



Trinity Health Operating Income Jumps to \$80 million in Q1 FY18

Summary Highlights for the First Quarter of FY18 (Quarter Ended September 30, 2017)

In the first quarter of fiscal year 2018, Trinity Health reported a \$36.7 million increase in operating income to \$80.0 million from \$43.3 million in the prior year. Its fiscal 2018 operating margin — of 1.8%, and its operating cash flow margin of 7.9% — significantly improved compared to the prior year's operating margin of 1.0% and operating cash flow margin of 7.3%. Revenue growth coupled with cost controls, improved length of stay and improved performance in Trinity Health's owned managed care plans helped to increase margins.

Revenue increased \$124 million to \$4.4 billion, a 2.9% increase over prior year. The increase is attributed to growth in patient volumes, payment rates and, to a lesser extent, case mix, as well as health plan premium revenue. Volume increased over the prior year in 11 of its 20 regional health ministries as measured by case mix adjusted equivalent discharges.

Expenses increased at a slower pace, \$87.8 million or 2.1%, to \$4.3 billion. Trinity Health continues to undertake targeted efficiency initiatives to improve performance and address unfavorable industry trends that have continued into fiscal year 2018. Cost efficiencies are focused primarily on labor, productivity and supply costs and clinical and administrative operations.

Highlights for the first quarter ended September 30, 2017, include:

- Total assets of \$25.1 billion
- Total net assets of \$12.4 billion
- Total unrestricted revenue of \$4.4 billion, a 2.9% increase over fiscal 2017
- Operating income of \$80.0 million
- Excess of revenue over expense of \$399 million with a net margin of 8.4%.
- Unrestricted cash and investments of \$8.5 billion
- Days cash on hand of 190 days

TRINITY HEALTH

UNAUDITED QUARTERLY REPORT

For the three months ended September 30, 2017 and 2016

TRINITY HEALTH

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

	As of	
	September 30, 2017	June 30, 2017
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 945,540	\$ 1,008,197
Investments	3,538,135	3,526,204
Security lending collateral	387,474	332,972
Assets limited or restricted as to use - current portion	337,683	328,712
Patient accounts receivable - net of allowance for doubtful accounts of \$433.9 million and \$428.9 million at September 30, 2017 and June 30, 2017, respectively	1,949,914	1,877,860
Estimated receivables from third-party payors	259,264	260,856
Other receivables	327,483	360,051
Inventories	284,268	274,830
Prepaid expenses and other current assets	215,562	172,051
Total current assets	8,245,323	8,141,733
ASSETS LIMITED OR RESTRICTED AS TO USE - noncurrent portion:		
Held by trustees under bond indenture agreements	7,355	7,139
Self-insurance, benefit plans and other	842,477	823,948
By Board	3,846,087	3,709,246
By donors	481,444	460,491
Total assets limited or restricted as to use - noncurrent portion	5,177,363	5,000,824
PROPERTY AND EQUIPMENT - Net	7,814,380	7,853,456
INVESTMENTS IN UNCONSOLIDATED AFFILIATES	3,214,658	3,105,173
GOODWILL	302,013	301,043
OTHER ASSETS	340,047	336,854
TOTAL ASSETS	\$ 25,093,784	\$ 24,739,083

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

(Continued)

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

	As of	
	September 30, 2017	June 30, 2017
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Commercial paper	\$ 99,874	\$ 99,861
Short-term borrowings	1,039,840	1,039,840
Current portion of long-term debt	192,564	192,680
Accounts payable and accrued expenses	1,340,969	1,404,413
Salaries, wages, and related liabilities	783,550	820,014
Payable under security lending agreements	387,474	332,972
Estimated payables to third-party payors	334,596	331,585
Current portion of self-insurance reserves	270,056	269,874
Total current liabilities	4,448,923	4,491,239
LONG-TERM DEBT - Net of current portion	5,263,587	5,269,862
SELF-INSURANCE RESERVES - Net of current portion	1,002,897	980,624
ACCRUED PENSION AND RETIREE HEALTH COSTS	1,230,682	1,315,991
OTHER LONG-TERM LIABILITIES	706,383	695,940
Total liabilities	12,652,472	12,753,656
NET ASSETS:		
Unrestricted net assets	11,711,565	11,282,433
Noncontrolling ownership interest in subsidiaries	171,666	173,703
Total unrestricted net assets	11,883,231	11,456,136
Temporarily restricted net assets	368,360	345,974
Permanently restricted net assets	189,721	183,317
Total net assets	12,441,312	11,985,427
TOTAL LIABILITIES AND NET ASSETS	\$ 25,093,784	\$ 24,739,083

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, 2017 and 2016
(In thousands)

	<u>2017</u>	<u>2016</u>
UNRESTRICTED REVENUE:		
Patient service revenue - net of contractual and other allowances	\$ 3,935,821	\$ 3,834,933
Provision for bad debts	(144,166)	(130,754)
Net patient service revenue less provision for bad debts	3,791,655	3,704,179
Premium and capitation revenue	273,975	251,764
Net assets released from restrictions	7,794	4,191
Other revenue	335,478	324,357
Total unrestricted revenue	<u>4,408,902</u>	<u>4,284,491</u>
EXPENSES:		
Salaries and wages	1,926,357	1,864,649
Employee benefits	343,238	350,514
Contract labor	64,004	60,082
Total labor expenses	<u>2,333,599</u>	<u>2,275,245</u>
Supplies	705,833	697,417
Purchased services	513,129	510,908
Depreciation and amortization	213,576	216,369
Occupancy	189,496	184,357
Medical claims	103,689	106,903
Interest	54,012	51,293
Other	215,575	198,729
Total expenses	<u>4,328,909</u>	<u>4,241,221</u>
OPERATING INCOME	<u>79,993</u>	<u>43,270</u>
NONOPERATING ITEMS:		
Investment earnings	243,237	278,411
Equity in earnings of unconsolidated affiliates	92,326	92,612
Change in market value and cash payments of interest rate swaps	(4,374)	2,219
Inherent contributions	-	62,057
Other, including income taxes	(2,203)	593
Total nonoperating items	<u>328,986</u>	<u>435,892</u>
EXCESS OF REVENUE OVER EXPENSES	408,979	479,162
EXCESS OF REVENUE OVER EXPENSES ATTRIBUTABLE TO NONCONTROLLING INTEREST	(10,113)	(11,674)
EXCESS OF REVENUE OVER EXPENSES, net of noncontrolling interest	<u>\$ 398,866</u>	<u>\$ 467,488</u>

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

(Continued)

TRINITY HEALTH
CONSOLIDATED STATEMENT OF OPERATIONS AND
CHANGES IN NET ASSETS (UNAUDITED)
THREE MONTHS ENDED SEPTEMBER 30, 2017 and 2016
(In thousands)

	<u>2017</u>	<u>2016</u>
UNRESTRICTED NET ASSETS:		
Unrestricted net asset attributable to Trinity Health:		
Excess of revenue over expenses	\$ 398,866	\$ 467,488
Net assets released from restrictions for capital acquisitions	3,961	2,369
Net change in retirement plan related items - consolidated organizations	21,770	27,821
Other	<u>4,534</u>	<u>(4,954)</u>
Increase in unrestricted net assets attributable to Trinity Health	429,131	492,724
Unrestricted net asset attributable to noncontrolling interests:		
Excess of revenue over expenses attributable to noncontrolling interests	10,113	11,674
Noncontrolling interest related to acquisitions	-	2,500
Dividends and other	<u>(12,149)</u>	<u>(9,544)</u>
(Decrease) increase in unrestricted net assets attributable to noncontrolling interest before discontinued operations	<u>(2,036)</u>	<u>4,630</u>
TEMPORARILY RESTRICTED NET ASSETS:		
Contributions	31,065	24,485
Net investment gain	2,768	4,945
Net assets released from restrictions	(11,755)	(6,560)
Acquisitions	-	3,078
Other	<u>308</u>	<u>(1,515)</u>
Increase in temporarily restricted net assets	<u>22,386</u>	<u>24,433</u>
PERMANENTLY RESTRICTED NET ASSETS:		
Contributions for endowment funds	1,091	340
Net investment gain	5,464	2,319
Acquisitions	-	16,526
Other	<u>(151)</u>	<u>(65)</u>
Increase in permanently restricted net assets	<u>6,404</u>	<u>19,120</u>
INCREASE IN NET ASSETS	455,885	540,907
NET ASSETS - BEGINNING OF YEAR	<u>11,985,427</u>	<u>10,247,213</u>
NET ASSETS - END OF YEAR	<u>\$ 12,441,312</u>	<u>\$ 10,788,120</u>

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

(Concluded)

TRINITY HEALTH
SUMMARIZED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
THREE MONTHS ENDED SEPTEMBER 2017 and 2016
(In thousands)

	<u>2017</u>	<u>2016</u>
OPERATING ACTIVITIES:		
Increase (decrease) in net assets	\$ 455,885	\$ 540,907
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	213,576	216,369
Provision for bad debts	144,166	130,754
Inherent contributions in acquisitions	-	(62,057)
Change in net unrealized and realized gains and losses on investments	(235,917)	(271,244)
Change in market values of interest rate swaps	(1,073)	(3,663)
Undistributed equity in earnings of unconsolidated affiliates	(105,233)	(100,221)
Deferred retirement items arising during the year	(4,772)	(8,690)
Increase in noncontrolling interest related to acquisitions	-	(2,500)
Restricted contributions and investment income received	(6,025)	(2,859)
Restricted net assets acquired related to acquisitions	-	(19,604)
Other adjustments	(4,017)	(8,035)
Changes in:		
Patient accounts receivable	(212,220)	(182,559)
Other assets	(30,905)	29,819
Accounts payable and accrued expenses	(45,210)	(103,517)
Estimated receivables from third-party payors	1,592	(4,032)
Estimated payables to third-party payors	3,011	(11,401)
Self-insurance and other liabilities	35,712	13,802
Accrued pension and retiree health costs	(80,832)	(90,223)
Total adjustments	<u>(328,147)</u>	<u>(479,861)</u>
Net cash provided by operating activities	<u>127,738</u>	<u>61,046</u>
INVESTING ACTIVITIES:		
Net sales of investments	46,150	101,591
Purchases of property and equipment	(228,935)	(241,742)
Proceeds from disposal of property and equipment	544	1,349
Proceeds from sale of divestitures	-	3,283
Net cash (used for) acquired from acquisitions	(899)	5,085
Change in other investing activities	(11,925)	(4,834)
Net cash used in investing activities	<u>(195,065)</u>	<u>(135,268)</u>
FINANCING ACTIVITIES:		
Proceeds from issuance of debt	24,305	13,918
Repayments of debt	(25,360)	(27,055)
Net change in commercial paper and line of credit	(295)	14,947
Increase in financing costs and other	(5)	(552)
Proceeds from restricted contributions and restricted investment income	6,025	2,859
Net cash provided by financing activities	<u>4,670</u>	<u>4,117</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	(62,657)	(70,105)
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	1,008,197	1,044,683
CASH AND CASH EQUIVALENTS - END OF PERIOD	\$ 945,540	\$ 974,578

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, 2017 AND 2016

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, 2017 are not necessarily indicative of the results to be expected for the year ending June 30, 2018.

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.

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 and unrealized gains and losses. Also included are equity earnings from investment funds accounted for using the equity method. Investment earnings on assets held by trustees under bond indenture agreements, assets designated by the Corporation's board of directors ("Board") for debt redemption, assets held for borrowings under the intercompany loan program, assets held by grant-making foundations, assets deposited in trust funds by a captive insurance company for self-insurance purposes and interest and dividends earned on life plan communities advance entrance fees, 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, 2017 and June 30, 2017, the Corporation had securities loaned of \$645.2 million and \$452.0 million, respectively, and received collateral (cash and noncash) totaling \$662.6 million and \$463.1 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 classifies certain assets as assets held for sale in the consolidated balance sheets when the assets have met applicable criteria for this classification. The Corporation also classifies 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 and prepaid 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 non-operating items in the consolidated statements of operations and changes in net assets.

Excess of Revenue Over Expenses – The consolidated statements of operations and changes in net assets includes excess of revenue over expenses. Changes in unrestricted net assets, which are excluded from excess 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.

Forthcoming Accounting Pronouncements –

In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-09, "*Revenue from Contracts with Customers (Topic 606)*". In August 2015, the FASB amended the guidance to defer the effective date of this standard by one year. ASU No. 2014-09 affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards. The core principle of the guidance in ASU No. 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The Corporation is currently evaluating the requirements of the new standard to insure that there are have processes, systems and internal controls in place to collect the necessary information to implement the standard, which will be effective for the Corporation beginning July 1, 2018. While the adoption of ASU No. 2014-09 will have a material effect on the amounts presented in certain categories on the consolidated statements of operations, the Corporation is still evaluating the impact this guidance may have 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. The main difference between the guidance in ASU No. 2016-02 and current GAAP is the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under current GAAP. Recognition of these lease assets and liabilities will have a material impact to the Corporation's consolidated balance sheet upon adoption. In transition, lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach, which includes a number of optional practical expedients. 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 March 2017, the FASB issued ASU No. 2017-07, "*Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost,*" which amends the requirements related to the presentation of the components of net periodic benefit cost in the statement of operations for an entity's sponsored defined benefit pension and other postretirement plans. This guidance is effective for the Corporation beginning July 1, 2019. The Corporation does not expect this guidance to have a material impact on its consolidated financial statements.

In March 2017, the FASB issued ASU No. 2017-08, "*Premium Amortization on Purchased Callable Debt Securities,*" which shortens the amortization period for certain callable debt securities held at a premium to be amortized to the earliest call date. Under current GAAP, the premium is generally amortized to the maturity date. This guidance is effective for the Corporation beginning July 1, 2020. The Corporation is still evaluating the impact this guidance may have on the 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. Specifically this guidance reduces the three classifications of net assets on the balance sheet to two classifications. 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 November 2016, the FASB issued ASU No. 2016-18, "*Restricted Cash,*" which adds and clarifies guidance in the presentation of changes in restricted cash on the statement of cash flows and requires restricted cash to be included with cash and cash equivalents in the statement of cash flows. This guidance does not provide a definition of restricted cash. This guidance is effective for the Corporation beginning

July 1, 2019. The Corporation is still evaluating the impact this guidance will have on the consolidated statement of cash flows.

In August 2016, the FASB issued ASU No. 2016-15, "*Classification of Certain Cash Receipts and Cash Payments.*" This guidance adds and 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 2017, the FASB issued ASU No. 2017-12, "*Derivatives and Hedging (Topic 815) Targeted Improvements to Accounting for Hedging Activities.*" This guidance changes the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities; this guidance also simplifies the application of the hedge accounting guidance. This guidance is effective for the Corporation beginning July 1, 2019. The Corporation does not expect this guidance to have a material 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 \$110.3 million and \$105.4 million for the three months ended September 30, 2017 and 2016, respectively, of which \$18.0 million and \$12.8 million, respectively, is included in other revenue and \$92.3 million and \$92.6 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, 2017 and June 30, 2017, the Corporation's investment in BayCare totaled \$2,539 million and \$2,447 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, 2017 and June 30, 2017, the Corporation's investment in GHP totaled \$176.3 million and \$170.3 million, respectively.

Catholic Health System, Inc. – The Corporation has a 50% 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. CHS was originally jointly sponsored by the Sisters of Mercy, Ascension Health System, the Franciscan Sisters of St. Joseph, and the Diocese of Buffalo. The

Corporation held a one-third interest in CHS until May 1, 2017, when Ascension Health System withdrew its sponsorship and corporate membership in CHS, which increased the Corporation's interest from one-third to 50%. 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, 2017 and June 30, 2017, the Corporation's investment in CHS totaled \$83.3 million and \$85.2 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, 2017 and June 30, 2017, the Corporation's investment in EH/SJHS totaled \$93.4 million and \$90.6 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. For the three months ended September 30, 2017, other expense includes a charge of \$2.2 million related to the cash flow sharing agreement.

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, 2017 and June 30, 2017, the Corporation's investment in MHN totaled \$95.6million and \$94.2 million, respectively.

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

	September 30, 2017				
	Baycare	GHP	CHS	EH/SJHS	MHN
Total assets	\$ 7,253,686	\$ 947,212	\$ 1,153,621	\$ 476,647	\$ 288,470
Total liabilities	\$ 2,028,781	\$ 593,492	\$ 911,545	\$ 285,925	\$ 89,998

	June 30, 2017				
	Baycare	GHP	CHS	EH/SJHS	MHN
Total assets	\$ 7,004,163	\$ 1,028,120	\$ 1,127,664	\$ 467,148	\$ 267,763
Total liabilities	\$ 1,962,261	\$ 687,510	\$ 882,229	\$ 281,171	\$ 71,001

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, 2017				
	Baycare	GHP	CHS	EH/SJHS	MHN
Revenue, net	\$ 886,261	\$ 615,378	\$ 278,256	\$ 146,070	\$ 91,103
Excess (deficiency) of revenue over expenses	\$ 89,898	\$ 11,768	\$ (3,630)	\$ 5,671	\$ 1,532

	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 over expenses	\$ 166,907	\$ 6,937	\$ (5,038)	\$ (4,351)	\$ 409

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, 2017				
	Baycare	GHP	CHS	EH/SJHS	MHN
Other revenue	\$ -	\$ 5,180	\$ -	\$ -	\$ (32)
Equity in earnings of unconsolidated organizations	91,529	-	(1,982)	2,773	-
Other changes in unrestricted net assets	577	1,060	91	-	1,500
	<u>\$ 92,106</u>	<u>\$ 6,240</u>	<u>\$ (1,891)</u>	<u>\$ 2,773</u>	<u>\$ 1,468</u>

	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>

Acquisitions:

Saint Mary's Health System ("SMHS") – On August 1, 2016, the Corporation became, through its Trinity Health Of New England, Inc. 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 amount of the inherent contribution related to this transaction was adjusted in subsequent periods of fiscal year 2017 to \$56.0 million for the year ended June 30, 2017. 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	39,735
Patient accounts receivable, net	31,029	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,		Total liabilities acquired	<u>155,105</u>
current portion	3,465		
Property and equipment	100,686	Unrestricted net assets	55,994
Assets limited or restricted as to use,		Unrestricted noncontrolling interest	<u>2,500</u>
noncurrent portion	62,150	Total unrestricted net assets	58,494
Other assets	5,859	Temporarily restricted net assets	1,978
Total assets acquired	<u>\$ 232,103</u>	Permanently restricted net assets	<u>16,526</u>
		Total net assets	<u>\$ 76,998</u>

For the three month period ended September 30, 2017, SMHS reported revenue of \$79.3 million and deficiency of revenue over expenses of \$3.8 million in the consolidated statements of operations. 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 statement of operations.

Pending Divestitures:

Lourdes Health System ("Lourdes") and Saint Francis Medical Center ("SFMC") – On August 31, 2017, the Corporation, through its subsidiary Maxis Health, signed a non-binding letter of intent ("LOI") to transfer control of Lourdes, based in Camden, New Jersey, and SFMC, located in Trenton, New Jersey, to Cooper University Health Care ("Cooper"). The agreement is subject to development of a definitive agreement, which is anticipated to be executed in early December 2017, as well as regulatory approval and other customary closing conditions, the timing of which is uncertain. Lourdes and SFMC had combined revenue of \$180.8 million and \$170.2 million for the three months ended September 30, 2017 and 2016, respectively and combined deficiency of revenue over expenses of \$6.4 million and \$11.4 million for the three months ended September 30, 2017 and 2016, respectively.

4. PROPERTY AND EQUIPMENT

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

	September 30, 2017	June 30, 2017
Land	\$ 359,617	\$ 360,356
Buildings and improvements	8,985,595	9,068,510
Equipment	6,235,885	6,160,546
Capital leased assets	179,773	179,814
Total	15,760,870	15,769,226
Accumulated depreciation and amortization	(8,895,628)	(8,839,049)
Construction in progress	949,138	923,279
Property and equipment, net	<u>\$ 7,814,380</u>	<u>\$ 7,853,456</u>

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

<u>Regional Health Ministry</u>	<u>Capital Commitment</u>	<u>Commitment Period Ending</u>	<u>Capital Spending through September 30, 2017*</u>
Loyola University Health System, Chicago, IL	\$300 million over 7 years, \$400 million if performance metrics are achieved	June 30, 2018	\$328 million
St. Joseph's Hospital Health Center, Syracuse, NY	\$60 million over 4 years, \$90 million if performance metrics are achieved	June 30, 2019	\$57 million
St. Francis Hospital and Medical Center, Hartford, CT	\$275 million over 5 years if performance metrics are achieved	June 30, 2020	\$108 million

**Excludes HUD and philanthropy spending*

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, 2017 and June 30, 2017 that has not been secured under the ARMI is generally collateralized by certain property and equipment.

Mercy Health System of Chicago ("MHSC") has a \$58.0 million mortgage loan outstanding at September 30, 2017 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, 2017 and June 30, 2017, the total amount of commercial paper outstanding was \$99.9 million at both dates. 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, 2017. 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, \$285 million expires in July 2019, \$325 expires in July 2020 and \$321 million expires in July 2021. The Credit Agreements are secured by obligations under the ARMI. As of September 30, 2017 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, 2017 and June 30, 2016, there were no amounts outstanding under this credit facility.

Transactions – 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).

During January 2017, the Trinity Health Credit Group issued \$344.2 million par value in tax-exempt fixed-rate hospital revenue bonds at a premium of \$26.1 million under the ARMI. Proceeds were used partially to refund \$66.5 million of certain tax-exempt bonds and pay down \$54.8 million of then outstanding taxable commercial paper obligations. 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 October 2017, the Corporation remarketed \$50 million in tax-exempt, variable rate hospital revenue bonds (the "Series 2011A bonds") under the ARMI, pursuant to a continuing covenant agreement with a private purchaser which provides for a three year mandatory tender period (subject to mandatory tender on October 2, 2020).

6. PROFESSIONAL AND GENERAL LIABILITY PROGRAMS

The Corporation operates a wholly owned insurance company, Trinity Assurance, Ltd ("TAL"). 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 other coverages from unrelated third-party commercial insurers. TAL has also limited its liability through commercial reinsurance arrangements.

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. SMICL did not, nor does it intend to, write or renew any insurance business after July 31, 2016. SMICL was merged into TAL on March 1, 2017 at which time all losses previous to August 1, 2016 for SMICL were assumed by TAL.

The Corporation's current self-insurance program includes \$15 million per occurrence for the primary layers of professional liability as well as \$10 million per occurrence for general and 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 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 per occurrence for first-party property damage with commercial insurance providing additional coverage.

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, 2017, 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, 2017 and June 30, 2017, the assets under these plans totaled \$207.7 million and \$198.7 million and liabilities totaled \$223.5 million and \$212.0 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. Employer contributions to these plans include a non-elective contribution of 3% for participants who satisfy certain eligibility requirements, with a minimum non-elective contribution for certain participants, 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 \$79.9 million and \$74.3 million for the three month period ended September 30, 2017 and 2016, 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 ERISA, which have not made an election under Section 410(d) of the Code to be subject to ERISA. The Corporation's adopted funding policy for the majority of its qualified church plans, which is reviewed annually, is to fund the current service cost based on the accumulated benefit obligations and amortization of any under or over funding.

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 cost sharing provisions. 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 SMHS on August 1, 2016, including all related benefit plans. 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	
	2017	2016	2017	2016
Service cost	\$ -	\$ 397	\$ 42	\$ 71
Interest cost	78,492	77,810	1,338	1,380
Expected return on assets	(109,762)	(102,024)	(1,934)	(1,770)
Amortization of prior service cost	(2,264)	(2,265)	(125)	(141)
Recognized net actuarial loss	19,466	21,803	(46)	(2)
Net periodic benefit cost (income)	\$ (14,068)	\$ (4,279)	\$ (725)	\$ (462)

8. CONTINGENCIES

For the year 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 has been determined to not be material to any of the prior period consolidated financial statements. The Corporation has completed the submission of corrected data for all affected years to the Centers for Medicare and Medicaid Services. The liability is included in accounts payable and accrued expenses in the consolidated balance sheet as of June 30, 2017 and was not materially different from the original estimate.

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, initiating investigations, or indicating the existence of whistleblower litigation. 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 November 27, 2017, the date the quarterly report was issued. The following subsequent event was noted:

MacNeal Hospital and Affiliated Healthcare Businesses ("MacNeal and its Affiliates"). On October 10, 2017, the Corporation's Loyola University Health System, through a wholly controlled subsidiary, agreed to purchase the assets of MacNeal Hospital, located in Berwyn, Illinois, and certain other healthcare operations affiliated with the hospital from an affiliate of Tenet Healthcare Corporation. The purchase price for MacNeal and its Affiliates to be paid upon closing is anticipated not to exceed \$300 million. MacNeal and its Affiliates' consolidated revenue is expected to be less than 2% of the Corporation's consolidated revenue for the year ended June 30, 2017. The transaction is expected to be completed in the third quarter of fiscal year 2018, subject to regulatory approvals and other customary closing conditions.

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

September 30, 2017



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 have resulted 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 have received reduced payments for care, millions of previously uninsured Americans have received coverage.

President Trump has repeatedly urged Congress to repeal all or a portion of the ACA. He has taken various executive actions including urging federal agencies to exercise their authority to waive or delay the implementation of the Act, directing the departments of

Treasury, Labor and Health and Human Services to consider proposing regulations or guidance to expand the availability of association health plans, short-term limited duration insurance and health reimbursement arrangements and stopping payment of the Cost Sharing Reductions ("CSRs"). Insurers use the federal CSRs to reduce out-of-pocket costs for low-income individuals purchasing coverage through the Health Insurance Marketplace. Additionally, both chambers of Congress have taken action on different versions of legislation aimed at repealing all or a portion of the ACA. However, there has yet to be legislation to repeal and replace all or portions of the ACA that has passed both chambers. The timing and likelihood of success of additional Congressional efforts to repeal and replace all or a portion of the ACA remain unclear.

Management of the Corporation cannot predict with any reasonable degree of certainty or reliability the ultimate effects of the legislation, the potential repeal of all or a portion of the legislation, or any replacement 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 ("SMHS")

On August 1, 2016, the Corporation became, through its Trinity Health Of New England subsidiary as part of a member substitution, the sole corporate member of SMHS, a regional health care system located in Waterbury, Connecticut. As a result of this transaction, the Corporation recognized an inherent contribution of \$56.0 million for the year ended June 30, 2017 in the consolidated statement of operations and changes in net assets.

Lourdes Health System ("Lourdes") and Saint Francis Medical Center ("SFMC")

On August 31, 2017, the Corporation, through its subsidiary Maxis Health, signed a non-binding letter of intent ("LOI") to transfer control of Lourdes, based in Camden, New Jersey, and SFMC, in Trenton, New Jersey, to Cooper

University Health Care ("Cooper"). The agreement will bring together health care providers from across south and central New Jersey, allowing expanded access to high quality care for thousands of new patients. The agreement is subject to development of a definitive agreement anticipated to be executed in early December 2017, as well as regulatory approval, the timing of which is uncertain. Lourdes and SFMC had combined revenue of \$180.8 million and \$170.2 million for the three months ended September 30, 2017 and 2016, respectively, and combined deficiency of revenue over expenses of \$6.4 million and \$11.4 million for the three months ended September 30, 2017 and 2016, respectively.

MacNeal Hospital and Affiliated Healthcare Businesses ("MacNeal and its Affiliates"). On October 10, 2017, the Corporation's Loyola University Health System, through a wholly controlled subsidiary, agreed to purchase the assets of MacNeal Hospital, located in Berwyn, Illinois, and certain other healthcare operations affiliated with the hospital from an affiliate of Tenet Healthcare Corporation. The purchase price for MacNeal and its Affiliates to be paid upon closing is anticipated not to exceed \$300 million. MacNeal and its Affiliates' consolidated revenue is expected to be less than 2% of the Corporation's consolidated revenue for the year ended June 30, 2017. The transaction is expected to be completed in the third quarter of fiscal year 2018, subject to regulatory approvals and other customary closing conditions.

Results from Operations

Operating Income

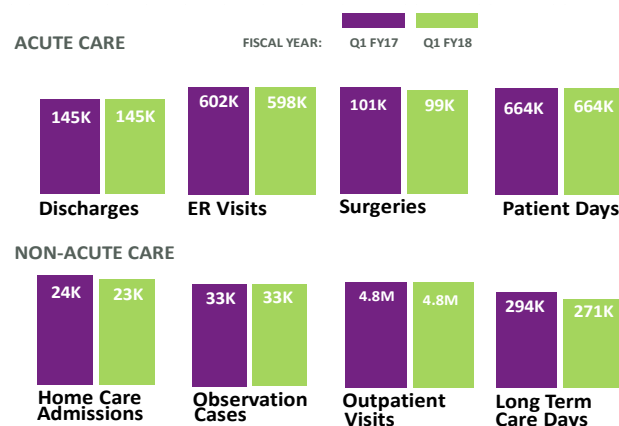
Operating income for the first three months of fiscal year 2018 increased to \$80.0 million compared to \$43.3 million for the same period in fiscal year 2017. Operating margin and operating cash flow margin were 1.8% and 7.9%, respectively, for the first three months of fiscal year 2018 compared to 1.0% and 7.3% for the same period in fiscal year 2017. The acquisition of SMHS did not have a material impact on operating income and margins. Revenue growth coupled with cost controls, improved length of stay and improved performance in the Corporation's owned managed care plans helped to increase margins.

(dollars in millions)	Q1 FY17	Q1 FY18	Q1 FY17*	Q1 FY18*
Operating Income	\$43.3	\$80.0	\$43.4	\$84.1
Operating Revenue	\$4,284	\$4,409	\$4,233	\$4,330
Operating Margin	1.0%	1.8%	1.0%	1.9%
Operating Cash Flow Margin	7.3%	7.9%	7.3%	8.0%

* Excluding the impact of the SMHS acquisition

Revenue

Total unrestricted revenue of \$4.4 billion increased \$124 million, or 2.9%, for the first three months of fiscal year 2018 compared to the same period in fiscal year 2017. Revenue from the SMHS acquisition accounted for \$27.7 million of the increase or 0.6%. The increase in revenue was due primarily to the following: (i) \$58.2 million from volume growth, (ii) \$36.8 million of payment rate increases, (iii) \$9.3 million from improvements in case mix, and (iii) an increase of \$32.3 million in other revenue, including \$12.3 million of health plan premium revenue. These increases were partially tempered by a continued unfavorable shift in payor mix. Same facility volumes were favorable to prior year with 11 of the 20 Regional Health Ministries experiencing increases in case mix adjusted equivalent discharges.



Expenses

Total operating expenses of \$4.3 billion increased \$88 million, or 2.1% for the first three months of fiscal year 2018 compared to the same period in fiscal year 2017. Expenses from the SMHS acquisition accounted for \$31.7 million of the increase or 0.7%. The increase in operating expenses was due primarily to the following: (i) labor expense increase of \$58.4 million (salaries and wages increase of \$61.7 million primarily due to a 3.0% increase in rate and a 0.3% increase in FTEs), (ii) supplies increase of \$11.3 million, driven by higher volumes, and (iii)

medical and professional fees increase of \$11.2 million, Expenses for medical claims, purchased services, occupancy, interest, depreciation and amortization, and other expenses did not materially change for the first three months of fiscal year 2018 compared to the same period in fiscal year 2017.

Nonoperating Items

The Corporation reported gains in nonoperating items of \$329 million for the first three months of fiscal year 2018 compared to gains of \$435.9 million for the same period in fiscal year 2017. The change was primarily due to a reduction in inherent contributions of \$62.1 million (related to acquisitions in FY17) and lower investment returns of \$41.8 million (primarily driven by overall global investment market conditions) compared to the first three months of fiscal year 2017.

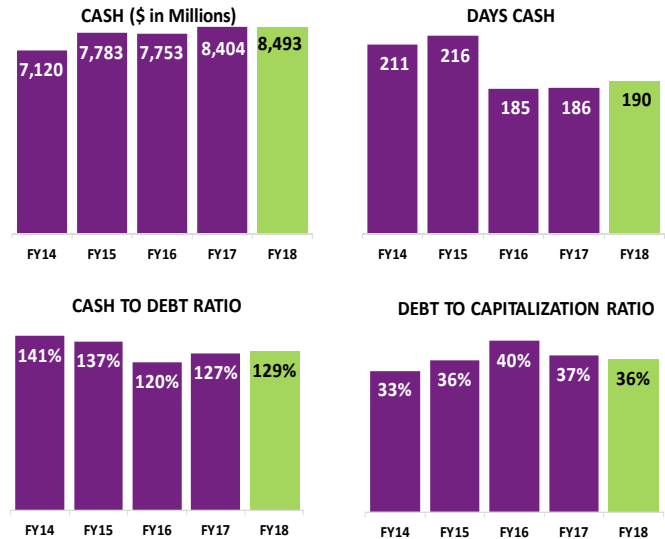
Excess of Revenue over Expenses

Excess of revenue over expenses for the first three months of fiscal year 2018 was \$398.9 million compared to \$467.5 million for the same period in fiscal year 2017. The decrease was primarily due to a \$62.1 million decrease in inherent contributions, primarily related to the acquisition of SMHS and lower investment income of \$41.8 million, partially offset by improved operating income of \$36.7 million compared to the same period in fiscal year 2017.

Balance Sheet

Total assets of \$25.1 billion increased \$355 million, or 1.4% as of September 30, 2017, compared to June 30, 2017. Asset growth was mainly driven by nonoperating investment income of \$329 million. Total assets include unrestricted cash and investments of \$8.5 billion or 190 days of cash on hand. Days cash on hand increased by four days during the first quarter due primarily to strong investment returns and positive operating cash flow. Net days in accounts receivable increased by 2.7 days to 45.5 days as of September 30, 2017 compared to fiscal year June 30, 2017. Total liabilities of \$12.7 billion decreased \$101.2 million, or 0.8%, primarily due to decreased accounts payable, salaries and wages related liabilities and accrued pension and retiree health costs which included cash funding of \$48.8 million. Debt to capitalization as of September 30, 2017 decreased to a

ratio of 36.0% from 36.9% compared to June 30, 2017 due primarily to an increase in unrestricted net assets of \$429.1 million driven by strong investment returns, other non-operating gains and income from operations.



Statement of Cash Flows

Cash and cash equivalents decreased \$62.7 million during the first quarter of FY2018. Operating activities provided \$127.7 million of cash. Investing activities used \$195.1 million of cash including \$228.9 million for purchases of property and equipment partially offset by \$46.2 million of net proceeds from the sale of investments. Financing activities provided \$4.7 million of cash due primarily to the proceeds from the issuance of debt of \$24.3 million and proceeds from restricted contributions and restricted investment income of \$6.0 million partially offset by repayments of debt of \$25.4 million.

TRINITY HEALTH**Liquidity Reporting**

Summary as of September 30, 2017

	(\$ in millions)
	<u>(unaudited)</u>
ASSETS	
<u>Daily Liquidity</u>	
Money Market Funds (Moody's rated Aaa)	\$ 803
Checking and Deposit Accounts (at P-1 rated bank)	321
Repurchase Agreements	-
U.S. Treasuries & Aaa-rated Agencies	-
Dedicated Bank Lines	<u>931</u>
Subtotal Daily Liquidity (Cash & Securities)	\$ 2,055
Undrawn Portion of \$600M Taxable Commercial Paper Program	<u>500</u>
Subtotal Daily Liquidity Including Taxable Commercial Paper Program	\$ 2,555
<u>Weekly Liquidity</u>	
Exchange Traded Equity	\$ 2,192
Publicly Traded Fixed Income Securities Rated at least Aa3 and Bond Funds	1,383
Equity Funds	954
Other	<u>517</u>
Subtotal Weekly Liquidity	<u>5,046</u>
TOTAL DAILY AND WEEKLY LIQUIDITY	<u><u>\$ 7,601</u></u>
<u>Longer Term Liquidity</u>	
Funds, vehicles, investments that allow withdrawals with less than one month notice	857
Funds, vehicles, investments that allow withdrawals with one month notice or longer	<u>1,645</u>
Total Longer Term Liquidity	<u><u>\$ 2,502</u></u>
LIABILITIES (Self-liquidity Variable Rate Demand Bonds & Commercial Paper)	
<u>Weekly Put Bonds</u>	
VRDO Bonds (7-day)	\$ 321
<u>Long-Mode Put Bonds</u>	
VRDO Bonds (Commercial Paper Mode)	417
<u>Taxable Commercial Paper Outstanding</u>	<u>100</u>
TOTAL SELF-LIQUIDITY DEBT AND COMMERCIAL PAPER	<u><u>\$ 838</u></u>

Trinity Health
Financial Ratios and Statistics (Unaudited)

	September 30, 2017	September 30, 2016
<u>Financial Indicators</u>		
Liquidity Ratios (at September 30)		
Days Cash on Hand	190	180
Days in Accounts Receivable, Net	46	46
Leverage Ratios (at September 30)		
Debt to Capitalization	36%	39%
Cash to Debt	129%	122%
Profitability Ratios (For the Three Months Ended September 30)		
Operating Margin	1.8%	1.0%
Operating Cash Flow Margin	7.9%	7.3%
<u>Statistical Indicators (For the Three Months Ended September 30)</u>		
Rounded to nearest thousand		
Discharges	145,000	145,000
Patient Days	664,000	664,000
Outpatient Visits	4,812,000	4,832,000
Emergency Room Visits	598,000	605,000
<u>Continuing Care</u>		
Home Health Admissions	23,000	23,000
Long-term Care Patient Days	271,000	294,000