

Aurora Health Care, Inc. and Affiliates

Consolidated Financial Statements as of and for the Years
Ended December 31, 2016 and 2015, and Independent
Auditors' Report

AURORA HEALTH CARE, INC. AND AFFILIATES

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of

Aurora Health Care, Inc.:

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

Management's Responsibility for the Consolidated Financial Statements

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to Aurora'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 Aurora'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 Aurora Health Care, Inc. and Affiliates as of December 31, 2016 and 2015, and the results of their operations, changes in their net assets, and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

April 7, 2017

AURORA HEALTH CARE, INC. AND AFFILIATES

CONSOLIDATED BALANCE SHEETS

AS OF DECEMBER 31, 2016 AND 2015

(In thousands)

	2016	2015
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 107,664	\$ 176,626
Investments	1,614,843	1,272,107
Assets whose use is limited or restricted	5,484	10,793
Patient accounts receivable — net of allowance for doubtful accounts of \$97,349 and \$96,351 in 2016 and 2015, respectively	731,746	760,058
Other receivables	102,791	81,626
Inventory	70,031	67,572
Prepays and other current assets	48,026	56,728
Estimated third-party payor settlements	9,989	7,494
Total current assets	<u>2,690,574</u>	<u>2,433,004</u>
ASSETS WHOSE USE IS LIMITED OR RESTRICTED:		
Board-designated and other	164,168	153,491
Contractually-restricted	154,267	135,558
Donor restricted	53,821	54,295
Debt service reserve	25,792	32,207
Total assets whose use is limited or restricted	<u>398,048</u>	<u>375,551</u>
PROPERTY, PLANT, AND EQUIPMENT — Net	<u>2,066,286</u>	<u>1,955,988</u>
OTHER ASSETS:		
Intangible assets — net	15,786	16,245
Investments in unconsolidated entities	72,313	73,788
Other	56,835	48,410
Total other assets	<u>144,934</u>	<u>138,443</u>
TOTAL	<u>\$ 5,299,842</u>	<u>\$ 4,902,986</u>

(Continued)

AURORA HEALTH CARE, INC. AND AFFILIATES

CONSOLIDATED BALANCE SHEETS

AS OF DECEMBER 31, 2016 AND 2015

(In thousands)

	2016	2015
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Current installments of long-term debt	\$ 161,936	\$ 136,542
Accounts payable	222,528	228,344
Accrued salaries and wages	259,225	277,070
Other accrued expenses	213,684	203,344
Estimated third-party payor settlements	34,041	22,061
Total current liabilities	<u>891,414</u>	<u>867,361</u>
LONG-TERM DEBT — Less current installments	<u>1,403,091</u>	<u>1,421,061</u>
OTHER LIABILITIES:		
Pension and other employee benefit liabilities	243,574	225,428
Self-insured liabilities	61,592	64,898
Deferred gain	36,662	41,863
Other	61,822	65,191
Total other liabilities	<u>403,650</u>	<u>397,380</u>
Total liabilities	<u>2,698,155</u>	<u>2,685,802</u>
NET ASSETS:		
Unrestricted:		
Controlling interest	2,439,653	2,066,225
Noncontrolling interest in subsidiaries	100,119	88,447
Total unrestricted net assets	<u>2,539,772</u>	<u>2,154,672</u>
Temporarily restricted	43,171	43,779
Permanently restricted	18,744	18,733
Total net assets	<u>2,601,687</u>	<u>2,217,184</u>
TOTAL	<u>\$ 5,299,842</u>	<u>\$ 4,902,986</u>

See accompanying notes to consolidated financial statements.

(Concluded)

AURORA HEALTH CARE, INC. AND AFFILIATES

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN UNRESTRICTED NET ASSETS FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

(In thousands)

	2016	2015
REVENUE:		
Patient service revenue (net of contractual allowances and discounts)	\$ 4,837,262	\$ 4,647,940
Less provision for bad debts	<u>140,151</u>	<u>132,805</u>
Net patient service revenue less provision for bad debts	4,697,111	4,515,135
Other revenue	<u>427,702</u>	<u>414,912</u>
Total revenue	<u>5,124,813</u>	<u>4,930,047</u>
EXPENSES:		
Salaries, wages and fringe benefits	2,805,198	2,564,106
Professional fees	82,707	79,893
Supplies	987,058	929,228
Depreciation and amortization	207,842	198,644
Interest	57,687	57,378
Maintenance and service contracts	119,659	111,637
Building and equipment rental	65,850	71,087
Hospital tax assessment	97,201	94,739
Utilities	48,751	47,118
Purchased services	137,940	123,854
Other expenses	141,582	153,111
Pension settlement loss	—	36,848
Total expenses	<u>4,751,475</u>	<u>4,467,643</u>
OPERATING INCOME	<u>373,338</u>	<u>462,404</u>
NONOPERATING INCOME (LOSS):		
Investment income (loss) — net	95,603	(1,949)
Other nonoperating income (loss) — net	<u>202</u>	<u>(17,725)</u>
Total nonoperating income (loss) — net	<u>95,805</u>	<u>(19,674)</u>
EXCESS OF REVENUE OVER EXPENSES	469,143	442,730
Pension-related changes other than periodic pension cost	(49,680)	25,234
Net assets released from restriction for purchase of property and equipment	3,292	2,643
Distributions to noncontrolling interests	(37,277)	(42,581)
Other - net	<u>(378)</u>	<u>394</u>
INCREASE IN UNRESTRICTED NET ASSETS	<u>\$ 385,100</u>	<u>\$ 428,420</u>

See accompanying notes to consolidated financial statements.

AURORA HEALTH CARE, INC. AND AFFILIATES

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

(In thousands)

	Controlling Interest Unrestricted	Noncontrolling Interest Unrestricted	Total Unrestricted	Temporarily Restricted	Permanently Restricted	Total
NET ASSETS — DECEMBER 31, 2014	\$ 1,639,621	\$ 86,631	\$ 1,726,252	\$ 46,697	\$ 18,472	\$ 1,791,421
Excess of revenue over expenses	398,333	44,397	442,730	—	—	442,730
Pension-related changes other than net periodic pension costs	25,234	—	25,234	—	—	25,234
Change in unrealized gains and losses on investments	—	—	—	(3,181)	—	(3,181)
Contributions	—	—	—	8,356	11	8,367
Investment income	—	—	—	1,034	—	1,034
Net assets released from restrictions for operations	—	—	—	(6,329)	—	(6,329)
Net assets released from restrictions for purchase of property and equipment	2,643	—	2,643	(2,643)	—	—
Distributions to noncontrolling interest	—	(42,581)	(42,581)	—	—	(42,581)
Other — net	394	—	394	(155)	250	489
Increase (decrease) in net assets	426,604	1,816	428,420	(2,918)	261	425,763
NET ASSETS — DECEMBER 31, 2015	2,066,225	88,447	2,154,672	43,779	18,733	2,217,184
Excess of revenue over expenses	420,194	48,949	469,143	—	—	469,143
Pension-related changes other than net periodic pension costs	(49,680)	—	(49,680)	—	—	(49,680)
Contributions	—	—	—	10,453	11	10,464
Investment income	—	—	—	2,685	—	2,685
Net assets released from restrictions for operations	—	—	—	(10,431)	—	(10,431)
Net assets released from restrictions for purchase of property and equipment	3,292	—	3,292	(3,292)	—	—
Distributions to noncontrolling interest	—	(37,277)	(37,277)	—	—	(37,277)
Other — net	(378)	—	(378)	(23)	—	(401)
Increase (decrease) in net assets	373,428	11,672	385,100	(608)	11	384,503
NET ASSETS — DECEMBER 31, 2016	\$ 2,439,653	\$ 100,119	\$ 2,539,772	\$ 43,171	\$ 18,744	\$ 2,601,687

See accompanying notes to consolidated financial statements.

AURORA HEALTH CARE, INC. AND AFFILIATES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015
(In thousands)

	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in net assets	\$ 384,503	\$ 425,763
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Restricted contributions and investment income	—	(90)
Pension-related changes other than net periodic pension cost	49,680	(25,234)
Realized and unrealized (gains) losses on investments, net	(62,374)	43,909
(Gain) loss on disposition of property, plant, and equipment	(1,511)	17,985
Loss on early extinguishment of debt	2,070	543
Impairment of long-lived assets	—	2,448
Amortization of intangible assets and other items	3,955	4,415
Amortization of deferred gains	(5,501)	(5,501)
Depreciation and amortization	207,842	198,644
Provision for bad debts	140,151	132,805
Distribution to noncontrolling interest	39,294	35,313
Increase in accounts receivable	(111,839)	(278,892)
Increase (decrease) in accounts payable and accrued expenses	17,972	(5,931)
Increase in estimated third-party payor settlements — net	9,485	1,482
Decrease in pension and other employee benefit liabilities	(31,534)	(31,780)
(Decrease) increase in self-insured liabilities	(3,306)	964
Other changes in assets and liabilities — net	(18,382)	(41,561)
Net cash provided by operating activities	<u>620,505</u>	<u>475,282</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(346,664)	(296,682)
Proceeds from sale of Marinette surgery center	—	9,900
Proceeds from sales of property, plant, and equipment	2,151	6,728
Investment in unconsolidated entities	(17,171)	(10,060)
Distributions from unconsolidated entities	6,719	6,253
Purchases of investments	(436,517)	(714,008)
Sales of investments	138,969	555,814
Net cash used in investing activities	<u>(652,513)</u>	<u>(442,055)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from long-term debt and financing arrangements	218,000	40,000
Repayments of long-term debt, capital leases, and financing arrangements	(215,660)	(100,150)
Distribution to noncontrolling interest	(39,294)	(35,313)
Restricted contributions and investment income	—	90
Net cash used in financing activities	<u>(36,954)</u>	<u>(95,373)</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	(68,962)	(62,146)
CASH AND CASH EQUIVALENTS:		
Beginning of year	176,626	238,772
End of year	<u>\$ 107,664</u>	<u>\$ 176,626</u>

(Continued)

AURORA HEALTH CARE. INC. AND AFFILIATES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015
(In thousands)

	2016	2015
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid for interest-net of capitalized interest	\$ 59,636	\$ 57,900
Cash paid for income taxes	\$ 1,275	\$ 6,738
SUPPLEMENTAL DISCLOSURES OF NONCASH INFORMATION:		
Capital expenditures funded through accounts payable	\$ 31,293	\$ 22,444
Capital expenditures funded through assumption of long-term debt	\$ 3,410	\$ 3,074

See notes to accompanying consolidated financial statements.

(Concluded)

AURORA HEALTH CARE, INC. AND AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

1. ORGANIZATION AND BASIS OF CONSOLIDATION

Aurora Health Care, Inc. and its affiliates (Aurora) constitute an integrated health care system providing health care services to communities throughout eastern Wisconsin, northern Illinois, and the upper peninsula of Michigan. Aurora provides a variety of health care related activities, education, philanthropic, medical research and other benefits to the communities in which they operate. Health care services include primary and specialty care, pharmacies, behavioral health care, emergency care, rehabilitation, home care, and end-of-life care.

Aurora Health Care, Inc. (the Corporation) is a Wisconsin nonstock, not-for-profit corporation. The Corporation is the parent corporation of a group of nonprofit and for profit corporations and other organizations that own and operate 14 acute-care hospital campuses, one psychiatric hospital, a network of approximately 157 physician clinic facilities, home health services, approximately 75 retail pharmacies, and other health care and related services.

The accompanying consolidated financial statements include the Corporation and its wholly owned or controlled affiliates, as disclosed in Note 18. All intercompany accounts and transactions have been eliminated in the preparation of the consolidated financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates - The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses as of the date and period of the consolidated financial statements. Actual results could differ from those estimates.

Cash and Cash Equivalents - Cash and cash equivalents include highly liquid investments purchased with an original maturity or maturity at the date of purchase of three months or less, except for any cash and money market funds included in assets whose use is limited or restricted.

Investments and Investment Income - Investments in equity securities with readily determinable fair values and all investments in debt securities are reported at fair value based upon quoted market prices in active markets or other observable inputs and are classified as trading securities. Investments in a real estate investment trust and an international equity limited partnership are reported at net asset value (NAV) reported by the fund, which approximates fair value. Certain investments considered available to support current operations are classified as current.

Investment income or loss on funds held for professional liability coverage and certain employee benefit investments is included in other operating revenue. All other investment income or loss (including

realized gains and losses, unrealized gains and losses, interest income, and dividends) is included in nonoperating income (loss), net, unless the income or loss is restricted by donor or law.

Assets Whose Use Is Limited or Restricted - Assets whose use is limited or restricted include investments and other assets set aside by the board of directors at their discretion for future capital improvements or for other purposes, assets held in trust under bond indenture for debt service reserve funds, contractually restricted funds, and donor-restricted funds.

Patient Accounts Receivable - Patient accounts receivable are stated at net realizable value. Patient accounts receivable are reduced by an allowance for contractual adjustments and also by an allowance for doubtful accounts. In evaluating the collectability of patient accounts receivable, Aurora analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for contractual adjustments and allowance for doubtful accounts. Management regularly reviews data about these major payor sources in evaluating the sufficiency of the allowance for contractual adjustments and allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party coverage, Aurora analyzes contractually due amounts and provides an allowance for contractual adjustments, as well as an allowance for doubtful accounts, if necessary. For receivables associated with self-pay patients, Aurora records a significant provision for bad debts and charity care in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates, if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts in the period they are determined to be uncollectible.

Aurora does not maintain a material allowance for doubtful accounts for the amount due from third-party payors and did not have significant write-offs from third-party payors.

Inventories - Medical supplies, durable medical equipment held-for-sale, and other inventories are stated at the lower of cost (primarily first-in, first-out) or market. Retail pharmaceutical inventories are stated at replacement cost.

Property, Plant, and Equipment - Property, plant, and equipment acquisitions are recorded at cost. Donated property, plant, and equipment are recorded at fair value at the date of donation, which is then treated as cost. Costs of computer software developed or obtained for internal use, including external direct costs of materials and services and payroll and payroll-related costs for employees directly associated with internal-use software development projects, are capitalized and included in property, plant, and equipment in the accompanying consolidated balance sheets and included in capital expenditures in the accompanying consolidated statements of cash flows. Interest expense incurred during the period of construction of significant capital projects is capitalized as a component of the cost of the asset.

Property, plant, and equipment assets are depreciated on the straight-line method over the following estimated useful lives:

Buildings	40-45 years
Fixed equipment	20-25 years
Movable equipment	3-15 years
Computer Software	3-10 years

Property, plant, and equipment capitalized under capital leases are recorded at the net present value of future minimum lease payments and are amortized on the straight-line method over the shorter of the related lease term or the estimated useful life of the asset. Amortization of property, plant, and equipment under capital leases is included in the accompanying consolidated statements of operations and changes in unrestricted net assets in depreciation and amortization expense.

Costs incurred for the use of cloud-based software for which Aurora does not own a license are expensed as incurred.

Assets Held for Sale - A long-lived asset or disposal group of assets and liabilities that is expected to be sold within one year is classified as held for sale and depreciation ceases to be recorded. For long-lived assets held for sale, an impairment charge is recorded if the carrying amount of the asset exceeds its fair value less costs to sell. Such valuations include estimates of fair values generally based upon discounted cash flows and incremental direct costs to transact a sale. Aurora has various properties which are actively being marketed for sale and are classified as held for sale in the accompanying consolidated balance sheets in prepaids and other current assets. As of December 2016, the carrying value of these properties was equal to their fair value less cost to sell of \$5.5 million. As of December 31, 2015, the carrying values of properties held for sale were written down to their fair value, less cost to sell, of \$6.1 million, resulting in an impairment adjustment of \$2.4 million, during 2015, which was recorded within other operating expenses in the accompanying consolidated statements of operations and changes in unrestricted net assets.

Pledges Receivable - Unconditional pledges receivable are reported at fair value as contribution revenue at the date the pledge is received. Conditional pledges receivable and indications of intentions to give are reported as contribution revenue and receivables at fair value when the conditions are substantially met. Conditional pledge revenue may be net of allowances where applicable, and is reflected as an increase in temporarily restricted contributions when the conditions are substantially met, and the related receivables are reported as other current or noncurrent assets based on the estimated time of collection.

Deferred Financing Costs and Original Issue Discounts/Premiums on Bond Indebtedness - Long-term debt issuance costs are deferred and amortized over the term of the debt. Long-term debt issuance costs and original issue discounts/premiums on bond indebtedness are amortized using methods that approximate the effective interest rate method over the estimated average period the related bonds will be outstanding. Deferred financing costs and original issue discounts/premiums are recorded as a reduction to or increase in the related debt in the accompanying consolidated balance sheets.

Intangible Assets - Intangible assets are amortized on a straight-line basis over periods ranging from 2 to 15 years. Amortization of intangible assets, other than non-compete agreements, is included in other expense in the accompanying consolidated statements of operations and changes in unrestricted net assets. The amortization of non-compete agreements is included in salaries, wages and fringe benefits expense in the accompanying consolidated statements of operations and changes in unrestricted net assets.

Asset Impairment - Aurora periodically assesses the impairment of long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset or group of assets may not be recoverable. Recoverability of an asset or group of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset, a quoted market price, or prices for similar assets. Management considers such factors as current results, trends, and future prospects, in addition to other economic factors, in determining the impairment of an asset. There were no impairment adjustments recorded in 2016 or 2015 other than the impairment of assets held for sale noted above.

Goodwill is evaluated for impairment annually at November 30, or more frequently if events or changes occur that suggest the carrying value may not be recoverable. If, after assessing events and circumstances, it is concluded that it is more likely than not that the asset is impaired, the fair value is determined and is compared to the carrying value. If the carrying value exceeds the fair value, an impairment charge is recognized.

Investments in Unconsolidated Entities - Investments in unconsolidated entities are accounted for using the cost or equity method. Aurora applies the equity method of accounting for joint ventures and for investments with ownership interests of 50% or less, if Aurora has the ability to exercise significant influence over the operating and financial policies of the investee. All other investees are accounted for using the cost method. The income (loss) on health-related unconsolidated entities is included in other operating revenue. All other income (loss) on unconsolidated entities is included within nonoperating income (loss), net.

Derivative Instrument - Aurora entered into an interest rate swap arrangement to manage its interest costs and achieve other risk management objectives. The swap agreement was not structured to qualify for hedge accounting. Aurora recorded the swap as either an asset or liability at its fair value. The net change in fair value was recorded as a nonoperating gain or loss. The difference between the actual amount paid and the actual amount received on the swap was accrued and recognized as an adjustment to interest expense. The terms of Aurora's swap agreement required Aurora to transfer collateral to the swap counterparty in certain circumstances. The amount of required collateral was determined based upon the estimated underlying market value of the individual bond supporting the swap. Collateral, if required, was reported as a separate asset, rather than as an offset to the fair value of the interest rate swap, and was included in noncurrent assets whose use was limited or restricted in the accompanying consolidated balance sheets. Aurora terminated the swap in August 2016.

Deferred Gain - Aurora has entered into various sale-leaseback transactions. Certain sale-leaseback transactions resulted in deferred gains, which are amortized over the term of the lease, ranging from 10 to 25 years.

Income Taxes - Aurora evaluates its uncertain tax positions on an annual basis. A tax benefit from an uncertain tax position may be recognized when it is more likely than not that the position will be sustained upon examination, including resolutions of any related appeals or litigation processes, based on the technical merits.

Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are classified as non-current in the accompanying consolidated balance sheets.

Aurora assesses the realization of its deferred tax assets to determine whether an income tax valuation allowance is required. Based on all available evidence, both positive and negative, and the weight of that evidence to the extent such evidence can be objectively verified, Aurora determines whether it is more likely than not that all or a portion of the deferred tax assets will be realized.

Restricted Net Assets - Restricted net assets are used to differentiate resources, the use of which is limited by the donor or grantor, from unrestricted net assets on which the donor or grantor places no restriction or which arise as a result of the operations of Aurora. Restricted gifts and other restricted resources are recorded as additions to restricted net assets.

Restricted net assets consist of specific purpose funds, which are temporarily restricted, and endowment funds, which are permanently restricted. Temporarily restricted net assets comprise donations restricted to various specific purposes by donors and investment earnings of temporarily and permanently restricted net assets. Permanently restricted net assets are used to account for the principal amounts of gifts and bequests accepted by Aurora with donor stipulations that the principal remain intact in perpetuity and only the income from investment of the principal be expended.

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 accompanying consolidated statements of operations and changes in unrestricted net assets as either other revenue or as net assets released from restrictions used for the purchase of property and equipment. Unrestricted contributions and donor-restricted contributions for operating purposes whose restrictions are met in the same year as received are reported as other revenue.

Patient Service Revenue (net of contractual allowances and discounts) - Patient service revenue is reported at the net realizable amounts from patients, third-party payors, and others for services rendered. Aurora has agreements with payors that provide for payments at amounts different from established rates. The basis for payment under these agreements includes prospectively determined rates, per diem payments, negotiated discounts from established charges, and retroactive settlements under reimbursement agreements with third-party payors.

Charity Care and Uninsured Care - Aurora provides care to patients who meet certain criteria under its Helping Hands program without charge. Because Aurora does not pursue collection of amounts determined to qualify as charity care under this program, they are not reported as revenue. Aurora also provides care to uninsured patients who do not meet the criteria of the Helping Hands program at amounts less than its established rates.

Provision for Bad Debts - Aurora recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates, if negotiated or provided by policy) at the time services are rendered, prior to assessing the patient's ability to pay. As such, the entire provision for bad debts is presented as a reduction from patient service revenue. On the basis of its historical experience, a significant portion of Aurora's uninsured patients will be unwilling or unable to pay for the services provided. In addition, a portion of Aurora's insured patients will be unwilling or unable to pay the portion of their bill for which they are financially responsible. Aurora records a provision for bad debts related to uninsured patients, and insured patients for the portion of their bill for which they are financially responsible in the period services were provided.

Other Revenue - Other revenue primarily comprises revenues from retail pharmacy sales, which are reported at the estimated net realizable amounts from third-party payors at the time the prescription is filled. Retail pharmacy sales were \$229.6 million and \$211.7 million for the years ended December 31, 2016 and 2015, respectively.

The American Recovery and Reinvestment Act of 2009 (ARRA) provides for Medicare and Medicaid incentive payments to hospitals, physicians, and certain other professionals that implement and achieve meaningful use of certified electronic health record (EHR) technology in ways that demonstrate improved quality, safety, and effectiveness of care. Eligibility for annual Medicare incentive payments is dependent upon providers demonstrating meaningful use of EHR technology in each period over a four-year period. An initial Medicaid incentive payment is available to providers that adopt, implement or upgrade certified EHR technology, but must demonstrate continued meaningful use of EHR technology in subsequent years in order to qualify for additional payments. Hospitals may be eligible for both Medicare and Medicaid EHR incentive payments; however, physicians and other professionals may be eligible for either Medicare or Medicaid incentive payments, but not both. Hospitals that are meaningful users under the Medicare EHR incentive payment program are deemed meaningful users under the Medicaid EHR incentive payment program and do not need to meet additional criteria imposed by a state.

Aurora recognizes Medicare and Medicaid EHR incentive payments in the accompanying consolidated statements of operations and changes in unrestricted net assets when compliance with the specified meaningful use criteria is reasonably assured. Aurora recognized approximately \$7.3 million and \$12.4 million of EHR incentive payments as other revenue for the years ended December 31, 2016 and 2015, respectively. Payments recognized under the program decreased in 2016, as under the terms of the program, Medicare and Medicaid incentive payments decline with each year of participation.

Other Expenses - Other expense primarily consists of taxes, media purchases, insurance, professional education, and banking fees.

Other Nonoperating Income (Loss)-Net - Revenues and expenses from delivering health care services and other activities that are consistent with Aurora's ongoing major or central purposes are reported in operations. Income and losses that arise from transactions that are peripheral or incidental to Aurora's main purpose, such as certain investment income; income and losses attributable to sale of property, plant, and equipment; income or loss attributable to extinguishment of debt; and equity income in non-health related joint ventures, are included in other nonoperating income (loss), net.

Excess of Revenue over Expenses - The performance indicator is the excess of revenue over expenses. Excess of revenue over expenses includes all changes in unrestricted net assets except for permanent transfers of assets to and from affiliates for other than goods and services, contributions of long-lived assets (including assets acquired using contributions, which by donor restriction were to be used for the purpose of acquiring such assets), distributions to noncontrolling interests, and pension-related changes other than net periodic pension costs.

New Accounting Pronouncements - In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers*, which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry specific guidance, and requires significantly expanded disclosures about revenue recognition. The core principal of the revenue model is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. This ASU is effective for Aurora as of January 1, 2019. Management of Aurora is currently in the process of evaluating the impact of this guidance on its consolidated financial position, results of operations and cash flows.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. This ASU introduces a lessee model that brings most leases on the balance sheet. The standard also aligns certain of the underlying principles of the new lessor model with those in ASU No. 2014-09, the new revenue recognition standard. This ASU is effective for Aurora as of January 1, 2019. Management of Aurora is currently in the process of evaluating the impact of this guidance on its consolidated financial position, results of operations and cash flows.

In August 2016, the FASB issued ASU 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*, which is intended to simplify how a not-for-profit presents net assets and other information in the financial statements. Specifically focusing on the complexity and understandability of net asset classifications, deficiencies in information about liquidity and availability of resources, lack of consistency in the type of information provided about expenses and investment return, and misunderstandings about and opportunities to enhance the utility of the statement of cash flows. This ASU will be effective for Aurora as of January 1, 2018. Management of Aurora is currently in the process of evaluating the impact of this guidance on its consolidated financial position, results of operations and cash flows.

In August 2016, the FASB issued ASU 2016-15, *Classification of Certain Cash Receipts and Cash Payments*, which amends guidance in Accounting Standards Codification (ASC) 230 on the classification of certain cash receipts and payments in the statement of cash flows. The primary purpose of the ASU is to reduce the diversity of practice that has resulted from the lack of consistent principles on this topic. This ASU is effective for Aurora beginning January 1, 2018. Management of Aurora is currently in the process of evaluating the impact of this guidance on its cash flows.

In March 2017, the FASB issued ASU 2017-07, *Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. This ASU requires the service cost component of net periodic benefit cost related to defined benefit

pension and postretirement benefit plans to be reported in the same financial statement line as other compensation costs arising from services rendered during the period. The other components of net periodic benefit cost are required to be presented separately from service costs and outside of operating income in the statement of operations. Only the service cost component of net periodic benefit cost will be eligible for capitalization in assets. This ASU is effective for Aurora beginning January 1, 2018. Management of Aurora is currently in the process of evaluating the impact of this guidance on its consolidated financial position, results of operations, and cash flows.

3. COMMUNITY BENEFIT

Aurora provides health care services without charge to patients who meet the criteria of its charity care policy. The amount of charity care provided, determined on the basis of cost, is estimated based on entity-specific cost-to-charge ratios. In addition to charity care, Aurora provides services to Medicaid and other public programs for financially needy patients, for which the payments received are less than the cost of providing services. The unpaid costs attributed to providing services under these programs are considered a community benefit. A summary of these unpaid costs are as follows for the years ended December 31, 2016 and 2015 (in thousands):

	2016	2015
Cost of charity care provided	\$ 47,477	\$ 29,771
Unpaid cost of Medicaid	335,431	320,475
Unpaid cost of other public programs	<u>9,254</u>	<u>9,452</u>
Total cost of uncompensated care	392,162	359,698
Unpaid cost of Medicare	<u>645,988</u>	<u>579,806</u>
Total cost of uncompensated care and unpaid cost of Medicare	<u>\$ 1,038,150</u>	<u>\$ 939,504</u>

In addition, Aurora is also involved in other numerous wide-ranging community benefit activities that include community health education and outreach in the form of free or low-cost clinics, health education, health promotion and wellness programs, such as health screenings and immunizations, and various community projects, transportation services, and support groups.

4. PATIENT SERVICE REVENUE AND PATIENT RECEIVABLES

Aurora has agreements with third-party payors that provide for payments to Aurora at amounts different from its established rates. A summary of the payment arrangements with major third-party payors is as follows:

- *Medicare*-Inpatient acute, most hospital outpatient services, and inpatient rehabilitation services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to patient classification systems that are based on clinical, diagnostic, and other factors. Certain inpatient nonacute and outpatient services, defined capital costs, medical education costs, select drugs, and devices related to Medicare beneficiaries are paid based on cost-reimbursement methodologies. Aurora is reimbursed for cost-reimbursable items at a tentative rate,

with final settlement determined after submission of annual cost reports by Aurora and audits thereof by the Medicare fiscal intermediary.

- *Medicaid*-Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed primarily based upon prospectively determined rates.
- *Other Third-Party Payors*-Services rendered to patients insured by other third-party payors are reimbursed based on a discount from customary charges, prospectively determined rates per discharge, or negotiated fee schedules.

Wisconsin assesses a fee or tax on gross patient service revenue. The revenues from this assessment are used to increase payments made to hospitals for services provided to Medicaid and other medically indigent patients. Aurora’s patient service revenue reflects this increase in payment for services to Medicaid and other medically indigent patients, and hospital tax assessment expense reflects the fees assessed by the State. For the years ended December 31, 2016 and 2015, patient service revenue includes \$116.2 million and \$108.4 million, respectively, related to this program, and expenses include \$97.2 million and \$94.7 million, respectively, of tax assessment fees.

The composition of patient service revenue, net of contractual allowances and discounts (before the provision for bad debts), by payor is as follows for the years ended December 31, 2016 and 2015:

	2016	2015
Managed care and all other	65%	63%
Medicare	26	27
Medicaid	8	8
Self-pay	<u>1</u>	<u>2</u>
	<u>100%</u>	<u>100%</u>

The self-pay revenue above includes only revenue from patients without insurance. The revenue related to amounts due from patients for co-insurance and deductibles is included with the primary insurance coverage.

Laws and regulations governing government and other payment programs are complex and subject to interpretation. As a result, there is a reasonable possibility that recorded estimated third-party settlements could change by a material amount. Changes in estimates relating to prior years decreased patient service revenue by \$10.4 million and increased patient service revenue by \$10.4 million for the years ended December 31, 2016 and 2015, respectively.

Aurora has filed formal appeals relating to the settlement of certain prior-year Medicare cost reports. The outcome of these appeals cannot be determined at this time.

The composition of patient accounts receivable, net of contractual allowances (before the allowance for doubtful accounts) is summarized as follows as of December 31, 2016 and 2015:

	2016	2015
Managed care and all other	51%	50%
Medicare	16	18
Medicaid	4	5
Self-pay	<u>29</u>	<u>27</u>
	100%	100%

The self-pay patient accounts receivable above includes amounts due from patients for co-insurance, deductibles, and amounts due from patients without insurance.

Aurora's allowance for doubtful accounts increased from 11.3% of gross receivable less contractual allowances for December 31, 2015 to 11.7% of gross accounts receivable less contractual allowances at December 31, 2016. The increase in the allowance during 2016 is due to an increase in amounts receivable from patients for co-insurance, deductible and amounts due from patients without insurance.

5. INVESTMENTS AND ASSETS WHOSE USE IS LIMITED OR RESTRICTED

Investments and assets whose use is limited or restricted consist of the following instruments, which were measured at fair value, as of December 31, 2016 and 2015 (in thousands):

	2016	2015
Cash and cash equivalents	\$ 24,995	\$ 26,431
Fixed-income securities:		
U.S. Treasury	94,596	80,456
Corporate bonds and other debt securities	194,651	187,999
Federal agency	97,665	89,889
Fixed income mutual funds	990,518	793,033
Domestic equity securities:		
Large-cap	17,961	16,156
Mid-cap	19,257	11,006
Small-cap	22,106	19,124
Real estate	470	279
Equity mutual funds and exchange-traded funds	384,410	300,598
Real estate investment trust	13,953	12,774
International equity securities	142,192	107,183
International equity limited partnerships	8,497	7,840
Accrued investment income and other	<u>7,104</u>	<u>5,683</u>
Total	<u>\$ 2,018,375</u>	<u>\$ 1,658,451</u>
Assets whose use is limited or restricted:		
Current	\$ 5,484	\$ 10,793
Non-current	398,048	375,551
Short-term investments	<u>1,614,843</u>	<u>1,272,107</u>
Total	<u>\$ 2,018,375</u>	<u>\$ 1,658,451</u>

The current portion of assets whose use is limited or restricted includes the amount of assets available to meet current obligations for claims payments under the professional liability program.

Investment income and losses for the years ended December 31, 2016 and 2015, consisted of the following (in thousands):

	2016	2015
Interest income and dividends	\$ 47,454	\$ 41,179
Net realized gains on securities	2,547	3,442
Changes in unrealized gains (losses) on investments	<u>59,827</u>	<u>(47,351)</u>
Total	<u>\$ 109,828</u>	<u>\$ (2,730)</u>

Investment income and losses for the years ended December 31, 2016 and 2015, were classified in the consolidated statements of operations and changes in unrestricted net assets and consolidated statements of changes in net assets as follows (in thousands):

	2016	2015
Other operating revenue	\$ 11,540	\$ 1,366
Investment income (loss) - net	95,603	(1,949)
Temporarily restricted net assets	<u>2,685</u>	<u>(2,147)</u>
Total	<u>\$ 109,828</u>	<u>\$ (2,730)</u>

6. FAIR VALUE

Financial instruments consist primarily of cash and cash equivalents, accounts receivable, accounts payable, accrued expenses, estimated third-party settlements, and long-term debt. Except for long-term debt, the fair values of these instruments approximate their carrying amounts, due to their short-term maturities, at December 31, 2016 and 2015. The estimated fair value of long-term debt, based on discounted cash flows at estimated current borrowing rates, was \$1,394.0 million and \$1,386.4 million at December 31, 2016 and 2015, respectively, and was categorized as Level 2 within the fair value hierarchy.

The fair values of financial assets and liabilities that are measured by the level of significant input as of December 31, 2016 and 2015 are as follows (in thousands):

	December 31, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Recurring fair value measurements:				
Cash equivalents	\$ 26,006	\$ 22,037	\$ 3,969	\$ —
Fixed-income securities:				
U.S. Treasury	94,596	—	94,596	—
Corporate bonds and other debt securities	194,651	—	194,651	—
Federal agency	97,665	—	97,665	—
Fixed income mutual funds	990,518	990,518	—	—
Domestic equity securities:				
Large-cap	17,961	17,961	—	—
Mid-cap	19,257	19,257	—	—
Small-cap	22,106	22,106	—	—
Real estate	470	470	—	—
Equity mutual funds and exchange-traded funds	384,410	384,410	—	—
International equity securities	142,192	142,192	—	—
Other	7,104	6,853	—	251
Total recurring fair value measurements	\$ 1,996,936	<u>\$ 1,605,804</u>	<u>\$ 390,881</u>	<u>\$ 251</u>
Cash	106,653			
Assets valued at net asset value	<u>22,450</u>			
Total cash and cash equivalents, investments and assets whose use is limited	<u>\$ 2,126,039</u>			
Nonrecurring fair value measurements:				
Long-lived assets held for sale	<u>\$ 5,467</u>	<u>\$ —</u>	<u>\$ 5,467</u>	<u>\$ —</u>
Total nonrecurring fair value measurements	<u>\$ 5,467</u>	<u>\$ —</u>	<u>\$ 5,467</u>	<u>\$ —</u>

	December 31, 2015	Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Recurring fair value measurements:				
Cash equivalents	\$ 27,821	\$ 19,611	\$ 8,211	\$ —
Fixed-income securities:				
U.S. Treasury	80,456	—	80,456	—
Corporate bonds and other debt securities	187,999	—	187,999	—
Federal agency	89,889	—	89,889	—
Fixed income mutual funds	793,033	793,033	—	—
Domestic equity securities:				
Large-cap	16,156	16,156	—	—
Mid-cap	11,006	11,006	—	—
Small-cap	19,124	19,124	—	—
Real estate	279	279	—	—
Equity mutual funds and exchange-traded funds	300,598	300,598	—	—
International equity securities	107,183	107,183	—	—
Other	5,683	5,434	—	249
Total recurring fair value measurements	<u>\$ 1,639,227</u>	<u>\$ 1,272,421</u>	<u>\$ 366,555</u>	<u>\$ 249</u>
Cash	175,236			
Assets valued at net asset value	<u>20,614</u>			
Total cash and cash equivalents, investments and assets whose use is limited	<u>\$ 1,835,077</u>			
Nonrecurring fair value measurements:				
Long-lived asset held for use	\$ 1,985	\$ —	\$ 1,985	\$ —
Long-lived assets held for sale	<u>6,073</u>	<u>—</u>	<u>6,073</u>	<u>—</u>
Total nonrecurring fair value measurements	<u>\$ 8,058</u>	<u>\$ —</u>	<u>\$ 8,058</u>	<u>\$ —</u>
Liabilities				
Recurring fair value measurements:				
Other noncurrent liabilities — interest rate swap agreement	<u>\$ (2,437)</u>	<u>\$ —</u>	<u>\$ (2,437)</u>	<u>\$ —</u>

Aurora categorizes assets and liabilities measured at fair value in the consolidated financial statements based upon whether the inputs used to determine their fair values are observable or unobservable. Observable inputs are inputs which are based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the reporting entity's own assumptions about pricing the asset or liability, based on the best information available under the circumstances.

The fair value of all assets and liabilities recognized or disclosed at fair value are classified based on the lowest level of significant inputs. Assets and liabilities that are measured at fair value are disclosed and classified in one of the three categories. Category inputs are defined as follows:

Level 1 — Quoted prices (unadjusted) in active markets for identical assets or liabilities on the reporting date. Investments in this level generally include exchange-traded equity securities, futures, pooled short-term investment funds, options, and exchange-traded mutual funds.

Level 2 — Inputs other than quoted market prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability. Investments in this level generally include fixed income securities, including fixed income government obligations; asset-backed securities; certificates of deposit; derivatives; as well as certain U.S. and international equities, which are not traded on an active exchange.

Level 3 — Inputs that are unobservable for the asset or liability.

Aurora believes its valuation methods and classification in fair value levels are appropriate and consistent with other market participants based on information readily available from its service providers. Transfers between fair value levels are only done when new or additional information regarding the observability of pricing inputs is received that could result in a different classification as of the reporting date. Aurora measures the transfer between fair value levels as of the end of the reporting period, December 31. There were no significant transfers between fair value levels during the twelve months ended December 31, 2016 or 2015.

The Level 2 and 3 instruments listed in the fair value tables above utilize the following valuation techniques and inputs:

Cash Equivalents — Cash equivalents are comprised primarily of money market funds, which are valued based upon a net asset value of \$1.

Fixed-Income Securities — The fair value of fixed-income securities is primarily determined with techniques consistent with the market approach. Significant observable inputs include benchmark yields, reported trades, observable broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data including market research publications.

Real Estate Investment Trust — The fair value of the real estate investment trust is determined using the calculated net asset value provided by the fund. The fair value of the underlying real estate properties held in the trust is determined giving consideration to the income, cost and sales comparison approaches of estimating property value.

International Equity Securities — The fair value of international equity securities is primarily determined using prices from the non-NASD (National Association of Securities Dealers) over-the-counter markets.

Interest Rate Swap Instrument — The fair value of the interest rate swap instrument was determined using an industry standard valuation model, which is based on a market approach.

Aurora holds interests in a real estate investment trust and an international equity limited partnership where the fair value of the investment held is estimated based on the net asset value of the fund. The following table summarizes the attributes relating to the nature and risk of such investments at December 31, 2016 and 2015 (dollars in thousands):

	Fair Value		Unfunded Commitments	Redemption Frequency	Redemption Notice Period
	December 31, 2016	December 31, 2015			
Real estate investment trust	\$ 13,953	\$ 12,774	\$ —	Quarterly	90 days
International equity limited partnership	8,497	7,840	—	Monthly	15 days
Total	<u>\$ 22,450</u>	<u>\$ 20,614</u>			

The real estate investment trust is a core return, fully specified, open-end commingled equity real estate fund diversified by property type and location designed to provide stable, income-driven rate of return over the long term with potential for growth of net investment income and appreciation of value. The objective of the real estate investment trust is to achieve long term aggregate annual return on invested equity of 8% to 10%, gross of fees, by investing in real estate and real estate-related investments, broadly defined, with the majority of the return being realized from income, with modest appreciation, and using leverage when appropriate.

The fair value of the real estate investment trust is determined using the calculated net asset value provided by the fund. The fair value of the underlying real estate properties held in the trust is determined giving consideration to the income, cost and sales comparison approaches of estimating property value.

The international equity limited partnership's investment objective is long-term total return. The fund pursues its investment objective primarily by investing in equity securities of non-U.S. emerging market companies. The fair value of this fund is determined using the calculated net asset value provided by the fund.

7. PROPERTY, PLANT, AND EQUIPMENT

The components of property, plant, and equipment at December 31, 2016 and 2015, were summarized as follows (in thousands):

	2016	2015
Land and improvements	\$ 109,260	\$ 103,620
Buildings and fixed equipment	2,726,168	2,525,788
Movable equipment	1,107,958	1,014,638
Computer software	65,530	48,513
Construction in progress	<u>109,973</u>	<u>132,387</u>
Total property, plant, and equipment	4,118,889	3,824,946
Accumulated depreciation and amortization	<u>(2,052,603)</u>	<u>(1,868,958)</u>
Property, plant, and equipment-net	<u>\$ 2,066,286</u>	<u>\$ 1,955,988</u>

Property, plant, and equipment includes net assets under capitalized leases and other financing arrangements totaling \$140.9 million (gross of \$277.6 million, accumulated amortization of \$136.7 million) and \$152.0 million (gross of \$281.9 million, accumulated amortization of \$129.9 million) at December 31, 2016 and 2015, respectively.

Construction in progress at December 31, 2016 primarily consisted of costs incurred related to the expansion of Aurora BayCare Medical Center and the Vince Lombardi Cancer Clinic in Green Bay, Wisconsin, construction of a parking structure in West Allis, Wisconsin, and various other hospital and clinic renovation and expansion projects.

Construction in progress at December 31, 2015 primarily consisted of costs incurred related to the construction of an ambulatory surgery center in Burlington, Wisconsin, infrastructure to support a new data center, and various hospital and clinic renovation and expansion projects.

During the year ended December 31, 2015, Aurora completed a comprehensive fixed asset physical inventory and subsequently wrote-off primarily movable equipment having an original cost of \$393.9 million resulting in a loss of \$25.3 million included within other non-operating income (loss) - net. In addition, Aurora also recorded the retirement of fully depreciated property and equipment, having an original cost of \$367.8 million.

8. INTANGIBLE ASSETS

A summary of intangible assets and goodwill is as follows as of December 31, 2016 and 2015 (in thousands):

	2016	2015
Non-compete agreements	\$ 11,961	\$ 11,142
Prescription lists	6,632	6,672
Other	9,075	12,149
	<hr/>	<hr/>
Total intangible assets	27,668	29,963
	<hr/>	<hr/>
Accumulated amortization	(20,428)	(21,403)
	<hr/>	<hr/>
Net intangible assets	7,240	8,560
	<hr/>	<hr/>
Goodwill	8,546	7,685
	<hr/>	<hr/>
Total intangible assets-net	<u>\$ 15,786</u>	<u>\$ 16,245</u>

9. INVESTMENTS IN UNCONSOLIDATED ENTITIES AND NONCONTROLLING INTEREST IN SUBSIDIARIES

In April 2016, Aurora partnered with Anthem Blue Cross and Blue Shield of Wisconsin (Anthem) to form a new, joint venture, Wisconsin Collaborative Insurance Company (WCIC). WCIC is a health insurance company. Aurora acquired a 50% interest in the joint venture for cash consideration of \$5.0 million and accounts for this investment under the equity method of accounting within investments in unconsolidated entities in the accompanying consolidated balance sheets. Aurora's investment in WCIC as of December 31, 2016 was \$1.8 million.

In June of 2015, Aurora acquired a 6.25% interest in StartUp Health Holdings, Inc., ("StartUp Health") for cash consideration of \$5.0 million. StartUp Health is a global health innovation company with more than 100 digital health portfolio companies. Aurora's goal is to help accelerate the review and adoption of innovations aimed at transforming the delivery of care. Aurora's investment in StartUp Health was \$5.0 million as of December 31, 2016 and 2015. Aurora's investment in StartUp Health is accounted for under the equity method of accounting and is presented within investments in unconsolidated entities in the accompanying consolidated balance sheets.

Aurora has a 49% minority interest in Bay Area Medical Center (BAMC), a 99 bed general acute care hospital located in Marinette, Wisconsin. Aurora's investment in BAMC is accounted for under the equity method of accounting and is presented within investments in unconsolidated entities in the accompanying consolidated balance sheets. Aurora's investment in BAMC as of December 31, 2016 and 2015 was \$36.3 million and \$46.4 million, respectively. The carrying amount of Aurora's investment in BAMC is \$33.0 million and \$32.7 million, less than the underlying equity in the net assets of BAMC as of December 31, 2016 and 2015, respectively. This difference represents a contingent gain, which would

be recognized in the event of dissolution of BAMC or if Aurora's interest in BAMC were to change, requiring BAMC to be included in the consolidated financial statements of Aurora.

In August of 2015, Aurora and BAMC combined their medical group practices in Marinette, Wisconsin and its surrounding communities to form Aurora Bay Area Medical Group (ABAMG). ABAMG provides inpatient, outpatient and other necessary professional medical services. Aurora holds a 27% ownership interest in ABAMG based on an initial cash contribution of \$1.8 million. BAMC holds the remaining 73% interest in ABAMG. Aurora's investment in ABAMG is accounted for under the equity method and is presented within investments in unconsolidated entities in the accompanying consolidated balance sheets.

In conjunction with the formation of ABAMG, Aurora sold its surgery center in the Marinette market to BAMC for cash of \$9.9 million and recorded a gain on the sale of assets of \$9.2 million, presented in other non-operating (loss) income in the accompanying consolidated statement of operations and changes in unrestricted net assets for the year ended December 31, 2015. Additionally, as part of this transaction, Aurora leases employees and buildings to ABAMG and recognized \$22.1 million and \$8.2 million of other revenue for the years ended December 31, 2016 and 2015, respectively. Aurora has made additional capital contributions to ABAMG of \$6.0 million during the year ended December 31, 2016. Aurora's investment in ABAMG as of December 31, 2016 and 2015, was \$0.8 million and \$0.7 million, respectively.

Aurora has a 50% investment in the Menomonee Falls Ambulatory Surgery Center, LLC, and a 20% investment in Froedtert Surgery Center, LLC (collectively, the Surgery Centers). The Surgery Centers provide various types of outpatient surgical procedures. Aurora's investment in the Surgery Centers of \$5.7 million and \$5.6 million as of December 31, 2016 and 2015, respectively, is accounted for under the equity method of accounting and is presented within investments in unconsolidated entities in the accompanying consolidated balance sheets. The carrying amount of Aurora's investment in the Surgery Centers is different from the underlying equity in the net assets of the investees due to goodwill recorded upon the initial investment in the Surgery Centers.

The summarized financial position and results of operations for the entities accounted for under the equity method as of and for the year ended December 31, 2016 and 2015, is as follows (in thousands):

	2016				
	Bay Area Medical Center ⁽¹⁾	ABAMG	Surgery Centers	Other Investees	Total
Total assets	\$ 198,957	\$ 6,896	\$ 13,109	\$ 28,800	\$ 247,762
Total liabilities	60,441	4,004	2,143	62,461	129,049
Equity	138,516	2,892	10,966	(33,661)	118,713
Total revenue	86,666	30,958	15,682	73,174	206,480
Net income	(3,902)	(21,928)	1,764	5,978	(18,088)

	2015				
	Bay Area Medical Center ⁽¹⁾	ABAMG	Surgery Centers	Other Investees	Total
Total assets	\$ 228,678	\$ 6,117	\$ 12,456	\$ 24,117	\$ 271,368
Total liabilities	67,305	3,412	2,184	51,509	124,410
Equity	161,373	2,705	10,272	(27,392)	146,958
Total revenue	103,461	9,748	17,422	68,448	199,079
Net income	4,184	(7,795)	3,460	8,981	8,830

⁽¹⁾ ABAMG is included in the consolidated financial results of Bay Area Medical Center.

Aurora Medical Group has a majority interest in BayCare Aurora, LLC (Aurora BayCare), a Wisconsin limited liability company established for the purpose of owning and operating a hospital and other medical care facilities in Green Bay, Wisconsin. Under certain circumstances, the operating agreements of Aurora BayCare may require additional contributions from the members and permit distributions of their equity. Aurora BayCare is included in the accompanying consolidated financial statements. At December 31, 2016 and 2015, the noncontrolling interest in Aurora BayCare totaled \$96.0 million and \$85.2 million, respectively, and was included in noncontrolling interest in subsidiaries' unrestricted net assets. During 2016 and 2015, distributions totaling \$32.5 million and \$38.9 million, respectively, were made to such minority shareholders.

Aurora has a controlling financial interest in three surgery centers. The accounts of the surgery centers are included in the consolidated financial statements. At December 31, 2016 and 2015, the noncontrolling interest in the surgery centers totaled \$4.1 million and \$3.2 million, respectively, and was included in noncontrolling interest in subsidiaries' unrestricted net assets. During 2016 and 2015, distributions totaling \$4.8 million and \$3.7 million, respectively, were made to such minority shareholders.

10. INCOME TAXES

The Corporation and certain of its affiliates are not-for-profit corporations as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and have been recognized as tax exempt on related income pursuant to Section 501(a) of the Code.

Aurora Health Care Ventures, Inc. (Ventures) and its subsidiaries are taxable entities. Ventures is a subsidiary of the Corporation.

Aurora BayCare is treated as a partnership for income tax purposes. Income and losses of Aurora BayCare are passed through to its members. Aurora BayCare income passed through to Aurora is not considered taxable income to Aurora unless it is considered unrelated business income.

Aurora Liability Assurance, Ltd. has elected to be treated as a disregarded entity for income tax purposes.

The provision for income taxes for the years ended December 31, 2016 and 2015, consists of the following (in thousands):

	2016	2015
Current tax expense:		
Federal	\$ 2,228	\$ 3,611
State	332	568
Deferred tax expense	<u>626</u>	<u>3,289</u>
Total tax expense	<u>\$ 3,186</u>	<u>\$ 7,468</u>

Income tax expense is included within other operating expenses in the accompanying consolidated statements of operations and changes in unrestricted net assets.

The following table discloses those significant components of deferred tax assets, including any valuation allowance, at December 31, 2016 and 2015 (in thousands):

	<u>2016</u>	<u>2015</u>
	<u>Assets</u>	<u>Assets</u>
Depreciation and fixed-asset differences	\$ 237	\$ 19
Receivables (doubtful accounts and adjustments)	260	1,959
Accruals for retained insurance risks	342	350
Investments and other assets	1,176	394
Other accrued liabilities	799	817
Benefit plans	6,222	6,341
Net operating loss carryforwards	<u>2,174</u>	<u>2,138</u>
Subtotal deferred tax assets	11,210	12,018
Valuation allowance	<u>(1,080)</u>	<u>(1,080)</u>
Total deferred income taxes	<u>\$ 10,130</u>	<u>\$ 10,938</u>

The valuation allowance of \$1.1 million as of December 31, 2016 and 2015, is primarily attributable to certain federal and state net operating loss carryovers that, more likely than not, will expire unutilized.

At December 31, 2016, federal net operating loss carryforwards totaled \$5.3 million, which expire from 2018 to 2030. At December 31, 2016, state loss carryforwards totaled \$6.3 million, which expire from 2024 to 2031.

There have been no uncertain tax positions recorded in 2016 or 2015.

11. LONG-TERM DEBT

Long-term debt at December 31, 2016 and 2015, is summarized as follows (in thousands):

	2016	2015
Wisconsin Health and Educational Facilities Authority (WHEFA)		
fixed-rate bonds:		
Series 1993 (5.25% weighted average coupon for 2016 and 5.58% for 2015)	\$ —	\$ 81,220
Series 2009A (5.12% weighted average coupon for 2016 and 5.28% for 2015)	22,750	23,650
Series 2009B (3.22% weighted average coupon for 2016 and 2015)	65,000	132,475
Series 2010A (5.43% weighted average coupon for 2016 and 5.42% for 2015)	162,375	166,780
Series 2010B (5.00% weighted average coupon for 2016 and 2015)	61,895	80,640
Series 2012A (4.77% weighted average coupon for 2016 and 4.76% for 2015)	208,120	212,015
Series 2013A (5.19% weighted average coupon for 2016 and 2015)	115,750	115,750
Total fixed-rate bonds	<u>635,890</u>	<u>812,530</u>
WHEFA variable-rate bonds:		
Series 1999C (0.43% effective rate for 2016 and 0.03% for 2015)	\$ 50,000	\$ 50,000
Series 2008A (0.49% effective rate for 2016 and 0.12% for 2015)	80,000	80,000
Series 2008B (0.43% effective rate for 2016 and 0.12% for 2015)	79,470	79,470
Series 2010C (0.36% effective rate for 2016 and 0.11% for 2015)	102,690	102,905
Series 2012B (0.36% effective rate for 2016 and 0.03% for 2015)	37,700	39,350
Series 2012C (0.36% effective rate for 2016 and 0.03% for 2015)	37,700	39,350
Series 2012D (0.41% effective rate for 2016 and 0.04% for 2015)	55,930	58,630
Total variable-rate bonds	<u>443,490</u>	<u>449,705</u>
Unamortized original issue, premium, net	11,786	12,682
Total WHEFA debt	<u>1,091,166</u>	<u>1,274,917</u>
Taxable bonds:		
Series 2015A (0.88% effective rate for 2016 and 0.62% for 2015)	40,000	40,000
Series 2016A (1.97% effective rate for 2016)	125,000	—
Series 2016B (1.99% effective rate for 2016)	93,000	—
Total taxable bonds	<u>258,000</u>	<u>40,000</u>
Capital lease obligations and financing arrangements	220,829	239,646
Term note	—	10,264
Notes payable	5,943	6,573
Deferred financing costs — net	(10,911)	(13,797)
Total long-term debt	<u>1,565,027</u>	<u>1,557,603</u>
Less amounts classified as current:		
Current installments	(79,480)	(69,067)
Long-term debt classified as current due to contractual requirements	(17,456)	—
Long-term rate bonds classified as current	(65,000)	(67,475)
Total amounts classified as current	<u>(161,936)</u>	<u>(136,542)</u>
Long-term debt — net of current portion	<u>\$ 1,403,091</u>	<u>\$ 1,421,061</u>

Under the terms of a Master Trust Indenture (the Aurora Indenture), Aurora's Obligated Group has issued revenue bonds through WHEFA. Aurora's Obligated Group members are defined in Note. 18, *Aurora Health Care, Inc., and Affiliates*. All outstanding debt under the Aurora Indenture represents general, joint, and several obligations of the members of the Obligated Group. Of the total fixed-rate WHEFA bonds, \$47.4 million is collateralized by bond insurance.

On August 15, 2016, Aurora issued \$218.0 million of Series 2016A and 2016B fixed rate taxable bonds which were directly placed with two commercial banks. The proceeds of the 2016A and 2016B Bonds were used to redeem \$81.2 million of the Series 1993 Fixed Rate Revenue Bonds, \$67.5 million of the Series 2009B-2 Fixed Rate Revenue Bonds and pay off the balance on the Term Note of \$9.8 million. The remaining proceeds will be used primarily to fund various capital projects. The financing resulted in a loss on early extinguishment of debt of \$2.0 million, included in nonoperating income (loss), net, in the accompanying consolidated statement of operations and changes in unrestricted net assets.

On April 15, 2015, Aurora redeemed \$40.0 million of Series 2010A Fixed Rate Revenue Bonds with the proceeds of its Aurora Health Care, Inc. Taxable Bonds (the "2015A Bonds"). The 2015A Bonds were a direct placement and bear interest at a taxable, variable rate. The 2015A Bonds are subject to a mandatory tender on April 15, 2018.

The variable-rate demand bonds (VRDBs) are collateralized by \$460.6 million of irrevocable direct-pay letters of credit issued by commercial banks, which provide interim financing to Aurora in the event that remarketing efforts fail for tendered bonds and are drawn upon in the period to pay scheduled debt service on the bonds. The letters of credit expire at various dates through 2019 and have various repayment terms. For \$327.3 million of the letters of credit, principal payments are due quarterly, beginning the earlier of one year from the date of the advance or two months after the expiration date of the letter of credit and amortize over a three-year period, not to exceed three years from the letter of credit's stated expiration date. For the remaining \$133.3 million letters of credit, principal payments are due quarterly, beginning the earlier of one year from the date of the advance or two months after the expiration date of the letter of credit and amortize over a two-year period, not to exceed two years from the letter of credit's stated expiration date. At December 31, 2016 and 2015, no draws were outstanding under the letters of credit.

At December 31, 2016 and 2015, Aurora had outstanding \$65.0 million and \$132.5 million of long-term rate bonds, respectively that have mandatory tenders. The long-term rate bonds bear interest at fixed rates for specified periods, and are subject to mandatory tender at the end of such periods, on the date and in the principal amounts below as of December 31, 2016 and 2015 (dollars in thousands):

December 31,

Series	Principal Amount		Mandatory Tender Date
	2016	2015	
Series 2009B-1	\$ 65,000	\$ 65,000	August 15, 2017
Series 2009B-2	—	67,475	August 15, 2016
Total	<u>\$ 65,000</u>	<u>\$ 132,475</u>	

There is no liquidity facility in effect with respect to the long-term rate bonds to pay the purchase price on the mandatory tender dates. Without a liquidity facility dedicated to these bonds, the bond holder is required to put these bonds to Aurora on the mandatory tender date. At December 31, 2016 and 2015, \$65.0 million and \$67.5 million of the long-term bonds were classified as current due to these requirements, respectively. The remainder of the long-term rate bonds were classified as long-term at December 31, 2015.

At December 31, 2016 and 2015, Aurora is obligated under capital lease and financing arrangements entered into in connection with certain leasing and sale-leaseback transactions. These arrangements, which relate to various administrative and medical support buildings, had initial lease terms of 15 to 25 years. In certain cases, the lease terms for these arrangements include renewal options, purchase options, expansion rights, and rent escalation clauses. The buyer-lessors for such transactions are unrelated special purpose entities. Aurora has excluded the unrelated special purpose entities' assets, liabilities, results of operations, and cash flows from its consolidated financial statements because the residual risks and rewards of the leased assets, as well as the obligations imposed by the underlying debt, reside with the lessors, not Aurora.

The Term Note was collateralized by a mortgage on the orthopedic and sports medicine complex and a pledge of Aurora BayCare's interest in, and proceeds from, certain lease agreements, and required monthly principal and interest payments at LIBOR, plus 1.375%. The Term Note was paid off in 2016.

At December 31, 2016 and 2015, Aurora had a \$60.0 million line of credit with a commercial bank, bearing interest at either the commercial bank floating rate or LIBOR plus 1.00%, based upon the option of Aurora. As of December 31, 2016 and 2015, two letters of credit issued under the line of credit totaling \$38.8 million and \$37.7 million, respectively, were outstanding. There were no outstanding draws on the line of credit or letters of credit as of December 31, 2016 or 2015.

Scheduled maturities on long-term debt (excluding amortization of remaining net unamortized original issue premiums of \$11.8 million and deferred financing costs of \$10.9 million), assuming the remarketing of the long-term rate bonds, capital lease obligations, and financing arrangements, and related sublease rental income, at December 31, 2016, were as follows (in thousands):

	Long-Term Debt	Capital Lease Obligations and Financing Arrangements	Sublease Rental Income
2017	\$ 58,574	\$ 34,370	\$ 5,701
2018	64,998	36,120	3,932
2019	67,346	36,621	1,484
2020	69,989	36,611	1,370
2021	72,287	34,697	357
Thereafter	<u>1,010,129</u>	<u>115,903</u>	<u>293</u>
Total long-term debt	<u>\$ 1,343,323</u>		
Total minimum lease payments and sublease rental income		<u>294,322</u>	<u>\$ 13,137</u>
Less amount representing interest		<u>(73,493)</u>	
Net present value of minimum lease payments for capital lease obligations and financing arrangements		<u>\$ 220,829</u>	

Certain borrowing agreements require sinking fund deposits with a trustee sufficient to pay principal and interest when due. Further, certain of the borrowing agreements contain various covenants regarding maintenance of property, continuation of operations, issuance of additional debt, and maintenance of certain financial ratios and indicators. Aurora was in compliance with all of its financial covenants as of December 31, 2016.

Aurora had a fixed-to-variable interest swap agreement which was terminated in August of 2016 in connection with the redemption of the Series 1993 Bonds. During the term of the Swap Agreement, Aurora paid interest on the underlying bonds at their fixed rate and paid a variable-rate based on the Securities Industry and Financial Markets Association Index (SIFMA) plus a spread calculated on a notional amount. Aurora received net swap payments of \$2.2 million and \$3.9 million during the years ended December 31, 2016 and December 31, 2015. The notional amount was \$81.2 million. These payments were recognized as a reduction of interest expense in the accompanying consolidated financial statements. At December 31, 2015, the fair value of the Swap Agreement was a liability of \$2.4 million, which was included in other noncurrent liabilities in the consolidated balance sheets.

12. EMPLOYEES' BENEFIT PLANS

Aurora has a defined benefit pension plan (the Pension Plan) covering substantially all of its employees hired before January 1, 2013, with at least 1,000 hours of work in a calendar year. The Pension Plan was frozen on December 31, 2012. Benefits are based on years of service and the employees' final average

earnings, as defined. Aurora funds the Pension Plan based on the amount calculated by the Pension Plan's actuaries to meet the minimum Employee Retirement Income Security Act (ERISA) funding requirements. The Pension Plan assets and obligations are measured at December 31. Employer contributions were \$50.0 million and \$72.3 million during 2016 and 2015, respectively. The actuarial cost method used to compute Pension Plan liabilities and expenses is the projected unit credit method.

During 2015, an option was provided to all terminated, vested participants of the Pension Plan to receive a lump sum settlement. Certain participants elected this option which was measured and paid on December 1, 2015. This settlement resulted in a settlement loss of \$36.8 million for the year ended December 31, 2015.

A summary of the changes in the projected benefit obligation, fair value of plan assets and funded status of the Pension Plan as of December 31, 2016 and 2015, is as follows (in thousands):

	2016	2015
Accumulated benefit obligation	<u>\$ 1,473,113</u>	<u>\$ 1,367,641</u>
Change in projected benefit obligation:		
Projected benefit obligation at beginning of measurement period	\$ 1,367,641	\$ 1,587,063
Interest cost	63,291	67,282
Plan amendments	111	—
Net actuarial loss (gain)	88,151	(116,287)
Benefits paid	(46,081)	(41,133)
Settlement paid	<u>—</u>	<u>(129,284)</u>
Projected benefit obligation at end of year	<u>1,473,113</u>	<u>1,367,641</u>
Change in plan assets:		
Fair value of plan assets at beginning of measurement period	1,249,653	1,404,316
Actual income (loss) on plan assets	102,513	(56,546)
Employer contributions	50,000	72,300
Benefits paid	(46,081)	(41,133)
Settlement paid	<u>—</u>	<u>(129,284)</u>
Fair value of plan assets at end of year	<u>1,356,085</u>	<u>1,249,653</u>
Unfunded status at end of year	<u>\$ (117,028)</u>	<u>\$ (117,988)</u>
Net periodic pension (income) cost is composed of the following:		
Interest cost on projected benefit obligation	\$ 63,291	\$ 67,281
Expected return on plan assets	(70,098)	(81,321)
Net amortization and deferral	6,166	9,966
Settlement loss	<u>—</u>	<u>36,848</u>
Net periodic pension (income) cost	<u>\$ (641)</u>	<u>\$ 32,774</u>

The unfunded status of the Pension Plan is recorded in the accompanying consolidated balance sheets in non-current pension and other employee benefit liabilities.

The net actuarial loss not yet recognized as a component of net periodic pension cost was \$443.7 million and \$394.1 million as of December 31, 2016 and 2015, respectively and is included in unrestricted net assets in the accompanying consolidated balance sheets.

The net actuarial gain or loss recognized as a component of pension-related changes other than net periodic pension cost was a loss of \$49.7 million for the year ended December 31, 2016, and a gain of \$25.2 million for the year ended December 31, 2015. The expected amortization amount to be included in the net periodic pension cost in 2017 is a net actuarial loss of \$8.2 million.

Assumptions used to determine the benefit obligation at the measurement date and the net periodic pension cost as of December 31, 2016 and 2015, were as follows:

	2016	2015
Discount rate-pension expense	4.70%	4.32%
Discount rate-projected benefit obligation	4.42	4.70
Expected long-term rate of return on assets-pension expense	5.50	5.50

The discount rate used by Aurora is based on a hypothetical portfolio of high-quality bonds with cash flows matching the Pension Plan's expected benefit payments.

The expected long-term rate of return is based on the asset allocation of the total portfolio considering capital return assumptions from various sources. Aurora's investment objective is to achieve its targeted long-term rate of return while avoiding excessive risk. Risk is effectively managed through diversifying the asset allocation across a broad spectrum of assets including domestic and international equities and fixed income securities with varying correlations to movements in interest rates along the yield curve. These investments are readily marketable and can be sold to fund benefit payment obligations as they become payable. Overall funded status risk of the Pension Plan is managed by matching the duration of plan assets to plan liabilities to mitigate the impact of changes in interest rates on funded status.

The fair market value of the Pension Plan assets at December 31, 2016 and 2015, is as follows (in thousands):

	December 31, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	\$ 28,838	\$ —	\$ 28,838	\$ —
Fixed-income securities:				
U.S. Treasury	139,500	—	139,500	—
Corporate bonds and other debt securities	596,518	—	596,518	—
Federal agency	1,434	—	1,434	—
Fixed-income mutual funds	53,520	53,520	—	—
Domestic equity securities:				
Large-cap	51,224	51,224	—	—
Mid-cap	31,184	31,184	—	—
Small-cap	63,972	63,972	—	—
Real estate	8,833	8,833	—	—
Equity mutual funds and exchange traded funds	137,349	137,349	—	—
International equity securities	127,374	127,374	—	—
Total recurring fair value measurements	<u>1,239,746</u>	<u>\$ 473,456</u>	<u>\$ 766,290</u>	<u>\$ —</u>
Assets valued at net asset value	<u>117,704</u>			
Total Pension Plan Assets	<u>\$ 1,357,450</u>			

	December 31, 2015	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservabl Inputs (Level 3)
Cash and cash equivalents	\$ 19,423	\$ 2,232	\$ 17,191	\$ —
Fixed-income securities:				
U.S. Treasury	153,072	—	153,072	—
Corporate bonds and other debt securities	559,589	—	559,589	—
Federal agency	1,361	—	1,361	—
Fixed-income mutual funds	48,842	48,842	—	—
Domestic equity securities:				
Large-cap	48,376	48,376	—	—
Mid-cap	26,931	26,931	—	—
Small-cap	49,949	49,949	—	—
Real estate	11,670	11,670	—	—
Equity mutual funds and exchange traded funds	120,146	120,146	—	—
International equity securities	118,065	118,065	—	—
Total recurring fair value measurements	<u>1,157,424</u>	<u>\$ 426,211</u>	<u>\$ 731,213</u>	<u>\$ —</u>
Assets valued at net asset value	<u>93,448</u>			
Total Pension Plan Assets	<u>\$ 1,250,872</u>			

There were no significant transfers between fair value levels during 2016 or 2015.

The Pension Plan holds shares or interests in investment funds where the fair value of the investment held is estimated based on the net asset value of the investment funds. The following table summarizes the attributes relating to the nature and risk of these investments at December 31, 2016 and 2015 (in thousands):

	Fair Value December 31, 2016	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Real estate investment trust	\$ 34,176	\$ —	Quarterly	90 Days
Commingled funds	44,351	—	Daily	0 Days
International equity limited partnership	39,177	—	Monthly	15 Days
Total	<u>\$ 117,704</u>			

	Fair Value				
	December 31,		Unfunded	Redemption	Redemption
	2015		Commitments	Frequency	Notice Period
Real estate investment trust	\$ 21,509	\$	10,000	Quarterly	90 Days
Commingled funds	40,215		—	Daily	0 Days
International equity limited partnership	31,724		—	Monthly	15 Days
Total	<u>\$ 93,448</u>				

The real estate investment trust is a core return, fully specified, open-end commingled equity real estate fund diversified by property type and location designed to provide stable, income-driven rate of return over the long term with potential for growth of net investment income and appreciation of value. The objective of the real estate investment trust is to achieve long term aggregate annual return on invested equity of 8% to 10%, gross of fees, by investing in real estate and real estate-related investments, broadly defined, with the majority of the return being realized from income, with modest appreciation, and using leverage when appropriate.

The commingled funds include investments held with two separate funds. The objectives of one of the commingled funds is to maximize total return and outperform the Barclays U.S. Long Government/Credit index, gross of fees, over a market cycle, while maintaining total return risk similar to that of the benchmark. This fund primarily invests in corporate bonds, U.S. Treasury obligations and other U.S. government and agency securities, debt securities of foreign governments and supranational organizations, municipal obligations, and asset-backed, mortgage related and mortgage backed securities. The objectives of the other commingled fund is to maximize the total return and outperform the Barclays Long Credit Index, while maintaining total return risk similar to that of the benchmark over a market cycle. This fund invests primarily in investment grade fixed income securities.

The international equity limited partnership's investment objective is long-term total return. The fund pursues its investment objective primarily by investing in equity securities of non-U.S. emerging market companies. The fair value of this fund is determined using the calculated net asset value provided by the fund.

A reconciliation of the fair value of Pension Plan assets, as presented above, to the fair value of plan assets utilized in determining the unfunded status of the Pension Plan as of December 31, 2016 and 2015, is as follows (in thousands):

	2016	2015
Fair value of plan assets	\$ 1,357,450	\$ 1,250,872
Payable for pending trades-net	<u>(1,365)</u>	<u>(1,219)</u>
Fair value of plan assets at end of measurement period	<u>\$ 1,356,085</u>	<u>\$ 1,249,653</u>

The asset allocation of Aurora's Pension Plan assets at December 31, 2016 and 2015, is as follows:

	2016		2015	
	Strategic Target	Actual	Strategic Target	Actual
Equity securities	33%	33%	33%	32%
Fixed-income securities	64	62	64	65
Real estate	3	3	3	3
Cash and cash equivalents	—	2	—	—
Total	100%	100%	100%	100%

Aurora expects to make the following contributions to and estimated benefit payments from its Pension Plan (in thousands):

Expected contributions in 2017	\$ —
Estimated benefit payments:	
2017	\$ 55,426
2018	62,134
2019	66,453
2020	70,197
2021	73,485
2022 through 2025	405,412
Total	\$ 733,107

Aurora and certain affiliates sponsor defined contribution and retirement savings plans (the Defined Contribution Plans), whereby Aurora contributes a percentage of participants' qualifying compensation up to certain limits as outlined in the Defined Contribution Plans or other amounts as designated by the affiliates' board of directors. Included in salaries, wages and fringe benefits expense in the accompanying consolidated statements of operations and changes in unrestricted net assets for the years ended December 31, 2016 and 2015, is \$144.9 million and \$136.9 million, respectively, for contributions to the Defined Contribution Plans.

Aurora also sponsors a noncontributory Section 457(b) defined contribution plan (the 457(b) Plan) covering select employees, where participants may contribute a percentage of qualifying compensation up to certain limits as defined by the 457(b) Plan. The 457(b) Plan assets and liabilities, each totaling \$102.6 million and \$84.6 million at December 31, 2016 and 2015, respectively, are included in long-term assets whose use is limited or restricted and pension and other employee benefit liabilities, in the accompanying consolidated balance sheets. The assets of this 457(b) Plan are subject to the claims of the general creditors of Aurora. Net investment income from the 457(b) Plan was \$8.7 million for the year ended December 31, 2016, net investment loss from the 457(b) Plan was \$1.3 million for the year ended December 31, 2015. Net investment income (loss) from the 457(b) Plan is included in other operating

revenue with an equal offsetting expense in salaries, wages and fringe benefits in the accompanying consolidated statements of operations and changes in unrestricted net assets.

13. SELF-FUNDED HEALTH, DENTAL, AND OTHER BENEFITS

Aurora sponsors self-funded health and dental insurance plans covering substantially all of their employees and their dependents. Health and dental insurance expense under the plans is based upon actual claims paid, administration fees, and provisions for unpaid and unreported claims at year-end. At December 31, 2016 and 2015, the estimated liability for unpaid and unreported claims of \$10.6 million and \$8.2 million, respectively, were included in accrued liabilities. Costs of Aurora's self-funded health and dental insurance program of \$31.7 million and \$21.8 million for the years ended December 31, 2016 and 2015, respectively, for services provided by non-affiliated providers were included in salaries, wages and fringe benefits expense.

Aurora also provides salary continuation payments to current and inactive employees who are eligible to receive long-term disability and workers' compensation, under self-funded arrangements. Aurora measures the cost of its unfunded obligations under such programs based upon actuarial calculations and records a liability on a discounted basis. At December 31, 2016 and 2015, Aurora had accrued estimated benefit obligations of \$9.2 million and \$11.0 million, respectively, included in accrued liabilities, and \$27.4 million and \$28.5 million, respectively, included in self-insured liabilities.

14. TEMPORARILY AND PERMANENTLY RESTRICTED NET ASSETS

Temporarily and permanently restricted net assets were available for the following purposes at December 31, 2016 and 2015 (in thousands):

	<u>Temporarily Restricted</u>		<u>Permanently Restricted</u>	
	<u>2016</u>	<u>2015</u>	<u>2016</u>	<u>2015</u>
Health education	\$ 7,467	\$ 7,485	\$ 10,082	\$ 10,076
Specific program services	24,494	23,751	6,941	6,937
Research	9,115	10,382	1,507	1,506
Purchase of building and equipment	1,209	1,346	—	—
Indigent care	<u>886</u>	<u>815</u>	<u>214</u>	<u>214</u>
Total restricted net assets	<u>\$ 43,171</u>	<u>\$ 43,779</u>	<u>\$ 18,744</u>	<u>\$ 18,733</u>

At December 31, 2016 and 2015, permanently restricted net assets represent the principal amount of gifts that are to be held in perpetuity. Investment income on the related assets is expendable to support health care and other services and is reported as temporarily restricted investment income.

Aurora's endowment consists of 48 individual funds, including donor-restricted endowment funds. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The Foundation Board has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit stipulations to the contrary. As a result of this interpretation, Aurora classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulation to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by Aurora. Aurora considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the fund, (2) the purposes of the organization and the donor-restricted endowment fund, (3) general economic conditions, (4) the possible effect of inflation and deflation, (5) the expected total return from income and the appreciation of investments, (6) other resources of Aurora, and (7) the investment policies of Aurora.

Aurora has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment, while seeking to maintain the purchasing power of the endowment assets. Aurora's investment objective is to achieve its targeted long-term rate of return while avoiding excessive risk. Risk is effectively managed through diversification, which is achieved by employing various investment managers and mutual funds to direct investments over a broad spectrum of assets, including equities and fixed-income securities.

Aurora has a spending policy that at least 5% of the funds available for expenditure held by the Foundation at the beginning of the fiscal year will be expended on an annual basis. The amount available for expenditure would exclude the corpus of permanently restricted and term donor-restricted endowment funds.

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires Aurora to retain as a fund of perpetual duration. There were no such deficiencies as of December 31, 2016 and 2015.

Information regarding the composition of the endowment investments and activity as of and for the years ended December 31, 2016 and 2015, is as follows (in thousands):

	Donor- Restricted Temporarily Restricted	Permanently Restricted	Total
Endowment net assets-December 31, 2014	\$ 10,809	\$ 18,472	\$ 29,281
Investment return:			
Investment income	906	—	906
Net change in unrealized gains	(87)	—	(87)
Total investment return	819	—	819
Contributions	—	11	11
Appropriation endowment assets for expenditure	(1,220)	—	(1,220)
Other changes-transfers between funds	(173)	250	77
Endowment net assets-December 31, 2015	10,235	18,733	28,968
Investment return:			
Investment income	736	—	736
Net change in unrealized gains	53	—	53
Total investment return	789	—	789
Contributions	10	11	21
Appropriation endowment assets for expenditure	(1,825)	—	(1,825)
Endowment net assets-December 31, 2016	<u>\$ 9,209</u>	<u>\$ 18,744</u>	<u>\$ 27,953</u>

15. FUNCTIONAL EXPENSES

Aurora provides health care services to residents within its geographic areas. Expenses related to providing these services for the years ended December 31, 2016 and 2015, are as follows (in thousands):

	2016	2015
Health care services	\$ 4,006,594	\$ 3,764,563
General and administrative	<u>744,881</u>	<u>703,080</u>
Total	<u>\$ 4,751,475</u>	<u>\$ 4,467,643</u>

General and administrative expenses primarily include information technology, legal, finance, purchasing, patient billing, and human resources.

16. COMMITMENTS AND CONTINGENCIES

Operating Lease Agreements - Aurora has various noncancelable operating lease agreements, primarily for medical support buildings and equipment, which have remaining fixed terms ranging from one to

15 years at December 31, 2016. Some leases contain renewal options, fair value purchase options, and escalation clauses. Aurora subleases certain of its medical support buildings.

Net future minimum lease payments under non-cancelable operating leases with initial or remaining lease terms in excess of one year at December 31, 2016, are as follows (in thousands):

	Lease Payments	Sublease Income	Net Future Minimum Lease Payments
2017	\$ 57,985	\$ (615)	\$ 57,370
2018	54,268	(208)	54,060
2019	53,301	(112)	53,189
2020	49,911	(75)	49,836
2021	46,823	(76)	46,747
Thereafter	124,334	(78)	124,256
	<u>\$ 386,622</u>	<u>\$ (1,164)</u>	<u>\$ 385,458</u>
Total	<u>\$ 386,622</u>	<u>\$ (1,164)</u>	<u>\$ 385,458</u>

Aurora West Allis Medical Center has the right to operate the hospital under the terms of a lease agreement with the City of West Allis (the City). In accordance with the lease agreement, the City has title to all assets and any subsequent additions (with the exception of certain equipment used by Aurora for laboratory services). Aurora West Allis Medical Center has exclusive right to the use of the assets and the obligation to maintain and replace them. The historical cost to Aurora of the leased facilities is included with Aurora's property, plant, and equipment. The agreement provides for annual payments of \$0.4 million in lieu of annual lease payments, and which includes payment escalations each subsequent year. The lease expires in 2063.

Litigation - Aurora is subject to various regulatory investigations, legal proceedings, and claims which are incidental to its normal business activities.

Aurora believes it has made adequate provision for potential exposures relating to its legal matters. In the opinion of management, the amount of ultimate liability with respect to these actions will not materially affect the consolidated results of operations or net assets of Aurora.

Vendor Arrangements - Aurora has a long-term agreement with a vendor for the licenses and maintenance associated with a computerized patient record system. Under the terms of the arrangements,

Aurora will pay a combination of licensing and maintenance fees in exchange for a perpetual license to use such software. Estimated payments in 2017 under the agreement are \$2.2 million.

Aurora routinely enters into long-term arrangements covering volume purchases of medical supplies and equipment. Certain of the agreements, which are generally cancelable without penalty, require Aurora to meet targeted levels of expenditures in order to maintain favorable pricing terms.

Insurance Coverage - Aurora is commercially insured for workers' compensation stop-loss, auto, property, boiler and machinery, umbrella/excess liability, directors' and officers' liability, and other customary business liabilities.

17. GENERAL AND PROFESSIONAL LIABILITY INSURANCE

Commercial insurance companies have issued policies covering Aurora's primary professional, general and managed care errors and omission liability risks. Aurora's professional and general liability insurance is on an occurrence basis, while managed care errors and omissions liability risks are written on a claims-made basis.

Aurora's hospitals, clinics, surgery centers, physicians, and certified registered nurse anesthetist providers that provide health care in Wisconsin are qualified health care providers as defined by Wisconsin state statute, and have separate professional liability limits of \$1.0 million per claim and \$3.0 million annual aggregate applied to each qualified provider. Losses in excess of these amounts are fully covered through mandatory participation in the State of Wisconsin Injured Patients and Families Compensation Fund (the Fund).

Aurora also has professional liability coverage for its providers and affiliates that do not qualify for the Fund coverage, as well as general liability for all of its entities. These coverages provide a number of shared professional liability limits and shared general liability limits totaling \$2.0 million per occurrence and \$4.0 million annual aggregate for most providers. Losses in excess of these amounts are covered by Aurora's umbrella/excess insurance.

The professional, general and managed care liabilities discussed above have been ceded back to Aurora Liability Assurance, Ltd. (ALA), a wholly-owned subsidiary of Aurora, through reinsurance agreements. Independent actuaries evaluate the required provision for outstanding losses related to these risks. At December 31, 2016 and 2015, Aurora has recorded a liability for outstanding losses, including incurred but not reported, discounted at 4.0% totaling \$35.2 million and \$37.9 million, respectively. Of this amount, a portion of the liability for outstanding losses was included in accrued expenses and a portion was included in self-insured liabilities in the accompanying consolidated balance sheets. In the opinion of management, the ultimate disposition of claims incurred to date will not have a material adverse effect on Aurora's consolidated financial position or results of operations. ALA maintains a reinsurance trust account, which in total represents security required by the reinsurance agreement between ALA and the insurance companies. At December 31, 2016 and 2015, assets held in the trust account were \$53.8 million and \$54.1 million, respectively.

18. AURORA HEALTH CARE, INC., AND AFFILIATES

Following is a list of corporations and subsidiaries that are included in the accompanying consolidated financial statements. The Obligated Group Members are denoted by an asterisk (*).

- Aurora Health Care, Inc.*
- Aurora Health Care Metro, Inc.* (d/b/a Aurora St. Luke's Medical Center, Aurora St. Luke's South Shore and Aurora Sinai Medical Center)
- West Allis Memorial Hospital, Inc. (d/b/a Aurora West Allis Medical Center)
- Aurora Medical Center of Washington County, Inc.* (d/b/a Aurora Medical Center Washington County)
- Aurora Medical Center Grafton, LLC* (d/b/a Aurora Medical Center Grafton)
- BayCare Aurora, LLC (d/b/a Aurora BayCare Medical Center)
- Aurora Health Care North, Inc.* (d/b/a Aurora Medical Center Manitowoc County)
- Aurora Health Care Central, Inc.* (d/b/a Aurora Sheboygan Memorial Medical Center)
- Aurora Medical Center of Oshkosh, Inc.* (d/b/a Aurora Medical Center Oshkosh)
- Aurora Health Care Southern Lakes, Inc.* (d/b/a Aurora Lakeland Medical Center, Aurora Memorial Hospital of Burlington, Aurora Medical Center Kenosha, and Aurora Medical Center Summit)
- Aurora Psychiatric Hospital, Inc. (d/b/a Aurora Psychiatric Hospital)
- Kradwell School, Inc.
- Aurora Medical Group, Inc.*
- Midwest Area Physicians, LLC
- AMG Illinois, Ltd.
- Aurora Quick Care, LLC
- Aurora Advanced Healthcare, Inc.
- Visiting Nurse Association of Wisconsin, Inc. (d/b/a Aurora At Home)
- Aurora UW Academic Medical Group, Inc.
- Aurora Family Service, Inc.
- Aurora Health Care Ventures, Inc.
- Lakeshore Medical Clinic, LLC
- Aurora Pharmacy, Inc.
- Diversified Care, Inc.
- Aurora Retail Stores, Inc.
- Advanced Healthcare, Inc.
- East Mequon Surgery Center, LLC
- North Shore Surgical Center
- Aurora Consolidated Laboratories, a Co-Tenancy
- Aurora Research Institute, LLC
- Aurora Health Network, Inc.
- Aurora Accountable Care Organization, LLC
- Aurora Health Care Foundation, Inc.
- Aurora Health Foundation, Inc.
- Vince Lombardi Cancer Foundation, Inc.
- Aurora Liability Assurance, Ltd. (Cayman Island corporation)
- Health Care Re, Ltd. (Cayman Island corporation)
- LMC, Inc.

- Wisconsin Surgery Center, LLC
- The Surgery Center, LLC
- Aurora Surgery Centers, LLC

19. SUBSEQUENT EVENTS

Aurora evaluated events and transactions subsequent to December 31, 2016 through April 7, 2017, the date of financial statement issuance. During this period, there were no subsequent events requiring recognition in or disclosure to the consolidated statements.