



West Penn Allegheny Health System

ANNUAL REPORT

(Based upon unaudited financial information)

For the Fiscal Year Ended June 30, 2012

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DISCLAIMER

This Management Discussion and Analysis of West Penn Allegheny Health System, Inc. and its operating entities for the fiscal year ended June 30, 2012 may contain “forward-looking statements” within the meaning of the United States *Private Securities Litigation Reform Act of 1995*, Section 21E of the United States *Securities Exchange Act of 1934*, as amended (the “*Exchange Act*”), and Section 27A of the United States *Securities Act of 1933*, as amended (the “*Securities Act*”). The achievement of certain results or other expectations contained in such forward-looking statements involves known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. The West Penn Allegheny Health System, Inc. and the members of the Obligated Group, expressly disclaim any obligation or undertaking to issue any updates or revisions to those forward-looking statements if or when their expectations change, or events, conditions or circumstances on which such statements are based occur.

INTRODUCTION

Organization of West Penn Allegheny Health System and the Obligated Group

The Annual Report is produced to comply with the \$752,370,000 Allegheny County Hospital Development Authority Health System Revenue Bonds (West Penn Allegheny Health System), Series 2007A, Continuing Disclosure Agreement. The following CUSIP numbers are covered by this Annual Report:

01728AG67	01728AF92 (matured)
01728AG75	01728AG83
01728AG34 (matured)	01728AG42
01728AG26 (matured)	01728AG59

West Penn Allegheny Health System

West Penn Allegheny Health System, Inc. (“Parent”, also referred to herein as “WPAHS” or the “System”) is a Pennsylvania nonprofit corporation that, together with other entities under its direct or indirect control, forms a regional health system operating five hospital campuses and other health care facilities and delivering the services of health care professionals, including over 600 employed physicians, to residents of Western Pennsylvania. In the fiscal year ended June 30, 2012, the hospital affiliates of the Parent recorded over 164,000 emergency department visits, over 56,000 acute discharges and delivered over 3,800 newborns. From these patient care activities, the Parent recorded, on a consolidated basis, total net patient service revenue of approximately \$1.5 billion. At June 30, 2012, the Parent’s consolidated total assets were approximately \$1.3 billion; its total liabilities were approximately \$1.5 billion.

The Obligated Group currently includes WPAHS and the following hospitals, physician practice networks, foundations, and research organizations which comprise the System:

Hospitals

- Allegheny General Hospital (AGH), a division of West Penn Allegheny Health System, Inc.
- The Western Pennsylvania Hospital which includes West Penn Campus (WPH) and Forbes Regional Campus (FRH), both of which are divisions of West Penn Allegheny Health System
- Alle-Kiski Medical Center (AKMC)
- Canonsburg General Hospital and Subsidiary (CGH)

Physician Practice Networks

- Allegheny Specialty Practice Network (ASPN)
- Allegheny Medical Practice Network (AMPN)
- West Penn Physician Practice Network (WPPPN)
- West Penn Allegheny Oncology Network (WPAON)
- West Penn Corporate Medical Services, Inc. (WPCMS)

Foundations and Research Organizations

- The Western Pennsylvania Hospital Foundation (WPHF)
- Forbes Health Foundation (FHF)
- Suburban Health Foundation (SHF)
- Allegheny-Singer Research Institute (ASRI)

Note: On December 31, 2007, Allegheny General Hospital and The Western Pennsylvania Hospital were merged into West Penn Allegheny Health System, Inc.

**I. MANAGEMENT'S DISCUSSION OF THE UNAUDITED
FINANCIAL RESULTS FOR THE FISCAL YEAR ENDED JUNE 30,
2012**

WEST PENN ALLEGHENY HEALTH SYSTEM

CONSOLIDATED STATEMENTS OF OPERATIONS - UNAUDITED

(dollars in thousands)

	QUARTER ENDED		FISCAL YEAR ENDED	
	JUNE 30,		JUNE 30,	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
Net patient service revenue	\$ 347,299	351,251	1,474,569	1,503,824
Other revenue	26,997	10,799	80,980	87,359
Net assets released from restrictions	994	1,192	3,652	4,900
Total unrestricted revenues and other support	<u>375,290</u>	<u>363,242</u>	<u>1,559,201</u>	<u>1,596,083</u>
Salaries, wages, and fringe benefits	194,060	186,261	866,488	848,956
Patient care supplies	71,445	66,795	279,937	275,392
Professional fees and purchased services	43,250	40,655	163,727	158,043
General and administrative	41,390	44,278	165,830	171,162
Provision for bad debts	20,755	15,164	80,805	69,092
Depreciation and amortization	17,538	15,771	65,740	60,507
Interest	10,604	9,541	40,335	37,941
Expenses, excluding restructuring	<u>399,042</u>	<u>378,465</u>	<u>1,662,862</u>	<u>1,621,093</u>
Operating income (loss) before restructuring	(23,752)	(15,223)	(103,661)	(25,010)
Restructuring	(981)	(11,065)	(8,841)	(26,782)
Operating income (loss)	(24,733)	(26,288)	(112,502)	(51,792)
Investment income	3,391	4,173	14,242	17,884
Gifts and donations	58,246	50,208	58,560	50,652
Gain from divestiture	-	9,606	-	9,606
Gain (loss) in joint venture investment	930	3,011	1,863	(5,908)
Excess (deficiency) of revenues over expenses	\$ <u>37,834</u>	\$ <u>40,710</u>	\$ <u>(37,837)</u>	\$ <u>20,442</u>

Operating Results

The System produced a deficiency of revenues over expenses of \$37.8 million for the year ended June 30, 2012. Net patient service revenue for the year ended June 30, 2012 decreased \$29.3 million, or 1.9%, as compared to the year ended June 30, 2011. Contributing factors to the decrease in revenues are reduced volumes mainly attributable to the closure of services at WPH, offset by marginally increased reimbursement for services on an adjusted discharge basis.

Inpatient discharges within the System declined by 6.4%, when compared to fiscal year 2011. This decrease in volume correlates to degradation of net revenue of approximately \$39.1 million. Closing of the emergency department and other services at WPH attributed to a decrease of 29% in inpatient discharges. This decline at WPH accounted for approximately 2,600 acute discharges, or 68%, of the total decrease across the System of approximately 3,800 discharges. The results reported through June 30, 2011 include a fully operational WPH for six months for fiscal year 2011, whereas the results reported through June 30, 2012 include a reopening and ramp up of services beginning four and a half months before year end. The emergency department at WPH was closed in December 2010 as part of the "Urban Consolidation" initiative. This initiative was reversed as a part of the Highmark Affiliation Agreement reopening the emergency department and selected acute care services on February 14, 2012.

Additional volume anticipated from physician recruitment by Highmark did not materialize in fiscal year 2012. The decrease in volume was partially offset by increased reimbursement rates, as contractually obligated, over fiscal year 2011. The total increased reimbursement for fiscal year 2012 over the fiscal year 2011 amount was approximately \$9.8 million.

The System received \$100.0 million from Highmark on October 31, 2011 as part of its executed Affiliation Agreement terms. Fifty million dollars was accounted for as a loan and \$50.0 million was accounted for as revenue in fiscal year 2012 as gifts and donations on the consolidated income statement. The System also received \$50.0 million from Highmark on April 27, 2012, which was accounted for as a loan. In addition, the System also received an unrestricted payment of \$8.0 million from Highmark during the fourth quarter of 2012, which is also included as revenue in fiscal year 2012 as gifts and donations on the consolidated income statement.

Expenses, excluding restructuring, through June 30, 2012 increased \$41.8 million (2.6%) as compared to June 30, 2011. The increase is attributable to an increase in salaries, wages, and fringe benefits (SWB) and the provision for bad debts (Provision). The System experienced an increase in SWB of \$17.5 million (2.1%) over the previous fiscal year. This increase was in-line with the annual market adjustment awarded to the employees of the System and normal increases in health insurance and other benefits.

System estimations for depreciation and amortization and the Provision contributed to an increase of \$16.9 million (13.1%). The calculation of the Provision is based upon trended historical information, current mix of business, and aging of the outstanding accounts receivable as of June 30, 2012. Patient responsibility balances for co-pays and deductibles over the prior fiscal year contributed to the increase in Provisions, along with an increase in a charge master without offsetting increases in reimbursement rates, which resulted in an increase of \$11.7 million (17%). The assumptions utilized in the calculation of depreciation and amortization remained consistent year over year. System total depreciable fixed assets increased from fiscal year 2011 due to asset additions from material capital improvements at WPH (approximately \$29.0 million), and other additions in the normal course of business.

Restructuring costs of \$8.8 million were incurred through June 30, 2012, which are primarily related to severance costs associated with changes in leadership over the past year.

Also included in the operating results are revenues and expenses relating to Pennsylvania's Medicaid Modernization Act (MMA), which was passed by the legislature in September 2010, and approved by the Centers for Medicare and Medicaid Services in January 2011. Total revenue recognized for the MMA was \$29.2 million and \$30.8 million for the year ended June 30, 2012 and 2011, respectively. That amount was offset by a related assessment (expense) of \$23.6 million and \$21.6 million for year ended June 30, 2012 and 2011, respectively. The net benefit from MMA to the System declined by \$3.6 million from 2011 to 2012.

A comparison of expense categories as a percentage of total revenue for the nine months ended June 30, 2012 and 2011 are as follows:

	<u>2012</u>	<u>2011</u>
Salaries, wages, and fringe benefits	55.6 %	53.2 %
Patient care supplies	18.0	17.3
Professional fees and purchased services	10.5	9.9
General and administrative	10.6	10.7
Provision for bad debts	5.2	4.3
Depreciation and amortization	4.2	3.8
Interest	2.6	2.4
Expenses, excluding restructuring	<u>106.7 %</u>	<u>101.6 %</u>
Restructuring	<u>0.6</u>	<u>1.7</u>
Total	<u><u>107.3 %</u></u>	<u><u>103.3 %</u></u>

Expenses, excluding restructuring, as a percentage of total revenue for the year ended June 30, 2012 increased in comparison to the year ended June 30, 2011. Driving the increase is a decrease in total revenue of 2.3%, coupled with an increase in SWB and the Provision.

SWB increased 2.1% over the previous year. Please see the previous page for further discussion.

The Provision increased 17.0% over the previous year. Please see the previous page for further discussion.

Liquidity and Capital Position

As of June 30, 2012, day's cash on hand as defined in the Master Indenture of Trust (MIT) was 62.2 days. Of the \$273.2 million included in this calculation, approximately 24.5% is subject to daily market value fluctuations, with approximately 24.4% invested in fixed income.

Contributions of \$32.0 million were made to the cash balance retirement plans during the year ended June 30, 2012, as required by the Internal Revenue Code and Employee Retirement Income Security Act and relevant regulations and guidance issued there under.

Capital expenditures during the year ended June 30, 2012 were \$89.8 million.

Principal debt payments made during the year ended June 30, 2012 were \$15.4 million.

The average number of days in net accounts receivable was 35.1 at June 30, 2012. Accounts payable are being paid in accordance with terms.

Subsequent Event Information

On September 28, 2012, WPAHS notified Highmark that Highmark had anticipatorily breached and repudiated the Affiliation Agreement and that as a result, WPAHS is excused, released, and discharged from performing its obligations under the Affiliation Agreement and related agreements. The System will be exploring new options for its future direction. On October 1, 2012 Highmark filed an injunction against the System to prevent the System from exploring other potential partners. A preliminary injunction hearing was held on October 25-26, 2012, to hear evidence regarding this motion. The hearing is scheduled to continue on November 1, 2012

**II. UNAUDITED FINANCIAL STATEMENTS FOR THE FISCAL YEAR
ENDED JUNE 30, 2012**

UNAUDITED

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Consolidated Financial Statements and Supplementary Information

June 30, 2012 and 2011

UNAUDITED

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

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UNAUDITED

Independent Auditors' Report

UNAUDITED**WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES**

Consolidated Balance Sheets

June 30, 2012 and 2011

(Amounts in thousands)

Assets	2012	2011
Current assets:		
Cash and cash equivalents	\$ 193,816	164,595
Short-term investments	5,108	5,075
Assets limited or restricted as to use	5,744	5,464
Receivables:		
Patient accounts – net of allowance for uncollectible accounts of \$44,116 and \$30,592 in 2012 and 2011, respectively	136,964	132,154
Other	25,094	32,845
Estimated third-party payor settlements	—	13,563
Inventories, net	21,289	22,554
Prepaid expenses	15,193	19,619
Total current assets	403,208	395,869
Assets limited or restricted as to use	395,487	425,554
Property and equipment, net	394,070	369,218
Other assets, net	75,296	80,008
Total assets	\$ 1,268,061	1,270,649

UNAUDITED**WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES**

Consolidated Balance Sheets

June 30, 2012 and 2011

(Amounts in thousands)

Liabilities and Net Deficit	2012	2011
Current liabilities:		
Current portion of long-term debt	\$ 15,866	14,742
Accounts payable	87,241	106,879
Accrued expenses	17,445	15,855
Accrued interest	6,699	4,954
Accrued salaries and vacation	55,843	63,309
Current portion of deferred revenue	15,632	13,779
Current portion of self-insurance liabilities	2,954	2,610
Estimated third-party payor settlements	1,163	—
Other current liabilities	4,497	11,855
Total current liabilities	<u>207,340</u>	<u>233,983</u>
Deferred revenue	36,869	39,692
Self-insurance liabilities	77,744	83,229
Long-term debt	878,836	792,492
Accrued pension obligation	278,663	196,256
Other noncurrent liabilities	23,168	24,090
Total liabilities	<u>1,502,620</u>	<u>1,369,742</u>
Net (deficit) assets:		
Unrestricted	(480,841)	(356,631)
Temporarily restricted	23,210	23,425
Permanently restricted	223,072	234,113
Total net deficit	<u>(234,559)</u>	<u>(99,093)</u>
Total liabilities and net deficit	<u>\$ 1,268,061</u>	<u>1,270,649</u>

See accompanying notes to consolidated financial statements.

UNAUDITED**WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES**

Consolidated Statements of Operations

Years ended June 30, 2012 and 2011

(Amounts in thousands)

	<u>2012</u>	<u>2011</u>
Unrestricted revenues and other support:		
Net patient service revenue	\$ 1,474,569	1,503,824
Other revenue	80,980	87,359
Net assets released from restrictions	3,652	4,900
Total unrestricted revenues and other support	<u>1,559,201</u>	<u>1,596,083</u>
Expenses:		
Salaries, wages, and fringe benefits	866,488	848,956
Patient care supplies	279,937	275,392
Professional fees and purchased services	163,727	158,043
General and administrative	165,830	171,162
Provision for bad debts	80,805	69,092
Depreciation and amortization	65,740	60,507
Interest	40,335	37,941
Restructuring	8,841	26,782
Total expenses	<u>1,671,703</u>	<u>1,647,875</u>
Operating loss	(112,502)	(51,792)
Investment income	14,242	17,884
Gifts and donations	58,560	50,652
Gain from divestiture	—	9,606
Gain (loss) in joint venture investment	1,863	(5,908)
(Deficiency) excess of revenues over expenses	(37,837)	20,442
Net assets released for property acquisitions and donated capital	781	2,400
Pension liability adjustments	(86,954)	55,707
Other transfers	(200)	(183)
(Decrease) increase in unrestricted net assets	<u>\$ (124,210)</u>	<u>78,366</u>

See accompanying notes to consolidated financial statements.

UNAUDITED**WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES**

Consolidated Statements of Changes in Net Deficit

Years ended June 30, 2012 and 2011

(Amounts in thousands)

	<u>2012</u>	<u>2011</u>
Unrestricted net deficit:		
(Deficiency) excess of revenues over expenses	\$ (37,837)	20,442
Net assets released for property acquisitions and donated capital	781	2,400
Pension liability adjustments	(86,954)	55,707
Other transfers	(200)	(183)
	<u>(124,210)</u>	<u>78,366</u>
(Increase) decrease in unrestricted net deficit		
Temporarily restricted net assets:		
Contributions	3,081	3,562
Investment income	882	1,168
Net assets released from restrictions used for:		
Operations	(3,652)	(4,900)
Acquisition of equipment	(781)	(2,400)
Change in net unrealized gains on other than trading securities	—	803
Other transfers	255	(407)
	<u>(215)</u>	<u>(2,174)</u>
Decrease in temporarily restricted net assets		
Permanently restricted net assets:		
Contributions	4	447
Investment income	7,205	8,632
Change in net unrealized (losses) gains other than trading securities	(8,574)	27,475
Transfers out of endowments/participating trust to investment income and operations	(9,695)	(9,911)
Other transfers	19	369
	<u>(11,041)</u>	<u>27,012</u>
(Decrease) increase in permanently restricted net assets		
(Increase) decrease in net deficit	(135,466)	103,204
Net deficit – beginning of year	<u>(99,093)</u>	<u>(202,297)</u>
Net deficit – end of year	<u>\$ (234,559)</u>	<u>(99,093)</u>

See accompanying notes to consolidated financial statements.

UNAUDITED

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended June 30, 2012 and 2011

(Amounts in thousands)

	<u>2012</u>	<u>2011</u>
Cash flows from operating activities:		
(Increase) decrease in net deficit	\$ (135,466)	103,204
Adjustments to reconcile (increase) decrease in net deficit to net cash (used in) provided by operating activities:		
Depreciation and amortization	65,740	60,507
Unrealized losses (gains) on unrestricted investments	1,286	(4,519)
Gain from divestiture	—	(9,606)
Noncash premium amortization	(299)	(304)
Change in pension liability	86,954	(55,707)
Noncash pension expense	27,492	29,850
Provision for bad debts	80,805	69,092
Unrealized losses (gains) on restricted investments	8,574	(28,278)
Realized gains on investments	(7,359)	(6,913)
Restricted contributions and investment income	(11,172)	(13,809)
Increase (decrease) in cash from changes in:		
Receivables	(77,864)	(48,043)
Prepaid expenses	4,426	(5,301)
Inventories	1,265	1,747
Accounts payable and accrued expenses	(35,940)	17,819
Estimated third-party payor settlements	14,726	(6,366)
Deferred revenue	(970)	2,981
Self-insurance liabilities	(576)	1,723
Pension contributions	(32,039)	(75,710)
Other assets	(688)	2,832
Other liabilities	(8,280)	(248)
Net cash (used in) provided by operating activities	<u>(19,385)</u>	<u>34,951</u>
Cash flows from investing activities:		
Acquisition of property and equipment	(77,586)	(101,050)
Proceeds from divestiture	—	10,245
Purchase of assets limited or restricted as to use and short-term investments	(449,149)	(657,230)
Sales of assets limited or restricted as to use and short-term investments	476,402	700,539
Net cash used in investing activities	<u>(50,333)</u>	<u>(47,496)</u>
Cash flows from financing activities:		
Repayments of long-term debt	(15,370)	(12,980)
Proceeds from issuance of long-term debt	103,137	7,643
Proceeds from restricted contributions and investment income	11,172	13,809
Net cash provided by financing activities	<u>98,939</u>	<u>8,472</u>
Net increase (decrease) in cash and cash equivalents	29,221	(4,073)
Cash and cash equivalents – beginning of year	<u>164,595</u>	<u>168,668</u>
Cash and cash equivalents – end of year	<u>\$ 193,816</u>	<u>164,595</u>
Supplemental disclosures:		
Cash paid for interest – net of amounts capitalized of \$2,984 and \$3,440 for 2012 and 2011, respectively	\$ 38,560	34,572
Property additions in accounts payable and other liabilities	12,171	10,477

See accompanying notes to consolidated financial statements.

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2012 and 2011

(1) Organization

West Penn Allegheny Health System and Subsidiaries (WPAHS or the System) is a Pennsylvania nonprofit charitable corporation that provides routine and tertiary healthcare services.

The System consists of the following entities, with WPAHS as the sole member of these entities:

Allegheny General Hospital and Subsidiaries (AGH)	Allegheny Medical Practice Network (AMPN)
The Western Pennsylvania Hospital and Subsidiaries (WPH)	Allegheny Specialty Practice Network (ASPN)
Alle-Kiski Medical Center (AKMC)	West Penn Corporate Medical Services, Inc. (WPCMSI)
The Western Pennsylvania Hospital – Forbes Regional Campus (FRC)	Allegheny Singer Research Institute (ASRI)
Canonsburg General Hospital and Subsidiary (CGH)	Friendship Insurance Company, Ltd. (FIC)
West Penn Allegheny Foundation, LLC (WPAF)	Alle-Kiski Medical Center Trust (AKMC Trust)
The Western Pennsylvania Hospital Foundation (WPHF)	
Forbes Health Foundation (FHF)	

WPAHS is the sole member of each of these entities. Each member of the Obligated Group (the Obligated Group) is jointly and severally liable for the satisfaction of the outstanding bond debt of WPAHS (note 11). All members of the System with the exception of FIC, AKMC Trust, and WPAF are members of the Obligated Group.

(2) Significant Developments and Going Concern Considerations

THIS FOOTNOTE HAS NOT YET BEEN DRAFTED

(3) Summary of Significant Accounting Policies

The significant accounting policies applied in preparing the accompanying consolidated financial statements are summarized below:

(a) Basis of Accounting

WPAHS maintains its accounts on the accrual basis of accounting.

(b) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the entities identified in note 1. Joint venture investments, investments in limited partnerships, and investments with an ownership interest greater than 20% where control is not demonstrated are accounted for using the equity method.

All significant intercompany balances and transactions have been eliminated in consolidation.

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2012 and 2011

(c) Use of Estimates in the Preparation of Consolidated Financial Statements

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles (U.S. GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Investment securities and pension obligations are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities and interest rates, it is at least reasonably possible that these changes in risks in the near term could materially affect the amounts reported in the accompanying consolidated balance sheets, statements of operations, and statements of changes in net assets.

(d) Net Patient Service Revenue

WPAHS has agreements with third-party payors that provide for payments to WPAHS at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services as they are rendered and includes estimated retroactive revenue adjustments due to future retrospective audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations. A summary of the payment arrangements with major third-party payors is as follows:

Medicare – Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. WPAHS is reimbursed for services rendered at a tentative rate with a final settlement determined after submission of annual cost reports by WPAHS and audits thereof by the Medicare fiscal intermediary. WPAHS' entities' Medicare cost reports have been audited by the Medicare fiscal intermediary through the year ended June 30, 2007 for all hospitals.

Medical Assistance – Inpatient care and outpatient services rendered to Medical Assistance eligible patients are paid at prospectively determined rates.

Blue Cross – Inpatient and outpatient services rendered to Blue Cross subscribers are reimbursed at prospectively determined rates.

WPAHS has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment to WPAHS under these agreements includes prospectively determined rates and discounts from established charges.

During the years ended June 30, 2012 and 2011, net patient service revenue increased \$4,313 and \$1,917, respectively, due to prior year retroactive adjustments in excess of amounts previously estimated.

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2012 and 2011

Revenue from the Medicare and Medical Assistance programs accounted for approximately 42% and 8%, respectively, of WPAHS' net patient service revenue for the year ended June 30, 2012, and 39% and 8%, respectively, for the year ended June 30, 2011. Laws and regulations governing the Medicare and Medical Assistance programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

On July 9, 2010, the Pennsylvania General Assembly passed the Medicaid Modernization and Hospital Fair Payment Act (Act 49), and as a result, healthcare providers in Pennsylvania are subject to a statewide hospital assessment (known as the Quality Care Assessment) subject to the conditions and requirements specified in Act 49 during the three-year period July 1, 2010 through June 30, 2013. Act 49 has the following goals: provide savings to the Commonwealth and to provide fairness and accuracy in payments to hospitals for inpatient services by funding the All Patient Refined-Diagnostic Related Groups (APR-DRG) prospective payment system.

Revenues generated from the assessment under Act 49 requires the Department of Public Welfare (DPW) to use a new prospective payment system (APR-DRG) to pay hospitals in the Medical Assistance fee-for-service program for inpatient services provided on or after July 1, 2010. In addition, it requires DPW to make supplemental payments to hospitals, such as inpatient disproportionate share and medical and health professional education hospitals, in accordance with the state plan approved by the federal government.

The net patient services revenue impact of Act 49 on WPAHS in fiscal year 2012 was \$29,242, while the expense impact of the assessment on WPAHS in fiscal year 2012 was \$23,588. The net patient services revenue impact of Act 49 on WPAHS in fiscal year 2011 was \$30,827, while the expense impact of the assessment on WPAHS in fiscal year 2011 was \$21,610. These amounts are included in patient service revenue and general administrative expenses, respectively.

WPAHS grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of net receivables from patients and third-party payors at June 30, 2012 and 2011 is as follows:

	<u>2012</u>	<u>2011</u>
Medicare	31%	36%
Medical Assistance	14	11
Blue Cross	19	21
Other third-party payors	34	30
Patients	2	2
	<u>100%</u>	<u>100%</u>

(e) Excess (Deficiency) of Revenues over Expenses

The consolidated statements of operations and changes in net assets include an excess (deficiency) of revenues over expenses. Changes in unrestricted net deficit, which are excluded from deficiency of revenues over expenses for the year ended June 30, 2012 and an excess of revenues over expenses at

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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June 30, 2011, consistent with industry practice, include changes in permanent transfers of assets to and from affiliates for other than goods and services, pension liability adjustments not reflected in pension expense, and contributions of long-lived assets (including assets acquired using contributions, which, by donor restriction, were to be used for the purposes of acquiring such assets).

(f) *Cash and Cash Equivalents*

Cash and cash equivalents include highly liquid investments purchased with original maturities of three months or less. Cash equivalents are stated at cost, which approximates fair value.

(g) *Inventories*

Inventories, consisting of drugs and medical supplies, are stated at the lower of cost (first-in, first-out) or market value.

(h) *Investments and Assets Limited or Restricted as to Use*

Investments classified as assets limited or restricted as to use in the accompanying consolidated balance sheets primarily include assets held by trustees under indenture agreements, temporarily and permanently restricted assets, and designated assets set aside by the board of directors for future capital improvements, over which the board retains control and may use for other purposes at its discretion. Amounts required to meet current liabilities have been included in current assets in the accompanying consolidated balance sheets at June 30, 2012 and 2011. Short-term investments include certificates of deposit with original maturities of greater than three months that will come due in one year or less.

Investment income or loss (including realized gains and losses on investments, interest and dividends, and unrealized gains and losses on investments) is included in the excess (deficiency) of revenues over expenses unless this income or loss is restricted by donor or law. Investment income (including realized gains and losses on investments and unrealized gains and losses on temporarily and permanently restricted gifts) is recorded based on donor restriction as part of the corresponding net asset class within the consolidated statements of changes in net assets.

Debt and equity securities are recorded at fair value. Beneficial interests in perpetual trusts are recorded at the fair value of the underlying assets in the trust. The present value of the estimated future cash receipts from the trusts approximates the fair value.

(i) *Temporarily and Permanently Restricted Net Assets*

Temporarily restricted net assets are those whose use has been limited by donors for a specific purpose or time period. Permanently restricted net assets have been restricted by donors to be maintained in perpetuity, except as provided by the provisions of Section 8113 of the Pennsylvania Probate, Estate, and Fiduciaries Code (note 5). Temporarily restricted net assets released from restriction, as their specific purpose or time period has been met during the reporting period, are reflected in the accompanying consolidated statements of operations.

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(j) Property and Equipment

Property and equipment acquisitions are recorded at cost, less accumulated depreciation. Depreciation is provided using the straight-line method over the estimated useful lives of the related asset, which are as follows:

	<u>Life</u>
Description of assets:	
Buildings and building improvements	10 – 40 years
Equipment	3 – 30 years
Leasehold improvements	5 – 25 years
Land improvements	10 – 20 years

(k) Other Assets

Deferred financing costs are being amortized over the respective terms of the related bond issues utilizing the effective-interest method. Other assets include noncompete arrangements and signing bonuses, which are amortized over the life of the respective arrangement.

(l) Long-Lived Assets and Goodwill

WPAHS reviews long-lived assets and certain identifiable intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Goodwill is reviewed for impairment at least annually. Management has reviewed the carrying amount of these assets and has determined that they are not impaired.

(m) Donor-Restricted Gifts

Unconditional promises to give cash and other assets to WPAHS are reported at fair market value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair market value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations as net assets released from restrictions. Donor-restricted contributions, whose restrictions are met within the same year as received, are reported as unrestricted contributions in the accompanying consolidated statements of operations.

(n) Income Taxes

WPAHS and all other member entities, with the exception of WPCMSI, WPAF, and FIC, are not-for-profit corporations that have been recognized as tax-exempt pursuant to Section 501(c)(3) of the Internal Revenue Code (IRC). WPCMSI is a taxable corporation. WPAF is a single member limited liability corporation. FIC is registered under the laws of the Cayman Islands.

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WPAHS adopted Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 740, *Income Taxes*, which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements. FASB ASC 740 prescribes a more-likely than-not recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken. Under FASB ASC 740, tax positions will be evaluated for recognition, de-recognition, and measurement using consistent criteria and will provide more information about the uncertainty in income tax assets and liabilities. Based on an analysis prepared by WPAHS, it was determined that the application of FASB ASC 740 had no material effect on the recorded tax assets and liabilities of WPAHS.

(o) ***Other Revenue***

Other revenue is derived from services other than providing healthcare services to patients. Included in other revenue are meaningful use incentive payments, grants, rent, parking, cafeteria, tuition, contract revenue, and sale leaseback gain amortization.

The Centers for Medicare & Medicaid Services (CMS) have implemented provisions of the American Recovery and Reinvestment Act of 2009 to provide incentive payments for the meaningful use of certified electronic health record (EHR) technology. CMS has defined meaningful use as meeting certain objectives and clinical quality measures based on current and updated technology capabilities over predetermined reporting periods as established by CMS. The Medicare EHR incentive program provides annual incentive payments to eligible professionals, hospitals, and critical access hospitals that are meaningful users of certified EHR technology. The Medicaid EHR incentive program provides annual incentive payments to eligible professionals and hospitals for efforts to adopt, implement, and meaningfully use certified EHR technology. WPAHS utilized a grant accounting model to recognize EHR incentive revenues. WPAHS records EHR incentive revenue ratably throughout the incentive reporting period when it is reasonably assured that it will meet the meaningful use objectives for the required reporting period and that the grants will be received. The EHR reporting period for the hospitals is based on the federal fiscal year, which runs from October 1 through September 30. In 2012, WPAHS recorded \$4,442 of Medicare revenues and \$5,350 of Medicaid revenues, for a total of \$9,792 in EHR incentives. Such amounts are included in other revenue on the consolidated statements of operations.

(p) ***Asset Retirement Obligations (ARO)***

WPAHS accounts for asset retirement obligations in accordance with FASB ASC 410, *Asset Retirement and Environmental Obligations*. FASB ASC 410 clarifies an entity is required to recognize a liability and capitalize costs for the fair value of a conditional ARO when incurred if the fair value of the liability can be reasonably estimated or when the entity has sufficient information to reasonably estimate the fair value of the ARO. FASB ASC 410 requires an ARO liability be recognized at its net present value, with a corresponding increase to the carrying amount of the long-lived asset to which the ARO relates. The ARO liability is accreted through periodic charges to accretion expense. The initially capitalized ARO long-lived asset cost is depreciated over the useful life of the related long-lived asset.

In the normal course of operations, WPAHS performs repairs and maintenance on its buildings. Additionally, WPAHS is involved in ongoing construction and renovation projects. WPAHS has

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identified costs that may be incurred for asbestos abatement, which would be legally required, if exposed as a result of such construction and renovation projects.

The significant assumptions and estimates used in the calculation of the AROs are based on the facts and circumstances known at that time of estimation. They include the estimated settlement date of the obligation, the estimated retirement obligation cost, the assumed inflation rate, and the discount rate.

WPAHS has an ARO liability to recognize the costs associated with future asbestos removal. This represents the present value of the expected future cash flows based on various potential settlement possibilities, including normal repairs and maintenance and currently known renovation plans between 2013 and 2049, which represents management's estimated time period for removal. The liability was \$4,280 and \$4,038 at June 30, 2012 and 2011, respectively. WPAHS has incurred costs of \$130 and \$548 in 2012 and 2011, respectively, relating to asbestos removal. Accretion expense and estimate revisions were \$372 in 2012 and \$364 in 2011. The ARO liability has been discounted using a rate of 9.0% as of the date of adoption.

(q) *Recently Issued Accounting Pronouncements*

In July 2011, the FASB issued Accounting Standards Update (ASU) No. 2011-07 (ASU 2011-07), *Health Care Entities (Topic 954): Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*. ASU 2011-07 requires health care entities that recognize significant amounts of patient service revenue at the time the services are rendered, even though they do not assess the patient's ability to pay, to present the provision for bad debts related to patient service revenue as a deduction from patient service revenue (net of contractual allowances and discounts) on their statement of operations. ASU 2011-07 will reclassify the provision for bad debts from an operating expense to a deduction from patient service revenue (net of contractual allowances and discounts). Additional disclosures are required related to policies for recognizing revenue and assessing bad debts and disclosures of patient service revenue (net of contractual allowances and discounts) as well as qualitative and quantitative information about changes in the allowance for doubtful accounts. This ASU is effective for the System on July 1, 2012. The System is currently evaluating the impact on its disclosures from the adoption of this pronouncement.

In May 2011, the FASB issued ASU No. 2011-04 (ASU 2011-04), *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. ASU 2011-04 resulted in common fair value measurement and disclosure requirements in U.S. generally accepted accounting principles (GAAP) and International Financial Reporting Standards (IFRSs). ASU 2011-04 is intended to clarify requirements in Topic 820, but also includes amendments where a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements has changed. For many of the requirements, this ASU is not intended to result in a change in the application of the requirements in Topic 820. This ASU is effective for the System on July 1, 2012. The adoption of this guidance is not expected to have a significant effect on the System's consolidated financial statements.

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In August 2010, the FASB issued ASU No. 2010-23 (ASU 2010-23), *Health Care Entities* (Topic 954): *Measuring Charity Care for Disclosure*. ASU 2010-23 is intended to reduce the diversity in practice regarding the measurement basis used in the disclosure of charity care. ASU 2010-23 requires that cost be used as the measurement basis for charity care disclosure purposes and that cost be identified as the direct and indirect costs of providing the charity care, and requires disclosure of the method used to identify or determine such costs. This ASU is effective for the System on July 1, 2011. The System adopted the provisions of this standard on July 1, 2011 and retrospectively applied the provisions to all periods presented. The adoption had no impact on the previously reported excess of expenses over revenues or net assets.

In August 2010, the FASB issued ASU No. 2010-24, *Health Care Entities* (Topic 954): *Presentation of Insurance Claims and Related Insurance Recoveries*. The amendments in the ASU clarify that a healthcare entity may not net insurance recoveries against related claim liabilities. In addition, the amount of the claim liability must be determined without consideration of insurance recoveries. This ASU is effective for the System on July 1, 2011. The System adopted the provisions of this standard on July 1, 2011 and retrospectively applied the provisions to all periods presented. The adoption had no impact on the previously reported excess of expenses over revenues or net assets.

In January 2010, the FASB issued ASU No. 2010-06 (ASU 2010-06), *Fair Value Measurements and Disclosures*, which clarifies certain existing fair value measurement disclosure requirements of ASC Topic 820 (Topic 820): *Fair Value Measurement* (formerly SFAS No. 157, *Fair Value Measurements*) and also requires additional fair value measurement disclosures. Specifically, ASU 2010-06 clarifies that assets and liabilities must be categorized by major class, or level, of asset or liability, and provides guidance regarding the identification of such major classes. Additionally, disclosures are required about valuation techniques and the inputs to those techniques, for those assets or liabilities designated as Level 2 or Level 3 instruments. Disclosures regarding transfers between Level 1 and Level 2 assets and liabilities are required, as well as a deeper level of disaggregation of activity within existing rollforwards of the fair value of Level 3 assets and liabilities. These additional fair value measurement disclosure requirements are applicable for interim and annual periods beginning after December 15, 2009, excluding the additional requirements related to Level 3 rollforward activity. This ASU is effective for the System on July 1, 2011. The System adopted the provisions of this standard on July 1, 2011 and retrospectively applied the provisions to all periods presented. The adoption had no impact on the previously reported excess of expenses over revenues or net assets.

(r) **Reclassifications**

Certain functional expenses included in the 2011 consolidated financial statements have been reclassified to conform with the 2012 presentation (see note 17).

(4) **Uncompensated Care and Community Service Benefits**

To improve the health of the people of the Western Pennsylvania region and consistent with its tax-exempt status, WPAHS provides needed healthcare services to individuals regardless of their ability to pay for all or part of the services rendered. These services include both inpatient and outpatient services as well as maintaining five emergency rooms that are available 24 hours a day, including a Level I regional resource

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trauma center, air and ground emergency transportation, and many primary care and specialty care practices that provide services to the community without regard to the ability to pay for services rendered.

WPAHS maintains a written charity care policy that defines the levels of household income that would qualify for various levels of charity care. Patients can qualify for charity care with household incomes of up to four times the federal poverty guidelines. WPAHS does not pursue collection of amounts that qualify as charity care in accordance with the policy, and as a result, these amounts are not reported as revenue. The cost for services and supplies provided for those individuals who applied for and qualified under the system charity care policy amount to \$4,832 and \$4,649 for the years ended June 30, 2012 and 2011, respectively. The System estimated these costs by applying the cost of total direct and indirect costs of each procedure to the individual charity care cases. Patients are required to apply for the charity care discount, but often do not complete the necessary paperwork to determine if they qualify. As a result, there is an unquantifiable amount of uncompensated services that would potentially be considered charity care under the policy, but rather are ultimately reflected in bad debt expense.

In addition to uncompensated care, WPAHS provides free and below cost services and programs for the benefit of the community. The cost of these programs is included in salaries, wages, and fringe benefits; patient care supplies; professional fees and purchased services; and other expense lines in the accompanying consolidated statements of operations.

Services are also provided to beneficiaries of government-sponsored programs, including state Medical Assistance and indigent care programs. Reimbursement from these programs is often less than the cost of providing these services.

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(5) Cash, Short-Term Investments, and Assets Limited or Restricted as to Use

Cash, short-term investments, and assets limited or restricted as to use as of June 30, 2012 and 2011 consist of the following components:

	<u>2012</u>	<u>2011</u>
Cash and cash equivalents	\$ 193,816	164,595
Short-term investments	5,108	5,075
Assets limited or restricted as to use:		
Unrestricted:		
Designated by board of directors for:		
Capital improvements	32,754	31,570
Foundation	41,088	39,693
Capital project funds	—	26,899
Debt service	57,479	57,175
Self-insurance	12,331	6,517
Grant funds and other	11,297	11,626
Total unrestricted	<u>154,949</u>	<u>173,480</u>
Temporarily restricted	23,210	23,425
Permanently restricted	223,072	234,113
Total assets limited or restricted as to use and beneficial interest in perpetual trust	<u>401,231</u>	<u>431,018</u>
Less current portion	<u>5,744</u>	<u>5,464</u>
Assets limited or restricted as to use, including beneficial interests in perpetual trusts – net of current portion	<u>395,487</u>	<u>425,554</u>
Total cash, short-term investments and assets limited or restricted as to use	<u>\$ 600,155</u>	<u>600,688</u>

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Cash, short-term investments, and assets limited or restricted as to use by investment type as of June 30, 2012 and 2011 consisted of the following:

	Fair value	
	2012	2011
Cash and short-term investments	\$ 237,258	245,625
Government and corporate obligations	158,118	125,633
Marketable equity securities	165	2,520
Endowments managed by donor selected trustees	196,062	207,020
Collective funds and fund of funds	122	4,506
Tactical asset allocation fund	165	7,137
Pledges receivable	828	1,032
Certificates of deposit	7,437	7,215
	<u>\$ 600,155</u>	<u>600,688</u>

The System's investments in collective funds and fund of funds are valued using net asset value (NAV) as a practical expedient for fair value. As of June 30, 2012 and 2011, there are no unfunded commitments to these investments. The conditions of withdrawal vary by individual investment and generally require a minimum notification of 90 days for withdrawal of funds as of quarterly measurement dates. Certain investments contain lock-up provisions for the first twelve months.

Investment income for the years ended June 30, 2012 and 2011 consisted of the following:

	2012		
	Unrestricted	Temporarily restricted	Permanently restricted
Dividends and interest – net of trustee fees	\$ 11,546	872	3,838
Net realized gains on investments	3,982	10	3,367
Net unrealized losses	(1,286)	—	—
	<u>\$ 14,242</u>	<u>882</u>	<u>7,205</u>

	2011		
	Unrestricted	Temporarily restricted	Permanently restricted
Dividends and interest – net of trustee fees	\$ 11,162	1,057	4,033
Net realized gains on investments	2,203	111	4,599
Net unrealized gains	4,519	—	—
	<u>\$ 17,884</u>	<u>1,168</u>	<u>8,632</u>

The recognition of unrealized gains and losses on investments that are restricted as to use are recorded directly to temporarily and permanently restricted net assets as required by donor or regulation. These

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investments consist primarily of marketable equity securities, federal agency mortgages, corporate bonds, and U.S. Treasury obligations. All unrealized gains and losses on unrestricted investments are recognized as part of investment income within the consolidated statements of operations.

During May 2000, the Orphan's Court of Pennsylvania permitted the election of a fixed investment income distribution under the provisions of Section 8113 (the Election) of the Pennsylvania Probate, Estate, and Fiduciaries Code for certain trust accounts, which name applicable WPAHS entities as the sole beneficiary. The Pennsylvania legislature enacted legislation with respect to charitable Trusts, which permits a Trustee of a charitable Trust to adopt a total return investment policy and, by doing so, to redefine income as a percentage of a rolling average market value of the charitable Trust as averaged over a period of at least three years; provided, however, that such election is not in contravention of the terms of the charitable Trust agreement and is consistent with the long term preservation of the principal value of the charitable Trust.

The provisions of the law governing these changes are found at 20 PA.C.S.A. 8113 and took effect December 21, 1998. If an election is made under this law, the percentage of the market value of the charitable Trust to be treated as income and the rolling time period upon which the percentage is based is to be redetermined annually by the Trustee; such election is to be in writing. Further, the percentage that may be elected is limited to a range between 2% – 7%. Lastly, the statute contains language that cautions against electing the highest ranges of 6% and 7% on a regular basis. Distributions from these charitable Trusts are included in investment income in the accompanying consolidated statements of operations and totaled \$5,620 and \$7,013 for the years ended June 30, 2012 and 2011, respectively. Under the provisions of the Election, there is no settlement with the Trustee should the Trustee be permitted to revoke the Election.

(6) Fair Value Measurements and the Fair Value Option

The following methods and assumptions were used in estimating the fair value of WPAHS' financial instruments:

(a) Fair Value of Financial Instruments

Cash and Cash Equivalents – The carrying value reported in the consolidated balance sheets for cash and cash equivalents approximates their fair value.

Marketable Securities, Short-Term Investments, and Assets Limited or Restricted as to Use – Fair values of the securities are reported in the consolidated balance sheets and are based on quoted market prices, if available, or estimated using quoted market prices for similar securities. Certain investments are considered alternative investments are reported at NAV, which is used as a practical expedient for fair value.

Accounts Payable and Other Accrued Liabilities – The carrying value reported in the consolidated balance sheets for these obligations approximates their fair value.

Self-Insurance Liabilities – The carrying and fair values of the self-insurance liabilities are actuarially determined.

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Long-Term Debt – Fair value of WPAHS' revenue bonds and notes are based on current traded value. The fair value and carrying amounts of the Series 2007A bonds were \$605,825 and \$725,775, respectively, at June 30, 2012 and \$622,731 and \$736,999, respectively, at June 30, 2011. WPAHS has determined that it is not practical to estimate the fair value of the Floating Rate Restructuring Certificates and the Series 2006A and B notes without incurring excessive costs as a quoted market price is not available. The fair value of the mortgage loan approximates its carrying value as it is a resettable rate debt. The fair value of the Highmark Note Payable approximates its carrying value.

Endowments Managed by Donor-Selected Trustees – Permanently restricted net assets consist of amounts held in perpetuity as designated by donors, including the System's portion of beneficial interests in several endowments managed by donor-selected trustees. The interest in these trusts is measured at the fair market value of the underlying investments, which approximates the present value of the expected future cash flows, for which the System is an income beneficiary.

Pledges Receivable – Pledges receivable are recorded upon receipt of written correspondence from the donor for the original amount of the pledge, less a reserve for potential uncollectible amounts estimated by management. This amount is assumed to approximate the fair value of the pledge receivable balance.

(b) ***Fair Value Hierarchy***

ASC 820, *Fair Value Measurement* establishes a framework in generally accepted accounting principles for measuring fair value and expands disclosures about fair value measurements. Although it does not require any new fair value measurements, ASC 820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and should be determined based on the assumptions that market participants would use in pricing the asset or liability.

ASC 820 establishes a hierarchy for ranking the quality and reliability of the information used to determine fair values. The hierarchy gives the highest priority to unadjusted quoted prices in active markets (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of fair value hierarchy are as follows:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 – Observable inputs other than quoted prices in Level 1. Inputs such as quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar liabilities that are not active, or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Unobservable inputs that are significant to the valuation of assets or liabilities and are supported by little or no market data.

Quoted market prices are used when available to determine the fair value of investment securities and these are categorized as Level 1. The inputs used to fair value Level 1 instruments are unadjusted quoted prices derived from stock exchanges as provided by the trustee. Level 1 instruments primarily consist of cash and cash equivalents, domestic equities, foreign equities, exchange traded funds, regulated investment companies, and exchange traded American deposit receipts and certain government securities.

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Investments in Level 2 primarily comprise corporate bonds, international bonds, and asset-backed securities and agency bonds. Level 2 inputs primarily consist of contract prices, quotes from independent pricing vendors based on recent trading activity and other relevant information including matrix pricing, market corroborated pricing, yield curves and other indices, which are used as provided by the trustee when Level 1 inputs are not available.

Investments classified as Level 3 in the fair value hierarchy include collective funds, the tactical asset allocation fund, and fund of funds. These assets are valued using inputs such as the funds' net asset value as of year-end as a practical expedient for the fair value of the investment.

The following table presents assets that are measured at fair value on a recurring basis at June 30, 2012:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Assets measured at fair value:				
Cash and cash equivalents	\$ 237,019	239	—	237,258
Government and corporate obligations	71,222	86,896	—	158,118
Marketable equity securities	165	—	—	165
Endowments managed by donor selected trustees	—	—	196,062	196,062
Collective funds and fund of funds	—	—	122	122
Tactical asset allocation fund	—	—	165	165
Pledges receivable	—	—	828	828
Certificates of deposit	7,437	—	—	7,437
	<u>315,843</u>	<u>87,135</u>	<u>197,177</u>	<u>600,155</u>
Total assets measured at fair value	\$ <u>315,843</u>	<u>87,135</u>	<u>197,177</u>	<u>600,155</u>

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The following table presents assets that are measured at fair value on a recurring basis at June 30, 2011:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Assets measured at fair value:				
Cash and cash equivalents	\$ 245,332	293	—	245,625
Government and corporate obligations	60,070	65,563	—	125,633
Marketable equity securities	2,520	—	—	2,520
Endowments managed by donor selected trustees	—	—	207,020	207,020
Collective funds and fund of funds	—	—	4,506	4,506
Tactical asset allocation fund	—	—	7,137	7,137
Pledges receivable	—	—	1,032	1,032
Certificates of deposit	7,215	—	—	7,215
	<u>315,137</u>	<u>65,856</u>	<u>219,695</u>	<u>600,688</u>
Total assets measured at fair value	\$ <u>315,137</u>	<u>65,856</u>	<u>219,695</u>	<u>600,688</u>

WPAHS holds assets valued using unobservable inputs (Level 3) at June 30, 2012. These assets increased (decreased) as a result of the changes below:

	<u>Tactical asset allocation fund</u>	<u>Collective funds and fund of funds</u>	<u>Endowments managed by donor selected trustees</u>	<u>Pledges receivable</u>	<u>Total</u>
Beginning balance	\$ 7,137	4,506	207,020	1,032	219,695
Realized and unrealized gains	425	214	7,211	—	7,850
Realized and unrealized losses	(425)	(470)	(8,474)	—	(9,369)
Disbursements and transfers out	(6,972)	(4,128)	(9,695)	(17)	(20,812)
Contributions and transfers in	—	—	—	131	131
Collection of pledges	—	—	—	(318)	(318)
Ending balance	\$ <u>165</u>	<u>122</u>	<u>196,062</u>	<u>828</u>	<u>197,177</u>

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WPAHS holds assets valued using unobservable inputs (Level 3) at June 30, 2011. These assets increased (decreased) as a result of the changes below:

	Tactical asset allocation fund	Collective funds and fund of funds	Endowments managed by donor selected trustees	Pledges receivable	Total
Beginning balance	\$ 5,689	8,150	181,508	2,004	197,351
Realized and unrealized gains	1,448	1,252	38,639	—	41,339
Realized and unrealized losses	—	—	(3,269)	—	(3,269)
Disbursements and transfers out	—	(4,896)	(9,911)	—	(14,807)
Contributions and transfers in	—	—	53	389	442
Collection of pledges	—	—	—	(1,361)	(1,361)
Ending balance	<u>\$ 7,137</u>	<u>4,506</u>	<u>207,020</u>	<u>1,032</u>	<u>219,695</u>

(c) Fair Value Option

WPAHS elected the fair value option for its unrestricted investments effective July 1, 2008. As a result, all unrealized gains and losses on unrestricted investments are included in the excess (deficiency) of revenues over expenses. The System has recorded \$1,286 of net unrealized losses and \$4,519 of net unrealized gains (included in investment income) in 2012 and 2011, respectively.

(7) Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets at June 30, 2012 and 2011 are available for the following purposes:

	<u>2012</u>	<u>2011</u>
Capital expansion and renovation	\$ 9,651	9,488
Clinical programs	13,559	13,937
	<u>\$ 23,210</u>	<u>23,425</u>

Temporarily restricted net assets for capital expansion and renovation represent donations, gifts, and pledges made for specific capital projects at WPAHS hospitals. Temporarily restricted net assets for clinical programs represent donations, gifts, and pledges made to support specific clinical programs or departments at WPAHS hospitals.

Permanently restricted net assets totaling \$223,072 and \$234,113 at June 30, 2012 and 2011, respectively, are restricted to be invested in perpetuity. Income distributions generated from these net assets are either classified as unrestricted and may be used for any purpose or are classified as temporarily restricted based on donor restrictions. At June 30, 2012, permanently restricted net assets consist of endowments managed by donor-selected trustees of \$196,062 and endowments managed by the System of \$27,010. Collectively,

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all these funds are included as permanently restricted assets within limited or restricted as to use. The System has determined that all such funds are donor restricted.

Changes in System-Managed Endowment Net Assets

	<u>2012</u>	<u>2011</u>
Beginning balance	\$ 27,093	25,593
Investment return:		
Interest and dividend income	25	55
Realized (losses) gains	(31)	25
Unrealized (losses) gains	(100)	657
Total investment (losses) gains	(106)	737
Contributions	4	447
Other transfers	19	316
Ending balance	\$ <u>27,010</u>	<u>27,093</u>

(8) Property and Equipment

Property and equipment at June 30, 2012 and 2011 consist of the following:

	<u>2012</u>	<u>2011</u>
Buildings and building improvements	\$ 597,888	595,211
Equipment	547,174	477,916
Leasehold improvements	43,203	37,377
Total depreciable assets	1,188,265	1,110,504
Less accumulated depreciation and amortization	(862,496)	(811,276)
Net depreciable assets	325,769	299,228
Land and land improvements	29,228	28,755
Construction in progress	39,073	41,235
Property and equipment – net	\$ <u>394,070</u>	<u>369,218</u>

WPAHS capitalizes interest on certain assets that require a period of time to prepare for their intended use. The amount capitalized is based on the weighted average outstanding borrowing rate of WPAHS' indebtedness. During the years ended June 30, 2012 and 2011, WPAHS capitalized \$2,984 and \$3,440, respectively, of related interest costs. Depreciation expense was \$64,905 and \$59,156 for the years ended June 30, 2012 and 2011, respectively.

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(9) Other Assets

Other assets at June 30, 2012 and 2011 consist of the following:

	<u>2012</u>	<u>2011</u>
Prefunded insurance deductible (note 15)	\$ 25,510	26,407
Deferred bond financing costs – net of accumulated amortization of \$3,965 and \$3,200, respectively	13,154	13,919
Note receivable in CHA RRG	3,185	3,185
Investment in CHA RRG (note 15)	4,465	2,602
Intangibles – net of accumulated amortization of \$10,587 and \$10,105, respectively	5,223	5,705
Insurance recoveries (note 15)	18,960	23,525
Other	4,799	4,665
Total	<u>\$ 75,296</u>	<u>80,008</u>

(10) Medical Resident FICA Refund

In March 2010, the Internal Revenue Service (IRS) issued an administrative determination to accept the position that medical students are excepted from FICA taxes based on the student exception for tax periods ending prior to April 1, 2005. The System had previously remitted such FICA taxes to the IRS, but had also filed protective claims pending the IRS administrative determination. The System has filed perfected claims with the IRS and has recorded \$16,652 and \$23,307 as the anticipated employer refund, including accrued interest. This amount is included in other receivables at June 30, 2012 and 2011, respectively. The System also recorded amounts payable to the former residents of approximately \$7,700 within other current liabilities at June 30, 2012 and 2011.

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(11) Long-Term Debt

Long-term debt as of June 30, 2012 and 2011 consists of the following:

	<u>2012</u>	<u>2011</u>
Allegheny County Hospital Development Authority (ACHDA) – Series 2007 A with maturity dates through November 15, 2040, and interest rates ranging from 5.00% to 5.375%, including a net unamortized premium of \$4,605 and \$4,904 at June 30, 2012 and 2011, respectively	\$ 725,775	736,999
Floating Rate Restructuring Certificates (FRRC) – payable based on attainment of defined income and cash levels, with a variable interest rate of the three-month London InterBank Offered Rate (LIBOR), plus 0.25% (0.72% and 0.50% at June 30, 2012 and 2011, respectively), thereafter until maturity on June 30, 2030	37,084	37,084
Series 2006 B Health Facilities Revenue Notes – payable in monthly principal and interest payments through October 2015, with interest rates ranging from 4.55% to 4.61%	18,450	19,741
Series 2006 A Health Facilities Revenue Notes – payable in monthly principal and interest payments through December 2016, at a fixed interest rate of 5.25% for all payments	1,811	2,450
Highmark Notes Payable – principal is payable in two \$50,000 payments due in 2023 and 2024 with interest payable semi-annually based on the prime rate plus 2.00% (5.25% at June 30, 2012)	100,000	—
Equipment Notes – payable in monthly principal and interest payments through June 2016, with interest rates ranging from 7.00% to 7.55%	8,516	7,466
Mortgage loan	3,066	3,205
Other	—	289
	<u>894,702</u>	<u>807,234</u>
Total		
Less current portion	<u>15,866</u>	<u>14,742</u>
Total long-term debt	<u>\$ 878,836</u>	<u>792,492</u>

(a) Series 2007 A

In June 2007, the System issued \$752,400 of Allegheny County Hospital Development Authority Health System Revenue Bonds (West Penn Allegheny Health System Series 2007 A, the Series 2007 A bonds). Proceeds of the Series 2007 A bonds were used to advance refund the outstanding Allegheny County Hospital Development Authority Series 2000 A and B bond issues and to current refund the Dauphin County General Authority Series 1992 A and B Hospital Revenue Bonds, the Pennsylvania Higher Education Facility Authority Series 1991 A Revenue Bonds, the Monroeville Hospital Authority Series 1992 and 1995 Revenue Bonds, and partially refund an outstanding loan from Highmark.

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The Series 2007 A bonds are a liability of the Obligated Group. Each member of the Obligated Group is jointly and severally liable for payment of this obligation.

The Series 2007 A bonds are subject to mandatory redemption on November 15, 2017, November 15, 2028, and November 15, 2040, based on the mandatory sinking fund dates as disclosed in the official statement. They are subject to redemption prior to their respective stated maturity dates, in part, or by lot, on variable dates as disclosed in the official statement at the discretion of WPAHS and the ACHDA. Under the Master Indenture of Trust (MIT), interest is payable to the bondholders semiannually on each May 15 and November 15.

The Series 2007A bonds are secured by (i) first mortgage liens on certain real property, (ii) security interests in certain equipment and other tangible and intangible personal property of the Obligated Group, and (iii) gross revenues of the Obligated Group. Debt service reserve accounts in the amount of \$51,735 and \$51,711 at June 30, 2012 and 2011, respectively, exist for the Series 2007A bonds, which must be maintained at required reserve levels.

Under the MIT, the Obligated Group has covenants including, but not limited to, a long-term debt service coverage ratio of 1.1 and days cash on hand of 35 (both measured annually at June 30). As of June 30, 2012 (most recent measurement date), WPAHS was in compliance with these covenants.

(b) FRRCs

In 2000, certain creditors of AGH and its affiliates restructured approximately \$114,000 of indebtedness by exchanging such indebtedness for approximately \$76,900 in cash and approximately \$37,100 in principal amount of FRRCs. Initially, no interest accrued on the FRRCs. Beginning July 1, 2003, the FRRCs bear interest at the three-month LIBOR plus 0.25%. Payment of interest is contingent upon achieving certain profitability thresholds and maintaining specified liquidity levels. AGH has never been required to make an interest payment. Management believes the probability of future interest payments to be remote and has, therefore, not recorded interest to date.

Subject to the FRRC Cap, if applicable, the owners of the FRRCs are entitled to receive an annual single payment of 25% (30% if unenhanced indebtedness of any other member of the Obligated Group is rated A or better) of the adjusted net operating income of the Obligated Group as defined in the FRRC indenture, calculated as of each June 30 commencing June 30, 2004. Payments are also contingent upon achieving and maintaining specified liquidity levels. No payments have ever been due under the FRRCs.

(c) Series 2006 B & A

In December 2006, WPAF entered into two note agreements with the issuance of Series 2006 B notes in the amount of \$24,000 and Series 2006 A note in the amount of \$4,950 to purchase four new helicopters and hospital beds, respectively. The notes are collateralized by the acquired helicopters and beds, respectively.

The Series 2006 B Health Facilities Revenue Notes (Series 2006 B Notes), and the Series 2006 A Health Facilities Revenue Note (Series 2006 A Note), and the mortgage loan are solely the obligation of WPAF.

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(d) Highmark Note Payable

In October 2011, WPAHS received a \$50,000 loan from Highmark with principal payments of \$25,000 each due in 2023 and 2024. In April 2012, WPAHS received an additional \$50,000 loan from Highmark with principal payments of \$25,000 each due in 2023 and 2024. Interest for both loans is payable semi-annually based on the prime rate plus 2.00%.

(e) Other Long-Term Debt

The System has entered into other notes and mortgages to finance various capital purchases. The interest and principal on these instruments are payable through 2026 at interest rates ranging from 2.16% to 7.55%.

Scheduled principal repayments and sinking fund requirements on all long-term debt for the next five years and thereafter as of June 30, 2012 are as follows:

	Total obligated group	WPAF	Total consolidated group
Year ending June 30:			
2013	\$ 13,764	2,102	15,866
2014	14,516	1,959	16,475
2015	15,073	8,958	24,031
2016	14,652	7,844	22,496
2017	14,134	340	14,474
Thereafter	794,631	2,124	796,755
	<u>\$ 866,770</u>	<u>23,327</u>	<u>890,097</u>

(12) Deferred Revenue

Deferred revenue at June 30, 2012 and 2011 consists of the following:

	2012	2011
Prepaid patient service revenue	\$ 25,000	25,000
Deferred grant revenue	22,950	23,495
Unamortized gains	3,123	3,830
Other	1,428	1,146
Total	<u>\$ 52,501</u>	<u>53,471</u>

In December 2006, WPAHS entered into a long-term contract with a commercial payor whereby System facilities and providers provide healthcare services to the payor's members at discounted amounts for a period of approximately 10 years. The System received \$35,000 in connection with this agreement, which has been reflected as deferred revenue in the accompanying consolidated financial statements and is being amortized on a straight-line basis over the life of the related contracts consistent with the earnings process.

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At June 30 2010, \$23,333 received from the agreements was included in deferred revenue within the accompanying consolidated balance sheets. During 2011 the agreement between the commercial provider and the System was terminated. The terms of the termination agreement allowed the System to retain the remaining unamortized deferred revenue. The remaining unamortized deferred revenue of \$23,333 was recognized into income as other revenue on the consolidated statements of operations.

In April 2011, WPAHS received an advance in the amount of \$25,000 from a commercial payor. This amount will be used to offset future reimbursements from the commercial payor. The terms of this agreement and the term for recognition have not been finalized.

The System records deferred revenue as nongovernmental grant monies are received. Revenue is subsequently recognized as grant proceeds are expended. During the years ended June 30, 2012 and 2011, grant proceeds of \$23,092 and \$21,461, respectively, were expended and recognized as other revenue. The System also records, as deferred revenue, governmental grant monies received for the acquisition of property and equipment. The amount deferred is amortized over the estimated useful life of the assets acquired. At June 30, 2012 and 2011, \$22,950 and \$23,495, respectively, of grant funds are included in deferred revenue within the accompanying consolidated balance sheets.

During the years ended June 30, 1997 and 1996, AGH sold certain nonclinical assets, which are being leased back by AGH over 20 years. These transactions resulted in gains, which have been deferred and will be amortized on a straight-line basis into income over the lease terms. The annual amortization is included in other revenue in the accompanying consolidated statements of operations. Unamortized gains of \$3,123 and \$3,830 are included in deferred revenue at June 30, 2012 and 2011, respectively.

(13) Commitments

Rental expense consists of amounts paid to lease property for physician offices, a network of ambulatory locations, parking garages, and administrative offices. In addition, WPAHS leases clinical and administrative equipment. Equipment leases involve both noncancelable operating leases as well as ordinary month-to-month rentals for items that are used as the need arises based on the volume or mix of procedures and, therefore, are not practical to purchase. The components of rental expense, which are recorded within general and administrative on the consolidated statements of operations for the years ended June 30, 2012 and 2011, are as follows:

	<u>2012</u>	<u>2011</u>
Property rentals	\$ 32,031	28,194
Equipment rentals and other	<u>16,515</u>	<u>17,558</u>
Total	<u>\$ 48,546</u>	<u>45,752</u>

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The future minimum lease payments under noncancelable operating leases entered into as of June 30, 2012 are as follows:

Year ending June 30:		
2013	\$	30,353
2014		25,967
2015		22,518
2016		21,719
2017		15,189
Thereafter		<u>77,517</u>
Total minimum payments	\$	<u><u>193,263</u></u>

The System has renewed a noncancelable sponsorship and advertising agreement that includes performance obligations that requires the System to spend an additional \$21,805 through 2020.

During 2011, the System terminated its previous agreements to replace the information systems at most of the WPAHS hospitals and subsequently entered into agreements committing approximately \$43,500. Of this amount, approximately \$16,000 has been expended at June 30, 2012. The implementation of the systems is expected to be completed by 2018. The agreement includes certain provisions for early termination by WPAHS after March 2012.

Approximately, 22% of employees are covered by collective bargaining agreements through participation in nine bargaining units. These bargaining units have expiration dates ranging between 2013 and 2015.

WPAHS has employment agreements with physicians, specialists, and others. These agreements are for periods up to 10 years and require services to be performed.

(14) Income Taxes

No provision for income taxes has been recognized in the accompanying consolidated financial statements as WPCMSI has incurred net operating losses in most years prior to fiscal year 2012, which are available to offset current and future taxes payable. A valuation allowance of approximately \$18,000 has been established to fully reserve the deferred tax asset associated with the cumulative net operating losses of approximately \$44,500, which expires between 2013 and 2031, as future earnings are not estimated to be sufficient to realize the asset before the net operating loss carry forward expires.

(15) Insurance**(a) Workers' Compensation**

Prior to 1999, WPAHS was self-insured for workers' compensation claims. From 1999 through October 14, 2004, WPAHS purchased occurrence-based commercial insurance for workers' compensation claims. The coverage was for \$250 per claim at AKMC, CGH, and FRC and \$350 per claim at AGH and WPH. From October 15, 2004, through October 15, 2011, WPAHS was self-insured for workers' compensation claims and purchased excess insurance coverage of \$350 per claim for all of its hospitals on an occurrence-basis. On October 15, 2011, WPAHS purchased high-deductible occurrence-based commercial insurance for workers' compensation claims. The

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coverage requires WPAHS to pay the first \$350 per claim. During the 12 months ended June 30, 2012 and 2011, WPAHS' workers' compensation expense was \$3,415 and \$2,875, respectively, and is recorded within the consolidated statements of operations. A liability for WPAHS' self-insured workers' compensation of \$9,799 and \$9,301 as of June 30, 2012 and 2011, respectively; this amount includes a related insurance recovery of \$3,160 and \$3,325, which is included in other assets.

(b) General and Professional Liability

Beginning in 2003, the System has been insured through Community Health Alliance Reciprocal Risk Retention Group (CHA), a Vermont domiciled risk retention group. The System owns 53% of CHA and has a 20% voting interest. The investment in CHA is accounted for using the equity method. The System's share of equity income or loss from CHA is included as a nonoperating income or loss. CHA provides medical professional liability and general liability coverages to the System and its physicians. The coverages provided are comprised of several layers, as described below.

The primary layer provides claims made medical professional liability coverage with limits of \$500 per occurrence for hospitals and physicians with annual aggregates of \$2,500 per hospital and \$1,500 per physician. The System records an actuarially determined reserve for aggregate primary layer losses in excess of the annual aggregate. The primary layer also provides occurrence basis general liability coverage to hospitals of \$1,000 per occurrence and \$3,000 in the annual aggregate. Defense costs do not erode the coverage limits provided within the primary layer. Policies in this layer are subject to various retroactive dates. The policy offers tail coverage to departing physicians for an additional premium. The coverage provided in the primary layer is retained 100% by CHA.

The limits within the primary layer are subject to a self-funded \$250 per occurrence deductible. The deductible paid by the System in any policy year is limited by a stop loss point. This stop loss point is calculated as two times the actuarially determined estimated deductible layer losses. The losses estimated to reach the deductible layer have been paid to CHA by the System. The amounts paid in for the deductible layer may be assessed in future years for additional amounts in the event that the System has loss experience pertaining to the deductible layer over and above the amounts paid in. Additional amounts charged in future periods will not exceed the stop loss point. Furthermore, these deposits may be refunded if the System's loss experience applied against the deductible layer is less than the amounts paid in.

The coverages provided by CHA are subjected to MCARE (Medical Care Availability and Reduction of Error Fund). Participation in the MCARE fund is required for all Pennsylvania hospitals and hospital physicians. System hospitals and physicians are required to pay assessments into the MCARE fund on an annual basis. The MCARE fund provides medical professional liability coverage in excess of the required primary layer coverages as described above. The coverage provided by the MCARE fund is \$500 per occurrence and \$1,500 in the annual aggregate for both hospitals and physicians. Claims, which penetrate the MCARE fund's limits, are filed directly with the Commonwealth of Pennsylvania. CHA bills the System for MCARE assessment and remits the entire amount to the MCARE Fund.

The first excess layer provides claims made medical professional liability coverage and occurrence based general liability coverage to the System in excess of the primary and MCARE layers.

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Additionally, the first excess layer provides occurrence basis coverage for employer's liability in excess of the System's third party coverage. Limits on coverage are the difference between \$2,000 plus the remaining amount of the underlying coverage per occurrence and \$5,000 in the annual aggregate for the System with a shared maximum annual aggregate of \$10,000 for CHA. The annual aggregate and shared annual aggregate is shared among all lines of coverage noted above. Coverage is subject to various retroactive dates. Defense costs erode the coverage limits provided in the first excess layer and coverage is 100% retained by CHA.

The second excess layer provides claims made medical professional liability coverage and occurrence based general liability coverage to hospitals in excess of the primary, MCARE and first excess layers. Additionally, the second excess layer provides occurrence basis coverage for employer's liability in excess of the System's third party coverage and the first excess layer. Limits on coverage are \$9,000 per occurrence and \$18,000 in the annual aggregate for the System. This coverage is subject to a shared maximum annual aggregate of \$45,000 for CHA. The annual aggregate and shared annual aggregate is shared among all lines of coverage noted above. Coverage is subject to various retroactive dates. Defense costs erode the coverage limits provided in the excess layer. Reinsurance has been obtained by CHA for the second excess layer from two commercial reinsurers. The reinsurance agreement provides for coverage of \$9,000 per occurrence with a shared maximum annual aggregate of \$27,000 in excess of an \$18,000 shared maximum annual aggregate retention by the CHA. Reinsurance coverage includes defense costs and a one-year extended reporting period option.

The System's first and second excess layers are subject to a self-insured retention layer of \$5,000. The System records an actuarially determined reserve for estimated losses in the self-insured retention layer.

The third excess layer provides claims made medical professional liability coverage and occurrence based general liability coverage to hospitals in excess of the primary, MCARE, first and second excess layers. Additionally, the third excess layer provides employers' liability occurrence basis coverage in excess of the System's third party coverage and the first and second excess layers. Limits on coverage are \$10,000 per occurrence and \$10,000 in the annual aggregate for the System with a shared maximum annual aggregate of \$30,000 for CHA. The annual aggregate and shared annual aggregate is shared among all lines of coverage noted above. Coverage is subject to various retroactive dates. Defense costs erode the coverage limits provided in this excess layer. This layer is 100% reinsured by CHA in the commercial market with one reinsurer. Reinsurance coverage includes defense costs.

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The unaudited financial statement information as of and for the year ended June 30, 2012 and 2011 of CHA RRG, which has a calendar year-end, is as follows:

	<u>2012</u>	<u>2011</u>
Total assets	\$ 135,070	142,079
Total liabilities	117,940	128,171
Total equity	17,131	13,908
Total revenue	19,209	19,045
Total expense	16,162	30,091
Net income (loss) (including federal income tax benefit)	3,047	(11,046)

WPAHS provides for the costs associated with general and professional liability claims based on actuarially determined projected settlements, which include estimates for claims incurred but not reported. There exists, however, inherent risks in the areas of general and professional liability insurance that stem from, among other things, coverage availability and the financial viability of the underlying insurance carrier.

During the 12 months ended June 30, 2012 and 2011, WPAHS' general and professional liability expense was \$22,060 and \$25,578, respectively. WPAHS' self-insured general and professional liability was \$70,899 and \$76,538, as of June 30, 2012 and 2011, respectively; this amount includes a related insurance recovery of \$15,800 and \$20,200, which is included in other assets.

(16) Pension Plans**(a) Defined Benefit Plans**

WPAHS maintains the Retirement Plan for the employees of West Penn Allegheny Health System, a defined benefit cash balance pension plan. Under this cash balance plan, pension accruals are determined using a defined percentage of an employee's current compensation based upon the employee's age and years of service. Each employee's individual retirement benefit is defined within the plan's obligation as notational cash balance retirement accounts and is credited with interest based upon a defined interest rate.

WPAHS' investment policy is to provide for the benefit obligations earned by employees during their career at WPAHS. Plan assets are invested to generate earnings over an extended time period to help fund the cost of benefits under the plan while controlling investment fees.

WPAHS' funding policy is to contribute such amounts, as necessary, on an actuarial basis to provide the plan with assets sufficient to meet benefits to be paid to retirees or their beneficiaries, and to satisfy minimum funding requirements of Employee Retirement Income Security Act of 1974, and the IRC. Plan assets are invested primarily in corporate common stocks, fixed income obligations of the United States government and corporations, and interests in collective trusts and mutual funds.

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The funded status at measurement dates of June 30, 2012 and 2011 and amounts recognized in the consolidated financial statements at June 30, 2012 and 2011, relating to employee retirement benefits are as follows:

	<u>2012</u>	<u>2011</u>
Accumulated benefit obligation, including vested benefits of \$581,106 and \$560,472 in 2012 and 2011, respectively	\$ 756,539	641,481
Change in projected benefit obligation:		
Projected benefit obligation – beginning	\$ 652,597	673,336
Service cost	21,198	22,269
Interest cost	33,447	33,281
Plan participants' contributions	205	—
Actuarial loss (gain)	104,744	(19,937)
Benefits paid	(43,638)	(56,352)
Projected benefit obligation – ending	<u>768,553</u>	<u>652,597</u>
Change in plan assets:		
Fair value plan assets – beginning	456,341	375,513
Actual gain on plan assets	44,943	61,470
Employer contributions	32,039	75,710
Plan participants' contributions	205	—
Benefits paid	(43,638)	(56,352)
Fair value of plan assets – ending	<u>489,890</u>	<u>456,341</u>
Projected benefit obligation in excess of fair value of plan assets	<u>\$ 278,663</u>	<u>196,256</u>
Weighted average assumption used to determine benefit obligations:		
Discount rate	3.90%	5.30%
Rate of compensation increase	2.9% – 6.1%	2.9% – 6.1%
	Graded	Graded

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	<u>2012</u>	<u>2011</u>
Components of net periodic pension costs:		
Service cost	\$ 21,198	22,269
Interest cost	33,447	33,281
Expected return on plan assets	(37,909)	(37,258)
Amortization of actuarial losses	17,194	18,332
Amortization of prior service cost	(6,438)	(6,773)
Net periodic pension cost	<u>\$ 27,492</u>	<u>29,851</u>
Weighted average assumptions used to determine net cost:		
Discount rate	5.30%	5.20%
Expected long-term return on plan assets	7.65	7.65
Rate of compensation increase	2.9% – 6.1%	2.9% – 6.1%
	Graded	Graded

The net actuarial loss and prior service cost (credit) not yet recognized into net periodic pension cost was \$353,363 and \$(40,902), respectively, at June 30, 2012. The net actuarial loss and prior service cost (credit) not yet recognized into net periodic pension cost was \$272,852 and \$(47,340), respectively, at June 30, 2011. The net actuarial losses and prior service costs (credits) that were amortized from unrestricted deficit into net periodic pension cost were \$17,194 and \$(6,439) in 2012 and \$18,332 and \$(6,773) in 2011. The net actuarial loss and prior service cost (credit) that will be amortized from unrestricted deficit into net periodic pension cost in 2013 is \$25,141 and \$(5,713).

The System is required to abide by the minimum funding requirements of Section 412 of the IRC. Based on most recent actuarial estimates, the System is required to fund \$37,651 during the year ending June 30, 2013.

The discount rate used to value plan liabilities is a weighted average spot rate generated by bond yield curves, rounded down to the next five basis points.

The long-term expected rate of return on pension investments is developed by independent estimates of forward looking rates of return by investment category, multiplied by the target investment allocation mix.

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WPAHS' pension plan weighted average asset allocation at June 30, 2012 and 2011 by asset category are as follows:

	<u>Actual 2012</u>	<u>Actual 2011</u>	<u>Target ranges</u>
Plan assets:			
Domestic equity securities and funds	37%	40%	35% – 45%
Debt securities and funds	40	40	35% – 45%
International equity securities and funds	11	17	8% – 18%
Alternative investment fund of funds	—	—	4% – 10%
Cash, cash equivalents, and others	12	3	0% – 10%
Total	<u>100%</u>	<u>100%</u>	

The adoption of Topic 715 required that the fair value hierarchy disclosures as defined by FASB ASC 820 be applied to assets held within the Plan. Refer to note 6 for Level definitions.

The following table presents assets that are measured at fair value on a recurring basis at June 30, 2012:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Plan assets:				
Domestic equity securities and funds	\$ 185,450	—	—	185,450
Debt securities and funds	54,480	137,268	—	191,748
International equity securities and funds	51,739	—	—	51,739
Alternative investment fund of funds	—	—	1,568	1,568
Cash and cash equivalents	—	59,385	—	59,385
Total	<u>\$ 291,669</u>	<u>196,653</u>	<u>1,568</u>	<u>489,890</u>

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The following table presents assets that are measured at fair value on a recurring basis at June 30, 2011:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Plan assets:				
Domestic equity securities and funds	\$ 184,134	—	—	184,134
Debt securities and funds	49,266	132,338	—	181,604
International equity securities and funds	76,324	—	—	76,324
Alternative investment fund of funds	—	—	1,568	1,568
Cash and cash equivalents	—	12,711	—	12,711
Total	<u>\$ 309,724</u>	<u>145,049</u>	<u>1,568</u>	<u>456,341</u>

The Plan holds certain alternative investments including hedge fund of funds and global real estate. Refer to note 6 for asset valuation information. The Plan holds assets valued using unobservable inputs (Level 3) at June 30, 2012. These assets did not fluctuate in value during the year ended June 30, 2012.

The Plan held assets valued using unobservable inputs (Level 3) at June 30, 2011. These assets increased (decreased) as a result of the changes below:

	<u>International equity securities and funds</u>	<u>Tactical asset allocation fund</u>	<u>Alternative investment fund of funds</u>	<u>Total</u>
Beginning balance	\$ 16,558	52,971	30,506	100,035
Realized and unrealized gains	9,219	13,248	1,881	24,348
Realized and unrealized losses	(5,882)	(1,776)	(1,128)	(8,786)
Contributions and cash receipts	—	—	2	2
Disbursements and transfers out	(19,895)	(64,443)	(29,693)	(114,031)
Ending balance	<u>\$ —</u>	<u>—</u>	<u>1,568</u>	<u>1,568</u>

WPAHS maintains no significant concentrations of a single investment within the plan assets.

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2012 and 2011

The following benefit payments, which reflect future service, as appropriate, are expected to be paid by WPAHS:

	Total pension benefits
Year ending June 30:	
2013	\$ 42,361
2014	43,521
2015	46,266
2016	48,933
2017	52,758
2018 – 2022	310,691

Plan Changes

Two changes in plan provisions were made to the Represented Plan effective January 1, 2012:

- Members of Local Union 95 IUOE bargained to cease benefit accruals in the Represented Plan. As a result, employees of Suburban who are and who become employees of AGH by merger do not receive Annual Retirement credits for service after July 14, 2011. Additionally, employees of Western Pennsylvania Hospital who are members of Local Union 95 IUOE do not receive Annual Retirement credits for service after November 23, 2010
- A change was also made to the prior vesting service for employees of Western Penn Medical Associates, PC, so that these participants now receive prior vesting service credit for periods before November 30, 2010.

These plan changes had a negligible effect on the results of the valuation.

There were no changes to the plans for the year ended June 30, 2011.

(b) Defined Contribution Plans

WPAHS sponsors a defined contribution savings plan, which is available to substantially all WPAHS employees in order to provide additional security during retirement by creating an incentive for employees to make regular contributions on their own behalf. Under these plans and as determined on an individual basis, WPAHS contributed an amount equal to 50% of an employee's contribution up to 2.5% of such employee's salary in a given year. WPAHS suspended their contribution to this plan in April 2009 for nonrepresented employees. Such expense related to these plans was based on actual contributions made.

WPAHS' expense associated with its contributions to these savings plans was \$629 and \$535 for the years ended June 30, 2012 and 2011, respectively.

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2012 and 2011

(17) Functional Expenses

WPAHS provides general healthcare services. Expenses related to such services for the years ended June 30, 2012 and 2011 are as follows:

	<u>2012</u>	<u>2011</u>
Healthcare services	\$ 1,494,810	1,465,136
General	152,940	161,961
Research	21,895	18,475
Fund-raising and other	<u>2,058</u>	<u>2,303</u>
Total	<u>\$ 1,671,703</u>	<u>1,647,875</u>

(18) Gain on Divestiture

On August 2, 2010 WPAHS entered into an agreement for the sale of the assets and inventory of its dialysis business with total book value of \$639. The dialysis business was sold for \$10,245, resulting in a net gain of \$9,606 in fiscal year 2011.

(19) Legal Matters

In August 2008, WPAHS received a letter from the United States Securities and Exchange Commission (Commission) stating that the Commission initiated an informal inquiry with regard to WPAHS and the consolidated financial statement adjustments reported in July 2008. In February 2009, the Commission changed the status of the inquiry to a formal investigation. The Commission has also sought information related to certain disclosures made by WPAHS. WPAHS is continuing to cooperate with the Commission.

In April 2009, a putative collective action was filed in the United States District Court for the Western District of Pennsylvania alleging claims under ERISA, RICO, and the Fair Labor Standards Act against WPAHS, certain of its related entities, and certain WPAHS executives. The suit alleges that current and former employees did not receive compensation for all hours worked. A companion class action suit alleging various state court claims was filed in the Court of Common Pleas of Allegheny County. In late December 2011, the District Court for the Western District of Pennsylvania denied the certification of the class action suit. Although WPAHS believes the matter will be resolved without any material adverse impact on WPAHS' financial condition, particularly in light of the district court's decision to deny collective action certification to the federal action, the final outcome and effect on WPAHS is unknown at this time.

In 2010, the System was informed by Highmark that it took exception to the conversion of several oncology infusion centers from free-standing to hospital-based. In August 2010, Highmark exercised its right under its provider contract to submit the dispute to binding arbitration. The System believes that the conversions of all of these sites are permissible under the provider contract and believes its position will prevail in the arbitration. At June 30, 2010, the System reserved \$8,500 of incremental revenue received from Highmark as a result of these conversions. Subsequent to year-end, Highmark agreed to forgo the arbitration as a term of the Affiliation Agreement. As a result, repayment of the incremental revenue is not required and the System reversed the reserves at June 30, 2011.

UNAUDITED

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2012 and 2011

WPAHS is additionally subject to various legal proceedings and claims consistent with an organization of its size arising in the ordinary course of its business and not yet adjudicated.

Based upon information known to WPAHS, and after consultation with legal counsel, the ultimate outcome of the lawsuits and claims discussed above are unlikely to have a material adverse effect on the consolidated balance sheet, results of operations, or cash flows of WPAHS.

(20) Subsequent Events

THIS FOOTNOTE HAS NOT YET BEEN DRAFTED

UNAUDITED

Independent Auditors' Report on Supplementary Information

UNAUDITED

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Consolidating Balance Sheet Information

June 30, 2012

(Amounts in thousands)

Assets	<u>Total obligated</u>	<u>Total nonobligated</u>	<u>Eliminations</u>	<u>Total consolidated</u>
Current assets:				
Cash and cash equivalents	\$ 192,688	1,128	—	193,816
Short-term investments	5,108	—	—	5,108
Assets limited or restricted as to use	5,744	—	—	5,744
Receivables:				
Patient accounts, less allowance for uncollectible accounts of \$44,116	136,964	—	—	136,964
Other	24,431	315	348	25,094
Inventories, net	21,289	—	—	21,289
Prepaid expenses	15,188	5	—	15,193
Total current assets	<u>401,412</u>	<u>1,448</u>	<u>348</u>	<u>403,208</u>
Assets limited or restricted as to use	393,269	2,218	—	395,487
Property and equipment, net	367,862	26,208	—	394,070
Other assets, net	75,376	1,541	(1,621)	75,296
Total assets	<u>\$ 1,237,919</u>	<u>31,415</u>	<u>(1,273)</u>	<u>1,268,061</u>

UNAUDITED

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Consolidating Balance Sheet Information

June 30, 2012

(Amounts in thousands)

Liabilities and Net Deficit	Total obligated	Total nonobligated	Eliminations	Total consolidated
Current liabilities:				
Current portion of long-term debt	\$ 13,764	2,102	—	15,866
Accounts payable	87,192	49	—	87,241
Accrued expenses	17,441	4	—	17,445
Accrued interest	6,597	102	—	6,699
Accrued salaries and vacation	55,838	5	—	55,843
Current portion of deferred revenue	15,632	—	—	15,632
Current portion of self-insurance liabilities	2,954	—	—	2,954
Estimated third-party payor settlements	1,163	—	—	1,163
Other current liabilities	4,104	393	—	4,497
Due to affiliate, net	—	(348)	348	—
Total current liabilities	<u>204,685</u>	<u>2,307</u>	<u>348</u>	<u>207,340</u>
Deferred revenue	36,869	—	—	36,869
Self-insurance liabilities	76,352	1,392	—	77,744
Long-term debt	857,611	21,225	—	878,836
Accrued pension obligation	278,663	—	—	278,663
Other noncurrent liabilities	21,212	1,956	—	23,168
Total liabilities	<u>1,475,392</u>	<u>26,880</u>	<u>348</u>	<u>1,502,620</u>
Net (deficit) assets:				
Unrestricted	(482,887)	3,667	(1,621)	(480,841)
Temporarily restricted	22,687	523	—	23,210
Permanently restricted	222,727	345	—	223,072
Total net (deficit) assets	<u>(237,473)</u>	<u>4,535</u>	<u>(1,621)</u>	<u>(234,559)</u>
Total liabilities and net (deficit) assets	<u>\$ 1,237,919</u>	<u>31,415</u>	<u>(1,273)</u>	<u>1,268,061</u>

See accompanying independent auditors' report.

UNAUDITED

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Consolidating Statement of Operations Information

Year ended June 30, 2012

(Amounts in thousands)

	<u>Total obligated</u>	<u>Total nonobligated</u>	<u>Eliminations</u>	<u>Total consolidated</u>
Unrestricted revenues and other support:				
Net patient service revenue	\$ 1,474,569	—	—	1,474,569
Other revenue	80,942	3,954	(3,916)	80,980
Net assets released from restrictions	3,643	9	—	3,652
Total unrestricted revenues other support	<u>1,559,154</u>	<u>3,963</u>	<u>(3,916)</u>	<u>1,559,201</u>
Expenses:				
Salaries, wages, and fringe benefits	866,306	182	—	866,488
Patient care supplies	279,937	—	—	279,937
Professional fees and purchased services	163,705	22	—	163,727
General and administrative	169,649	97	(3,916)	165,830
Provision for bad debts	80,805	—	—	80,805
Depreciation and amortization	64,001	1,739	—	65,740
Interest	39,013	1,322	—	40,335
Restructuring	8,841	—	—	8,841
Total expenses	<u>1,672,257</u>	<u>3,362</u>	<u>(3,916)</u>	<u>1,671,703</u>
Operating (loss) income	(113,103)	601	—	(112,502)
Investment income	14,242	—	—	14,242
Gifts and donations	58,393	167	—	58,560
Gain in joint venture investment	1,863	—	—	1,863
(Deficiency) excess of revenues over expenses	<u>\$ (38,605)</u>	<u>768</u>	<u>—</u>	<u>(37,837)</u>

See accompanying independent auditors' report.

UNAUDITED

WEST PENN ALLEGHENY HEALTH SYSTEM AND SUBSIDIARIES

Consolidating Statement of Changes in Net Deficit

Year ended June 30, 2012

(Amounts in thousands)

	<u>Total obligated</u>	<u>Total nonobligated</u>	<u>Eliminations</u>	<u>Total consolidated</u>
Unrestricted net (deficit) assets:				
(Deficiency) excess of revenues over expenses	\$ (38,605)	768	—	(37,837)
Net assets released for property acquisitions and donated capital	557	224	—	781
Pension liability adjustments	(86,954)	—	—	(86,954)
Other transfers	23	(223)	—	(200)
	<u>(124,979)</u>	<u>769</u>	<u>—</u>	<u>(124,210)</u>
(Increase) decrease in unrestricted net deficit				
Temporarily restricted net assets:				
Contributions	2,917	164	—	3,081
Investment income	881	1	—	882
Net assets released from restrictions used for:				
Operations	(3,643)	(9)	—	(3,652)
Acquisition of equipment	(557)	(224)	—	(781)
Other transfers	253	2	—	255
	<u>(149)</u>	<u>(66)</u>	<u>—</u>	<u>(215)</u>
Decrease in temporarily restricted net assets				
Permanently restricted net assets:				
Contributions	4	—	—	4
Investment income	7,205	—	—	7,205
Change in net unrealized gains on other than trading securities	(8,574)	—	—	(8,574)
Transfers out of endowments/participating trust to investment income and operations	(9,695)	—	—	(9,695)
Other transfers	21	(2)	—	19
	<u>(11,039)</u>	<u>(2)</u>	<u>—</u>	<u>(11,041)</u>
Decrease in permanently restricted net assets				
(Increase) decrease in net deficit	(136,167)	701	—	(135,466)
Net (deficit) assets – beginning of period	<u>(101,306)</u>	<u>3,834</u>	<u>(1,621)</u>	<u>(99,093)</u>
Net (deficit) assets – end of period	<u>\$ (237,473)</u>	<u>4,535</u>	<u>(1,621)</u>	<u>(234,559)</u>

See accompanying independent auditors' report.

III. ANNUAL REPORTING REQUIRED BY CONTINUING DISCLOSURE AGREEMENT

Active Medical Staff	1
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Sources of Revenue	3
Employee Retirement Plans	4
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Annual Debt Service Coverage Ratio	6
Days Cash on Hand	7

WEST PENN ALLEGHENY HEALTH SYSTEM
ACTIVE MEDICAL STAFF
As of June 30, 2012

<u>DEPARTMENT/SPECIALTY</u>	AGH	AKMC	CGH	FRH	WPH	ACTIVE *
Family Medicine	12	5	6	40	10	73
Medicine	277	53	34	196	199	759
Surgery	146	42	18	74	94	374
OB-Gyn	19	4	-	17	45	85
Pediatrics	11	-	-	24	45	80
Hospital-Based Specialties:						
Emergency Medicine	31	11	1	13	19	75
Anesthesiology	50	3	1	40	41	135
Diagnostic and Interventional Radiology	37	6	2	36	35	116
Radiation Oncology	15	2	-	8	5	30
Pathology	13	4	1	10	16	44
Pain Management	-	-	-	7	4	11
Nuclear Medicine	4	-	-	4	3	11
Subtotal Hospital-Based Specialties	150	26	5	118	123	422
TOTAL	615	130	63	469	516	1,793
Average Age	49.3	55.7	55.7	50.7	49.8	52.2
# Board Certified	561	118	56	446	476	1,657
% Board Certified	91.2%	90.8%	88.9%	95.1%	92.3%	92.4%

*Certain physicians have admitting privileges at multiple Hospitals within the System, as such a physician may be counted more than once in this table.

**WEST PENN ALLEGHENY HEALTH SYSTEM
EMPLOYEES
As of June 30, 2012**

Full-time employees	9,509
Part-time employees	1,438
Casual employees	<u>1,029</u>
Total Employees	<u>11,976</u>
Full-time equivalents	<u>10,237</u>
Employees represented by collective bargaining units	<u>2,214</u>

WEST PENN ALLGHENY HEALTH SYSTEM
SOURCES OF REVENUES
for Fiscal Years ended June 30,

	2008	2009	2010	2011	2012
Medicare (including managed care)	47%	46%	46%	46%	46%
Highmark	23%	24%	24%	24%	26%
Medicaid (including managed care)	11%	12%	12%	13%	12%
Commercial	2%	2%	2%	2%	4%
HMO / PPO	13%	12%	12%	11%	9%
Self Pay & Other	4%	4%	4%	4%	3%
Total	100%	100%	100%	100%	100%

**WEST PENN ALLEGHENY HEALTH SYSTEM
EMPLOYEE RETIREMENT PLANS**

As of January 1, 2012 (the date of the most recent actuarial report), the Retirement Plans for the Employees of West Penn Allegheny Health System were in an underfunded position, as follows:

Actuarial Current Liability (discount rate of 6.32%)	\$583,147,000
Actuarial Value of Plan Assets	<u>480,014,000</u>
Current Liability > Plan Assets	<u>\$ 103,133,000</u>

The System is required to abide by the minimum funding standards under ERISA. All plan years 2010 and prior have been funded as of June 30, 2012. Plan year 2011 was funded on January 15, 2012 and September 15, 2012 through contributions of \$6,736,737 and \$2,207,315, respectively. This is reflected in the actuarial value of plan assets above as a contribution receivable as is required under actuarial standards. The Plans are governed by the Pension Protection Act of 2006 ("PPA"). The Plans have been qualified for an exemption contained in Section 105 of PPA as Pension Benefit Guaranty Corporation settlement plans, which exempts the System from the accelerated funding rules of PPA until 2014. The Plans will be required to follow the previously existing minimum funding standards of ERISA until 2014.

The above disclosures are based on actuarial calculations for funding purposes. For financial reporting purposes as of June 30, 2012 the underfunded position is reflected as follows:

Projected Benefit Obligation (discount rate of 3.90%)	\$768,553,000
Fair Value of Plan Assets	<u>489,890,000</u>
Projected Benefit Obligation > Plan Assets	<u>\$278,663,000</u>

West Penn Allegheny Health System
Health System Totals
Selected Utilization Statistics

	Fiscal Years Ended June 30,				
	2008	2009	2010	2011	2012
Discharges					
Acute*	77,833	76,464	70,790	59,972	56,146
Rehab	1,124	1,181	1,610	1,514	1,309
Hospice	449	502	458	409	372
Patient Days (excludes newborns)					
Acute*	397,578	389,166	367,553	316,088	296,130
Rehab	13,071	13,573	18,805	18,068	15,397
Hospice	3,070	3,301	2,872	2,516	2,723
Staffed Beds					
Acute*	1,736	1,662	1,513	1,274	1,382
Rehab	61	61	99	88	61
Hospice	12	12	12	12	12
Occupancy Rate					
Acute*	62.6%	64.2%	66.6%	68.0%	58.5%
Rehab	58.5%	61.0%	52.0%	56.3%	69.0%
Hospice	69.9%	75.4%	65.6%	57.4%	62.0%
Length-of-Stay (based on discharges)					
Acute*	5.10	5.08	5.19	5.27	5.30
Rehab	11.67	11.41	11.68	11.93	11.87
Hospice	6.84	6.58	6.27	6.15	7.32
Observation Cases	12,347	13,291	14,557	15,313	16,688
Births	4,947	4,880	4,522	4,018	3,884
Emergency Visits					
Inpatient	44,485	45,160	44,531	37,281	33,668
Outpatient	150,130	151,695	151,979	134,216	130,624
Operating Room Cases					
Inpatient	23,886	23,541	22,635	19,982	18,692
Outpatient	34,876	33,455	32,915	31,411	30,522
Transplants					
Heart	17	13	16	36	18
Kidney	75	70	71	61	68
Bone Marrow	79	76	80	63	60
Liver	8	8	13	18	21
Pancreas	-	-	-	3	1
Lung	-	-	-	1	-

* Includes Psychiatrics

**WEST PENN ALLEGHENY HEALTH SYSTEM
OBLIGATED GROUP
ANNUAL DEBT SERVICE COVERAGE RATIO ***
as of June 30, 2012
(dollars in thousands)

Annual Debt Service Coverage Ratio

Excess of expenses over revenues	\$ (38,605)
Plus: depreciation and amortization	64,001
Plus: interest expense	39,013
Plus: net unrealized investment losses	863
Less: net unrealized gains in joint venture investments	<u>(1,440)</u>
Total	63,832
 Annual debt service requirement	 <u>\$ 55,223</u>
 ANNUAL DEBT SERVICE COVERAGE RATIO	 <u><u>1.16</u></u>

* - Based upon unaudited financial information

**WEST PENN ALLEGHENY HEALTH SYSTEM
OBLIGATED GROUP
DAYS CASH ON HAND *
as of June 30, 2012
(dollars in thousands)**

Days Cash on Hand:

Cash and cash equivalents/other	\$ 195,395
Short term investments	5,108
Board designated (funded depreciation)	<u>72,674</u>
Total	<u><u>\$ 273,177</u></u>
Total operating expenses, including restructuring	\$ 1,672,257
Less: depreciation and amortization	<u>(64,001)</u>
Operating expenses less depreciation and amortization	<u><u>\$ 1,608,256</u></u>
Days in fiscal period	366
Operating expense per day	<u><u>\$ 4,394</u></u>
DAYS CASH ON HAND	<u><u>62.2</u></u>

* - Based upon unaudited financial information

