TRINITY HEALTH

UNAUDITED QUARTERLY REPORT

For the three months ended September 30, 2014 and 2013

TRINITY HEALTH

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TRINITY HEALTH
CONSOLIDATED BALANCE SHEETS (UNAUDITED)
(In Thousands)

	As of	
ASSETS	**September 30, 2014**	**June 30, 2014**
CURRENT ASSETS:		
Cash and cash equivalents	$ 699,234	$ 901,282
Investments	3,368,204	3,231,318
Security lending collateral	198,355	187,882
Assets limited or restricted as to use - current portion	253,564	274,202
Patient accounts receivable - net of allowance for doubtful accounts of $555.8 million and $545.3 million at September 30, 2014 and June 30, 2014, respectively	1,546,691	1,475,579
Estimated receivables from third-party payors	160,495	155,527
Other receivables	262,296	269,110
Inventories	216,388	206,226
Assets held for sale	202,948	207,989
Prepaid expenses and other current assets	177,593	140,359
Total current assets	7,085,768	7,049,474
ASSETS LIMITED OR RESTRICTED AS TO USE - Noncurrent Portion:		
Held by trustees under bond indenture agreements	52,091	53,652
Self-insurance, benefit plans and other	773,804	672,537
By Board	2,844,107	2,891,790
By donors	310,846	308,572
Total assets limited or restricted as to use - noncurrent portion	3,980,848	3,926,551
PROPERTY AND EQUIPMENT - NET	6,582,396	6,592,913
INVESTMENTS IN UNCONSOLIDATED AFFILIATES	2,281,537	2,257,555
GOODWILL	288,619	153,773
OTHER ASSETS	459,478	452,923
TOTAL ASSETS	$ 20,678,646	$ 20,433,189

(Continued)

The accompanying notes are an integral part of the consolidated financial statements.

LIABILITIES AND NET ASSETS

	As of September 30, 2014	As of June 30, 2014
CURRENT LIABILITIES:		
Commercial paper	$ 239,979	$ 239,961
Short-term borrowings	1,123,620	1,123,620
Current portion of long-term debt	97,978	96,038
Accounts payable	617,721	685,748
Accrued expenses	259,390	275,960
Salary, wages, and related liabilities	670,070	656,467
Current portion of self-insurance reserves	197,005	197,040
Payable under security lending agreements	198,355	187,882
Liabilities held for sale	266,136	257,991
Estimated payables to third-party payors	350,131	323,546
Total current liabilities	4,020,385	4,044,253
LONG-TERM DEBT - Net of Current Portion	3,637,539	3,619,237
SELF-INSURANCE RESERVES - Net of Current Portion	970,048	920,799
ACCRUED PENSION AND RETIREE HEALTH COSTS	703,562	727,873
OTHER LONG-TERM LIABILITIES	579,872	577,565
Total liabilities	9,911,406	9,889,727
NET ASSETS:		
Unrestricted net assets	10,243,059	10,125,003
Noncontrolling ownership interest in subsidiaries	142,298	38,090
Total unrestricted net assets	10,385,357	10,163,093
Temporarily restricted net assets	295,055	293,306
Permanently restricted net assets	86,828	87,063
Total net assets	10,767,240	10,543,462
TOTAL LIABILITIES AND NET ASSETS	$ 20,678,646	$ 20,433,189

The accompanying notes are an integral part of the consolidated financial statements. (Concluded)

TRINITY HEALTH
CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS (UNAUDITED)
(In Thousands)

	Three Months Ended	
	September 30, 2014	**September 30, 2013**
UNRESTRICTED REVENUE:		
Patient service revenue - net of contractual and other allowances	$ 3,195,256	$ 3,065,356
Provision for bad debts	(152,655)	(181,851)
Net patient service revenue less provision for bad debts	3,042,601	2,883,505
Capitation and premium revenue	199,670	148,485
Net assets released from restrictions	3,729	4,803
Other revenue	252,474	254,531
Total unrestricted revenue	3,498,474	3,291,324
EXPENSES:		
Salaries and wages	1,508,116	1,440,530
Employee benefits	301,952	295,438
Contract labor	25,293	22,110
Total labor expenses	1,835,361	1,758,078
Supplies	558,282	528,767
Purchased services	390,669	361,657
Depreciation and amortization	182,295	173,708
Occupancy	147,369	142,716
Medical claims	94,361	67,555
Interest	39,698	38,605
Other	154,050	149,751
Total expenses	3,402,085	3,220,837
OPERATING INCOME BEFORE OTHER ITEMS	96,389	70,487
Consolidation costs	-	(9,017)
OPERATING INCOME	96,389	61,470
NONOPERATING ITEMS:		
Investment (loss) income	(55,410)	163,868
Equity gains in unconsolidated affiliates	38,846	17,123
Change in market value and cash payments of interest rate swaps	1,964	(3,735)
Other, including income taxes	40,083	(1,385)
Total nonoperating items	25,483	175,871
EXCESS OF REVENUE OVER EXPENSES	121,872	237,341
LESS EXCESS OF REVENUE OVER EXPENSES ATTRIBUTABLE TO NONCONTROLLING INTEREST	7,158	3,894
EXCESS OF REVENUE OVER EXPENSES - Net of noncontrolling interest	$ 114,714	$ 233,447

The accompanying notes are an integral part of the consolidated financial statements.

TRINITY HEALTH

CONSOLIDATED STATEMENT OF CHANGES IN NET ASSETS (UNAUDITED)
THREE MONTHS ENDED SEPTEMBER 30, 2014
(In Thousands)

	Controlling Interest	Noncontrolling Interest	Total
UNRESTRICTED NET ASSETS:			
Excess of revenue over expenses	$ 114,714	$ 7,158	$ 121,872
Net assets released from restrictions for capital acquisitions	3,455	-	3,455
Net change in retirement plan related items - consolidated organizations	6,220	-	6,220
Net change in retirement plan related items - unconsolidated organizations	61	-	61
Acquisition of a controlling interest in Siouxland Surgical Center ("Siouxland")	-	99,008	99,008
Other	(5,275)	(1,959)	(7,234)
Increase in unrestricted net assets before discontinued operations	119,175	104,207	223,382
Discontinued operations:			
Loss from operations	(1,119)	-	(1,119)
Increase in unrestricted net assets	118,056	104,207	222,263
TEMPORARILY RESTRICTED NET ASSETS:			
Contributions	8,634	-	8,634
Net investment gain	705	-	705
Net assets released from restrictions	(7,184)	-	(7,184)
Other	(405)	-	(405)
Increase in temporarily restricted net assets	1,750	-	1,750
PERMANENTLY RESTRICTED NET ASSETS:			
Contributions for endowment funds	771	-	771
Net investment loss	(908)	-	(908)
Other	(98)	-	(98)
Decrease in permanently restricted net assets	(235)	-	(235)
INCREASE IN NET ASSETS	119,571	104,207	223,778
NET ASSETS - JUNE 30, 2014	10,505,372	38,090	10,543,462
NET ASSETS - SEPTEMBER 30, 2014	$ 10,624,943	$ 142,297	$ 10,767,240

The accompanying notes are an integral part of the consolidated financial statements. (Continued)

TRINITY HEALTH

CONSOLIDATED STATEMENT OF CHANGES IN NET ASSETS (UNAUDITED)
THREE MONTHS ENDED SEPTEMBER 30, 2013
(In Thousands)

	Controlling Interest	Noncontrolling Interest	Total
UNRESTRICTED NET ASSETS:			
Excess of revenue over expenses	$ 233,447	$ 3,894	$ 237,341
Net assets released from restrictions for capital acquisitions	4,815	-	4,815
Net change in retirement plan related items - consolidated organizations	17,512	-	17,512
Net change in retirement plan related items - unconsolidated organizations	11,026	-	11,026
Other	(1,332)	(3,658)	(4,990)
Increase in unrestricted net assets before discontinued operations	265,468	236	265,704
Discontinued operations:			
Loss from operations	(8,009)	-	(8,009)
Increase in unrestricted net assets	257,459	236	257,695
TEMPORARILY RESTRICTED NET ASSETS:			
Contributions	12,493	-	12,493
Net investment gain	1,439	-	1,439
Net assets released from restrictions	(9,618)	-	(9,618)
Other	(22)	-	(22)
Increase in temporarily restricted net assets	4,292	-	4,292
PERMANENTLY RESTRICTED NET ASSETS:			
Contributions for endowment funds	384	-	384
Net investment gain	1,280	-	1,280
Other	19	-	19
Increase in permanently restricted net assets	1,683	-	1,683
INCREASE IN NET ASSETS	263,434	236	263,670
NET ASSETS - JUNE 30, 2013	9,413,928	31,034	9,444,962
Net asset changes due to alignment of accounting policies and adjustments	148,993	-	148,993
NET ASSETS - July 1, 2013	9,562,921	31,034	9,593,955
NET ASSETS - September 30, 2013	$ 9,826,355	$ 31,270	$ 9,857,625

The accompanying notes are an integral part of the consolidated financial statements. (Concluded)

TRINITY HEALTH

SUMMARIZED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(In Thousands)

	Three Months Ended	
	September 30, 2014	**September 30, 2013**
OPERATING ACTIVITIES:		
Increase in net assets	$ 223,778	$ 263,670
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	182,295	173,708
Provision for bad debts	152,655	181,851
Increase in noncontrolling interest related to acquisition of Siouxland	(99,008)	
Gain on acquisition of a controlling interest in Siouxland	(40,318)	-
Equity earnings from unconsolidated affiliates	(46,376)	(34,254)
Deferred retirement items - unconsolidated organizations	-	(11,026)
Change in net unrealized and realized gains and losses on investments	72,549	(153,887)
Change in market values of interest rate swaps	(6,076)	(1,202)
Restricted contributions and investment income received	(2,657)	(4,297)
Other adjustments	767	988
Changes in:		
Patient accounts receivable	(212,579)	(214,163)
Other assets	(45,997)	(14,341)
Accounts payable and accrued expenses	(7,286)	(100,199)
Estimated receivables from third-party payors	(4,968)	(13,061)
Estimated payables to third-party payors	26,585	(11,934)
Accrued pension and retiree health costs	(26,245)	(19,919)
Self-insurance and other liabilities	33,331	17,565
Net cash provided by (used in) operating activities of discontinued operations	15,512	(5,275)
Total adjustments	(7,816)	(209,446)
Net cash provided by operating activities	215,962	54,224
INVESTING ACTIVITIES:		
Net purchases of investments	(239,673)	(79,874)
Net purchases of property and equipment	(199,515)	(211,607)
Net cash acquired from acquisition of a controlling interest in Siouxland	1,778	-
Proceeds from disposal of property and equipment	424	1,264
Dividends received from unconsolidated affiliates and other changes	6,143	8,401
Net decrease (increase) in assets limited as to use	4,027	(22,933)
Net cash used in investing activities of discontinued operations	(2,207)	(7,011)
Net cash used in investing activities	(429,023)	(311,760)
FINANCING ACTIVITIES:		
Proceeds from issuance of debt	19,487	4,382
Repayments of debt	(11,221)	(20,276)
Net change in commercial paper	18	29,048
Increase in financing costs and other	62	-
Proceeds from restricted contributions and restricted investment income	2,657	4,297
Net cash provided by (used in) financing activities of discontinued operations	10	(4,349)
Net cash provided by financing activities	11,013	13,102
NET DECREASE IN CASH AND CASH EQUIVALENTS	(202,048)	(244,434)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	901,282	998,369
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 699,234	$ 753,935

1. ORGANIZATION AND MISSION

Effective May 1, 2013, CHE Trinity Inc. (now "Trinity Health" and "the Corporation") became the sole member of Catholic Health East, a Pennsylvania nonprofit corporation ("CHE"), and Trinity Health Corporation, an Indiana nonprofit corporation ("THC") creating a unified Catholic national health system that enhances the mission of service to people and communities across the United States. This transaction was accounted for as a merger and thus the Corporation's balance sheet is recorded at its historical basis under the carryover method. The Corporation incurred approximately $9.0 million of expenses for the three months ended September 30, 2013, as a result of the transaction, which are included in consolidation costs in the statement of operations and changes in net assets. In addition, in July 2013, the Corporation recorded adjustments to net assets totaling $149.0 million to align accounting policies and assumptions related to the valuation of pension and insurance liabilities. CHE Trinity Inc., CHE and THC were merged into one legal corporation, with Trinity Health being the surviving legal corporation on July 1, 2014.

The Corporation has adopted a fiscal year end of June 30. Effective July 1, 2013, CHE changed its fiscal year end from December 31 to June 30 in order to align CHE's year end with the Corporation. These statements reflect the adoption of a June 30 fiscal year end.

The Corporation is sponsored by Catholic Health Ministries, a Public Juridic Person of the Holy Roman Catholic Church. The Corporation operates a comprehensive integrated network of health services including inpatient and outpatient services, physician services, managed care coverage, home health care, long-term care, assisted living care and rehabilitation services located in twenty states. The operations are organized into Regional Health Ministries ("RHMs"). The mission statement for the Corporation is as follows:

> *We, Trinity Health, serve together in the spirit of the Gospel as a compassionate and transforming healing presence within our communities.*

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United Statements of America ("GAAP") for interim financial reporting information. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included and are of a normal and recurring nature. Operating results for the three months ended September 30, 2014 are not necessarily indicative of the results to be expected for the year ending June 30, 2015.

Principles of Consolidation **-** The consolidated financial statements include the accounts of the Corporation, and all wholly-owned, majority-owned and controlled organizations. Investments where the Corporation holds less than 20% of the ownership interest are accounted for using the cost method. All other investments that are not controlled by the Corporation are accounted for using the equity method of accounting. The Corporation has included its equity share of income or losses from investments in unconsolidated affiliates in other revenue and nonoperating items in the consolidated statements of operations and changes in net assets. All material intercompany transactions and account balances have been eliminated in consolidation.

Use of Estimates **-** The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management of the Corporation to make assumptions, estimates and judgments that affect the amounts reported in the consolidated financial statements, including the notes thereto, and related disclosures of commitments and contingencies, if any. The Corporation considers critical accounting policies to be those that require more significant judgments and estimates in the preparation of its consolidated financial statements, including the following: recognition of net patient service revenue, which includes contractual allowances; provisions for bad debts and charity care; recorded values of investments, derivatives and goodwill; reserves for losses and expenses related to health care professional and general liabilities; and risks and assumptions for measurement of pension and retiree medical liabilities. Management relies on historical experience and other assumptions believed to be reasonable in making its judgment and estimates. Actual results could differ materially from those estimates.

Cash and Cash Equivalents – For purposes of the consolidated statements of cash flows, cash and cash equivalents include certain investments in highly liquid debt instruments with original maturities of three months or less.

Investments **-** Investments, inclusive of assets limited or restricted as to use, include marketable debt and equity securities. Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value and are classified as trading securities. Investments also include investments in commingled funds, hedge funds and other investments structured as limited liability corporations or partnerships. Commingled funds and hedge funds that hold securities directly are stated at the fair value of the underlying securities, as determined by the administrator, based on readily determinable market values or based on net asset value, which is calculated using the most recent fund financial statements. Limited liability corporations and partnerships are accounted for under the equity method.

Investment Earnings – Investment earnings include interest, dividends, realized gains and losses on investments, holding gains and losses, and equity earnings. Investment earnings on assets held by trustees under bond indenture agreements, assets designated by the Board for debt redemption, assets held for borrowings under the intercompany loan program, assets held by grant making foundations and assets deposited in trust funds by a captive insurance company for self-insurance purposes in accordance with industry practices are included in other revenue in the consolidated statements of operations and changes in net assets. Investment earnings from all other investments and board designated funds are included in nonoperating investment (loss) income, unless the income or loss is restricted by donor or law.

Derivative Financial Instruments – The Corporation periodically utilizes various financial instruments (e.g. options and swaps) to hedge interest rate, equity downside risk and other exposures. The Corporation’s policies prohibit trading in derivative financial instruments on a speculative basis. The Corporation recognizes all derivative instruments in the balance sheets at fair value.

Securities Lending – The Corporation participates in securities lending transactions whereby a portion of its investments are loaned, through its agent, to various parties in return for cash and securities from the parties as collateral for the securities loaned. Each business day the Corporation, through its agent, and the borrower determine the market value of the collateral and the borrowed securities. If on any business day the market value of the collateral is less than the required value, additional collateral is obtained as appropriate. The amount of cash collateral received under securities lending is reported as an asset and a corresponding payable in the consolidated balance sheets and is up to 105% of the market value of securities loaned. At September 30, 2014 and June 30, 2014, the Corporation had securities loaned of $219.9 million and $207.1 million, respectively, and received collateral (cash and noncash) totaling $228.5 million and $212.7 million, respectively, relating to the securities loaned. The fees received for these transactions are recorded in investment (loss) income on the consolidated statements of operations and changes in net assets.

Assets Limited as to Use – Assets set aside by the Board for future capital improvements, future funding of retirement programs and insurance claims, retirement of debt, held for borrowings under the intercompany loan program, and other purposes over which the Board retains control and may at its discretion subsequently use for other purposes and self-insurance trust and benefit plan arrangements are included in assets limited as to use.

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

Inventories – Inventories are stated at the lower of cost or market. The cost of inventories is determined principally by the weighted average cost method.

Assets and Liabilities Held for Sale – The Corporation has classified certain long-lived assets as assets held for sale in the consolidated balance sheets when the assets have met applicable criteria for this classification. The Corporation has also classified as held for sale those liabilities related to assets held for sale.

Property and Equipment – Property and equipment, including internal-use software, are recorded at cost, if purchased, or at fair value at the date of donation, if donated. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using either the straight-line or an accelerated method and includes capital lease and internal-use software amortization. The useful lives of these assets range from 2 to 50 years. Interest costs incurred during the period of construction of capital assets are capitalized as a component of the cost of acquiring those assets.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support and are excluded from the excess of revenue over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support.

Goodwill – Goodwill represents the future economic benefits arising from assets acquired in a business combination that are not individually identified and separately recognized.

Asset Impairment:

> ***Property and Equipment*** – The Corporation evaluates long-lived assets for possible impairment annually or whenever events or changes in circumstances indicate that the carrying amount of the asset, or related group of assets, may not be recoverable from estimated future undiscounted cash flows. If the estimated future undiscounted cash flows are less than the carrying value of the assets, the impairment recognized is calculated as the carrying value of the long-lived assets in excess of the fair value of the assets. The fair value of the assets is estimated based on appraisals, established market values of comparable assets or internal estimates of future net cash flows expected to result from the use and ultimate disposition of the asset.
>
> ***Goodwill*** **–** Goodwill is tested for impairment on an annual basis or when an event or a change in circumstance indicates the value of a reporting unit may have changed. Testing is conducted at the reporting unit level. If the carrying amount of the reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. Estimates of fair value are based on appraisals, established market prices for comparable assets or internal estimates of future net cash flows and presume stable, improving or, in some cases, declining results at our hospitals, depending on their circumstances.

As of September 30, 2014, Goodwill increased $134.9 million related to the acquisition of Siouxland Surgery Center, LLP as further described in Note 3.

***Other Assets* –** Other assets includes long-term notes receivable, reinsurance recovery receivables, definite and indefinite-lived intangible assets, deferred financing costs, and prepaid pension and retiree health costs. The majority of the net balances of definite-lived intangible assets include noncompete agreements and physician guarantees with finite lives amortized using the straight-line method over their estimated useful lives, which generally range from 5 to 22 years and 2 to 12 years, respectively. Indefinite-lived intangible assets primarily include trade names.

Short-term borrowings – Short-term borrowings include puttable variable rate demand bonds supported by self-liquidity or liquidity facilities considered short-term in nature.

***Other Long-Term Liabilities* –** Other long-term liabilities include deferred compensation, asset retirement obligations, interest rate swaps and deferred revenue from entrance fees. Deferred revenue from entrance fees are fees paid by residents of facilities for the elderly upon entering into continuing care contracts (net of the portion that is refundable to the resident) which are recorded as deferred revenue and amortized to income using the straight-line method over the estimated remaining life expectancy of the resident.

Temporarily and Permanently Restricted Net Assets – Temporarily restricted net assets are those whose use by the Corporation has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Corporation in perpetuity.

Patient Accounts Receivable, Estimated Receivables from and Payables to Third-Party Payors and Net Patient Service Revenue – The Corporation has agreements with third-party payors that provide for payments to the Corporation's RHMs at amounts different from established rates. Patient accounts receivable and net patient service revenue are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered. Estimated retroactive adjustments under reimbursement agreements with third-party payors are included in net patient service revenue and estimated receivables from and payables to third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined. Estimated receivables from third-party payors include amounts receivable from Medicare and state Medicaid meaningful use programs.

***Self-Insured Employee Health Benefits* –** The Corporation administers self-insured employee health benefit plans for employees. The majority of the Corporation's employees participate in the programs. The provisions of the plans permit employees and their dependents to elect to receive medical care at either the Corporation's RHMs or other health care providers. Gross patient service revenue has been reduced by an allowance for self-insured employee health benefits which represents revenue attributable to medical services provided by the Corporation to its employees and dependents in such years.

***Allowance for Doubtful Accounts* –** The Corporation recognizes a significant amount of patient service revenue at the time the services are rendered even though the Corporation does not assess the patient's ability to pay at that time. As a result, the provision for bad debts is presented as a deduction from patient service revenue (net of contractual provisions and discounts). For uninsured and under insured patients that do not qualify for charity care, the Corporation establishes an allowance to reduce the carrying value of such receivables to their estimated net realizable value. This allowance is established based on the aging of accounts receivable and the historical collection experience by RHM and for each type of payor. A significant portion of the Corporation's provision for doubtful accounts relates to self-pay patients, as well as co-payments and deductibles owed to the Corporation by patients with insurance.

Premium and Capitation Revenue – The Corporation has certain RHMs that arrange for the delivery of health care services to enrollees through various contracts with providers and common provider entities. Enrollee contracts are negotiated on a yearly basis. Premiums are due monthly and are recognized as revenue during the period in which the Corporation is obligated to provide services to enrollees. Premiums received prior to the period of coverage are recorded as deferred revenue and included in accrued expenses in the consolidated balance sheet.

Certain of the Corporation's RHMs have entered into capitation arrangements whereby they accept the risk for the provision of certain health care services to health plan members. Under these agreements, the Corporation's RHMs are financially responsible for services provided to the health plan members by other institutional health care providers. Capitation revenue is recognized during the period for which the RHM is obligated to provide services to health plan enrollees under capitation contracts. Capitation receivables are included in other receivables in the consolidated balance sheets.

Reserves for incurred but not reported claims have been established to cover the unpaid costs of health care services covered under the premium and capitation arrangements. The premium and capitation arrangement reserves are classified with accrued expenses in the consolidated balance sheets. The liability is estimated based on actuarial studies, historical reporting, and payment trends. Subsequent actual claim experience will differ from the estimated liability due to variances in estimated and actual utilization of health care services, the amount of charges, and other factors. As settlements are made and estimates are revised, the differences are reflected in current operations.

Charity Care – The Corporation provides services to all patients regardless of ability to pay. In accordance with the Corporation's policy, a patient is classified as a charity patient based on income eligibility criteria as established by the *Federal Poverty Guidelines*. Charges for services to patients who meet the Corporation's guidelines for charity care are not reflected in the accompanying consolidated financial statements.

Income Taxes – The Corporation and substantially all of its subsidiaries have been recognized as tax-exempt pursuant to Section 501(a) of the Internal Revenue Code. The Corporation also has taxable subsidiaries, which are included in the consolidated financial statements. Certain of the taxable subsidiaries have entered into tax sharing agreements and file consolidated federal income tax returns with other corporate taxable subsidiaries. The Corporation includes penalties and interest, if any, with its provision for income taxes in other nonoperating items in the consolidated statements of operations and changes in net assets.

Excess of Revenue Over Expenses – The consolidated statement of operations and changes in net assets includes excess of revenue over expenses. Changes in unrestricted net assets which are excluded from excess of revenue over expenses, consistent with industry practice, include the effective portion of the change in market value of derivatives that meet hedge accounting requirements, permanent transfers of assets to and from affiliates for other than goods and services, contributions of long-lived assets received or gifted (including assets acquired using contributions, which by donor restriction were to be used for the purposes of acquiring such assets), net change in retirement plan related items, discontinued operations, extraordinary items and cumulative effects of changes in accounting principles.

Adopted Accounting Pronouncements –

On July 1, 2014, the Corporation adopted Accounting Standard Update ("ASU") 2013-04, "*Obligations Resulting From Joint and Several Liability Arrangements for Which the Total Amount of the Obligation is Fixed at the Reporting Date*." This guidance requires entities to measure obligations resulting from the joint and several liability arrangements for which the total amount of the obligation within the scope of this guidance is fixed at the reporting date. The adoption of this guidance had no impact on the Corporation's consolidated financial statements.

On July 1, 2014, the Corporation adopted ASU 2013-11, *"Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists."* This guidance requires entities to present an unrecognized tax benefit, or a portion of an unrecognized tax benefit, in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit, with some exceptions. The adoption of this guidance had no impact on the Corporation's consolidated financial statements.

Forthcoming Accounting Pronouncements –

In April 2014, the FASB issued ASU 2014-8, *"Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity."* This guidance amends the definition of a discontinued operation and requires entities to provide additional disclosures about discontinued operations as well as disposal transactions that do not meet the discontinued operations criteria. This guidance is effective for the Corporation beginning July 1, 2015, with early adoption permitted. The Corporation has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09, *"Revenue From Contracts With Customers."* This guidance outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. This guidance is effective for the Corporation beginning July 1, 2017. The Corporation has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In June 2014, the FASB issued ASU 2014-11, *"Transfers and Servicing: Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures."* This guidance requires entities to account for repurchase-to-maturity transactions as secured borrowings (rather than sales with forward repurchase agreements), eliminates accounting guidance on linked repurchase financing transactions, and expands disclosure requirements related to certain transfers (specifically repurchase agreements, securities lending transactions, and repurchase-to-maturity transactions) accounted for as secured borrowings. This guidance is effective for the Corporation beginning July 1, 2015. The Corporation has not yet evaluated the impact this guidance may have on its consolidated financial statements.

3. INVESTMENTS IN UNCONSOLIDATED AFFILIATES, BUSINESS ACQUISITIONS AND DISCONTINUED OPERATIONS

Investments in Unconsolidated Affiliates – The Corporation and certain of its RHMs have investments in entities that are recorded under the cost and equity methods of accounting. The Corporation’s share of equity earnings from entities accounted for under the equity method was $46.4 million and $34.3 million for the three months ended September 30, 2014 and 2013, respectively, of which $7.5 million and $17.1 million, respectively, is included in other revenue and $38.8 million and $17.1 million, respectively, is included in nonoperating items in the consolidated statements of operations and changes in net assets. The most significant of these investments include the following:

BayCare Health System – The Corporation has a 50.4% interest in BayCare Health System Inc. and Affiliates ("BayCare"), a Florida not-for-profit corporation exempt from state and federal income taxes. BayCare was formed in 1997 pursuant to a Joint Operating Agreement ("JOA") among the not-for-profit, tax-exempt members of the Catholic Health East BayCare Participants, Morton Plant Mease Health Care, Inc., and South Florida Baptist Hospital, Inc. (collectively, the Members). BayCare consists of three community health alliances located in the Tampa Bay area of Florida including St. Joseph's-Baptist Healthcare Hospital, St. Anthony's Health Care, and Morton Plant Mease Health Care. The Corporation has the right to appoint nine of the twenty-one voting members of the Board of Directors of BayCare, therefore the Corporation accounts for BayCare under the equity method of accounting. At September 30, 2014 and June 30, 2014, the Corporation's investment in BayCare totaled $1,806.5 million and $1,770.9 million, respectively.

Gateway Health Plan – The Corporation has a 50.0% interest in Gateway Health Plan, L.P. and Subsidiaries ("GHP"), a Pennsylvania limited partnership. GHP has two general partners, Highmark Ventures Inc. formerly known as Alliance Ventures, Inc., and Mercy Health Plan, each owning 1%. In addition to the general partners, there are two limited partners, Highmark Inc. and Mercy Health Plan, each owning 49%. At September 30, 2014 and June 30, 2014, the Corporation's investment in GHP totaled $175.8 million and $178.9 million, respectively.

Catholic Health System, Inc. – The Corporation has a one-third interest in Catholic Health System, Inc. and Subsidiaries ("CHS"). CHS, formed in 1998, is a not-for-profit integrated delivery healthcare system in western New York jointly sponsored by the Sisters of Mercy, Ascension Health System, the Franciscan Sisters of St.

Joseph, and the Diocese of Buffalo. The Corporation, Ascension Health System, and the Diocese of Buffalo are the corporate members of CHS. CHS operates several organizations, the largest of which are four acute care hospitals located in Buffalo, New York, Mercy Hospital of Buffalo, Kenmore Mercy Hospital, Sisters of Charity Hospital, and St. Joseph Hospital. At September 30, 2014 and June 30, 2014, the Corporation's investment in CHS totaled $71.5 million and $68.0 million, respectively.

Emory Healthcare/St. Joseph's Health System – The Corporation has a 49% interest in Emory Healthcare/St. Joseph's Health System ("EH/SJHS"). EH/SJHS operates several organizations, including two acute care hospitals, St. Joseph's Hospital of Atlanta and John's Creek Hospital. At both September 30, 2014 and June 30, 2014, the Corporation's investment in EH/SJHS totaled $60.3 million.

Condensed consolidated balance sheets of BayCare, GHP, CHS and EH/SJHS as of September 30 and June 30 are as follows:

(In Thousands)

	Baycare		**GHP**		**CHS**		**EH/SJHS**	
	September 30, 2014	**June 30, 2014**	**September 30, 2014**	**June 30, 2014**	**September 30, 2014**	**June 30, 2014**	**September 30, 2014**	**June 30, 2014**
Total assets	$5,539,659	$5,390,589	$620,022	$643,593	$935,549	$872,106	$450,449	$430,434
Total liabilities	$1,755,133	$1,676,157	$275,528	$285,835	$715,813	$662,733	$296,955	$289,101

Condensed consolidated statements of operations of BayCare, GHP, CHS and EH/SJHS for the three month periods ended September 30 are as follows:

(In Thousands)

	Baycare		**GHP**		**CHS**		**EH/SJHS**	
	2014	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
Revenue, net	$685,394	$642,682	$478,113	$436,280	$243,395	$236,069	$122,459	$100,202
Excess (deficiency) of revenue over expenses	$95,634	$162,333	($4,306)	$16,952	$9,855	$4,403	$653	($25,879)

The following amounts have been recognized in the accompanying consolidated statements of operations and changes in net assets related to the investments in BayCare, GHP, CHS and EH/SJHS for the three month periods ended September 30:

(In Thousands)

	Baycare		**GHP**		**CHS**		**EH/SJHS**	
	2014	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
Other Revenue	**$ -**	**$ -**	**$ 7,957**	**$ (841)**	**$ -**	**$ -**	**$ -**	**$ -**
Equity in earnings of unconsolidated organizations	35,545	26,832	-	-	3,418	2,680	(73)	(12,128)
Other changes in unrestricted net assets	(118)	-	910	-	91	-	-	11,371
	$ 35,427	$ 26,832	$ 8,867	$ (841)	$ 3,509	$ 2,680	$ (73)	$ (757)

Consolidation of Siouxland Surgery Center, LLP ("Siouxland") – Effective July 1, 2014, a joint venture was created between Mercy Health Services – Iowa, Corp. ("Mercy") and USP Health Ventures, LLC ("USP"), (collectively, "Mercy/USP"). Mercy owns a controlling interest of 55.71% and USP owns the remaining 44.29% interest of the joint venture. Mercy/USP then entered into a Securities Purchase Agreement with SSC Physician Investors, LLC ("Physician Investors"), whereby Mercy contributed 30.9% of their pre-existing ownership of Siouxland and USP contributed their newly acquired 24.6% ownership of Siouxland, resulting in Mercy/USP owning a controlling interest of 55.54% of Siouxland with the remaining 44.46% interest owned by Physician Investors. As a result of the transaction, Mercy reported a gain of $40.3 million other operating items in the consolidated statement of operations and changes in net assets in July, 2014 and recognized goodwill of $134.9 million on the consolidated balance sheet. Siouxland operates a surgical specialty hospital and medical facility in Dakota Dunes, South Dakota. Summarized consolidated opening balance sheet information for

Mercy/USP is shown below and includes the acquisition of $13.1 million of long-term debt including current portion:

(In Thousands)

Cash	$ 4,178	Accounts payable and accrued expenses	$ 9,409
Patient accounts receivable	11,191	Current portion of long-term debt	1,031
Other current assets	3,539	Long-term debt, net of current portion	12,075
Property and equipment	24,133	Total liabilities acquired	$ 22,515
Goodwill	134,947		
Other assets	799	Unrestricted net assets	$ 57,265
Total assets acquired	$ 178,787	Unrestricted noncontrolling interest	$ 99,008
		Total net assets	$ 156,273

The operating results for Siouxland for the three months ended September 30, 2014, include total unrestricted revenue of $17.3 million, operating income of $6.7 million and excess of revenue over expense, excluding non-controlling interest, of $2.1 million.

Discontinued Operations:

Mercy Health System of Maine ("Mercy Maine") – Effective October 1, 2013, membership of Mercy Maine was assumed by Eastern Maine Health System ("EMHS") via a membership substitution. Substantially all assets and liabilities transferred to EMHS on that date. As a result of the transfer, a loss on disposal of $80.7 million was recorded in unrestricted net assets. The consolidated financial statements for the three months ended September 30, 2013 present the operations of Mercy Maine as a discontinued operation. For the three month period ended September 30, 2013, the Corporation reported revenue of $55.5 million, and a loss on operations of $2.5 million, in discontinued operations in the statement of changes in net assets.

Saint Michael's Medical Center – On February 8, 2013, Saint Michael's Medical Center entered into an asset purchase agreement under which the hospital would be acquired by Prime Healthcare Services. The majority of assets and liabilities of Saint Michael's Medical Center have been classified as held for sale on the consolidated balance sheets. The transaction is pending subject to approval by the state of New Jersey. The consolidated financial statements for all periods present the operations of Saint Michael's Medical Center as a discontinued operation. For the three month periods ended September 30, 2014 and 2013, the Corporation reported revenue of $45.1 million and $63.5 million, respectively, and losses on operations of $4.9 million and $14.4 million, respectively, in discontinued operations in the statement of changes in net assets.

As of September 30, 2014 and June 30, 2014, assets held for sale were $125.0 million and $127.9 million, respectively, and liabilities held for sale were $266.1 million and $257.9 million, respectively. The assets and liabilities held for sale consisted of:

(In Thousands)

	September 30, 2014	June 30, 2014		September 30, 2014	June 30, 2014
Patient accounts receivable	18,335	21,475	Current portion of long-term debt	4,490	4,490
Other current assets	9,795	9,418	Accounts payable & accrued expenses	20,942	17,085
Property and equipment	81,350	81,465	Other current liabilities	12,831	8,546
Other assets	15,559	15,559	Long-term debt, net of current portion	227,809	227,799
Total assets	$ 125,039	$ 127,917	Total liabilities	$ 266,072	$ 257,920

Saint James Mercy Hospital ("SJMH") – During December 2013, the Board of Directors of SJMH approved a plan to undergo a visioning plan and to transfer substantially all of the operations of SJMH. Certain assets and liabilities of SJMH have been classified as held for sale on the consolidated balance sheets. The consolidated financial statements for all periods present the operations of SJMH as a discontinued operation. For the three month periods ended September 30, 2014 and 2013, the Corporation reported revenue of $11.8 million and $10.0 million, respectively, and income(losses) on operations of $0.2 million and ($2.3) million, respectively, in discontinued operations in the statement of changes in net assets. As of September 30, 2014 and June 30, 2014, assets held for sale were $12.3 million and $12.1 million, respectively. The majority of assets held for sale consist of property and equipment.

Mercy Health Partners, North ("North") – On October 17, 2014, the Corporation entered into a Definitive Agreement with Munson Health under which substantially all of the healthcare operations located in Cadillac, Michigan and Grayling, Michigan would be acquired by Munson Healthcare. Certain assets and liabilities of North have been classified as held for sale on the consolidated balance sheet. The consolidated financial statements present the hospital operations of North as a discontinued operation. For the three month periods ended September 30, 2014 and 2013, the Corporation reported revenue of $36.9 million and $37.0 million, respectively, and losses on operations of $0.3 million and $1.1 million in discontinued operations in the statement of changes in net assets. As of September 30, 2014 and June 30, 2014, assets held for sale of $44.2 million and $44.7 million, respectively, consisted of (in thousands):

	September 30, 2014	June 30, 2014
	(In Thousands)	
Inventories	$ 3,355	$ 3,369
Assets limited or restricted as to use	2,056	2,313
Property and equipment	36,472	36,710
Investments in unconsoldiated affiliates	2,314	2,314
Total assets	$ 44,197	$ 44,706

4. **PROPERTY AND EQUIPMENT**

A summary of property and equipment at September 30, 2014 and June 30, 2014 is as follows:

	September 30, 2014	June 30, 2014
	(In Thousands)	
Land	$ 318,964	$ 318,368
Buildings and improvements	7,681,010	7,655,128
Equipment and capital leased assets	5,230,432	5,190,900
Capital leased assets	193,330	192,754
Total	13,423,736	13,357,150
Accumulated depreciation and amortization	(7,466,974)	(7,324,759)
Construction in progress	625,634	560,522
Property and equipment, net	$ 6,582,396	$ 6,592,913

As part of the acquisition of LUHS that occurred in fiscal year 2012, the Corporation has committed to spend at least $300 million on capital projects for LUHS through fiscal year ending June 30, 2018. This amount may be increased to $400 million if certain operating thresholds are met. Through September 30, 2014, approximately $162 million of capital expenditures have been incurred on capital projects for LUHS. In addition, as part of the acquisition of Mercy Health System of Chicago (MHSC) that occurred in fiscal year 2012, the Corporation has committed to spend at least $140 million for capital, information systems and equipment needs to support the operations of MHSC through the fiscal year ending June 30, 2017. This amount may be increased to $150 million if certain operating thresholds are met. Through September 30, 2014 approximately $70 million of capital expenditures have been incurred on such MHSC projects.

5. LONG-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Obligated Group and Other Requirements – The Corporation has debt outstanding under a Master Trust Indenture dated October 3, 2013, as amended and supplemented, the Amended and Restated Master Indenture ("ARMI"). The ARMI permits the Corporation to issue obligations to finance certain activities. Obligations issued under the ARMI are joint and several obligations of the obligated group established thereunder (the "Obligated Group", which currently consists of the Corporation). Proceeds from tax-exempt bonds and refunding bonds are to be used to finance the construction, acquisition and equipping of capital improvements. Certain RHMs of the Corporation constitute designated affiliates and the Corporation covenants to cause each designated affiliate to pay, loan or otherwise transfer to the Obligated Group such amounts necessary to pay the amounts due on all obligations issued under the ARMI. The Obligated Group and the designated affiliates are referred to as the Credit Group.

The Credit Group does not include certain Affiliates that borrow on their own or are members of a separate New York obligated group, but which are included in the Corporation's consolidated financial statements. St. Peter's Hospital of the City of Albany ("St. Peter's") currently is the Obligated Group Agent of an obligated group created under that certain Master Trust Indenture dated as of January 1, 2008, between St. Peter's and Manufacturers and Traders Trust Company, as Master Trustee. St. Peter's has received approval from the New York State Department of Health to permit the entry into that obligated group of additional entities within St. Peter's Health Care Services, Northeast Health, Inc. and Seton Health System, Inc.

The Obligated Group agrees in the ARMI to cause Designated Affiliates to grant to the Master Trustee security interests in their Pledged Property in order to secure all Obligations issued under the Master Indenture. The Designated Affiliates when combined with the current Members of the Obligated Group represent no less than 85% of the consolidated net revenues of the Credit Group.

There are several conditions and covenants required by the ARMI with which the Corporation must comply, including covenants that require the Corporation to maintain a minimum debt service coverage and limitations on liens or security interests in property, except for certain permitted encumbrances, affecting the property of the Corporation or any material designated affiliate (a designated affiliate whose total revenues for the most recent fiscal year exceed 5% of the combined total revenues of the Corporation for the most recent fiscal year). Long-term debt outstanding as of September 30, 2014 and June 30, 2014, excluding amounts issued under the ARMI, is generally collateralized by certain property and equipment.

Mercy Health System of Chicago ("MHSC") has obtained a mortgage loan in the amount of approximately $66 million that is insured by the U.S. Department of Housing and Urban Development ("HUD") under the Federal Housing Administration's Section 242 Hospital Mortgage Insurance Program. Final closing of this HUD-insured loan occurred on June 30, 2014, at which time the remaining proceeds of this loan were disbursed to MHSC. At September 30, 2014 and June 30, 2014, the unpaid principal balance of this loan was $62.6 million and $63.1 million, respectively. The loan collateral includes MHSC's main hospital campus, two MHSC satellite facilities and personal property (including deposit accounts) of both MHSC and its affiliate Mercy Foundation, Inc. MHSC's payment obligations under the two mortgage notes evidencing this loan are guaranteed by the Corporation . The mortgage loan agreements with HUD contain various covenants including those relating to limitations on incurring additional debt, transactions with affiliates, transferring or disposing of designated property, use of funds and other assets of the mortgaged property, financial performance, required reserves, insurance coverage, timely submission of specified financial reports and restrictions on prepayment of the mortgage loan. Mercy Health System of Chicago and Trinity provided covenants to HUD not to interfere in the performance of MHSC's obligations under the HUD-insured loan documents.

In October 2014, the Corporation remarketed $50 million in tax-exempt, variable rate hospital revenue bonds (the "Series 2011A bonds") under the ARMI. Other increases in debt from June 30, 2014 were $13.1 million due to the acquisition of a controlling interest in Siouxland and $19.5 million related to issuance of notes payable at certain RHMs.

Commercial Paper – The Corporation's commercial paper program is authorized for borrowings up to $600 million. At September 30, 2014 and June 30, 2014, the total amount of commercial paper outstanding was $240 million. Proceeds from this program are used for general purposes of the Corporation. The notes are payable from the proceeds of subsequently issued notes and from other funds available to the Corporation, including funds derived from the liquidation of securities held by the Corporation in its investment portfolios.

Liquidity Facilities – In July 2014, the Corporation amended and restated the Trinity Health credit agreements (collectively, the "Credit Agreements") previously entered into between THC and U.S. Bank National Association, which acts as an administrative agent for a group of lenders thereunder. The Credit Agreements establish a revolving credit facility for the Corporation, under which that group of lenders agree to lend to the Corporation amounts that may fluctuate from time to time. In October 2013, the Corporation exercised its option to increase by $200 million the 2013 Credit Agreements from $731 million to $931 million. Amounts drawn under the 2013 Credit Agreements can only be used to support the Corporation's obligation to pay the purchase price of bonds which are subject to tender and that have not been successfully remarketed, and the maturing principal of and interest on commercial paper notes. Of the $931 million available balance, $150 million expires in July 2015, $175 million expires in July 2016, $321 million expires in July 2017 and $285 million expires in July 2018. The Credit Agreements are secured by Obligations under the Master Indenture. As of September 30, 2014 and June 30, 2014, there were no amounts outstanding on these credit agreements.

The Corporation also maintains a general purpose facility of $300 million, of which $42 million is related to letters of credit. At the Corporation's direction, this general purpose facility was reduced to $45 million effective March 14, 2014. As of September 30, 2014 and June 30, 2014, there were no draws on this general purpose credit facility.

In addition, in July 2013, the Corporation renewed a three year general purpose credit facility of $200 million. As of September 30, 2014 and June 30, 2014, there were no amounts outstanding under this credit facility.

6. PROFESSIONAL AND GENERAL LIABILITY PROGRAMS

The Corporation operates a wholly owned insurance company, Venzke Insurance Company, Ltd. ("Venzke) that qualifies as a captive insurance company and provides certain insurance coverage to the Corporation's RHMs under a centralized program. The Corporation is self-insured for certain levels of general and professional liability, workers' compensation and certain other claims. The Corporation has limited its liability by purchasing reinsurance and commercial coverage from unrelated third-party insurers.

Effective January 1, 2014, all assets and liabilities of Stella Maris Insurance Company, Ltd. ("Stella Maris") which qualified as a captive insurance company, merged into Venzke. Policies issued and reinsurance purchased by Stella Maris prior to January 1, 2014 and all losses previous to January 1, 2014 have been assumed by Venzke.

The Corporation's current self-insurance program includes $20 million per occurrence for the first layers of professional liability, as well as $10 million per occurrence for hospital government liability, $5 million per occurrence for errors and omission liability, and $1 million per occurrence for directors' and officers' liability. Additional layers of liability insurance are available with coverage provided through other insurance carriers and various reinsurance arrangements. The total amount available for these subsequent layers is $100 million in aggregate for the period of July 1, 2014 through July 1, 2017. The Corporation self-insures $750,000 per occurrence for workers' compensation in most states, with commercial insurance providing coverage up to the statutory limits, and self-insures up to $500,000 in property values per occurrence with commercial insurance providing coverage up to $1 billion.

The liability for self-insurance reserves represents estimates of the ultimate net cost of all losses and loss adjustment expenses which are incurred but unpaid at the consolidated balance sheet date. The reserves are based on the loss and loss adjustment expense factors inherent in the Corporation's premium structure. Independent consulting actuaries determined these factors from estimates of the Corporation's expenses and available industry-wide data. The Corporation discounts the reserves to their present value using a discount rate of 3.0%. The reserves include estimates of future trends in claim severity and frequency. Although considerable variability is inherent in such estimates, management believes that the liability for unpaid claims and related adjustment expenses is adequate based on the loss experience of the Corporation. The estimates are continually reviewed and adjusted as necessary.

Claims in excess of certain insurance coverage and the recorded self-insurance liability have been asserted against the Corporation by various claimants. The claims are in various stages of processing, and some may ultimately be brought to trial. There are known incidents occurring through September 30, 2014, that may result in the assertion of additional claims, and other claims may be asserted arising from services provided in the past. While it is possible that settlement of asserted claims and claims which may be asserted in the future could result in liabilities in excess of amounts for which the Corporation has provided, management, based upon the advice of Counsel, believes that the excess liability, if any, should not materially affect the consolidated financial position, operations or cash flows of the Corporation.

7. PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS

***Defined Contribution Benefits* –** The Corporation sponsors defined contribution pension plans covering substantially all of its employees. These programs vary by location and are funded by employee voluntary contributions, subject to legal limitations. Employer contributions to these plans include varying levels of matching and non-elective contributions. The employees direct their voluntary contributions and employer contributions among a variety of investment options. The Corporation suspended the majority of employer matching contributions for the calendar years 2013 and 2014 for the Trinity Health 403b Retirement Savings Plan. Contribution expense under the plans totaled $18.9 million and $15.2 million for the three month periods ended September 30, 2014 and 2013, respectively.

***Defined Benefit Pension Plans* –** The Corporation sponsors non-contributory defined benefit pension plans. Certain of the plans have been amended to freeze benefit accruals. The remaining active defined benefit pension plan is structured as a cash balance plan and was amended in June 2014 to freeze benefit accruals as of December 31, 2014. The Corporation recognizes in its consolidated balance sheets the funded status of its defined benefit pension and other post retirement plans, measured as the difference between the fair value of plan assets and the benefit obligation as of June 30. Further, actuarial gains and losses that are not recognized in net periodic pension cost when they arise are recognized as a component of unrestricted net assets and are amortized as a component of net periodic pension cost over the average future working lifetime of active participants, or the average future life expectancy of all participants for plans with frozen benefits.

Other Post Retirement Benefit Plans – The Corporation also sponsors both funded and unfunded contributory retiree health plans for certain hourly and salaried employees who are retired from or will retire from certain regional health ministries. Benefits provided under these plans and required retiree contributions differ by regional health ministry. The funded plans provide benefits to certain retirees at fixed dollar amounts in Health Reimbursement Account arrangements for Medicare eligible participants. As of January 1, 2002, all such plans were closed to additional participants.

Components of net periodic benefit cost for the three month periods ended September 30 consisted of the following:

	Pension Plans 2014	Pension Plans 2013	Postretirement Plans 2014	Postretirement Plans 2013
	(In Thousands)		(In Thousands)	
Service cost	$ 17,786	$ 37,285	$ 119	$ 157
Interest cost	74,403	81,324	1,220	1,324
Expected return on assets	(95,697)	(97,669)	(1,746)	(1,528)
Amortization of prior service cost	(1,469)	(6,720)	(141)	(1,441)
Recognized net actuarial loss	7,896	25,877	(65)	(42)
Net periodic benefit cost (income)	$ 2,919	$ 40,097	$ (613)	$ (1,530)

8. CONTINGENCIES

Saint Alphonsus Regional Medical Center and its subsidiary Saint Alphonsus Diversified Care, Inc. (together, "Saint Alphonsus") have been involved in litigation arising out of the withdrawal of Saint Alphonsus from an imaging center partnership. The matter first went to trial in 2007, was appealed and tried a second time in 2011. In the second trial, the jury held against Saint Alphonsus in the amount of $52 million, which was offset by the value of Saint Alphonsus' partnership interest, which, together with interest, was approximately $6.6 million at the time of judgment. Saint Alphonsus appealed the second jury verdict to Idaho Supreme Court. On June 16, 2014, the Idaho Supreme Court affirmed the jury award, which, when combined with attorney fees, costs and interest, is a total judgment of approximately $56 million. The Corporation recorded management's estimation for damages of $20 million in fiscal year 2007. As a result, an additional litigation accrual of $36 million was recorded in the fiscal year 2014 consolidated statement of operations and statement of changes in net assets. The judgment was paid in August 2014.

The Corporation as successor to CHE is the defendant in a purported class action lawsuit in New York state court brought by Emmet & Co, Inc., and First Manhattan Co, with respect to one series of bonds issued for the benefit of a hospital acquired by CHE. Those bonds, along with two other series of bonds issued for the benefit of hospitals acquired by CHE, were defeased in 1998 at the time of CHE's acquisition of the hospitals. The Corporation no longer controls the hospitals related to these bonds. Plaintiffs allege that the Corporation breached the Indenture relating to those bonds and violated the covenant of good faith and fair dealing in the exercise of its optional redemption rights for those bonds in connection with the Corporation's tender offer for those bonds. This lawsuit is similar to an earlier action by the plaintiffs against CHE and Merrill Lynch, Pierce, Fenner & Smith, one of the Corporation's underwriters, that was dismissed in 2013 by the trial court in New York. The present lawsuit was preceded by plaintiff's unsuccessful 2014 request that the Trustee bring an action against CHE on the bonds in question. In June 2013, the Corporation received notices from the IRS that the three series were under audit, asking for information. The Corporation has responded to the IRS information requests in detailed responses, most recently in May 2014, and is cooperating in the ongoing examinations. The Corporation believes that the tender and redemption process was properly conducted and received bond counsel and corporate counsel opinions to this effect at the time. With respect to both the lawsuit and the IRS audit, the Corporation's management does not believe that this matter, if decided adversely, would have a material adverse effect on the financial condition of the Corporation.

On March 29, 2013, CHE (now the Corporation) was notified that it is a defendant in a lawsuit filed in the United States District Court for the Eastern District of PA that challenges the church plan status of the CHE Employee Pension Plan. This is similar to at least eight other purported class action cases that have been brought against religiously affiliated health care systems or providers, including one described below making similar allegations with respect to the Trinity Health Employee Pension Plan. In response, the Corporation has filed a motion to dismiss the complaint, which is now pending before the United States District Court for the Eastern District of Pennsylvania. At this point, it is not possible to assess the exposure, if any, related to these claims and no amount has been reserved at this time.

On July 17, 2014, THC (now the Corporation) was notified that it is a defendant in a lawsuit filed in the United States District Court District of Maryland that challenges the church plan status of the Trinity Health Employee Pension Plan. In response thereto, the Corporation has filed a motion to dismiss the complaint, which is now pending before the United States District Court for the District of Maryland. Briefing is scheduled to be completed by the end of the year, and oral argument has been scheduled on February 23, 2015. At this point, it is not possible to assess the exposure, if any, related to these claims and the Corporation has not reserved any amounts at this time related to either the existing challenge with respect to the Catholic Health East Employee Pension Plan or the recently filed lawsuit against THC.

The Corporation is involved in other litigation and regulatory investigations arising in the course of doing business. After consultation with legal Counsel, management estimates that these matters will be resolved without material adverse effect on the Corporation's future consolidated financial position or results of operations.

9. SUBSEQUENT EVENTS

Management has evaluated subsequent events through November 24, 2014, the date the quarterly report was issued. The following subsequent event was noted:

St. Joseph Mercy Port Huron ("Port Huron") – On November 19, 2014, the Corporation entered into a Definitive Agreement with Prime Healthcare Services, a hospital system based in Ontario, California, under which substantially all of the healthcare operations and certain assets located in Port Huron, Michigan would be acquired by Prime Healthcare Services. Port Huron reported total unrestricted revenue of $19.8 million and $19.1 million and (deficiency) of revenue over expenses of ($0.7) million and ($0.7) million for the three month periods ended September 30, 2014 and 2013, respectively, that is consolidated in these financial statements. As of September 30, 2014 and June 30, 2014, the consolidated balance sheets include approximately $37.0 million of Port Huron assets expected to be sold pursuant to this transaction.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management of the Corporation to make assumptions, estimates and judgments that affect the amounts reported in the financial statements, including the notes thereto, and related disclosures of commitments and contingencies, if any. The Corporation considers critical accounting policies to be those that require the more significant judgments and estimates in the preparation of its financial statements, including the following: recognition of net patient service revenue, which includes contractual allowances, provisions for bad debt and charity care; recorded values of investments and goodwill; reserves for losses and expenses related to health care professional and general liability; and risks and assumptions for measurement of pension and retiree medical liabilities. Management relies on historical experience and on other assumptions believed to be reasonable under the circumstances in making its judgment and estimates. Actual results could differ materially from those estimates.

The Patient Protection and Affordable Care Act ("ACA") was enacted in March 2010. This legislation addresses almost all aspects of hospital and provider operations and health care delivery, and is changing how health care services are covered, delivered, and reimbursed. These changes will result in new payment models with the risk of lower hospital reimbursement from Medicare, utilization changes, increased government enforcement and the necessity for health care providers to assess, and potentially alter, their business strategy and practices, among other consequences. While many providers may receive reduced payments for care, millions of previously uninsured Americans may have coverage. Management of the Corporation has analyzed the ACA and will continue to do so in order to assess the effects of the legislation and evolving regulations on current and projected operations, financial performance and financial condition. However, management of the Corporation cannot predict with any reasonable degree of certainty or reliability any interim or ultimate effects of the legislation.

Effective May 1, 2013, CHE Trinity Inc. (now "Trinity Health" and "the Corporation") became the sole member of Catholic Health East, a Pennsylvania nonprofit corporation ("CHE"), and Trinity Health Corporation, an Indiana nonprofit corporation ("THC") creating a unified Catholic national health system that enhances the mission of service to people and communities across the United States. This transaction was accounted for as a merger and thus the Corporation's balance sheet is recorded at its historical basis under the carryover method. The Corporation incurred approximately $9.0 million of expenses for the three months ended September 30, 2013, as a result of the transaction, which are included in consolidation costs in the statement of operations and changes in net assets. In addition, in July 2013, the Corporation recorded adjustments to net assets totaling $149.0 million to align accounting policies and assumptions related to the valuation of pension and insurance liabilities. CHE Trinity Inc., CHE and THC were merged into one legal corporation, with Trinity Health being the surviving legal corporation on July 1, 2014.

Effective July 1, 2014, a joint venture was created between Mercy Health Services – Iowa, Corp. ("Mercy") and USP Health Ventures, LLC ("USP"), (collectively, "Mercy/USP"). Mercy owns a controlling interest of 55.71% and USP owns the remaining 44.29% interest of the joint venture. Mercy/USP then entered into a Securities Purchase Agreement with SSC Physician Investors, LLC ("Physician Investors"), whereby Mercy contributed 30.9% of their pre-existing ownership of Siouxland Surgery Center ("Siouxland") and USP contributed their newly acquired 24.6% ownership of Siouxland, resulting in Mercy/USP owning a controlling interest of 55.54% of Siouxland with the remaining 44.46% interest owned by Physician Investors. As a result of the transaction, Mercy reported a gain of $40.3 million in other nonoperating items in the consolidated statement of operations and changes in net assets in July, 2014 and recognized goodwill of $134.9 million on the consolidated balance sheet. Siouxland operates a surgical specialty hospital and medical facility in Dakota Dunes, South Dakota.

Historical Performance: Three Months Ended September 30, 2014 and 2013

Operating Income. Operating income before other items for the first three months of fiscal year 2015 of $96.4 million increased $25.9 million compared to the same period in fiscal year 2014. Operating cash flow margin and operating margin, before other items, were 9.1% and 2.8%, respectively, for the three months ended September 30, 2014, compared to 8.6% and 2.1% for the same period in fiscal year 2014. Results were favorably impacted by volume growth, a $10.8 million dividend from a cost method investment and $4.7 million of income from the acquisition of a controlling interest in Siouxland. Other items include transition and integration expenses as a result of the merger of $9.0 million for the three months ended September 30, 2013 which are included in consolidation costs in the statement of operations and changes in net assets.

Excess of Revenue over Expenses. Excess of revenue over expenses was $121.9 million for the three months ended September 30, 2014, compared to $237.3 million for the same period in fiscal year 2014. The $115.4 million decrease is primarily driven by a decrease in investment earnings of $219.3 million attributable to lower financial market returns during the first three months of fiscal year 2015. This was partially offset by the increase in operating income before other items of $25.9 million, non-cash gain of $40.3 million for a step-up in basis to fair value related to the acquisition of a controlling interest in Siouxland, and an increase equity gains in unconsolidated affiliates of $21.7 million.

Revenue. Operating revenue has continued to grow in fiscal year 2015. Total unrestricted revenue of $3.5 billion increased $207.2 million, or 6.3%, for the three months of fiscal year 2015, compared to the same period in fiscal year 2014. Contributors to the increase were due primarily to the following: (i) $123.4 million in volume growth as measured by case-mix adjusted equivalent discharges, (ii) a decrease in charity care of $87.1 million, (iii) a decrease in provision for bad debts of $30.1 million and (iv) the acquisition of a controlling interest in Siouxland of $16.0 million. These increases were partially offset by payor and service mix changes resulting in a decrease of $83.2 million to net patient service revenue. Volumes were primarily favorable compared to prior year with 16 of the 19 Regional Health Ministries experiencing increases in case-mix adjusted equivalent discharges.

Expenses. Total operating expenses of $3.4 billion, excluding other items, increased $181.2 million, or 5.6%, for the first three months of fiscal year 2015, compared to the same period in fiscal year 2014. Contributors to the increase were due primarily to the following: (i) labor expense of $74.6 million (salaries and wages $65.5 million primarily due to a 2.3% increase in rate and a 2.2% increase in FTEs driven by favorable volumes), (ii) supplies of $25.6 million, (iii) purchased services of $26.5 million, (iv) medical claims of $26.8 million and (v) $10.0 million of expenses as a result of the acquisition of a controlling interest Siouxland. Expenses for depreciation and amortization, occupancy and interest did not materially change during the three months ended September 30, 2014 compared to the same period in fiscal year 2014.

Nonoperating Items. The Corporation reported gains in nonoperating items of $25.5 million for the first three months of fiscal year 2015, compared to gains of $175.9 million for the same period of fiscal year 2014. The decrease of $150.4 million was primarily due to a decrease in investment earnings of $219.3 million attributable to lower financial market returns during the first three months of fiscal year 2015. This was partially offset by a non-cash gain of $40.3 million for a step-up in basis to fair value related to the acquisition of Siouxland and an increase equity gains in unconsolidated affiliates of $21.7 million.

Balance Sheet Trends. The Corporation’s total assets of $20.7 billion increased $245.5 million, or 1.2%, as of September 30, 2014, compared to June 30, 2014. The most significant increases include: (i) investments, current of $136.9 million, (ii) goodwill of $134.8 million as a result of the acquisition of Siouxland, (iii) assets limited or restricted as to use, non-current portion for self-insurance, benefit plans and other of $101.3 million, (iv) patient accounts receivable, net of allowance of doubtful accounts, of $71.1 million (of which $11.2M related to the Siouxland acquisition) and (v) prepaid expenses and other current assets of $37.2 million. These increases were partially offset by decreases in cash and cash equivalents of $202.0 million and assets limited or restricted as to use, non-current portion, by Board of $47.7 million. Total liabilities of $9.9 billion increased $21.7 million, or 0.2%. The most significant increases were in self-insurance reserves of $49.2 million and estimated payables to third-party payors of $26.6 million. These increases were partially offset by a decrease in accounts payable of $68.0 million.

Statement of Cash Flows. Cash and cash equivalents decreased $202.0 million during the three months ended September 30, 2014. During that period, operating activities provided $216.0 million of cash. Investing activities used $429.0 million of cash including $239.7 million for net purchases of investments and $199.5 million for net purchases of property and equipment. Financing activities generated $11.0 million of cash primarily from the issuance of debt of $19.5 million partially offset by repayments of debt of $11.2 million.

CHE TRINITY INC.
Liquidity Reporting
Summary as of September 30, 2014

	($ in millions) (unaudited)	
ASSETS		
Daily Liquidity		
Money Market Funds (Moody's rated Aaa)	$ 635	
Checking and Deposit Accounts (at P-1 rated bank)	-	
Repurchase Agreements	-	
U.S. Treasuries & Aaa-rated Agencies	238	
Dedicated Bank Lines	931	
Subtotal Daily Liquidity (Cash & Securities)	$ 1,804	
Undrawn Portion of $600M Taxable Commercial Paper Program	360	
Subtotal Daily Liquidity Including Taxable Commercial Paper Program		$ 2,164
Weekly Liquidity		
Exchange Traded Equity	$ 807	
Publicly Traded Fixed Income Securities Rated at least Aa3 and Bond Funds	655	
Equity Funds	951	
Other	382	
Subtotal Weekly Liquidity		2,795
TOTAL DAILY AND WEEKLY LIQUIDITY		$ 4,960
Longer Term Liquidity		
Funds, vehicles, investments that allow withdrawals with less than one month notice	557	
Funds, vehicles, investments that allow withdrawals with one month notice or longer	2,399	
Total Longer Term Liquidity		$ 2,955
LIABILITIES (Self-liquidity Variable Rate Demand Bonds & Commercial Paper)		
Weekly Put Bonds		
VRDO Bonds (7-day)		$ 380
Long-Mode Put Bonds		
VRDO Bonds (Commerical Paper Mode)		442
Taxable Commercial Paper Outstanding		240
TOTAL SELF-LIQUIDITY DEBT AND COMMERCIAL PAPER		$ 1,062

Trinity Health
Financial Ratios and Statistics (Unaudited)

	September 30, 2014	September 30, 2013
<u>Financial Indicators</u>		
Liquidity Ratios (at September 30)		
Days Cash on Hand	200	203
Days in Accounts Receivable, Net	45	45
Leverage Ratios (at September 30)		
Debt to Capitalization	33%	34%
Cash to Debt	137%	137%
Profitability Ratios Before Other Items (For the Three Months Ended September 30)		
Operating Margin	2.8%	2.1%
Operating Cash Flow Margin	9.1%	8.6%
<u>Statistical Indicators (For the Three Months Ended September 30)</u>		
Discharges	129,000	128,000
Patient Days	593,000	592,000
Outpatient Visits	3,574,000	3,383,000
Emergency Room Visits	546,000	522,000
<u>Continuing Care</u>		
Home Health Visits	428,000	404,000
Long-term Care Patient Days	300,000	308,000