CONSOLIDATED FINANCIAL STATEMENTS

CHRISTUS Health System

December 31, 2017

CHRISTUS Health System

Consolidated Financial Statements

December 31, 2017

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CHRISTUS Health

Consolidated Balance Sheet

	December 31, 2017 (unaudited)	June 30, 2017 (audited)
	(in thousands)	
Assets		
Current assets:		
Cash and cash equivalents	$ 524,438	$ 528,259
Short-term investments and equity in managed funds	658,579	586,560
Assets whose use is limited or restricted, required for current liabilities	62,356	58,831
Patient accounts receivable, net of allowance for doubtful accounts	548,648	505,480
Notes and other receivables	208,152	207,012
Inventories	109,702	105,104
Other current assets	112,197	103,142
Total current assets	2,224,072	2,094,388
Assets whose use is limited or restricted, less current portion	679,353	709,925
Property and equipment, net of accumulated depreciation	2,483,210	2,358,676
Other assets:		
Investments in unconsolidated organizations	195,737	150,823
Goodwill and intangible assets, net	161,981	132,668
Beneficial interest in supporting organizations and other restricted assets	88,410	87,730
Other assets, including notes receivable from related party	175,963	202,173
Total other assets	622,091	573,394
Total assets	$ 6,008,726	$ 5,736,383

(Continued)

Consolidated Balance Sheet

	December 31, 2017 (unaudited)	June 30, 2017 (audited)
	(in thousands)	
Liabilities and net assets		
Current liabilities:		
Accounts payable and accrued expenses	$ 580,712	$ 568,881
Accrued employee compensation and benefits	264,733	252,139
Estimated third party settlements, net	56,924	62,782
Current portion of long-term debt	48,037	44,880
Total current liabilities	950,406	928,682
Long-term debt, less current portion	1,231,094	1,117,125
Accrued pension benefits, long-term portion	155,339	170,356
Derivative financial instruments	107,362	116,160
Other long-term obligations – including self-funded liabilities, less current portion	233,897	227,601
Total liabilities	2,678,098	2,559,924
Net assets:		
Unrestricted:		
Attributable to CHRISTUS Health	2,926,474	2,798,703
Attributable to non-controlling interest	210,069	201,855
Temporarily restricted	176,926	159,021
Permanently restricted	17,159	16,880
Total net assets	3,330,628	3,176,459
Total liabilities and net assets	$ 6,008,726	$ 5,736,383

CHRISTUS Health

Consolidated Statements of Operations and Changes in Net Assets

	For the Six Months Ended December 31, 2017 (unaudited)	For the Six Months Ended December 31, 2016 (unaudited)
	(in thousands)	
Revenues:		
Patient service revenue (net of contractual allowance and discounts	$ 2,711,329	$ 2,285,388
Provision for bad debts	(302,565)	(189,322)
Net patient service revenue, less provision for bad debts	2,408,764	2,096,066
Premium revenue	140,071	96,141
Other revenue including gain on contribution to joint ventures	159,433	118,925
Equity in income of unconsolidated organizations	6,228	3,669
Total revenues	2,714,496	2,314,801
Expenses:		
Employee compensation and benefits	1,215,600	1,058,681
Services and other	796,626	708,502
Supplies	460,808	391,790
Depreciation and amortization	113,600	93,211
Interest	25,992	16,228
Total expenses	2,612,626	2,268,412
Operating gain	101,870	46,389
Nonoperating investment gain/(loss)	38,846	65,413
Other nonoperating gain/(loss)	(2,747)	(2,148)
Revenues in excess of expenses	137,969	109,654
Less revenues in excess of expenses attributable to non-controlling interest	18,458	13,261
Revenues in excess/(deficit) of expenses attributable to CHRISTUS Health	$ 119,511	$ 96,393

(Continued)

CHRISTUS Health

Consolidated Statements of Operations and Changes in Net Assets

	For the Six Months Ended	
	December 31, 2017 (unaudited)	December 31, 2016 (unaudited)
	(in thousands)	
Changes in unrestricted net assets:		
Revenues in excess of expenses attributable to CHRISTUS Health	$ 119,511	$ 96,393
Unrealized gain/(loss) on investments	3,797	503
Change in pension liabilities	3,808	2,648
Change in non-controlling interest	8,214	16,150
Net assets released from restrictions for capital and other	655	(10,692)
Changes in unrestricted net assets	135,985	105,002
Temporarily restricted net assets:		
Temporarily restricted net assets acquired	-	-
Net change in beneficial interest	(29)	36
Contributions	15,048	10,019
Unrealized gain/(loss) on investments	349	(39)
Net assets released from restrictions and other	2,537	(9,105)
Changes in temporarily restricted net assets	17,905	911
Permanently restricted net assets:		
Permanently restricted net assets acquired	-	-
Net change in beneficial interest	226	(232)
Other	53	2,522
Changes in permanently restricted net assets	279	2,290
Changes in net assets	154,169	108,203
Net assets – beginning of period	3,176,459	2,931,707
Net assets – end of period	$ 3,330,628	$ 3,039,910

CHRISTUS Health

Consolidated Statement of Cash Flows

	For the Six Months Ended	
	December 31, 2017	December 31, 2016
	(unaudited)	(unaudited)
	(in thousands)	(in thousands)
Operating activities		
Changes in net assets	$ 154,169	$ 108,203
Adjustments to reconcile changes in net assets to net cash provided by (used in) operating activities:		
Net gain on contributions to joint ventures	(36,340)	-
Inherent contribution from business combination	-	(2,078)
Change in beneficial interest	(197)	197
Change in pension liabilities recognized in net assets	(3,808)	(2,648)
Contributions of temporarily restricted net assets	(15,741)	(10,019)
Distributions to and acquisitions of non-controlling interest	-	3,749
Non-controlling interest acquired in business combination	(14,550)	(16,381)
Equity in income of unconsolidated organizations	(6,228)	(3,762)
Unrealized investment loss	8,333	10,292
Depreciation and amortization	113,600	93,211
Amortization of deferred financing costs	566	524
Provision for bad debts	302,565	189,322
Change in derivative fair value	(8,798)	(50,952)
Gain on extinguishment of debt	-	(11,866)
Loss on disposal of property and equipment	1,009	148
Changes in operating assets and liabilities, net of acquisitions:		
Increase in net patient accounts receivable	(344,035)	(225,022)
Decrease (increase) in investments	(53,305)	100,889
(Increase) decrease in notes and other receivables	(1,140)	(63,368)
Increase in other current assets and inventories	(10,410)	(16,236)
Increase (decrease) in accounts payable, accrued expenses, and accrued employee compensation and benefits	23,881	13,349
Increase in net third-party payor settlements	(5,858)	9,448
Decrease in other long term liabilities	(7,156)	(9,979)
Net cash provided by operating activities	$ 96,557	$ 117,021

(Continued)

CHRISTUS Health

Consolidated Statement of Cash Flows

	For the Six Months Ended	
	December 31, 2017	December 31, 2016
	(unaudited)	(unaudited)
	(in thousands)	(in thousands)
Investing activities		
Purchases of property and equipment	$ (209,233)	$ (126,755)
Proceeds from sale or disposal of property and equipment	-	26
Proceeds from sale of majority interest in operating entities	22,346	-
Distributions from investments in unconsolidated organizations	2,246	22,259
Purchases of investments in unconsolidated organizations	(24,428)	(17,110)
Decrease in other assets	22,277	(23,984)
Decrease in security lending collateral	-	-
Acquisitions of health care entities, net of cash acquired	(45,642)	10,065
Net cash used in investing activities	(232,434)	(135,499)
Financing activities		
Contributions of temporarily restricted net assets	15,741	10,019
Costs associated with debt refinancing/conversion	-	-
Proceeds from issuance of new debt	158,676	177,553
Payments on long-term debt	(42,361)	(239,457)
Distributions to and acquisitions of non-controlling interest	-	(3,749)
Net cash used in financing activities	132,056	(55,634)
Net (decrease) increase in cash and cash equivalents	(3,821)	(74,112)
Cash and cash equivalents - beginning of period	528,259	483,664
Cash and cash equivalents - end of period	524,438	409,552
Noncash investing and financing transactions		
Capital lease and debt obligations incurred for property and equipment	224	1,428
Supplemental disclosure of cash flow information		
Cash paid during the period for interest (net of amount capitalized)	$ 17,622	$ 15,213

See accompanying footnotes.

Notes to Consolidated Financial Statements (unaudited)

For the Six Months Ended December 31, 2017

1. Mission, Vision, and Organization of CHRISTUS Health

CHRISTUS Health (CHRISTUS or the System) was incorporated as a Texas nonprofit corporation on December 15, 1998. CHRISTUS is sponsored by the Congregation of the Sisters of Charity of the Incarnate Word of Houston, Texas, and the Congregation of the Sisters of Charity of the Incarnate Word of San Antonio, Texas, and the Congregation of the Sisters of the Holy Family of Nazareth.

The mission of CHRISTUS is to extend the healing ministry of Jesus Christ. The Gospel values underlying the mission statement challenge CHRISTUS to make choices that respond to the economically disadvantaged and the underserved with health care needs. The growth and development of CHRISTUS are determined by the health care needs of the communities that CHRISTUS serves, its available resources, and the interrelationship of those serving and those being served. Responsible stewardship mandates that CHRISTUS searches out new, effective means to deliver quality health care and to promote wholeness in the human person.

The vision of CHRISTUS is to be a leader, a partner, and an advocate in the creation of innovative health and wellness solutions that improve the lives of individuals and communities so that all may experience God's healing presence and love.

The consolidated financial statements of CHRISTUS include activities of its affiliated market-based organizations and other related entities, all of which are wholly or majority-owned or otherwise controlled and commonly referred to as ministries or entities. For purposes of these consolidated financial statements, the System is defined as CHRISTUS' affiliated market-based organizations and other related entities. The other related entities include, but are not limited to, hospital foundations, professional office buildings, management services organizations, physician groups, outpatient surgery centers, diagnostic imaging companies, urgent care centers, a collection agency, self-insurance trusts, an offshore captive insurance company, health plans, and integrated community health networks.

CHRISTUS controls or owns, directly or indirectly, or manages various nonprofit and for-profit corporations and other organizations that currently operate domestically in the states of Texas, Louisiana, New Mexico, and internationally in Grand Cayman, Mexico, Chile and Colombia.

CHRISTUS and certain affiliated nonprofit corporations are generally exempt from federal income taxes under Section 501(a) of the Internal Revenue Code, as organizations described in Section 501(c)(3).

2. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial 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 six months ended December 31, 2017, are not necessarily indicative of the results to be expected for the year ending June 30, 2018. For further information, refer to the audited consolidated financial statements and notes thereto for the year ended June 30, 2017.

Basis of Consolidation

The consolidated financial statements include the accounts of all entities of the System (see Note 1). All significant inter-entity transactions and accounts have been eliminated in consolidation.

3. New and Pending Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, enacting ASC 606, *Revenue from Contracts with Customers*, to clarify the principles for recognizing revenue and to improve financial reporting by creating common revenue recognition guidance for U.S. GAAP and International Financial Reporting Standards (IFRS). The core principle of the new guidance 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. ASU 2014-09 is now effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is permitted. The System is evaluating the guidance in ASU 2014-09 and the impact that the adoption of this update will have on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, enacting ASC 842, *Leases*, which requires a lessee to recognize a right-of-use asset and a lease liability for both operating and finance leases, whereas previous U.S. GAAP required the asset and liability be recognized only for capital leases. The amendment also requires qualitative and specific quantitative disclosures. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, with early adoption permitted. The System is evaluating the guidance of ASU 2016-02. The adoption of this update is expected to result in a significant increase in intangible assets and lease liabilities on the consolidated financial statements.

In August 2016, the FASB issued ASU 2016-14 *Presentation of Financial Statements of Not-for-Profit Entities*, as an update to ASC 958, *Not-for-Profit Entities*. This update makes several improvements to current reporting requirements that address complexities in the use of the currently required three classes of net assets and enhance required disclosures related to donor restrictions of net assets. The updated guidance will be effective for annual periods beginning after December 15, 2017, and interim periods within fiscal years beginning after December 15, 2018. Early adoption is permitted. The new guidance should be applied on a retrospective

3. New and Pending Accounting Pronouncements (continued)

basis. The updated guidance will result in a change in the classes of net assets reported on the face of the statement of financial position from three classes (unrestricted, temporarily restricted, and permanently restricted) to two classes (net assets without donor restrictions and net assets with donor restrictions). No other material impact is expected.

In November 2016, the FASB issued ASU 2016-18, *Restricted Cash*, as an update to ASC 230, *Statement of Cash Flows*. This update requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The updated guidance will be effective for annual periods beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The new guidance should be applied on a retrospective basis. The updated guidance will result in a change in the cash flow statement to include restricted cash and restricted cash equivalents. No other material impact is expected.

In January 2017, the FASB issued ASU 2017-04, *Simplifying the Test for Goodwill Impairment*, as an update to ASC 350, *Intangibles – Goodwill and Other*. This update eliminates step 2 of the goodwill impairment test which required an entity to determine the fair value of individual assets and liabilities of the reporting unit. Under this updated guidance, the impairment amount will be determined using the step 1 comparison of fair value to carrying value. The updated guidance will be effective for the annual and any interim goodwill impairment tests in fiscal years beginning after December 15, 2020. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The adoption of the guidance is not expected to have a material impact to the System's consolidated financial statements.

In March 2017, the FASB issued ASU 2017-07, *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. This update changes the presentation requirements of net period pension and postretirement benefit costs in the statement of operations by requiring the service cost component to be presented as part of compensation expense, and the remaining components to be presented separately from the service cost component and outside a subtotal of income from operations. The updated guidance is effective for annual periods beginning after December 15, 2017, including interim periods within those years, and is required to be applied retrospectively. Early adoption is permitted. The updated guidance will affect the classification of expense within the System's statement of operations and no other material impact is expected.

4. Fair Value Measurements

The three-level valuation hierarchy for disclosure of fair value measurements is based on the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 – Inputs to the valuation methodology are quoted market prices (unadjusted) for identical assets or liabilities at the reporting date.
- Level 2 – Inputs to the valuation methodology other than quoted market prices included in Level 1 that are observable for the asset or liability. Level 2 pricing inputs include quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 – Inputs that are generally unobservable and typically reflect management's estimate of assumptions that market participants would use in pricing the asset or liability.

A financial instrument's categorization within the valuation hierarchy is based on the lowest level of input that is significant to the fair value measurement. There were no materially significant transfers between levels during the six months ended December 31, 2017.

The following tables present the financial instruments carried at fair value as of December 31, 2017, and June 30, 2017, (in thousands) by the valuation hierarchy (as described above):

4. Fair Value Measurements (continued)

December 31, 2017

	Level 1	Level 2	Level 3	Total
Assets				
Investments:				
Cash and cash equivalents	$ 629,173	$ –	$ –	$ 629,173
Certificates of deposit	–	26,933	–	26,933
Domestic equities	94,457	–	–	94,457
International equities	24,481	–	–	24,481
Fixed-income securities	–	198,950	–	198,950
U.S. government securities	–	342,936	–	342,936
Mutual and exchange-traded funds:				
Domestic equity funds	40,803	–	–	40,803
International equity funds	33,473	–	–	33,473
Fixed income funds	73,008	–	–	73,008
Risk parity, blended and other funds	22,356	–	–	22,356
	$ 917,751	$ 568,819	$ –	$ 1,486,570
Investments measured at net asset value or equivalent:				
Equity funds				9,746
Fixed-income funds				90,837
Hedge funds				50,868
Private equity, real estate and other funds				21,600
Total assets at fair value				$ 1,659,621
Liabilities				
Interest rate swap agreements	$ –	$ 107,362	$ –	$ 107,362
Total liabilities at fair value	$ –	$ 107,362	$ –	$ 107,362

4. Fair Value Measurements (continued)

June 30, 2017

	Level 1	Level 2	Level 3	Total
Assets				
Investments:				
Cash and cash equivalents	$ 710,707	$ –	$ –	$ 710,707
Certificates of deposit	–	30,304	–	30,304
Domestic equities	79,165	–	–	79,165
International equities	20,873	–	–	20,873
Fixed-income securities	–	118,663	–	118,663
U.S. government securities	–	270,565	–	270,565
Mutual and exchange-traded funds:				
Domestic equity funds	35,560	–	–	35,560
International equity funds	36,847	–	–	36,847
Fixed income funds	86,745	–	–	86,745
Risk parity, blended and other funds	16,016	–	–	16,016
	$ 985,913	$ 419,532	$ –	$ 1,405,445
Investments measured at net asset value or equivalent:				
Equity funds				14,039
Fixed-income funds				109,758
Hedge funds				49,667
Private equity, real estate and other funds				10,643
Total assets at fair value				$ 1,589,552
Liabilities				
Interest rate swap agreements	$ –	$ 116,160	$ –	$ 116,160
Total liabilities at fair value	$ –	$ 116,160	$ –	$ 116,160

Investments measured at fair value using net asset value per share or its equivalent as a practical expedient, as permitted by ASC 820-10, have not been categorized within the fair value hierarchy in the tables above.

The tables above include equity investments in managed funds held within the System's foundations and captive insurer. Remaining equity investments in managed funds held by other System entities of $265,104,000 and $294,023,000 at December 31, 2017 and June 30, 2017, respectively, are not included in this table since they are accounted for using the equity method of accounting.

4. Fair Value Measurements (continued)

The valuation methodologies used for instruments measured at fair value as presented in the tables above are as follows:

- *Investments* – Investments valued at quoted prices available in an active market are classified within Level 1 of the valuation hierarchy. Investments valued based on evaluated bid prices provided by third-party pricing services, where quoted market prices are not available, are classified within Level 2 of the valuation hierarchy. Investments measured at fair value using net asset value per share or its equivalent as a practical expedient are not categorized within the fair value hierarchy. These investments consist of hedge funds, commodity funds, common collective trust funds, private equity funds, and real estate funds.

- *Interest rate swap agreements* – Interest rate swap agreements are valued using third-party models that use observable market conditions as their input and are classified within Level 2 of the valuation hierarchy.

At December 31, 2017 and June 30, 2017, the System's financial instruments included cash and cash equivalents, accounts receivable, assets limited as to use, accounts payable and accrued expenses, estimated third-party payor settlements, and long-term debt. The carrying amounts reported in the consolidated balance sheets for these financial instruments, except for long-term debt, approximate their fair values due to their short-term nature.

Some of the System's fixed-rate debt is enhanced with bond insurance. The estimated fair value of the fixed-rate debt, if it were not enhanced by insurance, approximates $469,652,000 compared to its carrying value of $453,795,000 at December 31, 2017. This fair value is based on a combination of quoted market prices for identical securities when available, a Level 1 input, and quoted market prices for similarly rated health care revenue bond issues, a Level 2 input.

At December 31, 2017, the System has several issues of variable-rate demand bonds outstanding. The System's continued participation in these debt programs depends on its ability to extend or replace the existing credit facilities supporting the respective standby purchase agreements. If these credit facilities are not available, the System will likely refund these outstanding series with available funds or funds derived from fixed-rate series proceeds. It is not practicable to estimate the fair value of the variable-rate demand bonds separate from the value supported by the credit facilities.

5. Investments in Unconsolidated Organizations

The System has investments in unconsolidated organizations of $195,737,000 and $150,823,000 at December 31, 2017 and June 30, 2017, respectively. The following investments account for 91% of the System's total investments in unconsolidated organizations at both December 31, 2017 and June 30, 2017:

5. Investments in Unconsolidated Organizations (continued)

Salud U.C. SpA

On January 31, 2014, CHRISTUS Chile SpA, a wholly-owned Chilean corporation, obtained a 40% non-controlling interest through the purchase of shares of Salud U.C. SpA (Salud U.C.) from Pontifica Universidad Catolica de Chile (PUC) for cash consideration of $20,878,000. As part of the reorganization described more fully in Note 9, PUC refunded $10,000,000 of the purchase price in 2016. During fiscal years 2017 and 2016, CHRISTUS made additional capital contributions of $2,838,000 and $836,000, respectively. CHRISTUS' recorded investment, accounted for under the equity method, was $13,269,000 and $13,278,000 at December 31, 2017 and June 30, 2017, respectively. The System's share of (losses) earnings for the six months ended December 31, 2017 and 2016 was $(9,000) and $58,000, respectively. There is additional discussion of the System's international operations in Note 9.

Inversiones San Carlos, SpA

In May 2014, CHRISTUS Chile Limitada, a wholly-owned Chilean subsidiary of CHRISTUS Chile, SpA, purchased 100% of the shares of Inversiones San Carlos, SpA, a Chilean corporation, from Colmena Salud S.A. for cash consideration of $68,000,000. Inversiones San Carlos SpA owns 50% interest in Servicios Clinicos San Carlos de Apoguindo S.A. and Immobiliaria Clinica San Carlos de Apoguindo S.A. (jointly referred to as "San Carlos"). On both September 27, 2017 and July 15, 2016, CHRISTUS made additional contributions of $14,560,000 each as part of a series of transactions outlined under new agreements with PUC signed in May 2016. CHRISTUS' recorded investment, accounted for under the equity method, was $96,894,000 and $82,114,000 at December 31, 2017 and June 30, 2017, respectively. The System's share of earnings (losses) for the six months ended December 31, 2017 and 2016 was $220,000 and $(197,000), respectively. There is additional discussion of the System's international operations in Note 9.

Coomeva Cooperativa Medica

Effective June 14, 2016, CHRISTUS signed definitive agreements with Cooperativa Medica del Valle y de Profesionales de Colombia (Coomeva) in Colombia. In September 2016, CHRISTUS closed on various transactions outlined in the definitive agreements and paid $22,198,000 to obtain a non-controlling ownership interest in various Coomeva companies. In September 2017 and March 2017, CHRISTUS paid an additional $9,231,000 and $5,087,000, respectively, to increase its ownership interest in these companies. At December 31, 2017 and June 30, 2017, CHRISTUS owned an equity interest of 50.0% and 31.25%, respectively, in and management of Sinergia Global en Salud SAS (Sinergia), a health care provider network including two hospitals, the largest home care company in the country and ambulatory facilities in nearly every community in Colombia. CHRISTUS also owns a 10% equity interest in Coomeva Medicina Prepagada (MP), a private health insurance company that contracts with individuals and employers to provide private health insurance nationwide.

The System's investment in Sinergia is accounted for under the equity method of accounting because CHRISTUS can exercise significant influence over the operations of Sinergia. The System's investment in MP is accounted for under the cost method because CHRISTUS does not exercise significant influence over MP's operations. The System's total investment was

5. Investments in Unconsolidated Organizations (continued)

$35,507,000 and $26,872,000 at December 31, 2017 and June 30, 2017, respectively. The System recorded its share of losses from the operations of Sinergia during the six months ended December 31, 2017 and 2016 of $(596,000) and $(111,000), respectively. There were no dividends received from MP during the six months ended December 31, 2017 or 2016.

Southwest Post-Acute Care Partnership

Effective September 1, 2017, CHRISTUS Continuing Care contributed substantially all of the assets of its long-term acute care hospitals (LTAC) and home care business to a newly formed entity, Southwest Post-Acute Care Partnership, LLC (Southwest Partnership), in exchange for cash proceeds and a 40% non-controlling interest in Southwest Partnership. The System recorded a gain on the transaction of $36,340,000, equal to the fair value of the cash proceeds and non-controlling interest in Southwest Partnership, less the carrying value of the contributed assets, and which is recorded as other revenue including gain on contribution to joint ventures in the accompanying consolidated financial statements. The System's recorded investment was $15,037,000 at December 31, 2017. The System recorded its share of losses from operations during the six months ended December 31, 2017 of $(992,000).

HealthSouth Rehabilitation Hospital

CHRISTUS Trinity Mother Frances Health System owns 50% of HealthSouth Rehabilitation Hospital – Tyler d/b/a/ Trinity Mother Frances Rehabilitation Hospital (HealthSouth). Because CHRISTUS can exercise significant influence over the operations of HealthSouth, but does not control HealthSouth, this investment is accounted for using the equity method of accounting. The System's recorded investment was $10,549,000 and $7,803,000 at December 31, 2017 and June 30, 2017, respectively. The System recorded its share of income from operations during the six months ended December 31, 2017 and 2016 of $2,746,000 and $1,913,000, respectively.

CS/USP Surgery Centers, L.P.

CHRISTUS Spohn Health System Corporation has a 50% ownership interest in a Texas limited liability partnership with United Surgical Partners International, Inc. for the purpose of owning and operating ambulatory surgery centers in Corpus Christi, Texas. The venture consists of two surgery centers near the campus of Spohn Shoreline, Corpus Christi Outpatient Surgery and SurgiCare, and one endoscopy center. CHRISTUS recorded investment, accounted for under the equity method, was $6,881,000 and $7,064,000 at December 31, 2017 and June 30, 2017, respectively. The System recorded its share of income from operations during the six months ended December 31, 2017 and 2016 of $496,000 and $556,000, respectively.

CHRISTUS and its affiliates hold immaterial investments in other unconsolidated subsidiaries. No single investment balance exceeded $5,000,000 at both December 31, 2017, and June 30, 2017, respectively.

6. Derivative Financial Instruments

Interest rate swap contracts between the System and third parties (counterparties) provide for the periodic exchange of payments between the parties based on either changes in a defined index or changes in a defined index and a fixed rate. These swaps expose the System to market risk and credit risk. Credit risk is the risk that contractual obligations of the counterparties will not be fulfilled. Concentrations of credit risk relate to groups of counterparties that have similar economic or industry characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. Counterparty credit risk is managed by requiring high credit standards for the System's counterparties. The counterparties to these contracts are financial institutions that carry investment-grade credit ratings.

Market risk is the adverse effect on the value of a financial instrument that results from a change in interest rates. The market risk associated with interest rate changes is managed by establishing and monitoring parameters that limit the types and degrees of market risk that may be undertaken. Management also mitigates risk through periodic reviews of their derivative positions in the context of their blended cost of capital. CHRISTUS has interest rate swap agreements to manage interest rate risk exposure, not designated as hedging instruments, with a total notional amount of $912,035,000 at December 31, 2017, and $921,035,000 at June 30, 2017, respectively.

The following table summarizes the fair value at December 31, 2017 and June 30, 2017, and the income (loss) recorded related to the interest rate swap agreements as of and for the six months ended December 31, 2017, and 2016 (in thousands).

Counterparty	Description	Termination Date	Interest Rate Agreements	Notional Amount	Fair Value		Change in Value		(Paid)/Received	
					12/31/2017	6/30/2017	12/31/2017	12/31/2016	12/31/2017	12/31/2016
Merrill Lynch	Var. Basis	2021-2023	6	470,000	$785	($420)	$1,205	($1,678)	$158	($435)
Wells Fargo	Fixed Payer	2031	1	162,775 / 171,775	(17,627)	(20,671)	3,044	10,442	(1,917)	(2,437)
Citigroup*	Fixed Payor	2047	2	166,100	(54,094)	(56,818)	2,724	25,086	(2,176)	(2,558)
Citigroup*	Fixed Payor	2047	1	113,160	(36,426)	(38,251)	1,825	17,101	(1,463)	(1,723)
			10	912,035 / 921,035	($107,362)	($116,160)	$8,798	$50,951	($5,398)	($7,153)

*Insured by MBIA

CHRISTUS is required to post collateral for negative valuations on each of its swaps according to the terms of (i) the swap insurance agreements, where applicable and (ii) the agreement with each counterparty. CHRISTUS has complied with this requirement. At December 31, 2017, and June 30, 2017, no collateral was posted. The System does not anticipate nonperformance by its counterparties.

The fair value of these swap agreements was a liability of $107,362,000 and $116,160,000 at December 31, 2017, and June 30, 2017, respectively. The fair value increased by $8,798,000 during the six months ended December 31, 2017, and increased by $50,591,000 during same period of the prior fiscal year. The changes in value are combined with the payments, net of receipts, made under the agreements. These payments, net of receipts, were $5,398,000 and $7,153,000 for the six months ended December 31, 2017 and 2016, respectively. This total is included in nonoperating investment gain (loss) in the statements of operations and changes in net assets.

6. Derivative Financial Instruments (continued)

CHRISTUS currently voluntarily posts, on a quarterly basis, selected information relating to its outstanding interest rate swap transactions on the Municipal Securities Rulemaking Board's (MSRB) Electronic Municipal Market Access system (EMMA). No assurances can be given that CHRISTUS Health will continue to post such information in the future.

7. Employee Benefit Plans

Defined Benefit Plans

Cash Balance Plan

The System has established a non-contributory, defined benefit retirement plan that operates as a cash balance plan and covers substantially all CHRISTUS employees who had met age and service requirements as of December 31, 2012. On October 23, 2012, the CHRISTUS board approved the closing of the plan to new participants, effective January 1, 2013.

The plan benefits are calculated based on a cash balance formula wherein participants earn an annual accrual based on compensation, and participant account balances accrue interest at a rate that tracks ten-year treasury notes; the maximum rate is 8%.

Mother Frances Hospital Defined Benefit Pension Plan

In connection with the acquisition of Trinity Mother Frances Health System, effective May 1, 2016, the System acquired the assets and obligations of the Mother Frances Hospital Defined Benefit Pension Plan (TMF Plan). The TMF Plan covers all employees who meet the eligibility requirements. The Plan was frozen as of December 31, 2009.

The measurement date for the cash balance plan and the TMF Plan (collectively, the Defined Benefit Plans) is June 30. Components of net periodic benefit cost, recorded as a component of employee compensation and benefits, for the six months ended December 31, 2017, consisted of the following (in thousands):

	Cash Balance Plan 12/31/17 (unaudited)	**TMF Plan 12/31/17 (unaudited)**
Service cost	**$ 8,146**	**$ –**
Interest cost	**14,520**	**3,419**
Expected return on assets	**(24,488)**	**(3,899)**
Amortization of prior service credit	**(5,942)**	**–**
Recognized net actuarial loss	**9,732**	**–**
Settlement credit	**–**	**(3,457)**
Net benefit cost (credit)	**$ 1,968**	**$ (3,937)**

7. Employee Benefit Plans (continued)

In fiscal year 2018, CHRISTUS expects to contribute $18,600,000 to the Defined Benefit Plans based on asset values for the plan year beginning January 1, 2017. Contributions to the cash balance plan of $13,500,000 were made during fiscal year 2017 for the plan year beginning January 1, 2017, and contributions to the TMF Plan of $9,000,000 were made during fiscal year 2017. The funded status of the Defined Benefit Plans was $153,788,000 and $168,864,000 at December 31, 2017 and June 30, 2017, respectively, which is included in accrued pension benefits on the accompanying consolidated balance sheets.

Postretirement Health Care Benefits

Comprehensive medical benefits are provided to eligible active employees who, immediately upon retirement and attainment of the age of 55, will receive a pension under the CHRISTUS retirement plan. Postretirement benefits are also provided to former employees who are currently receiving pension benefits. The comprehensive medical program, which is self-insured, provides reimbursement benefits until the participant attains the age of 65. The program also covers dependents of retirees, in addition to former employees. Contributions are required. Retirees may choose one of two self-insured indemnity plan options. Effective February 1, 1999, the CHRISTUS postretirement benefit plan was curtailed prospectively. As of the effective date, new employees or employees who had not vested as of that date are not eligible for the postretirement health care benefits. Effective January 1, 2016, the plan was amended to limit new participants to associates over the age of 52, who otherwise meet the eligibility requirements and elect to retire prior to December 31, 2018. Coverage for new participants is in the form of a subsidy for each retiree and qualifying dependents. The liability associated with the postretirement plan will be reduced as employee participation decreases. Net benefit credit under the postretirement plan was $(1,718,000) and $(2,794,000) for the six months ended December 31, 2017 and 2016. The net benefit obligation was $10,404,000 and $12,089,000 at December 31, 2017 and June 30, 2017, respectively, which is included in accrued other long-term liabilities on the accompanying balance sheets. The postretirement plan is unfunded.

Other defined benefit plans

In addition to the Defined Benefit Plans, CHRISTUS also participates in various defined benefit plans for executives that have been frozen or curtailed. The net benefit cost under these plans was $64,000 and $40,000 for the six months ended December 31, 2017 and 2016, respectively. The net benefit obligation was $5,274,000 and $5,977,000 at December 31, 2017 and June 30, 2017, respectively. These plans are unfunded.

8. Commitments and Contingencies

Other Contingencies

From time to time, the System is subject to litigation in the ordinary course of operations. In management's opinion, any future settlements or judgments on asserted or unasserted claims will not have a material effect on the System's consolidated financial statements.

8. Commitments and Contingencies (continued)

The System has a compliance program and various internal policies and procedures that management believes will effectively reduce exposure for violations of applicable federal and state health care laws, regulations, and policies. There are matters that may be the subject of reporting to appropriate regulatory authorities or payors, and subject to repayment obligations, recoupments, penalties, and/or fines. There are a number of voluntary and other reviews that may also result in disclosure and/or repayments. There are also matters in which government agencies are pursuing matters directly with CHRISTUS Health and/or its affiliates.

Because the government's present regulatory and enforcement efforts are widespread across the health care industry and may vary from region to region, the impact of such activities on the System is difficult to predict with certainty. The dynamic regulatory environment, political climate, and the effectiveness of our compliance efforts could affect the resolution of regulatory, enforcement and payor issues involving the System. The System has implemented, and is continually endeavoring to enhance, various procedures to ensure continued compliance with federal and state requirements. However, there can be no assurance that the compliance program or other measures will always reduce or completely eliminate the System's civil, criminal, regulatory, or payor exposure.

9. International Operations

CHRISTUS Muguerza

At December 31, 2017, the System owned an 85.6% interest in CHRISTUS Muguerza, S.A. de C.V. (CHRISTUS Muguerza), headquartered in Monterrey, Mexico. CHRISTUS Muguerza is a private health care system and is subject to taxes in accordance with the regulations of the Republic of Mexico. The financial statements of CHRISTUS Muguerza are presented in accordance with accounting principles generally accepted in the United States and are consolidated in the CHRISTUS consolidated financial statements. CHRISTUS Muguerza has net assets of $114,693,000 and $112,127,000 at December 31, 2017 and June 30, 2017, respectively.

In November 2012, the System and certain non-controlling interest holders entered into a revised shareholders' agreement, whereby the non-controlling interest holders of CHRISTUS Muguerza have a series of put options through December 31, 2028. These options will require the System to acquire shares, subject to an annual cap of either $3,500,000 or $2,000,000, depending on the year, at a formula price as defined. At both December 31, 2017 and June 30, 2017, the System had $5,507,000 recorded as unrestricted net assets attributable to non-controlling interest to reflect such obligation to the non-controlling interest holders in connection with the agreement.

CHRISTUS Chile SpA

CHRISTUS signed a memorandum of understanding (MOU) with Pontificia Universidad Católica de Chile (PUC) in Santiago, Chile, to enter into a joint venture agreement for the ownership, operation, and expansion of PUC's health network. PUC is owned by the Catholic Church and operates one of the largest health systems in Chile for medical care and teaching. The System anticipates achieving the structure outlined in the MOU through a series of transactions.

9. International Operations (continued)

CHRISTUS and PUC have entered into certain transactions as described below, and are currently undergoing due diligence and negotiations of such transactions.

In January 2014, under the terms of the MOU, CHRISTUS Chile SpA purchased a 40% interest in Salud U.C. from PUC for $20,878,000. Salud U.C. had an existing 0.74% interest in Centro Medico Monsenor Carlos Casanueva S.A., a 60% interest in Clinica UC S.A., and a 50% interest in both Servicos Clinicos San Carlos Apoquindo S.A. and Inmobilaria Clinicos San Carlos Apoquindo S.A. (collectively referred to as San Carlos).

In May 2014, CHRISTUS Chile Limitada, a wholly-owned Chilean subsidiary of CHRISTUS Chile SpA, purchased 100% of the shares of Inversiones San Carlos, SpA, a Chilean corporation, from Colmena Salud S.A. for cash consideration of $68,000,000. Inversiones San Carlos SpA owned a 50% interest in San Carlos, of which Salud U.C. was also a 50% owner.

Effective July 31, 2015, CHRISTUS and PUC completed a transaction to reorganize Salud U.C. into two separate entities. The first entity holds the 50% interest in San Carlos and is 100% owned by PUC. The second entity, Inversiones UC CH SpA (Inversiones UC), holds the remaining assets of Salud U.C. and is owned 60% by PUC and 40% by CHRISTUS. In consideration for this reorganization, PUC agreed to refund $10,000,000 of the original purchase price of $20,878,000 to CHRISTUS.

Effective October 1, 2015, CHRISTUS and PUC also completed a transaction to reorganize the San Carlos operations into one joint venture entity, Clinica San Carlos de Apoquindo SpA (Clinica San Carlos), which is owned 50% by CHRISTUS and 50% by PUC. Since CHRISTUS and PUC each had a 50% interest in the San Carlos operations both before and after this restructuring, no payments were made in connection with this transaction.

In May 2016, CHRISTUS and PUC executed several agreements, including a shareholders' agreement and an integration agreement (the PUC Agreements), that modify and finalize the specific terms and legal structure of the joint venture arrangement originally contemplated in the MOU. The PUC Agreements outline the timing of when specific assets and additional capital contributions will be made to Inversiones UC and Clinica San Carlos, which will occur in three closings. The first closing took place on July 15, 2016, at which time CHRISTUS made additional investments of $14,560,000 to Clinica San Carlos and $2,838,000 to Inversiones UC. The second closing took place on September 27, 2017, at which time CHRISTUS made an additional investment of $14,560,000 to Clinica San Carlos. The final closing is expected to occur prior to March 31, 2018. Under the terms of the PUC Agreements, CHRISTUS is expected to make additional capital contributions to Inversiones UC or Clinica San Carlos at each of the three closings. The specific amounts of capital contributions may vary but are expected to be no less than $119,940,000. The investments in Inversiones UC and Clinica San Carlos are treated as equity method investments. Discussion of the investments and earnings are in Note 5.

In fiscal year 2015, Amatista Financing, Ltd (Amatista), a wholly-owned subsidiary of CHRISTUS, executed a Loan Agreement with PUC, a related party, and during 2015 loaned PUC $30,000,000 under the terms of that agreement. The note carried a one-year maturity date, which

9. International Operations (continued)

was subsequently extended to April 2016. Under the terms of the PUC Agreements, repayment of this note is one of the various transactions expected to occur at the third closing.

The interest rate on the note is 3.35% per annum. In July 2016, in connection with the initial closing under the PUC Agreements discussed above, Amatista executed two new loans with PUC for $20,000,000 and $8,370,000. In August 2017, Amatista executed a new loan with PUC for $7,228,000 (collectively, the PUC Loans). At December 31, 2017 and June 30, 2017, accrued interest related to the PUC Loans was $3,703,000 and $3,411,000, respectively. Certain of the PUC Loans are convertible into additional capital contributions as outlined in the PUC Agreements. The PUC Loans are reported within other noncurrent assets in the accompanying consolidated balance sheets.

Concurrently with the execution of the PUC Agreements, CHRISTUS and PUC executed a management agreement, under which CHRISTUS provides management services to PUC's primary hospital. CHRISTUS and Clinica San Carlos also entered into a management agreement under which CHRISTUS provides management services to all of the San Carlos operations. The initial term of both management agreements is 25 years. CHRISTUS recorded other revenue related to the management agreements of $5,220,000 and $4,913,000 during the six months ended September 2017 and 2016, respectively.

10. Significant Events

Acquisition of Lake Area Medical Center

Effective July 1, 2017, CHRISTUS closed on a transaction with Community Health Systems, Inc. (CHS), in which CHRISTUS paid approximately $30,000,000 to acquire Lake Area Medical Center (LAMC). LAMC is a full-service acute care hospital located in Lake Charles, Louisiana. The purchase price is subject to certain working capital and other adjustments. The transaction has been accounted for as an acquisition, for which the purchase price allocation had not yet been finalized as of December 31, 2017. During the six months ended December 31, 2017, CHRISTUS recorded provisional amounts for the assets acquired and liabilities assumed, which resulted in immaterial goodwill or inherent contribution. CHRISTUS expects to finalize the purchase price allocation during the third quarter of 2018.

Acquisition of Imperial Calcasieu Surgical Center

Effective August 1, 2017, CHRISTUS closed on a transaction with Imperial Calcasieu Surgery Center, LLC (ICSC), in which CHRISTUS paid approximately $20,090,000 to acquire a 51% majority ownership in ICSC, an outpatient surgical center, and land previously owned by ICSC. The transaction has been accounted for as an acquisition, for which the purchase price allocation had not yet been finalized as of December 31, 2017. During the six months ended December 31, 2017, CHRISTUS recorded provisional amounts for the assets acquired and liabilities assumed, which resulted in the recognition of goodwill related to the acquisition of approximately $27,262,000. CHRISTUS expects to finalize the purchase price allocation during the third quarter of 2018.

10. Significant Events (continued)

Hurricane Harvey

In August 2017, various hospitals and other physical structures in the CHRISTUS Spohn, CHRISTUS Southeast Texas, CHRISTUS Gulf Coast, and CHRISTUS Louisiana Regions sustained damage from Hurricane Harvey resulting in property damage and business interruption. CHRISTUS is in the process of estimating total damages sustained as a result of this event though they are not expected to have a material impact to the System's consolidated financial statements. CHRISTUS maintains property and business interruption insurance coverage through independent property and casualty companies. Additionally, CHRISTUS has self-insured property and casualty losses at the individual facility level through a wholly-owned captive insurance company, Emerald Assurance.

Sale of Controlling Interest in Long Term Acute Care

On August 1, 2017, CHRISTUS Continuing Care executed an asset contribution agreement, under which CHRISTUS contributed substantially all of the assets of its long-term acute care hospitals (LTAC) to a newly formed entity, Southwest Post-Acute Care Partnership, LLC (Southwest Partnership), in exchange for $4,506,000 cash proceeds and a 7.28% non-controlling interest in Southwest Partnership. The transaction closed on September 1, 2017. As of December 31, 2017, CHRISTUS has recorded a preliminary gain from the sale of $3,436,000, subject to certain working capital and other adjustments.

Sale of Controlling Interest in Home Care

On August 1, 2017, CHRISTUS Continuing Care executed an asset contribution agreement, under which CHRISTUS contributed substantially all of the assets of its home care business to Southwest Partnership in exchange for $20,250,000 cash proceeds and a 32.72% non-controlling interest in Southwest Partnership. The transaction closed on September 1, 2017. As of December 31, 2017, CHRISTUS has recorded a preliminary gain from the sale of $32,904,000, subject to certain working capital and other adjustments.