receivable - net, accounts payable and accrued expenses, medical claims payable, due to associated medical groups, payroll and related charges, securities lending payable, and broker payables approximate fair value.

Investments, other than alternative investments, as discussed in the *Investments* note, are reported at fair value. The fair values of investments are based on quoted market prices, if available, or estimated using quoted market prices for similar investments. If listed prices or quotes are not available, fair value is based upon other observable inputs or models that primarily use market-based or independently sourced market parameters as inputs. In addition to market information, models also incorporate transaction details such as maturity. Fair value adjustments, including credit, liquidity, and other factors, are included, as appropriate, to arrive at a fair value measurement. Certain investments are illiquid and are valued based on the most current information available, which may be less current than the date of these combined financial statements.

The carrying value of alternative investments, which include absolute return, risk parity, and private equity, is reported under the equity method, which management believes to approximate fair value. The

fair values of alternative investments have been estimated by management based on all available data, including information provided by fund managers or the general partners. The underlying securities within absolute return investments are typically valued using quoted prices for identical or similar instruments within active and inactive markets. The underlying holdings within private equity investments are valued based on recent transactions, operating results, and industry and other general market conditions.

Health Plans and Hospitals utilize a three-level valuation hierarchy for fair value measurements. An instrument's categorization within the hierarchy is based upon the lowest level of input that is significant to the fair value measurement. For instruments classified in level 1 of the hierarchy, valuation inputs are quoted prices for identical instruments in active markets at the measurement date. For instruments classified in level 2 of the hierarchy, valuation inputs are directly observable but do not qualify as level 1 inputs. Examples of level 2 inputs include: quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in inactive markets; other observable inputs such as interest rates and yield curves observable at commonly quoted intervals, volatilities, prepayment speeds, loss severities, credit risks, and default rates; and market-correlated inputs that are derived principally from or corroborated by observable market data. For instruments classified in level 3 of the hierarchy, valuation inputs are unobservable inputs for the instrument. Level 3 inputs incorporate assumptions about the factors that market participants would use in pricing the instrument.

The fair value of long-term debt is based on level 2 inputs for debt with similar risk, terms, and remaining maturities. At December 31, 2015 and 2014, the carrying amount of long-term debt totaled $6.9 billion and $7.0 billion, respectively. At December 31, 2015 and 2014, the estimated fair value of long-term debt was approximately $7.1 billion and $7.2 billion, respectively.

At December 31, 2015 and 2014, Health Plans and Hospitals held derivative financial instruments including interest rate swaps, as well as futures, swaps, and forwards held within investment portfolios. The estimated fair values of derivative instruments were determined using level 2 inputs, including available market information and valuation methodologies, primarily discounted cash flows. Additional description and the fair value of derivative instruments are contained in the *Derivative Instruments* note.

(5) Investments

Management's methods for estimating fair value of financial instruments are discussed in the *Fair Value Estimates* note.

At December 31, 2015, the estimated fair value of current investments by level was as follows (in millions):

	Quoted prices in active markets for identical assets level 1	Significant other observable inputs level 2	Significant unobservable inputs level 3	Total
U.S. equity securities	$ 31	$ —	$ —	$ 31
Debt securities issued by the U.S. government	—	1,500	—	1,500
Debt securities issued by U.S. government agencies and corporations	—	48	—	48
Debt securities issued by U.S. states and political subdivisions of states	—	56	—	56
Foreign government debt securities	—	40	—	40
U.S. corporate debt securities	—	2,003	—	2,003
Foreign corporate debt securities	—	966	—	966
U.S. agency mortgage-backed securities	—	660	—	660
Non-U.S. agency mortgage-backed securities	—	351	—	351
Other asset-backed securities	—	593	—	593
Short-term investment funds	—	297	—	297
Other	—	9		9
Total	$ 31	$ 6,523	$ —	$ 6,554

At December 31, 2015, the estimated fair value of noncurrent investments by level was as follows (in millions):

	Quoted prices in active markets for identical assets level 1	Significant other observable inputs level 2	Significant unobservable inputs level 3	Total
U.S. equity securities	$ 3,538	$ 10	$ —	$ 3,548
Foreign equity securities	2,888	1,281	—	4,169
Global equity funds	—	751	—	751
Debt securities issued by the U.S. government	—	1,139	—	1,139
Debt securities issued by U.S. government agencies and corporations	—	117	—	117
Debt securities issued by U.S. states and political subdivisions of states	—	184	—	184
Foreign government debt securities	—	1,101	—	1,101
U.S. corporate debt securities	—	3,322	—	3,322
Foreign corporate debt securities	—	1,407	—	1,407
U.S. agency mortgage-backed securities	—	663	—	663
Non-U.S. agency mortgage-backed securities	—	179	11	190
Other asset-backed securities	—	196	—	196
Short-term investment funds	—	2,613	—	2,613
Other	82	429	1	512
Alternative investments:				
Absolute return	—	1,272	964	2,236
Private equity	—	—	3,234	3,234
Risk parity	—	—	807	807
Total	$ 6,508	$ 14,664	$ 5,017	$ 26,189

At December 31, 2014, the estimated fair value of current investments by level was as follows (in millions):

	Quoted prices in active markets for identical assets level 1	Significant other observable inputs level 2	Significant unobservable inputs level 3	Total
U.S. equity securities	$ 35	$ —	$ —	$ 35
Debt securities issued by the U.S. government	—	1,641	—	1,641
Debt securities issued by U.S. government agencies and corporations	—	116	—	116
Debt securities issued by U.S. states and political subdivisions of states	—	36	—	36
Foreign government debt securities	—	14	—	14
U.S. corporate debt securities	—	1,807	—	1,807
Foreign corporate debt securities	—	1,034	—	1,034
U.S. agency mortgage-backed securities	—	371	—	371
Non-U.S. agency mortgage-backed securities	—	476	—	476
Other asset-backed securities	—	528	—	528
Short-term investment funds	—	332	—	332
Total	$ 35	$ 6,355	$ —	$ 6,390

At December 31, 2014, the estimated fair value of noncurrent investments by level was as follows (in millions):

	Quoted prices in active markets for identical assets level 1	Significant other observable inputs level 2	Significant unobservable inputs level 3	Total
U.S. equity securities	$ 3,952	$ —	$ —	$ 3,952
Foreign equity securities	2,926	1,502	26	4,454
Global equity funds	—	761	—	761
Debt securities issued by the U.S. government	—	1,335	—	1,335
Debt securities issued by U.S. government agencies and corporations	—	220	—	220
Debt securities issued by U.S. states and political subdivisions of states	—	250	—	250
Foreign government debt securities	—	1,164	—	1,164
U.S. corporate debt securities	1	4,190	—	4,191
Foreign corporate debt securities	—	1,662	—	1,662
U.S. agency mortgage-backed securities	—	1,024	—	1,024
Non-U.S. agency mortgage-backed securities	—	249	12	261
Other asset-backed securities	—	399	—	399
Short-term investment funds	—	870	—	870
Other	200	400	2	602
Alternative investments:				
Absolute return	—	1,435	881	2,316
Private equity	—	—	1,961	1,961
Risk parity	—	—	659	659
Total	$ 7,079	$ 15,461	$ 3,541	$ 26,081

At December 31, 2015, debt and equity securities available-for-sale were as follows (in millions):

	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
U.S. equity securities	$ 3,031	$ 548	$ —	$ 3,579
Foreign equity securities	3,657	512	—	4,169
Global equity funds	506	245	—	751
Debt securities issued by the U.S. government	2,630	9	—	2,639
Debt securities issued by U.S. government agencies and corporations	158	7	—	165
Debt securities issued by U.S. states and political subdivisions of states	214	26	—	240
Foreign government debt securities	1,109	32	—	1,141
U.S. corporate debt securities	5,225	100	—	5,325
Foreign corporate debt securities	2,347	26	—	2,373
U.S. agency mortgage-backed securities	1,311	12	—	1,323
Non-U.S. agency mortgage-backed securities	534	7	—	541
Other asset-backed securities	782	7	—	789
Short-term investment funds	2,910	—	—	2,910
Other	521	—	—	521
Total	$ 24,935	$ 1,531	$ —	$ 26,466

At December 31, 2014, debt and equity securities available-for-sale were as follows (in millions):

	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
U.S. equity securities	$ 3,021	$ 966	$ —	$ 3,987
Foreign equity securities	3,903	551	—	4,454
Global equity funds	466	295	—	761
Debt securities issued by the U.S. government	2,945	31	—	2,976
Debt securities issued by U.S. government agencies and corporations	326	10	—	336
Debt securities issued by U.S. states and political subdivisions of states	239	47	—	286
Foreign government debt securities	1,127	51	—	1,178
U.S. corporate debt securities	5,750	248	—	5,998
Foreign corporate debt securities	2,645	51	—	2,696
U.S. agency mortgage-backed securities	1,365	30	—	1,395
Non-U.S. agency mortgage-backed securities	721	16	—	737
Other asset-backed securities	924	3	—	927
Short-term investment funds	1,202	—	—	1,202
Other	577	25	—	602
Total	$ 25,211	$ 2,324	$ —	$ 27,535

At December 31, available-for-sale debt securities by contractual maturity and mortgage-backed and other asset-backed debt securities were as follows (in millions):

	2015		2014	
	Amortized cost	Fair value	Amortized cost	Fair value
Due in one year or less	$ 3,585	$ 3,587	$ 2,371	$ 2,376
Due after one year through five years	5,852	5,881	6,676	6,735
Due after five years through ten years	2,536	2,567	2,797	2,848
Due after ten years	3,141	3,279	2,967	3,315
U.S. agency mortgage-backed securities	1,311	1,323	1,365	1,395
Non-U.S. agency mortgage-backed securities	534	541	721	737
Other asset-backed securities	782	789	924	927
Total	$ 17,741	$ 17,967	$ 17,821	$ 18,333

For the year ended December 31, 2015, the reconciliation of investments with fair value measurements using significant unobservable inputs (level 3) was as follows (in millions):

	Equity securities	Debt securities	Alternative investments	Total
Beginning balance	$ 26	$ 14	$ 3,501	$ 3,541
Transfers out of level 3	(28)	—	—	(28)
Total net gains:				
Realized	1	1	(42)	(40)
Unrealized	6	(1)	—	5
Purchases	—	—	1,834	1,834
Sales	(5)	—	(288)	(293)
Settlements	—	(2)	—	(2)
Ending balance	$ —	$ 12	$ 5,005	$ 5,017
Total realized and unrealized year-to-date net gains (losses) related to assets held at December 31, 2015	$ 5	$ —	$ (42)	$ (37)

For the year ended December 31, 2014, the reconciliation of investments with fair value measurements using significant unobservable inputs (level 3) was as follows (in millions):

	Equity securities	Debt securities	Alternative investments	Total
Beginning balance	$ 17	$ 23	$ 2,540	$ 2,580
Transfers out of level 3	—	(8)	(15)	(23)
Total net gains (losses):				
Realized	(4)	1	181	178
Unrealized	(2)	—	3	1
Purchases	34	—	1,029	1,063
Sales	(19)	—	(237)	(256)
Settlements	—	(2)	—	(2)
Ending balance	$ 26	$ 14	$ 3,501	$ 3,541
Total realized and unrealized year-to-date net gains (losses) related to assets held at December 31, 2014	$ (5)	$ 1	$ 170	$ 166

Transfers between fair value input levels, if any, are recorded at the end of the reporting period. Transfers between fair value input levels occur when valuation inputs used to record or disclose assets or liabilities change from one level of the valuation hierarchy to another. During the years ended December 31, 2015 and 2014, there were no transfers between assets with inputs with quoted prices in active markets for identical assets (level 1) and assets with inputs with significant other observable inputs (level 2).

Investments include specific funds held in trust accounts related to collateral requirements for certain reinsurance agreements. At December 31, 2015 and 2014, the values of these funds were $53 million and $30 million, respectively.

Absolute return investments use advanced investment strategies, including derivatives, to generate positive long-term risk adjusted returns. Private equity investments consist of funds that make direct investments in private companies. Risk parity funds use risk as the primary factor to allocate investments among asset classes. Management meets with alternative investment fund managers periodically to assess portfolio performance and reporting and exercises oversight over fund managers. At December 31, 2015, Hospitals had original commitments related to alternative investments of $6.7 billion, of which $3.7 billion was invested, leaving $3.0 billion of remaining commitments. At December 31, 2014, Hospitals had original commitments related to alternative investments of $4.7 billion, of which $2.3 billion was invested, leaving $2.4 billion of remaining commitments.

For the years ended December 31, investment income - net was comprised of the following (in millions):

	2015	2014
Other-than-temporary impairment	$ (1,426)	$ (657)
Recognized gains	1,401	1,123
Recognized losses	(299)	(206)
Income from equity method alternative investments	152	317
Interest, dividends, and other income - net	771	710
Derivative income	136	132
Total investment income - net	735	1,419
Less investment income included in operating income	(435)	(318)
Investment income - net	$ 300	$ 1,101

For the years ended December 31, 2015 and 2014, Health Plans and Hospitals recorded impairment of certain investments in accordance with the policy described in the *Summary of Significant Accounting Policies - Investments* note. During 2015 and 2014, there was $1 million and $5 million, respectively, of impairment of alternative investments.

Absolute return, risk parity, and private equity investments include redemption restrictions. Absolute return and risk parity investments require 10 to 90 day written notice of intent to withdraw and are often subject to the approval and capital requirements of the fund manager. Absolute return and risk parity investments of $668 million are subject to lock-up periods of up to 3 years. Private equity agreements do not include provisions for redemption. Distributions will be received as the underlying investments of the funds are liquidated, which is expected over the next 11 years.

Certain debt and equity investment funds have a redemption period of greater than 10 days. Debt and equity investment funds of $1.6 billion are redeemable between 10 and 30 days. Equity investment funds of $264 million have a redemption period of between 30 days and 1 year.

(6) Derivative Instruments

(a) Interest Rate Swaps

At December 31, 2015 and 2014, Health Plans and Hospitals had 11 agreements to manage interest rate fluctuations (Interest Rate Swaps) with a total notional amount of $1.2 billion for each period. At December 31, 2015 and 2014, the fair values of these agreements were $(274) million and $(267) million, respectively, and were recorded in other long-term liabilities. For both the years ended December 31, 2015 and 2014, Health Plans and Hospitals recorded $35 million in interest expense relating to the Interest Rate Swaps. For the years ended December 31, 2015 and 2014, net changes in fair values totaled $(7) million and $(107) million, respectively, and were recorded in investment income - net.

These derivatives contain reciprocal provisions whereby if Health Plans' and Hospitals' or the counterparties' credit rating was to decline to certain levels, provisions would be triggered requiring Health Plans and Hospitals or the counterparties to provide certain collateral. At December 31, 2015 and 2014, no collateral was required to be posted by either Health Plans and Hospitals or the counterparties.

(b) Derivatives Held in Investment Portfolios

At December 31, 2015 and 2014, Health Plans' and Hospitals' portfolio managers held $(3) million and $38 million, respectively, of futures, forwards, options, and swaps to attempt to protect investments against volatility. For the years ended December 31, 2015 and 2014, net changes in fair values totaled $(9) million and $25 million, respectively, and were recorded in investment income - net. For the years ended December 31, 2015 and 2014, gains resulting from derivative settlements totaled $152 million and $214 million, respectively, and were recorded in investment income - net.

(c) Information on Derivative Gain (Loss) and Fair Value

Management's methods for estimating fair value of financial instruments are discussed in the *Fair Value Estimates* note.

Information on Derivative Gain (Loss) Mark-to-Market Valuation Recognized in Income

(In millions)

Derivatives not designated as hedging instruments	Statement of operations category	Gain (loss) recognized in income on derivatives for the years ended December 31, 2015	2014
Interest rate swaps - related to debt	Investment income - net	$ (7)	$ (107)
Interest rate swaps - other	Investment income - net	1	(14)
Options, rights, and warrants	Investment income - net	19	(1)
Futures and forwards	Investment income - net	(29)	40
		$ (16)	$ (82)

Information on Derivative Settlement Costs Recognized in Income

(In millions)

Derivatives not designated as hedging instruments	Statement of operations category	Gain (loss) recognized in income on derivatives for the years ended December 31, 2015	2014
Interest rate swaps - related to debt	Interest expense	$ (35)	$ (35)
Interest rate swaps - other	Investment income - net	(51)	7
Futures and forwards	Investment income - net	202	201
Options, rights, and warrants	Investment income - net	1	6
		$ 117	$ 179

Information on Fair Value of Derivative Instruments - Assets

(In millions)

Derivatives not designated as hedging instruments	Balance sheet category	Fair value at December 31, 2015	2014
Interest rate swaps - other	Noncurrent investments	$ 13	$ 15
Futures and forwards	Noncurrent investments	33	67
Options, rights, and warrants	Noncurrent investments	1	3
		$ 47	$ 85

Information on Fair Value of Derivative Instruments - Liabilities

(In millions)

Derivatives not designated as hedging instruments	Balance sheet category	Fair value at December 31, 2015	2014
Interest rate swaps - related to debt	Other long-term liabilities	$ 274	$ 267
Interest rate swaps - other	Other long-term liabilities	22	21
Futures and forwards	Other long-term liabilities	25	21
Options, rights, and warrants	Other long-term liabilities	3	5
		$ 324	$ 314

(7) Accounts Receivable - net

At December 31, accounts receivable - net were as follows (in millions):

	2015	2014
Members' dues	$ 709	$ 697
Patient services	390	367
Medicare	317	283
Reinsurance recoveries	231	228
Risk Adjustment receivables	66	—
Other	399	425
	2,112	2,000
Allowances for bad debt	(146)	(159)
Total	$ 1,966	$ 1,841

(8) Inventories and Other Current Assets

At December 31, inventories and other current assets were as follows (in millions):

	2015	2014
Inventories - net	$ 871	$ 832
Prepaid expenses	481	317
Other	75	59
Total	$ 1,427	$ 1,208

(9) Land, Buildings, Equipment, and Software - net

Land, buildings, equipment, and software - net were as follows (in millions):

	2015	2014
Land	$ 1,821	$ 1,777
Buildings and improvements	30,761	29,754
Furniture, equipment, and software	10,791	10,257
Construction and software development in progress	1,920	1,500
	45,293	43,288
Accumulated depreciation and amortization	(21,511)	(19,804)
Total	$ 23,782	$ 23,484

Health Plans and Hospitals capitalize interest costs on borrowings incurred during the construction, upgrade, or development of qualifying assets. Capitalized interest is added to the cost of the underlying assets and is depreciated or amortized over the useful lives of the assets. During 2015 and 2014, Health Plans and Hospitals capitalized $28 million and $36 million, respectively, of interest in connection with various capital projects.

Asset retirement obligations relate primarily to the following: leased building restoration, building materials containing asbestos, leaded wall shielding, storage tanks (above ground and below ground), chillers or cooling tower chemicals, mercury in large fixed-components, and hard drives requiring data wiping prior to disposal. At December 31, 2015 and 2014, the liability for asset retirement obligations was $85 million and $84 million, respectively. During 2015 and 2014, amortization and other adjustments of the associated assets totaled $4 million and $18 million, respectively. At December 31, 2015 and 2014, the unamortized asset related to these retirement obligations was $13 million and $9 million, respectively.

(10) Medical Claims Payable

For the years ended December 31, activity in the liability for medical claims payable was as follows (in millions):

	2015	2014
Balances at January 1	$ 1,393	$ 1,260
Incurred related to:		
Current year	8,342	7,453
Prior years	(33)	(83)
Total incurred	8,309	7,370
Paid related to:		
Current year	6,795	6,277
Prior years	1,157	960
Total paid	7,952	7,237
Balances at December 31	$ 1,750	$ 1,393

Amounts incurred related to prior years vary from previously estimated liabilities as the claims are ultimately adjudicated and paid. Liabilities are reviewed and revised as information regarding actual claims payments becomes known. Negative amounts reported for incurred related to prior years result from claims being adjudicated and paid for amounts less than originally estimated.

(11) Other Liabilities

At December 31, other current liabilities were as follows (in millions):

	2015	2014
Self-insured risks	$ 393	$ 376
Dues collected in advance	628	568
Medicare liabilities	45	37
Postretirement benefits	—	80
Physicians' retirement plan liability	171	155
TBA commitments	149	141
Other	641	402
Total	$ 2,027	$ 1,759

At December 31, other long-term liabilities were as follows (in millions):

	2015	2014
Self-insured risks	$ 1,500	$ 1,451
Derivatives liability	324	314
Due to associated medical groups	289	294
Other	305	331
Total	$ 2,418	$ 2,390

(12) Debt

At December 31, debt was as follows (in millions):

	2015	2014
Tax-exempt revenue bonds and taxable bonds and notes:		
0.01% to 2.00% variable rate due through 2052	$ 4,097	$ 4,114
3.60% to 5.25% fixed rate due through 2045	3,497	3,506
Others at various rates due through 2026	2	2
Total	$ 7,596	$ 7,622
Other current debt:		
Commercial paper	$ 654	$ 654
Current portion of long-term debt	121	18
Long-term debt subject to short-term remarketing arrangements - net	732	1,445
Long-term debt classified as a long-term liability	6,089	5,505
Total	$ 7,596	$ 7,622

At both December 31, 2015 and 2014, repurchase of variable rate bonds totaling $3.4 billion may be required at earlier than stated maturity. These bonds may be remarketed rather than repurchased. Health Plans and Hospitals have provided self liquidity for the variable rate demand bonds with put options. Additionally, at December 31, 2015 and 2014, management had the ability to finance the acquisition of up to $2.4 billion and $1.5 billion, respectively, of any unremarketed bonds that are put, using available credit facilities. At December 31, 2015 and 2014, $0.7 billion and $1.4 billion, respectively, of these variable rate demand bonds were classified in current liabilities. At December 31, 2015 and 2014, these amounts were net of available long-term credit facilities of $2.4 billion and $1.5 billion, respectively.

At December 31, 2015 and 2014, $52 million and $60 million, respectively, of the above tax-exempt fixed-rate revenue bonds represented a net unamortized premium balance.

Scheduled principal payments for each of the next five years and thereafter considering obligations subject to short-term remarketing as due according to their long-term amortization schedule, except as described below, were as follows (in millions):

2016	$	775
2017		18
2018		18
2019		246
2020		18
Thereafter		6,469
Total	$	7,544

At December 31, 2015, Hospitals had certain bonds that require mandatory tender by the holder on a date certain as follows: $205 million in 2016 and $275 million in 2017. Hospitals intends to remarket these bonds until final maturity of the bonds.

Credit Facility

Hospitals' credit facility of $2.4 billion terminates in September 2020. Various interest rate options are available under this facility. Any revolving borrowings mature on the termination date. Hospitals pays facility fees, which range from 0.05% to 0.15% per annum, depending upon Hospitals' long-term senior unsecured debt rating. At December 31, 2015, the facility fee was at an annual rate of 0.06%. At December 31, 2015 and 2014, no amounts were outstanding under this credit facility.

Hospitals' revolving credit facility contains financial covenants. Under the terms of this facility, Hospitals is required to maintain a ratio of total debt to capital, as defined.

Taxable Commercial Paper Program

Hospitals maintains a commercial paper program providing for the issuance of up to $1.5 billion in aggregate maturity value of short-term indebtedness. The commercial paper is issued in denominations of $100,000 and will bear such interest rates, if interest-bearing, or will be sold at such discount from their face amounts, as agreed upon by Hospitals and the dealer acting in connection with the commercial paper program. The commercial paper may be issued with varying maturities up to a maximum of 270 days from the date of issuance. At both December 31, 2015 and 2014, commercial paper of $654 million was outstanding under this program and is included within other current debt.

(13) Pension Plans

(a) Defined Benefit Plan

Health Plans and Hospitals have a defined benefit pension plan (Plan) covering substantially all their employees. Benefits are based on age at retirement, years of credited service, and average

compensation for a specified period prior to retirement. Contributions are intended to provide not only for benefits attributed to service to date but also for those expected to be earned in the future.

For financial reporting purposes, the projected unit credit method is used. At December 31, 2015 and 2014, substantially all pension fund assets were held in a group trust. At December 31, 2015 and 2014, the trust's assets were invested primarily in fixed-income and equity securities, with approximately 22% and 18% of trust assets, net of liabilities, respectively, invested in alternative investments.

At December 31, the funded status of the Plan was as follows (in millions):

	2015	2014
Change in projected benefit obligation (PBO):		
Benefit obligation at beginning of year	$ 16,361	$ 12,964
Service cost	1,130	879
Interest cost	713	646
Plan amendments	118	1
Net actuarial loss (gain)	(1,137)	2,567
Benefits paid	(649)	(696)
Benefit obligation at end of year	$ 16,536	$ 16,361
Accumulated benefit obligation at end of year	$ 12,846	$ 12,453
Change in Health Plans' and Hospitals' share of trust assets:		
Fair value of plan assets at beginning of year	$ 9,374	$ 8,503
Actual return on plan assets	(165)	627
Contributions	1,589	940
Benefits paid	(649)	(696)
Fair value of plan assets at end of year	$ 10,149	$ 9,374
Funded status	$ (6,387)	$ (6,987)
Amounts recognized in the balance sheet consist of:		
Noncurrent assets	$ —	$ —
Current liabilities	—	—
Pension and other retirement liabilities	(6,387)	(6,987)
	$ (6,387)	$ (6,987)
Amounts recognized in net worth:		
Net actuarial loss	$ 4,701	$ 5,381
Prior service cost	113	6
	$ 4,814	$ 5,387

The measurement date used to determine pension valuations was December 31.

For the years ended December 31, pension expense was as follows (in millions):

	2015	2014
Service cost	$ 1,130	$ 879
Interest cost	713	646
Expected return on plan assets	(678)	(610)
Amortization of net actuarial loss	386	173
Amortization of prior service cost	11	15
Net pension expense	1,562	1,103
Other changes in plan assets and PBO recognized in net worth:		
Net actuarial loss (gain)	(294)	2,550
Prior service cost	118	1
Amortization of net actuarial loss	(386)	(173)
Amortization of prior service cost	(11)	(15)
Total recognized in net worth	(573)	2,363
Total recognized in net periodic benefit cost and net worth	$ 989	$ 3,466

During 2016, $200 million and $15 million in estimated net actuarial loss and prior service cost, respectively, will be amortized from net worth into net pension expense.

Actuarial assumptions used were as follows:

	2015	2014
Weighted average discount rate at January 1 for calculating pension expense	4.25%	5.15%
Weighted average discount rate for calculating December 31 PBO	4.70%	4.25%
Weighted average salary scale for calculating pension expense	4.20%	4.60%
Weighted average salary scale for calculating December 31 PBO	4.20%	4.20%
Expected long-term rate of return on plan assets for calculating pension expense	7.25%	7.25%

During 2016, management expects to contribute approximately $1.0 billion to the Plan.

The following benefit payments, which reflect expected future service, are expected to be paid (in millions):

2016	$	648
2017		721
2018		809
2019		892
2020		983
2021 - 2025		5,997

Explanation of Investment Strategies and Policies

A total return investment approach is employed for the Plan whereby the Plan invests in a mix of equity, fixed-income, and alternative asset classes to maximize the long-term return of plan assets for a prudent level of risk. The intent of this strategy is to minimize plan expenses by outperforming plan liabilities over the long run. Risk tolerance is established through consideration of plan liabilities, plan funded status, and corporate financial condition. The investment portfolio will consist over time of a varying but diversified blend of equity, fixed-income, and alternative investments. Diversification includes such factors as geographic location, equity capitalization size and style, placement in the capital structure, and security type. Investment risk is measured and monitored on an ongoing basis through annual liability measurements, periodic asset/liability studies, and quarterly investment portfolio reviews. The Plan's investment policy has restrictions relating to credit quality, industry/sector concentration, duration, concentration of ownership, and use of derivatives.

Capital Market Assumption Methodology

To determine the long-term rate of return assumption for plan assets, management incorporates historical relationships among the various asset classes and subclasses to be accessed over the investment horizon. Management's intent is to maximize portfolio efficiency. This will be accomplished by seeking the highest returns prudently available among the available asset classes. Overall portfolio volatility is managed through diversification among asset classes. Current market factors such as inflation and interest rates are evaluated before long-term capital market assumptions are determined. From time to time, management reviews its long-term investment strategy and reconciles that strategy with the long-term liabilities of the Plan. This asset-liability study produces a range of expected returns over medium and long-term time periods. Those intermediate and long-term investment projections form the basis for the expected long-term rate of return on assets.

At December 31, 2015, the estimated fair value of total pension trust assets - net by level was as follows (in millions):

	Quoted prices in active markets for identical assets level 1	Significant other observable inputs level 2	Significant unobservable inputs level 3	Total
Assets:				
Cash and cash equivalents	$ 110	$ 1,082	$ —	$ 1,192
Broker receivables	—	156	—	156
Securities lending collateral	—	1,332	—	1,332
U.S. equity securities	4,219	365	—	4,584
Foreign equity securities	4,125	1,616	—	5,741
Global equity funds	—	187	—	187
Debt securities issued by the U.S. government	—	841	—	841
Debt securities issued by U.S. government agencies and corporations	—	70	—	70
Debt securities issued by U.S. states and political subdivisions of states	—	199	—	199
Foreign government debt securities	—	486	—	486
U.S. corporate debt securities	—	3,722	—	3,722
Non-U.S. corporate debt securities	—	957	—	957
U.S. agency mortgage-backed securities	—	159	—	159
Non-U.S. agency mortgage-backed securities	—	40	—	40
Other	1	569	—	570
Alternative investments:				
Absolute return	—	900	1,249	2,149
Private equity	—	—	2,339	2,339
Risk parity	—	—	597	597
Total assets	8,455	12,681	4,185	25,321
Liabilities:				
Broker payables	—	282	—	282
Securities lending payable	—	1,332	—	1,332
Other liabilities	12	117	—	129
Total liabilities	12	1,731	—	1,743
Fair value of pension trust assets - net	$ 8,443	$ 10,950	$ 4,185	$ 23,578

At December 31, 2015, Health Plans' and Hospitals' share of pension trust assets was 43.0%, or $10.1 billion. The remaining share of pension trust assets is for Medical Groups and a related party associated with Medical Groups.

At December 31, 2014, the estimated fair value of total pension trust assets - net by level was as follows (in millions):

	Quoted prices in active markets for identical assets level 1	Significant other observable inputs level 2	Significant unobservable inputs level 3	Total
Assets:				
Cash and cash equivalents	$ 82	$ 430	$ —	$ 512
Broker receivables	—	212	—	212
Securities lending collateral	—	1,593	—	1,593
U.S. equity securities	4,166	291	—	4,457
Foreign equity securities	4,092	1,762	—	5,854
Global equity funds	—	438	—	438
Debt securities issued by the U.S. government	—	718	—	718
Debt securities issued by U.S. government agencies and corporations	—	93	—	93
Debt securities issued by U.S. states and political subdivisions of states	—	213	—	213
Foreign government debt securities	—	537	—	537
U.S. corporate debt securities	—	3,955	—	3,955
Non-U.S. corporate debt securities	—	1,113	—	1,113
U.S. agency mortgage-backed securities	—	173	—	173
Non-U.S. agency mortgage-backed securities	—	53	—	53
Other	1	621	—	622
Alternative investments:				
Absolute return	—	897	1,118	2,015
Private equity	—	—	1,603	1,603
Risk parity	—	—	382	382
Total assets	8,341	13,099	3,103	24,543
Liabilities:				
Broker payables	—	293	—	293
Securities lending payable	—	1,593	—	1,593
Other liabilities	15	160	—	175
Total liabilities	15	2,046	—	2,061
Fair value of pension trust assets - net	$ 8,326	$ 11,053	$ 3,103	$ 22,482

At December 31, 2014, Health Plans' and Hospitals' share of pension trust assets was 41.7%, or $9.4 billion. The remaining share of pension trust assets is for Medical Groups and a related party associated with Medical Groups.

For the year ended December 31, 2015, the reconciliation of assets with fair value measurements using significant unobservable inputs (level 3) was as follows (in millions):

	Alternative investments
Beginning balance	$ 3,103
Transfers into level 3	—
Changes related to actual return on plan assets	22
Purchases, sales, and settlements - net	1,060
Ending balance	$ 4,185
Total year-to-date net gains related to assets held at December 31, 2015	$ 21

For the year ended December 31, 2014, the reconciliation of assets with fair value measurements using significant unobservable inputs (level 3) was as follows (in millions):

	Debt securities	Alternative investments	Total
Beginning balance	$ 3	$ 2,014	$ 2,017
Transfers into level 3	—	—	—
Changes related to actual return on plan assets	—	218	218
Purchases, sales, and settlements - net	(3)	871	868
Ending balance	$ —	$ 3,103	$ 3,103
Total year-to-date net gains related to assets held at December 31, 2014	$ —	$ 218	$ 218

During the years ended December 31, 2015 and 2014, there were no significant transfers of assets with inputs with quoted prices in active markets for identical assets (level 1) and assets with inputs with significant other observable inputs (level 2).

The target asset allocation and expected long-term rate of return on assets (ELTRA) for calculating pension expense were as follows:

	2015 and 2014 target range	2015 and 2014 ELTRA
Cash and cash equivalents	0%-3%	3.00%
Equity securities	43%-55%	8.65%
Debt securities	28%-45%	5.50%
Alternative investments	10%-25%	7.60%
Total	100%	7.25%

Alternative investments, which include absolute return, risk parity, and private equity, held in the pension trust are reported at net asset value as a practical expedient for fair value. Absolute return investments use advanced investment strategies, including derivatives, to generate positive long-term risk adjusted returns. Private equity investments consist of funds that make direct investments in private companies. Risk parity funds use risk as the primary factor to allocate investments among asset classes. At December 31, 2015, the trust had original commitments related to alternative investments of $5.4 billion, of which $2.4 billion was invested, leaving $3.0 billion of remaining commitments. At December 31, 2014, the trust had original commitments related to alternative investments of $3.8 billion, of which $1.5 billion was invested, leaving $2.3 billion of remaining commitments.

Absolute return, risk parity, and private equity investments include redemption restrictions. Absolute return and risk parity investments require 10 to 90 day written notice of intent to withdraw and are often subject to the approval and capital requirements of the fund manager. Absolute return and risk parity investments of $663 million are subject to lock-up periods of up to 3 years. Private equity agreements do not include provisions for redemption. Distributions will be received as the underlying investments of the funds are liquidated, which is expected over the next 11 years.

Certain debt and equity investment funds have a redemption period of greater than 10 days. Debt and equity investment funds of $1.4 billion are redeemable between 10 and 30 days. Equity investment funds of $149 million have a redemption period of up to 120 days.

(b) Defined Contribution Plans

Health Plans and Hospitals have defined contribution plans for eligible employees. Employer contributions and costs are typically based on a percentage of covered employees' eligible compensation. During 2015 and 2014, there were no required employee contributions. For the years ended December 31, 2015 and 2014, plan expense, primarily employer contributions, was $247 million and $253 million, respectively.

(c) Multi-Employer Plans

Health Plans and Hospitals participate in a number of multi-employer defined benefit pension plans under the terms of collective bargaining agreements that cover some union-represented employees. Some risks of participating in these multi-employer plans that differ from single-employer plans include:

- Assets contributed to the multi-employer plan by one employer may be used to provide benefits to employees of other participating employers.
- If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.
- Employers that choose to stop participating in a multi-employer plan may be required to pay the plan an amount based on the underfunded status of the plan, referred to as a withdrawal liability.

Health Plans' and Hospitals' participation in these plans for the annual period ended December 31, 2015 is outlined in the table below. The "EIN/PN" column provides the Employee Identification Number (EIN) and the three-digit plan number (PN), if applicable. Unless otherwise noted, the most recent Pension Protection Act (PPA) zone status available in 2015 and 2014 is for the plan's year-end in 2014 and 2013, respectively. The zone status is based on information that Health Plans and Hospitals obtained from publicly available information provided by the United States Department of Labor. Among other factors, plans in the red zone are generally less than 65% funded, plans in the yellow zone are between 65% and 80% funded, and plans in the green zone are at least 80% funded. The "FIP/RP Status Pending/Implemented" column indicates plans for which a financial improvement plan (FIP) or a rehabilitation plan (RP) is either pending or has been implemented. The "Health Plans' and Hospitals' Contributions to Plan Exceeded More Than 5% of Total Contributions" columns represent those plans where Health Plans and Hospitals were listed in the plans' Forms 5500 as providing more than 5% of the total contributions for the plan years listed. The last column lists the expiration dates of the collective bargaining agreements to which the plans are subject. There have been no significant changes that affect the comparability of 2015 and 2014 employer expense.

KAISER FOUNDATION HEALTH PLAN, INC. AND SUBSIDIARIES AND KAISER FOUNDATION HOSPITALS AND SUBSIDIARIES

Notes to Combined Financial Statements

December 31, 2015 and 2014

Pension Fund	EIN-PN	Pension Protection Act Zone Status 2015	Pension Protection Act Zone Status 2014	FIP/RP Status Pending / Implemented	(in millions) Health Plans' and Hospitals' Contributions December 31, 2015	(in millions) Health Plans' and Hospitals' Contributions December 31, 2014	Surcharge Imposed	Health Plans' and Hospitals' Contributions to Plan Exceeded More Than 5% of Total Contributions [(1)] 2014	Health Plans' and Hospitals' Contributions to Plan Exceeded More Than 5% of Total Contributions [(1)] 2013	Expiration Date of Collective Bargaining Agreement
IUOE Stationary Engineers Local 39 Pension Fund	946118939 -001	Green	Green	N/A	$ 10	$ 10	No	Yes	Yes	9/17/2018
Southern California United Food and Commercial Workers Unions and Drug Employers Pension Fund	516029925 -001	Red	Red	Implemented	5	4	Yes	Yes	Yes	2/1/2017
Oregon Retail Employees Pension Trust[(2)]	936074377 -001	Red	Red	Implemented	4	3	Yes	Yes	Yes	9/30/2018-10/31/2018
Carpenters Pension Trust Fund for Northern California	946050970 -001	Red	Red	Implemented	6	5	No	No	No	6/30/2019
Other	Various	Green	Green		13	13		No	No	3/7/2016-5/31/2019
Other	Various	Yellow	Yellow		3	3		No	No	6/30/2016-6/30/2019
Total Expense					$ 41	$ 38				

(1) Forms 5500 information was available for all plan years ended in 2014. The majority of plans have a plan year end of December 31.

(2) Includes UFCW Local 555 Pharmacy Techs and Radiologists expiring September 30, 2018 and October 31, 2018, respectively.

(14) Postretirement Benefits Other than Pensions

(a) Defined Benefit Plan

Certain employees may become eligible for postretirement health care and life insurance benefits while working for Health Plans and Hospitals. Benefits available to retirees, through both affiliated and unaffiliated provider networks, vary by employee group. Postretirement health care benefits available to retirees include subsidized Medicare premiums, medical and prescription drug benefits, dental benefits, and vision benefits.

In January 2015, Health Plans and Hospitals modified postretirement health care benefits for certain union represented employees. Under the terms of the agreement, cost sharing will increase for plan participants and future employer-paid monthly premiums will be fixed. The impact of the agreement resulted in a negative plan amendment and a reduction in liabilities of $477 million.

At December 31, the accrued liability for postretirement benefits was as follows (in millions):

	2015	2014
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 7,193	$ 5,483
Service cost	192	156
Interest cost	256	278
Plan amendments	(756)	2
Benefits paid or provided	(136)	(132)
Net actuarial loss (gain)	(1,246)	1,406
Benefit obligation at end of year	$ 5,503	$ 7,193
Change in plan assets:		
Fair value of plan assets at beginning of year	$ 400	$ —
Actual return on plan assets	(35)	—
Contributions	1,136	532
Benefits paid or provided	(136)	(132)
Fair value of plan assets at end of year	$ 1,365	$ 400
Funded status	$ (4,138)	$ (6,793)
Amounts recognized in the balance sheet consist of:		
Noncurrent assets	$ —	$ —
Current liabilities	—	(80)
Pension and other retirement liabilities	(4,138)	(6,713)
	$ (4,138)	$ (6,793)
Amounts recognized in net worth:		
Net actuarial loss	$ 2,671	$ 4,078
Prior service credit	(2,724)	(2,407)
	$ (53)	$ 1,671

The measurement date used to determine postretirement benefits valuations was December 31.

For the years ended December 31, postretirement benefits expense was as follows (in millions):

	2015	2014
Service cost	$ 192	$ 156
Interest cost	256	278
Expected return on plan assets	(28)	—
Amortization of net actuarial loss	224	143
Amortization of prior service credit	(439)	(354)
Postretirement benefits expense	205	223
Other changes in plan assets and benefit obligations recognized in net worth:		
Net actuarial loss (gain)	(1,183)	1,406
Prior service cost (credit)	(756)	2
Amortization of net actuarial loss	(224)	(143)
Amortization of prior service credit	439	354
Total recognized in net worth	(1,724)	1,619
Total recognized in net periodic benefit cost and net worth	$ (1,519)	$ 1,842

During 2016, $137 million and $(432) million in estimated net actuarial loss and prior service credit, respectively, will be amortized from net worth into postretirement benefits expense.

During 2015, the employer contributions and benefits paid or provided were $1,136 million and $136 million, respectively. During 2014, the employer contributions and benefits paid or provided were $532 million and $132 million, respectively. In December 2014, $400 million was deposited into a retirement benefits trust account to fund the postretirement benefits of certain employees. During 2015 and 2014, there were no participant contributions from active employees.

Actuarial assumptions used were as follows:

	2015	2014
Weighted average discount rate used for calculating non-union plan postretirement benefits expense from January 1 to December 31	4.35%	5.25%
Weighted average discount rate for calculating union plan postretirement benefits expense from January 1 to January 24	4.35%	5.25%
Weighted average discount rate for calculating union plan postretirement benefits expense from January 25 to December 31	3.90%	5.25%
Weighted average discount rate for calculating December 31 accumulated postretirement benefit obligation	4.75%	4.35%
Expected long-term rate of return on plan assets for calculating benefits expense	7.00%	N/A

The following were the assumed health care cost trend rates used to determine postretirement benefits expense for the year ended December 31, 2014:

	Basic medical Pre-65/Post-65	Prescription drug Pre-65/Post-65	Medicare Part D	Dental	Medicare Part A&B	Medicare Part C	Supplemental medical Pre-65/Post-65
Initial trend rate - 2014	7.00% / 6.00%	6.00% / 6.00%	6.00%	4.50%	5.50%	0.75%	7.00% / 6.00%
Ultimate trend rate	4.50% / 4.50%	4.50% / 4.50%	4.50%	4.50%	4.50%	4.50%	4.50% / 4.50%
First year at ultimate trend rate	2026 / 2022	2025 / 2025	2025	2014	2020	2018	2026 / 2022

The following were the assumed health care cost trend rates used to determine the December 31, 2014 and 2015 benefit obligation and postretirement benefits expense for the year ended December 31, 2015:

	Basic medical Pre-65/Post-65	Prescription drug Pre-65/Post-65	Medicare Part D	Dental	Medicare Part A&B	Medicare Part C	Supplemental medical Pre-65/Post-65
Initial trend rate - 2014	5.50% / 5.25%	9.00% / 9.00%	4.00%	4.50%	5.25%	-2.00%	5.50% / 5.25%
Initial trend rate - 2015	5.50% / 5.25%	8.00% / 8.00%	4.00%	4.50%	5.25%	2.00%	5.50% / 5.25%
Ultimate trend rate	4.50% / 4.50%	4.50% / 4.50%	4.50%	4.50%	4.50%	4.50%	4.50% / 4.50%
First year at ultimate trend rate	2026 / 2022	2025 / 2025	2026	2014	2022	2018	2026 / 2022

A 1% increase in the health care medical trend rate would increase the benefit obligation by $741 million and the service cost plus interest by $61 million. A decrease of 1% in the health care medical trend rate would decrease the benefit obligation by $605 million and the service cost plus interest by $49 million.

The following benefit payments, which reflect expected future service, are expected to be paid or provided (in millions):

2016	$	141
2017		158
2018		177
2019		199
2020		221
2021 - 2025		1,476

Explanation of Investment Strategies and Policies

A total return investment approach is employed for the retirement benefit trust whereby the assets are invested in various asset classes to maximize the long-term return of plan assets for a prudent level of risk. The intent of this strategy is to minimize plan expenses by outperforming plan liabilities over the long run. Risk tolerance is established through consideration of plan liabilities, plan funded status, and corporate financial condition. The investment portfolio will consist over time of a varying but diversified blend of equity, fixed-income, and alternative investments. Diversification includes such factors as geographic location, equity capitalization size and style, placement in the capital structure, and security type. Investment risk is measured and monitored on an ongoing basis through annual liability measurements, periodic asset/liability studies, and quarterly investment portfolio reviews. The retirement benefit trust investment policy has restrictions relating to credit quality, industry/sector concentration, duration, concentration of ownership, and use of derivatives.

Capital Market Assumption Methodology

To determine the long-term rate of return assumption for plan assets, management incorporates historical relationships among the various asset classes and subclasses to be accessed over the investment horizon. Management’s intent is to maximize portfolio efficiency. This will be accomplished by seeking the highest returns prudently available among the available asset classes. Overall portfolio volatility is managed through diversification among asset classes. Current market factors such as inflation and interest rates are evaluated before long-term capital market assumptions are determined. From time to time, management reviews its long-term investment strategy and reconciles that strategy with the long-term liabilities of the Plan. This asset-liability study produces a range of expected returns over medium and long-term time periods. Those intermediate and long-term investment projections form the basis for the expected long-term rate of return on assets.

At December 31, 2015, the estimated fair value of retirement benefit trust assets by level was as follows (in millions):

	Quoted prices in active markets for identical assets level 1	Significant other observable inputs level 2	Significant unobservable inputs level 3	Total
Assets:				
Cash and cash equivalents	$ —	$ 650	$ —	$ 650
Alternative investments:				
Risk parity	—	375	340	715
Total assets	$ —	$ 1,025	$ 340	$ 1,365

For the year ended December 31, 2015, the reconciliation of assets with fair value measurements using significant unobservable inputs (level 3) was as follows (in millions):

	Alternative investments
Beginning balance	$ —
Transfers into level 3	—
Changes related to actual return on plan assets	(10)
Purchases, sales, and settlements - net	350
Ending balance	$ 340
Total year-to-date net gains related to assets held at December 31, 2015	$ (10)

The target asset allocation and expected long-term rate of return on assets (ELTRA) for calculating postretirement benefits expense were as follows:

	2015 target range	2015 ELTRA
Alternative investments	100%	7.00%
Total	100%	7.00%

Risk parity investments include redemption restrictions. Risk parity investments require 10 to 90 day written notice of intent to withdraw and are often subject to the approval and capital requirements of the fund manager. Risk parity investments of $100 million are subject to lock-up periods of up to 9 months.

(b) Multi-Employer Plans

Health Plans and Hospitals participate in multi-employer union-administered retiree medical health and welfare plans that provide benefits to some union employees. Benefits for retirees under these plans are negotiated as part of the collective bargaining process. For the years ended December 31, 2015 and 2014, Health Plans' and Hospitals' employer expense for both current and retiree benefits was $77 million and $73 million, respectively.

(15) Physicians' Retirement Plan

Kaiser Foundation Health Plan, Inc. provides defined retirement benefits for physicians associated with certain Medical Groups. Benefits are determined based on the length of service and level of compensation of each participant. The plan is unfunded and is not subject to the Employee Retirement Income Security Act.

At December 31, the accrued liability for physicians' retirement plan was as follows (in millions):

	2015	2014
Change in projected benefit obligation:		
Physicians' retirement plan liability at January 1	$ 6,078	$ 4,522
Service cost	327	231
Interest cost	258	231
Net actuarial loss (gain)	(608)	1,236
Benefits paid	(154)	(142)
Physicians' retirement plan liability at December 31	$ 5,901	$ 6,078
Accumulated benefit obligation at end of year	$ 4,624	$ 4,565
Change in plan assets:		
Fair value of plan assets at the beginning of year	$ —	$ —
Company contributions	154	142
Benefits paid	(154)	(142)
Fair value of plan assets at end of year	$ —	$ —
Funded status	$ (5,901)	$ (6,078)
Amounts recognized in the balance sheet consist of:		
Noncurrent assets	$ —	$ —
Current liabilities	(171)	(155)
Noncurrent liability	(5,730)	(5,923)
	$ (5,901)	$ (6,078)
Amounts recognized in net worth:		
Net actuarial loss	$ 1,373	$ 2,073

The measurement date used to determine physicians' retirement valuation was December 31.

A portion of the investments of Health Plans has been designated by management for the liabilities of the physicians' retirement plan. These investments are not held in trust or otherwise legally segregated and are not restricted even though it has been intended that these assets be used to pay the obligations of the physicians' retirement plan.

For purposes of the physicians' retirement plan expense, the expected return on assets is the portion of investment income that represents the expected return on the investments designated for the physicians' retirement plan. This amount is recorded as a reduction in the expense for the physicians' retirement plan

and is excluded from investment income - net, as described below and in the *Summary of Significant Accounting Policies - Investments* note.

For the years ended December 31, physicians' retirement plan provision was as follows (in millions):

	2015	2014
Service cost	$ 327	$ 231
Interest cost	258	231
Amortization of net actuarial loss	92	22
Total benefit expense	677	484
Expected return on assets - investment income included in operating expenses	(435)	(318)
Net benefit expense	242	166
Other changes in projected benefit obligations recognized in net worth		
Net actuarial loss (gain)	(608)	1,236
Amortization of net actuarial loss	(92)	(22)
Total recognized in net worth	(700)	1,214
Total recognized in net periodic benefit cost and net worth	$ (458)	$ 1,380

During 2016, $49 million in estimated net actuarial loss will be amortized from net worth into net benefit expense.

Actuarial assumptions used were as follows:

	2015	2014
Weighted average discount rate at January 1 for calculating benefit expense	4.30%	5.25%
Weighted average discount rate for calculating December 31 PBO	4.80%	4.30%
Weighted average salary scale for calculating pension expense	4.40%	4.90%
Weighted average salary scale for calculating December 31 PBO	4.40%	4.40%
Expected long-term rate of return on designated investments for calculating benefit expense	7.25%	7.25%

The following benefit payments, which reflect expected future service, are expected to be paid (in millions):

2016	$	171
2017		187
2018		206
2019		226
2020		245
2021 - 2025		1,508

(16) Commitments and Contingencies

(a) Lease and Purchase Commitments

Health Plans and Hospitals lease primarily office space, medical facilities, and equipment under various leases that expire through 2048. Certain leases contain rent escalation clauses and renewal options for additional periods.

At December 31, 2015, minimum commitments under noncancelable leases extending beyond one year were as follows (in millions):

2016	$	314
2017		298
2018		218
2019		151
2020		134
Thereafter		405
Total	$	1,520

Minimum payments above have not been reduced by minimum sublease rentals of $4 million due in the future under noncancelable subleases.

For the years ended December 31, 2015 and 2014, total lease expense for all leases was $459 million and $430 million, respectively.

Health Plans and Hospitals have entered into long-term agreements that require certain minimum purchases of goods and services. These commitments are at levels that are consistent with normal business requirements. Health Plans has committed to directing most of its purchasing volume for selected products through an outside agency and has committed to at least $1 billion in purchasing per annum through March 31, 2017. During 2015 and 2014, Health Plans' total purchases through this outside agency exceeded $1 billion. Should the $1 billion level not be achieved, financial penalties would be assessed at an established percentage of any shortfalls. In addition, should the purchasing volume for certain product categories be redirected from the outside agency, a financial

penalty would be assessed at an established percentage. In management's judgment, there is a remote probability of material financial penalties under this contract.

At December 31, 2015, minimum purchase commitments, excluding contracts that count towards the $1 billion per annum commitment noted above, extending beyond one year were as follows (in millions):

2016	$	305
2017		280
2018		133
2019		115
2020		60
Thereafter		14
Total	$	907

During 2015 and 2014, Health Plans' and Hospitals' total purchases under contracts with minimum purchase commitments, excluding those purchases which count towards the $1 billion per annum commitment noted above, were $542 million and $330 million, respectively.

(b) Renewable Energy Contracts

Hospitals has entered into 20 year renewable energy contracts to reduce the financial risk of unexpected increases in utility prices and help achieve its renewable energy goals. Under the renewable energy contracts, Hospitals will net settle with the counterparty based on 100% of the output of two renewable energy sites and also realize renewable energy credits from the production of energy from wind and solar sites. The wind site started its production in December 2015 and the start date of the solar site is anticipated to be no later than December 31, 2016. To the extent that the price of electrical energy varies from the fixed amounts in the contracts, Hospitals will pay more or less than the current value of electrical energy over the term of the contracts. Management cannot reasonably estimate the financial impact of these contracts as they are subject to market fluctuations in energy prices and to the actual production volume of the sites. In addition, Health Plans and Hospitals have entered into multiple on-site renewable energy contracts ranging between 10 and 20 years that are recorded as either contingent operating leases or purchase agreements.

(c) Surety Instruments and Standby Letters of Credit

In the normal course of business, Health Plans and Hospitals contract to perform certain financial obligations that require a guarantee from a third party. This guarantee creates a contingent liability to the entity that provides that guarantee. At December 31, 2015 and 2014, Health Plans and Hospitals had entered into surety instruments and standby letters of credit that totaled $81 million and $125 million, respectively.

Health Plan, Inc. and Hospitals also guarantee payment of workers' compensation liabilities of certain Medical Groups under self-insurance programs. The majority of such liabilities are recorded as other long-term liabilities of Health Plan, Inc., as payment is provided for under the applicable medical service agreements. In addition to amounts accrued, at December 31, 2015 and 2014, pursuant to such guarantees, Health Plan, Inc. and Hospitals are contingently liable for approximately $200 million and $180 million, respectively, of certain Medical Groups' self-insured workers' compensation liabilities.

(d) Regulatory

Health Plans are required to periodically file financial statements with regulatory agencies in accordance with statutory accounting and reporting practices. Health Plans must comply with the various states' minimum regulatory net worth requirements generally under the regulation of the California Department of Managed Health Care and various state departments of insurance. Such requirements are generally based on tangible net equity or risk-based capital, and for California are calculated on the basis of combined net worth of Health Plans and Hospitals. At December 31, 2015 and 2014, the regulatory net worth, so defined, exceeded the aggregate regulatory minimum requirements by approximately $23 billion and $19 billion, respectively.

Health Plans' regulated subsidiaries maintain investments in various states where they are licensed. At both December 31, 2015 and 2014, $5 million in securities were held to satisfy various state regulatory requirements.

Health Plans and Hospitals are subject to numerous and complex laws and regulations of federal, state, and local governments, and accreditation requirements. Compliance with such laws, regulations, and accreditation requirements can be subject to retrospective review and interpretation, as well as regulatory actions. These laws and regulations include, but are not necessarily limited to, requirements of tax exemption, government reimbursement, government program participation, privacy and security, false claims, anti-kickback, accreditation, healthcare reform, controlled substances, facilities, and professional licensure. In recent years, government activity has increased with respect to compliance and enforcement actions.

In the ordinary course of our business operations, Health Plans and Hospitals are subject to periodic reviews, investigations, and audits by various federal, state, and local regulatory agencies and accreditation agencies, including, without limitation, CMS, Department of Managed Health Care, Office of Personnel Management, Occupational Safety and Health Administration, Drug Enforcement Administration, State Boards of Pharmacy, Food and Drug Administration, IRS, National Committee for Quality Assurance, and state departments of insurance.

Health Plans' and Hospitals' compliance with the wide variety of rules and regulations and accreditation requirements applicable to their business may result in certain remediation activities and regulatory fines and penalties, which could be substantial. Where appropriate, reserves have been established for such sanctions. While management believes these reserves are adequate, the

outcome of legal and regulatory matters is inherently uncertain, and it is possible that one or more of the legal or regulatory matters currently pending or threatened could have a material adverse effect on the combined financial position or results of operations.

(e) Litigation

Health Plans and Hospitals are involved in lawsuits and various governmental investigations, audits, reviews, and administrative proceedings arising, for the most part, in the ordinary course of business operations. Lawsuits have been brought under a wide range of laws and include, but are not limited to, business disputes, employment and retaliation claims, claims alleging professional liability, improper disclosure of personal information, labor disputes, administrative regulations, the False Claims Act, information privacy and HIPAA laws, mental health parity laws, and consumer protection laws. In addition, Health Plans indemnifies the Medical Groups against various claims, including professional liability claims.

Health Plans and Hospitals record reserves for legal proceedings and regulatory matters where available information indicates that at the date of the combined financial statements a loss is probable and the amount can be reasonably estimated. While such reserves reflect management's best estimate of the probable loss for such matters, Health Plans' and Hospitals' recorded amounts may differ materially from the actual amount of any such losses.

In September 2015, a lawsuit was filed seeking to have the State of California impose the gross premiums tax on Health Plan, Inc. In the opinion of management, strong defenses exist regarding this claim. However, an unfavorable outcome could have a material adverse effect. No reserves have been provided related to this lawsuit.

Health Plan, Inc. and one of the Medical Groups disagree regarding the interpretation of certain terms in the parties' contract for provision of medical services. Health Plan, Inc. has reduced 2015 medical services expenses by $112 million in the combined statements of operations and changes in net worth, representing Health Plan, Inc.'s estimate of the value of Health Plan, Inc.'s interpretation of this contract language for 2015. No reserves have been provided against this $112 million.

In the opinion of management, based upon current facts and circumstances, the resolution of these matters is not expected to have a material adverse effect on the combined financial position or combined results of operations of Health Plans and Hospitals. The outcome of litigation and other legal and regulatory matters is inherently uncertain, however, and it is possible that one or more of the legal or regulatory matters currently pending or threatened could have a material adverse effect.

(17) Subsequent Events

In January 2016, Maui Health System, a Kaiser Foundation Hospitals LLC (MHSKFH), a subsidiary of Hospitals, entered into a contract with State of Hawaii entities to manage, operate, and provide health care services at hospitals of the Maui Region of Hawaii Health Systems Corporation under the terms of a 30

year transfer agreement. The agreement includes an option for MHSKFH to extend for a potential of two more 10 year terms. If regulatory approvals are obtained, operations are expected to commence July 1, 2016. All existing facilities will be leased from the State of Hawaii entities with financial responsibility of any additional investments to the facilities to be shared between MHSKFH and the State of Hawaii entities during the first 10 years.