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March 30, 2018

**VIA HAND DELIVERY**

Joseph DiMemmo, CPA  
Deputy Insurance Commissioner  
Office of Corporate and Financial Regulation  
Pennsylvania Insurance Department  
1345 Strawberry Square  
Harrisburg, PA 17120

**RECEIVED**  
Corporate & Financial Regulation

MAR 30 2018


**Pennsylvania  
Insurance Department**

**Re: Order # ID-RC-13-06  
Highmark Health Consolidated Financial Statements**

Dear Deputy Commissioner DiMemmo:

In compliance with Condition 13 of the above-captioned Approving Determination dated April 29, 2013, Highmark Health is submitting the enclosed non-confidential consolidated financial statements for the period ending December 31, 2017. A copy has been forwarded to Mr. Beaser and Mr. DeLacey by email.

Very truly yours,



Jack M. Stover

JMS/jls

Enclosure

cc: Lawrence J. Beaser, Esquire (via email)  
Patrick T. DeLacey (via Email)

# **Highmark Health**

**Consolidated Financial Statements**  
**December 31, 2017 and 2016**

**Highmark Health**  
**Index**  
**December 31, 2017 and 2016**

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## **Report of Independent Auditors**

To the Board of Directors of Highmark Health:

We have audited the accompanying consolidated financial statements of Highmark Health and its subsidiaries and affiliates (the "Company"), which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended.

### ***Management's Responsibility for the Consolidated Financial Statements***

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; 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 the 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 our 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, we consider internal control relevant to the Company'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 Company'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 Highmark Health and its subsidiaries and affiliates as of December 31, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Other Matter***

Accounting principles generally accepted in the United States of America require that the reconciliation of the Cumulative Incurred Claims and Allocated Claims Adjustment Expenses, Net of Reinsurance on pages 41 and 42 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Financial Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

PRICEWATERHOUSE COOPERS LLP

March 28, 2018

**Highmark Health**  
**Consolidated Balance Sheets**  
**December 31, 2017 and 2016**

*(in thousands of dollars)*

	<b>2017</b>	<b>2016</b>
<b>Assets</b>		
Cash and cash equivalents	\$ 2,354,529	\$ 1,510,771
Accounts receivable		
Insurance, less allowance for doubtful accounts of \$38,979 and \$49,384, respectively	2,207,252	2,335,487
Patient service, less allowance for doubtful accounts of \$47,176 and \$60,464, respectively	210,287	186,745
Other	175,060	165,235
Investments		
Debt securities, available-for-sale at fair value	2,923,676	2,937,648
Equity securities, available-for-sale at fair value	1,194,188	1,039,158
Board designated, restricted and other investments at fair value	837,041	634,561
Investment in affiliates	434,131	211,460
Other	195,265	136,693
Reinsurance recoverables	117,023	176,465
Securities lending invested collateral	112,429	163,592
Inventory, net	152,022	146,782
Income tax recoverable, net	18,221	41,689
Deferred income taxes, net	260,899	193,350
Property and equipment, net	1,820,033	1,785,039
Goodwill and other intangible assets, net	500,314	835,580
Prepaid pension plan assets	1,129	2,402
Other assets	599,507	536,390
Assets held for sale	-	243,787
<b>Total assets</b>	<b>\$ 14,113,006</b>	<b>\$ 13,282,834</b>
<b>Liabilities and Net Assets</b>		
Claims outstanding	\$ 2,571,476	\$ 2,608,533
Unearned revenue	214,281	211,888
Amounts held for others	654,088	698,260
Accrued salaries and benefits	374,504	365,214
Other payables and accrued expenses	1,052,612	895,922
Securities lending payable	112,423	163,523
Benefit plan liabilities	741,240	909,705
Debt	1,680,079	1,780,531
Other liabilities	247,399	242,720
Liabilities held for sale	-	232,722
<b>Total liabilities</b>	<b>7,648,102</b>	<b>8,109,018</b>
<b>Net Assets</b>		
Unrestricted - Highmark Health	6,027,983	4,876,658
Unrestricted - noncontrolling interest	128,527	16,093
<b>Total unrestricted</b>	<b>6,156,510</b>	<b>4,892,751</b>
Temporarily restricted	22,810	23,859
Permanently restricted	285,584	257,206
<b>Total net assets</b>	<b>6,464,904</b>	<b>5,173,816</b>
<b>Total liabilities and net assets</b>	<b>\$ 14,113,006</b>	<b>\$ 13,282,834</b>

The accompanying notes are an integral part of these Consolidated Financial Statements.

**Highmark Health**  
**Consolidated Statements of Operations**  
**Years Ended December 31, 2017 and 2016**

*(in thousands of dollars)*

	2017	2016
<b>Unrestricted revenue and other support</b>		
Premium revenue, net	\$ 13,139,665	\$ 13,445,678
Net patient service revenue	2,223,814	2,004,702
Vision revenue	1,351,158	1,384,973
Service revenue	1,510,879	1,396,604
Affiliates income (loss)	31,213	(4,823)
Net assets released from restriction	4,203	6,191
Total unrestricted revenue and other support	18,260,932	18,233,325
<b>Expenses</b>		
Claims and claim adjustment expenses	10,851,046	11,549,884
Salaries, wages and fringe benefits	3,775,617	3,642,678
Patient care supplies	606,405	559,973
Depreciation and amortization	302,500	281,793
Other operating expenses, net	2,109,688	2,136,495
Goodwill impairment	277,738	-
Total operating expenses	17,922,994	18,170,823
Operating gain	337,938	62,502
Net investment income, including net realized gains on investments	238,564	166,514
Interest expense	(69,335)	(60,274)
Gain on sale of subsidiary and consolidation of affiliate	609,465	-
Excess of revenue over expenses before income taxes	1,116,632	168,742
Income tax provision	51,585	109,182
Excess of revenue over expenses before noncontrolling interest	1,065,047	59,560
Excess of revenue over expenses attributable to noncontrolling interest	2,306	993
Excess of revenue over expenses attributable to Highmark Health	\$ 1,062,741	\$ 58,567

The accompanying notes are an integral part of these Consolidated Financial Statements.

**Highmark Health**  
**Consolidated Statements of Changes in Net Assets**  
**Years Ended December 31, 2017 and 2016**

*(in thousands of dollars)*

	2017	2016
<b>Unrestricted net assets - Highmark Health</b>		
Excess of revenue over expenses	\$ 1,062,741	\$ 58,567
Unrealized net holding gains on available-for-sale securities, net of tax of (\$70,822) and (\$27,901), respectively	123,515	60,212
Reclassification for net gains on available-for-sale securities included in income, net of tax of \$10,631 and \$2,558, respectively	(19,745)	(4,751)
Benefit plan asset and liability changes, net of tax of \$13,462 and and \$32,467, respectively	(17,459)	(130,392)
Net assets released from restriction for acquisition of equipment	809	1,274
Income tax benefit on transfers to related parties	-	12,500
Other, net	1,464	7,981
Increase in unrestricted net assets - Highmark Health	1,151,325	5,391
<b>Unrestricted net assets - noncontrolling interest</b>		
Excess of revenue over expenses	2,306	993
Recognition of noncontrolling interest	109,836	-
Other	292	1,031
Increase in unrestricted net assets - noncontrolling interest	112,434	2,024
<b>Temporarily restricted net assets</b>		
Contributions	2,644	2,486
Net investment income	2,437	1,384
Net assets released from restrictions used for:		
Operations	(4,203)	(6,191)
Acquisition of equipment	(809)	(1,274)
Other, net	(1,118)	1,874
Decrease in temporarily restricted net assets	(1,049)	(1,721)
<b>Permanently restricted net assets</b>		
Contributions	841	7
Net investment income	36,471	13,091
Transfer out of trusts to net investment income	(9,047)	(8,578)
Other, net	113	2
Increase in permanently restricted net assets	28,378	4,522
Increase in net assets	1,291,088	10,216
<b>Net assets</b>		
Beginning of the year	5,173,816	5,163,600
End of the year	\$ 6,464,904	\$ 5,173,816

The accompanying notes are an integral part of these Consolidated Financial Statements.



**Highmark Health**  
**Consolidated Statements of Cash Flows**  
**Years Ended December 31, 2017 and 2016**

*(in thousands of dollars)*

	2017	2016
<b>Cash flows from operating activities</b>		
Increase in net assets	\$ 1,291,088	\$ 10,216
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Bad debt expense	53,622	78,222
Depreciation and amortization, including investments	322,474	307,650
Change in premium deficiency reserves	-	(46,952)
Partial sale of subsidiary and consolidation of affiliate	(109,836)	-
Gain on sale of subsidiary and consolidation of affiliate	(609,465)	-
Goodwill impairment	277,738	-
Net realized gains on investments	(58,526)	(32,951)
Net unrealized gains on investments	(112,802)	(72,847)
Dividends received from affiliates	4,869	5,995
Undistributed (gain) loss of affiliates	(36,751)	1,737
Beneficial interest in perpetual trusts	(26,772)	-
Benefit plan asset and liability changes	17,459	130,392
Deferred income tax (benefit) provision	(122,650)	26,895
Income tax benefit on related party transfers	-	(12,500)
Restricted contributions	(3,485)	(2,493)
Increase (decrease) due to change in		
Accounts receivable	13,797	(134,323)
Reinsurance recoverables	245,995	(44,290)
Pharmacy rebates receivable	(69,098)	(3,661)
Other assets	(17,490)	33,685
Claims outstanding	(262,335)	(144,528)
Amounts held for others	(44,858)	198,213
Benefit plan liabilities, net	(199,386)	(120,711)
Other liabilities	125,776	147,459
Net cash provided by operating activities	<u>679,364</u>	<u>325,208</u>
<b>Cash flows from investing activities</b>		
Purchases of investments	(2,796,355)	(2,731,899)
Proceeds from sales of investments	2,146,785	2,457,969
Proceeds from maturities of investments	291,282	204,748
Net collection of notes receivable	25,837	1,345
Purchases of property and equipment, net	(311,879)	(308,161)
Change in securities lending invested collateral	51,100	16,803
Proceeds from sale of subsidiary and noncontrolling interest of subsidiary, net of cash included and transaction costs	853,569	-
Cash obtained in consolidation of affiliate	55,085	-
Cash included in assets held for sale	-	(21,704)
Net cash provided by (used in) investing activities	<u>315,424</u>	<u>(380,899)</u>
<b>Cash flows from financing activities</b>		
Restricted contributions	3,485	2,493
Change in book overdrafts	10,388	(2,432)
Receipts from contract deposits	317,563	332,931
Withdrawals from contract deposits	(280,131)	(336,686)
Change in securities lending payable	(51,100)	(16,803)
Proceeds from issuance of debt	1,019,196	84,864
Repayment of debt	(1,170,431)	(14,493)
Net cash (used in) provided by financing activities	<u>(151,030)</u>	<u>49,874</u>
Increase (decrease) in cash and cash equivalents	843,758	(5,817)
<b>Cash and cash equivalents</b>		
Beginning of year	1,510,771	1,516,588
End of year	<u>\$ 2,354,529</u>	<u>\$ 1,510,771</u>

The accompanying notes are an integral part of these Consolidated Financial Statements.

**Highmark Health**  
**Consolidated Statements of Cash Flows**  
**Years Ended December 31, 2017 and 2016**

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*(in thousands of dollars)*

	2017	2016
<b>Supplemental disclosure of cash flow information</b>		
Interest paid, net	\$ 71,224	\$ 62,105
Income taxes paid (collected), net	\$ 138,918	\$ (34,518)
<b>Supplemental disclosure of noncash investing and financing</b>		
Assets acquired through other payables	\$ 21,816	\$ (5,164)
Capital lease acquisitions	\$ 50,308	\$ -

The accompanying notes are an integral part of these Consolidated Financial Statements.

# Highmark Health

## Notes to Consolidated Financial Statements

### December 31, 2017 and 2016

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*(in thousands of dollars)*

#### 1. Nature of Operations

Highmark Health is incorporated as a nonprofit corporation in the Commonwealth of Pennsylvania and is federally recognized as a 501(c)(3). Highmark Health, through its affiliates, Highmark Inc. and its subsidiaries and affiliates (collectively "Highmark"), HM Health Solutions ("HMHS"), HM Health Holding Company ("HHHCO"), and Allegheny Health Network and its subsidiaries and affiliates (collectively "AHN"), is a diversified health and wellness enterprise based in Pittsburgh, Pennsylvania. Highmark Health, Highmark, HMHS, HHHCO and Allegheny Health are herein referred to as the "Corporation".

Highmark Inc. is incorporated as a nonprofit corporation and operates as a hospital plan corporation and a professional health services plan in the Commonwealth of Pennsylvania. Highmark Inc.'s affiliates, Highmark West Virginia Inc. ("Highmark WV") and Highmark BCBSD Inc. ("Highmark DE"), are nonprofit health services corporations and operate in the states of West Virginia and Delaware, respectively. As a licensee of the Blue Cross Blue Shield Association ("BCBSA"), Highmark underwrites various indemnity and managed care health insurance products for national accounts (groups headquartered in Pennsylvania, West Virginia and Delaware that have operations in other locations), regional accounts and individual accounts. In addition, Highmark also underwrites Medicaid, Medicare Advantage, Medicare Part D prescription drug and Medicare supplemental insurance products.

Highmark's diversified health business includes vision, dental and stop-loss business. Highmark Inc.'s wholly owned for-profit subsidiary, HVHC LLC ("HVHC"), operates a retail vision business, Visionworks of America, Inc. ("Visionworks"), and operated a managed vision care business, Davis Vision, Inc. ("Davis Vision"), through November 2017 (see Note 3). The retail line of business operates specialty optical retail stores, and the managed vision care line of business provides fully integrated eye care services. Highmark Inc.'s wholly owned for-profit subsidiary, United Concordia Companies, Inc. ("UCCI") and its subsidiaries, provide dental services through preferred provider and managed care networks as well as third party administrative services. Highmark Inc.'s other for-profit subsidiaries, including HM Insurance Group, Inc. ("HMIG") offer stop-loss insurance and other services.

HMHS is a for-profit corporation that provides health plan platform services, infrastructure management, data center hosting and print management.

HHHCO, a holding company, currently has one subsidiary that performs utilization management and care coordination services. Operations began during 2016 and are primarily intercompany.

AHN is incorporated as a nonprofit corporation in the Commonwealth of Pennsylvania and is federally recognized as a 501(c)(3). AHN's subsidiaries and affiliates primarily are nonprofit health care providers offering routine and tertiary healthcare services, clinical support and healthcare education in Western Pennsylvania. Additionally, AHN's other for-profit and nonprofit subsidiaries manage and develop outpatient medical facilities, which offer a variety of services including pharmacies, primary care and imaging and provide group hospital purchasing services.

**Highmark Health**  
**Notes to Consolidated Financial Statements**  
**December 31, 2017 and 2016**

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*(in thousands of dollars)*

**2. Acquisition**

On July 1, 2017, Highmark WV exercised a warrant to purchase up to 60% voting interest in West Virginia Family Health ("WVFH") for an exercise price of \$0.001 per share. Through the exercise of the warrant Highmark WV obtained an additional 85,000 shares of preferred stock. For accounting purposes, as control was obtained through the transaction, the transaction was treated as an acquisition. The results of WVFH's operations have been included in the Consolidated Financial Statements since the date of the warrant exercise. As less than 100 percent interest is acquired, the Corporation recognized the non-controlling interest at fair value.

In addition, in conjunction with the transaction, a WVFH surplus note held by Highmark WV was adjusted to the determined fair value of the note and accrued interest.

The following table summarizes the value of the assets acquired and liabilities assumed at the acquisition date.

Recognized amounts of identifiable assets acquired and liabilities assumed:

Cash and cash equivalents	\$ 55,085
Accounts receivable	21,483
Pharmacy rebates receivables	959
Intangibles	30,300
Goodwill	14,880
Claims outstanding	(44,203)
Other payables and accrued expenses	(16,647)
Surplus note	(25,500)
Deferred income taxes, net	(11,885)
Total identifiable net assets	<u>24,472</u>
Noncontrolling interest	(9,786)
Fair value adjustment for surplus note and related interest receivable held by Highmark WV	30,830
Gain on transaction	<u>\$ 45,516</u>

The fair value of the equity interest in WVFH held by the Corporation immediately before the acquisition was \$10,523.

The fair value of the acquired intangible assets of \$30,300 was determined by a third party valuation expert. The intangible assets that make up that amount include member relationships of \$17,700 (18-year useful life), provider contracts of \$8,700 (15-year useful life), and a trademark/tradename of \$3,900 (8-year useful life).

# Highmark Health

## Notes to Consolidated Financial Statements

### December 31, 2017 and 2016

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*(in thousands of dollars)*

#### 3. Divestitures

Effective December 1, 2017, HVHC finalized the sale of Davis Vision to a third party (“the Buyer”). In addition, HVHC sold a 20 percent non-controlling interest in Visionworks and included options for the Buyer to acquire the remainder of the company over seven years. The buyer also has the option to require HVHC to repurchase its initial interest in Visionworks at its purchase price within a three year period following the effective date of the transaction. Davis Vision was combined with the Buyer’s existing managed care business and the Corporation acquired a non-controlling interest in the newly formed company in the amount of \$21,496, which is recorded in Other Investments in the Consolidated Balance Sheets. The gain on the sale of \$563,949 incorporates the fair value of consideration received less fair value of consideration given, and was recorded within gain on sale of subsidiary and consolidation of affiliate in the Consolidated Statements of Operations. The fair value of the Buyer’s interest in Visionworks, including the fair value of the options, of \$100,050 was recorded as a non-controlling interest.

As a part of the sale of Davis Vision and the non-controlling interest in Visionworks, HVHC agreed to indemnify the Buyer from certain losses and settle any purchase price adjustments as described in the Davis Vision and Visionworks Stock Purchase Agreement. Highmark Inc. agreed to guarantee HVHC’s indemnification obligations, the payment of any purchase price adjustments and the Buyer’s option to have HVHC repurchase its initial interest in Visionworks at its purchase price.

On July 1, 2016, HMIG exited the workers’ compensation business through a sale of renewal rights and reinsurance transaction with a third party. As part of the reinsurance transaction, HMIG agreed to cede 100% of the premium and claims and related net policyholder liabilities of existing policies in exchange for a payment of associated policy assets. In addition, on January 1, 2017, HMIG sold 100% of the outstanding shares of its subsidiary, HM Casualty Insurance Company, which underwrote workers’ compensation business. The loss on the transaction of approximately \$4,327 was included within other operating expenses and incorporates the loss on the settlement of the policy assets and liabilities partially offset by the proceeds from the renewal rights and sale of the subsidiary.

At December 31, 2016, the workers’ compensation business reported total assets of \$243,787, which included \$21,704 of cash and cash equivalents, \$18,959 of trade accounts receivable, \$15,171 of other receivables, \$186,554 of reinsurance recoverables, and \$1,399 of other assets, as well as total liabilities of \$232,722, which included \$181,075 of claims outstanding, and \$51,647 of other liabilities. These workers’ compensation business assets and liabilities were reported in Assets held for sale and Liabilities held for sale, respectively, in the Consolidated Balance Sheets.

Effective February 1, 2017, HMIG finalized the workers’ compensation divestiture and novated the policies to the third party through a novation and assumption reinsurance agreement.

#### 4. Summary of Significant Accounting Policies

##### **Basis of Financial Presentation**

The accompanying Consolidated Financial Statements include the accounts of the Corporation.

The Consolidated Financial Statements are presented on the accrual basis of accounting, in accordance with accounting principles generally accepted in the United States of America (“GAAP”).

# Highmark Health

## Notes to Consolidated Financial Statements

### December 31, 2017 and 2016

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*(in thousands of dollars)*

All significant intercompany balances and transactions have been eliminated from the Consolidated Financial Statements.

The Corporation uses the equity method of accounting for 50% or less owned affiliates or those affiliates for which the Corporation does not hold a controlling financial interest but may influence operating or financial decisions.

#### **Reclassifications**

The Company has reclassified certain amounts relating to its prior period results to conform to its current period presentation. These reclassifications have not changed the results of operations of prior periods.

Effective January 1, 2017, "Management services revenue" was renamed "Service revenue" to more broadly reflect the types of service business offerings. As a result of this change, the Corporation reclassified drug rebates retained in lieu of fees charged for services performed, claims processing and provider networks fees, platform services, grants, contributions and other ancillary hospital revenue from "Other revenue" to "Service revenue" in the Consolidated Statements of Operations for the year ended December 31, 2016.

Effective January 1, 2017, the Company adopted ASU 2015-09, Disclosures about Short-Duration Contracts. In conjunction with adopting this standard, the Corporation changed its accounting policy to include claims adjustment expenses in claims incurred. Therefore, the Corporation reclassified claims adjustment expenses from "Other operating expense" to "Claims and claim adjustment expenses" in the Consolidated Statements of Operations for the year ended December 31, 2016. In addition, the liability to reflect the cost to process outstanding claims was reclassified from "Other payables and accrued expenses" to "Claims outstanding" in the Consolidated Balance Sheet as of December 31, 2016.

#### **New Accounting Pronouncements**

##### ***Implemented***

In January 2017, Financial Accounting Standards Board ("FASB") issued new guidance eliminating Step 2 from the goodwill impairment test. The new guidance is effective for fiscal years beginning after December 15, 2021. The Corporation elected to early adopt the guidance for the current reporting period, which is permitted. The early adoption of this new guidance did not materially impact the financial position, results of operations and cash flows of the Corporation.

In March 2016, FASB issued new guidance to simplify the accounting for equity method investments by eliminating the requirement that an entity retroactively adopt the equity method if an investment qualifies for use of the equity method as a result of an increase in the level of ownership. The new guidance is effective for fiscal years beginning after December 15, 2016. The adoption of this new guidance did not impact the financial position, results of operations and cash flows of the Corporation.

## Highmark Health

### Notes to Consolidated Financial Statements

#### December 31, 2017 and 2016

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*(in thousands of dollars)*

In July 2015, FASB issued new guidance requiring that inventory that is not measured using last-in, first-out ("LIFO") or the retail inventory method should be measured at the lower of cost and net realizable value. The new guidance is effective for fiscal years beginning after December 15, 2016. The adoption of this new guidance did not materially impact the financial position, results of operations and cash flows of the Corporation.

In May 2015, FASB issued new guidance regarding the accounting for insurance contracts. The guidance requires additional footnote disclosures surrounding paid claims and incurred-but-not-reported liabilities. The Corporation adopted this new guidance and has included additional disclosures in the Claims footnote (see Note 10).

In May 2015, FASB issued new guidance removing the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. In addition, the new guidance requires the disclosure of information that helps users of its financial statements to understand the nature and risks of the investments and whether the investments, if sold, are probable of being sold at amounts different from net asset value per share. The Corporation adopted this new guidance and has included additional disclosures in the Fair Value of Financial Instruments footnote (see Note 7).

#### ***Under Evaluation***

In March 2017, FASB issued new guidance regarding the presentation of net periodic pension and postretirement benefit costs. The new guidance requires an entity to disaggregate the service cost component from the other components of net benefit cost, and is effective for fiscal years beginning after December 15, 2018. The Corporation is evaluating the impact of the new guidance on its results of operations.

In August 2016, FASB issued new guidance regarding the presentation of financial statements of not-for-profit entities. The new guidance replaces the currently required three classes of net assets with two classes: net assets with donor restrictions and net assets without donor restrictions, eliminates the requirement to present or disclose the indirect method reconciliation if using the direct method on the cash flow statement, and requires enhanced disclosures about governing board designations and appropriations, composition of net assets with donor restrictions, management of liquidity, expenses, methods of cost allocation, and underwater endowment funds. The new guidance is effective for fiscal years beginning after December 15, 2017. The Corporation is evaluating the impact of the new guidance on its financial position, statements of changes in net assets and footnote disclosures.

In February 2016, FASB issued new guidance regarding the recognition of leases. The new guidance requires lessees to recognize a lease liability and a lease asset for all leases, including operating leases, with a term greater than 12 months on its balance sheet. The guidance also expands the required quantitative and qualitative disclosures surrounding leases. The new guidance is effective for fiscal years beginning after December 15, 2019. The Corporation is evaluating the impact of the new guidance on its financial position, results of operations and cash flows.

# Highmark Health

## Notes to Consolidated Financial Statements

### December 31, 2017 and 2016

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*(in thousands of dollars)*

In January 2016, FASB issued new guidance requiring all equity investments, other than those accounted for under the equity method or those that result in the consolidation of the investee, to be measured at fair value with changes in the fair value recognized through net income. The new guidance also eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for non-public business entities. The new guidance is effective for fiscal years beginning after December 15, 2018. The Corporation is evaluating the impact of the new guidance on its financial position, results of operations and cash flows.

In May 2014, FASB issued new guidance related to revenue recognition for contracts with customers. This new guidance removes most industry-specific revenue recognition requirements and requires that an entity recognize revenue for the transfer of goods or services to a customer at an amount that reflects the consideration to which an entity expects to be entitled in exchange for the goods or services. Insurance contracts are not covered by this guidance. The new guidance also requires additional disclosures regarding the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts. The new guidance is effective for fiscal years beginning after December 15, 2018. The Corporation is evaluating the impact of the adoption of this new guidance on the financial position, results of operations and cash flows.

#### **Use of Estimates**

The preparation of the Corporation's Consolidated Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Actual results could differ from those estimates.

#### **Cash and Cash Equivalents**

The Corporation considers all highly liquid investments with maturities of three months or less when purchased, excluding donor restricted trusts, to be cash equivalents.

#### **Accounts Receivable**

In the normal course of business, the Corporation grants credit to its customers under various contractual arrangements. The Corporation carries its accounts receivable at estimated net realizable value, which reflects the impact of potential credit losses.

Insurance accounts receivable is specific to Highmark business and includes amounts related to health, dental, vision, stop-loss and government business accounts receivable.

Patient service accounts receivable is specific to AHN business and includes amounts receivable from patients, third-party payors and others for services as they are rendered.

Other accounts receivable primarily includes receivables from affiliates, accrued interest revenue, receivables from securities sold and other receivables not associated with the Corporation's core business.

An allowance for doubtful accounts is based on a number of factors, including economic experience, past history, trends, coverage type and other indicators. When it is determined an accounts receivable balance is not collectible, it is written off.



## Highmark Health

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Concentrations of credit risk, excluding government payors, are limited due to the large number of Highmark Health customers.

#### **Investments**

Debt and equity securities classified as available-for-sale are carried at fair value (based on quoted or estimated market prices), except for certain available-for-sale investments which are valued at net asset value (NAV) as a practical expedient to fair value. Unrealized gains and losses are reported in unrestricted net assets, net of deferred income taxes. Derivatives embedded within convertible debt securities are bifurcated, with changes in fair value included in earnings; any remaining unrealized gains or losses of the convertible bonds are reported in unrestricted net assets, net of deferred income taxes. Premiums and discounts are amortized using the effective interest method. Realized gains and losses on debt securities are based on amortized cost. Realized gains and losses on equity securities are based on cost (specific identification method). Realized gains and losses on available-for-sale debt and equity securities are reported in net investment income in the Consolidated Statements of Operations.

The Corporation monitors its available-for-sale investments portfolio for unrealized losses that appear to be other-than-temporary. At the time an equity security is determined to be other-than-temporarily impaired, the Corporation reduces the book value of the security to the current market value and records a realized loss in net investment income in the Consolidated Statements of Operations.

In determining if an available-for-sale debt security is other-than-temporarily impaired, the Corporation considers whether it has intent to sell the available-for-sale debt security or whether it is more likely than not that the Corporation will be required to sell the available-for-sale debt security before recovery of its amortized cost basis, which may be at maturity. If the Corporation intends to sell the debt security or it is more likely than not that the Corporation will be required to sell the debt security before recovery of its amortized cost basis, an other-than-temporary impairment is recorded as a realized loss in net investment income in the Consolidated Statements of Operations for the difference between fair value and amortized cost.

If the Corporation does not have the intent to sell and it does not believe that it is more likely than not that it will be required to sell the debt security before recovery of its amortized cost, the Corporation performs a detailed review to determine the underlying cause of the unrealized loss and whether an other-than-temporary impairment is warranted. At the time a debt security is determined to be other-than-temporarily impaired, the credit component of the other-than-temporary impairment is recognized in income in the consolidated statements of operations and the non-credit component of the other-than-temporary investment is recognized in the Consolidated Statement of Changes in Net Assets, net of deferred income taxes.

Board designated, restricted and other investments include assets whose use is contractually limited by external parties and assets set aside by the Board of Directors for future capital improvements or liquidity, over which the Board retains control and may, at its discretion, subsequently use for other purposes, as well as assets held by trustees under indenture agreements. Other investments consist primarily of marketable debt and equity securities and marketable securities maintained in a master trust fund. Investment income or loss (including realized gains and losses, interest and dividends, and unrealized gains and losses) is recorded in net investment income in the consolidated statements of operations unless restricted by donor or law. Investment income related to temporarily and permanently restricted gifts is recorded based on donor restriction as part of the corresponding net asset class in the Consolidated Statements of Changes in Net Assets.

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Other investments include investments in private limited partnerships, real estate trusts and limited liability companies. Private limited partnerships are accounted for under the equity method. The Corporation has committed \$132,852 and \$111,446 to various private limited partnership investments at December 31, 2017 and 2016, respectively. These commitments are due upon capital calls by the general partners of the partnerships. Generally, limited liability companies are accounted for under the cost or equity method, dependent on certain factors including ownership. Fair values of real estate investment trusts are approximated based on trustee estimates. Certain other investments are valued at NAV as a practical expedient to fair value. The Corporation monitors its other investments for unrealized losses that appear to be other-than-temporary. At the time an investment is determined to be other-than-temporarily impaired, the Corporation reduces the book value to the current market value and records a realized loss in net investment income in the Consolidated Statements of Operations.

The Corporation participates in securities lending transactions, which are accounted for as secured borrowings. The Corporation utilizes a custodian as a lending agent, maintains effective control over the loaned securities and requires collateral initially equal to at least 102% of loaned domestic securities and 105% of loaned international securities at the loan date. Collateral received consists of cash and fixed-income securities. Non-cash collateral is not recorded in the Consolidated Balance Sheets, as the Corporation does not have the right to sell, pledge or otherwise reinvest the non-cash collateral. Cash collateral is invested in short-term debt securities and is carried at fair value. Changes in fair value are reported as unrealized gains and losses within unrestricted net assets.

The fair value of securities held as invested collateral was \$112,429 and \$163,592 at December 31, 2017 and 2016, respectively. The corresponding liability that represents the Corporation's obligation to return the collateral was \$112,423 and \$163,523 at December 31, 2017 and 2016, respectively.

The potential risks associated with the transactions include counterparty credit risk, non-cash collateral security risk, lending agent operational risk, and cash collateral reinvestment risk, including the risk that the reinvested collateral would be illiquid, insufficient to repay borrowers, would differ in maturity, or be otherwise unavailable to return the cash collateral to counterparties.

The Corporation and its lending agent mitigate those risks by limiting the amount of investments available for loan, limiting the amount of borrowings by any one counterparty, maintaining effective control over loaned securities, evaluating the credit of counterparties, maintaining a list of approved borrowers, requiring overcollateralization, placing limitations, including duration and credit quality, on the investment of cash collateral, conducting daily mark-to-market pricing of securities, collateral and invested collateral, and maintaining a written agreement with the lending agent that includes certain protections.

The Corporation's assets are invested in a variety of financial instruments. Accordingly, the related values as presented in the Consolidated Financial Statements are subject to various market fluctuations, which include changes in the interest rate environment, equity markets and general economic conditions.

#### **Reinsurance**

In the normal course of business, the Corporation seeks to reduce losses that may arise from risks or occurrences of an unexpected nature that may cause unfavorable underwriting results by reinsuring certain levels of risk in various areas of exposure with other insurance enterprises or reinsurers. Additionally, the Corporation participated in the ACA temporary reinsurance program through 2016.

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Reinsurance premiums and benefits paid or provided are accounted for in a manner consistent with the original policies issued and the terms of the reinsurance contracts. The Corporation also assumes risks from other insurance companies. Such assumed reinsurance activity is recorded principally on the basis of reports received from the ceding companies.

#### **Inventory, Net**

Inventory consists primarily of vision related eyewear components and health care delivery related drugs, medical supplies and surgical supplies. Vision related eyewear components include frames, lenses and cases, contact lenses and solutions, laboratory supplies, and packaging materials. Inventory is stated at the lower of cost or market. Vision related inventory cost is determined using the weighted average or first-in first-out basis. Health care delivery related inventory cost is determined using the first-in first-out basis. Obsolescence reserves were \$8,621 and \$10,962 at December 31, 2017 and 2016, respectively.

#### **Property and Equipment, Net**

Property and equipment is recorded at cost, net of accumulated depreciation and amortization. If a donor contributes property and equipment, it is recorded at the fair market value on the date contributed. Maintenance, repairs and minor improvements are expensed as incurred. Certain costs related to the internal development of software or software purchased for internal use are capitalized. Gains or losses on sales or disposals of property and equipment are included in operations.

Depreciation is computed under the straight-line method by annual charges to expense over the estimated useful lives of the various asset types as follows: buildings and building or land improvements, up to 40 years; leasehold improvements, lesser of lease term or useful life; office furniture and equipment, three-30 years; and capitalized software, three-10 years.

Property and equipment is reviewed for impairment whenever changes in circumstances indicate that the carrying value of the assets may not be recoverable. Impairment losses are recognized to the extent the carrying amount of an asset exceeds the undiscounted future cash flows expected to result from the use of the asset and its eventual disposal. An equipment impairment of \$10,984 existed during 2017. This impairment is reflected in operating expenses in the Consolidated Statements of Operations. No impairment losses were recorded in 2016.

#### **Goodwill and Other Intangible Assets, Net**

Intangible assets with definite lives are amortized using the straight-line method over their estimated lives, which range from three to 25 years. Intangible assets with indefinite useful lives, including goodwill, are not amortized, but are tested for impairment at least annually and more frequently if events or changes in circumstances indicate that an asset may be impaired. If fair value is less than carrying value, the asset is adjusted to the fair value and an impairment loss is recorded in the Consolidated Statements of Operations. Management tested goodwill and other intangible assets with indefinite lives for impairment and concluded that a goodwill impairment occurred (see Note 9).

#### **Other Assets**

Other assets primarily include prepaid expenses, pharmacy rebates receivable, insurance recoveries associated with medical malpractice, notes receivable and cash surrender values of corporate-owned life insurance policies held in grantor trusts.

# Highmark Health

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Pharmacy rebates receivable, and the related customer liabilities, is an actuarial estimate based on prescriptions filled and terms of rebate contracts. The actuarial estimates are continually reviewed and any resulting adjustments are included in current operations. The Corporation carries its notes receivable at estimated net realizable value, which reflects the impact of potential credit losses. Changes in cash surrender value are reported in net investment income in the Consolidated Statements of Operations.

#### **Claims Outstanding**

Claims outstanding include claims reported and adjudicated but unpaid as well as an estimate of incurred but not reported ("IBNR") claims. The liability for IBNR claims is an actuarial estimate based on historical claims paid data, modified for current conditions and coverage changes. The methods to determine the estimate of IBNR claims use past experience adjusted for current trends. The methods and assumptions are continually reviewed and any resulting adjustments are included in current operations. Corresponding administrative costs to process outstanding claims are estimated and accrued and are also included in claims outstanding.

The Corporation records certain non-risk administrative arrangements in claims liabilities. The non-risk administrative receivable is included in insurance accounts receivable and the corresponding provider liability is included in claims outstanding in the Consolidated Balance Sheets.

#### **Amounts Held for Others**

Amounts held for others include reserves for refunds and deposits received from groups for non-risk administrative arrangements. Amounts held for others also include amounts related to the BlueCard program, which allows the Highmark members to access other Blue Cross and Blue Shield plans' provider networks.

#### **Other Liabilities**

Other liabilities include medical malpractice reserves, deferred grant revenue, asset retirement obligations, book overdraft and interest rate swap liabilities.

The provision for medical malpractice claims includes estimates of the ultimate costs for both reported claims and claims incurred but not reported, including costs associated with litigating or settling claims. Anticipated insurance recoveries associated with reported and unreported claims are reported in other assets in the Consolidated Balance Sheets at net realizable value.

The Corporation records deferred grant revenue for grant monies received until the revenue is earned or related costs have been incurred. Governmental grant monies received for the acquisition of property and equipment are deferred until the asset is provided or until depreciation expense is recognized.

#### **Temporarily and Permanently Restricted Net Assets**

Temporarily restricted net assets are those whose use is limited by donor-imposed stipulations that either expire with the passage of time or can be fulfilled and removed by actions of the Corporation pursuant to those stipulations. Temporarily restricted net assets are available for capital and other program expenditures.

Permanently restricted net assets are those whose use is limited by donor-imposed stipulations that neither expire with the passage of time nor can be fulfilled or otherwise removed by the actions of the Corporation. Investment earnings from permanently restricted net assets may be unrestricted or

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temporarily restricted for capital or operating needs depending upon the original intent of the donor. AHN elected a total return investment policy for certain trust accounts which permits income to be redefined as a percentage of a rolling average market value of the charitable trust as averaged over a period of at least three years provided the election is consistent with the charitable trust agreement and long term preservation of principal value of the charitable trust. The investment income percentage distribution is recorded as a transfer out of trusts in permanently restricted net assets.

Net assets are released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by donors. Net assets released from restrictions and used for operations are recorded in net assets released from restriction. Net assets released from restriction and used for capital purposes are recorded in unrestricted net assets in the Consolidated Statements of Changes in Net Assets.

#### **Insurance Revenue Recognition**

Highmark's business consists of at-risk insurance arrangements and non-risk administrative arrangements. Risk business includes all insurance contracts. Premiums are generally billed in advance of the contractual coverage periods and are included in premium revenue as they are earned during the coverage period. The unearned portion of premiums collected is reflected in the Consolidated Balance Sheets as unearned revenue. Premium revenue is received from the federal government and certain states according to government specified payment rates and various contractual terms. Changes in revenues from Medicare, ACA and Medicaid products resulting from the periodic changes in risk-adjustment scores derived from medical diagnoses for the Corporation's membership are recognized when the amounts become determinable and the collectability is reasonably assured.

#### **Service Revenue**

The administrative fees received under non-risk administrative arrangements are included in service revenue and recognized in the period in which the related services are performed. This also includes fees for management of medical services, claims processing and access to provider networks. Under non-risk administrative arrangements, the customer assumes the risk of funding claims. The Corporation does not record premium revenue or claims incurred on non-risk administrative arrangements. The expenses associated with administering the risk and non-risk business are included in salaries, wages and fringe benefits and other operating expenses in the Consolidated Statements of Operations.

Service revenue also includes pharmacy rebates retained in lieu of fees charged for non-risk administrative arrangements, health plan platform services, grants, contributions, physician stipends, Medicare and Medicaid electronic health record ("EHR") incentive payments and other ancillary hospital services revenue such as parking, cafeteria, tuition and rent.

#### **Vision Revenue**

Vision revenue includes sales from fully integrated eye care services through November 2017 and optical retail stores. Fully integrated eye care service revenues are recognized based upon services rendered. Sales are recognized when title and the risk of loss transfer to the customer, there is evidence of a contractual arrangement and collectability of the resulting receivable is reasonably assured.

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**Net Patient Service Revenue**

Net patient service revenue is comprised of gross patient service revenues less contractual allowances, charity care and provision for doubtful accounts. Net patient service revenue is reported at estimated net realizable amounts from patients, third-party payors and others for services rendered at the time the service is performed and includes estimated retroactive revenue adjustments due to future audits, reviews and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews and investigations.

AHN has agreements with third-party payors that provide for payments to AHN at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, per diem payments and contracted amounts. AHN recognizes patient service revenues associated with services provided to patients who have third-party payor coverage on the basis of established rates for services rendered. AHN provides discounts to uninsured patients who do not qualify for medical assistance or charity care.

Net patient service revenue, by major payor in 2017 and 2016 was as follows:

	2017	2016
Medicare	\$ 998,878	\$ 881,050
Medical assistance	225,856	229,838
Blue Cross Blue Shield payors	535,502	458,314
Other third-party payors	472,946	445,512
Patients and residents	41,299	59,459
Total patient service revenue, net of contractual allowances and discounts	<u>2,274,481</u>	<u>2,074,173</u>
Less: Provision for doubtful accounts	(50,667)	(69,471)
Total net patient service revenue	<u>\$ 2,223,814</u>	<u>\$ 2,004,702</u>

In 2017, revenue from Medicare and Medical Assistance programs accounted for 44% and 10%, respectively, of patient service revenue, net of contractual allowances and discounts. In 2016, revenue from Medicare and Medical Assistance programs accounted for 43% and 11%, respectively, of patient service revenue, net of contractual allowances and discounts. Laws and regulations governing Medicare and Medical Assistance programs are complex and subject to interpretation and there is at least a reasonable possibility that actual results could differ from revenue recognized.

**Charity Care**

AHN hospitals provide services to all patients regardless of ability to pay. AHN hospitals each have a charity care policy under which they provide care to patients at no charge or at discounted rates, provided the patients meet the eligibility requirements stipulated in their policies. AHN does not pursue collection of amounts determined to qualify for charity care; therefore, charity care amounts are not recorded as revenue or deducted from gross patient service revenue in arriving at net patient service revenue.

**Affiliates Income (Loss)**

Affiliate income (loss) includes the Corporation's proportionate share of affiliate earnings.

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## Notes to Consolidated Financial Statements

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#### **Donor-Restricted Contributions**

Unconditional promises to give cash and other assets to the Corporation are reported at fair value at the date the promise is received as unrestricted gifts within service revenue in the Consolidated Statements of Operations. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the Consolidated Statements of Operations as net assets released from restrictions. Donor restricted contributions whose restrictions are met within the same year are reported as unrestricted contributions in the accompanying Consolidated Financial Statements.

#### **Income Taxes**

Highmark Health and certain of the entities within AHN are tax-exempt organizations under Section 501(c)(3) of the Internal Revenue Code ("IRC") and are exempt from federal income taxes on exempt purpose income. These tax-exempt organizations are subject to federal taxes on unrelated business income under section 511 of the IRC.

Highmark Inc., Highmark WV and Highmark DE are subject to federal income taxes, although they remain exempt from state and local taxes. Highmark Inc., Highmark WV and Highmark DE file separate consolidated federal income tax returns. Only the non-insurance subsidiaries and health maintenance organizations of Highmark Inc., Highmark WV and Highmark DE are subject to state income taxes. Certain insurance subsidiaries are subject to state premium taxes. Provisions for the applicable tax liabilities have been made in the Consolidated Financial Statements.

Deferred tax assets and liabilities are determined based on differences between the financial reporting and tax basis of assets and liabilities and are measured using tax rates and laws that are expected to be in effect when the difference is reversed. The Corporation records a valuation allowance against its deferred tax assets when it determines that it is more likely than not that some portion or all of the deferred tax asset will not be realized.

#### **Excess of Revenue Over Expenses**

The Consolidated Statements of Operations include an excess of revenue over expenses. Changes in unrestricted net assets which are excluded from the excess of revenue over expenses, consistent with industry practice, include unrealized gains and losses on available-for-sale securities, benefit plan asset and liability changes, contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets) and certain tax benefits.

#### **Subsequent Events**

In connection with the preparation of the Consolidated Financial Statements, the Corporation evaluated events subsequent to the balance sheet date of December 31, 2017 through March 28, 2018, which is also the date the financial statements were available to be issued, and has determined that all material transactions have been recorded and disclosed properly.

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**5. Insurance Regulation**

Highmark Inc. and its insurance subsidiaries and affiliates file financial statements with insurance departments in their states of domicile. These financial statements are prepared in accordance with statutory accounting principles prescribed by such regulatory authorities. Prescribed statutory accounting principles include state laws, regulations and general administrative rules, as well as a variety of publications of the National Association of Insurance Commissioners ("NAIC"). Permitted statutory accounting practices encompass all accounting practices not prescribed.

Financial statements prepared for state insurance departments in accordance with statutory accounting principles differ from the Consolidated Financial Statements prepared in accordance with GAAP. The principal differences in statutory accounting are: (1) certain assets, such as accounts receivable aged more than 90 days, office furniture and equipment, nonoperating software, certain provider advances, certain intangible assets and prepaid expenses, are excluded from statutory reserves; (2) pharmaceutical rebates receivable are limited based on the timing of billing and collection activities; (3) certain bonds and preferred stocks are carried at amortized cost or fair value, not fair value as required under GAAP; (4) equity income or loss of subsidiaries, affiliates and limited partnerships is recorded directly to reserves rather than in results of operations as required under GAAP, with dividends or distributions recognized in statutory net income when declared; (5) certain reserve transfers to related parties are expensed; (6) certain assets and liabilities pertaining to reinsurance transactions are reported net of reinsurance; (7) acquisitions are accounted for at historical statutory amounts; (8) deferred tax asset recognition is limited; and (9) uncertain tax positions are fully recognized if the probability is greater than 50%.

As a result of the foregoing, statutory reserves at December 31, 2017 and 2016 and statutory net loss for the years then ended was:

	2017	2016
<b>Highmark (excluding Highmark WV and Highmark DE)</b>		
Statutory reserves	\$ 3,798,960	\$ 3,886,331
Statutory net income (loss)	\$ 660,075	\$ (73,907)
<b>Highmark WV</b>		
Statutory reserves	\$ 421,870	\$ 312,661
Statutory net income (loss)	\$ 72,347	\$ (4,229)
<b>Highmark DE</b>		
Statutory reserves	\$ 253,909	\$ 149,565
Statutory net income	\$ 58,438	\$ 19,070

Highmark Inc. and its insurance subsidiaries and affiliates are subject to minimum risk-based capital ("RBC") requirements that were developed by the NAIC and adopted by various state legislatures. The formula for determining the amount of RBC specifies various weighting factors that are applied to financial balances and various levels of activity based on perceived degrees of risk.



## Highmark Health

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The RBC ratios of Highmark Inc. and its insurance subsidiaries and affiliates are compared to authorized control levels established by the NAIC. Companies below specific ratio thresholds may be required to take specific corrective actions. At December 31, 2017 and 2016, Highmark Inc. and its insurance subsidiaries and affiliates exceeded their respective minimum RBC requirements.

The Pennsylvania Insurance Commissioner has determined that an appropriate sufficient operating surplus range for Highmark Inc. is 550% - 750% of the health RBC ratio or the Pennsylvania Insurance Department's (the "Department") consolidated risk factor ratio, whichever is lower. As long as Highmark Inc. operates above the 550% ratio, it is not permitted to include a risk and contingency factor in its filed premium rates. If Highmark Inc.'s ratio exceeds 750%, it will be required to justify its surplus level and could be required to submit a plan to bring its surplus within the designated appropriate sufficient operating surplus range. At December 31, 2017 and 2016, Highmark Inc.'s health RBC ratio was within the appropriate sufficient operating surplus range determined by the Department.

The ACA enacted significant reforms to various aspects of the U.S. health insurance industry. Certain of these reforms became effective January 1, 2014, including the establishment of federally-facilitated or state-based exchanges which provide individuals and small businesses access to affordable and quality health insurance. Highmark participates in the Pennsylvania, West Virginia and Delaware markets.

The ACA imposes an annual premium-based fee on health insurers for each calendar year beginning on or after January 1, 2014, which is not deductible for tax purposes. The Consolidated Appropriation Act, 2016, enacted on December 18, 2015, included a one year suspension in 2017 of the health insurer fee. However, the health insurer fee will resume in 2018. The aggregate annual fee for all insurers was \$11,300,000 for 2016. This amount was apportioned among all insurers based on a ratio designated to reflect relative market share of U.S. health insurance business. The fee is based on the ratio of the Highmark's applicable net written premium to total applicable net premiums for all such issuers. Highmark is required to estimate a liability for the health insurer fee and record it in full once qualifying insurance coverage is provided in the applicable calendar year in which the fee is payable with a corresponding deferred cost that is amortized ratably to expense over the same calendar year. In September 2016, Highmark paid the federal government \$139,442 for its portion of the health insurer fee.

The ACA also established three premium stabilization programs effective January 1, 2014. These risk spreading programs are applicable to certain commercial medical insurance products. In the aggregate, Highmark's commercial medical insurance products subject to the premium stabilization programs represented approximately 8% and 10% of the total premiums for the years ending December 31, 2017 and 2016, respectively. These programs, commonly referred to as the "3Rs", include a permanent risk adjustment program, a temporary risk corridor program and a transitional reinsurance program designed to more evenly spread the financial risk borne by issuers and to mitigate the risk that issuers would have mispriced products. The transitional reinsurance and risk corridor programs were available for years 2014 through 2016.

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The permanent risk adjustment program adjusts the premiums that commercial individual and small group health insurance issuers receive based on the demographic factors and health status of each member as derived from current year medical diagnosis as reported throughout the year. This program transfers funds from lower risk plans to higher risk plans in the same state. The risk adjustment program is applicable to commercial individual and small group health plans (except certain exempt, grandfathered and grandmothered plans) operating both inside and outside of the health insurance exchanges established under the ACA. Under the risk adjustment program, a risk score is assigned to each covered member to determine an average risk score at the individual and small group level by legal entity in a particular market in a state. Additionally, an average risk score is determined for the entire subject population for each market in each state. Settlement amounts are determined by utilizing the Centers for Medicare and Medicaid Services ("CMS") risk transfer formula which averages all risk scores in risk adjustment covered plans and uses the plan average risk scores with other factors to calculate the settlement. Settlements are determined on a net basis by legal entity and state.

The estimate of amounts receivable or payable under the risk adjustment program is based on an estimate of both Highmark's and the state average risk scores. Assumptions used in these estimates include but are not limited to historical market experience, member demographics, including age and gender, pricing model, membership data, the mix of previously underwritten membership as compared to new members in plans compliant with the ACA, published third party studies and other publicly available data including regulatory plan filings. Highmark generally relies on providers to appropriately document all medical data, including the diagnosis data submitted with claims, as the basis for risk scores under the program.

For the permanent risk adjustment program, Highmark records receivables or payables as adjustments to premium revenue based on year-to-date experience when the amounts are reasonably estimable and collection is reasonably assured. Final revenue adjustments are determined by CMS in the year following the policy year. Under the risk adjustment program, the Corporation received net payments of \$47,998 in 2017 to settle the 2016 plan year and \$767 in 2016 to settle the 2015 and 2014 plan years.

The temporary 2016 risk corridor program applied to qualifying individual and small group Qualified Health Plans, as defined by CMS, operating both inside and outside of the exchanges. The risk corridor provisions limited issuer gains and losses by comparing allowable medical costs to a target amount, defined by CMS, and sharing the risk for allowable costs with the federal government. Allowable medical costs are adjusted for risk adjustment settlements, transitional reinsurance recoveries and cost sharing reductions received from CMS. Variances from the target exceeding certain thresholds may result in CMS making additional payments to Highmark or require Highmark to refund CMS a portion of the premiums received.

For the temporary risk corridor program, Highmark records receivables upon communication by CMS of funds available that it intends to pay. Highmark recorded premium revenue of \$1,939 and \$7,102 for the 2014 benefit year risk corridor for the years ended December 31, 2017 and 2016, respectively. Highmark did not record any additional risk corridor premium revenue for the 2014 benefit year and recorded no premium revenue for the 2015 and 2016 benefit years as collection is not reasonably assured. However, the Corporation continues to believe that CMS has a binding obligation to satisfy the risk corridor receivable.

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The transitional reinsurance program required Highmark to make reinsurance contributions for calendar years 2014 through 2016 based on a national contribution rate per covered member as determined annually by CMS. The total amount assessed through this provision is \$25,000,000 in the 3-year period and an additional administrative expense charge for 2016 of \$32,000. The contribution rate was two dollars and twenty-five cents per member per month for calendar year 2016. While all commercial medical plans, including self-funded plans, were required to fund the reinsurance entity, only fully-insured non-grandfathered plans compliant with the ACA in the individual commercial market were eligible for recoveries if individual claims exceed a specific threshold. In 2016, the reinsurance program thresholds include an attachment point of \$90 and a cap of \$250 of eligible individuals claims. A coinsurance rate is applied to eligible individual claims that met the program's criteria.

Highmark's reinsurance contribution expense in 2016 was \$17,940. Under the reinsurance program, final settlements for ceded claims resulted in amounts owed to the Corporation of \$73,410 for the 2016 plan year. As of December 31, 2017, \$12,194 of the reinsurance recoverable was outstanding relative to the 2016 plan year.

The 3Rs receivable and payable amounts at December 31, 2017 were as follows:

	Risk Adjustment	Risk Corridor	Reinsurance	Total
Accounts receivable, insurance	\$ -	\$ 1,939	\$ -	\$ 1,939
Reinsurance recoverables	-	-	12,194	12,194
Other payables and accrued expenses	(1,707)	-	(6,189)	(7,896)
Net receivable	<u>\$ (1,707)</u>	<u>\$ 1,939</u>	<u>\$ 6,005</u>	<u>\$ 6,237</u>

The 3Rs receivable and payable amounts at December 31, 2016 were as follows:

	Risk Adjustment	Risk Corridor	Reinsurance	Total
Accounts receivable, insurance	\$ (3,099)	\$ 2,023	\$ -	\$ (1,076)
Reinsurance recoverables	-	-	78,114	78,114
Other payables and accrued expenses	-	-	(26,528)	(26,528)
Net receivable	<u>\$ (3,099)</u>	<u>\$ 2,023</u>	<u>\$ 51,586</u>	<u>\$ 50,510</u>

In addition to the 3Rs ACA established a cost-sharing reduction ("CSR") program that requires Qualified Health Plans to provide reduced cost sharing for essential health benefits to eligible enrollees. Under the CSR program issuers must ensure eligible enrollees pay only the cost sharing required for applicable covered services. Issuers are then required to notify CMS of cost-sharing reductions provided on behalf of eligible enrollees. Monthly, CMS makes payments estimated to be the value of cost-sharing reductions provided by the issuers. In the subsequent benefit year CMS reconciles the estimated payments to the cost-sharing reductions provided and a final settlement is made. In 2017, the Corporation settled the 2016 CSR program benefit year resulting in a reduction to claims incurred of \$786. In 2016, the Corporation settled the 2014 and 2015 CSR program benefit

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*(in thousands of dollars)*

years resulting in a reduction to claims incurred of \$44,355. The CSR program was terminated in November 2017.

Highmark Inc. is subject to a Community Health Reinvestment ("CHR") Agreement with the Department, which establishes an annual CHR commitment for Highmark Inc. based on direct written health premiums. Highmark met its minimum social mission commitment of \$77,482 in each of 2017 and 2016. The 2018 commitment is expected to approximate the 2017 and 2016 amounts. Highmark Inc. has the ability to direct the funds related to the CHR endeavors provided that the funds are used to provide health care coverage for persons who are uninsured or unable to pay for coverage, to fund programs for the prevention and treatment of disease or injury including mental health counseling or the promotion of health or wellness, to fund the prevention of conditions, behavior or activities that are adverse to good health or donations for the benefit of health care providers in furtherance of any of the foregoing purposes.

Because Highmark is not eligible to participate in a Pennsylvania-sponsored guarantee fund, it has established and funded a trust in order to meet a licensing requirement of BCBSA. The fair value of the trust was \$356,587 and \$344,563 at December 31, 2017 and 2016, respectively, and was reported as debt securities in the Consolidated Balance Sheets.

Medicare Advantage and Medicare Part D Prescription Drug Plan products offered under contracts with CMS accounted for 25.5% and 29.3% of total premiums for the years ended December 31, 2017 and 2016, respectively.

CMS uses a risk-adjustment model which apportions premiums paid to Medicare Advantage plans according to the health severity of their members. The risk-adjustment model pays higher premiums for members with certain medical conditions identified with specific diagnostic codes. Under the risk-adjustment methodology, all Medicare Advantage plan sponsors must collect and submit the necessary diagnosis code information from providers to CMS within prescribed deadlines. The CMS risk-adjustment model uses the diagnosis data to calculate the risk-adjusted premium payment to Medicare Advantage plans. Highmark generally relies on providers to code their claim submissions with appropriate diagnoses, which are sent to CMS as the basis for the payment received from CMS under the risk-adjustment model. Highmark also relies on these providers to document appropriately all medical data, including the diagnosis data submitted with claims.

CMS continues to perform audits of selected companies' Medicare Advantage contracts related to this risk adjustment diagnosis data. In February 2012, CMS announced a final Risk Adjustment Data Validation ("RADV") audit and payment adjustment methodology that it will utilize to conduct RADV audits beginning with the 2011 payment year. RADV audits review medical records in an attempt to validate provider medical record documentation and coding practices which influence the calculation of premium payments to Medicare Advantage plans. These audits may result in retrospective adjustments to payments made to health plans. Selected Medicare Advantage contracts will be notified of an audit after the close of the final reconciliation for the payment year being audited. Through the date of this report, Highmark has not been notified by CMS that any of its Medicare Advantage contracts have been selected for audit.

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**6. Investments**

The cost or amortized cost, gross unrealized gains and losses and fair value of investments in debt and equity securities classified as available-for-sale at December 31, 2017 were as follows:

	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Debt securities				
U.S. Treasury and agency obligations	\$ 750,252	\$ 2,180	\$ (13,244)	\$ 739,188
Agency mortgage-backed securities	497,814	5,640	(6,909)	496,545
State and political obligations	10,366	984	(35)	11,315
Mortgage-backed securities	18,142	109	(144)	18,107
Asset-backed securities	54,877	507	(150)	55,234
Corporate and other debt securities	1,579,063	33,290	(9,066)	1,603,287
Total debt securities	<u>2,910,514</u>	<u>42,710</u>	<u>(29,548)</u>	<u>2,923,676</u>
Equity securities				
Domestic	425,647	190,292	(5,171)	610,768
Foreign	487,741	97,485	(1,806)	583,420
Total equity securities	<u>913,388</u>	<u>287,777</u>	<u>(6,977)</u>	<u>1,194,188</u>
Total	<u>\$ 3,823,902</u>	<u>\$ 330,487</u>	<u>\$ (36,525)</u>	<u>\$ 4,117,864</u>

The cost or amortized cost, gross unrealized gains and losses and fair value of investments in debt and equity securities classified as available-for-sale at December 31, 2016 were as follows:

	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Debt securities				
U.S. Treasury and agency obligations	\$ 731,368	\$ 1,297	\$ (25,265)	\$ 707,400
Agency mortgage-backed securities	443,314	3,681	(4,625)	442,370
State and political obligations	25,710	728	(75)	26,363
Mortgage-backed securities	23,688	96	(160)	23,624
Asset-backed securities	48,581	937	(171)	49,347
Corporate and other debt securities	1,666,779	37,169	(15,404)	1,688,544
Total debt securities	<u>2,939,440</u>	<u>43,908</u>	<u>(45,700)</u>	<u>2,937,648</u>
Equity securities				
Domestic	432,942	128,310	(6,216)	555,036
Foreign	465,827	27,474	(9,179)	484,122
Total equity securities	<u>898,769</u>	<u>155,784</u>	<u>(15,395)</u>	<u>1,039,158</u>
Total	<u>\$ 3,838,209</u>	<u>\$ 199,692</u>	<u>\$ (61,095)</u>	<u>\$ 3,976,806</u>

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The gross unrealized losses and fair value of debt and equity investments classified as available-for-sale securities by investment category and length of time an individual security was in a continuous unrealized loss position at December 31, 2017 were as follows:

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>Debt securities</b>						
U.S. Treasury and agency obligations	\$ 292,154	\$ (2,189)	\$ 300,204	\$ (11,055)	\$ 592,358	\$ (13,244)
Agency mortgage-backed securities	197,544	(1,914)	199,375	(4,995)	396,919	(6,909)
State and political obligations	2,791	(9)	2,164	(26)	4,955	(35)
Mortgage-backed securities	3,006	(15)	7,620	(129)	10,626	(144)
Asset-backed securities	21,147	(64)	12,450	(86)	33,597	(150)
Corporate and other debt securities	561,564	(6,438)	117,741	(2,628)	679,305	(9,066)
Total debt securities	<u>1,078,206</u>	<u>(10,629)</u>	<u>639,554</u>	<u>(18,919)</u>	<u>1,717,760</u>	<u>(29,548)</u>
<b>Equity securities</b>						
Domestic	29,697	(4,511)	8,113	(660)	37,810	(5,171)
Foreign	112,233	(1,706)	409	(100)	112,642	(1,806)
Total equity securities	<u>141,930</u>	<u>(6,217)</u>	<u>8,522</u>	<u>(760)</u>	<u>150,452</u>	<u>(6,977)</u>
Total	<u>\$ 1,220,136</u>	<u>\$ (16,846)</u>	<u>\$ 648,076</u>	<u>\$ (19,679)</u>	<u>\$ 1,868,212</u>	<u>\$ (36,525)</u>

The gross unrealized losses and fair value of debt and equity investments classified as available-for-sale securities by investment category and length of time an individual security was in a continuous unrealized loss position at December 31, 2016 were as follows:

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>Debt securities</b>						
U.S. Treasury and agency obligations	\$ 526,074	\$ (25,265)	\$ -	\$ -	\$ 526,074	\$ (25,265)
Agency mortgage-backed securities	286,465	(4,181)	16,201	(444)	302,666	(4,625)
State and political obligations	9,073	(69)	1,020	(6)	10,093	(75)
Mortgage-backed securities	14,923	(159)	251	(1)	15,174	(160)
Asset-backed securities	19,567	(170)	484	-	20,051	(170)
Corporate and other debt securities	593,465	(13,054)	44,117	(2,351)	637,582	(15,405)
Total debt securities	<u>1,449,567</u>	<u>(42,898)</u>	<u>62,073</u>	<u>(2,802)</u>	<u>1,511,640</u>	<u>(45,700)</u>
<b>Equity securities</b>						
Domestic	39,551	(5,400)	9,364	(816)	48,915	(6,216)
Foreign	299,755	(5,328)	26,839	(3,851)	326,594	(9,179)
Total equity securities	<u>339,306</u>	<u>(10,728)</u>	<u>36,203</u>	<u>(4,667)</u>	<u>375,509</u>	<u>(15,395)</u>
Total	<u>\$ 1,788,873</u>	<u>\$ (53,626)</u>	<u>\$ 98,276</u>	<u>\$ (7,469)</u>	<u>\$ 1,887,149</u>	<u>\$ (61,095)</u>

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At December 31, 2017 and 2016, the Corporation held available-for-sale debt securities with gross unrealized losses of \$29,548 and \$45,700, respectively. Management evaluated the unrealized losses and determined that they were due primarily to volatility in the interest rate environment and market conditions. The Corporation does not intend to sell the related debt securities and it is not likely that the Corporation will be required to sell the debt securities before recovery of their amortized cost basis, which may be maturity. Therefore, management does not consider the available-for-sale debt securities to be other-than-temporarily impaired as of December 31, 2017 and 2016.

At December 31, 2017 and 2016, the Corporation held available-for-sale equity securities with gross unrealized losses of \$6,977 and \$15,395, respectively. Management reviews equity securities in which fair value falls below cost. In determining whether an equity security is other-than-temporarily impaired, management considers both quantitative and qualitative information. The impairment review process is subjective and considers a number of factors, including, but not limited to, the length of time and extent to which the fair value has been less than book value, the financial condition and near-term prospects of the issuer, recommendations of investment advisors, the intent and ability to hold securities for a time sufficient to allow for any anticipated recovery in value and general market conditions and industry or sector-specific factors, including forecasts of economic, market or industry trends. Management does not consider the available-for-sale equity securities to be other-than-temporarily impaired as of December 31, 2017 and 2016.

The amortized cost and fair value of available-for-sale debt securities at December 31, 2017 are shown below by contractual maturity. Expected maturities could differ from contractual maturities as borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	<b>Amortized Cost</b>	<b>Fair Value</b>
Due within one year or less	\$ 251,702	\$ 251,726
Due after one year through five years	1,051,919	1,058,616
Due after five years through ten years	706,068	710,650
Due after ten years	329,993	332,799
Mortgage and asset-backed securities	570,832	569,885
Total debt securities	\$ 2,910,514	\$ 2,923,676

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*(in thousands of dollars)*

Board designated, restricted and other investments by investment type at December 31, 2017 and 2016 consisted of the following:

	<b>2017</b>	<b>2016</b>
Cash and cash equivalents	\$ 249,354	\$ 70,075
Debt securities		
U.S. Treasury and agency obligations	99,713	64,242
Agency mortgage-backed securities	3,732	4,833
Asset and mortgage-backed securities	2,198	5,102
Corporate and other debt securities	61,187	94,112
Total debt securities	<u>166,830</u>	<u>168,289</u>
Equity securities		
Domestic	100,708	128,939
Foreign	68,710	42,613
Endowments managed by donor selected trustees	251,177	224,405
Common collective trust interests	262	240
Total board designated, restricted and other investments	<u>\$ 837,041</u>	<u>\$ 634,561</u>

Board designated, restricted and other investments consist of the following components at December 31, 2017 and 2016:

	<b>2017</b>	<b>2016</b>
Unrestricted		
Other investments	\$ 271,300	\$ 278,379
Board designated		
Capital improvements	-	4,110
Foundation	35,335	34,973
Capital project funds	194,556	-
Debt service	-	5,596
Self-insurance reserves	807	2,913
Grant funds and other	29,335	26,844
Total unrestricted	<u>531,333</u>	<u>352,815</u>
Temporarily restricted	20,057	24,540
Permanently restricted	285,651	257,206
Total board designated, restricted and other investments	<u>\$ 837,041</u>	<u>\$ 634,561</u>



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The following is a summary of net investment income for the year ended December 31, 2017:

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>
Interest and dividends, net	\$ 162,405	\$ 1,239	\$ 3,910
Net realized gains on investments	66,388	2,031	9,353
Net unrealized gains (losses) on board designated, restricted and other investments	9,771	(833)	23,208
Total net investment income	<u>\$ 238,564</u>	<u>\$ 2,437</u>	<u>\$ 36,471</u>

The following is a summary of net investment income for the year ended December 31, 2016:

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>
Interest and dividends, net	\$ 131,629	\$ 878	\$ 3,658
Net realized gains (losses) on investments	25,744	(43)	2,068
Net unrealized gains on board designated, restricted and other investments	9,141	549	7,365
Total net investment income	<u>\$ 166,514</u>	<u>\$ 1,384</u>	<u>\$ 13,091</u>

Net realized gains (losses) on unrestricted investments include \$10,839 and \$18,826 in 2017 and 2016, respectively, in other-than-temporary impairment charges on available-for-sale securities. Other-than-temporary impairments recognized in 2017 and 2016 resulted from the extent and duration of fair value declines due to market conditions, along with credit related concerns in certain instances. Impaired securities included mainly equity and debt securities within the domestic financial services, commodity and energy business sectors, along with international market holdings.

The recognition of unrealized gains and losses on investments that are restricted as to use are recorded directly to temporarily and permanently restricted net assets as required by donor or regulation. These investments consist primarily of equity securities, agency mortgage-backed securities, corporate debt securities and U.S. Treasury obligations. All unrealized gains and losses on marketable unrestricted board designated and other investments are recognized in net investment income.

Certain investment partnership and trust vehicles of the Corporation have redemption restrictions relating to both timing and amounts of withdrawals. Generally, the amounts are available for withdrawal subject to a 30 days' notice requirement. At December 31, 2017 and 2016, these investments totaled \$384,336 and \$314,198, respectively.

Certain other private equity limited partnership interests of the Corporation have redemption restrictions relating to both timing and amounts of withdrawals. Distributions are received as the underlying investments generate income or are liquidated. The Corporation estimates that the underlying assets of certain other private equity limited partnership interests will be liquidated over the next seven to ten years, and the Corporation assumes that the interests will be held until liquidation. At December 31, 2017 and 2016, these investments totaled \$163,657 and \$123,994, respectively.

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The following is a summary of the remaining contractual maturity of securities lending transactions accounted for as secured borrowings as of December 31, 2017:

	2017				
	Remaining Contractual Maturity of the Agreements				
	Overnight and Continuous	Up to 30 days	30-90 days	Greater than 90 days	Total
Securities Lending Transactions					
Corporate fixed income securities	\$ -	\$ 1,645	\$ 1,514	\$ 4,041	\$ 7,200
International fixed income securities	-	5,208	13,092	35,443	53,743
Other	3,177	47,394	909	-	51,480
Total borrowings	\$ 3,177	\$ 54,247	\$ 15,515	\$ 39,484	\$ 112,423

The following is a summary of the remaining contractual maturity of securities lending transactions accounted for as secured borrowings as of December 31, 2016:

	2016				
	Remaining Contractual Maturity of the Agreements				
	Overnight and Continuous	Up to 30 days	30-90 days	Greater than 90 days	Total
Securities Lending Transactions					
Corporate fixed income securities	\$ -	\$ 2,770	\$ 2,418	\$ 11,088	\$ 16,276
International fixed income securities	-	10,930	10,252	61,888	83,070
Other	22,220	35,255	5,466	1,305	64,246
Total borrowings	\$ 22,220	\$ 48,955	\$ 18,136	\$ 74,281	\$ 163,592

**7. Fair Value of Financial Instruments**

Input levels, as defined by FASB, are as follows:

*Level 1:* Pricing inputs are based on unadjusted quoted market prices for identical financial assets or liabilities in active markets. Active markets are those in which transactions occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

*Level 2:* Pricing inputs include observable inputs other than Level 1 pricing inputs, such as quoted prices in active markets for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

*Level 3:* Pricing inputs include observable inputs that are supported by little or no market activity and that reflect management's best estimate of what market participants would use in pricing the asset or liability at the measurement date.

# Highmark Health

## Notes to Consolidated Financial Statements

### December 31, 2017 and 2016

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*(in thousands of dollars)*

The following methods and assumptions were used to determine the fair value of each class of the following assets and liabilities recorded at fair value in the Consolidated Balance Sheets:

*Cash equivalents:* Cash equivalents include highly rated money market funds, commercial paper or discount notes with maturities of three months or less and bank deposits, and are purchased or deposited daily with specified yield rates. Cash equivalents are designated as Level 1 or Level 2, depending on structure and the extent of credit-related features.

*Debt securities, available-for-sale:* Fair values of available-for-sale debt securities are based on quoted market prices, where available. These fair values are obtained primarily from a third party pricing service, which generally use Level 1 or Level 2 inputs, for the determination of fair value to facilitate fair value measurements and disclosures. U.S. Treasury securities generally are designated Level 1 securities, while Level 2 securities generally include corporate securities, state and political obligations, mortgage-backed securities, and asset-backed securities. Level 2 inputs that are often used in the valuation methodologies include, but are not limited to, broker quotes, benchmark yields, credit spreads, default rates and prepayment speeds. The Corporation has certain fixed maturity, corporate and other debt securities, which are designated as Level 3 securities. For these securities, the valuation methodologies may incorporate broker quotes or assumptions for benchmark yields, credit spreads, default rates and prepayment speeds that are not observable in the markets.

*Equity securities, available-for-sale:* Fair values of equity securities are generally designated as Level 1 and are based on quoted market prices for identical assets in active markets. For certain equity securities, quoted market prices for identical securities are not always available and the fair value is estimated by reference to similar or underlying securities for which quoted prices are available. These securities are designated Level 2. The Corporation also has certain equity securities, including private equity securities, for which fair value is estimated based on each security's current condition and future cash flow projections or based on the Corporation's share of the entities' undistributed earnings, which approximates fair value. Such securities are designated Level 3. Certain equity securities are valued at NAV as a practical expedient to fair value. The holdings of the underlying investments are measured at fair value as of the reporting date. These investments, if sold, are probable of being sold at amounts equal to NAV per share.

*Board designated, restricted and other investments:* Board designated, restricted and other investments include cash equivalents, debt securities and equity securities that follow the same methods and assumptions and fair value designations described above. The fair value for endowments managed by donor selected trustees are designated as Level 3 securities with the interest in these trusts based on the fair value of the underlying trust investments, which approximates the present value of the expected future cash flows for which the Corporation is an income beneficiary. Certain board designated, restricted and other investments are valued at NAV as a practical expedient to fair value.

*Other Investments:* The fair value of ownership interest in real estate trusts are approximated based on trustee estimates and are designated as Level 3 securities. Limited partnerships and limited liability companies are accounted for using the equity method and are based on the estimated fair values from the financial statements obtained from the investment vehicle. Limited partnerships and limited liability companies are designated at Level 3. Certain other investments' prices have been estimated using the NAV per share of the investments, which are based on market prices of underlying securities.

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*(in thousands of dollars)*

*Securities lending invested collateral:* Fair values of securities lending collateral are based on quoted market prices, where available. These fair values are obtained primarily from third party pricing services, which generally use Level 1 or Level 2 inputs for the determination of fair value to facilitate fair value measurements and disclosures.

The Corporation uses a third party pricing service to obtain quoted prices for each security. The third party service provides pricing based on recent trades of the specific security or like securities, as well as a variety of valuation methodologies for those securities where an observable market price may not exist. The third party service may derive pricing for Level 2 securities from market corroborated pricing, matrix pricing, discounted cash flow analyses and inputs such as yield curves and indices. Pricing for Level 3 securities may be obtained from investment managers for private placements or derived from discounted cash flows, or ratio analysis and price comparisons of similar companies.

The Corporation performs an analysis of reasonableness of the prices received for fair value by monitoring month-to-month fluctuations and determining reasons for significant differences, selectively testing fair values against prices obtained from other sources, and comparing the consolidated fair value of a class of assets against an appropriate index benchmark. The Corporation did not make adjustments to the quoted market prices obtained from third party pricing services that were material to the Consolidated Financial Statements.

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The following table summarizes fair value measurements by level at December 31, 2017 for financial assets measured at fair value on a recurring basis:

	Fair Value	Level 1	Level 2	Level 3	Net Asset Value
<b>Assets</b>					
Cash and cash equivalents	\$ 2,354,529	\$ 2,113,092	\$ 241,437	\$ -	\$ -
Investments					
Debt securities, available-for-sale					
U.S. Treasury and agency obligations	739,188	455,843	283,345	-	-
Agency mortgage-backed securities	496,545	-	496,545	-	-
State and political obligations	11,315	-	11,315	-	-
Mortgage-backed securities	18,107	-	18,107	-	-
Asset-backed securities	55,234	-	55,234	-	-
Corporate and other debt securities	1,603,287	-	1,557,735	45,552	-
Total debt securities	2,923,676	455,843	2,422,281	45,552	-
Equity securities, available-for-sale					
Domestic	610,768	598,826	-	11,942	-
Foreign	583,420	209,349	-	-	374,071
Total equity securities	1,194,188	808,175	-	11,942	374,071
Board designated, restricted and other investments					
Cash and cash equivalents	249,354	249,354	-	-	-
Debt securities					
U.S. Treasury and agency obligations	99,713	49,263	50,450	-	-
Agency mortgage-backed securities	3,732	-	3,732	-	-
Asset and mortgage-backed securities	2,198	-	2,198	-	-
Corporate and other debt securities	61,187	-	61,187	-	-
Equity securities					
Domestic	100,708	93,209	-	7,499	-
Foreign	68,710	68,710	-	-	-
Endowments	251,177	-	-	251,177	-
Common Collective Trust Interests	262	-	-	-	262
Total board designated, restricted and other investments	837,041	460,536	117,567	258,676	262
Other investments					
Real estate investment trusts	10,265	-	-	-	10,265
Private limited partnerships and limited liability companies	163,504	-	-	-	163,504
Private Equity	21,496	-	-	21,496	-
Total other investments	195,265	-	-	21,496	173,769
Securities lending invested collateral	112,429	-	112,429	-	-
<b>Total assets</b>	<b>\$ 7,617,128</b>	<b>\$ 3,837,646</b>	<b>\$ 2,893,714</b>	<b>\$ 337,666</b>	<b>\$ 548,102</b>

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The following table summarizes fair value measurements by level at December 31, 2016 for financial assets measured at fair value on a recurring basis:

	Fair Value	Level 1	Level 2	Level 3	Net Asset Value
<b>Assets</b>					
Cash and cash equivalents	\$ 1,510,771	\$ 1,495,323	\$ 15,448	\$ -	\$ -
<b>Investments</b>					
Debt securities, available-for-sale					
U.S. Treasury and agency obligations	707,400	432,673	274,727	-	-
Agency mortgage-backed securities	442,370	-	442,370	-	-
State and political obligations	26,363	-	26,282	81	-
Mortgage-backed securities	23,624	-	23,624	-	-
Asset-backed securities	49,347	-	49,347	-	-
Corporate and other debt securities	1,688,544	-	1,639,823	48,721	-
Total debt securities	2,937,648	432,673	2,456,173	48,802	-
Equity securities, available-for-sale					
Domestic	555,036	541,416	-	13,620	-
Foreign	484,122	179,622	-	-	304,500
Total equity securities	1,039,158	721,038	-	13,620	304,500
Board designated, restricted and other investments					
Cash and cash equivalents	70,075	70,075	-	-	-
Debt securities					
U.S. Treasury and agency obligations	64,242	56,798	7,444	-	-
Agency mortgage-backed securities	4,833	-	4,833	-	-
State and political obligations	2,005	-	2,005	-	-
Asset and mortgage-backed securities	5,102	-	5,102	-	-
Corporate and other debt securities	92,107	-	92,107	-	-
Equity securities					
Domestic	128,939	121,440	-	7,499	-
Foreign	42,613	42,613	-	-	-
Endowments	224,405	-	-	224,405	-
Common Collective Trust Interests	240	-	-	-	240
Total board designated, restricted and other investments	634,561	290,926	111,491	231,904	240
Other investments					
Real estate investment trusts	9,698	-	-	-	9,698
Private limited partnerships and limited liability companies	126,995	-	-	3,000	123,995
Total other investments	136,693	-	-	3,000	133,693
Securities lending invested collateral	163,592	-	163,592	-	-
<b>Total assets</b>	<b>\$ 6,422,423</b>	<b>\$ 2,939,960</b>	<b>\$ 2,746,704</b>	<b>\$ 297,326</b>	<b>\$ 438,433</b>

Transfers between levels, if any, are recorded annually as of the end of the reporting period unless, with respect to a particular issue, a significant event occurred that necessitated the transfer be reported at the date of the event.

There were no material transfers between Levels 1 and 2 during the years ended December 31, 2017 and 2016.

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*(in thousands of dollars)*

The changes in fair value for assets measured using significant unobservable inputs (Level 3) for the year ended December 31, 2017 was as follows:

	Corporate and other debt securities	Equity securities	Endowments	Private limited partnerships and limited liability companies	Private Equity	Total
Balance at January 1	\$ 48,802	\$ 21,119	\$ 224,405	\$ 3,000	\$ -	\$ 297,326
Net unrealized (losses) gains	(564)	-	20,255	-	-	19,691
Net realized gains (losses)	345	(1,678)	15,084	-	-	13,751
Impairments	(110)	-	-	-	-	(110)
Purchases	23,717	932	11	-	21,496	46,156
Sales	(26,638)	(932)	(8,578)	(3,000)	-	(39,148)
Balance at December 31	\$ 45,552	\$ 19,441	\$ 251,177	\$ -	\$ 21,496	\$ 337,666

The changes in fair value for assets measured using significant unobservable inputs (Level 3) for the year ended December 31, 2016 was as follows:

	Corporate and other debt securities	Equity securities	Endowments	Private limited partnerships and limited liability companies	Total
Balance at January 1	\$ 41,900	\$ 12,627	\$ 219,772	\$ 3,000	\$ 277,299
Net unrealized gains	2,170	-	7,452	-	9,622
Net realized gains (losses)	54	(675)	5,759	-	5,138
Impairments	(475)	-	-	-	(475)
Purchases	31,002	9,167	-	-	40,169
Sales	(25,849)	-	(8,578)	-	(34,427)
Balance at December 31	\$ 48,802	\$ 21,119	\$ 224,405	\$ 3,000	\$ 297,326

The following table summarizes the nature of the funds valued based on net asset value as a practical expedient for fair value as of December 31, 2017:

	Fair Value	Unfunded Commitments	Redemption Frequency (if currently eligible)	Redemption Notice Period
Common Collective Trust Interests	\$ 374,333	\$ -	Daily, Quarterly, Monthly	1-120 Days
Real estate investment trust	10,265	-		
Private limited partnerships	163,504	132,852		
Total	\$ 548,102	\$ 132,852		

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The following table summarizes the nature of the funds valued based on net asset value as a practical expedient for fair value as of December 31, 2016:

	<u>Fair Value</u>	<u>Unfunded Commitments</u>	<u>Redemption Frequency (if currently eligible)</u>	<u>Redemption Notice Period</u>
Common Collective Trust Interests	\$ 304,740	\$ -	Daily, Quarterly, Monthly	1-120 Days
Real estate investment trust	9,698	-		
Private limited partnerships	123,995	111,446		
Total	<u>\$ 438,433</u>	<u>\$ 111,446</u>		

**8. Property and Equipment, Net**

Property and equipment at December 31, 2017 and 2016 was comprised of the following:

	<b>2017</b>	<b>2016</b>
Land, buildings and leasehold improvements	\$ 1,583,779	\$ 1,487,231
Office furniture and equipment	1,197,031	1,177,242
Capitalized software	841,335	729,592
Construction in progress	76,938	110,803
	<u>3,699,083</u>	<u>3,504,868</u>
Less accumulated depreciation and amortization	<u>(1,879,050)</u>	<u>(1,719,829)</u>
Property and equipment, net	<u>\$ 1,820,033</u>	<u>\$ 1,785,039</u>

Depreciation and amortization expense related to property and equipment amounted to \$297,572 and \$276,798 for 2017 and 2016, respectively.

**9. Goodwill and Other Intangible Assets, Net**

Goodwill consisted of the following at December 31, 2017 and 2016:

Goodwill, at January 1, 2016	\$ 793,719
Acquisitions	667
Other	(3,799)
Goodwill, at December 31, 2016	<u>\$ 790,587</u>
Impairment	(277,738)
Sale of subsidiary	(96,837)
Consolidation of affiliate	14,880
Goodwill, at December 31, 2017	<u>\$ 430,892</u>



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As part of the annual impairment analysis, a goodwill impairment charge of \$277,738 was recorded within the Consolidated Statement of Operations related to a subsidiary. The impairment charge represents the excess of the book value of the subsidiary over the fair value, as determined by a valuation model. No impairment charges were recorded in 2016.

The gross carrying amount of intangible assets and accumulated amortization in 2017 and 2016 was as follows:

	2017			2016		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	\$ 60,412	\$ 18,400	\$ 42,012	\$ 42,712	\$ 15,933	\$ 26,779
Trademarks	20,575	11,144	9,431	16,675	10,316	6,359
Patient records	9,021	5,489	3,532	9,021	5,188	3,833
Other	36,243	21,796	14,447	29,445	21,423	8,022
Total	\$ 126,251	\$ 56,829	\$ 69,422	\$ 97,853	\$ 52,860	\$ 44,993

Amortization expense related to intangible assets was \$4,025 and \$7,015 in 2017 and 2016, respectively.

At December 31, 2017, estimated future amortization expense for the intangible assets, excluding insurance licenses with indefinite lives of \$3,915, was as follows:

Years ending December 31,	
2018	\$ 5,342
2019	5,255
2020	4,252
2021	4,210
2022	4,176
Thereafter	42,272
Total	\$ 65,507

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**10. Claims Outstanding**

In accordance with ASU 2015-09, the Corporation's insurance business has three business segments, which are referred to as Commercial business, Government business and Diversified business. The Commercial business segment is a combination of fully-insured business and self-funded business. The Government business includes fully-insured health business such as Medicare products, Medicaid products, pre-65 individual including ACA products and Small Group products. The Diversified business includes Vision, Dental and Stop-loss insurance product offerings.

A reconciliation of the beginning and ending balance for claims outstanding, by segment, for the year ended December 31, 2017 is as follows:

	<b>Commercial</b>	<b>Government</b>	<b>Diversified</b>	<b>Total</b>
Gross claims payable, beginning of year	\$ 1,391,745	\$ 810,481	\$ 406,307	\$ 2,608,533
Provider advances, beginning of year	47,747	6	-	47,753
Reinsurance recoverables, beginning of year	(30,055)	(81,901)	(64,509)	(176,465)
Non-risk claim liabilities, beginning of year	(910,151)	-	(35,862)	(946,013)
Net balance, beginning of year	<u>499,286</u>	<u>728,586</u>	<u>305,936</u>	<u>1,533,808</u>
Claim liabilities assumed through acquisition	-	44,203	-	44,203
Net incurred claims				
Current year	3,532,325	5,600,385	1,922,561	11,055,271
Prior year	(12,185)	(188,713)	(3,327)	(204,225)
Total net incurred claims	<u>3,520,140</u>	<u>5,411,672</u>	<u>1,919,234</u>	<u>10,851,046</u>
Net payments attributable to:				
Current year	(3,149,273)	(5,036,986)	(1,549,668)	(9,735,927)
Prior year	(468,395)	(505,456)	(286,212)	(1,260,063)
Total net payments	<u>(3,617,668)</u>	<u>(5,542,442)</u>	<u>(1,835,880)</u>	<u>(10,995,990)</u>
Net claims payable, end of year	401,758	642,019	389,290	1,433,067
Provider advances, end of year	(39,909)	-	-	(39,909)
Reinsurance recoverables, end of year	34,749	16,953	65,321	117,023
Non-risk claim liabilities, end of year	1,029,738	-	31,557	1,061,295
Gross claims, end of year	<u>\$ 1,426,336</u>	<u>\$ 658,972</u>	<u>\$ 486,168</u>	<u>\$ 2,571,476</u>

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A reconciliation of the beginning and ending balance for claims outstanding, by segment, for the year ended December 31, 2016 is as follows:

	<b>Commercial</b>	<b>Government</b>	<b>Diversified</b>	<b>Total</b>
Gross claims payable, beginning of year	\$ 1,452,545	\$ 927,462	\$ 555,200	\$ 2,935,207
Provider advances, beginning of year	42,533	86	-	42,619
Reinsurance recoverables, beginning of year	(24,915)	(223,875)	(69,938)	(318,728)
Non-risk claim liabilities, beginning of year	(1,143,705)	-	(37,080)	(1,180,785)
Net balance, beginning of year	<u>326,458</u>	<u>703,673</u>	<u>448,182</u>	<u>1,478,313</u>
Net incurred claims				
Current year	3,561,947	6,462,725	1,557,136	11,581,808
Prior year	24,108	(38,695)	(17,337)	(31,924)
Total net incurred claims	<u>3,586,055</u>	<u>6,424,030</u>	<u>1,539,799</u>	<u>11,549,884</u>
Net payments attributable to:				
Current year	(3,077,865)	(5,793,450)	(1,226,082)	(10,097,397)
Prior year	(335,362)	(605,667)	(305,603)	(1,246,632)
Total net payments	<u>(3,413,227)</u>	<u>(6,399,117)</u>	<u>(1,531,685)</u>	<u>(11,344,029)</u>
Transfer to Assets and Liabilities held for sale at July 1	-	-	(150,360)	(150,360)
Net claims payable, end of year	499,286	728,586	305,936	1,533,808
Provider advances, end of year	(47,747)	(6)	-	(47,753)
Reinsurance recoverables, end of year	30,055	81,901	64,509	176,465
Non-risk claim liabilities, end of year	910,151	-	35,862	946,013
Gross claims, end of year	<u>\$ 1,391,745</u>	<u>\$ 810,481</u>	<u>\$ 406,307</u>	<u>\$ 2,608,533</u>

Amounts incurred related to prior years vary from previously estimated liabilities as the claims ultimately are settled. Negative amounts reported for incurred related to prior years result from claims being ultimately settled for amounts less than originally estimated (favorable development).

The cumulative number of reported claims for each claim year for each segment has been developed using historical data captured by our enterprise data warehouse.

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Incurred and paid claims development, net of reinsurance, for the Commercial Business for the years ended December 31, 2017 and 2016 is as follows:

<i>Commercial</i>	Cumulative Incurred Claims and Allocated Claim Adjustment Expenses, Net of Reinsurance (Unaudited)			As of December 31, 2017		
	Claim Year	2015	2016	2017	Total of Incurred-but-Not-Reported Liabilities Plus Expected Development on Reported Claims	Cumulative Number of Reported Claims
2015	\$ 3,001,024	\$ 3,045,957	\$ 3,046,936	\$	1,219	11,434
2016	-	3,561,947	3,548,783	\$	5,758	12,091
2017	-	-	3,532,325	\$	272,076	12,007
Total	\$ 3,001,024	\$ 6,607,904	\$ 10,128,044			

<i>Commercial</i>	Cumulative Paid Claims and Allocated Claim Adjustment Expenses, Net of Reinsurance (Unaudited)		
Claim Year	2015	2016	2017
2015	\$ 2,713,042	\$ 3,030,753	\$ 3,046,236
2016	-	3,077,865	3,530,777
2017	-	-	3,149,273
Total	\$ 2,713,042	\$ 6,108,618	\$ 9,726,286

Incurred and paid claims development, net of reinsurance, for the Government Business as of and for the years ended December 31, 2017 and 2016 is as follows:

<i>Government</i>	Cumulative Incurred Claims and Allocated Claim Adjustment Expenses, Net of Reinsurance (Unaudited)			As of December 31, 2017		
	Claim Year	2015	2016	2017	Total of Incurred-but-Not-Reported Liabilities Plus Expected Development on Reported Claims	Cumulative Number of Reported Claims
2015	\$ 7,178,989	\$ 7,153,537	\$ 7,143,252	\$	909	27,506
2016	-	6,462,725	6,284,296	\$	7,708	27,916
2017	-	-	5,600,385	\$	561,467	25,013
Total	\$ 7,178,989	\$ 13,616,262	\$ 19,027,933			

<i>Government</i>	Cumulative Paid Claims and Allocated Claim Adjustment Expenses, Net of Reinsurance (Unaudited)		
Claim Year	2015	2016	2017
2015	\$ 6,536,833	\$ 7,094,226	\$ 7,121,968
2016	-	5,793,450	6,271,163
2017	-	-	5,036,986
Total	\$ 6,536,833	\$ 12,887,676	\$ 18,430,117

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Incurred and paid claims development, net of reinsurance, for the Diversified Business as of and for the years ended December 31, 2017 and 2016 is as follows:

<i>Diversified</i>	Cumulative Incurred Claims and Allocated Claim Adjustment Expenses, Net of Reinsurance			As of December 31, 2017	
	(Unaudited)			Total of Incurred-but-Not-Reported Liabilities Plus Expected Development on Reported Claims	Cumulative Number of Reported Claims
	Claim Year	2015	2016		
2015	\$ 1,518,429	\$ 1,555,794	\$ 1,540,539	\$ -	6,445
2016	-	1,557,136	1,569,064	\$ 6,811	6,034
2017	-	-	1,922,561	\$ 470,990	7,173
Total	\$ 1,518,429	\$ 3,112,930	\$ 5,032,164		

<i>Diversified</i>	Cumulative Paid Claims and Allocated Claim Adjustment Expenses, Net of Reinsurance		
	(Unaudited)		
	Claim Year	2015	2016
2015	\$ 1,159,436	\$ 1,535,189	\$ 1,536,752
2016	-	1,226,082	1,556,454
2017	-	-	1,549,668
Total	\$ 1,159,436	\$ 2,761,271	\$ 4,642,874

The reconciliation of the Commercial, Government, and Diversified Businesses incurred and paid claims development information, reflected in the tables above, to the consolidated ending balance for claims outstanding, as of December 31, 2017, is as follows:

	Commercial	Government	Diversified	Total
Cumulative incurred claims and allocated claim adjustment expenses, net of reinsurance	\$ 10,128,044	\$ 19,027,933	\$ 5,032,164	\$ 34,188,141
Less: cumulative paid claims and allocated claim adjustment expenses, net of reinsurance	9,726,286	18,430,117	4,642,874	32,799,277
Net claims payable, end of year	401,758	597,816	389,290	1,388,864
Claim liabilities assumed through consolidation of affiliate	-	44,203	-	44,203
Net claims payable, end of year	\$ 401,758	\$ 642,019	\$ 389,290	\$ 1,433,067

# Highmark Health

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#### 11. Employee Benefit Plans

The Corporation covers certain employees meeting age and service requirements through multiple non-contributory defined benefit pension plans (the "pension plans"); the Highmark Retirement Plan ("Highmark pension plan"), the West Penn Retirement Plan for Represented Employees and the West Penn Retirement Plan for Nonrepresented Employees (collectively the "WPAHS pension plans"), the Jefferson Retirement Plan (the "JRMC pension plan"), and the Saint Vincent Health System Pension Plan (the "SVHS pension plan"). The Highmark and WPAHS pension plans provide participants with a frozen legacy benefit as well as a cash-balance account consisting of pay credits, based on age and years of service, interest credits and limited transition credits. The JRMC and SVHS pension plans are frozen. In March 2017, WPAHS approved a plan to freeze its Non-Represented Employees pension plan effective December 31, 2017. As a result of this change, a curtailment gain of \$13,336 was recognized in 2017, which reduced the plan's unrecognized loss. Effective January 1, 2016, the Highmark West Virginia Inc. Retirement Program merged into the Highmark Retirement Plan. On July 26, 2016, various amendments to the Highmark pension plan were approved by the Highmark Health Personnel and Compensation Committee. Pursuant to these amendments, the Highmark pension plan was closed to new participants effective June 30, 2017, and benefit accruals will freeze effective December 31, 2020. As a result of these amendments, a curtailment gain of \$50,123 was recognized in 2016 which reduced other operating expenses. Additionally, the BCNEPA Pension Plan was frozen effective December 31, 2016 and merged into the Highmark pension plan effective January 1, 2017. As a result of these changes, a settlement loss of \$400 was recognized in 2016 which increased other operating expenses.

The Corporation funds its pension plans according to minimum funding requirements of the Employee Retirement Income Security Act of 1974 ("ERISA"), as amended. During 2018, the Corporation expects to contribute \$80,100 to the pension plans.

Highmark sponsors a defined benefit other postretirement plan; the Highmark Postretirement Welfare Benefits Plan (the "welfare plan"). The welfare plan provides various postretirement health and life insurance benefits to retirees of participating subsidiaries and affiliates and is closed to new employees. On July 26, 2016, various amendments to the welfare plan were approved by the Highmark Health Personnel and Compensation Committee. Pursuant to these amendments, the benefit accruals under the welfare plan were frozen as of December 31, 2016 and the life insurance benefit will not be provided to participants who retired after December 31, 2016. As a result of these amendments, a curtailment gain of \$19,435 was recognized in 2016 which reduced other operating expenses. Additionally, various changes were made to the BCNEPA Postretirement Medical Plan (the "NEPA welfare plan") to align plan provisions with the welfare plan and the NEPA welfare plan merged into the welfare plan effective January 1, 2017. As a result of these changes, a curtailment gain of \$2,327 was recognized in 2016 which reduced other operating expenses.

Highmark Inc. uses voluntary employees' beneficiary association ("VEBA") trusts and a 401(h) account to fund its retiree other postretirement benefits. The Corporation expects to contribute \$1,500 to the VEBA trusts and 401(h) account in 2018.

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The amounts recognized in the Consolidated Balance Sheets were as follows:

	<b>Pension Benefits</b>		<b>Other Postretirement Benefits</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
<b>Change in benefit obligations</b>				
Benefit obligations at beginning of year	\$ 3,444,378	\$ 3,394,838	\$ 515,487	\$ 508,644
Service cost	77,160	83,030	537	23,329
Interest cost	112,494	115,062	16,117	15,519
Plan amendments	-	-	916	(8,905)
Participant contributions	22	37	4,987	4,544
Benefit payments	(196,326)	(214,425)	(33,261)	(30,792)
Settlement gain	-	(4,925)	-	-
Curtailement gain	(13,336)	(35,330)	-	(2,327)
Actuarial loss	261,228	106,091	35,674	5,475
Benefit obligations at end of year	<u>\$ 3,685,620</u>	<u>\$ 3,444,378</u>	<u>\$ 540,457</u>	<u>\$ 515,487</u>
<b>Change in plan assets</b>				
Net plan assets at beginning of year	\$ 2,797,569	\$ 2,775,567	\$ 254,993	\$ 262,697
Actual return on plan assets	418,971	153,924	44,513	13,919
Participant contributions	22	37	4,987	4,544
Employer contributions	114,926	87,204	78,809	4,893
Benefit payments	(196,326)	(214,425)	(32,498)	(31,060)
Settlement payments	-	(4,738)	-	-
Net plan assets at end of year	<u>\$ 3,135,162</u>	<u>\$ 2,797,569</u>	<u>\$ 350,804</u>	<u>\$ 254,993</u>
<b>Amounts recognized in the consolidated balance sheets</b>				
Benefit plan assets	\$ 1,129	\$ 2,402	\$ -	\$ -
Benefit plan liabilities	\$ (551,587)	\$ (649,211)	\$ (189,653)	\$ (260,494)
<b>Amounts included in unrestricted net assets</b>				
Prior service credit	\$ 81,933	\$ 110,499	\$ 8,864	\$ 10,492
Actuarial loss	(805,637)	(795,331)	(122,165)	(122,815)
Net amounts recognized	<u>\$ (723,704)</u>	<u>\$ (684,832)</u>	<u>\$ (113,301)</u>	<u>\$ (112,323)</u>

The estimated prior service credit and actuarial loss for the pension plans that will be amortized from net assets in 2018 are \$27,400 and \$40,478, respectively. The estimated prior service credit and actuarial loss for the welfare plan that will be amortized from net assets in 2018 are \$1,100 and \$2,800, respectively.

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The following table provides the components of net periodic benefit (income) cost for the years ended December 31, 2017 and 2016:

	<b>Pension Benefits</b>		<b>Other Postretirement Benefits</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Service cost	\$ 77,160	\$ 83,030	\$ 537	\$ 23,329
Interest cost	112,494	115,062	16,117	15,519
Expected return on plan assets	(200,447)	(199,737)	(12,958)	(13,472)
Amortization of:				
Prior service credit	(27,362)	(27,363)	(1,193)	(2,444)
Actuarial loss	30,037	31,658	2,856	7,054
Curtailment gain	-	(50,123)	-	(21,762)
Settlement loss	-	400	-	-
Net periodic benefit (income) costs	\$ (8,118)	\$ (47,073)	\$ 5,359	\$ 8,224

The Corporation's weighted-average assumptions related to the calculation of the pension benefit obligations and net periodic benefit cost for the pension and other postretirement plans are presented in the table below:

<b>Weighted-average assumptions</b>	<b>Pension Benefits</b>		<b>Other Postretirement Benefits</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Discount rate - benefit obligations	3.51%	4.02%	3.24%	3.59%
Discount rate - net periodic costs	4.01%	3.99%	3.61%	3.88%
Expected return on plan assets	7.10%	7.10%	5.00%; 7.00%	5.00%; 7.00%
Rate of compensation increase	2.45 - 7.50%	2.88 - 7.15%	3.40 - 7.50%	3.40 - 7.10%

The expected return on pension plan assets is developed using inflation expectations, risk factors and input from actuaries to arrive at a long-term nominal expected return for each asset class. The nominal expected return for each asset class is then weighted based on the target asset allocation to develop the expected long-term rate of return on plan assets.

The expected return on other postretirement plan assets is developed based on historical returns and the future expectations for returns for each asset class as well as the asset allocation of the other postretirement plan assets.

For measurement purposes, at December 31, 2017, the assumed annual rate of increase in the per capita costs of covered health care benefits of the other postretirement plans was 6.78% in 2018, gradually decreasing to 4.50% by the year 2039 and remaining at that level thereafter.



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Assumed health care cost trend rates have a significant effect on the amounts reported for the other postretirement plans. At December 31, 2017, a one-percentage-point change in assumed health care cost trend rates would have had the following effects:

	<b>One-Percentage-Point</b>	
	<b>Increase</b>	<b>Decrease</b>
Effect on total of service and interest cost components	\$ 200	\$ (200)
Effect on other postretirement benefit plan obligations	\$ 11,000	\$ (10,000)

Estimated benefit payments are expected as follows:

	<b>Pension Benefits</b>	<b>Other Postretirement Benefits</b>
2018	\$ 177,000	\$ 32,000
2019	\$ 202,000	\$ 34,000
2020	\$ 208,000	\$ 38,000
2021	\$ 213,000	\$ 40,000
2022	\$ 218,000	\$ 42,000
2023-2027	\$ 1,099,000	\$ 221,000

Highmark pension plans represent approximately 68% and 70% of total plan assets as of December 31, 2017 and 2016, respectively. Allegheny Health pension plans represent approximately 32% and 30% of total plan assets as of December 31, 2017 and 2016, respectively. Highmark pension plans primarily set an investment strategy to achieve a mix of 54% of long-duration fixed income securities meant to hedge the benefit obligations, 42% of investments for long-term growth and 4% for near-term benefit payments with a diversification of asset types, fund strategies and fund managers. The target allocations for Highmark pension plan assets are approximately 63.5% fixed income securities, 23% equity securities, 9.5% alternative investments and 4% cash equivalents. The Allegheny Health pension plans primarily set an investment strategy to achieve a mix of 25% of long-duration fixed income securities meant to hedge the benefit obligations, 73% of investments for long-term growth and 2% for near-term benefit payments with a diversification of asset types, fund strategies and fund managers. The target allocations for Allegheny Health plan assets are approximately 25% fixed income securities, 60% equity securities, 13% alternative investments and 2% cash equivalents. Equity securities primarily include stock investments in U.S. developed and emerging market corporations. Fixed income securities primarily include bonds of domestic and foreign companies from diversified industries, domestic mortgage-backed securities and bonds of U.S. and foreign governments and agencies. Alternative investments include investments in real estate and private equity funds that follow several different strategies.

For the welfare plan, the Corporation's overall investment strategy is to achieve a mix of 95% of investments for long-term growth and 5% for near-term benefit payments with a diversification of asset types, fund strategies and fund managers. The target allocations for plan assets are 60% equity securities, 35% fixed income securities and 5% cash equivalents. Equity securities primarily include stock investments in U.S., developed and emerging market corporations. Fixed income securities primarily include bonds of domestic and foreign companies from diversified industries and bonds of U.S. and foreign governments and agencies.

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The pension plans' and welfare plan's overall investment strategies are determined by the plans' investment committees, investment advisors and plan administrators. Overall, the goals of the Corporation are to achieve sufficient diversification of asset types, fund strategies and fund managers in order to minimize volatility and maximize returns over the long term, while still having sufficient funds to pay those benefits due in the near term.

The following table summarizes the fair value measurements by level at December 31, 2017:

	Fair Value	Level 1	Level 2	Level 3	Net Asset Value
<b>Pension plan assets</b>					
Cash and cash equivalents	\$ 4,589	\$ 4,589	\$ -	\$ -	\$ -
Debt securities:					
U.S. Treasury and agency obligations	578,443	573,853	4,590	-	-
Agency mortgage-backed securities	14,390	-	14,390	-	-
State and political obligations	8,564	-	8,564	-	-
Corporate and other debt securities	726,943	-	726,443	500	-
Total debt securities	1,328,340	573,853	753,987	500	-
Equity securities:					
Domestic	375,857	375,603	254	-	-
Foreign	202,345	202,345	-	-	-
Total equity securities	578,202	577,948	254	-	-
Registered investment company shares	603,224	603,224	-	-	-
Private equity limited partnerships	166,251	-	-	-	166,251
Common collective trust interests	443,528	-	73,792	-	369,736
Total	\$ 3,124,134	\$ 1,759,614	\$ 828,033	\$ 500	\$ 535,987
<b>Other postretirement plan assets</b>					
Cash and cash equivalents	\$ 191	\$ 191	\$ -	\$ -	\$ -
U.S. Treasury and agency obligations	15,321	15,321	-	-	-
Agency mortgage backed securities	15,460	-	15,460	-	-
Corporate and other debt securities	38,530	-	38,530	-	-
Domestic equity securities	53,774	53,774	-	-	-
Foreign equity securities	1,871	1,871	-	-	-
Registered investment company shares	216,003	216,003	-	-	-
Common collective trust funds	7,903	-	-	-	7,903
Total	\$ 349,053	\$ 287,160	\$ 53,990	\$ -	\$ 7,903

At December 31, 2017, the fair value of pension plan assets excluded guaranteed insurance contract assets of \$2,469, carried at contract value, as well as accrued interest and other receivables of \$8,559.

At December 31, 2017, the fair value of other postretirement plan assets excluded accrued interest and other receivables of \$1,751.

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The following table summarizes the nature of the funds valued based on net asset value as a practical expedient for fair value as of December 31, 2017:

**Pension plan assets**

	<u>Fair Value</u>	<u>Unfunded Commitments</u>	<u>Redemption Frequency (if currently eligible)</u>	<u>Redemption Notice Period</u>
Private equity limited partnerships	\$ 166,251	\$ 212,000	Quarterly, N/A	30 Days, NA
Common collective trust funds	369,736	-	Daily, Monthly	1-15 Days
Total	<u>\$ 535,987</u>	<u>\$ 212,000</u>		

**Other postretirement plan assets**

	<u>Fair Value</u>	<u>Unfunded Commitments</u>	<u>Redemption Frequency (if currently eligible)</u>	<u>Redemption Notice Period</u>
Common collective trust funds	\$ 7,903	\$ -	Daily	1 Day
Total	<u>\$ 7,903</u>	<u>\$ -</u>		

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The following table summarizes the fair value measurements by level at December 31, 2016:

	Fair Value	Level 1	Level 2	Level 3	Net Asset Value
<b>Pension plan assets</b>					
Cash and cash equivalents	\$ 5	\$ 5	\$ -	\$ -	\$ -
Debt securities:					
U.S. Treasury and agency obligations	539,497	535,219	4,278	-	-
Agency mortgage-backed securities	15,313	-	15,313	-	-
State and political obligations	7,651	-	7,651	-	-
Corporate and other debt securities	662,382	-	661,617	765	-
Total debt securities	1,224,843	535,219	688,859	765	-
Equity securities:					
Domestic	503,400	503,150	250	-	-
Foreign	192,835	192,825	4	6	-
Total equity securities	696,235	695,975	254	6	-
Registered investment company shares	367,793	338,855	28,938	-	-
Private equity limited partnerships	119,489	-	-	-	119,489
Common collective trust interests	377,562	-	90,531	-	287,031
Total	\$ 2,785,927	\$ 1,570,054	\$ 808,582	\$ 771	\$ 406,520
<b>Other postretirement plan assets</b>					
U.S. Treasury and agency obligations	\$ 20,154	\$ 20,154	\$ -	\$ -	\$ -
Agency mortgage backed securities	14,176	-	14,176	-	-
Corporate and other debt securities	32,698	-	32,698	-	-
Domestic equity securities	43,580	43,580	-	-	-
Foreign equity securities	1,406	1,406	-	-	-
Registered investment company shares	135,801	120,185	15,616	-	-
Common collective trust funds	8,129	-	718	-	7,411
Total	\$ 255,944	\$ 185,325	\$ 63,208	\$ -	\$ 7,411

At December 31, 2016, the fair value of pension plan assets excluded guaranteed insurance contract assets of \$3,500, carried at contract value as well as accrued interest and other receivables of \$8,142.

At December 31, 2016, the fair value of other postretirement plan assets excluded accrued interest and other receivables of \$951.

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The following table summarizes the nature of the funds valued based on net asset value as a practical expedient for fair value as of December 31, 2016:

**Pension plan assets**

	<b>Fair Value</b>	<b>Unfunded Commitments</b>	<b>Redemption Frequency (if currently eligible)</b>	<b>Redemption Notice Period</b>
Private equity limited partnerships	\$ 119,489	\$ 145,000	Daily, Monthly	1-10 Days
Common collective trust funds	287,031	-	Quarterly, N/A	30 Days, N/A
<b>Total</b>	<b>\$ 406,520</b>	<b>\$ 145,000</b>		

**Other postretirement plan assets**

	<b>Fair Value</b>	<b>Unfunded Commitments</b>	<b>Redemption Frequency (if currently eligible)</b>	<b>Redemption Notice Period</b>
Common collective trust funds	\$ 7,411	\$ -	Daily	1 Day
<b>Total</b>	<b>\$ 7,411</b>	<b>\$ -</b>		

The changes in fair value for pension plan and other postretirement assets measured using significant unobservable inputs (Level 3) for the years ended December 31, 2017 and 2016 were as follows:

	<b>2017</b>	<b>2016</b>
<b>Balance at January 1,</b>	\$ 771	\$ 11
Realized net losses on investments	(4)	-
Unrealized net holding losses arising during the period	(765)	(30)
Impairments (when applicable)	-	(3)
Purchases	500	46
Sales	(2)	(1)
Transfers in (when applicable)	-	770
Transfers out (when applicable)	-	(22)
<b>Balance at December 31,</b>	<b>\$ 500</b>	<b>\$ 771</b>

The Corporation sponsors several defined contribution savings plans (the "savings plans"), covering substantially all of the Corporation's employees and employees of certain participating affiliates. The savings plans allow participating employees to contribute a percentage of their annual salaries, subject to current Internal Revenue Service ("IRS") limitations. Employee contributions are matched by the Corporation at various percentages. The NEPA 401(k) plan was merged into the Highmark 401(k) plan effective January 1, 2017. A new 401(k) plan was established in 2017 and will be effective January 1, 2018 for the benefit of eligible employees at AHN and existing 401(k) and 403(b) plans sponsored by the AHN hospitals and their subsidiaries were frozen effective December 31, 2017. The Corporation recognized expense associated with its contributions to the savings plans of \$47,852 and \$38,405 for the years ended December 31, 2017 and 2016, respectively.

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The Corporation also sponsors deferred compensation plans for certain eligible employees. Participating employees may contribute a certain amount of their annual compensation to these plans. Certain deferred compensation plans provide for matching contributions based on employee deferrals. The deferred compensation plan pays interest on the deferrals at various rates. The Corporation made matching contributions to the deferred compensation plans of \$607 and \$540 in 2017 and 2016, respectively. Deferred compensation plan liabilities of \$52,037 and \$45,256 were recorded in other payables and accrued expenses in the Consolidated Balance Sheets at December 31, 2017 and 2016, respectively. Changes in the liability are reported in other operating expenses in the Consolidated Statements of Operations.

The Corporation also sponsors an unfunded nonqualified supplemental retirement plan (the "nonqualified retirement plan") covering certain eligible employees. The weighted-average assumptions used in the measurement of the nonqualified plan liabilities were consistent with the assumptions used in the measurement of the pension plans and adjusted, when needed, for nonqualified plan specific characteristics. In 2017 and 2016, respectively, lump-sum benefit payments of \$6,686 and \$17,238 resulted in recognition of settlement losses of \$1,525 and \$6,553 for the nonqualified retirement plan. The nonqualified retirement plan liabilities recorded in other payables and accrued expenses in the Consolidated Balance Sheets at December 31, 2017 and 2016 were \$56,101 and \$59,364, respectively.

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**12. Debt**

The Corporation's total debt at December 31, 2017 and 2016 consisted of the following:

	2017	2016
Unsecured Senior Notes due May 15, 2021	\$ 348,612	\$ 348,201
Unsecured Senior Notes due May 15, 2041	237,834	237,702
AHN Allegheny County Hospital Development Authority Bonds	992,268	-
JRMC Allegheny County Hospital Development Authority Bonds	-	93,588
Erie County Hospital Authority Bonds	-	87,450
Term Loan due May 22, 2019	-	699,054
Revolving credit facility with maximum available for draw of \$275,000 expires July 2018	-	275,000
Revolving credit facility with maximum available for for draw of \$85,000 expires December 2022	20,000	-
Floating Rate Restructuring Certificates	-	3,973
Mortgage loan, due March 15, 2032, interest at 6.00%	22,668	23,423
Capital leases due through 2021 at varying interest rates	50,435	6,810
Mortgage and other loans due through 2021 at varying interest rates	8,262	5,330
Total debt	\$ 1,680,079	\$ 1,780,531

A summary of scheduled principal repayments on debt for the next five years and thereafter is as follows:

<b>Years ending December 31,</b>	
2018	\$ 10,988
2019	42,544
2020	3,366
2021	350,847
2022	1,014,164
Thereafter	258,170
Total	\$ 1,680,079

## Highmark Health

### Notes to Consolidated Financial Statements

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#### **Unsecured Notes**

At December 31, 2017 and 2016, Highmark Inc. had outstanding unsecured Senior Notes of \$348,612 and \$348,201, respectively, due May 15, 2021 with interest payable semi-annually at 4.75%. The unamortized discount was \$476 and \$617 at December 31, 2017 and 2016, respectively. The debt issuance costs were \$912 and \$1,182 at December 31, 2017 and 2016, respectively.

At December 31, 2017 and 2016, Highmark Inc. also had outstanding unsecured Senior Notes of \$237,834 and \$237,702, respectively, due May 15, 2041 with interest payable semi-annually at 6.125%. The unamortized discount was \$1,170 and \$1,223 at December 31, 2017 and 2016, respectively. The debt issuance costs were \$1,872 and \$1,951 at December 31, 2017 and 2016, respectively.

#### **AHN Allegheny County Hospital Development Authority Bond ("AHN Authority Bonds")**

In December 2017, AHN issued aggregate tax exempt revenue bonds of \$1,000,000 (\$300,000 (Series 2017A); \$250,000 (Series 2017B); \$250,000 (Series 2018C); and \$200,000 (Series 2017D)) through the Allegheny County Hospital Development Authority for direct purchase by a financial institution. While the bonds are scheduled to mature in April 2047, the current structure of the multimodal master trust agreement requires that the initial mode with the financial institution end by December 1, 2022, to be replaced with an alternate mode of the bond instrument as remarketed. Under the multimodal structure of the bonds, the bonds can be remarketed in a fixed rate mode. The variable rate interest on the bonds under the initial mode is payable monthly, and AHN has an option during the initial mode to select the interest rate based on either one-month LIBOR, 60 day LIBOR or 90 day LIBOR plus a credit spread. The interest rate is subject to change upon a revision in the federal corporate tax rate. AHN has selected one-month LIBOR at December 31, 2017, with a rate of 2.59% at December 31, 2017. Proceeds from the bonds were used to refinance existing bond debt at Jefferson Regional Medical Center ("JRMC") and Saint Vincent Health System ("SVHS") as well as the 2014 Term Loan at West Penn Allegheny Health System, Inc. ("WPAHS") and provide funding of \$194,000 for various capital projects, which are reported in a project fund included in board designated, restricted and other investments in the Consolidated Balance Sheets. The bonds are collateralized by a guarantee from Highmark Inc. (related only to the initial mode) as well as the gross receivables (excluding restricted amounts) and mortgages on property and equipment of the WPAHS hospitals. Deferred bond issuance costs of \$7,732 were recognized in association with the issuance and will be amortized over the life of the bonds.

#### **JRMC Allegheny County Hospital Development Authority Bonds ("JRMC Authority Bonds")**

JRMC issued JRMC Authority Bonds in September 2010, July 2008, February 2007, May 2006, May 2000 and March 1998. In December 2017, these bonds were retired and all outstanding amounts and related unamortized premiums and discounts were settled. At December 31, 2016, the Corporation had outstanding \$93,588 of JRMC Authority Bonds. Interest rates ranged from 0.78% to 5.125% at December 31, 2016.

#### **Erie County Hospital Authority ("Erie Authority")**

SVHS issued the Series 2009 and Series 2010A in December 2009 and the Series 2010B were issued in January 2010. In December 2017, these Erie Authority bonds were retired and all outstanding amounts were settled. At December 31, 2016, the Corporation had a total of \$81,889 outstanding in Series 2009 and 2010 Erie Authority Bonds. Interest rates ranged from 0.03% to 7.00% at December 31, 2016.



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SVHS issued the Series 2011A Erie Authority Bonds in August 2011. In December 2017, bonds were retired and all outstanding amounts were settled. At December 31, 2016, the Corporation had outstanding \$5,561 of Series 2011A Erie Authority Bonds. Principal and interest were payable monthly and calculated based on 70.00% of LIBOR plus 2.75%. Interest rates were 2.36% at December 31, 2016.

#### **Term Loan**

In May 2014, WPAHS entered into a \$700,000 Term Loan Credit Facility. In December 2017, the Term Loan was repaid and all outstanding amounts and related deferred issuance costs were settled. At December 31, 2016, the carrying value was \$699,054, net of debt issuance costs of \$945. The interest for the term loan was payable monthly and calculated based on LIBOR plus 0.75%.

Interest rates were 0.97% at December 31, 2016. The Term Loan Credit Facility was fully guaranteed by Highmark and secured by a pledge of cash and securities. The fair value of the pledged assets was \$855,960 at December 31, 2016, which satisfied the minimum level needed to maintain the guarantee. Upon repayment of the term loan in December 2017, Highmark was released from this guarantee, and its assets were no longer pledged as security for the loan.

#### **Revolving Credit Facilities**

Highmark holds a \$275,000 revolving credit facility with four financial institutions that expires on July 17, 2018. Amounts borrowed under this facility bear interest at variable interest rates. In September 2017, Highmark repaid its outstanding borrowings totaling \$275,000.

On November 30, 2017, HVHC terminated its revolving credit facility, which had a total commitment of \$275,000 and an expiration date of December 29, 2020. There was no outstanding balance on this revolving credit facility as of the date of termination or December 31, 2016. On December 1, 2017, the revolving credit facility was replaced with a revolving credit and security agreement with a total commitment of \$85,000 and an expiration date of December 1, 2022. Amounts borrowed under this agreement bear interest at variable interest rates. As of December 31, 2017, \$20,000 was outstanding on the revolving credit and security agreement.

In addition to the arrangements set forth in the table above, the Corporation also has a revolving credit facility that provides for total borrowings of \$15,000. As of December 31, 2017 and 2016, there were no amounts outstanding.

#### **Other Debt**

WPAHS had outstanding Floating Rate Restructuring Certificates ("FRRCs") of \$3,973, at December 31, 2016. The remaining FRRC debt was settled and extinguished in 2017 without a material impact. The FRRCs bore interest at the three-month LIBOR plus 0.25%.

SVHS has an outstanding mortgage loan of \$22,668 and \$23,423 at December 31, 2017 and 2016, respectively, related to a medical office building. The mortgage note matures on March 15, 2032 and requires monthly principal and interest payments. The note is secured by the related medical office building.

Several of the debt agreements referred to above contain covenants, including covenants relating to such matters as indebtedness, minimum net worth and financial ratings. At December 31, 2017 and 2016, the Corporation was in compliance with all debt covenants that could affect the financial position or results from operations of the Corporation.

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The carrying amount of debt reported in the Consolidated Balance Sheets at December 31, 2017 and 2016 was \$1,680,079 and \$1,780,531, respectively. Using a discounted cash flow technique that considered credit ratings, with adjustments for duration and risk profile, the Corporation determined that the fair value of its debt at December 31, 2017 and 2016 was \$1,729,327 and \$1,808,671, respectively.

**13. Income Taxes**

The components of the income tax provision for the years ended December 31, 2017 and 2016 were as follows:

	<b>2017</b>	<b>2016</b>
<b>Federal</b>		
Current	\$ 170,904	\$ 75,361
Deferred	(129,224)	27,541
	<u>41,680</u>	<u>102,902</u>
<b>Foreign</b>		
Current	1,147	628
	<u>1,147</u>	<u>628</u>
<b>State</b>		
Current	2,184	6,298
Deferred	6,574	(646)
	<u>8,758</u>	<u>5,652</u>
 Total income tax provision	 <u>\$ 51,585</u>	 <u>\$ 109,182</u>

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The components of deferred income taxes at December 31, 2017 and 2016 were as follows:

	2017	2016
<b>Deferred tax assets</b>		
Benefit plan liabilities	\$ 86,722	\$ 184,473
Net operating loss carryforwards	128,416	158,338
Tax credit carryforwards	233,506	80,810
Other payables and accrued expenses	68,085	79,067
Charitable contribution carryforwards	37,275	87,695
Allowance for doubtful accounts	8,989	26,261
Goodwill and other intangible assets	730	11,853
Unearned revenue	1,647	6,766
Other	9,958	23,173
Total deferred tax assets	<u>575,328</u>	<u>658,436</u>
Less valuation allowance	<u>(211,439)</u>	<u>(349,033)</u>
Total deferred tax assets, net of valuation allowance	<u>363,889</u>	<u>309,403</u>
<b>Deferred tax liabilities</b>		
Net unrealized gains on available-for-sale securities	67,070	53,836
Property and equipment	24,032	42,919
Investment in partnerships/affiliates	10,122	14,901
Other	1,766	4,397
Total deferred tax liabilities	<u>102,990</u>	<u>116,053</u>
Deferred income taxes, net	<u>\$ 260,899</u>	<u>\$ 193,350</u>

In addition to the income tax provision, the deferred tax asset (decreased) increased by (\$47,126) and \$7,136 in 2017 and 2016, respectively, as a result of the tax effect of changes in foreign currency translation adjustments, derivative instruments, changes in benefit plan assets and liabilities, the net unrealized gains on available-for-sale securities, and the contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets) and certain tax benefits. As these changes were recorded within net assets, they did not impact the income tax provision.

The realization of net deferred tax assets is dependent on the Corporation's ability to generate sufficient taxable income in future periods. The amount of deferred tax assets considered realizable, however, could change if estimates of future taxable income change.

The Tax Cuts and Jobs Act of 2017 (the "TCJA"), signed into law on December 22, 2017, reduces the federal income tax rate of the Corporation's taxable entities from 35% to 21% for periods beginning after December 31, 2017. This change resulted in a decrease in the value of the Corporation's net deferred tax assets in 2017 due to the reduced deferred benefit of deductible temporary differences reversing in future periods. Although this change does not have an immediate cash tax impact, the revaluation resulted in \$101,803 of deferred tax expense being recorded through the Statement of Operations for the year ended December 31, 2017. Except as otherwise provided below, any additional impact of the TCJA in future periods is currently being evaluated by

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the Corporation and will be separately disclosed in those periods in which an adjustment is deemed necessary.

At December 31, 2017, the Corporation had non-expiring alternative minimum tax credit carryforwards related to Highmark, Highmark WV and Highmark DE of \$132,126, \$46,532, and \$54,826, respectively, available to offset future taxes. At December 31, 2016, the Corporation recognized a valuation allowance for Highmark WV and Highmark DE due to the uncertainty of realizing a tax benefit for alternative minimum tax credits and because the lower alternative minimum tax rate is expected to apply when net deductible temporary differences reverse. The TCJA repealed alternative minimum tax for corporations and provided a mechanism for taxpayers to monetize related historical credits. As such, the valuation allowance was released in 2017.

At December 31, 2017, various subsidiaries and affiliates of the Corporation had state net operating loss carryforwards totaling \$577,153 that expire between 2018 and 2037 and are available to offset future state taxable income of the subsidiary that generated the loss carryforward. The utilization of the state net operating loss carryforwards is subject to certain limitations. Therefore, the Corporation recognized a valuation allowance given uncertainty surrounding the realizability of the carryforwards.

At December 31, 2017, the Corporation had federal net operating loss carryforwards, related to Highmark DE, Highmark WV, First Priority Life Insurance Co Inc., and Allegheny Health subsidiaries of \$29,866, \$11,918, \$15,715, and \$342,683, respectively, which expire in various amounts through 2037. The utilization of the federal net operating loss carryforwards is subject to certain limitations; therefore, the Corporation recognized a valuation allowance for that portion of the federal net operating loss carryforward not expected to be utilized.

At December 31, 2017, the Corporation had charitable contributions carryforwards of \$177,740 related to Highmark Inc. which expire in various amounts through 2022. The utilization of the charitable contributions carryforwards is subject to certain limitations; therefore, the Corporation recognized a valuation allowance for that portion of the charitable contributions carryforward not expected to be utilized.

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A reconciliation of income tax expense recorded in the Consolidated Statements of Operations and amounts computed at the statutory federal rate for the years ended December 31, 2017 and 2016 was as follows:

	2017	2016
Income taxes at statutory rate	\$ 390,914	\$ 58,712
State taxes, net of federal tax benefit	5,693	3,674
Health insurance providers fee	-	48,805
Change in valuation allowance	(149,765)	15,522
Net impact of tax reform	101,803	-
Gain on sale of subsidiary	(29,343)	-
Impairment of goodwill	84,745	-
Nondeductible compensation	10,365	11,420
IRC section 833(b) deduction	(351,543)	(41,744)
Imputed Interest	7,350	7,350
Income from tax exempt entities	(21,466)	3,557
Other	2,832	1,886
	<u>\$ 51,585</u>	<u>\$ 109,182</u>
Total income tax provision		

Prior to January 1, 1987, the Corporation was exempt from federal income taxes. With the enactment of the Tax Reform Act of 1986 (the "Act"), the Corporation, and all other Blue Cross and Blue Shield plans, became subject to federal income tax. Among other provisions of the Internal Revenue Code, these plans were granted a deduction under Code Section 833(b) (the "special deduction") for regular tax calculation purposes. The special deduction is calculated as the excess of 25% of incurred claims and claim adjustment expenses for the tax year over adjusted surplus, as defined, limited to taxable income. The amount of taxable income before the special deduction has the effect of increasing the adjusted surplus balance used in calculating the special deduction. Once the cumulative adjusted surplus balance exceeds 25% of incurred claims and claim adjustment expenses for the current taxable year, the deduction is eliminated. Little technical guidance has been issued by the taxing authorities regarding the special deduction and therefore some uncertainty exists in its calculation. In 2011, the Corporation requested refunds of approximately \$185,000 (plus interest) for the 2004 through 2007 tax years related to the Special Deduction that have not yet been received. On June 30, 2017 the Corporation filed suit in the United States Court of Federal Claims requesting the refund. In the opinion of management, an adequate reserve against the requested refunds receivable has been made in the consolidated financial statements related to this matter, and the amount that is ultimately received is not expected to materially affect the financial position of the Corporation. Future adjustments may be made to the Corporation's estimated tax benefit as additional information becomes available.

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The changes in the carrying amount of gross unrecognized tax benefits from uncertain tax positions in 2017 and 2016 were as follows:

	2017	2016
Balance at January 1	\$ 169,796	\$ 167,231
Additions for tax positions related to		
Current year	586	3,802
Prior years	771	1,464
Reductions to balance relating to		
Changes in tax positions of prior years	(2,799)	(239)
Statute of limitation expiration	(4,649)	(2,462)
Settlements	(486)	-
Balance at December 31	<u>\$ 163,219</u>	<u>\$ 169,796</u>

At December 31, 2017 and 2016, gross unrecognized tax benefits (excluding the federal benefit received from state positions) were \$157,830 and \$158,491, respectively, and, if recognized, would have impacted the effective tax rate.

At December 31, 2017 and 2016, the Corporation recorded no significant potential interest and penalties receivable or payable in net income tax recoverable in the Consolidated Balance Sheets.

Highmark's consolidated federal income tax return has been examined by the IRS through 2015.

The Corporation does not anticipate that any significant increase or decrease to unrecognized tax benefits will be recorded in 2018.

**14. Temporarily and Permanently Restricted Net Assets**

Temporarily restricted net assets were available for the following purposes at December 31, 2017 and 2016, respectively:

	2017	2016
Clinical programs	\$ 16,546	\$ 18,522
Capital expansion and renovation	1,207	923
Health education and other support	5,057	4,414
Total temporarily restricted net assets	<u>\$ 22,810</u>	<u>\$ 23,859</u>

Temporarily restricted net assets for capital expansion and renovation represent donations, gifts and pledges made for specific hospitals and other facilities. Similarly, temporarily restricted net assets for clinical programs, health education and other support represents donations, gifts and pledges made to support specific programs or departments at hospitals and other facilities. In 2017 and 2016, temporarily restricted net assets were released from donor restrictions by incurring expenditures satisfying the specified restricted purposes in the amount of \$5,012 and \$7,465, respectively.

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Permanently restricted net assets at December 31, 2017 and 2016 were \$285,584 and \$257,206, respectively. These net assets are restricted in perpetuity. Income distributions generated from permanently restricted net assets are either classified as unrestricted or are classified as temporarily restricted based on donor imposed restrictions. At December 31, 2017 and 2016, permanently restricted net assets consisted of endowments managed by donor selected trustees as well as endowments managed by the hospitals of the Corporation.

**15. Leases**

Several noncancellable operating leases, primarily for EDP equipment and office space, were in effect at December 31, 2017. Rental expense is recognized on a straight-line basis over the lease term. Aggregate future rental commitments for all operating leases having initial or remaining noncancellable lease terms in excess of one year with commitments in one or more of the next five years and thereafter are shown in the following table:

Years ending December 31,	Operating Lease Commitments
2018	\$ 176,921
2019	151,844
2020	131,506
2021	103,349
2022	76,761
Thereafter	226,519
Total	<u>\$ 866,900</u>

Rent expense of \$214,941 and \$209,489 in 2017 and 2016, respectively, was recorded in other operating expenses in the accompanying Consolidated Statements of Operations.

**16. Contingencies**

The National Organization of Life & Health Insurance Guaranty Associations ("NOLHGA") is a voluntary organization consisting of the state life and health insurance guaranty associations located throughout the U.S. Such associations, working together with NOLHGA, provide a safety net for their state policyholders, ensuring that they continue to receive coverage, subject to state maximum limits, even if their insurer is declared insolvent. Penn Treaty Network America Insurance Company and its subsidiary American Network Insurance Company (collectively "Penn Treaty") were placed into rehabilitation by order of the Commonwealth Court of Pennsylvania on January 6, 2009. On July 27, 2016, the Pennsylvania Insurance Commissioner, as Rehabilitator for Penn Treaty, filed in Commonwealth Court a petition to convert the rehabilitation to liquidation. The Court granted that petition on March 1, 2017, declaring that Penn Treaty was insolvent and placing Penn Treaty into liquidation. The liquidation order triggered state guaranty association assessments of member insurers. As of December 31, 2017, certain of the Corporation's subsidiaries, which are subject to these assessments, recorded a combined liability of \$59,000. Through December 31, 2017, the Corporation has been assessed a combined amount of \$46,500, which was paid in April 2017 and have an estimated liability remaining of \$13,000 related to anticipated future assessments.

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*(in thousands of dollars)*

On October 1, 2014, Cole's Wexford Hotel, Inc., on behalf of small group purchasers which have obtained health insurance coverage from July 2010 through March 2012, filed a third amended class action complaint in the United States District Court for the Western District of Pennsylvania alleging that the Corporation and UPMC Health System violated antitrust laws by entering into an illegal agreement to restrain trade and by conspiring to create monopolies in the Western Pennsylvania health insurance market. The Corporation believes, based on consultation with legal counsel, that it has meritorious defenses to the claims in this matter, but it is unable to predict the outcome of the matter or to reasonably estimate a range of possible loss.

A number of class action lawsuits filed throughout the United States against the Corporation and/or other Blue Cross and/or Blue Shield plans (the "BCBS Plans") have been consolidated in a multi-district litigation in the U.S. District Court for the Northern District of Alabama under the caption In re: Blue Cross Blue Shield Antitrust Litigation. The lawsuits state that they were filed on behalf of (i) healthcare providers in the United States who have provided services to any patient insured by or who was a member or beneficiary of the Corporation or any other BCBS Plan and/or (ii) members and subscribers of the Corporation and/or any other BCBS Plan. The lawsuits primarily deal with alleged conspiracy and price fixing by and among the BCBS Plans and BCBSA, the competitive impact of exclusive service areas granted by the Association, and alleged contract provisions of the BCBS Plans. Plaintiffs generally seek a judgment that the defendants have violated Section 1 of the Sherman Act, an injunction prohibiting defendants from entering into agreements that restrict the territories in which any BCBS Plan may compete, and an award of treble damages. The Corporation believes, based on consultation with legal counsel, that it has meritorious defenses to the claims in this matter, but it is unable to predict the outcome of the matter or to reasonably estimate a range of possible loss.

Cyndie Nordi, a direct pay subscriber, brought a class action lawsuit in Allegheny County Orphan's Court on September 26, 2014 which has been subsequently transferred to the Civil Division of the Allegheny County Court of Common Pleas. The complaint seeks relief from the Corporation's alleged unlawful conduct on behalf of policyholders. The case challenges the Corporation's operations and accumulation of surplus funds following a February 2005 Determination ("Determination") by the Department that set parameters for an appropriate, sufficient operating surplus. The plaintiff alleges that, despite acceptance of the Determination, the Corporation unlawfully continues to generate significant underwriting gains. Ms. Nordi seeks relief in the form of monetary damages up to disgorging the Corporation of all profits unjustly received and retained. A Petition to Intervene by three other prospective plaintiffs was granted on August 7, 2017 and the plaintiffs filed a First Amended Class Action Complaint on September 6, 2017. The Corporation believes, based on consultation with legal counsel, that it has meritorious defenses to the claims in this matter, but it is unable to predict the outcome of the matter or to reasonably estimate a range of possible loss.



## Highmark Health

### Notes to Consolidated Financial Statements

#### December 31, 2017 and 2016

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*(in thousands of dollars)*

Plains Township and Plymouth Borough, purchasers of insurance from Blue Cross of Northeastern Pennsylvania, filed an amended class action complaint on October 15, 2015 which was transferred to the Commonwealth Court on behalf of itself and all others similarly situated, alleging that Blue Cross of Northeastern Pennsylvania improperly transferred \$90,000 to the AllOne Foundation and AllOne Charities prior to its merger into the Corporation. The Plaintiffs contend that the \$90,000 in donations was to be used solely for the benefit of its policyholders. On January 24, 2017, the Commonwealth Court sustained the Preliminary Objections to such Complaint filed by Blue Cross of Northeastern Pennsylvania and dismissed the Complaint with prejudice. On November 22, 2017, this matter was resolved in favor of the Corporation as the Pennsylvania Supreme Court affirmed the order of the Commonwealth Court.

Factor Health Management LLC ("Factor Health"), filed a complaint on November 6, 2013 against BCBSA, six BCBSA licensees, including the Corporation, and four internal Blue plan fraud investigators. Factor Health alleges that the defendants conspired to drive them out of the specialty pharmacy business, by among other things, delaying and denying payment for Factor Health drugs to treat hemophiliac patients. Specifically, the claims asserted are antitrust under Florida law, tortious interference with an advantageous business relationship, civil conspiracy, conspiracy through abuse of economic power, defamation, and unfair competition. The Plaintiffs have asserted \$100,000 in damages, which they assert may be trebled under applicable antitrust law, as well as attorneys' fees and costs. The Corporation believes, based on consultation with legal counsel, that it has meritorious defenses to the claims in this matter, but it is unable to predict the outcome of the matter or to reasonably estimate a range of possible loss.

On May 11, 2017, Presque Isle Colon and Rectal Surgery, on behalf of all independent physicians and physician practices in Pennsylvania, filed a class action complaint in the United States District Court for the Western District of Pennsylvania against the Corporation and Highmark Health containing antitrust, breach of contract and unjust enrichment claims based on allegations that such physicians were subjected to anticompetitive and other unlawful practices in relation to services rendered to patients covered by an ACA health insurance exchange product. The Corporation believes, based on consultation with legal counsel, that it has meritorious defenses to the claims in this matter, but it is unable to predict the outcome of the matter or to reasonably estimate a range of possible loss.

On January 30, 2017, Charleston Diabetes and Endocrine Consultants, PLLC and Prasuna Jami, M.D. filed an amended class action complaint against the Corporation on behalf of themselves and all providers similarly situated in Wood County (WV) Circuit Court alleging that the Corporation conducted retrospective audits of providers for the period 2013 to 2015 in violation of the West Virginia Prompt Pay Act. By order dated March 3, 2017, the Court granted the plaintiffs' motion to transfer the lawsuit to the Business Court Division. The Corporation believes, based on consultation with legal counsel, that it has meritorious defenses to the claims in this matter, but it is unable to predict the outcome of the matter or to reasonably estimate a range of possible loss.

**Highmark Health**  
**Notes to Consolidated Financial Statements**  
**December 31, 2017 and 2016**

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*(in thousands of dollars)*

Participation in government sponsored health care programs subjects the Corporation to a variety of federal laws and regulations and risks associated with audits conducted under these programs. These audits may occur in years subsequent to the Corporation providing the relevant services under audit. These risks may include reimbursement claims as well as potential fines and penalties. The Corporation believes, based on consultation with legal counsel, adequate provision has been made in the financial statements for any potential liability related to these matters, and the amount of ultimate liability is not expected to materially affect the financial position or results from operations of the Corporation.

The Corporation is subject to various other contingencies, including legal and compliance actions and proceedings that arise in the ordinary course of its business. Due to the complex nature of these actions and proceedings, the timing of the ultimate resolution of these matters is uncertain. In the opinion of management, based on consultation with legal counsel, adequate provision has been made in the financial statements for any potential liability related to these matters, and the amount of ultimate liability is not expected to materially affect the financial position or results from operations of the Corporation.



## Report of Independent Auditors

To the Board of Directors of Highmark Health:

We have audited the consolidated financial statements of Highmark Health as of December 31, 2017 and for the year then ended and our report thereon appears on page one of this document. That audit was conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The consolidating 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 consolidating 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 consolidating information is fairly stated, in all material respects, in relation to the consolidated financial statements taken as a whole. The consolidating information is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position, results of operations and cash flows of the individual companies and is not a required part of the consolidated financial statements. Accordingly, we do not express an opinion on the financial position, results of operations and cash flows of the individual companies.

PRICEWATERHOUSE COOPERS LLP

March 28, 2018

# Highmark Health Consolidating Balance Sheet December 31, 2017

(In thousands of dollars)

	Highmark Health	Highmark Inc.	HM Health Solutions	HM Health Holding Co.	Allegheny Health	Eliminations	Total
<b>Assets</b>							
Cash and cash equivalents	\$ 15,661	\$ 2,057,467	\$ 60,441	\$ 943	\$ 220,017	\$ -	\$ 2,354,529
Accounts receivable	-	2,207,252	-	-	319,422	-	2,207,252
Insurance, less allowance for doubtful accounts of \$38,979	-	-	-	-	52,735	(109,135)	210,287
Patient service, less allowance for doubtful accounts of \$47,176	53,964	193,289	60,022	822	-	(185,772)	175,060
Other	-	-	-	-	-	-	-
Investments	1,595	2,853,875	-	-	69,801	-	2,923,676
Debt securities, available-for-sale at fair value	-	1,181,058	-	-	11,535	-	1,194,188
Equity securities, available-for-sale at fair value	-	-	-	-	-	-	-
Board designated, restricted and other investments at fair value	6,209,636	-	-	-	837,041	-	837,041
Other	-	190,111	3,533	38	40,449	(6,009,636)	434,131
Reinsurance recoverables	-	195,285	-	-	-	-	195,285
Securities lending invested collateral	-	117,023	-	-	-	-	117,023
Inventory, net	-	112,429	-	-	-	-	112,429
Income tax recoverable, net	-	92,871	-	-	59,151	-	152,022
Deferred income taxes, net	-	10,709	7,753	(121)	(120)	-	18,221
Property and equipment, net	-	253,318	8,137	70	(626)	-	260,899
Goodwill and other intangible assets, net	140,540	523,598	3,893	-	1,152,002	-	1,820,033
Prepaid pension plan assets	-	385,087	663	-	114,564	-	500,314
Other assets	-	1,129	-	-	-	-	1,129
	5,326	463,321	7,159	-	136,208	(12,607)	599,507
<b>Total assets</b>	<b>\$ 6,426,722</b>	<b>\$ 10,837,802</b>	<b>\$ 151,601</b>	<b>\$ 1,752</b>	<b>\$ 3,012,179</b>	<b>\$ (6,317,050)</b>	<b>\$ 14,113,006</b>
<b>Liabilities and Net Assets</b>							
Claims outstanding	-	\$ 2,663,932	\$ -	\$ -	\$ -	\$ (92,456)	\$ 2,571,476
Unearned revenue	-	207,821	6,460	-	-	-	214,281
Amounts held for others	-	654,088	-	-	-	-	654,088
Accrued salaries and benefits	51,435	153,239	45,870	1,015	122,945	-	374,504
Other payables and accrued expenses	38,897	813,995	99,580	232	272,500	(172,592)	1,052,612
Securities lending payable	-	112,423	-	-	-	-	112,423
Benefit plan liabilities	-	399,564	-	-	341,676	-	741,240
Debt	-	606,446	12,138	-	1,073,245	(11,750)	1,680,079
Other liabilities	-	20,124	-	-	257,892	(30,617)	247,399
<b>Total liabilities</b>	<b>90,332</b>	<b>5,631,632</b>	<b>164,048</b>	<b>1,247</b>	<b>2,068,258</b>	<b>(307,415)</b>	<b>7,648,102</b>
<b>Net Assets</b>							
Unrestricted - Highmark Health	6,027,996	5,093,799	(12,485)	505	619,371	(5,701,203)	6,027,983
Unrestricted - noncontrolling interest	-	112,371	38	-	16,156	(38)	128,527
<b>Total unrestricted</b>	<b>6,027,996</b>	<b>5,206,170</b>	<b>(12,447)</b>	<b>505</b>	<b>635,527</b>	<b>(5,701,241)</b>	<b>6,156,510</b>
Temporarily restricted	22,810	-	-	-	22,810	(22,810)	22,810
Permanently restricted	285,584	-	-	-	285,584	(285,584)	285,584
<b>Total net assets</b>	<b>6,336,390</b>	<b>5,206,170</b>	<b>(12,447)</b>	<b>505</b>	<b>943,921</b>	<b>(6,009,635)</b>	<b>6,464,904</b>
<b>Total liabilities and net assets</b>	<b>\$ 6,426,722</b>	<b>\$ 10,837,802</b>	<b>\$ 151,601</b>	<b>\$ 1,752</b>	<b>\$ 3,012,179</b>	<b>\$ (6,317,050)</b>	<b>\$ 14,113,006</b>

**Highmark Health**  
**Consolidating Statement of Operations**  
**Year Ended December 31, 2017**

*(in thousands of dollars)*

	Highmark Health	Highmark Inc.	HM Health Solutions	HM Health Holding Co.	Allegheny Health	Eliminations	Total
<b>Unrestricted revenue and other support</b>							
Premium revenue, net	\$ -	\$ 13,139,665	\$ -	\$ -	\$ -	\$ -	\$ 13,139,665
Net patient service revenue	-	-	-	-	2,887,910	(654,096)	2,223,814
Vision revenue	-	1,351,158	-	-	-	-	1,351,158
Service revenue	33,464	1,116,353	806,526	585	179,249	(625,298)	1,510,879
Affiliates revenue	-	30,789	424	-	-	-	31,213
Net assets released from restrictions	-	-	-	-	4,203	-	4,203
Total unrestricted revenue and other support	33,464	15,637,965	806,950	585	3,071,362	(1,289,394)	18,260,932
<b>Operating expenses</b>							
Claims and claim adjustment expenses, net	-	11,461,842	-	-	-	(610,796)	10,851,046
Salaries, wages and fringe benefits	182,296	1,524,858	439,165	5,033	1,647,241	(22,976)	3,775,617
Patient care supplies	-	-	-	-	606,405	-	606,405
Depreciation and amortization	16,771	142,577	1,221	-	141,931	-	302,500
Other operating expenses, net	(139,373)	1,888,330	375,585	(4,991)	645,759	(655,622)	2,109,688
Goodwill impairment	-	277,738	-	-	-	-	277,738
Total operating expenses	59,694	15,295,345	815,971	42	3,041,336	(1,289,394)	17,922,994
Operating (loss) gain	(26,230)	342,620	(9,021)	543	30,026	-	337,938
Net investment income (expense), including net realized gains on investments	63	188,897	263	(10)	58,202	(8,851)	238,564
Interest expense	(2,219)	(36,306)	(341)	-	(39,320)	8,851	(69,335)
Gain on sale of subsidiary and consolidation of affiliate	-	609,465	-	-	-	-	609,465
Equity gains of subsidiaries	1,091,127	-	-	25	-	(1,091,152)	-
Excess (deficit) of revenues over expenses before income taxes	1,062,741	1,104,676	(9,099)	558	48,908	(1,091,152)	1,116,632
Income tax provision (benefit)	-	54,238	(947)	255	(1,961)	-	51,585
Excess (deficit) of revenues over expenses before noncontrolling interest	1,062,741	1,050,438	(8,152)	303	50,869	(1,091,152)	1,065,047
Excess (deficit) of revenue over expenses attributable to noncontrolling interest	-	2,540	25	-	(234)	(25)	2,306
Excess (deficit) of revenue over expenses attributable to Highmark Health	\$ 1,062,741	\$ 1,047,898	\$ (8,177)	\$ 303	\$ 51,103	\$ (1,091,127)	\$ 1,062,741