



Continuing Disclosure

Quarterly Financial Report

Six Months Ended June 30, 2017

(Unaudited)

August 18, 2017

TEXAS HEALTH RESOURCES

SYSTEM REVENUE BONDS						
Series	Taxable or Tax-Exempt	Issuer	Bond Type	Final Maturity	Principal Amount	Interest Rate
2016A	Tax-Exempt	TCCEFFC ¹	Term	2/15/2047	\$ 631,105,000	Multiple
2015	Taxable	THR	Term	11/15/2055	\$ 300,000,000	4.330%
2015A	Tax-Exempt	TCCEFFC ¹	Term	11/15/2052	\$ 40,000,000	4.250%
2015A	Tax-Exempt	TCCEFFC ¹	Term	11/15/2052	\$ 20,000,000	5.000%
2012A	Taxable	TCCEFFC ¹	Term	11/15/2047	\$ 100,000,000	4.366%
2012B	Tax-Exempt	TCCEFFC ¹	VRDB ²	11/15/2047	\$ 50,000,000	Variable
2010	Tax-Exempt	TCCEFFC ¹	Term	11/15/2040	\$ 157,550,000	5.000%
2008A	Tax-Exempt	TCCEFFC ¹	VRDB ²	11/15/2033	\$ 65,000,000	Variable
2008B	Tax-Exempt	TCCEFFC ¹	VRDB ²	11/15/2033	\$ 50,285,000	Variable
2008C	Tax-Exempt	TCCEFFC ¹	VRDB ²	11/15/2033	\$ 60,770,000	Variable
2007B	Tax-Exempt	TCCEFFC ¹	Term	11/15/2047	\$ 100,000,000	5.000%
SYSTEM BANK LOANS						
Taxable or Tax-Exempt	Bank	Bond Type	Final Maturity	Principal Amount	Interest Rate	
Tax-Exempt	UMB ³	Variable	9/1/2035	\$ 67,025,000	Variable	
Tax-Exempt	Northern ⁴	Variable	12/1/2033	\$ 67,500,000	Variable	

¹ Tarrant County Cultural Education Facilities Finance Corporation

² Variable Rate Demand Bond

³ Kansas City Financial Corporation, an affiliate of UMB Bank, N.A.

⁴ The Northern Trust Company

**TEXAS HEALTH RESOURCES
SYSTEM REVENUE BONDS**

WARNING

This document is marked with a dated date and speaks only as of that dated date. Readers are cautioned not to assume that any information has been updated beyond the dated date except as to any portion of the document that expressly states that it constitutes an update concerning specific recent events occurring after the dated date of the document. Any information contained in the portion of the document indicated to concern recent events speaks only as of its date. Texas Health Resources ("THR") expressly disclaims any duty to provide an update of any information contained in this document. The information contained in this document may include "forward looking statements" by using forward-looking words such as "may," "will," "should," "expects," "believes," "anticipates," "estimates," or others. You are cautioned that forward-looking statements are subject to a variety of uncertainties that could cause actual results to differ from the projected results. Those risks and uncertainties include general economic and business conditions, receipt of funding grants, and various other factors which are beyond our control. Because we cannot predict all factors that may affect future decisions, actions, events, or financial circumstances, what actually happens may be different from what THR includes in forward-looking statements.

THR is obligated to provide certain updated financial information and operating data quarterly as specified in the Master Indenture. This document is designed to fulfill that obligation. It does not represent a complete set of financial statements as stipulated by U.S. generally accepted accounting principles.

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TEXAS HEALTH RESOURCES
QUARTERLY CONSOLIDATED CONDENSED FINANCIAL INFORMATION
(Dollars in Thousands)

	Mar 31	Jun 30	Sep 30	Dec 31	Total Year
Fiscal Year 2017					
(Unaudited)					
Net patient service revenue	\$ 1,068,424	\$ 1,084,769	\$ -	\$ -	\$ 2,153,193
Other operating revenue	43,329	62,161	-	-	105,490
Total operating revenue	1,111,753	1,146,930	-	-	2,258,683
Operating expenses	1,051,180	1,083,867	-	-	2,135,047
Operating income	60,573	63,063	-	-	123,636
Nonoperating gains, net	187,220	150,710	-	-	337,930
Revenue and gains in excess of expenses and losses before income taxes	247,793	213,773	-	-	461,566
Less: Income tax expense	1,495	1,219	-	-	2,714
Revenue and gains in excess of expenses and losses	246,298	212,554	-	-	458,852
Less: Revenue and gains in excess of expenses and losses attributable to non-controlling interest	16,140	21,063	-	-	37,203
Revenue and gains in excess of expenses and losses from continuing operations attributable to THR	<u>\$ 230,158</u>	<u>\$ 191,491</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 421,649</u>
Fiscal Year 2016					
(Unaudited)					
Net patient service revenue	\$ 1,056,777	\$ 1,039,701	\$ 1,050,894	\$ 1,153,175	\$ 4,300,547
Other operating revenue	43,806	55,105	47,007	75,544	221,462
Total operating revenue	1,100,583	1,094,806	1,097,901	1,228,719	4,522,009
Operating expenses	1,001,316	1,034,103	1,050,721	1,096,799	4,182,939
Operating income	99,267	60,703	47,180	131,920	339,070
Nonoperating gains, net	16,855	75,640	153,617	23,627	269,739
Revenue and gains in excess of expenses and losses before income taxes	116,122	136,343	200,797	155,547	608,809
Less: Income tax expense	1,128	1,218	914	346	3,606
Revenue and gains in excess of expenses and losses	114,994	135,125	199,883	155,201	605,203
Less: Revenue and gains in excess of expenses and losses attributable to non-controlling interest	16,510	18,192	21,727	26,855	83,284
Revenue and gains in excess of expenses and losses from continuing operations attributable to THR	<u>\$ 98,484</u>	<u>\$ 116,933</u>	<u>\$ 178,156</u>	<u>\$ 128,346</u>	<u>\$ 521,919</u>

TEXAS HEALTH RESOURCES
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands)

	June 30, 2017	December 31, 2016
	(Unaudited)	(Audited)
Assets		
Current Assets:		
Cash and cash equivalents	\$ 385,427	\$ 501,826
Short-term investments	7,250	6,250
Receivables -		
Patient, net	466,325	495,667
Other, net	60,249	62,925
Assets limited as to use	309,051	353,161
Other current assets	152,578	147,614
Total current assets	<u>1,380,880</u>	<u>1,567,443</u>
Assets Limited as to Use	4,366,138	3,945,898
Property and Equipment, net	1,994,369	2,007,745
Investments in Unconsolidated Affiliates	354,853	224,500
Goodwill and Intangible Assets, net	150,971	153,816
Other Assets, net	<u>85,360</u>	<u>85,302</u>
Total assets	<u><u>\$ 8,332,571</u></u>	<u><u>\$ 7,984,704</u></u>
Liabilities and Net Assets		
Current Liabilities:		
Current portion of long-term debt	\$ 245,936	\$ 268,628
Accounts payable	195,052	262,885
Estimated third-party payor settlements	35,359	29,971
Accrued salaries, wages, and employee benefits	214,366	231,387
Other accrued liabilities	190,261	160,655
Total current liabilities	<u>880,974</u>	<u>953,526</u>
Long-Term Debt, net of current portion	1,710,878	1,719,571
Other Noncurrent Liabilities	<u>51,140</u>	<u>46,092</u>
Total liabilities	<u>2,642,992</u>	<u>2,719,189</u>
Net Assets:		
Net assets of THR:		
Unrestricted	5,412,566	4,993,413
Temporarily restricted	98,483	91,762
Permanently restricted	70,345	69,643
Total net assets of THR	<u>5,581,394</u>	<u>5,154,818</u>
Noncontrolling ownership interest in equity of consolidated affiliates - unrestricted	<u>108,185</u>	<u>110,697</u>
Total net assets	<u>5,689,579</u>	<u>5,265,515</u>
Total liabilities and net assets	<u><u>\$ 8,332,571</u></u>	<u><u>\$ 7,984,704</u></u>

TEXAS HEALTH RESOURCES
CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS
(Dollars in Thousands)

	Six Months Ended June 30,	
	2017	2016
	(Unaudited)	(Unaudited)
Operating Revenue:		
Net patient service revenue before provision for bad debts	\$ 2,335,674	\$ 2,232,829
Less: Provision for bad debts	182,481	136,351
Net patient service revenue	2,153,193	2,096,478
Equity in earnings of unconsolidated affiliates	22,470	31,039
Other operating revenue	83,020	67,872
Total operating revenue	2,258,683	2,195,389
Operating Expenses:		
Salaries, wages, and employee benefits	1,175,130	1,117,232
Supplies	375,833	345,535
Other operating expenses	424,574	421,991
Depreciation and amortization	114,942	110,098
Interest expense	44,568	40,563
Total operating expenses	2,135,047	2,035,419
Operating Income	123,636	159,970
Nonoperating Gains (Losses), Net:		
Net realized investment income and gains	106,326	34,164
Net unrealized gains on investments	219,788	58,900
Equity in earning (losses) of unconsolidated affiliates, nonoperating	84	(739)
Settlement of interest rate swap agreement	-	(1,031)
Loss on extinguishment of long-term debt	-	(28)
Other, net	11,732	1,229
Total nonoperating gains, net	337,930	92,495
Revenue and Gains In Excess of Expenses and Losses before Income Taxes	461,566	252,465
Less: Income Tax Expense	2,714	2,346
Revenue and Gains In Excess of Expenses and Losses	458,852	250,119
Less: Revenue and Gains in Excess of Expenses and Losses Attributable to Non-Controlling Interest	37,203	34,702
Revenue and Gains In Excess of Expenses and Losses from Continuing Operations Attributable to THR	421,649	215,417

(Continued)

TEXAS HEALTH RESOURCES
CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS, Continued
(Dollars in Thousands)

	Six Months Ended June 30,	
	2017	2016
	(Unaudited)	(Unaudited)
Other Changes in Unrestricted Net Assets:		
Net unrealized gains (losses) on investments, other than trading securities	\$ (1,500)	\$ 6,159
Net assets released from restrictions used for purchase of property and equipment	505	4,371
Change in fair value of interest rate swap agreements	(12)	396
Other changes, net	(1,489)	(45)
Increase in Unrestricted Net Assets	419,153	226,298
Changes in Temporarily Restricted Net Assets:		
Contributions received for purchase of property and equipment	424	105
Contributions received for operations	4,093	10,281
Net realized investment income and gains	2,146	553
Net unrealized gains on investments	4,670	1,288
Change in value of split-interest agreements	130	120
Net assets released from restrictions	(4,742)	(8,636)
Increase in Temporarily Restricted Net Assets	6,721	3,711
Changes in Permanently Restricted Net Assets:		
Contributions	281	243
Unrealized investment gains (losses) on beneficial interest in perpetual trust, net	421	(64)
Change in value of split-interest agreements	-	58
Increase in Permanently Restricted Net Assets	702	237
Increase in Net Assets of THR	\$ 426,576	\$ 230,246

TEXAS HEALTH RESOURCES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Thousands)

	Six Months Ended June 30,	
	2017	2016
	(Unaudited)	(Unaudited)
Cash Flows From Operating Activities:		
Increase in net assets of THR	\$ 426,576	\$ 230,246
Adjustments to reconcile increase in net assets to net cash provided by operating activities -		
Loss on extinguishment of long-term debt	-	28
Settlement of interest rate swap agreement	-	1,031
Net unrealized gains on investments	(223,379)	(66,283)
Net realized gains on investments	(73,417)	(4,603)
Change in value of split-interest agreements	(130)	(178)
Provision for bad debts	186,656	136,881
Restricted contributions received for purchase of property and equipment	(424)	(105)
Depreciation and amortization	114,942	110,098
Amortization of bond premiums/discounts and debt issuance costs	(1,282)	(386)
Net gain on impairment and disposal of property and equipment	(9,553)	(41)
Equity in earnings of unconsolidated affiliates	(22,470)	(31,039)
Distributions from unconsolidated affiliates	23,104	20,895
Equity in (earnings) losses of unconsolidated affiliates, nonoperating	(84)	739
Change in fair value of interest rate swap agreements	12	(396)
Revenue and gains in excess of expenses and losses attributable to non-controlling interest	37,203	34,702
(Increase) decrease in:		
Receivables, patient, net	(153,139)	(153,092)
Receivables, other, net	(1,499)	37,134
Goodwill & intangible assets, net	(10)	(417)
Other assets, net	(5,000)	(17,268)
Increase (decrease) in:		
Accounts payable and accrued liabilities	(49,860)	69,004
Other noncurrent liabilities	5,027	(5,829)
Net cash provided by operating activities	<u>253,273</u>	<u>361,121</u>
Cash Flows From Investing Activities:		
Purchases of property and equipment, net	(126,805)	(268,943)
Proceeds from disposal of property and equipment	38,092	3,342
Cash used to acquire physician practices and other consolidated affiliates	(467)	(1,256)
Investment in unconsolidated affiliates, net	(130,903)	(7,795)
Purchases of short-term investments and assets limited as to use, net	(80,204)	(9,899)
Net cash used in investing activities	<u>(300,287)</u>	<u>(284,551)</u>

(Continued)

TEXAS HEALTH RESOURCES
CONSOLIDATED STATEMENTS OF CASH FLOWS, Continued
(Dollars in Thousands)

	Six Months Ended June 30,	
	2017	2016
	(Unaudited)	(Unaudited)
Cash Flows From Financing Activities:		
Proceeds from issuance of long-term debt	\$ 2,535	\$ 40,241
Debt issuance costs	-	(109)
Principal payments on capital lease obligations	(78)	(426)
Principal payments on long-term debt	(32,560)	(30,823)
Redemption of long term debt	-	(35,214)
Settlement of interest rate swap agreement	-	(1,031)
Contributions from non-controlling interest holders	1,075	1,414
Distributions to non-controlling interest holders	(40,781)	(38,413)
Proceeds from restricted contributions received for purchase of property and equipment	424	105
	<u>(69,385)</u>	<u>(64,256)</u>
Net cash used in financing activities	(69,385)	(64,256)
Net Increase (Decrease) in Cash and Cash Equivalents	(116,399)	12,314
Cash and Cash Equivalents, beginning of year	501,826	463,079
Cash and Cash Equivalents, current	<u>\$ 385,427</u>	<u>\$ 475,393</u>
Supplemental Disclosure of Cash Flow Information:		
Cash paid for interest	<u>\$ 34,142</u>	<u>\$ 38,310</u>
Supplemental Schedule of Noncash Financing Activities:		
Property and equipment acquired through capital lease obligations	<u>\$ -</u>	<u>\$ 174</u>

**TEXAS HEALTH RESOURCES
OPERATING AND FINANCIAL DATA
UTILIZATION OF SYSTEM FACILITIES**

Statistic	Six Months Ended June 30,	
	2017	2016
Licensed Beds (at month-end)	3,991	3,866
Operated Beds in Service (at month-end)	3,369	3,185
Patient Days (inpatient)	385,009	383,677
Discharges (inpatient)	82,794	82,950
Average Length of Stay (days)	4.7	4.6
Average Daily Census ¹	2,127	2,108
Percent Occupancy	63.1%	66.2%
Outpatient Visits ²	775,447	768,745
Total Surgeries	50,853	49,873
Emergency Room Visits	361,571	365,919
Outpatient Gross Patient Service Revenue to Total Gross Patient Service Revenue ³	43.6%	42.7%

¹ Average Daily Census is calculated using 181 days for the six months ended June 30, 2017 and 182 days for the six months ended June 30, 2016.

² Includes hospital based outpatient clinic visits and other outpatient facilities' visits. Excludes physician office visits.

³ Excludes physician activities, which represent 9.5% and 9.3% of THR's consolidated net patient service revenue for the six months ended June 30, 2017 and 2016, respectively.

**SOURCES OF COMBINED GROSS PATIENT SERVICE REVENUES
(Excludes Physician Activities)**

Payer Type	Six Months Ended June 30, 2017	Fiscal Years Ended December 31,	
		2016	2015
Managed Care	37.6%	38.7%	39.2%
Medicare	27.2%	27.0%	27.3%
Medicare Managed	18.0%	17.1%	16.4%
Medicaid	1.8%	2.0%	2.2%
Medicaid Managed	6.4%	6.5%	6.5%
Commercial Insurance	0.8%	0.8%	0.6%
Uninsured	8.2%	7.9%	7.8%
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

**TEXAS HEALTH RESOURCES
OPERATING AND FINANCIAL DATA**

HISTORICAL LIQUIDITY – DAYS CASH ON HAND

	June 30, 2017	December 31, 2016	December 31, 2015
	(Dollars in Thousands)		
Cash and Cash Equivalents	\$ 385,427	\$ 501,826	\$ 463,079
Short-Term Investments	7,250	6,250	1,447
Assets Limited as to Use - Internally Designated	<u>4,371,032</u>	<u>3,975,536</u>	<u>3,620,158</u>
Total Available Cash ¹	<u><u>\$ 4,763,709</u></u>	<u><u>\$ 4,483,612</u></u>	<u><u>\$ 4,084,684</u></u>
Total Operating Expenses	\$ 2,135,047	\$ 4,182,939	\$ 3,922,180
Plus - Income Taxes	2,714	3,606	4,608
Less - Depreciation and Amortization	<u>(114,942)</u>	<u>(224,263)</u>	<u>(220,277)</u>
Adjusted Total Operating Expenses	<u><u>\$ 2,022,819</u></u>	<u><u>\$ 3,962,282</u></u>	<u><u>\$ 3,706,511</u></u>
Average Daily Operating Expense ²	<u><u>\$ 11,176</u></u>	<u><u>\$ 10,826</u></u>	<u><u>\$ 10,155</u></u>
Days Cash Ratio (days) ³	<u><u>426.2</u></u>	<u><u>414.2</u></u>	<u><u>402.2</u></u>

¹ To provide for the purchase of the Series 2012B Bonds and Series 2008A, B & C Bonds that are tendered and not remarketed, THR maintains a combination of unrestricted cash, cash equivalents, and high grade fixed income securities that may be sold for same day settlement in an amount (value at market) sufficient to purchase the entire principal amount of such bonds, if all tendered for purchase.

² Average Daily Operating Expense is calculated using 181 days for the six months ended June 30, 2017, 366 days for the fiscal year ended December 31, 2016, and 365 days for the fiscal year ended December 31, 2015.

³ Total Available Cash divided by Average Daily Operating Expense.

**TEXAS HEALTH RESOURCES
OPERATING AND FINANCIAL DATA**

HISTORICAL CAPITALIZATION – DEBT TO CAPITALIZATION RATIO

	Fixed or Variable	June 30, 2017	December 31, 2016	December 31, 2015
(Dollars in Thousands)				
Debt:				
Series 2016A Bonds ¹	Fixed	\$ 701,643	\$ 703,051	\$ -
Series 2015 Taxable Bonds	Fixed	296,803	296,786	296,753
Series 2015A Bonds ¹	Fixed	59,982	59,983	59,983
Series 2012A (Taxable) Bonds	Fixed	98,882	98,871	98,851
Series 2012B Bonds ²	Variable	50,000	50,000	50,000
Series 2010 Bonds ¹	Fixed	151,226	151,147	150,998
Bank Loans ³	Variable	134,068	134,053	134,218
Series 2008A, B & C Bonds ²	Variable	176,055	176,055	176,055
Series 2007A Bonds ¹	Fixed	-	22,254	536,896
Series 2007B Bonds ¹	Fixed	101,552	101,568	101,598
FMHP Term and Revolving Loans ⁴	Combination	80,870	83,946	90,100
RRH Term and Revolving Loans ⁵	Combination	34,461	36,432	38,914
HIP Term and Revolving Loans ⁶	Combination	9,896	11,973	18,201
ACL Term and Revolving Loans ⁷	Combination	17,733	18,159	19,009
Other Non-Obligated Group Debt ⁸	Combination	43,643	43,921	43,491
Total Debt		<u>\$ 1,956,814</u>	<u>\$ 1,988,199</u>	<u>\$ 1,815,067</u>
Unrestricted Net Assets of THR		<u>\$ 5,412,566</u>	<u>\$ 4,993,413</u>	<u>\$ 4,470,386</u>
Debt to Capitalization Ratio ⁹		<u>26.6%</u>	<u>28.5%</u>	<u>28.9%</u>

¹ Net of premium/discounts.

² Series 2012B and 2008A, B & C Bonds are demand securities supported by self-liquidity provisions.

³ The unpaid principal balance of the Bank Loans may come due at the option of the respective banks at the end of each respective ten and fifteen year term. The Bank Loans bear interest at variable rates calculated as a percentage of LIBOR plus a spread.

⁴ FMHP is Flower Mound Hospital Partners, LLC (d/b/a Texas Health Presbyterian Hospital Flower Mound).

⁵ RRH is Rockwall Regional Hospital, LLC (d/b/a Texas Health Presbyterian Hospital Rockwall).

⁶ HIP is Health Imaging Partners, LLC.

⁷ ACL is AMH Cath Labs, LLC (d/b/a Texas Health Heart & Vascular Hospital Arlington).

⁸ Represents loans, notes payable, and capitalized leases of other Consolidated Joint Ventures.

⁹ Total Debt divided by Total Debt plus Unrestricted Net Assets of THR.

THR entered into credit agreements for general corporate purposes in December, 2012, with Wells Fargo Bank N.A. and U.S. Bank N.A. for lines of credit of \$75,000,000 each (the "Credit Agreements"). Under the Credit Agreements, outstanding balances under the lines of credit generally bear interest at variable rates calculated as a percentage of LIBOR plus a spread. At June 30, 2017, there were no outstanding balances under these Credit Agreements. The Wells Fargo and U.S. Bank Credit Agreements will expire on December 31, 2019 and December 31, 2017, respectively.

Certain reclassifications have been made to the fiscal year 2015 debt balance information to conform to the fiscal years 2017 and 2016 presentations. Unamortized debt issuance costs are now presented as a direct deduction from the carrying amount of the related debt liability.

**TEXAS HEALTH RESOURCES
OPERATING AND FINANCIAL DATA**

COMPOSITION OF INVESTMENTS AND ASSETS LIMITED AS TO USE

	June 30, 2017	December 31, 2016	December 31, 2015
	(Dollars in Thousands)		
Cash and cash equivalents	\$ 85,298	\$ 107,161	\$ 46,811
Domestic equity securities:			
Cash equivalents	49,277	55,634	35,645
Mutual funds	79,569	97,331	87,166
Common collective trust	208,416	259,320	230,933
Energy	87,545	104,471	76,196
Materials	91,843	79,073	71,000
Industrials	135,495	115,275	105,468
Consumer discretionary	192,166	198,337	194,211
Consumer staples	101,093	99,384	73,007
Health care	262,400	225,337	235,282
Financials	411,325	385,032	332,596
Information technology	466,815	381,900	348,254
Telecommunication services	35,164	30,616	30,123
Utilities	27,311	30,377	29,011
Other	15,141	15,413	16,408
International equity securities:			
Mutual funds	264,713	228,589	245,535
Common collective trust	516,488	440,039	304,129
Fixed income securities:			
Cash equivalents	175,044	49,859	35,915
U.S. Government	26,183	25,964	38,422
Corporate bonds	327,080	306,299	264,035
Agency mortgages	537,339	514,348	485,628
U.S. Agencies	553,563	522,421	556,827
Other	7,528	6,393	2,809
Mutual funds (blended securities)	9,266	8,875	6,760
Hedge funds	167	-	1,347
Texas Methodist Foundation	1,194	1,188	1,179
Real estate	736	736	736
Mineral interests	2,018	2,050	3,065
Contributions receivable from split-interest agreements	1,563	1,510	1,574
Total investments and assets limited as to use	<u>\$ 4,671,740</u>	<u>\$ 4,292,932</u>	<u>\$ 3,860,072</u>

Note: Included in assets limited as to use in the accompanying consolidated balance sheets is approximately \$10,699,000, \$12,377,000 and \$8,747,000 of unconditional promises to give from donors at June 30, 2017, December 31, 2016, and December 31, 2015, respectively, that are excluded from the above table.

TEXAS HEALTH RESOURCES SUPPLEMENTAL INFORMATION

STRATEGIC PLANS AND RECENT DEVELOPMENTS

On May 10, 2016, THR and Adeptus Health Inc. ("Adeptus Health") formed a joint venture to increase access to high quality, convenient emergency medical care in the Dallas-Fort Worth area. Under the joint venture, Adeptus Health's freestanding First Choice Emergency Rooms in North Texas, and its First Texas Hospital in Carrollton, aligned with THR to grow THR's network of hospitals and outpatient centers. On April 19, 2017, Adeptus Health filed for reorganization under Chapter 11 of the U.S. Bankruptcy Code. The joint venture between THR and Adeptus Health is not part of the court-supervised process, and all freestanding emergency rooms under the joint venture will continue to operate as normal. At this time, there is not sufficient information available regarding the impact the reorganization will have on the joint venture. THR management is monitoring the situation and is actively reviewing its options with respect to the joint venture.

THR has announced the development of Texas Health Hospital Frisco to be located on 20 acres off the Dallas North Tollway in northeast Collin County. The campus will include an 80-bed acute care hospital and a 120,000 square-foot medical office building to house primary care practices and a multispecialty clinic. Construction is anticipated to begin around the middle of 2017 with a projected opening in late 2019.

LITIGATION AND REGULATORY MATTERS

In May 2013, THR learned sheets of microfiche containing records for patients treated at Texas Health Harris Methodist Hospital Fort Worth from 1980-1990 were not securely handled by the outside vendor with which THR contracted for all of its document destruction. THR has made all legally required notifications of the incident, including letters to the patients involved, a notice posted on THR's public website, and a press release. The Office of Civil Rights has closed this matter; however, to date, the State of Texas has not responded. THR does not anticipate a material financial impact due to this incident.

In March 2015, the System made a disclosure to the Office of Inspector General ("OIG") regarding THPG billing of certain PET scan tests and nuclear stress tests that did not meet Medicare medical necessity requirements. Management believes it is too early to predict with certainty the outcome of this matter; however, management does not anticipate a material financial impact.

In December 2011, the federal government approved the Texas Healthcare Transformation and Quality Improvement Program: 1115 Waiver ("Section 1115 Waiver Program"), which was implemented by the Texas Health and Human Services Commission ("HHSC"). The Section 1115 Waiver Program has been extended through December 31, 2017. The Uncompensated Care ("UC") pool under the Section 1115 Waiver Program helps hospitals and certain other providers offset the uncompensated costs they incur by providing services to Medicaid patients. Funding for UC depends on the Tarrant County Hospital District and Dallas County Hospital District providing intergovernmental transfers to HHSC as the state share, which is then matched by federal funds. The public entities have the sole discretion to make or not make intergovernmental transfers. In a letter dated September 1, 2016, to HHSC, Centers for Medicare and Medicaid Services ("CMS") disallowed federal matching funds applicable to the Dallas County and Tarrant County affiliations for the quarter ended December 31, 2015. CMS alleges that the private hospitals participating in these affiliations fail to comply with the federal provider-related donation requirements. On October 28, 2016, HHSC requested a reconsideration by the Secretary of Health & Human Services. CMS responded on December 21, 2016 stating they believe HHSC's arguments do not merit a withdrawal or revision to the disallowance. HHSC is currently evaluating a decision to appeal the disallowance to the HHS Departmental Appeals Board. It is too early to predict the outcome of this matter, including whether HHSC will prevail in the litigation and whether CMS will disallow federal matching funds to the Dallas County and Tarrant County affiliations for additional federal fiscal year quarters.

**TEXAS HEALTH RESOURCES
SUPPLEMENTAL INFORMATION**

LITIGATION AND REGULATORY MATTERS (Continued)

THR's Corporate Compliance Department investigates all compliance matters reported through its compliance program. As of the date of this disclosure, there was no additional pending or, to the knowledge of System management, threatened litigation, including professional liability claims, or reported compliance issues which in the opinion of System management involves any substantial risk of material liability for the System, and where applicable, in excess of available reserves and insurance coverages.