GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Consolidated Financial Statements and Supplemental Information

December 31, 2013 and 2012

(With Independent Auditors' Report Thereon)

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Table of Contents

	Page(s)
Independent Auditors’ Report	1–2
Consolidated Financial Statements:	
Consolidated Balance Sheets	3–4
Consolidated Statements of Operations and Changes in Net Assets	5
Consolidated Statements of Cash Flows	6
Notes to Consolidated Financial Statements	7–46
Supplemental Information	
Supplemental Consolidating Balance Sheet Information	47–48
Supplemental Consolidating Statement of Operations and Changes in Net Assets Information	49

KPMG LLP
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

Independent Auditors' Report

The Board of Trustees
Group Health Cooperative and Subsidiaries:

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Group Health Cooperative and its Subsidiaries (the Group), which comprise the consolidated balance sheets as of December 31, 2013 and 2012, and the related consolidated statements of operations and changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly in all material respects, the financial position of Group Health Cooperative and its Subsidiaries as of December 31, 2013 and 2012, and the results of their operations, and their cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

KPMG LLP is a Delaware limited liability partnership,
the U.S. member firm of KPMG International Cooperative
("KPMG International"), a Swiss entity.

Other Matter

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidating balance sheet information and statement of operations information included on pages 47 through 49 is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position and results of operations of the individual companies, and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

Seattle, Washington
April 9, 2014

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2013 and 2012

(In thousands)

Assets		2013	2012
Current assets:			
Cash and cash equivalents	$	212,244	71,272
Short-term marketable securities		12,709	20,211
Accounts receivable – net		120,216	135,025
Inventories		12,823	17,957
Other		27,317	32,501
Total current assets		385,309	276,966
Long-term marketable securities		894,677	832,178
Long-term investment – other		56,018	22,059
Funds held by trustee		8,848	8,848
Land, buildings and equipment:			
Land		31,022	23,275
Buildings and improvements		589,314	557,388
Equipment		491,541	471,548
Construction in progress		14,160	21,995
Total land, buildings, and equipment		1,126,037	1,074,206
Less accumulated depreciation		(700,125)	(655,353)
Land, buildings, and equipment – net		425,912	418,853
Other assets		62,595	56,303
Total	$	1,833,359	1,615,207

(Continued)

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2013 and 2012

(In thousands)

Liabilities and Net Assets	2013	2012
Current liabilities:		
Accounts payable	$ 113,011	100,891
External delivery services payable	224,011	240,199
Unearned premiums and deposits	54,344	33,901
Accrued employee compensation	84,392	69,084
Accrued taxes and interest	16,708	9,404
Current portion of long-term debt	5,271	5,045
Current portion of reserve for self-insurance	23,279	20,111
Current portion of retiree medical benefits	4,492	4,506
Total current liabilities	525,508	483,141
Noncurrent liabilities:		
Long-term debt	124,535	134,859
Self-insurance	50,459	49,436
Retiree medical benefits	41,509	45,510
Pension	78,089	219,361
Other	42,877	33,467
Total noncurrent liabilities	337,469	482,633
Total liabilities	862,977	965,774
Net assets:		
Unrestricted	953,765	635,709
Temporarily restricted	7,349	5,568
Permanently restricted	9,268	8,156
Total net assets	970,382	649,433
Total	$ 1,833,359	1,615,207

See accompanying notes to consolidated financial statements.

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Consolidated Statements of Operations and Changes in Net Assets

Years ended December 31, 2013 and 2012

(In thousands)

		2013	2012
Revenues:			
Premiums	$	3,270,632	3,269,263
Clinical services revenue, net		282,003	254,963
Other		109,292	103,535
Total operating revenues		3,661,927	3,627,761
Expenses:			
External delivery services		1,793,798	1,891,300
Employee compensation		666,433	678,213
Group Health Permanente expense		392,822	367,137
Medical and operating supplies		292,087	290,910
Other expenses		157,101	154,081
Services purchased		126,211	141,945
Business taxes and insurance		84,034	88,600
Depreciation and amortization		58,166	57,513
Total operating expenses		3,570,652	3,669,699
Operating gain (loss)		91,275	(41,938)
Nonoperating income (expense):			
Investment income, net		73,383	32,322
Interest expense		(10,939)	(1,083)
Total nonoperating income		62,444	31,239
Excess (deficit) of revenues over expenses		153,719	(10,699)
Change in net unrealized investment gains and losses		17,830	29,261
Change in defined benefit pension and other post retirement plans		146,628	(67,770)
Other		(121)	(121)
Change in unrestricted net assets		318,056	(49,329)
Change in temporarily restricted net assets		1,781	1,395
Change in permanently restricted net assets		1,112	79
Change in net assets		320,949	(47,855)
Net assets:			
Beginning of year		649,433	697,288
End of period	$	970,382	649,433

See accompanying notes to consolidated financial statements.

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended December 31, 2013 and 2012

(In thousands)

		2013	2012
Cash flows from operating activities:			
Change in net assets	$	320,949	(47,855)
Adjustments to reconcile change in net assets to net cash provided by operating activities:			
Depreciation and amortization		58,166	57,513
Provision for self-insurance		21,720	21,252
Change in realized and unrealized investments gains and losses		(17,766)	(35,502)
Change in fair value of interest rate swap		(6,198)	2,791
Recognized other-than-temporary impairment losses		20	385
Change in deferred gain on sale – leaseback		(2,917)	(2,917)
Equity income of equity method investees		(44,673)	(7,427)
Other		(7,667)	(3,101)
Cash provided by operating assets and liabilities:			
Accounts receivable – net		14,797	11,142
Inventories		5,134	5,763
Other current and noncurrent assets		4,194	(27,644)
Accounts payable		14,134	4,467
External delivery services payable		(16,188)	(13,859)
Accrued employee compensation		15,309	15,967
Self-insurance		(17,529)	(12,535)
Accrued taxes and interest		7,304	(8,734)
Unearned premiums and deposits		23,361	(24,286)
Pension		(141,272)	57,141
Retiree medical benefits		(4,015)	5,605
Other noncurrent liabilities		10,296	1,622
Net cash provided by (used in) operating assets and liabilities		237,159	(212)
Cash flows from investing activities:			
Payments for land, buildings, and equipment		(64,241)	(59,024)
Proceeds from disposal of land, buildings, and equipment		5,330	2,540
Proceeds from sale of marketable securities		344,196	514,009
Purchases of marketable securities		(382,055)	(733,073)
Distribution from equity investments		40,839	2,880
Purchases of equity investments		(30,245)	(250)
Net cash used in by investing activities		(86,176)	(272,918)
Cash flows from financing activities:			
Repayment of long-term debt		(9,890)	(4,595)
Net short-term borrowings		—	(8,998)
Other		(121)	(121)
Net cash used in financing activities		(10,011)	(13,714)
Net increase (decrease) in cash and cash equivalents		140,972	(286,844)
Cash and cash equivalents :			
Beginning of year		71,272	358,116
End of period	$	212,244	71,272
Supplemental disclosure of cash flow information:			
Cash paid during the year for:			
Interest	$	4,135	4,224
Income taxes		2,980	2,782

See accompanying notes to consolidated financial statements.

(1) Organization

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

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

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

KPS is a Washington taxable nonprofit corporation registered and operating as a health care service contractor headquartered in Bremerton, Washington. KPS provides health care services through contracts with participating physicians and hospitals.

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

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

(2) Summary of Significant Accounting Policies

(a) Principles of Consolidation

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

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

(b) Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements. Significant estimates and assumptions are used in the recording of external delivery services payable, fair value of financial instruments, allowances for uncollectible accounts, self-insurance reserves,

pension liabilities, retiree medical liabilities, and the evaluation of contingencies and litigation. Changes in these estimates and assumptions may have a material impact on the consolidated financial statements.

(c) Cash and Cash Equivalents

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

The Group is potentially subject to a concentration of credit risk related to financial instruments such as funds held at high credit quality financial institutions, and at times, such balances with any one financial institution may exceed the Federal Deposit Insurance Corporation's (FDIC) insured limits. In 2013, deposits held in noninterest bearing transaction accounts are aggregated with any interest bearing deposits and the combined total is insured up to $250,000.

(d) Marketable Securities

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

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

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

For debt securities, if the Group does not intend to sell or it is more likely than not it will be required to sell the security before recovery, OTTI is separated into the amount representing the credit loss and the amount related to all other factors. The credit component of the OTTI is recognized in income and the noncredit component is recognized as a component of the changes in net assets. The credit component of OTTI is determined by comparing the present value of projected future cash flows with the amortized cost basis of the fixed income security. The present value is calculated by discounting the projected future cash flows at the effective interest rate implicit in the fixed income maturity at the date of acquisition. For mortgage-backed and asset-backed securities, cash flow

estimates are based on assumptions regarding the underlying collateral including prepayment speeds, type of underlying assets, geographic concentrations, default rates, recoveries, and changes in value. For all other debt securities, cash flow estimates are driven by assumptions regarding probability of default, including changes in credit ratings, and estimates regarding timing and amount of recoveries associated with a default. Unrealized losses caused by noncredit related factors related to debt securities, for which the Group expects to fully recover the amortized cost basis, continue to be recognized as a component of net assets.

(f) Accounts Receivable

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

(g) Provision for Uncollectible Accounts and Retroactivity

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

The Group estimates the allowance for receivables of noncovered health care services, fee-for-service clinical services, and other receivables based on the aging of accounts receivable, historical collection experience, and other relevant factors. The allowance for uncollectible accounts was $3,451,000 and $4,093,000 at December 31, 2013 and 2012, respectively.

The allowance for receivables of premiums is based on aging of accounts receivable and historical experience of enrollment retroactive changes. The allowance for retroactivity was $2,234,000 and $2,600,000 as of December 31, 2013 and 2012, respectively.

(h) Inventories

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

(i) Long-Term Investments – Other

Long-term investment – other consists of equity and cost method investments, which includes a commingled securities trust.

(j) Fair Value Measurement for Alternative Investments

The Group may elect to measure alternative instruments, as defined by GAAP, using the net asset value (NAV) or its equivalent as a practical expedient if there is no readily determinable fair value. The election will occur at inception and on an instrument-by-instrument basis.

(k) Funds Held by Trustee

Funds held by trustee are assets restricted as to use pursuant to terms and conditions of the revenue bonds (see note 6).

The Series 2006 revenue bonds require a debt service reserve fund for the benefit of the bond owners, which shall be maintained as long as any Series 2006 bonds remain outstanding. The amount of the debt service reserve fund is $8,848,000 for December 31, 2013 and 2012.

(l) Charitable Gift Annuities

As of December 31, 2013 and 2012, the Foundation had a charitable gift annuities liability of $1,146,000 and $1,195,000, respectively, which is recorded as a component of other noncurrent liabilities in the accompanying consolidated balance sheets. Investments held for the charitable gift annuities are $2,129,000 and $2,432,000 as of December 31, 2013 and 2012, respectively, and are recorded as a component of other assets in the accompanying consolidated balance sheets.

(m) Land, Buildings, and Equipment

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

(n) Construction in Progress (CIP)

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

(o) Long-Lived Assets

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

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

(p) *Intangible Assets*

Intangible assets are recorded at fair value and those that are subject to amortization are amortized on a straight-line basis over their estimated useful lives, of 3 to 15 years. Intangible assets consist of trade name, favorable contracts and future compensation. As of December 31, 2013 and 2012, the net carrying amount was $675,000 and $860,000, respectively, and is a component of other assets in the accompanying consolidated balance sheets.

The Group performs an impairment review annually or when a triggering event occurs between annual impairment tests. Impairment losses of zero and $647,000 were recorded for the years ended December 31, 2013 and 2012, respectively, as a component of depreciation and amortization expense.

(q) *Notes Receivable*

Notes receivable relate to long-term financing arrangements that exceed one year and bear interest at a market rate based on negotiated terms and are recorded at face value. Interest is recognized over the life of the note. The Group requires collateral for notes for real estate transactions. The Group does not intend to sell these receivables. Amounts collected on notes receivable are included in net cash provided by investing activities in the consolidated statements of cash flows. In 2013, the Group financed a land and building sale, which increased the balance of notes receivable. Notes receivable balance was $27,679,000 and $1,769,000 at December 31, 2013 and 2012, respectively, and is a component of other noncurrent assets. At December 31, 2013, future annual payments on notes receivable due within one year is $823,000 and due in five years or more is $26,856,000.

(r) *Other Current Assets and Other Assets*

Other current assets and other assets consist of interest receivable, notes receivable, deferred financing costs, interest rate swap, deposits, prepaid assets, deferred tax assets and federal tax receivable.

(s) *Self-Insurance*

The Group is self-insured for professional liability, industrial accident claims, and unemployment benefits. The Group purchases excess insurance coverage to limit its exposure for professional liability claims and industrial accident claims and maintains excess insurance on a claims-made basis. Retention levels for professional liability are $10,000,000 per claim with annual aggregates of $40,000,000 and $50,000,000 in 2013 and 2012, respectively. Retention levels for industrial accident claims are $750,000 and $500,000, per claim and in aggregate, in 2013 and 2012, respectively. Professional liability and industrial accident claims liability are determined using case-based estimates for reported claims and actuarial estimates for incurred but not reported claims. These estimates are based on historical information along with certain assumptions about future events. Changes in assumptions related to expected claims development as well as changes in actual experience could cause these estimates to change. At December 31, 2013 and 2012, the estimated liability for professional liability claims was $61,652,000 and $57,703,000, respectively. At December 31, 2013 and 2012, the estimated liability for industrial accident claims was $7,942,000 and $8,075,000, respectively. At December 31, 2013 and 2012, the estimated liability for unemployment claims was $4,144,000 and $3,769,000, respectively. Insurance recovery receivables

for 2013 and 2012 are $1,732,000 and $1,631,000, respectively, and are a component of other assets. The Group recorded prepaid excess insurance premiums of $820,000 and $824,000 as of December 31, 2013 and 2012, respectively, as a component of other current assets. The Group is a subscriber of and purchases its professional liability excess insurance coverage from a Risk Retention Group (RRG). As a subscriber of the RRG, the Group is also an owner granting it rights to its subscriber's equity in the RRG. The Group's portion of the RRG's subscriber equity was $22,331,000 and $17,811,000 as of December 31, 2013 and 2012, respectively, and is included as a component of long-term investment-other.

(t) Reinsurance

The Group limits certain exposure to claims loss by ceding reinsurance to other insurance companies. KPS purchases reinsurance to limit its exposure on all of its insured contracts except the Federal Employees Health Benefit Plan and Medicare Supplemental products. Retention levels of $600,000 and $500,000 per claim with a coinsurance level of 90% were held in 2013 and 2012, respectively by KPS.

Reinsurance contracts do not relieve the Group from its obligations to claimants. Failure of reinsurers to honor their obligations could result in losses to the Group. The Group recorded reinsurance receivables of zero and $11,000 as of December 31, 2013 and 2012, respectively, as a component of accounts receivable.

(u) Derivatives

In certain instances, the Group enters into derivative instruments to hedge specific assets and liabilities, which are carried at fair value. Prior to entering into a derivative contract designated as a hedge, the relationship between the hedging instruments and the hedged items, as well as its risk management objective and strategy, is formally documented. On the date the Group enters into a derivative contract utilized as a hedge, the derivative instrument is designated as either a hedge of the fair value of a recognized asset or liability of an unrecognized firm commitment (known as a fair value hedge) or a hedge of the variability in expected future cash flows associated with an existing recognized asset or liability or a forecasted transaction (known as a cash flow hedge).

(v) Revenues

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

GHC participates in the Medicare Advantage program and offers both Medicare Advantage (MA) and Medicare Advantage Prescription Drug (MA-PD) plans. MA plans offer Part C Medicare benefits to members and GHC receives capitated revenue from the Centers for Medicare and Medicaid Services (CMS), as well as supplemental premiums from the member. MA-PD plans offer Part C and Part D Medicare benefits to members and GHC receives capitated revenue from CMS, as

well as supplemental premiums from the member. GHO offers MA-PD plans to its Medicare eligible members.

The capitated revenue from CMS for Part C and Part D is based on a Risk Adjustment model, where the demographic and health status (i.e. risk score) of the member is a factor used in determining payment. The other major factors of the capitated payment are the member's county of residence and the plan/product in which the member is enrolled. Capitated payments from CMS are received monthly and are prospective. Adjustments for enrollment and certain member status updates are made to the payments retrospectively. Various accruals related to Part C and Part D revenue as a result of the risk-sharing arrangement, as well as federal reinsurance, and low-income cost-sharing subsidies are recognized as well. Retrospective settlements of payment are made after the end of the calendar year.

In July 2012, GHC stopped participating as a health plan serving Medicaid patients. The care of Medicaid patients continues through a contractual arrangement with another health plan. Revenue for this care is a component of clinical services revenue.

The table below presents the balances of the significant operating revenue types for the years ended December 31, 2013 and 2012 (in thousands):

		2013	2012
Premiums:			
Group	$	2,094,836	2,153,999
Medicare		998,116	907,564
Individual and family		177,680	183,857
Medicaid		—	23,843
Total premiums		3,270,632	3,269,263
Clinical services revenue, net of contractual allowances and discounts		291,871	264,828
Less provision for bad debt		(9,868)	(9,865)
Clinical services revenue, net		282,003	254,963
Other revenue:			
Grants		46,559	46,573
Other		25,963	25,206
Self-funded administrative service fees		20,490	15,232
Sales		16,280	16,524
Total other		109,292	103,535
Total operating revenues	$	3,661,927	3,627,761

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

	2013	2012
Commercial/other	50%	42%
Private	45	52
Medicare	4	4
Medicaid	1	2
Total	100%	100%

There is a corresponding significant concentration of credit risk in net accounts receivable balances at December 31, 2013 and 2012:

	2013	2012
Private	48%	54%
Commercial/other	48	42
Medicare	3	3
Medicaid	1	1
Total	100%	100%

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

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

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

Reimbursement for inpatient services rendered to Medicare recipients has been made principally under a prospective pricing system based on diagnosis-related groups. Most outpatient services provided to Medicare patients are reimbursed based on prospectively determined rates. Medicaid patients are also reimbursed based on a combination of prospectively determined rates and cost reimbursement methodology. Continuation of these reimbursement programs at the present level,

and on the present basis, is dependent upon future policies of the federal and state governmental agencies.

The Medicare and Medicaid Electronic Health Records (EHR) Incentive Program provides incentive payments to eligible professionals and hospitals as they adopt, implement, upgrade and demonstrate meaningful use of certified EHR technology. The Group has eligible professionals, as well as an eligible hospital participating in the program. Incentives earned through this program are recognized in other revenues and were $4,853,000 and $6,921,000 for the years ended December 31, 2013 and 2012, respectively.

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

(w) Premium Deficiencies

A premium deficiency reserve is recognized when the expected future claims payments and administrative costs of a grouping of existing contracts exceed the premiums to be collected for the remainder of a contract period. Deficiencies in one grouping of contracts are not offset by anticipated surpluses in other groupings. The Group considers anticipated investment income in determining if a premium deficiency exists. Reserves are regularly reviewed and adjusted as experience develops or new information becomes known. Such adjustments would be included in current operations. No reserve was considered necessary at December 31, 2013 and 2012.

(x) Charity Care

Charity care represents medically necessary hospital-based care to patients who have demonstrated an inability to pay and receive care at a Group facility. Patients must have income at or less than 200% of the Federal Poverty Level. Only the portion of a patient’s account that meets the Group’s criteria is recognized as charity care. The method to estimate costs associated with charity care involves a ratio of gross charges. The cost of charity care was estimated at $939,000 and $1,078,000 for the years ended December 31, 2013 and 2012, respectively.

(y) External Delivery Services

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

(z) Group Health Permanente Expense

Group Health Permanente P.C. is an independent medical group with an exclusive contract to provide medical services at the Group's facilities providing primary, specialty, and inpatient care. The Group's net liability to Group Health Permanente P.C. was $41,911,000 and $25,339,000 as of December 31, 2013 and 2012, respectively, which is a component of accounts payable in the accompanying consolidated balance sheets.

(aa) Advertising

Advertising costs are expensed as incurred and are recorded within services purchased in the consolidated statements of operations and changes in net assets. The Group recorded advertising expense of $3,927,000 and $1,736,000 for the years ended December 31, 2013 and 2012, respectively.

(bb) Leases

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

The Group is obligated under capital leases covering certain equipment that expire at various dates during the next three years. Amortization of assets held under capital leases is included with depreciation.

(cc) Income Taxes

GHO and KPS are subject to federal income taxes. These companies file federal tax returns and are not subject to any state income tax filing requirements. GHC is exempt from federal income taxes under Section 501(a) of the Internal Revenue Code (the Code) as a charitable organization under Section 501(c)(3) of the Code, except for unrelated business income tax. The Foundation has received a determination letter from the Internal Revenue Service (IRS) that it is a tax-exempt public foundation in accordance with Section 501(c)(3) and a public charity in accordance with Section 170(b)(1)(A)(vi) of the Code. CMA is considered a disregarded entity for federal tax purposes and would be included with any GHC federal income tax filing.

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

(dd) Net Assets

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

Temporarily restricted net assets are available for the following purposes as of December 31, 2013 and 2012 (in thousands):

		2013	2012
Health care services	$	4,890	3,734
Health education		1,726	1,115
Health care research and development		649	640
Time restricted		84	79
Total temporarily restricted net assets	$	7,349	5,568

When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets. Permanently restricted net assets as of December 31, 2013 and 2012 are contributions restricted by the donor to be invested in perpetuity.

The change in temporarily restricted net assets was comprised of $1,347,000 and $1,563,000 of contributions, $(1,689,000) and $(1,582,000) of release from restrictions, and investment income of $2,123,000 and 1,414,000, for the years ended December 31, 2013 and 2012, respectively.

(ee) Reclassifications

Certain reclassifications have been made to the 2012 consolidated financial statements to conform to the 2013 consolidated financial statement presentation.

(ff) Accounting Changes

In October 2012, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2012-05, *Statement of Cash Flows (Topic 230): Not-for-Profit Entities: Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows*. ASU 2012-05 requires all cash receipts from the sale of donated financial assets to be classified as cash flows from operating activities with two exceptions related to donor limitations and restrictions. This standard was effective for the Group's 2013 consolidated financial statements. The adoption of this standard did not have a material impact on the Group's consolidated financial statements.

(gg) New Accounting Pronouncements

In July 2011, the FASB issued ASU No. 2011-06, *Other Expenses (Topic 720): Fees Paid to the Federal Government by Health Insurers (a consensus of the FASB Emerging Issues Task Force)*, which requires fees imposed on health insurers mandated by the Patient Protection and Affordable Care Act as amended by the Health Care and Education Reconciliation Act be estimated and recorded in full once the entity provides qualifying health insurance in the applicable calendar year in which the fee is payable. Once adopted, this standard will require the Group to record a deferred cost that is amortized to expense using a straight-line method. The estimated 2014 fee assessment is $27,910,000. This standard will be effective for the Group's 2014 consolidated financial statements.

In April 2013, the FASB issued ASU No. 2013-06, *Not-for-Profit Entities (Topic 958) Services Received from Personnel of an Affiliate (a consensus of the FASB Emerging Issues Task Force)*. ASU 2013-06 provides guidance to not-for-profit entities that receive services from personnel of an affiliate company, including shared services, for which they are not charged at least the approximate amount of the direct personnel costs. The recipient entity is required to recognize the services rendered at an amount equal to the cost incurred by the affiliate for the personnel providing the services. If recognizing the value at cost would result in a significant overstatement or understatement of the actual value of the services received, then fair value of the service rendered may be used. Presentation of these transactions should be similar to the presentation of other such expenses or assets and should not be presented as a contra-expense or contra-asset. Disclosures of these transactions are required in accordance with *Topic 850 Related Party Disclosures. Topic 954, Not-for-Profit, Business-Oriented Health Care Entities* is also updated to add references pointing back to these changes to Topic 958. The new standard is to be applied prospectively for fiscal years beginning after June 15, 2014. This standard will be effective for the Group's 2015 consolidated financial statements. The adoption of this standard is not expected to have a material impact on the Group's consolidated financial statements.

In July 2013, the FASB issued ASU No. 2013-11, *Income taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*. ASU 2013-11 requires an unrecognized tax benefit, or a portion of an unrecognized tax benefit, to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward. This standard will be effective for the Group's 2015 consolidated financial statements. The adoption of this standard is not expected to have a material impact on the Group's consolidated financial statements.

(Continued)

(3) Marketable Securities

Marketable securities as of December 31, 2013 and 2012 consist of the following (in thousands):

	2013			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Debt:				
U.S. government securities	$ 78,779	27	(3,111)	75,695
U.S. government agencies	52,419	28	(491)	51,956
Municipal debt securities	49,916	613	(1,911)	48,618
International government	5,852	18	(128)	5,742
Corporate debt securities	322,186	4,876	(2,476)	324,586
Mortgage-backed securities	145,024	527	(4,117)	141,434
Asset-backed securities	25,969	93	(118)	25,944
Collateralized mortgage obligations	10,790	169	(55)	10,904
Domestic equity securities:				
Mutual funds:				
Large blend	55,257	22,212	(153)	77,316
Large value	12,481	4,373	(300)	16,554
Large growth	1,956	1,269	—	3,225
Medium growth	10,919	2,792	—	13,711
Small blend	20,307	5,409	(11)	25,705
Small value	369	157	—	526
Small growth	243	281	—	524
Intermediate term	2,439	44	(13)	2,470
Other	3,866	1	(406)	3,461
Common stock:				
Communications	2,533	322	(7)	2,848
Consumer	8,884	2,012	(21)	10,875
Energy	3,038	450	(59)	3,429
Financial	6,216	1,349	(196)	7,369
Industrial	2,888	1,129	(5)	4,012
Technology	4,576	948	(54)	5,470
Other	3,416	607	(41)	3,982
Foreign equity securities:				
Mutual funds:				
Large value	32,960	8,064	—	41,024
Other	7	—	—	7
Total	$ 863,290	57,770	(13,673)	907,387

	2012			
	Amortized cost	**Gross unrealized gains**	**Gross unrealized losses**	**Fair value**
Debt:				
U.S. government securities	$ 88,723	1,524	(144)	90,103
U.S. government agencies	55,444	826	(7)	56,263
Municipal debt securities	46,020	2,015	(62)	47,973
International government	2,349	44	—	2,393
Corporate debt securities	315,802	9,562	(272)	325,092
Mortgage-backed securities	126,292	3,048	(240)	129,100
Asset-backed securities	12,405	100	(11)	12,494
Collateralized mortgage obligations	24,559	546	(33)	25,072
Domestic equity securities:				
Mutual funds:				
Large blend	78,784	6,416	(346)	84,854
Large value	12,173	1,111	(140)	13,144
Large growth	1,936	526	—	2,462
Medium growth	10,919	308	(224)	11,003
Small blend	8,001	288	(151)	8,138
Small value	12,650	748	(14)	13,384
Small growth	243	139	—	382
Intermediate term	2,363	124	(1)	2,486
Other	4,829	96	(469)	4,456
Common stock:				
Communications	1,281	27	(9)	1,299
Consumer	4,084	87	(103)	4,068
Energy	1,483	17	(14)	1,486
Financial	2,709	135	(12)	2,832
Industrial	1,421	59	(4)	1,476
Technology	2,334	13	(88)	2,259
Other	1,713	66	(18)	1,761
Foreign equity securities:				
Mutual funds:				
Large value	8,266	169	(35)	8,400
Other	9	—	—	9
Total	$ 826,792	27,994	(2,397)	852,389

Contractual maturities of debt securities held as of December 31, 2013 include the following (in thousands):

	Fair value				
	Within 1 year	After 1 year through 5 years	After 5 years through 10 years	After 10 years	Total fair value
Debt:					
U.S. government securities	$ 699	20,039	53,915	1,042	75,695
U.S. government agencies	100	43,723	7,728	405	51,956
Municipal debt securities	1,662	15,437	13,839	17,680	48,618
International government	—	3,742	2,000	—	5,742
Corporate debt securities	10,240	213,776	89,998	10,572	324,586
Mortgage-backed securities	8	1,076	5,298	135,052	141,434
Asset-backed securities	—	5,942	8,884	11,118	25,944
Collateralized mortgage obligations	—	3,605	1,148	6,151	10,904
Total	$ 12,709	307,340	182,810	182,020	684,879

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

The Group records investment income net of related expenses and consists of the following as of December 31, 2013 and 2012 (in thousands):

	2013	2012
Interest	$ 23,669	23,743
Realized gains on sale	45,712	11,342
Realized losses on sale	(1,424)	(306)
Dividends and capital gains	9,312	4,336
Amortization, accretion, and other	(3,866)	(6,408)
OTTI	(20)	(385)
Total investment income	$ 73,383	32,322

In January 2013, GHC's investment in the joint venture, Westlake Terry, LLC, sold two buildings that it had developed. GHC's portion of the gain from the sale was $35,922,000 and is included in realized gains.

The Group evaluates investment securities for OTTI losses based on qualitative and quantitative factors. The amount of OTTI losses on fixed income securities recognized was zero in 2013 and 2012, respectively. OTTI losses on equity investments recognized in income were $20,000 and $385,000 in 2013 and 2012, respectively.

The following tables show the fair value and gross unrealized losses of the Group's marketable securities with unrealized losses. These securities are aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2013 and 2012 (in thousands):

	Less than 12 months		12 months or greater		Total	
2013	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Debt:						
U.S. government securities	$ 70,605	(3,111)	—	—	70,605	(3,111)
U.S. government agencies	39,271	(491)	—	—	39,271	(491)
Municipal debt securities	25,061	(1,826)	1,097	(85)	26,158	(1,911)
International government	3,412	(128)	—	—	3,412	(128)
Corporate debt securities	118,043	(2,386)	3,263	(90)	121,306	(2,476)
Mortgage-backed securities	105,761	(3,808)	7,322	(309)	113,083	(4,117)
Asset-backed securities	16,017	(118)	—	—	16,017	(118)
Collateralized mortgage obligations	1,760	(49)	509	(6)	2,269	(55)
Domestic equity securities:						
Mutual funds:						
Large blend	—	—	973	(153)	973	(153)
Large value	52	(2)	1,016	(298)	1,068	(300)
Small blend	989	(11)	—	—	989	(11)
Intermediate term	440	(9)	62	(4)	502	(13)
Other	2,385	(38)	754	(368)	3,139	(406)
Common stock:						
Communications	702	(7)	—	—	702	(7)
Consumer	451	(21)	—	—	451	(21)
Energy	497	(59)	—	—	497	(59)
Financial	1,418	(196)	—	—	1,418	(196)
Industrial	118	(5)	—	—	118	(5)
Technology	1,497	(54)	—	—	1,497	(54)
Other	556	(41)	—	—	556	(41)
Total	$ 389,035	(12,360)	14,996	(1,313)	404,031	(13,673)

2012	Less than 12 months Fair value	Less than 12 months Unrealized losses	12 months or greater Fair value	12 months or greater Unrealized losses	Total Fair value	Total Unrealized losses
Debt:						
U.S. government securities	$ 14,136	(144)	—	—	14,136	(144)
U.S. government agencies	2,114	(7)	—	—	2,114	(7)
Municipal debt securities	6,838	(62)	—	—	6,838	(62)
Corporate debt securities	34,585	(205)	1,629	(67)	36,214	(272)
Mortgage-backed securities	16,373	(216)	744	(24)	17,117	(240)
Asset-backed securities	3,619	(11)	—	—	3,619	(11)
Collateralized mortgage obligations	2,502	(28)	489	(5)	2,991	(33)
Domestic equity securities:						
Mutual funds:						
Large blend	272	(2)	802	(344)	1,074	(346)
Large value	4	—	568	(140)	572	(140)
Medium growth	6,776	(224)	—	—	6,776	(224)
Small blend	3,849	(151)	—	—	3,849	(151)
Small value	349	(8)	56	(6)	405	(14)
Intermediate term	72	(1)	4	—	76	(1)
Other	243	(1)	1,750	(468)	1,993	(469)
Common stock:						
Communications	941	(9)	—	—	941	(9)
Consumer	2,202	(103)	—	—	2,202	(103)
Energy	673	(14)	—	—	673	(14)
Financial	335	(12)	—	—	335	(12)
Industrial	336	(4)	—	—	336	(4)
Technology	1,805	(88)	—	—	1,805	(88)
Other	544	(18)	—	—	544	(18)
Foreign equity securities:						
Mutual funds:						
Large value	—	—	2,471	(35)	2,471	(35)
Total	$ 98,568	(1,308)	8,513	(1,089)	107,081	(2,397)

The unrealized losses in the Group's marketable securities in 2013 were due primarily to changes in interest rates. The majority of debt security positions are investment grade and rated high quality, AA, or higher by Standard & Poor's rating agency. Securities with contractual payments are current and no payments were missed in 2013. The Group has the ability and intent to hold these investments until a recovery of fair value, which may be maturity, and considers these investments to be temporarily impaired.

(4) External Delivery Services Payable

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

		2013	2012
Balances at January 1	$	240,199	254,058
Incurred related to:			
Current year		1,815,994	1,903,569
Prior years		(22,196)	(12,269)
Total incurred		1,793,798	1,891,300
Paid related to:			
Current year		1,603,279	1,672,050
Prior years		206,707	233,109
Total paid		1,809,986	1,905,159
Balances at December 31	$	224,011	240,199

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

(5) Medical Loss Ratio (MLR)

Effective January 1, 2011, as part of the Patient Protection and Affordable Care Act (Health Care Reform), minimum medical loss ratios were mandated for all commercial fully insured medical plans with annual rebates owed to policyholders if the actual loss ratios, calculated in a manner prescribed by the U.S. Department of Health and Human Services (HHS), fall below certain targets (85% for large employer groups and 80% for small employer groups and individuals). HHS issued guidance specifying the types of costs that should be included in benefit expense for purposes of calculating medical loss ratios. The Group's medical loss ratios were above the minimum target levels and no liability for rebates was recorded in 2013 and 2012.

Beginning with the 2014 contract year, MA and MA-PD will become subject to MLR requirements similar to the commercial fully insured medical plans. The target medical loss ratios for the Medicare plans is 85%.

(6) Borrowing Arrangements

GHC has a commercial paper financing program under which notes may be issued from time to time up to the aggregate face amount of $75,000,000. The notes may be sold at a discount from the par amount to reflect an interest component to the maturity date. The maturity date of the notes will be 1 to 270 days and the notes are not subject to redemption prior to the maturity date. The notes are secured by GHC's gross

receivables, certain equipment, and a lien on certain real property. There were no issued notes outstanding under the program at December 31, 2013 and 2012.

Revenue bonds were issued through the Washington Health Care Facilities Authority (the Authority). As security for the repayment of the bonds, GHC has granted the Authority a security interest in its gross receivables, bond funds, and liens against certain facilities and equipment. The loan agreements for the revenue bonds require, among other restrictions, that GHC achieve certain minimum debt service coverage ratios. Management believes GHC was in compliance with all debt covenants at December 31, 2013 and 2012.

Long-term debt at December 31, 2013 and 2012 consists of the following (in thousands):

	Years of maturity		2013	2012
Revenue bonds:				
Series 2001, 4.00% to 5-3/8%, plus bond premium of $323 and $446 in 2013 and 2012, respectively	2013–2019	$	30,408	40,422
Series 2006, 4-1/2% to 5.00%, plus bond premium of $1,432 and $1,518 in 2013 and 2012, respectively	2022–2036		99,398	99,482
Subtotal			129,806	139,904
Less current portion			(5,271)	(5,045)
Total long-term debt		$	124,535	134,859

Future annual principal payments on long-term debt for each of the next five years and thereafter at December 31, 2013 are as follows (in thousands):

Years ending December 31:		
2014	$	5,400
2015		5,690
2016		6,005
2017		6,330
2018		6,660
Thereafter		97,965
Subtotal		128,050
Add unamortized premium net		1,756
Total	$	129,806

Interest paid during 2013 and 2012 was $4,135,000 and $4,224,000, respectively. Interest expense was $10,939,000 and $1,083,000 during 2013 and 2012, respectively, and the amount of interest capitalized

(Continued)

was $56,000 and $440,000 in 2013 and 2012, respectively. The effect of the interest rate swap increased interest expense by $3,206,000 in 2013 and decreased interest expense by $5,738,000 in 2012.

(7) Derivative Financial Instruments

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

(8) Disclosure about Fair Value of Financial Instruments

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

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

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

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

(a) Assets and Liabilities

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

(b) Notes Receivable

Long-term notes receivable are carried at face value; however, accounting standards require the Group to disclose the fair value. The fair value of the Group's long-term notes receivable is determined as the present value of future contractual cash flows discounted at an interest rate that reflects the risk inherent in those cash flows. The discount rate is 5% and approximates rates currently observed in publicly traded debt markets for debt of similar terms with companies with comparable credit risk. The fair value of the long-term notes receivable was $19,870,000 and $1,645,000 as of December 31, 2013 and 2012, respectively.

(c) Long-Term Debt

Long-term debt is carried at amortized cost; however, accounting standards require the Group to disclose the fair value. The fair value of the Group's long-term debt is based on quoted market prices in markets that are not active, which are Level 2 inputs. The fair value of the long-term debt was $118,420,000 and $138,133,000 as of December 31, 2013 and 2012, respectively.

(d) Marketable Securities, Funds Held by Trustee, Commingled Securities Trust and Interest Rate Swap

The table below presents the balances of assets and liabilities measured at fair value on a recurring basis as of December 31, 2013 and 2012 (in thousands):

		Fair value measurements at December 31, 2013 using		
	Fair value at December 31, 2013	**Quoted prices in active markets for identical assets (Level 1)**	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Marketable securities:				
Debt:				
U.S. government securities	$ 75,695	75,695	—	—
U.S. government agencies	51,956	—	51,956	—
Municipal debt securities	48,618	—	48,618	—
International government	5,742	—	5,742	—
Corporate debt securities	324,586	—	324,586	—
Mortgage-backed securities	141,434	—	141,434	—
Asset-backed securities	25,944	—	25,944	—
Collateralized mortgage obligations	10,904	—	10,904	—
Domestic equity securities:				
Mutual funds:				
Large blend	77,316	77,316	—	—
Large value	16,554	16,554	—	—
Large growth	3,225	3,225	—	—
Medium growth	13,711	13,711	—	—
Small blend	25,705	25,705	—	—
Small value	526	526	—	—
Small growth	524	524	—	—
Intermediate term	2,470	2,470	—	—
Other	3,461	3,461	—	—
Common stock:				
Communications	2,848	2,848	—	—
Consumer	10,875	10,875	—	—
Energy	3,429	3,429	—	—
Financial	7,369	7,369	—	—
Industrial	4,012	4,012	—	—
Technology	5,470	5,470	—	—
Other	3,982	3,982	—	—

	Fair value at December 31, 2013	Fair value measurements at December 31, 2013 using: Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Foreign equity securities:				
Mutual funds:				
Large value	$ 41,024	41,024	—	—
Other	7	—	—	7
Total marketable securities	$ 907,387	298,196	609,184	7
Funds held by trustee:				
Guaranteed investment contract	$ 8,848	—	—	8,848
Total funds held by trustee	$ 8,848	—	—	8,848
Long-term investment – other:				
Commingled securities trust	$ 30,582	—	—	30,582
Other assets:				
Interest rate swap	3,503	—	—	3,503

(Continued)

	Fair value at December 31, 2012	Fair value measurements at December 31, 2012 using		
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Marketable securities:				
Debt:				
U.S. government securities	$ 90,103	90,103	—	—
U.S. government agencies	56,263	—	56,263	—
Municipal debt securities	47,973	—	47,973	—
International government	2,393	—	2,393	—
Corporate debt securities	325,092	—	325,092	—
Mortgage-backed securities	129,100	—	129,100	—
Asset-backed securities	12,494	—	12,494	—
Collateralized mortgage obligations	25,072	—	25,072	—
Domestic equity securities:				
Mutual funds:				
Large blend	84,854	84,854	—	—
Large value	13,144	13,144	—	—
Large growth	2,462	2,462	—	—
Medium growth	11,003	11,003	—	—
Small blend	8,138	8,138	—	—
Small value	13,384	13,384	—	—
Small growth	382	382	—	—
Intermediate term	2,486	2,486	—	—
Other	4,456	4,456	—	—
Common stock:				
Communications	1,299	1,299	—	—
Consumer	4,068	4,068	—	—
Energy	1,486	1,486	—	—
Financial	2,832	2,832	—	—
Industrial	1,476	1,476	—	—
Technology	2,259	2,259	—	—
Other	1,761	1,761	—	—
Foreign equity securities:				
Mutual funds:				
Large value	8,400	8,400	—	—
Other	9	—	—	9
Total marketable securities	$ 852,389	253,993	598,387	9

	Fair value at December 31, 2012	Fair value measurements at December 31, 2012 using		
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Funds held by trustee:				
Guaranteed investment contract	$ 8,848	—	—	8,848
Total funds held by trustee	$ 8,848	—	—	8,848
Interest rate swap	$ 9,701	—	—	9,701

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows (in thousands):

	Fair value measurements using significant unobservable inputs (Level 3)				
	Marketable securities	Commingled securities trust	Funds held by trustee	Interest rate swap	Total
Beginning balance at January 1, 2012	$ 9	—	8,848	6,910	15,767
Total unrealized gains included in changes in net assets	—	—	—	2,791	2,791
Ending balance at December 31, 2012	9	—	8,848	9,701	18,558
Purchases	—	30,000	—	—	30,000
Sales	—	—	—	—	—
Total unrealized gains (losses) included in changes in net assets	(2)	582	—	(6,198)	(5,618)
Ending balance at December 31, 2013	$ 7	30,582	8,848	3,503	42,940

There were no transfers between assets with inputs with quoted prices in active markets for identical assets (Level 1) and assets with inputs with other observable inputs (Level 2) during the years ended December 31, 2013 and 2012.

(e) Commingled Securities Trust Net Asset Valuation

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

		Fair value at December 31, 2013	Redemption frequency	Redemption notice period
Commingled securities trust (a)	$	30,582	Monthly	30–60 days
Total	$	30,582		

a. This category is comprised of a long-term strategy to maximize returns by investing in high yield bank loan fund in 2013. This investment is reported at NAV and grouped with other Level 3 assets and liabilities. Additionally, it is accounted for under the equity method as the Group's ownership percentage in the fund was 34% as of December 31, 2013. The fair value option was elected.

At December 31, 2013 there were no outstanding funding commitments.

(9) Pension Plans

The Group sponsors two defined benefit plans (the Plans), a defined contribution plan (the DC Plan), three 401(k) plans, a 403(b) plan, and contributes to several union negotiated plans that collectively cover substantially all of its employees. The Group's policy is to fund pension costs for the Plans based on actuarially determined funding requirements, thereby accumulating funds adequate to provide for all accrued benefits. Contributions for the defined contribution plan are based on a percentage of covered employees' salaries. Matching contributions to the 401(k) and 403(b) plans are based on a percentage of participants' contributions as set forth in the plan agreements. The total expense for the defined benefit plans was $41,273,000 and $36,748,000 in 2013 and 2012, respectively, and the total expense for the other plans was $28,626,000 and $29,531,000 in 2013 and 2012, respectively.

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

KPS amended its defined benefit pension plan to freeze benefits in 2009. As a result, each active participant's pension benefit was determined based on the participant's compensation and duration of employment. The most significant financial effect is that no new benefits are being accrued after the date of freeze.

For the defined benefit plans, the actuarial cost method used in determining the net periodic pension cost is the projected unit credit cost method. At December 31, 2013 and 2012, net periodic pension expense related to the Group's participation in the Plans for 2013 and 2012 included the following components (in thousands):

		2013	2012
Service cost	$	27,829	24,778
Interest cost on projected benefits		30,804	31,522
Expected return on plan assets		(45,815)	(41,591)
Amortization of net loss		28,318	22,039
Actuarial loss		137	—
Net periodic benefit cost	$	41,273	36,748
Discount rate (preretirement)		4.15%–4.20%	4.80%–5.05%
Discount rate (postretirement)		4.10–4.20	4.75–4.80
Rate of increase in compensation levels		4.00	4.00
Expected return on plan assets		6.50–8.50	6.50–8.50

The Plans' funded status and amounts included in unrestricted net assets to be recognized as a component of net periodic pension cost as of December 31, 2013 and 2012 are shown in the following table (in thousands):

		2013	2012
Change in projected benefit obligation:			
Projected benefit obligation – beginning of year	$	758,822	640,952
Service cost		27,829	24,778
Interest cost		30,804	31,522
Employee after tax account		—	(6,032)
Actuarial loss (gain)		(89,040)	95,542
Mergers, sales, and closures		(10,419)	—
Benefits paid		(40,092)	(27,940)
Projected benefit obligation – end of year		677,904	758,822
Change in plan assets:			
Fair value of plan assets – beginning of year		539,461	478,732
Actual return on plan assets		63,446	54,701
Employee after tax account		—	(6,032)
Employer contributions		37,000	40,000
Benefits paid		(40,092)	(27,940)
Fair value of plan assets – end of year		599,815	539,461
Funded status	$	(78,089)	(219,361)

		2013	2012
Amounts recognized in unrestricted net assets consist of:			
Net actuarial loss	$	137,046	282,591
Accumulated benefit obligation – end of year		652,585	709,700
Discount rate (preretirement)		5.10%–5.25%	4.15%–4.20%
Discount rate (postretirement)		4.95–5.25	4.10–4.20
Rate of increase in compensation levels		4.00	4.00

The funded status is recorded as a component of noncurrent liabilities as of December 31, 2013 and 2012 in the consolidated balance sheets.

Expected amounts to be recognized as components of 2014 net periodic pension cost are as follows (in thousands):

Service cost	$	20,012
Interest cost on projected benefits		33,507
Expected return on plan assets		(51,819)
Amortization of net loss		9,439
Net periodic pension cost	$	11,139

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

The benefits expected to be paid in each of the next five years, and in the aggregate for the five fiscal years thereafter, as of December 31, 2013 are as follows (in thousands):

Years ending December 31:		
2014	$	43,126
2015		45,621
2016		47,317
2017		48,749
2018		49,613
2019 – 2023		257,360
Total	$	491,786

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

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

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

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

The Group participates in the Sound Retirement Trust, formerly Retail Clerks Pension Trust (Federal Identification Number 91-6069306), which includes Pharmacy and Optical employees under the United Food and Commercial Workers (UWFC) union. The collective bargaining agreement with Pharmacy employees expires June 30, 2016 and the Optical employees expires April 30, 2015. The most recent Pension Protection Act (PPA) zone status available is for the plan's year end of September 30, 2013. The zone status has been designated as red status. The zone status is based on information that the Group received from the plan and is certified by the plan's actuary. Among other factors, plans in the red zone are generally less than 65% funded, plans in the yellow zone are between 65% and 79% funded, and plans in the green zone are at least 80% funded. The Plan has a financial improvement plan (FIP) or rehabilitation plan that is pending or has been implemented. The contributions to the plan were $1,144,000 and $1,132,000 for the years ended December 31, 2013 and 2012, respectively. The Group's contributions represent less than five percent of total contributions to the plan. The Group paid a surcharge to the plan of 5% in 2013 and 2012. No minimum contributions are required for future periods.

(a) Investment Policies and Strategies

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

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

As of December 31, 2013 and 2012, the following table summarizes the target allocation range defined in the investment policies compared to the actual allocations of the Group's plan assets:

	2013		2012	
	Target allocation	**Actual allocation**	**Target allocation**	**Actual allocation**
Equity securities	30%–66%	58%	33%–57%	46%
Debt securities	14–45	30	18–60	49
Cash equivalents	0–5	1	0–5	—
Other investments	0–16	11	0–10	5

The investment policy emphasizes the following key objectives:

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

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

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

There are required employer contributions expected to be made to the Plans in 2014 of $40,000,000.

(c) Fair Value of Pension Assets

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

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

The table below presents the balances of plan assets measured at fair value on a recurring basis as of December 31, 2013 and 2012 (in thousands):

	Fair Value at December 31, 2013	Fair value measurements at December 31, 2013 using		
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Plan assets:				
Cash and cash equivalents	$ 11,489	11,489	—	—
Commingled trusts	170,794	—	170,794	—
Common stocks	170,530	170,530	—	—
Limited partnership	153,237	—	132,129	21,108
Private equity	27,996	—	—	27,996
Trust index fund	10,480	—	10,480	—
Mutual funds:				
Domestic equities:				
Large blend	2,287	2,287	—	—
Long-term bond	19,230	19,230	—	—
Intermediate-term bond	32,628	32,628	—	—
Foreign equities:				
Large blend	1,144	1,144	—	—
Total plan assets	$ 599,815	237,308	313,403	49,104

	Fair Value at December 31, 2012	Fair value measurements at December 31, 2012 using: Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Plan assets:				
Cash and cash equivalents	$ 8,993	8,993	—	—
Commingled trusts	187,303	—	187,303	—
Common stocks	129,308	129,308	—	—
Limited partnership	104,150	—	74,420	29,730
Private equity	6,949	—	—	6,949
Trust index fund	11,130	—	11,130	—
Mutual funds:				
Domestic equities:				
Large blend	6,138	6,138	—	—
Long-term bond	12,850	12,850	—	—
Intermediate-term bond	69,989	69,989	—	—
Foreign equities:				
Large blend	2,651	2,651	—	—
Total plan assets	$ 539,461	229,929	272,853	36,679

The changes in Level 3 plan assets measured at fair value on a recurring basis are summarized as follows (in thousands):

	Fair value measurements using significant unobservable inputs (Level 3): Limited partnership	Private equity	Total
Beginning balance at January 1, 2012	$ 26,594	1,833	28,427
Purchases, sales, and settlements	—	4,891	4,891
Total net gains (realized/unrealized)	3,136	225	3,361
Ending balance at December 31, 2012	29,730	6,949	36,679
Purchases, sales, and settlements	(10,000)	20,324	10,324
Total net gains (realized/unrealized)	1,378	723	2,101
Ending balance at December 31, 2013	$ 21,108	27,996	49,104

(Continued)

	Fair value measurements using significant unobservable inputs (Level 3)		
	Limited partnership	Private equity	Total
Net unrealized gains (losses) relating to assets held at December 31, 2012	$ 3,136	225	3,361
Net unrealized gains (losses) relating to assets held at December 31, 2013	(401)	662	261

There were no transfers between assets with inputs with quoted prices in active markets for identical assets (Level 1) and assets with inputs with other observable inputs (Level 2) during the years ended December 31, 2013 and 2012.

(d) Pension Net Asset Valuation

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

	Fair value at December 31, 2013	Redemption frequency	Redemption notice period
Commingled trust (a)	$ 170,794	Daily, Semi-monthly, Monthly	1–15 days
Limited partnership (b)	153,237	Daily, Monthly, Quarterly	5–15 days
Private equity (c)	27,996	—	—
Trust index fund (d)	10,480	Monthly	10 days
Total	$ 362,507		

a. This category is comprised of six different fund strategies: 1) An index fund that invests in treasury inflation protected securities. 2) An index fund that invests in U.S. investment grade bonds. 3) An index fund that invests in non-U.S. global equities. 4) A global index fund that invests in equities in energy, materials and agriculture industries. 5) An actively managed fund that invests in non-U.S. developed markets equities (Europe, Australia, Asia and Far East) employing a long-term value approach to stock selection. 6) An actively managed fund that invests in emerging market local debt employing a long-term strategy focused on income and capital appreciation.

b. This category is comprised of three fund strategies: 1) An index fund that invests in Russell 3000 equities that meet a defined criteria related to quality, stability and income. 2) An actively managed fund that invests in noninvestment grade bonds employing a long-term strategy focused on income and capital appreciation. 3) An actively managed fund that invests in noninvestment grade bonds with average maturities of 1 to 3 years.

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

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

At December 31, 2013 and 2012, the private equity investments have outstanding funding commitments totaling $45,429,000 and $25,421,000, respectively.

(10) Retiree Medical Plan

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

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

At December 31, 2013 and 2012, net periodic postretirement benefit cost is comprised of interest costs on accumulated benefit obligation of $2,351,000 and $2,326,000, respectively.

Amounts recognized in unrestricted net assets consisted of net actuarial losses of $8,745,000 and $10,551,000 at December 31, 2013 and 2012, respectively.

GHC's accumulated postretirement benefit obligation (APBO) is unfunded. The APBO is included in the components of the retiree medical benefits liability on the consolidated balance sheets at December 31, 2013 and 2012, and comprises the following components (in thousands):

		2013	2012
Change in accumulated postretirement benefit obligation:			
Accumulated postretirement benefit obligation – beginning of year	$	50,016	44,411
Interest cost		1,805	2,192
Actuarial loss		(1,260)	7,997
Benefits paid		(4,560)	(4,584)
Accumulated postretirement benefit obligation – end of year	$	46,001	50,016
Change in plan assets:			
Employer contributions	$	4,560	4,584
Benefits paid		(4,560)	(4,584)

Future benefit costs were estimated assuming medical costs would increase at a 7.30% annual rate. A 1% increase in this annual trend rate would have increased the APBO at December 31, 2013, by $3,542,000 and the sum of service cost and interest cost for 2013 by $145,000. A 1% decrease in this annual trend rate would have decreased the APBO at December 31, 2013 by $3,128,000 and the sum of service cost and interest cost for 2013 by $129,000.

The weighted average discount rate used in determining the APBO was 3.65% in 2013 and 4.75% in 2012. The assumptions used to determine the APBO are measured at year-end. The weighted average discount rate used in determining the net periodic postretirement benefit cost was 4.35% in 2013 and 3.50% in 2012, and is based on beginning of year assumptions.

Expected amounts to be recognized as components of 2014 net periodic postretirement benefit cost are interest cost on projected benefits of $1,969,000 and amortization of net loss of $319,000.

GHC funds the plan as benefit payments are required. The expected benefit payments to be paid, and contributions to be made, in each of the next five years, and in the aggregate for the five fiscal years thereafter, as of December 31, 2013, are as follows (in thousands):

Years ending December 31:		
2014	$	4,492
2015		4,416
2016		4,360
2017		4,247
2018		4,106
2019 – 2023		18,103
Total	$	39,724

(11) Commitments and Contingencies

(a) Leases

The Group is obligated under capital leases covering certain equipment that expires at various dates during the next three years. At December 31, 2013 and 2012, the gross amount of equipment and related accumulated amortization recorded under capital leases were as follows (in thousands):

		2013	2012
Equipment	$	5,056	5,056
Less accumulated amortization		(1,464)	(254)
Net equipment under capital lease	$	3,592	4,802

The Group has various operating leases for land, buildings, and equipment. Total rent expense was $24,248,000 and $22,981,000 on these leases in 2013 and 2012, respectively. Total sublease rental revenue was $3,314,000 and $3,648,000 in 2013 and 2012, respectively, and is recorded as a component of other revenue. Future minimum rental payments, future minimum sublease rental receipts under noncancelable operating lease and sublease agreements, and future minimum capital lease payments as of December 31, 2013 are as follows (in thousands):

		Operating lease rental payments	Operating sublease rental receipts	Capital lease payments
Years ending December 31:				
2014	$	22,761	2,287	1,465
2015		21,292	1,818	1,463
2016		20,154	1,670	1,463
2017		14,183	1,540	—
2018		5,658	1,250	—
Thereafter		7,264	205	—
Total	$	91,312	8,770	4,391
Less amount representing interest (at rates ranging from 7.25% to 7.43%)				(466)
Present value of net minimum capital lease payments				3,925
Less current installments of obligations under capital leases				(1,215)
Obligations under capital leases, excluding current installments			$	2,710

GHC entered into a sale-leaseback transaction in 2006 involving the sale of its administrative main building located in Tukwila, Washington, and then entered into a 10-year operating lease with the purchaser. The gain on sale was deferred and is being amortized over 120 months with the amortization recorded in other expense in the consolidated statements of operations and changes in net assets. The deferred gain is a component of unearned premiums and deposits and other noncurrent liabilities in the consolidated balance sheets in the amount of $7,536,000 and $10,453,000 as of December 31, 2013 and 2012, respectively.

(b) *Labor*

Approximately 60% of GHC’s employees are covered under collective bargaining agreements. These employees provide nursing and other technical services to GHC. None of the collective bargaining agreements expire within one year. Bargaining disputes could adversely affect GHC.

(c) *Litigation*

The Group is involved in litigation and regulatory investigations arising in the normal course of business. After consultation with legal counsel, management estimates accruals, if any, that are

necessary related to these matters. Management believes the recorded amounts are adequate and the ultimate outcome of the matters will not have a material adverse effect on the Group's consolidated financial position or results of operations.

(d) Government Contracts

The Group's Medicare business primarily consists of products covered under MA and MA-PD contracts with the federal government. CMS performs coding audits to validate the supporting documentation maintained by health plans and their care providers. These coding audits may result in retrospective payment adjustments to health plans.

In February 2013, the Group received a subpoena from the United States Attorney's Office, Western District of New York, requesting information related to the Group's Medicare Advantage Risk Adjustment submissions made for payment years 2008 through 2012. The Group is in the process of responding to the request for information. No amounts have been accrued in the accompanying consolidated financial statements related to this matter as the investigation is in an early stage and it is not possible to estimate the possible loss or range of loss, if any.

(12) Federal Income Taxes

The components of income tax expense for GHO and KPS related to continuing operations and the change in unrestricted net assets for the years ended December 31, 2013 and 2012 are summarized as follows (in thousands):

		2013	2012
Federal income tax expense (benefit) on operations	$	928	(8,359)
Federal income tax expense (benefit) included in the change in unrestricted net assets		1,476	(340)
Federal income tax expense (benefit)	$	2,404	(8,699)

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

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

		2013	2012
Deferred tax asset	$	7,183	7,557
Deferred tax liability		(1,906)	(2,503)
Net deferred tax asset	$	5,277	5,054

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

No valuation allowance has been provided for the net deferred tax asset as management believes it is more likely than not that the entire amount will be realized. At December 31, 2013, the Group has net operating loss carryforwards for federal income tax purposes of $10,841,000, which expire between 2019 and 2033.

(13) Endowments

Endowment funds held at the Foundation consist of approximately 40 individual funds established for a variety of purposes and all are donor-restricted. The change in net assets associated with the endowment funds is classified and reported based on the existence or absence of donor-imposed restrictions. Donor-restricted endowment assets were $14,331,000 and $11,355,000 at December 31, 2013 and 2012, respectively, and are recorded in temporarily and permanently restricted net assets.

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

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

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

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

The Foundation policy limits spending in any calendar year to 5% of the fair market value of the endowments' three-year moving average. The Foundation may in any year choose to spend less than 5%. The Foundation may also choose to charge up to 1% of the endowment market value as an annual management fee. Total annual spending, including both management fee and spending allocations, cannot exceed the 5% limit. Newly received and named endowment funds are invested for one year before disbursements are made.

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

(14) Statutory Net Worth

GHC, GHO, and KPS (the Companies) are required to periodically file financial statements with regulatory agencies in accordance with statutory accounting and reporting practices. The Companies must comply with the minimum regulatory net worth requirements under the regulations of the Washington State Office of the Insurance Commissioner. Such requirements are generally based on 100% risk-based capital. The regulatory net worth, so defined, at December 31, 2013 and 2012 was $934,157,000 and $555,751,000, respectively. These balances exceed the minimum regulatory requirements at December 31, 2013 and 2012 by approximately $896,684,000 and $518,340,000, respectively.

(15) Patient Protection and Affordable Care Act

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

Health Care Reform requires public health exchanges be available in every state by January 1, 2014. GHC is offering individual products in the Washington State Health Benefit Exchange (WSHBE) in 2014. GHC and GHO will also offer products in the outside, non-Exchange market for both individuals and small groups. To deal with the potentially high-cost enrollees who will enter the market, Health Care Reform created a temporary reinsurance program for the individual market that will be in operation from 2014 to 2016. Health insurers are required to contribute to this program beginning in 2014.

Beginning in 2014, Health Care Reform imposes an annual fee on the health insurance sector of $8 billion and growing to $14.3 billion in 2018 that will be allocated to health insurers based on the written premium.

(16) Immaterial Correction of an Error

During the year ended December 31, 2013, the Group identified an error in the recording of an asset related to its ownership participation in RRG prior to January 1, 2012. As a result, the 2012 consolidated financial statements, including beginning net assets as of January 1, 2012, have been restated from amounts previously reported as follows (in thousands):

		2012	
	As previously reported	**As restated**	**Change**
At December 31:			
Long-term investment – other	$ —	17,811	17,811
Unrestricted assets	617,898	635,709	17,811
For the year ended December 31:			
Other revenue	104,930	103,535	(1,395)
Operating loss	(40,543)	(41,938)	(1,395)
Investment income	27,772	32,322	4,550
Excess (deficit) of revenues over expenses	(13,854)	(10,699)	3,155
Changes in net unrealized investments gains and losses	28,177	29,261	1,084
Change in unrestricted assets	(53,568)	(49,329)	4,239
Change in net assets	(52,094)	(47,855)	4,239
Net assets, end of the year	631,622	649,433	17,811

The impact to opening net assets for January 1, 2012 was an increase of $13,572,000.

(17) Subsequent Events

Subsequent events are events or transactions that occur after the consolidated balance sheet date but before financial statements are issued that provide additional evidence about conditions that existed at the date of the balance sheet. The Group has evaluated subsequent events for recognition or disclosure through April 9, 2014, the date these consolidated financial statements were available to be issued.

SUPPLEMENTAL INFORMATION

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Supplemental Consolidating Balance Sheet Information

December 31, 2013

(In thousands)

Assets		GHC	GHO	Foundation	KPS	CMA	Eliminations	Total
Current assets:								
Cash and cash equivalents	$	202,979	1,386	1,552	5,706	621	—	212,244
Short-term marketable securities		8,902	2,742	—	1,065	—	—	12,709
Accounts receivable – net		96,296	12,912	19	12,257	1,524	(2,792)	120,216
Receivable from affiliate		290	21,787	596	—	—	(22,673)	—
Inventories		12,823	—	—	—	—	—	12,823
Other		19,795	6,313	—	688	521	—	27,317
Total current assets		341,085	45,140	2,167	19,716	2,666	(25,465)	385,309
Long-term marketable securities		679,518	175,621	21,776	17,762	—	—	894,677
Long-term investment – other		55,892	467	—	—	—	(341)	56,018
Funds held by trustee		8,848	—	—	—	—	—	8,848
Land, buildings, and equipment:								
Land		30,809	—	—	—	—	213	31,022
Buildings and improvements		580,219	—	—	—	1,600	7,495	589,314
Equipment		484,291	—	—	4,951	2,244	55	491,541
Construction in progress		14,160	—	—	—	—	—	14,160
Total land, buildings and equipment		1,109,479	—	—	4,951	3,844	7,763	1,126,037
Less accumulated depreciation		(686,494)	—	—	(4,938)	(1,271)	(7,422)	(700,125)
Land, buildings, and equipment-net		422,985	—	—	13	2,573	341	425,912
Other assets		212,206	2,570	2,211	7,668	675	(162,735)	62,595
Total	$	1,720,534	223,798	26,154	45,159	5,914	(188,200)	1,833,359

(Continued)

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Supplemental Consolidating Balance Sheet Information

December 31, 2013

(In thousands)

Liabilities and Net Assets		GHC	GHO	Foundation	KPS	CMA	Eliminations	Total
Current liabilities:								
Accounts payable	$	94,194	10,037	383	6,848	1,565	(16)	113,011
External delivery services payable		144,357	68,645	—	12,226	—	(1,217)	224,011
Unearned premiums and deposits		24,033	30,053	—	258	—	—	54,344
Accrued employee compensation		82,911	246	—	802	433	—	84,392
Accrued taxes and interest		14,697	1,897	—	85	29	—	16,708
Current portion of long-term debt		5,271	—	—	—	—	—	5,271
Current portion of reserve for self-insurance		23,279	—	—	—	—	—	23,279
Current portion of retiree medical benefits		4,492	—	—	—	—	—	4,492
Liability to affiliate		22,374	—	1,290	290	9	(23,963)	—
Total current liabilities		415,608	110,878	1,673	20,509	2,036	(25,196)	525,508
Noncurrent liabilities:								
Long-term debt		124,535	—	—	—	—	—	124,535
Self-insurance		50,459	—	—	—	—	—	50,459
Retiree medical benefits		41,509	—	—	—	—	—	41,509
Pension		77,646	—	—	443	—	—	78,089
Other		40,395	—	1,416	1,292	44	(270)	42,877
Total noncurrent liabilities		334,544	—	1,416	1,735	44	(270)	337,469
Total liabilities		750,152	110,878	3,089	22,244	2,080	(25,466)	862,977
Commitments and contingencies (note 11)								
Net assets:								
Unrestricted		953,735	112,920	6,418	22,915	3,834	(146,057)	953,765
Temporarily restricted		7,349	—	7,349	—	—	(7,349)	7,349
Permanently restricted		9,298	—	9,298	—	—	(9,328)	9,268
Total net assets		970,382	112,920	23,065	22,915	3,834	(162,734)	970,382
Total	$	1,720,534	223,798	26,154	45,159	5,914	(188,200)	1,833,359

See accompanying independent auditors' report.

GROUP HEALTH COOPERATIVE AND SUBSIDIARIES

Supplemental Consolidating Statement of Operations and Changes in Net Assets Information

Year ended December 31, 2013

(In thousands)

	GHC	GHO	Foundation	KPS	CMA	Eliminations	Total
Revenues:							
Premium revenue	$ 2,275,520	893,606	—	108,449	—	(6,943)	3,270,632
Clinical services, net	282,613	—	—	—	18,822	(19,432)	282,003
Other	387,520	10,472	5,462	7,633	1,019	(302,814)	109,292
Total operating revenues	2,945,653	904,078	5,462	116,082	19,841	(329,189)	3,661,927
Expenses:							
External delivery services	1,144,450	768,463	—	102,580	—	(221,695)	1,793,798
Employee compensation	661,570	997	70	3,984	10,870	(11,058)	666,433
Group Health Permanente expense	385,241	—	—	—	7,581	—	392,822
Medical and operating supplies	290,929	37	55	74	1,014	(22)	292,087
Other expenses	127,992	21,742	4,176	3,035	3,268	(3,112)	157,101
Services purchased	122,875	90,788	935	4,149	912	(93,448)	126,211
Business taxes and insurance	56,709	25,740	—	914	671	—	84,034
Depreciation and amortization	57,350	—	—	23	793	—	58,166
Total operating expenses	2,847,116	907,767	5,236	114,759	25,109	(329,335)	3,570,652
Operating gain (loss)	98,537	(3,689)	226	1,323	(5,268)	146	91,275
Nonoperating income (expense):							
Investment income (loss)	65,545	4,608	1,243	370	(335)	1,952	73,383
Interest expense	(10,363)	(306)	—	(267)	(3)	—	(10,939)
Total other income (expense)	55,182	4,302	1,243	103	(338)	1,952	62,444
Excess (deficit) of revenues over expenses	153,719	613	1,469	1,426	(5,606)	2,098	153,719
Change in net unrealized investment gains and losses	17,830	(4,112)	—	(158)	—	4,270	17,830
Change in defined benefit pension and other postretirement plans	146,628	—	—	1,405	—	(1,405)	146,628
Capital contributions	—	—	—	—	5,600	(5,600)	—
Other	(121)	—	—	—	—	—	(121)
Change in unrestricted net assets	318,056	(3,499)	1,469	2,673	(6)	(637)	318,056
Change in temporarily restricted net assets	1,781	—	1,781	—	—	(1,781)	1,781
Change in permanently restricted net assets	1,112	—	1,112	—	—	(1,112)	1,112
Change in net assets	320,949	(3,499)	4,362	2,673	(6)	(3,530)	320,949
Net assets:							
Beginning of year	649,433	116,419	18,703	20,242	3,840	(159,204)	649,433
End of period	$ 970,382	112,920	23,065	22,915	3,834	(162,734)	970,382

See accompanying independent auditors' report.