Catholic Health Initiatives

Imagine better health.®

Annual Report

As of and for the fiscal year ended June 30, 2017

Information Concerning Catholic Health Initiatives

Table of Contents

Certain of the discussions included in this Annual Report may include forward-looking statements. Such statements are generally identiifiable by the terminology used such as "believes," "anticipates," "intends," "scheduled," "plans," "expects," "estimates," "budget" or other similar words. Such forward-looking statements are primarily included in PARTS II, III, IV and VII. These statements reflect the current views of management with respect to future events based on certain assumptions, and are subject to risks and uncertainties. Catholic Health Initiatives, a Colorado non-profit corporation (the "Corporation"), undertakes no obligation to publicly update or review any forward-looking statement as a result of new information or future events.

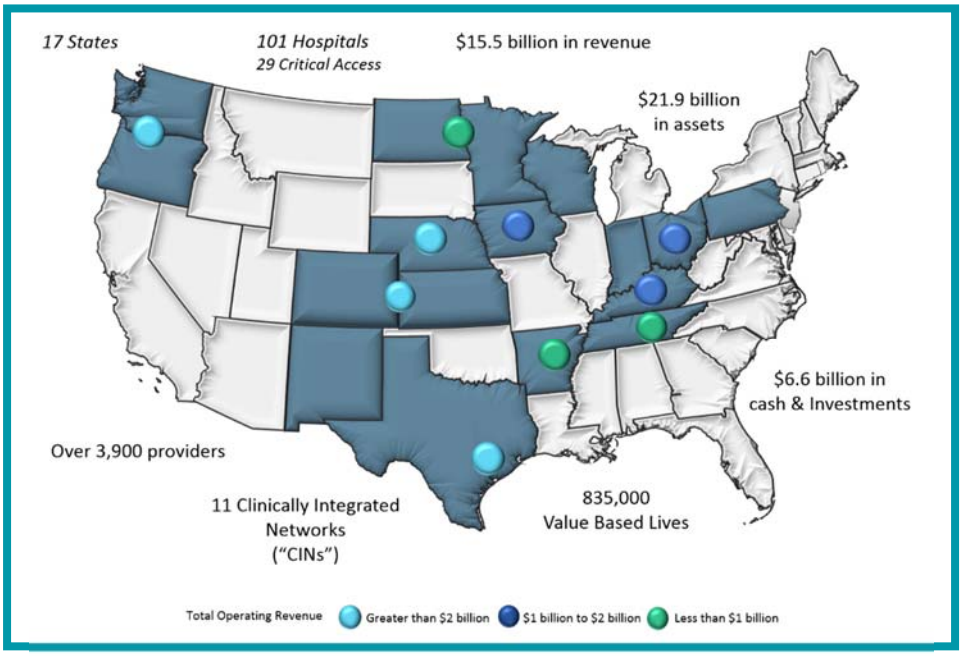
References to "CHI" in this Annual Report are to the Corporation and all of the affiliates and subsidiaries ("Participants") consolidated with it pursuant to generally accepted accounting principles ("GAAP"). References to the Corporation are references only to the parent corporation, and should not be read to include any of the Participants.

Unless otherwise noted, all financial informaion in this Annual Report, for both fiscal year 2016 and 2017, refers to continuing operations only.

PART I: OVERVIEW

Catholic Health Initiatives ("CHI") is a group of non-profit and for profit organizations that comprise one of the nation's largest Catholic health care systems, serving more than four million people each year through operations and facilities that span the continuum of care, including acute care hospitals; physician practices; long-term care facilities; assisted-living and residential-living facilities; community-based health services; home care; research and development; medical and nursing education; reference laboratory services; virtual health services; managed care programs; and clinically integrated networks. Today, CHI has operations in 17 states, with a service area that covers approximately 54 million people, or approximately 17% of the U.S. population.

CHI is currently comprised of ten regions that are operated as integrated health systems including several joint operating agreements ("JOAs"), joint operating companies ("JOCs") or joint ventures. The geographic diversity and total operating revenues by region for the fiscal year ended June 30, 2017 are depicted in the accompanying map.



PART II: FISCAL YEAR 2017 HIGHLIGHTS & SUMMARY

Fiscal year 2017 represented a transformational year for CHI operationally and strategically. As seen in the table below CHI generated operating EBIDA before restructuring, impairment and other losses of $930.7 million. When adjusted for business combination and other transactional gains, as well as one-time items, this represents a $114.5 million improvement over fiscal year 2016. This year over year improvement was driven primarily by CHI's performance improvement efforts, many of which were accomplished in the second half of the fiscal year, led by:

- Labor improvements – same store total labor costs as a percentage of net patient services revenues decreased to 51.8% for the fiscal year ended June 30, 2017, compared to 52.7% for the corresponding period of the prior fiscal year. CHI continues to address labor productivity across the enterprise, as well as monitoring growth initiatives in certain physician practices where labor costs and medical professional fees have been added in anticipation of future increased patient volumes.
- Supply cost improvements – same store supply cost as a percentage of net patient services revenues decreased to 17.6% for the fiscal year ended June 30, 2017, compared to 18.0% in the same period of the prior fiscal year due in part to CHI's expense management initiatives.

The operational improvements were offset by increases in other expense categories and changes in revenue driven by certain decreased volumes, shifts from inpatient to outpatient setting and unfavorable shifts in payer mix.

Operating EBIDA before restructuring, impairment and other losses				
$ in millions	**FY16**	**FY17**	**Chg**	**% Chg**
Totals before transactional gains and other items	$ 696.2	$ 810.7	$ 114.5	16.4%
Business combination gains	223.0	-	(223.0)	
Transactional gains and other items	117.1	120.0	2.9	
Operating EBIDA before restructuring, impairment and other losses	$ 1,036.3	$ 930.7	$ (105.6)	

In addition to the operational initiatives across the enterprise, fiscal year 2017 marked a transition year for KentuckyOne Health ("KentuckyOne") highlighted below and detailed in *Part IV: Strategic & Operational Initiatives and Part V: Strategic Affiliations & Acquisitions - Pending and Completed Divestitures.*

- CHI transitioned the University of Louisville Medical Center operations, management and control back to the University of Louisville ("U of L"), effective July 1, 2017.
- In May 2017, CHI's Board approved the divestiture of substantially all of the Louisville-area acute care operations.
- CHI assumed complete ownership of KentuckyOne, effective September 1, 2017, when the Corporation purchased the non-controlling interest from the remaining partner for $150 million. The payment will be used by the partner to further invest in the healthcare needs of the community.

Regarding the Texas region, fiscal year 2017 proved a challenging year for operations. While the region made some progress in various aspects of their performance improvement plan, revenue offsets, including unfavorable payer and service mix changes, resulted in operating EBIDA before restructuring of $64.3 million compared to $119.1 million in fiscal year 2016.

In May 2016, CHI approved a plan to sell or otherwise dispose of certain entities of QualChoice Health, Inc. ("QualChoice Health"), a consolidated CHI subsidiary, whose primary business is to develop, manage and market

commercial and Medicare Advantage health insurance programs, as well as a wide range of products and administrative services. A letter of intent for the Medicare Advantage health insurance operations has been received, with an anticipated sale in fiscal year 2018. Although there has been significant interest in the QualChoice Health commercial operations, the uncertainty surrounding the Affordable Care Act and current political environment has delayed the anticipated sale of this operation to a timeline outside of CHI's control. CHI remains committed to selling or otherwise disposing of the QualChoice Health commercial operations and continues to actively market these operations.

Finally, non-operating performance for fiscal year 2017 was strong, with investment gains of $638.5 million and a positive benefit from interest rate swaps and other non-operating expenses of $94.7 million, partially offset by a $19.6 million loss on the defeasance of bonds. When operating and non-operating performance are combined for fiscal 2017, the resulting excess margin before non-controlling interests was 0.8% or $128.4 million, compared to (3.8%) or ($575.6) million in fiscal 2016.

PART III: COMPETITIVE STRENGTHS

CHI's size and geographic diversity enable greater economies of scale and efficiencies, and provide a level of insulation from unfavorable performance in specific regions. CHI continues to develop a greater market presence in certain legacy regions and to further expand into newer regions as described below in *Part V: Strategic Affiliations & Acquisitions.* CHI's regions in Colorado, Pacific Northwest, Nebraska, and Texas each generated approximately $2 billion or more in total revenues in fiscal year 2017. CHI's key strengths include:

- Strong geographic diversification, with a mix of facilities located in both rural and urban settings, helping to mitigate the effect of changes in reimbursement
- Diversification of operating revenue, with no single region representing more than 17.8% of total operating revenue in fiscal year 2017
- Experienced corporate and clinical management team

Notwithstanding the competitive advantages associated with its size and geographic diversity, CHI has experienced operational and financial challenges in certain key regions, most notably Kentucky and Texas. Various improvement initiatives over the past several years have been successful in driving changes to operations. However, changes in the health care industry have resulted in additional challenges that have led to decreased volumes and reimbursement shifts between inpatient and outpatient/ambulatory care and payer mix.

CHI Regions

CHI's operations are located primarily within ten regions: Colorado, Pacific Northwest, Nebraska, Kentucky, Texas, Iowa, Ohio, Arkansas, Tennessee and North Dakota/Minnesota. A brief description of these regions is below. These descriptions provide a broad overview of each region. Additional detail regarding certain financial and operating information for five of CHI's largest regions, Colorado, Pacific Northwest, Nebraska, Texas and Kentucky is included later in this Annual Report.

Colorado - CHI's Colorado region includes ten acute care hospitals located in Colorado and two in western Kansas. All of these hospitals are operated by Centura Health, the joint operating company created in 1996 by CHI and Adventist Health System (Adventist Health System is based in Altamonte Springs, Florida).

Pacific Northwest - CHI's Pacific Northwest region includes CHI Franciscan Health, which operates seven acute care hospitals in Washington, two in Oregon, as well as Franciscan Medical Group, a regional network of primary-care and specialty-care clinics, physicians and other professional providers.

Nebraska - CHI's Nebraska region consists of 15 acute care hospitals, two stand-alone behavioral health

facilities, and more than 120 clinics throughout Nebraska and southwest Iowa. Creighton University Medical Center - Bergan Mercy is the primary teaching partner of Creighton University's health sciences schools.

Kentucky - Prior to 2012, CHI's Kentucky region consisted primarily of the St. Joseph Health System, which is based in Lexington, Kentucky and operated eight acute care hospitals throughout Kentucky. In 2012, CHI created KentuckyOne, which integrated certain Louisville operations with CHI's existing Kentucky hospitals. As described below under *Part V: Strategic Affiliations & Acquisitions – Pending and Completed Divestitures*, CHI has reconfigured the Kentucky Region, including the separation of University of Louisville Medical Center from KentuckyOne and the approved divestiture of all or substantially all of the other Louisville-area facilities in the Kentucky region. As of July 1, 2017, the continuing operations of the Kentucky region were segregated from and are operated independently of the discontinued operations (located in central and eastern Kentucky, with the original eight acute care hospitals, as well as physician practices).

Texas - CHI's Texas region operates seven acute care facilities operating in the greater Houston area. In 2014, CHI St. Luke's entered into a joint venture with Baylor College of Medicine ("BCM") to open a new, acute-care, open-staff hospital on BCM's McNair Campus in the central area of the Texas Medical Center, which is currently home to two outpatient facilities owned by BCM—the Baylor College of Medicine Medical Center and the Lee and Joe Jamal Specialty Care Center. CHI St. Luke's and BCM also entered into a 25-year academic affiliation at that time. BCM and St. Luke's Health System ("SLHS") became co-members of St. Luke's Medical Center ("SLMC"), with membership percentages of 35% and 65%, respectively. Through SLMC, BCM and SLHS plan to jointly operate a new hospital, to replace the current SLHS hospital in the Texas Medical Center.) BCM and SLHS have also formed a joint venture that serves as a vehicle for efforts by BCM and SLHS to create a health care network in the Houston region.

In addition to the Houston hospitals and facilities, the Texas region also includes CHI St. Joseph Health System ("SJHS") and CHI St. Luke's Health Memorial of East Texas ("SLHMET"). SJHS operates five acute care hospitals, a long-term care facility and provides other services, all in the Brazos Valley region of Texas. SJHS joined CHI in 2014 in connection with the Corporation's acquisition of Sylvania Franciscan Health ("SFH"). SLHMET also joined CHI in 2014 and operates three acute care hospitals, one specialty hospital and various clinics in the East Texas region.

In 2016, CHI St. Luke's became the sole corporate member of Brazosport Regional Health System ("BRHS"), a nonprofit health care organization that includes a 158 licensed bed hospital that operates the only Level III trauma center in Brazoria County, Lake Jackson, Texas.

Iowa - Most of CHI's Iowa operations are managed by Mercy Health Network ("MHN"), which was created in 1998 pursuant to a joint operating agreement between CHI and Trinity Health, based in Livonia, Michigan. See *Part V: Pending and Completed Affiliations/Acquisitions* for additional detail regarding MHN. Operations in this region include four acute care hospitals located in Central Iowa.

Ohio - CHI's Ohio region includes Good Samaritan Hospital, an acute care hospital located in Cincinnati, which is managed by TriHealth, the joint operating company established in 1995 pursuant to a joint operating agreement between Bethesda Hospital, Inc. and CHI, as well as Good Samaritan Hospital, an acute care hospital (including the Dayton Heart & Vascular Hospital at Good Samaritan) located in Dayton, which is managed by Premier Health Partners, the joint operating company established in 1995 as part of a joint operating agreement between certain regional providers in Ohio and CHI.

In 2014, CHI became the sole member of SFH and, in 2016, CHI and SFH became the corporate members of Trinity Health System ("THS"), of which SFH was previously a 50% member. SFH operates long term care facilities in Ohio and Kentucky and a critical access hospital in Dennison, Ohio. THS operates two acute care hospitals and provides other services in Steubenville, Ohio.

Arkansas - CHI's Arkansas region includes four acute care hospitals as well as primary care facilities, specialty physician clinics and convenient care clinics.

Tennessee - CHI's Tennessee region includes two acute care hospitals, as well as primary care facilities,

specialty clinics, an imaging center and a home health agency.

North Dakota/Minnesota - CHI's North Dakota/Minnesota region includes 14 acute care hospitals in Minnesota and North Dakota, of which 13 are critical access hospitals. The region also operates primary care facilities, specialty clinics and long-term care facilities.

PART IV: STRATEGIC & OPERATIONAL INITIATIVES

A. Strategic Intent

CHI adopted a multi-faceted approach to achieve success in both the existing fee-for-service and new payment-for-value environments. To sustain its ministry into the future, CHI has introduced four strategic objectives that are part of the CHI Strategic Plan 2016-2020 that are depicted below.

With a shared vision and strategic objectives setting the course, CHI regions and functional areas consisting of supply chain, revenue cycle, information technology, human resources, treasury and finance, marketing and communication, strategy and other shared services established strategic imperatives to address the realities, opportunities and needs within their communities, with a goal of providing greater clarity of purpose and accountability. CHI is measuring, monitoring and advancing these efforts through the use of *Living Our Mission Measures* and other key metrics described in *Part III: B. Clarify Purpose and Accountability* below.

B. Strategic Intent

Living Our Mission Measures are nine CHI-wide performance goals that are most vital to our mission: from safety and quality to patient experience and the transition to value-based health care. The Board of

Stewardship Trustees ("the Board") established more granular goals in each of the functional areas. Region-specific goals align to these CHI-wide goals.

CHI also established four strategic measures intended to complement the *Living Our Mission Measures* and to move beyond care delivery to impact the determinants of health. These measures assess:

- Collaboration with community leaders to define and implement initiatives to address health priorities
- Commitments to advance equity of care for people in the communities it serves
- Expansion of ambulatory care sites to address consumer needs and expectations
- Growing the number of consumers CHI serves

Each region and functional area creates its own tactical, measurable plan that integrates CHI-wide strategies into day-to-day operations.

C. Transformative Change Requires Multi-faceted Approach to Success

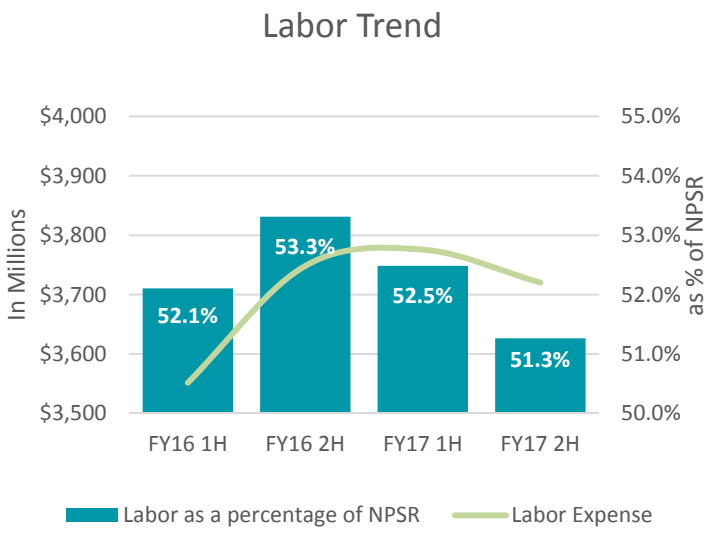
CHI has grown from $7.9 billion in total operating revenues in fiscal year 2011 to nearly $15.5 billion in fiscal year 2017, and has diversified into new lines of business. To meet the continuing challenges of a changing health care landscape and financial and operational performance shortfalls, in fiscal year 2016, CHI accelerated performance improvement efforts in the following functional areas/work streams: labor management, revenue cycle, supply chain, the physician enterprise, non-labor overhead, organic growth and information technology. To further this work, in December 2016, CHI hired Anthony K. Jones, FACHE, interim executive vice president of operations.

Mr. Jones specializes in leading organizations through financial and operational turnarounds. CHI believes its largest opportunities for improvement in the near term are in labor management across all regions and in additional areas of opportunity in the Kentucky and Texas regions.

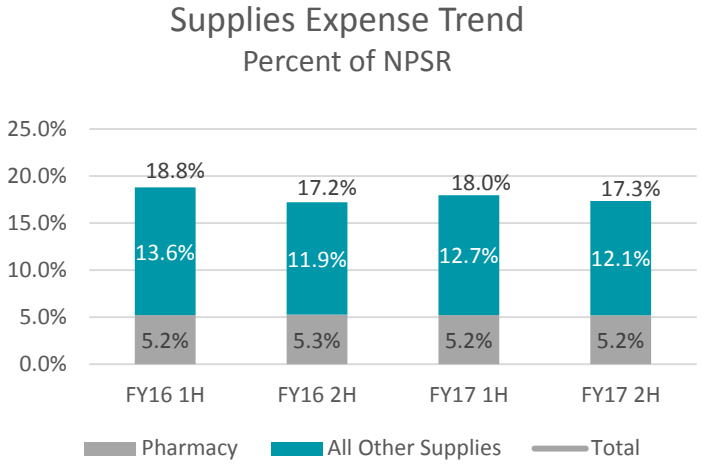
CHI has accelerated the efforts of its performance improvement plan, with a near-term focus on change in processes of driving and measuring financial and operational improvement across functional areas. The change in processes provides operational accountability while aligning governance and operating models to ensure high performance.

CHI set a June 30, 2017 goal to drive over $800 million in run rate improvement by the end of fiscal year 2017. Management selected functional leaders for each work stream and an Executive Steering Committee was established at the corporate level to oversee all performance improvement work streams and activities. Each work stream had specific targets and initiatives by region. The philosophy underlying this work was to create operational efficiency, economies of scale, standardization of systems and processes, cost reductions and savings, growth and revenue enhancement and consolidation and centralization of back-office and core services. To further assist in its efforts to reach this goal, CHI adopted a new system of key measures and accountability in 2016 described above in *Part III: B. Clarify Purpose and Accountability.* By June 30, 2017, CHI realized performance improvement initiatives that increased revenues and/or decreased expenses by approximately $800 million annually.

Labor expense management initiatives were addressed in each region and at the corporate level to achieve labor reductions. Labor reduction plans were derived from reductions-in-force, management elimination, attrition of recently vacated positions, premium pay and overtime reductions, decreased use of contract labor and through more effective staff scheduling. By June 30, 2017, total FTEs deceased by 2,911, compared to June 30, 2016, despite adding 615 physicians/providers in the Physician Enterprise (defined as the employed physicians and advanced practice clinicians operating within the regional delivery systems). CHI believes these savings to be sustainable and to drive additional improvements into fiscal year 2018 through adherence to new enterprise wide staffing standards. Dedicated resources have been put in place to assist regions with their labor reduction plans and support implementation.



Supply chain initiatives are led by CHI supply chain management with third-party support to assist in operational transformation. For the second half of fiscal year 2017, supplies as a percentage of net patient services revenues improved to 17.3% as compared to 18.0% for the first half of fiscal year 2017. Management has a goal to reduce this expense to 15.5%-16.5% within the next 36 months. As part of the operational transformation, CHI has implemented a clinically driven, professionally managed supply chain operating model to assist in achieving this goal. This model establishes clear roles for clinician engagement and entails a rigorous formulary and process management. CHI supply chain manages all applicable expenditures to ensure total cost of ownership and group purchasing organization ("GPO") optimization.



In addition to the supply chain initiatives discussed above, CHI has initiated a review of all purchased services expenditures across the system to identify opportunities for elimination or re-negotiation of purchased services arrangements.

As discussed above, CHI has continued to increase the number of employed physicians through the addition of 615 providers in the last year. The total operating loss in the Physician Enterprise was $719.7 million during the fiscal year ended June 30, 2017, on a consolidated basis. CHI views this loss as a strategic investment to build integrated regional delivery networks. To address the loss, a review of all physician arrangements to identify those where productivity levels are less than expected. In addition, revenue cycle processes are being reviewed across the enterprise.

In addition to the work streams identified above, in February 2017, CHI deployed additional measures to support performance improvement teams in its Kentucky and Texas regions, with the goal of expediting performance improvement activities in those regions. These teams are further supplemented by third party resources with experience in labor management and rapid expense reduction, and with subject matter experts from within CHI.

The operating improvements were offset by increases in other expense categories and changes in revenue driven by certain decreased volumes, shifts in inpatient to outpatient settings and unfavorable shifts to payer mix.

D. Regional Positioning and Performance

During fiscal year 2017, approximately 67% of CHI's total operating revenues and 79% of Operating EBIDA before Restructuring were derived from the following five markets:

Colorado – Under Centura Health, the Colorado region continues to be one of CHI's strongest regions. Its statewide network has grown substantially through ownership, management and affiliation, and capitalizing on the rapid population growth in the Denver metropolitan area. New ambulatory service centers are being built and have opened in the north corridor of the Denver metropolitan area and in the Colorado Springs metropolitan area. The Colorado region has extensive brand and ambulatory presence across metro Denver, Colorado Springs, and other Colorado communities and western Kansas. The anticipated 2019 completion of the St. Francis Medical Center in Colorado Springs is expected to address favorable market conditions and population growth in that market. The Colorado region is working to optimize its payer relationships and risk sharing agreements through FullWell, Centura's population health partner. Centura is continuing to grow and advance Colorado Health Neighborhoods ("CHN"), its statewide CIN. CHN currently has the largest pool of specialists and the most facilities of any CIN in Colorado and western Kansas.

Pacific Northwest ("PNW") - The PNW region continues to be a strong performer for CHI. Areas of strategic focus in the PNW region include extending both geographic reach and access through growth of partnerships and ambulatory facilities and expanding the Rainier Health Network, the PNW's CIN. In March 2017, CHI Franciscan Health entered into a clinical partnership and strategic affiliation with Virginia Mason Medical Center with a goal of serving new patients through combined clinical institutes in key service lines, enabling the integration of Virginia Mason providers into the Rainier Health Network.

As part of the performance improvement plan, management has improved labor expense productivity and reduced supply costs. Specifically, management has reduced FTEs by 780, resulting in salaries as a percent of net patient services revenues decreasing from 54.2% to 51.4% for the years ended June 30, 2016 and 2017, respectively.

In May 2017, CHI Franciscan Health received initial approval to build a new, state-of-the-art hospital at Harrison Medical Center-Silverdale. However, the Washington State Department of Health held a hearing in September to reconsider this approval. A final decision is expected in November. If confirmed, the multi-phase, $484 million expansion and consolidation of multiple campuses, is expected to feature leading-edge medical technology, a new acute care center, and

an efficient design. The expected completion date will be in 2020. In addition, CHI Franciscan is making investments in Bremerton, with plans to open a 30,000 square foot outpatient clinic with primary care and urgent care services. The clinic will be part of Harrison Medical Center's new Family Medicine Residency program, which will train highly qualified family medicine physicians. Recruitment is underway for the program, and residents are expected to begin working out of the clinic in 2018.

The Franciscan Medical Group added 91 providers during fiscal year 2017, totaling 872 providers as of June 30, 2017, which has resulted in a 12.5% increase in physician visits and a 22.2% increase in outpatient surgeries for the fiscal year ended June 30, 2017. The operating loss in the Physician Enterprise, however, also increased compared to the prior fiscal year. Again, management is addressing this increased loss through operational initiatives, including increased provider and staff productivity, as well as through provider compensation arrangements. In addition, CHI and regional management are pursuing partnership opportunities to expand ambulatory presence across the region.

Nebraska - The Nebraska region, known as CHI Health, experienced weaker financial performance for the fiscal year ended June 30, 2017. To address this performance, CHI and regional management have implemented labor expense and supply costs reduction initiatives. At June 30, 2017, the Nebraska region has reduced FTEs by 895, despite an increase of 2.9% in adjusted admissions for the fiscal year ended June 30, 2017. Management's efforts to reduce supply costs were limited, largely due to cardiac and orthopedic procedures and physician acceptance issues relating to purchasing compliance.Management is also addressing the increased loss from the Physician Enterprise through operational initiatives, including increased provider and staff productivity, as well as through provider compensation arrangements.

Management is focused on expanding and solidifying CHI Health, one of the largest state-wide integrated health systems in the state of Nebraska. Through its CIN, UniNet, the Nebraska region continues to grow and seek value-based contracts that position the Nebraska region to expand its capability in population health management, including new employer contracts. In June 2017, CHI and regional management completed the consolidation of Creighton University Medical Center's current operations to new facilities under construction at CHI's Bergan Mercy Medical Center, with the goal of reducing operating expenses, rationalizing clinical services and stimulating market share growth. Approximately 200 of the overall 895 reduction in FTEs relates to the consolidation of these campuses.

Texas – Fiscal year 2017 proved a challenging year for operations in the Texas region. Despite significant progress in various aspects of their performance improvement plan, revenue offsets, including unfavorable payer and service mix changes, resulted in operating EBIDA before restructuring of $64.3 million compared to $119.1 million in fiscal 2016. During the year, the number of FTEs was reduced by 591 through a series of reductions in force and implementation of productivity management systems and processes, despite a 10.6% increase in adjusted admissions. A comprehensive productivity management system has been implemented similar to that in place in other CHI regions. In July 2017, the Texas region experienced the turnover of two executive positions. While a national search is underway for both of these positions, the current regional CEO will continue until a successor is named. In addition, an interim CFO has been retained. CHI management has also deployed a corporate leadership team focused on the implementation of best practice techniques, driving day-to-day performance improvement and increasing labor productivity and supply chain savings in the Texas region.

CHI is focused on strengthening the local partnership with the Baylor College of Medicine. The flagship Texas facility, CHI Baylor St. Luke's Medical Center ("BSLMC"), located in the Texas Medical Center, has hired new senior leaders in its president and its chief financial officer. Both executives have extensive experience in the health care industry and intend to focus on building new and renewed relationships with physicians in the Houston community and strengthening operational efficiencies within BSLMC. The regional leadership and CHI continues to move forward with a plan to expand and or relocate certain operations in the Texas Medical Center to the McNair campus while enhancing existing facilities and equipment at the current campus.

The Texas region is also implementing growth strategies with the goals of expanding its patient base, growing and improving physician alignment and further developing primary care in the region.

The Texas region increased the number of employed physicians/providers from 270 to 453 as of June 30, 2017. This increase occurred through the acquisition of several independent practices, as well as other recruitment efforts. Due to the relatively rapid development of the Texas region through acquisitions and affiliations, the focus in fiscal 2018 will be the integration of BSLMC, the Houston suburban facilities, CHI St. Joseph Health in Bryan, Texas, CHI St. Luke's Health Memorial in Lufkin, Texas and a multitude of ambulatory and physician office locations into a cohesive operating model. This will include the adoption of consistent financial applications across the region and consolidation of revenue cycle platforms within the Physician Enterprise.

During August 2017, CHI St. Luke's in Houston, Texas, was impacted by Hurricane Harvey, which caused the temporary closure and evacuation of certain area facilities for a few days. Although all hospitals in Houston, Texas, are now operational, CHI is evaluating the impact of the hurricane on its facilities and operations in the state.

Kentucky – Fiscal 2017 marks a transition year for KentuckyOne. As described in *Part V: Strategic Affiliations & Acquisitions - Pending and Completed Divestitures.* CHI transitioned the University of Louisville Medical Center operations, management and control back to U of L, effective July 1, 2017. Additionally, the CHI Board also approved the divestiture of substantially all of the other Louisville-area acute facilities in the Kentucky region. During this strategic repositioning period, CHI's Louisville operations will be operated separately from the remainder of the Kentucky region. To address immediate operational and financial challenges the Kentucky region is experiencing, CHI management has deployed a corporate leadership team focused on the implementation of operational best practices, driving day-to-day performance improvement, addressing nursing and other staff shortfalls, and implementing improvements in patient throughput and quality. Labor management has reduced contract nursing FTEs, from 443 in November 2016 to 128 at June 30, 2017. Further, labor cost reductions of 289 FTEs, primarily in overhead functions were completed in April 2017. The Kentucky region is implementing new staffing productivity targets in nearly all departments and has implemented CHI's system-wide labor management strategies. Management has also transitioned 50 employed physicians back to private practice, effective in July 2017.

E. Transformative Change Requires Multi-faceted Approach to Success

CHI continues to strengthen its position in value-based care and population health management. Driven by further changes in healthcare policy and payment practices, CHI's 2017 multi-pronged action plan includes:

- Continue growing CHI's CINs and Accountable Care Organizations ("ACOs") in all regions;
- Expedite the further alignment of each regions payer agreements with value-based outcomes;
- Complete the conversion of CHI employee and partner performance incentive programs to value-based outcomes; and
- Finalize CHI's plan to divest ownership of its national health plans.

With the healthcare industry accelerating the transformation to value-based care and population health payment arrangements, CHI has strengthened its readiness with CINs and ACOs in all its regions. Some of CHI's CINs have achieved nationally ranked performance.

CHI's CINs are essential to manage the 835,000 contracted lives under value-based arrangements. Within the CINs, over 200 clinical care management team members work with the 12,000 CIN providers (physicians and advanced practice clinicians). Most of these providers are not employed by CHI, rather have chosen to join CHI's CINs as their value-based care vehicle.

Additionally, non-CHI facilities and businesses across the healthcare spectrum such as post-acute providers

(Skilled Nursing Facilities, Home Health, Hospice) and ancillary providers (Physical Therapy, Lab, Pharmacies, Optometrists), recognized the success of CHI's CIN operations and are joining the CINs to help expedite care transitions, improve care quality and enhance the experience for the patient and family.

Within CHI's regional CINs, eight Medicare ACOs currently manage $2.7 billion of medical spend for over 300,000 Medicare beneficiaries. Mercy ACO in Iowa was the first ACO to form in 2012. To date, Mercy ACO, Rainier Health Network (WA) and KentuckyOne Health Partners have each driven improved quality outcomes and generated net savings resulting in gain share payments from CMS.

Given the initial successes of its CIN performance, CHI has been carefully expanding value-based arrangements with additional payer groups, including Commercial Managed Care, CHI's Employee Health Plan, Medicare Accountable Care Organizations, Bundled Payment Programs, Medicare Advantage Plans and Medicaid Managed Care Plans.

PART V: STRATEGIC AFFILIATIONS & ACQUISITIONS

CHI actively engages in ongoing monitoring and evaluation of potential facility expansion, relationships with academic health center partners, mergers, acquisitions, divestitures, and affiliation opportunities consistent with its strategic goal of creating, maintaining and/or strengthening its CINs in key existing markets and, in certain cases, new markets. CHI's strategic vision is supported by focused system growth in both existing and new markets, as evidenced by recent acquisition activity and strategic divestitures, and realignments, certain of which are described below.

Pending and Completed Affiliations/Acquisitions

Dignity Health. On October 24, 2016, CHI and Dignity Health signed a non-binding letter of intent to explore aligning their organizations and expanding their mission of service in communities across the nation.

The boards and sponsors of the two health systems are evaluating the potential alignment to strengthen their leadership role in transforming health care through increased access and enhanced clinical excellence.

The letter of intent follows the September 2016 announcement that the two systems formed a partnership called the Precision Medicine Alliance LLC, which will create the largest community-based precision medicine program in the country.

The organizations complement one another in many other important ways. CHI brings a diverse geographic footprint with proven clinical service lines and home health capabilities, as well as successful partnerships in research and education. Dignity Health has an operating model that has scaled enterprise-wide initiatives to ensure consistent practices across the system, and is well known for its work with innovative, diversified care-delivery partnerships. There is no geographical overlap of acute care facilities of the two health systems.

Dignity Health owns and operates 39 hospitals in California, Arizona and Nevada and 400+ ancillary care sites across 22 states. As of and for the fiscal year ended June 30, 2016, Dignity Health reported approximately $17.1 billion of total assets, $6.2 billion of net assets and $12.6 billion in total operating revenue. Any definitive agreement would need to be approved by Dignity Health's governing body and both organizations' Boards, and also requires the approval by the California Attorney General and other regulatory agencies as well as satisfaction of customary closing conditions.

Catholic Health Initiatives and Dignity Health are in the final stages of the due diligence process to assess the potential alignment of the ministries and are pleased with the progress made to date. CHI and Dignity Health will share additional information as it becomes available.

CHI can give no assurance that the transaction will occur.

Virginia Mason (Washington). In March 2017, CHI Franciscan Health and Virginia Mason Medical Center, a nonprofit health system based in Seattle that includes 336 licensed-bed Virginia Mason Hospital, primary and

special care group practices and regional medical centers, agreed to a clinical partnership and strategic affiliation, pursuant to which FHS and Virginia Mason are jointly exploring several opportunities where they believe that their collaboration will benefit communities throughout the Puget Sound area. Possibilities being evaluated include developing shared centers of excellence for key clinical service lines; examining ways to further improve health care delivery in various communities that both organizations presently serve; and seeking ways to offer greater continuity of care for patients around the region who need services. The organizations also plan to explore jointly offering programs in new markets in the greater Puget Sound region. In February 2017, Virginia Mason joined the CHI Franciscan Health accountable care organization and CIN.

***Texas Physician Practice*.** Effective November 11, 2016, a subsidiary of CHI acquired a multi-specialty group in the state of Texas. The acquisition included a general acute care hospital and emergency room, an ambulatory surgery center, a management company, and an independent physician association comprising more than 80 health care providers (59 physicians). The hospital, emergency room and other ancillary services have been redirected to nearby CHI facilities.

For the three months ended June 30, 2017, the acquired Texas Physician Practice reported $18.4 million in total operating revenues and $(5.6) million in operating EBIDA before restructuring, impairment, and other losses in the CHI consolidated results of operations. For the period from November 11, 2016 through June 30, 2017, the acquired Texas Physician Practice reported $52.0 million in total operating revenues and $(10.8) million in operating EBIDA before restructuring, impairment, and other losses in the CHI consolidated results of operations.

Mercy Health Network, Inc. (Iowa). Effective March 1, 2016, the Corporation and Trinity Health Corporation, based in Livonia, Michigan ("THC"), amended and restated their existing Mercy Health Network Inc. ("MHN") joint operating agreement that governs certain of their respective legacy operations in Iowa (collectively, the "Iowa Operations") to (a) strengthen MHN's management responsibilities over the Iowa Operations; (b) jointly acquire health care systems in Iowa and contiguous markets; and (c) provide for greater financial, governance, and clinical integration among the parties. Each of the respective party's wholly-owned Iowa assets will continue to be consolidated in their respective financial statements, and commencing in July 2016, combined free cash flow from the Iowa Operations was allocated equally between CHI and THC. MHN's financial results, including any subsidiaries of MHN, however, are not and will not be consolidated with either CHI or THC. CHI's ownership interest in MHN is reflected as an investment in equity of unconsolidated organizations in its consolidated financial statements.

Effective May 1, 2016, MHN became the sole corporate member of Wheaton Franciscan Healthcare-Iowa, which is a faith-based 511-bed non-profit, comprehensive medical/surgical health care provider offering acute levels of medical care at Covenant Medical Center, Waterloo; Sartori Memorial Hospital, Cedar Falls and Mercy Hospital, Oelwein.

Brazosport (Texas). Effective February 1, 2016, Brazosport Regional Health System ("BRHS"), Lake Jackson, Texas and CHI St. Luke's, Houston, Texas, signed an affiliation agreement for BRHS to become part of CHI. Pursuant to the affiliation agreement, CHI St. Luke's became the sole corporate member of BRHS. CHI St. Luke's Health Brazosport (formerly "BRHS") is a non-profit health care organization that includes a 158-bed hospital that operates the only Level III trauma center in Brazoria County.

As a result of the BRHS acquisition, CHI reported approximately $21.3 million in additional total unrestricted net assets in fiscal year 2016, as well as total long-term indebtedness outstanding of $38.5 million (the "BRHS Debt"). In May 2017, CHI defeased the BRHS Debt which was funded by $24.4 million of cash, restricted investments, and the issuance of $14.4 million in commercial paper.

Excluding business combination gains, for the three months ended June 30, 2017 and 2016, BRHS reported $20.2 million and $19.7 million in total operating revenues, respectively, and $0.4 million and $(0.2) million in operating EBIDA before restructuring, impairment, and other losses, respectively, in the CHI consolidated results of operations. For the fiscal year ended June 30, 2017, and for the period from February 1, 2016 through June 30, 2016, BRHS reported

$78.7 million and $33.7 million in total operating revenues, respectively, and $(0.9) million and $0.6 million in operating EBIDA before restructuring, impairment, and other losses, respectively, in the CHI consolidated results of operations.

Trinity Health System (Ohio). Effective February 1, 2016, the Corporation assumed control of Trinity Health System ("Trinity") based in Steubenville, Ohio. Prior to that date, Trinity was controlled by its two corporate members, Sylvania Franciscan Health ("SFH"), a CHI subsidiary, and another entity unrelated to CHI and SFH. In February 2016, CHI replaced that unrelated entity and became a corporate member of Trinity. Trinity owns and operates Trinity Medical Center East, Trinity Medical Center West, Tony Teramana Cancer Center and numerous outpatient clinics located in eastern Ohio.

As a result of the Trinity acquisition, CHI reported approximately $145.1 million in additional total unrestricted net assets in fiscal year 2016, as well as total long-term indebtedness outstanding of $40.1 million (the "Trinity Debt"). In August 2017, CHI redeemed the Trinity debt which was funded by $32.2 million in unrestricted investments and $5.3 million in trustee held funds.

Excluding business combination gains, for the three months ended June 30, 2017 and 2016, Trinity reported $60.2 million and $64.0 million in total operating revenues, respectively, and $2.8 million and $6.4 million in operating EBIDA before restructuring, impairment, and other losses, respectively, in the CHI consolidated results of operations. For the fiscal year ended June 30, 2017, and for the period from February 1, 2016 through June 30, 2016, Trinity reported $237.6 million and $103.7 million in total operating revenues, respectively, and $15.2 million and $7.7 million in operating EBIDA before restructuring, impairment, and other losses, respectively, in the CHI consolidated results of operations.

Longmont United Hospital (Colorado). Effective August 1, 2015, Longmont United Hospital, a Colorado non-profit corporation ("LUH") became affiliated with CHI pursuant to a Joint Operating and Management Agreement, between the Corporation, LUH, Centura Health and Catholic Health Initiatives Colorado. LUH owns and operates Longmont United Hospital, a general acute care hospital licensed for 186 acute care beds and 15 skilled nursing beds, and operates an integrated health care delivery system providing health care services to patients residing in Longmont, Colorado, as well as Boulder, Weld and Larimer Counties in Colorado.

As a result of the LUH acquisition, CHI reported approximately $111.6 million in additional total unrestricted net assets in fiscal year 2016, as well as total long-term indebtedness outstanding of $97.8 million (the "LUH Debt"). In May 2016, CHI issued $34.1 million of commercial paper notes, the proceeds of which were used along with restricted investments, to defease $37.1 million of the LUH Debt. Neither the Corporation nor any of its affiliates (other than LUH) is obligated on the remaining LUH Debt.

Excluding business combination gains, for the three months ended June 30, 2017 and 2016, LUH reported $47.4 million and $44.9 million in total operating revenues, respectively, and $3.4 million and $1.5 million in operating EBIDA before restructuring, impairment, and other losses, respectively, in the CHI consolidated results of operations. For the fiscal year ended June 30, 2017, and for the period from August 1, 2015 through June 30, 2016, LUH reported $183.0 million and $160.9 million in total operating revenues, respectively, and $2.3 million and $4.3 million in operating EBIDA before restructuring, impairment, and other losses, respectively, in the CHI consolidated results of operations.

Pending and Completed Divestitures

KentuckyOne Health. In November 2012, KentuckyOne entered into a Joint Operating Agreement ("Kentucky JOA") and an Academic Affiliation Agreement ("AAA") (collectively "Agreements") with University Medical Center, Inc. ("UMC"), which owns the University of Louisville Hospital, the U of L, and other parties.

On December 17, 2016, KentuckyOne, UMC and U of L agreed to restructure their existing Kentucky JOA.

Under the terms of that agreement, the operations, management and control of the University of Louisville Hospital was transferred back to UMC effective July 1, 2017. The AAA was restructured and various transition services agreements were entered into in connection with the transfer of the University of Louisville Hospital back to UMC.

As described in *Part IV: A. Strategic Intent*, in May 2017, CHI approved a plan to sell or otherwise dispose of substantially all of the Louisville market acute care operations, including certain entities of Jewish Hospital and St. Mary's Healthcare, Inc. ("JHSMH"). As a result, CHI will refocus the Kentucky region on a smaller community footprint, centered in central and eastern Kentucky. CHI assumed complete ownership of KentuckyOne, effective September 1, 2017, when the Corporation purchased the non-controlling interest from the remaining partner for $150 million. The payment will be used by the partner to further invest in the healthcare needs of the community.

The following summarizes the financial results of UMC reported in the CHI consolidated statements of operations, and JHSMH reported in the CHI consolidated statements of changes in net assets:

	Three Months Ended June 30			Twelve Months Ended June 30		
$ in millions	2017	2016	% Change	2017	2016	% Change
UMC						
Operating revenues	$133.2	$152.4	(12.6%)	$515.2	$528.7	(2.6%)
Operating EBIDA before restructuring, impairment and other losses	$21.3	$41.5	48.7%	$47.4	$73.7	35.7%
JHSMH						
Operating revenues	$183.5	$171.1	7.3%	$780.7	$752.9	3.7%
Operating EBIDA before restructuring, impairment and other losses	$(16.9)	$(25.2)	33.0%	$(43.9)	$(45.4)	3.5%

The CHI consolidated balance sheets included UMC total assets of $605.5 million and total liabilities of $330.3 million at June 30, 2017. Upon deconsolidation of UMC on July 1, 2017, CHI incurred a loss of approximately $318.0 million. The CHI consolidated balance sheets include JHSMH discontinued operations total assets held for sale of $393.8 million and total liabilities held for sale of $47.4 million at June 30, 2017.

QualChoice. As described in *Part II: Fiscal Year 2017 Highlights and Summary*, in May 2016, CHI approved a plan to sell or otherwise dispose of certain entities of QualChoice, a consolidated CHI subsidiary, whose primary business is to develop, manage and market commercial and Medicare Advantage health insurance programs, as well as a wide range of products and administrative services. A letter of intent for the Medicare Advantage health insurance operations has been received, with an anticipated sale in fiscal year 2018. Although there has been significant interest in the QualChoice Health commercial operations, the uncertainty surrounding the Affordable Care Act and current political environment has delayed the anticipated sale of this operation to a timeline outside of CHI's control. CHI remains committed to selling or otherwise disposing of the QualChoice Health commercial operations and continues to actively market these operations (see *Part II:* herein for further information).

The following summarizes the financial results of QualChoice reported in the CHI consolidated statements of changes in net assets:

$ in millions	Three Months Ended June 30			Twelve Months Ended June 30		
	2017	2016	% Change	2017	2016	% Change
QualChoice						
Operating revenues	$132.3	$143.8	(8.0%)	$578.0	$520.4	11.1%
Operating EBIDA before restructuring	$(10.6)	$(24.7)	57.3%	$(38.6)	$(85.4)	54.8%

The CHI consolidated balance sheets include QualChoice discontinued operations total assets held for sale of $185.4 million and total liabilities held for sale of $118.3 million at June 30, 2017.

Real Estate and Other Asset Sales. During fiscal year 2017 and 2016, CHI sold various real estate assets across the enterprise as part of a long-term effort to improve the mix of owned and leased assets. In conjunction with the sale, CHI entered into 10-year operating lease agreements with the buyer, and in accordance with ASC 840-40 – Leases – Sale-Lease Back Transactions, certain of the gains on the sale of the real estate assets were deferred and will be amortized to lease expense over the life of the operating leases.

In fiscal year 2017 and 2016, real estate assets with a net book value of $281.8 million and $332.3 million, respectively, were sold for gross proceeds of $366.5 million and $601.7 million, respectively. As a result of the sales, CHI recognized $22.0 million and $59.4 million gain on sales in the consolidated statements of operations for the years ended June 30, 2017 and 2016, respectively. CHI also recorded short-term deferred gains of $5.8 million and $20.1 million, respectively, and long-term deferred gains of $52.2 million and $180.6 million, respectively, for fiscal year 2017 and fiscal year 2016. On the consolidated balance sheet, the short-term deferred gains are a component of accrued expenses, and the long-term deferred gains are a component of other long-term liabilities. The deferred gains will be amortized against rent expense over the terms of the respective operating lease agreements.

CHI expects to close on the sale of certain additional real estate assets during the three months ended September 30, 2017, with gross proceeds of approximately $34.3 million.

Pathology Associates Medical Laboratories, LLC (PAML). In February 2017, CHI entered into a definitive agreement with Laboratory Corporation of America Holdings (LabCorp) to sell all of CHI's interests in PAML to LabCorp. As part of the agreement, LabCorp will also acquire CHI's direct and indirect interests in three CHI joint ventures with PAML in the states of Colorado, Kentucky and Washington. The agreement will close in stages beginning in May 2017, and continuing through 2018. Non-refundable gross sales proceeds attributable to CHI and its affiliates of $96.7 million were received in May 2017, resulting in a net gain on sale of $40.2 million.

Additionally, CHI also sold various other ambulatory assets during fiscal year 2017 for net proceeds of $101.7 million reflected within other operating revenues as gain on sale on the consolidated statement of operations for the year ended June 30, 2017.

Change in Composition of Credit Group

Bethesda Hospital, Inc. In 2001, Bethesda Hospital, Inc. ("Bethesda") became a member of the CHI Credit Group as a Designated Affiliate. Bethesda and The Good Samaritan Hospital of Cincinnati, Ohio, an affiliate of the Corporation, are jointly operated pursuant to a JOA between Bethesda, Inc. and the Corporation. The Corporation previously loaned funds to Bethesda pursuant to its loan program, and the proceeds of a portion of the Corporation's existing debt was used to finance Bethesda's assets. In February 2017, Bethesda provided $139.7 million to the Corporation as repayment for its loans, and Bethesda is no longer a Designated Affiliate.

In February and March 2017, the Corporation prepaid, redeemed or defeased, as applicable, all outstanding CHI debt related to Bethesda's assets, in the approximate principal amount of $130.0 million.

The Good Samaritan Hospital of Cincinnati, Ohio remains a Participant under the Capital Obligation Document, and the JOA remains in effect. The financial statements of The Good Samaritan Hospital of Cincinnati, Ohio, continue to be included in the CHI consolidated financial statements.

PART VI: SELECTED FINANCIAL DATA

The selected financial data that follows has been prepared by management, based on (i) CHI's unaudited interim financial statements for the three month periods ended June 30, 2017 and 2016, and (ii) CHI's audited financial statements as of and for the fiscal years ended June 30, 2017 and 2016. The unaudited financial statements include all adjustments, consisting of normal recurring accruals, which management of CHI considers necessary for a fair presentation of the combined financial position and results of operations for these periods. The unaudited interim financial statements for the three month period ended June 30, 2017 are not necessarily indicative of the results that may be expected for the full fiscal year ending June 30, 2017.

The CHI consolidated financial information should be read in conjunction with the unaudited financial statements, related notes, and other financial information of CHI included in Appendix A of this Annual Report.

The results of operations for recently acquired entities that have been accounted for as acquisitions are included in the CHI consolidated financial and operating information from the respective dates of acquisition.

CHI participates in JOAs with hospital-based organizations in Colorado, Iowa and Ohio. The agreements generally provide for, among other things, joint management of the combined operations of the local facilities included in the JOAs through JOCs. CHI retains ownership of the assets, liabilities, equity, revenues and expenses of the CHI facilities that participate in the JOAs. Transfers of assets from facilities owned by the JOA participants are generally restricted under the terms of the agreements. The financial statements of the CHI facilities managed under all JOAs are included in the CHI consolidated financial statements.

As of June 30, 2017, CHI has investment interests of 65%, 50%, and 50% in JOCs based in Colorado, Iowa, and Ohio, respectively. CHI's interests in the JOCs are included in investments in unconsolidated organizations and totaled $381.7 million at June 30, 2017. CHI recognizes its investment in all JOCs under the equity method of accounting. The JOCs provide various levels of services to the related JOA sponsors, and operating expenses of the JOCs are allocated to each sponsoring organization.

Certain joint venture agreements do not result in the consolidation of the jointly owned controlled entities with the Corporation. The results of those operations are instead reflected in the consolidated financial statements of CHI under the line item "Changes in equity of unconsolidated organizations". Additional detail regarding certain of CHI's JOAs and investments in Unconsolidated Organizations can be found in Note 3 of the CHI Audited Financial Statements included in Appendix A of this Annual Report.

A. The following table provides condensed consolidated balance sheets for CHI as of June 30, 2017 and 2016.

CHI Condensed Consolidated Balance Sheets	June 30, 2017	June 30, 2016
Assets	(in Thousands)	
Current assets:		
Cash and equivalents	$ 1,033,166	$ 1,305,242
Net patient accounts receivable	2,154,248	2,161,237
Assets held for sale	582,344	665,428
Other current assets	772,330	765,755
Total current assets	4,542,088	4,897,662
Investments and assets limited as to use:		
Internally designated investments	5,574,188	5,338,803
Restricted investments	1,212,283	1,219,232
Total investments and assets limited as to use	6,786,471	6,558,035
Property and equipment, net	8,569,313	9,034,052
Other assets	2,033,878	2,169,381
Total assets	$ 21,931,750	$ 22,659,130
Liabilities and net assets		
Current liabilities:		
Accounts payable and accrued expenses	$ 2,417,559	$ 2,546,520
Liabilities held for sale	165,735	175,239
Short-term and current portion of debt	2,114,208	1,864,728
Total current liabilities	4,697,502	4,586,487
Other liabilities	2,919,312	3,444,622
Long-term debt	6,588,202	7,180,925
Total liabilities	14,205,016	15,212,034
Net assets:		
Unrestricted	7,415,388	7,127,641
Temporarily restricted	214,250	224,524
Permanently restricted	97,096	94,931
Total net assets	7,726,734	7,447,096
Total liabilities and net assets	$ 21,931,750	$ 22,659,130

B. The following table presents condensed consolidated statements of operations for CHI for the three month period ended June 30, 2017 and 2016, and fiscal years ended June 30, 2017 and 2016.

CHI Condensed Consolidated Statements of Operations	Three Months Ended June 30		Fiscal Year Ended June 30	
	2017	2016	2017	2016
Revenues		(in Thousands)		
Net patient services revenues	$ 3,609,543	$ 3,501,983	$ 14,450,868	$ 13,847,027
Business combination gains	-	(12,806)	-	223,036
Other	302,081	413,745	1,096,596	1,119,524
Total operating revenues	3,911,624	3,902,922	15,547,464	15,189,587
Expenses				
Salaries and employee benefits	1,858,796	1,893,793	7,495,878	7,299,915
Supplies, purchased services and other	1,806,579	1,777,366	7,120,899	6,853,350
Depreciation and amortization	225,770	221,201	846,291	833,394
Interest	75,356	71,522	295,476	281,581
Total operating expenses before restructuring, impairment and other losses	3,966,501	3,963,882	15,758,544	15,268,240
Loss from operations before restructuring, impairment and other losses	(54,877)	(60,960)	(211,080)	(78,653)
Restructuring, impairment and other losses	191,000	197,089	374,167	292,758
Loss from operations	(245,877)	(258,049)	(585,247)	(371,411)
Nonoperating gains (losses)	172,286	77,374	713,637	(204,160)
(Deficit) excess of revenues over expenses	$ (73,591)	$ (180,675)	$ 128,390	$ (575,571)

1. CRITICAL ACCOUNTING POLICIES

The preparation of financial statements in conformity with GAAP requires that management make assumptions, estimates and judgments affecting the amounts reported in the financial statements, including the notes thereto, and related disclosures of commitments and contingencies, if any. Management considers critical accounting policies to be those that require more significant judgments and estimates in the preparation of its financial statements, including the following: recognition of net patient service revenues, which includes contractual allowances, bad debt and charity care reserves; cost report settlements; impairment of goodwill, intangibles and long-lived assets; provisions for bad debt; valuations of investments; and reserves for losses and expenses related to health care professional and general liability risks. In making such judgments and estimates, management relies on historical experience and on other assumptions believed to be reasonable under the circumstances. Actual results could differ materially from the estimates. A description of CHI's significant accounting policies can be found in Note 1 of the CHI Audited Financial Statements included in Appendix A of this Annual Report.

PART VII: MANAGEMENT'S DISCUSSION & ANALYSIS

The following table provides key balance sheet metrics for CHI as of June 30, 2017 and 2016.

CHI Key Balance Sheet Metrics	June 30, 2017	June 30, 2016
Consolidated Balance Sheet Summary		
Total assets	$ 21.9 billion	$ 22.6 billion
Total liabilities	$ 14.2 billion	$ 15.2 billion
Total net assets	$ 7.7 billion	$ 7.4 billion
Financial Position and Leverage Ratios (Unaudited)		
Total cash and unrestricted investments	$ 6.6 billion	$ 6.6 billion
Days of cash on hand[1]	162	168
Total debt	$ 8.7 billion	$ 9.0 billion
Debt to capitalization[2]	54.0%	55.9%
Debt to cash flow[3]	24.0x	30.1x
Historical Debt Service Coverage Ratio	2.6x	2.0x

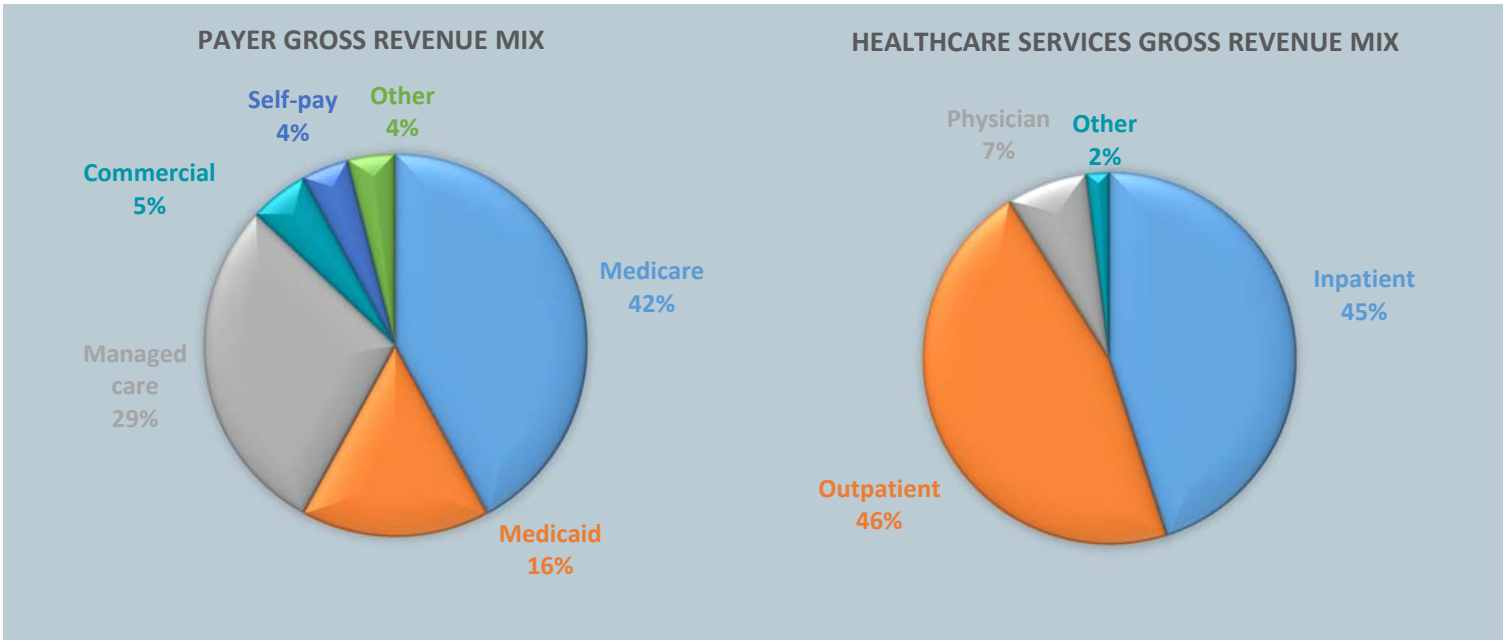
[1] (Cash and equivalents + Investments and assets limited as to use: Internally designated investments)/((Total operating expenses before restructuring, impairment and other losses - Depreciation and amortization)/365). For the days of cash on hand one day of operating expenses represented $40.9 million at June 30, 2017 and $39.4 million at June 30, 2016.
[2] (Short-term and current portion of debt + Long-term debt)/(Short-term and current portion of debt + Long-term debt + Unrestricted net assets).
[3] (Short-term and current portion of debt + Long-term debt)/(Loss from operations + Depreciation and amortization + Non-cash restructuring, impairment and other losses - business combinations gains and other non-cash losses included in Loss from operations).

The following table presents key operating metrics and utilization statistics for CHI for the three months ended June 30, 2017 and 2016, and fiscal years ended June 30, 2017 and 2016.

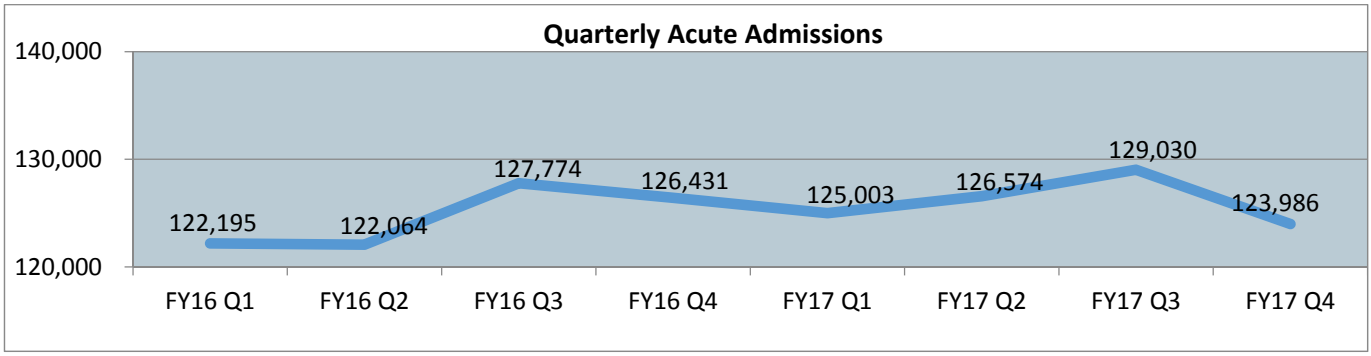
CHI Key Operating Metrics and Utilization Statistics	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	Fiscal Year Ended June 30, 2017	Fiscal Year Ended June 30, 2016
Consolidated Revenues, Expenses and Key Operating Metrics*				
Total net patient services revenues	$ 3.6 billion	$ 3.5 billion	$ 14.5 billion	$ 13.8 billion
Total operating revenues	$ 3.9 billion	$ 3.9 billion	$ 15.5 billion	$ 15.2 billion
Total operating expenses before restructuring, impairment and other losses	$ 4.0 billion	$ 4.0 billion	$ 15.8 billion	$ 15.3 billion
Operating EBIDA before restructuring, impairment and other losses[1]	$ 246.2 million	$ 231.8 million	$ 930.7 million	$ 1,036.3 million
Operating EBIDA margin before restructuring, impairment and other losses[2]	6.3%	5.9%	6.0%	6.8%
Operating loss before restructuring, impairment and other losses	$ (54.9) million	$ (61.0) million	$ (211.1) million	$ (78.7) million
Operating loss margin before restructuring, impairment and other losses[3]	(1.4)%	(1.6)%	(1.4)%	(0.5)%
Operating EBIDA[4]	$ 55.2 million	$ 34.7 million	$ 556.5 million	$ 743.6 million
Operating EBIDA margin[5]	1.4%	0.9%	3.6%	4.9%
Operating loss	$ (245.9) million	$ (258.0) million	$ (585.2) million	$ (371.4) million
Operating loss margin[6]	(6.3)%	(6.6)%	(3.8)%	(2.4)%
(Deficit) excess margin[7]	(1.8)%	(4.5)%	0.8%	(3.8)%
Utilization Statistics				
Acute admissions	123,986	126,431	504,593	498,464
Acute inpatient days	573,283	602,059	2,366,980	2,382,402
Acute average length of stay in days	4.6	4.8	4.7	4.8
Long-term care days	116,968	127,879	483,151	503,450
Medicare case-mix index	1.8	1.8	1.8	1.8
Adjusted admissions[8]	275,854	275,042	1,109,556	1,067,394
Inpatient ER visits	67,572	69,309	273,580	268,678
Inpatient surgeries	38,740	39,715	156,211	156,760
Outpatient ER visits	480,665	500,767	1,966,342	1,951,714
Outpatient non-ER visits	1,459,562	1,473,296	5,804,586	5,557,647
Outpatient surgeries	62,802	61,619	253,839	239,672
Physician visits	2,725,679	2,511,864	10,540,482	9,635,875

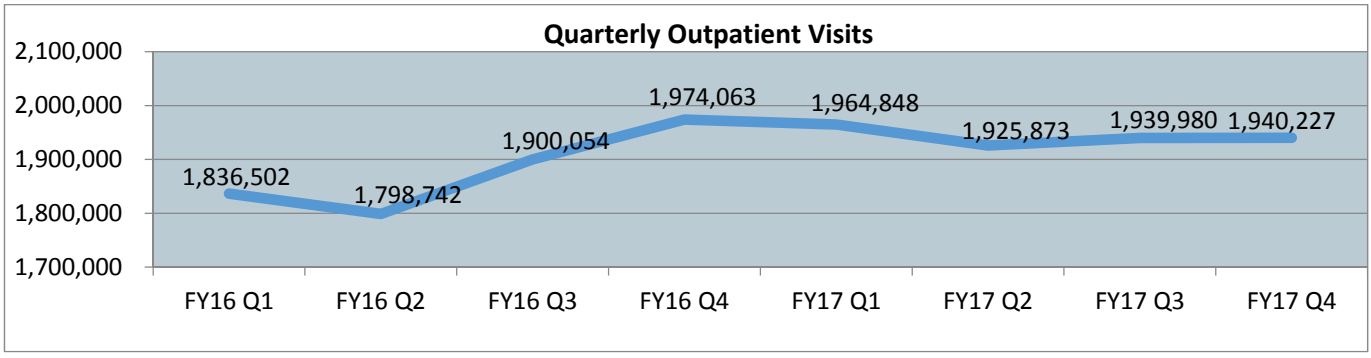
* Includes business combination gains.
[1] Income (loss) from operations before restructuring, impairment and other losses + depreciation and amortization + interest.
[2] Income (loss) from operations before restructuring, impairment and other losses + depreciation and amortization + interest/total operating revenues.
[3] Income (loss) from operations before restructuring, impairment and other losses/total operating revenues.
[4] Income (loss) from operations + depreciation and amortization + interest.
[5] Income (loss) from operations + depreciation and amortization + interest/total operating revenues.
[6] Income (loss) from operations/total operating revenues.
[7] (Deficit) excess of revenues over expenses/(total operating revenues + nonoperating gains (losses).
[8] (Total gross patient revenues/total gross inpatient revenues) x acute admissions.

The following charts represent the payer gross revenue mix and healthcare services gross revenue mix for CHI's consolidated operations for the fiscal year ended June 30, 2017.



The following charts represent quarterly patient volume activity for CHI's consolidated operations over the previous eight quarters and includes the effects of acquisitions.





1. SUMMARY OF OPERATING RESULTS FOR THE THREE MONTHS ENDED JUNE 30, 2017 AND 2016

OPERATING EBIDA/LOSS FROM OPERATIONS

Operating EBIDA before restructuring, impairment and other losses totaled $246.2 million and $231.8 million for the three months ended June 30, 2017 and 2016, respectively, equivalent to an operating EBIDA margin before restructuring, impairment and other losses percentage of 6.3% and 5.9%, respectively. Excluding the following transactional gains and other items, CHI operating EBIDA before restructuring, impairment and other losses totaled $204.0 million and $154.6 million for the three months ended June 30, 2017 and 2016, respectively, equivalent to an operating EBIDA margin before restructuring, impairment and other losses percentage of 5.3% and 4.0%, respectively.

$ in millions	Three Months Ended June 30 2017	2016	Change
Operating EBIDA before restructuring, impairment and other losses, excluding transactional gains and other items	$204.0	$154.6	$49.4
Operating EBIDA margin before restructuring, impairment and other losses, adjusted	5.3%	4.0%	1.3%
Business combination gains	-	(12.8)	
Gain on sale of lab operations	40.2	-	
Iowa equity gain*	-	89.1	
Gains on real estate sales	2.0	59.4	
Net patient service revenue adjustments	-	(58.5)	
Operating EBIDA before restructuring, impairment and other losses	$246.2	$231.8	$14.5
Operating EBIDA margin before restructuring, impairment and other losses	6.3%	5.9%	0.4%

*Equity gain is result of the Wheaton Franciscan HealthCare – Iowa acquisition

The $49.4 million in improved normalized results were due to increased net patient services revenues combined with favorable expense management as several of CHI's productivity initiatives related to expense reduction strategies began to show improvements, particularly within labor costs. As part of CHI's on-going comprehensive expense reduction strategy, focused clinical and operational initiatives across the system continue to be implemented to include targeted initiatives at the regional levels, as well as at corporate services.

Total net patient services revenues, normalized to exclude the transactional gains and other net patient services revenues adjustments noted below, increased 1.4%, or $49.1 million, of which $19.4 million was due to recently completed acquisitions as well as increased acuity, whereas total operating expenses increased by 0.1%, or $2.6 million. Normalized total operating expenses also increased $27.5 million due to recently completed acquisitions, but the increase was offset by favorable expense management.

Quarterly results for the fiscal year 2017 have also shown improvements over the previous rolling four quarters. CHI reported operating EBIDA in the first fiscal quarter of 3.6%, or $136.0 million, in the second fiscal quarter of 5.5%, or $215.6 million, in the third quarter of 8.4%, or $332.8 million, and in the fourth fiscal quarter of 6.3%, or $246.2 million. Quarterly

results included the following material transactions: net gains of $85.7 million in the Pacific Northwest region primarily from the sale of certain outpatient ambulatory business lines in the third fiscal quarter, and gains of $40.2 million from the sale of CHI's ownership interest in various laboratory operations in the fourth fiscal quarter as part of the PAML divestiture.

Loss from operations before restructuring, impairment and other losses totaled $(54.9) million and $(61.0) million for the three months ended June 30, 2017 and 2016, respectively, or an operating loss margin before restructuring, impairment and other losses percentage of (1.4)% and (1.6)%, respectively.

The strategic affiliations completed in fiscal years 2017 and 2016 contributed total operating revenues of $164.8 million and $143.3 million; operating EBIDA before restructuring, impairment and other losses of $6.2 million and $9.7 million; and (loss) income from operations before restructuring, impairment and other losses of $(3.9) million and $2.1 million, for the three months ended June 30, 2017 and 2016, respectively, excluding business combination gains in fiscal year 2016.

The table below presents total operating EBIDA before restructuring, impairment and other losses, total operating EBIDA margin before restructuring, impairment and other losses and total operating revenues of CHI by region for the three months ended June 30, 2017 and 2016. Further information on CHI's regional operating results is discussed within the regional operating trends section below.

Catholic Health Initiatives Operations Summary – Three Months Ended June 30, 2017 and 2016

Region	QTD 6/30/2017 Operating EBIDA before restructuring, impairment and other losses (in Thousands)	QTD 6/30/2016 Operating EBIDA before restructuring, impairment and other losses (in Thousands)	QTD 6/30/2017 Operating EBIDA margin before restructuring, impairment and other losses	QTD 6/30/2016 Operating EBIDA margin before restructuring, impairment and other losses	QTD 6/30/2017 Operating revenues percentage of CHI consolidated	QTD 6/30/2016 Operating revenues percentage of CHI consolidated
Pacific Northwest	$ 84,523	$ 36,498	12.3%	5.8%	17.5%	16.0%
Colorado	96,814	42,481	15.9%	7.8%	15.6%	13.9%
Texas	1,505	5,294	0.3%	1.0%	13.9%	13.7%
Nebraska	31,492	58,558	6.2%	10.8%	13.0%	13.8%
Kentucky	56,940	60,423	13.4%	14.6%	10.9%	10.6%
Ohio	17,508	42,432	6.2%	13.5%	7.2%	8.1%
Iowa[1]	11,543	113,476	4.5%	32.8%	6.5%	8.9%
Arkansas	1,969	(652)	1.0%	(0.4)%	4.9%	4.7%
North Dakota/Minnesota	1,508	23,277	0.8%	12.0%	4.6%	5.0%
Tennessee	12,012	(5,570)	7.5%	(3.7)%	4.1%	3.8%
National business lines[2]	11,981	2,621	15.7%	4.2%	2.0%	1.6%
Other[3]	(7,051)	(9,140)	N/A	N/A	0.0%	(0.1)%
Total Regional	320,744	369,698	8.2%	9.5%	100.2%	100.0%
Corporate services and other business lines[4]	(74,495)	(125,129)	N/A	N/A	(0.2)%	0.3%
Business combination gains	-	(12,806)	N/A	N/A	0.0%	(0.3)%
Total CHI Consolidated	$ 246,249	$ 231,763	6.3%	5.9%	100.0%	100.0%

[1] Includes an $89.1 million equity gain in the prior fiscal year as a result of the Wheaton Franciscan Healthcare-Iowa acquisition.
[2] Includes Home Care and Senior Living business lines.
[3] Includes the operations of Albuquerque Health Ministries and Lancaster Health Ministries MBOs as well as regional eliminations.
[4] Includes CHI Corporate and First Initiatives Insurance, Ltd. ("FIIL"), CHI's wholly-owned captive insurance company as well as CHI system eliminations.

OPERATING REVENUE AND VOLUME TRENDS

Total operating revenue and net patient service revenue changes are summarized below. Normalized amounts have been adjusted to exclude transactional gains and other items as noted above:

Three months ended June 30, 2017 compared to three months ended June 30,2016		
Revenue	Dollar Change	Percentage Change
Operating revenue	$8.7 million	0.2%
Operating revenue normalized	$43.7 million	1.2%
Net patient service revenue	$107.6 million	3.1%
Net patient service revenue normalized	$49.1 million	1.4%
Net patient service revenue due to new acquisitions	$19.4 million	-

Also impacting net patient services revenues were volume increases of $19.5 million, favorable shifts in acuity of $26.4 million, offset by unfavorable shifts in payer mix of $(26.5) million.

Excluding the impacts of current and prior year acquisitions (same store basis), same store patient volumes increases (decreases) were as follows for the three months ended June 30, 2017, as compared to the corresponding period of the prior fiscal year.

Three months ended June 30, 2017 compared to three months ended June 30, 2016		
Patient Volumes	Percentage Change	Volume Change
Adjusted Admissions	(0.3)%	(896)
Acute Admissions	(2.0)%	(2,447)
Acute Inpatient Days	(4.8)%	(27,574)
Inpatient ER Visits	(2.2)%	(1,463)
Inpatient Surgeries	(2.7)%	(1,042)
Outpatient ER Visits	(4.4)%	(20,861)
Outpatient Non-ER Visits	(0.2)%	(2,785)
Outpatient Surgeries	2.6%	1,520
Physician Visits	5.9%	144,995

Other Operating Revenue - Total other operating revenues, normalized to exclude the transactional gains and other items noted above, decreased (2.0)%, or $(5.4) million for the three months ended June 30, 2017, compared to the corresponding period of the prior fiscal year.

OPERATING EXPENSES

CHI total operating expenses before restructuring, impairment and other losses are summarized below:

Three months ended June 30, 2017 compared to three months ended June 30,2016		
Expense	Dollar Change	Percent Change
Total operating expense	$2.6 million	0.1%
Total operating expense – same store	$(24.9) million	(0.7)%
Total labor expense – same store	$(43.8) million	(2.4)%
Supply expense – same store	$(8.2) million	(1.3)%
Medical Pro Fees – same store	$19.0 million	16.9%
Purchased Service – same store	$(2.5) million	(0.6)%

Labor and Productivity indicators are summarized as follows:

	Three Months Ended June 30 2017	Three Months Ended June 30 2016
Labor % of Net patient service revenue – same store	51.5%	54.2%
Labor % of total operating expense – same store	46.9%	47.7%
Supplies % of net patient service revenue – same store	17.4%	18.1%

Same store total operating expenses before restructuring, impairment and other losses decreased primarily due to reductions in total labor costs, offset by increases in operating expenses, primarily as a result of annual inflation increases and strategic initiatives across CHI as described in more detail below.

Same store total labor costs decreased (2.4)%, or $(43.8) million, for the three months ended June 30, 2017, as compared to the corresponding period of the prior fiscal year, due to $(13.6) million increase in the average hourly rate (0.8%) and $(57.4) million in decreased FTEs as a result of labor productivity improvements. CHI continues to address labor productivity within the regions, as well as growth initiatives in certain physician practices where labor

costs have been added in anticipation of future increased patient volumes. Several labor productivity improvement initiatives are being implemented throughout CHI, with a particular focus on the Kentucky and Texas regions.

Same store medical professional fees increased 16.9%, or $19.0 million due to growth initiatives in certain physician practices where medical professional fees costs have been added in anticipation of future increased patient volumes.

Same store supplies expense decreased (1.3)% or $(8.2) million, for the three months ended June 30, 2017, as compared to the corresponding period of the prior year. Same store supplies as a percentage of net patient services revenues decreased to 17.4% for the three months ended June 30, 2017, compared to 18.1% in the same period of the prior fiscal year.

REGIONAL OPERATING TRENDS

CHI periodically reviews its allocation methodology for Corporate support services and may adjust those allocations based on the strategic needs and resource consumption of the regions and CHI overall. These changes in allocation methodologies may increase or decrease a region's operating results from year to year, but have no impact on the consolidated results of CHI.

CHI's regional operations were mixed, with favorable expense management offsetting reduced patient volumes in the quarter. The Pacific Northwest, Colorado, Texas, Nebraska and Kentucky regions represent CHI's five largest operating regions, and for the three months ended June 30, 2017, represented 70.9% of CHI's consolidated operating revenues. Additional information on these regions is discussed below.

Pacific Northwest - the region's operating EBIDA before restructuring, impairment and other losses totaled $84.5 million for the three months ended June 30, 2017, and increased $48.0 million compared to the corresponding period of the prior fiscal year. Results for the three months ended June 30, 2017, included a $14.9 million gain on sale of interests in various laboratory operations, and results for the three months ended June 30, 2016 included $20.3 million in gains from asset sales in the region. The remainder of the region's favorable results were due to overall increased patient volumes, combined with the implementation of expense management and productivity improvements. Net patient services revenue increased $69.1 million, and included favorable gains related to patient volumes, acuity and service mix. The net patient services revenues increase exceeded the $15.3 million in increased operating expenses, compared to the corresponding period of the prior fiscal year. Total net revenue per adjusted admission increased 13.0% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 3.4%. Total labor as a percentage of net patient services revenue decreased to 51.3% compared to 56.4% in the same period of the prior fiscal year as a result of ongoing labor productivity improvements, representing a favorable expense variance of $33.0 million. Supply expense as a percentage of net patient services revenue declined to 13.2% compared to 15.0% in the prior fiscal year due to revenue growth and improved utilization.

Colorado - the region's operating EBIDA before restructuring, impairment and other losses totaled $96.8 million for the three months ended June 30, 2017, and increased $54.3 million compared to the corresponding period of the prior fiscal year. Results for the three months ended June 30, 2017 included a $25.3 million gains on asset sales. Net patient services revenues increased $36.8 million, including $2.5 million as a result of the Longmont transaction. Net patient services revenues were also favorably impacted by $8.7 million in increased same store patient volumes and $(7.7) million decrease in provider fee revenue. The net patient services revenues increase exceeded the $15.9 million in increased operating expenses, compared to the corresponding period of the prior fiscal year. Total net revenue per adjusted admission increased 9.5% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 5.2%. Total labor as a percentage of net patient services revenues decreased to 41.8% compared to 43.5% in the same period of the prior fiscal year, representing a favorable expense variance of $9.4 million.

Texas - the region's operating EBIDA before restructuring, impairment and other losses totaled $1.5 million for the three months ended June 30, 2017, and decreased $(3.8) million compared to the same period

of the prior fiscal year. The region's unfavorable results were due primarily to reductions in other operating revenues which were favorably offset by increased net patient services revenues and operating expense improvements, compared to the same period of the prior fiscal year. Other operating revenues decreased $(15.0) million compared to the same period of the prior fiscal year due to $(4.9) million in reduced Medicare and Medical meaningful use revenues, as well as reduced third party rental income since the underlying real estate assets were sold at the beginning of fiscal year 2017. Net patient services revenues increased $25.1 million and included $16.8 million from recently completed affiliations. Total operating expenses increased $12.7 million and included $24.7 million from recently completed affiliations, compared to the same period of the prior fiscal year. Net patient services revenues were also favorably impacted by increases in patient volumes and acuity offset by unfavorable shift in payer mix. Total net revenue per adjusted admission increased 1.0% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission decreased (1.7)%. Total labor as a percentage of net patient services revenues decreased to 45.9% compared to 49.5% in the same period of the prior fiscal year, representing a favorable expense variance of $19.0 million. Management is implementing strategies to improve labor productivity, supply chain, and overall expense savings in the Texas region, and continues to expand its referral base for additional future growth in the region through acquiring and expanding the Texas Physician Enterprise in the greater Houston area.

Nebraska - the region's operating EBIDA before restructuring, impairment and other losses totaled $31.5 million for the three months ended June 30, 2017, and decreased $(27.1) million compared to the corresponding period of the prior fiscal year. Results for the three months ended June 30, 2016 included $25.0 million in gains from asset sales in the region. Net patient services revenue decreased $(6.0) million, mostly due to unfavorable shifts in payer mix. Total net revenue per adjusted admission decreased (2.7)% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission decreased (2.5)%. Total operating expenses decreased (1.1)%, or $(5.5) million in the region for the three months ended June 30, 2017, primarily in the areas of total compensation, purchased services and supplies expenses, compared to the corresponding period of the prior fiscal year. Total labor as a percentage of net patient services revenue decreased to 55.9% compared to 57.6% in the same period of the prior fiscal year, representing a favorable expense variance of $8.0 million. Supply expense as a percentage of net patient service revenues increased to 16.4% compared to 15.6% in the prior fiscal year. Increases in utilization and cost are concentrated in pharmacy, cardiovascular and orthopedic/spine, and are a continued focus and opportunity for reduction.

Kentucky - the region's operating EBIDA before restructuring, impairment and other losses totaled $56.9 million for the three months ended June 30, 2017, and decreased $(3.5) million compared to the corresponding period of the prior fiscal year. Results for the three months ended June 30, 2017 included a $6.2 million gain on sale of interests in various laboratory operations, and results for the three months ended June 30, 2016 included $7.7 million in gains from asset sales in the region. The region's unfavorable results were due primarily to greater operating expenses which increased 4.2%, or $15.7 million, outpacing net patient services revenues which increased 3.0%, or $11.1 million, compared to the same period of the prior fiscal year. Net patient services revenue increased $11.1 million, including $(3.3) million in unfavorable shifts in payer mix, $(3.1) in service mix and $(4.5) million in volume decreases which were offset by the negative accounts receivable reserve adjustment in the prior year not recurring. Total net revenue per adjusted admission increased 4.1% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 5.2%. Total labor as a percentage of net patient services revenues increased to 43.1% compared to 41.9% in the same period of the prior fiscal year, representing an unfavorable expense variance of $(4.6) million. The region is continuing its efforts to address nursing and other staff shortages which have resulted in increases to overall labor costs, including contract labor costs, overtime and premium pay.

CHI Corporate services and other business lines - operating EBIDA before restructuring, impairment and other losses totaled $(74.5) million for the three months ended June 30, 2017, and improved $50.6 million for the three months ended June 30, 2017,

compared to the corresponding period of the prior fiscal year. Results for the fiscal year ended June 30, 2017 included a gain of $8.7 million on the sale of CHI's interests in various laboratory operations. Changes in support services activities relate to a variety of factors, and include strategic transfers of certain activities from the regions and other service lines to Corporate services in order to build Corporate support functions, and new implementations of system-wide services such as revenue cycle and food programs. Support services allocations to the regions consider the strategic needs and resource consumption of the regions and CHI overall. Expense increases for the three months ended June 30, 2017 include $(4.6) million of revenue cycle implementations and services for new facilities, and $(1.9) million related to new facilities implementations for national food services, and $(4.8) million related to Clinical Engineering programs and expansion. IT expenses decreased $9.3 million compared to the corresponding period of the prior fiscal year due to reduced system implementation activity, and overall corporate services departments declined $25.6 million due to a wide range of cost reduction activities. Pension operating expenses decreased $(2.4) million as a result of actuarial changes impacting the net periodic pension costs which were offset by the operations of the self-insurance plans which increased $6.5 million due to unfavorable claims experience for the three months ended June 30, 2017 compared to the corresponding period of the prior fiscal year.

Restructuring, Impairment and Other Losses

	Three Months Ended June 30	
	2017	2016
	(in Thousands)	
Impairment charges	$ 917	$ 111,154
Changes in business operations	118,985	39,931
Severance costs	31,420	18,741
Pension settlement costs	39,678	27,263
Total restructuring, impairment and other losses	$ 191,000	$ 197,089
Non-cash restructuring, impairment and other losses	$104,400	$138,800

Restructuring, impairment, and other losses include charges relating to changes in business operations, severance costs, EPIC go-live support costs and goodwill impairments, acquisition-related costs, and pension settlement activity. Changes in business operations include costs incurred periodically to implement reorganization efforts within specific operations, in order to align CHI's operations in the most strategic and cost-effective manner. The non-cash portion of total restructuring, impairment and other losses relates primarily to impairment charges, project cost abandonment charges in changes in business operations, and pension settlement costs.

Non-Operating Results

	Three Months Ended June 30	
	2017	2016
	($ in thousands)	
Investment gains, net	$ 188,213	$ 115,994
(Losses) gains on defeasance of bonds	(3,402)	92
Realized and unrealized losses on interest rate swaps	(13,444)	(43,447)
Other nonoperating gains	919	4,735
Total nonoperating gains	$ 172,286	$ 77,374

2. SUMMARY OF OPERATING RESULTS FOR FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

OPERATING EBIDA/INCOME FROM OPERATIONS

Operating EBIDA before restructuring, impairment and other losses totaled $930.7 million and $1.0 billion for the fiscal years ended June 30, 2017 and 2016, respectively, equivalent to an operating EBIDA margin before restructuring, impairment and other losses percentage of 6.0% and 6.8%, respectively. Excluding the following transactional gains and other items, CHI operating EBIDA before restructuring, impairment and other losses totaled $810.7 million and $696.2 million for the fiscal years ended June 30, 2017 and 2016, respectively, equivalent to an operating EBIDA margin before restructuring, impairment and other losses percentage of 5.3% and 4.7%, respectively.

	Twelve Months Ended June 30,		
$ in millions	**2017**	**2016**	**Change**
Operating EBIDA before restructuring, impairment and other losses, excluding transactional gains and other items	$810.7	$696.2	$114.5
Operating EBIDA margin before restructuring, impairment and other losses, adjusted	5.3%	4.7%	0.6%
Business combination gains	-	223.0	
Gain on sale of lab operations	40.2	-	
Net gain on ambulatory sale	85.7	-	
Iowa equity gain	-	89.1	
Gains on real estate sales	22.1	59.4	
Net patient service revenue adjustments	(28.0)	(31.4)	
Operating EBIDA before restructuring, impairment and other losses	$930.7	$1,036.3	$(105.6)
Operating EBIDA margin before restructuring, impairment and other losses	6.0%	6.8%	(0.8%)

The $114.5 million in improved normalized results were a result of increased net patient services revenues combined with favorable expense management as several of CHI's productivity initiatives related to expense reduction strategies began to show improvements, particularly within labor costs. As part of CHI's on-going comprehensive expense reduction strategy, focused clinical and operational initiatives across the system continue to be implemented to include targeted initiatives at the regional levels, as well as at corporate services.

Total net patient services revenues, normalized to exclude the transactional gains and other net patient services revenues adjustments noted below, increased 4.3%, or $600.4 million, of which $257.8 million was due to recently completed acquisitions, whereas total operating expenses increased by 3.2%, or $490.3 million, of which $284.1 million was due to recently completed acquisitions.

CHI loss from operations before restructuring, impairment and other losses totaled $(211.1) million and $(78.7) million for the fiscal years ended June 30, 2017 and 2016, respectively, or an operating loss margin before restructuring, impairment and other losses percentage of (1.4)% and (0.5)%, respectively.

The strategic affiliations completed in fiscal years 2017 and 2016 contributed total operating revenues of $607.8 million and $338.6 million; operating EBIDA before restructuring, impairment and other losses of $11.5 million and $14.2 million; and a loss from operations before restructuring, impairment and other losses of $(23.6) million and $(8.6) million, for the fiscal years ended June 30, 2017 and 2016, respectively, excluding business combination gains in fiscal year 2016.

The table below presents total operating EBIDA before restructuring, impairment and other losses, total operating EBIDA margin before restructuring,

impairment and other losses, and total operating revenues of CHI by region for the fiscal years ended June 30, 2017 and 2016. Further information on CHI's regional operating results is discussed within the regional operating trends section below.

Catholic Health Initiatives Operations Summary Fiscal Years Ended – June 30, 2017 and 2016

Region	6/30/2017 Operating EBIDA before restructuring, Impairment and other losses	6/30/2016 Operating EBIDA before restructuring, Impairment and other losses	6/30/2017 Operating EBIDA margin before restructuring, Impairment and other losses	6/30/2016 Operating EBIDA margin before restructuring, Impairment and other losses	6/30/2017 Operating revenues percentage of CHI consolidated	6/30/2016 Operating revenues percentage of CHI consolidated
	(in Thousands)					
Pacific Northwest[1]	$ 369,519	$ 207,740	13.4%	8.4%	17.8%	16.4%
Colorado	275,949	231,021	11.7%	10.5%	15.1%	14.5%
Texas	64,332	119,064	3.0%	5.8%	13.9%	13.5%
Nebraska	106,715	184,037	5.3%	9.1%	13.1%	13.3%
Kentucky	115,578	167,914	7.1%	10.5%	10.4%	10.5%
Ohio	89,551	85,054	7.8%	7.8%	7.4%	7.2%
Iowa[2]	62,561	176,822	6.1%	16.1%	6.5%	7.2%
Arkansas	10,885	30,196	1.4%	4.0%	4.9%	5.0%
North Dakota/Minnesota	38,420	71,835	5.1%	9.3%	4.8%	5.1%
Tennessee	59,239	30,592	9.0%	4.9%	4.2%	4.1%
National business lines[3]	28,201	13,049	9.9%	5.1%	1.8%	1.7%
Other[4]	(35,054)	(55,930)	N/A	N/A	(0.1)%	(0.2)%
Total Regional	1,185,896	1,261,394	7.6%	8.5%	99.8%	98.3%
Corporate services and other business lines[5]	(255,209)	(448,108)	N/A	N/A	0.2%	0.2%
Business combination gains	-	223,036	N/A	N/A	0.0%	1.5%
Total CHI Consolidated	$ 930,687	$ 1,036,322	6.0%	6.8%	100.0%	100.0%

[1] Includes $85.7 million net favorable results in the current fiscal year primarily from the sale of certain outpatient ambulatory business lines.
[2] Includes an $89.1 million equity gain in the prior fiscal year as a result of the Wheaton Franciscan Healthcare-Iowa acquisition.
[3] Includes Home Care and Senior Living business lines.
[4] Includes the operations of Albuquerque Health Ministries and Lancaster Health Ministries MBOs as well as regional eliminations.
[5] Includes CHI Corporate and FIIL, as well as CHI system eliminations.

OPERATING REVENUE AND VOLUME TRENDS

CHI total operating and net patient service revenue changes are summarized below. Normalized amounts have been adjusted to exclude transactional gains and other items as noted above:

Twelve months ended June 30, 2017 compared to twelve months ended June 30,2016		
Revenue	Change	Percent Change
Operating revenue	$357.9 million	2.4%
Operating revenue normalized	$562.0 million	3.8%
Net patient service revenue	$603.8 million	4.4%
Net patient service revenue normalized	$600.4 million	4.3%
Operating revenue due to new acquisitions	$269.2 million	-
Net patient service revenue due to new acquisitions	$257.8 million	-

Also impacting net patient services revenues were increased patient volumes of $105.5 million, revenue cycle improvements and higher acuity of $259.9 million offset by unfavorable shifts in payer mix of $(76.0) million.

Excluding the impacts of current and prior year acquisitions (same store basis), same store patient volumes increases (decreases) were as follows for the fiscal year ended June 30, 2017, as compared to the corresponding period of the prior fiscal year.

Twelve months ended June 30, 2017 compared to twelve months ended June 30,2016		
Patient Volumes	Percentage Change	Volume Change
Adjusted Admissions	1.4%	14,688
Acute Admissions	(0.4)%	(2,053)
Acute Inpatient Days	(2.1)%	(49,755)
Inpatient ER Visits	0.3%	667
Inpatient Surgeries	(1.7)%	(2,563)
Outpatient ER Visits	(2.1)%	(38,660)
Outpatient Non-ER Visits	1.4%	71,883
Outpatient Surgeries	5.2%	11,983
Physician Visits	6.6%	628,823

Other Operating Revenue - Total other operating revenues, normalized to exclude the transactional gains and other items noted above, decreased (4.0)%, or $(38.5) million for the fiscal year ended June 30, 2017 compared to the prior fiscal year, primarily as a result of meaningful use revenue reductions of $(40.1) million.

OPERATING EXPENSES

Total operating expenses before restructuring, impairment and other losses are summarized below:

Twelve months ended June 30, 2017 compared to twelve months ended June 30,2016		
Expense	Increase (Decrease)	Percent Change
Total operating expense	$490.3 million	3.2%
Total operating expense – same store	$206.2 million	1.4%
Total labor expense – same store	$61.5 million	0.9%
Supply expense – same store	$6.1 million	0.2%
Medical Pro Fees – same store	$59.8 million	14.3%
Purchased Service – same store	$68.7 million	4.1%

Labor and Productivity indicators are summarized as follows:

	Twelve Months Ended June 30, 2017	Twelve Months Ended June 30, 2016
Labor % of Net patient service revenue – same store	51.8%	52.7%
Labor % of total operating expense – same store	47.5%	47.8%
Supplies % of net patient service revenue – same store	17.6%	18.0%

Same store total operating expenses before restructuring, impairment and other losses increased 1.4%, or $206.2 million, for the fiscal year ended June 30, 2017, as compared to the corresponding period of the prior fiscal year, primarily due to increases in total labor costs, purchased services and medical professional fees, as a result of annual inflation increases and strategic initiatives across CHI as described in more detail below.

Same store total labor costs increased 0.9%, or $61.5 million, for the fiscal year ended June 30, 2017, as compared to the corresponding period of the prior fiscal year, due to $84.2 million of annual inflation and merit increases (1.2)%, offset by $(22.7) million in decreased FTEs as a result of labor productivity improvements. CHI same store total labor costs represented 47.5% and 47.8% of same store total operating expenses for the fiscal year ended June 30, 2017 and 2016, respectively. CHI same store total labor costs as a percentage of net patient services revenues decreased to 51.8% for the fiscal year ended June 30, 2017, compared to 52.7% for the corresponding period of the prior fiscal year. CHI continues to address labor productivity within the regions, as well as monitoring growth initiatives in certain physician practices where labor costs and medical professional fees have been added in anticipation of future increased patient volumes. CHI is currently implementing several ongoing labor productivity improvement initiatives throughout CHI, with a particular focus on the Kentucky and Texas regions.

Same store supplies expense increased 0.2% or $6.1 million, for the fiscal year ended June 30, 2017, as compared to the corresponding period of the prior fiscal year. However, same store supplies as a percentage of net patient services revenues decreased to 17.6% for the fiscal year ended June 30, 2017, compared to 18.0% in the same period of the prior fiscal year due in part to CHI's expense management initiatives.

Same store medical professional fees increased 14.3%, or $59.8 million, for the fiscal year ended June 30, 2017, as compared to the corresponding period of the prior fiscal year, due to growth initiatives in certain physician practices where medical professional fees costs have been added in anticipation of future increased patient volumes.

Same store purchased services expenses increased 4.1% or $68.7 million, for the fiscal year ended June 30, 2017, as compared to the corresponding period of the prior fiscal year, as a result of new market implementations of revenue cycle services with Conifer during the latter part of the prior fiscal year, outsourcing and expansion of IT services, and physician alignment.

REGIONAL OPERATING TRENDS

CHI periodically reviews its allocation methodology for Corporate support services and may adjust those allocations based on the strategic needs and resource consumption of the regions and CHI overall. These changes in allocation methodologies may increase or decrease a region's operating results from year to year, but have no impact on the consolidated results.

CHI's regional operations were mixed, but several markets reported improved patient volume trends, decreased total compensation expense as a percentage of net patient services revenues and decreased supplies as a percentage of net patient services revenues.

The reduction in the Iowa region's operating EBIDA for the fiscal year ended June 30, 2017, is due primarily to the recognition in the prior fiscal year of a gain of $89.1 million within changes in equity of unconsolidated organizations as a result of the Wheaton Franciscan Healthcare-Iowa acquisition in the prior fiscal year.

The Pacific Northwest, Colorado, Texas, Nebraska and Kentucky regions represent CHI's five largest operating regions, and for the fiscal year ended June 30, 2017, represented 70.3% of CHI's consolidated operating revenues.

Pacific Northwest - the region's operating EBIDA before restructuring, impairment and other losses totaled $369.5 million for the fiscal year ended June 30, 2017, and increased $161.8 million compared to the corresponding period of the prior fiscal year. Results for the fiscal year ended June 30, 2017 included $85.7 million of net gains in the Pacific Northwest region primarily from the sale of certain outpatient ambulatory business lines and a $14.9 million gain on sale of interests in various laboratory operations. Results for the fiscal year ended June 30, 2016 included $20.3 million in gains from asset sales in the region. The remainder of the region's favorable results were due to overall increased patient volumes combined with the implementation of favorable expense management and productivity improvements. Net patient services revenues increased $204.4 million, including $88.4 million in patient volumes and $42.3 million in revenue cycle improvements and greater acuity compared to the same period of the prior fiscal year. The net patient services revenues increase exceeded the $118.0 million in increased operating expenses, compared to the corresponding period of the prior fiscal year. Total net revenue per adjusted admission increased 7.8% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 4.1%. Total labor as a percentage of net patient services revenues decreased to 51.9% compared to 54.8% in the same period of the prior fiscal year as a result of ongoing labor productivity improvements, representing a favorable expense variance of $71.9 million. Supply expense as a percentage of net patient services revenues declined to 13.8% compared to 14.5% in the prior fiscal year due to revenue growth and improved utilization.

Colorado - the region's operating EBIDA before restructuring, impairment and other losses totaled $275.9 million for the fiscal year ended June 30, 2017, and increased $44.9 million compared to the corresponding period of the prior fiscal year. Results for the fiscal year ended June 30, 2017 included a $25.3 million gain on asset sales and a net unfavorable $(32.5) million related to provider fee activity reductions in the region which resulted in $(58.7) million in net patient services revenues decreases and $(26.2) million in

decreased operating expenses. The remainder of the region's favorable results were due primarily to overall increased patient volumes. Net patient services revenues increased $122.5 million, including $21.8 million as a result of the Longmont transaction. Net patient services revenues were also impacted by increased same store patient volume increases which were offset by $(13.4) million in unfavorable shifts in payer mix, and $(58.7) million decrease in provider fee revenue. The net patient services revenues increase exceeded the $115.9 million in increased operating expenses, compared to the corresponding period of the prior fiscal year. Total net revenue per adjusted admission increased 4.7% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 4.4%. Total labor as a percentage of net patient services revenues increased to 42.5% compared to 41.6% in the same period of the prior fiscal year, representing an unfavorable expense variance of $(19.8) million.

Texas - the region's operating EBIDA before restructuring, impairment and other losses totaled $64.3 million for the fiscal year ended June 30, 2017, and decreased $(54.7) million compared to the same period of the prior fiscal year. Results for the fiscal year ended June 30, 2017 included $24.4 million in gains from asset sales in the region. The region's unfavorable results were due primarily to increased same store operating expenses, which increased 1.9%, or $38.4 million, outpacing same store net patient services revenues, which increased 0.2%, or $4.4 million, compared to the same period of the prior fiscal year. Net patient services revenues increased $108.5 million compared to the same period of the prior fiscal year, and included $104.2 million from recently completed affiliations. Net patient services revenues were also favorably impacted by Medicaid 1115 waiver reimbursement increases of $14.0 million which were offset by $(40.6) million in unfavorable shifts in payer mix. Total net revenue per adjusted admission decreased (4.6)% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission decreased (2.4)%. Total labor as a percentage of net patient services revenues increased to 48.4% compared to 48.1% in the same period of the prior fiscal year, representing an unfavorable expense variance of $(6.2) million. Management is implementing strategies to improve labor productivity, supply chain, and overall expense savings in the Texas region, and continues to expand its referral base for additional future growth in the region through acquiring and expanding the Texas physician enterprise in the greater Houston area.

Nebraska - the region's operating EBIDA before restructuring, impairment and other losses totaled $106.7 million for the fiscal year ended June 30, 2017, and decreased $(77.3) million compared to the corresponding period of the prior fiscal year. Results for the fiscal year ended June 30, 2017 included $(28.0) million of unfavorable net patient services revenues adjustments, and results for the fiscal year ended June 30, 2016 included $25.0 million in gains from asset sales in the region. The net patient services revenues adjustments were due to moving the accounts receivable reserve methodology for one facility to the CHI standard, revenue realization adjustments and to reflect more current collection experience including a reduction in recoveries. Net patient services revenues were also favorably impacted by volume growth of $45.9 million, favorable increases in acuity of $20.3 million and unfavorable shifts in payer mix of $(13.6) million. Total net revenue per adjusted admission decreased (1.3)% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 0.7%. Total operating expenses increased 3.6%, or $70.8 million in the region for the fiscal year ended June 30, 2017, primarily in the areas of total compensation, purchased services and supplies expenses, compared to the corresponding period of the prior fiscal year. Total labor as a percentage of net patient services revenues was 56.5% in both the current and prior fiscal years. Supply expense as a percentage of net patient service revenues increased to 16.8% compared to 15.8% in the prior fiscal year. Increases in utilization and cost are concentrated in pharmacy, cardiovascular and orthopedic/spine, and is a continued focus and opportunity for reduction.

Kentucky – the region's operating EBIDA before restructuring, impairment and other losses totaled $115.6 million for the fiscal year ended June 30, 2017, and decreased $(52.3) million compared to the corresponding period of the prior fiscal year. Results for the fiscal year ended June 30, 2017 included a $6.2 million gain on sale of interest in various laboratory operations, and results for the fiscal year ended June 30, 2016 included $7.7 million in gains from asset sales

in the region. The region's unfavorable results were due to operating expense increases of 4.4%, or $67.3 million, outpacing net patient services revenues increases of 1.2%, or $17.3 million, compared to the same period of the prior fiscal year. Net patient services revenues included unfavorable shifts in payer mix $(13.0) million, acuity $(10.5) million and service mix $(7.5) million, offset by rate improvements due to revenue cycle improvements. Total net revenue per adjusted admission decreased (2.1)% compared to the same period of the prior fiscal year, while total operating expense per adjusted admission increased 1.1%. Total labor as a percentage of net patient services revenues increased to 43.4% compared to 40.6% in the same period of the prior fiscal year, representing an unfavorable expense variance of $(42.0) million. The region is continuing its efforts to address nursing and other staff shortages which have resulted in increases to overall labor costs, including contract labor costs, overtime and premium pay.

CHI Corporate services and other business lines - operating EBIDA before restructuring, impairment and other losses totaled $(255.2) million, and improved $192.9 million for the fiscal year ended June 30, 2017, compared to the corresponding period of the prior fiscal year. Changes in support services activities relate to a variety of factors, and include strategic transfers of certain activities from the regions and other service lines to Corporate services in order to build Corporate support functions, and new implementations of system-wide services such as revenue cycle and food programs. Support services allocations to the regions consider the strategic needs and resource consumption of the regions and CHI overall. Expense increases for the fiscal year ended June 30, 2017 include $50.5 million of revenue cycle implementations and services for new facilities, and $16.3 million related to new facilities implementations for national food services. IT expenses decreased $(40.7) million compared to the corresponding period of the prior fiscal year due to reduced system implementation activity, and regional compensation decreased $(18.4) million due to personnel transfers of regional executive leaders from Corporate services to the regions. The operations of the self-insurance plans also improved $25.3 million due to favorable claims experience and pension operating expenses decreased $(14.2) million as a result of actuarial changes impacting the net periodic pension costs for the fiscal year ended June 30, 2017 compared to the corresponding period of the prior fiscal year.

RESTRUCTURING, IMPAIRMENT AND OTHER LOSSES

	Fiscal Year Ended June 30 ,	
	2017	2016
	($ in thousands)	
Impairment charges	$ 48,356	$ 111,188
Changes in business operations	207,539	115,809
Severance costs	78,594	40,708
Pension settlement costs	39,678	25,053
Total restructuring, impairment and other losses	$ 374,167	$ 292,758
Non-cash restructuring, impairment and other losses	$ 150,100	$ 169,000

Restructuring, impairment, and other losses include charges relating to changes in business operations, severance costs, EPIC go-live support costs, goodwill impairments, acquisition-related costs, and pension settlement activity. Changes in business operations include costs incurred periodically to implement reorganization efforts within specific operations, in order to align CHI's operations in the most strategic and cost-effective manner. The non-cash portion of total restructuring, impairment and other losses relates primarily to impairment charges, project cost abandonment charges included in changes in business operations, and pension settlement costs.

NON-OPERATING RESULTS

	Fiscal Year Ended June 30 ,	
	2017	2016
	($ in thousands)	
Investment gains (losses), net	$ 638,519	$ (3,384)
Losses on defeasance of bonds	(19,586)	(29,469)
Realized and unrealized gains (losses) on interest rate swaps	92,698	(154,816)
Other nonoperating gains (losses)	2,006	(16,491)
Total nonoperating gains (losses)	$ 713,637	$ (204,160)

3. SUMMARY OF CHI BALANCE SHEETS AS OF JUNE 30, 2017 AND 2016

Total assets were $21.9 billion and $22.7 billion at June 30, 2017 and 2016, respectively, representing a decrease of (3.2)%, or $(727.4) million, during the fiscal year ended June 30, 2017. The decrease was primarily attributable to a $(464.7) million reduction in net property and equipment balances, a result of decreased capital spending across the regions and of real estate asset sales in the current fiscal year.

Total cash and equivalents, and unrestricted investments were $6.6 billion at both June 30, 2017 and 2016, representing a decrease of (0.6)%, or $(36.7) million during the fiscal year ended June 30, 2017. For the fiscal year ended June 30, 2017, CHI spent a net $(106.5) million in investing cash flow activities, including $(705.1) million of on-going capital investment activity, offset by the receipt of $597.4 million in proceeds from asset sales. CHI capital investment activity includes maintenance costs for CHI OneCare program and IT infrastructure investments, as well as new hospital construction and facility renovations across the regions. CHI financing cash flow activities for the fiscal year ended June 30, 2017, totaled $(313.9) million and include net debt, interest and net swap collateral receipts. CHI cash flows from operations, including investments and assets limited to use, and working capital changes, were $383.7 million for the fiscal year ended June 30, 2017.

Days of cash on hand decreased to 162 days at June 30, 2017, from 168 at June 30, 2016. This decrease is primarily attributable to increases in operating expenses during the current reported fiscal year, whereas overall total cash and investment balances in both periods remained fairly constant. For each respective fiscal year, one day of operating expenses utilized in the days of cash on hand calculation represented $40.9 million and $39.4 million at June 30, 2017 and June 30, 2016, respectively.

Net patient accounts receivable were $2.2 billion at both June 30, 2017 and 2016, representing a decrease of (0.3)%, or $(7.0) million, during the fiscal year ended June 30, 2017.

Total liabilities were $14.2 billion and $15.2 billion at June 30, 2017 and 2016, respectively, representing a decrease of (6.6)%, or $(1.0) billion, during the fiscal year ended June 30, 2017, including a $(424.9) million decrease in pension liability balances, a $(343.2) million decrease in outstanding debt balance, a $(128.9) million decrease in accounts payable and accrued expenses as a result of working capital changes, and a $(110.0) million decrease in other current and long-term liabilities.

The unfunded pension benefit obligation, reported as long term liabilities, was $1.1 billion and $1.5 billion at June 30, 2017 and 2016, respectively, representing a $(424.9) million decrease. The pension benefit obligation decreased during the fiscal year ended June 30, 2017 due to favorable actuarial assumption changes, including a reduction of $(146.3) million as a result of the increase in the discount rate assumption, and a $(106.8) million reduction relating to other actuarial assumptions, including expected future returns on plan assets, form of payment, demographic and other plan assumptions changes. Pension plan assets increased $171.8 million during the fiscal year ended June 30, 2017, due to $360.2 million in investment income and $79.5 million in plan contributions, offset by $(267.9) million of plan distributions to participants.

CHI total debt was $8.7 billion and $9.0 billion at June 30, 2017 and 2016, respectively, representing a decrease of $(343.2) million, due to $(208.2) million in net debt redemptions and $(135.0) million in scheduled debt service payments during the fiscal year ended June 30, 2017.

CHI's debt-to-capitalization ratio decreased to 54.0% at June 30, 2017, from 55.9% at June 30, 2016, primarily as a result of the $(343.2) million reduction in CHI debt during fiscal year 2017, and a $287.7 million increase to unrestricted net assets. CHI total unrestricted net assets increased 4.0%, or $287.7 million, during the fiscal year ended June 30, 2017, due to a $336.0 million change in pension funded status, and $128.4 million in excess of revenues over expenses, offset by a $(152.9) million net loss from discontinued operations and $(23.8) million in other changes, including distributions to noncontrolling owners.

4. CERTAIN CONTRACTUAL OBLIGATIONS

CAPITAL OBLIGATION DOCUMENT

The obligations of the Corporation to pay amounts due on its commercial paper notes, revenue bonds, guarantees and certain swap agreements are evidenced by Obligations issued under the Capital Obligation Document ("COD"). Obligations also evidence the Corporation's obligations to banks that provide funds for the purchase of indebtedness tendered for purchase or subject to mandatory tender for purchase and not remarketed under the Corporation's self-liquidity program, funded loans and for general purpose revolving lines of credit.

At June 30, 2017, the Corporation's outstanding indebtedness evidenced by Obligations issued under the COD totaled $7.95 billion. Payment obligations under the COD are limited to the Obligated Group (defined in the COD), which only includes the Corporation. Certain covenants under the COD are tested based on the combination of the Obligated Group and Participants. However, holders of Obligations have no recourse to Participants or their property for payment thereof.

INDEBTEDNESS

(in Millions)	June 30, 2017	June 30, 2016
Capital Obligation Debt		
Fixed Rate Bonds[1]	$ 4,894	$ 5,121
Variable Rate Bonds[2]	508	508
Long Term Rate Bonds[3]	142	142
Direct Purchase Bonds[4]	1,002	824
Commercial Paper Notes	815	815
Short term bank loans and lines of credit	584	784
Total Capital Obligation Debt	**$ 7,945**	**$ 8,194**
Non-Capital Obligation Debt		
Other MBO Debt[5]	$ 458	$ 518
Capital Leases	169	166
Note Payable issued to Episcopal Health Foundation	134	167
Total Non-Capital Obligation Debt	**$ 761**	**$ 851**
Total CHI Debt	**$ 8,706**	**$ 9,045**

[1] Excludes unamortized original issue premium, discount and issuance costs.

[2] Includes bonds that bear interest at variable rates (currently determined weekly) and are subject to optional tender for purchase by their holders, FRNs that bear interest at variable rates (currently determined weekly and monthly), for a specified period and are subject to mandatory tender as set forth below and direct purchase debt of affiliates that is placed directly with holders, bears interest at variable rates determined monthly based upon a percentage of LIBOR or SIFMA plus a spread, and is subject to mandatory tender on certain dates.

[3] Long-term rate bonds bear interest at a fixed rate for a specified period and are subject to mandatory tender at the end of such period as set forth below.

[4] Direct purchase debt of the Corporation is placed directly with holders, bears interest at variable rates determined monthly based upon a percentage of LIBOR or SIFMA plus a spread, and is subject to mandatory tender on certain dates as set forth below. On December 2, 2016, the Corporation issued a $200 million taxable bond (the "2016A Taxable Bond") that was purchased by Morgan Stanley & Co. LLC. The proceeds from the sale of the 2016A Taxable Bond retired in full the Morgan Stanley revolving line of credit.

[5] Other debt is comprised mostly of $194.0 million of CHI St. Luke's affiliate debt, $94.9 million of Centura affiliate debt and $56.8 million of SFH affiliate debt.

The required principal payments on the total CHI long-term debt during fiscal year 2018 is approximately $618.2 million.

At June 30, 2017, the Corporation had one revolving line of credit with Mizuho Bank, LTD. ("Mizuho"), in the amount of $250 million that was fully drawn and matured on July 6, 2017. On July 6, 2017, the Corporation entered into a revolving line of credit with PNC Bank that was fully drawn on July 6, 2017, the proceeds were used to repay the $250 million revolving line of credit with Mizuho. On December 2, 2016, the Corporation issued a $200 million 2016 Taxable Bond that was purchased by Morgan Stanley & Co. LLC., and the proceeds of which were used to prepay a line of credit with an affiliate of Morgan Stanley. The 2016 Taxable Bond matures December 1, 2021, but may be tendered to the Corporation for purchase on December 1, 2017. On February 10, 2016, the Corporation borrowed $333.7 million from JPMorgan Chase Bank, National Association to provide for the defeasance of certain fixed rate bonds (the "JPMorgan Loan"). This loan matures on December 20, 2017, unless the parties mutually agree to renew or extend.

A. Direct Purchase Debt

The Corporation's direct purchase debt is subject to mandatory tender on the dates set forth below. Prior to the mandatory tender of direct purchase debt, management expects that it would analyze the then current market conditions and availability and relative cost of refinancing or restructuring alternatives which could include without limitation, conversion to another interest mode, refinancing or repayment.

Series	Par Outstanding June 30, 2017	Mandatory Tender Date
Providence Series 2009A[1]	$6.8 million	October 1, 2017
Providence Series 2009B[1]	5.9 million	October 1, 2017
Providence Series 2009C[1]	4.2 million	October 1, 2017
Taxable 2016	200.0 million	December 1, 2017
Colorado 2011C[2]	118.0 million	November 10, 2018
Washington 2008A[2]	119.5 million	January 29, 2019
Colorado 2004B6[2]	54.2 million	September 15, 2020
Taxable 2013F	75.0 million	December 18, 2020
Colorado 2015-1	36.7 million	August 1, 2021
Colorado 2015-2	63.5 million	August 1, 2021
Colorado 2013C	100.0 million	December 18, 2023
Taxable 2013E	125.0 million	December 18, 2023
Colorado 2015A	18.6 million	August 1, 2024
Colorado 2015B	27.3 million	August 1, 2024
Washington 2015A	47.5 million	August 1, 2024
Total Direct Purchase Bonds	**$1,002 million**	

[1] Bond holder has given notice that they will not elect to tender bonds on October 1, 2017, and will provide a 364 day extension.
[2] Includes a "term out" provision that varies among agreements, which permits repayment after the mandatory tender date absent any defaults or events of default.

The Corporation's direct purchase agreements are publicly available, and can be accessed through the Digital Assurance Certification LLC website ("DAC") at www.dacbond.com and the Municipal Securities Rulemaking Board ("MSRB") through the Electronic Municipal Market Access ("EMMA") website of the MSRB, which can be found at http://emma.msrb.org.

B. Long-Term Rate Bonds

The Corporation's long-term rate bonds are subject to mandatory tender on the dates set forth below. Prior to the mandatory tender of long-term rate bonds, management expects that it would analyze the then current market conditions and availability and relative cost of refinancing or restructuring alternatives, which could include without limitation, conversion to another interest mode, refinancing or repayment.

Series *$in millions*	Par Outstanding June 30, 2017	Mandatory Tender Date
CO 2009B-3	$40.0	Nov 6, 2019
KY 2009B	60.0	Nov 10, 2021
CO 2008D-3	41.9	Nov 12, 2021
Total Long-Term Rate Bonds	**$141.9**	

C. Floating Rate Notes ("FRNs")

The Corporation's FRNs are subject to mandatory tender on the dates set forth below. Prior to the mandatory tender of the FRNs, management expects that it would analyze the then current market conditions and availability and relative cost of refinancing or restructuring alternatives, which could include without limitation, conversion to another interest mode, refinancing or repayment.

Series *$in millions*	Par Outstanding June 30, 2017	Mandatory Tender Date
KY 2011B-1	$ 52.7	Jan 31, 2020
KY 2011B-2	52.7	Jan 31, 2020
CO 2008C-2	26.5	Nov 12, 2020
CO 2008C-4	26.5	Nov 12, 2020
WA 2013B-1	100.0	Dec 31, 2020
WA 2013B-2	100.0	Dec 31, 2024
KY 2011B-3	52.7	Jan 31, 2025
Total FRNs	**$411.1**	

D. Variable Rate Bonds

The Corporation's variable rate demand bonds are subject to optional and mandatory tender. As of June 30, 2017, variable rate demand bonds are outstanding in the amount of $96.7 million, supported by the Corporation's self-liquidity, not by a dedicated liquidity or credit facility. See *Part VII: 5. Liquidity and Capital Resources - Liquidity Arrangements*.

E. Taxable Commercial Paper

The Corporation's commercial paper note program permits the issuance of up to $881 million in aggregate principal amount outstanding, with maturities limited to 270 day periods. The Corporation has directed the commercial paper dealers to tranche the commercial paper maturities so that no greater than approximately one-third of the outstanding balance matures in any one month, and no more than $100 million matures per dealer within any five business-day period while the outstanding balance of the commercial paper is greater than $500 million. The Corporation has, from time to time, directed its dealers to deviate from such directions, and may do so again in the future. As of June 30, 2017, $815.5 million of commercial paper notes were outstanding. The commercial paper notes are supported by the Corporation's self-liquidity, and are not supported by a dedicated liquidity or credit facility. See *Part VII: 5. Liquidity and Capital Resources - Liquidity Arrangements*.

F. Swap Agreements

The Corporation or its affiliates are currently party to 41 swap transactions that had an aggregate notional amount of approximately $1.6 billion at June 30, 2017. The 41 transactions have varying termination dates ranging from 2017 to 2047. The swap agreements require the Corporation (or with respect to certain swap agreements, affiliates of the corporation) to provide collateral if its respective liability, determined on a mark-to-market basis, exceeds a specified threshold that varies based upon the rating on the Corporation's long-term indebtedness. The swap agreements of Memorial East Texas and Centura Health do not require collateral postings. The fair value of the swaps is estimated based on the present value sum of anticipated future net cash settlements until the swaps'

maturities. Cash collateral balances are netted against the fair value of the swaps, and the net amount is reflected in other liabilities in the accompanying consolidated balance sheets. At June 30, 2017, the net swap liability reflected in other liabilities was $28.9 million, net of swap collateral posted of $259.1 million. The swap agreements, excluding the Centura Health swap, are secured by Obligations issued under the COD. *(See Note 9 in the Consolidated Financial Statements (Audited) as of June 30, 2017 and 2016.)*

Obligated Party	Type	Outstanding Notional June 30, 2017	Termination Date
CHI[1]	Total Return	$ 90.9 million	September 5, 2017-January 16, 2020
CHI	Fixed Payer	150.9 million	May 1, 2025
CHI	Fixed Payer	235.4 million	March 1, 2032
CHI	Fixed Payer	98.8 million	September 1, 2036
CHI	Fixed Payer	128.5 million	September 1, 2036
CHI	Fixed Payer	19.8 million	September 1, 2036
CHI	Fixed Payer	99.4 million	December 1, 2036
CHI	Fixed Payer	149.1 million	December 1, 2036
CHI St. Luke's	Fixed Payer	124.4 million	February 18, 2031
CHI St. Luke's	Fixed Payer	101.1 million	February 15, 2032
CHI St. Luke's	Fixed Payer	100.0 million	February 15, 2047
CHI St. Luke's	Fixed Payer	100.0 million	February 15, 2047
Centura Health[2]	Fixed Payer	15.3 million	May 20, 2024
Madonna Manor	Total Return	27.5 million	August 15, 2020
Memorial East Texas	Fixed Payer	25.2 million	February 15, 2035
Memorial East Texas	Fixed Payer	17.8 million	February 15, 2028
St. Joseph Regional Health[3]	Total Return	56.4 million	April 4, 2018 - August 15, 2020
St. Joseph Regional Health	Fixed Payer	45.6 million	January 1, 2028
St. Joseph Regional Health	Basis	30.0 million	March 1, 2028
Total Notional Amount		**$1,616.0 million**	

[1]Represents 19 Total Return Swaps.
[2] Not secured by CHI COD obligations.
[3] Represents 5 Total Return Swaps.

5. LIQUIDITY AND CAPITAL RESOURCES

Cash Equivalents and Internally Designated Investments

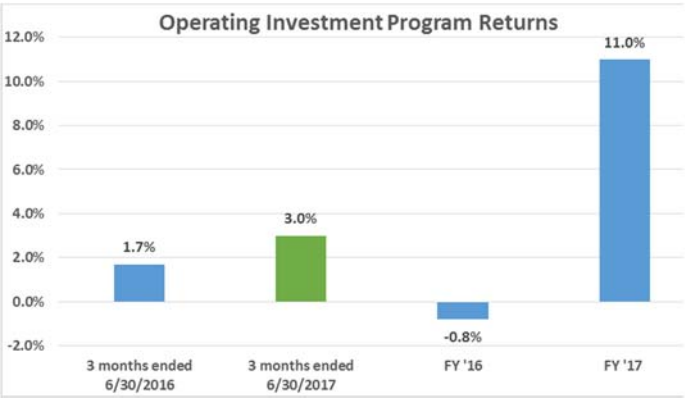
CHI holds highly liquid investments to enhance its ability to satisfy liquidity needs. Asset allocations are reviewed on a monthly basis and compared to investment allocation targets included within CHI's investment policy. At June 30, 2017 and June 30, 2016, CHI had cash and equivalents and internally designated investments (including net unrealized gains and losses) as described in the table below.

($ in thousands)	June 30, 2017	June 30, 2016
Cash and equivalents	$ 1,033,166	$ 1,305,242
Internally designated investments	5,574,188	5,338,803
Total	**$ 6,607,354**	**$ 6,644,045**

CHI maintains an Operating Investment Program (the "Program") administered by the Corporation. The Program is structured as a limited partnership with the Corporation as the managing general partner.

The Program contracts with investment advisers to manage the investments within the Program. Substantially all CHI long-term investments are held in the Program. The Corporation requires all Participants to invest in the Program. The Program consists of equity securities, fixed-income securities and alternative investments (e.g., private equity, hedge funds and real estate interests). The asset allocation is established by the Finance Committee of the Board of Stewardship Trustees. At June 30, 2017, the asset

allocation for the Program's Long-Term Pool was 45% equity securities, 30% fixed-income securities, 25% alternative investments, and 0% cash and equivalents. Alternative investments within the Program have limited liquidity. As of June 30, 2017, illiquid investments not available for redemption totaled $378.9 million, and investments available for redemption within 180 days at the request of the Program totaled $813.2 million. The asset allocation for the Program's Intermediate Pool was 100% fixed-income securities. As of June 30, 2017, 90.2% of the Program's assets were invested in the Long-Term Pool, with 9.8% of assets invested in the Intermediate Pool. The Program's return was 11.0% for the fiscal year ended June 30, 2017.



LIQUIDITY ARRANGEMENTS

The Corporation maintains several liquidity facilities that are dedicated to funding optional or mandatory tenders of its variable rate debt and paying the maturing principal of the commercial paper notes in the event remarketing proceeds are unavailable for such purpose. At June 30, 2017, no amounts were drawn on these lines. The Corporation's dedicated self-liquidity lines are set forth below and can be found at http://emma.msrb.org.

CHI Dedicated Self-Liquidity Lines – June 30, 2017

Bank *($ in millions)*	Committed Amount	Expiration
Bank of New York Mellon	$ 60.0	June 30, 2017[1]
PNC Bank	125.0	Aug 24, 2017[2]
J.P. Morgan	50.0	Sept 30, 2017[3]
Bank of New York Mellon	50.0	Dec 15, 2017
MUFG Union Bank	75.0	Sept 28, 2018
Northern Trust	65.0	June 28, 2019
Total Self-Liquidity Lines	**$ 425.0**	

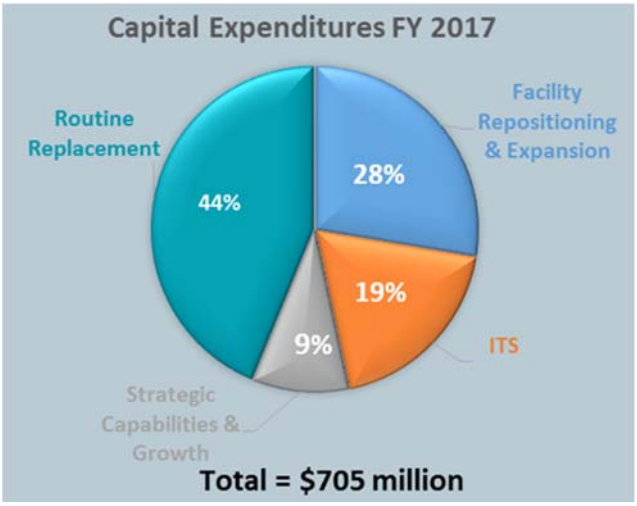
[1] The line of credit was not renewed on June 30, 2017. Total committed amount at the time of this report is $365 million.
[2] This line of credit was renewed to a new expiration date of August 24, 2017
[3] This line of credit was renewed to a September 30, 2017

6. LIQUIDITY REPORT

CHI posts a liquidity report monthly, which can be found at www.catholichealth.net and http://emma.msrb.org.

7. CAPITAL EXPENDITURES

The chart below reflects capital allocations for fiscal year 2017 to information technology ("ITS"), strategic capabilities and growth, facility repositioning and expansion, as well as routine replacement of capital assets.



CHI's capital budget for fiscal year 2018 is $835 million with ability to increase or decrease based on performance with a not to exceed amount of $960 million.

Information Technology

CHI has implemented an information technology program known as "OneCare". The OneCare program is designed to improve patient safety, clinical outcomes and care coordination; enhance patient experiences; provide clinicians and staff with necessary tools and information; and eliminate duplication and waste. The OneCare program includes a shared, electronic health record for each CHI patient. CHI began an implementation schedule for electronic health records beginning in 2010. The implementation for CHI's wholly-owned hospital facilities and physician practices was completed at June 30, 2016, but as shown above, a significant portion of CHI's spending continues for

information technology services for ongoing maintenance and support, as well as program implementation in recently acquired facilities. The total investment in the OneCare program is approximately $2.4 billion ($1.6 billion in capital expenses and $0.8 billion in operating expenses). Ongoing annual maintenance costs to support the OneCare program are expected to be approximately $185 million in operating expenses. CHI has a stated goal to drive overall IT costs to best in class with regards to operating expense and capital investment.

8. COVENANT COMPLIANCE

The following table presents the Historical Long-Term Debt Service Coverage Ratio for CHI for fiscal years ended June 30, 2017 and 2016.

CHI Historical Long-Term Debt Service Coverage

	June 30, 2017	June 30, 2016
	($ in thousands)	
Income available for debt service		
Total Revenues	$ 16,261,101	$ 14,985,427
Total Operating Expenses (includes restructuring)	16,132,711	15,560,998
Excess (Deficiency) of Revenues over Expenses	128,390	(575,571)
Add: Interest on Long-Term Indebtedness	273,948	263,994
Add: Depreciation and Amortization	846,291	833,394
Add: Non-Cash Restructuring, Impairment and Other Losses	110,453	143,977
Add: Losses on Defeasance of Bonds and Escrow	19,586	29,469
Add: Business Combination (Gains)	-	(223,036)
Add: Change in equity of unconsolidated org Gains on Business combination contribution	-	(89,095)
Add: Net periodic pension expense (income)	(9,348)	6,283
Add: Unrealized Losses (Gains) on Interest Rate Swaps	(127,866)	115,369
Add: Net Investment Unrealized Losses (Gains)	(153,537)	302,986
Total Adjustments to Excess (Deficiency) of Revenues Over Expenses	959,527	1,383,341
Total income available for debt service	**$ 1,087,917**	**$ 807,770**
Debt service requirements on Long Term Indebtedness:		
Total CHI Principal Payments	135,001	114,996
Total CHI Interest Payments	286,928	281,482
Total Debt Service Requirements on Long Term Indebtedness:	**$ 421,929**	**$ 396,478**
Historical Long-Term Debt Service Coverage Ratio	**2.6x**	**2.0x**

9. PENSION AND RETIREMENT PLAN OBLIGATIONS

CHI Pension Plan

CHI and its direct affiliates maintain a variety of noncontributory, defined benefit retirement plans (Retirement Plans) for their employees. Certain of these plans were frozen in previous fiscal years, and benefits

earned by employees through that time period remain in the Retirement Plans, where employees continue to receive interest credits and vesting credits, if applicable. Beginning January 1, 2014, CHI introduced a new 401(k) Retirement Savings Plan – see *CHI 401(k) Retirement Savings Plan* below for additional information. Vesting occurs over a five-year period. Benefits in the Retirement Plans are based on compensation, retirement age, and years of service. Substantially all of the Retirement Plans are qualified as church plans and are exempt from certain provisions of both the Employee Retirement Income Security Act of 1974 and Pension Benefit Guaranty Corporation premiums and coverage. Funding requirements are determined through consultation with independent actuaries.

CHI recognizes the funded status (the difference between the fair value of plan assets and the projected benefit obligations) of its Plans in the consolidated balance sheets, with a corresponding adjustment to net assets. Actuarial gains and losses that arise and are not recognized as net periodic pension cost in the same periods are recognized as a component of changes in net assets. CHI recognized an unfunded status for the Plans of $1.1 billion and $1.5 billion at the June 30, 2017 and 2016 measurement dates, respectively. The fair value of the Plan assets were $4.1 billion and $3.9 billion at June 30, 2017 and 2016, respectively.

During fiscal year 2016, CHI acquired the pension plan assets and liabilities of Trinity with unfunded obligations of $16.4 million.

CHI recognized net periodic pension expense (income) of $26.4 million and $17.2 million for the three months ended June 30, 2017 and 2016, respectively, and $(9.3) million and $6.3 million for the fiscal years ended June 30, 2017 and 2016, respectively. Pension income is the result of the decline in the service cost of the frozen CHI plan and lower discount assumptions in the current fiscal year The service cost, interest cost, expected return on the Plans' assets, actuarial losses, and amortization of prior service benefit components of net periodic pension expense (income) are recognized in the consolidated statements of operations within employee benefits expense. The curtailment and settlement components of net periodic pension expense (income) are recognized in the consolidated statements of operations within restructuring, impairment and other losses.

The expected return on the Plans' assets for determining pension cost was 7.2% for both fiscal years ended June 30, 2017 and 2016. The assumption for the expected return on the Plans' assets is based on historical returns and adherence to the asset allocations set forth in the Plans' investment policies.

Certain of the Plans' investments are held in the CHI Master Trust, which was established for the investment of assets of the Plans. The CHI Master Trust investment portfolio is designed to preserve principal and obtain competitive investment returns and long-term investment growth, consistent with actuarial assumptions, while minimizing unnecessary investment risk. Diversification is achieved by allocating assets to various asset classes and investment styles and by retaining multiple investment managers with complementary philosophies, styles and approaches. Although the objective of the CHI Master Trust is to maintain asset allocations close to target, temporary periods may exist where allocations are outside of the expected range due to market conditions. The use of leverage is prohibited except as specifically directed in the alternative investment allocation. The portfolio is managed on a basis consistent with the CHI social responsibility guidelines.

A summary of the CHI Master Trust asset allocation targets and allocations by asset class at the measurement dates of June 30, 2017 and 2016 are as follows:

	June 30,		
	2017	2016	Target
Equity securities	48.2%	46.0%	45.0%
Fixed-income securities	32.4%	33.9%	35.0%
Alternative investments	19.4%	20.1%	20.0%

CHI 401(k) Retirement Savings Plan

CHI sponsors the CHI 401(k) Retirement Savings Plan (401(k) Savings Plan) for its employees whereby CHI matches 100.0% of the first 1.0% of eligible pay an employee contributes to the plan, and 50.0% of the next 5.0% of eligible pay contributed to the plan, for a maximum employer matching rate of 3.5% of eligible pay. On an annual basis and regardless of whether or

not an employee participates in the 401(k) Savings Plan, CHI will also contribute 2.5% of eligible pay to an employee's 401(k) Savings Plan account. This contribution is made if an employee reaches 1,000 hours in the first year of employment, or every calendar year thereafter, and is employed on the last day of the calendar year. An employee is fully vested in the plan for employer contributions after three years of service. CHI recorded 401(k) Savings Plan expense of $57.0 million and $54.7 million for the three months ended June 30, 2017 and 2016, respectively, $229.7 million and $209.4 million for the fiscal years ended June 30, 2017 and 2016, respectively.

10. COMMUNITY BENEFIT

In accordance with its mission and values, CHI commits substantial resources to sponsor a broad range of services to the poor as well as the broader community. Community benefit to the poor includes the cost of providing services to persons who cannot afford health care due to inadequate resources and/or who are uninsured or underinsured. This type of community benefit includes the costs of traditional charity care; unpaid costs of care provided to beneficiaries of Medicaid and other indigent public programs; services such as free clinics and meal programs for which a patient is not billed or for which a nominal fee has been assessed; and cash and in-kind donations of equipment, supplies or staff time volunteered on behalf of the community. Community benefit provided to the broader community includes the costs of providing services to other populations that may not qualify as poor but may need special services and support. This type of community benefit includes the costs of services such as health promotion, education, clinics and screenings. In addition, it includes all services that are not billed or can be operated only on a deficit basis; unpaid portions of training health professionals such as medical residents, nursing students and students in allied health professions; and the unpaid portions of testing medical equipment and controlled studies of therapeutic protocols.

The cost to CHI of community benefit provided to the poor and the broader community (excluding unpaid Medicare costs) totaled $1.2 billion and $1.1 million in the fiscal years ended June 30, 2017 and 2016, respectively.

11. LONG TERM BOND RATINGS

In July 2016, Fitch Ratings affirmed its long-term rating on the Corporation's fixed rate unenhanced debt of BBB+ (negative outlook). In March 2017, Standard & Poor's Rating Service assigned a rating to the Corporation's fixed rate unenhanced debt of BBB+ (stable outlook). In March 2017, Moody's Investors Service, Inc. assigned a long-term rating to the Corporation's unenhanced debt of BBB+ (negative outlook).

12. EMPLOYEES/PROFESSIONAL STAFF

At June 30, 2017, CHI employed over 3,900 providers (including advanced practice clinicians and physicians). At June 30, 2017, CHI employed 95,968 employees. Salary levels and benefit packages for CHI employees are market competitive. Less than 10% of CHI's employees are represented by collective bargaining units.

13. ACCREDITATIONS AND LICENSES

CHI's hospital facilities, skilled nursing facilities and long-term care facilities have all of the necessary licenses to operate their facilities and necessary certifications and licenses for Medicare and Medicaid reimbursement.

14. CONFLICTS OF INTEREST

The Corporation maintains policies that require internal reporting of outside financial and fiduciary activities to protect its interests in circumstances that may result in a conflict between the personal interests of its employees and Trustees and those of CHI. Those policies put in place a general obligation for employed medical staff members, researchers, employees, and trustees to report potential conflicts of interest. In addition, on an annual basis, CHI requires all managers and above, employed medical staff members, researchers and trustees to complete a conflict of interest disclosure. A process is in place to review any potential conflicts of interest disclosed through this annual disclosure process.

PART VIII: GOVERNANCE

CATHOLIC HEALTH INITIATIVES

Participating Congregations. As of June 30, 2016, there are 13 Participating Congregations and one Partnering Congregations of CHI. CHI honors the traditions and services established by the foundresses of these congregations and continue by their participation. The Participating Congregations are: Benedictine Sisters of Mother of God Monastery, Watertown, South Dakota; Congregation of the Dominican Sisters of St. Catherine of Siena, Saratoga, CA; Franciscan Sisters of Little Falls, Minnesota; Dominican Sisters of Peace, Columbus, Ohio; Sisters of Charity of Cincinnati, Ohio; Sisters of Mercy, West Midwest Community, Omaha, Nebraska; Sisters of St. Francis of Philadelphia, Pennsylvania; Sisters of Presentation of the Blessed Virgin Mary of Fargo, North Dakota; The Congregation of the Sisters of Charity of Nazareth, Kentucky; Sisters of St. Francis of the Immaculate Heart of Mary of Hankinson, North Dakota; Sisters of the Holy Family of Nazareth, Des Plaines, Illinois; Sisters of St. Francis of Colorado Springs, Colorado; and Sisters of St. Francis of Sylvania, Ohio. All rights of the Participating Congregations as stated in the Corporation bylaws are exercised through a representative appointed by each Participating Congregation. The Partnering Congregation of CHI is – the Benedictine Sisters of Annunciation Monastery, Bismarck, North Dakota. Such rights include (1) approving any substantial change in the mission or philosophical direction of CHI; (2) approving amendments to the Corporation's articles of incorporation or bylaws affecting any provision governing the qualification, rights or responsibilities of the Participating Congregations; (3) selecting and removing without cause a person to represent the Participating Congregation in exercising the rights and duties as described in the Corporation's bylaws; (4) participating in the distribution of assets upon the dissolution of the Corporation, in accordance with the Corporation's Bylaws; (5) participating in organizational advocacy efforts; (6) encouraging members of the Participating Congregations to participate in the ministries sponsored by the Corporation; and (7) participating through their representatives in meetings held at least annually.

Board of Stewardship Trustees. The Corporation's Bylaws provide for the governance of the Corporation by a Board of Stewardship Trustees of at least nine and no more than 21 appointed Trustees one of which is an *ex officio* Trustee with voting powers. All Trustees serve regular staggered terms of three years. The Board of Stewardship Trustees has the power and the authority to supervise, control, direct and manage the property, affairs, and activities of the Corporation, to determine the policies of the Corporation, to do or cause to be done any and all things for and on behalf of the Corporation, to exercise or cause to be exercised any or all of its powers, privileges, or franchises, and to seek the effectuation of CHI's objectives and purposes.

There are currently six committees of the Board of Stewardship Trustees: the Executive Committee, the Sponsorship and Governance Committee, the Finance Committee, the Human Resources Committee, the Quality and Safety Committee and the Audit and Compliance Committee.

The Board of Stewardship Trustees currently consists of 11 elected Trustees plus the *ex officio* Trustee and meets in person five times a year. The Chief Executive Officer of the Corporation serves as the *ex officio* Trustee and is able to vote. The table below lists the current Trustees, their professional affiliations and the expiration of their terms in office.

Board of Stewardship Trustees		
Name	**Professional Affiliation**	**Term Expires June 30***
Margaret Ormond, OP	President Dominican Academy	2017
Gary Yates, MD	Partner, Strategic Consulting Press Ganey Associates, Inc	2017
Betsy (Ruth) Goodwin, OSF	Director of Sponsorship Sisters of St. Francis of Philadelphia	2017
Christopher Lowney, Chairperson	Public Speaker/Author	2018
James P. Hamill	Retired President & Chief Executive Officer Healthcare Administration	2018
Antoinette Hardy-Waller, RN, BSN, MJ	CEO The Leverage Network Inc.	2018
Geraldine "Polly" Bednash, PhD, RN, FAAN	Visiting Professor -University of Vermont College of Nursing and Health Science Adjunct Faculty - Australian Catholic University	2019
Barbara Hagedorn, SC	Volunteer Good Samaritan Free Health Center	2019
Lillian Murphy, RSM	Retired Chief Executive Officer Mercy Housing	2019
Challis Lowe	Retired Human Resources	2019
Kevin E. Lofton, FACHE Ex-officio member of the Board	Chief Executive Officer Catholic Health Initiatives	N/A

** Board Members will remain in place until a successor is appointed.*

GOVERNANCE OF PARTICIPANTS AND RELATIONSHIP WITH DESIGNATED AFFILIATE

Governance of Participants. Each Participant is governed by a Board of Directors, subject to the powers reserved to its corporate member. The corporate member or sole shareholder of each of the Participants (other than Centura Health and certain Participants that are parties to JOAs, as described immediately below) is the Corporation or a local "parent organization," the sole corporate member or sole shareholder of which is the Corporation. The Corporation as sole corporate member has the right to appoint and remove Participant board members, except as otherwise described herein.

Certain Relationship and Control Mechanisms within the Corporation. The Corporation has the right, directly or indirectly, to appoint and remove a majority of the Board of Directors of each Participant, except for certain Participants affiliated with certain JOAs. In addition, the bylaws of substantially all non-profit Participants that own and operate a substantial portion of the property of CHI and constitute a substantial portion of the revenues of CHI permit the Corporation to require such Participants to transfer assets to the Corporation to the extent necessary to accomplish CHI's goals and objectives. The bylaws of such Participants also permit the Corporation to provide for the payment of all indebtedness of the Corporation in furtherance of CHI's goals and objectives, including indebtedness secured by the Capital Obligation Document. The Corporation's Board of Stewardship Trustees also maintains other powers over the Participants, including approval of operating and capital budgets.

Joint Operating Agreements and Joint Ventures. As discussed above, the Corporation is a party to several joint ventures and JOAs. Certain of the JOAs create corporate entities or operating companies to operate health care facilities within a system or network. The Corporation shares certain reserved powers over those corporations or operating companies with the other health system or hospital corporation that is a party to the related joint operating agreement. Each JOA may contain limitations on the ability of CHI entities to transfer property to others, including transfers to CHI and to the other party to the agreement. Such limitations may limit the ability of the applicable Designated Affiliate or Participant to transfer property to CHI if so requested by CHI pursuant to the Capital Obligation Document.

PART IX: CHI LEADERSHIP

Under the leadership of the CEO, CHI has two levels of management, management at the regional level and management at the national office level. CHI operations are overseen by two Presidents who serve as President, Health System Delivery and Chief Operating Officer; and President, Enterprise Business Lines and Chief Financial Officer. The position of President, Health System Delivery and Chief Operating Officer, is currently open; that role is now being filled by an interim executive vice president for operations. Key executives lead mission, strategy, clinical services, physician enterprise, legal services and human resources. CHI's geographic regions are each led by a senior vice president of operations. CHI leverages expertise across the system in areas such as mission, human resources, marketing and communications, finance, legal services, clinical effectiveness, supply chain, information technology, insurance, risk management, and strategy and business development. Several functions have been nationalized including information technology, legal services, clinical engineering and corporate responsibility. Day-to-day operations of the local markets is the responsibility of a local executive who reports to the regional senior vice president of operations. CHI continues to evolve its operating model to include clinical leaders as it moves from a hospital-centric organization to one that provides a full continuum of care in support of the creation of healthier communities.

CHI has strong, experienced leadership teams with a solid understanding of the formation and ongoing management of partnership relationships. Short biographies of key employees are discussed below.

Kevin E. Lofton, FACHE, Chief Executive Officer. Mr. Lofton joined the Corporation in 1998 and has served in his current position since 2003. Prior to that time, he served as Executive Vice President and Chief Operating Officer of the Corporation from 1999 and as the Regional President responsible for MBOs in seven states from 1998 through 1999. Before joining the Corporation in February 1998, Mr. Lofton was the Chief Executive Officer of the UAB Hospital in Birmingham. In previous positions, Mr. Lofton served as the Chief Executive Officer of Howard University Hospital in Washington, D.C., and Chief Operating Officer at Shands Hospital in Jacksonville, Florida. Mr. Lofton served as the 2007 Chairman of the Board of the American Hospital Association and on the board and executive committee of the Catholic Health Association of the United States. Mr. Lofton received a bachelor's degree in management from Boston University and a master of health administration degree from Georgia State University. In May, 2016, Mr. Lofton received an honorary doctor of humanities in medicine from the Baylor College of Medicine.

J. Dean Swindle, President, Enterprise Business Lines and Chief Financial Officer. Mr. Swindle joined the Corporation in May 2010 and has overall responsibility for financial strategy and planning, and corporate business services, including revenue cycle, supply chain, enterprise support centers, treasury services and payer strategy and operations. In addition, Mr. Swindle leads the Corporation's enterprise business lines including home health, senior living, virtual health services, payer strategy, health plan product offerings and population health resources. Prior to joining the Corporation, Mr. Swindle served as Senior Vice President of Finance, Executive Vice President and Chief Financial Officer and most recently as President, Ambulatory Services and Chief Financial Officer with Novant Health System, Winston-Salem, North Carolina. Mr. Swindle has also served as Vice President, Financial Services, at General Health System in Baton Rouge, Louisiana. He began his career with KPMG LLP in Jackson, Mississippi. Mr. Swindle earned a master of business administration from Duke University Fuqua School of Business in Durham, North Carolina, and a bachelor of business administration degree from Millsaps College, Jackson, Mississippi. He is a member of the Health Care Financial Management Association and the American Institute of Certified Public Accountants.

Anthony Jones, FACHE, Interim Executive Vice President of Operations. Mr. Jones has been named interim Executive Vice President of Operations, effective December 5, 2016, replacing Michael T. Rowan, President, Health System Delivery and Chief Operating Officer who departed CHI effective December 31, 2016.

Mr. Jones currently serves as president and CEO of Alliance Health Partners, a health care management

and consulting company specializing in operations management, strategic planning and financial management for hospitals and health care organizations. He previously served as interim CEO for both State University of New York (SUNY), University Hospital of Brooklyn, NY, and for Tulare Healthcare District and Regional Medical Center in Tulare, CA, during financial turnarounds.

In addition, Mr. Jones has been an executive consultant with KPMG/Beacon Partners, Boston, MA, and has served as interim president and CEO for two systems in Maryland that went through financial turnarounds. Among his accomplishments are: reversing financial losses to achieve operating margins; developing and implementing a physician engagement strategy for an academic medical center; repairing and rebuilding physician relationships; implementing improvements in productivity and standardization; and improving employee satisfaction ratings. Mr. Jones is a fellow in the American College of Healthcare Executives (ACHE). He earned a master's degree in Health Administration from St. Louis University in St. Louis, MO, and a bachelor's degree in Business from Abilene Christian University in Garland, TX. He is certified in LEAN Management and Six Sigma.

Reverend Thomas R. Kopfensteiner, STD, Executive Vice President, Mission. Fr. Kopfensteiner is Executive Vice President of Mission for the Corporation. Prior to joining the Corporation, he was previously an associate professor of moral theology and chair of the Department of Theology at Fordham University, Bronx, NY. Fr. Kopfensteiner has written extensively in the area of moral theology and health care ethics. He has served as a board member and ethical consultant for several health care organizations. Fr. Kopfensteiner holds a doctorate in sacred theology from Gregorian University in Rome.

Mitch H. Melfi, Esq., Executive Vice President, Corporate Affairs and Chief Legal Officer. Mitch Melfi is the Executive Vice President for Corporate Affairs and Chief Legal Officer for Catholic Health Initiatives (CHI) in Denver Colorado. In his current role, Mr. Melfi provides oversight for Legal Services, including legal mergers and acquisitions, Enterprise Risk Management, Corporate Governance, Audit and Tax. He has also held other positions for CHI, including Senior Vice President and General Counsel, Senior Vice President and Chief Risk Officer, and as President and CEO of First Initiatives Insurance, LTD, CHI's wholly owned captive insurance company. Prior to CHI, Mr. Melfi was the Vice President for Risk/Claim Management and Associate General Counsel for the Sisters of Charity Health Care Systems, Inc. in Cincinnati, Ohio until it merged with two other Catholic health systems to form CHI. Prior to his move to Cincinnati, Mr. Melfi served on the executive management team for Children's Hospital in Columbus, Ohio, where he provided oversight for all legal operations. He has authored several publications and spoken on various legal and risk management topics for lawyers, physicians, nurses, risk managers and other allied healthcare professionals, and has provided consulting services in various areas of risk management and loss prevention.

Mr. Melfi taught at the College of Medicine at The Ohio State University and served as a guest lecturer at Capital University Law School. He serves on the board of directors of several organizations including health care systems, insurance companies and internal audit. Mr. Melfi received his B.A. from The Ohio State University and his J.D. from Capital University Law School in Columbus. Mr. Melfi taught at the College of Medicine at The Ohio State University and served as a guest lecturer at Capital University Law School. He serves on the board of directors of several organizations including health care systems, insurance companies and internal audit. Mr. Melfi received his bachelor of arts from The Ohio State University and his juris doctor from Capital University Law School in Columbus.

Paul W. Edgett, III, Executive Vice President, Chief Strategy Officer. Mr. Edgett joined one of CHI's predecessor health systems in August 1993 as Senior Vice President of Network Services, and most recently served as Executive Vice President, Growth & Business Acquisitions for CHI. In his current role, Mr. Edgett provides leadership and direction for enterprise strategic development, strategic transactions, managemnt of JOA and JV investments and formation of strategic partnerships.

Previously, Mr. Edgett was senior vice president of St. Vincent Health System, Little Rock, Arkansas. Prior to that, he was assistant vice president for Methodist Hospitals of Dallas in Dallas, Texas. He has also worked for Voluntary Hospitals of America in Irving, Texas, and for Humana, Inc. in Mt. Prospect, Illinois. Mr. Edgett

holds a bachelor of arts from Dallas Baptist University and a master of business administration from the University of Colorado.

Patricia G. Webb, Executive Vice President, Chief Administrative Officer and Chief Human Resources Officer. Ms. Webb joined the Corporation in December 2010. She has more than 30 years of experience in leading operations and human resource functions in non-union, union and multi-facility health care organizations. Prior to joining the Corporation, Ms. Webb was Senior Vice President and Chief Human Resources Officer at UMass Memorial Health Care, Worcester, MA. She has also served as human resources executive at Boston Medical Center, Boston, MA; Wake Medical Center, Raleigh, NC; and University Medical Center, Jacksonville, FL. Ms. Webb has a master's degree in business and human resources management from the University of North Florida, Jacksonville; and a bachelor's degree in management and marketing from Florida A&M University, Tallahassee. She is a Fellow in the American College of Health Care Executives and participates frequently on national forums and panels.

Kathleen Sanford, DBA, RN, CENP, FACHE, Senior Vice President and Chief Nursing Officer. Dr. Sanford joined the Corporation in 2006. She has over 40 years of experience in health care, including staff nursing, middle management, chief nurse executive, hospital administrator, and strategy executive roles. In addition to acute care leadership, she has worked in long term care; founded, initiated and managed a Medicare-certified home health agency; built and managed urgent care services; and managed employed physician office practices. A former Army Nurse, she retired as Chief Nurse of the Washington Army National Guard. She served as the 2006 President of the American Organization of Nurse Executives, and in that role, also participated in the Tri-Council for Nursing. She has served on the American Hospital Association Board in addition to multiple regional and local boards. She is currently editor-in-chief for Nursing Administration Quarterly (NAQ). As a former newspaper health care columnist and author of multiple publications, she has published many articles and the management book, "Leading with Love." Dr. Sanford co-wrote the 2015 management book on Dyad Leadership with her former Dyad Partner, the CHI Chief Medical Officer, titled, "Dyad Leadership In Healthcare: When One Plus One Is Greater Than Two." Her education includes a bachelor's degree in Nursing from the University of Maryland/Walter Reed Army Institute of Nursing, a master of arts in Human Resources Management from Pepperdine University, a master of business administration from Pacific Lutheran University, and a doctorate in business from Nova Southeastern University. She is a Fellow in the Wharton School of Business Nursing Administration Program, a Fellow of the American College of Healthcare Executives, and a Fellow of the American Academy of Nursing.

Robert J. Weil, M.D., Senior Vice President and Chief Medical Officer. Dr. Weil joined the Corporation in September 2016 and provides strategic clinical and cultural leadership to ensure the delivery of high-quality, cost-effective and patient-centered care. Among other responsibilities, Dr. Weil manages the clinical service lines, the physician enterprise and CHI's Institute for Research and Innovation ("CIRI").

Previously, Dr. Weil held several roles at Geisinger Health System, including Chief Medical Executive in Northeastern Pennsylvania, Associate Chief Scientific Officer for Clinical and Translational Research for the system, and as Medical Director of Care Support Services, Geisinger's enterprise supply chain and pharmacy division. Prior to joining Geisinger, Dr. Weil was a staff neurosurgeon at the Cleveland Clinic where he was President of Lakewood Hospital in Lakewood, Ohio, part of the Cleveland Clinic Health System. Dr. Weil graduated from Yale College, received his medical degree from the University of Missouri, and a master of business administration from Case Western Reserve University.

PART X: LEGAL PROCEEDINGS

PENDING LITIGATION/REGULATORY MATTERS

CHI operates in a highly litigious industry. As a result, various lawsuits, claims and regulatory proceedings have been instituted or asserted against it from time to time. CHI has knowledge of certain pending suits against certain of its entities that have arisen in the ordinary course of business. In the opinion of management, CHI maintains adequate insurance and/or other financial reserves to cover the estimated potential liability for damages in these cases, or, to the extent such liability is uninsured, adverse decisions will not have a material adverse effect on the financial position or operations of CHI.

General Observation Relating to Status as Health Care System. CHI, like all major health care systems, periodically may be subject to investigations or audits by federal, state and local agencies involving compliance with a variety of laws and regulations. These investigations seek to determine compliance with, among other things, laws and regulations relating to Medicare and Medicaid reimbursement, including billing practices for certain services. Violation of such laws could result in substantial monetary fines, civil and/or criminal penalties and exclusion from participation in Medicare, Medicaid or similar programs.

St. Joseph–London. Following a voluntary disclosure of compliance-related issues concerning cardiac stent cases performed at a CHI direct affiliate, St. Joseph London ("SJHS"), by a single, independent/non-employed interventional cardiologist, on January 22, 2014, SJHS entered into a settlement agreement with the federal government, the Commonwealth of Kentucky, and three relators and paid $16.5 million to resolve civil and administrative monetary claims raised in a *qui tam* lawsuit relating to certain diagnostic and therapeutic cardiac procedures performed at SJHS's facility and the financial relationship with certain cardiac physicians and physician groups. In addition, SJHS entered into a five-year corporate integrity agreement ("CIA") with the OIG that imposes certain compliance oversight obligations solely at SJHS's facility. The CIA is approaching the end of its third year.

In a separate matter, numerous civil lawsuits have been filed against the Corporation and SJHS claiming damages for alleged unnecessary cardiac stent placements and other cardiac procedures. Both CHI and SJHS are vigorously defending these lawsuits. The first case, *Edward Marshall, et al. v. Catholic Health Initiatives et al.*, Case No. 11-CI-00972, was tried to a defense verdict in favor of both CHI and SJHS. Plaintiffs agreed to dismiss the second case to be tried, *Blair Apgar and Mary Apgar, his wife v. Catholic Health Initiatives, et al.,* Case No. 12-CI-00445. CHI and SJHS were dismissed before trial from the third case to be tried, *James Davis*, part of *Anthony Adams et al. v. Catholic Health Initiatives, et al.*, Case No. 12-CI-00802, which resulted in a defense verdict in favor of the remaining defendants. The fourth case, *LeMaster v. Catholic Health Initiatives, et al.,* Case No. 12-CI-00975, which was originally scheduled for trial in April 2016, was dismissed by the court following a grant of summary judgment in favor of SJHS due to plaintiff's failure to establish a causal link between the alleged negligence and plaintiff's injuries. The fifth case, *Dolly Wathen*, also part of *Anthony Adams, et al. v. Catholic Health Initiatives, et al.,* Case No. 12-CI-00802, was dismissed by plaintiffs prior to trial. The sixth case, *Kevin Ray Wells, Sr. v. Catholic Health Initiatives, et. al.,* Case No. 12-CI-00090, was tried to verdict in August 2016. The jury found in favor of the plaintiff and awarded compensatory damages in an amount just under $1.3 million and punitive damages of $20.0 million. Post-trial motions have been filed and, while the trial court did not set aside the verdict, it did reduce the punitive damage award to $5.0 million. The rulings of the trial court are now being appealed. The *E/O Vada Owens v. Catholic Health Initiatives, et al.* Case No. 12-CI-00405 commenced trial on January 9, 2017 in the Circuit Court of Laurel County with the Honorable Judge Lay presiding. Prior to the case going to the jury, a Settlement in Principle was reached with Plaintiffs on all of the cardiac claims, including the *E/O Owens*, but excluding *Kevin Wells* which is on appeal. Management believes that adequate reserves have been established and that the outcome of the current litigation will not have a material adverse effect on the financial position or results of operations of CHI.

Pension Plan Litigation. In May 2013, the Corporation and two employees were named as defendants in a class action lawsuit under the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), challenging the "church plan" status of one of CHI's defined benefit plans. *Medina v. Catholic Health Initiatives, et. al.*, Civil No 13-1249 (District of Colorado). Subsequently, the Complaint was amended to name additional CHI-related defendants. The Complaint alleges that CHI's defined benefit plan (i) does not meet the definition of a "church plan" under ERISA; (ii) does not satisfy ERISA's minimum funding standards; (iii) violates various other provisions of ERISA applicable to covered defined benefit plans; or (iv) alternatively, if CHI's defined benefit plan qualifies for "church plan" status, the "church plan" exemption is nonetheless an unconstitutional accommodation under the Establishment Clause of the First Amendment. On December 8, 2015, the U.S. District Court for the District of Colorado entered summary judgment in favor of CHI and the individual defendants on all of plaintiff's claims, dismissing the claims with prejudice, and awarding defendants their costs. Plaintiff filed a notice of appeal on January 6, 2016. The parties have filed their initial briefs with the Tenth Circuit Court of Appeals and oral argument on the appeal was originally scheduled for January 18, 2017. However, on December 13, 2016, following certain action taken by the United States Supreme Court in other non-CHI-related "church plan" litigation (described below), the Tenth Circuit vacated the hearing and stayed the appeal. With the Supreme Court now having rendered its decision in the non-CHI-related litigation, the Tenth Circuit has rescheduled oral argument for September 7, 2017. While no assurance can be given as to the outcome of the appeal, management does not believe that this matter, if decided adversely to CHI, would have a material adverse effect on the financial position or results of operations of CHI. In other non-CHI-related "church plan" litigation (i.e., *Advocate Health Care Network v. Stapleton*, *St. Peter's Healthcare System v. Kaplan*, and *Dignity Health v. Rollins*), the Supreme Court, on December 2, 2016, granted *certiorari* on the legal question of whether only a church can establish a "church plan" within the meaning of ERISA. The Supreme Court heard oral arguments of the noted legal question on March 27, 2017. The Supreme Court rendered its decision on the question presented on June 5, 2017, finding that such plans do not have to be established by a church in order to qualify for ERISA's church plan exemption. While the Supreme Court's decision was rendered in non-CHI-related litigation, it is dispositive of one of the questions in the CHI "church plan" litigation and is a very favorable finding for CHI.

EXHIBIT A
List of Certain CHI Facilities As of June 30, 2017

State / Market	Facilities	Location	Acute Care Facility Licensed Beds	LTC Licensed Beds
Arkansas				
CHI St. Vincent				
	CHI St. Vincent Hospital Hot Springs	Hot Springs	289	
	CHI St. Vincent Infirmary	Little Rock	615	
	CHI St. Vincent Morrilton (CAH)	Morrilton	25	
	CHI St. Vincent North	Sherwood	69	
Colorado and Kansas				
Centura Health[2]				
	St. Thomas More Hospital	Canon City	55	
	Progressive Care Center	Canon City		108
	St. Francis Medical Center	Colorado Springs	195	
	Penrose Hospital	Colorado Springs	327	
	Mercy Regional Medical Center	Durango	82	
	St. Anthony Summit Medical Center	Frisco	35	
	OrthoColorado Hospital (Joint Venture)	Lakewood	48	
	St. Anthony Hospital	Lakewood	285	
	Longmont United Hospital	Longmont	201	
	St. Mary-Corwin Medical Center	Pueblo	408	
	St. Anthony North Health Campus	Westminster	100	
	St. Catherine Hospital	Garden City (Kansas)	100	
	Bob Wilson Memorial Grant County Hospital	Ulysses (Kansas)	26	
Iowa and Nebraska				
Mercy Health Network (Iowa)[3]				
	Mercy Medical Center - Centerville (CAH)	Centerville	25	20
	Mercy Medical Center	Des Moines	656	
	Skiff Medical Center	Newton	48	
	Mercy Medical Center West Lakes	West Des Moines	146	
CHI Health				
	CHI Health Mercy Corning	Corning (Iowa)	22	
	CHI Health Mercy Council Bluffs	Council Bluffs (Iowa)	278	
	CHI Health Missouri Valley	Missouri Valley (Iowa)	25	
	CHI Health St. Francis	Grand Island (Nebraska)	159	36
	CHI Health Good Samaritan	Kearney (Nebraska)	233	22
	CHI Health Richard Young Behavioral Health	Kearney (Nebraska)	61	

State / Market	Facilities[1]	Location	Acute Care Facility Licensed Beds	LTC Licensed Beds
	CHI Health Nebraska Heart	Lincoln (Nebraska)	63	
	CHI Health St. Elizabeth	Lincoln (Nebraska)	260	
	CHI Health St. Mary's (CAH)	Nebraska City (Nebraska)	18	
	CHI Health Creighton University Medical Center - Bergan Mercy	Omaha (Nebraska)	400	
	Lasting Hope Recovery Center	Omaha (Nebraska)	64	
	CHI Health Immanuel	Omaha (Nebraska)	356	
	CHI Health Creighton University Medical Center (consolidated into Bergan Mercy campus June 2017)	Omaha (Nebraska)	334	
	CHI Health Lakeside	Omaha (Nebraska)	157	
	CHI Health Midlands	Papillion (Nebraska)	148	
	CHI Health Plainview (CAH)	Plainview (Nebraska)	15	
	CHI Health Schuyler	Schuyler (Nebraska)	25	
Kentucky				
KentuckyOne Health, Inc.				
	Flaget Memorial Hospital	Bardstown	40	12
	Saint Joseph -Berea (CAH)	Berea	25	
	Saint Joseph East, including Women's Hospital at Saint Joseph East	Lexington	185	
	Saint Joseph Hospital	Lexington	408	
	Saint Joseph-London	London	150	
	Frazier Rehabilitation and Neuroscience Center[4]	Louisville	135	
	Jewish Hospital[4]	Louisville	462	
	Our Lady of Peace	Louisville	396	
	Sts. Mary & Elizabeth Hospital[4]	Louisville	298	
	University of Louisville Hospital[5]	Louisville	320	
	Saint Joseph-Martin (CAH)	Martin	25	
	Saint Joseph-Mount Sterling	Mount Sterling	42	
	Jewish Hospital Shelbyville	Shelbyville	70	
Minnesota				
CHI Lakewood Health				
	CHI Lakewood Health (Hospital) (CAH)	Baudette	15	36
CHI St. Francis Health				
	St. Francis Home	Breckenridge		80
	CHI St. Francis Health (Hospital) (CAH)	Breckenridge	25	
Unity Family Healthcare				
	CHI St. Gabriel's Health (Hospital) (CAH)	Little Falls	25	
	St. Camillus Place	Little Falls		14

State / Market	Facilities[1]	Location	Acute Care Facility Licensed Beds	LTC Licensed Beds
CHI St. Joseph's Health				
	CHI St. Joseph's Health (Hospital) (CAH)	Park Rapids	54	
North Dakota				
CHI Villa Nazareth				
	CHI Villa Nazareth	Fargo		90
CHI Lisbon Health				
	CHI Lisbon Health (Hospital) (CAH)	Lisbon	25	
CHI Oakes Hospital				
	CHI Oakes Hospital (CAH)	Oakes	20	
CHI St. Alexius Health				
	CHI St. Alexius Medical Center	Bismarck	306	
	CHI St. Alexius Turtle Lake (CAH)	Turtle Lake	25	
	CHI St. Alexius Health Garrison (CAH)	Garrison	22	28
	CHI St. Alexius Health Carrington (CAH)	Carrington	25	
	CHI St. Alexius Health Devils Lake (CAH)	Devils Lake	25	
	CHI St. Alexius Health Williston (CAH)	Williston	25	
	CHI St. Alexius Health Dickinson (Hospital) (CAH)	Dickinson	25	
CHI Mercy Health				
	CHI Mercy Health (Hospital) (CAH)	Valley City	25	
Ohio				
Premier Heath Partners				
	Good Samaritan Hospital, including the Dayton Heart & Vascular Hospital at Good Samaritan[6]	Dayton	491	
Sylvania Franciscan Health				
CHI Living Communities ***Ohio, Colorado, and Iowa***				
	Medalion Retirement Community	Colorado Springs (Colorado)		60
	Namaste Alzheimer Center	Colorado Springs (Colorado)		64
	The Gardens at St. Elizabeth	Denver (Colorado)		126
	The Villas at Sunny Acres	Thornton (Colorado		134
	Bishop Drumm Retirement Center	Johnston (Iowa)		150
	Franciscan Care Center	Sylvania		109
	Madonna Manor	Villa Hills		60
	Providence Care Center	Sandusky		138
	St. Clare Commons	Perrysburg		60
	St. Leonard	Centerville		150

State / Market	Facilities(1)	Location	Acute Care Facility Licensed Beds	LTC Licensed Beds
Trinity Health System				
	Trinity East	Steubenville	194	50
	Trinity West	Steubenville	238	
Trinity Hospital Twin City				
	Trinity Hospital Twin City (CAH)	Dennison	25	
TriHealth, Inc.				
	Good Samaritan Hospital[7]	Cincinnati	502	
Oregon				
Mercy Medical Center				
	Mercy Medical Center	Roseburg	174	
St. Anthony Hospital				
	St. Anthony Hospital (CAH)	Pendleton	49	
Tennessee				
CHI Memorial				
	Memorial Hospital	Chattanooga	336	
	Memorial Hospital-Hixson	Hixson	69	
Texas				
CHI St. Luke's Health				
	Brazosport Regional Health System	Lake Jackson	158	
	St. Luke's Hospital at The Vintage	Houston	106	
	Baylor St. Luke's Medical Center[8]	Houston	879	
	Patients Medical Center	South Pasadena	61	
	St. Luke's Sugar Land Hospital	Sugar Land	100	
	St. Luke's Lakeside Hospital	The Woodlands	30	
	St. Luke's The Woodlands Hospital	The Woodlands	236	
	CHI St. Luke's Health Springwoods Village	Spring	4	
CHI St. Luke's Health - Memorial				
	CHI St. Luke's Health Memorial Livingston	Livingston	66	
	CHI St. Luke's Health Memorial Lufkin	Lufkin	271	
	CHI St. Luke's Memorial Specialty Hospital	Lufkin		26
	CHI St. Luke's Memorial San Augustine	San Augustine	18	
CHI St. Joseph Health				
	CHI St. Joseph Health Bellville Hospital (CAH)	Bellville	**32**	
	CHI St. Joseph Health Burleson Hospital (CAH)	Caldwell	**25**	
	CHI St. Joseph Health Madison Hospital (CAH)	Madisonville	**25**	
	St. Joseph Manor	Bryan		88

State / Market	Facilities(1)	Location	Acute Care Facility Licensed Beds	LTC Licensed Beds
	CHI St. Joseph Health Regional Hospital	Bryan	235	
	CHI St. Joseph Health Grimes Hospital	Navasota	25	
Washington				
CHI Franciscan Health				
	Harrison Medical Center	Bremerton, Silverdale	347	
	Highline Medical Center	Burien	128	
	Regional Hospital for Respiratory and Complex Care	Burien	40	
	St. Anthony Hospital	Gig Harbor	80	
	St. Clare Hospital	Lakewood	106	
	St. Elizabeth Hospital (CAH)	Enumclaw	38	
	St. Francis Hospital	Federal Way	124	
	St. Joseph Medical Center	Tacoma	366	
Wisconsin				
CHI Franciscan Villa				
	CHI Franciscan Villa	South Milwaukee		150

(1) (CAH) denotes a Critical Access Hospital.

(2) These facilities operated under the Centura Health (Colorado) Joint Operating Agreement.

(3) These facilities operated under the Mercy Health Network (Iowa) Joint Operating Agreement.

(4) These facilities are part of the planned divestiture described in *Part V: Strategic Affiliations and Acquisitions-Pending and Completed Divestitures, KentuckyOne Health*

(5) This facility was transitioned as described in *Part V: Strategic Affiliations and Acquisitions-Pending and Completed Divestitures, KentuckyOne Health*

(5) Operated under the Premier Health Partners (Ohio) Joint Operating Agreement.

(6) Operated under the TriHealth Inc. (Ohio) Joint Operating Agreement

(7) This facility managed and operated under the Joint Operating Agreement with Baylor College of Medicine.

APPENDIX A

CATHOLIC HEALTH INITIATIVES

CONSOLIDATED FINANCIAL STATEMENTS

AND SUPPLEMENTAL INFORMATION

YEARS ENDED JUNE 30, 2017 AND 2016

Consolidated Financial Statements and Supplementary Information

Catholic Health Initiatives
Years Ended June 30, 2017 and 2016
With Report of Independent Auditors

Ernst & Young LLP

Building a better working world

Catholic Health Initiatives

Consolidated Financial Statements
and Supplementary Information

Years Ended June 30, 2017 and 2016

Contents

Building a better working world

Ernst & Young LLP
Suite 3300
370 17th Street
Denver, CO 80202

Tel: +1 720 931 4000
Fax: +1 720 931 4444
ey.com

Report of Independent Auditors

The Board of Stewardship Trustees
Catholic Health Initiatives

We have audited the accompanying consolidated financial statements of Catholic Health Initiatives, which comprise the consolidated balance sheets as of June 30, 2017 and 2016, and the related consolidated statements of operations, changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Building a better working world

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Catholic Health Initiatives as of June 30, 2017 and 2016, and the consolidated results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

September 15, 2017

Catholic Health Initiatives

Consolidated Balance Sheets
(In Thousands)

	June 30	
	2017	**2016**
Assets		
Current assets:		
Cash and equivalents	**$ 1,033,166**	$ 1,305,242
Net patient accounts receivable, less allowances for bad debts of $1,024,099 and $968,148 at June 30, 2017 and 2016, respectively	**2,154,248**	2,161,237
Other accounts receivable	**251,137**	274,432
Current portion of investments and assets limited as to use	**65,161**	63,146
Inventories	**302,406**	280,623
Assets held for sale	**582,344**	665,428
Prepaid and other	**153,626**	147,554
Total current assets	**4,542,088**	4,897,662
Investments and assets limited as to use:		
Internally designated for capital and other funds	**5,310,808**	4,952,065
Mission and ministry fund	**126,795**	125,166
Capital resource pool	**136,585**	261,572
Held by trustees	**76,850**	113,235
Held for insurance purposes	**876,922**	841,048
Restricted by donors	**258,511**	264,949
Total investments and assets limited as to use	**6,786,471**	6,558,035
Property and equipment, net	**8,569,313**	9,034,052
Investments in unconsolidated organizations	**1,321,453**	1,260,021
Intangible assets and goodwill, net	**473,837**	462,838
Notes receivable and other	**238,588**	446,522
Total assets	**$ 21,931,750**	$ 22,659,130

	June 30	
	2017	**2016**
Liabilities and net assets		
Current liabilities:		
Compensation and benefits	**$ 642,623**	$ 682,053
Third-party liabilities, net	**85,087**	114,065
Accounts payable and accrued expenses	**1,689,849**	1,750,402
Liabilities held for sale	**165,735**	175,239
Variable-rate debt with self-liquidity	**96,700**	96,700
Commercial paper and current portion of debt	**2,017,508**	1,768,028
Total current liabilities	**4,697,502**	4,586,487
Pension liability	**1,110,983**	1,535,840
Self-insured reserves and claims	**635,780**	646,714
Other liabilities	**1,172,549**	1,262,068
Long-term debt	**6,588,202**	7,180,925
Total liabilities	**14,205,016**	15,212,034
Net assets:		
Net assets attributable to CHI	**7,047,905**	6,704,217
Net assets attributable to noncontrolling interests	**367,483**	423,424
Unrestricted	**7,415,388**	7,127,641
Temporarily restricted	**214,250**	224,524
Permanently restricted	**97,096**	94,931
Total net assets	**7,726,734**	7,447,096
Total liabilities and net assets	**$ 21,931,750**	$ 22,659,130

See accompanying notes.

Catholic Health Initiatives

Consolidated Statements of Operations
(In Thousands)

	Year Ended June 30	
	2017	**2016**
Revenues:		
Net patient services revenues before provision for doubtful accounts	**$ 15,335,886**	$ 14,688,559
Provision for doubtful accounts	**(885,018)**	(841,532)
Net patient services revenues	**14,450,868**	13,847,027
Other operating revenues:		
Donations	**30,954**	36,983
Changes in equity of unconsolidated organizations	**48,404**	133,375
Gains on business combinations	**–**	223,036
Hospital ancillary revenues	**339,072**	351,509
Other	**678,166**	597,657
Total other operating revenues	**1,096,596**	1,342,560
Total operating revenues	**15,547,464**	15,189,587
Expenses:		
Salaries and wages	**6,294,834**	6,117,712
Employee benefits	**1,201,044**	1,182,203
Purchased services, medical professional fees, medical claims and consulting	**2,402,478**	2,232,689
Supplies	**2,550,328**	2,490,524
Utilities	**210,285**	212,732
Rentals, leases, maintenance and insurance	**901,272**	898,020
Depreciation and amortization	**846,291**	833,394
Interest	**295,476**	281,581
Other	**1,056,536**	1,019,385
Total operating expenses before restructuring, impairment and other losses	**15,758,544**	15,268,240
Loss from operations before restructuring, impairment and other losses	**(211,080)**	(78,653)
Restructuring, impairment and other losses	**374,167**	292,758
Loss from operations	**(585,247)**	(371,411)
Nonoperating gains (losses):		
Investment gains (losses), net	**638,519**	(3,384)
Losses on extinguishment of debt	**(19,586)**	(29,469)
Realized and unrealized gains (losses) on interest rate swaps	**92,698**	(154,816)
Other nonoperating gains (losses)	**2,006**	(16,491)
Total nonoperating gains (losses)	**713,637**	(204,160)
Excess (deficit) of revenues over expenses	**128,390**	(575,571)
Excess of revenues over expenses attributable to noncontrolling interest	**19,948**	25,082
Excess (deficit) of revenues over expenses attributable to CHI	**$ 108,442**	$ (600,653)

See accompanying notes.

Catholic Health Initiatives

Consolidated Statements of Changes in Net Assets
(In Thousands)

	Unrestricted Net Assets					
	Attributable to CHI	**Attributable to Noncontrolling Interests**	**Total**	**Temporarily Restricted Net Assets**	**Permanently Restricted Net Assets**	**Total Net Assets**
Balances, July 1, 2015	$ 8,150,235	$ 445,687	$ 8,595,922	$ 268,317	$ 97,776	$ 8,962,015
(Deficit) excess of revenues over expenses	(600,653)	25,082	(575,571)	–	–	(575,571)
Net loss from discontinued operations	(133,469)	(21,056)	(154,525)	–	–	(154,525)
Change in pension funded status	(768,468)	(4,877)	(773,345)	–	–	(773,345)
Temporarily and permanently restricted contributions	–	–	–	39,276	3,487	42,763
Net assets released from restriction for capital	66,487	–	66,487	(66,487)	–	–
Net assets released from restriction for operations	–	–	–	(17,912)	–	(17,912)
Investment income (losses)	423	–	423	27	(378)	72
Temporarily and permanently restricted assets from acquisitons	–	–	–	11,672	2,531	14,203
Temporarily and permanently restricted assets from dispositions	–	–	–	(5,700)	(11,373)	(17,073)
Distributions to noncontrolling owners	–	(19,669)	(19,669)	–	–	(19,669)
Noncontrolling ownership acquisitions	–	9,275	9,275	–	–	9,275
Other changes in net assets	(10,338)	(11,018)	(21,356)	(4,669)	2,888	(23,137)
Net decrease in net assets	(1,446,018)	(22,263)	(1,468,281)	(43,793)	(2,845)	(1,514,919)
Balances, June 30, 2016	6,704,217	423,424	7,127,641	224,524	94,931	7,447,096
Excess of revenues over expenses	**108,442**	**19,948**	**128,390**	**–**	**–**	**128,390**
Net loss from discontinued operations	**(134,388)**	**(18,500)**	**(152,888)**	**–**	**–**	**(152,888)**
Change in pension funded status	**335,923**	**73**	**335,996**	**–**	**–**	**335,996**
Temporarily and permanently restricted contributions	**–**	**–**	**–**	**40,754**	**2,034**	**42,788**
Net assets released from restriction for capital	**33,737**	**–**	**33,737**	**(33,737)**	**–**	**–**
Net assets released from restriction for operations	**–**	**–**	**–**	**(19,939)**	**–**	**(19,939)**
Investment (losses) income	**(423)**	**–**	**(423)**	**7,811**	**1,113**	**8,501**
Distributions to noncontrolling owners	**–**	**(28,935)**	**(28,935)**	**–**	**–**	**(28,935)**
Other changes in net assets	**397**	**(28,527)**	**(28,130)**	**(5,163)**	**(982)**	**(34,275)**
Net increase (decrease) in net assets	**343,688**	**(55,941)**	**287,747**	**(10,274)**	**2,165**	**279,638**
Balances, June 30, 2017	**$ 7,047,905**	**$ 367,483**	**$ 7,415,388**	**$ 214,250**	**$ 97,096**	**$ 7,726,734**

See accompanying notes.

Catholic Health Initiatives

Consolidated Statements of Cash Flows
(In Thousands)

	Year Ended June 30, 2017	2016
Operating activities		
Increase (decrease) in net assets	**$ 279,638**	$ (1,514,919)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities:		
Depreciation and amortization	**846,291**	833,394
Provision for bad debts	**885,018**	841,532
Changes in equity of unconsolidated organizations	**(48,404)**	(133,375)
Net gains on business combinations	**–**	(223,036)
Net gains on sales of facilities and investments in unconsolidated organizations	**(195,583)**	(244,003)
Noncash operating expenses related to restructuring, impairment and other losses	**110,453**	143,977
Losses on extinguishment of debt	**19,586**	29,469
(Increase) decrease in fair value of interest rate swaps	**(127,866)**	116,327
Noncash pension adjustments	**(345,344)**	806,373
Pension cash contributions	**(79,513)**	(19,521)
Net changes in current assets and liabilities:		
Net patient and other accounts receivable	**(850,461)**	(974,031)
Other current assets	**(27,796)**	35,815
Current liabilities	**(101,894)**	99,709
Other changes	**30,246**	107,291
Net cash used in operating activities, before net change in investments and assets limited as to use	**394,371**	(94,998)
Net (increase) decrease in investments and assets limited as to use	**(246,020)**	703,181
Net cash provided by operating activities	**148,351**	608,183
Investing activities		
Purchases of property, equipment, and other capital assets	**(705,147)**	(885,054)
Investments in unconsolidated organizations	**(106,082)**	(62,670)
Business acquisitions, net of cash acquired	**(64,432)**	(2,453)
Proceeds from asset sales	**597,434**	750,266
Distributions from investments in unconsolidated organizations	**39,696**	65,411
Loans to unconsolidated affiliates	**(3,721)**	–
Net repayments of notes receivable	**148,154**	16,575
Other changes	**(12,380)**	(12,711)
Net cash used in investing activities	**(106,478)**	(130,636)
Financing activities		
Proceeds from issuance of debt and bank loans	**240,129**	993,998
Costs associated with issuance of debt	**–**	(1,076)
Repayment of debt	**(636,114)**	(948,871)
Swap cash collateral received (posted)	**82,036**	(164,725)
Net cash used in financing activities	**(313,949)**	(120,674)
(Decrease) increase in cash and equivalents	**(272,076)**	356,873
Cash and equivalents at beginning of period	**1,305,242**	948,369
Cash and equivalents at end of period	**$ 1,033,166**	$ 1,305,242
Supplemental disclosures of noncash investing activity		
Noncash purchases of property and equipment	**$ 53,881**	$ 77,983
Supplemental disclosures of cash flow information		
Cash paid during the year for interest, including amounts capitalized	**$ 325,142**	$ 324,799

See accompanying notes.

1. Summary of Significant Accounting Policies

Organization

Catholic Health Initiatives (CHI), established in 1996, is a tax-exempt Colorado corporation and has been granted an exemption from federal income tax under Section 501(c)(3) of the Internal Revenue Code. CHI sponsors market-based organizations (MBO) and other facilities operating in 17 states and includes 101 hospitals, including four academic medical centers, and 29 critical access facilities; community health service organizations; accredited nursing colleges; home health agencies; and other facilities that span the inpatient and outpatient continuum of care. CHI also has an offshore captive insurance company, First Initiatives Insurance, Ltd. (FIIL).

The mission of CHI is to nurture the healing ministry of the Church, supported by education and research. Fidelity to the Gospel urges CHI to emphasize human dignity and social justice as CHI creates healthier communities.

Principles of Consolidation

CHI consolidates all direct affiliates in which it has sole corporate membership or ownership (Direct Affiliates) and all entities in which it has greater than 50% equity interest with commensurate control. All significant intercompany accounts and transactions are eliminated in consolidation.

Fair Value of Financial Instruments

Financial instruments consist primarily of cash and equivalents, patient accounts receivable, investments and assets limited as to use, notes receivable and accounts payable. The carrying amounts reported in the consolidated balance sheets for these items, other than investments and assets limited as to use, approximate fair value. See Note 7, *Fair Value of Assets and Liabilities,* for a discussion of the fair value of investments and assets limited as to use.

1. Summary of Significant Accounting Policies (continued)

Cash and Equivalents

Cash and equivalents include all deposits with banks and investments in interest-bearing securities with maturity dates of 90 days or less from the date of purchase. In addition, cash and equivalents include deposits in short-term funds held by professional managers. The funds generally invest in high-quality, short-term debt securities, including U.S. government securities, securities issued by domestic and foreign banks, such as certificates of deposit and bankers' acceptances, repurchase agreements, asset-backed securities, high-grade commercial paper, and corporate short-term obligations.

Net Patient Accounts Receivable and Net Patient Services Revenues

Net patient accounts receivable has been adjusted to the estimated amounts expected to be collected. These estimated amounts are subject to further adjustments upon review by third-party payors.

The provision for bad debts is based upon management's assessment of historical and expected net collections, taking into consideration historical business and economic conditions, trends in health care coverage, and other collection indicators. Management routinely assesses the adequacy of the allowances for uncollectible accounts based upon historical write-off experience by payor category. The results of these reviews are used to modify, as necessary, the provision for bad debts and to establish appropriate allowances for uncollectible net patient accounts receivable. After satisfaction of amounts due from insurance, CHI follows established guidelines for placing certain patient balances with collection agencies, subject to the terms of certain restrictions on collection efforts as determined by each facility. The provision for bad debts is presented in the consolidated statement of operations as a deduction from patient services revenues (net of contractual allowances and discounts) since CHI accepts and treats all patients without regard to the ability to pay.

During fiscal year 2016, CHI added approximately $93.3 million in net patient and other accounts receivable due to the acquisition of various new subsidiaries – see Note 4, *Acquisitions, Affiliations and Divestitures*.

1. Summary of Significant Accounting Policies (continued)

Details of CHI's allowance activity is as follows (in thousands):

	Reserve for Contractual Allowance	Allowance for Bad Debts	Reserve for Charity	Total Accounts Receivable Allowances
Balance at July 1, 2015	$ (3,712,688)	$ (903,127)	$ (304,135)	$ (4,919,950)
Additions	(34,452,201)	(841,532)	(893,974)	(36,187,707)
Reductions	34,188,433	776,511	1,019,938	35,984,882
Balance at June 30, 2016	(3,976,456)	(968,148)	(178,171)	(5,122,775)
Additions	**(36,770,178)**	**(885,018)**	**(1,078,658)**	**(38,733,854)**
Reductions	**37,061,610**	**829,067**	**1,026,052**	**38,916,729**
Balance at June 30, 2017	**$ (3,685,024)**	**$ (1,024,099)**	**$ (230,777)**	**$ (4,939,900)**

CHI records net patient services revenues in the period in which services are performed. CHI has agreements with third-party payors that provide for payments at amounts different from its established rates. The basis for payment under these agreements includes prospectively determined rates, cost reimbursement and negotiated discounts from established rates, and per diem payments.

Net patient services revenues are reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments due to future audits, reviews and investigations, and excluding estimated amounts considered uncollectible. The differences between the estimated and actual adjustments are recorded as part of net patient services revenues in future periods, as the amounts become known, or as years are no longer subject to such audits, reviews and investigations.

Investments and Assets Limited as to Use

Investments and assets limited as to use include assets set aside by CHI for future long-term purposes, including capital improvements and self-insurance. In addition, assets limited as to use include amounts held by trustees under bond indenture agreements, amounts contributed by donors with stipulated restrictions and amounts held for Mission and Ministry programs.

1. Summary of Significant Accounting Policies (continued)

CHI has designated its investment portfolio as trading as the portfolio is actively managed to achieve investment returns. Accordingly, unrealized gains and losses on marketable securities are reported within excess (deficit) of revenues over expenses. In addition, cash flows from the purchases and sales of marketable securities are reported as a component of operating activities in the accompanying consolidated statements of cash flows.

Direct investments in equity securities with readily determinable fair values and all direct investments in debt securities have been measured at fair value in the accompanying consolidated balance sheets. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in excess (deficit) of revenues over expenses unless the income or loss is restricted by donor or law.

Investments in limited partnerships and limited liability companies are recorded using the equity method of accounting (which approximates fair value as determined by the net asset values of the related unitized interests) with the related changes in value in earnings reported as investment income in the accompanying consolidated financial statements.

Inventories

Inventories, primarily consisting of pharmacy drugs, and medical and surgical supplies, are stated at lower of cost (first-in, first-out method) or market.

Assets and Liabilities Held for Sale

A long-lived asset or disposal group of assets and liabilities that is expected to be sold within one year is classified as held for sale if it meets certain criteria. For long-lived assets held for sale, an impairment charge is recorded if the carrying amount of the asset exceeds its fair value less costs to sell. Such valuations include estimates of fair values generally based upon firm offers, discounted cash flows and incremental direct costs to transact a sale (Level 2 and Level 3 inputs).

1. Summary of Significant Accounting Policies (continued)

Property and Equipment

Property and equipment are stated at historical cost or, if donated or impaired, at fair value at the date of receipt or impairment. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Buildings and improvements are depreciated over estimated useful lives of 5 to 84 years, equipment over 3 to 30 years, and land improvements over 2 to 25 years. For property and equipment under capital lease, amortization is determined over the shorter period of the lease term or the estimated useful life of the property and equipment.

Interest cost incurred during the period of construction of major capital projects is capitalized as a component of the cost of acquiring those assets. Capitalized interest of $12.9 million and $17.5 million was recorded in the years ended June 30, 2017 and 2016, respectively.

Costs incurred in the development and installation of internal-use software are expensed if they are incurred in the preliminary project stage or post-implementation stage, while certain costs are capitalized if incurred during the application development stage. Internal-use software is amortized over its expected useful life, generally between 2 and 15 years, with amortization beginning when the project is completed and the software is placed in service.

Investments in Unconsolidated Organizations

Investments in unconsolidated organizations are accounted for under the cost or equity method of accounting, as appropriate, based on the relative percentage of ownership or degree of influence over that organization. The income or loss on the equity method investments is recorded in the consolidated statements of operations as changes in equity of unconsolidated organizations.

Intangible Assets and Goodwill

Intangible assets are comprised primarily of trade names, which are amortized over the estimated useful lives ranging from 10 to 25 years using the straight-line method. The weighted average useful life of the trade names is 16 years. Amortization expense of $12.6 million and $12.8 million was recorded in the years ended June 30, 2017 and 2016, respectively.

1. Summary of Significant Accounting Policies (continued)

Goodwill is not amortized but is subject to annual impairment tests during the third quarter of the fiscal year, as well as more frequent reviews whenever circumstances indicate a possible impairment may exist; no such circumstances were identified at June 30, 2017, with the exception of the Houston MBO discussed below. Impairment testing of goodwill is done at the reporting unit level by comparing the fair value of the reporting unit's net assets against the carrying value of the reporting unit's net assets, including goodwill. Each MBO is defined as a reporting unit for purposes of impairment testing. The fair value of the reporting unit's net assets is generally estimated based on quantitative analysis of discounted cash flows (Level 3 measurement). The fair value of goodwill is determined by assigning fair values to assets and liabilities, with the remaining fair value reported as the implied fair value of goodwill.

Effective in November 2016 and January 2017, the Houston MBO acquired various physician and diagnostic operations in Texas, which resulted in the recognition of $43.9 million of total goodwill, calculated as the difference between the consideration paid and the fair value of assets acquired and liabilities assumed. Based upon the Houston MBO's quantitative goodwill analysis performed as of June 30, 2016, which resulted in the impairment of the Houston MBO's goodwill balances, CHI performed a goodwill impairment review of the Houston MBO as of December 31, 2016 and March 31, 2017. The goodwill impairment reviews indicated that the fair value of the Houston MBO's net assets remained below its carrying value. As a result, CHI determined that the $43.9 million of goodwill acquired during fiscal year 2017 was impaired, and impairment charges were recorded in the consolidated statement of operations for fiscal year 2017.

As of June 30, 2016, CHI revised the Houston MBO's projected cash flows due to operating results in the fourth quarter of fiscal year 2016 being below historical run rates. As a result of this update, CHI determined that $111.2 million of goodwill attributable to the Houston MBO operations was impaired. The impairment charge is reflected in the consolidated statement of operations for fiscal year 2016.

As a result of its impairment testing during the third quarter of fiscal year 2016, CHI determined that $16.8 million of goodwill attributable to the discontinued operations of QualChoice Health was impaired. The impairment charge is reflected in net loss from discontinued operations within the consolidated statements of changes in net assets for fiscal year 2016.

1. Summary of Significant Accounting Policies (continued)

The changes in the carrying amount of goodwill and intangibles is as follows (in thousands):

	2017	2016
Intangible assets, beginning of year	**$ 251,776**	$ 238,491
Current year acquisitions	**4,783**	13,285
Sale and other adjustments	**(20,525)**	–
Intangible assets, end of year	**236,034**	251,776
Accumulated amortization, beginning of year	**(50,680)**	(38,140)
Intangible amortization expense	**(12,581)**	(12,783)
Sale and other adjustments	**15,891**	243
Accumulated amortization, end of year	**(47,370)**	(50,680)
Intangible assets, net	**188,664**	201,096
Goodwill, beginning of year	**261,742**	350,149
Current year acquisitions	**67,567**	22,766
Impairments	**(44,136)**	(111,173)
Goodwill, end of year	**285,173**	261,742
Total intangible assets and goodwill, net	**$ 473,837**	$ 462,838

Notes Receivable and Other Assets

Other assets consist primarily of notes receivable, pledges receivable, deferred compensation assets, long-term prepaid service contracts, deposits and other long-term assets. Notes receivable from related entities as of June 30, 2016, include balances from Bethesda Hospital, Inc. (Bethesda), the non-CHI joint operating agreement (JOA) partner in the Cincinnati, Ohio JOA. As of June 30, 2016, Bethesda was a Designated Affiliate in the CHI credit group under the Capital Obligation Document (COD). In February 2017, Bethesda repaid its notes receivable balance of $139.7 million payable to CHI and is no longer considered a Designated Affiliate in the CHI credit group under the COD.

1. Summary of Significant Accounting Policies (continued)

A summary of notes receivable and other assets is as follows as of June 30 (in thousands):

	2017	2016
Notes receivable:		
From related entities	**$ 135**	$ 148,289
Other	**25,483**	36,384
Long-term pledge receivables	**37,911**	36,324
Reinsurance recoverable on unpaid losses and loss adjustment expense	**29,089**	32,226
Deferred compensation assets	**58,558**	76,679
Other long-term assets	**87,412**	116,620
Total notes receivable and other	**$ 238,588**	$ 446,522

Net Assets

Temporarily restricted net assets are those whose use has been limited by donors to a specific time period or purpose. Permanently restricted net assets consist of gifts with corpus values that have been restricted by donors to be maintained in perpetuity, including endowment funds. Temporarily restricted net assets and earnings on permanently restricted net assets, including earnings on endowment funds, are used in accordance with the donor's wishes primarily to purchase equipment, to provide charity care, and to provide other health and educational programs and services.

Unconditional promises to receive cash and other assets are reported at fair value at the date the promise is received. Conditional promises and indications of donors' intentions to give are reported at fair value at the date the conditions are met or the gifts are received. All unrestricted contributions are included in the excess (deficit) of revenue over expenses as donation revenues. Other gifts are reported as either temporarily or permanently restricted 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 donations revenue when restricted for operations or as unrestricted net assets when restricted for property and equipment.

1. Summary of Significant Accounting Policies (continued)

Performance Indicator

The performance indicator is the excess (deficit) of revenues over expenses, which includes all changes in unrestricted net assets other than changes in the pension liability funded status, net assets released from restrictions for property acquisitions, cumulative effect of changes in accounting principles, discontinued operations, contributions of property and equipment, and other changes not required to be included within the performance indicator under U.S. generally accepted accounting principles (U.S. GAAP).

Operating and Nonoperating Activities

CHI's primary mission is to meet the health care needs in its market areas through a broad range of general and specialized health care services, including inpatient acute care, outpatient services, physician services, long-term care, and other health care services. Activities directly associated with the furtherance of this purpose are considered to be operating activities. Other activities that result in gains or losses peripheral to CHI's primary mission are considered to be nonoperating. Nonoperating activities include investment earnings, gains/losses from extinguishment of debt, net interest cost and changes in fair value of interest rate swaps, and the nonoperating component of JOA income share adjustments. Any infrequent and nonreciprocal contribution that CHI makes to enter a new market community or to expand upon existing affiliations is also classified as nonoperating.

Charity Care

As an integral part of its mission, CHI accepts and provides medically necessary health care to all patients without regard to the patient's financial ability to pay. Services to patients are classified as charity care in accordance with standards established across all MBOs. Charity care represents services rendered for which partial or no payment is expected, and includes the cost of providing services to persons who cannot afford health care due to inadequate resources and/or who are uninsured or underinsured. CHI determines the cost of charity care on the basis of an MBO's total cost as a percentage of total charges applied to the charges incurred by patients qualifying for charity care under CHI's policy. This amount is not included in net patient services revenue in the accompanying consolidated statements of operations and changes in net assets. The estimated cost of charity care provided was $251.6 million and $204.9 million in 2017 and 2016, respectively, for continuing operations, and $15.9 million and $8.0 million in 2017 and 2016, respectively, for discontinued operations.

1. Summary of Significant Accounting Policies (continued)

Other Operating Revenues

Other operating revenues include services sold to external health care providers, gains on acquisitions of subsidiaries, cafeteria sales, rental income, retail pharmacy and durable medical equipment sales, auxiliary and gift shop revenues, electronic health records incentive payments, gains and losses on asset disposals, the operating portion of revenue-sharing income or expense associated with Direct Affiliates that are part of JOAs, premium revenues, and revenues from other miscellaneous sources.

Derivative and Hedging Instruments

CHI uses derivative financial instruments (interest rate swaps) in managing its capital costs. These interest rate swaps are recognized at fair value on the consolidated balance sheets. CHI has not designated its interest rate swaps related to CHI's long-term debt as hedges. The net interest cost and change in the fair value of such interest rate swaps is recognized as a component of nonoperating gains (losses) in the accompanying consolidated statements of operations. It is CHI's policy to net the value of collateral on deposit with counterparties against the fair value of its interest rate swaps in other liabilities on the consolidated balance sheets.

Functional Expenses

CHI provides healthcare services, including inpatient, outpatient, ambulatory, long-term care and community-based services to individuals within the various geographic areas supported by its facilities. Support services include administration, finance and accounting, information technology, public relations, human resources, legal, mission services, and other functions that are supported centrally for all of CHI. Support services expenses as a percentage of total operating expenses were approximately 6.2% and 6.0% in 2017 and 2016, respectively.

1. Summary of Significant Accounting Policies (continued)

Restructuring, Impairment, and Other Losses

Restructuring, impairment, and other losses include charges relating to changes in business operations, severance costs, EPIC go-live support costs and goodwill impairments, acquisition-related costs, and pension settlement activity. Changes in business operations include costs incurred periodically to implement reorganization efforts within specific operations, in order to align CHI's operations in the most strategic and cost-effective manner. Details of CHI's restructuring, impairment and other losses is as follows (in thousands):

	2017	2016
Impairment charges	**$ 48,356**	$ 111,188
Changes in business operations	**207,539**	115,809
Severance costs	**78,594**	40,708
Pension settlement costs	**39,678**	25,053
Total from continuing operations	**374,167**	292,758
Discontinued operations	**14,540**	28,253
Total restructuring, impairment and other losses	**$ 388,707**	$ 321,011

Noncash impairment charges, changes in business operations and pension settlement costs from continuing operations included in the consolidated statements of operations totaled $150.1 million and $169.0 million for the fiscal years ended June 30, 2017 and 2016, respectively. Discontinued operations are reported in the consolidated statements of changes in net assets.

Income Taxes

CHI is a tax-exempt Colorado corporation and has been granted an exemption from federal income tax under Section 501(c)(3) of the Internal Revenue Code. CHI owns certain taxable subsidiaries and engages in certain activities that are unrelated to its exempt purpose and therefore subject to income tax. As of June 30, 2017, CHI has a deferred tax asset of $100.4 million related to net operating loss (NOL) carryforwards. CHI believes that most of the NOL carryforwards will expire unused and has established a valuation allowance of $95.7 million against the deferred tax asset associated with these NOL carryforwards.

1. Summary of Significant Accounting Policies (continued)

Management reviews its tax positions annually and has determined that there are no material uncertain tax positions that require recognition in the accompanying consolidated financial statements.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results could vary from the estimates.

New Accounting Pronouncements

Revenue Recognition – In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers*, to clarify the principles for recognizing revenue and to improve financial reporting by creating common revenue recognition guidance for U.S. GAAP and International Financial Reporting Standards. The core principle of the new guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 is now effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is not permitted. CHI is evaluating the guidance in ASU 2014-09 and the impact that the adoption of this update will have on its consolidated financial statements.

Cloud Computing Arrangements – In April 2015, the FASB issued ASU No. 2015-05, *Intangibles-Goodwill and Other – Internal-Use Software (Subtopics 340-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement,* to provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The amendments in this update apply only to internal-use software that a customer obtains access to in a hosting arrangement if certain criteria are met. ASU 2015-05 is effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years, with early adoption permitted. The adoption of ASU 2015-05 did not have a material effect on CHI's consolidated financial statements.

1. Summary of Significant Accounting Policies (continued)

Leases – In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, to require a lessee to recognize a right-of-use asset and a lease liability for both operating and finance leases, whereas previous U.S. GAAP required the asset and liability be recognized only for capital leases. The amendment also requires qualitative and specific quantitative disclosures. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, with early adoption permitted. CHI is evaluating the guidance of ASU 2016-02 and the impact that the adoption of this update will have on its consolidated financial statements.

Presentation of Financial Statements of Not-for-Profit Entities – In August 2016, the FASB issued ASU No. 2016-14, *Not-for Profit Entities (Topic 958)*, to change the way a not-for-profit entity (NFP) classifies and presents net assets on the face of the financial statements, and presents information in the financial statements and notes about the NFP's liquidity, financial performance and cash flows. The amendment changes the way an NFP reports classes of net assets, from the currently required three classes to two, by eliminating the distinction between resources with permanent restrictions and those with temporary restrictions. The amendment also requires the NFP to provide enhanced disclosure about the nature, amounts and effects of the various types of donor-imposed restrictions, the NFP's management of its liquidity to meet short-term demands for cash, and the types of resources used and how they are allocated to carrying out the NFP's activities. ASU 2016-14 is effective for fiscal years beginning after December 15, 2017, and for interim periods within fiscal years beginning after December 15, 2018. Early application is permitted.

Classification of Certain Cash Receipts and Cash Payments – In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230)*, to provide guidance on the presentation and classification of eight specific cash flow issues, including debt prepayment or debt extinguishment costs, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, distributions received from equity method investees, and separately identifiable cash flows and application of the predominance principle. The objective of the amendment is to reduce the existing diversity in practice. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted.

1. Summary of Significant Accounting Policies (continued)

Restricted Cash – In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230)*, to provide guidance on the presentation of restricted cash or restricted cash equivalents in the statement of cash flows. The amendments require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. ASU 2016-18 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted.

Simplifying the Test for Goodwill Impairment – In January 2017, the FASB issued ASU No. 2017-04, *Intangibles–Goodwill and Other (Topic 350)*, to provide guidance on simplifying how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of the reporting unit's goodwill with the carrying amount of that goodwill. Instead, the entity will record a goodwill impairment loss based on the excess of the reporting unit's carrying amount of goodwill over its fair value, which is based on the current Step 1. ASU 2017-04 is effective for annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2021. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017, and CHI has elected early adoption of this amendment.

Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost – In March 2017, the FASB issued ASU No. 2017-07, *Compensation – Retirement Benefits (Topic 715)*, to improve the presentation of net periodic pension cost and net periodic postretirement benefit cost. The amendments in this update require that an employer disaggregate the service cost component and the other components of net benefit cost, and that the service cost component be reflected in the same line item as other employee compensation costs. The other components of net benefit cost would be reported as nonoperating gains (losses) on the consolidated statement of operations. ASU 2017-07 is effective for annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Early adoption is permitted.

Reclassifications

Certain reclassifications were made to the fiscal year 2016 consolidated financial statement presentation to conform to the 2017 presentation – supply costs not related to direct patient care in the amount of $125.9 million for the year ended June 30, 2017, were reclassified from supplies expenses to other expenses on the consolidated statements of operations.

2. Community Benefit (Unaudited)

In accordance with its mission and philosophy, CHI commits substantial resources to sponsor a broad range of services to both the poor and the broader community. Community benefit provided to the poor includes the cost of providing services to persons who cannot afford health care due to inadequate resources and/or who are uninsured or underinsured. This type of community benefit includes the costs of traditional charity care; unpaid costs of care provided to beneficiaries of Medicaid and other indigent public programs; services such as free clinics and meal programs for which a patient is not billed or for which a nominal fee has been assessed; and cash and in-kind donations of equipment, supplies or staff time volunteered on behalf of the community.

Community benefit provided to the broader community includes the costs of providing services to other populations who may not qualify as poor but may need special services and support. This type of community benefit includes the costs of services such as health promotion and education, health clinics and screenings, all of which are not billed or can be operated only on a deficit basis; unpaid portions of training health professionals such as medical residents, nursing students and students in allied health professions; and the unpaid portions of testing medical equipment and controlled studies of therapeutic protocols.

A summary of the cost of community benefit provided to both the poor and the broader community is as follows (in thousands):

	2017	2016
Cost of community benefit:		
Cost of charity care provided	**$ 251,634**	$ 204,927
Unpaid cost of public programs, Medicaid and other indigent care programs	**605,930**	523,348
Nonbilled services	**29,355**	34,700
Cash and in-kind donations	**19,559**	28,974
Education research	**123,883**	115,410
Other benefit	**109,463**	117,802
Total cost of community benefit from continuing operations	**1,139,824**	1,025,161
Total cost of community benefit from discontinued operations	**75,929**	72,913
Total cost of community benefit	**1,215,753**	1,098,074
Unpaid cost of Medicare from continuing operations	**911,572**	956,725
Total cost of community benefit and the unpaid cost of Medicare	**$ 2,127,325**	$ 2,054,799

2. Community Benefit (Unaudited) (continued)

The summary above has been prepared in accordance with the Catholic Health Association of the United States (CHA) publication, *A Guide for Planning & Reporting Community Benefit*. Community benefit is measured on the basis of total cost, net of any offsetting revenues, donations or other funds used to defray cost. During fiscal years 2017 and 2016, CHI received $20.9 million and $29.5 million, respectively, in funds used to subsidize charity care provided.

The total cost of community benefit from continuing and discontinued operations was 7.0% and 6.5% of total operating expenses before restructuring, impairment and other losses in fiscal years 2017 and 2016, respectively. The total cost of community benefit and the unpaid cost of Medicare from continuing and discontinued operations was 12.3% and 12.2% of total operating expenses before restructuring, impairment and other losses in 2017 and 2016, respectively.

3. Joint Operating Agreements and Investments in Unconsolidated Organizations

Joint Operating Agreements

CHI participates in JOAs with hospital-based organizations in three separate market areas. The agreements generally provide for, among other things, joint management of the combined operations of the local facilities included in the JOAs through Joint Operating Companies (JOC). CHI retains ownership of the assets, liabilities, equity, revenues and expenses of the CHI facilities that participate in the JOAs. The financial statements of the CHI facilities managed under all JOAs are included in the CHI consolidated financial statements. Transfers of assets from facilities owned by the JOA participants generally are restricted under the terms of the agreements.

As of June 30, 2017 and 2016, CHI has investment interests of 65%, 50%, and 50% in JOCs based in Colorado, Iowa, and Ohio, respectively. CHI's interests in the JOCs are included in investments in unconsolidated organizations and totaled $381.7 million and $351.9 million at June 30, 2017 and 2016, respectively. CHI recognizes its investment in all JOCs under the equity method of accounting. The JOCs provide varying levels of services to the related JOA sponsors, and operating expenses of the JOCs are allocated to each sponsoring organization.

3. Joint Operating Agreements and Investments in Unconsolidated Organizations (continued)

In March 2016, CHI amended the existing Iowa JOA to among other items, allow for the Iowa JOC to acquire health care systems in Iowa and contiguous markets, which would be owned equally between CHI and the existing JOC partner. In May 2016, the Iowa JOC acquired Wheaton Franciscan Healthcare and recorded a business combination gain on the acquisition. As a result, CHI recognized $89.1 million of its proportionate share of the gain, which is reflected in the consolidated statements of operations as changes in equity of unconsolidated organizations for the year ended June 30, 2016.

Investments in Unconsolidated Organizations

CHI holds noncontrolling interests in various organizations, accounted for under the cost or equity method of accounting, as appropriate. Significant investments are described below.

Conifer Health Solutions (Conifer) – As of June 30, 2017 and 2016, CHI holds a 23.8% equity method investment in Conifer totaling $614.0 million and $570.7 million, respectively. The investment in Conifer was acquired as part of a multi-year agreement with Conifer where Conifer provides revenue cycle services and health information management solutions for CHI acute care operations. Since CHI was granted incremental shares in Conifer in conjunction with the multi-year agreement with Conifer, CHI also has a deferred income balance related to the Conifer agreement of $431.1 million and $458.9 million, as of June 30, 2017 and 2016, respectively, reported in other liabilities on the accompanying consolidated balance sheets. The deferred income balances are being amortized straight line over the remaining agreement term expiring in January 2033, offsetting revenue cycle services fees paid to Conifer, which are reported in purchased services expense in the accompanying consolidated statements of operations.

As a result of CHI recording its incremental equity ownership in Conifer at fair value, the carrying value of its equity method investment in Conifer was $253.3 million and $261.8 million greater than CHI's equity interest in the underlying net assets of Conifer as of June 30, 2017 and 2016, respectively, due to basis differences in the carrying amounts of the tangible and intangible assets of $186.6 million and $195.1 million, respectively, and of goodwill of $66.7 million in both periods. Goodwill is not amortized but is subject to annual impairment tests during the third quarter of the fiscal year, as well as more frequent reviews whenever circumstances indicate a possible impairment may exist. No impairment of goodwill was identified as of June 30, 2017 and 2016. The basis differences of the tangible and intangible assets are being amortized over the average useful lives of the underlying assets, ranging from 8 to 25 years, as a reduction of CHI's equity earnings in Conifer.

3. Joint Operating Agreements and Investments in Unconsolidated Organizations (continued)

Other Entities – The summarized financial positions and results of operations for the other entities accounted for under the equity method of accounting as of and for the periods ended June 30, excluding the investments described above, are as follows (in thousands):

	2017							
	Medical Office Buildings	**Outpatient and Diagnostic Services**	**Ambulatory Surgery Centers**	**Physician Practices**	**Hospital-Based Services**	**ACO/ CCO/ CIN**	**Other Investees**	**Total**
Total assets	**$ 17,345**	**$ 90,399**	**$ 87,958**	**$ 13,469**	**$ 185,356**	**$ 107,722**	**$ 256,017**	**$ 758,266**
Total debt	**170**	**5,976**	**21,996**	**2**	**17,343**	**31,063**	**87,992**	**164,542**
Net assets	**17,233**	**75,284**	**61,527**	**9,658**	**150,231**	**76,659**	**142,455**	**533,047**
Net patient services revenues	**–**	**84,779**	**119,056**	**7,332**	**177,431**	**–**	**193,722**	**582,320**
Total revenues, net	**3,577**	**137,557**	**130,356**	**7,332**	**177,889**	**180,436**	**272,215**	**909,362**
Excess (deficit) of revenues over expenses	**3,157**	**23,789**	**35,460**	**(1,747)**	**32,968**	**1,723**	**20,610**	**115,960**

	2016							
	Medical Office Buildings	**Outpatient and Diagnostic Services**	**Ambulatory Surgery Centers**	**Physician Practices**	**Hospital-Based Services**	**ACO/ CCO/ CIN**	**Other Investees**	**Total**
Total assets	$ 8,416	$ 325,839	$ 61,443	$ 8,621	$ 176,015	$ 128,069	$ 176,054	$ 884,457
Total debt	1,241	50,495	14,028	1	18,775	–	59,848	144,388
Net assets	6,013	220,849	31,488	8,197	143,318	78,961	104,998	593,824
Net patient services revenues	–	312,518	98,850	6,271	138,390	–	116,540	672,569
Total revenues, net	1,889	419,513	100,251	6,628	138,657	179,066	161,319	1,007,323
Excess of revenues over expenses	10,012	41,496	30,364	105	33,155	7,091	6,399	128,622

4. Acquisitions, Affiliations, and Divestitures

The following table is a summary of significant business combinations and affiliations that occurred in fiscal year 2017 (in thousands):

Purchase consideration:	
Cash	**$ 64,432**
Current liabilities	**723**
Debt	**27,755**
	$ 92,910
Purchase price allocation:	
Inventory	**$ 3,041**
Property and equipment	**39,681**
Intangible assets	**4,343**
Goodwill	**50,702**
Current liabilities	**(752)**
Debt	**(4,105)**
	$ 92,910

During fiscal year 2017, CHI entered into various business combinations and affiliations, including the acquisition by a subsidiary of CHI of the operations of a multi-specialty group in the state of Texas. The operations include a general acute care hospital and emergency room, an ambulatory surgery center, a management company, and an independent physician association comprising of more than 80 health care providers. For the fiscal year ended June 30, 2017, the affiliations and acquisitions reported a combined $52.0 million in operating revenues and $(17.5) million in deficit of revenues over expenses in the CHI consolidated results of operations.

4. Acquisitions, Affiliations and Divestitures (continued)

The following table is a summary of significant business combinations and affiliations that occurred in fiscal year 2016 (in thousands):

	Trinity	Brazosport	LUH	Other	Total
Purchase consideration:					
Cash	$ –	$ –	$ –	$ 17,225	$ 17,225
Noncontrolling interest	–	–	–	9,275	9,275
Business combination gains	72,717	21,293	111,551	17,475	223,036
	72,717	21,293	111,551	43,975	249,536
Equity interest in Trinity	72,392	–	–	–	72,392
	$ 145,109	$ 21,293	$ 111,551	$ 43,975	$ 321,928

	Trinity	Brazosport	LUH	Other	Total
Purchase price allocation:					
Cash and investments	$ 133,349	$ 18,650	$ 70,416	$ 5,420	$ 227,835
Patient and other A/R	40,363	22,191	25,346	5,443	93,343
Other current assets	6,373	3,200	9,775	786	20,134
Property and equipment	57,598	36,292	111,609	16,970	222,469
Intangible assets	210	–	–	1,200	1,410
Goodwill	–	–	–	18,648	18,648
Other assets	8,962	144	13,276	–	22,382
Current liabilities	(26,246)	(18,777)	(17,455)	(2,994)	(65,472)
Pension liability	(16,408)	–	–	–	(16,408)
Other liabilities	(9,818)	(671)	–	–	(10,489)
Debt	(40,069)	(38,450)	(97,765)	(1,437)	(177,721)
Restricted net assets	(9,205)	(1,286)	(3,651)	(61)	(14,203)
	$ 145,109	$ 21,293	$ 111,551	$ 43,975	$ 321,928

4. Acquisitions, Affiliations, and Divestitures (continued)

Trinity Health System – Effective February 1, 2016, CHI became the sole owner of Trinity Health System (Trinity) based in Steubenville, Ohio, when it acquired the remaining 50% ownership in Trinity. The other 50% ownership in Trinity was held by Sylvania Franciscan Health (Sylvania), which CHI acquired in November 2014; the remeasurement of Sylvania's investment in Trinity resulted in an immaterial gain on Sylvania's 50% equity ownership. Trinity owns and operates Trinity Medical Center East, Trinity Medical Center West, Tony Teramana Cancer Center, and numerous outpatient clinics located in eastern Ohio. The transaction resulted in the recognition of a $72.7 million gain calculated as the fair value of identifiable assets acquired and liabilities assumed, determined based upon Level 3 inputs, including estimated future cash flows and probability-weighted performance assumptions. Excluding the business combination gain, Trinity reported $237.6 million and $103.7 million in operating revenues, respectively, and $27.8 million and $13.0 million of excess of revenues over expenses, respectively, to the CHI consolidated results of operations for the fiscal year ended June 30, 2017 and for the period February 1, 2016 through June 30, 2016, respectively.

Brazosport Regional Health System – Effective February 1, 2016, a consolidated subsidiary of CHI signed an affiliation agreement with Brazosport Regional Health System (Brazosport) in Lake Jackson, Texas, to become part of CHI. Brazosport is a nonprofit health care organization that includes a 158-bed hospital that operates the only Level III trauma center in Brazoria County. The transaction resulted in the recognition of a $21.3 million gain calculated as the fair value of identifiable assets acquired and liabilities assumed, determined based upon Level 3 inputs, including estimated future cash flows and probability-weighted performance assumptions. Excluding the business combination gain, Brazosport reported $78.7 million and $33.7 million in operating revenues, respectively, and $(10.7) million and $(1.3) million of deficit of revenues over expenses, respectively, to the CHI consolidated results of operations for the fiscal year ended June 30, 2017 and for the period from February 1, 2016 through June 30, 2016, respectively.

Longmont United Hospital – Effective August 1, 2015, a direct affiliate of CHI entered into a Joint Operating and Management Agreement with Longmont United Hospital (LUH) to become the sole and exclusive agent to manage and operate the LUH business for a period of 99 years. The transaction resulted in the recognition of a $111.6 million gain calculated as the fair value of identifiable assets acquired and liabilities assumed, determined based upon Level 3 inputs, including estimated future cash flows and probability-weighted performance assumptions. Excluding the business combination gain, LUH reported $183.0 million and $160.9 million in operating revenues, respectively, and $(12.5) million and $(8.6) million of deficit of revenues over expenses, respectively, to the CHI consolidated results of operations for the fiscal year ended June 30, 2017 and for the period from August 1, 2015 through June 30, 2016, respectively.

4. Acquisitions, Affiliations, and Divestitures (continued)

Had CHI owned the above acquired entities as of the beginning of each fiscal year, CHI's unaudited pro forma results, excluding business combination gains, for the years ended June 30 would have been as presented below (in thousands):

	2017 Pro Forma Total CHI	2016 Pro Forma Total CHI
Operating revenues	**$ 15,583,123**	$ 15,312,149
Operating loss before restructuring	**(208,473)**	(294,984)
Excess (deficit) of revenues over expenses	**130,997**	(800,823)

Unaudited pro forma information is not necessarily indicative of the historical results that would have been obtained had the transaction actually occurred on those dates, nor of future results.

Other Affiliations

Pathology Associates Medical Laboratories, LLC (PAML) – Effective in May 2017, CHI sold all of its interests in PAML to Laboratory Corporation of America Holdings (LabCorp). As part of the agreement, LabCorp will also acquire CHI's direct and indirect interests in three CHI joint ventures with PAML in the states of Colorado, Kentucky and Washington. Nonrefundable gross sales proceeds attributable to CHI and its affiliates of $96.7 million were received in May 2017, resulting in a gain on sale of $40.2 million reflected in other operating revenues in the consolidated statements of operations.

KentuckyOne/UMC JOA dissolution – In December 2016, KentuckyOne Health, a subsidiary of CHI, and University Medical Center (UMC) agreed to restructure their existing JOA, originally entered into in March 2013, which had given KentuckyOne Health control over substantially all of UMC's operations, including University of Louisville Hospital and the James Graham Brown Cancer Center. Among the various capital investment and funding aspects of the new agreement, the new agreement also called for UMC to take over the management of UMC operations effective on July 1, 2017, at which time CHI ceased consolidating the operations of UMC.

4. Acquisitions, Affiliations, and Divestitures (continued)

For the fiscal years ended June 30, 2017 and 2016, UMC reported total operating revenues of $515.2 million and $528.7 million, respectively, and excess of revenues over expenses of $18.1 million and $43.8 million, respectively. The CHI consolidated balance sheets also included UMC total assets of $605.5 million and $516.9 million as of June 30, 2017 and 2016, respectively. Upon deconsolidation of UMC on July 1, 2017, CHI incurred a loss of approximately $318.0 million.

Dignity Health – On October 24, 2016, CHI and Dignity Health signed a nonbinding letter of intent to explore aligning their organizations and expanding their mission of service in communities across the nation. The potential alignment would strengthen CHI and Dignity Health's leadership role in transforming health care through increased patient access and enhanced clinical excellence. The boards and sponsors of the two health systems are continuing to evaluate the potential alignment and are in the final stages of the due diligence process. CHI can give no assurance that the transaction will occur.

Discontinued Operations

In May 2017, CHI approved a plan to sell or otherwise dispose of certain entities of Jewish Hospital and St. Mary's Healthcare, Inc. System (JHSMH). CHI will begin to market the sale of these operations and anticipates closing on a sale by the end of the calendar year.

In May 2016, CHI approved a plan to sell or otherwise dispose of certain entities of QualChoice Health, Inc. (QualChoice Health), a consolidated CHI subsidiary, whose primary business is to develop, manage and market commercial and Medicare Advantage health insurance programs, as well as a wide range of products and administrative services. A letter of intent for the Medicare Advantage health insurance operations has been received, with an anticipated sale in fiscal year 2018. Although there has been significant interest in the QualChoice Health commercial operations, the uncertainty surrounding the Affordable Care Act and current political environment has delayed the anticipated sale of this operation to a timeline outside of CHI's control. CHI remains committed to selling or otherwise disposing of the QualChoice Health commercial operations and continues to actively market these operations.

The JHSMH and QualChoice Health operations are reflected as discontinued operations and held for sale as of June 30, 2017 and 2016, in accordance with ASU No. 2014-08, *Reporting Discontinued Operations and Disclosure of Disposals of Components of an Entity*, as the operations held for sale are deemed to represent a strategic shift in CHI's operations, which will have a major effect on its financial results.

4. Acquisitions, Affiliations, and Divestitures (continued)

Effective in fiscal year 2016, CHI sold the operations of the Reading, Pennsylvania MBO and the Denville, New Jersey MBO, for total gross proceeds of $206.0 million. The Denville MBO sale included $20.9 million of working capital settlements; as of June 30, 2016, CHI had received $62.0 million for the sale of the hospital operations of the Denville MBO plus $16.0 million in estimated working capital settlements net of closing costs. The Reading and Denville MBOs are reflected as discontinued operations in accordance with Accounting Standards Codification (ASC) 205-20, *Discontinued Operations*.

The results of operations of Louisville, QualChoice Health, and the Reading and Denville MBOs are reported in the consolidated statements of changes in net assets as discontinued operations.

A reconciliation of major classes of assets and liabilities of the discontinued operations is presented below as of June 30 (in thousands):

	2017	2016
Other accounts receivable	**$ 31,204**	$ 75,769
Investments held for insurance purposes	**132,519**	116,950
Property and equipment, net	**380,495**	430,556
Other assets	**35,725**	35,165
Total major classes of assets of the discontinued operations	**579,943**	658,440
Other assets classified as held for sale	**2,401**	6,988
Total assets classified as held for sale	**$ 582,344**	$ 665,428
Compensation and benefits	**$ 48,530**	$ 54,775
Accounts payable and accrued expenses	**44,898**	34,214
Debt	**10,258**	11,621
Self-insured reserves	**62,049**	74,629
Total major classes of liabilities of the discontinued operations classified as held for sale	**$ 165,735**	$ 175,239

4. Acquisitions, Affiliations, and Divestitures (continued)

The $2.4 million and $7.0 million of other assets classified as held for sale as of June 30, 2017 and 2016, respectively, represent real estate assets which are scheduled to be sold in fiscal year 2018, measured at the lower of their carrying amount or fair value less cost to sell.

Operating results of discontinued operations are reported in the accompanying consolidated statements of changes in net assets and are summarized as follows for the years ended June 30 (in thousands):

	2017	2016
Net patient service revenues	**$ 763,007**	$ 827,096
Insurance premium revenues	**573,811**	516,844
Gain on sale	**751**	73,711
Other revenues	**26,441**	84,090
Total operating revenues	**1,364,010**	1,501,741
Salaries, wages, and employee benefits	**(491,504)**	(584,955)
Medical claims	**(526,683)**	(482,402)
Depreciation	**(42,931)**	(49,870)
Other expenses	**(439,656)**	(502,364)
Total operating expenses before restructuring, impairment and other losses	**(1,500,774)**	(1,619,591)
Loss from operations before restructuring, impairment and other losses	**(136,764)**	(117,850)
Restructuring, impairment, and other losses	**(14,540)**	(28,253)
Loss from operations	**(151,304)**	(146,103)
Nonoperating losses	**(1,584)**	(8,422)
Deficit of revenues over expenses	**$ (152,888)**	$ (154,525)

Total operating revenues in fiscal year 2016 include a gain of $59.6 million on the sale of the Denville MBO's long-term care operations in May 2016.

The discontinued operations reported $23.0 million and $48.0 million in capital expenditures for fiscal years 2017 and 2016, respectively.

5. Net Patient Services Revenues

Net patient services revenues are derived from services provided to patients who are either directly responsible for payment or are covered by various insurance or managed care programs. CHI receives payments from the federal government on behalf of patients covered by the Medicare program, from state governments for Medicaid and other state-sponsored programs, from certain private insurance companies and managed care programs, and from patients themselves. A summary of payment arrangements with major third-party payors follows:

Medicare – Inpatient acute care and certain outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge or procedure. These rates vary according to patient classification systems based on clinical, diagnostic and other factors. Certain CHI facilities have been designated as critical access hospitals and, accordingly, are reimbursed their cost of providing services to Medicare beneficiaries. Professional services rendered by physicians are paid based on the Medicare allowable fee schedule.

Medicaid – Inpatient services rendered to Medicaid program beneficiaries are primarily paid under the traditional Medicaid plan at prospectively determined rates per discharge. Certain outpatient services are reimbursed based on a cost reimbursement methodology, fee schedules or discounts from established charges.

Other – CHI has also entered into payment agreements with certain managed care and commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to CHI under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

CHI's Medicare, Medicaid and other payor utilization percentages, based upon net patient services revenues before provision for doubtful accounts, are summarized as follows:

	2017	2016
Medicare	**36%**	32%
Medicaid	**13**	13
Managed care	**38**	38
Self-pay	**3**	4
Commercial and other	**10**	13
	100%	100%

5. Net Patient Services Revenues (continued)

Laws and regulations governing the Medicare and Medicaid 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. Estimated settlements related to Medicare and Medicaid of $86.1 million and $112.1 million at June 30, 2017 and 2016, respectively, are included in third-party liabilities. Net patient services revenues from continuing operations increased by $78.2 million and $94.6 million in fiscal year 2017 and 2016, respectively, due to favorable changes in estimates related to prior-year settlements.

6. Investments and Assets Limited as to Use

CHI's investments and assets limited as to use as of June 30 are reported in the accompanying consolidated balance sheets as presented in the following table (in thousands):

	2017	2016
Cash and equivalents	**$ 150,960**	$ 185,325
CHI Investment Program	**5,730,972**	5,266,787
Marketable equity securities	**274,948**	342,327
Marketable fixed-income securities	**664,433**	802,382
Hedge funds and other investments	**30,319**	24,360
	6,851,632	6,621,181
Less current portion	**(65,161)**	(63,146)
	$ 6,786,471	$ 6,558,035

CHI attempts to reduce its market risk by diversifying its investment portfolio using cash equivalents, fixed-income securities, marketable equity securities and alternative investments. Most of the U.S. Treasury, money market funds and corporate debt obligations as well as exchange-traded marketable securities held directly by CHI and by the CHI Investment Program (the Program) have an actively traded market. However, CHI also invests in commercial paper, mortgage-backed or other asset-backed securities, alternative investments (hedge funds, private equity investments, real estate funds, funds of funds, etc.), collateralized debt obligations, municipal securities and other investments that have potential complexities in valuation based upon the current conditions in the credit markets. For some of these instruments, evidence supporting the determination of fair value may not come from trading in active primary or secondary markets. Because these investments may not be readily marketable, the estimated value

6. Investments and Assets Limited as to Use (continued)

is subject to uncertainty and, therefore, may differ from the value that would have been used had an active market for such investments existed. Such differences could be material. However, management reviews the CHI investment portfolio on a regular basis and seeks guidance from its professional portfolio managers related to U.S. and global market conditions to determine the fair value of its investments. CHI believes the carrying amount of these financial instruments in the accompanying consolidated financial statements is a reasonable estimate of fair value.

The majority of all CHI long-term investments are held in the Program. The Program is structured under a Limited Partnership Agreement with CHI as managing general partner and numerous limited partners, most sponsored by CHI. The partnership provides a vehicle whereby virtually all entities associated with CHI, as well as certain other unrelated entities, can optimize investment returns while managing investment risk. Entities participating in the Program that are not consolidated in the accompanying financial statements have the ability to direct their invested amounts and liquidate and/or withdraw their interest without penalty as soon as practicable based on market conditions but within 180 days of notification. The Limited Partnership Agreement permits a simple-majority vote of the noncontrolling limited partners to terminate the partnership. Accordingly, CHI recognizes only the unitized portion of Program assets attributable to CHI and its direct affiliates. Program assets attributable to CHI and its Direct Affiliates represented 89% of total Program assets at June 30, 2017 and 2016, respectively.

The Program asset allocation at June 30 is as follows:

	2017	**2016**
Equity securities	**41%**	44%
Fixed-income securities	**39**	32
Alternative investments	**19**	23
Cash and equivalents	**1**	1
	100%	100%

The CHI Finance Committee (the Committee) of the Board of Stewardship Trustees is responsible for determining asset allocations among fixed-income, equity, and alternative investments. At least annually, the Committee reviews targeted allocations and, if necessary, makes adjustments to targeted asset allocations. Given the diversity of the underlying securities in which the Program invests, management does not believe there is a significant concentration of credit risk.

6. Investments and Assets Limited as to Use (continued)

The Program allocation to alternative investments is based upon contractual commitment levels to various funds. These commitments are drawn by the fund managers as opportunities arise to invest the capital. As of June 30, 2017, the Program had committed to invest $815.0 million in 41 funds, of which $698.6 million had been invested. The remaining $116.4 million will be invested when, and if, requested by the funds. Alternative investments within the Program have limited liquidity. As of June 30, 2017, illiquid investments not available for redemption totaled $378.9 million, and investments available for redemption within 180 days at the request of the Program totaled $813.2 million.

Investment gains (losses) are comprised of the following for the years ended June 30 (in thousands):

	2017	2016
Dividend and interest income	**$ 146,582**	$ 149,800
Net realized gains	**338,400**	149,802
Net unrealized gains (losses)	**153,537**	(302,986)
Total investment gains (losses) from continuing operations	**638,519**	(3,384)
Total investment losses from discontinued operations	**(1,584)**	(8,422)
Total investment gains (losses)	**$ 636,935**	$ (11,806)

Direct expenses of the Program are less than 0.3% of total assets. Fees paid to the alternative investment managers are not included in the total expense calculation as they are not a direct expense of the Program.

7. Fair Value of Assets and Liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820, *Fair Value Measurements and Disclosures,* establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 inputs) and the lowest priority to unobservable inputs (Level 3 inputs).

The three levels of the fair value hierarchy and a description of the valuation methodologies used for instruments measured at fair value are as follows:

Level 1 – Valuation is based upon quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 – Valuation is based upon quoted prices for similar assets and liabilities in active markets or other inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial asset or liability.

Level 3 – Valuation is based upon other unobservable inputs that are significant to the fair value measurement.

Certain of CHI's alternative investments are made through limited liability companies (LLC) and limited liability partnerships (LLP). These LLCs and LLPs provide CHI with a proportionate share of the investment gains (losses). CHI accounts for its ownership in the LLCs and LLPs under the equity method. CHI also accounts for its ownership in the Program under the equity method. As such, these investments are excluded from the scope of ASC 820.

7. Fair Value of Assets and Liabilities (continued)

Financial assets and liabilities measured at fair value on a recurring basis were determined using the market approach based upon the following inputs at June 30 (in thousands):

	2017			
	Fair Value Measurements at Reporting Date Using			
		(Level 1)	(Level 2)	(Level 3)
	Fair Value as of June 30	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs
Assets				
Assets limited as to use:				
Cash and short-term investments	**$ 150,960**	**$ 130,400**	**$ 20,560**	**$ –**
Equity securities	**274,948**	**274,948**	**–**	**–**
Fixed-income securities	**664,433**	**170,425**	**494,008**	**–**
Other investments	**3,523**	**–**	**–**	**3,523**
Deferred compensation assets:				
Cash and short-term investments	**6,708**	**6,708**	**–**	**–**
	$ 1,100,572	**$ 582,481**	**$ 514,568**	**$ 3,523**
Liabilities				
Interest rate swaps	**$ 287,990**	**$ –**	**$ 287,990**	**$ –**
Contingent consideration	**177,189**	**–**	**–**	**177,189**
Deferred compensation liability	**6,708**	**6,708**	**–**	**–**
	$ 471,887	**$ 6,708**	**$ 287,990**	**$ 177,189**

7. Fair Value of Assets and Liabilities (continued)

	2016			
	Fair Value Measurements at Reporting Date Using			
		(Level 1)	(Level 2)	(Level 3)
	Fair Value as of June 30	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs
Assets				
Assets limited as to use:				
Cash and short-term investments	$ 185,325	$ 183,641	$ 1,684	$ –
Equity securities	342,327	342,327	–	–
Fixed-income securities	802,382	143,263	659,119	–
Other investments	428	–	–	428
Deferred compensation assets:				
Cash and short-term investments	8,248	8,248	–	–
	$ 1,338,710	$ 677,479	$ 660,803	$ 428
Liabilities				
Interest rate swaps	$ 416,277	$ –	$ 416,277	$ –
Contingent consideration	207,204	–	–	207,204
Deferred compensation liability	8,248	8,248	–	–
	$ 631,729	$ 8,248	$ 416,277	$ 207,204

The fair values of the securities included in Level 1 were determined through quoted market prices. Level 1 instruments include money market funds, mutual funds and marketable debt and equity securities. The fair values of Level 2 instruments were determined through evaluated bid prices based on recent trading activity and other relevant information, including market interest rate curves and referenced credit spreads; estimated prepayment rates, where applicable, are used for valuation purposes and are provided by third-party services where quoted market values are not available. Level 2 instruments include corporate fixed-income securities, government bonds, mortgage and asset-backed securities, and interest rate swaps. The fair values of Level 3 securities are determined primarily through information obtained from the relevant counterparties for such

7. Fair Value of Assets and Liabilities (continued)

investments. Information on which these securities' fair values are based is generally not readily available in the market. The fair value of the contingent consideration liability was determined based on estimated future cash flows and probability-weighted performance assumptions, discounted to net present value. The contingent consideration liability balance was adjusted to reflect $37.4 million of payments made since June 30, 2016, and to reflect a $7.4 million increase for changes in payment assumptions.

8. Property and Equipment

A summary of property, equipment, and software is as follows as of June 30 (in thousands):

	2017	2016
Land and improvements	**$ 780,135**	$ 687,279
Buildings and improvements	**7,244,245**	7,316,817
Equipment	**5,691,549**	5,486,136
Software	**1,113,667**	1,008,466
	14,829,596	14,498,698
Less accumulated depreciation and amortization	**(7,146,842)**	(6,537,012)
	7,682,754	7,961,686
Construction in progress	**886,559**	1,072,366
	$ 8,569,313	$ 9,034,052

CHI incurs a variety of direct and indirect costs to develop internal-use software. In order for software to be considered internal use, it must be acquired, internally developed or modified solely to meet CHI's needs and no plan exists or is being developed to sell the software externally during the software's development or modification. Unamortized software costs as of June 30, 2017 and 2016, were $746.3 million and $784.1 million, respectively. For the fiscal years ended June 30, 2017 and 2016, CHI recorded $137.8 million and $111.6 million, respectively, related to amortization of internal-use software. Amortization of internal-use software begins when the software is placed in service, and is based on the expected useful life of the software, which is generally between 2 and 10 years.

8. Property and Equipment (continued)

During fiscal years 2017 and 2016, CHI sold various real estate assets across the enterprise as part of a long-term effort to improve the mix of owned and leased assets. In conjunction with the sale, CHI entered into 10-year operating lease agreements with the buyers, and in accordance with ASC 840-40, *Leases – Sale-Lease Back Transactions*, certain of the gains on the sale of the real estate assets were deferred and will be amortized to lease expense over the life of the operating leases.

In fiscal years 2017 and 2016, real estate assets with a net book value of $281.8 million and $332.3 million, respectively, were sold for gross proceeds of $366.5 million and $601.7 million, respectively. As a result of the sales, CHI recognized $22.0 million and $59.4 million gains on sales, reflected in other operating revenues in the consolidated statements of operations for the years ended June 30, 2017 and 2016, respectively. CHI also recorded short-term deferred gains of $5.8 million and $20.1 million, respectively, and long-term deferred gains of $52.2 million and $180.6 million, respectively, for fiscal year 2017 and fiscal year 2016. On the consolidated balance sheets, the short-term deferred gains are a component of accrued expenses, and the long-term deferred gains are a component of other long-term liabilities.

CHI also sold various other assets during fiscal year 2017 for net proceeds of $101.7 million reflected within other operating revenues as gain on sale on the consolidated statement of operations for the year ended June 30, 2017.

9. Debt Obligations

The following is a summary of debt obligations as of June 30 (in thousands):

	Maturity Date	Interest Rates at June 30, 2017	2017	2016
Debt secured under the CHI COD				
Variable-rate bonds:				
CHI Series 2004B	2044	1.97%	**$ 54,200**	$ 54,200
CHI Series 2004C	2039	1.25–1.32	**96,700**	96,700
CHI Series 2008A	2037	1.72	**119,450**	120,175
CHI Series 2008C	2040	1.96	**52,990**	52,990
CHI Series 2011B	2046	2.31	**158,155**	158,155
CHI Series 2011C	2046	1.80	**118,000**	118,000
CHI Series 2013B	2035	1.91–2.31	**200,000**	200,000
CHI Series 2013C	2046	2.49	**100,000**	100,000
CHI Series 2013E Taxable	2046	2.55	**125,000**	125,000
CHI Series 2013F Taxable	2046	2.42	**75,000**	75,000
CHI Series 2015-1	2032	1.61	**36,700**	38,400
CHI Series 2015-2	2027	1.61	**63,472**	73,700
CHI Series 2015A	2032	1.71–1.79	**66,100**	69,500
CHI Series 2015B	2042	1.71	**27,270**	50,000
CHI Series 2016 Taxable	2021	3.80	**200,000**	–
Commons of Providence Series 2009B	2034	2.71	**5,860**	–
Providence Care Center Series 2009C	2034	2.71	**4,160**	–
Providence Residential Community Series 2009A	2034	2.71	**6,770**	–
Fixed-rate bonds:				
CHI Series 2002A	–	–	**–**	920
CHI Series 2004A	2034	4.75–5.0	**123,170**	140,985
CHI Series 2006A	2042	4.0–5.0	**268,015**	270,635
CHI Series 2008D	2039	5.0–6.38	**445,220**	452,065
CHI Series 2009A	2040	4.0–5.5	**573,680**	672,050
CHI Series 2009B	2040	1.88–5.25	**208,560**	217,720
CHI Series 2011A	2041	3.25–5.25	**436,470**	451,270
CHI Series 2012A	2036	3.5–5.0	**199,670**	264,170
CHI Series 2012 Taxable	2043	1.6–4.35	**1,500,000**	1,500,000
CHI Series 2013A	2045	5.0–5.75	**600,600**	600,600
CHI Series 2013D Taxable	2024	2.6–4.2	**540,000**	540,000
Madonna Manor Series 2010	2040	7.0	**27,510**	27,990
St. Clare Commons Series 2012A	2042	3.17	**30,945**	31,720
St. Joseph Manor Series 1997B	2028	5.38	**13,895**	13,895
St. Joseph Regional Health Center Series 1993B	2019	6.0	**6,010**	8,760
St. Joseph Regional Health Center Series 1997A	2028	5.38	**36,472**	45,017
St. Joseph Regional Health Center Series 2014	2032	2.84	**25,255**	25,255

9. Debt Obligations (continued)

	Maturity Date	Interest Rates at June 30, 2017	2017	2016
Debt secured under the CHI COD (continued)				
Bank line of credit	7/2017	2.17%	**$ 250,000**	$ 250,000
Bank line of credit	–	–	**–**	200,000
Bank loan	12/2017	2.86	**333,741**	333,741
Commercial paper	2017	1.49	**815,519**	815,519
Unamortized debt premium and discount, net			**24,842**	31,580
Unamortized debt issuance costs			**(28,605)**	(31,295)
Total debt secured under the CHI COD			**7,940,796**	8,194,417
Other debt				
St. Leonard Master Trust Indenture	2040	6.0–6.63	**40,732**	41,892
Note payable issued to Episcopal Health Foundation	2020	4.0	**133,560**	167,053
Capital leases			**168,642**	166,150
Other debt			**418,680**	476,141
Total debt obligations			**8,702,410**	9,045,653
Less amounts classified as current:				
Variable-rate debt with self-liquidity			**(96,700)**	(96,700)
Commercial paper and current portion of debt			**(2,017,508)**	(1,768,028)
Long-term debt			**$ 6,588,202**	$ 7,180,925

The fair value of debt obligations was approximately $8.8 billion at June 30, 2017. Management has determined the carrying values of the variable-rate bonds are representative of fair values as of June 30, 2017, as the interest rates are set by the market participants. The fair value of the fixed-rate tax-exempt bond obligations is determined by applying credit spreads for similar tax-exempt obligations in the marketplace, which are then used to calculate a price/yield for the outstanding obligations (Level 2 inputs).

A summary of scheduled principal payments, based upon stated maturities, on debt obligations for the next five years is as follows (in thousands):

	Amounts Due
Year Ending June 30:	
2018	$ 2,114,208
2019	437,239
2020	180,950
2021	126,271
2022	130,410

9. Debt Obligations (continued)

CHI issues the majority of its debt under the COD and is the sole obligor. Bondholder security resides both in the unsecured promise by CHI to pay its obligations and in its control of its Direct and Designated Affiliates. Covenants include a minimum CHI debt service coverage ratio and certain limitations on secured debt. The Direct Affiliates of CHI, defined as Participants under the COD, have agreed to certain covenants related to corporate existence, maintenance of insurance and exempt use of bond-financed facilities. Effective in September 2016, CHI issued obligations under the COD to support the repayment of three series of previously outstanding Providence, Ohio, bonds (the Ohio bonds); the Ohio bonds were classified as other debt as of June 30, 2016, in the table above. There were no modifications to the payment terms or holders of the Ohio bonds.

Debt issued under the St. Leonard Master Trust Indenture is secured by the property of St. Leonard in Centerville, Ohio, and a pledge of gross revenues.

During March 2017, CHI's long-term credit ratings were adjusted to BBB+ with a stable outlook from Standard & Poor's, and to Baa1 with a negative outlook from Moody's. CHI's long-term credit rating from Fitch remains at BBB+ with a negative outlook.

Debt Redemptions and Reissuances

In February 2016, CHI redeemed $300.0 million of Series 2006C fixed-rate bonds. The bond redemption was funded by the issuance of a $333.7 million bank loan with an original maturity of December 2016, which was subsequently extended to December 2017. The bond redemption resulted in a loss on redemption of $30.5 million for the year ended June 30, 2016.

In August 2016, CHI redeemed $62.0 million of Series 2012A fixed-rate bonds in connection with the sale in the prior fiscal year of the underlying real estate assets. The bond redemption was funded from the real estate sale proceeds and resulted in a loss on redemption of $8.5 million included in losses on extinguishment of debt in the consolidated statement of operations.

In September 2016, CHI redeemed $37.1 million of bonds that were originally acquired as part of the LUH business combination in fiscal year 2016. The bond redemption was funded by the issuance of $34.1 million of commercial paper and restricted investments.

In December 2016, CHI issued $200.0 million of Series 2016 Taxable variable-rate bonds. Proceeds were used to repay the $200.0 million bank line of credit which matured in December 2016.

9. Debt Obligations (continued)

As discussed in Note 1, *Summary of Significant Accounting Policies-Notes Receivable and Other Assets*, in February 2017, Bethesda repaid its notes receivable to CHI for previously loaned funds. CHI used those proceeds in February and March 2017 to redeem $97.0 million of Series 2004 and Series 2009 fixed-rate bonds, and $33.0 million of Series 2015 variable-rate bonds. The bond redemption resulted in a loss on redemption of $7.7 million. Bethesda is no longer a Designated Affiliate in the CHI credit group under the COD.

In May 2017, CHI redeemed $38.8 million of bonds originally acquired in fiscal year 2016 as part of the Brazosport acquisition. The bond redemption was funded by $24.4 million of cash, restricted investments, and the issuance of $14.4 million in commercial paper, resulting in a loss on redemption of $3.4 million.

Liquidity Facilities, Credit Facilities, and Other Lines of Credit

CHI has external liquidity facilities totaling $365.0 million and $425.0 million at June 30, 2017 and 2016, respectively, which can be used to support CHI's obligations to fund tenders of variable rate demand bonds (VRDB) and to pay maturing principal of commercial paper.

At both June 30, 2017 and 2016, CHI classified as current $815.5 million of commercial paper due to maturities of less than one year and $96.7 million of VRDBs due to the holder's ability to put such VRDBs back to CHI on a daily basis, after providing a seven-day notice to tender.

At both June 30, 2017 and 2016, CHI had a credit facility with a third-party bank totaling $69.0 million, of which letters of credit totaling $63.8 million and $63.9 million, respectively, have been designated for the benefit of third parties, principally in support of the self-insurance programs administered by FIIL. No amounts were outstanding under this credit facility at June 30, 2017 and June 30, 2016.

At June 30, 2017 and 2016, CHI had $250.0 million and $450.0 million, respectively, of outstanding bank lines of credit which were classified as current due to maturities of less than one year. As previously disclosed, the $200.0 million line of credit matured in December 2016 and was funded by the issuance of $200.0 million of Series 2016 Taxable variable-rate bonds. The $250.0 million line of credit matured in July 2017 and was funded by the issuance of a new $250.0 million line of credit agreement with a third-party bank which matures in July 2018.

9. Debt Obligations (continued)

Interest Rate Swap Agreements

CHI utilizes various interest rate swap contracts to manage the risk of increased interest rates payable of certain variable-rate bonds. The fixed-payor swap agreements convert CHI's variable-rate debt to fixed-rate debt. Generally, it is CHI's policy that all counterparties have an AA rating or better. The swap agreements generally require CHI to provide collateral if CHI's liability, determined on a mark-to-market basis, exceeds a specified threshold that varies based upon the rating on CHI's long-term indebtedness.

The fair value of the swaps is estimated based on the present value sum of anticipated future net cash settlements until the swaps' maturities. Cash collateral balances are netted against the fair value of the swaps, and the net amount is reflected in other liabilities in the accompanying consolidated balance sheets. At June 30, 2017 and 2016, the net swap liability reflected in other liabilities was $28.9 million and $75.1 million, respectively, net of swap collateral posted of $259.1 million and $341.1 million, respectively. The change in the fair value of swap agreements was a net gain (loss) of $127.9 million and $(115.4) million for the years ended June 30, 2017 and 2016, respectively, reflected in realized and unrealized losses on interest rate swaps in the accompanying consolidated statements of operations.

Based upon the swap agreements in place as of June 30, 2017, a reduction in CHI's credit rating to BBB would obligate CHI to post additional cash collateral of $28.9 million. If CHI's credit rating were to fall below BBB, the swap counterparties would have the option to require CHI to settle the swap liabilities at the recorded fair value, which was $28.9 million as of June 30, 2017.

Following is a summary of interest rate swap contracts (in thousands):

		Swap Contracts Outstanding		**Fair Value Liability (Asset)**		**Notional Amount**	
	Maturity Date	**June 30, 2017**	**June 30, 2016**	**June 30, 2017**	**June 30, 2016**	**June 30, 2017**	**June 30, 2016**
Basis swaps	2028	**1**	1	**$ (374)**	$ (736)	**$ 30,000**	$ 30,000
Fixed-payer swaps	2024–2047	**15**	16	**286,882**	415,308	**1,411,223**	1,452,710
Total return swaps	2017–2020	**25**	29	**1,482**	1,705	**174,777**	223,337
		41	46	**$ 287,990**	$ 416,277	**$ 1,616,000**	$ 1,706,047

10. Retirement Plans

CHI Pension Plan

CHI and its direct affiliates maintain a variety of noncontributory, defined benefit retirement plans (Retirement Plans) for their employees. Certain of these plans were frozen in previous fiscal years, and benefits earned by employees through that time period remain in the Retirement Plans, where employees continue to receive interest credits and vesting credits, if applicable. Benefits in the Retirement Plans are based on compensation, retirement age, and years of service. Substantially all of the Retirement Plans are qualified as church plans and are exempt from certain provisions of both the Employee Retirement Income Security Act of 1974 and Pension Benefit Guaranty Corporation premiums and coverage. Funding requirements are determined through consultation with independent actuaries.

CHI recognizes the funded status (that is, the difference between the fair value of plan assets and the projected benefit obligations) of its Plans in the consolidated balance sheets, with a corresponding adjustment to net assets. Actuarial gains and losses that arise and are not recognized as net periodic pension cost in the same periods are recognized as a component of changes in net assets.

During fiscal year 2016, CHI acquired the pension plan assets and liabilities of Trinity (the Acquired plan) which is included below from the date of acquisition.

10. Retirement Plans (continued)

A summary of the changes in the benefit obligation, fair value of plan assets and funded status of the Plans at the June 30 measurement dates is as follows (in thousands):

	2017	2016
Change in benefit obligation:		
Benefit obligation, beginning of year	**$ 5,431,434**	$ 4,865,377
Service cost	**9,340**	15,518
Interest cost	**152,067**	201,192
Actuarial (gain) loss	**(146,604)**	634,831
Acquired plan	**–**	64,354
Plan amendments	**–**	(24)
Curtailments	**–**	(2,806)
Settlements	**(162,860)**	(58,111)
Benefits paid	**(103,315)**	(285,904)
Expenses paid	**(1,697)**	(2,993)
Benefit obligation, end of year	**5,178,365**	5,431,434
Change in the Plans' assets:		
Fair value of the Plans' assets, beginning of year	**3,895,594**	4,132,797
Actual return on the Plans' assets, net of expenses	**360,147**	68,999
Employer contributions	**79,513**	19,521
Acquired plan	**–**	47,946
Transfers	**–**	(26,746)
Settlements	**(162,860)**	(58,111)
Benefits paid	**(103,315)**	(285,819)
Expenses paid	**(1,697)**	(2,993)
Fair value of the Plans' assets, end of year	**4,067,382**	3,895,594
Funded status of the Plans	**$ (1,110,983)**	$ (1,535,840)
End-of-year values:		
Projected benefit obligation	**$ 5,178,365**	$ 5,431,434
Accumulated benefit obligation	**5,170,046**	5,422,498

10. Retirement Plans (continued)

Included in unrestricted net assets at June 30, 2017, are unrecognized actuarial losses of $1.3 billion that have not yet been recognized in net periodic pension cost. The actuarial losses included in unrestricted net assets and expected to be recognized in net periodic pension cost during the fiscal year ending June 30, 2017, total $44.8 million.

The components of net periodic pension expense (income) are as follows (in thousands):

	2017	2016
Components of net periodic pension expense (income):		
Service cost	**$ 9,340**	$ 15,518
Interest cost	**152,067**	201,192
Expected return on the Plans' assets	**(271,545)**	(274,718)
Actuarial losses	**60,182**	38,134
Settlements	**40,608**	26,157
	$ (9,348)	$ 6,283

The service cost, interest cost, expected return on the Plans' assets, actuarial losses, and amortization of prior service benefit components of net periodic pension expense (income) are recognized in the consolidated statements of operations within employee benefits expense. Curtailments and settlements components of net periodic pension expense (income) are recognized in the consolidated statements of operations within restructuring, impairment and other losses.

Effective on July 1, 2017, CHI changed the method used to estimate the service cost and interest cost components of net periodic pension cost to use a full yield curve "spot rate" approach that applies the specific spot rates along the yield curve to the plans' projected cash flows for certain benefit plans that had a remeasurement event during the year, the impact of which was immaterial. Additionally, for 2017 and going forward, CHI has determined that adopting the full yield curve "spot rate" approach for all other plans is preferable because it provides a more direct matching between the individual cash flows and the discount rates applied to those cash flows. As a result of this change in accounting method, service and interest costs decreased by approximately $34.9 million for the year ended June 30, 2017.

The assumption for the expected return on the Plans' assets is based on historical returns and adherence to the asset allocations set forth in the Plans' investment policies.

10. Retirement Plans (continued)

Weighted-average assumptions used to determine the pension benefit obligation for the years ended June 30 are as follows:

	2017	2016
Discount rate	**3.78%**	3.53%
Rate of compensation increase	**n/a**	n/a

The increase in the discount rate to 3.78% at June 30, 2017, decreased the pension benefit obligation by approximately $146.3 million.

Weighted-average assumptions used to determine the net periodic pension expense (income) for the years ended June 30 are as follows:

	2017	2016
Discount rate	**3.53%**	4.29%
Expected return on Plans' assets	**7.20**	7.20
Rate of compensation increase	**n/a**	n/a

CHI expects to contribute $114.3 million to the Plans in fiscal year 2018. A summary of expected benefits to be paid to the Plans' participants and beneficiaries is as follows (in thousands):

	Estimated Payments
Year Ending June 30:	
2018	$ 331,231
2019	280,908
2020	283,250
2021	286,590
2022	292,003
2023–2027	1,511,296

10. Retirement Plans (continued)

A summary of the Plans' assets at June 30 is as follows (in thousands):

	2017	2016
Assets		
Plans' interest in the CHI Master Trust	**$ 3,743,308**	$ 3,610,915
Investments in securities	**331,168**	319,782
Receivables for securities sold	**14,089**	2,580
Foreign currency exchange contracts	**20,455**	49,611
Other receivables	**6,497**	5,346
Total assets	**4,115,517**	3,988,234
Liabilities		
Payable for securities purchased	**27,324**	42,902
Foreign currency exchange contracts	**20,541**	49,671
Other liabilities	**270**	67
Total liabilities	**48,135**	92,640
Total Plans' assets	**$ 4,067,382**	$ 3,895,594

10. Retirement Plans (continued)

The Plans' financial instruments measured at fair value on a recurring basis were determined using the following inputs at June 30 (in thousands):

	2017			
	Fair Value Measurements at Reporting Date Using			
		(Level 1)	(Level 2)	(Level 3)
	Total	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs
Assets				
Cash and short-term investments	**$ 62,061**	**$ 55,925**	**$ 6,136**	**$ –**
Equity securities	**44,679**	**38,796**	**5,883**	**–**
Fixed-income securities	**224,428**	**47,209**	**173,068**	**4,151**
Investments in securities	**331,168**	**141,930**	**185,087**	**4,151**
Foreign currency exchange contracts	**20,455**	**–**	**20,455**	**–**
Total assets	**$ 351,623**	**$ 141,930**	**$ 205,542**	**$ 4,151**
Liabilities				
Foreign currency exchange contracts	**$ 20,541**	**$ –**	**$ 20,541**	**$ –**
Total liabilities	**$ 20,541**	**$ –**	**$ 20,541**	**$ –**

	2016			
	Fair Value Measurements at Reporting Date Using			
		(Level 1)	(Level 2)	(Level 3)
	Total	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs
Assets				
Cash and short-term investments	$ 34,511	$ 30,859	$ 3,652	$ –
Equity securities	33,288	25,800	7,488	–
Fixed-income securities	251,983	66,549	164,039	21,395
Investments in securities	319,782	123,208	175,179	21,395
Foreign currency exchange contracts	49,611	–	49,611	–
Total assets	$ 369,393	$ 123,208	$ 224,790	$ 21,395
Liabilities				
Foreign currency exchange contracts	$ 49,671	$ –	$ 49,671	$ –
Total liabilities	$ 49,671	$ –	$ 49,671	$ –

10. Retirement Plans (continued)

For the years ended June 30, 2017 and 2016, the changes in fair value of the Plans' investments in securities, for which Level 3 inputs were used, are as follows (in thousands):

	Fixed-income Securities
Investments at fair value at July 1, 2015	$ 22,629
Purchases/contributions of investments	6,429
Sales/distributions of investments	(8,573)
Net change in unrealized appreciation on investments and effect of foreign currency translation	625
Net realized gains on investments	285
Investments at fair value at June 30, 2016	21,395
Purchases/contributions of investments	**6,145**
Sales/distributions of investments	**(22,621)**
Net change in unrealized depreciation on investments and effect of foreign currency translation	**(172)**
Net realized losses on investments	**(596)**
Investments at fair value at June 30, 2017	**$ 4,151**

There were no significant transfers between Levels 1 and 2 during any period presented.

Certain of the Plans' investments are held in the CHI Master Trust, which was established for the investment of assets of the Plans. Each participating plan has an undivided interest in the CHI Master Trust. The CHI Master Trust assets are allocated among the participating plans by assigning to each plan those transactions (primarily contributions, benefit payments, and plan-specific expenses) that can be specifically identified and by allocating among all plans, in proportion to each plan's beneficial interest in the CHI Master Trust, income and expenses resulting from the collective investment of the assets of the CHI Master Trust.

The CHI Master Trust investment portfolio is designed to preserve principal and obtain competitive investment returns and long-term investment growth, consistent with actuarial assumptions, while minimizing unnecessary investment risk. Diversification is achieved by allocating assets to various asset classes and investment styles and by retaining multiple investment managers with complementary philosophies, styles and approaches. Although the objective of the

10. Retirement Plans (continued)

CHI Master Trust is to maintain asset allocations close to target, temporary periods may exist where allocations are outside of the expected range due to market conditions. The use of leverage is prohibited except as specifically directed in the alternative investment allocation. The portfolio is managed on a basis consistent with the CHI social responsibility guidelines.

A summary of the CHI Master Trust asset allocation targets, ranges by asset class and allocations by asset class within the CHI Master Trust at the measurement dates of June 30 is as follows:

	2017	2016	Target	Range
Equity securities	**48.2%**	46.0%	45.0%	35.0–55.0%
Fixed-income securities	**32.4**	33.9	35.0	25.0–45.0
Alternative investments	**19.4**	20.1	20.0	10.0–30.0

The CHI Master Trust allocation to alternative investments is based upon contractual commitment levels to various funds. These commitments are drawn by the fund managers as opportunities arise to invest the capital. As of June 30, 2017, the CHI Master Trust had committed to invest $380.5 million in 26 funds, of which $364.7 million had been invested. The remaining $15.8 million will be invested when, and if, requested by the funds. Alternative investments within the CHI Master Trust have limited liquidity and as of June 30, 2017, $125.0 million of investments are illiquid and not available for redemption, and $600.6 million of investments are available for redemption within 180 days at the request of the CHI Master Trust.

A summary of the CHI Master Trust's assets at June 30 is as follows (in thousands). At both June 30, 2017 and 2016, the Plans' interest in the net assets of the CHI Master Trust was approximately 99.9%.

10. Retirement Plans (continued)

	2017	2016
Assets		
Investments in securities	**$ 3,719,449**	$ 3,610,005
Receivables for securities sold	**68,884**	40,243
Foreign currency exchange contracts	**49,037**	57,155
Other receivables	**11,618**	10,499
Total assets	**3,848,988**	3,717,902
Liabilities		
Payable for securities purchased	**53,561**	46,641
Foreign currency exchange contracts	**49,408**	57,601
Other liabilities	**2,706**	2,742
Total liabilities	**105,675**	106,984
Total CHI Master Trust assets	**$ 3,743,313**	$ 3,610,918

The CHI Master Trust's financial instruments measured at fair value on a recurring basis were determined using the following inputs at June 30 (in thousands):

	2017					
			Fair Value Measurements at Reporting Date Using			
		Investments		(Level 1)	(Level 2)	(Level 3)
	Total	Measured at Net Asset Value (NAV)	Total	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs
Assets						
Cash and short-term investments	**$ 106,397**	**$ –**	**$ 106,397**	**$ 100,642**	**$ 5,755**	**$ –**
Equity securities	**1,710,426**	**–**	**1,710,426**	**1,707,864**	**2,562**	**–**
Fixed-income securities	**1,171,383**	**–**	**1,171,383**	**330,660**	**662,532**	**178,191**
Alternative investments	**731,243**	**731,243**	**–**	**–**	**–**	**–**
Investments in securities	**3,719,449**	**731,243**	**2,988,206**	**2,139,166**	**670,849**	**178,191**
Foreign currency exchange contracts	**49,037**	**–**	**49,037**	**–**	**49,037**	**–**
Total assets	**$ 3,768,486**	**$ 731,243**	**$ 3,037,243**	**$ 2,139,166**	**$ 719,886**	**$ 178,191**
Liabilities						
Foreign currency exchange contracts	**$ 49,408**	**$ –**	**$ 49,408**	**$ –**	**$ 49,408**	**$ –**
Total liabilities	**$ 49,408**	**$ –**	**$ 49,408**	**$ –**	**$ 49,408**	**$ –**

10. Retirement Plans (continued)

	2016					
			Fair Value Measurements at Reporting Date Using			
		Investments		(Level 1)	(Level 2)	(Level 3)
	Total	Measured at Net Asset Value (NAV)	Total	Quoted Prices in Active Markets	Other Observable Inputs	Unobservable Inputs
Assets						
Cash and short-term investments	$ 107,654	$ –	$ 107,654	$ 97,376	$ 10,278	$ –
Equity securities	1,609,188	–	1,609,188	1,605,648	3,540	–
Fixed-income securities	1,159,154	–	1,159,154	339,928	655,080	164,146
Alternative investments	734,009	734,009	–	–	–	–
Investments in securities	3,610,005	734,009	2,875,996	2,042,952	668,898	164,146
Foreign currency exchange contracts	57,155	–	57,155	–	57,155	–
Total assets	$ 3,667,160	$ 734,009	$ 2,933,151	$ 2,042,952	$ 726,053	$ 164,146
Liabilities						
Foreign currency exchange contracts	$ 57,601	$ –	$ 57,601	$ –	$ 57,601	$ –
Total liabilities	$ 57,601	$ –	$ 57,601	$ –	$ 57,601	$ –

For the years ended June 30, 2017 and 2016, the changes in fair value of the CHI Master Trust's investments, for which Level 3 inputs were used, are as follows (in thousands):

	Fixed-income Securities
Investments at fair value at July 1, 2015	$ 162,321
Purchases/contributions of investments	148,796
Sales/distributions of investments	(142,434)
Net change in unrealized depreciation on investments and effect of foreign currency translation	(2,205)
Net realized losses on investments	(2,332)
Investments at fair value at June 30, 2016	164,146
Purchases/contributions of investments	**166,065**
Sales/distributions of investments	**(155,094)**
Net change in unrealized appreciation on investments and effect of foreign currency translation	**5,556**
Net realized losses on investments	**(2,482)**
Investments at fair value at June 30, 2017	**$ 178,191**

10. Retirement Plans (continued)

There were no significant transfers between Levels 1 and 2 during any period presented.

CHI 401(k) Retirement Savings Plan

CHI sponsors the CHI 401(k) Retirement Savings Plan (401(k) Savings Plan) for its employees whereby CHI matches 100.0% of the first 1.0% of eligible pay an employee contributes to the plan, and 50.0% of the next 5.0% of eligible pay contributed to the plan, for a maximum employer matching rate of 3.5% of eligible pay. On an annual basis and regardless of whether or not an employee participates in the 401(k) Savings Plan, CHI will also contribute 2.5% of eligible pay to an employee's 401(k) Savings Plan account. This contribution is made if an employee reaches 1,000 hours in the first year of employment, or every calendar year thereafter, and is employed on the last day of the calendar year. An employee is fully vested in the plan for employer contributions after three years of service. CHI recorded 401(k) Savings Plan expense of $229.7 million and $209.4 million for the years ended June 30, 2017 and 2016, respectively, which is reflected in employee benefits expenses in the accompanying consolidated statements of operations.

11. Concentrations of Credit Risk

CHI grants credit without collateral to its patients, most of whom are insured under third-party payor agreements. CHI's exposure to credit risk on patient accounts receivable is limited by the geographical diversity of its MBOs. The mix of net patient accounts receivable at June 30 approximated the following:

	2017	2016
Medicare	**26%**	27%
Medicaid	**14**	11
Managed care	**33**	33
Self-pay	**10**	11
Commercial and other	**17**	18
	100%	100%

CHI maintains long-term investments with various financial institutions and investment management firms through its investment program, and its policy is designed to limit exposure to any one institution or investment. Management does not believe there are significant concentrations of credit risk at June 30, 2017 and 2016.

12. Commitments and Contingencies

Litigation

During the normal course of business, CHI may become involved in litigation. Management assesses the probable outcome of unresolved litigation and records estimated settlements. After consultation with legal counsel, management believes that any such matters will be resolved without material adverse impact to the consolidated financial position or results of operations of CHI.

Health Care Regulatory Environment

The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Management believes CHI is in compliance with all applicable laws and regulations of the Medicare and Medicaid programs. Compliance with such laws and regulations is complex and can be subject to future governmental interpretation as well as significant regulatory action, including fines, penalties and exclusion from the Medicare and Medicaid programs. Certain CHI entities have been contacted by governmental agencies regarding alleged violations of Medicare practices for certain services. In the opinion of management after consultation with legal counsel, the ultimate outcome of these matters will not have a material adverse effect on CHI's consolidated financial statements.

12. Commitments and Contingencies (continued)

Operating Leases

CHI leases certain real estate and equipment under operating leases, which may include renewal options and escalation clauses. Future minimum lease payments required for the next five years and thereafter for all operating leases that have initial or remaining noncancelable lease terms in excess of one year at June 30, 2017, are as follows (in thousands):

	Amounts Due
Year Ending June 30:	
2018	$ 219,753
2019	185,662
2020	163,378
2021	138,308
2022	116,542
Thereafter	2,230,385
	$ 3,054,028

Lease expense under operating leases for continuing operations for the years ended June 30, 2017 and 2016, totaled approximately $294.2 million and $272.4 million, respectively.

Capital Commitments

As of June 30, 2017, CHI has legally committed to fund $841.9 million of capital improvements related to certain acquisitions and affiliations.

13. Insurance Programs

FIIL, a wholly owned captive insurance company of CHI, provides hospital professional liability, employment practices liability, miscellaneous professional liability, and commercial general liability coverage, primarily to CHI healthcare providers and all employees, including employed physicians. Coverage is provided either on a directly written basis or through a reinsurance fronting relationship with commercial insurance carriers. Policies written provide coverage with primary limits in the amount of $10.0 million for each and every claim in fiscal years 2017 and 2016. For the policy year July 1, 2016 to July 1, 2017, there is an annual policy aggregate of $85.0 million eroded by hospital professional liability and commercial general liability claims, subject to a $175,000 continuing underlying per claim limit. Effective July 1, 2011, FIIL provided excess

13. Insurance Programs (continued)

umbrella liability coverage to CHI for claims in excess of the underlying limits discussed above. The limits provided under such excess coverage are $200.0 million per claim and in the aggregate. FIIL reinsured 100% of the excess layer with various commercial insurance companies. At June 30, 2017 and 2016, investments and assets limited as to use held for insurance purposes included $55.9 million and $59.9 million, respectively, held as collateral for the reinsurance fronting arrangement.

FIIL provided workers' compensation coverage to CHI entities on a directly written basis for the current and prior fiscal years, with limits of liability of $1 million per claim. FIIL did not reinsure this coverage for the current and prior fiscal years.

The liability for self-insured reserves and claims represents the estimated ultimate net cost of all reported and unreported losses incurred through June 30. The reserves for unpaid losses and loss adjustment expenses are estimated using individual case-based valuations, statistical analyses and the expertise of an independent actuary.

The estimates for loss reserves are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes that the reserves for unpaid losses and loss adjustment expenses are adequate. The estimates are reviewed periodically, with consultation from independent actuaries, and any adjustments to the loss reserves are reflected in current operations. As a result of these reviews of claims experience, estimated reserves were reduced by $63.3 million and $46.6 million in fiscal years 2017 and 2016, respectively. The reserves for unpaid losses and loss adjustment expenses relating to the workers' compensation program were discounted, assuming a 4.0% annual return at June 30, 2017 and 2016, to a present value of $155.5 million and $156.9 million at June 30, 2017 and 2016, respectively, and represented a discount of $50.2 million and $51.8 million in 2017 and 2016, respectively. Reserves related to professional liability, employment practices and general liability are not discounted.

FIIL holds $848.8 million and $809.8 million of investments held for insurance purposes as of June 30, 2017 and 2016, respectively. Distribution of amounts from FIIL to CHI are subject to the approval of the Cayman Island Monetary Authority. CHI established a captive management operation (Captive Management Initiatives, Ltd.) based in the Cayman Islands, which currently manages FIIL as well as operations of other unrelated parties.

13. Insurance Programs (continued)

CHI, through its Welfare Benefit Administration and Development Trust, provides comprehensive health and dental coverage to certain employees and dependents through a self-insured medical plan. Accounts payable and accrued expenses include $58.8 million and $63.7 million for unpaid claims and claims adjustment expenses for CHI's self-insured medical plan at June 30, 2017 and 2016, respectively. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes that the reserves for unpaid losses and loss adjustment expenses are adequate. The estimates are reviewed periodically and, as adjustments to the liability become necessary, such adjustments are reflected in current operations. CHI has stop-loss insurance to cover unusually high costs of care beyond a predetermined annual amount per enrolled participant.

14. Subsequent Events

CHI's management has evaluated events subsequent to June 30, 2017 through September 15, 2017, which is the date these consolidated financial statements were issued. There have been no material events noted during this period that would either impact the results reflected herein or CHI's results going forward, except as disclosed below.

In September 2017, CHI purchased the noncontrolling interest in KentuckyOne Health from the remaining partner for $150 million – see Note 4, *Acquisitions, Affiliations and Divestitures*.

During August 2017, CHI St. Luke's in Houston, Texas, was impacted by Hurricane Harvey, which caused the temporary closure and evacuation of certain area facilities for a few days. Although all hospitals in Houston, Texas, are now operational, CHI is evaluating the impact of the hurricane on its facilities and operations in the state.

Supplementary Information

Ernst & Young LLP
Suite 3300
370 17th Street
Denver, CO 80202

Tel: +1 720 931 4000
Fax: +1 720 931 4444
ey.com

Report of Independent Auditors on Supplementary Information

The Board of Stewardship Trustees
Catholic Health Initiatives

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements of Catholic Health Initiatives as a whole. The consolidating details appearing in conjunction with the financial statements are presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Ernst & Young LLP

September 15, 2017

Catholic Health Initiatives

Consolidating Balance Sheet
(In Thousands)

June 30, 2017

	MBOs	Corporate	FIIL	CHI Welfare Benefits Trust	Other	Eliminations and Adjustments	Consolidated
Assets							
Current assets:							
Cash and equivalents	$ 759,353	$ 177,590	$ 67	$ 19,567	$ 76,589	$ –	$ 1,033,166
Net patient accounts receivable, less allowance for bad debts of $1,024,099	2,168,221	–	–	–	–	(13,973)	2,154,248
Other accounts receivable	228,352	413,369	1,080	(93)	12,166	(403,737)	251,137
Current portion of investments and assets limited as to use	5,312	59,849	–	–	–	–	65,161
Inventories	302,406	–	–	–	–	–	302,406
Assets held for sale	396,935	–	–	–	185,409	–	582,344
Prepaid and other	76,738	76,350	6	–	532	–	153,626
Total current assets	3,937,317	727,158	1,153	19,474	274,696	(417,710)	4,542,088
Investments and assets limited as to use:							
Internally designated for capital and other funds	5,126,640	103,025	–	75,664	–	5,479	5,310,808
Mission and ministry fund	–	151,795	–	–	–	(25,000)	126,795
Capital resource pool	–	136,585	–	–	–	–	136,585
Held by trustees	16,707	60,143	–	–	–	–	76,850
Held for insurance purposes	15,090	–	848,753	–	13,079	–	876,922
Restricted by donors	257,738	657	–	–	116	–	258,511
Total investments and assets limited as to use	5,416,175	452,205	848,753	75,664	13,195	(19,521)	6,786,471
Property and equipment, net	7,867,403	687,832	–	–	14,078	–	8,569,313
Investments in unconsolidated organizations	647,633	1,025,372	–	–	15,522	(367,074)	1,321,453
Intangible assets and goodwill, net	459,537	14,300	–	–	–	–	473,837
Notes receivable and other	787,617	3,213,327	24,842	1,674	54	(3,788,926)	238,588
Total assets	$ 19,115,682	$ 6,120,194	$ 874,748	$ 96,812	$ 317,545	$ (4,593,231)	$ 21,931,750

Catholic Health Initiatives

Consolidating Balance Sheet (continued)

(In Thousands)

	MBOs	Corporate	FIIL	CHI Welfare Benefits Trust	Other	Eliminations and Adjustments	Consolidated
Liabilities and net assets							
Current liabilities:							
Compensation and benefits	$ 498,250	$ 127,021	$ –	$ 1,155	$ 16,197	$ –	$ 642,623
Third-party liabilities, net	85,087	–	–	–	–	–	85,087
Accounts payable and accrued expenses	1,618,020	352,646	6,448	58,759	71,687	(417,711)	1,689,849
Liabilities held for sale	47,402	–	–	–	118,333	–	165,735
Variable-rate debt with self-liquidity	–	96,700	–	–	–	–	96,700
Current portion of long-term debt	206,888	1,955,188	–	–	–	(144,568)	2,017,508
Total current liabilities	2,455,647	2,531,555	6,448	59,914	206,217	(562,279)	4,697,502
Pension liability	268,073	848,489	–	–	–	(5,579)	1,110,983
Self-insured reserves and claims	13,856	4,246	617,553	–	125	–	635,780
Other liabilities	498,687	672,841	–	–	1,021	–	1,172,549
Long-term debt	3,704,208	6,517,952	–	–	10,700	(3,644,658)	6,588,202
Total liabilities	6,940,471	10,575,083	624,001	59,914	218,063	(4,212,516)	14,205,016
Net assets:							
Net assets attributable to CHI	11,554,064	(4,540,869)	250,747	36,898	99,328	(352,263)	7,047,905
Net assets attributable to noncontrolling interests	310,395	85,540	–	–	–	(28,452)	367,483
Unrestricted	11,864,459	(4,455,329)	250,747	36,898	99,328	(380,715)	7,415,388
Temporarily restricted	213,656	440	–	–	154	–	214,250
Permanently restricted	97,096	–	–	–	–	–	97,096
Total net assets	12,175,211	(4,454,889)	250,747	36,898	99,482	(380,715)	7,726,734
Total liabilities and net assets	$ 19,115,682	$ 6,120,194	$ 874,748	$ 96,812	$ 317,545	$ (4,593,231)	$ 21,931,750

Catholic Health Initiatives

Consolidating Statement of Operations
(In Thousands)

Year Ended June 30, 2017

	MBOs	Corporate	FIIL	CHI Welfare Benefits Trust	Other	Eliminations and Adjustments	Consolidated
Revenues:							
Net patient services revenues	$ 14,634,150	$ –	$ –	$ –	$ –	$ (183,282)	$ 14,450,868
Other operating revenues:							
Donations	30,951	1	–	–	2	–	30,954
Changes in equity of unconsolidated organizations	8,318	(99,478)	–	–	2,401	137,163	48,404
Hospital ancillary revenues	336,467	48	–	–	2,557	–	339,072
Other	523,710	1,653,993	191,164	647,464	398,230	(2,736,395)	678,166
Total other operating revenues	899,446	1,554,564	191,164	647,464	403,190	(2,599,232)	1,096,596
Total operating revenues	15,533,596	1,554,564	191,164	647,464	403,190	(2,782,514)	15,547,464
Expenses:							
Salaries and wages	5,990,014	291,481	–	–	202,527	(189,188)	6,294,834
Employee benefits	1,336,787	40,328	32,314	664,064	56,090	(928,539)	1,201,044
Purchased services, medical professional fees, medical claims and consulting	2,542,714	856,627	11,970	3,173	149,661	(1,161,667)	2,402,478
Supplies	2,543,198	7,038	–	–	92	–	2,550,328
Utilities	190,201	19,987	–	–	97	–	210,285
Rentals, leases, maintenance and insurance	568,735	545,846	93,667	–	2,115	(309,091)	901,272
Depreciation and amortization	730,877	113,589	–	–	1,825	–	846,291
Interest	179,861	267,042	–	–	519	(151,946)	295,476
Other	1,176,052	47,412	486	2,190	9,641	(179,245)	1,056,536
Total operating expenses before restructuring, impairment and other losses	15,258,439	2,189,350	138,437	669,427	422,567	(2,919,676)	15,758,544
Income (loss) from operations before restructuring, impairment and other losses	275,157	(634,786)	52,727	(21,963)	(19,377)	137,162	(211,080)
Restructuring, impairment and other losses	161,986	199,850	6,715	–	5,616	–	374,167
Income (loss) from operations	113,171	(834,636)	46,012	(21,963)	(24,993)	137,162	(585,247)

Catholic Health Initiatives

Consolidating Statement of Operations (continued)
(In Thousands)

	MBOs	Corporate	FIIL	CHI Welfare Benefits Trust	Other	Eliminations and Adjustments	Consolidated
Nonoperating gains (losses):							
Investment gains (losses), net	$ 528,951	$ 46,541	$ 52,124	$ 5,524	$ (101)	$ 5,480	$ 638,519
Losses on extinguishment of debt	(3,408)	(16,178)	–	–	–	–	(19,586)
Realized and unrealized gains on interest rate swaps	7,506	85,192	–	–	–	–	92,698
Other nonoperating gains	1,553	–	–	–	–	453	2,006
Total nonoperating gains (losses)	534,602	115,555	52,124	5,524	(101)	5,933	713,637
Excess (deficit) of revenues over expenses	647,773	(719,081)	98,136	(16,439)	(25,094)	143,095	128,390
Excess (deficit) of revenues over expenses attributable to noncontrolling interest	32,989	(13,041)	–	–	–	–	19,948
Excess (deficit) of revenues over expenses attributable to CHI	$ 614,784	$ (706,040)	$ 98,136	$ (16,439)	$ (25,094)	$ 143,095	$ 108,442

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