



NARRATIVE: TRINITY HEALTH UNAUDITED QUARTERLY REPORT

Trinity Health Unrestricted Revenue Reaches \$4.3 billion in Q1 FY17; Operating and Nonoperating margins drive positive results

Summary Highlights for the First Quarter of FY17 (Quarter Ended September 30, 2016)

In the first quarter of fiscal year 2017, Trinity Health experienced volume growth from acquisitions and same ministries, driving revenue growth of \$489 million to \$4.3 billion, a 12.9% increase over prior year. Trinity Health's Connecticut acquisitions accounted for \$299 million or 7.9% of the increase. Volume increased over the prior year in 15 of its 20 regional health ministries. Revenue, excluding the impact of acquisitions, increased primarily due to volume growth across the system and modestly improved case mix.

For the first quarter of fiscal year 2017, Trinity Health reported operating income of \$43.3 million, operating margin of 1.0%, and operating cash flow margin of 7.3%. These represent a slight reduction from fiscal year 2016 which included operating income of \$48.3 million, operating margin of 1.3% and operating cash flow margin of 7.8%. While an unfavorable shift in payor mix and pressure on payment rates continued in fiscal year 2017, the decline from the prior year is largely attributed to increased costs for labor (including contract labor), purchased services, and supplies. Trinity Health has undertaken targeted efficiency initiatives ("Transforming Operations") to improve performance and address the unfavorable industry trends that have continued into fiscal year 2017. Transforming Operations initiatives are focused primarily on labor and supply costs, and on clinical operational efficiencies.

Nonoperating income of \$436 million for the first quarter of fiscal year 2017 improved \$762 million from the prior year driven by investment earnings.

Highlights of results for the first quarter ended September 30, 2016, include:

- Total assets of \$24.0 billion
- Total net assets of \$10.8 billion
- Total unrestricted revenue of \$4.3 billion, a 12.9% increase over fiscal 2016 with a 5.0% increase excluding the impact of the Connecticut acquisitions
- Operating income of \$43.3 million
- Nonoperating Income of \$436 million
- Unrestricted cash and investments of \$7.9 billion
- Days cash on hand of 180 days

TRINITY HEALTH

UNAUDITED QUARTERLY REPORT

For the three months ended September 30, 2016 and 2015

TRINITY HEALTH

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

ASSETS	As of	
	September 30, 2016	June 30, 2016
CURRENT ASSETS:		
Cash and cash equivalents	\$ 974,578	\$ 1,044,683
Investments	3,593,884	3,617,501
Security lending collateral	343,963	262,035
Assets limited or restricted as to use - current portion	312,565	314,706
Patient accounts receivable - net of allowance for doubtful accounts of \$413.2 million and \$385.2 million at September 30, 2016 and June 30, 2016, respectively	1,942,354	1,849,736
Estimated receivables from third-party payors	252,210	248,179
Other receivables	308,966	336,705
Inventories	253,998	248,092
Assets held for sale	8,491	64,272
Prepaid expenses and other current assets	228,670	212,008
Total current assets	<u>8,219,679</u>	<u>8,197,917</u>
ASSETS LIMITED OR RESTRICTED AS TO USE - noncurrent portion:		
Held by trustees under bond indenture agreements	7,207	4,881
Self-insurance, benefit plans and other	809,214	780,102
By Board	3,196,118	2,959,641
By donors	457,650	409,493
Total assets limited or restricted as to use - noncurrent portion	<u>4,470,189</u>	<u>4,154,117</u>
PROPERTY AND EQUIPMENT - Net	7,801,855	7,676,734
INVESTMENTS IN UNCONSOLIDATED AFFILIATES	2,782,047	2,681,778
GOODWILL	320,411	304,845
OTHER ASSETS	<u>356,056</u>	<u>363,480</u>
TOTAL ASSETS	<u>\$ 23,950,237</u>	<u>\$ 23,378,871</u>

(Continued)

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

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

	As of	
	September 30, 2016	June 30, 2016
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Commercial paper	\$ 160,905	\$ 145,958
Short-term borrowings	1,067,730	1,067,730
Current portion of long-term debt	107,232	106,345
Accounts payable	897,179	987,225
Accrued expenses	453,565	374,213
Salaries, wages, and related liabilities	760,673	861,757
Current portion of self-insurance reserves	256,682	255,552
Payable under security lending agreements	343,963	262,035
Liabilities held for sale	11,809	67,453
Estimated payables to third-party payors	370,903	374,014
Total current liabilities	4,430,641	4,502,282
 LONG-TERM DEBT - Net of current portion	 5,151,915	 5,132,377
 SELF-INSURANCE RESERVES - Net of current portion	 973,179	 933,362
 ACCRUED PENSION AND RETIREE HEALTH COSTS	 1,848,156	 1,857,639
 OTHER LONG-TERM LIABILITIES	 758,226	 705,998
Total liabilities	13,162,117	13,131,658
 NET ASSETS:		
Unrestricted net assets	10,069,103	9,576,379
Noncontrolling ownership interest in subsidiaries	191,225	186,595
Total unrestricted net assets	10,260,328	9,762,974
Temporarily restricted net assets	351,084	326,651
Permanently restricted net assets	176,708	157,588
Total net assets	10,788,120	10,247,213
 TOTAL LIABILITIES AND NET ASSETS	 \$ 23,950,237	 \$ 23,378,871

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

(Concluded)

TRINITY HEALTH
CONSOLIDATED STATEMENTS OF OPERATIONS AND
CHANGES IN NET ASSETS (UNAUDITED)
THREE MONTHS ENDED SEPTEMBER 30, 2016 and 2015
(In thousands)

	<u>2016</u>	<u>2015</u>
UNRESTRICTED REVENUE:		
Patient service revenue - net of contractual and other allowances	\$ 3,834,933	\$ 3,448,881
Provision for bad debts	(130,754)	(109,203)
Net patient service revenue less provision for bad debts	3,704,179	3,339,678
Premium and capitation revenue	251,764	207,892
Net assets released from restrictions	4,191	4,178
Other revenue	324,357	243,441
Total unrestricted revenue	<u>4,284,491</u>	<u>3,795,189</u>
EXPENSES:		
Salaries and wages	1,864,649	1,650,247
Employee benefits	350,514	334,161
Contract labor	60,082	41,514
Total labor expenses	<u>2,275,245</u>	<u>2,025,922</u>
Supplies	697,417	624,658
Purchased services	510,908	429,863
Depreciation and amortization	216,369	200,022
Occupancy	184,357	166,983
Medical claims	106,903	91,519
Interest	51,293	47,248
Other	198,729	160,667
Total expenses	<u>4,241,221</u>	<u>3,746,882</u>
OPERATING INCOME	<u>43,270</u>	<u>48,307</u>
NONOPERATING ITEMS:		
Investment earnings (losses)	278,411	(366,706)
Equity in earnings (losses) of unconsolidated affiliates	92,612	(28,695)
Change in market value and cash payments of interest rate swaps	2,219	(29,593)
Inherent contributions	62,057	99,654
Other, including income taxes	593	(367)
Total nonoperating items	<u>435,892</u>	<u>(325,707)</u>
EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES	479,162	(277,400)
EXCESS OF REVENUE OVER EXPENSES ATTRIBUTABLE TO NONCONTROLLING INTEREST	(11,674)	(9,772)
EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES, net of noncontrolling interest	<u>\$ 467,488</u>	<u>\$ (287,172)</u>

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

TRINITY HEALTH

CONSOLIDATED STATEMENT OF CHANGES IN NET ASSETS (UNAUDITED)

THREE MONTHS ENDED SEPTEMBER 30, 2016 and 2015

(In thousands)

	<u>2016</u>	<u>2015</u>
UNRESTRICTED NET ASSETS:		
Unrestricted net asset attributable to Trinity Health:		
Excess (deficiency) of revenue over expenses	\$ 467,488	\$ (287,172)
Net assets released from restrictions for capital acquisitions	2,369	4,095
Net change in retirement plan related items - consolidated organizations	27,821	9,406
Other	<u>(4,225)</u>	<u>(2,757)</u>
Increase (decrease) in unrestricted net assets before discontinued operations	493,453	(276,428)
Discontinued operations:		
Loss from operations	(729)	(13,612)
Loss on disposals and substitutions of membership interests	-	(9,652)
Increase (decrease) in unrestricted net assets attributable to Trinity Health	<u>492,724</u>	<u>(299,692)</u>
Unrestricted net asset attributable to noncontrolling interests:		
Excess of revenue over expenses attributable to noncontrolling interests	11,674	9,772
Noncontrolling interest related to acquisitions	2,500	29,272
Dividends	<u>(9,544)</u>	<u>(6,803)</u>
Increase in unrestricted net assets attributable to noncontrolling interest before discontinued operations	4,630	32,241
Discontinued operations attributable to noncontrolling interests:		
Income from operations	-	47
Increase in unrestricted net assets attributable to noncontrolling interest	<u>4,630</u>	<u>32,288</u>
TEMPORARILY RESTRICTED NET ASSETS:		
Contributions	24,485	11,758
Net investment gain (loss)	4,945	(6,190)
Net assets released from restrictions	(6,560)	(8,273)
Acquisitions	3,078	11,948
Other	<u>(1,515)</u>	<u>(3,709)</u>
Increase in temporarily restricted net assets	<u>24,433</u>	<u>5,534</u>
PERMANENTLY RESTRICTED NET ASSETS:		
Contributions for endowment funds	340	160
Net investment gain (loss)	2,319	(1,430)
Acquisitions	16,526	3,232
Other	<u>(65)</u>	<u>(631)</u>
Increase in permanently restricted net assets	<u>19,120</u>	<u>1,331</u>
INCREASE (DECREASE) IN NET ASSETS	540,907	(260,539)
NET ASSETS - BEGINNING OF YEAR	<u>10,247,213</u>	<u>10,795,906</u>
NET ASSETS - END OF YEAR	<u>\$ 10,788,120</u>	<u>\$ 10,535,367</u>

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

TRINITY HEALTH**SUMMARIZED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)****THREE MONTHS ENDED SEPTEMBER 30, 2016 and 2015****(In thousands)**

	<u>2016</u>	<u>2015</u>
OPERATING ACTIVITIES:		
Increase (decrease) in net assets	\$ 540,907	\$ (260,539)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	216,369	200,022
Provision for bad debts	130,754	109,203
Inherent contribution in acquisitions	(62,057)	(99,654)
Change in net unrealized and realized gains and losses on investments	(271,244)	405,343
Change in market values of interest rate swaps	(3,663)	35,765
Undistributed equity in losses (earnings) of unconsolidated affiliates	(100,221)	29,166
Net change in retirement items - consolidated organizations	8,690	(31)
Noncash items including net (gains) losses on disposal - discontinued items	-	15,757
Increase in noncontrolling interest related to acquisitions	(2,500)	(29,272)
Restricted contributions and investment income received	(2,859)	(857)
Restricted net assets acquired related to acquisitions	(19,604)	(15,181)
Other adjustments	(8,035)	(2,354)
Changes in:		
Patient accounts receivable	(182,559)	(148,612)
Other assets	29,682	(27,648)
Accounts payable and accrued expenses	(103,517)	42,746
Estimated receivables from third-party payors	(4,032)	(10,843)
Estimated payables to third-party payors	(11,401)	(37,108)
Self-insurance and other liabilities	13,802	(917)
Accrued pension and retiree health costs	(107,603)	(52,222)
Net cash provided by operating activities of discontinued operations	137	4,066
Total adjustments	<u>(479,861)</u>	<u>417,369</u>
Net cash provided by operating activities	<u>61,046</u>	<u>156,830</u>
INVESTING ACTIVITIES:		
Net sales (purchases) of investments	101,591	(279,447)
Purchases of property and equipment	(241,742)	(211,120)
Proceeds from disposal of property and equipment	1,349	1,681
Proceeds from the sale of divestitures	3,283	29,348
Net cash acquired from acquisitions	5,085	25,967
Change in investments in unconsolidated affiliates	2,471	2,304
Net decrease in assets limited as to use	(7,305)	(441)
Net cash used in investing activities of discontinued operations	-	(1,834)
Net cash used in investing activities	<u>(135,268)</u>	<u>(433,542)</u>
FINANCING ACTIVITIES:		
Proceeds from issuance of debt	13,918	11,926
Repayments of debt	(27,055)	(23,186)
Net change in commercial paper	14,947	259,938
Increase in financing costs and other	(552)	89
Proceeds from restricted contributions and restricted investment income	2,859	857
Net cash provided by financing activities of discontinued operations	-	5,431
Net cash provided by financing activities	<u>4,117</u>	<u>255,055</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	(70,105)	(21,657)
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	<u>1,044,683</u>	<u>843,210</u>
CASH AND CASH EQUIVALENTS - END OF PERIOD	<u>\$ 974,578</u>	<u>\$ 821,553</u>

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

TRINITY HEALTH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) THREE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015

1. ORGANIZATION AND MISSION

Trinity Health Corporation, an Indiana nonprofit corporation headquartered in Livonia, Michigan, and its subsidiaries (“Trinity Health” or the “Corporation”), controls one of the largest health care systems in the United States. The Corporation is sponsored by Catholic Health Ministries, a Public Juridic Person of the Holy Roman Catholic Church. The Corporation operates a comprehensive integrated network of health services, including inpatient and outpatient services, physician services, managed care coverage, home health care, long-term care, assisted living care, and rehabilitation services located in 22 states. The operations are organized into Regional Health Ministries, National Health Ministries and Mission Health Ministries (“Health Ministries”). The mission statement for the Corporation is as follows:

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial reporting information. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included and are of a normal and recurring nature. Operating results for the three months ended September 30, 2016 are not necessarily indicative of the results to be expected for the year ending June 30, 2017.

Principles of Consolidation – The consolidated financial statements include the accounts of the Corporation, and all wholly-owned, majority-owned and controlled organizations. Investments where the Corporation holds less than 20% of the ownership interest are accounted for using the cost method. All other investments that are not controlled by the Corporation are accounted for using the equity method of accounting. The equity share of income or losses from investments in unconsolidated affiliates is recorded in other revenue if the unconsolidated affiliate is operational and projected to make routine and regular cash distributions; otherwise, the equity share of income or losses from investments in unconsolidated affiliates is recorded in nonoperating items in the consolidated statements of operations and changes in net assets. All material intercompany transactions and account balances have been eliminated in consolidation. Mercy Suburban Hospital and East Norriton Physician Services (“Mercy Suburban”), St. Joseph Mercy Port Huron (“Port Huron”), and Saint Michael's Medical Center (“St. Michael's”) were divested in fiscal year 2016 and the operations of these entities are reflected as discontinued operations for the three months ended September 30, 2015. The consolidated statements of cash flows include impacts of cash flows related to these entities. Notes to these consolidated financial statements exclude these entities.

Use of Estimates – The preparation of consolidated financial statements in conformity with GAAP requires management of the Corporation to make assumptions, estimates and judgments that affect the amounts reported in the consolidated financial statements, including the notes thereto, and related disclosures of commitments and contingencies, if any. The Corporation considers critical accounting policies to be those that require more significant judgments and estimates in the preparation of its consolidated financial statements, including the following: recognition of net patient service revenue, which includes contractual allowances; provisions for bad

debts and charity care; premium revenue; recorded values of investments, derivatives and goodwill; reserves for losses and expenses related to health care professional and general liabilities; and risks and assumptions for measurement of pension and retiree medical liabilities. Management relies on historical experience and other assumptions believed to be reasonable in making its judgment and estimates. Actual results could differ materially from those estimates.

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

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

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

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

Securities Lending – The Corporation participates in securities lending transactions whereby a portion of its investments are loaned, through its agent, to various parties in return for cash and securities from the parties as collateral for the securities loaned. Each business day, the Corporation, through its agent, and the borrower determine the market value of the collateral and the borrowed securities. If on any business day the market value of the collateral is less than the required value, additional collateral is obtained as appropriate. The amount of cash collateral received under securities lending is reported as an asset and a corresponding payable in the consolidated balance sheets and is up to 105% of the market value of securities loaned. As of September 30, 2016 and June 30, 2016, the Corporation had securities loaned of \$371.2 million and \$272.6 million, respectively, and received collateral (cash and noncash) totaling \$378.2 million and \$277.7 million, respectively, relating to the securities loaned. The fees received for these transactions are recorded in non-operating investment income in the consolidated statements of operations and changes in net assets. In addition, certain pension plans participate in securities lending programs with the Northern Trust Company, the plans' agent.

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

Donor-Restricted Gifts – Unconditional promises to give cash and other assets to the Corporation are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or

permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the consolidated statements of operations and changes in net assets.

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

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

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

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

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

Asset Impairments –

Property and Equipment – The Corporation evaluates long-lived assets for possible impairment whenever events or changes in circumstances indicate that the carrying amount of the asset, or related group of assets, may not be recoverable from estimated future undiscounted cash flows. If the estimated future undiscounted cash flows are less than the carrying value of the assets, the impairment recognized is calculated as the carrying value of the long-lived assets in excess of the fair value of the assets. The fair value of the assets is estimated based on appraisals, established market values of comparable assets or internal estimates of future net cash flows expected to result from the use and ultimate disposition of the assets.

Goodwill – Goodwill is tested for impairment on an annual basis or when an event or change in circumstance indicates the value of a reporting unit may have changed. Testing is conducted at the reporting unit level. If the carrying amount of the reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. Estimates of fair value are based on appraisals, established market prices for comparable assets or internal estimates of future net cash flows.

Other Assets – Other assets includes long-term notes receivable, reinsurance recovery receivables, definite and indefinite-lived intangible assets other than goodwill, prepaid pension and retiree health costs. The net balances of definite-lived intangible assets include noncompete agreements, physician guarantees and other definite-lived intangible assets with finite lives amortized using the straight-line method over their estimated useful lives, which generally range from 2 to 10 years. Indefinite-lived intangible assets primarily include trade names.

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

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

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

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

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

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

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

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

Reserves for incurred but not reported claims have been established to cover the unpaid costs of health care services covered under the premium and capitation arrangements. The premium and capitation arrangement reserves are classified with accrued expenses in the consolidated balance sheets. The liability is estimated based

on actuarial studies, historical reporting, and payment trends. Subsequent actual claim experience will differ from the estimated liability due to variances in estimated and actual utilization of health care services, the amount of charges, and other factors. As settlements are made and estimates are revised, the differences are reflected in current operations.

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

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

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

Adopted Accounting Pronouncements –

On July 1, 2016, the Corporation adopted Accounting Standards Update ("ASU") No. 2016-07, *"Investments – Equity Method and Joint Ventures: Simplifying the Transition to the Equity Method of Accounting."* This guidance eliminates the requirement to retrospectively apply the equity method to an investment that subsequently qualifies for such accounting as a result of an increase in the level of ownership interest or degree of influence. The adoption of this guidance did not have an impact on the Corporation's consolidated financial statements.

Forthcoming Accounting Pronouncements –

In August 2016, the FASB issued ASU No. 2016-15, *"Classification of Certain Cash Receipts and Cash Payments."* This guidance adds or clarifies guidance on the classification of certain cash receipts and payments in the consolidated statement of cash flows. This guidance is effective for the Corporation beginning July 1, 2019. The Corporation is still evaluating the impact this guidance may have on its consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-14, *"Presentation of Financial Statements of Not-For-Profit Entities."* This guidance simplifies and improves how not-for-profit entities classify net assets as well as the information presented in financial statements and notes about liquidity, financial performance and cash flows. This guidance is effective for the Corporation beginning July 1, 2018. The Corporation is still evaluating the impact this guidance may have on its consolidated financial statements.

In May 2016, the FASB issued ASU No. 2016-12, *"Revenue From Contracts With Customers: Narrow-Scope Improvements and Practical Expedients,"* which amends certain aspects of the FASB's revenue standard ASU No. 2014-09, *"Revenue From Contracts With Customers."* In March 2016, the FASB issued ASU No. 2016-08, *"Revenue From Contracts With Customers: Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net)."* This guidance amends the principal versus agent implementation guidance and illustrations in the FASB's revenue standard ASU No. 2014-09. In July 2015, the FASB issued ASU No. 2015-14, *"Revenue From*

Contracts With Customers (Topic 606): Deferral of the Effective Date," which defers the effective date of the FASB's revenue standard, ASU No. 2014-09, by one year for all entities and permits early adoption on a limited basis. In May 2014, the FASB issued ASU No. 2014-09. This guidance outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. After the deferral of the effective date, this guidance is effective for the Corporation beginning July 1, 2018. The Corporation is still evaluating the impact this guidance may have on its consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-06, *"Derivatives & Hedging: Contingent Put & Call Options in Debt Instruments."* This guidance clarifies that in assessing whether an embedded contingent put or call option is clearly and closely related to the debt host, an entity is required to perform only the four step sequence in Accounting Standards Codification 815-15-25-42. This guidance is effective for the Corporation beginning July 1, 2018. The Corporation does not expect this guidance to have a material impact on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *"Leases."* This guidance introduces a lessee model that brings substantially all leases on the consolidated balance sheet. This guidance is effective for the Corporation beginning July 1, 2019. Modified retrospective application is required. The Corporation is still evaluating the impact this guidance may have on its consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, *"Recognition and Measurement of Financial Assets and Financial Liabilities."* This guidance revises accounting related to (1) the classification and measurement of investments in equity securities and (2) the presentation of certain fair value changes for financial liabilities measured at fair value. It also amends certain disclosure requirements associated with the fair value of financial instruments. This guidance is effective for the Corporation beginning July 1, 2019. The Corporation is still evaluating the impact this guidance may have on its consolidated financial statements.

In September 2015, the FASB issued ASU No. 2015-16, *"Simplifying the Accounting for Measurement-Period Adjustments."* This guidance requires an acquirer in a business combination to recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The effect on earnings of changes in depreciation or amortization, or other income effects (if any) as a result of change to the provisional amounts, calculated as if the accounting had been completed as of the acquisition date, must be recorded in the reporting period in which the adjustment amounts are determined rather than retrospectively. Also, the acquirer must present separately on the face of the income statement, or disclose in the notes, the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. This guidance is effective for the Corporation beginning July 1, 2017. The Corporation does not expect this guidance to have a material impact on its consolidated financial statements.

In July 2015, the FASB issued ASU No. 2015-11, *"Simplifying the Measurement of Inventory."* This guidance requires entities to measure most inventories at the lower of cost or net realizable value. This guidance is effective for the Corporation beginning July 1, 2017. The Corporation does not expect this guidance to have a material impact on its consolidated financial statements.

In May 2015, the FASB issued ASU No. 2015-09, *"Disclosures About Short-Duration Contracts."* This guidance expands the disclosures that an insurance entity must provide about its short-duration insurance contracts. This guidance is effective for the Corporation beginning July 1, 2017. The Corporation does not expect this guidance to have a material impact on its consolidated financial statements.

In February 2015, the FASB issued ASU No. 2015-02, *"Amendments to the Consolidation Analysis."* This guidance significantly changes the consolidation analysis required under GAAP. This guidance is effective for the Corporation beginning July 1, 2017. The Corporation does not expect this guidance to have a material impact on its consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, *"Disclosure of Uncertainties About an Entity's Ability to Continue as a Going Concern,"* which provides guidance on determining when and how reporting entities must

disclose going-concern uncertainties in their financial statements. This guidance is effective for the Corporation beginning July 1, 2017. The Corporation does not expect this guidance to have an impact on its consolidated financial statements.

3. INVESTMENTS IN UNCONSOLIDATED AFFILIATES, BUSINESS ACQUISITIONS AND DIVESTITURES

Investments in Unconsolidated Affiliates – The Corporation and certain of its Health Ministries have investments in entities that are recorded under the cost and equity methods of accounting. The Corporation's share of equity earnings from entities accounted for under the equity method was \$105.4 million and (\$23.1) million for the three months ended September 30, 2016 and 2015, respectively, of which \$12.8 million and \$5.6 million, respectively, is included in other revenue and \$92.6 million and (\$28.7) million, respectively, is included in nonoperating items in the consolidated statements of operations and changes in net assets. The most significant of these investments include the following:

BayCare Health System – The Corporation has a 50.4% interest in BayCare Health System Inc. and Affiliates ("BayCare"), a Florida not-for-profit corporation exempt from state and federal income taxes. BayCare was formed in 1997 pursuant to a Joint Operating Agreement ("JOA") among the not-for-profit, tax-exempt members of the Catholic Health East BayCare Participants, Morton Plant Mease Health Care, Inc., and South Florida Baptist Hospital, Inc. (collectively, the "Members"). BayCare consists of three community health alliances located in the Tampa Bay area of Florida, including St. Joseph's-Baptist Healthcare Hospital, St. Anthony's Health Care, and Morton Plant Mease Health Care. The Corporation has the right to appoint nine of the 21 voting members of the board of directors of BayCare, therefore the Corporation accounts for BayCare under the equity method of accounting. As of September 30, 2016 and June 30, 2016, the Corporation's investment in BayCare totaled \$2,183 million and \$2,079 million, respectively.

Gateway Health Plan – The Corporation has a 50% interest in Gateway Health Plan, L.P. and subsidiaries ("GHP"), a Pennsylvania limited partnership. GHP has two general partners, Highmark Ventures Inc., formerly known as Alliance Ventures, Inc., and Mercy Health Plan (a wholly owned subsidiary of the Corporation), each owning 1%. In addition to the general partners, there are two limited partners, Highmark Inc. and Mercy Health Plan, each owning 49%. As of September 30, 2016 and June 30, 2016, the Corporation's investment in GHP totaled \$152.6 million and \$147.6 million, respectively.

Catholic Health System, Inc. – The Corporation has a one-third interest in Catholic Health System, Inc. and subsidiaries ("CHS"). CHS, formed in 1998, is a not-for-profit integrated delivery healthcare system in western New York jointly sponsored by the Sisters of Mercy, Ascension Health System, the Franciscan Sisters of St. Joseph, and the Diocese of Buffalo. The Corporation, Ascension Health System, and the Diocese of Buffalo are the corporate members of CHS. CHS operates several organizations, the largest of which are four acute care hospitals located in Buffalo, New York: Mercy Hospital of Buffalo; Kenmore Mercy Hospital; Sisters of Charity Hospital; and St. Joseph Hospital. As of September 30, 2016 and June 30, 2016, the Corporation's investment in CHS totaled \$73.8 million and \$73.3 million, respectively.

Emory Healthcare/St. Joseph's Health System – The Corporation has a 49% interest in Emory Healthcare/St. Joseph's Health System ("EH/SJHS"). EH/SJHS operates several organizations, including two acute care hospitals, St. Joseph's Hospital of Atlanta and John's Creek Hospital. As of September 30, 2016 and June 30, 2016, the Corporation's investment in EH/SJHS totaled \$70.7 million and \$82.3 million, respectively.

Mercy Health Network – The Corporation has a 50% interest in Mercy Health Network ("MHN"), a nonstock basis membership corporation with Catholic Health Initiatives ("CHI") holding the remaining 50% interest. Effective March 1, 2016, the Corporation and CHI amended and restated their existing MHN JOA that governs certain of their legacy operations in Iowa to strengthen MHN's management responsibilities over the Iowa Operations, to jointly acquire health care operations in Iowa and contiguous markets, and to provide for greater financial, governance, and clinical integration. The JOA provides for the Corporation

and CHI to maintain ownership of their respective assets in Iowa while agreeing to operate the Corporation's Iowa hospitals in collaboration with CHI's Mercy Hospital Medical Center, Des Moines, Iowa, as one organization with common governance and management. MHN has developed a regional health care network that provides for a collaborative effort in the areas of community health care development, enhanced access to health services for the poor and sharing of other common goals. Under the JOA, the Corporation and CHI equally share adjusted operating cash flow from Iowa operations which commenced in July 2016. The amount recorded under the cash flow sharing agreement for the three months ended September 30, 2017 was immaterial.

On May 1, 2016, MHN became the sole member of Wheaton Franciscan Services, Inc. ("WFSI"). WFSI operates three hospitals in Iowa located in Waterloo (Covenant Medical Center), Cedar Falls (Sartori Memorial Hospital) and Oelwein (Mercy Hospital of Franciscan Sisters). As a result, WFSI is consolidated into MHN's financial statements. As a result of this transaction, MHN recognized an inherent contribution in their consolidated statement of operations and changes in net assets in subsequent periods of fiscal year 2016, of which, the Corporation's share is \$87.2 million. As of September 30, 2016 and June 30, 2016, the Corporation's investment in MHN totaled \$91.5 million and \$91.0 million, respectively.

Condensed consolidated balance sheets of BayCare, GHP, CHS, EH/SJHS and MHN are as follows (in thousands):

	September 30, 2016				
	Baycare	GHP	CHS	EH/SJHS	MHN
Total assets	\$6,581,700	\$961,266	\$1,109,940	\$447,804	\$231,032
Total liabilities	\$2,062,191	\$654,965	\$892,319	\$289,549	\$43,513

	June 30, 2016				
	Baycare	GHP	CHS	EH/SJHS	MHN
Total assets	\$6,378,411	\$984,457	\$1,105,078	\$452,892	\$240,151
Total liabilities	\$2,068,541	\$689,217	\$884,839	\$283,450	\$53,768

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

	Three months ended September 30, 2016				
	Baycare	GHP	CHS	EH/SJHS	MHN
Revenue, net	\$ 831,438	\$ 593,223	\$ 268,721	\$ 131,914	\$ 85,829
Excess (deficiency) of revenue over expenses	\$ 166,907	\$ 6,937	\$ (5,038)	\$ (4,351)	\$ 409

	Three months ended September 30, 2015				
	Baycare	GHP	CHS	EH/SJHS	MHN
Revenue, net	\$784,335	\$549,959	\$262,592	\$117,848	\$ 3,445
Excess (deficiency) of revenue over expenses	(\$77,090)	(\$5,510)	\$24,013	(\$961)	\$ (90)

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

	Three months ended September 30, 2016				
	Baycare	GHP	CHS	EH/SJHS	MHN
Other revenue	\$ -	\$ 2,887	\$ -	\$ -	\$ 469
Equity in earnings of unconsolidated organizations	104,051	-	(103)	(2,132)	-
Other changes in unrestricted net assets	2	2,274	521	-	-
	<u>\$ 104,053</u>	<u>\$ 5,161</u>	<u>\$ 418</u>	<u>\$ (2,132)</u>	<u>\$ 469</u>

	Three months ended September 30, 2015				
	Baycare	GHP	CHS	EH/SJHS	MHN
Other revenue	\$ -	\$ (2,746)	\$ -	\$ -	\$ (45)
Equity in earnings of unconsolidated organizations	(38,935)	-	9,770	(591)	-
Other changes in unrestricted net assets	(653)	(3,109)	(525)	-	-
	<u>\$ (39,588)</u>	<u>\$ (5,855)</u>	<u>\$ 9,245</u>	<u>\$ (591)</u>	<u>\$ (45)</u>

Acquisitions:

Saint Mary's Health System ("SMHS") – On August 1, 2016, the Corporation became, through its Trinity Health-New England subsidiary, the sole corporate member of SMHS, a regional health care system located in Waterbury, Connecticut, as part of a member substitution. As a result of this transaction, the Corporation recognized an inherent contribution of \$54.5 million for the three months ended September 30, 2016 in the consolidated statement of operations and changes in net assets. The Corporation is still in the process of assessing the economic characteristics of certain assets acquired and liabilities assumed. The Corporation expects to substantially complete this assessment within 12 months following the acquisition date and may adjust the amounts recorded as of August 1, 2016 to reflect revised evaluations. Summarized consolidated balance sheet information for SMHS at August 1, 2016 is shown below (in thousands):

Cash, cash equivalents, and investments	\$ 18,252	Accounts payable and accrued expenses	41,879
Patient accounts receivable, net	31,696	Accrued pension and retiree health costs	89,167
Other current assets	10,662	Other long-term liabilities	26,203
Assets limited or restricted as to use, current portion	3,465	Total liabilities acquired	<u>157,249</u>
Property and equipment	100,686	Unrestricted net assets	54,517
Assets limited or restricted as to use, noncurrent portion	62,150	Unrestricted noncontrolling interest	2,500
Other assets	5,859	Total unrestricted net assets	<u>57,017</u>
Total assets acquired	<u>\$ 232,770</u>	Temporarily restricted net assets	1,978
		Permanently restricted net assets	16,526
		Total net assets	<u>\$ 75,521</u>

For the two month period ended September 30, 2016, SMHS reported revenue of \$51.6 million and deficiency of revenue over expenses of \$0.1 million in the consolidated statements of operations.

Saint Francis Care ("SFC") - On October 1, 2015, the Corporation became the sole corporate member of SFC, a Connecticut nonstock corporation. On November 17, 2015, Saint Francis Care, Inc. changed its name to Trinity Health-New England, Inc. SFC is the sole member of Saint Francis Hospital and Medical Center ("SFHMC"), a Connecticut nonstock corporation that operates a hospital in Hartford, Connecticut, and is also the sole member of Mount Sinai Rehabilitation Hospital, a Connecticut nonstock corporation that operates a rehabilitation facility. As a result of this transaction, the Corporation recognized an inherent contribution of \$70.9 million in the consolidated statement of operations and changes in net assets in subsequent periods of fiscal year 2016. Summarized consolidated balance sheet information for SFC at October 1, 2015 is shown below (in thousands):

Cash, cash equivalents, and investments	\$ 135,568	Current portion of long-term debt	\$ 7,298
Patient accounts receivable, net	75,415	Accounts payable and accrued expenses	98,922
Other receivables	10,159	Other current liabilities	17,381
Inventories	9,701	Long-term debt	244,154
Other current assets	16,418	Accrued pension and retiree health costs	197,562
Property and equipment	411,067	Other long-term liabilities	106,717
Assets limited or restricted as to use,		Total liabilities acquired	<u>672,034</u>
noncurrent portion	145,992		
Other assets	18,069	Unrestricted net assets	70,996
Total assets acquired	<u>\$ 822,389</u>	Temporarily restricted net assets	26,180
		Permanently restricted net assets	53,179
		Total net assets	<u>\$ 150,355</u>

As part of the transaction, an investment of \$275 million in capital has been committed over a five year period by the Corporation. As disclosed in Note 5, the transaction included the extinguishment of bonds. In addition, on October 1, 2015, the Corporation novated an interest rate swap from SFC that increased other long-term liabilities in the consolidated balance sheets by \$44.0 million.

For the three month period ended September 30, 2016, SFC reported revenue of \$232.0 million and excess of revenue over expenses of \$56.1 million in the consolidated statements of operations.

Johnson Memorial Medical Center, Inc. ("Johnson") - On January 1, 2016, SFC acquired the assets of Johnson, a non-profit, nonstock holding company located in Stafford Springs, Connecticut. Johnson, through its subsidiaries, provides health care services throughout the Hartford and Tolland Connecticut counties. As a result of this acquisition, the Corporation recognized an inherent contribution of \$4.0 million in the consolidated statement of operations and changes in net assets in subsequent periods of fiscal year 2016. The Corporation is still in the process of assessing the economic characteristics of certain assets acquired and liabilities assumed. The Corporation expects to substantially complete this assessment during the period ending December 31, 2016 and may adjust the amounts recorded as of January 1, 2016 to reflect revised evaluations. Summarized consolidated balance sheet information for Johnson at January 1, 2016 is shown below (in thousands):

Patient accounts receivable, net	\$ 9,330	Current portion of long-term debt	\$ 801
Other receivables	777	Accounts payable and accrued expenses	11,765
Inventories	1,577	Other current liabilities	2,682
Other current assets	1,585	Long-term debt	22,749
Property and equipment	25,908	Other long-term liabilities	141
Other assets	3,472	Total liabilities acquired	<u>38,138</u>
Total assets acquired	<u>\$ 42,649</u>		
		Unrestricted net assets	3,971
		Temporarily restricted net assets	540
		Total net assets	<u>\$ 4,511</u>

For the three month period ended September 30, 2016, Johnson reported revenue of \$17.1 million and deficiency of revenue over expenses of \$0.7 million in the consolidated statements of operations.

Saint Joseph's Hospital Health Center ("SJHHC") – On July 1, 2015, the Corporation became the sole corporate member of SJHHC, a regional health care system located in Syracuse, New York as part of a member substitution. As a result of this transaction, the Corporation recognized an inherent contribution of \$99.7 million for the three months ended September 30, 2015 in the consolidated statement of operations and changes in net assets. The amount of the inherent contribution was adjusted in subsequent periods of the fiscal year 2016, to \$58.3 million for the year ended June 30, 2016. Summarized consolidated balance sheet information for SJHHC at July 1, 2015 is shown below (in thousands):

Cash, cash equivalents, and investments	\$ 104,827	Current portion of long-term debt	\$ 20,723
Patient accounts receivable, net	98,584	Accounts payable and accrued expenses	113,514
Assets limited or restricted as to use,		Long-term debt	321,459
current portion	16,057	Accrued pension and retiree health costs	19,176
Other current assets	25,684	Other long-term liabilities	40,073
Property and equipment	316,294	Total liabilities acquired	<u>514,945</u>
Assets limited or restricted as to use,			
noncurrent portion	34,759	Unrestricted net assets	60,460
Other assets	23,003	Unrestricted noncontrolling interest	28,623
Total assets acquired	<u>\$ 619,208</u>	Total unrestricted net assets	89,083
		Temporarily restricted net assets	11,948
		Permanently restricted net assets	3,232
		Total net assets	<u>\$ 104,263</u>

As part of the transaction, an investment of \$60 million in capital has been committed over a four year period by the Corporation. This amount may be increased to \$90 million if certain operating thresholds are met. As disclosed in Note 5, the transaction included the extinguishment of bonds. For the three month periods ended September 30, 2016 and 2015, SJHHC reported revenue of \$165.6 million and \$162.9 million, respectively, and

deficiency of revenue over expenses of \$1.6 million and \$8.9 million in the consolidated statements of operations, respectively.

Other acquisitions – On July 1, 2016, the Corporation acquired the following entities: Riverbend Medical Group, Inc., a physician practice in Springfield, Massachusetts; Glacier Hills, a continuing care retirement community in Ann Arbor, Michigan; and Mount St. Joseph, a senior living community in Waterville, Maine. The acquisitions of Riverbend Medical Group, Inc. and Glacier Hills resulted in goodwill of \$5.9 million and \$9.7 million, respectively while the acquisition of Mount St. Joseph resulted in inherent contribution of \$7.5 million for the three months ended September 30, 2016. The impact of these acquisitions was otherwise not material to the Corporations consolidated financial statements.

Divestitures:

The consolidated financial statements for all periods present the operations of the following entities as discontinued operations as the transactions were in process prior to the adoption of ASU No. 2014-8 *Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity.*”

Saint Michael's Medical Center ("St. Michael's") – On August 10, 2015, St. Michael's and certain of its affiliates voluntarily filed for reorganization under Chapter 11 of the Bankruptcy Code. Pursuant to the provisions of the Bankruptcy Code, the transaction with Prime Healthcare Services ("Prime"), a hospital system based in Ontario, California, was subject to an "auction sale" process. By order of November 12, 2015, the Bankruptcy Court approved Prime as the successful bidder for the hospital resulting in a first amended and restated asset purchase agreement between the parties. The Corporation provided debtor-in-possession financing of \$15 million to St. Michael's which was subsequently forgiven in consideration of releases by the Official Unsecured Creditors Committee and Debtors of any claims against Trinity Health arising out of Trinity's and Debtors' prepetition relationship, transactions or conduct as more fully described in a Global Settlement Agreement approved by the Bankruptcy Court on April 26, 2016.

Effective May 1, 2016, the Corporation sold substantially all of the health care operations and assets of St. Michael's to Prime and recorded a loss on disposal of \$35.7 million in discontinued operations in the consolidated statements of operations and changes in net assets in subsequent periods of fiscal year 2016.

As part of a court order to settle St. Michael's outstanding debt and accrued interest, the Corporation paid \$55.8 million in July 2016 to settle \$233.4 million of St. Michael's debt and subsequently resulted in a \$177.6 million gain in discontinued operations in the consolidated statements of changes in net assets in June of 2016. St. Michael's continues to operate their remaining businesses as debtor in possession under the jurisdiction of the Court and in accordance with the applicable provisions of the Bankruptcy Code and orders of the Court. St. Michael's prepetition liabilities retained by the Corporation remain subject to settlement under the Bankruptcy Code. For the period ended September 30, 2015, St. Michael's reported revenue of \$47.2 million and deficiency of revenue over expenses of \$6.3 million in discontinued operations in the consolidated statements of changes in net assets.

Mercy Suburban and East Norriton Physician Services ("Mercy Suburban") – Effective February 1, 2016, the Corporation sold substantially all of the health care operations and assets of Mercy Suburban to Prime. The impact of the disposal recorded in discontinued operations in the consolidated statements of changes in net assets at the effective date was immaterial to the Corporation. For the period ended September 30, 2015, Mercy Suburban reported revenue of \$24.0 million and deficiency of revenue over expenses of \$3.0 million, in discontinued operations in the consolidated statements of changes in net assets. As disclosed in Note 4, the transaction resulted in the defeasance of bonds.

St. Joseph Mercy Port Huron ("Port Huron") – Effective September 1, 2015, the Corporation sold substantially all of the Corporation's healthcare operations located in Port Huron, Michigan to Prime. As a result of the sale, a loss on disposal of \$10.2 million was recorded for the months ended September 30, 2015 in the statement of changes in net assets. For the period ended September 30, 2015, Port Huron reported revenue of \$16.1 million and deficiency of revenue over expenses of \$2.2 million in discontinued operations in the

consolidated statements of changes in net assets. As disclosed in Note 4, the transaction resulted in the defeasance of bonds.

4. PROPERTY AND EQUIPMENT

A summary of property and equipment is as follows (in thousands):

	September 30, 2016	June 30, 2016
Land	\$ 354,662	\$ 348,265
Buildings and improvements	9,077,243	8,867,512
Equipment	5,968,802	5,899,324
Capital leased assets	172,641	179,315
Total	15,573,348	15,294,416
Accumulated depreciation and amortization	(8,423,466)	(8,213,922)
Construction in progress	651,973	596,240
Property and equipment, net	<u>\$ 7,801,855</u>	<u>\$ 7,676,734</u>

The following table details the Corporation's committed capital spending in conjunction with recent acquisitions of affiliates:

<u>Regional Health Ministry</u>	<u>Capital Commitment</u>	<u>Commitment Period Ending</u>	<u>Capital Spending through September 30, 2016</u>
Mercy Health System of Chicago	\$140 million over 5 years, \$150 million if performance metrics are achieved	June 30, 2017	\$97 million
Loyola University Health System	\$300 million over 7 years, \$400 million if performance metrics are achieved	June 30, 2018	\$294 million
SJHHC	\$60 million over 4 years, \$90 million if performance metrics are achieved	June 30, 2019	\$21 million
SFC	\$275 million over 5 years if performance metrics are achieved	June 30, 2020	\$38 million

5. LONG-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

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

The Trinity Health Credit Group does not include certain affiliates that borrow on their own or are (or may become) members of a separate New York obligated group, but which are included in the Corporation's consolidated financial statements. St. Peter's Hospital of the City of Albany currently is the obligated group agent of an obligated group created under that certain master trust indenture dated as of January 1, 2008, among St. Peter's Hospital of the City of Albany; St Peter's Health Partners; Memorial Hospital, Albany, N.Y.; Samaritan Hospital of Troy, New York; Seton Health System, Inc.; Sunnyview Hospital and Rehabilitation Center; the Capital Region Geriatric Center, Inc.; Hawthorne Ridge, Inc.; and Manufacturers and Traders Trust Company, as master trustee. In addition, St. Joseph's Hospital Health Center, acquired on July 1, 2015, is not a designated affiliate and is not a part of the Trinity Health Credit Group.

Pursuant to the ARMI, the Obligated Group agent (which is the Corporation) has caused the designated affiliates representing, when combined with the Obligated Group members, at least 85% of the consolidated net revenues of the Trinity Health Credit Group to grant to the master trustee security interests in their pledged property which security interests secure all obligations issued under the ARMI. There are several conditions and covenants required by the ARMI with which the Corporation must comply, including covenants that require the Corporation to maintain a minimum historical debt-service coverage and limitations on liens or security interests in property, except for certain permitted encumbrances, affecting the property of the Corporation or any material designated affiliate (a designated affiliate whose total revenues for the most recent fiscal year exceed 5% of the combined total revenues of the Corporation for the most recent fiscal year). Long-term debt outstanding as of September 30, 2016 and June 30, 2016 that has not been secured under the ARMI is generally collateralized by certain property and equipment.

Mercy Health System of Chicago ("MHSC") has a \$59.9 million mortgage loan outstanding at September 30, 2016 that is insured by the U.S. Department of Housing and Urban Development ("HUD"). MHSC's payment obligations under the two mortgage notes evidencing this loan are guaranteed by the Corporation. The mortgage loan agreements with HUD contain various covenants, including those relating to limitations on incurring additional debt, transactions with affiliates, transferring or disposing of designated property, use of funds and other assets of the mortgaged property, financial performance, required reserves, insurance coverage, timely submission of specified financial reports, and restrictions on prepayment of the mortgage loan. MHSC and the Corporation provided covenants to HUD not to interfere in the performance of MHSC's obligations under the HUD-insured loan documents. MHSC is not a Designated Affiliate and is not part of the Trinity Health Credit Group.

Commercial Paper – The Corporation's commercial paper program is authorized for borrowings up to \$600 million. As of September 30, 2016 and June 30, 2016, the total amount of commercial paper outstanding was \$161 million and \$146 million, respectively. Proceeds from this program are to be used for general purposes of the Corporation. The notes are payable from the proceeds of subsequently issued notes and from other funds available to the Corporation, including funds derived from the liquidation of securities held by the Corporation in its investment portfolio.

Liquidity Facilities – The Corporation has entered into four credit agreements (collectively, the "Credit Agreements") with US Bank National Association, which acts as an administrative agent for a group of lenders thereunder. The Credit Agreements establish a revolving credit facility for the Corporation, under which that group of lenders agree to lend to the Corporation amounts that may fluctuate from time to time and totaled \$931 million as of September 30, 2016. In September 2016, the Corporation amended and restated the credit agreements previously expiring in July 2017 and extended those facilities to July 2020. Amounts drawn under the Credit Agreements can only be used to support the Corporation's obligation to pay the purchase price of bonds that are subject to tender and that have not been successfully remarketed and the maturing principal of and interest on commercial paper notes. Of the \$931 million available balance, \$321 million expires in July 2018, \$285 million expires in July 2019 and \$325 expires in July 2020. The Credit Agreements are secured by obligations under the ARMI. As of September 30, 2016 and June 30, 2016, there were no amounts outstanding on these credit agreements. In addition, in July 2015, the Corporation renewed a three year general purpose credit facility of \$200 million. As of September 30, 2016 and June 30, 2016, there were no amounts outstanding under this credit facility.

Transactions

The acquisitions of SJHHC and SFC, as described in Note 3, resulted in the assumption of debt of \$342.2 million and \$251.5 million, respectively. The majority of this debt was retired or defeased using proceeds from the issuance of \$372 million of commercial paper and a \$190 million draw on a general purpose credit facility, both of which were later replenished with proceeds from the issuance of long-term debt in January and February 2016 as described below. In addition, the acquisition of Johnson, as described in Note 3, resulted in the assumption of debt of \$23.3 million the majority of which was subsequently redeemed.

As the result of the divestiture of Port Huron on September 1, 2015, the Corporation defeased approximately \$31.9 million of bonds through the funding of various escrow accounts on November 5, 2015. In addition, the Corporation redeemed approximately \$12.2 million of bonds on November 25, 2015.

On November 24, 2015, the Corporation issued \$55.0 million of commercial paper that was used to redeem \$53.3 million in outstanding revenue bonds. On January 15, 2016, the Corporation issued \$63 million of commercial paper to finance the construction, acquisition and equipping of capital improvements.

During January 2016, the Trinity Health Credit Group issued \$555.6 million par value in tax-exempt fixed-rate hospital revenue bonds at a premium of \$76.7 million under the ARMI. During February 2016, the Trinity Health Credit Group issued \$263.8 million par value in tax-exempt variable-rate private placement bonds and \$54.7 million par value in taxable variable-rate private placement bonds. Proceeds from these issuances were used to retire \$600 million of then-outstanding taxable commercial paper obligations, pay down \$152.1 million of the then-outstanding line of credit draw, extinguish the remaining \$43.9 million of debt assumed with the acquisition of SJHHC and pay related transaction costs and to defease \$25.5 million of tax-exempt bonds. The remaining proceeds will be used to finance, refinance and reimburse a portion of the costs of acquisition, construction, renovation and equipping of health facilities, and to pay related costs of issuance.

In February 2016, the Corporation issued \$100 million of commercial paper for general corporate purposes and \$21 million to pay down the remaining outstanding line of credit draw.

As the result of the divestiture of Mercy Suburban described in Note 3, the Corporation defeased approximately \$25 million of bonds through the funding of various escrow accounts on April 27, 2016.

In October 2016, the Corporation remarketed \$50 million in tax-exempt, variable rate hospital revenue bonds (the "Series 2011B bonds") under the ARMI, pursuant to a continuing covenant agreement with a private purchaser which provides for a ten year mandatory tender period (subject to mandatory tender on October 1, 2026).

6. PROFESSIONAL AND GENERAL LIABILITY PROGRAMS

The Corporation operates a wholly owned insurance company, Trinity Assurance, Ltd ("TAL"). Effective July 1, 2015, TAL's name was changed from Venzke Insurance Company, Ltd. TAL qualifies as a captive insurance company and provides certain insurance coverage to the Corporation's Health Ministries under a centralized program. The Corporation is self-insured for certain levels of general and professional liability, workers' compensation and certain other claims. The Corporation has limited its liability by purchasing reinsurance and commercial coverage from unrelated third-party commercial insurers.

Effective October 1, 2015, TAL policies include the facilities and individuals that were previously insured with Saint Francis Indemnity Company, LLC ("SFICL"), a captive insurance company domiciled in the State of Vermont, whose sole member is SFHMC. Policies issued and reinsurance purchased by SFICL prior to October 1, 2015 will remain in effect. SFICL did not, nor does it intend to, write or renew any insurance business after September 30, 2015. SFICL was merged into TAL on May 1, 2016 at which time all losses previous to October 1, 2015 for SFICL were assumed by TAL.

Effective August 1, 2016, TAL policies include the facilities and individuals that were previously insured with Saint Mary's Indemnity Company, LLC ("SMICL"), a captive insurance company domiciled in the State of Vermont, whose sole member is SMHS. Policies issued and reinsurance purchased by SMICL prior to August 1, 2016 will remain in effect. SMICL did not, nor does it intend to, write or renew any insurance business after July 31, 2016 but will effectively run-off its existing business. Management intends to fully merge SMICL into TAL by March 1, 2017 at which time all losses previous to August 1, 2016 for SMICL will be assumed by TAL.

The Corporation's current self-insurance program includes \$20 million per occurrence for the primary layers of professional and general liability, as well as \$10 million per occurrence for hospital government liability, \$5 million per occurrence for miscellaneous errors and omissions liability, and \$1 million per occurrence for

management liability (directors' and officers' and employment practices), network security and privacy liability and certain other coverages. In addition, through TAL and its various commercial reinsurers, the Corporation maintains integrated excess liability coverage with separate annual limits of \$100 million for professional/general liability, and management liability, network security and privacy liability. The Corporation self-insures \$750,000 per occurrence for workers' compensation in most states, with commercial insurance providing coverage up to the statutory limits, and self-insures up to \$500,000 in property values per occurrence with commercial insurance providing coverage up to \$1 billion.

The liability for self-insurance reserves represents estimates of the ultimate net cost of all losses and loss adjustment expenses, which are incurred but unpaid at the consolidated balance sheet date. The reserves are based on the loss and loss adjustment expense factors inherent in the Corporation's premium structure. Independent consulting actuaries determined these factors from estimates of the Corporation's expenses and available industry-wide data. The Corporation discounts the reserves to their present value using a discount rate of 3%. The reserves include estimates of future trends in claim severity and frequency. Although considerable variability is inherent in such estimates, management believes that the liability for unpaid claims and related adjustment expenses is adequate based on the loss experience of the Corporation. The estimates are continually reviewed and adjusted as necessary. The changes to the estimated self-insurance reserves were determined based upon the annual independent actuarial analyses.

Claims in excess of certain insurance coverage and the recorded self-insurance liability have been asserted against the Corporation by various claimants. The claims are in various stages of processing and some may ultimately be brought to trial. There are known incidents occurring through September 30, 2016, that may result in the assertion of additional claims and other claims may be asserted arising from services provided in the past. While it is possible that settlement of asserted claims and claims which may be asserted in the future could result in liabilities in excess of amounts for which the Corporation has provided, management, based upon the advice of the legal counsel, believes that the excess liability, if any, should not materially affect the consolidated financial position, operations, or cash flows of the Corporation.

7. PENSION AND OTHER BENEFIT PLANS

Deferred Compensation – The Corporation has nonqualified deferred compensation plans at certain Health Ministries that permit eligible employees to defer a portion of their compensation. The deferred amounts are distributable in cash after retirement or termination of employment. As of September 30, 2016 and June 30, 2016, the assets under these plans totaled \$184.7 million and \$171.3 million and liabilities totaled \$200.0 million and \$183.7 million, respectively, which are included in self-insurance, benefit plans and other assets and other long-term liabilities in the consolidated balance sheets.

Defined Contribution Benefits – The Corporation sponsors defined contribution pension plans covering substantially all of its employees. These programs are funded by employee voluntary contributions, subject to legal limitations. Effective January 1, 2015, employer contributions to these plans include nonelective contributions of 3% of eligible compensation, and varying levels of matching contributions based on employee service. The employees direct their voluntary contributions and employer contributions among a variety of investment options. Contribution expense under the plans totaled \$81.3 million and \$69.7 million for the three month periods ended September 30, 2016 and 2015, respectively.

Noncontributory Defined Benefit Pension Plans ("Pension Plans") – The Corporation maintains qualified, noncontributory defined benefit pension plans under which benefit accruals are frozen for the majority of employees. Certain nonqualified, supplemental plan arrangements also provide retirement benefits to specified groups of participants.

Certain plans are subject to the provisions of the Employee Retirement Security Act of 1974 ("ERISA"). The majority of the plans sponsored by the Corporation are intended to be "Church Plans", as defined in Code Section 414(e) and Section 3(33) of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), which have not made an election under Section 410(d) of the Code to be subject to ERISA. Effective June 2014, the Trinity Health Pension Plan was amended to freeze all future benefit accruals as of

December 31, 2014. The Corporation's adopted funding policy for the majority of its qualified church plans, which is reviewed annually, is to fund the current normal cost or service cost based on the accumulated benefit obligations and amortization of any under or over funding. The remaining church plan has historically funded amounts equal to annual pension expense.

Postretirement Health Care and Life Insurance Benefits ("Postretirement Plans") – The Corporation sponsors both funded and unfunded contributory plans to provide health care benefits to certain of its retirees. All of the Postretirement Plans are closed to new participants. The Postretirement Plans cover certain hourly and salaried employees who retire from certain Health Ministries. Medical benefits for these retirees are subject to deductibles and copayment provisions. Effective January 1, 2011, the funded plans provide benefits to certain retirees at fixed dollar amounts in health reimbursement account arrangements for Medicare eligible participants.

Plan Acquisitions – As discussed in Note 3, the Corporation acquired SJHHC on July 1, 2015, SFC on October 1, 2015, and SMHS on August 1, 2016, including all related benefit plans. SJHHC maintains one qualified, noncontributory defined benefit pension plan that provides retirement benefits for substantially all full-time employees. Benefit accruals were frozen and the plan was closed to new participants in April 2014. The plan is subject to the provisions of ERISA. In addition, SJHHC provides other postretirement benefits (primarily health benefits) to an eligible group of employees. The postretirement plan was closed to new participants in 2000, and is unfunded. SFC maintains two qualified, noncontributory defined benefit plans that provide benefits for substantially all full-time employees. One of the plans is subject to ERISA, and the other is intended to be a "Church Plan.". Both plans were frozen and closed to new participants in September 2006. SFC also provides other postretirement benefits, primarily health benefits, to an eligible group of employees. The postretirement plan is closed to new participants. SMHS maintains one qualified, noncontributory defined benefit pension plan that is intended to be a "Church Plan." . The plan was frozen to new entrants in 1997 and curtailed to eliminate future benefit accruals in 2004.

Components of net periodic benefit cost (income) for the three month periods ended September 30 consisted of the following (in thousands):

	Pension Plans		Postretirement Plans	
	2016	2015	2016	2015
Service cost	\$ 397	\$ 514	\$ 71	\$ 105
Interest cost	77,810	79,691	1,380	1,473
Expected return on assets	(102,024)	(97,532)	(1,770)	(1,763)
Amortization of prior service cost	(2,265)	(1,142)	(141)	(141)
Recognized net actuarial loss	21,803	10,697	(2)	(40)
Net periodic benefit cost (income)	<u>\$ (4,279)</u>	<u>\$ (7,772)</u>	<u>\$ (462)</u>	<u>\$ (366)</u>

8. CONTINGENCIES

The Corporation, as successor to Catholic Health East ("CHE"), is the defendant in a purported class action lawsuit in New York state court brought by Emmet & Co., Inc., and First Manhattan Co., with respect to one series of certificates (the "Bonds") issued for the benefit of a hospital acquired by CHE. The Bonds were defeased in 1998 at the time of CHE's acquisition of the hospital. The Corporation does not currently control the hospital. Plaintiffs alleged that CHE breached the indenture relating to the Bonds and violated the covenant of good faith and fair dealing in the exercise of its optional redemption rights for the Bonds in connection with the CHE's tender offer for the Bonds. The Corporation has reached an agreement of settlement with the named plaintiffs only which has received judicial approval. The litigation has been resolved in all respects. The settlement did not have a material effect on the financial condition of the Corporation.

In June 2013, the Corporation received notices from the IRS that each of the three series initially at issue in the Emmet & Co., Inc. case was under separate examination and requested certain information. Closing agreements with respect to all of the bond issues have been fully executed and implemented and the IRS examination of each

of those bond issues is closed. The resolution of these matters did not have a material adverse effect on the financial condition of the Corporation.

On March 29, 2013, CHE was notified that it is a defendant in a lawsuit filed in the United States District Court for the Eastern District of Pennsylvania that challenges the church plan status of the CHE Employee Pension Plan. This is similar to other purported class action cases that have been brought against religiously affiliated health care systems or providers. On July 17, 2014, Trinity Health Corporation was notified that it is a defendant in a lawsuit filed in the United States District Court for the District of Maryland that challenges the church plan status of the Trinity Health Pension Plan. In response thereto, the Corporation filed a partial motion to dismiss the complaint, which was granted on February 23, 2015. In August 2015, the parties commenced a mediation process to explore opportunities for the settlement of both cases. A final settlement agreement covering both litigations was executed on April 26, 2016. A motion for preliminary approval of the settlement remains pending before the Court. Final approval remains subject to class notification and further judicial approval. The terms of the final settlement, if approved, will not have a material adverse effect on the financial condition of the Corporation.

On July 21, 2015, Saint Francis Hospital and Medical Center in Hartford, Connecticut, was notified that it was a defendant in a similar class action lawsuit filed in the United States Court for the District of Connecticut challenging the church plan status of its employee pension plan. Saint Francis Hospital and Medical Center became a subsidiary of the Corporation effective October 1, 2015. Although a motion to dismiss the complaint was filed, a mediation process has resulted in a settlement term sheet being executed on February 18, 2016. A final settlement agreement has been executed. The settlement agreement received judicial approval and the matter concluded as of December 3, 2016. The terms of the final settlement will not have a material adverse effect on the financial condition of the Corporation.

During the twelve months ended June 30, 2016, the Corporation recorded a \$65.3 million liability for the estimated impact of identified data submission errors, ranging over a six year period, related to Medigold, the Corporation's Medicare Advantage plans in Ohio. The impact of these errors was determined to not be material to any of the prior period financial statements. The Corporation currently is working to resolve this matter through the submission of corrected data to the Centers for Medicare and Medicaid Services.

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

Health Care Regulatory Environment – The health care industry is subject to numerous and complex laws and regulations of federal, state and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, privacy, government health care program participation requirements and government reimbursement for patient services, fraud and abuse, and requirements for tax exemption for tax-exempt organizations. Compliance with such laws and regulations is complex and can be subject to future government interpretation as well as regulatory enforcement actions, including fines, penalties and exclusion from government health care programs such as Medicare and Medicaid. The Corporation and its Health Ministries periodically receive notices from governmental agencies requesting information regarding billing, payment or other reimbursement matters or notices of the initiation of government investigations. The health care industry in general is experiencing an increase in these activities as federal and state governments increase their enforcement activities and institute new programs designed to identify potential irregularities in reimbursement or quality of patient care. Based on the information received to date, management does not believe the ultimate resolution of these matters will have a material adverse effect on the Corporation's future consolidated financial position or results of operations.

9. SUBSEQUENT EVENTS

Management has evaluated subsequent events through December 13, 2016, the date the quarterly report was issued. No subsequent events were noted.

Discussion and Analysis of Financial Condition and Results of Operations for Trinity Health

September 30, 2016



Introduction to Management's Discussion & Analysis

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

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

or reliability any interim or ultimate effects of the legislation.

Trinity Health Corporation, an Indiana nonprofit corporation headquartered in Livonia, Michigan, and its subsidiaries ("Trinity Health" or the "Corporation"), , controls one of the largest health care systems in the United States.

Recent Developments

Saint Mary's Health System

On August 1, 2016, the Corporation became, through its Trinity Health-New England subsidiary, the sole corporate member of Saint Mary's Health System ("SMHS"), a regional health care system located in Waterbury, Connecticut, as part of a member substitution. As a result of this transaction, the Corporation recognized an inherent contribution of \$54.5 million for the three months ended September 30, 2016 in the consolidated statement of operations and changes in net assets. The Corporation is still in the process of assessing the economic characteristics of certain assets acquired and liabilities assumed. The Corporation expects to substantially complete this assessment within 12 months following the acquisition date and may adjust the amounts recorded as of August 1, 2016 to reflect revised evaluations. For the two month period ended September 30, 2016, SMHS reported revenue of \$51.6 million and deficiency of revenue over expenses of \$0.1 million in the consolidated statements of operations.

Mercy Health Network

The Corporation has a 50% interest in Mercy Health Network ("MHN"), a nonstock basis membership corporation with Catholic Health Initiatives ("CHI") holding the remaining 50% interest. Effective March 1, 2016, the Corporation and CHI amended and restated their existing MHN Joint Operating Agreement ("JOA") that governs certain of their respective legacy operations in Iowa to strengthen MHN's management responsibilities over the Iowa Operations, to jointly acquire health care operations in Iowa and contiguous markets; and to provide for greater financial, governance, and clinical integration. The JOA provides for the Corporation and CHI to maintain ownership of their respective assets in Iowa while agreeing to operate

the corporations Iowa hospitals in collaboration with CHI's Mercy Hospital Medical Center, Des Moines, Iowa, as one organization with common governance and management. MHN has developed a regional healthcare network that provides for a collaborative effort in the areas of community healthcare development, enhanced access to health services for the poor and sharing of other common goals. Under the JOA, the Corporation and CHI equally share adjusted operating cash flow from Iowa operations.

On May 1, 2016, MHN became the sole member of Wheaton Franciscan Services, Inc. ("WFSI"). WFSI operates three hospitals in Iowa located in Waterloo (Covenant Medical Center), Cedar Falls (Sartori Memorial Hospital) and Oelwein (Mercy Hospital of Franciscan Sisters). WFSI is consolidated in MHN's financial statements. As a result of this transaction, MHN recognized an inherent contribution in their consolidated statement of operations and changes in net assets in subsequent periods of fiscal year 2016, of which, the Corporation's share was \$87.2 million. As of September 30, 2016, the Corporation's investment in MHN totaled \$91.5 million.

St. Francis Care

Effective October 1, 2015, the Corporation became the sole corporate member of Saint Francis Care and subsidiaries ("SFC"), a Connecticut nonstock corporation. On November 17, 2015, Saint Francis Care, Inc. changed its name to Trinity Health-New England, Inc. SFC is the sole member of Saint Francis Hospital and Medical Center, a Connecticut nonstock corporation that operates a hospital in Hartford, Connecticut and is also the sole member of Mount Sinai Rehabilitation Hospital, a Connecticut nonstock corporation that operates a rehabilitation facility. As a result of this transaction, the Corporation recognized an inherent contribution of \$70.9 million in the consolidated statement of operations and changes in net assets in subsequent periods of fiscal year 2016.

Furthermore, on January 1, 2016, SFC acquired the assets of Johnson Memorial Medical Center, Inc. ("Johnson"), a non-profit, nonstock holding company located in Stafford Springs, Connecticut. Johnson, through its subsidiaries,

provides health care services throughout the Hartford and Tolland Connecticut counties. As a result of this acquisition, the Corporation recognized an inherent contribution of \$4.0 million in the consolidated statement of operations and changes in net assets in subsequent periods of fiscal year 2016. SFC, inclusive of Johnson, has been consolidated in the fiscal year 2016 financial statements as of the acquisition dates. For the three month period ended September 30, 2016, SFC reported revenue of \$232.0 million and excess of revenue over expenses of \$56.1 million in the consolidated statements of operations. SFC, Johnson and SMHS are collectively referred to as "Connecticut".

St. Joseph's Hospital Health Center

On July 1, 2015, the Corporation became the sole corporate member of Saint Joseph's Hospital Health Center ("SJHHC"), a regional health care system located in Syracuse, New York as part of a member substitution. As a result of this transaction, the Corporation recognized an inherent contribution of \$99.7 million for the three months ended September 30, 2015 in the consolidated statement of operations and changes in net assets. The amount of the inherent contribution was adjusted in subsequent periods of fiscal year 2016, resulting in an inherent contribution of \$58.3 million for the fiscal year ended June 30, 2016. SJHHC has been consolidated in the fiscal year 2016 financial statements. For the three month period ended September 30, 2016 and 2015, SJHHC reported revenue of \$165.6 million and \$162.9 million, respectively, and deficiency of revenue over expenses of \$1.6 million and \$8.9 million in the consolidated statements of operations, respectively.

Results from Operations

Operating Income

Operating income for the first three months of fiscal year 2017 was \$43.3 million compared to \$48.3 million for the same period in fiscal year 2016. The Connecticut acquisitions unfavorably impacted operating income with a combined operating loss of \$2.1 million reported for fiscal year 2017. Operating margin and operating cash flow margin were 1.0% and 7.3%, respectively, for the first three months of fiscal year 2017 compared to 1.3% and 7.8% for the same period in fiscal year 2016.

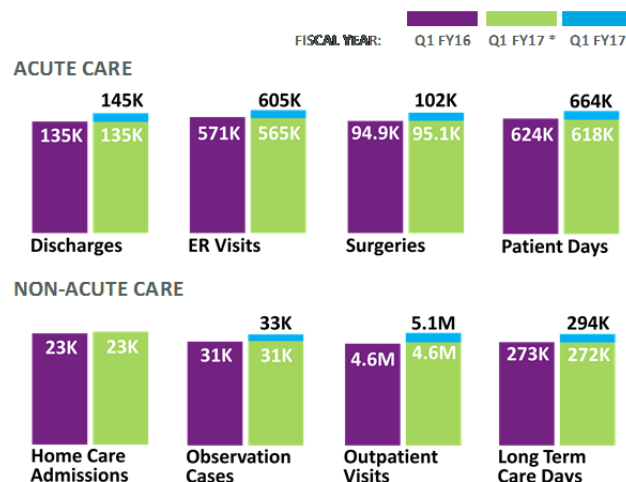
Excluding the impact of the Connecticut acquisitions, fiscal year 2017 operating margin and operating cash flow margin were 1.1% and 7.4%, respectively. Pressure on margins continues from increased costs for labor (including contract labor), purchased services, supplies, and increasing claims in the Ohio Medicare Advantage health plans with a continued unfavorable shift in payor mix and continued stress on payment rates. These items were partially offset by case mix improvements, volume growth and favorable shifts in service mix.

(dollars in millions)	Q1 FY16	Q1 FY17	Q1 FY17 *
Operating Income	\$48.3	\$43.3	\$45.4
Operating Revenue	\$3,795	\$4,284	\$3,985
Operating Margin	1.3%	1.0%	1.1%
Operating Cash Flow Margin	7.8%	7.3%	7.4%

* Excluding the impact of acquisitions of SFC in FY16 and SMHS in FY17

Revenue

Total unrestricted revenue of \$4.3 billion increased \$489 million, or 12.9%, for the first three months of fiscal year 2017 compared to the same period in fiscal year 2016. Revenue from the Connecticut acquisitions accounted for \$299 million of the increase or 7.9%. Excluding the impact of the aforementioned acquisitions, the increase was due primarily to the following: (i) an increase of \$73.6 million in other revenue, (ii) an increase of \$48.4 million from improvements in case mix, and (iii) \$34.5 million from volume growth. These increases were partially tempered by a continued unfavorable shift in payor mix, and to a lesser extent payment rates. Same facility volumes were favorable to prior year with 15 of the 20 Regional Health Ministries experiencing increases in case mix adjusted equivalent discharges.



* Excluding the impact of acquisitions of SFC in FY16 and SMHS in FY17

Expenses

Total operating expenses of \$4.2 billion increased \$494 million, or 13.2% for the first three months of fiscal year 2017 compared to the same period in fiscal year 2016. Expenses from the Connecticut acquisitions accounted for \$301 million of the increase or 8.0%. Excluding the impact of the aforementioned acquisitions, the change was due primarily to the following: (i) labor expense increase of \$82.5 million (salaries and wages increase of \$85.0 million primarily due to a 2.2% increase in rate and a 1.8% increase in FTEs driven by higher volumes), (ii) purchased services increase of \$45.8 million, (iii) supplies increase of \$25.7 million driven by higher volumes and (iv) medical claims increase of \$15.4 million due to increased membership as well as increasing claims experience at Medigold, the Corporation's Medicare Advantage plans in Ohio. Expenses for occupancy, interest, depreciation and amortization, and other did not materially change for the first three months of fiscal year 2017 compared to the same period in fiscal year 2016.

Nonoperating Items

The Corporation reported gains in nonoperating items of \$435.9 million for the first three months of fiscal year 2017 compared to losses of \$325.7 million for the same period in fiscal year 2016. The change was primarily due to a \$645.1 million improvement in nonoperating investment earnings, a \$121.3 million improvement in equity in earnings of unconsolidated affiliates, an

improvement in interest rate swaps of \$31.8 million (all primarily driven by overall global investment market conditions), partially offset by a decrease of \$36.6 million in other non-operating income of which a majority is related to differences in inherent contributions from acquisitions as described above.

Excess of Revenue over Expenses

Excess of revenue over expenses for the first three months of fiscal year 2017 was \$467.5 million compared to a deficiency of revenue over expense of \$287.2 million for the same period in fiscal year 2016. The change was primarily due to a \$761.6 million increase in nonoperating items compared to the same period in fiscal year 2016.

Balance Sheet

Total assets of \$24.0 billion increased \$571 million, or 2.4% as of September 30, 2016, compared to June 30, 2016, of which SMHS accounted for \$229 million or 1% of the increase. Excluding SMHS, asset growth was mainly driven by non-operating investment income of \$278 million. Total assets include unrestricted cash and investments of \$7.9 billion or 180 days of cash on hand. Days cash on hand decreased by five days during the year due primarily to the impact of the Connecticut acquisitions and increased expenses, capital expenditures, and balance sheet timing, partially offset with strong investment returns and positive operating cash flow. Net days in accounts receivable increased by 2.7 days to 46.2 days as of September 30, 2016 compared to fiscal year June 30, 2016. Total liabilities of \$13.2 billion increased \$30.5 million, or 0.2%, primarily due to the SMHS acquisition, which accounted for \$150.7 million of the increase, partially offset by decreased accounts payable, salaries and wages related liabilities and accrued pension and retiree health costs which included cash funding of \$62.3 million. Debt to capitalization as of September 30, 2016 decreased to a ratio of 39.2% from 40.3% compared to June 30, 2016 due primarily to an increase in unrestricted net assets of \$492.7 million driven by strong investment returns, other non-operating gains and income from operations.



Statement of Cash Flows

Cash and cash equivalents decreased \$70.1 million during the year. Operating activities provided \$61.0 million of cash. Investing activities used \$135.3 million of cash including \$241.7 million for purchases of property and equipment partially offset by \$101.6 million of net proceeds from the sale of investments. Financing activities provided \$4.1 million of cash due primarily to the proceeds from the issuance of debt of \$13.9 million and net change in commercial paper of \$14.9 million partially offset by repayments of debt of \$27.1 million.

TRINITY HEALTH**Liquidity Reporting**

Summary as of September 30, 2016

(\$ in millions)
(unaudited)**ASSETS****Daily Liquidity**

Money Market Funds (Moody's rated Aaa)	\$	618
Checking and Deposit Accounts (at P-1 rated bank)		-
Repurchase Agreements		-
U.S. Treasuries & Aaa-rated Agencies		1
Dedicated Bank Lines		931
Subtotal Daily Liquidity (Cash & Securities)	\$	<u>1,549</u>

Undrawn Portion of \$600M Taxable Commercial Paper Program		<u>439</u>
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Subtotal Daily Liquidity Including Taxable Commercial Paper Program \$ 1,988

Weekly Liquidity

Exchange Traded Equity	\$	1,366
Publicly Traded Fixed Income Securities Rated at least Aa3 and Bond Funds		1,195
Equity Funds		1,265
Other		551
Subtotal Weekly Liquidity		<u>4,377</u>

TOTAL DAILY AND WEEKLY LIQUIDITY \$ 6,365

Longer Term Liquidity

Funds, vehicles, investments that allow withdrawals with less than one month notice		1,468
Funds, vehicles, investments that allow withdrawals with one month notice or longer		1,825
Total Longer Term Liquidity		<u>\$ 3,293</u>

LIABILITIES (Self-liquidity Variable Rate Demand Bonds & Commercial Paper)**Weekly Put Bonds**

VRDO Bonds (7-day)	\$	340
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Long-Mode Put Bonds

VRDO Bonds (Commercial Paper Mode)		426
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<u>Taxable Commercial Paper Outstanding</u>		<u>161</u>
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TOTAL SELF-LIQUIDITY DEBT AND COMMERCIAL PAPER \$ 927

Trinity Health
Financial Ratios and Statistics (Unaudited)

	September 30, 2016	September 30, 2015
<u>Financial Indicators</u>		
Liquidity Ratios (at September 30)		
Days Cash on Hand	180	201
Days in Accounts Receivable, Net	46	47
Leverage Ratios (at September 30)		
Debt to Capitalization	39%	39%
Cash to Debt	122%	124%
Profitability Ratios (For the Three Months Ended September 30)		
Operating Margin	1.0%	1.3%
Operating Cash Flow Margin	7.3%	7.8%
<u>Statistical Indicators (For the Three Months Ended September 30)</u>		
Rounded to nearest thousand		
Discharges	145,000	135,000
Patient Days	664,000	624,000
Outpatient Visits	5,054,000	4,576,000
Emergency Room Visits	605,000	571,000
<u>Continuing Care</u>		
Home Health Admissions	23,000	23,000
Long-term Care Patient Days	294,000	273,000