

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

Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

(Unaudited)

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

**Table of Contents**

	<b>Page</b>
Financial Statements (Unaudited):	
Kaiser Foundation Health Plan, Inc. and Subsidiaries and Kaiser Foundation Hospitals and Subsidiaries:	
Combined Balance Sheets	1
Combined Statements of Operations and Changes in Net Worth	
Nine months ended September 30, 2021 and 2020	2
Three months ended September 30, 2021 and 2020	3
Combined Statements of Cash Flows	4
Notes to Combined Financial Statements	5

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

Combined Balance Sheets

September 30, 2021 and December 31, 2020

(In millions)

<b>Assets</b>	<b>2021</b>	<b>2020</b>
Current assets:		
Cash and cash equivalents	\$ 783	\$ 674
Current investments	8,374	8,361
Securities lending collateral	848	636
Broker receivables	209	390
Due from associated medical groups	4	24
Accounts receivable – net	3,346	3,300
Inventories – net and other current assets	1,912	2,285
Total current assets	15,476	15,670
Noncurrent investments	45,003	35,486
Land, buildings, equipment, and software – net	29,269	28,882
Operating lease right-of-use assets	1,227	1,326
Other long-term assets	1,272	1,062
Total assets	\$ 92,247	\$ 82,426
<b>Liabilities and Net Worth</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 4,475	\$ 4,943
Medical claims payable	2,703	2,611
Due to associated medical groups	1,354	1,245
Payroll and related charges	2,582	2,721
Securities lending payable	848	636
Broker payables	431	846
Other current debt	784	384
Other current liabilities	3,396	3,320
Total current liabilities	16,573	16,706
Long-term debt	12,074	9,873
Physicians' retirement plan liability	12,295	11,780
Pension and other retirement liabilities	3,476	3,093
Operating lease liabilities	1,035	1,142
Other long-term liabilities	2,899	2,852
Total liabilities	48,352	45,446
Net worth	43,895	36,980
Total liabilities and net worth	\$ 92,247	\$ 82,426

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

Nine months ended September 30, 2021 and 2020

(In millions)

	<u>2021</u>	<u>2020</u>
Revenues:		
Members' dues	\$ 45,476	\$ 44,882
Medicare	17,264	16,590
Copays, deductibles, and other	<u>7,284</u>	<u>5,170</u>
Total operating revenues	<u>70,024</u>	<u>66,642</u>
Expenses:		
Medical services	33,572	30,957
Hospital services	18,886	16,669
Outpatient pharmacy and optical services	7,520	7,170
Other benefit costs	<u>5,433</u>	<u>4,332</u>
Total medical and hospital services	65,411	59,128
Health Plan administration	<u>3,196</u>	<u>3,731</u>
Total operating expenses	<u>68,607</u>	<u>62,859</u>
Operating income	<u>1,417</u>	<u>3,783</u>
Other income and expense:		
Investment income – net	4,519	1,301
Interest expense and other income (expense) – net	<u>620</u>	<u>280</u>
Total other income and expense	<u>5,139</u>	<u>1,581</u>
Net income	6,556	5,364
Change in pension and other retirement liability charges	644	440
Change in net unrealized gains on investments	(252)	(236)
Other	<u>(33)</u>	<u>14</u>
Change in net worth	6,915	5,582
Net worth at beginning of year	<u>36,980</u>	<u>35,054</u>
Net worth at end of period	<u>\$ 43,895</u>	<u>\$ 40,636</u>

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

Three months ended September 30, 2021 and 2020

(In millions)

	<u>2021</u>	<u>2020</u>
Revenues:		
Members' dues	\$ 15,235	\$ 14,686
Medicare	5,727	5,546
Copays, deductibles, and other	2,192	1,720
Total operating revenues	<u>23,154</u>	<u>21,952</u>
Expenses:		
Medical services	11,148	10,656
Hospital services	6,171	5,762
Outpatient pharmacy and optical services	2,555	2,423
Other benefit costs	2,164	1,453
Total medical and hospital services	<u>22,038</u>	<u>20,294</u>
Health Plan administration	1,078	1,202
Total operating expenses	<u>23,116</u>	<u>21,496</u>
Operating income	<u>38</u>	<u>456</u>
Other income and expense:		
Investment income – net	1,318	1,410
Interest expense and other income (expense) – net	200	105
Total other income and expense	<u>1,518</u>	<u>1,515</u>
Net income	1,556	1,971
Change in pension and other retirement liability charges	245	146
Change in net unrealized gains on investments	(127)	(186)
Other	1	21
Change in net worth	<u>1,675</u>	<u>1,952</u>
Net worth at beginning of quarter	<u>42,220</u>	<u>38,684</u>
Net worth at end of quarter	<u>\$ 43,895</u>	<u>\$ 40,636</u>

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

Nine months ended September 30, 2021 and 2020

(In millions)

	<u>2021</u>	<u>2020</u>
Cash flows from operating activities:		
Net income	\$ 6,556	\$ 5,364
Adjustments to reconcile net income to net cash provided by by operating activities:		
Depreciation and software amortization	2,113	2,022
Other amortization	200	185
Gain recognized on investments – net	(4,073)	(1,083)
Loss on land, buildings, equipment, and software – net	26	34
Releases of restricted donations	(15)	(20)
Changes in assets and liabilities:		
Accounts receivable – net	(57)	(1,073)
Due from associated medical groups	20	(31)
Other assets	(159)	(916)
Accounts payable and accrued expenses	(355)	(138)
Medical claims payable	92	(51)
Due to associated medical groups	114	(488)
Payroll and related charges	(139)	(69)
Pension and other retirement liabilities	876	(2,342)
Physicians' retirement plan liability	666	606
Other liabilities	(73)	590
Net cash provided by operating activities	<u>5,792</u>	<u>2,590</u>
Cash flows from investing activities:		
Additions to land, buildings, equipment, and software	(2,648)	(2,783)
Proceeds from investments	23,420	74,102
Investment purchases	(29,076)	(73,869)
Decrease (increase) in securities lending collateral	(212)	368
Broker receivables / payables	(234)	105
Issuance of notes receivable	(66)	(69)
Prepayment and repayment of notes receivable	110	73
Other investing	201	(101)
Net cash used in investing activities	<u>(8,505)</u>	<u>(2,174)</u>
Cash flows from financing activities:		
Issuance of debt	3,266	3,297
Prepayment and repayment of debt	(642)	(3,444)
Increase (decrease) in securities lending payable	212	(368)
Other financing	(14)	7
Net cash provided by (used in) financing activities	<u>2,822</u>	<u>(508)</u>
Net change in cash and cash equivalents	109	(92)
Cash and cash equivalents at beginning of year	674	904
Cash and cash equivalents at end of period	<u>\$ 783</u>	<u>\$ 812</u>
Supplemental cash flows disclosure:		
Cash paid for interest – net of capitalized amounts	\$ 168	\$ 183

See accompanying notes to combined financial statements.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**(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) (collectively referred to herein as Health Plans and Hospitals). Health Plans and Hospitals is primarily comprised of not-for-profit corporations whose capital is available for charitable, educational, research, and related purposes. Health Plans is primarily comprised of health maintenance organizations that are generally exempt from federal and state income taxes. At September 30, 2021 and December 31, 2020 membership was 12.5 million and 12.4 million, respectively. At both September 30, 2021 and December 31, 2020, the percentage of enrolled membership in California was approximately 74%. 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 Foundation Health Plan of Washington

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 both September 30, 2021 and December 31, 2020, the percentage of Health Plans and Hospitals' total labor force covered under collective bargaining agreements was approximately 71%. At September 30, 2021, approximately 36% of the workforce was covered under collective bargaining agreements that were scheduled to expire within one year. At September 30, 2021, approximately 2% of the workforce was under an expired agreement, and less than 1% of the workforce was organizing and negotiating an agreement.

At November 15, 2021, approximately 66% of the labor-represented workforce that was operating under collective bargaining agreements that were set to expire within one year reached a tentative agreement, which is subject to ratification in the coming weeks.

Health Plans and Hospitals strives to improve the health and welfare of the communities it serves through its Community Benefit investment programs. Community Benefit expenditures provide funding for programs that serve communities through research, community-based health partnerships, the provision of charity care to low-income patients, direct health coverage for low-income families, and collaboration with community clinics, health departments, and public hospitals.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

Cost-based methods are used to account for losses incurred under the care and coverage by members and patient types qualifying for treatment as Community Benefit. Assigned members and patients must first prove eligibility based upon family income relative to the Federal Poverty Guidelines. Certain Community Benefit costs are determined using the out-of-pocket costs directly billed to patients or a cost-to-charge ratio applied to uncompensated charges associated with care provided to these patients.

For the year ended December 31, 2020, Community Benefit expenditures (at cost, net of approximately \$4.0 billion of related revenues) were \$3.6 billion, representing 4.1% of operating revenues.

On March 11, 2020, the World Health Organization declared the outbreak of a novel strain of coronavirus (COVID-19) a pandemic, and on March 13, 2020, the President of the United States declared a state of national emergency. COVID-19 precipitated both health and economic crises worldwide, while impacting all of the geographical markets in which Health Plans and Hospitals operates. Health Plans and Hospitals' response to COVID-19 has included actions to maintain continuity of essential operations, while also taking steps to support the health and safety of members, employees, and the communities Health Plans and Hospitals serves. As part of Health Plans and Hospitals' commitment to helping end the COVID-19 pandemic, Health Plans and Hospitals has implemented a vaccination mandate for its workforce. Additionally, a vaccination requirement was extended to certain vendors and suppliers that enter Health Plans and Hospitals' facilities.

As discussed in the *Summary of Significant Accounting Policies – Use of Estimates* note, under accounting principles generally accepted in the United States of America (GAAP), management is required to make estimates and assumptions that affect reported amounts. The impact of COVID-19 has increased the uncertainty associated with several of the assumptions underlying management's estimates. COVID-19's overall impact on Health Plans and Hospitals will be driven primarily by the severity and duration of the pandemic; the pandemic's impact on the United States economy and the timing, scope, and effectiveness of federal, state, and local governmental responses to the pandemic. Those primary drivers are uncertain and beyond management's control and may adversely impact Health Plans and Hospitals' membership levels, supply chain, values of investments, and workforce, among other aspects of Health Plans and Hospitals' business. The actual impact of COVID-19 on Health Plans and Hospitals' combined financial statements may differ significantly from the judgments and estimates made as of the current reporting period.

**(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 GAAP. All material intercompany balances and transactions have been eliminated. Management has evaluated subsequent events through November 15, 2021, which is the date that these combined financial statements were issued.



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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**(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 cash equivalents held by outside investment managers are classified as investments. Cash, cash equivalents, and investments that are restricted per contractual or regulatory requirements are classified as noncurrent investments.

**(c) Investments**

Investments including equity, U.S. Treasury, government agencies, money market funds, and other marketable debt securities are reported at fair value. Investments are categorized as current assets if they are designated 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 has designated a portion of its 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 these guidelines:

- Substantially all investments are managed by outside investment managers who do not need Health Plans and Hospitals' management preapproval for sales; therefore, substantially all declines in value below cost are recognized as impairment that is other-than-temporary. Changes in estimated value for equity method alternative investments and equity investments that do not result in consolidation, are recognized in investment income – net. Therefore, these investments do not typically require impairment.
- 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 fixed income securities 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.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**(d) *Securities Lending Collateral and Payable***

Health Plans and Hospitals enters into securities lending agreements whereby certain securities from its portfolios are loaned to other institutions. Securities lent under such agreements remain in the portfolios of Health Plans and Hospitals. Health Plans and Hospitals receives 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 *Summary of Significant Accounting Policies – 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) *Accounts Receivable – Net***

Accounts receivable – net are comprised of members' dues, Medicare receivables, patient receivables, and other receivables.

**(g) *Inventories – Net***

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

**(h) *Land, Buildings, Equipment, and Software***

Land, buildings, equipment, and software are stated at cost less accumulated depreciation and amortization. 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. Interest is capitalized on facilities construction and internally developed software work in progress and is added to the cost of the underlying asset.

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 three to seven 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 40 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.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

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.

**(i) Medical Claims Payable**

The cost of health care services is recognized in the period in which services are incurred. 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 claim payments are received, adjudicated, and paid, estimates are revised and are reflected in current operations. Such estimates are subject to actual utilization of medical services, changes in membership and product mix, claim submission and processing patterns, medical inflation, and other relevant factors. Given the inherent variability of such estimates, the actual liability could differ significantly from the amounts provided.

**(j) 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.

**(k) 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. The limit and scope of the self-insured layer and the amounts of excess insurance purchased are reviewed each year, subject to

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

management's analysis of actuarial loss projections and the price and availability of acceptable commercial insurance.

**(l) 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 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 estimates are periodically updated, and any resulting adjustments are reflected in current operations. At September 30, 2021 and December 31, 2020, premium deficiency reserves were \$403 million and \$203 million, respectively. Given the inherent variability of such estimates, the actual liability could differ from the calculated amount.

**(m) 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 enters into interest rate swaps with investment or commercial banks with significant experience with such instruments. 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 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.

**(n) Revenue Recognition**

Revenues from contracts with customers include revenues from the following categories: members' dues, Medicare, copays, deductibles, and other revenues. Health Plans and Hospitals recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which Health Plans and Hospitals expects to be entitled in exchange for those goods or services. At contract inception, Health Plans and Hospitals assesses the promised goods or services in the contract and identifies the performance obligation for each promise to transfer a good or service (or bundle of goods or services) that is distinct. Revenue is recognized when performance obligations are satisfied by transferring control of the good or service provided. For the majority of Health Plans and Hospitals' operations, the primary performance obligation is to provide access to integrated health care services.

The consideration received for goods and services may include variable components. Variable consideration is included in the transaction price to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

Health Plans satisfies its performance obligation and recognizes revenue ratably over the period in which members are eligible to access integrated health care services.

*Members' Dues*

Members' dues generally include amounts received from employer groups, individuals, and government entities. The service promised is access to integrated health care services for a typical term of one year. Members' dues are generally based on a prepaid fee and billed on a monthly, fixed, per member per month basis.

Significant variable consideration includes the following:

- *Commercial Risk Adjustment:* Health Plans participates in certain contracts with commercial large group plan sponsors that include provision for risk adjustment of members' dues 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 the nine months ended September 30, 2021 and 2020, dues subject to these risk adjustment arrangements comprise 2.8% and 1.8%, respectively, of total members' dues. For the nine months ended September 30, 2021 and 2020, \$28 million and \$16 million, respectively, have been recorded as reductions to revenue for these risk adjustment arrangements.
- *Affordable Care Act (ACA) Risk Adjustment Program:* The ACA Risk Adjustment Program provides for retrospective adjustment of revenue for non-grandfathered individual and small group market plans, whether inside or outside ACA exchanges. The ACA 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 nine months ended September 30, 2021 and 2020, Health Plans recorded \$463 million and \$941 million, respectively, in net revenue reductions to members' dues related to the ACA Risk Adjustment Program. At September 30, 2021 and December 31, 2020, net payables for Risk Adjustment settlements were \$723 million and \$1.1 billion, respectively. Receivables are recorded in accounts receivable – net and payables are recorded in accounts payable and accrued expenses on the combined financial statements.

*Medicare*

Health Plans provides various Medicare products, including the Medicare Advantage Program (Part C) and Medicare cost plans with and without prescription drug coverage and Medicare supplemental products that supplement traditional fee-for-service Medicare coverage. The majority of Health Plans and Hospitals' Medicare revenue is received from Part C. Medicare revenues are based on contracts to provide access to integrated health care services to enrolled Medicare recipients.

Revenues for Part C plans include monthly capitated payments made from the Centers for Medicare & Medicaid Services (CMS), which vary based on member health status, demographic status, and other factors.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

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 Health Plans in current operations.

Revenues for Medicare also include a voluntary prescription drug benefit (Part D). Revenues for Part D include monthly capitated payments made from CMS, which are adjusted for health risk factor scores. Revenues for Part D 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.

Medicare Part C and D revenue is subject to governmental audits and potential payment adjustments. CMS performs audits to validate the supporting documentation maintained by Health Plans and its care providers.

Significant variable consideration includes the following:

- *Medicare Part C and D:* Adjustments related to annual settlements from CMS, changes in members risk scores, member demographics, and data reconciliations.

In connection with Medicare, members may have to pay copays and/or deductibles.

*Copays, Deductibles, and Other*

These revenues include copays and deductibles, third party Medicaid contracts, hospital provider fee programs, and other revenues.

Third party Medicaid contracts represents coverage to certain Medicaid enrollees through contracts with third parties known as plan partners and is recorded in copays, deductibles, and other revenues. Health Plans generally receives capitation payments on a monthly, fixed, per member per month basis. Health Plans satisfies its performance obligation and recognizes revenue ratably over the period in which enrollees are eligible to access integrated health care services, which is generally over a one year period. For the nine months ended September 30, 2021 and 2020, revenues related to third party Medicaid contracts were \$1.9 billion and \$1.4 billion, respectively.

Significant variable consideration includes the following:

- *Copays and Deductibles:* These are member cost share amounts due to Health Plans and Hospitals. Amounts due are based on contractual agreements and evidence of coverage documentation and are typically calculated and collected at the point of service. Amounts may be fixed per unit/service or vary based on venue of care, coverage, and/or whether certain maximum out of pocket or deductible thresholds have been met.
- *Third Party Medicaid Rate Retroactivity:* Periodic settlements from third party Medicaid plan partners based on rate retroactivity.
- *Hospital Provider Fee Programs:* Certain states where Hospitals operate have enacted legislation for a hospital fee program to largely help fund Medicaid. The hospital provider fee programs charge certain hospital providers a fee that is then used to obtain federal matching funds for Medicaid. For

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

the nine months ended September 30, 2021 and 2020, expenses recognized for amounts paid to the states were \$982 million and \$152 million, respectively. The fees collected from hospital providers and the federal matching funds are used by states to fund Medicaid related initiatives and associated costs of administration. A portion of the funds are redistributed to hospital providers within the state as supplemental payments. The supplemental payments received by Hospitals under these programs vary based on Medicaid utilization, among other factors. For the nine months ended September 30, 2021 and 2020, revenues related to hospital provider fee programs were \$1.2 billion and \$198 million, respectively.

**Collectibility Assessment**

Health Plans and Hospitals generally collects payments for contracts with customers in advance of the services provided or in the month due, thus a collectibility assessment is typically not required. Health Plans and Hospitals includes an estimate of collectibility as an implicit price concession in the transaction price at contract inception and bases the amount of adjustments on a monthly evaluation of historical collection experience, aged accounts receivable, and current market conditions using a portfolio approach for certain revenue arrangements. If actual amounts of consideration ultimately received differ from the estimates, Health Plans and Hospitals adjusts these estimates, which would affect revenues in the period such variances become known.

**Disaggregation of Revenue**

Health Plans and Hospitals earns substantially all of its revenues from contracts with customers. Revenue not related to contracts with customers are included in other revenue in the table below.

For the nine months ended September 30, contracts with customers revenue disaggregated by geographical market were as follows (in millions):

<b><u>Primary Geographical Markets:</u></b>	<b><u>2021</u></b>	<b><u>2020</u></b>
Northern California	\$ 27,426	\$ 25,967
Southern California	24,775	23,171
Colorado	3,088	3,256
Georgia	1,543	1,516
Hawaii	1,390	1,381
Mid-Atlantic	3,948	3,862
Northwest	3,645	3,565
Washington	3,507	3,433
Other	452	373
Total contracts with customers revenue	69,774	66,524
Other revenue	250	118
Total operating revenue	\$ 70,024	\$ 66,642

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**Contract Asset / Liability Balances**

Health Plans and Hospitals generally satisfies its performance obligation when it provides access to integrated health care services in exchange for consideration from its customers. The timing of Health Plans and Hospitals' performance may differ from the timing of the customer's payment, which may result in the recognition of a contract asset or a contract liability. At both September 30, 2021 and December 31, 2020, there were no material contract assets with customers.

Health Plans and Hospitals' contract liabilities, recorded in other current liabilities, were as follows (in millions):

	<b>At September 30, 2021</b>	<b>At December 31, 2020</b>
Opening (January 1)	\$ 945	\$ 935
Closing balance	<u>1,009</u>	<u>945</u>
Increase	<u>\$ 64</u>	<u>\$ 10</u>

For the nine months ended September 30, 2021 and the year ended December 31, 2020, the majority of both contract liability balances at January 1, 2021 and 2020 of \$945 million and \$935 million, respectively, were recognized.

**Significant Judgments**

Below is a summary of significant judgments related to the recognition of revenue that significantly affect the determination of the amount and timing of revenue for Health Plans and Hospitals.

For the performance obligation related to access to integrated health care services, Health Plans and Hospitals transfers promised services by providing access to integrated health care services over time. A time-elapsed output method is used for revenue recognition to measure progress because Health Plans and Hospitals transfers promised services by providing access to integrated health care services over the period that the member is entitled to the services.

Determining a measure of progress requires management to make judgments that affect the timing of revenue recognized. Health Plans and Hospitals has determined that the above method provides a faithful depiction of the transfer of goods or services to the customer. Health Plans and Hospitals stands ready to provide coverage for integrated health care services as needed and efforts are expended evenly throughout the period.

**Practical Expedients**

Health Plans and Hospitals has elected the following significant practical expedient:

- *Incremental costs of obtaining a contract:* Health Plans and Hospitals has elected to recognize the incremental costs of obtaining a contract (primarily brokerage commissions) as an expense when



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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

incurred as the time period of most contracts with customers is one year or less and renewal commission rates are commensurate with new commission rates.

**Remaining Performance Obligations**

The remaining performance obligations greater than one year relate to contracts with customers in which the transaction price is not yet determinable for future years as the members' dues rate has not yet been negotiated and is also dependent on membership volume. For the nine months ended September 30, 2021 and 2020, the amount of revenues from contracts with customers with performance obligations greater than one year was \$3.0 billion and \$2.8 billion, respectively.

**(o) 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 evaluates assumptions annually, or when significant plan amendments occur, and modifies them as appropriate. Pension and other postretirement costs are allocated over the service period of the employees in the plans. The non-service cost components of net benefit expense for pension, other postretirement benefits, and the physicians' retirement plan are included in interest expense and other income (expense) – net.

Health Plans and Hospitals uses a discount rate to determine the present value of the future benefit obligations. The discount rate is established based on the development of a sample bond portfolio consisting of high quality corporate bonds. From this portfolio, a spot rate curve is interpolated and used to derive a single discount rate.

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 that arise from plan amendments are amortized into postretirement benefits expense over the expected average future service to full eligibility of active participants and pension benefits expense over the expected future service of active participants.

**(p) Donations and Grants Made or Received**

Donations and grants made or received, that are contributions, are recognized at fair value in the period in which a commitment is made unconditionally, or in the period that conditions placed on the donations or grants are met. A condition is present if there is a barrier that the recipient must overcome to be entitled to the assets, and either a right of return of assets transferred or a right of release of a promisor's obligation to transfer assets exists.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**(q) *Income Taxes***

Health Plans and Hospitals are not-for-profit corporations exempt from income taxes under Internal Revenue Code Section 501(a) as organizations described in section 501(c)(3) and the laws of the states in which they operate. Accordingly, Health Plans and Hospitals are generally not subject to federal or state income taxes. Health Plans and Hospitals are subject to income taxes on unrelated business income. A limited number of Health Plans and Hospitals' subsidiaries are for profit entities and are subject to income taxes. For the nine months ended September 30, 2021 and 2020, no significant income tax provision has been recorded.

**(r) *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. Estimated fair value and impairment of investments; Medicare revenue accruals; incurred but not reported medical claims payable; physicians' retirement plan liabilities; pension and other retirement liabilities; self-insured professional liabilities; self-insured general and workers' compensation liabilities; land, buildings, equipment, and software impairment and useful lives; and certain amounts accrued related to the ACA Risk Adjustment Program represent significant estimates. Actual results could differ materially from those estimates.

**(s) *Fair Value Estimates***

The carrying amounts reported in the combined 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 incorporate transaction details such as timing of cash flows, including maturity. Fair value adjustments, including credit, liquidity, and other factors, are included, as appropriate, to arrive at a fair value measurement.

Health Plans and Hospitals utilizes 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

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

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.

At September 30, 2021 and December 31, 2020, Health Plans and Hospitals held derivative financial instruments including interest rate swaps, as well as futures, forwards, options, and swaps 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.

**(t) The ACA Health Insurance Providers Fee**

The ACA requires Health Plans to pay a Health Insurance Providers (HIP) 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) assessed a HIP fee of \$741 million for 2020 and the amount was paid and expensed in 2020. The HIP fee has been permanently suspended for 2021 and all future years.

**(u) Natural Classification of Expenses**

For the nine months ended September 30, operating expenses classified by function in the combined statements of operations and changes in net worth are presented by their natural classifications as follows (in millions):

	<b>2021</b>					
	<b>Salaries, wages, and benefits</b>	<b>Outside medical costs</b>	<b>Depreciation and software amortization</b>	<b>Pharmacy and supplies costs</b>	<b>Other operating expenses</b>	<b>Total operating expenses</b>
Medical services	\$ 4,140	\$ 24,025	\$ 845	\$ 2,903	\$ 1,659	\$ 33,572
Hospital services	7,858	5,440	1,086	1,727	2,775	18,886
Outpatient pharmacy and optical services	1,455	156	69	5,596	244	7,520
Other benefit costs	609	4,315	17	154	338	5,433
Health Plan administration	1,262	-	96	70	1,768	3,196
Total operating expenses	<u>\$ 15,324</u>	<u>\$ 33,936</u>	<u>\$ 2,113</u>	<u>\$ 10,450</u>	<u>\$ 6,784</u>	<u>\$ 68,607</u>

  

	<b>2020</b>					
	<b>Salaries, wages, and benefits</b>	<b>Outside medical costs</b>	<b>Depreciation and software amortization</b>	<b>Pharmacy and supplies costs</b>	<b>Other operating expenses</b>	<b>Total operating expenses</b>
Medical services	\$ 3,941	\$ 22,324	\$ 766	\$ 2,542	\$ 1,384	\$ 30,957
Hospital services	7,281	4,737	1,074	1,483	2,094	16,669
Outpatient pharmacy and optical services	1,453	129	64	5,293	231	7,170
Other benefit costs	587	3,216	16	141	372	4,332
Health Plan administration	1,388	-	102	71	2,170	3,731
Total operating expenses	<u>\$ 14,650</u>	<u>\$ 30,406</u>	<u>\$ 2,022</u>	<u>\$ 9,530</u>	<u>\$ 6,251</u>	<u>\$ 62,859</u>

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

Some categories of natural class expenses are attributable to more than one function and require allocation, applied on a consistent basis. Outside medical costs include Medical Group costs and other outside medical costs. Property costs including depreciation are allocated on the basis of square footage. Indirect salaries and benefits are allocated on the basis of budgeted full time equivalent employees. Other expenses are assigned directly to specific functions as expenditures are made.

**(v) Liquidity and Availability of Resources**

Cash and cash equivalents, current investments, and accounts receivable – net, as reported on the combined balance sheets at September 30, 2021 and December 31, 2020, are the primary liquid resources used by Health Plans and Hospitals to meet general expenditure needs within the next year. As part of liquidity management, Health Plans and Hospitals' policy is to structure and manage its financial assets to be available to meet its general expenditure needs. Health Plans and Hospitals invests cash in excess of daily requirements in current investments. To help manage unanticipated liquidity needs, Hospitals has both a credit facility and commercial paper program, as described in the *Debt* note. Additionally, although intended to satisfy long-term obligations, 61% of noncurrent investments at September 30, 2021, could be utilized within the next year if necessary.

**(w) Recently Issued Accounting Standards**

In March 2020, the FASB issued Accounting Standards Update (ASU) No. 2020-04 *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting* and subsequently refined the scope of Topic 848 in January 2021. The amendments in the standard are elective and apply to contracts, hedging relationships, and other transactions that reference LIBOR or other reference rates expected to be discontinued because of reference rate reform as well as certain other instruments that are impacted as a result of reference rate reform. The standard provides optional guidance to ease the potential burden in accounting for (or recognizing the effects of) reference rate reform on financial reporting. Expedients and exceptions can be elected for applying GAAP to contracts and other transactions affected by reference rate reform if certain criteria are met. The amendments are effective immediately and will be available through December 31, 2022. Management has not adopted the optional elections in Topic 848 and is evaluating the effect the new standard will have on its ongoing financial reporting.

**(x) Leases**

Transactions give rise to leases when Health Plans and Hospitals receives substantially all the economic benefits from and has the ability to direct the use of specified property, plant, and equipment. Health Plans and Hospitals primarily has lessee activity that is classified as operating leases. Operating leases are included in operating lease right-of-use assets, other current liabilities, and operating lease liabilities in the combined balance sheets. Finance leases are included in land, buildings, equipment, and software – net, other current debt, and long-term debt in the combined balance sheets.

Right-of-use assets represent the right to use underlying assets for the lease term and lease liabilities represent obligations to make lease payments arising from the lease. Operating lease right-of-use assets and liabilities are recognized at the commencement date based on the present value of lease payments over the lease term. When discount rates implicit in leases cannot be readily determined, Health Plans and Hospitals uses the applicable incremental borrowing rate at lease commencement to

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

perform lease classification tests and to measure lease liabilities and right-of-use assets. Lease expense for operating lease payments is recognized on a straight-line basis over the lease term.

Health Plans and Hospitals has agreements with lease and non-lease components (such as common area maintenance), and generally has elected to account for the lease and non-lease components as a single lease component. For certain leases, such as service contracts with real estate and supply contracts with equipment leases, the lease and non-lease components are accounted for separately. Health Plans and Hospitals elected not to recognize right-of-use assets and lease liabilities that arise from short-term leases (i.e. leases with terms of 12 months or less).

**(y) Reclassifications**

Certain reclassifications have been made in these combined financial statements to conform 2020 information to the 2021 presentation.

**(3) Investments**

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

At September 30, 2021, 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	\$ 584	\$ —	\$ —	\$ 584
Debt securities issued by the U.S. government	—	2,452	—	2,452
Debt securities issued by U.S. government agencies and corporations	—	9	—	9
Debt securities issued by U.S. states and political subdivisions of states	—	63	—	63
Foreign government debt securities	—	11	—	11
U.S. corporate debt securities	—	2,015	—	2,015
Foreign corporate debt securities	—	999	—	999
U.S. agency mortgage-backed securities	—	814	—	814
Non-U.S. agency mortgage-backed securities	—	74	—	74
Other asset-backed securities	—	855	—	855
Short-term investment funds	—	498	—	498
Total	\$ 584	\$ 7,790	\$ —	\$ 8,374

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At September 30, 2021, 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	\$ 4,862	\$ 296	\$ —	\$ 5,158
Foreign equity securities	3,209	439	—	3,648
Global equity funds	—	4,487	—	4,487
Debt securities issued by the U.S. government	—	6,024	—	6,024
Debt securities issued by U.S. government agencies and corporations	—	154	—	154
Debt securities issued by U.S. states and political subdivisions of states	—	1	—	1
Foreign government debt securities	—	534	—	534
U.S. corporate debt securities	—	683	—	683
Foreign corporate debt securities	—	540	—	540
U.S. agency mortgage-backed securities	—	6	—	6
Non-U.S. agency mortgage-backed securities	—	13	1	14
Other asset-backed securities	—	39	—	39
Short-term investment funds	—	3,080	—	3,080
Other	—	146	1	147
	<u>\$ 8,071</u>	<u>\$ 16,442</u>	<u>\$ 2</u>	<u>24,515</u>
Alternative investments:				
Absolute return				2,782
Private equity				<u>17,706</u>
Total			\$	<u>45,003</u>

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At December 31, 2020, the estimated fair value of current investments by level was as follows (in millions):

	<b>Quoted prices in active markets for identical assets level 1</b>	<b>Significant other observable inputs level 2</b>	<b>Significant unobservable inputs level 3</b>	<b>Total</b>
U.S. equity securities	\$ 678	\$ —	\$ —	\$ 678
Debt securities issued by the U.S. government	—	1,967	—	1,967
Debt securities issued by U.S. government agencies and corporations	—	14	—	14
Debt securities issued by U.S. states and political subdivisions of states	—	69	—	69
Foreign government debt securities	—	31	—	31
U.S. corporate debt securities	—	2,462	—	2,462
Foreign corporate debt securities	—	1,012	—	1,012
U.S. agency mortgage-backed securities	—	934	—	934
Non-U.S. agency mortgage-backed securities	—	155	—	155
Other asset-backed securities	—	871	—	871
Short-term investment funds	—	168	—	168
Total	\$ <u>678</u>	\$ <u>7,683</u>	\$ <u>—</u>	\$ <u>8,361</u>

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At December 31, 2020, 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	\$ 5,024	\$ 174	\$ —	\$ 5,198
Foreign equity securities	3,011	650	—	3,661
Global equity funds	—	3,250	—	3,250
Debt securities issued by the U.S. government	—	6,614	—	6,614
Debt securities issued by U.S. government agencies and corporations	—	273	—	273
Debt securities issued by U.S. states and political subdivisions of states	—	2	—	2
Foreign government debt securities	—	618	—	618
U.S. corporate debt securities	—	964	—	964
Foreign corporate debt securities	—	665	—	665
U.S. agency mortgage-backed securities	—	17	—	17
Non-U.S. agency mortgage-backed securities	—	33	1	34
Other asset-backed securities	—	53	—	53
Short-term investment funds	—	995	—	995
Other	—	141	1	142
	<u>\$ 8,035</u>	<u>\$ 14,449</u>	<u>\$ 2</u>	<u>22,486</u>
Alternative investments:				
Absolute return				2,820
Private equity				<u>10,180</u>
Total			\$	<u><u>35,486</u></u>



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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At September 30, 2021, available-for-sale debt and other securities were as follows (in millions):

	<u>Amortized cost</u>	<u>Gross unrealized gains</u>	<u>Gross unrealized losses</u>	<u>Fair value</u>
Debt securities issued by the U.S. government	\$ 8,178	\$ 298	\$ —	\$ 8,476
Debt securities issued by U.S. government agencies and corporations	156	7	—	163
Debt securities issued by U.S. states and political subdivisions of states	59	5	—	64
Foreign government debt securities	510	35	—	545
U.S. corporate debt securities	2,572	126	—	2,698
Foreign corporate debt securities	1,459	80	—	1,539
U.S. agency mortgage-backed securities	802	18	—	820
Non-U.S. agency mortgage-backed securities	84	4	—	88
Other asset-backed securities	875	19	—	894
Short-term investment funds	3,578	—	—	3,578
Other	147	—	—	147
Total	\$ <u>18,420</u>	\$ <u>592</u>	\$ <u>—</u>	\$ <u>19,012</u>

At December 31, 2020, available-for-sale debt and other securities were as follows (in millions):

	<u>Amortized cost</u>	<u>Gross unrealized gains</u>	<u>Gross unrealized losses</u>	<u>Fair value</u>
Debt securities issued by the U.S. government	\$ 8,396	\$ 185	\$ —	\$ 8,581
Debt securities issued by U.S. government agencies and corporations	276	11	—	287
Debt securities issued by U.S. states and political subdivisions of states	64	7	—	71
Foreign government debt securities	556	93	—	649
U.S. corporate debt securities	3,129	297	—	3,426
Foreign corporate debt securities	1,514	163	—	1,677
U.S. agency mortgage-backed securities	913	38	—	951
Non-U.S. agency mortgage-backed securities	178	11	—	189
Other asset-backed securities	884	40	—	924
Short-term investment funds	1,163	—	—	1,163
Other	142	—	—	142
Total	\$ <u>17,215</u>	\$ <u>845</u>	\$ <u>—</u>	\$ <u>18,060</u>

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

Available-for-sale debt and other securities by contractual maturity and mortgage-backed and other asset-backed debt securities were as follows (in millions):

	<b>At September 30, 2021</b>		<b>At December 31, 2020</b>	
	<b>Amortized cost</b>	<b>Fair value</b>	<b>Amortized cost</b>	<b>Fair value</b>
Due in one year or less	\$ 4,133	\$ 4,140	\$ 1,688	\$ 1,701
Due after one year through five years	5,107	5,217	4,595	4,833
Due after five years through ten years	1,454	1,528	2,103	2,302
Due after ten years	5,965	6,325	6,854	7,160
U.S. agency mortgage-backed securities	802	820	913	951
Non-U.S. agency mortgage-backed securities	84	88	178	189
Other asset-backed securities	875	894	884	924
Total	<u>\$ 18,420</u>	<u>\$ 19,012</u>	<u>\$ 17,215</u>	<u>\$ 18,060</u>

The carrying value of alternative investments, which may include absolute return, risk parity, and private equity, is reported under the equity method. The carrying value of alternative investments have been determined by management based on available data, including information provided by fund managers or the general partners. The underlying securities within absolute return and risk parity 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. 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.

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. Management meets with alternative investment fund managers periodically to assess portfolio performance and reporting and exercises oversight over fund managers. At September 30, 2021, Hospitals' had original commitments related to alternative investments of \$28.8 billion, of which \$16.2 billion was invested, leaving \$12.6 billion of remaining commitments. At December 31, 2020, Hospitals had original commitments related to alternative investments of \$19.9 billion, of which \$10.9 billion was invested, leaving \$9.0 billion of remaining commitments.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

For the nine months ended September 30, investment income – net was comprised of the following (in millions):

	<u>2021</u>	<u>2020</u>
Other-than-temporary impairment	\$ (861)	\$ (989)
Recognized gains	1,652	2,996
Recognized losses	(178)	(458)
Income from equity method alternative investments	3,449	291
Change in fair value from equity investments	452	(1,405)
Interest, dividends, and other income – net	429	639
Derivative income	174	737
	<u>5,117</u>	<u>1,811</u>
Total investment income – net		
Less investment income included in interest expense and other income (expense) – net	<u>(598)</u>	<u>(510)</u>
Investment income – net	<u>\$ 4,519</u>	<u>\$ 1,301</u>

Absolute return and private equity investments include redemption restrictions. Absolute return 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. At September 30, 2021, absolute return investments of \$412 million were subject to lock-up periods of up to two 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.

The majority of debt and equity securities or funds can be redeemed within 10 days. At September 30, 2021, equity investment funds of \$4.5 billion were redeemable between 10 and 30 days. At September 30, 2021, equity investment funds of \$423 million had a redemption period of between 30 days and one year. No debt or equity investments require a redemption period of greater than one year.

**(4) Derivative Instruments**

**(a) Interest Rate Swaps**

At both September 30, 2021 and December 31, 2020, Health Plans and Hospitals had 11 agreements to manage interest rate fluctuations (Interest Rate Swaps) with a total notional amount of \$1.1 billion. At September 30, 2021 and December 31, 2020, the fair values of these agreements were \$(254) million and \$(322) million, respectively, and were recorded in other long-term liabilities. For the nine months ended September 30, 2021 and 2020, Health Plans and Hospitals recorded \$25 million and \$22 million, respectively, in interest expense relating to the Interest Rate Swaps. For the nine months ended September 30, 2021 and 2020, net changes in fair values totaled \$68 million and \$(96) 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 both September 30,

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

2021 and December 31, 2020, no collateral was required to be posted by either Health Plans and Hospitals or the counterparties.

**(b) Derivatives Held in Investment Portfolios**

At September 30, 2021 and December 31, 2020, Health Plans and Hospitals' portfolio managers held \$45 million and \$(21) million, respectively, of futures, forwards, options, and swaps to attempt to protect certain investments against volatility. For the nine months ended September 30, 2021 and 2020, net changes in fair values totaled \$196 million and \$(45) million, respectively, and were recorded in investment income – net. For the nine months ended September 30, 2021 and 2020, gains (losses) resulting from derivative settlements totaled \$(90) million and \$878 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 *Summary of Significant Accounting Policies – 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 nine months ended September 30,	
		2021	2020
Interest rate swaps – related to debt	Investment income – net	\$ 68	\$ (96)
Interest rate swaps – other	Investment income – net	(8)	(8)
Futures and forwards	Investment income – net	198	(32)
Options, rights, and warrants	Investment income – net	6	(5)
		<u>\$ 264</u>	<u>\$ (141)</u>

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**Information on Derivative Settlement Costs  
Recognized in Income**

(In millions)

<b>Derivatives not designated as hedging instruments</b>	<b>Statement of operations category</b>	<b>Gain (loss) recognized in income on derivatives for the nine months ended September 30,</b>	
		<b>2021</b>	<b>2020</b>
Interest rate swaps – related to debt	Interest expense	\$ (25)	\$ (22)
Interest rate swaps – other	Investment income – net	58	(26)
Futures and forwards	Investment income – net	(156)	877
Options, rights, and warrants	Investment income – net	8	27
		<u>\$ (115)</u>	<u>\$ 856</u>

**Information on Fair Value of Derivative Instruments – Assets**

(In millions)

<b>Derivatives not designated as hedging instruments</b>	<b>Balance sheet category</b>	<b>Fair value at</b>	
		<b>September 30, 2021</b>	<b>December 31, 2020</b>
Interest rate swaps – other	Noncurrent investments	\$ 38	\$ 57
Futures and forwards	Noncurrent investments	43	36
Options, rights, and warrants	Noncurrent investments	1	2
		<u>\$ 82</u>	<u>\$ 95</u>

**Information on Fair Value of Derivative Instruments – Liabilities**

(In millions)

<b>Derivatives not designated as hedging instruments</b>	<b>Balance sheet category</b>	<b>Fair value at</b>	
		<b>September 30, 2021</b>	<b>December 31, 2020</b>
Interest rate swaps – related to debt	Other long-term liabilities	\$ 254	\$ 322
Interest rate swaps – other	Other long-term liabilities	13	22
Futures and forwards	Other long-term liabilities	22	86
Options, rights, and warrants	Other long-term liabilities	2	8
		<u>\$ 291</u>	<u>\$ 438</u>

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**(5) Accounts Receivable – Net**

Accounts receivable – net were as follows (in millions):

	<u>At September 30, 2021</u>	<u>At December 31, 2020</u>
Members' dues	\$ 1,119	\$ 931
Patient services	586	430
Medicare	466	448
Other	<u>1,175</u>	<u>1,491</u>
Total	<u>\$ 3,346</u>	<u>\$ 3,300</u>

At both September 30, 2021 and December 31, 2020, the allowances for bad debt were not material.

**(6) Inventories and Other Current Assets**

Inventories and other current assets were as follows (in millions):

	<u>At September 30, 2021</u>	<u>At December 31, 2020</u>
Inventories – net	\$ 1,295	\$ 1,281
Prepaid expenses	500	912
Other	<u>117</u>	<u>92</u>
Total	<u>\$ 1,912</u>	<u>\$ 2,285</u>

**(7) Land, Buildings, Equipment, and Software – Net**

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

	<u>At September 30, 2021</u>	<u>At December 31, 2020</u>
Land	\$ 2,501	\$ 2,429
Buildings and improvements	41,890	40,289
Furniture, equipment, and software	14,587	14,148
Construction and software development in progress	<u>2,800</u>	<u>2,720</u>
	61,778	59,586
Accumulated depreciation and amortization	<u>(32,509)</u>	<u>(30,704)</u>
Total	<u>\$ 29,269</u>	<u>\$ 28,882</u>

Health Plans and Hospitals capitalizes 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 the nine months ended

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

September 30, 2021 and 2020, Health Plans and Hospitals capitalized \$48 million and \$49 million, respectively, of interest in connection with various capital projects.

**(8) Medical Claims Payable**

Activity in the liability for medical claims payable was as follows (in millions):

	<u>At September 30, 2021</u>	<u>At December 31, 2020</u>
Balances at January 1	\$ 2,611	\$ 2,341
Incurred related to:		
Current year	12,750	14,379
Prior years	<u>(325)</u>	<u>(121)</u>
Total incurred	<u>12,425</u>	<u>14,258</u>
Paid related to:		
Current year	10,241	12,190
Prior years	<u>2,092</u>	<u>1,798</u>
Total paid	<u>12,333</u>	<u>13,988</u>
Ending balances	\$ <u>2,703</u>	\$ <u>2,611</u>

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.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**(9) Other Liabilities**

Other current liabilities were as follows (in millions):

	<u>At September 30, 2021</u>	<u>At December 31, 2020</u>
Self-insured risks	\$ 463	\$ 458
Dues collected in advance	983	926
Physicians' retirement plan liability	255	255
Other	<u>1,695</u>	<u>1,681</u>
Total	<u>\$ 3,396</u>	<u>\$ 3,320</u>

Other long-term liabilities were as follows (in millions):

	<u>At September 30, 2021</u>	<u>At December 31, 2020</u>
Self-insured risks	\$ 1,859	\$ 1,805
Derivatives liability	291	438
Due to associated medical groups	318	313
Other	<u>431</u>	<u>296</u>
Total	<u>\$ 2,899</u>	<u>\$ 2,852</u>

**(10) Debt**

Debt was as follows (in millions):

	<u>At September 30, 2021</u>	<u>At December 31, 2020</u>
Tax-exempt revenue bonds and taxable bonds and notes:		
0.09% to 0.27% variable rate due through 2049	\$ 1,848	\$ 1,858
2.81% to 5.00% fixed rate due through 2051	10,789	8,172
Others at various rates due through 2047	<u>221</u>	<u>227</u>
Total	<u>\$ 12,858</u>	<u>\$ 10,257</u>
Other current debt:		
Commercial paper	\$ 366	\$ 366
Current portion of long-term debt	418	18
Long-term debt classified as a long-term liability	<u>12,074</u>	<u>9,873</u>
Total	<u>\$ 12,858</u>	<u>\$ 10,257</u>



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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

In June 2021, Hospitals issued \$2.7 billion of taxable fixed rate bonds at par value. The bonds consist of \$1.3 billion with a twenty-year term at a rate of 2.81% and \$1.4 billion with a thirty-year term at a rate of 3.00%.

The fair value of long-term debt is based on level 2 inputs for debt with similar risk, terms, and remaining maturities. At September 30, 2021 and December 31, 2020, the carrying amount of long-term debt totaled \$12.5 billion and \$9.9 billion, respectively. At September 30, 2021 and December 31, 2020, the estimated fair value of long-term debt was approximately \$13.5 billion and \$11.3 billion, respectively.

At both September 30, 2021 and December 31, 2020, repurchase of variable rate bonds totaling \$1.5 billion may be required at earlier than stated maturity. These bonds may be remarketed rather than repurchased. Health Plans and Hospitals has provided self liquidity for the variable rate demand bonds with put options. Additionally, at September 30, 2021 and December 31, 2020, management had the ability to finance the acquisition of up to \$3.0 billion and \$2.4 billion, respectively, of any unremarketed bonds that are put, using an available long-term credit facility. At both September 30, 2021 and December 31, 2020, none of these variable rate demand bonds were classified in current liabilities.

At September 30, 2021 and December 31, 2020, \$359 million and \$379 million, respectively, of the above tax-exempt fixed-rate revenue bonds and taxable fixed-rate bonds represented a net unamortized premium balance. At September 30, 2021 and December 31, 2020, \$(51) million and \$(38) million, respectively, of unamortized debt issuance cost was presented within long-term debt.

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 were as follows (in millions):

2021	\$	177
2022		989
2023		131
2024		16
2025		16
Thereafter		<u>11,221</u>
Total	\$	<u><u>12,550</u></u>

***Credit Facility***

Hospitals' credit facility of \$3.0 billion terminates in September 2026. Various interest rate options are available under this facility. Any revolving borrowings mature on the termination date. Hospitals pays facility fees, which range from 0.03% to 0.13% per annum, depending upon Hospitals' long-term senior unsecured debt rating. At September 30, 2021, the facility fee was at an annual rate of 0.04%. At both September 30, 2021 and December 31, 2020, no amounts were outstanding under this credit facility.

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

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

*Taxable Commercial Paper Program*

Hospitals maintains a commercial paper program providing for the issuance of up to \$2.4 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 September 30, 2021 and December 31, 2020, commercial paper of \$366 million was outstanding under this program and is included within other current debt.

**(11) Pension Plans**

**(a) Defined Benefit Plan**

Health Plans and Hospitals has 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 September 30, 2021 and December 31, 2020, pension fund assets were held in a group trust. At September 30, 2021 and December 31, 2020, trust assets were invested primarily in fixed-income and equity securities, with approximately 38% and 22%, respectively, of trust assets, net of liabilities, invested in alternative investments.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At December 31, 2020, the funded status of the Plan was as follows (in millions):

Change in projected benefit obligation (PBO):	
Benefit obligation at beginning of year	\$ 29,713
Service cost	1,808
Interest cost	887
Plan amendments	1
Net actuarial loss	5,166
Benefits paid	(1,137)
	<u>36,438</u>
Benefit obligation at end of year	\$ 36,438
Accumulated benefit obligation at end of year	\$ 26,947
Change in Health Plans and Hospitals' share of trust assets:	
Fair value of plan assets at beginning of year	\$ 26,061
Actual return on plan assets	3,137
Contributions	5,866
Benefits paid	(1,137)
	<u>33,927</u>
Fair value of plan assets at end of year	\$ 33,927
Funded status	\$ (2,511)
Amounts recognized in the combined balance sheets consist of:	
Noncurrent assets	\$ —
Other current liabilities	—
Pension and other retirement liabilities	(2,511)
	<u>(2,511)</u>
Amounts recognized in net worth:	
Net actuarial loss	\$ 12,663
Prior service cost	63
	<u>12,726</u>

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

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

The accrued pension plan liability at December 31, 2020 and the change through September 30, 2021 are as follows (in millions):

Accrued pension plan liability at December 31, 2020	\$ 2,511
Provision	569
Plan contributions	(206)
Plan amendments	55
Accrued pension plan liability at September 30, 2021	2,929
Less: current portion	-
Long-term portion of accrued pension liability at September 30, 2021	\$ 2,929

For the nine months ended September 30, pension expense was as follows (in millions):

	<u>2021</u>	<u>2020</u>
Service cost	\$ 1,594	\$ 1,356
Interest cost	578	665
Expected return on plan assets	(1,603)	(1,269)
Amortization of net actuarial loss	734	564
Amortization of prior service cost	9	6
Net pension expense	1,312	1,322
Other changes in plan assets and PBO recognized in net worth:		
Prior service cost	55	1
Amortization of net actuarial loss	(734)	(564)
Amortization of prior service cost	(9)	(6)
Total recognized in net worth	(688)	(569)
Total recognized in net periodic benefit cost and net worth	\$ 624	\$ 753

At December 31, 2020, the benefit obligation included a net actuarial loss of \$5.2 billion, primarily due to the decrease in the discount rate used to determine the benefit obligation from 3.40% in 2019 to 2.80% in 2020.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

Actuarial assumptions used were as follows:

	<u>2021</u>	<u>2020</u>
Discount rate at January 1 for calculating service cost	3.04%	3.57%
Discount rate at January 1 for calculating interest cost	2.18%	3.03%
Discount rate for calculating December 31 PBO	N/A	2.80%
Salary scale for calculating pension expense	4.20%	4.20%
Salary scale for calculating December 31 PBO	N/A	4.20%
Expected long-term rate of return on plan assets for calculating pension expense	6.75%	6.75%

During 2021, management expects to contribute approximately \$618 million to the Plan.

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

2021	\$ 1,167
2022	1,257
2023	1,356
2024	1,449
2025	1,547
2026–2030	9,120

*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

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

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.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At September 30, 2021, 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	Total
<b>Assets:</b>			
Cash and cash equivalents	\$ 904	\$ 3,007	\$ 3,911
Broker receivables	—	344	344
Securities lending collateral	—	1,448	1,448
U.S. equity securities	6,794	2,331	9,125
Foreign equity securities	5,059	225	5,284
Global equity funds	—	8,402	8,402
Debt securities issued by the U.S. government	—	5,868	5,868
Debt securities issued by U.S. government agencies and corporations	—	1	1
Debt securities issued by U.S. states and political subdivisions of states	—	379	379
Foreign government debt securities	—	415	415
U.S. corporate debt securities	—	7,608	7,608
Foreign corporate debt securities	—	944	944
U.S. agency mortgage-backed securities	—	20	20
Non-U.S. agency mortgage-backed securities	—	28	28
Other	—	309	309
<b>Total assets</b>	<b>12,757</b>	<b>31,329</b>	<b>44,086</b>
<b>Liabilities:</b>			
Broker payables	—	462	462
Securities lending payable	—	1,448	1,448
Other liabilities	583	853	1,436
<b>Total liabilities</b>	<b>583</b>	<b>2,763</b>	<b>3,346</b>
<b>Fair value of pension trust assets – net</b>	<b>\$ 12,174</b>	<b>\$ 28,566</b>	<b>40,740</b>
<b>Investments measured at net asset value (NAV):</b>			
Alternative investments:			
Absolute return			3,243
Private equity			21,496
<b>Total pension trust assets – net</b>			<b>\$ 65,479</b>

At September 30, 2021, Health Plans and Hospitals' share of pension trust assets was 56.3%, or \$36.8 billion. The remaining share of pension trust assets is for Medical Groups and a related party associated with Medical Groups.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At December 31, 2020, 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	Total
<b>Assets:</b>			
Cash and cash equivalents	\$ 5	\$ 4,872	\$ 4,877
Broker receivables	—	321	321
Securities lending collateral	—	1,257	1,257
U.S. equity securities	8,596	2,913	11,509
Foreign equity securities	6,912	260	7,172
Global equity funds	—	7,583	7,583
Debt securities issued by the U.S. government	—	5,276	5,276
Debt securities issued by U.S. government agencies and corporations	—	1	1
Debt securities issued by U.S. states and political subdivisions of states	—	356	356
Foreign government debt securities	—	498	498
U.S. corporate debt securities	—	7,779	7,779
Foreign corporate debt securities	—	990	990
U.S. agency mortgage-backed securities	—	145	145
Non-U.S. agency mortgage-backed securities	—	29	29
Other	—	331	331
<b>Total assets</b>	<b>15,513</b>	<b>32,611</b>	<b>48,124</b>
<b>Liabilities:</b>			
Broker payables	—	562	562
Securities lending payable	—	1,257	1,257
Other liabilities	12	200	212
<b>Total liabilities</b>	<b>12</b>	<b>2,019</b>	<b>2,031</b>
<b>Fair value of pension trust assets – net</b>	<b>\$ 15,501</b>	<b>\$ 30,592</b>	<b>46,093</b>
<b>Investments measured at net asset value (NAV):</b>			
Alternative investments:			
Absolute return			2,862
Private equity			10,456
<b>Total pension trust assets – net</b>			<b>\$ 59,411</b>



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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At December 31, 2020, Health Plans and Hospitals' share of pension trust assets was 57.1%, or \$33.9 billion. The remaining share of pension trust assets is for Medical Groups and a related party associated with Medical Groups.

The change in fair value of pension trust assets for the nine months ended September 30, 2021 is not reflected within the funded status of the pension and other retirement liabilities. The change in fair value of pension trust assets will be reflected in the funded status at December 31, 2021, the measurement date of the pension benefit obligation.

The target asset allocations for calculating pension expense were as follows:

	<u>2021 target</u>	<u>2020 target</u>
Equity securities	32%	45%
Debt securities	30%	30%
Alternative investments	38%	25%
Total	<u>100%</u>	<u>100%</u>

Alternative investments, which include absolute return and private equity, held in the pension trust are reported at NAV 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. At September 30, 2021, the pension trust had original commitments related to alternative investments of \$36.9 billion, of which \$19.2 billion was invested, leaving \$17.7 billion of remaining commitments. At December 31, 2020, the pension trust had original commitments related to alternative investments of \$21.7 billion, of which \$10.7 billion was invested, leaving \$11.0 billion of remaining commitments.

Absolute return and private equity investments include redemption restrictions. Absolute return 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. At September 30, 2021, absolute return investments of \$304 million were subject to lock-up periods of up to two 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.

The majority of debt and equity securities can be redeemed within 10 days. At September 30, 2021, equity investment funds of \$8.3 billion were redeemable between 10 and 30 days. No debt or equity investments require a redemption period of greater than 30 days.

**(b) Defined Contribution Plans**

Health Plans and Hospitals has defined contribution plans for eligible employees. Employer contributions and costs are typically based on a percentage of covered employees' eligible compensation. During the nine months ended September 30, 2021 and 2020, there were no required employee contributions. For the nine months ended September 30, 2021 and 2020, plan expense was \$319 million and \$313 million, respectively.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**(c) Multi-Employer Plans**

Health Plans and Hospitals participates 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.

For the nine months ended September 30, 2021 and 2020, Health Plans and Hospitals' participation in these plans is outlined in the table below. The "EIN/PN" column provides the Employer Identification Number (EIN) and the three-digit plan number (PN), if applicable. Unless otherwise noted, the most recent Pension Protection Act zone status available in 2021 and 2020 is for the plan's year-end in 2020 and 2019, 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 was 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 2021 and 2020 employer expense.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

Pension fund	EIN-PN	Pension Protection Act zone status		FIP/RP status pending / implemented	(in millions) Health Plans and Hospitals' contributions September 30,		Surcharge imposed	Health Plans and Hospitals' contributions to plan exceeded more than 5% of total contributions <sup>(1)</sup>		Expiration date of collective bargaining agreement
		2021	2020		2021	2020		2021	2020	
IUOE Stationary Engineers Local 39 Pension Fund <sup>(2)</sup>	946118939 -001	Green	Green	N/A	\$ 11	\$ 10	N/A	Yes	Yes	9/17/2021
Southern California United Food and Commercial Workers Unions and Drug Employers Pension Fund	516029925 -001	Red	Red	Implemented	5	5	No	Yes	Yes	11/1/2021
Oregon Retail Employees Pension Trust <sup>(3)</sup>	936074377 -001	Red	Red	Implemented	3	3	Yes	Yes	Yes	9/30/2021 - 10/31/2021
International Painters and Allied Trades Industry Pension Fund (IUPAT Industry Pension Fund)	526073909 -001	Red	Red	Implemented	1	1	No	No	No	6/30/2023
Other <sup>(4) (2)</sup>	Various	Green	Green	N/A	14	14	N/A	No	No	7/31/2021 - 6/30/2023
Other	Various	Yellow	Yellow	Implemented	10	10	No	No	No	10/31/2021 - 6/30/2023
Total expense					\$ 44	\$ 43				

<sup>(1)</sup> The majority of plans have a plan year end of December 31<sup>st</sup> and information is available via form 5500.

<sup>(2)</sup> Expired Agreements: IUOE Stationary Engineers Local 39 expired as of September 17, 2021 and IUOE Local 701 Trust Fund expired July 31, 2021.

<sup>(3)</sup> Includes UFCW Local 555 Pharmacy Techs and Radiologists expiring September 30, 2021 and October 31, 2021, respectively.

<sup>(4)</sup> Local 180 was previously reported individually. Beginning Q3 2020 Kaiser is no longer a 5% contributor and is now included in the "Other" Green status row.

**(12) 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, vision benefits, and contributions to health care savings accounts.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At December 31, 2020, the accrued liability for postretirement benefits was as follows (in millions):

Change in benefit obligation:	
Benefit obligation at beginning of year	\$ 6,033
Service cost	175
Interest cost	177
Plan amendments	(1)
Benefits paid or provided	(174)
Net actuarial loss	49
Benefit obligation at end of year	<u>\$ 6,259</u>
Change in plan assets:	
Fair value of plan assets at beginning of year	5,203
Actual return on plan assets	549
Contributions	99
Benefits paid or provided	(174)
Fair value of plan assets at end of year	<u>\$ 5,677</u>
Funded status	<u>\$ (582)</u>
Amounts recognized in the combined balance sheets consist of:	
Noncurrent assets	\$ —
Other current liabilities	—
Pension and other retirement liabilities	(582)
	<u>\$ (582)</u>
Amounts recognized in net worth:	
Net actuarial loss	\$ 1,310
Prior service credit	(615)
	<u>\$ 695</u>

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

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

The accrued liability for postretirement benefits at December 31, 2020 and the change through September 30, 2021 are as follows (in millions):

Accrued postretirement benefits liability at December 31, 2020	\$ 582
Provision	45
Plan amendments	4
Plan contributions	—
Unfunded benefits paid or provided	(84)
Accrued postretirement benefits liability at September 30, 2021	547
Less: current portion	—
Long-term portion of accrued postretirement benefits liability at September 30, 2021	\$ 547

For the nine months ended September 30, postretirement benefits expense was as follows (in millions):

	<u>2021</u>	<u>2020</u>
Service cost	\$ 137	\$ 132
Interest cost	103	133
Expected return on plan assets	(195)	(246)
Amortization of net actuarial loss	56	57
Amortization of prior service credit	(249)	(301)
Postretirement benefits expense	(148)	(225)
Other changes in plan assets and benefit obligations recognized in net worth:		
Prior service cost (credit)	4	(1)
Amortization of net actuarial loss	(56)	(57)
Amortization of prior service credit	249	301
Total recognized in net worth	197	243
Total recognized in net periodic benefit cost and net worth	\$ 49	\$ 18

During the nine months ended September 30, 2021, employer contributions and benefits paid or provided were \$84 million and \$134 million, respectively. During the nine months ended September 30, 2020, employer contributions and benefits paid or provided were \$74 million and \$131 million, respectively. During 2021 and 2020, there were no participant contributions from active employees.

At December 31, 2020, the benefit obligation included a net actuarial loss of \$49 million, primarily due to the decrease in discount rates used to determine the benefit obligation from 3.40% in 2019 to 2.80% in 2020.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

Actuarial assumptions used were as follows:

	<u>2021</u>	<u>2020</u>
Discount rates at January 1 for calculating service cost	3.20%	3.68%
Discount rates at January 1 for calculating interest cost	2.22%	3.07%
Discount rate for calculating December 31 accumulated postretirement benefit obligation	N/A	2.80%
Expected long-term rate of return on plan assets for calculating benefits expense	5.00%	6.75%

The following were the assumed health care cost trend rates used to determine the December 31, 2020 benefit obligation and postretirement benefits expense for the nine months ended September 30, 2021 and 2020:

	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 – 2020	5.00% / 5.00%	5.75% / 5.75%	4.00%	4.50%	5.00%	4.50%	5.00% / 5.00%
Initial trend rate – 2021	5.00% / 4.75%	5.50% / 5.50%	4.00%	4.50%	4.75%	4.50%	5.00% / 4.75%
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	n/a	2022	n/a	2026 / 2022

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

2021	\$ 179
2022	193
2023	209
2024	225
2025	243
2026-2030	1,379

*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 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

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

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 benefit 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 September 30, 2021, the estimated fair value of retirement benefit trust assets – net by level was as follows (in millions):

	<b>Quoted prices in active markets for identical assets level 1</b>	<b>Significant other observable inputs level 2</b>	<b>Total</b>
<b>Assets:</b>			
Cash and cash equivalents	\$ —	\$ 33	\$ 33
Broker receivables	—	3	3
Other	—	3	3
Total assets	—	39	39
<b>Liabilities:</b>			
Other liabilities	—	2	2
Total liabilities	—	2	2
Total fair value of retirement benefit trust assets	\$ —	\$ 37	37
<b>Investments measured at NAV:</b>			
Alternative investments:			
Absolute return			101
Risk parity			5,911
Total retirement benefit trust assets			\$ 6,049

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At December 31, 2020, the estimated fair value of retirement benefit trust assets – net by level was as follows (in millions):

	<b>Quoted prices in active markets for identical assets level 1</b>	<b>Significant other observable inputs level 2</b>	<b>Total</b>
<b>Assets:</b>			
Cash and cash equivalents	\$ 4	\$ —	\$ 4
Other	—	3	3
Total assets	4	3	7
<b>Liabilities:</b>			
Other liabilities	—	2	2
Total liabilities	—	2	2
Total fair value of retirement benefit trust assets	\$ 4	\$ 1	5
<b>Investments measured at NAV:</b>			
Alternative investments:			
Absolute return			216
Risk parity			5,456
Total retirement benefit trust assets			\$ 5,677

The change in fair value of postretirement benefit trust assets for the nine months ended September 30, 2021 is not reflected within the funded status of pension and other retirement liabilities. The change in fair value of postretirement benefit trust assets will be reflected in the funded status at December 31, 2021, the measurement date of the postretirement benefit obligation.

The target asset allocations for calculating postretirement benefits expense were as follows:

	<b>2021 target</b>	<b>2020 target</b>
Equity securities	0%	45%
Debt securities	0%	30%
Alternative investments	100%	25%
Total	100%	100%

Alternative investments, which include absolute return and risk parity, held in the retirement benefit trust are reported at NAV as a practical expedient for fair value. Absolute return investments use



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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

advanced investment strategies, including derivatives, to generate positive long-term risk adjusted returns. Risk parity funds use risk as the primary factor to allocate investments among asset classes.

Absolute return and risk parity 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. At September 30, 2021, absolute return investments of \$36 million were subject to lock-up periods of up to two years.

**(b) Multi-Employer Plans**

Health Plans and Hospitals participates 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 nine months ended September 30, 2021 and 2020, Health Plans and Hospitals' employer expense for current and retiree benefits was \$80 million and \$81 million, respectively.

**(13) 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.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

At December 31, 2020, the accrued liability for physicians' retirement plan was as follows (in millions):

Change in projected benefit obligation:	
Physicians' retirement plan liability at January 1	\$ 10,159
Service cost	557
Interest cost	315
Net actuarial loss	1,221
Benefits paid	(217)
Physicians' retirement plan liability at December 31	<u>\$ 12,035</u>
Accumulated benefit obligation at end of year	\$ 9,010
Change in plan assets:	
Fair value of plan assets at the beginning of year	\$ —
Company contributions	217
Benefits paid	(217)
Fair value of plan assets at end of year	<u>\$ —</u>
Funded status	\$ (12,035)
Amounts recognized in the combined balance sheets consist of:	
Noncurrent assets	\$ —
Other current liabilities	(255)
Physicians' retirement plan liability	(11,780)
	<u>\$ (12,035)</u>
Amounts recognized in net worth:	
Net actuarial loss	\$ 4,461

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.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

The accrued liability for the physicians' retirement plan liability at December 31, 2020 and the change through September 30, 2021 are as follows (in millions):

Accrued physicians' retirement plan liability at December 31, 2020	\$ 12,035
Provision	689
Payments	<u>(174)</u>
Accrued physicians' retirement plan liability at September 30, 2021	12,550
Less: current portion	<u>(255)</u>
Long-term portion of accrued physicians' retirement plan liability at September 30, 2021	<u>\$ 12,295</u>

For the nine months ended September 30, physicians' retirement plan provision was as follows (in millions):

	<u>2021</u>	<u>2020</u>
Service cost	\$ 482	\$ 418
Interest cost	207	236
Amortization of net actuarial loss	<u>151</u>	<u>113</u>
Total benefit expense	840	767
Expected return on assets – investment income included in interest expense and other income (expense) – net	<u>(598)</u>	<u>(510)</u>
Net benefit expense	<u>242</u>	<u>257</u>
Other changes in projected benefit obligations recognized in net worth:		
Amortization of net actuarial loss	<u>(151)</u>	<u>(113)</u>
Total recognized in net worth	<u>(151)</u>	<u>(113)</u>
Total recognized in net periodic benefit cost and net worth	<u>\$ 91</u>	<u>\$ 144</u>

At December 31, 2020, the benefit obligation included a net actuarial loss of \$1.2 billion, primarily due to the decrease in the discount rate used to determine the benefit obligation from 3.50% in 2019 to 2.95% in 2020.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

Actuarial assumptions used were as follows:

	<b>2021</b>	<b>2020</b>
Discount rate at January 1 for calculating service cost	3.27%	3.72%
Discount rate at January 1 for calculating interest cost	2.42%	3.17%
Discount rate for calculating December 31 PBO	N/A	2.95%
Salary scale for calculating pension expense	4.40%	4.40%
Salary scale for calculating December 31 PBO	N/A	4.40%
Expected long-term rate of return on designated investments for calculating benefit expense	6.75%	6.75%

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

2021	\$	255
2022		280
2023		306
2024		335
2025		360
2026–2030		2,176

**(14) Leases**

Health Plans and Hospitals leases land, medical office buildings, office space, data centers, and equipment. The remaining lease term for leases primarily ranges from 1-16 years. Many leases contain renewal options. For those contracts where options are reasonably certain to be exercised, Health Plans and Hospitals recognizes renewal options as part of the right-of-use assets and lease liabilities.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**Quantitative disclosures**

Lease assets and lease liabilities were as follows (in millions):

		<b>At September 30, 2021</b>	<b>At December 31, 2020</b>
<b>Assets</b>	<b>Classification</b>		
Operating	Operating lease right-of-use assets	\$ 1,227	\$ 1,326
Finance	Land, buildings, equipment, and software — net	203	211
	Total	<u>\$ 1,430</u>	<u>\$ 1,537</u>
<b>Liabilities</b>	<b>Classification</b>		
Current			
Operating	Other current liabilities	\$ 333	\$ 333
Finance	Other current debt	8	8
Noncurrent			
Operating	Operating lease liabilities	1,035	1,142
Finance	Long-term debt	214	220
	Total	<u>\$ 1,590</u>	<u>\$ 1,703</u>

For the nine months ended September 30, total lease costs incurred by lease type and type of payment were as follows (in millions):

	<b>2021</b>	<b>2020</b>
Operating lease cost	\$ 361	\$ 359
Finance lease cost:		
Amortization of lease assets	8	8
Interest on lease liabilities	4	5
Short-term lease cost	49	44
Variable lease cost	74	62
Total	<u>\$ 496</u>	<u>\$ 478</u>

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

For the nine months ended September 30, other supplemental quantitative disclosures were as follows (in millions):

	<u>2021</u>	<u>2020</u>
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash flows used for operating leases	\$ 380	\$ (361)
Financing cash flows used for finance leases	\$ (9)	\$ (8)
Additions to right-of-use assets obtained in the period from operating leases	\$ 136	\$ 114
Additions to right-of-use assets obtained in the period from finance leases	\$ —	\$ 4
Weighted-average remaining lease term (years):		
Operating leases	5.64	6.06
Finance leases	8.10	8.01
Weighted-average discount rate:		
Operating leases	3.00%	3.25%
Finance leases	2.37%	3.15%

At September 30, 2021, the undiscounted future lease payments under non-cancelable operating leases and finance leases, along with a reconciliation of the undiscounted cash flows to operating and finance lease liabilities were as follows (in millions):

Lease Maturity	<u>Operating leases</u>	<u>Finance leases</u>	<u>Total</u>
2021 remaining	\$ 96	\$ 3	\$ 99
2022	357	13	370
2023	305	126	431
2024	227	9	236
2025	162	9	171
Thereafter	353	98	451
Total lease payments	1,500	258	1,758
Less amount representing interest	(132)	(36)	(168)
Present value of undiscounted future cash flows	<u>\$ 1,368</u>	<u>\$ 222</u>	<u>\$ 1,590</u>

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

**(15) Commitments and Contingencies**

**(a) Purchase Commitments**

At December 31, 2020, minimum purchase commitments extending beyond one year were as follows (in millions):

2021	\$	550
2022		456
2023		312
2024		112
2025		114
Thereafter		222
Total	\$	<u>1,766</u>

During the nine months ended September 30, 2021 and 2020, Health Plans and Hospitals' total purchases under contracts with minimum purchase commitments were \$564 million and \$548 million, respectively.

**(b) Regulatory**

Health Plans is 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 September 30, 2021 and December 31, 2020, the regulatory net worth, so defined, exceeded the aggregate regulatory minimum requirements by approximately \$40.8 billion and \$34.0 billion, respectively.

Health Plans and Hospitals is 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, health care 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 business operations, Health Plans and Hospitals is 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, U.S. Office of Personnel Management, Occupational Safety and Health Administration, Drug Enforcement Administration (DEA), State Boards of Pharmacy, Food and Drug Administration, IRS, National Committee for Quality Assurance, and state departments of insurance.

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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

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.

**(c) *Litigation***

Health Plans and Hospitals is 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 Health Insurance Portability and Accountability Act 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 records 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 the opinion of management, based upon current facts and circumstances, and except as stated below with respect to particular matters, 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.

In September 2015, a lawsuit was filed seeking to have the State of California impose the gross premiums tax on Health Plan, Inc. In March 2020, Health Plan, Inc. obtained a favorable summary judgment decision at the trial court. Plaintiff has appealed this decision. 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.

Pursuant to civil subpoenas, Health Plans and Hospitals has provided documents and information to the U.S. Department of Justice (DOJ) and Department of Health and Human Services – Office of Inspector General relating to Medicare Part C risk adjustment practices, policies, and programs. On July 27, 2021, the Civil Division of the DOJ filed a notice indicating its intervention in certain aspects of lawsuits previously filed under seal against several Kaiser Permanente Medical Care Program entities. On October 25, 2021, the DOJ filed its complaint in intervention against those entities. The defendant entities intend to vigorously defend the case, but can provide no assurance as to the outcome of the



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

Notes to Combined Financial Statements

For the nine months ended September 30, 2021 and 2020

litigation. No reserves have been provided related to this matter; however, an unfavorable outcome in the litigation could have a material adverse effect.

On September 17, 2019, the DEA served administrative inspection warrants at eight Health Plans and Hospitals pharmacies in six states, as part of a broader investigation by the DOJ into Health Plans' and Hospitals' controlled substance prescribing practices, policies, and controls. Health Plans and Hospitals have been providing documents and information to the DEA and DOJ related to this matter. Although management is unaware at this time of any material undisclosed compliance risks relating to the investigation, the outcomes of this matter are inherently uncertain and could result in False Claims Act litigation, citations, fines, criminal penalties, termination of the Medicare provider status of a Hospitals' facility and other sanctions upon Health Plans and Hospitals. No reserves have been provided related to this matter.