Obligated Group
Financial Statements

2nd Quarter
March 31, 2016

Scripps

Scripps Health
Obligated Group

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For the Quarter and Six Months Ended March 31, 2016

SCRIPPS HEALTH

OBLIGATED GROUP
STATEMENTS OF FINANCIAL POSITION
March 31, 2016
($000s)

	March 2016	March 2015	September 2015
ASSETS			
Current Assets:			
Cash and Cash Equivalents	$ 274,058	$ 244,362	$ 292,596
Accounts Receivable, Net	351,395	297,228	296,673
Assets Limited As To Use	2,288	2,367	5,542
Other Current Assets	132,571	172,266	134,268
Total Current Assets	760,312	716,223	729,079
Investments:			
Assets Limited As To Use	203,288	222,148	210,893
Unrestricted	1,953,370	1,890,069	1,773,543
Property, Plant and Equipment	3,053,937	2,812,754	2,947,792
Less Accumulated Depreciation	(1,445,261)	(1,326,309)	(1,393,593)
Property, Plant and Equipment, Net	1,608,676	1,486,445	1,554,199
Other Assets	160,577	150,709	152,325
Total Assets	$ 4,686,223	$ 4,465,594	$ 4,420,039
LIABILITIES AND EQUITY			
Current Liabilities:			
Current Portion of Long-term Debt	$ 34,976	$ 19,856	$ 19,992
Accounts Payable	136,738	157,234	133,012
Accrued Liabilities	230,771	219,354	242,108
Total Current Liabilities	402,485	396,444	395,112
Long Term Debt	1,040,585	867,897	866,577
Other Liabilities	111,845	93,192	112,002
Total Liabilities	1,554,916	1,357,533	1,373,691
Equity:			
Unrestricted	2,936,349	2,898,018	2,847,894
Temporarily Restricted	109,422	130,779	118,262
Permanently Restricted	85,536	79,264	80,192
Total Equity	3,131,307	3,108,061	3,046,348
Total Liabilities and Equity	$ 4,686,223	$ 4,465,594	$ 4,420,039

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENT OF OPERATIONS
($000s)

	FOR THE QUARTER ENDED MARCH 31, 2016	2015
Operating revenues:		
Net patient service revenue, net of contractual allowances and discounts	$ 622,660	$ 559,262
Provision for bad debts	(13,653)	(7,366)
Net patient service revenue less provision for bad debts before provider fee	609,007	551,897
Provider fee	24,761	28,357
Net patient service revenue	633,768	580,253
Capitation premium	31,425	43,655
Other	22,728	19,940
Meaningful use	8	-
Net assets released from restrictions used for operations	8,008	5,129
Total operating revenues	695,937	648,977
Operating expenses:		
Wages and benefits	310,175	288,788
Supplies	112,947	102,615
Physician services	102,468	94,428
Other services	76,354	72,694
Provider fee	18,652	18,600
Capitation services	1,178	560
Depreciation and amortization	33,179	31,551
Interest	6,158	4,665
Restructuring	2,374	-
Total operating expenses	663,483	613,900
Operating income before corporate overhead allocation & income tax	32,453	35,077
Corporate overhead allocation	1,751	1,549
Provision for income tax expense	(8)	-
Operating income after corporate overhead allocation & income tax	34,196	36,626
Nonoperating gains (losses):		
Interest and dividends	5,978	5,937
Realized (losses) gains	(28,101)	97,898
Unrealized gains (losses) on trading portfolio	5,719	(66,539)
Contributions	558	310
Market adjustment on interest rate swaps	(3,965)	(2,443)
Excess of revenues over expenses	$ 14,386	$ 71,789

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENTS OF CHANGES IN NET ASSETS
($000s)

	FOR THE QUARTER ENDED MARCH 31, 2016	2015
Unrestricted net assets:		
Excess of revenues over expenses attributable to controlling interests	$ 14,386	$ 71,789
Net assets released from restrictions used for purchase of property & equipment	4,730	6,000
Other	(118)	(126)
Increase in unrestricted net assets	18,998	77,663
Temporarily restricted net assets:		
Contributions	2,495	4,182
Interest and dividends	476	529
Realized (losses) gains	(1,134)	6,327
Unrealized losses on trading portfolio	(609)	(4,340)
Net assets released from restrictions used for operations	(8,008)	(5,219)
Net assets released from restrictions used for purchases of property & equipment	(4,730)	(6,000)
Change in value of deferred gifts	791	463
Other	-	(198)
Decrease in temporarily restricted net assets	(10,720)	(4,256)
Permanently restricted net assets:		
Contributions	5,058	36
Change in value of deferred gifts	-	16
Other	(3)	56
Increase in permanently restricted net assets	5,055	109
Total increase in net assets	$ 13,333	$ 73,515

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENT OF OPERATIONS
($000s)

	FOR THE SIX MONTHS ENDED MARCH 31, 2016	2015
Operating revenues:		
Net patient service revenue, net of contractual allowances and discounts	$ 1,227,785	$ 1,144,650
Provision for bad debts	(19,939)	(19,491)
Net patient service revenue less provision for bad debts before provider fee	1,207,846	1,125,159
Provider fee	45,516	106,038
Net patient service revenue	1,253,362	1,231,197
Capitation premium	62,289	73,197
Other	43,989	40,543
Meaningful use	866	1,150
Net assets released from restrictions used for operations	13,721	10,536
Total operating revenues	1,374,226	1,356,624
Operating expenses:		
Wages and benefits	621,170	584,598
Supplies	229,726	207,470
Physician services	199,319	182,062
Other services	153,977	144,051
Provider fee	35,049	84,015
Capitation services	1,981	966
Depreciation and amortization	69,051	59,858
Interest	11,995	10,376
Restructuring	2,374	-
Total operating expenses	1,324,641	1,273,396
Operating income before corporate overhead allocation & income tax	49,585	83,227
Corporate overhead allocation	3,532	2,935
Provision for income tax expense	(16)	3
Operating income after corporate overhead allocation & income tax	53,102	86,165
Nonoperating gains (losses):		
Interest and dividends	18,679	17,526
Realized (losses) gains	(18,740)	148,163
Unrealized gains (losses) on trading portfolio	24,453	(111,406)
Contributions	4,460	844
Market adjustment on interest rate swaps	(2,615)	(5,693)
Excess of revenues over expenses	$ 79,338	$ 135,599

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENTS OF CHANGES IN NET ASSETS
($000s)

	FOR THE SIX MONTHS ENDED MARCH 31, 2016	2015
Unrestricted net assets:		
Excess of revenues over expenses attributable to controlling interests	$ 79,338	$ 135,599
Net assets released from restrictions used for purchase of property & equipment	8,317	13,399
Other	(188)	(205)
Increase in unrestricted net assets	87,467	148,793
Temporarily restricted net assets:		
Contributions	10,479	23,109
Interest and dividends	1,254	1,309
Realized (losses) gains	(596)	9,647
Unrealized gains (losses) on trading portfolio	894	(7,023)
Net assets released from restrictions used for operations	(13,721)	(10,536)
Net assets released from restrictions used for purchases of property & equipment	(8,317)	(13,399)
Change in value of deferred gifts	1,067	161
Other	101	(377)
(Decrease) increase in temporarily restricted net assets	(8,840)	2,891
Permanently restricted net assets:		
Contributions	5,275	356
Change in value of deferred gifts	-	16
Other	69	58
Increase in permanently restricted net assets	5,344	430
Total increase in net assets	$ 83,972	$ 152,115

Scripps

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENT OF CASH FLOWS
($000)

	For the Six Months Ended March 31 2016	2015
Operating activities and nonoperating gains		
Total increase in net assets	$83,972	$152,115
Reconciliation of total change in net assets to cash flows (used in) provided by operating activities and nonoperating gains and losses:		
Depreciation and amortization	69,050	59,858
Amortization of debt issuance costs	192	202
Amortization of original issue premium	(302)	(303)
Provision for bad debts	19,951	19,473
Realized and unrealized gains on investments	(6,011)	(39,381)
Increase in investments designated as trading	(162,957)	(23,692)
Market adjustment on interest rate swaps	1,142	5,693
Loss on disposal of property	338	19
Restricted contributions and investment income	(16,412)	(34,421)
Change in assets and liabilities:		
Accounts receivables - net	(74,673)	(42,857)
Other current assets	1,697	(73,303)
Other assets	(8,134)	(39,257)
Accounts payable and accrued liabilities	(10,551)	34,243
Other liabilities	831	(1,753)
Net cash (used in) provided by operating activities:	(101,868)	16,636
Investing activities:		
Purchases of property, plant and equipment	(115,254)	(109,691)
Net cash used in investing activities:	(115,254)	(109,691)
Financing activities:		
Proceeds from restricted contributions and investment income	15,958	35,316
Proceeds from line of credit	-	35,400
Payments on notes / lease payable	(1,957)	(1,797)
Proceeds from long-term debt	200,000	-
Payments on long-term debt	(15,500)	(14,945)
Proceeds from sale of donated financial assets	83	204
Net cash provided by financing activities:	198,584	54,178
Decrease in cash and cash equivalents	(18,538)	(38,877)
Cash and cash equivalents at beginning of period	292,596	283,239
Cash and cash equivalents at end of period	$274,058	$244,362

SCRIPPS HEALTH
OBLIGATED GROUP
NOTES TO THE OBLIGATED GROUP FINANCIAL STATEMENTS
(UNAUDITED)

NOTE (1) BASIS OF PRESENTATION

In the opinion of management, all adjustments, consisting of normal recurring adjustments necessary for the fair presentation of the statements of financial position and results of operations as of and for the quarter ended March 31, 2016 and 2015 as well as for the year-to-date September 30, 2015 have been made.

NOTE (2) FAIR VALUE MEASUREMENTS

The Organization accounts for certain assets and liabilities at fair value. A fair value hierarchy for valuation inputs prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels and is determined by the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

Level 1: Quoted prices are available in active markets for identical assets or liabilities as of the measurement date. Financial assets and liabilities in Level 1 include U.S. and foreign equity securities.

Level 2: Pricing inputs are based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the asset or liabilities. Financial assets and liabilities in this category generally include U.S. and foreign government securities, asset-backed securities, U.S. and foreign corporate bonds and loans, municipal bonds, commingled funds, interest rate swaps, real estate, and annuity/unitrust liabilities.

Level 3: Pricing inputs are generally unobservable for the assets or liabilities and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require management's judgment or estimation of assumptions that market participants would use in pricing the assets or liabilities. The fair values are therefore determined using factors that involve considerable judgment and interpretations, including but not limited to, private and public comparables, third-party appraisals, discounted cash flow models, and fund manager estimates. There are no Level 3 financial assets or liabilities at March 31, 2016 and 2015.

Assets and liabilities measured at fair value are based on one or more of the three valuation techniques. The three valuation techniques are identified in the tables below. Where more than one technique is noted, individual assets or liabilities were valued using one or more of the noted techniques. The valuation techniques are as follows:

a) Market approach. Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.

b) Cost approach. Amount that would be required to replace the service capacity of asset (replacement cost).

c) Income approach. Techniques to convert future amounts to a single present amount based on market expectations (including present value techniques, option-pricing, and excess earnings models).

The following represents financial assets and liabilities measured at fair value on a recurring basis as of March 31, 2016 (in thousands). Alternative investments are accounted for using the equity method of accounting, which is not a fair value measurement.

			Active Markets for Identical Assets		Significant Other Observable Inputs				Equity	Valuation Technique
		March 31, 2016		(Level 1)		(Level 2)		Fair Value	Method	(a,b,c)
Investments:										
Liquid investments										
Cash equivalents	$	13,548	$	13,548	$	-	$	13,548	$ -	a
Equity securities										
U.S. equity	$	372,189	$	372,189	$	-	$	372,189	$ -	a
Foreign equity		352,324		352,324		-		352,324	-	a
Foreign equity (commingled)		150,644		-		150,644		150,644	-	a
	$	875,157	$	724,513	$	150,644	$	875,157	$ -	
Fixed income securities										
U.S. government	$	17,849	$	-	$	17,849	$	17,849	$ -	a
U.S. government agencies		57,463		-		57,463		57,463	-	a
U.S. federal agency mortgage-backed		10,179		-		10,179		10,179	-	a
Foreign government		489		-		489		489	-	a
U.S. corporate		342,513		-		342,513		342,513	-	a
U.S. corporate (commingled)		418,555		-		418,555		418,555	-	a
Foreign corporate		11,211		-		11,211		11,211	-	a
	$	858,259	$	-	$	858,259	$	858,259	$ -	
Other investments										
Multi-strategy hedge funds	$	370,673	$	-		-	$	-	$ 370,673	a
Private equity funds		33,447		-		-		-	33,447	a
Real estate		7,862		-		7,862		7,862	-	a
	$	411,982	$	-	$	7,862	$	7,862	$ 404,120	
Total investments	$	2,158,946	$	738,061	$	1,016,765	$	1,754,826	$ 404,120	
Other assets										
Land held for sale		310		-		310		310	-	a
	$	310	$	-	$	310	$	310	$ -	
Total assets at fair value	$	2,159,256	$	738,061	$	1,017,075	$	1,755,136	$ 404,120	
Current liabilities										
Swap hedge	$	27,531	$	-	$	27,531	$	27,531	$ -	c
Other liabilities										
Annuity/unitrust liabilities	$	10,205	$	-	$	10,205	$	10,205	$ -	c
Total liabilities at fair value	$	37,736	$	-	$	37,736	$	37,736	$ -	

The following represents financial assets and liabilities measured at fair value on a recurring basis as of September 30, 2015 (in thousands). Alternative investments are accounted for using the equity method of accounting, which is not a fair value measurement.

	September 30, 2015	Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Fair Value	Equity Method	Valuation Technique (a,b,c)
Investments:						
Liquid investments						
Cash equivalents	$ 16,077	$ 16,077	$ -	$ 16,077	$ -	a
Equity securities						
U.S. equity	$ 349,613	$ 349,613	$ -	$ 349,613	$ -	a
Foreign equity	417,168	417,168	-	417,168	-	a
Foreign equity (commingled)	79,525	-	79,525	79,525	-	a
	$ 846,306	$ 766,781	$ 79,525	$ 846,306	$ -	
Fixed income securities						
U.S. government	$ 20,372	$ -	$ 20,372	$ 20,372	$ -	a
U.S. government agencies	56,182	-	56,182	56,182	-	a
U.S. federal agency mortgage-backed	11,558	-	11,558	11,558	-	a
Foreign government	494	-	494	494	-	a
U.S. corporate	336,923	-	336,923	336,923	-	a
U.S. corporate (commingled)	261,892	-	261,892	261,892	-	a
Foreign corporate	12,216	-	12,216	12,216	-	a
	$ 699,637	$ -	$ 699,637	$ 699,637	$ -	
Other investments						
Multi-strategy hedge funds	$ 395,400	$ -	-	$ -	$ 395,400	a
Private equity funds	25,891	-	-	-	25,891	a
Real estate	8,105	-	8,105	8,105	-	a
	$ 429,396	$ -	$ 8,105	$ 8,105	$ 421,291	
Total investments	$ 1,991,416	$ 782,858	$ 787,267	$ 1,570,125	$ 421,291	
Other assets						
Pledges receivable, net	$ 16,821	$ -	$ 16,821	$ 16,821	$ -	c
Land held for sale	-	-	-	-	-	b
	$ 16,821	$ -	$ 16,821	$ 16,821	$ -	
Total assets at fair value	$ 2,008,237	$ 782,858	$ 804,088	$ 1,586,946	$ 421,291	
Current liabilities						
Swap hedge	$ 24,916	$ -	$ 24,916	$ 24,916	$ -	c
Other liabilities						
Annuity/unitrust liabilities	$ 11,379	$ -	$ 11,379	$ 11,379	$ -	c
Total liabilities at fair value	$ 36,295	$ -	$ 36,295	$ 36,295	$ -	

Transfers to/from Levels 1, 2, and 3 are recognized at the end of the reporting period. There were no transfers for the six months ended March 31, 2016 and 2015.

As of March 31, 2016 and September 30, 2015, the Level 2 instruments listed in the fair value hierarchy table above use the following valuation techniques and inputs:

U.S. and Foreign Government Securities

The fair value of investments in U.S. and foreign government securities, classified as Level 2, was primarily determined using techniques consistent with the market approach. Significant observable inputs to the income approach include data points for benchmark constant maturity curves and spreads.

U.S. and Foreign Corporate Bonds

The fair value of the investments in U.S. and foreign corporate bonds, including mutual and commingled funds that invest primarily in such bonds, classified as Level 2 was primarily determined using techniques that are consistent with the market approach. Significant observable inputs include benchmark yields, reported trades, observable broker/dealer quotes, issuer spreads, and security specific characteristics (such as early redemption options).

Real Estate

The fair value of the real estate investments classified as Level 2 was primarily determined using techniques that are consistent with the market approach. Significant observable inputs include sales of comparable properties, market rents and market rent growth trends.

Annuity/Unitrust Liabilities

The fair value of the annuity/unitrust liabilities as Level 2 was primarily determined using techniques that are consistent with the income approach. Significant observable inputs to the income approach include data points for benchmark constant maturity curves and spreads.

Commingled Funds

The fair value of commingled fund investments classified as Level 2 was determined using the calculated NAV. The values for underlying investments are fair value estimates determined either internally or by an external fund manager based on recent filings, operating results, balance sheet stability, growth, and other business and market sector fundamentals. Due to the significant unobservable inputs present in these valuations, Scripps Health classifies all such investments as Level 2.

Swap Hedge

The fair value of the Swap hedge liability classified as Level 2 is based on independent valuations obtained and is determined by calculating the fair value of the discounted cash flows of the differences between the fixed interest rate of the interest rate swaps and the counterparty's forward LIBOR curve, which is the input used in the valuation, taking also into account any nonperformance risk.

Included within the assets above are investments in certain entities that report fair value using a calculated NAV or its equivalent. The following table and explanations identify attributes relating to the nature and risk of such investments as of March 31, 2016 (in thousands):

NAV Valuation	Fair Value	Unfunded Commitments	Redemption Frequency (if Currently Eligible)	Redemption Notice Period
Commingled:				
Equity securities[1]	$ 150,644	$ -	Monthly	10 days
Fixed income securities[2]	418,555	-	Daily	15 days
	$ 569,199	$ -		

(1) Commingled Funds: Equity – This category includes investments in commingled funds with underlying investments that are fair value estimates determined either internally or by an external fund manager based on recent filings, operating results, balance sheet stability, growth and other business and market sector fundamentals. The investments are diversified by geography, sector, and organization. Liquidity is provided on a monthly basis.

(2) Commingled Funds: Fixed Income – This category includes investments in two commingled funds with underlying investments that are fair value estimates determined either internally or by an external fund manager based on recent filings, operating results, balance sheet stability, growth and other business and market sector fundamentals. The investments are diversified by geography, sector, maturity, and issue. Liquidity is provided on a daily basis. As of March 31, 2016, the category consisted of 100% daily liquidity.

NOTE (3) ENDOWMENTS

The Organization's endowments consist of 87 and 85 individual funds as of March 31, 2016 and 2015, respectively, established for a variety of purposes. Net assets associated with the endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

On September 30, 2008, California Senate Bill No. 1329 was signed into law which enacted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) for California. The Board of Trustees of the Organization has interpreted this as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of the interpretation, the Organization classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Organization in a manner consistent with the standard of prudence described by UPMIFA. In accordance with UPMIFA, the Organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) duration and preservation of the fund, (2) purposes of the Organization and the donor-restricted endowment fund, (3) general economic conditions, (4) possible effect of inflation or deflation, (5) expected total return from income and the appreciation of investments, (6) other resources of the Organization, and (7) investment policies of the Organization.

From time-to-time, the fair value of assets associated with individual endowment funds may fall below the level that the donor or UPMIFA requires the Organization to retain as a fund of perpetual duration.

The Organization has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results while assuming a moderate level of investment risk. The Organization expects its endowment funds, over time, to provide an average rate of return of approximately 5% over the rate of inflation annually. Actual returns in any given year may vary from this amount.

To satisfy its long-term rate-of-return objectives, the Organization relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Organization targets a diversified asset allocation that places an emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

The Organization has a policy of appropriating for distribution each year 6% (with an additional 1% administrative fee) of its endowment fund's average fair value over the prior three-year rolling average market values. In establishing this policy, the Organization considered the long-term expected return on its endowment. Accordingly, over the long term, the Organization expects the current spending policy to allow its endowment to grow at an average of 3% to 4% annually, above inflation. This is consistent with the Organization's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

Changes in endowment net assets for the six months ended March 31, 2016 are as follows (in thousands):

	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets as of September 30, 2015	$ 27,629	$ 80,192	$ 107,821
Investment return:			
Investment income	1,111	-	1,111
Net depreciation (realized and unrealized)	359	-	359
Total investment return	1,470	-	1,470
Contributions	-	5,275	5,275
Appropriation of endowment assets for expenditure	(5,161)	-	(5,161)
Other changes	-	69	69
Endowment net assets as of March 31, 2016	$ 23,938	$ 85,536	$ 109,474

Changes in endowment net assets for the six months ended March 31, 2015 are as follows (in thousands):

	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets as of September 30, 2014	$ 37,165	$ 78,834	$ 115,999
Investment return:			
Investment income	1,158	–	1,158
Net depreciation (realized and unrealized)	2,078	–	2,078
Total investment return	3,236	-	3,236
Contributions	-	356	356
Appropriation of endowment assets for expenditure	(4,908)	–	(4,908)
Other changes	–	74	74
Endowment net assets as of March 31, 2015	$ 35,493	$ 79,264	$ 114,757

Temporarily restricted endowment net assets is as follows at March 31 (in thousands):

	2016	2015
Temporarily restricted net assets:		
The portion of perpetual endowment funds subject to a time restriction under UPMIFA:		
Without purpose restrictions	$ 565	$ 1,786
With purpose restrictions	23,373	33,707
Total endowment funds classified as temporarily restricted net assets	$ 23,938	$ 35,493

NOTE (4) GOODWILL

Goodwill

Impairment assessments of the carrying amount of goodwill are completed annually, or whenever impairment indicators are present for SMF, which includes Scripps Clinic and Scripps Coastal Medical Centers. No goodwill impairment was recorded in 2016 or 2015.

Scripps Clinic

In 2000, Scripps Health acquired all the outstanding shares of SCPO and its wholly owned subsidiaries and substantially all the assets and liabilities of Scripps Clinic Medical Group (SCMG). As a result of the SCMG acquisition, the excess of the purchase price over the fair value of the net assets acquired was recorded as goodwill in the accompanying consolidated statements of financial position in the amount of $50,216,000. Accumulated amortization of goodwill totaled $20,421,000 at March 31, 2016 and 2015. Amortization ceased in fiscal year 2011.

Scripps Coastal Medical Centers

In 2008, Scripps Health purchased substantially all of the net assets of Sharp Mission Park Medical Clinic. As a result of the acquisition, the excess of the purchase price over the fair value of the net assets acquired was recorded as goodwill in the accompanying consolidated statements of financial position in the amount of $6,884,000. Accumulated amortization of goodwill totaled $2,983,000 at March 31, 2016 and 2015. Amortization ceased in fiscal year 2011.

NOTE (5) SUBSEQUENT EVENTS

Scripps Health has evaluated subsequent events occurring between the quarter and six months ended March 31, 2016 and April 26, 2016, the date the financial statements were issued.

SCRIPPS HEALTH
OBLIGATED GROUP FINANCIAL STATEMENTS
MANAGEMENT DISCUSSION AND ANALYSIS
FOR THE QUARTER AND SIX MONTHS ENDED MARCH 31, 2016

	For the Quarter Ended ($000s)	
	March 31, 2016	March 31, 2015
	Actual	Actual
Operating Revenue	$695,937	$648,977
Operating Revenue (Excluding Provider Fee)	$671,175	$620,620
Operating Income	$34,196	$36,626
Operating Income (Excluding Net Proceeds from Provider Fee)	$28,087	$26,869
Operating Margin	4.9%	5.6%
Operating Margin (Excluding Net Proceeds from Provider Fee)	4.2%	4.3%
Operating EBITDA	$73,540	$72,842
Operating EBITDA (Excluding Net Proceeds from Provider Fee)	$67,431	$63,084
Operating EBITDA Margin	10.6%	11.2%
Operating EBITDA Margin (Excluding Net Proceeds from Provider Fee)	10.0%	10.2%
Excess Margin	$14,386	$71,789
Excess Margin %	2.1%	10.5%

Operating revenue for the quarter ended March 31, 2016 was $46,960,000 higher than the quarter ended March 31, 2015 primarily attributable to higher patient service revenue. Patient service revenue, including capitation premium revenue, increased by $44,880,000 due to positive impact of higher volumes, including higher Hospital emergency room visits and outpatient visits, as well as higher trauma cases.

Operating expenses for the quarter ended March 31, 2016 were $49,583,000 higher than the quarter ended March 31, 2015 primarily attributable to $21,387,000 higher wages and benefits due to higher full-time employee headcount and merit increases, $10,331,000 higher supplies expense primarily due to higher prosthesis and pharmaceutical expenses, and $8,040,000 higher physician services expense.

Excess margin for the quarter ended March 31, 2016 compared to the quarter ended March 31, 2015 was $57,403,000 lower than prior year primarily attributable to $53,700,000 less realized and unrealized investment income.

	For the Six Months Ended ($000s)	
	March 31, 2016	March 31, 2015
	Actual	Actual
Operating Revenue	$1,374,226	$1,356,624
Operating Revenue (Excluding Provider Fee)	$1,328,711	$1,250,586
Operating Income	$53,102	$86,165
Operating Income (Excluding Net Proceeds from Provider Fee)	$42,635	$64,142
Operating Margin	3.9%	6.4%
Operating Margin (Excluding Net Proceeds from Provider Fee)	3.2%	5.1%
Operating EBITDA	$134,163	$156,397
Operating EBITDA (Excluding Net Proceeds from Provider Fee)	$123,696	$134,374
Operating EBITDA Margin	9.8%	11.5%
Operating EBITDA Margin (Excluding Net Proceeds from Provider Fee)	9.3%	10.7%
Excess Margin	$79,338	$135,599
Excess Margin %	5.7%	9.6%

Operating revenue for the six months ended March 31, 2016 was $17,603,000 higher than the six months ended March 31, 2015 primarily attributable to higher patient service revenue. Patient service revenue, including capitation premium revenue, increased by $71,778,000 due to positive impact of higher volumes, including higher Hospital emergency room visits and outpatient visits, as well as higher trauma cases, partially offset by $60,522,000 lower provider fee revenue recognized for The California Hospital Fee Program.

Operating expenses for the six months ended March 31, 2016 were $51,245,000 higher than the six months ended March 31, 2015 primarily attributable to $36,572,000 higher wages and benefits due to higher full-time employee headcount and merit increases, $22,256,000 higher supplies expense primarily due to higher prosthesis and pharmaceutical expenses, $17,257,000 higher physician services expense, as well as $9,192,000 higher depreciation expense related to the Scripps Prebys Cardiovascular Institute (SPCI) at La Jolla Hospital which was placed in service during December 2014 and ICD-10 placed in service effective October 1, 2015, partially offset by $48,966,000 lower Provider Fee expense recognized for The California Hospital Fee Program.

Excess margin for the six months ended March 31, 2016 compared to the six months ended March 31, 2015 was $56,261,000 lower than prior year primarily attributable to $33,063,000 lower operating income and less favorable investment income of $29,891,000.

	March 31, 2016	March 31, 2015	September 30, 2015
Unrestricted Cash & Investments ($000s)	$ 2,227,429	$ 2,134,431	$2,066,139
Days Unrestricted Cash on Hand *	340.8	350.4	327.6
Days in AR, Net *	53.2	48.1	47.3
Accounts Payable & Accrued Liabilities ($000s)*	$ 357,304	$ 343,829	$358,524
Days in AP & Accrued Liabilities *	52.4	53.8	56.9
Unrestricted Cash & Investments to Total Debt	207.1%	240.4%	233.0%
Long Term Debt ($000s)	$ 1,040,585	$ 867,900	$ 866,577
Current Portion of Long-Term Debt ($000s)	$ 34,976	$ 19,856	$19,992
Total Debt ($000s)	$ 1,075,561	$ 887,756	$ 886,570
Debt to Capitalization	26.8%	23.4%	23.7%

* Amounts and ratios exclude the impact of provider tax revenues and expenses.

SIGNIFICANT TRANSACTIONS

Tax Exempt Bonds

In October 2015, Scripps Health made scheduled annual bond principal payments amounting to $12,650,000, which included $3,175,000 payment on the 2008A and $9,475,000 payment on the 2008G tax-exempt bond series. In November 2015, Scripps Health made scheduled annual principal payments amounting to $2,850,000 on the 2010A tax-exempt bond series.

2016 Taxable Financing

On January 14th, Scripps closed on a $50,000,000 taxable term loan with Union Bank. The loan is interest-only until October 2018 and then fully amortized over the remainder of the term. The amortization was structured to maintain level debt service, taking into consideration the planned call of the 2008A bonds in 2018. Proceeds of the financing are unrestricted and can be used for general corporate purposes.

2016 Tax-Exempt Financing

On February 29, 2016, Scripps received $100,000,000 from the issuance of Series 2016B Bonds through California Health Facilities Financing Authority ("CHFFA") on behalf of Scripps Health. The bonds have a ten-year term.

On February 29, 2016, Scripps received $50,000,000 from the issuance of Series 2016A Bonds through California Health Facilities Financing Authority ("CHFFA") on behalf of Scripps Health. The bonds have a ten-year term.

Proceeds of the financings were used to reimburse Scripps for prior qualified capital expenditures; therefore the funds were unrestricted immediately upon closing the transaction.

Provider Fee Program

CY2014-CY2016 Provider Fee Program

In September 2013, SB 239 was approved and created a three-year hospital fee program effective January 1, 2014 through December 31, 2016. It is estimated to result in nearly $10 billion in new federal Medi-Cal funding for California hospitals by making supplemental payments for inpatient and outpatient traditional and managed care services, as well as specialty care including trauma, high acuity, inpatient psychiatric, sub-acute care and transplant services.

On December 10, 2014, CHA announced that the Centers for Medicare & Medicaid Services (CMS) approved the fee-for-service payments for CY2014-CY2016. On June 30, 2015 the Centers for Medicare & Medicaid Services approved the non-expansion managed care rates for the first six months of the CY2014-16 hospital fee program. On March 29, 2016, the Centers for Medicare & Medicaid Services (CMS) issued the approval letters for the 2014-16 hospital fee program expansion population managed care rates for January 1, 2014 to June 30, 2014. In FY2016, Scripps Health recognized $10,467,000 net program income based on final CHA model for 2014-2016 Provider Fee Program as follows:

Medi-Cal Supplemental Provider Fee Schedule for 2014-2016 Program For the Six Months Ended 3/31/16 ($000s)				
Hospitals	Supplemental Revenue	Provider Fee	CHFT Fee	Net Operating Income (Loss)
La Jolla	$ -	$ -	$ -	$ -
Green	1,055	(4,907)	-	(3,852)
Encinitas	3,161	(5,662)	-	(2,501)
Mercy	41,300	(24,660)	181	16,821
Hospitals	$ 45,516	$ (35,229)	$ 181	$ 10,467

Epic

On April 30, 2015, the Board of Trustees of Scripps Health approved the implementation of an integrated information platform for Scripps Health inpatient and ambulatory Electronic Health Record ("EHR") and revenue cycle management system ("Epic Capital Project"), in accordance with the project plan, cost model, and timeline presented by management. Epic Systems Corporation was selected as the vendor for the new Scripps EHR and revenue cycle system. Accordingly, the Chief Executive Officer of Scripps Health executed the License and Support Agreement with Epic Systems Corporation for the project plan, implementation cost, and system support, as described and recommended by Management.

The project has an approved capital plan budget of $308.6 million and an estimated operating cost of $360.5 million over 10 years ($277.0 million and $180.7 million respectively, net of savings from retiring the software applications being replaced by the Epic implementation).

As of March 31, 2016 life-to-date, Scripps Health has capitalized $52.9 million of related costs and incurred $10.9 million of related operating expenses. The capital costs to date are accumulated in designated CIP accounts on the balance sheet until various modules of the EHR and revenue cycle system are placed in service (system go-live dates). At in-service date(s), Scripps will record identifiable equipment and software assets from CIP and will begin depreciating these assets on a straight line basis over the estimated useful lives of the EHR and revenue cycle system modules. The planned go-live dates range from April 2017 to January 2018.

Furthermore, as a result of Epic implementation a number of current EHR applications will be phased out and decommissioned. As a result, Scripps Health made revisions in estimates regarding the remaining useful lives of related fixed assets on the books. The remaining useful lives of assets with a combined net book value of $22.0 million were reduced to coincide with planned phase-out dates. This will add approximately $3.7 million to FY2016 depreciation expense.

ICD-10

Scripps Health implemented ICD-10 effective October 1, 2015. As a result, Scripps Health placed in service related software and hardware assets totaling $19,855,000 with useful lives ranging from 29 to 60 months. This will add approximately $5,662,000 to depreciation and amortization expense in FY2016.

Credit Ratings

In March 2016, Fitch affirmed Scripps Health bond ratings of AA/F1+, with an outlook of Stable. In April 2016, Moody's affirmed Scripps Health bond ratings of Aa3 with an outlook of stable.