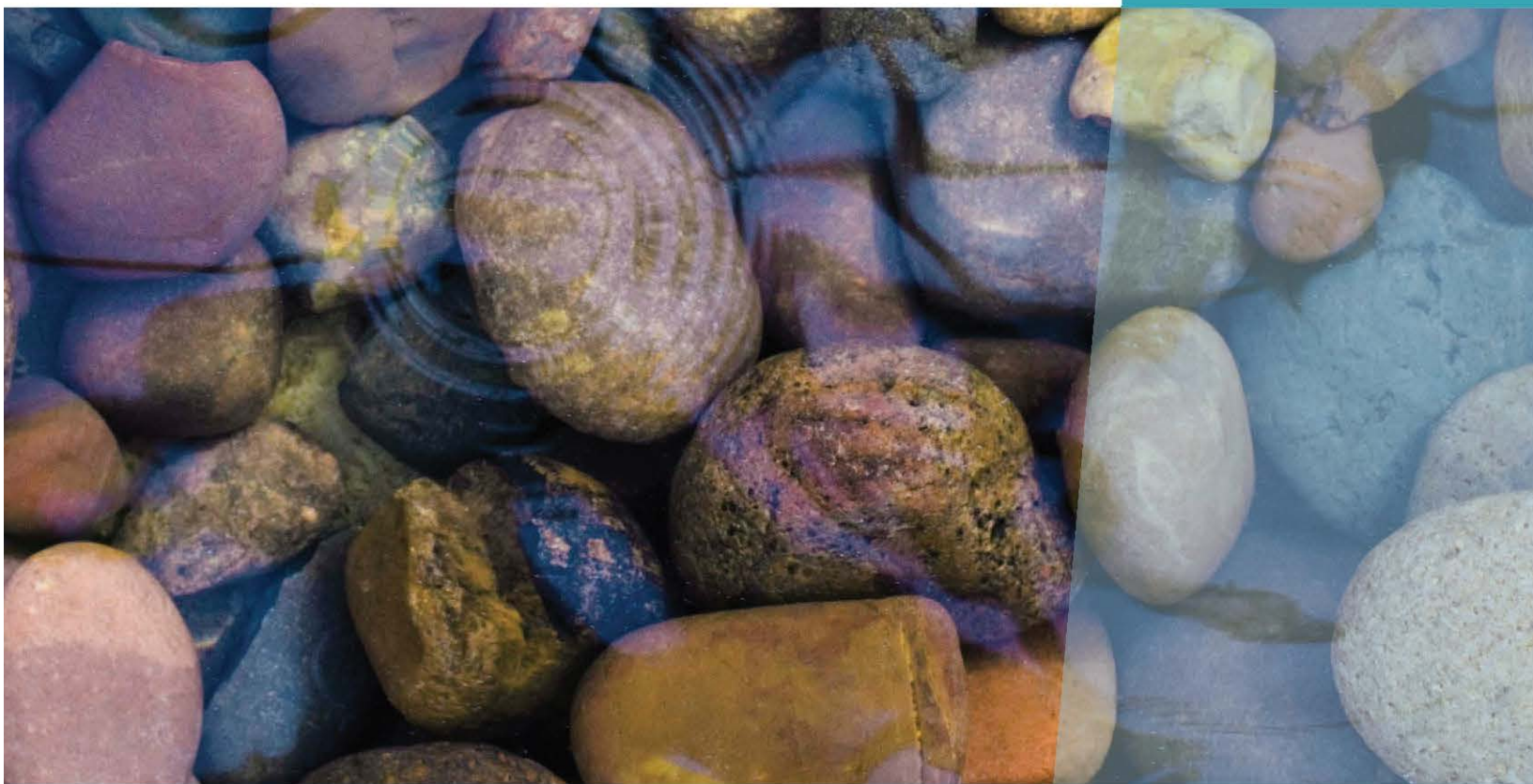


## Quarterly Report

As of March 31, 2017 and for the  
three and nine months ended  
March 31, 2017 and 2016



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*This Quarterly Report should be reviewed in conjunction with the information contained in the Annual Report dated November 23, 2016 (the "Annual Report"), which can be found on <http://emma.msrb.org>.*

*Certain of the discussions included in this Quarterly Report may include forward-looking statements. Such statements are generally identifiable by the terminology used such as "believes," "anticipates," "intends," "scheduled," "plans," "expects," "estimates," "budget" or other similar words. Such forward-looking statements are primarily included in PARTS III, IV and V. These statements reflect the current views of management with respect to future events based on certain assumptions, and are subject to risks and uncertainties. Catholic Health Initiatives, a Colorado non-profit corporation (the "Corporation"), undertakes no obligation to publicly update or review any forward-looking statement as a result of new information or future events.*

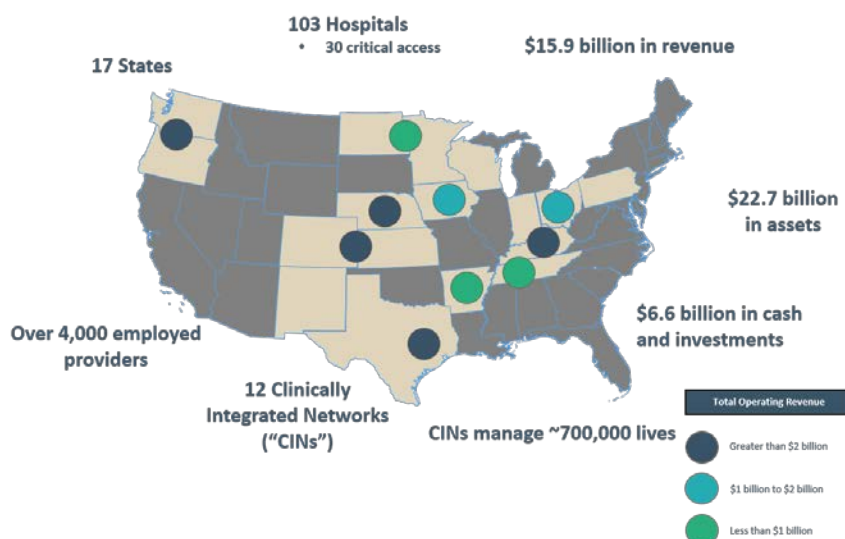
*References to "CHI" in this Quarterly Report are to the Corporation and all of the affiliates and subsidiaries ("Participants") consolidated with it pursuant to generally accepted accounting principles ("GAAP"). References to the Corporation are references only to the parent corporation, and should not be read to include any of the Participants.*

## PART I: OVERVIEW

The Corporation is the parent corporation of a group of non-profit and for profit corporations and other organizations that comprise one of the nation's largest Catholic health care systems. Together with its Participants (collectively, "CHI"), the Corporation serves more than four million people each year through operations and facilities that span the continuum of care, including acute care hospitals; physician practices; long-term care facilities; assisted-living and residential-living facilities; community-based health services; home care; research and development; medical and nursing education; reference laboratory services; virtual health services; managed care programs; and insurance products.

CHI was formed in 1996 through the consolidation of four national Catholic health care systems. The goal of the consolidation was to develop and nurture a national health ministry sponsored and governed by a religious-lay partnership to transform health care delivery and to build healthy communities through the creation of new ministries across the nation. In doing so, the founders created a new model of sponsorship by engaging the laity as partners in bringing their shared mission of nurturing the healing ministry of the church. Today, CHI has operations in 17 states, with a service area that covers approximately 54 million people, or approximately 17% of the U.S. population.

CHI is currently comprised of ten regions that are operated as integrated health systems and include five joint operating agreements ("JOAs"), joint operating companies ("JOs") or joint ventures. The geographic diversity and total operating revenues by region for the fiscal year ended June 30, 2016 are depicted in the accompanying map.



## ***PART II: CHI LEADERSHIP CHANGES***

Anthony K. Jones, FACHE, has been named interim Executive Vice President of Operations, effective December 5, 2016, replacing Michael T. Rowan, President, Health System Delivery and Chief Operating Officer who departed CHI effective December 31, 2016. Mr. Jones currently serves as president and CEO of Alliance Partners, Los Angeles, CA, a health care management and consulting company specializing in operations management, strategic planning and

financial management for hospitals and health care organizations. He has served as interim CEO for both SUNY University Hospital of Brooklyn, NY, and for Tulare Healthcare District and Regional Medical Center in Tulare, CA, during financial turnarounds. In addition, Mr. Jones has been an executive consultant with KPMG/Beacon Partners, Boston, MA, and has served as interim President/CEO leading several hospitals through financial and operational turnarounds.

## ***PART III: STRATEGIC AFFILIATIONS/ACQUISITIONS***

CHI actively engages in ongoing monitoring and evaluation of potential facility expansion, relationships with academic health center partners, mergers, acquisitions, divestitures, and affiliation opportunities consistent with its strategic goal of creating, maintaining and/or strengthening its CINs in key

existing markets and, in certain cases, new markets. CHI's strategic vision is supported by targeted system growth in both existing and new markets, as evidenced by CHI's recent acquisition activity and strategic divestitures, and realignments, certain of which are described below.

### **Pending and Completed Affiliations/Acquisitions**

**Dignity Health, (California, Arizona and Nevada) ("Dignity").** On October 24, 2016, CHI and Dignity signed a non-binding letter of intent to explore aligning their organizations and expanding their mission of service in communities across the nation.

The boards and sponsors of the two health systems are evaluating the potential alignment to strengthen their leadership role in transforming health care through increased access and enhanced clinical excellence.

The letter of intent follows the September 2016 announcement that the two systems formed a partnership called the Precision Medicine Alliance LLC, which will create the largest community-based precision medicine program in the country.

The organizations complement one another in many other important ways. CHI brings a diverse geographic footprint with proven clinical service lines and home health capabilities, as well as successful partnerships in research and education. Dignity has an operating model that has scaled enterprise-wide initiatives to ensure consistent practices across the system, and is

well known for its work with innovative, diversified care-delivery partnerships. There is no geographical overlap of acute care facilities of the two health systems.

Dignity owns and operates health care facilities in California, Arizona and Nevada, including 39 hospitals. As of and for the fiscal year ended June 30, 2016, Dignity reported approximately \$17.1 billion of total assets, \$6.2 billion of net assets and \$12.6 billion in total operating revenue. Any definitive agreement would need to be approved by Dignity's governing body and both organizations' Boards, and also requires the approval by the California Attorney General and other regulatory agencies as well as satisfaction of customary closing conditions. CHI can give no assurance that the transaction will occur.

**Virginia Mason (Washington)** In March 2017, CHI Franciscan Health and Virginia Mason Medical Center, a nonprofit health system based in Seattle that includes 336 licensed-bed Virginia Mason Hospital, primary and special care group practices and regional medical

centers, agreed to a clinical partnership and strategic affiliation, pursuant to which they are jointly exploring several opportunities where they believe that their collaboration will benefit communities throughout the Puget Sound area. Possibilities that will be evaluated over the next several months include developing shared centers of excellence for key clinical service lines; examining ways to further improve health care delivery in various communities that both organizations presently serve; and seeking to establish ways to offer greater continuity of care for patients around the region who need services. The organizations also plan to explore jointly offering new programs to new markets in the greater Puget Sound region. In February 2017, Virginia Mason also joined the CHI Franciscan Health accountable care organization.

**Texas Physician Practice.** In November 2016, a subsidiary of CHI acquired a multi-specialty group in the state of Texas. The operations include a general acute care hospital and emergency room, an ambulatory surgery center, a management company, and an independent physician association comprising more than 80 health care providers (59 physicians).

For the three and nine months ended March 31, 2017, the affiliations and acquisitions reported a combined \$18.8 million and \$33.6 million in operating revenues, respectively, and \$(10.6) million and \$(9.5) million in deficit of revenues over expenses, respectively, in the CHI consolidated results of operations.

**Mercy Health Network, Inc. (Iowa).** Effective March 1, 2016, the Corporation and Trinity Health Corporation, based in Livonia, Michigan (“THC”), amended and restated their existing Mercy Health Network Inc. (“MHN”) joint operating agreement that governs certain of their respective legacy operations in Iowa (collectively, the “Iowa Operations”) to (a) strengthen MHN’s management responsibilities over the Iowa Operations; (b) jointly acquire health care systems in Iowa and contiguous markets; and (c) provide for greater financial, governance, and clinical integration among the parties. Each of the respective party’s wholly-owned Iowa assets will continue to be consolidated in their respective financial statements, and commencing in July 2016, combined free cash flow from the Iowa Operations will be allocated equally between CHI and THC. MHN’s financial results,

including any subsidiaries of MHN, however, are not and will not be consolidated with either CHI or THC. CHI’s ownership interest in MHN is reflected as an investment in equity of unconsolidated organizations in its consolidated financial statements.

Effective May 1, 2016, MHN became the sole corporate member of Wheaton Franciscan Healthcare-Iowa, which is a faith-based 511-bed non-profit, comprehensive medical/surgical health care provider offering acute levels of medical care at Covenant Medical Center, Waterloo; Sartori Memorial Hospital, Cedar Falls and Mercy Hospital, Oelwein.

**Brazosport (Texas).** Effective February 1, 2016, Brazosport Regional Health System (“BRHS”), Lake Jackson, Texas and CHI St. Luke’s, Houston, Texas, signed an affiliation agreement for BRHS to become part of CHI. Pursuant to the affiliation agreement, CHI St. Luke’s became the sole corporate member of BRHS. BRHS is a non-profit health care organization that includes a 158-bed hospital that operates the only Level III trauma center in Brazoria County.

As a result of the BRHS acquisition, CHI reported approximately \$21.3 million in additional total unrestricted net assets in fiscal year 2016, as well as a total par value of long-term indebtedness outstanding of approximately \$36 million (the “BRHS Debt”). In May 2017, the total par value of the BRHS Debt in the amount of approximately \$36 million was defeased.

Excluding business combination gains, for the three months ended March 31, 2017, and for the period from February 1, 2016 through March 31, 2016, BRHS reported \$19.1 and \$14.1 million in operating revenues, respectively, and \$(2.1) and \$0.1 million of (deficit)/excess of revenues over expenses, respectively, in the CHI consolidated results of operations. For the nine months ended March 31, 2017, BRHS reported \$58.5 million in operating revenues and \$(5.9) million of deficit of revenues over expenses in the CHI consolidated results of operations.

**Trinity Health System (Ohio).** Effective February 1, 2016, the Corporation assumed control of Trinity Health System (“Trinity”) based in Steubenville, Ohio. Prior to that date, Trinity was controlled by its two corporate members, Sylvania Franciscan Health (“SFH”), a CHI subsidiary, and another entity unrelated to CHI and SFH.



In February 2016, CHI replaced that unrelated entity and became a corporate member of Trinity. Trinity owns and operates Trinity Medical Center East, Trinity Medical Center West, Tony Teramana Cancer Center and numerous outpatient clinics located in eastern Ohio.

As a result of the Trinity acquisition, CHI reported approximately \$145.1 million in additional total unrestricted net assets in fiscal year 2016, as well as total long-term indebtedness outstanding of \$40.1 million (the “Trinity Debt”). Neither the Corporation, SFH nor any their respective affiliates (other than Trinity and/or its affiliates) is obligated on the Trinity Debt as a result of the transaction.

Excluding business combination gains, for the three months ended March 31, 2017, and for the period from February 1, 2016 through March 31, 2016, Trinity reported \$60.7 and \$39.8 million in operating revenues, respectively, and \$10.5 and \$6.0 million of excess of revenues over expenses, respectively, in the CHI consolidated results of operations. For the nine months ended March 31, 2017, Trinity reported \$177.4 million in operating revenues and \$20.4 million of excess of revenues over expenses in the CHI consolidated results of operations.

**Longmont United Hospital (Colorado).** Effective August 1, 2015, Longmont United Hospital, a Colorado non-profit corporation (“LUH”) became affiliated with CHI pursuant to a Joint Operating and Management Agreement, between the Corporation, LUH, Centura Health and Catholic Health Initiatives Colorado. LUH

owns and operates Longmont United Hospital, a general acute care hospital licensed for 186 acute care beds and 15 skilled nursing beds, and operates an integrated health care delivery system providing health care services to patients residing in Longmont, Colorado, as well as Boulder, Weld and Larimer Counties in Colorado.

As a result of the LUH acquisition, CHI reported approximately \$111.6 million in additional total unrestricted net assets in fiscal year 2016, as well as total long-term indebtedness outstanding of \$97.8 million (the “LUH Debt”). In May 2016, CHI issued \$34.0 million of commercial paper notes, the proceeds of which were used to defease \$37.1 million of the LUH Debt. That commercial paper will be refinanced using a portion of the proceeds of the Bonds. Neither the Corporation nor any of its affiliates (other than LUH) is obligated on the remaining LUH Debt.

Excluding business combination gains, for the three months ended March 31, 2017 and 2016, LUH reported \$46.9 million and \$43.5 million in operating revenues, respectively, and \$(2.1) million and \$(1.7) million of deficit of revenues over expenses, respectively, in the CHI consolidated results of operations. For the nine months ended March 31, 2017, and for the period from August 1, 2015 through March 31, 2016, LUH reported \$135.6 million and \$116.0 million in operating revenues, respectively, and \$(11.6) million and \$(7.2) million of deficit of revenues over expenses, respectively, in the CHI consolidated results of operations.

## Pending and Completed Divestitures

**Pathology Associates Medical Laboratories, LLC (PAML)** - In February 2017, CHI entered into a definitive agreement with Laboratory Corporation of America Holdings (LabCorp) to sell all of CHI’s interests in PAML to LabCorp subject to regulatory approval. As part of the agreement, LabCorp will also acquire CHI’s direct and indirect interests in three CHI joint ventures with PAML in the states of Colorado, Kentucky and Washington. Regulatory approval was received and

non-refundable sales proceeds attributable to CHI and its affiliates of \$96.7 million were received in May 2017. The agreement will close in stages beginning in May 2017, and continuing through 2018.

**KentuckyOne Health** - In November 2012, KentuckyOne entered into a Joint Operating Agreement (“KY JOA”) and an Academic Affiliation Agreement (“AAA”) (collectively “Agreements”) with University of Louisville Medical Center (“UMC”), which owns the University of

Louisville Hospital, the University of Louisville (“U of L”), and other parties.

On December 17, 2016, KentuckyOne, UMC and U of L agreed to restructure their existing KY JOA. Under the terms of that agreement, the operations, management and control of UMC will be transferred back to the U of L effective July 1, 2017. Other provisions in the agreement call for a continued negotiation to restructure the AAA between HSC and KentuckyOne affiliates, Jewish Medical Center and the Frazier Rehab Institute, the development of various transition services agreements, and fulfillment of ongoing capital commitments.

For the nine months ended March 31, 2017, UMC reported total operating revenues of \$382.0 million and excess of revenues over expenses of \$13.1 million. The CHI consolidated balance sheets also included UMC total assets of \$543.3 million as of March 31, 2017. Upon the disposition described herein, CHI expects to incur a loss of approximately \$279.4 million.

In May 2017, CHI approved a plan to sell certain of the KentuckyOne operations located in Louisville, Kentucky. CHI will begin to market the sale of these operations and anticipates to close on a sale by the end of the calendar year.

Estimated results for the KentuckyOne operations being divested were as follows: For the three months ended March 31, 2017 and 2016, total operating revenues of \$231.0 million and \$221.3 million, respectively, and a deficit of revenues over expenses of \$(12.7) million and \$(23.8) million, respectively. For the nine months ended March 31, 2017 and 2016, total operating revenues of \$679.0 million and \$661.5 million, respectively, and a deficit of revenues over expenses of \$(61.0) million and \$(72.0) million, respectively. The CHI consolidated balance sheets also included estimated total assets for the KentuckyOne operations being divested of \$534.9 million and \$485.5 million as of March 31, 2017 and June 30, 2016.

**QualChoice.** As a part of the performance improvement efforts described in *Part IV B, Transformative Change Sharpens Focus* in the Annual Report, CHI approved, in May 2016, a plan to sell or otherwise dispose of certain entities of QualChoice, a consolidated CHI subsidiary, whose primary business is to develop, manage and market commercial and Medicare Advantage health

insurance programs, as well as a wide range of products and administrative services (see *Part IV A* in the Annual Report for further information). QualChoice reported a deficiency of revenues over expenses of \$(30.9) million for the nine months ended March 31, 2017, which is reported in the accompanying CHI consolidated statements of changes in net assets.

**Real Estate Asset Sale.** In April 2016, CHI entered into an agreement to sell certain real estate assets as part of a long-term effort to improve the mix of owned and leased real estate. The sale of the majority of that real estate portfolio closed in fiscal year 2016 for gross proceeds of \$601.7 million and a total net book value of \$323.3 million. As a result of those fiscal year 2016 real estate sales, CHI recognized a \$59.4 million gain on sale (net of commission and closing costs) in the consolidated statements of operations for the year ended June 30, 2016, as well as \$20.1 million in short-term deferred gains reported in accrued expenses and \$180.6 million in long-term deferred gains reported in other long-term liabilities reflected on the consolidated balance sheet as of June 30, 2016. The deferred gains are being amortized as a reduction of lease expense over the life of the operating leases. In conjunction with the sales, CHI entered into 10-year operating lease agreements with the buyer, with a base rent of approximately \$40.1 million in the first year, increasing 2.5% annually thereafter.

During the nine months ended March 31, 2017, CHI sold certain additional real estate assets and entered into multi-year operating lease agreements with the buyers. Those assets were sold for gross proceeds of \$247.7 million and had a total net book value of \$216.9 million. That sale resulted in the recognition of a \$20.1 million gain on sale reported in the consolidated statements of operations and \$11.0 million in long-term deferred gains and \$1.2 million in short-term deferred gains reported in other long-term liabilities and accrued expenses, respectively, on the consolidated balance sheet as of March 31, 2017. In conjunction with the sales, CHI entered into 10 year operating lease agreements with the buyer, with a base rent of approximately \$12.6 million in the first year, increasing 2.5 – 3.0% annually thereafter.

CHI expects to close on the sale of certain additional real estate assets by June 30, 2017, with gross proceeds of approximately \$175 million.

## Change in Composition of Credit Group

**Bethesda Hospital, Inc.** In 2001, Bethesda Hospital, Inc. (“Bethesda”) became a member of the CHI Credit Group as a Designated Affiliate. Bethesda and The Good Samaritan Hospital of Cincinnati, Ohio, an affiliate of the Corporation, are jointly operated pursuant to a JOA between Bethesda, Inc. and the Corporation. The Corporation previously loaned funds to Bethesda pursuant to its loan program, and the proceeds of a portion of the Corporation’s existing debt was used to finance Bethesda’s assets. In February 2017, Bethesda provided \$139.7 million to the Corporation as repayment for its loans, and Bethesda is no longer a

Designated Affiliate.

In February and March 2016, the Corporation prepaid, redeemed or defeased, as applicable, all outstanding CHI debt related to Bethesda’s assets, in the approximate principal amount of \$130.0 million.

The Good Samaritan Hospital of Cincinnati, Ohio remains a Participant under the Capital Obligation Document, and the JOA remains in effect. The financial statements of the Good Samaritan Hospital of Cincinnati, Ohio continue to be included in the CHI consolidated financial statements.

## PART IV: SELECTED FINANCIAL DATA

The selected financial data that follows has been prepared by management, based on CHI’s unaudited interim financial statements as of March 31, 2017 and for the three and nine month periods ended March 31, 2017 and 2016. The financial statements include all adjustments consisting of normal recurring accruals, which management of CHI considers necessary for a fair presentation of the combined financial position and results of operations for these periods. The unaudited interim financial statements for the three and nine months ended March 31, 2017 and 2016 are not necessarily indicative of the results that may be expected for the full fiscal year ending June 30, 2017.

The CHI consolidated financial information should be read in conjunction with the unaudited financial statements, related notes, and other financial information of CHI included in Appendix A of this Quarterly Report.

The results of operations for recently acquired entities that have been accounted for as acquisitions are included in the CHI consolidated financial and operating information from the respective dates of acquisition.

CHI participates in JOAs with hospital-based organizations in Colorado, Iowa and Ohio. The agreements generally provide for, among other things, joint management of the combined operations of the local facilities included in the JOAs through JOCs. CHI retains ownership of the assets, liabilities, equity, revenues and expenses of the CHI facilities that participate in the JOAs. Transfers of assets from facilities owned by the JOA participants are generally restricted under the terms of the agreements. The financial statements of the CHI facilities managed under all JOAs are included in the CHI consolidated financial statements.

As of March 31, 2017, CHI has investment interests of 65%, 50%, and 50% in JOCs based in Colorado, Iowa, and Ohio, respectively. CHI’s interests in the JOCs are included in investments in unconsolidated organizations and totaled \$379.9 million at March 31, 2017. CHI recognizes its investment in all JOCs under the equity method of accounting. The JOCs provide various levels of services to the related JOA sponsors, and operating expenses of the JOCs are allocated to each sponsoring organization.



**A. The following table provides condensed consolidated balance sheets for CHI as of March 31, 2017, and June 30, 2016.**

CHI Condensed Consolidated Balance Sheets	March 31, 2017 (Unaudited)	June 30, 2016
	(in Thousands)	
<b>Assets</b>		
Current assets:		
Cash and equivalents	\$ 918,285	\$ 1,305,242
Net patient accounts receivable	2,292,584	2,161,237
Assets held for sale	190,363	223,285
Other current assets	761,773	786,455
Total current assets	4,163,005	4,476,219
Investments and assets limited as to use:		
Internally designated investments	5,336,171	5,338,803
Restricted investments	1,193,468	1,219,232
Total investments and assets limited as to use	6,529,639	6,558,035
Property and equipment, net	9,037,708	9,452,010
Other assets	2,047,109	2,172,866
Total assets	\$ 21,777,461	\$ 22,659,130
<b>Liabilities and net assets</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 2,114,079	\$ 2,578,324
Liabilities held for sale	117,076	131,814
Short-term and current portion of debt	2,088,814	1,866,090
Total current liabilities	4,319,969	4,576,228
Other liabilities	3,227,743	3,444,622
Long-term debt	6,717,162	7,191,184
Total liabilities	14,264,874	15,212,034
Net assets:		
Unrestricted	7,189,674	7,127,641
Temporarily restricted	226,391	224,524
Permanently restricted	96,522	94,931
Total net assets	7,512,587	7,447,096
Total liabilities and net assets	\$ 21,777,461	\$ 22,659,130

**B. The following table presents condensed consolidated statements of operations for CHI for the three and nine month periods ended March 31, 2017 and 2016.**

CHI Condensed Consolidated Statements of Operations	Three Months Ended March 31,		Nine Months Ended March 31,	
	2017 (Unaudited)	2016 (Unaudited)	2017 (Unaudited)	2016 (Unaudited)
<b>Revenues</b>	(in Thousands)			
Net patient services revenues	\$ 3,845,064	\$ 3,717,738	\$ 11,415,994	\$ 10,914,359
Business combination gains	-	94,174	-	235,842
Other	324,698	243,959	817,031	718,319
Total operating revenues	4,169,762	4,055,871	12,233,025	11,868,520
<b>Expenses</b>				
Salaries and employee benefits	1,975,613	1,968,911	5,983,154	5,727,253
Supplies, purchased services and other	1,868,750	1,816,978	5,592,401	5,356,934
Depreciation and amortization	221,483	215,778	657,529	648,562
Interest	78,418	77,689	231,535	224,355
Total operating expenses before restructuring, impairment and other losses	4,144,264	4,079,356	12,464,619	11,957,104
Income (loss) from operations before restructuring, impairment and other losses	25,498	(23,485)	(231,594)	(88,584)
Restructuring, impairment and other losses	65,601	58,142	192,217	99,435
<b>Loss from operations</b>	(40,103)	(81,627)	(423,811)	(188,019)
Nonoperating gains (losses)	197,580	(66,986)	538,990	(293,307)
<b>Excess (deficit) of revenues over expenses</b>	\$ 157,477	\$ (148,613)	\$ 115,179	\$ (481,326)

## 1. CRITICAL ACCOUNTING POLICIES

The preparation of financial statements in conformity with GAAP requires that management make assumptions, estimates and judgments affecting the amounts reported in the financial statements, including the notes thereto, and related disclosures of commitments and contingencies, if any. Management considers critical accounting policies to be those that require more significant judgments and estimates in the preparation of its financial statements, including the following: recognition of net patient service revenues, which includes contractual allowances, bad debt and charity care reserves; cost report settlements;

impairment of goodwill, intangibles and long-lived assets; provisions for bad debt; valuations of investments; and reserves for losses and expenses related to health care professional and general liability risks. In making such judgments and estimates, management relies on historical experience and on other assumptions believed to be reasonable under the circumstances. Actual results could differ materially from the estimates. A description of CHI's significant accounting policies can be found in Note 1 of the CHI unaudited interim financial statements included in Appendix A of this Quarterly Report.

# PART V: MANAGEMENT'S DISCUSSION AND ANALYSIS

The following table provides key balance sheet metrics for CHI as of March 31, 2017 and June 30, 2016.

CHI Key Balance Sheet Metrics	March 31, 2017 (Unaudited)	June 30, 2016
<b><u>Consolidated Balance Sheet Summary</u></b>		
Total assets	\$ 21.8 billion	\$ 22.6 billion
Total liabilities	\$ 14.3 billion	\$ 15.2 billion
Total net assets	\$ 7.5 billion	\$ 7.4 billion
<b><u>Financial Position and Leverage Ratios (Unaudited)</u></b>		
Total cash and unrestricted investments	\$ 6.3 billion	\$ 6.6 billion
Days of cash on hand <sup>1</sup>	145	159
Total debt	\$ 8.8 billion	\$ 9.1 billion
Debt to capitalization <sup>2</sup>	55.1%	56.0%

<sup>1</sup> (Cash and equivalents + Investments and assets limited as to use: Internally designated investments)/((Total operating expenses before restructuring, impairment and other losses last twelve months - Depreciation and amortization last twelve months)/365). For the days of cash on hand last twelve months one day of operating expenses represented \$43.0 million and \$41.7 million at March 31, 2017 and June 30, 2016, respectively.

<sup>2</sup> (Short-term and current portion of debt + Long-term debt)/(Short-term and current portion of debt + Long-term debt + Unrestricted net assets).

***The following table presents key operating metrics and utilization statistics for CHI for the three and nine months ended March 31, 2017 and 2016.***

CHI Key Operating Metrics and Utilization Statistics	Three Months Ended March 31,		Nine Months Ended March 31,	
	2017 (Unaudited)	2016 (Unaudited)	2017 (Unaudited)	2016 (Unaudited)

**Consolidated Revenues, Expenses and Key Operating Metrics\***

Total net patient services revenues	\$ 3.8 billion	\$ 3.7 billion	\$ 11.4 billion	\$ 10.9 billion
Total operating revenues	\$ 4.2 billion	\$ 4.1 billion	\$ 12.2 billion	\$ 11.9 billion
Total operating expenses before restructuring, impairment and other losses	\$ 4.1 billion	\$ 4.1 billion	\$ 12.5 billion	\$ 12.0 billion
Operating EBIDA before restructuring, impairment and other losses <sup>1</sup>	\$ 325.4 million	\$ 270.0 million	\$ 657.5 million	\$ 784.3 million
Operating EBIDA margin before restructuring, impairment and other losses <sup>2</sup>	7.8%	6.7%	5.4%	6.6%
Operating income (loss) before restructuring, impairment and other losses	\$ 25.5 million	\$ (23.5) million	\$ (231.6) million	\$ (88.6) million
Operating income (loss) margin before restructuring, impairment and other losses <sup>3</sup>	0.6%	(0.6)%	(1.9)%	(0.7)%
Operating EBIDA <sup>4</sup>	\$ 259.8 million	\$ 211.8 million	\$ 465.3 million	\$ 684.9 million
Operating EBIDA margin <sup>5</sup>	6.2%	5.2%	3.8%	5.8%
Operating loss	\$ (40.1) million	\$ (81.6) million	\$ (423.8) million	\$ (188.0) million
Operating loss margin <sup>6</sup>	(1.0)%	(2.0)%	(3.5)%	(1.6)%

**Utilization Statistics**

Acute admissions	136,115	134,495	401,050	392,191
Acute inpatient days	654,628	655,859	1,909,808	1,892,693
Acute average length of stay in days	4.8	4.9	4.8	4.8
Long-term care days	119,533	125,272	366,183	375,571
Medicare case-mix index	1.8	1.8	1.8	1.8
Adjusted admissions <sup>7</sup>	295,955	286,296	880,180	838,416
Inpatient ER visits	76,309	75,209	220,558	212,875
Inpatient surgeries	40,900	41,165	123,844	123,245
Outpatient ER visits	538,293	530,912	1,601,867	1,564,896
Outpatient non-ER visits	1,526,097	1,494,760	4,602,140	4,352,702
Outpatient surgeries	67,278	65,319	206,555	194,180
Physician visits	2,895,774	2,712,576	8,338,587	7,683,779

\* Includes business combination gains.

<sup>1</sup> Income (loss) from operations before restructuring, impairment and other losses + depreciation and amortization + interest.

<sup>2</sup> Income (loss) from operations before restructuring, impairment and other losses + depreciation and amortization + interest/total operating revenues.

<sup>3</sup> Income (loss) from operations before restructuring, impairment and other losses/total operating revenues.

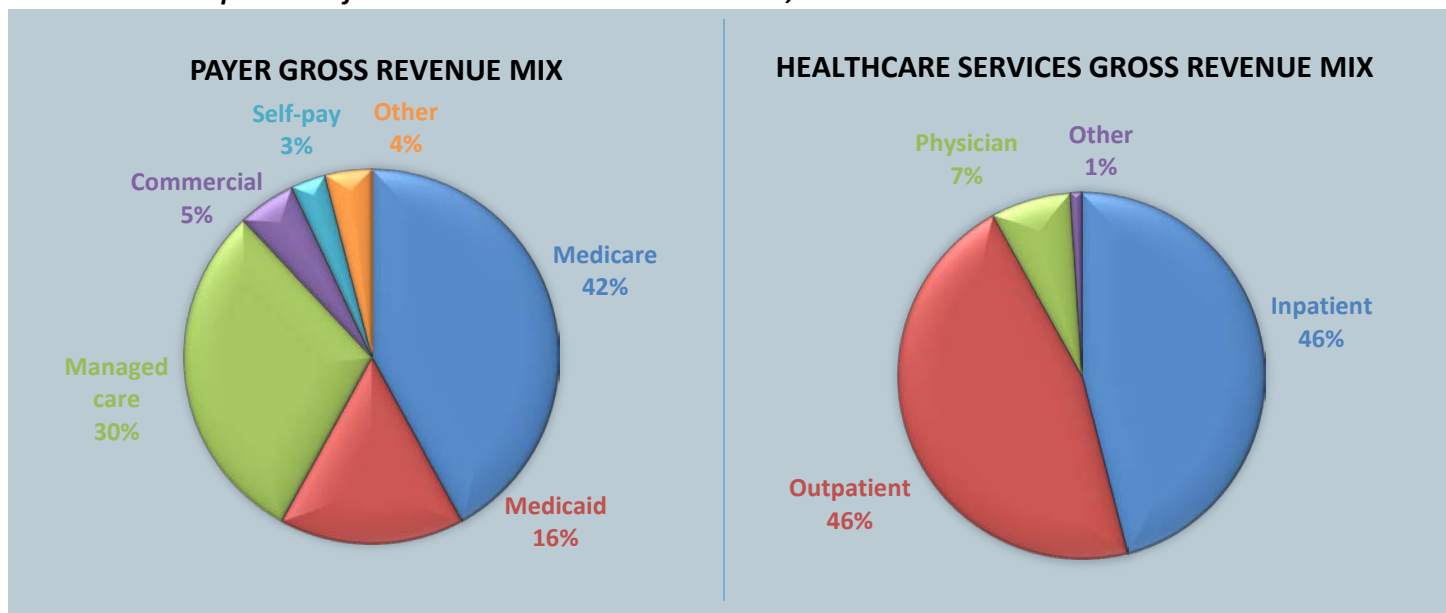
<sup>4</sup> Income (loss) from operations + depreciation and amortization + interest.

<sup>5</sup> Income (loss) from operations + depreciation and amortization + interest/total operating revenues.

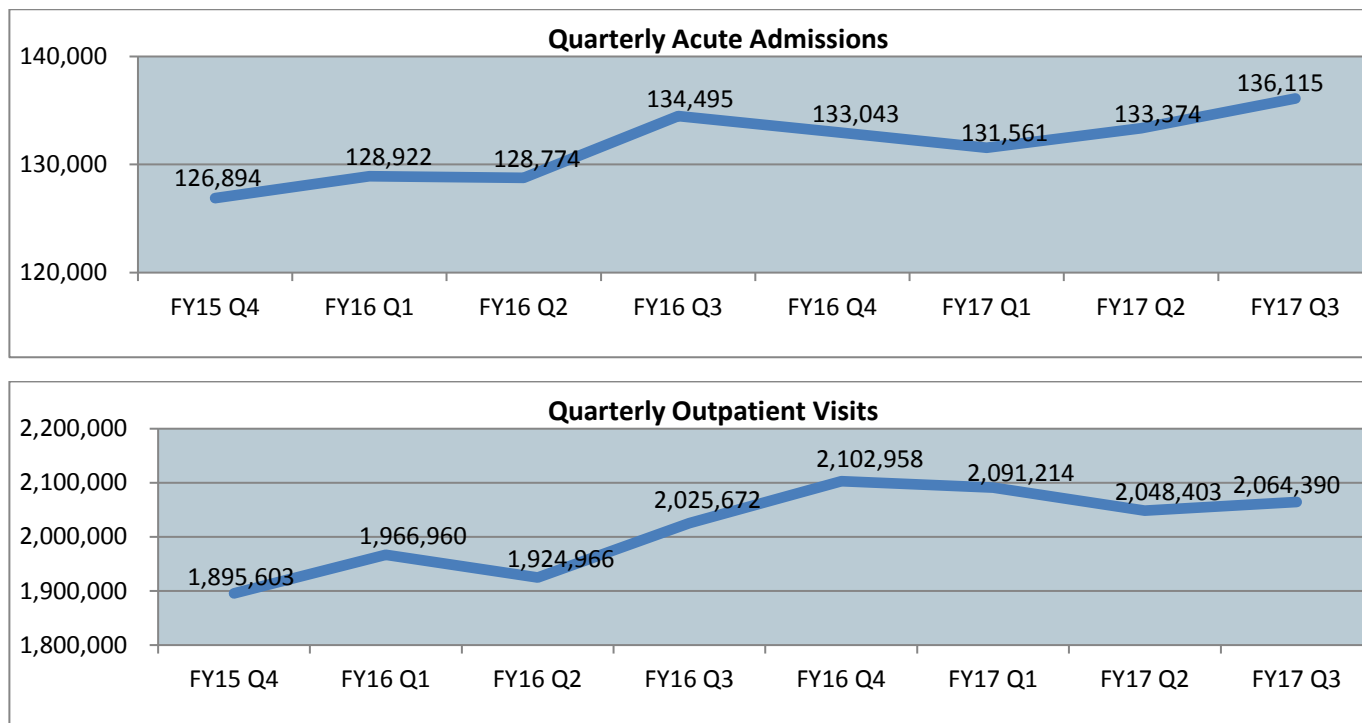
<sup>6</sup> Income (loss) from operations/total operating revenues.

<sup>7</sup> (Total gross patient revenues/total gross inpatient revenues) x acute admissions.

The following charts represent the payer gross revenue mix and healthcare services gross revenue mix for CHI's consolidated operations for the nine months ended March 31, 2017.



The following charts represent quarterly patient volume activity for CHI's consolidated operations over the previous eight quarters and includes the effects of acquisitions.





# **1. SUMMARY OF OPERATING RESULTS FOR THE THREE MONTHS ENDED MARCH 31, 2017 AND 2016**

## **OPERATING EBIDA/LOSS FROM OPERATIONS**

CHI operating EBIDA before restructuring, impairment and other losses totaled \$325.4 million and \$270.0 million for the three months ended March 31, 2017 and 2016, respectively, equivalent to an operating EBIDA margin before restructuring, impairment and other losses percentage of 7.8% and 6.7%, respectively. Excluding the prior year \$94.2 million in business combination gains, CHI's operating EBIDA before restructuring, impairment and other losses increased \$149.6 million compared to the same period in the prior fiscal year. Results for the three months ended March 31, 2017 included \$85.7 million of net gains in the Pacific Northwest region primarily from the sale of certain outpatient ambulatory business lines, and \$10.2 million of gains on asset sales in the Texas region. CHI experienced overall increases in net patient services revenues as a result of strategic affiliation growth, increased patient volumes, and increased acuity, somewhat offset by unfavorable shifts in payer mix. Overall revenue improvements were offset by increases in compensation, purchased services and supplies costs. Current year results have improved from an operating EBIDA in the first fiscal quarter of \$122.0 million or 3.1%, to \$210.1 million or 5.1% in the second fiscal quarter, and \$325.4 million or 7.8% in the third fiscal quarter.

CHI income (loss) from operations before restructuring, impairment and other losses totaled \$25.5 million and \$(23.5) million for the three months ended March 31, 2017 and 2016, respectively, or an operating income (loss) margin before restructuring, impairment and other losses percentage of 0.6% and (0.6)%, respectively. The strategic affiliations completed in fiscal years 2017 and 2016 contributed operating revenues of \$158.0 million and \$107.1 million, operating EBIDA before restructuring, impairment and

other losses of \$(1.0) million and \$3.4 million, and loss from operations before restructuring, impairment and other losses of \$(10.1) million and \$(3.8) million, for the three months ended March 31, 2017 and 2016, respectively, all excluding business combination gains.

CHI's regional operations were mixed, but several markets reported improved patient volume trends and decreased total compensation expense as a percentage of net patient service revenues. As compared to the prior three month period, operating EBIDA before restructuring, impairment and other losses in the Pacific Northwest, Ohio, Colorado, and Tennessee regions improved \$116.8 million for the three months ended March 31, 2017. However, operating EBIDA before restructuring, impairment and other losses in the Arkansas, Iowa, Texas, Nebraska, North Dakota/Minnesota and Kentucky regions decreased \$(36.2) million for the three months ended March 31, 2017, compared to the same period of the prior fiscal year. Overall operations were impacted by same store operating expense growth outpacing same store net patient services revenue growth, and unfavorable shifts in payer mix. As part of CHI's ongoing comprehensive expense reduction strategy, focused clinical and operational initiatives across the system continue to be implemented to include targeted initiatives at the regional levels, as well as at CHI's Corporate office.

The table below presents total operating EBIDA before restructuring, impairment and other losses, total operating EBIDA margin before restructuring, impairment and other losses and total operating revenues of CHI by region for the three months ended March 31, 2017 and 2016. Further information on CHI's regional operating results is discussed within the regional operating trends section below.

### Catholic Health Initiatives Operations Summary – Three Months Ended March 31, 2017 and 2016

Region	QTD 3/31/2017 Operating EBIDA before restructuring, impairment and other losses (in Thousands)	QTD 3/31/2016 Operating EBIDA before restructuring, impairment and other losses (in Thousands)	QTD 3/31/2017 Operating EBIDA margin before restructuring, impairment and other losses	QTD 3/31/2016 Operating EBIDA margin before restructuring, impairment and other losses	QTD 3/31/2017 Operating revenues percentage of CHI consolidated	QTD 3/31/2016 Operating revenues percentage of CHI consolidated
Colorado	\$ 72,042	\$ 64,049	11.9%	11.3%	14.5%	14.0%
Pacific Northwest <sup>1</sup>	147,551	58,696	19.4%	9.3%	18.2%	15.5%
Nebraska	35,528	38,551	6.9%	7.8%	12.4%	12.2%
Kentucky	20,034	22,314	3.3%	3.8%	14.5%	14.5%
Texas	39,998	46,019	7.2%	8.7%	13.3%	13.1%
Iowa	13,649	23,236	5.4%	9.2%	6.1%	6.2%
Ohio	26,368	14,407	10.1%	5.0%	6.2%	7.1%
Arkansas	(3,357)	9,092	(1.8)%	4.7%	4.5%	4.7%
Tennessee	18,337	10,376	10.8%	6.6%	4.1%	3.9%
North Dakota/Minnesota	10,997	13,855	5.8%	7.2%	4.6%	4.8%
National business lines <sup>2</sup>	6,856	3,604	9.8%	5.6%	1.7%	1.6%
Other <sup>3</sup>	(8,136)	(8,032)	N/A	N/A	(0.2)%	(0.2)%
Total Regional	379,867	296,167	9.1%	7.5%	99.9%	97.4%
Corporate services and other business lines <sup>4</sup>	(54,468)	(120,359)	N/A	N/A	0.1%	0.3%
Total CHI Consolidated before business combination gains	325,399	175,808	7.8%	4.4%	100.0%	97.7%
Business combination gains	-	94,174	N/A	N/A	0.0%	2.3%
Total CHI Consolidated	\$ 325,399	\$ 269,982	7.8%	6.7%	100.0%	100.0%

<sup>1</sup>Includes \$85.7 million net gain for the three months ended March 31, 2017, primarily from the sale of certain outpatient ambulatory business lines in the Pacific Northwest region.

<sup>2</sup>Includes Home Care and Senior Living business lines.

<sup>3</sup>Includes the operations of Albuquerque Health Ministries and Lancaster Health Ministries MBOs as well as regional eliminations.

<sup>4</sup>Includes CHI Corporate and First Initiatives Insurance, Ltd. ("FIIL"), CHI's wholly-owned captive insurance company as well as CHI system eliminations.

### OPERATING REVENUE AND VOLUME TRENDS

CHI total operating revenues increased 2.8%, or \$113.9 million, for the three months ended March 31, 2017 compared to the corresponding period of the prior fiscal year, and included \$111.9 million in gains on asset sales. Excluding the \$94.2 million of business combination gains reflected in the prior fiscal year, CHI total operating revenues increased 5.3%, or \$208.1 million. Excluding the impacts of current and prior year acquisitions (same store basis), CHI total operating revenues increased 4.1%, or \$157.0 million, for the three months ended March 31, 2017, compared to the corresponding period of the prior fiscal year.

CHI total net patient services revenues increased 3.4%, or \$127.3 million, for the three months ended March 31, 2017, compared to the corresponding period of the prior fiscal year, of which \$50.1 million was due to

recently completed acquisitions. CHI same store net patient services revenues increased 2.1%, or \$77.3 million, for the three months ended March 31, 2017 compared to the corresponding period of the prior fiscal year mostly due to overall increased patient volumes of \$48.8 million, favorable shifts in acuity of \$7.1 million, offset by unfavorable shifts in payer mix of \$(21.2) million.

CHI same store patient volumes increases (decreases) were as follows for the three months ended March 31, 2017, as compared to the corresponding period of the prior fiscal year.

Patient Volumes	Percentage Change	Volume Change
Adjusted Admissions	1.7%	4,648
Acute Admissions	0.3%	435
Acute Inpatient Days	(1.0)%	(6,260)
Inpatient ER Visits	1.3%	905
Inpatient Surgeries	(1.6)%	(665)
Outpatient ER Visits	(0.6)%	(2,960)
Outpatient Non-ER Visits	0.8%	11,441
Outpatient Surgeries	2.7%	1,736
Physician Visits	3.1%	83,499

## OPERATING EXPENSES

CHI total operating expenses before restructuring, impairment and other losses increased 1.6%, or \$64.9 million, for the three months ended March 31, 2017, as compared to the corresponding period of the prior fiscal year, of which \$57.2 million was due to recently completed acquisitions. CHI same store total operating expenses before restructuring, impairment and other losses increased 0.2%, or \$7.7 million, for the three months ended March 31, 2017, as compared to the corresponding period of the prior fiscal year, primarily due to reductions in total labor costs, combined with annual inflation increases in other operating expenses across CHI as described in more detail below.

CHI same store total labor costs decreased (1.0)%, or \$(19.2) million, for the three months ended March 31, 2017, as compared to the corresponding period of the prior fiscal year, due to \$(16.4) million in reduced rates primarily related to mix (0.9%), and \$(2.8) million in decreased FTEs as a result of labor productivity improvements. CHI same store total labor costs represented 47.6% and 48.2% of same store total operating expenses for the three months ended March 31, 2017 and 2016, respectively. CHI same store total labor costs as a percentage of net patient services revenues decreased to 51.3% for the three months ended March 31, 2017, compared to 52.9% for the corresponding period of the prior fiscal year. CHI continues to address labor productivity in certain regions, most notably in the Kentucky and Texas regions, as well as growth initiatives in certain physician practices where labor costs have been added in anticipation of future increased patient volumes. CHI is currently implementing several ongoing labor productivity improvement initiatives throughout CHI,

CHI total other operating revenues decreased (4.0)%, or \$(13.4) million, for the three months ended March 31, 2017, compared to the corresponding period of the prior fiscal year, due to the inclusion of \$94.2 million in business combination gains in the prior fiscal year. CHI same store total other operating revenues increased 33.3%, or \$79.8million, for the three months ended March 31, 2017, compared to the corresponding period of the prior fiscal year, primarily due to the current period gains on sale of business lines and asset sales discussed above.

with a particular focus on the Kentucky and Texas regions.

CHI same store purchased services expenses increased 1.1% or \$4.8 million, for the three months ended March 31, 2017, as compared to the corresponding period of the prior fiscal year, primarily as a result of general economic inflation.

CHI same store supplies expense increased 0.2% or \$1.3 million, for the three months ended March 31, 2017, as compared to the corresponding period of the prior year. Same store supplies as a percentage of net patient services revenues decreased to 18.2% for the three months ended March 31, 2017, compared to 18.6% in the same period of the prior fiscal year.

## REGIONAL OPERATING TRENDS

CHI periodically reviews its allocation methodology for Corporate support services and may adjust those allocations based on the strategic needs and resource consumption of the regions and CHI overall. These changes in allocation methodologies may increase or decrease a region's operating results from year to year, but have no impact on the consolidated results of CHI.

Operating results for the three months ended March 31, 2017 improved in the Pacific Northwest, Ohio, Colorado, and Tennessee regions, as well as within CHI Corporate services, but were offset slightly by declines in the remaining CHI regions compared to the corresponding period of the prior fiscal year. Although overall patient volumes trended up in the current fiscal year compared to the prior fiscal year, several regions have experienced decreases in patient volumes and unfavorable shifts in payer mix which have resulted in

decreased net patient revenue yields and increases in operating expenses outpacing overall net patient services revenue growth.

The Colorado, Pacific Northwest, Nebraska, Kentucky and Texas regions represent CHI's five largest operating regions, and for the three months ended March 31, 2017, represented 72.9% of CHI's consolidated operating revenues.

**Colorado** - the region's operating EBIDA before restructuring, impairment and other losses totaled \$72.0 million for the three months ended March 31, 2017, and increased \$8.0 million compared to the corresponding period of the prior fiscal year, due to increased patient volumes. Net patient services revenue increased \$31.4 million compared to the same period of the prior fiscal year, including \$11.2 million in increased patient volumes, and \$7.5 million in favorable shifts in acuity and service mix, compared to the same period of the prior fiscal year. The positive impacts were offset by a net unfavorable \$(9.6) million related to provider fee activity in the Colorado region, which included an \$(11.3) million decrease in provider fee revenue and a \$1.7 million decrease in provider fee expenses. The Colorado region is in the process of installing the Epic electronic health record system across its various hospitals, and for the three months ended March 31, 2017, Epic operating expenses and training costs were \$3.8 million higher, compared to the same period of the prior fiscal year. Total net revenue per adjusted admission increased 7.2% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 8.0%. Total labor as a percentage of net patient services revenue increased to 41.6% compared to 41.4% in the same period of the prior fiscal year, representing an unfavorable expense variance of \$(1.2) million.

**Pacific Northwest** - the region's operating EBIDA before restructuring, impairment and other losses totaled \$147.6 million for the three months ended March 31, 2017, an increase of \$88.9 million compared to the corresponding period of the prior fiscal year. Results for the three months ended March 31, 2017 included \$85.7 million of net gains in the Pacific Northwest region primarily from the sale of certain outpatient ambulatory business lines. The remainder of the region's favorable results were due to increases in non-

patient revenues of \$4.6 million, and to overall increased patient volumes combined with labor improvements. Net patient services revenue increased \$39.6 million, including \$22.3 million in patient volumes and \$4.6 million in greater acuity, and \$4.9 in improved service mix compared to the same period of the prior fiscal year. Operating expenses increased \$42.1 million compared to the corresponding period of the prior fiscal year, primarily due to increased volumes. Total net revenue per adjusted admission increased 7.6% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 8.0%. Total labor as a percentage of net patient services revenue decreased to 53.4% compared to 55.0% in the same period of the prior fiscal year as a result of ongoing labor productivity improvements, representing a favorable expense variance of \$10.2 million. Supply expense as a percentage of net patient services revenue declined to 14.4% compared to 14.7% in the prior fiscal year due to revenue growth and improved utilization.

**Nebraska** - the region's operating EBIDA before restructuring, impairment and other losses totaled \$35.5 million for the three months ended March 31, 2017, and decreased \$(3.0) million compared to the corresponding period of the prior fiscal year. Net patient services revenue increased \$23.5 million, including \$17.2 million in patient volumes and \$2.4 million in greater acuity. Total net revenue per adjusted admission increased 1.2% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 0.5%. Total labor as a percentage of net patient services revenue decreased to 55.5% compared to 57.3% in the same period of the prior fiscal year, representing a favorable expense variance of \$8.8 million. Total operating expenses increased 4.4%, or \$21.3 million in the Nebraska region for the three months ended March 31, 2017, primarily in the areas of total compensation, purchased services and supplies expenses, compared to the corresponding period of the prior fiscal year. Supply expense as a percentage of net patient service revenues increased to 18.0% compared to 17.0% in the prior fiscal year. Increases in utilization and cost are concentrated in pharmacy, cardiovascular and orthopedic/spine, and are a continued focus and opportunity for reduction.

**Kentucky** - the region's operating EBIDA before restructuring, impairment and other losses totaled \$20.0 million for the three months ended March 31, 2017, and decreased \$(2.3) million compared to the corresponding period of the prior fiscal year. Net patient services revenues increased \$17.9 million, for the three months ended March 31, 2017, including \$12.6 million in patient volumes offset by unfavorable shifts in payer mix of \$(6.9) million compared to the same period of the prior fiscal year. Total labor as a percentage of net patient services revenue decreased to 47.8% compared to 48.4% in the same period of the prior fiscal year, representing a favorable expense variance of \$3.4 million. The Kentucky region is continuing its efforts to address nursing and other staff shortages which have resulted in increases to overall labor costs, including contract labor costs, and overtime and premium pay.

**Texas** - the region's operating EBIDA before restructuring, impairment and other losses totaled \$40.0 million for the three months ended March 31, 2017, and decreased \$(6.0) million compared to the same period of the prior fiscal year, due to increased operating expenses outpacing net patient services revenue growth. Results for the three months ended March 31, 2017 included \$10.2 million in gains from asset sales in the Texas region. Net patient services revenue increased \$16.0 million, including \$26.6 million from several recently completed affiliations. Net patient services revenues were also impacted by unfavorable shift in payer mix of \$(11.4) million. Total labor as a percentage of net patient services revenue increased to 47.7% compared to 45.1% in the same period of the prior fiscal year. Same store operating expenses decreased (1.9)%, or \$(9.5) million in the Texas region for the three months ended March 31, 2017. Management is implementing strategies to improve labor productivity and supply chain savings in the Texas region, and is continuing to expand its referral base for additional growth in the region through acquiring and expanding the Texas physician enterprise in the greater Houston area.

**CHI Corporate services and other business lines** - operating EBIDA before restructuring, impairment and other losses totaled \$(54.5) million, representing an improvement of \$65.9 million for the three months ended March 31, 2017, compared to the corresponding period of the prior fiscal year. Changes in support services activities relate to a variety of factors, and include strategic transfers of certain activities from the markets and other service lines to the Corporate office in order to build Corporate support functions, and new implementations of system-wide services such as revenue cycle and food programs. Support services allocations to the regions consider the strategic needs and resource consumption of the regions and CHI overall. CHI has experienced a decline in overall information technology expense of \$11.6 million, and improved results on the self-insurance programs of \$18.5 million due to favorable claims experience.

#### **RESTRUCTURING, IMPAIRMENT AND OTHER LOSSES**

CHI restructuring, impairment and other losses totaled \$65.6 million and \$58.1 million for the three months ended March 31, 2017 and 2016, respectively. For the three months ended March 31, 2017 and 2016, restructuring, impairment and other losses expenses included \$12.2 million and \$32.4 million of goodwill and long-lived asset impairment charges, respectively, \$27.4 million and \$13.0 million of changes in business operations, respectively, and \$26.0 million and \$12.7 million of severance costs, respectively. CHI changes in business operations include contract termination costs, as well as ongoing reorganization efforts which include consulting costs related to revenue cycle, supply chain, and labor productivity.

#### **NON-OPERATING RESULTS**

CHI non-operating gains (losses) totaled \$197.6 million and \$(67.0) million for the three months ended March 31, 2017 and 2016, respectively. CHI investment gains were \$203.2 million and \$40.9 million for the three months ended March 31, 2017 and 2016, respectively, and realized and unrealized gains (losses) on interest rate swaps were \$0.8 and \$(64.6) million for the three months ended March 31, 2017 and 2016, respectively.



## **2. SUMMARY OF CHI OPERATING RESULTS FOR THE NINE MONTHS ENDED MARCH 31, 2017 AND 2016**

### **OPERATING EBIDA/INCOME (LOSS) FROM OPERATIONS**

CHI operating EBIDA before restructuring, impairment and other losses totaled \$657.5 million and \$784.3 million for the nine months ended March 31, 2017 and 2016, respectively, equivalent to an operating EBIDA margin before restructuring, impairment and other losses percentage of 5.4% and 6.6%, respectively. Excluding the prior year \$235.8 million in business combination gains, CHI's operating EBIDA before restructuring, impairment and other losses increased \$109.0 million compared to the same period in the prior fiscal year. Results for the nine months ended March 31, 2017 included \$85.7 million of net gains in the Pacific Northwest region primarily from the sale of certain outpatient ambulatory business lines and \$27.0 million of gains on asset sales in the Texas region, offset by \$(28.0) million of unfavorable net patient services revenues adjustments in the Nebraska region. CHI experienced overall increases in net patient services revenues as a result of strategic affiliation growth, increased patient volumes, and increased acuity, somewhat offset by unfavorable shifts in payer mix. Overall revenue improvements were offset by increases in compensation, purchased services and supplies costs.

CHI loss from operations before restructuring, impairment and other losses totaled \$(231.6) million and \$(88.6) million for the nine months ended March 31, 2017 and 2016, respectively, or an operating loss margin before restructuring, impairment and other losses percentage of (1.9)% and (0.7)%, respectively.

The strategic affiliations completed in fiscal years 2017 and 2016 contributed operating revenues of \$443.0 million and \$195.3 million, operating EBIDA before restructuring, impairment and other losses of \$5.4 million and \$4.5 million, and loss from operations before restructuring, impairment and other losses of \$(19.7) million and \$(10.7) million, for the nine months ended March 31, 2017 and 2016, respectively, all excluding business combination gains.

CHI's regional operations were mixed, but several markets reported improved patient volume trends and decreased total compensation expense as a percentage of net patient services revenues. As compared to the prior fiscal year-to-date, operating EBIDA before restructuring, impairment and other losses in the Pacific Northwest, Ohio and Tennessee regions improved \$154.2 million for the nine months ended March 31, 2017. However, operating EBIDA before restructuring, impairment and other losses in the Colorado, Kentucky, Texas, Nebraska, Iowa, Arkansas and North Dakota/Minnesota regions decreased \$(212.1) million for the nine months ended March 31, 2017, compared to the same period of the prior fiscal year. Overall operations were impacted by same store operating expense growth outpacing same store net patient services revenues growth, and unfavorable shifts in payer mix. As part of CHI's ongoing comprehensive expense reduction strategy, focused clinical and operational initiatives across the system continue to be implemented to include targeted initiatives at the regional levels, as well as at CHI's Corporate office.

The table below presents the total operating EBIDA before restructuring, total operating EBIDA margin before restructuring and total operating revenues of CHI by region for the nine months ended March 31, 2017 and 2016. Further information on CHI's regional operating results is discussed within the regional operating trends section below.

**Catholic Health Initiatives Operations Summary – Nine Months Ended March 31, 2017 and 2016**

Region	YTD 3/31/2017 Operating EBIDA before restructuring, impairment and other losses (\$ Thousands)	YTD 3/31/2016 Operating EBIDA before restructuring, impairment and other losses (\$ Thousands)	YTD 3/31/2017 Operating EBIDA margin before restructuring, impairment and other losses	YTD 3/31/2016 Operating EBIDA margin before restructuring, impairment and other losses	YTD 3/31/2017 Operating revenues percentage of CHI consolidated	YTD 3/31/2016 Operating revenues percentage of CHI consolidated
Colorado	\$ 179,135	\$ 188,540	10.3%	11.4%	14.2%	13.9%
Pacific Northwest <sup>1</sup>	284,996	171,242	13.7%	9.2%	17.0%	15.7%
Nebraska	75,223	125,478	4.9%	8.5%	12.4%	12.5%
Kentucky	31,670	87,264	1.8%	4.9%	14.6%	14.9%
Texas	62,827	113,769	3.9%	7.5%	13.2%	12.8%
Iowa	51,019	63,346	6.7%	8.4%	6.2%	6.3%
Ohio	72,043	42,621	8.3%	5.5%	7.1%	6.6%
Arkansas	8,916	30,848	1.6%	5.4%	4.7%	4.8%
Tennessee	47,226	36,161	9.6%	7.6%	4.0%	4.0%
North Dakota/Minnesota	36,912	48,558	6.5%	8.4%	4.7%	4.9%
National business lines <sup>2</sup>	16,220	10,428	7.8%	5.4%	1.7%	1.6%
Other <sup>3</sup>	(28,004)	(46,790)	N/A	N/A	(0.1)%	(0.2)%
Total Regional	838,183	871,465	6.9%	7.5%	99.7%	97.8%
Corporate services and other business lines <sup>4</sup>	(180,713)	(322,974)	N/A	N/A	0.3%	0.2%
Total CHI Consolidated before business combination gains	657,470	548,491	5.4%	4.7%	100.0%	98.0%
Business combination gains	-	235,842	N/A	N/A	-	2.0%
Total CHI Consolidated	\$ 657,470	\$ 784,333	5.4%	6.6%	100.0%	100.0%

<sup>1</sup>Includes \$85.7 million net favorable results, compared to the same period in the prior year for the nine months ended March 31, 2017.

<sup>2</sup>Includes Home Care and Senior Living business lines.

<sup>3</sup>Includes the operations of Albuquerque Health Ministries and Lancaster Health Ministries MBOs as well as regional eliminations.

<sup>4</sup>Includes CHI Corporate and First Initiatives Insurance, Ltd. ("FIIL"), CHI's wholly-owned captive insurance company as well as CHI system eliminations.

**OPERATING REVENUE AND VOLUME TRENDS**

CHI total operating revenues increased 3.1%, or \$364.5 million, for the nine months ended March 31, 2017, compared to the corresponding period of the prior fiscal year, and included \$128.7 million in gains on asset sales. Excluding the \$235.8 million of business combination gains reflected in the prior fiscal year, CHI total operating revenues increased 5.2%, or \$600.3 million. Excluding the impacts of current and prior year acquisitions (same store basis), CHI total operating revenues increased 3.1%, or \$352.7 million, for the nine months ended March 31, 2017, compared to the corresponding period of the prior fiscal year.

CHI total net patient services revenues increased 4.6%, or \$501.6 million, for the nine months ended March 31, 2017, compared to the corresponding period of the prior fiscal year, of which \$235.8 million was due to recently completed acquisitions. CHI same store net patient services revenues increased 2.5%, or \$263.2 million, for the nine months ended March 31, 2017 compared to the corresponding period of the prior fiscal year mostly due to overall increased patient volumes of \$139.6 million, favorable shifts in acuity of \$98.7 million, offset by unfavorable shifts in payer mix of \$(70.7) million and unfavorable net patient services

revenues adjustments in the Nebraska region of (\$28.0) million discussed below.

CHI same store patient volume increases (decreases) were as follows for the nine months ended March 31, 2017, as compared to the corresponding period of the prior fiscal year.

Patient Volumes	Percentage Change	Volume Change
Adjusted Admissions	2.0%	16,048
Acute Admissions	0.2%	679
Acute Inpatient Days	(1.0)%	(18,420)
Inpatient ER Visits	1.5%	3,174
Inpatient Surgeries	(1.1)%	(1,348)
Outpatient ER Visits	(1.0)%	(15,558)
Outpatient Non-ER Visits	1.5%	63,433
Outpatient Surgeries	5.2%	9,854
Physician Visits	5.9%	447,844

CHI total other operating revenues decreased (14.4)%, or \$(137.1) million, for the nine months ended March 31, 2017, compared to the corresponding period of the prior fiscal year, due to the inclusion of \$235.8 million in business combination gains in the prior fiscal year. CHI same store total other operating revenues increased 12.6%, or \$89.5 million, for the nine months ended March 31, 2017, compared to the corresponding period of the prior fiscal year, primarily due to the current period gains on sale of business lines and asset sales discussed above.

## OPERATING EXPENSES

CHI total operating expenses before restructuring, impairment and other losses increased 4.2%, or \$507.5 million, for the nine months ended March 31, 2017, as compared to the corresponding period of the prior fiscal year, of which \$256.7 million was due to recently completed acquisitions. CHI same store total operating expenses before restructuring, impairment and other losses increased 2.1%, or \$250.9 million, for the nine months ended March 31, 2017, as compared to the corresponding period of the prior fiscal year, primarily due to increases in total labor costs and purchased services, combined with annual inflation increases in other operating expenses across CHI as described in more detail below.

CHI same store total labor costs increased 2.3%, or \$130.2 million, for the nine months ended March 31, 2017, as compared to the corresponding period of the prior fiscal year, due to \$159.3 million of annual inflation and merit increases (2.8%), offset by \$(29.1) million in decreased FTEs as a result of labor productivity improvements. CHI same store total labor costs represented 48.0% and 47.9% of same store total operating expenses for the nine months ended March 31, 2017 and 2016, respectively. CHI same store total labor costs as a percentage of same store net patient services revenues were 52.4% for both the nine months ended March 31, 2017 and the corresponding period of the prior fiscal year. CHI continues to address labor productivity in certain regions, most notably in the Kentucky and Texas regions, as well as growth initiatives in certain physician practices where labor costs have been added in anticipation of future increased patient volumes. CHI is currently implementing several ongoing labor productivity improvement initiatives throughout CHI, with a focus on the Kentucky and Texas regions.

CHI same store purchased services expenses increased 7.9% or \$102.2 million, for the nine months ended March 31, 2017, as compared to the corresponding period of the prior fiscal year, as a result of new market implementations of revenue cycle services with Conifer during the latter part of the prior fiscal year, outsourcing and expansion of IT services, and physician alignment.

CHI same store supplies expense increased 1.3% or \$26.4 million, for the nine months ended March 31, 2017, as compared to the corresponding period of the prior year, due to increased pharmacy costs. However, same store supplies as a percentage of net patient services revenues decreased to 18.8% for the nine months ended March 31, 2017, compared to 19.0% in the same period of the prior fiscal year.

## REGIONAL OPERATING TRENDS

CHI periodically reviews its allocation methodology for Corporate support services and may adjust those allocations based on the strategic needs and resource consumption of the regions and CHI overall. These changes in allocation methodologies may increase or decrease a region's operating results from year to year, but have no impact on the consolidated results of CHI.

Operating results for the nine months ended March 31, 2017 improved in the Pacific Northwest, Ohio, and Tennessee regions, as well as within CHI Corporate services, but were offset by a decline in the remaining CHI regions compared to the corresponding period of the prior fiscal year. Although overall patient volumes trended up in the current fiscal year compared to the prior fiscal year, several regions have experienced decreases in patient volumes and unfavorable shifts in payer mix which have resulted in decreased net patient revenue yields and increases in operating expenses outpacing overall net patient services revenues growth.

The Colorado, Pacific Northwest, Nebraska, Kentucky and Texas regions represent CHI's five largest operating regions, and for the nine months ended March 31, 2017, represented 71.4% of CHI's consolidated operating revenues.

**Colorado** - the region's operating EBIDA before restructuring, impairment and other losses totaled \$179.1 million for the nine months ended March 31, 2017, and decreased \$(9.4) million compared to the corresponding period of the prior fiscal year, due to unfavorable shifts in payer mix and reductions in net provider fee revenue from Colorado's provider fee program. Net patient services revenues increased \$85.7 million, including \$24.6 million in increased same store patient volumes, \$15.1 million in favorable shifts in acuity and service mix, and \$18.8 million as a result of the Longmont acquisition, compared to the same period of the prior fiscal year. The positive impacts were offset by \$(10.1) million in unfavorable shifts in payer mix, and a net unfavorable \$(26.5) million related to provider fee activity in the Colorado region, which included a \$(51.0) million decrease in provider fee revenue and a \$24.5 million decrease in provider fee expense. The Colorado region is in the process of installing the Epic electronic health record system across its various hospitals, and for the nine months ended March 1, 2017, Epic operating expenses and training costs were \$9.8 million higher, compared to the same period of the prior fiscal year. Total net revenue per adjusted admission increased 3.1% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 4.1%. Total labor as a percentage of net patient services revenues increased to 42.8% compared to 41.0% in the

same period of the prior fiscal year, representing an unfavorable expense variance of \$(29.8) million.

**Pacific Northwest** - the region's operating EBIDA before restructuring, impairment and other losses totaled \$285.0 million for the nine months ended March 31, 2017, and increased \$113.8 million compared to the corresponding period of the prior fiscal year. Results for the nine months ended March 31, 2017 included \$85.7 million of net gains in the Pacific Northwest region primarily from the sale of certain outpatient ambulatory business lines. The remainder of the region's favorable results were due to overall increased patient volumes combined with the implementation of expense management and productivity improvements. Net patient services revenues increased \$135.3 million, including \$93.6 million in patient volumes, \$35.5 million in greater acuity, and \$8.9 million in improved service mix compared to the same period of the prior fiscal year. The net patient services revenues increase exceeded the \$102.8 million in increased operating expenses, including total compensation, purchased services and supplies expenses, compared to the corresponding period of the prior fiscal year. Total net revenue per adjusted admission increased 6.1% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 4.3%. Total labor as a percentage of net patient services revenues decreased to 52.1% compared to 54.2% in the same period of the prior fiscal year as a result of ongoing labor productivity improvements, representing a favorable expense variance of \$40.3 million. Supply expense as a percentage of net patient services revenues declined to 14.4% compared to 14.9% in the prior fiscal year due to revenue growth and improved utilization.

**Nebraska** - the region's operating EBIDA before restructuring, impairment and other losses totaled \$75.2 million for the nine months ended March 31, 2017, and decreased \$(50.3) million compared to the corresponding period of the prior fiscal year, due primarily to \$(28.0) million of unfavorable net patient services revenues adjustments for the nine months ended March 31, 2017. The net patient services revenues adjustments were due to moving the accounts receivable reserve methodology for one facility to the CHI standard, revenue realization

adjustments and to reflect more current collection experience including a reduction in recoveries. Net patient services revenues also included volume growth of \$43.1 million, and favorable increases in acuity of \$16.1 million. Total net revenue per adjusted admission decreased (0.8)% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 1.9%. Total labor as a percentage of net patient services revenues increased to 56.8% due to increased contract labor, compared to 56.1% in the same period of the prior fiscal year. Total operating expenses increased 5.2%, or \$76.3 million in the Nebraska region for the nine months ended March 31, 2017, primarily in the areas of total compensation, purchased services and supplies expenses, compared to the corresponding period of the prior fiscal year. Supply expense as a percentage of net patient service revenues increased to 18.9% compared to 17.4% in the prior fiscal year. Increases in utilization and cost are concentrated in pharmacy, cardiovascular and orthopedic/spine, and is a continued focus and opportunity for reduction.

**Kentucky** - the region's operating EBIDA before restructuring, impairment and other losses totaled \$31.7 million for the nine months ended March 31, 2017, and decreased \$(55.6) million compared to the corresponding period of the prior fiscal year due to increased operating expenses, primarily in labor costs, outpacing net patient services revenues growth. Net patient services revenues increased \$11.6 million, including unfavorable shifts in payer mix (\$20.2) million, acuity (\$12.3) million and service mix (\$8.9) million, offset by improved collections and contract rate improvements. Total labor as a percentage of net patient services revenues increased to 49.2% compared to 45.7% in the same period of the prior fiscal year, representing an unfavorable expense variance of \$(59.2) million. The Kentucky region is continuing its efforts to address nursing and other staff shortages which have resulted in increases to overall labor costs, including a \$16.6 million increase to contract labor costs as well as overtime and premium pay. Operations for the nine months ended March 31, 2017 were favorably impacted by a \$14.3 million decrease in a contingent consideration liability as a result of planned payments related to certain obligations to the UofL affiliation with KentuckyOne Health.

**Texas** - the Texas region's operating EBIDA before restructuring, impairment and other losses totaled \$62.8 million for the nine months ended March 31, 2017, and decreased \$(50.9) million for the nine months ended March 31, 2017, compared to the same period of the prior fiscal year, due to increased operating expenses outpacing net patient services revenues growth. Results for the current year included \$27.0 million in gains from asset sales in the Texas region. Net patient services revenues increased \$83.4 million compared to the same period of the prior fiscal year, and included \$87.4 million from recently completed affiliations. Net patient services revenues were also favorably impacted by Medicaid 1115 waiver reimbursement increases of \$14.0 million which were offset by \$(33.6) million in unfavorable shifts in payer mix. Total labor as a percentage of net patient services revenues increased to 49.3% compared to 47.6% in the same period of the prior fiscal year, representing an unfavorable expense variance of \$(26.3) million. Same store operating expenses increased 3.3%, or \$50.5 million in the Texas region for the nine months ended March 31, 2017. Management is implementing strategies to improve labor productivity and supply chain savings in the Texas region, and is continuing to expand its referral base for additional growth in the region through acquiring and expanding the Texas physician enterprise in the greater Houston area.

**CHI Corporate services and other business lines** - operating EBIDA before restructuring, impairment and other losses totaled \$(180.7) million, representing an improvement of \$142.3 million for the nine months ended March 31, 2017, compared to the corresponding period of the prior fiscal year. Changes in support services activities relate to a variety of factors, and include strategic transfers of certain activities from the regions and other service lines to the Corporate office in order to build Corporate support functions, and new implementations of system-wide services such as revenue cycle and food programs. Support services allocations to the regions consider the strategic needs and resource consumption of the regions and CHI overall. Increases for the nine months ended March 31, 2017 include \$45.8 million of revenue cycle implementations and services for new facilities, and \$14.3 million related to new facilities implementations for national food services. IT expenses decreased \$31.4



million compared to the corresponding period of the prior fiscal year due to reduced system implementation activity, and regional compensation decreased \$19.6 million due to personnel transfers of regional executive leaders from the Corporate Office to the regions. The operations of the self-insurance plans also improved \$31.8 million due to favorable claims experience for the nine months ended March 31, 2017 compared to the corresponding period of the prior fiscal year.

#### **RESTRUCTURING, IMPAIRMENT AND OTHER LOSSES**

CHI restructuring, impairment and other losses totaled \$192.2 million and \$99.4 million for the nine months ended March 31, 2017 and 2016, respectively. For the nine months ended March 31, 2017 and 2016, restructuring, impairment and other losses expenses included \$92.5 million and \$43.8 million of changes in business operations, respectively, \$47.4 million and \$32.5 million of goodwill and long-lived asset

impairment charges, respectively, and \$52.3 million and \$23.1 million of severance costs, respectively. CHI changes in business operations include contract termination costs, as well as ongoing reorganization efforts which include consulting costs related to revenue cycle, supply chain, and labor productivity.

#### **NON-OPERATING RESULTS**

CHI non-operating gains (losses) totaled \$539.0 million and \$(293.3) million for the nine months ended March 31, 2017 and 2016, respectively, primarily driven by CHI's investment portfolio gains (losses), and realized and unrealized gains (losses) on interest rate swaps. CHI investment gains (losses) were \$447.9 million and \$(131.2) million for the nine months ended March 31, 2017 and 2016, respectively, and realized and unrealized gains (losses) on interest rate swaps were \$106.1 million and \$(111.4) million for the nine months ended March 31, 2017 and 2016, respectively.

### ***3. SUMMARY OF CHI BALANCE SHEET AS OF MARCH 31, 2017 AND JUNE 30, 2016***

CHI total assets were \$21.8 billion and \$22.7 billion at March 31, 2017 and June 30, 2016, respectively, representing a decrease of (3.9)%, or \$(881.7) million, during the nine months ended March 31, 2017. The decrease was primarily attributable to a \$(389.6) million decrease in cash and unrestricted investments, as described further below, as well as a \$(414.3) million reduction in net property and equipment balances as a result of decreased capital spending across the regions and of real estate asset sales in the current fiscal year.

CHI total cash and equivalents and unrestricted investments were \$6.3 billion and \$6.6 billion at March 31, 2017 and June 30, 2016, respectively, representing a decrease of (5.9)%, or \$(389.6) million during the nine months ended March 31, 2017. For the nine months ended March 31, 2017, CHI spent a net \$(84.4) million in investing cash flow activities, including \$(475.0) million of ongoing capital investment activity, offset by the receipt of \$372.3 million in proceeds from asset sales. CHI capital investment activity includes maintenance costs for CHI OneCare program and IT infrastructure investments, as well as new hospital construction and facility renovations across the regions. CHI financing cash flow activities for the nine months

ended March 31, 2017, totaled \$(209.8) million and include net debt, interest and net swap collateral receipts. CHI cash flows from operations, including investments and assets limited to use, and working capital changes, were \$(95.4) million for the nine months ended March 31, 2017.

CHI days of cash on hand decreased to 145 days at March 31, 2017, from 159 at June 30, 2016. This decrease is primarily attributable to reductions of cash flows from operations and working capital changes, as well as CHI cash spent on capital additions and debt payments.

CHI net patient accounts receivable were \$2.3 billion and \$2.2 billion at March 31, 2017 and June 30, 2016, respectively, representing an increase of 6.1%, or \$131.3 million, during the nine months ended March 31, 2017, primarily as a result of the increase in CHI net patient services revenues discussed above.

CHI total liabilities were \$14.3 billion and \$15.2 billion at March 31, 2017 and June 30, 2016, respectively, representing a decrease of (6.2)%, or \$(947.2) million, during the nine months ended March 31, 2017, primarily attributable to a \$(464.2) million decrease in

accounts payable and accrued expenses as a result of working capital changes and a \$(251.3) million decrease in outstanding debt balances, as well as decreases in overall other long-term liabilities. CHI total debt was \$8.8 billion and \$9.1 billion at March 31, 2017 and June 30, 2016, respectively, representing a decrease of \$(251.3) million, primarily due to \$(437.0) million in CHI debt redemptions and \$(86.5) million in scheduled debt service payments, and \$72.2 million in increases in capital leases and other debt issued during the nine months ended March 31, 2017.

CHI's debt-to-capitalization ratio was 55.1% and 56.0% at March 31, 2017 and June 30, 2016, respectively, primarily as a result of the \$(251.3) million decrease in CHI debt during the nine months ended March 31, 2017 and a \$62.0 million increase to unrestricted net assets. CHI total unrestricted net assets increased during the nine months ended March 31, 2017, driven by CHI's excess of revenues over expenses of \$115.2 million offset by a \$(32.2) million net loss from CHI's discontinued operations for the nine months ended March 31, 2017.

## **4. CERTAIN CONTRACTUAL OBLIGATIONS**

### **CAPITAL OBLIGATION DOCUMENT**

The obligations of the Corporation to pay amounts due on its commercial paper notes, revenue bonds, guarantees and certain swap agreements are evidenced by Obligations issued under the Capital Obligation Document ("COD"). Obligations also evidence the Corporation's obligations to banks that provide funds for the purchase of indebtedness tendered for purchase or subject to mandatory tender for purchase and not remarketed under the Corporation's self-liquidity program and for general purpose revolving lines of credit.

At March 31, 2017, the Corporation's outstanding indebtedness evidenced by Obligations issued under the COD totaled \$8.0 billion. Payment obligations under the COD are limited to the Obligated Group (defined in the COD), which only includes the Corporation. Certain covenants under the COD are tested based on the combination of the Obligated Group, Participants and Designated Affiliates. However, holders of Obligations have no recourse to Participants or Designated Affiliates or their property for payment thereof.

## INDEBTEDNESS

(in Millions)	March 31, 2017
<b>Capital Obligation Debt</b>	
Fixed Rate Bonds <sup>1</sup>	\$4,903
Variable Rate Bonds <sup>2</sup>	508
Long Term Rate Bonds <sup>3</sup>	142
Direct Purchase Bonds <sup>4</sup>	1,002
Commercial Paper Notes	815
Short term bank loans	<u>584</u>
<b>Total Capital Obligation Debt</b>	<b>\$ 7,954</b>
<b>Non-Capital Obligation Debt</b>	
Other MBO Debt <sup>5</sup>	\$504
Capital Leases	185
Note Payable issued to Episcopal Health Foundation	<u>167</u>
<b>Total Non-Capital Obligation Debt</b>	<b><u>\$856</u></b>
<b>Total CHI Debt</b>	<b><u>\$8,810</u></b>

<sup>1</sup> Excludes unamortized original issue premium, discount and issuance costs.

<sup>2</sup> Includes bonds that bear interest at variable rates (currently determined weekly) and are subject to optional tender for purchase by their holders, FRNs that bear interest at variable rates (currently determined weekly and monthly), for a specified period and are subject to mandatory tender as set forth below and direct purchase debt of affiliates that is placed directly with holders, bears interest at variable rates determined monthly based upon a percentage of LIBOR or SIFMA plus a spread, and is subject to mandatory tender on certain dates.

<sup>3</sup> Long-term rate bonds bear interest at a fixed rate for a specified period and are subject to mandatory tender at the end of such period as set forth below.

<sup>4</sup> Direct purchase debt of the Corporation is placed directly with holders, bears interest at variable rates determined monthly based upon a percentage of LIBOR or SIFMA plus a spread, and is subject to mandatory tender on certain dates as set forth below. On December 2, 2016, the Corporation issued a \$200 million taxable bond (the "2016A Taxable Bond") that was purchased by Morgan Stanley & Co. LLC.

<sup>5</sup> Other debt is comprised mostly of \$235.3 million of CHI St. Luke's affiliate debt, \$95.4 million of Centura affiliate debt and \$58.1 million of SFH affiliate debt.

The required principal payments on the total CHI long-term debt during fiscal year 2017 is approximately \$135.0 million.

At March 31, 2017, the Corporation had one revolving line of credit with Mizuho Bank, LTD., in the amount of \$250 million that was fully drawn and matures on June 29, 2017, unless the parties mutually agree to renew or extend the loan. The Corporation and Mizuho are in discussion regarding renewal of the line. On December 2, 2016, the Corporation issued a \$200 million 2016A Taxable Bond that was purchased by Morgan Stanley & Co. LLC. The 2016A Taxable Bond matures December 1, 2021, but may be tendered to the Corporation for purchase on December 1, 2017. On February 10, 2016, the Corporation borrowed \$333.7 million from JPMorgan Chase Bank, National Association to provide for the defeasance of certain fixed rate bonds. This

loan matures on December 20, 2017, unless the parties mutually agree to renew or extend.

### A. Direct Purchase Debt

The Corporation's direct purchase debt is subject to mandatory tender on the dates set forth below. Prior to the mandatory tender of direct purchase debt, management expects that it would analyze the then current market conditions and availability and relative cost of refinancing or restructuring alternatives which could include without limitation, conversion to another interest mode, refinancing or repayment.

Series	Par Outstanding March 31, 2017	Mandatory Tender Date
Providence Series 2009A	\$6.8 million	October 1, 2017
Providence Series 2009B	5.9 million	October 1, 2017
Providence Series 2009C	4.2 million	October 1, 2017
Taxable 2016A	200.0 million	December 1, 2017
Colorado 2011C <sup>1</sup>	118.0 million	November 10, 2018
Washington 2008A <sup>1</sup>	119.5 million	January 29, 2019
Colorado 2004B6 <sup>1</sup>	54.2 million	September 15, 2020
Taxable 2013F	75.0 million	December 18, 2020
Colorado 2015-1	36.7 million	August 1, 2021
Colorado 2015-2	63.5 million	August 1, 2021
Colorado 2013C	100.0 million	December 18, 2023
Taxable 2013E	125.0 million	December 18, 2023
Colorado 2015A	18.6 million	August 1, 2024
Colorado 2015B	27.3 million	August 1, 2024
Washington 2015A	<u>47.5 million</u>	August 1, 2024
<b>Total Direct Purchase Bonds</b>	<b><u>\$1,002 million</u></b>	

<sup>1</sup> Includes a "term out" provision that varies among agreements, which permits repayment after the mandatory tender date absent any defaults or events of default.

The Corporation's direct purchase agreements are publicly available, and can be accessed through the Digital Assurance Certification LLC website ("DAC") at [www.dacbond.com](http://www.dacbond.com) and the Municipal Securities

Rulemaking Board ("MSRB") through the Electronic Municipal Market Access ("EMMA") website of the MSRB, which can be found at <http://emma.msrb.org>.

## B. Long-Term Rate Bonds

The Corporation's long-term rate bonds are subject to mandatory tender on the dates set forth below. Prior to the mandatory tender of long-term rate bonds, management expects that it would analyze the then

current market conditions and availability and relative cost of refinancing or restructuring alternatives, which could include without limitation, conversion to another interest mode, refinancing or repayment.

Series	Par Outstanding March 31, 2017	Mandatory Tender Date
Colorado 2009B-3	\$40.0 million	November 6, 2019
Kentucky 2009B	60.0 million	November 10, 2021
Colorado 2008D-3	<u>41.9 million</u>	November 12, 2021
<b>Total Long-Term Rate Bonds</b>	<b><u>\$141.9 million</u></b>	

### C. Floating Rate Notes (“FRNs”)

The Corporation’s FRNs are subject to mandatory tender on the dates set forth below. Upon the mandatory tender of the FRNs, management expects that it would analyze the then current market conditions and availability and relative cost of

refinancing or restructuring alternatives prior to the applicable tender date, which could include, without limitation, conversion to another interest mode, refinancing or repayment.

Series	Par Outstanding March 31, 2017	Mandatory Tender Date
Kentucky 2011B-1	\$ 52.7 million	January 31, 2020
Kentucky 2011B-2	52.7 million	January 31, 2020
Colorado 2008C-2	26.5 million	November 12, 2020
Colorado 2008C-4	26.5 million	November 12, 2020
Washington 2013B-1	100.0 million	December 31, 2020
Washington 2013B-2	100.0 million	December 31, 2024
Kentucky 2011B-3	<u>52.7 million</u>	January 31, 2025
<b>Total FRNs</b>	<b><u>\$411.1 million</u></b>	

### D. Variable Rate Bonds

The Corporation’s variable rate demand bonds are subject to optional and mandatory tender. As of March 31, 2017, variable rate demand bonds are outstanding in the amount of \$96.7 million, supported by the Corporation’s self-liquidity, not by a dedicated liquidity or credit facility. See “*Liquidity Arrangements*” below.

### E. Taxable Commercial Paper

The Corporation’s commercial paper note program permits the issuance of up to \$881 million in aggregate principal amount outstanding, with maturities limited to 270 day period. The Corporation has directed the commercial paper dealers to tranche the commercial paper maturities so that no greater than approximately one-third of the outstanding balance matures in any one month, and no more than \$100 million matures per dealer within any five business-day period while the outstanding balance of the commercial paper is greater than \$500 million. The Corporation has, from time to time, directed its dealers to deviate from such directions, and may do so again in the future. As of March 31, 2017, \$815.5 million of commercial paper notes were outstanding. The commercial paper notes are supported by the Corporation’s self-liquidity, and

are not supported by a dedicated liquidity or credit facility. See “*Liquidity Arrangements*” below.

### F. Swap Agreements

The Corporation or its affiliates are currently party to 41 swap transactions that had an aggregate notional amount of approximately \$1.6 billion at March 31, 2017. The 41 transactions have varying termination dates ranging from 2017 to 2047. The swap agreements require the Corporation (or with respect to certain swap agreements, CHI St. Luke’s or SFH) to provide collateral if its respective liability, determined on a mark-to-market basis, exceeds a specified threshold that varies based upon the rating on the Corporation’s long-term indebtedness. The swap agreements of Memorial East Texas and Centura do not require collateral postings. The fair value of the swaps is estimated based on the present value sum of anticipated future net cash settlements until the swaps’ maturities. Cash collateral balances are netted against the fair value of the swaps, and the net amount is reflected in other liabilities in the accompanying consolidated balance sheets. At March 31, 2017, the net swap liability reflected in other liabilities was \$35.8 million, net of swap collateral posted of \$247.0 million. The swap agreements, excluding the Centura Health swap, are secured by



Obligations issued under the COD. (See Note 7 in the Consolidated Interim Financial Statements (Unaudited)

as of March 31, 2017 and for the three and nine months ended March 31, 2017 and 2016.)

Obligated Party	Type	Outstanding Notional March 31, 2017	Termination Date
CHI <sup>1</sup>	Total Return	\$ 90.9 million	September 5, 2017-January 16, 2020
CHI	Fixed Payer	150.9 million	May 1, 2025
CHI	Fixed Payer	246.8 million	March 1, 2032
CHI	Fixed Payer	98.8 million	September 1, 2036
CHI	Fixed Payer	128.5 million	September 1, 2036
CHI	Fixed Payer	19.8 million	September 1, 2036
CHI	Fixed Payer	99.4 million	December 1, 2036
CHI	Fixed Payer	149.1 million	December 1, 2036
CHI St. Luke's	Fixed Payer	124.4 million	February 18, 2031
CHI St. Luke's	Fixed Payer	101.1 million	February 15, 2032
CHI St. Luke's	Fixed Payer	100.0 million	February 15, 2047
CHI St. Luke's	Fixed Payer	100.0 million	February 15, 2047
Centura Health <sup>2</sup>	Fixed Payer	15.4 million	May 20, 2024
Madonna Manor	Total Return	28.4 million	August 15, 2020
Memorial East Texas	Fixed Payer	25.2 million	February 15, 2035
Memorial East Texas	Fixed Payer	17.8 million	February 15, 2028
St. Joseph Regional Health <sup>3</sup>	Total Return	69.3 million	April 4, 2018 - August 15, 2020
St. Joseph Regional Health	Fixed Payer	45.6 million	January 1, 2028
St. Joseph Regional Health	Basis	<u>30.0 million</u>	March 1, 2028
<b>Total Notional Amount</b>		<b><u>\$1,641.4 million</u></b>	

<sup>1</sup>Represents 19 Total Return Swaps.

<sup>2</sup> Not secured by CHI COD obligations.

<sup>3</sup> Represents 5 Total Return Swaps.

## 5. LIQUIDITY AND CAPITAL RESOURCES

### Cash Equivalents and Internally Designated Investments

CHI holds highly liquid investments to enhance its ability to satisfy liquidity needs. Asset allocations are reviewed on a monthly basis and compared to investment allocation targets included within CHI's investment

policy. At March 31, 2017 and June 30, 2016, CHI had cash and equivalents and internally designated investments (including net unrealized gains and losses) as described in the table below.

(in Thousands)	March 31, 2017	June 30, 2016
Cash and equivalents	\$ 918,285	\$ 1,305,242
Internally designated investments	<u>5,336,171</u>	<u>5,338,803</u>
<b>Total</b>	<b><u>\$ 6,254,456</u></b>	<b><u>\$ 6,644,045</u></b>

CHI maintains an Operating Investment Program (the "Program") administered by the Corporation. The Program is structured as a limited partnership with the Corporation as the managing general partner.

The Program contracts with investment advisers to manage the investments within the Program.

Substantially all CHI long-term investments are held in the Program. The Corporation requires all Participants to invest in the Program. The Program consists of equity securities, fixed-income securities and alternative investments (e.g., private equity, hedge funds and real estate interests). The asset allocation is established by the Finance Committee of the Board of Stewardship Trustees. At March 31, 2017, the asset

allocation for the Program's Long-Term Pool was 45% equity securities, 30% fixed-income securities, 25% alternative investments, and 0% cash and equivalents. Alternative investments within the Program have limited liquidity. As of March 31, 2017, illiquid investments not available for redemption totaled \$381.0 million, and investments available for redemption within 180 days at the request of the Program totaled \$765.8 million. The asset allocation for the Program's Intermediate Pool was 100% fixed-income securities. As of March 31, 2017, 89.6% of the Program's assets were invested in the Long-Term Pool, with 10.4% of assets invested in the Intermediate Pool. The Program's return was 7.8% for the nine months ended March 31, 2017.

## LIQUIDITY ARRANGEMENTS

The Corporation maintains several liquidity facilities that are dedicated to funding optional or mandatory tenders of its variable rate debt and paying the maturing principal of the commercial paper notes in the event remarketing proceeds are unavailable for such

purpose. At March 31, 2017 and June 30, 2016, no amounts were drawn on these lines. The Corporation's dedicated self-liquidity lines are set forth below and can be found at <http://emma.msrb.org>.

### CHI Dedicated Self-Liquidity Lines – March 31, 2017

Bank	Committed Amount	Expiration
Bank of New York Mellon	\$ 60.0 million	June 30, 2017*
PNC Bank	125.0 million	August 24, 2017
J.P. Morgan	50.0 million	September 30, 2017
Bank of New York Mellon	50.0 million	December 15, 2017
MUFG Union Bank	75.0 million	September 28, 2018
Northern Trust	<u>65.0 million</u>	June 28, 2019
<b>Total Self-Liquidity Lines</b>	<b><u>\$ 425.0 million</u></b>	

\* The Corporation does not intend to renew the line upon expiration on June 30, 2017.

## 6. LIQUIDITY REPORT

CHI posts a liquidity report monthly, which can be found at [www.catholichealth.net](http://www.catholichealth.net) and <http://emma.msrb.org>.

## PART VI: LEGAL PROCEEDINGS

### PENDING LITIGATION/REGULATORY MATTERS

CHI operates in a highly litigious industry. As a result, various lawsuits, claims and regulatory proceedings have been instituted or asserted against it from time to time. CHI has knowledge of certain pending suits against certain of its entities that have arisen in the

ordinary course of business. In the opinion of management, CHI maintains adequate insurance and/or other financial reserves to cover the estimated potential liability for damages in these cases, or, to the extent such liability is uninsured, adverse decisions will not have a material adverse effect on the financial

position or operations of CHI.

**General Observation Relating to Status as Health Care System.** CHI, like all major health care systems, periodically may be subject to investigations or audits by federal, state and local agencies involving compliance with a variety of laws and regulations. These investigations seek to determine compliance with, among other things, laws and regulations relating to Medicare and Medicaid reimbursement, including billing practices for certain services. Violation of such laws could result in substantial monetary fines, civil and/or criminal penalties and exclusion from participation in Medicare, Medicaid or similar programs.

**St. Joseph–London.** Following a voluntary disclosure of compliance-related issues concerning cardiac stent cases performed at a CHI direct affiliate, St. Joseph London (“SJHS”), by a single, independent/non-employed interventional cardiologist, on January 22, 2014, SJHS entered into a settlement agreement with the federal government, the Commonwealth of Kentucky, and three relators and paid \$16.5 million to resolve civil and administrative monetary claims raised in a *qui tam* lawsuit relating to certain diagnostic and therapeutic cardiac procedures performed at SJHS’s facility and the financial relationship with certain cardiac physicians and physician groups. In addition, SJHS entered into a five-year corporate integrity agreement (“CIA”) with the OIG that imposes certain compliance oversight obligations solely at SJHS’s facility. The CIA is approaching the end of its third year.

In a separate matter, numerous civil lawsuits have been filed against the Corporation and SJHS claiming damages for alleged unnecessary cardiac stent placements and other cardiac procedures. Both CHI and SJHS are vigorously defending these lawsuits. The first case, Edward Marshall, et al. v. Catholic Health Initiatives et al., Case No. 11-CI-00972, was tried to a defense verdict in favor of both CHI and SJHS. Plaintiffs agreed to dismiss the second case to be tried, Blair Apgar and Mary Apgar, his wife v. Catholic Health Initiatives, et al., Case No. 12-CI-00445. CHI and SJHS were dismissed before trial from the third case to be tried, James Davis, part of Anthony Adams et al. v. Catholic Health Initiatives, et al., Case No. 12-CI-00802, which resulted in a defense verdict in favor of the

remaining defendants. The fourth case, LeMaster v. Catholic Health Initiatives, et al., Case No. 12-CI-00975, which was originally scheduled for trial in April 2016, was dismissed by the court following a grant of summary judgment in favor of SJHS due to plaintiff’s failure to establish a causal link between the alleged negligence and plaintiff’s injuries. The fifth case, Dolly Wathen, also part of Anthony Adams, et al. v. Catholic Health Initiatives, et al., Case No. 12-CI-00802, was dismissed by plaintiffs prior to trial. The sixth case, Kevin Ray Wells, Sr. v. Catholic Health Initiatives, et al., Case No. 12-CI-00090, was tried to verdict in August 2016. The jury found in favor of the plaintiff and awarded compensatory damages in an amount just under \$1.3 million and punitive damages of \$20.0 million. Post-trial motions have been filed and, while the trial court did not set aside the verdict, it did reduce the punitive damage award to \$5.0 million. The rulings of the trial court are now being appealed. The E/O Vada Owens v. Catholic Health Initiatives, et al. Case No. 12-CI-00405 commenced trial on January 9, 2017 in the Circuit Court of Laurel County with the Honorable Judge Lay presiding. Prior to the case going to the jury, a Settlement in Principle was reached with Plaintiffs on all of the cardiac claims, including the E/O Owens, but excluding Kevin Wells which is on appeal. Management believes that adequate reserves have been established and that the outcome of the current litigation will not have a material adverse effect on the financial position or results of operations of CHI.

**Pension Plan Litigation.** In May 2013, the Corporation and two employees were named as defendants in a class action lawsuit under the Employee Retirement Income Security Act of 1974, as amended (“ERISA”), challenging the “church plan” status of one of CHI’s defined benefit plans. Medina v. Catholic Health Initiatives, et al., Civil No 13-1249 (District of Colorado). Subsequently, the Complaint was amended to name additional CHI-related defendants. The Complaint alleges that CHI’s defined benefit plan (1) does not meet the definition of a “church plan” under ERISA; (ii) does not satisfy ERISA’s minimum funding standards; (iii) violates various other provisions of ERISA applicable to covered defined benefit plans; or (iv) alternatively, if CHI’s defined benefit plan qualifies for “church plan” status, the “church plan” exemption is nonetheless an unconstitutional accommodation under the

Establishment Clause of the First Amendment. On December 8, 2015, the U.S. District Court for the District of Colorado entered summary judgment in favor of CHI and the individual defendants on all of plaintiff's claims, dismissing the claims with prejudice, and awarding defendants their costs. Plaintiff filed a notice of appeal on January 6, 2016. The parties have filed their initial briefs with the Tenth Circuit Court of Appeals and oral argument on the appeal was scheduled for January 18, 2017. However, on December 13, 2016, following certain action taken by the United States Supreme Court in other non-CHI-related "church plan" litigation (described below), the Tenth Circuit vacated the hearing and stayed the appeal. The parties filed a joint report with the Tenth Circuit on the status of the Supreme Court proceedings by March 15, 2017. While no assurance can be given as to the outcome of the

appeal, management does not believe that this matter, if decided adversely to CHI, would have a material adverse effect on the financial position or results of operations of CHI. In other non-CHI-related "church plan" litigation (i.e., Advocate Health Care Network v. Stapleton, St. Peter's Healthcare System v. Kaplan, and Dignity Health v. Rollins), the Supreme Court, on December 2, 2016, granted *certiorari* on the legal question of whether only a church can establish a "church plan" within the meaning of ERISA. The Supreme Court heard oral arguments of the noted legal question on March 27, 2017. It is not yet known what the outcome of the Supreme Court proceedings in the three cases will be or what impact they will ultimately have on the CHI litigation, but as noted, the appeal is stayed pending the Supreme Court proceedings.

***APPENDIX A***  
***CATHOLIC HEALTH INITIATIVES***  
***CONSOLIDATED INTERIM FINANCIAL***  
***STATEMENTS (Unaudited)***

***As of March 31, 2017 and for the Three and Nine  
Months Ended March 31, 2017 and 2016***

CONSOLIDATED INTERIM FINANCIAL STATEMENTS  
(UNAUDITED)

Catholic Health Initiatives  
As of March 31, 2017, and for the Three and  
Nine Months Ended March 31, 2017 and 2016  
With Review Report of Independent Auditors

Ernst & Young LLP



# Catholic Health Initiatives

## Consolidated Interim Financial Statements (Unaudited)

As of March 31, 2017, and for the Three and  
Nine Months Ended March 31, 2017 and 2016

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## Review Report of Independent Auditors

The Board of Stewardship Trustees  
Catholic Health Initiatives

We have reviewed the consolidated financial information of Catholic Health Initiatives, which comprise the consolidated balance sheet as of March 31, 2017, and the related consolidated statements of operations for the three-month and nine-month periods ended March 31, 2017 and 2016, changes in net assets for the nine-month period ended March 31, 2017, and cash flows for the nine-month periods ended March 31, 2017 and 2016.

### Management's Responsibility for the Financial Information

Management is responsible for the preparation and fair presentation of the interim financial information in conformity with U.S. generally accepted accounting principles; this includes the design, implementation and maintenance of internal control sufficient to provide a reasonable basis for the preparation and fair presentation of interim financial information in conformity with U.S. generally accepted accounting principles.

### Auditor's Responsibility

Our responsibility is to conduct our review in accordance with auditing standards generally accepted in the United States applicable to reviews of interim financial information. A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the United States, the objective of which is the expression of an opinion regarding the financial information. Accordingly, we do not express such an opinion.

### Conclusion

Based on our review, we are not aware of any material modifications that should be made to the consolidated financial information referred to above for it to be in conformity with U.S. generally accepted accounting principles.

*Ernst & Young LLP*

May 19, 2017

Catholic Health Initiatives

Consolidated Balance Sheets

(In Thousands)

	March 31, 2017	June 30, 2016
	<i>(Unaudited)</i>	
<b>Assets</b>		
Current assets:		
Cash and equivalents	\$ 918,285	\$ 1,305,242
Net patient accounts receivable, less allowances for bad debts of \$1,007,923 and \$968,147 at March and June, respectively	2,292,584	2,161,237
Other accounts receivable	238,340	274,432
Current portion of investments and assets limited as to use	34,494	63,146
Inventories	314,721	296,647
Assets held for sale	190,363	223,285
Prepaid and other	174,218	152,230
Total current assets	4,163,005	4,476,219
Investments and assets limited as to use:		
Internally designated for capital and other funds	5,073,479	4,952,065
Mission and Ministry Fund	130,269	125,166
Capital Resource Pool	132,423	261,572
Held by trustees	78,224	113,235
Held for insurance purposes	845,985	841,048
Restricted by donors	269,259	264,949
Total investments and assets limited as to use	6,529,639	6,558,035
Property and equipment, net	9,037,708	9,452,010
Investments in unconsolidated organizations	1,331,003	1,263,506
Intangible assets and goodwill, net	477,201	462,838
Notes receivable and other	238,905	446,522
Total assets	<u>\$ 21,777,461</u>	<u>\$ 22,659,130</u>

*Continued on following page*

	<b>March 31, 2017</b>	<b>June 30, 2016</b>
	<b>(Unaudited)</b>	
<b>Liabilities and net assets</b>		
Current liabilities:		
Compensation and benefits	\$ 568,516	\$ 717,638
Third-party liabilities, net	141,548	110,284
Accounts payable and accrued expenses	1,404,015	1,750,402
Liabilities held for sale	117,076	131,814
Variable-rate debt with self-liquidity	96,700	96,700
Commercial paper and current portion of debt	1,992,114	1,769,390
Total current liabilities	4,319,969	4,576,228
 Pension liability	 1,432,885	 1,535,840
Self-insured reserves and claims	643,820	646,714
Other liabilities	1,151,038	1,262,068
Long-term debt	6,717,162	7,191,184
Total liabilities	14,264,874	15,212,034
 Net assets:		
Net assets attributable to CHI	6,789,336	6,704,217
Net assets attributable to noncontrolling interests	400,338	423,424
Unrestricted	7,189,674	7,127,641
Temporarily restricted	226,391	224,524
Permanently restricted	96,522	94,931
Total net assets	7,512,587	7,447,096
 Total liabilities and net assets	 <u><u>\$ 21,777,461</u></u>	 <u><u>\$ 22,659,130</u></u>

*See accompanying notes.*

# Catholic Health Initiatives

## Consolidated Statements of Operations (Unaudited) (In Thousands)

	Three Months Ended March 31		Nine Months Ended March 31	
	2017	2016	2017	2016
<b>Revenues</b>				
Net patient services revenues before provision for doubtful accounts	\$ 4,082,690	\$ 3,982,174	\$ 12,103,405	\$ 11,654,321
Provision for doubtful accounts	(237,626)	(264,436)	(687,411)	(739,962)
Net patient services revenues	3,845,064	3,717,738	11,415,994	10,914,359
Other operating revenues:				
Donations	9,366	10,613	27,936	25,858
Changes in equity of unconsolidated organizations	7,837	438	24,952	31,360
Gains on business combinations	—	94,174	—	235,842
Hospital ancillary revenues	83,290	88,054	258,555	264,164
Other	224,205	144,854	505,588	396,937
Total other operating revenues	324,698	338,133	817,031	954,161
Total operating revenues	4,169,762	4,055,871	12,233,025	11,868,520
<b>Expenses</b>				
Salaries and wages	1,648,136	1,624,801	5,021,813	4,797,506
Employee benefits	327,477	344,110	961,341	929,747
Purchased services, medical professional fees, medical claims and consulting	648,000	612,607	1,908,255	1,727,096
Supplies	706,552	690,930	2,149,761	2,069,352
Utilities	56,729	57,190	172,891	172,932
Rentals, leases, maintenance and insurance	249,474	230,372	705,741	693,904
Depreciation and amortization	221,483	215,778	657,529	648,562
Interest	78,418	77,689	231,535	224,355
Other	207,995	225,879	655,753	693,650
Total operating expenses before restructuring, impairment and other losses	4,144,264	4,079,356	12,464,619	11,957,104
Income (loss) from operations before restructuring, impairment and other losses	25,498	(23,485)	(231,594)	(88,584)
Restructuring, impairment and other losses	65,601	58,142	192,217	99,435
Loss from operations	(40,103)	(81,627)	(423,811)	(188,019)
<b>Nonoperating gains (losses)</b>				
Investment income (losses), net	203,208	40,865	447,945	(131,150)
Loss on defeasance of bonds	(7,678)	(30,469)	(16,184)	(29,561)
Realized and unrealized gains (losses) on interest rate swaps	820	(64,649)	106,142	(111,369)
Other nonoperating gains (losses)	1,230	(12,733)	1,087	(21,227)
Total nonoperating gains (losses)	197,580	(66,986)	538,990	(293,307)
Excess (deficit) of revenues over expenses	157,477	(148,613)	115,179	(481,326)
Excess of revenues over expenses attributable to noncontrolling interest	3,331	3,935	4,518	11,406
Excess (deficit) of revenues over expenses attributable to CHI	\$ 154,146	\$ (152,548)	\$ 110,661	\$ (492,732)

See accompanying notes.

# Catholic Health Initiatives

## Consolidated Statements of Changes in Net Assets (Unaudited) (In Thousands)

	Unrestricted Net Assets			Temporarily Restricted Net Assets	Permanently Restricted Net Assets	Total Net Assets
	Attributable to CHI	Attributable to Noncontrolling Interests	Total			
Balances, July 1, 2015	\$ 8,150,235	\$ 445,687	\$ 8,595,922	\$ 268,317	\$ 97,776	\$ 8,962,015
(Deficit) excess of revenues over expenses	(703,207)	3,779	(699,428)	—	—	(699,428)
Net loss from discontinued operations	(30,667)	—	(30,667)	—	—	(30,667)
Change in pension funded status	(768,468)	(4,877)	(773,345)	—	—	(773,345)
Temporarily and permanently restricted contributions	—	—	—	39,276	3,487	42,763
Net assets released from restriction for capital	66,487	—	66,487	(66,487)	—	—
Net assets released from restriction for operations	—	—	—	(17,912)	—	(17,912)
Investment income (losses)	423	—	423	27	(378)	72
Temporarily and permanently restricted assets from acquisitions	—	—	—	11,672	2,531	14,203
Temporarily and permanently restricted assets from dispositions	—	—	—	(5,700)	(11,373)	(17,073)
Distributions to noncontrolling owners	—	(19,669)	(19,669)	—	—	(19,669)
Noncontrolling ownership acquisitions	—	9,275	9,275	—	—	9,275
Other changes in net assets	(10,586)	(10,771)	(21,357)	(4,669)	2,888	(23,138)
Net decrease in net assets	(1,446,018)	(22,263)	(1,468,281)	(43,793)	(2,845)	(1,514,919)
Balances, June 30, 2016	6,704,217	423,424	7,127,641	224,524	94,931	7,447,096
Excess of revenues over expenses	110,661	4,518	115,179	—	—	115,179
Net loss from discontinued operations	(32,238)	—	(32,238)	—	—	(32,238)
Change in pension funded status	(4,422)	—	(4,422)	—	—	(4,422)
Temporarily and permanently restricted contributions	—	—	—	31,507	1,692	33,199
Net assets released from restriction for capital	19,119	—	19,119	(19,119)	—	—
Net assets released from restriction for operations	—	—	—	(12,456)	—	(12,456)
Investment (losses) income	(423)	—	(423)	6,044	860	6,481
Distributions to noncontrolling owners	—	(15,508)	(15,508)	—	—	(15,508)
Other changes in net assets	(7,578)	(12,096)	(19,674)	(4,109)	(961)	(24,744)
Net increase (decrease) in net assets	85,119	(23,086)	62,033	1,867	1,591	65,491
Balances, March 31, 2017 (unaudited)	\$ 6,789,336	\$ 400,338	\$ 7,189,674	\$ 226,391	\$ 96,522	\$ 7,512,587

See accompanying notes.

# Catholic Health Initiatives

## Consolidated Statements of Cash Flows (Unaudited) (In Thousands)

	Nine Months Ended March 31	
	2017	2016
<b>Operating activities</b>		
Increase (decrease) in net assets	\$ 65,491	\$ (578,517)
Adjustments to reconcile increase (decrease) in net assets to net cash (used in) provided by operating activities:		
Depreciation and amortization	657,529	648,562
Provision for bad debts	687,411	739,962
Changes in equity of unconsolidated organizations	(24,952)	(31,360)
Net gains on business combinations	—	(235,842)
Net gains on sales of facilities and investments in unconsolidated organizations	(131,124)	(20,448)
Non-cash operating expenses related to restructuring, impairment and other losses	47,434	51,618
Losses on defeasance of bonds	16,184	29,561
(Increase) decrease in fair value of interest rate swaps	(133,100)	81,803
Non-cash pension adjustments	(33,028)	(11,184)
Pension cash contributions	(69,928)	(7,521)
Net changes in current assets and liabilities:		
Net patient and other accounts receivable	(741,228)	(991,238)
Other current assets	(40,368)	1,659
Current liabilities	(403,203)	(146,045)
Other changes	(33,674)	47,830
Net cash used in operating activities, before net decrease in investments and assets limited as to use	(136,556)	(421,160)
Net decrease in investments and assets limited as to use	43,712	992,114
Net cash (used in) provided by operating activities	(92,844)	570,954
<b>Investing activities</b>		
Purchases of property, equipment and other capital assets	(475,044)	(628,728)
Investments in unconsolidated organizations	(86,675)	(30,367)
Business acquisitions, net of cash acquired	(64,432)	(3,214)
Proceeds from asset sales	372,317	91,443
Distributions from investments in unconsolidated organizations	32,417	50,163
Loans to unconsolidated affiliates	(1,113)	(30,711)
Net repayments of notes receivable	148,088	10,687
Other changes	(9,915)	(8,467)
Net cash used in investing activities	(84,357)	(549,194)
<b>Financing activities</b>		
Proceeds from issuance of debt and bank loans	240,128	916,978
Costs associated with issuance of debt	—	(1,076)
Repayment of debt	(544,015)	(892,979)
Swap cash collateral returned (posted)	94,131	(99,575)
Net cash used in financing activities	(209,756)	(76,652)
Decrease in cash and equivalents	(386,957)	(54,892)
Cash and equivalents at beginning of period	1,305,242	948,369
Cash and equivalents at end of period	\$ 918,285	\$ 893,477

See accompanying notes.

# Catholic Health Initiatives

## Notes to Consolidated Interim Financial Statements (Unaudited)

March 31, 2017

### 1. Summary of Significant Accounting Policies

#### Organization

Catholic Health Initiatives (CHI), established in 1996, is a tax-exempt Colorado corporation and has been granted an exemption from federal income tax under Section 501(c)(3) of the Internal Revenue Code. CHI sponsors market-based organizations (MBOs) and other facilities operating in 17 states and includes 104 hospitals, including 4 academic medical centers, and 29 critical access facilities; community health service organizations; accredited nursing colleges; home health agencies; and other facilities that span the inpatient and outpatient continuum of care. CHI also has an offshore captive insurance company, First Initiatives Insurance, Ltd. (FIIL).

The mission of CHI is to nurture the healing ministry of the Church, supported by education and research. Fidelity to the Gospel urges CHI to emphasize human dignity and social justice as CHI creates healthier communities.

#### Basis of Presentation

The consolidated interim financial statements of CHI as of March 31, 2017, and for the three and nine months ended March 31, 2017 and 2016, reflect all adjustments, consisting only of normal recurring adjustments, which in the opinion of management are necessary to fairly state its financial position, results of operations and cash flows for the periods presented. The consolidated interim financial statements have been prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) for interim reporting, and accordingly, certain information and footnote disclosures normally included in annual financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to U.S. GAAP. However, CHI believes that the disclosures are adequate to make the information presented not misleading. These consolidated interim financial statements should be read in conjunction with the audited financial statements as of and for the year ended June 30, 2016.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results could vary from the estimates. Operating results for the three and nine months ended March 31, 2017 and 2016, are not necessarily indicative of the results that may be expected for any future period or for a full fiscal year as revenues, expenses, assets and liabilities can vary during each quarter of the year.



## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 1. Summary of Significant Accounting Policies (continued)

##### Principles of Consolidation

CHI consolidates all direct affiliates in which it has sole corporate membership or ownership (Direct Affiliates) and all entities in which it has greater than 50% equity interest with commensurate control. All significant intercompany accounts and transactions are eliminated in consolidation.

##### Fair Value of Financial Instruments

Financial instruments consist primarily of cash and equivalents, patient accounts receivable, investments and assets limited as to use, notes receivable and accounts payable. The carrying amounts reported in the consolidated balance sheets for these items, other than investments and assets limited as to use, approximate fair value. See Note 6, *Fair Value of Assets and Liabilities*, for a discussion of the fair value of investments and assets limited as to use.

##### Cash and Equivalents

Cash and equivalents include all deposits with banks and investments in interest-bearing securities with maturity dates of 90 days or less from the date of purchase. In addition, cash and equivalents include deposits in short-term funds held by professional managers. The funds generally invest in high-quality, short-term debt securities, including U.S. government securities, securities issued by domestic and foreign banks, such as certificates of deposit and bankers' acceptances, repurchase agreements, asset-backed securities, high-grade commercial paper and corporate short-term obligations.

##### Net Patient Accounts Receivable and Net Patient Services Revenues

Net patient accounts receivable have been adjusted to the estimated amounts expected to be collected. These estimated amounts are subject to further adjustments upon review by third-party payors.

The provision for bad debts is based upon management's assessment of historical and expected net collections, taking into consideration historical business and economic conditions, trends in health care coverage and other collection indicators. Management routinely assesses the adequacy of the allowances for uncollectible accounts based upon historical write-off experience by payor category. The results of these reviews are used to modify, as necessary, the provision for bad debts

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 1. Summary of Significant Accounting Policies (continued)

and to establish appropriate allowances for uncollectible net patient accounts receivable. After satisfaction of amounts due from insurance, CHI follows established guidelines for placing certain patient balances with collection agencies, subject to the terms of certain restrictions on collection efforts as determined by each facility. The provision for bad debts is presented on the consolidated statement of operations as a deduction from patient services revenues (net of contractual allowances and discounts) since CHI accepts and treats all patients, regardless of their ability to pay.

For the year ended June 30, 2016, CHI added approximately \$93.3 million in net patient and other accounts receivable due to the acquisition of various new subsidiaries – see Note 3, *Acquisitions, Affiliations and Divestitures*.

Details of CHI's allowance activity are as follows (in thousands):

	<b>Reserve for Contractual Allowance</b>	<b>Allowance for Bad Debt</b>	<b>Reserve for Charity</b>	<b>Total Accounts Receivable Allowances</b>
Balance at July 1, 2015	\$ (3,712,688)	\$ (903,127)	\$ (304,135)	\$ (4,919,950)
Additions	(36,732,943)	(879,841)	(903,790)	(38,516,574)
Reductions	36,469,175	814,821	1,029,754	38,313,750
Balance at June 30, 2016	(3,976,456)	(968,147)	(178,171)	(5,122,774)
Additions	<b>(29,190,851)</b>	<b>(687,411)</b>	<b>(832,701)</b>	<b>(30,710,963)</b>
Reductions	<b>29,077,143</b>	<b>647,635</b>	<b>775,214</b>	<b>30,499,992</b>
Balance at March 31, 2017	<b><u>\$ (4,090,164)</u></b>	<b><u>\$ (1,007,923)</u></b>	<b><u>\$ (235,658)</u></b>	<b><u>\$ (5,333,745)</u></b>

CHI records net patient services revenues in the period in which services are performed. CHI has agreements with third-party payors that provide for payments at amounts different from its established rates. The basis for payment under these agreements includes prospectively determined rates, cost reimbursement and negotiated discounts from established rates, and per diem payments. Net patient services revenues are reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments due to future audits, reviews and investigations, and excluding estimated amounts considered uncollectible. The differences between the estimated and actual adjustments are recorded as part of net patient services revenues in future periods, as the amounts become known, or as years are no longer subject to such audits, reviews and investigations.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

##### **Investments and Assets Limited as to Use**

Investments and assets limited as to use include assets set aside by CHI for future long-term purposes, including capital improvements and self-insurance. In addition, assets limited as to use include amounts held by trustees under bond indenture agreements, amounts contributed by donors with stipulated restrictions, and amounts held for Mission and Ministry programs.

CHI has designated its investment portfolio as trading as the portfolio is actively managed to achieve investment returns. Accordingly, unrealized gains and losses on marketable securities are reported within excess of revenues over expenses. In addition, cash flows from the purchases and sales of marketable securities are reported as a component of operating activities in the accompanying consolidated statements of cash flows.

Direct investments in equity securities with readily determinable fair values and all direct investments in debt securities have been measured at fair value in the accompanying consolidated balance sheets. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in excess of revenues over expenses unless the income or loss is restricted by donor or law.

Investments in limited partnerships and limited liability companies are recorded using the equity method of accounting (which approximates fair value as determined by the net asset values of the related unitized interests) with the related changes in value in earnings reported as investment income in the accompanying consolidated financial statements.

##### **Inventories**

Inventories, primarily consisting of pharmacy drugs and medical and surgical supplies, are stated at the lower of cost (first-in, first-out method) or market.

##### **Assets and Liabilities 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. 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 firm offers, discounted cash flows and incremental direct costs to transact a sale (Level 2 and Level 3 inputs).

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 1. Summary of Significant Accounting Policies (continued)

##### Property and Equipment

Property and equipment are stated at historical cost or, if donated or impaired, at fair value at the date of receipt or impairment. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Buildings and improvements are depreciated over estimated useful lives of 5 to 84 years, equipment over 3 to 30 years, and land improvements over 2 to 25 years. For property and equipment under capital lease, amortization is determined over the shorter period of the lease term or the estimated useful life of the property and equipment.

For the nine months ended March 31, 2017, and as part of CHI's long-term effort to improve the mix of owned and leased assets, CHI sold various real estate assets and entered into operating lease agreements with the buyers. The assets had a total net book value of \$211.8 million, including \$5.1 million of net intangible assets, and were sold for gross proceeds of \$247.7 million, resulting in the recognition of a \$20.1 million gain on sale reflected on the consolidated statement of operations for the nine months ended March 31, 2017, as well as \$11.0 million in long-term deferred gains and \$1.2 million in short-term deferred gains reflected in other long-term liabilities and accrued expenses, respectively, on the consolidated balance sheet, which will be amortized over the lease term. Additionally, CHI sold various other assets during the three months ended March 31, 2017, for net proceeds of \$101.7 million reflected as gain on sale on the consolidated statement of operations.

Interest cost incurred during the period of construction of major capital projects is capitalized as a component of the cost of acquiring those assets. Capitalized interest of \$3.1 million and \$3.5 million was recorded in the three months ended March 31, 2017 and 2016, respectively, and \$9.3 million and \$13.9 million was recorded in the nine months ended March 31, 2017 and 2016, respectively.

Costs incurred in the development and installation of internal-use software are expensed if they are incurred in the preliminary project stage or post-implementation stage, while certain costs are capitalized if incurred during the application development stage. Internal-use software is amortized over its expected useful life, generally between 2 and 15 years, with amortization beginning when the project is completed and the software is placed in service.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 1. Summary of Significant Accounting Policies (continued)

##### Investments in Unconsolidated Organizations

Investments in unconsolidated organizations are accounted for under the cost or equity method of accounting, as appropriate, based on the relative percentage of ownership and degree of influence over that organization. The income or loss on equity method investments is recorded in the consolidated statements of operations as changes in equity of unconsolidated organizations.

##### Intangible Assets and Goodwill

Intangible assets are comprised primarily of trade names, which are amortized over the estimated useful lives ranging from 10 to 25 years using the straight-line method. The weighted average useful life of the trade names is 16 years. Amortization expense of \$2.5 million and \$3.2 million was recorded in the three months ended March 31, 2017 and 2016, respectively, and \$9.2 million and \$9.5 million was recorded in the nine months ended March 31, 2017 and 2016, respectively.

Goodwill is not amortized but is subject to annual impairment tests during the third quarter of the fiscal year, as well as more frequent reviews whenever circumstances indicate a possible impairment may exist; no such circumstances were identified at March 31, 2017, with the exception of the Houston MBO discussed below. Impairment testing of goodwill is done at the reporting unit level by comparing the fair value of the reporting unit's net assets with the carrying value of the reporting unit's net assets, including goodwill. Each MBO is defined as a reporting unit for purposes of impairment testing. The fair value of net assets is generally estimated based on quantitative analysis of discounted cash flows (Level 3 measurement). The fair value of goodwill is determined by assigning fair values to assets and liabilities, with the remaining fair value reported as the implied fair value of goodwill.

Effective in November 2016 and January 2017, the Houston MBO acquired various physician and diagnostic operations in Texas, which resulted in the recognition of \$43.9 million of total goodwill, calculated as the difference between the consideration paid and the fair value of assets acquired and liabilities assumed. Based upon the Houston MBO's quantitative goodwill analysis performed as of June 30, 2016, which determined that all of the Houston MBO's goodwill balances were impaired, CHI performed a goodwill impairment review of the Houston MBO as of December 31, 2016 and March 31, 2017. The goodwill impairment reviews indicated that the fair value of the Houston MBO's net assets remained below its carrying value and could not support a goodwill balance. As a result, CHI determined that the \$34.4 million and \$9.5 million of goodwill recorded

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 1. Summary of Significant Accounting Policies (continued)

in November 2016 and January 31, 2017, respectively, was impaired and impairment charges were recorded in the consolidated statements of operations for the three months ended December 31, 2016 and March 31, 2017, respectively.

As of June 30, 2016, CHI revised the Houston MBO's projected cash flows due to operating results in the fourth quarter of fiscal year 2016 being below historical run rates. As a result of this update, CHI determined that \$111.2 million of goodwill attributable to the Houston MBO operations was impaired and an impairment charge was recorded on the consolidated statement of operations for the fourth quarter of fiscal year 2016.

The changes in the carrying amount of goodwill and intangibles are as follows as of the beginning of each fiscal period presented (in thousands):

	<b>March 31, 2017</b>	<b>June 30, 2016</b>
Intangible assets, beginning of period	\$ 251,776	\$ 238,491
Current year acquisitions	2,719	13,285
Other adjustments	(11,325)	—
Intangible assets, end of period	<u>243,170</u>	<u>251,776</u>
Accumulated amortization, beginning of period	(50,680)	(38,140)
Intangible amortization expense	(9,181)	(12,783)
Other adjustments	8,719	243
Accumulated amortization, end of period	<u>(51,142)</u>	<u>(50,680)</u>
Intangible assets, net	<u>192,028</u>	<u>201,096</u>
Goodwill, beginning of period	261,742	350,149
Current year acquisitions	67,567	22,766
Impairments	(43,865)	(111,173)
Other adjustments	(271)	—
Goodwill, end of period	<u>285,173</u>	<u>261,742</u>
Total intangible assets and goodwill, net	<u><u>\$ 477,201</u></u>	<u><u>\$ 462,838</u></u>

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 1. Summary of Significant Accounting Policies (continued)

##### Notes Receivable and Other Assets

Other assets consist primarily of notes receivable, pledges receivable, deferred compensation assets, long-term prepaid service contracts, deposits and other long-term assets. Notes receivable from related entities at June 30, 2016, included balances from Bethesda Hospital, Inc. (Bethesda), the non-CHI joint operating agreement (JOA) partner in the Cincinnati, Ohio, JOA. As of June 30, 2016, Bethesda was a Designated Affiliate in the CHI credit group under the Capital Obligation Document (COD). In February 2017, Bethesda repaid its notes receivable balance of \$139.7 million payable to CHI and is no longer considered a Designated Affiliate in the CHI credit group under the COD.

A summary of notes receivable and other assets is as follows (in thousands):

	<b>March 31, 2017</b>	<b>June 30, 2016</b>
Notes receivable –		
From related entities	\$ 201	\$ 148,289
Other	20,513	36,384
Long-term pledge receivables	37,403	36,324
Reinsurance recoverable on unpaid losses and loss adjustment expense	32,226	32,226
Deferred compensation assets	54,431	81,722
Other long-term assets	94,131	111,577
Total notes receivable and other	<u>\$ 238,905</u>	<u>\$ 446,522</u>

##### Net Assets

Temporarily restricted net assets are those whose use has been limited by donors to a specific time period or purpose. Permanently restricted net assets consist of gifts with corpus values that have been restricted by donors to be maintained in perpetuity, including endowment funds. Temporarily restricted net assets and earnings on permanently restricted net assets, including earnings on endowment funds, are used in accordance with the donor's wishes primarily to purchase equipment, to provide charity care and to provide other health and educational programs and services.



## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

Unconditional promises to receive cash and other assets are reported at fair value at the date the promise is received. Conditional promises and indications of donors' intentions to give are reported at fair value at the date the conditions are met or the gifts are received. All unrestricted contributions are included in the excess of revenue over expenses as donation revenues. Other gifts are reported as either temporarily or permanently restricted if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as donations revenue when restricted for operations or as unrestricted net assets when restricted for property and equipment.

#### **Performance Indicator**

The performance indicator is the excess of revenues over expenses, which includes all changes in unrestricted net assets other than changes in the pension liability funded status, net assets released from restrictions for property acquisitions, cumulative effect of changes in accounting principles, discontinued operations, contributions of property and equipment, and other changes not required to be included within the performance indicator under generally accepted accounting principles.

#### **Operating and Nonoperating Activities**

CHI's primary mission is to meet the health care needs in its market areas through a broad range of general and specialized health care services, including inpatient acute care, outpatient services, physician services, long-term care and other health care services. Activities directly associated with the furtherance of this purpose are considered to be operating activities. Other activities that result in gains or losses peripheral to CHI's primary mission are considered to be nonoperating. Nonoperating activities include investment earnings, gains or losses from bond defeasance, net interest cost and changes in fair value of interest rate swaps, and the nonoperating component of JOA income share adjustments. Any infrequent and nonreciprocal contribution that CHI makes to enter a new market community or to expand upon existing affiliations is also classified as nonoperating.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

##### **Charity Care**

As an integral part of its mission, CHI accepts and provides medically necessary health care to all patients without regard to the patient's financial ability to pay. Services to patients are classified as charity care in accordance with standards established across all MBOs. Charity care represents services rendered for which partial or no payment is expected, and includes the cost of providing services to persons who cannot afford health care due to inadequate resources and/or who are uninsured or underinsured. CHI determines the cost of charity care on the basis of an MBO's total cost as a percentage of total charges, applied to the charges incurred by patients qualifying for charity care under CHI's policy. This amount is not included in net patient services revenue in the accompanying consolidated statements of operations and changes in net assets. The estimated cost of charity care provided was \$59.4 million and \$55.9 million for the three months ended March 31, 2017 and 2016, respectively, and \$174.2 million and \$163.0 million for the nine months ended March 31, 2017 and 2016, respectively.

##### **Other Operating Revenues**

Other operating revenues include services sold to external health care providers, gains on the acquisitions of subsidiaries, cafeteria sales, rental income, retail pharmacy and durable medical equipment sales, auxiliary and gift shop revenues, electronic health records incentive payments, gains and losses on the sales of assets, the operating portion of revenue-sharing income or expense associated with Direct Affiliates that are part of JOAs, premium revenues and revenues from other miscellaneous sources.

##### **Derivative and Hedging Instruments**

CHI uses derivative financial instruments (interest rate swaps) in managing its capital costs. These interest rate swaps are recognized at fair value on the consolidated balance sheets. CHI has not designated its interest rate swaps related to CHI's long-term debt as hedges. The net interest cost and change in the fair value of such interest rate swaps is recognized as a component of nonoperating gains (losses) in the accompanying consolidated statements of operations. It is CHI's policy to net the value of collateral on deposit with counterparties against the fair value of its interest rate swaps in other liabilities on the consolidated balance sheets.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 1. Summary of Significant Accounting Policies (continued)

##### Functional Expenses

CHI provides health care services, including inpatient, outpatient, ambulatory, long-term care and community-based services to individuals within the various geographic areas supported by its facilities. Support services include administration, finance and accounting, information technology, public relations, human resources, legal, mission services and other functions that are supported centrally for all of CHI. Support services expenses as a percentage of total operating expenses were approximately 4.9% and 6.2% for the three months ended March 31, 2017 and 2016, respectively, and 5.5% and 5.8% for the nine months ended March 31, 2017 and 2016, respectively.

##### Restructuring, Impairment and Other Losses

Restructuring, impairment and other losses include charges relating to changes in business operations, severance costs, EPIC go-live support costs, goodwill and long-lived asset impairments, acquisition-related costs, and pension settlement activity. Changes in business operations include costs incurred periodically to implement reorganization efforts within specific operations, in order to align CHI's operations in the most strategic and cost-effective manner.

Following is detail of restructuring, impairment and other losses (thousands):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2017	2016	2017	2016
Impairment charges	\$ 12,237	\$ 32,420	\$ 47,440	\$ 32,454
Changes in business operations	27,387	13,039	92,510	43,842
Severance costs	25,977	12,683	52,267	23,139
Total from continuing operations	65,601	58,142	192,217	99,435
Discontinued operations	—	25,401	1,107	25,396
Total restructuring, impairment and other losses	\$ 65,601	\$ 83,543	\$ 193,324	\$ 124,831

Discontinued operations are reported on the consolidated statements of changes in net assets.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 1. Summary of Significant Accounting Policies (continued)

##### Income Taxes

CHI is a tax-exempt Colorado corporation and has been granted an exemption from federal income tax under Section 501(c)(3) of the Internal Revenue Code. CHI owns certain taxable subsidiaries and engages in certain activities that are unrelated to its exempt purpose and therefore subject to income tax.

Management reviews its tax positions quarterly and has determined that there are no material uncertain tax positions that require recognition in the accompanying consolidated financial statements.

##### Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results could vary from the estimates.

##### New Accounting Pronouncements

**Presentation of Financial Statements of Not-for-Profit Entities** – In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-14, *Not-for Profit Entities (Topic 958)*, to change the way a not-for-profit entity (NFP) classifies and presents net assets on the face of the financial statements, and presents information in the financial statements and notes about the NFP's liquidity, financial performance and cash flows. The amendment changes the way an NFP reports classes of net assets, from the currently required three classes to two, by eliminating the distinction between resources with permanent restrictions and those with temporary restrictions. The amendment also requires the NFP to provide enhanced disclosure about the nature, amounts and effects of the various types of donor-imposed restrictions; the NFP's management of its liquidity to meet short-term demands for cash; and the types of resources used and how they are allocated to carry out the NFP's activities. ASU 2016-14 is effective for fiscal years beginning after December 15, 2017, and for interim periods within fiscal years beginning after December 15, 2018. Early application is permitted.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 1. Summary of Significant Accounting Policies (continued)

**Classification of Certain Cash Receipts and Cash Payments** – In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230)*, to provide guidance on the presentation and classification of eight specific cash flow issues, which includes debt prepayment or debt extinguishment costs, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, distributions received from equity method investees, and separately identifiable cash flows and application of the predominance principle. The objective of the amendment is to reduce the existing diversity in practice. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted.

**Restricted Cash** – In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230)*, to provide guidance on the presentation of restricted cash or restricted cash equivalents in the statement of cash flows. The amendments require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. ASU 2016-18 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted.

**Simplifying the Test for Goodwill Impairment** – In January 2017, the FASB issued ASU No. 2017-04, *Intangibles–Goodwill and Other (Topic 350)*, to provide guidance on simplifying how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of the reporting unit's goodwill with the carrying amount of that goodwill. Instead, the entity will record a goodwill impairment loss based on the excess of the reporting unit's carrying amount of goodwill over its fair value, which is based on the current Step 1. ASU 2017-04 is effective for annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2021. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. CHI elected early adoption of this amendment, which had no impact on its consolidated financial statements.

**Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost** – In March 2017, the FASB issued ASU No. 2017-07, *Compensation – Retirement Benefits (Topic 715)*, to improve the presentation of net periodic pension cost and net periodic postretirement benefit cost. The amendments in this update require that an employer disaggregate the service cost component and the other components of net benefit cost, and that the service cost component be reflected in the same line item as other employee compensation costs. The other

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 1. Summary of Significant Accounting Policies (continued)

components of net benefit cost would be reported as nonoperating gains (losses) on the consolidated statement of operations. ASU 2017-07 is effective for annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Early adoption is permitted.

#### 2. Joint Operating Agreements and Investments in Unconsolidated Organizations

##### Joint Operating Agreements

CHI participates in JOAs with hospital-based organizations in three separate market areas. The agreements generally provide for, among other things, joint management of the combined operations of the local facilities included in the JOAs through Joint Operating Companies (JOCs). CHI retains ownership of the assets, liabilities, equity, revenues and expenses of the CHI facilities that participate in the JOAs. The financial statements of the CHI facilities managed under all JOAs are included in the CHI consolidated financial statements. Transfers of assets from facilities owned by the JOA participants generally are restricted under the terms of the agreements.

As of March 31, 2017 and June 30, 2016, CHI has investment interests of 65%, 50%, and 50% in JOCs based in Colorado, Iowa, and Ohio, respectively. CHI's interests in the JOCs are included in investments in unconsolidated organizations and totaled \$379.9 million and \$351.9 million at March 31, 2017 and June 30, 2016, respectively. CHI recognizes its investment in all JOCs under the equity method of accounting. The JOCs provide varying levels of services to the related JOA sponsors, and operating expenses of the JOCs are allocated to each sponsoring organization.

##### Investments in Unconsolidated Organizations

CHI holds noncontrolling interests in various organizations, accounted for under the cost or equity method of accounting, as appropriate. Significant investments are described below.

**Conifer Health Solutions (Conifer)** – As of March 31, 2017 and June 30, 2016, CHI holds a 23.8% equity method investment in Conifer totaling \$604.9 million and \$570.7 million, respectively. The investment in Conifer was acquired as part of a multiyear agreement with Conifer where Conifer provides revenue cycle services and health information management solutions for CHI acute care operations. Since CHI was granted incremental shares in Conifer in conjunction with the multiyear agreement with Conifer, CHI also has a deferred income balance related to the

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### **2. Joint Operating Agreements and Investments in Unconsolidated Organizations (continued)**

Conifer agreement of \$438.0 million and \$458.9 million as of March 31, 2017 and June 30, 2016, respectively, reported in other liabilities on the consolidated balance sheets. The deferred income balances are being amortized straight line over the remaining agreement term expiring in January 2033, offsetting revenue cycle services fees paid to Conifer, which are reported in purchased services expense on the consolidated statements of operations.

As a result of CHI recording its incremental equity ownership in Conifer at fair value, the carrying value of its equity method investment in Conifer was \$255.3 million and \$261.8 million greater than CHI's equity interest in the underlying net assets of Conifer as of March 31, 2017 and June 30, 2016, respectively, due to basis differences in the carrying amounts of the tangible and intangible assets of \$188.6 million and \$195.1 million, respectively, and of goodwill of \$66.7 million in both periods. Goodwill is not amortized but is subject to annual impairment tests during the third quarter of the fiscal year, as well as more frequent reviews whenever circumstances indicate a possible impairment may exist. No impairment of goodwill was identified as of March 31, 2017 or June 30, 2016.

The basis differences of the tangible and intangible assets are being amortized over the average useful lives of the underlying assets, ranging from 8 to 25 years, as a reduction of CHI's equity earnings in Conifer.



## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 3. Acquisitions, Affiliations and Divestitures

The following table is a summary of the business combinations and affiliations that occurred in fiscal year 2017 (in thousands):

##### **Fiscal year 2017**

##### Purchase consideration:

Cash	\$ 64,432
Current liabilities	723
Debt	27,755
	<u>\$ 92,910</u>

##### Purchase price allocation:

Inventory	\$ 3,041
Property and equipment	39,681
Intangible assets	11,180
Goodwill	43,865
Current liabilities	(752)
Debt	(4,105)
	<u>\$ 92,910</u>

During fiscal year to date March 31, 2017, CHI entered into various business combinations and affiliations, including the acquisition by a subsidiary of CHI of the operations of a multi-specialty group in the state of Texas. The operations include a general acute care hospital and emergency room, an ambulatory surgery center, a management company and an independent physician association comprising more than 80 health care providers. For the three and nine months ended March 31, 2017, the affiliations and acquisitions reported a combined \$18.8 million and \$33.6 million in operating revenues, respectively, and \$(10.6) million and \$(9.5) million in deficit of revenues over expenses, respectively, in the CHI consolidated results of operations.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 3. Acquisitions, Affiliations and Divestitures (continued)

The following table is a summary of the business combinations and affiliations that occurred in fiscal year 2016 (in thousands):

	Trinity	Brazosport	LUH	Other	Total
<b>Fiscal year 2016</b>					
Purchase consideration:					
Cash	\$ —	\$ —	\$ —	\$ 17,225	\$ 17,225
Noncontrolling interest	—	—	—	9,275	9,275
Business combination gains	72,717	21,293	111,551	17,475	223,036
	72,717	21,293	111,551	43,975	249,536
Equity interest in Trinity	72,392	—	—	—	72,392
	<u>\$ 145,109</u>	<u>\$ 21,293</u>	<u>\$ 111,551</u>	<u>\$ 43,975</u>	<u>\$ 321,928</u>
	Trinity	Brazosport	LUH	Other	Total
<b>Fiscal year 2016</b>					
Purchase price allocation:					
Cash and investments	\$ 133,349	\$ 18,650	\$ 70,416	\$ 5,420	\$ 227,835
Patient and other A/R	40,363	22,191	25,346	5,443	93,343
Other current assets	6,373	3,200	9,775	786	20,134
Property and equipment	57,598	36,292	111,609	16,970	222,469
Intangible assets	210	—	—	19,848	20,058
Other assets	8,962	144	13,276	—	22,382
Current liabilities	(26,246)	(18,777)	(17,455)	(2,994)	(65,472)
Pension liability	(16,408)	—	—	—	(16,408)
Other liabilities	(9,818)	(671)	—	—	(10,489)
Debt	(40,069)	(38,450)	(97,765)	(1,437)	(177,721)
Restricted assets	(9,205)	(1,286)	(3,651)	(61)	(14,203)
	<u>\$ 145,109</u>	<u>\$ 21,293</u>	<u>\$ 111,551</u>	<u>\$ 43,975</u>	<u>\$ 321,928</u>

**Trinity Health System** – Effective February 1, 2016, CHI became the sole owner of Trinity Health System (Trinity) based in Steubenville, Ohio, when it acquired the remaining 50% ownership in Trinity. The other 50% ownership in Trinity was held by Sylvania Franciscan Health (Sylvania), which CHI acquired in November 2014; the remeasurement of Sylvania's investment in Trinity resulted in an immaterial gain on Sylvania's 50% equity ownership. Trinity owns and operates Trinity Medical Center East, Trinity Medical Center West, Tony Teramana Cancer Center and numerous outpatient clinics located in eastern Ohio. The transaction resulted in the recognition of a \$72.7 million gain in the third quarter of fiscal year 2016, calculated as the fair value of identifiable assets acquired and liabilities assumed, determined based upon Level 3 inputs, including estimated future cash flows and probability-weighted performance assumptions. For the

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 3. Acquisitions, Affiliations and Divestitures (continued)

three months ended March 31, 2017, and for the period from February 1, 2016 through March 31, 2016, Trinity reported \$60.7 million and \$39.8 million in operating revenues, respectively, and \$10.5 million and \$6.0 million of excess of revenues over expenses, respectively, in the CHI consolidated results of operations. For the nine months ended March 31, 2017, Trinity reported \$177.4 million in operating revenues and \$20.4 million of excess of revenues over expenses in the CHI consolidated results of operations.

**Brazosport Regional Health System** – Effective February 1, 2016, a consolidated subsidiary of CHI signed an affiliation agreement with Brazosport Regional Health System (Brazosport) in Lake Jackson, Texas, to become part of CHI. Brazosport is a nonprofit health care organization that includes a 158-bed hospital that operates the only Level III trauma center in Brazoria County. The transaction resulted in the recognition of a \$21.3 million gain in the third quarter of fiscal year 2016, calculated as the fair value of identifiable assets acquired and liabilities assumed, determined based upon Level 3 inputs, including estimated future cash flows and probability-weighted performance assumptions. For the three months ended March 31, 2017, and for the period from February 1, 2016 through March 31, 2016, Brazosport reported \$19.1 million and \$14.1 million in operating revenues, respectively, and \$(2.1) million and \$0.1 million of (deficit) excess of revenues over expenses, respectively, on the CHI consolidated results of operations. For the nine months ended March 31, 2017, Brazosport reported \$58.5 million in operating revenues and \$(5.9) million of deficit of revenues over expenses on the CHI consolidated results of operations.

**Longmont United Hospital** – Effective August 1, 2015, a direct affiliate of CHI entered into a Joint Operating and Management Agreement with Longmont United Hospital (LUH) to become the sole and exclusive agent to manage and operate the LUH business for a period of 99 years. The transaction resulted in the recognition of an estimated gain of \$124.4 million for the nine months ended March 31, 2016, and a total gain of \$111.6 million for fiscal year 2016, calculated as the fair value of identifiable assets acquired and liabilities assumed, determined based upon Level 3 inputs, including estimated future cash flows and probability-weighted performance assumptions. For the three months ended March 31, 2017 and 2016, LUH reported \$46.9 million and \$43.5 million in operating revenues, respectively, and \$(2.1) million and \$(1.7) million of deficit of revenues over expenses, respectively, on the CHI consolidated results of operations. For the nine months ended March 31, 2017, and for the period from August 1, 2015 through March 31, 2016, LUH reported \$135.6 million and \$116.0 million in operating revenues, respectively, and \$(11.6) million and \$(7.2) million of deficit of revenues over expenses, respectively, on the CHI consolidated results of operations.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 3. Acquisitions, Affiliations and Divestitures (continued)

Had CHI owned the above acquired entities as of the beginning of the 2016 fiscal year, CHI's unaudited pro forma results for the three months ended March 31, 2016, and nine months ended March 31, 2017 and 2016, would have been as presented below (in thousands):

	<b>Three Months Ended March 31</b>	<b>Nine Months Ended March 31,</b>	
	<b>2016</b>	<b>2017</b>	<b>2016</b>
	<b>Pro Forma Total CHI</b>	<b>Pro Forma Total CHI</b>	<b>Pro Forma Total CHI</b>
Operating revenues	\$ 4,025,602	\$ <b>12,268,684</b>	\$ 11,941,544
Operating income (loss) before restructuring	(114,821)	<b>(228,987)</b>	(321,243)
Excess (deficit) of revenues over expenses	(243,608)	<b>117,786</b>	(722,907)

Unaudited pro forma information is not necessarily indicative of the historical results that would have been obtained had the transaction actually occurred on those dates, or of future results.

**Pathology Associates Medical Laboratories, LLC (PAML)** – In February 2017, CHI entered into a definitive agreement with Laboratory Corporation of America Holdings (LabCorp) to sell all of CHI's interests in PAML to LabCorp, subject to regulatory approval. As part of the agreement, LabCorp will also acquire CHI's direct and indirect interests in three CHI joint ventures with PAML in the states of Colorado, Kentucky and Washington. The agreement will close in stages beginning in May 2017, and continuing through 2018. Regulatory approval was received and nonrefundable sales proceeds attributable to CHI and its affiliates of \$96.7 million were received in May 2017.

**KentuckyOne/UMC JOA dissolution** – In December 2016, KentuckyOne Health, a subsidiary of CHI, and University Medical Center (UMC) agreed to restructure their existing JOA, originally entered into in March 2013, which had given KentuckyOne Health control over substantially all of UMC's operations, including University of Louisville Hospital and the James Graham Brown Cancer Center. Among the various capital investment and funding aspects of the new agreement, the new agreement also calls for UMC to take over the management of UMC operations effective July 1, 2017, at which time CHI would cease consolidating the operations of UMC.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 3. Acquisitions, Affiliations and Divestitures (continued)

For the three months ended March 31, 2017 and 2016, UMC reported total operating revenues of \$125.7 million and \$122.5 million, respectively, and excess of revenues over expenses of \$6.0 million and \$0.7 million, respectively. For the nine months ended March 31, 2017 and 2016, UMC reported total operating revenues of \$382.0 million and \$376.3 million, respectively, and excess of revenues over expenses of \$13.1 million and \$9.8 million, respectively. The CHI consolidated balance sheets also included UMC total assets of \$543.3 million and \$516.9 million as of March 31, 2017 and June 30, 2016, respectively. Upon deconsolidation of UMC, CHI expects to incur a loss of approximately \$279.4 million.

**Dignity Health** – In October 2016, CHI signed a non-binding letter of intent with Dignity Health to explore aligning the organizations. Discussions are anticipated to continue through midyear 2017.

#### Discontinued Operations

In May 2016, CHI approved a plan to sell or otherwise dispose of certain entities of QualChoice Health, Inc. (QualChoice Health), a consolidated CHI subsidiary, whose primary business is to develop, manage and market commercial and Medicare Advantage health insurance programs, as well as a wide range of products and administrative services. The sale of the operations is being actively marketed and is anticipated to close in fiscal year 2017. The QualChoice Health operations are reflected as discontinued operations and held for sale as of March 31, 2017 and June 30, 2016, in accordance with ASU No. 2014-08, *Reporting Discontinued Operations and Disclosure of Disposals of Components of an Entity*, as the operations held for sale are deemed to represent a strategic shift in CHI's operations, which will have a major effect on its financial results.

Effective in fiscal year 2016, CHI sold the operations of the Reading, Pennsylvania, MBO and the Denville, New Jersey, MBO for gross proceeds of \$206.0 million. The Denville MBO sale included \$20.9 million of working capital settlements; as of March 31, 2016, CHI had received \$62.0 million for the sale of the hospital operations of the Denville MBO plus \$16.0 million in estimated working capital settlements net of closing costs. The Reading and Denville MBOs are reflected as discontinued operations in accordance with Accounting Standards Codification (ASC) 205-20, *Discontinued Operations*.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 3. Acquisitions, Affiliations and Divestitures (continued)

The results of operations of QualChoice Health, the Reading MBO and the Denville MBO are reported in the consolidated statements of changes in net assets as discontinued operations.

A reconciliation of major classes of assets and liabilities of the discontinued operations is presented below (in thousands):

	<b>March 31, 2017</b>	<b>June 30, 2016</b>
Net patient accounts receivable	\$ 63	\$ 810
Other accounts receivable	35,076	75,769
Investments held for insurance purposes	130,286	116,950
Property and equipment, net	9,763	12,598
Other assets	12,122	10,171
Total major classes of assets of the discontinued operations	187,310	216,298
Other assets classified as held for sale	3,053	6,987
Total assets classified as held for sale	<u>\$ 190,363</u>	<u>\$ 223,285</u>
Accounts payable and accrued expenses	\$ 47,810	\$ 37,995
Self-insured reserves	64,972	74,629
Other liabilities	4,294	19,190
Total major classes of liabilities of the discontinued operations classified as held for sale	<u>\$ 117,076</u>	<u>\$ 131,814</u>

The \$3.1 million and \$7.0 million of other assets classified as held for sale as of March 31, 2017 and June 30, 2016, respectively, represents real estate assets that are scheduled to be sold in fiscal year 2017, measured at the lower of their carrying amount or fair value, less cost to sell.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 3. Acquisitions, Affiliations and Divestitures (continued)

Operating results of discontinued operations are reported in the accompanying consolidated statements of changes in net assets and are summarized as follows for the three and nine months ended March 31 (in thousands):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2017	2016	2017	2016
Net patient service revenues	\$ 94	\$ 5,958	\$ 385	\$ 81,995
Insurance premium revenues	129,960	139,026	442,646	373,608
Other revenues	142	3,740	3,790	69,933
Total operating revenues	130,196	148,724	446,821	525,536
Salaries, wages and employee benefits	9,403	14,304	30,175	140,021
Medical claims	119,803	136,808	406,661	343,865
Depreciation and amortization	765	1,171	2,050	3,853
Other expenses	8,727	17,200	38,688	96,707
Total operating expenses	138,698	169,483	477,574	584,446
Restructuring and other losses	—	(25,401)	(1,107)	(25,396)
Nonoperating (losses) income	521	1,478	(378)	2,214
Deficit of revenues over expenses	\$ (7,981)	\$ (44,682)	\$ (32,238)	\$ (82,092)

The discontinued operations reported \$0.3 million and \$0.1 million in capital expenditures for the three months ended March 31, 2017 and 2016, respectively, and \$1.2 million and \$0.7 million for the nine months ended March 31, 2017 and 2016, respectively.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 4. Net Patient Services Revenues

Net patient services revenues are derived from services provided to patients who are either directly responsible for payment or are covered by various insurance or managed care programs. CHI receives payments from the federal government on behalf of patients covered by the Medicare program, from state governments for Medicaid and other state-sponsored programs, from certain private insurance companies and managed care programs and from patients themselves. A summary of payment arrangements with major third-party payors follows:

**Medicare** – Inpatient acute care and certain outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge or procedure. These rates vary according to patient classification systems based on clinical, diagnostic and other factors. Certain CHI facilities have been designated as critical access hospitals and, accordingly, are reimbursed their cost of providing services to Medicare beneficiaries. Professional services rendered by physicians are paid based on the Medicare allowable fee schedule.

**Medicaid** – Inpatient services rendered to Medicaid program beneficiaries are primarily paid under the traditional Medicaid plan at prospectively determined rates per discharge. Certain outpatient services are reimbursed based on a cost reimbursement methodology, fee schedules or discounts from established charges.

**Other** – CHI has also entered into payment agreements with certain managed care and commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to CHI under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.



## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 4. Net Patient Services Revenues (continued)

CHI's Medicare, Medicaid and other payor utilization percentages, based upon net patient services revenues before provision for doubtful accounts, are summarized as follows:

	<b>Three Months Ended March 31,</b>		<b>Nine Months Ended March 31,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Medicare	<b>40%</b>	31%	<b>35%</b>	32%
Medicaid	<b>15</b>	13	<b>14</b>	12
Managed care	<b>37</b>	38	<b>38</b>	38
Self-pay	<b>4</b>	3	<b>3</b>	5
Commercial and other	<b>4</b>	15	<b>10</b>	13
	<b>100%</b>	100%	<b>100%</b>	100%

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Estimated settlements related to Medicare and Medicaid of \$139.0 million and \$108.4 million at March 31, 2017 and June 30, 2016, respectively, are included in third-party liabilities. Net patient services revenues from continuing operations decreased \$4.7 million and increased \$14.5 million for the three months ended March 31, 2017 and 2016, respectively, and increased \$48.6 million and \$61.1 million for the nine months ended March 31, 2017 and 2016, respectively, due to favorable changes in estimates related to prior year settlements.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 5. Investments and Assets Limited as to Use

CHI's investments and assets limited as to use are reported on the accompanying consolidated balance sheets as presented in the following table (in thousands):

	<b>March 31, 2017</b>	<b>June 30, 2016</b>
Cash and equivalents	\$ 121,601	\$ 185,325
CHI Investment Program	5,505,724	5,266,787
Marketable equity securities	270,721	342,327
Marketable fixed-income securities	636,340	802,382
Hedge funds and other investments	29,747	24,360
	<u>6,564,133</u>	<u>6,621,181</u>
Less current portion	(34,494)	(63,146)
	<u><u>\$ 6,529,639</u></u>	<u><u>\$ 6,558,035</u></u>

CHI attempts to reduce its market risk by diversifying its investment portfolio using cash equivalents, marketable equity securities, fixed-income securities and alternative investments. Most of the U.S. Treasury, money market funds and corporate debt obligations as well as exchange-traded marketable securities held by CHI and the CHI Investment Program (the Program) have an actively traded market. However, CHI also invests in commercial paper, mortgage-backed or other asset-backed securities, alternative investments (hedge funds, private equity investments, real estate funds, funds of funds, etc.), collateralized debt obligations, municipal securities and other investments that have potential complexities in valuation based upon the current conditions in the credit markets. For some of these instruments, evidence supporting the determination of fair value may not come from trading in active primary or secondary markets. Because these investments may not be readily marketable, the estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had an active market for such investments existed. Such differences could be material. However, management reviews the CHI investment portfolio on a regular basis and seeks guidance from its professional portfolio managers related to U.S. and global market conditions to determine the fair value of its investments. CHI believes the carrying amount of these financial instruments in the consolidated financial statements approximates fair value.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 5. Investments and Assets Limited as to Use (continued)

The majority of all CHI long-term investments are held in the Program. The Program is structured under a Limited Partnership Agreement with CHI as managing general partner and numerous limited partners, most sponsored by CHI. The partnership provides a vehicle whereby virtually all entities associated with CHI, as well as certain other unrelated entities, can optimize investment returns while managing investment risk. Entities participating in the Program that are not consolidated in the accompanying financial statements have the ability to direct their invested amounts and liquidate and/or withdraw their interest without penalty as soon as practicable based on market conditions but within 180 days of notification. The Limited Partnership Agreement permits a simple-majority vote of the noncontrolling limited partners to terminate the partnership. Accordingly, CHI recognizes only the unitized portion of Program assets attributable to CHI and its direct affiliates. Program assets attributable to CHI and its direct affiliates represented 89% of total Program assets at March 31, 2017 and June 30, 2016.

The Program asset allocation is as follows:

	<b>March 31, 2017</b>	<b>June 30, 2016</b>
Equity securities	<b>41%</b>	44%
Fixed-income securities	<b>39</b>	32
Alternative investments	<b>19</b>	23
Cash and equivalents	<b>1</b>	1
	<b>100%</b>	100%

The CHI Finance Committee (the Committee) of the Board of Stewardship Trustees is responsible for determining asset allocations among fixed-income, equity and alternative investments. At least annually, the Committee reviews targeted allocations and, if necessary, makes adjustments to targeted asset allocations. Given the diversity of the underlying securities in which the Program invests, management does not believe there is a significant concentration of credit risk.

The Program allocation to alternative investments is based upon contractual commitment levels to various funds. These commitments are drawn by the fund managers as opportunities arise to invest the capital. As of March 31, 2017, the Program had committed to invest \$800.0 million in 39 funds, of which \$686.5 million had been invested. The remaining \$113.5 million will be invested when,

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 5. Investments and Assets Limited as to Use (continued)

and if, requested by the funds. Alternative investments within the Program have limited liquidity. As of March 31, 2017, illiquid investments not available for redemption totaled \$381.0 million, and investments available for redemption within 180 days at the request of the Program totaled \$765.8 million.

Investment income (loss) comprises the following (in thousands):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2017	2016	2017	2016
Dividend and interest income	\$ 33,219	\$ 37,540	\$ 102,802	\$ 111,562
Net realized gains (losses)	125,644	(31,406)	267,014	10,412
Net unrealized gains (losses)	44,345	34,731	78,129	(253,124)
Total investment income (loss) from continuing operations	203,208	40,865	447,945	(131,150)
Total investment income (loss) from discontinued operations	520	1,478	(378)	2,213
Total investment income (loss)	\$ 203,728	\$ 42,343	\$ 447,567	\$ (128,937)

Net unrealized gains in investments and assets limited to use restricted by donors are recognized within temporarily and permanently restricted net assets on the consolidated balance sheets. At March 31, 2017 and June 30, 2016, cumulative net unrealized gains for investments restricted by donors were \$201.7 million and \$120.1 million, respectively.

Direct expenses of the Program are less than 0.4% of total assets during the prior fiscal year and are estimated to remain below this level in the current fiscal year. Fees paid to the alternative investment managers are not included in the total expense calculation as they are not a direct expense of the Program.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### **6. Fair Value of Assets and Liabilities**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820, *Fair Value Measurement*, establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 inputs) and the lowest priority to unobservable inputs (Level 3 inputs).

The three levels of the fair value hierarchy and a description of the valuation methodologies used for instruments measured at fair value are as follows:

Level 1 – Valuation is based upon quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 – Valuation is based upon quoted prices for similar assets and liabilities in active markets or other inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial asset or liability.

Level 3 – Valuation is based upon other unobservable inputs that are significant to the fair value measurement.

Certain of CHI's alternative investments are made through limited liability companies (LLCs) and limited liability partnerships (LLPs). These LLCs and LLPs provide CHI with a proportionate share of the investment gains (losses). CHI accounts for its ownership in the LLCs and LLPs under the equity method. CHI also accounts for its ownership in the CHI Investment Program under the equity method. As such, these investments are excluded from the scope of ASC 820.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 6. Fair Value of Assets and Liabilities (continued)

Financial assets and liabilities measured at fair value on a recurring basis were determined using the market approach based upon the following inputs at March 31, 2017 and June 30, 2016 (in thousands):

		<b>March 31, 2017</b>			
		<b>Fair Value Measurements at Reporting Date Using</b>			
		<b>(Level 1)</b>	<b>(Level 2)</b>	<b>(Level 3)</b>	
	<b>Fair Value as of March 31</b>	<b>Quoted Prices in Active Markets</b>	<b>Other Observable Inputs</b>	<b>Unobservable Inputs</b>	
<b>Assets</b>					
Assets limited as to use:					
Cash and short-term investments	\$ 121,602	\$ 91,565	\$ 30,037	\$ —	
Equity securities	270,721	270,721	—	—	
Fixed-income securities	636,340	159,136	477,204	—	
Other investments	3,381	—	—	3,381	
Deferred compensation assets:					
Cash and short-term investments	4,451	4,451	—	—	
	<u>\$ 1,036,495</u>	<u>\$ 525,873</u>	<u>\$ 507,241</u>	<u>\$ 3,381</u>	
<b>Liabilities</b>					
Interest rate swaps	\$ 282,770	\$ —	\$ 282,770	\$ —	
Contingent consideration	174,979	—	—	174,979	
Deferred compensation liability	4,451	4,451	—	—	
	<u>\$ 462,200</u>	<u>\$ 4,451</u>	<u>\$ 282,770</u>	<u>\$ 174,979</u>	

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 6. Fair Value of Assets and Liabilities (continued)

		June 30, 2016			
		Fair Value Measurements at Reporting Date Using			
		(Level 1)	(Level 2)	(Level 3)	
	Fair Value as of June 30	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs	
<b>Assets</b>					
Assets limited as to use:					
Cash and short-term investments	\$ 185,325	\$ 183,641	\$ 1,684	\$	—
Marketable equity securities	342,327	342,327	—		—
Marketable fixed-income securities	802,382	143,263	659,119		—
Other investments	428	—	—		428
Deferred compensation assets:					
Cash and short-term investments	8,248	8,248	—		—
	\$ 1,338,710	\$ 677,479	\$ 660,803	\$	428
<b>Liabilities</b>					
Interest rate swaps	\$ 416,277	\$ —	\$ 416,277	\$	—
Contingent consideration	207,204	—	—		207,204
Deferred compensation liability	8,248	8,248	—		—
	\$ 631,729	\$ 8,248	\$ 416,277	\$	207,204

The fair values of the securities included in Level 1 were determined through quoted market prices. Level 1 instruments include money market funds, mutual funds, and marketable debt and equity securities. The fair values of Level 2 instruments were determined through evaluated bid prices based on recent trading activity and other relevant information, including market interest rate curves and referenced credit spreads; estimated prepayment rates, where applicable, are used for valuation purposes and are provided by third-party services where quoted market values are not available. Level 2 instruments include corporate fixed-income securities, government bonds, mortgage and asset-backed securities, and interest rate swaps. The fair values of Level 3 securities are determined primarily through information obtained from the relevant counterparties for such investments. Information on which these securities' fair values are based is generally not readily available in the market. The fair value of the contingent consideration liability was determined based on estimated future cash flows and probability-weighted performance assumptions, discounted to net present value. The contingent consideration liability balance was adjusted to reflect \$33.3 million of payments made since June 30, 2016, and to reflect a \$1.1 million increase for changes in payment assumptions.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 7. Debt Obligations

The following is a summary of debt obligations (dollars in thousands):

	Maturity Date	Interest Rates at March 31, 2017	March 31, 2017	June 30, 2016
<b>Debt secured under the CHI COD</b>				
Variable-rate bonds:				
CHI Series 2004B	2044	1.78%	\$ 54,200	\$ 54,200
CHI Series 2004C	2039	1.15	96,700	96,700
CHI Series 2008A	2037	1.28	119,450	120,175
CHI Series 2008C	2040	1.78	52,990	52,990
CHI Series 2011B	2046	1.43–2.31	158,155	158,155
CHI Series 2011C	2046	1.63	118,000	118,000
CHI Series 2013B	2035	1.91–2.31	200,000	200,000
CHI Series 2013C	2046	2.30	100,000	100,000
CHI Series 2013E Taxable	2046	2.28	125,000	125,000
CHI Series 2013F Taxable	2046	2.15	75,000	75,000
CHI Series 2015-1	2032	1.43	36,700	38,400
CHI Series 2015-2	2027	1.43	63,472	73,700
CHI Series 2015A	2032	1.53–1.60	66,100	69,500
CHI Series 2015B	2042	1.53	27,270	50,000
CHI Series 2016 Taxable	2021	3.53	200,000	—
Commons of Providence Series 2009B	2034	2.54	5,860	—
Providence Care Center Series 2009C	2034	2.54	4,160	—
Providence Residential Community Series 2009A	2034	2.54	6,770	—
Fixed-rate bonds:				
CHI Series 2002A	—	—	—	920
CHI Series 2004A	2034	4.75–5.0	128,285	140,985
CHI Series 2006A	2042	4.00–5.0	268,015	270,635
CHI Series 2008D	2039	5.00–6.38	445,220	452,065
CHI Series 2009A	2040	4.00–5.5	578,090	672,050
CHI Series 2009B	2040	1.88–5.25	208,560	217,720
CHI Series 2011A	2041	3.25–5.25	436,470	451,270
CHI Series 2012A	2036	3.50–5.0	199,670	264,170
CHI Series 2012 Taxable	2043	1.60–4.35	1,500,000	1,500,000
CHI Series 2013A	2045	5.00–5.75	600,600	600,600
CHI Series 2013D Taxable	2024	2.60–4.2	540,000	540,000
Madonna Manor Series 2010	2040	7.00	27,510	27,990
St. Clare Commons Series 2012A	2042	3.17	31,140	31,720
St. Joseph Manor Series 1997B	2028	5.38	13,895	13,895
St. Joseph Regional Health Center Series 1993B	2019	6.00	6,010	8,760
St. Joseph Regional Health Center Series 1997A	2028	5.38	36,472	45,017
St. Joseph Regional Health Center Series 2014	2032	2.84	25,255	25,255



## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 7. Debt Obligations (continued)

	Maturity Date	Interest Rates at March 31, 2017	March 31, 2017	June 30, 2016
<b>Debt secured under the CHI COD (continued)</b>				
Bank line of credit	6/2017	2.11%	\$ 250,000	\$ 250,000
Bank line of credit	—	—	—	200,000
Bank loan	12/2017	2.8	333,741	333,741
Commercial paper	2017	1.13	815,519	815,519
Unamortized debt premium and discount, net			25,393	31,580
Unamortized debt issuance costs			(29,026)	(31,295)
<b>Total debt secured under the CHI COD</b>			<b>7,950,646</b>	<b>8,194,417</b>
<b>Other debt</b>				
St. Leonard Master Trust Indenture	2040	6.00–6.63	41,585	41,892
Note payable issued to Episcopal Health Foundation	2020	4.0	167,053	167,053
Capital leases			184,846	177,771
Other debt			461,846	476,141
Total debt obligations			<b>8,805,976</b>	<b>9,057,274</b>
Less amounts classified as current:				
Variable-rate debt with self-liquidity			(96,700)	(96,700)
Commercial paper and current portion of debt			(1,992,114)	(1,769,390)
<b>Long-term debt</b>			<b>\$ 6,717,162</b>	<b>\$ 7,191,184</b>

The fair value of debt obligations was approximately \$8.8 billion at March 31, 2017. Management has determined the carrying values of the variable-rate bonds are representative of fair values as of March 31, 2017, as the interest rates are set by the market participants. The fair value of the fixed-rate tax-exempt bond obligations is determined by applying credit spreads for similar tax-exempt obligations in the marketplace, which are then used to calculate a price/yield for the outstanding obligations (Level 2 inputs).

CHI issues the majority of its debt under the COD and is the sole obligor. Bondholder security resides both in the unsecured promise by CHI to pay its obligations and in its control of its Direct and Designated Affiliates. Covenants include a minimum CHI debt service coverage ratio and certain limitations on secured debt. The Direct Affiliates of CHI, defined as Participants under the COD, have agreed to certain covenants related to corporate existence, maintenance of insurance and exempt use of bond-financed facilities. Effective in September 2016, CHI issued obligations under the COD to support the repayment of three series of previously outstanding Providence, Ohio, bonds (the Ohio bonds); the Ohio bonds were classified as other debt as of June 30, 2016, in the table above. There were no modifications to the payment terms or holders of the Ohio bonds.

Debt issued under the St. Leonard Master Trust Indenture is secured by the property of St. Leonard in Centerville, Ohio, and a pledge of gross revenues.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 7. Debt Obligations (continued)

During March 2017, CHI's long-term credit ratings were adjusted to BBB+ with a stable outlook from Standard & Poor's, and to Baa1 with a negative outlook from Moody's. CHI's long-term credit rating from Fitch remains at BBB+ with a negative outlook.

#### Debt Redemptions and Reissuances

In September 2016, CHI redeemed \$37.1 million of bonds that were originally acquired as part of the LUH business combination in fiscal year 2016. The bond redemption was funded by the issuance of \$34.1 million of commercial paper and restricted investments.

In August 2016, CHI redeemed \$62.0 million of Series 2012A fixed-rate bonds in connection with the sale in the prior fiscal year of the underlying real estate assets. The bond redemption was funded from the real estate sale proceeds and resulted in a loss on redemption of \$8.5 million for the three months ended September 30, 2016.

In December 2016, CHI issued \$200.0 million of Series 2016 Taxable variable-rate bonds. Proceeds were used to repay the \$200.0 million bank line of credit that matured in November 2016.

As discussed in Note 1, *Summary of Significant Accounting Policies – Notes Receivable and Other Assets*, in February 2017, Bethesda repaid its notes receivable to CHI for previously loaned funds. CHI used those proceeds to redeem in February and March 2017 \$97.0 million of Series 2004 and Series 2009 fixed-rate bonds, and \$33.0 million of Series 2015 variable-rate bonds. The bond redemption resulted in a loss on redemption of \$7.7 million for the three months ended March 31, 2017. Bethesda is no longer a Designated Affiliate in the CHI credit group under the COD.

#### Liquidity Facilities, Credit Facilities and Other Lines of Credit

CHI has two types of external liquidity facilities: those that are dedicated to specific series of variable-rate demand bonds (VRDBs) and those that are not dedicated to a particular series of VRDBs but may be used to support CHI's obligations to fund tenders of VRDBs and pay the maturing principal of commercial paper. Liquidity facilities that are dedicated to specific series of bonds were \$1.0 billion and \$824.0 million at March 31, 2017 and June 30, 2016, respectively, of which \$207.4 million and \$5.8 million is classified as current at March 31, 2017 and June 30, 2016, respectively. The remaining \$1.2 billion is reported as long-term debt at both March 31, 2017 and June 30, 2016, due to the repayment terms on any associated drawings extending beyond one year under the terms of the specific agreements.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### **7. Debt Obligations (continued)**

Liquidity facilities not dedicated for specific series of VRDBs but used to support CHI's obligations to fund tenders and to pay maturing principal of commercial paper were \$425.0 million at March 31, 2017 and June 30, 2016. Commercial paper balances of \$815.5 million at March 31, 2017 and June 30, 2016, were classified as current due to maturities of less than one year.

At both March 31, 2017, and June 30, 2016, \$96.7 million of VRDBs was classified as current due to the holder's ability to put such VRDBs back to CHI on a daily basis, after providing a seven-day notice to tender, without liquidity facilities dedicated to these bonds.

CHI had a credit facility with Bank of New York Mellon totaling \$69.0 million at both March 31, 2017 and June 30, 2016, of which letters of credit totaling \$63.8 million and \$63.9 million have been designated for the benefit of third parties at March 31, 2017 and June 30, 2016, respectively, principally in support of the self-insurance programs administered by FIIL. No amounts were outstanding under this credit facility at March 31, 2017 or June 30, 2016.

#### **Interest Rate Swap Agreements**

CHI utilizes various interest rate swap contracts to manage the risk of increased interest rates payable of certain variable-rate bonds. The fixed-payor swap agreements convert CHI's variable-rate debt to fixed-rate debt. Generally, it is CHI policy that all counterparties have an AA rating or better. The swap agreements generally require CHI to provide collateral if CHI's liability, determined on a mark-to-market basis, exceeds a specified threshold that varies based upon the rating on CHI's long-term indebtedness.

The fair value of the swaps is estimated based on the present value sum of anticipated future net cash settlements until the swaps' maturities. Cash collateral balances are netted against the fair value of the swaps, and the net amount is reflected in other liabilities in the accompanying consolidated balance sheets. At March 31, 2017 and June 30, 2016, the net swap liability reflected in other liabilities was \$35.8 million and \$75.1 million, respectively, net of swap collateral posted of \$247.0 million and \$341.1 million, respectively. The change in the fair value of swap agreements was a net gain of \$9.3 million and a net loss of \$(55.9) million for the three months ended March 31, 2017 and 2016, respectively, and a net gain of \$133.1 million and a net loss of \$(81.8) million for the nine months ended March 31, 2017 and 2016, respectively, reflected in realized and unrealized gains (losses) on interest rate swaps in the accompanying consolidated statements of operations.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 7. Debt Obligations (continued)

Based upon the swap agreements in place as of March 31, 2017, a reduction in CHI's credit rating to BBB would obligate CHI to post additional cash collateral of \$29 million. If CHI's credit rating were to fall below BBB, the swap counterparties would have the option to require CHI to settle the swap liabilities at the recorded fair value, which was \$35.8 million as of March 31, 2017.

The following is a summary of interest rate swap contracts (in thousands):

	Maturity Date	Swap Contracts Outstanding		Fair Value Liability (Asset)		Notional Amount	
		March 31, 2017	June 30, 2016	March 31, 2017	June 30, 2016	March 31, 2017	June 30, 2016
Basis swaps	3/2028	1	1	\$ (163)	\$ (736)	\$ 30,000	\$ 30,000
Fixed payor swaps	2028–2047	15	16	281,228	415,308	1,422,776	1,452,710
Total return swaps	2017–2020	25	29	1,705	1,705	188,642	223,787
		<b>41</b>	<b>46</b>	<b>282,770</b>	<b>\$ 416,277</b>	<b>\$ 1,641,418</b>	<b>\$ 1,706,497</b>

#### 8. Retirement Plans

##### CHI Pension Plan

CHI and its direct affiliates maintain a variety of noncontributory, defined benefit retirement plans (Retirement Plans) for their employees. Certain of these plans were frozen in previous fiscal years, and benefits earned by employees through that time period remain in the Retirement Plans, where employees continue to receive interest credits and vesting credits, if applicable. Vesting occurs over a five-year period. Benefits in the Retirement Plans are based on compensation, retirement age and years of service. Substantially all of the Retirement Plans are qualified as church plans and are exempt from certain provisions of both the Employee Retirement Income Security Act of 1974 and Pension Benefit Guaranty Corporation premiums and coverage. Funding requirements are determined through consultation with independent actuaries.

CHI recognizes the funded status (that is, the difference between the fair value of plan assets and the projected benefit obligations) of its Retirement Plans in the consolidated balance sheets, with a corresponding adjustment to net assets. Actuarial gains and losses that arise and are not recognized as net periodic pension cost in the same periods are recognized as a component of changes in net assets.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 8. Retirement Plans (continued)

In January and February 2017, CHI made \$59.8 million in elective contributions to the Retirement Plans. The total expected fiscal year 2017 contributions to the Retirement Plans have been increased to \$66.5 million.

Estimated amounts for the components of net periodic pension expense (income) are summarized in the table below. Amounts will be adjusted at year-end to reflect actual results, based on the final annual actuarial reports (in thousands).

	<b>Three Months Ended March 31,</b>		<b>Nine Months Ended March 31,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Components of net periodic pension (credit) expense:				
Service cost	\$ 2,335	\$ 3,880	\$ 7,005	\$ 11,639
Interest cost	37,915	50,298	113,746	150,894
Expected return on the Plans' assets	(67,925)	(68,680)	(203,776)	(206,039)
Actuarial losses	15,028	9,534	45,084	28,601
	<u>\$ (12,647)</u>	<u>\$ (4,968)</u>	<u>\$ (37,941)</u>	<u>\$ (14,905)</u>

#### CHI 401(k) Retirement Savings Plan

CHI sponsors the CHI 401(k) Retirement Savings Plan (401(k) Savings Plan) for its employees whereby CHI matches 100.0% of the first 1.0% of eligible pay an employee contributes to the plan, and 50.0% of the next 5.0% of eligible pay contributed to the plan, for a maximum employer matching rate of 3.5% of eligible pay. On an annual basis and regardless of whether an employee participates in the 401(k) Savings Plan, CHI will also contribute 2.5% of eligible pay to an employee's 401(k) Savings Plan account. This contribution is made if an employee reaches 1,000 hours in the first year of employment or every calendar year thereafter, and is employed on the last day of the calendar year. An employee is fully vested in the plan for employer contributions after three years of service. CHI recorded 401(k) Savings Plan expense of \$63.7 million and \$65.3 million for the three months ended March 31, 2017 and 2016, respectively, and \$182.4 million and \$164.5 million for the nine months ended March 31, 2017 and 2016, respectively.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 9. Concentrations of Credit Risk

CHI grants credit without collateral to its patients, most of whom are insured under third-party payor agreements. CHI's exposure to credit risk on patient accounts receivable is limited by the geographical diversity of its MBOs. The mix of receivables from patients and third-party payors approximated the following:

	<b>March 31, 2017</b>	<b>June 30, 2016</b>
Medicare	<b>27%</b>	27%
Medicaid	<b>13</b>	11
Managed care	<b>34</b>	33
Self-pay	<b>10</b>	11
Commercial and other	<b>16</b>	18
	<b>100%</b>	100%

CHI maintains long-term investments with various financial institutions and investment management firms through its investment program, and its policy is designed to limit exposure to any one institution or investment. Management does not believe there are significant concentrations of credit risk at March 31, 2017 or June 30, 2016.

#### 10. Commitments and Contingencies

##### Litigation

During the normal course of business, CHI may become involved in litigation. Management assesses the probable outcome of unresolved litigation and records estimated settlements. After consultation with legal counsel, management believes that any such matters will be resolved without material adverse impact to the consolidated financial position or results of operations of CHI.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### 10. Commitments and Contingencies (continued)

##### Health Care Regulatory Environment

The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services and Medicare and Medicaid fraud and abuse. Management believes CHI is in compliance with all applicable laws and regulations of the Medicare and Medicaid programs. Compliance with such laws and regulations is complex and can be subject to future governmental interpretation as well as significant regulatory action, including fines, penalties and exclusion from the Medicare and Medicaid programs. Certain CHI entities have been contacted by governmental agencies regarding alleged violations of Medicare practices for certain services. In the opinion of management after consultation with legal counsel, the ultimate outcome of these matters will not have a material adverse effect on CHI's consolidated financial position.

#### 11. Subsequent Events

CHI's management has evaluated events subsequent to March 31, 2017 through May 19, 2017, which is the date these consolidated financial statements were available to be issued. There have been no material events noted during this period that would either impact the results reflected herein or CHI's results going forward, except as disclosed below.

**KentuckyOne Strategic Repositioning** – In May 2017, CHI approved a plan to sell certain of the KentuckyOne operations located in Louisville, Kentucky. CHI will begin to market the sale of these operations and anticipates closing on a sale by the end of the calendar year.

Estimated results for the KentuckyOne operations being divested were as follows: for the three months ended March 31, 2017 and 2016, total operating revenues of \$231.0 million and \$221.3 million, respectively, and a deficit of revenues over expenses of \$(12.7) million and \$(23.8) million, respectively. For the nine months ended March 31, 2017 and 2016, total operating revenues of \$679.0 million and \$661.5 million, respectively, and a deficit of revenues over expenses of \$(61.0) million and \$(72.0) million, respectively. The CHI consolidated balance sheets also included estimated total assets for the KentuckyOne operations being divested of \$534.9 million and \$485.5 million as of March 31, 2017 and June 30, 2016, respectively.

## Catholic Health Initiatives

### Notes to Consolidated Interim Financial Statements (Unaudited) (continued)

#### **11. Subsequent Events (continued)**

**Debt** – In May 2017, CHI defeased \$38.8 million of bonds that were originally acquired as part of the Brazosport affiliation in February 2016. The bond defeasance was funded from cash on hand and the issuance of commercial paper, and resulted in an estimated loss on defeasance of \$(3.6) million.



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