MedStar Health

Fiscal 2019

Quarterly Financial Report

Three Months and Six Months Ended December 31, 2018

Notice to Readers

The quarterly financial reports of MedStar Health, Inc. (MedStar) are intended to reasonably reflect the financial condition of MedStar as of the end of each quarter of the fiscal year. **THE QUARTERLY REPORTS ARE NOT BASED UPON AUDITED FINANCIAL INFORMATION.** Each quarterly report includes all known adjustments to present a fair statement of MedStar's results of operations, financial position and cash flows at the end of the quarter. While MedStar makes reasonable good faith efforts to prepare these reports to reflect the financial condition at the end of each quarter, the reader must be aware that there may be subsequent adjustments made at the end of the fiscal year, including any adjustments made during MedStar's annual audit, that relate back to prior quarters. Certain of the discussions included in the Management Discussion and Analysis of Financial Condition and Results of Operations section of the quarterly report may include "forward-looking statements" which involve known and unknown risks and uncertainties inherent in the operation of healthcare facilities. In particular, statements preceded by, followed by or that include the words "expected," "anticipated," or "possible" or other similar expressions are or may constitute forward-looking statements. No information or statement in this report is intended to suggest or guarantee any future performance or results in future quarters. MedStar does not intend to update any forward-looking statements and undertakes no duty to any person to provide any such update under any circumstances. These financial statements also include a comparison to budget. The budget was prepared by management as a management tool and not as a prediction of actual performance. The budget is based on numerous assumptions which will vary from actual circumstances, developments in healthcare regulation and other applicable factors.

Any questions concerning MedStar's quarterly financial report should be addressed to: Susan K. Nelson, Executive Vice President and Chief Financial Officer, MedStar Health, Inc., 10980 Grantchester Way, Columbia, Maryland 21044.

MedStar Health, Inc.

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MedStar Health, Inc.

Consolidated Statements of Operations and Changes in Net Assets
For the Three Months and Six Months Ended December 31, 2018 and 2017

(Dollars in millions)

	Three Months Ended December 31,			Six Months Ended December 31,		
	2018 Actual	2018 Budget	2017 Actual	2018 Actual	2018 Budget	2017 Actual
Operating revenues:						
Net patient service revenue	$1,229.3	$1,219.0	$1,187.3	$2,408.2	$2,423.2	$2,301.9
Premium revenue	143.7	139.9	142.7	283.6	280.1	363.1
Other operating revenue	53.5	55.9	64.2	104.1	108.4	113.2
Net operating revenues	**1,426.5**	**1,414.8**	**1,394.2**	**2,795.9**	**2,811.7**	**2,778.2**
Operating expenses:						
Personnel	810.6	790.3	774.3	1,580.1	1,565.6	1,509.3
Supplies	211.2	206.3	203.3	414.9	409.2	392.7
Purchased services	194.6	198.3	207.9	382.9	396.9	447.5
Other operating	122.0	129.6	118.6	239.2	258.6	242.4
Interest expense	11.8	12.1	11.5	23.5	24.2	22.8
Depreciation and amortization	52.4	54.5	52.5	103.3	108.0	104.9
Total operating expenses	**1,402.6**	**1,391.1**	**1,368.1**	**2,743.9**	**2,762.5**	**2,719.6**
Earnings from operations	**23.9**	**23.7**	**26.1**	**52.0**	**49.2**	**58.6**
Non-operating (losses) gains:						
Investment income	8.5	6.9	5.8	14.4	13.9	10.4
Net realized (losses) gains on sale of investments	(0.3)	5.7	17.0	4.7	11.4	24.6
Unrealized (losses) gains on derivative instruments	(0.6)	-	0.9	0.1	-	1.4
Unrealized (losses) gains on investments	(172.4)	13.3	31.1	(150.2)	26.7	83.1
Other	(5.1)	(3.3)	(3.2)	(8.5)	(6.8)	(6.6)
Total non-operating (losses) gains	**(169.9)**	**22.6**	**51.6**	**(139.5)**	**45.2**	**112.9**
(Deficiency) excess of revenue over expenses	**($146.0)**	**$46.3**	**$77.7**	**($87.5)**	**$94.4**	**$171.5**

MedStar Health, Inc.

Consolidated Statements of Operations and Changes in Net Assets
For the Three Months and Six Months Ended December 31, 2018 and 2017

(Dollars in millions)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2018	**2017**	**2018**	**2017**
Unrestricted net assets:				
(Deficiency) excess of revenue over expenses	($146.0)	$77.7	($87.5)	$171.5
Distributions to noncontrolling interests	(1.5)	-	(1.5)	-
Net assets released from restrictions used for purchase of property and equipment	2.5	0.9	3.7	1.8
(Decrease) increase in unrestricted net assets	**(145.0)**	**78.6**	**(85.3)**	**173.3**
Temporarily restricted net assets:				
Contributions	3.1	8.2	9.9	9.1
Realized net gains on restricted investments	0.2	0.6	0.4	1.0
Change in unrealized (losses) gains on investments	(4.1)	0.7	(3.6)	2.0
(Decrease) increase in net assets of foundation	(7.6)	2.0	(5.5)	3.5
Net assets released from restrictions	(3.6)	(2.7)	(5.6)	(5.6)
(Decrease) increase in temporarily restricted net assets	**(12.0)**	**8.8**	**(4.4)**	**10.0**
Permanently restricted net assets:				
Contributions	0.6	-	0.7	-
Net realized gains on investments	0.1	0.1	0.1	0.2
Change in unrealized (losses) gains on investments	(0.7)	0.2	(0.6)	0.4
Increase in permanently restricted net assets	-	**0.3**	**0.2**	**0.6**
(Decrease) increase in net assets	**(157.0)**	**87.7**	**(89.5)**	**183.9**
Net assets, beginning of period	**2,062.4**	**1,766.5**	**1,994.9**	**1,670.3**
Net assets, end of period	**$1,905.4**	**$1,854.2**	**$1,905.4**	**$1,854.2**

MedStar Health, Inc.

Consolidated Balance Sheets
As of December 31, 2018, June 30, 2018, and December 31, 2017

(Dollars in millions)

	December 31, 2018	June 30, 2018	December 31, 2017
Assets			
Current assets:			
Cash and cash equivalents	$631.7	$692.6	$662.6
Investments	107.6	162.7	33.4
Assets whose use is limited or restricted	64.3	64.3	61.9
	803.6	919.6	757.9
Receivables:			
Net patient account receivables	668.3	651.5	638.4
Other	85.7	88.5	96.2
	754.0	740.0	734.6
Inventories	67.7	67.1	67.9
Prepaids and other current assets	68.4	53.2	57.2
Total current assets	**1,693.7**	**1,779.9**	**1,617.6**
Investments, net of current portion	1,100.8	1,077.2	1,196.1
Assets whose use is limited or restricted, net of current portion	885.4	938.1	960.2
	1,986.2	2,015.3	2,156.3
Property and equipment, net	1,343.2	1,321.0	1,295.8
Goodwill and other intangibles, net	377.9	380.9	382.1
Interest in net assets of foundation	57.0	62.5	62.8
Other assets	130.5	129.9	116.1
Total assets	**$5,588.5**	**$5,689.5**	**$5,630.7**

MedStar Health, Inc.

Consolidated Balance Sheets
As of December 31, 2018, June 30, 2018, and December 31, 2017

(Dollars in millions)

	December 31, 2018	June 30, 2018	December 31, 2017
Liabilities and net assets			
Current liabilities:			
Accounts payable and accrued expenses	$499.6	$471.8	$456.7
Accrued salaries, benefits and payroll taxes	353.6	368.8	349.0
Amounts due to third-party payors, net	94.9	96.6	80.1
Current portion of long-term debt (Note 1)	28.8	157.3	27.5
Current portion of self-insurance liabilities	95.7	95.5	93.7
Other current liabilities	160.5	158.0	157.5
Total current liabilities	**1,233.1**	**1,348.0**	**1,164.5**
Long-term debt, net of current portion (Note 1)	1,612.5	1,514.0	1,646.0
Self-insurance liabilities, net of current portion	291.9	283.2	310.6
Pension liabilities	288.3	290.0	396.7
Other long-term liabilities, net of current portion	257.3	259.4	258.7
Total liabilities	**3,683.1**	**3,694.6**	**3,776.5**
Net assets:			
Unrestricted	1,702.5	1,787.7	1,645.2
Unrestricted noncontrolling interest	16.1	16.2	18.6
Total unrestricted net assets	1,718.6	1,803.9	1,663.8
Temporarily restricted	143.2	147.6	148.0
Permanently restricted	43.6	43.4	42.4
Total net assets	**1,905.4**	**1,994.9**	**1,854.2**
Total liabilities and net assets	**$5,588.5**	**$5,689.5**	**$5,630.7**

Note 1: Current portion of long-term debt includes amounts associated with credit agreements that expire within 12 months from the balance sheet date and principal payments related to outstanding indebtedness due within 12 months of the balance sheet date. In January 2019, the Corporation renewed its $250.0 million revolving credit facility which will now expire in January 2022. The outstanding amount of $129.8 million was reclassified to long-term debt at December 31, 2018. Corresponding amounts for the above were reclassified in investments.

MedStar Health, Inc.

Consolidated Statements of Cash Flows
For the Six Months Ended December 31, 2018 and 2017

(Dollars in millions)

	Six Months Ended December 31, 2018	Six Months Ended December 31, 2017
Cash flows from operating activities:		
Change in net assets	($89.5)	$183.9
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	103.3	104.9
Loss (gain) on sale of property and equipment and other	0.1	(4.8)
Realized net gains on marketable investments	(5.2)	(25.8)
Change in unrealized losses (gains) on marketable investments and derivative	154.3	(86.9)
Decrease (increase) in net assets of foundation	5.5	(3.5)
Temporarily and permanently restricted contributions	(10.6)	(9.1)
Changes in operating assets and liabilities:		
Net receivables	(14.0)	(31.0)
Accounts payable and accrued expenses	40.8	(5.9)
Other	(11.6)	(23.8)
Net cash provided by operating activities	**173.1**	**98.0**
Cash flows from investing activities:		
(Purchases) proceeds from sales of investments and assets whose use is limited or restricted, net	(60.9)	71.8
Purchases of alternative investments	(29.4)	(89.9)
Proceeds from sales of alternative investments	16.0	15.4
Net settlement payment on derivative instrument	(0.8)	(1.1)
Purchases of property and equipment and other, net	(137.4)	(87.1)
Net cash used in investing activities	**(212.5)**	**(90.9)**
Cash flows from financing activities:		
Repayment of long-term borrowings	(30.6)	(28.3)
Temporarily and permanently restricted contributions	10.6	9.1
Distributions to noncontrolling interests	(1.5)	-
Net cash used in financing activities	**(21.5)**	**(19.2)**
Decrease in cash and cash equivalents	**(60.9)**	**(12.1)**
Cash and cash equivalents at beginning of period	**692.6**	**674.7**
Cash and cash equivalents at end of period	**$631.7**	**$662.6**
Supplemental disclosure of cash flow information:		
Cash paid for interest	$34.5	$32.0
Noncash investing and financing activities:		
Noncash purchases of property, plant and equipment	$5.1	$1.2

MedStar Health, Inc.

Management Discussion and Analysis of Financial Condition and Results of Operations

Overview

MedStar Health, Inc. (MedStar or the Corporation) is a tax-exempt Maryland corporation which, through its controlled entities and other affiliates, provides and manages healthcare services in the region encompassing Maryland, Washington D.C. and Northern Virginia. The Corporation operates ten hospitals which include MedStar Franklin Square Medical Center, MedStar Good Samaritan Hospital, MedStar Harbor Hospital, MedStar Union Memorial Hospital, MedStar Georgetown University Hospital, MedStar Montgomery Medical Center, MedStar National Rehabilitation Network, MedStar Southern Maryland Hospital Center, MedStar St. Mary's Hospital and MedStar Washington Hospital Center. At December 31, 2018, the Corporation had 3,076 licensed beds.

In addition, the Corporation provides urgent care and other healthcare services, education and research through numerous affiliates including, but not limited to MedStar PromptCare, MedStar Ambulatory Services, MedStar Medical Group, LLC, MedStar Health Research Institute, MedStar Health Visiting Nurse Association and Parkway Venture Companies ("Other Businesses"). At December 31, 2018, MedStar Family Choice provided Medicaid and Medicare insurance services to approximately 96,500 members in select areas within the region. See 'Other Disclosures' section below for additional information.

Reclassifications

Certain prior year amounts have been reclassified to conform with the current period presentation, the effects of which are not material.

Financial Performance

Three Months Ended December 31, 2018

Results of Operations

Earnings from operations for the three months ended December 31, 2018 were $23.9 million compared to the budget of $23.7 million and the prior year of $26.1 million. The operating margin of 1.7% was consistent with the budgeted operating margin of 1.7% and lower than the prior year operating margin of 1.9%. The favorable to budget operating results were driven by higher than budgeted growth in net patient service revenue, partially offset by unfavorable expenses. Operating earnings before interest, depreciation and amortization (EBIDA) for the three months ended December 31, 2018, were $88.1 million compared to the budget of $90.3 million and $90.1 million for the prior year. The EBIDA margin of 6.2% was below the budgeted margin of 6.4% and the prior year margin of 6.5%.

Total net operating revenue for the three months ended December 31, 2018 of $1,426.5 million was favorable to budget of $1,414.8 million by $11.7 million or 0.8% and increased $32.3 million or 2.3% over the prior year.

Net patient service revenue of $1,229.3 million was favorable to budget by $10.3 million or 0.8% and increased by $42.0 million or 3.5% over the prior year. The variance from budget was primarily due to favorable implicit price concessions, favorable outpatient volumes, and favorable inpatient case mix in our Washington, D.C. hospitals, partially offset by soft inpatient volumes and unfavorable rates. Hospital admissions (excluding sub-acute) for the three months ended December 31, 2018 totaled 32,885, which were 935 or 2.8% unfavorable to the budget of

33,820 and 706 or 2.1% below the prior year of 33,591. For the Maryland hospitals under the Global Budget Revenue (GBR) model, revenue is no longer recognized based on volumes alone. Total outpatient visits for the quarter totaled 1,267,366, which were 24,098 or 1.9% favorable to the budget of 1,243,268 and 56,647 or 4.7% above the prior year of 1,210,719. See schedule on page 16 for additional outpatient data.

Premium revenue for the three months ended December 31, 2018 was $143.7 million compared to a budget of $139.9 million, a favorable variance of $3.8 million or 2.7%, and was $1.0 million or 0.7% above the prior year of $142.7 million. MedStar Family Choice's (MFC) covered lives of 96,475 were unfavorable to the budget of 100,201 by 3,726 or 3.7% and were 3,888 or 3.9% below the prior year covered lives of 100,363.

Other operating revenue for the three months ended December 31, 2018 was $53.5 million compared to a budget of $55.9 million, unfavorable by $2.4 million or 4.3% and $10.7 million or 16.7% below the prior year of $64.2 million. The unfavorable budget variance is primarily due to unfavorable retail pharmacy revenue.

Personnel expenses for the three months ended December 31, 2018 were $810.6 million compared to a budget of $790.3 million, an unfavorable variance of $20.3 million or 2.6%. The unfavorable budget variance is primarily related to nursing and other agency usage and overtime, driven by nursing shortages in key areas, favorable inpatient case mix in our Washington D.C. hospitals, and an increase in Emergency Room visits at MedStar Washington Hospital Center due to the closure of a local non-affiliated hospital.

Supply expenses for the three months ended December 31, 2018 were $211.2 million compared to a budget of $206.3 million, an unfavorable variance of $4.9 million or 2.4%, primarily due to the increased inpatient case mix discussed above.

Purchased services expenses for the three months ended December 31, 2018 were $194.6 million compared to a budget of $198.3 million, a favorable variance of $3.7 million or 1.9%. The favorable budget variance is primarily related to the timing of certain IT initiatives and favorable clinical and administrative support services.

Other operating expenses for the three months ended December 31, 2018 were $122.0 million compared to a budget of $129.6 million, a favorable variance of $7.6 million or 5.9%. The variance from budget is primarily due to the favorable advertising and marketing, facilities and consulting expenses.

Interest expense for the three months ended December 31, 2018 was $11.8 million compared to a budget of $12.1 million, a favorable variance of $0.3 million or 2.5%, due to lower-than-budgeted interest rates on the Corporation's variable rate debt.

Depreciation and amortization for the three months ended December 31, 2018 was $52.4 million compared to a budget of $54.5 million, a favorable variance of $2.1 million or 3.9%. The variance from budget was due to the timing of the completion of certain capital projects.

Non-Operating Activity

Non-operating losses for the three months ended December 31, 2018 totaled $169.9 million compared to budgeted gains of $22.6 million and prior year gains of $51.6 million. The unfavorable variance from budget is due to the investment markets' below-budget performance. For the three months ended December 31, 2018, realized and unrealized losses on investments were $172.7 million, investment income was $8.5 million, and there was a $0.6 million unrealized loss on the Corporation's interest rate hedging derivative.

(Deficiency) Excess of Revenue Over Expenses

Deficiency of revenue over expenses for the three months ended December 31, 2018 was $146.0 million or $192.3 million unfavorable when compared to the budgeted excess of revenue over expenses of $46.3 million and $223.7 million below the prior year excess of revenue over expenses of $77.7 million. The unfavorable performance to budget was primarily a result of the non-operating losses described above.

Six Months Ended December 31, 2018

Results of Operations

Earnings from operations for the six months ended December 31, 2018 of $52.0 million exceeded the budget of $49.2 million; however, were below the prior year earnings of $58.6 million. The operating margin of 1.9% exceeded the budgeted operating margin of 1.8%; however, was below the prior year operating margin of 2.1%. The favorable to budget operating results were driven by favorable expense management, partially offset by lower-than-budgeted growth in revenue. Operating EBIDA for the six months ended December 31, 2018, was $178.8 million compared to the budget of $181.4 million and $186.3 million for the prior year. The operating EBIDA margin of 6.4% was below the budgeted margin of 6.5% and the prior year of 6.7%.

Total net operating revenue for the six months ended December 31, 2018 was $2,795.9 million compared to a budget of $2,811.7 million, unfavorable to budget by $15.8 million or 0.6%; however, increased $17.7 million or 0.6% over the prior year.

Net patient service revenue for the six months ended December 31, 2018 of $2,408.2 million was unfavorable to budget by $15.0 million or 0.6%; however, increased by $106.3 million or 4.6% over the prior year. The variance from budget was primarily due to unfavorable rates and soft inpatient volumes, partially offset by favorable case mix in the Washington D.C. hospitals and favorable implicit price concessions. Hospital admissions (excluding sub-acute) for the six months ended December 31, 2018 totaled 65,632, which were 1,755 or 2.6% below the budget of 67,387 and 1,623 or 2.4% below the prior year of 67,255. For the Maryland hospitals under the GBR model, revenue is no longer recognized based on volumes alone. Total outpatient visits for the year totaled 2,490,240, which were 20,371 or 0.8% above the budget of 2,469,869 and 87,769 or 3.7% above the prior year of 2,402,471. See schedule on page 16 for additional outpatient data.

Premium revenue for the six months ended December 31, 2018 was $283.6 million compared to a budget of $280.1 million, a favorable variance of $3.5 million or 1.2%; however, $79.5 million or 21.9% below the prior year of $363.1 million. The decrease from the prior year was due to the reduction in covered lives associated with the expiration of MFC's contract with the District of Columbia (DC) Medicaid program on September 30, 2017 (see 'Other Disclosures' section below). MFC covered lives of 96,475 were unfavorable to the budget of 100,201 by 3,726 or 3.7% and were 3,888 or 3.9% below the prior year covered lives of 100,363.

Other operating revenue for the six months ended December 31, 2018 was $104.1 million compared to a budget of $108.4 million, unfavorable by $4.3 million or 4.0%, and was $9.1 million or 8.0% below the prior year of $113.2 million. The unfavorable budget variance is primarily due to unfavorable retail pharmacy revenue.

Personnel expenses for the six months ended December 31, 2018 were $1,580.1 million compared to a budget of $1,565.6 million, an unfavorable variance of $14.5 million or 0.9%. The unfavorable budget variance is primarily related to nursing and other agency usage and overtime, driven by nursing shortages in key areas, favorable inpatient case mix in our Washington D.C. hospitals, and an increase in Emergency Room visits at MedStar Washington Hospital Center due to the closure of a local non-affiliated hospital.

Supply costs for the six months ended December 31, 2018 were $414.9 million compared to a budget of $409.2 million, an unfavorable variance of $5.7 million or 1.4%, primarily due to the increased inpatient case mix discussed above.

Purchased services for the six months ended December 31, 2018 were $382.9 million compared to a budget of $396.9 million, a favorable variance of $14.0 million or 3.5%. The favorable budget variance is primarily related to the timing of certain IT initiatives and favorable clinical and administrative support services.

Other operating expenses for the six months ended December 31, 2018 were $239.2 million compared to a budget of $258.6 million, a favorable variance of $19.4 million or 7.5%. The favorable budget variance is primarily due to favorable facilities, consulting, and advertising and marketing expenses.

Interest expense for the six months ended December 31, 2018 was $23.5 million compared to a budget of $24.2 million, a favorable variance of $0.7 million or 2.9%, due to lower-than-budgeted interest rates on the Corporation's variable rate debt.

Depreciation and amortization for the six months ended December 31, 2018 was $103.3 million compared to a budget of $108.0 million, a favorable variance of $4.7 million or 4.4%. The favorable budget variance is due to the timing of the completion of certain capital projects.

Non-Operating Activity

Non-operating losses for the six months ended December 31, 2018 totaled $139.5 million compared to budgeted gains of $45.2 million and prior year gains of $112.9 million. The unfavorable variance from budget is due to the investment markets' below-budget performance for the six months ended December 31, 2018. For the six months ended December 31, 2018, realized and unrealized losses on investments were $145.5 million, investment income was $14.4 million and there was a $0.1 million unrealized gain on the Corporation's interest rate hedging derivative.

(Deficiency) Excess of Revenue Over Expenses

Deficiency of revenue over expenses for the six months ended December 31, 2018 was $87.5 million or $181.9 million unfavorable when compared to the budgeted excess of revenue over expenses of $94.4 million, and $259.0 million below the excess of revenue over expenses of $171.5 million in the prior year. The unfavorable performance to budget was primarily a result of the non-operating losses discussed above.

Liquidity and Capital Resources

The Corporation maintains a $250.0 million revolving credit agreement that has a three-year term expiring January 2022, with an outstanding balance of $129.8 million at December 31, 2018, June 30, 2018, and December 31, 2017. As of December 31, 2018, the Corporation is in compliance with all covenants under this agreement and there have been no events of default.

The Corporation's total unrestricted cash and investments (including board-designated funds) were $2,010.0 million at December 31, 2018, $2,114.1 million at June 30, 2018 and $2,079.3 million at December 31, 2017. Days cash on hand were 139 days at December 31, 2018 compared to 147 days at June 30, 2018 and 145 days at December 31, 2017. The decrease in days cash on hand is primarily attributable to the decline in the investment markets. Days in accounts payable were 85 days at December 31, 2018, compared to 77 days at June 30, 2018 and 74 days at December 31, 2017. Days in accounts receivable were 45 days at December 31, 2018 compared to 43 days at June 30, 2018 and 44 days at December 31, 2017.

New Accounting Guidance for Revenue Recognition

Effective July 1, 2018, the Corporation adopted the Financial Accounting Standards Board ("FASB") Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers" (collectively Topic 606) using the modified retrospective method of adoption. This guidance establishes principles for reporting useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts with customers. Particularly, the standard requires that an entity recognizes 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. As a result of the adoption of Topic 606, what was previously classified as the provision for bad debts in the statement of operations and changes in net assets is now reflected as implicit price concessions (as defined in Topic 606) and therefore included as a reduction to net patient service revenue. Additionally, the allowance for uncollectible accounts of approximately $185.6 million as of July 1, 2018 was collapsed as a component of net patient accounts receivable. Other than these changes in presentation, the adoption of Topic 606 did not have a material impact on the consolidated results of operations for the three and six months ended December 31, 2018, and the Corporation does not expect it to have

a material impact on its consolidated results of operations going forward. For the three months and six months ended December 31, 2018, the Corporation recorded $43.6 and $89.9 million, respectively, of implicit price concessions as a reduction of net patient service revenue, respectively, compared to $55.1 and $108.8 million for the three months and six months ended December 31, 2017, respectively, that would have been recorded as provision for bad debts prior to the adoption of Topic 606. The Corporation's MFC insurance business is accounted for under insurance guidance (ASC 944) and as a result, premium revenue is not subject to Topic 606.

Net patient service revenue is recorded at the transaction price estimated by the Corporation to reflect the total consideration due from patients and third-party payors in exchange for providing goods and services in patient care. The Corporation recognizes net patient service revenue in the period in which we satisfy our performance obligations under contracts by transferring our services to our customers.

The Corporation determines performance obligations based on the nature of the services we provide. Generally, performance obligations satisfied over time relate to patients in our hospitals receiving inpatient services. The Corporation measures the performance obligation from admission into the hospital to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge. Revenue for performance obligations satisfied at a point in time, such as outpatient services, is recognized when goods or services are provided and the Corporation does not believe it is required to provide additional goods or services to the patient. Inpatient goods and/or services may include room, meals, ancillary services, etc. These services represent a bundle of goods and services that are distinct and accounted for as a single performance obligation within a patient stay or encounter.

The Corporation's estimate of the transaction price includes estimates of price concessions for such items as contractual allowances, charity care, potential adjustments that may arise from payment and other reviews, and uncollectible amounts, which are determined using a portfolio approach as a practical expedient to account for patient contracts as collective groups rather than individually. Estimates for uncollectible amounts are based on the aging of our accounts receivable, our historical collection experience for similar payors and patients, current market conditions, and other relevant factors. Settlements with third-party payors for retroactive revenue adjustments due to audits, reviews or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payor, correspondence from the payor and our historical settlement activity, including an assessment to ensure that it is probable that a significant reversal of revenue recognized will not occur. Estimated settlements are adjusted in future periods as adjustments become known or as years are settled or are no longer subject to such audits, reviews or investigations. In addition, the Corporation is committed to ensuring that patients within the communities it serves who lack financial resources have access to necessary hospital services. The Corporation works with uninsured and underinsured patients to gain an understanding of each patient's financial resources prior to admission (for scheduled services) or prior to billing (for emergency services). Based on this information and patient eligibility for charity care, the Corporation records estimated price concessions accordingly.

Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to net patient service revenue in the period of the change. Subsequent changes that are determined to be the result of an adverse change in the payor's or patient's ability to pay are recorded as bad debt expense. Bad debt expense for the three and six month periods ended December 31, 2018 was not significant.

A summary of net patient service revenue by major category of payor for the three months ended December 31, 2018 and 2017 is as follows:

	2018	2017
Medicare and Medicare HMO	36 %	36 %
Medicaid and Medicaid HMO	16	15
Carefirst Blue Cross Blue Shield	19	19
Other commercial and managed care payors	24	24
Self-pay including deductibles and coinsurance	5	6
	100 %	100 %

A summary of net patient service revenue by major category of payor for the six months ended December 31, 2018 and 2017 is as follows:

	2018	2017
Medicare and Medicare HMO	36 %	37 %
Medicaid and Medicaid HMO	16	16
Carefirst Blue Cross Blue Shield	19	20
Other commercial and managed care payors	23	22
Self-pay including deductibles and coinsurance	6	5
	100 %	100 %

For purposes of the table above, net patient service revenue for the three and six months ended December 31, 2017 is net of the provision of bad debt to be consistent with the presentation required under Topic 606 for the three and six months ended December 31, 2018.

Other Disclosures

The healthcare industry is subject to numerous laws and regulations from federal, state and local governments, and the government has increased enforcement of Medicare and Medicaid anti-fraud and abuse laws, as well as the physician self referral law (Stark Law). The Corporation's compliance with these laws and regulations is subject to periodic governmental inquiries, and the Corporation has responded appropriately to any such inquiries. The Corporation is aware of certain asserted and unasserted legal claims by the government, and from time to time, the Corporation may agree to resolve certain legal claims asserted by the government. The Corporation will continue to monitor all government inquiries and respond appropriately. The final outcomes of these government investigations cannot be determined at this time.

Recent government initiatives have focused on curtailing fraud, waste, and abuse in government-funded healthcare programs. To this end, the federal government and many states, have implemented programs to audit and recover potential overpayments to providers from the Medicare and Medicaid programs. The Corporation's hospitals and providers have periodically received audit requests from Medicare and Medicaid audit contractors, as well as the Office of Inspector General of the U.S. Department of Health & Human Services (OIG). These audit requests have targeted, among other things, medical necessity of inpatient admissions and provider documentation and coding practices. The Corporation's hospitals and providers have cooperated with each of these audit requests and implemented a program to track and manage their effect.

As a result of federal healthcare reform legislation, rules and regulations, substantial changes are occurring in the United States healthcare system. These include numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, reimbursement to healthcare providers, the privacy and security of health information, and the legal obligations of health insurers, providers and employers.

The Corporation, in the normal course of business, is a party to a number of other legal and regulatory proceedings. In June 2008, the Corporation received a U.S. Department of Health and Human Services, Office of Inspector

General (HHS-OIG) subpoena requesting documents relating to the contractual arrangements between a private cardiology group and MedStar Union Memorial Hospital (MUMH) and, in one instance, MedStar Franklin Square Medical Center (MFSMC). The U.S. Attorney's Office for the District of Maryland (USAO) subsequently informed the Corporation that the contractual arrangements were under civil investigation for potential violations of certain laws and regulations governing Federal health care programs. The USAO later informed the Corporation of another pending civil enforcement matter relating to allegations involving certain historic cardiac stent procedures performed at MUMH. The Corporation, MUMH, and MFSMC recently concluded negotiating a formal settlement agreement with the U.S. Department of Justice under which the Corporation will pay the government a settlement amount of $35.0 million, which is consistent with the Corporation's recorded accrual as of June 30, 2018, in exchange for full releases covering the conduct at issue as well as the dismissal of the civil actions underlying the government investigations. There is no admission of wrongdoing under the settlement and no corporate integrity agreement is required. The Corporation expects that the settlement agreement will be fully executed, and the settlement amount paid in March 2019.

On April 26, 2016, the Corporation was notified of a whistleblower lawsuit filed in the U.S. District Court in Northern District of Illinois alleging False Claims Act violations against Accretive Health and MedStar. The unsealing of the complaint was the result of the federal government's decision not to intervene in the lawsuit at the time, which decision permits the whistleblower to proceed with the lawsuit against the defendants. The Corporation is defending against the lawsuit. At the present time, management cannot conclude, based on the nature of this matter, how this matter will be resolved or whether the resolution will have a material adverse financial impact on the Corporation.

Certain Maryland-based hospital charges are subject to review and approval by the Health Services Cost Review Commission (HSCRC). The HSCRC has jurisdiction over hospital reimbursement in Maryland by agreement with the Centers for Medicare and Medicaid Services (CMS). This agreement is based on a waiver from the Medicare Prospective Payment System reimbursement principles granted under Section 1814(b) of the Social Security Act. In January 2014, CMS approved Maryland's waiver for a five-year period beginning January 1, 2014 for inpatient and outpatient hospital services. The waiver tied hospital per capita revenue growth to the state's economic growth of 3.58% and required growth in Medicare spending per beneficiary in Maryland to be 0.5% below the national average. The waiver also imposed quality measures and encouraged population health management.

In connection with the waiver, the HSCRC introduced the GBR model, which covers the Corporation's seven Maryland hospitals. This model moves payment to hospitals from each individual service to a total revenue for each hospital (or a combination of hospitals) to provide hospitals flexibility in the objectives of better care for individuals, higher levels of overall population health, and improved health care affordability. The model removes the financial incentive from increasing volume and provides incentive to work with partners to provide care in the appropriate setting. Additionally, the GBR model has the potential of including both prospective and retrospective rate adjustments.

In 2018, Maryland entered into a new ten-year waiver with CMS to include total cost of care benchmarks and savings, which took effect January 1, 2019, and will be re-evaluated at the end of five years. The new waiver is intended to shift care into lower cost settings, improve care coordination, and align incentives among various healthcare providers.

On January 1, 2016, MedStar Accountable Care, LLC (ACO) became active as a Medicare Shared Savings Program Track 3 ACO to improve the quality of care for Medicare Fee-For-Service (FFS) beneficiaries and reduce unnecessary costs. Under this three-year agreement with CMS, the ACO is eligible for annual bonus payments from CMS if it is able to achieve certain quality and savings benchmarks. Conversely, the ACO is at financial risk to the extent that costs exceed the CMS established benchmarks. The agreement includes a provision allowing cancellation with 60 days written notification. The ACO currently has approximately 45,000 attributed members tied to the Corporation's primary care network. The results of the ACO's operations did not have a material impact on the Corporation's financial results for the three months and six months ended December 31, 2018.

MFC's contract with the DC Medicaid program expired September 30, 2017. As a large healthcare provider in the District, the Corporation continues to provide medical care at our facilities for many of these Medicaid participants who are now enrolled in other managed care organizations. In June 2018, MFC notified CMS that it will not renew its contracts for participation in the Medicare Advantage program effective January 1, 2019.

Subsequent Events

In January 2019, the Company renewed its $250.0 million revolving credit facility which will now expire in January 2022. The outstanding amount of $129.8 million was reclassified to long-term debt at December 31, 2018. Corresponding amounts for the above were also reclassified in investments.

In February 2019, MedStar Washington Hospital Center (MWHC) agreed on a new collective bargaining agreement with the union that represents its nurses, National Nurses United. That agreement replaced the existing agreement and provides for a five-year term commencing March 1, 2019 and running through February 29, 2024.

MedStar Health, Inc.

Selected Other Information

	Quarter Ended December 31				
	2018 Actual	2018 Budget	% Variance	2017 Actual	% Variance
Admissions (excluding sub-acute)	32,885	33,820	(2.8%)	33,591	(2.1%)
Observations	9,380	9,688	(3.2%)	9,796	(4.2%)
Emergency Room visits	118,304	120,017	(1.4%)	121,133	(2.3%)
Home Health visits	81,304	80,342	1.2%	76,913	5.7%
Physician Office visits	561,216	527,004	6.5%	502,809	11.6%
Other Outpatient visits*	497,162	506,217	(1.8%)	500,068*	(0.6%)
Total Outpatient Visits	**1,267,366**	**1,243,268**	**1.9%**	**1,210,719**	**4.7%**
MedStar Family Choice Covered Lives	**96,475**	**100,201**	**(3.7%)**	**100,363**	**(3.9%)**

	Year-To-Date December 31				
	2018 Actual	2018 Budget	% Variance	2017 Actual	% Variance
Admissions (excluding sub-acute)	65,632	67,387	(2.6%)	67,255	(2.4%)
Observations	19,100	19,456	(1.8%)	19,713	(3.1%)
Emergency Room visits	238,440	242,812	(1.8%)	244,727	(2.6%)
Home Health visits	158,012	157,826	0.1%	151,089	4.6%
Physician Office visits	1,086,282	1,044,232	4.0%	990,006	9.7%
Other Outpatient visits*	988,406	1,005,543	(1.7%)	996,936*	(0.9%)
Total Outpatient Visits	**2,490,240**	**2,469,869**	**0.8%**	**2,402,471**	**3.7%**
MedStar Family Choice Covered Lives	**96,475**	**100,201**	**(3.7%)**	**100,363**	**(3.9%)**

*For comparative purposes, actual other outpatient visits for the three and six month periods ended December 31, 2017 have been revised to include visits associated with joint ventures.

KEY LIQUIDITY INDICATORS	December 31, 2018	June 30, 2018	December 31, 2017
Days cash on hand *	139	147	145
Maximum Annual Debt Service coverage	4.22	4.47	4.58
Days revenue in accounts receivable	45	43	44
Days expense in accounts payable	85	77	74

*Under the Corporation's bank agreements, the Corporation is required to maintain certain covenants, including days cash on hand of 70 (measured semi-annually at each June 30 and December 31) and a maximum annual debt service coverage of 1.25 (measured quarterly on a rolling four quarters basis). The Corporation is in compliance with these covenants as of December 31, 2018, June 30, 2018 and December 31, 2017. Similar covenants are also included under the Corporation's Master Trust Indenture, although they are measured annually and required covenant levels are lower.

CASH AND INVESTMENTS (in millions)	December 31, 2018	June 30, 2018	December 31, 2017
Cash and cash equivalents	$ 631.7	$ 692.6	$ 662.6
Investments	1,208.4	1,239.9	1,229.5
Assets whose use is limited or restricted			
Funds held by trustees	675.5	713.2	733.7
Funds restricted by donors for specific purposes and endowment	104.1	100.0	97.9
Funds designated by board and management	170.1	189.2	190.5
Total assets whose use is limited or restricted	949.7	1,002.4	1,022.1
Total cash and cash equivalents, investments and assets whose use is limited or restricted	$ 2,789.8	$ 2,934.9	$ 2,914.2
Less cash and cash equivalents, and current portion of investments and assets whose use is limited or restricted	(803.6)	(919.6)	(757.9)
Total long-term investments and long-term assets whose use is limited or restricted	$ 1,986.2	$ 2,015.3	$ 2,156.3