WHEATON FRANCISCAN SERVICES, INC.

Consolidated Financial Statements and
Supplementary Information

June 30, 2013 and 2012

(With Independent Auditors' Report Thereon)

WHEATON FRANCISCAN SERVICES, INC.

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Independent Auditors' Report

The Board of Directors
Wheaton Franciscan Services, Inc.:

Report on the Financial Statements

We have audited the accompanying consolidated balance sheets of Wheaton Franciscan Services, Inc. (WFSI), which comprise the consolidated balance sheets as of June 30, 2013 and 2012, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements. We did not audit the financial statements of Franciscan Ministries, Inc. (FMI), a wholly owned subsidiary, which statements reflect total assets constituting 4.7% for both 2013 and 2012 and total revenues constituting 1.5% and 1.6% in 2013 and 2012, respectively, of the related consolidated totals. Those statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for FMI, is based solely on the reports of the other auditors.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Wheaton Franciscan Services, Inc. as of June 30, 2013 and 2012, and the results of their operations and their cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

Other Matter

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary information included in schedules 1 through 6 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

Chicago, Illinois
October 22, 2013

WHEATON FRANCISCAN SERVICES, INC.

Consolidated Balance Sheets

June 30, 2013 and 2012

(In thousands)

Assets		**2013**	**2012**
Current assets:			
Cash and cash equivalents	$	25,660	59,870
Short-term investments		11,448	41,353
Assets whose use is limited – required for current liabilities		57,286	56,951
Patient accounts receivable, net of uncollectible accounts of approximately $56,767 in 2013 and $55,626 in 2012		220,309	201,437
Securities lending collateral		—	4,514
Inventories of supplies		25,229	25,309
Prepaid expenses and other		46,285	42,225
Total current assets		386,217	431,659
Noncurrent assets whose use is limited		733,766	722,853
Property, plant, and equipment, net		1,103,788	1,086,294
Other assets:			
Restricted assets		19,288	16,739
Deferred expenses, net		5,367	5,523
Investments in unconsolidated affiliates		24,472	22,198
Other long-term assets		28,988	25,067
Total other assets		78,115	69,527
Total assets	$	2,301,886	2,310,333
Liabilities and Net Assets			
Current liabilities:			
Current installments of long-term debt – bonds	$	11,760	9,255
Long-term debt subject to short-term remarketing agreements		39,978	40,038
Current installments of long-term debt – mortgages		8,234	1,912
Accounts payable and accrued expenses		255,221	265,571
Payable under securities lending agreement		—	4,514
Estimated third-party payor settlements		18,817	22,383
Total current liabilities		334,010	343,673
Long-term debt, excluding current installments and net unamortized bond issue premiums – bonds		699,131	712,233
Long-term debt, excluding current installments – mortgages		30,738	36,298
Accrued pension liability		136,712	298,198
Other		101,913	98,008
Total liabilities		1,302,504	1,488,410
Net assets:			
Unrestricted		980,094	805,184
Temporarily restricted		16,190	13,842
Permanently restricted		3,098	2,897
Total net assets		999,382	821,923
Total liabilities and net assets	$	2,301,886	2,310,333

See accompanying notes to consolidated financial statements.

WHEATON FRANCISCAN SERVICES, INC.

Consolidated Statements of Operations

Years ended June 30, 2013 and 2012

(In thousands)

	2013	2012
Net patient service revenues before bad debt	$ 1,642,700	1,622,196
Provision for bad debts	75,197	80,564
Net patient service revenues	1,567,503	1,541,632
Other revenues:		
Other	194,413	180,144
Net assets released from restrictions	1,499	1,766
Total revenues	1,763,415	1,723,542
Expenses:		
Salaries and fringe benefits	1,015,594	986,429
Purchased services, supplies, and other	566,539	550,361
Interest	33,119	34,346
Depreciation and amortization	108,675	108,841
Total expenses	1,723,927	1,679,977
Income from operations	39,488	43,565
Nonoperating gains (losses):		
Investment return	26,242	17,517
Loss on early extinguishment of debt	—	(123)
Loan forgiveness	—	797
Swap valuation adjustments	2,037	(1,294)
Loss on sale of business assets	—	(770)
Other, net	855	(22,369)
Nonoperating gains (losses), net	29,134	(6,242)
Revenues and gains in excess of expenses and losses before discontinued operations	68,622	37,323
Gain from discontinued operations (including loss on sale of $2,318 in 2012)	—	4,403
Revenues and gains in excess of expenses and losses	68,622	41,726
Other changes in unrestricted net assets:		
Net assets released from restrictions used for purchase of property, plant, and equipment	2,135	2,707
Change in unrecognized net defined-benefit plan costs	103,708	(151,426)
Equity transactions of unconsolidated affiliates and other, net	445	(3,903)
Change in unrestricted net assets	$ 174,910	(110,896)

See accompanying notes to consolidated financial statements.

WHEATON FRANCISCAN SERVICES, INC.

Consolidated Statements of Changes in Net Assets

Years ended June 30, 2013 and 2012

(In thousands)

		2013	2012
Unrestricted net assets:			
Revenues and gains in excess of expenses and losses	$	68,622	41,726
Net assets released from restrictions used for purchase of property, plant, and equipment		2,135	2,707
Change in unrecognized net defined-benefit plan costs		103,708	(151,426)
Equity transactions of unconsolidated affiliates and other, net		445	(3,903)
Change in unrestricted net assets		174,910	(110,896)
Temporarily restricted net assets:			
Contributions for specific purposes		5,557	4,417
Net assets released from restrictions used for purchase of property, plant, and equipment		(2,135)	(2,707)
Net assets released from restrictions for operations		(1,499)	(1,766)
Investment income		425	486
Equity transactions of unconsolidated affiliates and other, net		—	(2,232)
Change in temporarily restricted net assets		2,348	(1,802)
Permanently restricted net assets:			
Contributions for endowment funds		—	100
Investment income		201	34
Change in permanently restricted net assets		201	134
Change in net assets		177,459	(112,564)
Net assets at beginning of year		821,923	934,487
Net assets at end of year	$	999,382	821,923

See accompanying notes to consolidated financial statements.

WHEATON FRANCISCAN SERVICES, INC.

Consolidated Statements of Cash Flows

Years ended June 30, 2013 and 2012

(In thousands)

		2013	2012
Cash flows from operating activities:			
Change in net assets	$	177,459	(112,564)
Adjustments to reconcile change in net assets to net cash provided by operating activities:			
Gain from discontinued operations		—	(4,403)
Depreciation and amortization		108,675	108,841
Provision for bad debts		75,197	80,564
Amortization of bond issuance costs and premiums or discounts included in interest expense		(1,134)	(1,073)
Net realized and change in unrealized gains and losses on investments		(2,332)	3,162
Loss on early extinguishment of debt		—	123
Loan forgiveness		—	(797)
Loss on sale of business assets		—	770
Net assets released from restrictions and used for operations		1,499	1,766
Restricted contributions and investment income		(6,183)	(5,037)
Income of unconsolidated affiliates		(18,456)	(16,508)
Investment in unconsolidated affiliates, net of cash distributions		16,182	15,028
Change in unrecognized net defined-benefit plan costs, net of additional pension contribution in 2013 of $57,777 and 2012 of $17,488		(161,486)	133,938
Equity transactions of unconsolidated affiliates and other		(445)	6,135
Nonoperating gains – swap valuation adjustments		(2,037)	1,294
Changes in assets and liabilities:			
Patient accounts receivable		(94,069)	(96,865)
Estimated third-party payor settlements, net		(3,566)	4,245
Inventories of supplies		80	(1,055)
Prepaid expenses and other		(4,172)	5,012
Deferred tax assets, net		—	13,408
Accounts payable and accrued expenses		(10,350)	9,441
Other liabilities		5,942	(6,924)
Net cash provided by continuing operating activities		80,804	138,501
Net cash used in operating activities of discontinued operations		—	(448)
Cash flows from investing activities:			
Purchase of property, plant, and equipment		(125,371)	(111,161)
Gross purchases of investments		(702,124)	(1,288,919)
Gross sales or maturities of investments		723,113	1,141,495
Proceeds from sale of business and other assets		—	167,565
Net change in notes receivable and other		(4,719)	145
Net change in restricted assets		(2,549)	1,668
Net cash used in continuing investing activities		(111,650)	(89,207)
Cash flows from financing activities:			
Repayments of long-term debt – bonds		(9,255)	(35,790)
Repayments of long-term debt – mortgages		(11,798)	(2,416)
Proceeds from issuance of long-term debt-mortgages		12,560	—
Transfers from (to) unconsolidated affiliates and other		445	(2,600)
Net assets released from restrictions and used for operations		(1,499)	(1,766)
Proceeds from restricted contributions and investment income		6,183	5,037
Net cash used in continuing financing activities		(3,364)	(37,535)
Net change in cash and cash equivalents		(34,210)	11,311
Cash and cash equivalents at beginning of year		59,870	48,559
Cash and cash equivalents at end of year	$	25,660	59,870
Supplemental disclosure of cash flow information:			
Cash paid for interest, net of amounts capitalized	$	34,443	35,637

See accompanying notes to consolidated financial statements.

(1) Organization

Wheaton Franciscan Services, Inc. (WFSI) is organized as an Illinois not-for-profit organization and operates under the tenets of the Roman Catholic Church and in accordance with the philosophy and values of the Franciscan Sisters. WFSI's subsidiaries provide: (1) general healthcare services to residents within their geographic locations including inpatient, outpatient, emergency room, physician, long-term care, and other related services and (2) affordable housing for low-income families and the elderly. Expenses included in the accompanying consolidated financial statements relate primarily to the provision of healthcare services, housing services, and general and administrative costs.

(2) Basis of Consolidation

WFSI considers all wholly owned or controlled entities in which it has an economic interest as subsidiaries for consolidated financial statement purposes. The accompanying consolidated financial statements include WFSI and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

WFSI and its subsidiaries are not-for-profit corporations as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code, except as follows:

- Wheaton Franciscan Holdings, Inc., Wheaton Franciscan Provider Network, Inc., Wheaton Franciscan Enterprises, Inc., and Wheaton Franciscan Medical Group – Sussex are for-profit organizations.
- Northeast Iowa Real Estate Investments, Ltd. is a not-for-profit corporation exempt from federal income taxes on related income under Section 501(c)(2) of the Code.

WFSI and certain of its subsidiaries (herein referred to as The Obligated Group) entered into a Master Trust Indenture (MTI), dated as of June 1, 1985 and amended and restated as of April 22, 2004, in order to obtain financing or refinancing for the acquisition or betterment of various hospital and long-term care facilities. The Obligated Group members comprise the following at June 30, 2013:

Wheaton Franciscan Services, Inc.
Southeast Wisconsin Region:
  Wheaton Franciscan Healthcare – Southeast Wisconsin, Inc.
  Wheaton Franciscan, Inc. (previously named St. Joseph Regional Medical Center, Inc., The Heart Hospital of Wisconsin, Inc., and Wheaton Franciscan Healthcare – Elmbrook Memorial, Inc.)
  Wheaton Franciscan Healthcare – St. Francis, Inc.
  Wheaton Franciscan Healthcare – Franklin, Inc.
  Wheaton Franciscan Healthcare – All Saints, Inc.
  Wheaton Franciscan Medical Group, Inc.
Marianjoy Rehabilitation Hospital & Clinics, Inc.

Iowa Region:
Wheaton Franciscan Healthcare-Iowa Inc.
Covenant Medical Center, Inc.

St. Catherine's Hospital, Inc. (St. Catherine's)

The non-Obligated Group members are as follows:

O.S.F. Services, Inc.

Southeast Wisconsin Region:
Wheaton Franciscan Healthcare-Terrace at St. Francis, Inc.
Wheaton Franciscan Home Health and Hospice, Inc.
Wheaton Franciscan Healthcare-Pharmacy Enterprises and Franciscan Woods, Inc.
Wheaton Franciscan Holdings, Inc.

Marianjoy Region:
Marianjoy, Inc.
Rehabilitation Medicine Clinic, Inc.

Iowa Region:
Sartori Memorial Hospital, Inc.
Mercy Hospital of Franciscan Sisters, Inc.

Franciscan Ministries, Inc.

(3) Summary of Significant Accounting Policies

- The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.
- The consolidated statements of operations include revenues and gains in excess of expenses and losses. Transactions deemed by management to be ongoing, major, or central to the provision of healthcare services are reported as revenue and expenses. Transactions incidental to the provision of healthcare services are reported as nonoperating gains and losses.
- Net patient service revenues are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.
- Cash and cash equivalents include demand deposits and investments in highly liquid debt instruments with a maturity of three months or less at the time of purchase, excluding amounts

(Continued)

presented as assets whose use is limited and restricted assets. Short-term investments are comprised of highly liquid debt instruments with maturity greater than three months and less than 12 months at the time of purchase.

- Inventories of supplies are stated at the lower of cost (first-in, first-out) or market.
- Investments are measured at fair value in the accompanying consolidated balance sheets. Fair value is determined primarily on the basis of quoted market prices or observable market inputs. All investments are classified as trading securities. Investment income or loss (including realized gains and losses on investments, unrealized gains and losses on trading securities, interest, and dividends) is included in revenues and gains in excess of expenses and losses unless the income or loss is restricted by donors, in which case the investment return is recorded directly to temporarily or permanently restricted net assets. Unrealized gains and losses on investments designated as other-than-trading securities are excluded from income from operations.
- Assets whose use is limited include assets set aside by the boards of directors for specific purposes, OSF Services, Inc., and deferred compensation plans, over which the boards retain control and may at their discretion subsequently use for other purposes; assets held under escrow agreements; assets held by trustees under bond indenture agreements; assets posted as collateral for swap agreements; assets held through interests in foundations; assets held by a captive insurance company; and assets held by Franciscan Ministries, Inc. (FMI). Assets whose use is limited, which are required for obligations classified as current liabilities, are reported as current assets in the accompanying consolidated balance sheets.
- Property, plant, and equipment acquisitions are recorded at cost. Property, plant, and equipment donated for operations are recorded as additions to temporarily restricted net assets at fair value at the date of receipt and as net assets released from restriction when the assets are placed in service. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Net interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component cost of acquiring those assets.
- Deferred finance charges are included in deferred expenses and are amortized over the life of the respective debt or underlying liquidity facility, whichever is shorter, using either the straight-line or the weighted average bonds outstanding method. Bond discounts and premiums are amortized over the life of the respective debt using the straight-line or the weighted average bonds outstanding method. Amortization of deferred finance charges and bond discounts and premiums are reflected as a component of interest expense in the accompanying consolidated statements of operations.
- Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income within nonoperating gains (losses) in the period that includes the enactment date. WFSI recognizes the effect of income tax positions only if those

positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs.

At June 30, 2013 and 2012, WFSI had net operating loss (NOL) carryforwards for financial reporting and federal and state income tax purposes aggregating approximately $228 and $501, respectively, for federal and $491 and $716, respectively, for state. Using a federal tax rate of 34.0% and state tax rate of 7.9%, these NOL carryforwards give rise to deferred tax assets before valuation allowance of $116 and $227 at June 30, 2013 and 2012, respectively. The valuation allowance for deferred tax assets was $116 and $227 at June 30, 2013 and 2012, respectively. The NOL carryforwards have expiration dates through 2029. Management evaluates the need to maintain a valuation allowance for deferred tax assets based on the assessment of whether it is more likely than not that deferred tax benefits will be realized through the generation of future taxable income. Appropriate consideration is given to all available evidence, both positive and negative, in assessing the need for a valuation allowance. Amounts released from the valuation allowance are included in other, net in nonoperating gains (losses) in the consolidated statements of operations. The quantitative and qualitative analysis of current and expected earnings, tax-planning strategies, and general business risks resulted in a more likely than not conclusion of being able to realize a significant portion of the deferred tax assets during 2012.

On January 1, 2012, WF-Holdings, Inc. completed a technical transfer of its 50% interest in Midwest Orthopedic Specialty Hospital, LLC. (MOSH) to WFH-Southeast Wisconsin, Inc. Federal and state income tax expense was $21,438 in 2012 reported in other, net nonoperating gains (losses) in the consolidated statements of operations; however, $13,408 was offset by the utilization of NOL carryforwards in 2012.

No other temporary differences have been considered based on materiality to the consolidated financial statements.

- Goodwill is an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognized. Goodwill is to be reviewed for impairment at least annually or whenever events or circumstances indicate that the carrying value may not be recoverable. In September 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-08, *Testing Goodwill for Impairment*, which provides an entity the option to perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount prior to performing the two-step goodwill impairment test. If this is the case, the two-step goodwill impairment test is required. If it is more likely than not that the fair value of a reporting is greater than its carrying amount, the two-step goodwill impairment test is not required. WFSI adopted this guidance in 2013.

If the two-step goodwill impairment test is required, first, the fair value of the reporting unit is compared with its carrying value including goodwill. If the fair value of the reporting unit is less than its carrying value, an indication of goodwill impairment exists for the reporting unit and the entity must perform step two of the impairment test (measurement). Under step two, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit in a manner similar to a purchase price allocation and the residual fair value after this allocation is the implied fair value of the reporting unit goodwill. Fair value of the reporting unit is determined using a discounted cash flow analysis. If the fair value of the reporting unit exceeds its carrying value, step two does not need to be performed.

WFSI performed its annual goodwill impairment test as of June 30, 2013 and did not identify any impairment issues. The fair value of the reporting unit is in excess of its carrying value. Goodwill totaling $5,136 at June 30, 2013 and 2012 is reported in the accompanying consolidated balance sheets within other long-term assets.

WFSI has net amortizable intangible assets of $10,110 and $5,818 at June 30, 2013 and 2012, respectively, included in other long-term assets on the consolidated balance sheets, which are being amortized from 2 to 10 years. WFSI recorded amortization expense of $1,019 and $1,113 for 2013 and 2012, respectively.

- Long-lived assets (including property, plant, and equipment, goodwill, and other intangibles) are periodically assessed for recoverability based on the occurrence of a significant adverse event or change in the environment in which WFSI operates, or if the expected future cash flows generated by the long-lived asset (undiscounted and without interest) are less than the carrying amount of the long-lived asset. An impairment loss is recognized in the period an impairment determination is made to the extent the impaired long-lived asset's carrying value exceeds its fair value.
- Amounts reported as loss on sale of business assets represent the loss by WFSI of its interest in various healthcare-related assets and joint ventures.
- Changes in unrestricted net assets, which are excluded from revenues and gains in excess of expenses and losses, consistent with industry practice, include unrealized gains and losses on investments on other-than-trading securities, permanent transfers of assets to and from unconsolidated subsidiaries and affiliates for other than goods and services, contributions of long-lived assets (including assets acquired using contributions, which by donor restriction were to be used for the purposes of acquiring such assets), changes in the funded status of the defined-benefit pension plan, and equity transactions of unconsolidated affiliates.
- Certain subsidiaries of WFSI provide care to patients who meet criteria under the community care program (charity care) without charge or at amounts less than their established rates. Because there is no effort to pursue collection of amounts determined to qualify as charity care, they are not reported as revenues.
- WFSI accounts for discontinued operations under Accounting Standard Codification guidance surrounding accounting for the impairment or disposal of long-lived assets. The guidance requires that a component entity that has been disposed of or is classified as held-for-sale and has operations and cash flows that can be clearly distinguished from the rest of the entity be reported as discontinued operations. In the period that a component entity has been disposed of or is classified as

held-for-sale, the results of operations for current and prior periods are reclassified to discontinued operations in the accompanying consolidated statements of operations.

- Temporarily restricted net assets represent those net assets whose use by WFSI and its subsidiaries has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by WFSI and its subsidiaries in perpetuity. WFSI and its subsidiaries' temporarily restricted net assets are restricted for various programs related to the provision of health and pastoral care. WFSI and its subsidiaries' investment income from permanently restricted net assets is expendable to support healthcare or other donor-designated services.
- Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received, which is then treated as cost. Conditional promises to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reflected as other revenue in the accompanying consolidated statements of operations.
- Gifts of long-lived assets such as land, buildings, and equipment are reported as unrestricted support and are excluded from the revenues and gains in excess of expenses and losses unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted contributions. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.
- Provisions for self-insured liability claims include estimates of the ultimate costs for both reported claims and claims incurred but not reported as of the respective consolidated balance sheet dates.
- ASC No. 815, *Derivatives and Hedging*, requires that an entity recognize all derivatives as either assets or liabilities in the consolidated balance sheets and measure those instruments at fair value. The accounting for changes in the fair value of a derivative is dependent upon the intended use of the derivative and the resulting designation. WFSI is involved in various interest rate swap programs. These derivatives are not designated as hedge instruments, and therefore, changes in their fair value are recognized in the consolidated statements of operations as nonoperating gains or losses in the period of change. WFSI is exposed to credit loss in the event of nonperformance by the counterparty in any of its interest rate swap agreements.

  WFSI also maintains interest rate swap agreements, which were originally intended to effectively change the interest rate exposure on Series 1998B Bonds and the St. Francis Series 1997 Bonds, prior to redemption of debt (note 11). Notional amounts on these interest rate swap agreements are being reduced over the original term of the debt agreements to correspond with the originally scheduled reductions in principal of the related bonds. A summary of the outstanding positions under these swaps at June 30, 2013 is as follows:

(In thousands)

	Notional amount	Maturity date	Rate received	Rate paid
$	6,300	January 2015	SIFMA Index	4.83%
	28,000	August 2024	Lesser of SIFMA Index or 72% of LIBOR	4.36

The carrying value equals fair value. As of June 30, 2013 and 2012, the fair value of all outstanding swap agreements was a liability of $4,987 and $7,024, respectively, which is included as a component of other long-term liabilities. For the years ended June 30, 2013 and 2012, WFSI recognized valuation adjustments of $2,037 and ($1,294), respectively, for the change in fair value of all swap agreements. Net payments equal to differentials received or paid under all swap agreements are recognized monthly and amounted to $1,555 and $1,694 in 2013 and 2012, respectively, which have been included as interest expense in the accompanying consolidated statements of operations.

Pursuant to certain terms of its interest rate swap agreements, WFSI was required to post collateral with its counterparty for the full settlement amount of the derivative liabilities related to the floating-to-fixed swaps. As of June 30, 2013 and 2012, WFSI posted $5,548 and $7,658, respectively, of collateral related to these swaps, which are included within the current portion of assets whose use is limited.

- FMI has entered into various regulatory agreements with the U.S. Department of Housing and Urban Development (HUD) that provide both Housing Assistance Payments and Rental Assistance Payments. These subsidy payments are designed to provide for the difference between the cash needs of the housing project and the cash generated by the tenants' rental payments. Tenant leases are generally one year in duration and expire at various times during the year. The HUD subsidies are adjusted at the beginning of the lease to reflect any changes to the tenant's rent payment established during the annual recertification process.
- WFSI applies the provisions of ASC No. 820, *Fair Value Measurements and Disclosures*, for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the consolidated financial statements on a recurring basis. ASC No. 820 defines fair value as 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 No. 820 establishes a framework for measuring fair value and expands disclosures about fair value measurements (note 8).
- WFSI applies the provisions of ASC No. 825-10, *Financial Instruments – Overall*, which gives WFSI the irrevocable option to report most financial assets and financial liabilities at fair value on an instrument-by-instrument basis, with changes in fair value reported in earnings. WFSI has not elected any additional eligible financial assets or financial liabilities to be reported at fair value.

- In August 2010, the FASB issued ASU No. 2010-24, *Presentation of Insurance Claims and Related Insurance Recoveries*. ASU No. 2010-24 clarifies that a healthcare entity should not net insurance recoveries against a related malpractice claim liability or similar liability, which is consistent with the guidance in ASC 210-20, *Balance Sheet – Offsetting*. The provisions of ASU No. 2010-24 were adopted for the year ended June 30, 2013.
- ASU 2011-07, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*. ASU 2011-07 required that entities that recognize significant amounts of patient service revenue at the time the services are rendered even though they do not assess the patient's ability to pay must present the provision for bad debts related to patient service revenue as a deduction from patient service revenue (net of contractual allowances and discounts) on their consolidated statements of operations. The ASU also required disclosures of patient service revenue as well as qualitative and quantitative information about changes in the allowance for doubtful accounts.
- The Medicare and Medicaid Electronic Health Record (EHR) Incentive Programs (the Programs) provide incentive payments to eligible hospitals and professionals as they adopt, implement, upgrade, or demonstrate meaningful use of certified EHR technology in their first year of participation and demonstrate meaningful use for up to five remaining participation years. The Programs define meaningful use as meeting certain core and menu criteria at certain levels dependent upon the program, the stage of meaningful use, and whether the participant is a hospital or provider professional. WFSI accounts for the Programs using International Accounting Standards (IAS) 20, *Accounting for Government Grants and Disclosures of Government Assistance*. WFSI applies the "ratable recognition" approach, which states that the grant income can be recognized ratably over the entire EHR reporting period once the "reasonable assurance" income recognition threshold of IAS 20 is met. For the years ended June 30, 2013 and 2012, WFSI recognized $21,158 and $7,536, respectively, as other revenue related to the Medicare and Medicaid EHR incentives, which have been received or are expected to be received based on certifications prepared by management under the appropriate guidelines for stage 1 meaningful use attestation.

(4) Net Patient Service Revenues

WFSI's hospitals and other patient care facilities have agreements with third-party payors that provide for payments at amounts different from established rates. A summary of the payment arrangements with major third-party payors is as follows:

- ***Medicare*** – Inpatient acute care services, certain outpatient, rehabilitation, and home health services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to their respective patient classification systems that are based on clinical, diagnostic, and other factors. The prospectively determined rates are not subject to retroactive adjustment. The classification of patients under the Medicare prospective payment systems and the appropriateness of patients' admissions are subject to validation reviews. Certain outpatient services and medical education costs related to Medicare beneficiaries are paid based upon either a cost-reimbursement method, established fee screens, or a combination thereof. WFSI is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual reimbursement reports and audits thereof by Medicare fiscal intermediaries. WFSI has received final settlements through FY 2009.

- ***Medicaid*** – Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed in accordance with each state's Medicaid reimbursement program. Reimbursement under these programs is based primarily upon prospectively determined rates

  The states of Illinois, Wisconsin, and Iowa have hospital assessment programs to assist in the financing of their Medicaid programs. Pursuant to these programs, hospitals within the states of Illinois, Wisconsin, and Iowa are required to remit payment to the respective state under a tax assessment formula. WFSI has included its related assessments of $38,932 and $38,535 as purchased services, supplies, and other expense in the accompanying 2013 and 2012 consolidated statements of operations, respectively. The additional Medicaid reimbursement associated with these programs is approximately $109,383 and $105,397 for 2013 and 2012, respectively, and is included in net patient service revenue.

  The aforementioned assessment programs increase the amount of federal matching for the respective Medicaid programs, which is then passed on to hospitals as increased Medicaid reimbursement. Wisconsin's assessment program prohibits the use of assessment revenue to supplant current revenue used to support existing hospital payment levels. The State distributes the assessment revenue as increased rates for both Medicaid and Medicaid HMO patients.

- ***Other*** – WFSI's hospitals and other patient care facilities have also entered into reimbursement agreements with certain commercial insurance carriers, HMOs, and preferred provider organizations. The basis for reimbursement under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined per diem rates.

  Net patient service revenue for the years ended June 30, 2013 and 2012 includes approximately $14,329 and $5,699, respectively, of net favorable retroactively determined reimbursement settlements from prior years with third-party payors. In addition, net patient service revenues for the year ended June 30, 2012 includes approximately $9,117 due to a settlement from Medicare for fiscal years 2007-2011 related to the Rural Floor Budget Neutrality Adjustment Appeal, which was ruled on in June 2012.

Patients' accounts receivable are reduced by an allowance for uncollectible accounts. In evaluating the collectibility of patients' accounts receivable, WFSI analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for uncollectible accounts and provision for bad debts. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, WFSI analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary. For receivables associated with patient responsibility (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the patients are screened against the WFSI charity care policy and uninsured discount policy. For any remaining patient responsibility balance, WFSI records a provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

(In thousands)

WFSI's allowance for uncollectible accounts for self-pay patients, which includes uninsured patients and residual copayments and deductibles for which managed care has already paid, decreased from 91.0% of self-pay accounts receivable at June 30, 2012, to 83.2% of self-pay accounts receivable at June 30, 2013. In addition, WFSI's self-pay write-offs decreased from $82,753 for fiscal year 2012 to $79,861 for fiscal year 2013 due to favorable trends. WFSI has not changed its charity care or uninsured discount policies during fiscal years 2013 or 2012. WFSI does not maintain a material allowance for uncollectible accounts from third-party payors, nor did it have significant write-offs from third-party payors.

WFSI recognizes patient service revenue associated with services provided to patients who have third-party payor coverage on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for charity care, WFSI recognizes revenue for services provided (on the basis of discounted rates, as provided by policy). On the basis of historical experience, a portion of WFSI's uninsured patients will be unable or unwilling to pay for the services provided. Thus, WFSI records a provision for bad debts related to uninsured patients in the period the services are provided. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized in the period from these major payor sources, is as follows:

		2013	2012
Medicare	$	568,268	551,871
Medicaid		243,425	243,574
Managed care/contracted payor		692,160	691,681
Self-pay		105,465	95,647
Other		33,382	39,423
Net patient service revenues	$	1,642,700	1,622,196

(5) Concentration of Credit Risk

Patient care subsidiaries of WFSI grant credit without collateral to their patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors for 2013 and 2012 is as follows:

	2013	2012
Medicare	28.0%	31.5%
Medicaid	9.0	8.3
Managed care	42.8	40.5
Other	20.2	19.7
	100.0%	100.0%

(In thousands)

(6) Uncompensated and Charity Care

WFSI shares its talents and resources to benefit the many communities it serves. This includes providing education to health professional and community members, research, community health improvement offerings, and subsidized health services, in addition to charity care benefits.

For charity care benefits, patient care subsidiaries of WFSI maintain records to identify and monitor the level of charity care they provide. This represents free or discounted health services provided to those who cannot afford to pay and who meet criteria for financial assistance. Charity care is based on estimated cost and does not include bad debt. The level of charity care provided during the years ended June 30, 2013 and 2012 was $43,946 and $37,796, respectively.

(7) Investments

During 1998, WFSI created the Wheaton Franciscan Services, Inc. Investment Trust (the Trust) for the sole purpose of administering a pooled investment program for WFSI, its subsidiaries, and affiliates. WFSI serves as the trustee and is responsible for managing and investing the pooled assets of the Trust. Participants accrue interest based on the Trust's actual realized earnings. The fair value of the assets in the Trust was $669,623 and $712,526 at June 30, 2013 and 2012, respectively, and is recorded as a component of assets whose use is limited.

A summary of the composition of the investment portfolio (including assets whose use is limited and restricted assets) at June 30, 2013 and 2012 is as follows:

		2013	2012
At fair value:			
Cash and cash equivalents	$	45,998	41,067
U.S. government obligations		364,931	374,811
Corporate debt securities		199,200	221,642
Asset-backed securities		27,524	36,335
Equity securities		150,543	136,718
Mutual funds		32,769	26,609
Total investments at fair value		820,965	837,182
At cost:			
Pledges receivable		823	714
Total investments	$	821,788	837,896

(In thousands)

Investments are reported in the accompanying June 30, 2013 and 2012 consolidated balance sheets as follows:

	2013	2012
Short-term investments	$ 11,448	41,353
Assets whose use is limited (current and long-term):		
By boards for specific purposes	597,848	583,916
By boards for deferred compensation plans	33,234	28,173
By boards for Clara Pfaender Fund, Inc.	32,487	32,487
Held by FMI	12,858	11,215
Held by captive insurance company	35,379	40,779
Under escrow agreement	21,078	21,078
Held as collateral for swap agreements	5,548	7,658
Under indenture agreements by trustee	52,620	54,498
Restricted assets	19,288	16,739
Total investments	$ 821,788	837,896

The composition of investment return on the investment portfolio for the years ended June 30, 2013 and 2012 is as follows:

	2013	2012
Interest and dividend income	$ 24,665	25,416
Net realized gains on sale of investments	8,006	7,598
Change in net unrealized gains and losses	(5,674)	(10,760)
	$ 26,997	22,254

Investment returns are included in the accompanying consolidated statements of operations and changes in net assets for the years ended June 30, 2013 and 2012 as follows:

	2013	2012
Other operating revenue	$ 129	4,217
Investment return	26,242	17,517
Temporarily restricted net assets – investment income	425	486
Permanently restricted net assets – investment income	201	34
	$ 26,997	22,254

During 2005, WFSI began participating in a securities lending program. Through this securities lending program, managed by its investment custodian, WFSI loans fixed income and equity securities included in its investment portfolio. In June 2013, WFSI exited the security lending program. At June 30, 2012, the fair value of the securities loaned was $4,380. The custodian's loan agreements require the borrowers to maintain collateral equal to at least 102% of the market value of the securities loaned. This collateral is in the form of cash and cash equivalents and fixed income securities and is revalued on a daily basis. At June 30, 2012, WFSI has presented the collateral received as securities lending collateral within current assets and the obligation to return that collateral as a current liability as payable under securities lending agreement in the accompanying consolidated balance sheets.

(8) Fair Value Measurements

(a) Fair Value of Financial Instruments

The following methods and assumptions were used by WFSI in estimating the fair value of its financial instruments:

- The carrying amount reported in the consolidated balance sheets for the following approximates fair value because of the short maturities of these instruments: cash and cash equivalents, patient accounts receivable, accounts payable and accrued expenses, and estimated third-party payor settlements.
- Assets whose use is limited, short-term investments, securities lending collateral, and restricted assets: equity securities, mutual funds, and direct U.S. government obligations are measured using quoted market prices at the reporting date multiplied by the quantity held. Corporate bonds, notes, and U.S. agency securities are measured using other observable inputs. Corporate debt securities, U.S. governmental agency securities, and asset-backed securities are measured using other observable inputs. The carrying value equals fair value. ASU No. 2009-12, *Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*, which creates a practical expedient allowing measurement of fair value based on the net asset value per share of the investment. Mutual funds are valued using net asset value per share as a practical expedient.
- Interest rate swap agreements: The fair value of interest rate swaps is determined using pricing models developed based on the LIBOR swap rate and other observable market data. The value was determined after considering the potential impact of collateralization and netting agreements, adjusted to reflect nonperformance risk of both the counterparty and WFSI. The carrying value equals fair value.
- The fair value of the fixed-rate long-term debt of WFSI and its subsidiaries was $618,142 and $629,727 at June 30, 2013 and 2012, respectively. The recorded amount of these obligations at June 30, 2013 and 2012 was $594,050 and $603,105, respectively. Fair value of fixed-rate long-term debt is estimated based on the quoted market prices for the same or similar issues or on the current rates offered to WFSI for debt of the same remaining maturities. For variable rate debt, carrying amounts approximate fair value. Fair value was estimated using quoted market prices based upon WFSI's current borrowing rating for rates for similar types of long-term debt securities.

(b) Fair Value Hierarchy

WFSI applies the provision of ASC No. 820, which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between mutual participants at a measurement date. These provisions describe a fair value hierarchy that prioritizes the inputs to valuation techniques 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 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that WFSI has the ability to access at the measurement date.
- Level 2 are observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 inputs are unobservable inputs for the asset or liability. Level 3 assets and liabilities include financial instruments whose value is determined by using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant judgment or estimation.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

(In thousands)

The following table presents assets and liabilities that are measured at fair value on a recurring basis at June 30, 2013:

	Total	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Assets:				
Cash and cash equivalents	$ 25,660	25,660	—	—
Short-term investments:				
Cash and cash equivalents	14	14	—	—
U.S. government obligations	3,507	—	3,507	—
Corporate debt securities	7,927	—	7,927	—
Assets whose use is limited and restricted assets, excluding $823 of pledges receivable:				
Cash and cash equivalents	45,984	45,984	—	—
Mutual funds	32,769	32,769	—	—
U.S. government obligations	361,424	256,662	104,762	—
Corporate debt securities	191,273	—	191,273	—
Asset-backed securities	27,524	4,443	23,081	—
Equity securities	150,543	150,543	—	—
Total assets	$ 846,625	516,075	330,550	—
Liabilities:				
Interest rate swap agreement	$ 4,987	—	4,987	—

(In thousands)

The following table presents assets and liabilities that are measured at fair value on a recurring basis at June 30, 2012:

		Total	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Assets:					
Cash and cash equivalents	$	59,870	59,870	—	—
Short-term investments:					
Cash and cash equivalents		614	614	—	—
U.S. government obligations		13,737	—	13,737	—
Corporate debt securities		27,002	—	27,002	—
Securities lending collateral:					
Cash and cash equivalents		4,514	4,514	—	—
Assets whose use is limited and restricted assets, excluding $714 of pledges receivable:					
Cash and cash equivalents		40,453	40,453	—	—
Mutual funds		26,609	26,609	—	—
U.S. government obligations		361,074	261,162	99,912	—
Corporate debt securities		194,640	—	194,640	—
Asset-backed securities		36,335	3,106	33,229	—
Equity securities		136,718	136,718	—	—
Total assets	$	901,566	533,046	368,520	—
Liabilities:					
Interest rate swap agreement	$	7,024	—	7,024	—

Transfers between Levels

The availability of observable market data is monitored to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period. WFSI evaluated the significance of transfers between levels based upon the nature of the financial instrument and size of the transfer relative to total assets. For the year ended June 30, 2013, there were no significant transfers in or out of Levels 1, 2, or 3.

(In thousands)

(9) Asset Divestitures

Effective January 1995, WFSI and Ministry Health Care (MHC) entered into an integration agreement. This agreement was amended and restated effective October 1, 1997 creating a fully integrated economic system called Affinity. Pursuant to this agreement, WFSI and MHC continued to own and sponsor their respective operating entities within Affinity and participate in the sharing of income (loss) of all Affinity organizations. WFSI has consolidated St. Elizabeth's Hospital, its sponsored organization, in the consolidated financial statements and has reflected its share of the unconsolidated Affinity organizations, except the MHC sponsored organizations, under the equity method of accounting. In June 2011, the board of directors of WFSI approved a plan to sell all of the assets and liabilities of St. Elizabeth's Hospital, which, pursuant to the integration agreement, includes a 50% interest in Affinity. In February 2012, the sale was completed and WFSI received cash proceeds of $167,565 from the sale and the repayment of intercompany debt and recognized a loss on sale of $2,318.

The operations of Affinity and St. Elizabeth's Hospital have been presented in the accompanying consolidated statements of operations within discontinued operations. Further, all net cash flows related to the operating, investing, and financing activities of Affinity and St. Elizabeth's Hospital are reported separately as discontinued operations in the accompanying consolidated statements of cash flows. The sale transaction closed on February 8, 2012.

A summary of the operating components of discontinued operations as of and for the years ended June 30, 2012 is as follows:

Discontinued operations:		
Total revenues and gains	$	98,055
Expenses:		
Salaries and fringe benefits		44,773
Purchased services, supplies, and other		35,742
Provision for bad debts		2,506
Interest		2,448
Depreciation and amortization		5,865
Total expenses		91,334
Income from discontinued operations		6,721
Other changes in unrestricted net assets		(2,751)
Change in unrestricted net assets	$	3,970

(In thousands)

(10) Property, Plant, and Equipment

A summary of property, plant, and equipment at June 30, 2013 and 2012 is as follows:

		2013	2012
Land and land improvements	$	113,969	112,162
Buildings		1,272,944	1,231,210
Building equipment		353,059	334,194
Departmental equipment		610,563	617,105
		2,350,535	2,294,671
Less accumulated depreciation and amortization		1,307,448	1,266,187
		1,043,087	1,028,484
Construction in progress		60,701	57,810
Total property, plant, and equipment, net	$	1,103,788	1,086,294

Construction in progress at June 30, 2013 consists of various expansion and renovation projects. As of June 30, 2013, construction commitments are primarily related to St. Francis Hospital and St. Catherine's expansion project (note 15(c)). During the years ended June 30, 2013 and 2012, WFSI capitalized net interest cost in the amount of $1,553 and $1,687, respectively.

(11) Long-Term Debt – Bonds

Long-term debt – bonds at June 30, 2013 and 2012 are as follows:

		2013	2012
Wheaton Franciscan Services, Inc. (System Financing) – Wisconsin Health and Educational Facilities Authority, Revenue Bonds, Series 2003A (Series 2003A Bonds) with fixed interest rates ranging from 5.0% to 5.5% and varying debt service payments through August 2033	$	99,860	101,925
Wheaton Franciscan Services, Inc. (System Financing) – Wisconsin Health and Educational Facilities Authority, Variable Rate Demand Revenue Bonds, Series 2003B (Series 2003B Bonds) with variable interest rate (effective average interest rate of 0.14% and 0.12% for the years ended June 30, 2013 and 2012, respectively) and debt service payments through August 2033		75,000	75,000

(Continued)

(In thousands)

		2013	2012
Wheaton Franciscan Services, Inc. (System Refinancing) – Wisconsin Health and Educational Facilities Authority Revenue Bonds, Series 2006A (Series 2006A Bonds) with fixed interest rates ranging from 5.00% to 5.25% and varying debt service payments through August 2034	$	289,300	294,095
Wheaton Franciscan Services, Inc. (System Refinancing) – Wisconsin Health and Educational Facilities Authority Revenue Refunding Bonds, Series 2006B (Series 2006B Bonds) with fixed interest rates ranging from 4.000% to 5.125% and varying debt service payments through August 2030		204,890	207,085
Wheaton Franciscan Services, Inc. (System Financing) – Wisconsin Health and Educational Facilities Authority, Variable Rate Demand Revenue Bonds, Series 2007 (Series 2007 Bonds) with variable interest rates (effective average interest rate of 0.14% and 0.12% for the years ended June 30, 2013 and 2012, respectively) and varying debt service payments through August 2036		64,180	64,380
		733,230	742,485
Unamortized net bond issue premiums		17,639	19,041
Total long-term debt		750,869	761,526
Less:			
Current installments of long-term debt		11,760	9,255
Long-term debt subject to short-term remarketing agreements		39,978	40,038
Long-term debt, excluding current installments and net unamortized bond issue premiums	$	699,131	712,233

All of the outstanding long-term bond indebtedness has been issued pursuant to the MTI, and is comprised of unsecured obligations of The Obligated Group. Each member of The Obligated Group has jointly and severally guaranteed the payment of any and all amounts due on the outstanding indebtedness issued under the MTI.

(In thousands)

The following is a summary of the bond insurer and liquidity facility for the outstanding long-term debt:

Outstanding debt series	Liquidity facility
Series 2003B Bonds*	Letter of Credit – U.S. Bank National Association, expiring in December 2016
Series 2007 Bonds*	Letter of Credit – PNC Bank, expiring in December 2016

* Bear interest at a variable rate, which is currently determined weekly

In the event that the letters of credit are not renewed, mandatory redemption provisions become applicable, which require the then outstanding indebtedness to be paid in full or within an 18-month period.

On November 1, 2011, WFSI redeemed at par $5,300, $10,300, and $8,200 of the then outstanding principal balance on the Series 1998A Bank Bonds, Series 1998B Bank Bonds, and Series 1997 Bank Bonds, respectively. The unamortized deferred financing costs and bond discount related to the Series 1993 Revenue Bonds were written off at the time of retirement and are reported as loss on early extinguishment of debt in the amount of $123 in the accompanying 2012 consolidated statement of operations.

The Series 2003B and Series 2007 bonds are secured by letters of credit with U.S. Bank National Association and PNC Bank (collectively, the Commercial Banks), respectively. These bonds have put options that allow the holders to redeem the bonds prior to maturity. The Obligated Group has agreements with remarketing agents to remarket any bonds redeemed as a result of the exercise of the put options. If the bonds cannot be remarketed, the Commercial Banks will purchase the bonds under the letters of credit. Any liquidity advances as a result of failed remarketing are repayable to US Bank National Association and PNC Bank within 367 and 60 days, respectively, unless converted to term loans by meeting certain criteria as defined in the letter-of-credit agreements (the Agreements). Any term loans must be repaid in full by the earlier of the letter-of-credit expiration date or the date of certain other events as defined in the Agreements. The repayment terms per the Agreements for the Series 2003B and Series 2007 bonds require repayment within 24 and 18 months, respectively.

Subsequent to year end, on July 16, 2013, the Obligated Group issued $87,300 of Wisconsin Health and Educational Facilities Authority Wheaton Franciscan Services, Inc. System Revenue Bonds, Series 2013A due in varying installments through August 15, 2023 and bearing fixed interest of 2.0%. The proceeds were used for the redemption of the Wisconsin Health and Educational Facilities Authority Wheaton Franciscan Services, Inc. System Revenue Bonds, Series 2003A.

Subsequent to year end, on August 15, 2013, WFSI redeemed all of the outstanding Series 2003A Revenue Bonds $97,695. As part of this redemption, WFSI incurred a loss of $622.

(In thousands)

The principal repayment schedules shown below does not include the redemption of the 2003A debt or the issuance of the 2013A debt.

The first chart represents future principal repayments on long-term debt assuming the Series 2003B and Series 2007 variable rate demand bonds failed to be remarketed and were subsequently purchased by the letter-of-credit banks on June 30, 2013 with principal repayments accelerated in accordance with the terms of the letter-of-credit agreements. The second chart represents principal repayments based on the current status under the terms of the Standby Bond Purchase Agreements for the Bank Bonds, and all other long-term debt – bonds based on scheduled maturities or repayments as specified in the related long-term debt agreements.

Chart I

Year ending June 30:		
2014	$	51,738
2015		73,642
2016		50,080
2017		16,335
2018		15,995
Thereafter		525,440
	$	733,230

Chart II

Year ending June 30:		
2014	$	11,760
2015		12,340
2016		16,380
2017		16,850
2018		17,705
Thereafter		658,195
	$	733,230

(In thousands)

(12) Long-Term Debt – Mortgages

Long-term debt – mortgages held by FMI at June 30, 2013 and 2012 are as follows:

Housing project	Interest rate	Final maturity date	Security	2013	2012
Assisi homes:					
Batavia Apartments, Inc.	6.75%	November 1, 2041	HUD	$ —	9,873
Batavia Apartments, Inc.	7.00	August 1, 2012	HUD	—	59
Batavia Apartments, Inc.	2.65	November 1, 2047	GMAC	12,432	—
Colony Park, Inc.	7.49	July 1, 2018	IHDA	1,259	1,480
Constitution House, Inc.	7.81	July 1, 2016	IHDA	743	1,003
Jefferson Court, Inc.	6.21	March 1, 2038	HUD	6,994	7,111
Saxony, Inc.	5.54	June 1, 2035	Citigroup	6,564	6,721
Clare Gardens, Inc.	5.25	July 1, 2038	HUD	2,699	2,750
Francis Heights, Inc. Capmark A	6.50	February 28, 2014	HUD	174	420
Francis Heights, Inc. Flex	1.00	No fixed maturity date	HUD	1,902	1,902
Francis Heights, Inc. Capmark B	6.50	February 28, 2038	HUD	93	95
Francis Heights, Inc. 2nd Mtge	4.00	January 31, 2038	HUD	506	861
Marian Housing Center, Inc.	5.50	June 1, 2040	HUD	1,404	1,426
Marian Park, Inc.	7.00	January 1, 2014	FHA	1,943	2,213
Starved Rock – LaSalle Manor Limited Partnership (SR)	3.00	July 1, 2020	GMAC	423	400
SR	6.50	April 1, 2037	GMAC	464	471
Villa St. Clare, Inc.	4.00	April 1, 2027	WHEDA	1,196	1,249
Other mortgages	6.13% – 7.68%			176	176
Total long-term debt – mortgages				38,972	38,210
Less current installments of mortgages				8,234	1,912
Long-term debt – mortgages, excluding current installments				$ 30,738	36,298

(In thousands)

As of June 30, 2013, scheduled annual maturities of long-term debt – mortgages for the next five years and thereafter are as follows:

Year ending June 30:		
2014	$	8,234
2015		1,037
2016		990
2017		840
2018		808
Thereafter		27,063
	$	38,972

(13) Pension Plans

WFSI and certain of its subsidiaries participate in a qualified noncontributory defined-benefit pension plan (the Plan), covering all employees who are at least 21 years of age and work 1,000 or more hours per year. The normal retirement benefit of the Plan is a monthly retirement income, a lump-sum payment, or a combination thereof which is computed based on a cash balance accumulated from contributions and interest earnings thereon equal to the one-year Treasury bill rate or a rate approved by the WFSI Finance and Operations Committee. The benefit is payable commencing any time after the vested employee’s termination date but not later than age 65 unless still working. The Plan is funded based on the estimated pension cost as determined by the Plan’s consulting actuary.

The cost related to employee service is recognized using the Projected Unit Credit Cost Method. Gains and losses, calculated as the difference between estimates and actual amounts of plan assets and the projected benefit obligation, are amortized over the expected future service period. The prior service credits are also amortized over the expected future service period.

Prior to January 1, 1995, the Plan had a traditional annuity benefit formula. Participants who were covered under the prior plan are grandfathered and entitled to a retirement benefit equal to the greater of their benefit as defined by the Plan or their benefit as defined by the prior plan.

(In thousands)

The following table sets forth information on the funded status, amounts recognized in the consolidated financial statements, and weighted average assumptions related to WFSI's Plan for the years ended June 30, 2013 and 2012:

		2013	2012
Change in benefit obligation:			
Benefit obligation at beginning of year	$	877,828	730,259
Service cost		34,263	29,395
Interest cost		38,887	42,327
Benefits paid		(39,237)	(35,526)
Actuarial loss		(28,552)	111,373
Curtailment		(339)	—
Plan amendment		(28,625)	—
Benefit obligation of end of year		854,225	877,828
Change in plan assets:			
Fair value of plan assets at beginning of year		579,630	565,999
Actual return on plan assets		77,120	(2,343)
Employer contributions		100,000	51,500
Benefits paid		(39,237)	(35,526)
Fair value of plan assets at end of year		717,513	579,630
Funded status	$	(136,712)	(298,198)
Amounts recognized in the accompanying consolidated balance sheets:			
Accrued pension liability	$	(136,712)	(298,198)
Accumulated charge to unrestricted net assets		194,964	298,672
Net amounts recognized in the accompanying consolidated balance sheets	$	58,252	474

The accumulated charge to unrestricted net assets represents charges or credits arising from the defined-benefit pension plan, but not yet recognized as components of net periodic benefit cost. The accumulated charge to unrestricted net assets at June 30, 2013 and 2012 of $194,964 and $298,672, respectively, comprised $263,525 and $352,275 of unrecognized net actuarial losses offset by a reduction for unrecognized prior service credits of $68,561 and $53,603 at June 30, 2013 and 2012, respectively.

The accumulated benefit obligation for the Plan was $813,839 and $831,328 at June 30, 2013 and 2012, respectively.

Several organizations participate in the Plan but are not included in the accompanying consolidated financial statements. Therefore, the amounts recognized by the participants are shown in the above table, but are not included in the consolidated financial statements. The net periodic pension cost for the years ended June 30, 2013 and 2012 related to unconsolidated subsidiaries and affiliates amounted to $2,448 and 2,304, respectively.

(In thousands)

Net periodic benefit cost for the Plan for the years ended June 30, 2013 and 2012 included the following components:

		2013	2012
Components of net periodic benefit cost:			
Service cost	$	34,263	29,395
Interest cost		38,887	42,328
Expected return on plan assets		(47,001)	(43,856)
Curtailment impact		(3,927)	—
Net amortization amounts		20,001	6,145
Net periodic benefit cost	$	42,223	34,012
Weighted average assumptions:			
Discount rate used to determine obligation		3.75%/7.75%	5.26%/8.00%
Discount rate used to determine net periodic benefit cost		3.75%/7.75%	5.26%/8.00%
Rate of compensation increase		Age-based	Age-based
Expected return on plan assets		7.00%	7.75%
Cash balance interest rate assumption		3.1%	3.1%

The weighted average discount rate used in determining the actuarial present value of the projected benefit obligation at June 30, 2013 and 2012 is 8.00%, for grandfathered participants estimated to take their retirement benefit in the form of a lump sum and 4.37% and 3.75% at June 30, 2013 and 2012, respectively, for all other participants.

Effective for terminations on or after July 1, 2013, the actuarial equivalence interest rate used for converting account balances to annuity form was updated from 8% to 4% effective July 1, 2013 and 2% effective July 1, 2014. The plan amendment resulted in a decrease to the projected benefit obligation of $28,625.

Effective July 1st, 2013, Rush Oak Park Hospital (ROPH) will no longer participate in the pension plan. This curtailment to the plan reduced the projected benefit obligation by $1,015. In addition, the plan was amended to credit ROPH participants with a full year of benefit accrual for calendar year 2013 based on pay and hours through July 1, 2013. This special termination benefit increased the projected benefit obligation by $676.

The Plan’s overall expected long-term rate of return on assets is 7.00% and 7.75% for 2013 and 2012, respectively. The expected long-term rate of return is based on the portfolio as a whole and not on the sum of the returns on individual asset categories. The return is based exclusively on historical returns, without adjustments.

(In thousands)

WFSI is expected to contribute $50,000 to the Plan in 2014 of which approximately $29,135 is the expense of the Plan.

The benefits expected to be paid in each year from 2014 through 2017 are approximately $42,952, $51,013, $52,345, and $54,900, respectively. The aggregate benefits expected to be paid in the five years from 2018 through 2022 are approximately $354,065. The expected benefits are based on the same assumptions used to measure WFSI's benefit obligation at June 30 and include estimated future employee service.

The Plan has a statement of Investment Policy, which is reviewed and approved by the WFSI board of directors. The policy establishes goals and objectives of the fund, asset allocations, allowable and prohibited investments, socially responsible guidelines, and asset classifications as well as specific investment manager guidelines. The policy states that the rebalancing of these assets to the target allocations will be reviewed on a semiannual basis. Investments are managed by independent advisors. Management monitors the performance of these managers on a monthly basis.

The table below lists the target asset allocation and acceptable ranges and actual asset allocations as of June 30, 2013 and 2012:

	2013			2012		
Asset	Target allocation	Acceptable range	Actual allocation	Target allocation	Acceptable range	Actual allocation
Equity – large cap growth	5%	0% – 10%	5%	5%	0% – 10%	8%
Equity – large cap value	20	15% – 25%	20	20	15% – 25%	19
Equity – mid cap	10	5% – 15%	10	10	5% – 15%	10
Equity – small cap	10	5% – 15%	10	10	5% – 15%	10
Equity international	15	10% – 20%	13	15	10% – 20%	14
Fixed income and cash	40	30% – 50%	42	40	30% – 50%	39

Fair Value of Financial Instruments

The following methods and assumptions were used by WFSI in estimating the fair value of its financial instruments of the Plan:

- Common stocks, quoted mutual funds, and direct U.S. government obligations are measured using quoted market prices at the reporting date multiplied by the quantity held. Corporate bonds, notes, and U.S. agency securities are measured using other observable inputs. The carrying value equals fair value.

(In thousands)

Fair Value Hierarchy

The following tables present the Plan's fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of June 30, 2013 and 2012:

		Total, June 30, 2013	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Investments:					
Cash and cash equivalents	$	49,194	49,194	—	—
U.S. government obligations		152,987	94,967	58,020	—
Corporate debt securities		106,922	—	106,922	—
Asset-backed securities		10,863	—	10,863	—
Equity securities		397,547	397,547		—
Total	$	717,513	541,708	175,805	—

		Total, June 30, 2012	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Investments:					
Cash and cash equivalents	$	27,513	27,513	—	—
U.S. government obligations		96,925	45,154	51,771	—
Corporate debt securities		101,712	—	101,712	—
Asset-backed securities		13,702	—	13,702	—
Equity securities		341,516	341,516	—	—
Total *	$	581,368	414,183	167,185	—

Transfers between Levels

The availability of observable market data is monitored to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period. WFSI evaluated the significance of transfers between levels based upon the nature of the financial instrument and size of the transfer relative to total assets. For the year ended June 30, 2013, there were no significant transfers in or out of Levels 1, 2, or 3.

* Total excludes $1,738 of unsettled payables to custodian of pension plan assets as of June 30, 2012.

During 1996, WFSI created a nonqualified Benefit Restoration Plan (the BRP) for senior executives employed in the organization whose benefits under the qualified plan are limited due to limitations imposed by income tax regulations. In 2001, the Plan was amended to cover certain benefits previously provided under the BRP. In 2008, the BRP was amended to vest the accrued benefits as of December 29, 2008. The payout started in January 2009 with future accrued benefits being paid out annually. Accounts payable to BRP participants of $750 and $200 at June 30, 2013 and 2012, respectively, are included in other long-term liabilities.

(14) Insurance

Professional and General Liability

Wheaton Franciscan Insurance Company (the Captive), a wholly owned subsidiary of WFSI, was formed to provide comprehensive professional and general liability insurance to the organization. Professional liability coverage for WFSI qualified subsidiaries located in Wisconsin is procured through Preferred Professional Insurance Company (PPIC), which reinsures all of the risk with the Captive. All other WFSI subsidiaries are insured directly by the Captive for professional and general liability risks.

For primary professional liability coverage for Wisconsin-based providers, WFSI pays premiums to PPIC based upon actuarial computations that estimate the expected ultimate losses by policy year. PPIC then pays the premium, net of PPIC’s administrative expenses, to the Captive pursuant to a reinsurance agreement. All primary professional liability insurance coverage provided through PPIC is on an occurrence basis.

Losses in excess of the primary professional liability limits for the Wisconsin-based providers are fully covered through the hospitals’ and employed physicians’ mandatory participation in the Patients’ Compensation Fund of the State of Wisconsin. For other regions, the Captive obtains varying levels of commercial umbrella and excess reinsurance coverage by policy year on a claims-made basis.

WFSI recognizes provisions for the ultimate cost of reported losses and for losses incurred but not reported based upon projections by WFSI management and independent actuaries. At June 30, 2013 and 2012, loss reserve accruals of $24,688 and $25,703, respectively, are included in the accompanying consolidated financial statements in other long-term liabilities. It is management’s opinion that the recorded claim reserves are adequate to cover ultimate losses incurred to date. Provisions for professional and general liability self-insurance expense amounted to $3,463 and $1,708 for the years ended June 30, 2013 and 2012, respectively, and are included in purchased services, supplies, and other expenses in the accompanying consolidated statements of operations. As related to the professional and general liability, the adoption of ASU 2010-24 for the year ended June 30, 2012 had no impact on the consolidated financial statements.

Workers' Compensation and Employee Benefits

WFSI is self-insured for workers' compensation claims up to the first $250. WFSI purchases workers' compensation umbrella and excess policies to provide various levels of additional coverage by policy year. Workers' compensation self-insurance expense amounted to $5,995 and $6,238 for the years ended June 30, 2013 and 2012, respectively, and is included in salaries and fringe benefits expense in the accompanying consolidated statements of operations. The gross liability for estimated self-insured workers' compensation claims of $10,426 and $11,241 at June 30, 2013 and 2012, respectively, is included within accounts payable and accrued expenses in the accompanying consolidated balance sheets.

WFSI adopted the provisions of ASU 2010-24 for the year ended June 30, 2012. The estimated workers' compensation insurance recoveries was $1,318 and $1,045, and is included as a component of prepaid expenses and other, respectively, as of June 30, 2013 and 2012, respectively.

All claims, premiums, and administrative expenses related to benefits are processed, recorded, and paid directly through WFSI, with the exception of commercially insured HMO's in Illinois and Colorado, life insurance for all associates and long-term disability coverage for executives and physicians. Long-term disability coverage, which became commercially insured effective January 1, 2010.

WFSI internally estimates the claims incurred but unreported as of the consolidated balance sheet dates for healthcare and other employee benefits. Accrued healthcare and other benefits claims of approximately $17,746 and $19,239 at June 30, 2013 and 2012, respectively, consist of the estimated ultimate cost of reported claims and claims incurred but not reported as of the consolidated balance sheet dates and are included within accounts payable and accrued expenses. Provisions for self-insured employee healthcare and other employee benefit claims amounted to approximately $97,330 and $96,982 for the years ended June 30, 2013 and 2012, respectively, and are included with salaries and fringe benefits expense in the accompanying consolidated statements of operations. There was no impact to the consolidated financial statements for the adoption of ASU 2010-24 with respect to self-insured employee healthcare.

(15) Integration Agreements and Investments in Unconsolidated Affiliates

WFSI and certain subsidiaries also have investments in organizations that are not majority owned or controlled by WFSI organizations. WFSI and its subsidiaries account for their investments in these organizations using the equity method of accounting. The equity method of accounting is discontinued when the equity investment is reduced to zero unless WFSI or its subsidiaries has guaranteed the obligations of the organization or is committed to provide additional capital support.

(a) Felician Services, Inc.

In 2008, WFSI and Southeast Wisconsin Region entered into a Restated Integration Agreement with Felician Services, Inc. (FSI) to better fulfill both WFSI's and FSI's commitment to the mission of the health ministry of the Roman Catholic Church. The Restated Integration Agreement was retroactively effective July 1, 2006 and gives Southeast Wisconsin Region authority to manage and direct the FSI-sponsored entities at (Wheaton Franciscan Healthcare – St. Francis, Inc. and Wheaton Franciscan Healthcare – Terrace at St. Francis, Inc.,). The FSI-sponsored entities are consolidated by

WFSI within the accompanying consolidated financial statements given the degree of control and economic interest that WFSI has over the FSI-sponsored entities.

The Restated Integration Agreement provides FSI a put option that can be exercised by giving WFSI written notice. The execution of the put option requires WFSI to pay FSI an acquisition price of $28,000 for the FSI-sponsored entities, which is accrued and included in other long-term liabilities in the accompanying consolidated balance sheets. The put option has not been exercised as of June 30, 2013.

(b) United Hospital System, Inc.

Effective July 6, 1998, St. Catherine's entered into an integration agreement with United Hospital System, Inc. to operate as a single system through the formation of UHS, Inc. (United). The intent of the integration was to facilitate the development and operation of a healthcare system for the Kenosha, Wisconsin regional community and reduce the cost of and duplication of services. The integration agreement provides for the sharing of income or losses on a percentage basis of the consolidated results of operations.

WFSI accounts for its 25% equity investment in United on the equity method of accounting. WFSI has included its proportional share of United net income of $9,174 and $8,654 in 2013 and 2012, respectively, as other revenue in the accompanying consolidated statements of operations. WFSI received no cash distributions from United in 2013 or 2012. As of and for the years ended June 30, 2013 and 2012, respectively, United Hospital System, Inc. had total assets of $343,701 and $323,781, total net assets of $259,399 and $204,818, and revenue of $287,150 and $284,048.

Construction in progress at June 30, 2013 relates primarily to costs incurred for St. Catherine's expansion project. At June 30, 2013, St. Catherine's has incurred and capitalized approximately $98,000 of the costs related to the project. The project is being partially funded by United. As of June 30, 2013 and 2012, a due to United in the amount of $49,527 and $63,000, respectively, for repayment of construction advances is included in accounts payable and accrued expenses in the accompanying consolidated balance sheets.

(c) Midwest Orthopedic Specialty Hospital, LLC (MOSH)

MOSH, a joint venture entity, was formed in late 2008 to own and operate an orthopedic specialty hospital located on the second floor of the Wheaton Franciscan Healthcare – Franklin (WFH-Franklin). MOSH was granted its hospital license by the State of Wisconsin and opened for operations effective July 31, 2009. The members of MOSH are WFH-Southeast Wisconsin, Inc. and TS Ortho, LLC, an independent physician-owned entity. Each member has a 50% ownership interest in MOSH.

As of June 30, 2013 and 2012, respectively, MOSH has total assets of $46,913 and $45,523, member equity of $43,673 and $42,951, and total revenue of $75,121 and $69,885. WFH accounts for its 50% interest in MOSH under the equity method of accounting. For the years ended June 30, 2013 and 2012, WFSI has included its proportional share of MOSH's net income of $18,863 and $16,406, respectively, as other operating revenue in the accompanying consolidated statements of operations.

(Continued)

(In thousands)

Distributions are payable by MOSH at the discretion of the joint venture's board of managers. WFH received cash distributions of $18,500 and $15,000 from the joint venture during 2013 and 2012, respectively.

(16) Commitments and Contingencies

(a) Operating Leases

WFSI and its subsidiaries have entered into various contracts for operating leases of office space, buildings, and equipment. During 2013 and 2012, WFSI and its subsidiaries recognized $10,747 and $10,723, respectively, of lease expense under these agreements.

As of June 30, 2013, scheduled annual contractual payments under operating leases for the next five years and thereafter are as follows:

Year ending June 30:		
2014	$	7,002
2015		5,483
2016		4,354
2017		3,513
2018		3,065
Thereafter		10,605
	$	34,022

(b) Housing Contingencies

FMI entered into multiple Capital Advance Program Mortgage Notes (the Notes) in the amount of $17,100. The Notes bear no interest and repayment is not required as long as the housing projects remain available to low-income, elderly, or disabled persons in accordance with the National Affordable Housing Act of 1990 and are operated in accordance with the Regulatory Agreements and HUD Regulations. The Notes are secured by the mortgage upon the land, building, and equipment, and other amounts held by FMI. If a default occurs under the terms of the Notes, mortgages, the Regulatory Agreements, or the regulations, the entire principal and interest accrued at the stated rate would become immediately due and payable without notice. These Notes have been recorded as a direct addition to unrestricted net assets in the year received. FMI has not entered into any new notes in 2013 or 2012.

FMI also entered into agreements with various federal and state agencies whereby FMI received grants. In connection with these grants, FMI must not, among other things, dispose of any property under its control that was acquired and/or improved with grant funds for a period between 15 and 40 years. In the event of noncompliance, FMI would reimburse the agency the current fair market value of the property, less any portion of the value attributable to expenditures of nongrant funds for acquisition of, or improvement to, the property. These grants have been recorded as a direct addition to unrestricted net assets in the year received. Management believes FMI is in compliance with the grant agreements as of June 30, 2013 and 2012 and no amounts have been accrued in the accompanying consolidated balance sheets.

FMI refinanced Assisi Homes – Batavia Apartments, Inc., a wholly owned entity, on October 31, 2012. Management is working with HUD to amend its Use Agreement with final resolution expected during 2014.

(c) Litigation

WFSI and its subsidiaries are involved in litigation arising in the ordinary course of business. In the opinion of management, after consultation with legal counsel, the ultimate resolution of professional liability and other litigation matters will not have a material effect on the consolidated financial position or results from operations of WFSI and its subsidiaries.

(d) State Sales and Property Tax Exemption

Local taxing authorities throughout the country are increasingly challenging the sales and real estate tax exemptions of not-for-profit healthcare providers.

WFSI prevailed in the Wisconsin Supreme Court in its litigation related to the property tax exemption of one of its Wisconsin facilities. Since opening the Wheaton Franciscan, Inc – Wauwatosa Campus outpatient center in 2003, the City of Wauwatosa (the City) has taken the stand that because there are physician offices in the building, the entire building is taxable and the City has assessed property taxes accordingly. WFSI has paid and expensed property taxes as assessed, which are included in purchased services, supplies, and other expenses. WFSI has maintained that the majority of the facility is dedicated to hospital-based services as an extension of Wheaton Franciscan, Inc., and therefore, it should be required to pay taxes only on the physician office space in the facility. WFSI appealed the City decision to tax the entire facility seeking a refund of the taxes it has paid to date on the property plus interest. That appeals process led to the case going before a Wisconsin Circuit Court in August 2007. On March 30, 2009, the court issued a decision in the matter in WFSI's favor granting the facility's tax exemption and ordered the City to refund the taxes paid to date. The City appealed the case. In August 2010, the Wisconsin Court of Appeals reversed the trial court decision and determined that the outpatient center in the City of Wauwatosa constitutes a "doctor's office" and, therefore, is ineligible for property tax exemption under Wisconsin law. In September 2010, WFSI filed a Petition for Review to the Wisconsin Supreme Court. On July 19, 2011, the Wisconsin Supreme Court reversed the Court of Appeals' decision and ruled in favor upholding the tax-exempt status of Wheaton Franciscan, Inc. The Court concluded that two-thirds of the outpatient facility was exempt from property tax. The Court reasoned that the facility was exempt because it was used for the primary purpose of a hospital.

Notwithstanding the recent favorable decision in Wisconsin, where the majority of Wheaton Franciscan Healthcare's business is conducted, the State of Illinois is taking an alternative approach to property and sales tax for healthcare providers conducting business in its state. To date, the State of Illinois has revoked and/or is currently reviewing the ongoing property and sales tax exemption of several Illinois Hospitals (unrelated to Wheaton Franciscan Healthcare). The State's focus has been exclusively on the level of free or discounted care being provided by the hospital. Other charitable factors, such as the level of government payors and/or other community services provided by the hospitals, are generally not being considered by the State as factors relevant to exemption. As of September 2013, the state of Illinois requires hospitals to report the value of services or activities provided by the hospital compared to the value of the estimated property tax bill.

(e) Legal, Regulatory, and Other Contingencies and Commitments

The laws and regulations governing the Medicare, Medicaid, and other government healthcare programs are extremely complex and subject to interpretation, making compliance an ongoing challenge for WFSI and other healthcare organizations. Recently the federal government has increased its enforcement activity, including audits and investigations related to billing practices, clinical documentation, and related matters. WFSI maintains a compliance program designed to educate employees and to detect and correct possible violations.

In 2013 and 2012, WFSI received and expects to receive future notices from the Medicare program requiring that they provide Medicare with documentation for claims to carry out the Recovery Audit Contract (RAC) program. WFSI is responding to these requests. Review of claims through the RAC program may result in a liability to the Medicare program and could have an adverse impact on the WFSI's net patient service revenues.

(f) The Patient Protection and Affordable Care Act

The Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act of 2010 (often referred to, collectively, as the Affordable Care Act of the healthcare reform law), was signed into law on March 23, 2010. The statute will change how healthcare services are delivered and reimbursed through a variety of mechanisms. The law contains stronger anti-fraud enforcement provisions and provides additional funding for enforcement activity.

On May 6, 2011, CMS issued a final rule establishing a value-based purchasing program for acute care hospitals paid under the Medicare Inpatient Prospective Payment System. Beginning in federal fiscal year 2013, incentive payments will be made based on achievement of or improvement in a set of clinical and quality measures designed to foster improved clinical outcomes. WFSI continues to monitor the impact of this regulation as regulations become finalized.

(g) Investment Risks and Uncertainties

WFSI invests in various investment securities. Investment securities are exposed to various risks such as interest rate, credit, and overall market volatility risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the accompanying consolidated balance sheets.

(17) Subsequent Events

WFSI evaluated events and transactions through October 22, 2013, which is the date the consolidated financial statements were issued, noting no subsequent events other than those as previously described in the preceding notes, requiring recording or disclosure in the consolidated financial statements or related notes to the consolidated financial statements.

Schedule 1

WHEATON FRANCISCAN SERVICES, INC.

Consolidating Balance Sheet Information

June 30, 2013

(In thousands)

Assets		WFSI Healthcare	WFSI Housing	Eliminations	WFSI consolidated
Current assets:					
Cash and cash equivalents	$	16,082	9,578	—	25,660
Short-term investments		11,448	—	—	11,448
Assets whose use is limited – required for current liabilities		57,286	—	—	57,286
Patient accounts receivable, net of uncollectible accounts of approximately $56,767		220,309	—	—	220,309
Inventories of supplies		25,229	—	—	25,229
Prepaid expenses and other		46,019	517	(251)	46,285
Total current assets		376,373	10,095	(251)	386,217
Noncurrent assets whose use is limited		720,908	12,858	—	733,766
Property, plant, and equipment, net		1,022,870	80,918	—	1,103,788
Other assets:					
Restricted assets		19,288	—	—	19,288
Deferred expenses, net		3,412	1,955	—	5,367
Investments in unconsolidated affiliates		24,472	—	—	24,472
Notes and accounts receivable, affiliated organizations		2,872	—	(2,872)	—
Other long-term assets		25,736	3,252	—	28,988
Total other assets		75,780	5,207	(2,872)	78,115
Total assets	$	2,195,931	109,078	(3,123)	2,301,886
Liabilities and Net Assets					
Current liabilities:					
Current installments of long-term debt – bonds	$	11,760	—	—	11,760
Long-term debt subject to short-term remarketing agreements		39,978	—	—	39,978
Current installments of long-term debt – mortgages		—	8,234	—	8,234
Current installments of notes payable to affiliates		—	4,114	(4,114)	—
Accounts payable and accrued expenses		250,926	4,546	(251)	255,221
Estimated third-party payor settlements		18,817	—	—	18,817
Total current liabilities		321,481	16,894	(4,365)	334,010
Long-term debt, excluding current installments and net unamortized bond issue premiums – bonds		699,131	—	—	699,131
Long-term debt, excluding current installments – mortgages		—	30,738	—	30,738
Notes payable to affiliates, excluding current installments		—	2,872	(2,872)	—
Accrued pension liability		136,712	—	—	136,712
Other		100,931	982	—	101,913
Total liabilities		1,258,255	51,486	(7,237)	1,302,504
Net assets:					
Unrestricted		918,388	57,592	4,114	980,094
Temporarily restricted		16,190	—	—	16,190
Permanently restricted		3,098	—	—	3,098
Total net assets		937,676	57,592	4,114	999,382
Total liabilities and net assets	$	2,195,931	109,078	(3,123)	2,301,886

See accompanying independent auditors' report.

Schedule 2

WHEATON FRANCISCAN SERVICES, INC.

Consolidating Statement of Operations Information

Year ended June 30, 2013

(In thousands)

	WFSI Healthcare	WFSI Housing	Eliminations	WFSI consolidated
Net patient service revenues before bad debt	$ 1,642,700	—	—	1,642,700
Provision for bad debts	75,197	—	—	75,197
Net patient service revenues before bad debt	1,567,503	—	—	1,567,503
Other revenues:				
Other	168,496	27,188	(1,271)	194,413
Net assets released from restrictions	1,499	—	—	1,499
Total revenues	1,737,498	27,188	(1,271)	1,763,415
Expenses:				
Salaries and fringe benefits	1,008,097	7,746	(249)	1,015,594
Purchased services, supplies, and other	555,567	11,904	(932)	566,539
Interest	31,304	1,905	(90)	33,119
Depreciation and amortization	103,782	4,893	—	108,675
Total expenses	1,698,750	26,448	(1,271)	1,723,927
Income from operations	38,748	740	—	39,488
Nonoperating gains:				
Investment return	25,506	736	—	26,242
Swap valuation adjustments	2,037	—	—	2,037
Other, net	594	261	—	855
Nonoperating gains, net	28,137	997	—	29,134
Revenues and gains in excess of expenses and losses	66,885	1,737	—	68,622
Other changes in unrestricted net assets:				
Net assets released from restrictions used for purchase of property, plant, and equipment	2,135	—	—	2,135
Change in unrecognized net defined-benefit plan costs	103,708	—	—	103,708
Equity transactions of unconsolidated affiliates and other, net	445	—	—	445
Change in unrestricted net assets	$ 173,173	1,737	—	174,910

See accompanying independent auditors' report.

WHEATON FRANCISCAN SERVICES, INC.

Consolidating Balance Sheet Information

June 30, 2013

(In thousands)

Assets		Wheaton Franciscan Services, Inc.	Wheaton Franciscan Healthcare Southeast WI/ Medical Group	Marianjoy Rehabilitation Hospital & Clinics, Inc.
Current assets:				
Cash and cash equivalents	$	13,359	147,325	17,268
Short-term investments		11,448	—	—
Assets whose use is limited – required for current liabilities		57,286	—	—
Patient accounts receivable, net of uncollectible accounts of approximately $56,767		—	176,604	9,296
Inventories of supplies		182	21,051	224
Prepaid expenses and other		22,287	17,221	3,617
Total current assets		104,562	362,201	30,405
Noncurrent assets whose use is limited		547,877	5,566	704
Property, plant, and equipment, net		70,543	654,456	61,104
Other assets:				
Restricted assets		29	11,976	3,994
Deferred expenses, net		3,412	—	—
Investments in unconsolidated affiliates		916	23,556	—
Notes and accounts receivable, affiliated organizations		451,475	—	—
Other long-term assets		—	29,805	—
Total other assets		455,832	65,337	3,994
Total assets	$	1,178,814	1,087,560	96,207
Liabilities and Net Assets (Deficit)				
Current liabilities:				
Current installments of long-term debt – bonds	$	11,760	—	—
Long-term debt subject to short-term remarketing agreements		39,978	—	—
Current installments of long-term debt – mortgages		—	—	—
Current installments of notes payable to affiliates		—	—	—
Accounts payable and accrued expenses		341,156	93,005	6,060
Estimated third-party payor settlements		—	12,290	946
Total current liabilities		392,894	105,295	7,006
Long-term debt, excluding current installments and net unamortized bond issue premiums – bonds		699,131	—	—
Long-term debt, excluding current installments – mortgages		—	—	—
Notes payable to affiliates, excluding current installments		—	404,025	33,216
Accrued pension liability		136,712	—	—
Other		96,081	5,018	384
Total liabilities		1,324,818	514,338	40,606
Net assets (deficit):				
Unrestricted		(146,033)	561,246	51,607
Temporarily restricted		29	10,243	3,994
Permanently restricted		—	1,733	—
Total net assets (deficit)		(146,004)	573,222	55,601
Total liabilities and net assets (deficit)	$	1,178,814	1,087,560	96,207

See accompanying independent auditors’ report.

Schedule 3

WFH-Iowa, Inc.	St. Catherine's Hospital, Inc.	OSF Services, Inc.	Franciscan Ministries, Inc.	Subtotal	Adjustments/ eliminations	Total
94,692	6,022	466	9,578	288,710	(263,050)	25,660
—	—	—	—	11,448	—	11,448
—	—	—	—	57,286	—	57,286
34,409	—	—	—	220,309	—	220,309
3,772	—	—	—	25,229	—	25,229
2,759	15	643	517	47,059	(774)	46,285
135,632	6,037	1,109	10,095	650,041	(263,824)	386,217
8,553	—	158,208	12,858	733,766	—	733,766
107,322	129,026	419	80,918	1,103,788	—	1,103,788
3,261	—	28	—	19,288	—	19,288
—	—	—	1,955	5,367	—	5,367
—	—	—	—	24,472	—	24,472
—	—	—	—	451,475	(451,475)	—
265	—	3	3,252	33,325	(4,337)	28,988
3,526	—	31	5,207	533,927	(455,812)	78,115
255,033	135,063	159,767	109,078	3,021,522	(719,636)	2,301,886
—	—	—	—	11,760	—	11,760
—	—	—	—	39,978	—	39,978
—	—	—	8,234	8,234	—	8,234
—	—	—	4,114	4,114	(4,114)	—
23,899	49,527	852	4,546	519,045	(263,824)	255,221
5,581	—	—	—	18,817		18,817
29,480	49,527	852	16,894	601,948	(267,938)	334,010
—	—	—	—	699,131	—	699,131
—	—	—	30,738	30,738	—	30,738
11,362	—	—	2,872	451,475	(451,475)	—
—	—	—	—	136,712	—	136,712
3,785	—	—	982	106,250	(4,337)	101,913
44,627	49,527	852	51,486	2,026,254	(723,750)	1,302,504
207,145	85,536	158,887	57,592	975,980	4,114	980,094
1,896	—	28	—	16,190	—	16,190
1,365	—	—	—	3,098	—	3,098
210,406	85,536	158,915	57,592	995,268	4,114	999,382
255,033	135,063	159,767	109,078	3,021,522	(719,636)	2,301,886

WHEATON FRANCISCAN SERVICES, INC.

Consolidating Statement of Operations Information

Year ended June 30, 2013

(In thousands)

	Wheaton Franciscan Services, Inc.	Wheaton Franciscan Healthcare Southeast WI/ Medical Group	Marianjoy Rehabilitation Hospital & Clinics, Inc.
Net patient service revenues before bad debt	$ —	1,280,702	71,471
Provision for bad debts	—	63,384	602
Net patient service revenues	—	1,217,318	70,869
Other revenues:			
Other	321,714	106,069	10,310
Net assets released from restrictions	—	819	382
Total revenues	321,714	1,324,206	81,561
Expenses:			
Salaries and fringe benefits	206,246	698,716	56,661
Purchased services, supplies, and other	70,298	517,432	19,877
Interest	32,304	19,187	1,680
Depreciation and amortization	21,413	60,287	3,328
Total expenses	330,261	1,295,622	81,546
Income from operations	(8,547)	28,584	15
Nonoperating gains (losses):			
Investment return	8,168	6,962	745
Swap valuation adjustments	2,037	—	—
Other, net	(23)	167	(100)
Nonoperating gains, net	10,182	7,129	645
Revenues and gains in excess of expenses and losses	1,635	35,713	660
Other changes in unrestricted net assets:			
Net assets released from restrictions used for purchase of property, plant, and equipment	—	256	60
Change in unrecognized net defined-benefit plan costs	103,708	—	—
Equity transactions of unconsolidated affiliates and other, net	—	—	—
Change in unrestricted net assets	$ 105,343	35,969	720

See accompanying independent auditors' report.

Schedule 4

WFH-Iowa, Inc.	St. Catherine's Hospital, Inc.	OSF Services, Inc.	Franciscan Ministries, Inc.	Subtotal	Adjustments/ eliminations	Total
290,527	—	—	—	1,642,700	—	1,642,700
11,211	—	—	—	75,197	—	75,197
279,316	—	—	—	1,567,503	—	1,567,503
25,721	13,868	3,347	27,188	508,217	(313,804)	194,413
298	—	—	—	1,499	—	1,499
305,335	13,868	3,347	27,188	2,077,219	(313,804)	1,763,415
165,707	—	4,524	7,746	1,139,600	(124,006)	1,015,594
111,471	357	2,507	11,904	733,846	(167,307)	566,539
534	—	—	1,905	55,610	(22,491)	33,119
11,080	7,621	53	4,893	108,675	—	108,675
288,792	7,978	7,084	26,448	2,037,731	(313,804)	1,723,927
16,543	5,890	(3,737)	740	39,488	—	39,488
4,204	—	5,427	736	26,242	—	26,242
—	—	—		2,037	—	2,037
(988)	7	1,531	261	855	—	855
3,216	7	6,958	997	29,134	—	29,134
19,759	5,897	3,221	1,737	68,622	—	68,622
1,819	—	—	—	2,135	—	2,135
—	—	—	—	103,708	—	103,708
(321)	—	766	—	445	—	445
21,257	5,897	3,987	1,737	174,910	—	174,910

WHEATON FRANCISCAN SERVICES, INC.

Consolidating Balance Sheet Information – The Obligated Group

June 30, 2013

(In thousands)

Assets	Wheaton Franciscan Services, Inc.	Southeast Wisconsin Region	Marianjoy Rehabilitation Hospital & Clinics, Inc.
Current assets:			
Cash and cash equivalents	$ 12,159	147,145	17,268
Short-term investments	11,448	—	—
Assets whose use is limited – required for current liabilities	57,286	—	—
Patient accounts receivable, net of uncollectible accounts of approximately $54,074	—	171,105	8,129
Inventories of supplies	182	18,008	224
Prepaid expenses and other	19,200	751,574	3,502
Total current assets	100,275	1,087,832	29,123
Noncurrent assets whose use is limited	512,498	5,376	—
Property, plant, and equipment, net	70,543	647,044	60,961
Other assets:			
Restricted assets	29	5,397	—
Deferred expenses, net	3,412	—	—
Investments in unconsolidated affiliates	15,346	57,971	—
Notes and accounts receivable, affiliated organizations	451,476	45	—
Other long-term assets	—	27,278	—
Total other assets	470,263	90,691	—
Total assets	$ 1,153,579	1,830,943	90,084
Liabilities and Net Assets (Deficit)			
Current liabilities:			
Current installments of long-term debt – bonds	$ 11,760	—	—
Long-term debt subject to short-term remarketing agreements	39,978	—	—
Accounts payable and accrued expenses	341,087	844,021	4,808
Estimated third-party payor settlements	—	12,044	946
Total current liabilities	392,825	856,065	5,754
Long-term debt, excluding current installments and net unamortized bond issue premiums – bonds	699,131	—	—
Notes payable to affiliates, excluding current installments	—	401,541	33,216
Accrued pension liability	136,712	—	—
Other	70,915	5,018	384
Total liabilities	1,299,583	1,262,624	39,354
Net assets (deficit):			
Unrestricted	(146,033)	562,922	50,730
Temporarily restricted	29	4,679	—
Permanently restricted	—	718	—
Total net assets (deficit)	(146,004)	568,319	50,730
Total liabilities and net assets (deficit)	$ 1,153,579	1,830,943	90,084

See accompanying independent auditors' report.

Schedule 5

Iowa Region	St. Catherine's Hospital, Inc.	Subtotal	Adjustments/ eliminations	Total
94,691	6,022	277,285	(263,159)	14,126
—	—	11,448	—	11,448
—	—	57,286	—	57,286
28,469	—	207,703	—	207,703
3,372	—	21,786	—	21,786
2,780	15	777,071	(733,507)	43,564
129,312	6,037	1,352,579	(996,666)	355,913
—	—	517,874	6,397	524,271
93,905	129,026	1,001,479	—	1,001,479
272	—	5,698	11,259	16,957
—	—	3,412	—	3,412
—	—	73,317	(18,650)	54,667
10,511	—	462,032	(456,630)	5,402
265	—	27,543	(4,337)	23,206
11,048	—	572,002	(468,358)	103,644
234,265	135,063	3,443,934	(1,458,627)	1,985,307
—	—	11,760	—	11,760
—	—	39,978	—	39,978
21,803	49,527	1,261,246	(996,666)	264,580
3,842	—	16,832	—	16,832
25,645	49,527	1,329,816	(996,666)	333,150
—	—	699,131	—	699,131
21,873	—	456,630	(456,630)	—
—	—	136,712	—	136,712
2,462	—	78,779	(4,337)	74,442
49,980	49,527	2,701,068	(1,457,633)	1,243,435
184,013	85,536	737,168	(12,253)	724,915
272	—	4,980	10,244	15,224
—	—	718	1,015	1,733
184,285	85,536	742,866	(994)	741,872
234,265	135,063	3,443,934	(1,458,627)	1,985,307

WHEATON FRANCISCAN SERVICES, INC.

Consolidating Statement of Operations Information – The Obligated Group

Year ended June 30, 2013

(In thousands)

	Wheaton Franciscan Services, Inc.	Southeast Wisconsin Region	Marianjoy Rehabilitation Hospital & Clinics, Inc.
Net patient service revenues before bad debt	$ —	1,233,092	62,045
Provision for bad debts	—	62,821	334
Net patient service revenues	—	1,170,271	61,711
Other revenues:			
Other	317,979	293,540	10,132
Net assets released from restrictions	—	736	382
Total revenues	317,979	1,464,547	72,225
Expenses:			
Salaries and fringe benefits	206,246	656,199	46,013
Purchased services, supplies, and other	66,563	700,507	19,110
Interest	32,304	19,032	1,680
Depreciation and amortization	21,413	59,529	3,305
Total expenses	326,526	1,435,267	70,108
Income from operations	(8,547)	29,280	2,117
Nonoperating gains (losses):			
Investment return	8,168	6,962	572
Swap valuation adjustments	2,037	—	—
Other, net	(23)	350	(100)
Nonoperating gains, net	10,182	7,312	472
Revenues and gains in excess of expenses and losses	1,635	36,592	2,589
Other changes in unrestricted net assets:			
Net assets released from restrictions used for purchase of property, plant, and equipment	—	253	60
Change in unrecognized net defined-benefit plan costs	103,708	—	—
Equity transactions of unconsolidated affiliates and other, net	—	(775)	(3,083)
Change in unrestricted net assets	$ 105,343	36,070	(434)

See accompanying independent auditors’ report.

Schedule 6

Iowa Region	St. Catherine's Hospital, Inc.	Subtotal	Adjustments/ eliminations	Total
241,824	—	1,536,961	—	1,536,961
9,550	—	72,705	—	72,705
232,274	—	1,464,256	—	1,464,256
38,172	13,868	673,691	(525,039)	148,652
283	—	1,401	—	1,401
270,729	13,868	2,139,348	(525,039)	1,614,309
146,117	—	1,054,575	(123,757)	930,818
106,121	357	892,658	(379,617)	513,041
511	—	53,527	(22,246)	31,281
8,897	7,621	100,765	—	100,765
261,646	7,978	2,101,525	(525,620)	1,575,905
9,083	5,890	37,823	581	38,404
3,313	—	19,015	—	19,015
—	—	2,037	—	2,037
(689)	7	(455)	—	(455)
2,624	7	20,597	—	20,597
11,707	5,897	58,420	581	59,001
1,542	—	1,855	—	1,855
—	—	103,708	—	103,708
7,268	—	3,410	—	3,410
20,517	5,897	167,393	581	167,974