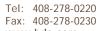
Consolidated Financial Statements As of and for the Years Ended June 30, 2017 and 2016 and Supplementary Information as of and for the Year Ended June 30, 2017



Consolidated Financial Statements
As of and for the Years Ended June 30, 2017 and 2016 and
Supplementary Information as of and for the Year Ended June 30, 2017

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Independent Auditor's Report

Board of Directors Verity Health System Redwood City, California

We have audited the accompanying consolidated financial statements of Verity Health System of California, Inc., which comprise the consolidated balance sheet as of June 30, 2017, and the related consolidated statements of operations and changes in net (deficit) assets and cash flows for the year 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 consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We did not audit the financial statements of Marillac Insurance Company, Ltd. (Marillac), a wholly-owned subsidiary, which statements reflect total assets of \$52,503,262 at June 30, 2017 and total revenues of \$12,635,815 for the year then ended. Those statements were audited by other auditors, whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for such subsidiary, is based solely on the report of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

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

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Opinion

In our opinion, based on our audit and the report of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Verity Health System of California, Inc. as of June 30, 2017, and the consolidated results of its operations, and the changes in its net (deficit) assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

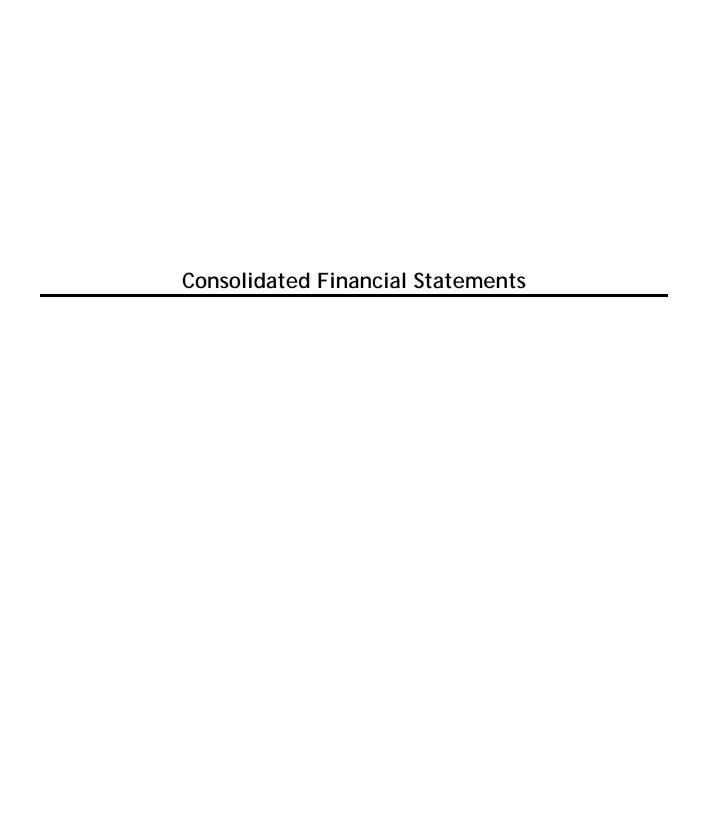
Other Matters

The consolidated financial statements of Verity Health System of California, Inc. for the year ended June 30, 2016 were audited by other auditors, whose report dated December 8, 2016 expressed an unmodified opinion on those statements.

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidating financial statement schedules for Verity Health System of California, Inc. are presented for purposes of additional analysis and are 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 consolidated financial statements. The consolidating information has been subjected to the auditing procedures applied in the audit 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 consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidating information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

BDO USA, LLP

November 8, 2017



Consolidated Balance Sheets (In Thousands)

luna 20		2017		2017
June 30,		2017		2016
Assets				
Current Assets: Cash and cash equivalents	\$	60,647	\$	66,357
Patient accounts receivable, net of allowance for	φ	00,047	φ	00,337
doubtful accounts of \$47,600 and \$31,700				
as of June 30, 2017 and 2016, respectively		235,767		160,324
Due from government agencies		15,938		20,137
Other current assets		95,192		106,273
Other restricted assets		-		12,074
Total current assets		407,544		365,165
Assets Limited as to Use:				
Other investments		61,181		112,243
Under bond indenture agreements		63,493		25,154
Total assets limited as to use		124,674		137,397
Property and equipment, net		247,042		244,912
Other long-term assets		25,085		5,878
Total Assets	\$	804,345	\$	753,352
Liabilities and Net (Deficit) Assets				
Current Liabilities:				
Accounts payable	\$	74,577	\$	36,362
Accrued expenses and other current liabilities		254,129		217,403
Current portion of long-term debt, net of debt issuance costs		12,480		6,647
Due to government agencies		5,299		1,155
Total current liabilities		346,485		261,567
Pension obligations		254,002		301,527
Long-term portion of workers' compensation and		36,142		33,547
hospital professional and general liability Other long-term liabilities		42,692		33,366
Long-term debt - net of current portion and debt issuance costs		459,156		375,873
Total liabilities		1,138,477		1,005,880
Net (Deficit) Assets:				
Unrestricted - Verity Health System		(358,144)		(333,995)
Unrestricted - Noncontrolling		2,366		-
Temporarily restricted		13,444		73,330
Permanently restricted		8,202		8,137
Total net deficit		(334,132)		(252,528)
Total Liabilities and Net (Deficit) Assets	\$	804,345	\$	753,352

See accompanying notes to consolidated financial statements.

Consolidated Statements of Operations and Changes in Net (Deficit) Assets (In Thousands)

Years Ended June 30,	2017	2016
Unrestricted Revenues and Other Support		
Net patient service revenue	\$ 1,301,005	\$ 1,161,679
Provision for doubtful accounts	(33,770)	(26,734)
Net patient service revenue less provision for		
doubtful accounts	1,267,235	1,134,945
doubtral accounts	1,207,233	1,134,743
Premium revenue	120,293	122,849
Other operating revenue	26,304	22,962
Contributions	65,717	16,645
Total unrestricted revenues and other support	1,479,549	1,297,401
Expenses:		
Salaries and benefits	730,299	723,281
Purchased services and other	476,892	471,901
Supplies	172,392	165,417
Medical claims	61,959	65,380
Depreciation and amortization	34,918	48,308
Interest - net	28,134	20,593
Goodwill and intangible asset impairment loss	10,232	
Total expenses	1,514,826	1,494,880
Operating loss	(35,277)	(197,479)
Investment (loss) income	(2,573)	2,050
(Deficit) excess of revenues over expenses	(37,850)	(195,429)
Less (deficit) excess of revenues over expenses attributable		
to noncontrolling interest	(5,087)	
(Deficit) excess of revenues over expenses, net of		
noncontrolling interest	\$ (32,763)	\$ (195,429)

(Continued)

See accompanying notes to consolidated financial statements.

Consolidated Statements of Operations and Changes in Net (Deficit) Assets (In Thousands)

Years Ended June 30,	2017	2016
Unrestricted Net (Deficit) Assets		
Unrestricted Net (Deficit) Assets attributable to Verity Health Sys (Deficit) excess of revenues over expenses attributable to	stem:	
Verity Health System \$ Change in funded status of pension and other postretirement	(32,763)	\$ (195,429)
benefit plans Net assets released from restrictions used for purchase	7,667	(53,981)
of property and equipment Other	610 337	1,882 (58)
Decrease in unrestricted net (deficit) assets attributable to Verity Health System	(24,149)	(247,586)
Unrestricted Net Assets attributable to noncontrolling interests: (Deficit) excess of revenues over expenses attributable to		
noncontrolling interests Noncontrolling interest related to acquisitions and other	(5,087) 7,453	- -
Increase in unrestricted net assets attributable to noncontrolling interest	2,366	_
Temporarily Restricted Net (Deficit) Assets Contributions	5,309	76,152
Net realized and unrealized gains on investments Net assets released from restrictions:	173	12
Operations Property, plant, and equipment Other	(64,551) (610) (207)	(16,275) (1,780) (232)
(Decrease) increase in temporarily restricted net (deficit) assets	(59,886)	57,877
Permanently Restricted Net Assets Net realized and unrealized gains (losses) on investments Contributions Other	65 - -	(73) 107 (104)
Increase (decrease) in permanently restricted net assets	65	(70)
Decrease in net (deficit) assets	(81,604)	(189,779)
Net (deficit) assets, beginning of year	(252,528)	 (62,749)
Net (Deficit) Assets, End of Year \$	(334,132)	\$ (252,528)

(Concluded)

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows (In Thousands)

Years Ended June 30,	2	017	2016
Operating Activities			
Decrease in net (deficit) assets	\$ (81,604)	\$ (189,779)
Adjustments to reconcile decrease in net (deficit) assets to net cash			
used in operating activities:			
Depreciation and amortization		34,918	48,397
Provision for doubtful accounts		33,770	26,734
Changes in fair value and unrealized and realized losses (gains)		(a aa ()	(4.000)
on investments, net		(3,896)	(1,330)
Losses (gains) on equity method investments		7,016	- (00)
Amortization of bond premium and debt issuance costs		692	(89) 53,981
Pension related changes		(7,667)	(2,584)
Gain on disposal of property and equipment Goodwill and intangible asset impairment		(4,503) 10,232	(2,364)
Changes in operating assets and liabilities:		10,232	-
Patient accounts receivable	(1	09,213)	(30,310)
Due to/from government agencies	(1	8,344	(1,748)
Other current assets		26,093	77,983
Other long-term assets		36,525	(47,299)
Accounts payable and other accrued expenses		73,091	(25,968)
Non-current liabilities		35,979)	6,637
Net cash used in operating activities		12,181)	(85,375)
Investing Activities			
Purchases of investments	(78,254)	(250,547)
Acquisitions of controlled entities	·	(8,208)	-
Purchases of equity method investments		(7,297)	-
Proceeds from disposal of property and equipment		4,778	4,388
Proceeds from sales of investments		86,719	251,518
Changes in other assets limited as to use		(2,932)	216
Changes in assets under bond indenture agreements	(38,339)	718
Changes in loans and receivables		(2,164)	-
Purchases of property and equipment	(34,393)	(12,357)
Net cash used in investing activities	(80,090)	(6,064)
Financing Activities			
Retirement of debt		-	(47,643)
Repayment of debt		(7,099)	(6,779)
Issuance of debt		95,000	105,000
Bond issuance costs		(1,340)	(1,212)
Net cash provided by financing activities		86,561	49,366
Net (decrease) increase in cash and cash equivalents		(5,710)	(42,073)
Cash and cash equivalents at beginning of year		66,357	108,430
Cash and Cash Equivalents at End of Year	\$	60,647	\$ 66,357
Supplemental Disclosures of Cash Flow Information			
Cash paid for interest - net of capitalized interest	\$	26,319	\$ 20,593
Supplemental Disclosures of Noncash Items			
Capitalized interest	\$	907	\$ 350
Assets acquired through capital leases or notes payable	\$	1,862	\$ -
Accrued purchases of property and equipment	\$	3,526	\$ 555

 ${\it See \ accompanying \ notes \ to \ consolidated \ financial \ statements}.$

Notes to Consolidated Financial Statements (All amounts in Thousands)

1. Organization and Business of the Company

Verity Health System of California, Inc., a California nonprofit public benefit corporation (Parent) (formerly named Daughters of Charity Health System) is the sole corporate member of five California nonprofit public benefit corporations that operate five acute care hospitals and other facilities (the Hospitals, see list below) in the state of California. The Parent and the following affiliated entities (collectively, Verity Health System or VHS) operate as a nonprofit health care system in the state of California, with approximately 1,680 licensed acute care and skilled nursing beds.

Verity Health System consists of Parent* and the following:

- O'Connor Hospital *
- Saint Louise Regional Hospital *
- St. Francis Medical Center *
- St. Vincent Medical Center *
- Seton Medical Center (including its unincorporated division, Seton Medical Center Coastside) *
- Verity Business Services
- Marillac Insurance Company, Ltd.
- O'Connor Hospital Foundation
- Saint Louise Regional Hospital Foundation
- St. Francis Medical Center Foundation
- St. Vincent Medical Center Foundation
- Seton Medical Center Foundation
- St. Vincent de Paul Ethics Corporation
- St. Vincent Dialysis Center
- De Paul Ventures, LLC
- Verity Medical Foundation
- Verity Holdings, LLC
- Verity BASM Holdco, LLC

With the exceptions of De Paul Ventures, LLC, Marillac Insurance Company, Ltd. (Marillac) and Verity BASM Holdco, LLC, each Verity Health System entity named above is exempt from federal income taxation as an organization described in Section 501(c)(3) of the Internal Revenue Code of 1986 (IRC).

On July 17, 2015, Daughters of Charity Ministry Services Corporation (subsequently renamed Verity Health System of California, Inc.), Blue Mountain Capital Management, LLC (Blue Mountain), and Integrity Healthcare, LLC (Integrity) entered into a System Restructuring and Support Agreement (as subsequently amended, the Restructuring Agreement) to change the governance of and recapitalize the Parent and certain of its subsidiaries. Integrity represents the management company for Verity Health System that was formed to carry out the management services under the Management Agreement, which is part of the overall Restructuring Agreement. Through June 30, 2017, Integrity was wholly owned by Blue Mountain. In July 2017, NantWorks LLC, the parent

^{*} Member of the Obligated Group

Notes to Consolidated Financial Statements (All amounts in Thousands)

organization for health technology and biotech companies founded by Dr. Patrick Soon-Shiong, acquired a majority stake in Integrity from Blue Mountain. Refer to subsequent events at Note 13 for additional details.

Under the Restructuring Agreement, the Parent and other members of the Obligated Group were converted from religious corporations to public benefit corporations. In exchange for options to acquire the assets of Verity Health System at a purchase price to be determined based on a specified percentage of outstanding liabilities of Verity Health System at the time of closing, Blue Mountain agreed to provide \$100,000 in funding to the Parent and a commitment to provide additional debt financing at the option of the Parent. To fulfill this commitment, Blue Mountain arranged for an additional \$160,000 in working capital financing that was privately placed with third parties (the "2015 Notes" - see Note 9 for additional details). After approval was obtained from the California Attorney General's office, the transactions contemplated by the Restructuring Agreement closed on December 14, 2015. Effective upon the closing of the transaction, the Parent's board of directors resigned and Daughters of Charity Ministry Services Corporation, acting as sole corporate member of the Parent, appointed an independent board of the Parent and amended the bylaws of the Parent to eliminate the corporate membership rights of Daughters of Charity Ministry Services Corporation as sole corporate member of the Parent and to convert the Parent into a nonprofit corporation without members. The Parent and all of its nonprofit corporate affiliates that were not previously public benefit corporations changed status from religious corporations to public benefit corporations under the California Nonprofit Corporation Law.

In connection with the initial accounting for the \$100,000 Blue Mountain contribution received during the fiscal year ended June 30, 2016, \$27,559 was recorded as deferred revenue for the value of the option to purchase the real estate and operating assets of VHS and \$72,441 was recorded as a restricted asset for contributions to be released pursuant to the terms of the Restructuring Agreement. For the years ended June 30, 2017 and 2016, VHS recorded approximately \$60,367 and \$12,074 of contribution revenue, respectively, associated with the releases of these funds from restrictions. \$27,559 is recorded as deferred revenue in other long-term liabilities as of June 30, 2017, as such amount will be recognized upon exercise or expiration of the option.

On a monthly basis, VHS records management fee expense and makes payments to Integrity associated with the management services received under the Management Agreement. During the initial fiscal year which ended June 30, 2016, the monthly management fee was determined based on a specified percentage of trailing 12 month operating revenues for VHS. Such management fees are adjusted each succeeding fiscal year based on changes in the consumer price index. VHS defers payment for a portion of management fees based on its days' cash on hand over the most recent 90 day period. All deferred management fees accrue interest at 2.82% per annum to the extent such amounts are not paid in the fiscal year that services are received. Such deferred management fees are contingently payable based on the terms of the Management Agreement, which include annual calculations of excess cash on hand.

For the years ended June 30, 2017 and 2016, VHS recorded approximately \$59,333 and \$32,215 of management fee expense within the purchased services and other expense line item, respectively. As of June 30, 2017 and 2016, VHS had a liability of \$46,228 and \$16,108 within accrued expenses and other current liabilities, respectively, associated with deferred management fees.

Notes to Consolidated Financial Statements (All amounts in Thousands)

Pursuant to the Master Indenture of Trust, dated as of December 1, 2001 (as amended and supplemented, the Master Indenture) among the Members of the Obligated Group and U.S. Bank National Association (Master Trustee), an Obligated Group (see listing of entities included in the Obligated Group above) was established to access the capital markets. Obligated Group members are jointly and severally liable for the long-term debt outstanding secured by an Obligation issued under the Master Indenture.

Liquidity

VHS had working capital of \$61,059 and \$103,598 as of June 30, 2017 and 2016, respectively. VHS had a deficit of revenues over expenses of \$37,850 and cash used in operations of \$12,181 for the year ended June 30, 2017 compared to a deficit of revenues over expenses of \$195,429 and cash used in operations of \$85,375 for the year ended June 30, 2016. The current year deficit of revenues over expenses and cash used in operations represented an improvement of \$157,579 and \$73,194, respectively, from the prior year. Such improvements have been largely driven by increases in patient volumes, additional reimbursement under the California Hospital Fee Program (see Note 2 for details), and overall cost-cutting initiatives that have been implemented. Additionally, VHS has been successful in raising additional financing, which includes issuance of the 2017 Notes for \$21,000 in September 2017 and the MOB Loan for \$46,220 in October 2017 (see subsequent events at Note 13 for additional details). Management believes that cash flows from operations and financing activities will provide sufficient capital resources to sustain operations through at least the next twelve months from the date the financial statements were issued.

2. Summary of Significant Accounting Policies

Basis for Presentation

The accompanying consolidated financial statements are prepared in conformity with U.S. generally accepted accounting principles and include the accounts of VHS after elimination of intercompany transactions. Certain reclassifications and changes in presentation were made in the 2016 consolidated financial statements to conform to the 2017 presentation. See the recent accounting pronouncements section below for additional details. All amounts in the consolidated financial statements and footnotes are presented in thousands.

Use of Estimates

The preparation of the consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make certain estimates and assumptions that affect the reported amounts of assets, liabilities, and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. VHS considers critical accounting policies to be those that require more significant judgments and estimates in the preparation of its consolidated financial statements, including the following: recognition of net patient service revenue, which includes contractual allowances and discounts; provisions for doubtful accounts and charity care; assumptions for measurement of pension and other postretirement liabilities; and reserves for losses and expenses related to hospital professional and general liabilities, workers' compensation claims and out-of-

Notes to Consolidated Financial Statements (All amounts in Thousands)

network services associated with certain at-risk capitation arrangements. Management bases its estimates on historical experience and various other assumptions that it believes are reasonable under the particular facts and circumstances. Actual results could differ materially from those estimates.

Medical Foundation

The VHS Medical Foundation was established in December 2011 and incorporated under the California regulations as a not-for-profit corporation exempted from income taxes under IRC Section 501(c)(3). The sole member of this corporation is VHS, acting through its board of directors.

Cash and Cash Equivalents

Cash equivalents consist primarily of highly liquid marketable securities with original maturities, at the time of purchase, of three months or less.

Patient Accounts Receivable, Allowance for Doubtful Accounts, and Net Patient Service Revenue

Patient accounts receivable and net patient service revenue are reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, including estimated settlements under reimbursement agreements with third-party payers. Settlements with third-party payers are accrued on an estimated basis in the period in which the related services are rendered and are adjusted in future periods as final settlements are determined.

VHS manages the receivables by regularly reviewing its patient accounts and contracts and by providing appropriate contractual allowances and allowances for doubtful accounts. These allowances are estimated based upon an evaluation of historical payments, negotiated contracts, and governmental reimbursements. Adjustments and changes in estimates are recorded in the period in which they are determined. The gross self-pay accounts receivable was reserved at 92% and 90% at June 30, 2017 and 2016, respectively, in total between the allowance for doubtful accounts and contractual allowances.

Patient service revenues, net of contractual allowances and discounts, are as follows:

Year Ended June 30,	2017	2016
Government Contracted Self-pay and others	\$ 913,460 333,258 54,287	\$ 780,884 332,686 48,109
Net patient service revenue Less: Provision for doubtful accounts	1,301,005 (33,770)	1,161,679 (26,734)
Net patient service revenue less provision for doubtful accounts	\$ 1,267,235	\$ 1,134,945

Net patient service revenue includes contractual and other allowances (excluding charity care) of \$5,260,897 and \$4,676,402 for the years ended June 30, 2017 and 2016, respectively.

Notes to Consolidated Financial Statements (All amounts in Thousands)

Significant concentrations of net patient accounts receivable are as follows:

As of June 30,	2017	2016
HMO/PPO/Commercial	40%	42%
Medicare	25	29
Medi-Cal	32	28
Other	3	1
Total	100%	100%

Inpatient acute care services, outpatient services, and skilled nursing services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Certain inpatient non-acute services and defined capital and medical education costs related to Medicare beneficiaries are paid using a cost reimbursement methodology.

Health care services are provided free of charge or at a significant discount based on a sliding scale to individuals who meet certain financial criteria. VHS makes an effort to determine if a patient qualifies for charity care upon admission. If a patient is determined to qualify for charity care, services are rendered to the patient free of cost. The costs of providing these services are included in unsponsored community benefit expense and included as a deduction to net patient service revenue in the consolidated statement of operations. VHS estimates the cost of charity care by calculating a ratio of cost to usual and customary charges and applying that ratio to the usual and customary uncompensated charges associated with providing care to patients that qualify for charity care. The amount of charity care at cost was \$10,444 and \$13,981 for the years ended June 30, 2017 and 2016, respectively.

After satisfaction of amounts due from insurance and the application of financial discounts to patients' balances, and after exhausting all reasonable efforts to collect from the patients, a significant portion of VHS's uninsured and self-pay patient accounts are referred to third-party agencies based on VHS's established guidelines for further collection activities. As a result, VHS records a significant provision for doubtful accounts related to these uninsured patients in the period the services are rendered based on historical collection experience.

As part of VHS's mission to serve the community, VHS provides care to patients even though they may lack adequate insurance or may participate in programs that do not pay full charges. Reserves for charity care and uncollectible amounts have been established and are netted against patient accounts receivable in the consolidated balance sheets.

Payments from Medi-Cal and contracted-rate payers are based on a per-diem, per-discharge, modified cost, or capitated basis or a combination of these.

Notes to Consolidated Financial Statements (All amounts in Thousands)

Adjustments for the finalization of prior year cost reports from both Medicare and Medi-Cal resulted in an increase to patient service revenues of \$4,402 and \$5,613, for the years ended June 30, 2017 and 2016, respectively. St. Francis Medical Center qualified for and received Medi-Cal funding as a disproportionate-share hospital from the state of California under Senate Bill (SB) 855. Related revenues were \$30,542 and \$27,029, for the years ended June 30, 2017 and 2016, respectively, and are included in net patient service revenue. Amounts to be received in future years, if any, are subject to annual determination.

The St. Francis Medical Center also received funding for Medi-Cal disproportionate-share hospitals under SB 1255. These SB 1255 funds are paid from the Emergency Services and Supplemental Payments Fund. Related revenues were \$8,040 and \$7,908, for the years ended June 30, 2017 and 2016, respectively, and are included in net patient service revenue. This funding must be applied for and approved each year.

The St. Francis Medical Center also qualifies for Medi-Cal funding as a disproportionate-share hospital from the state of California under SB 1732. This SB 1732 program permits health care facilities servicing a disproportionate share of Medi-Cal patients to receive supplemental reimbursement for a portion of their debt service for qualified capital projects. St. Francis Medical Center has an amendment to its Medi-Cal contract, which was executed on June 19, 1993, for reimbursement related to the St. Francis Medical Center Health Services Pavilion, which was completed in 1991. Related revenues were \$2,213 and \$2,220, for the years ended June 30, 2017 and 2016, respectively, and are included in net patient service revenue.

Other than St. Francis Medical Center, no other VHS entities received funding under SB 855, SB 1255 or SB 1732 for the years ended June 30, 2017 and 2016.

Inventories

Inventories consist of supplies and are stated at the lower of cost or market value, which is determined using the first-in, first-out method. Inventories are reviewed for obsolescence on a periodic basis. Amounts are included in other current assets.

Assets Limited as to Use

Assets limited as to use represent assets designated by the board of directors for future capital improvements, assets at Marillac designated by the board of directors for payment of workers' compensation and hospital professional and general liability claims, assets held by trustees under bond indenture agreements (refer the Series 2005 Bonds, Series 2015 Notes, and 2017 Assessment C-PACE Bonds at Note 9), and investments restricted by donors. Investment income or loss is included in deficiency of revenues over expenses, unless the income or loss is restricted by donor or law. The assets are reflected in the assets limited as to use line items in the consolidated balance sheets.

Investments

Investments received through gifts are recorded at estimated fair value at the date of donation. Gains and losses that result from market fluctuations are recognized in the period that such fluctuations occur. Realized gains or losses resulting from sales or maturities are calculated on an adjusted-cost basis. Adjusted-cost is the original cost of the security adjusted for any purchases or sales during the year. Dividend and interest income are accrued when earned.

Notes to Consolidated Financial Statements (All amounts in Thousands)

VHS also maintains ownership interests in certain entities that are recorded under the equity method of accounting as VHS has the ability to exercise significant influence over the operating and financial policies of the investee. Equity method investments are recorded as other long-term assets in the consolidated balance sheet and earnings or losses associated with equity method investments are recorded as investment income (loss) in the consolidated statement of operations and changes in net assets.

Investment (loss) income includes the following:

Years Ended June 30,	2017	2016
Interest and dividends	\$ 953	\$ 867
Investment fees	(168)	(208)
Change in unrealized gains (losses) on investments - net	(1,489)	775
Net realized gains on sales of investments	5,385	555
Equity method investments - other-than-temporary impairment		
losses	(3,310)	-
Equity method investments - guarantee losses	(3,588)	-
Equity method investments - share of earnings (losses)	(118)	-
	(2,335)	1,989
Amounts included in changes in temporarily restricted net assets	(173)	(12)
	• •	, ,
Amounts included in changes in permanently restricted net assets	(65)	73
Investment (loss) income	\$ (2,573)	\$ 2,050

During the year ended June 30, 2017, VHS recorded other-than-temporary impairment losses of \$3,310 associated with the decline in the fair value of certain surgery center investments that were purchased in January 2017. The decline in fair value resulted from the degradation in future estimated cash flows due to adverse changes in business conditions that occurred subsequent to the acquisition date. See Note 3 for additional details related to the initial purchase of non-controlling ownership interests in the surgery centers and a controlling ownership interest in the management company, Verity BASM Holdco, LLC. See Note 4 for additional details on the valuation methodology utilized to determine the fair value of the surgery center investments as of June 30, 2017.

During the year ended June 30, 2017, VHS also recorded investment losses of \$3,588 associated with the guarantee of certain outstanding legal obligations on behalf of the surgery center equity method investees. See Note 3 for additional details on the terms of the guarantee. As of June 30, 2017, VHS estimated the fair value of the guarantee obligation to be \$4,760, which resulted in the recording of a guarantee liability within other long-term liabilities. As this guarantee obligation was determined to represent an additional contribution to the investees, \$1,172 was recorded as an increase in carrying value of VHS's equity method investment associated with VHS's portion of the investment and \$3,588 was recorded as an investment loss associated with the non-contributing investees' portion of the investment. See Note 4 for additional details on the valuation methodology utilized to determine the fair value of the guarantee as of June 30, 2017.

Notes to Consolidated Financial Statements (All amounts in Thousands)

Fair Value of Financial Instruments

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, accounts receivable, accounts payable, accrued expenses, and due to/from government agencies approximate fair value due to their short-term nature. The fair value of investments is disclosed in Notes 4 and 8, and the fair value of debt is disclosed in Note 9.

Property and Equipment

Property and equipment are stated at cost if purchased, and at fair market value if donated. Depreciation of property and equipment is calculated using a half-year convention and the straight-line method for financial statement purposes. Estimated useful lives by classification are as follows:

Land improvements	5-25 years
Buildings	10-40 years
Building service equipment	5-25 years
Equipment	3-20 years
Software development	3-5 years

Long-Lived Asset Impairment

VHS routinely evaluates the carrying value of its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset, or related group of assets, may not be recoverable from estimated future undiscounted cash flows generated by the underlying tangible assets. When the carrying value of an asset exceeds the estimated recoverability, an asset impairment charge is recognized. The impairment tests are based on financial projections prepared by management that incorporate anticipated results from programs and initiatives being implemented and market value assessments of the assets. If the projections are not met, or if negative trends occur that impact the future outlook, the value of the long-lived assets may be impaired, which could be material. There was no long-lived asset impairment recorded for the years ended June 30, 2017 and 2016 associated with tangible assets.

VHS recorded an impairment loss of \$6,858 associated with long-lived management contract intangible assets for the year ended June 30, 2017, which is included in goodwill and intangible asset impairment loss in the consolidated statement of operations and changes in net assets. See Note 3 for additional details.

Self Insurance

VHS is self-insured for hospital professional and general liabilities by a wholly-owned self-insured captive insurance company (Marillac). The provisions for estimated hospital professional and general liability claims include estimates of the ultimate costs for both uninsured reported claims and claims incurred-but-not-reported (IBNR), in accordance with actuarial projections or paid claims lag models based on past experience. Such claim reserves are based on the best data available to VHS; however, these estimates are subject to a significant degree of inherent variability. There is at least a reasonable possibility that a material change to the estimated reserves will occur in the near term. Such estimates are continually monitored and reviewed, and as reserves are adjusted, the

Notes to Consolidated Financial Statements (All amounts in Thousands)

differences are reflected in current operations. Management is of the opinion that the associated liabilities recognized in the accompanying consolidated financial statements are adequate to cover such claims.

VHS has entered into reinsurance, stop loss, and excess policy agreements with independent insurance companies to limit its losses on hospital professional and general liability claims.

Hospital professional and general liabilities (HPL/GL) were \$18,723 and \$16,802, discounted at a rate of 4% as of June 30, 2017 and 2016, respectively. Management is not aware of any potential hospital professional and general liability claims whose settlement would have a material adverse effect on VHS's consolidated financial position.

Workers' Compensation Insurance

VHS is insured for workers' compensation claims with major independent insurance companies, subject to certain deductibles of \$500 per occurrence as of June 30, 2017 and 2016. Based on actuarially determined estimates, provisions have been made in the consolidated financial statements, with the current portion included within accrued liabilities and the non-current portion within workers' compensation and hospital professional and general liabilities, for all known claims and IBNR claims as of June 30, 2017 and 2016. Workers' compensation liabilities were \$26,274 and \$24,752, discounted using a rate of 4%, as of June 30, 2017 and 2016, respectively. Estimation differences between actual payments and amounts recorded in previous years are recognized as expense in the year such amounts become determinable.

IBNR Claims under Premium Revenue Arrangements

Certain entities of VHS have capitation arrangements with various payers to provide medical services to enrollees. VHS accrues costs when services are rendered under these contracts, including estimates of IBNR claims and amounts receivable/payable under risk-sharing arrangements. The IBNR accrual includes an estimate of the costs for which VHS is responsible, including out-of-network services. The IBNR reserves are reported in accrued expenses and other current liabilities in the consolidated balance sheets (see Note 7 for additional information). Medical claims expense associated with premium revenue arrangements is separately reported in the consolidated statement of operations and changes in net (deficit) assets.

IBNR reserves are estimated based on actuarial studies, historical reporting, and payment trends. Subsequent actual claims experience will differ from the estimated liability due to variances in estimated and actual utilization of health care services, the amount of charges, and other factors. As settlement are made and estimates are revised, the differences are reflected in current operations.

Notes to Consolidated Financial Statements (All amounts in Thousands)

The following table presents the roll-forward of the medical claims and IBNR liabilities as of and for each of the fiscal years ended June 30, 2017 and 2016:

June 30,	2017	2016
Medical claims and IBNR liabilities as of beginning of year Claims expenses incurred during the year Claims paid during the year	\$ 31,415 61,959 (61,477)	\$ 35,556 65,380 (69,521)
Medical claims and IBNR liabilities as of end of year	\$ 31,897	\$ 31,415

Asset Retirement Obligations (AROs)

AROs are legal obligations associated with the retirement of long-lived assets. These liabilities are initially recorded at fair value, and the related asset retirement costs are capitalized by increasing the carrying amount of the related assets by the same amount as the liability. Asset retirement costs are subsequently depreciated over the useful lives of the related assets. Subsequent to initial recognition, VHS records period-to-period changes in the ARO liability resulting from the passage of time. VHS has recorded ARO liabilities of \$3,844 and \$3,627 in other long-term liabilities as of June 30, 2017 and 2016, respectively.

Revenue Guarantees

VHS has agreements with physicians whereby minimum revenues are guaranteed by VHS for stipulated dollar amounts over specified periods, as defined in the contracts. VHS records a liability for the amount of the guaranteed revenue at the time the contract is entered into and adjusts the liability as it is expended. VHS has recorded liabilities of \$754 and \$922 in accrued expenses and other current liabilities as of June 30, 2017 and 2016, respectively.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those for which use by VHS has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by VHS in perpetuity.

California Hospital Fee Program

California legislation established a program in 2009 that imposes a Quality Assurance Fee (QA Fee) on certain general acute-care hospitals in order to make supplemental and grant payments and increased capitation payments (Supplemental Payments) to hospitals up to the aggregate upper payment limit for various periods. There have been four such programs (the Programs) since inception.

The Programs are designed to make supplemental inpatient and outpatient Medi-Cal payments to private hospitals, including additional payments for certain facilities that provide high-acuity care and trauma services to the Medi-Cal population. This hospital QA Fee program provides a mechanism for increasing payments to hospitals that serve Medi-Cal patients, with no impact on the state's General Fund. Payments are made directly by the state or Medi-Cal managed care plans, which will receive increased capitation rates from the state in amounts equal to the Supplemental Payments. Outside of the legislation, the California Hospital Association has created a private program,

Notes to Consolidated Financial Statements (All amounts in Thousands)

operated by the California Health Foundation and Trust (CHFT), which was established to alleviate disparities potentially resulting from the implementation of the Programs.

The Programs require full federal approval by the Centers for Medicare and Medicaid Services (CMS) in order for them to be fully enacted. If final federal approval is not ultimately obtained, provisions in the underlying legislation allowed for the QA Fee, previously assessed, and Supplemental Payments, previously received, to be returned and recouped, respectively.

In October 2013, the fourth program (36-Month Program), covering the period from January 2014 to December 2016, was signed into law by the governor of California. The fee-for-service payments of the 36-Month Program were approved in December 2014 by CMS. The first six months of non-expansion managed care payments were approved by CMS in June 2015. The first six months of expansion managed care payments were approved by CMS in March 2016. On December 30, 2016, CMS approved the managed care payments spanning July 1, 2014, to December 31, 2014 for the expansion population and July 1, 2014 to June 30, 2015, for the non-expansion population.

VHS recognized payments to the California Department of Health Care Services for the QA Fee in the amount of \$70,032 and \$84,221 and pledge payments to CHFT of \$2,428 and \$1,228 within purchased services and other expenses for the years ended June 30, 2017 and 2016, respectively. VHS also recognized Supplemental Payment revenue in the amount of \$169,686 and \$134,061 within the net patient service revenues for the years ended June 30, 2017 and 2016, respectively. For the year ended June 30, 2017, these amounts include the six months of the 36-Month Program related to the fee-for-service portion (July 1, 2016 through December 31, 2016) and the managed care rates approved by CMS on December 30, 2016 noted above.

Refer to Note 6 and Note 7 for additional information on the assets and liabilities recorded at June 30, 2017 and 2016, associated with the provider fee programs.

Premium Revenue

Certain entities of VHS have capitation arrangements with various payers to provide medical services to enrollees. Under these arrangements, VHS receives monthly payments on a per member per month basis (PMPM), regardless of services actually performed by VHS. Premium revenues are recognized during the period in which VHS is obligated to provide services to enrollees.

Meaningful Use Incentives

The American Recovery and Reinvestment Act of 2009 established payments under the Medicare and Medi-Cal programs for certain professionals and hospitals that meaningfully use certified electronic health record (EHR) technology. The Medicare incentive payments are paid out to qualifying hospitals over four consecutive years on a transitional schedule. To qualify for Medi-Cal incentives, hospitals and physicians must annually meet EHR "meaningful use" criteria that become more stringent over three stages as determined by CMS. For the years ended June 30, 2017 and 2016, VHS has recorded meaningful use incentive payments of \$1,378 and \$507, respectively. These incentive payments have been recorded as other operating revenue in the VHS consolidated statements of operations and are recorded under the gain contingency method. Such incentives are subject to audit and recapture by the relevant authorities.

Notes to Consolidated Financial Statements (All amounts in Thousands)

Other Operating Revenue

Included in other operating revenue are amounts from rental revenues, cafeteria revenues, meaningful use incentives, grant revenues, and other non-patient care revenue.

Contributions

Unconditional promises to give cash and other assets to VHS are reported at fair value at the date the promise is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets. Net assets released from restrictions used for operations are also included in other operating revenue as contribution revenue to the Hospitals.

Refer to Note 1 for additional information on the unrestricted contribution revenue recorded during the years ended June 30, 2017 and 2016, associated with the release of the Blue Mountain restricted contributions.

Interest Expense

Interest expense on debt issued for construction projects, net of income earned on the funds held pending use, is capitalized from the date of the borrowing until the projects are placed in service. Interest components include the following:

Years Ended June 30,	2017	2016
Total interest expense Less: capitalized interest expense	\$ 29,041 (907)	\$ 20,943 (350)
Net interest expense	\$ 28,134	\$ 20,593

Income Taxes

VHS has established its status as an organization exempt from income taxes under IRC Section 501(c)(3) and the laws of California. Certain activities of the operating entities of VHS may be subject to income taxes; however, such activities are not significant to the consolidated financial statements.

Performance Indicator

Management considers the (deficit) excess of revenues over expenses to be VHS's performance indicator. (Deficit) excess of revenues over expenses includes all changes in unrestricted net assets, except net assets released from restrictions used for purchase of property and equipment, the change in funded status of pension plans, and other.

Certain Obligated Group members have a policy whereby assets are periodically transferred as charitable distributions to subsidiaries of VHS that are not members of the Obligated Group. These transfers are accounted for as direct charges to the Obligated Group members' unrestricted net assets. It is anticipated that Obligated Group members will continue to make asset transfers to the subsidiaries. These transfers are eliminated upon consolidation.

Notes to Consolidated Financial Statements (All amounts in Thousands)

Recent Accounting Pronouncements

In March 2017, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2017-07, Compensation – Retirement Benefits: Improving the Presentation of Net Periodic Pension Costs and Net Periodic Postretirement Benefit Cost. This guidance was issued to improve the reporting of net benefit cost in the financial statements to make this information more transparent. Under the guidance, an employer must report the service cost component in the same line item or items as other compensation costs arising from services rendered by pertinent employees during the period. The other components of net benefit cost are required to be presented in the statement of operations separately from the service cost component and outside the subtotal of income from operations if one is presented. ASU 2017-07 is effective for annual reporting periods beginning after December 15, 2017. Early adoption is permitted. VHS is currently evaluating the impact of this new standard on the consolidated financial statements.

In January 2017, the FASB issued ASU 2017-02, *Not-For-Profit Entities - Consolidation: Clarifying When a Not-For-Profit Entity That is a General Partner or Limited Partner Should Consolidate a For-Profit Limited Partnership or Similar Entity.* The amendments in this ASU retain the consolidation guidance that existed in Subtopic 810-20 by including it in Subtopic 958-810 (not-for-profit consolidation guidance). ASU 2017-02 is effective for annual periods beginning after December 15, 2016 and early adoption is permitted. VHS early adopted this guidance for the year ended June 30, 2017. Adoption of this guidance did not have a material effect on the consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, *Classification of Certain Cash Receipts and Payments*. This guidance adds or clarifies guidance on the classification of certain cash receipts and payments in the statement of cash flows. ASU 2016-15 is effective for annual periods beginning after December 15, 2018. VHS is currently evaluating the impact of this new standard on the consolidated financial statements.

In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958)*: *Presentation of Financial Statements for Not-For-Profit Entities*, which will require not-for-profit entities to revise financial presentation to include: net asset classifications, provide quantitative and qualitative information as to available resources and management of liquidity and liquidity risk, information on investment expenses and returns, and the presentation of operating cash flows. The standard aims to help the reader of the financial statements to better understand the financial position of the organization and enhance consistency among similar organizations. ASU 2016-14 is effective for annual periods beginning after December 15, 2017. Early adoption is permitted. VHS is currently evaluating the impact of this new standard on the consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases, (Topic 842): Amendments to the FASB ASC. ASU 2016-02 amends the existing accounting standards for lease accounting, including requiring lessees to recognize most leases on their balance sheets and making targeted changes to lessor accounting. The new standard requires a modified retrospective transition approach for all leases existing at, or entered into after, the date of initial application, with an option to use certain transition relief. The amendments in this update are effective for fiscal years (and interim reporting periods within fiscal years) beginning after December 15, 2018. Early adoption of the amendments is permitted for all entities. VHS is currently evaluating the impact of this new standard on the consolidated financial statements.

Notes to Consolidated Financial Statements (All amounts in Thousands)

In July 2015, the FASB issued ASU 2015-11, *Simplifying the Measurement of Inventory*. This standard requires entities to measure most inventories at the lower of cost or net realizable value. ASU 2015-11 is effective for annual periods beginning after December 15, 2016. VHS does not expect this guidance to have a material effect on the consolidated financial statements.

In April 2015, the FASB issued ASU 2015-07, Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or its Equivalent). The standard removes the requirement to categorize, within the fair value hierarchy, investments for which fair value is measured using the net asset value per share as a practical expedient. VHS adopted ASU 2015-07 retrospectively for the fiscal year ended June 30, 2017. As a result of the retrospective adoption, VHS removed any investments from the fair value hierarchy for which fair value is measured using the NAV per share as a practical expedient. Refer to the fair value disclosures for VHS's pension plan assets in Note 8 for additional details.

In April 2015, the FASB issued ASU 2015-03, *Interest-Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs*. The standard amends existing guidance to require the presentation of debt issuance costs in the balance sheet as a deduction from the carrying amount of the related debt liability instead of as an asset. VHS adopted ASU 2015-03 retrospectively for the fiscal year ended June 30, 2017. As a result of the retrospective adoption, VHS reclassified unamortized debt issuance costs of \$4,483 from other long-term assets to a reduction in long-term debt in the consolidated balance sheet as of June 30, 2016.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), and in August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date, which defers the effective date of ASU 2014-09 by one year. ASU 2014-09 requires the entity to recognize revenue for the transfer of goods or services equal to the amount that it expects to be entitled to receive for those goods or services, effective for periods beginning after December 15, 2017. VHS is currently evaluating the impact of this new standard on the consolidated financial statements.

3. Acquisitions

In January 2017, VHS expanded it ambulatory footprint by obtaining (1) a 51% controlling ownership interest in a newly formed management company, Verity BASM Holdco, LLC (a.k.a. Surgical Partners of California or BASM) which has agreements to manage multiple ambulatory surgery centers in the San Francisco Bay Area and (2) a non-controlling ownership interest in five of the surgery centers managed by BASM. The partnership is expected to advance VHS's goal of evolving into an integrated healthcare delivery network for the communities served.

VHS determined that the acquisition of BASM should be consolidated in the financial statements of VHS and the 49% non-controlling ownership interest should be separately presented. Refer below for additional details on the assets, liabilities and net assets recorded in connection with the purchase price allocation for BASM. VHS also determined that its non-controlling ownership interests in five of the surgery centers managed by BASM ranging from 20% - 25% should be accounted for under the equity method of accounting.

Notes to Consolidated Financial Statements (All amounts in Thousands)

The consideration for the above ownership interests included a cash payment of approximately \$15,000 and the assumption of a guarantee associated with an outstanding legal obligation owed by BASM and the five surgery centers for which VHS acquired an ownership interest (collectively, the "defendants"). The \$15,000 purchase price was allocated between BASM and the five surgery centers based on the respective business valuations for VHS's ownership interest in each entity, which were determined using a discounted cash flow approach and appropriate discounts for lack of control and marketability, as required. Discount rates utilized to determine the business valuations ranged from 13% - 17% depending on the level of risk associated with the business operations.

Based on the valuations, approximately \$7,165 was allocated to the five surgery centers and was recorded as equity-method investments and \$7,835 was allocated to BASM, representing VHS's ownership interests in the net assets of BASM. In the opening balance sheet of BASM as of January 2017, VHS recorded (1) total assets of \$21,799, including \$12,720 of intangible assets, \$5,702 of goodwill and \$3,377 of tangible assets; and (2) total liabilities of \$6,436 associated with the assumed legal obligations. The total net assets of \$15,363 were allocated as \$7,835 for VHS's controlling interest and \$7,528 for the non-controlling interest. The intangible assets are associated with the management contracts assumed and are being amortized over a useful life ranging from 5 to 15 years in accordance with the duration of the contracts.

In connection with the transaction, VHS simultaneously entered into a series of Reimbursement Agreements with the defendants requiring that they reimburse VHS for any payments made under the guarantee agreement. Such reimbursement may either be in the form of cash payments or VHS has the ability to recover such amounts by acquiring additional membership units in the respective entities. The initial amount of the guarantee was \$20,000 plus accrued interest at 6% per annum. As of June 30, 2017, the outstanding obligation at risk under the guarantee is \$15,000 plus interest.

On June 30, 2017, which represents the annual impairment testing date, VHS concluded there were impairment indicators associated with VHS's equity method investments in certain of the surgery centers and the management contract intangible assets and goodwill recorded at BASM. Such impairment indicators resulted from significant adverse trends in the most recent estimates of future cash flows for both the surgery centers and BASM. As a result of the impairment analysis, VHS recorded (1) \$3,310 of other-than-temporary impairment losses for its equity method investments in investment loss (see Note 2 for additional detail); (2) \$6,858 of impairment losses for the management contract intangible assets at BASM in operating expenses; and (3) \$3,374 of impairment losses for goodwill at BASM in operating expenses. See Note 4 for additional details on the valuation methodology utilized to determine the fair value of the respective assets and record the impairment charges as of June 30, 2017.

As a result of the impairment indicators identified at June 30, 2017, VHS also re-assessed the probability associated with a contingent loss under the guarantee agreement and recorded a guarantee obligation of \$4,760 in other long-term liabilities. As this guarantee obligation was determined to represent an additional contribution to the surgery centers investees, \$1,172 was recorded as an increase in carrying value of VHS's equity method investment associated with VHS's portion of the investment and \$3,588 was recorded as an investment loss associated with the non-contributing investees' portion of the investment. See Note 4 for additional details on the valuation methodology utilized to determine the fair value of the guarantee as of June 30, 2017.

Notes to Consolidated Financial Statements (All amounts in Thousands)

4. Fair Value Measurements

VHS accounts for certain assets at fair value or on a basis that approximates fair value. A fair value hierarchy for valuation inputs has been established to prioritize the valuation inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels, which is determined by the lowest-level input that is significant to the fair value measurement in its entirety. These levels are as follows:

- Level 1 Quoted prices are available in active markets for identical assets as of the measurement date. Financial assets in Level 1 include listed equities and money market balances.
- Level 2 Pricing inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets. Financial assets in this category generally include asset-backed securities, corporate bonds, municipal bonds, and commingled investment funds.
- Level 3 Pricing inputs are generally unobservable for the assets and include situations where there is little, if any, market activity for the investment. The inputs used in determination of fair value require management's judgment or estimation of assumptions that market participants would use in pricing the assets. Therefore, the fair values are determined using factors that involve judgment and interpretations, including discounted cash flow models and similar techniques.

The following represents assets measured at fair value on a recurring basis:

		June	30, 2017		
	Total	Active M Identic	d Prices in Markets for cal Assets evel 1)	Significant Other Observable Inputs (Level 2)	
Other investments - assets limited as to use:					
Cash equivalents	\$ 16,949	\$	16,949	\$	-
Debt securities issued by foreign corporations	262		-		262
Debt securities issued by the U.S. Treasury and other					
U.S. government corporations	21,162		-		21,162
Government mortgage-backed securities	7,376		-		7,376
Corporate U.S. debt securities	11,194		-		11,194
Investment held in trust account	4,238		-		4,238
Under bond indenture agreements - assets limited as to use:	61,181		16,949		44,232
Cash equivalents	63,493		63,493		-
Total assets limited as to use	\$ 124,674	\$	80,442	\$	44,232

Notes to Consolidated Financial Statements (All amounts in Thousands)

	June 30, 2016							
		Total	Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)			
Other investments - assets limited as to use:								
Cash equivalents	\$	60,264	\$	60,264	\$	-		
Debt securities issued by foreign corporations		2,063		-		2,063		
Debt securities issued by the U.S. Treasury and other								
U.S. government corporations		13,919		-		13,919		
Government mortgage-backed securities		1,096		-		1,096		
Commercial mortgage-backed securities		5,111		-		5,111		
Corporate U.S. debt securities		13,450		-		13,450		
Index funds		10,416		-		10,416		
Investment held in trust account		5,924		-		5,924		
Under hand indeed, and a second secon		112,243		60,264		51,979		
Under bond indenture agreements - assets limited as to use: Cash equivalents		25,154		25,154		-		
Total assets limited as to use	\$	137,397	\$	85,418	\$	51,979		

There were no transfers to or from Levels 1, 2, or 3 during the years presented. The Level 2 financial assets listed in the fair value hierarchy tables above use the following valuation techniques and inputs:

For marketable securities, such as foreign corporation and U.S. government debt securities, government and commercial mortgage-backed securities, corporate U.S. debt securities, index funds, and beneficial interest held in trust accounts, wherein identical quoted market prices are not readily available, the fair value of such investments is determined based on market participant pricing or other available market data for comparable instruments and transactions at the measurement date. VHS, therefore, incorporates industry-standard valuation techniques as inputs to fair valuation of its investments designated as Level 2.

VHS's rationale for the assignment of levels is based on types or classes of financial assets, rather than an analysis of each individual asset. Key consideration in the assignment of levels was given to the determination of a security's fair valuation measurement if obtained from an active market, and then further consideration was given for the types of inputs used to evaluate the fair value price. This approach has been supported by management's analysis of the methodology, the evaluated pricing models, and inputs used by its pricing vendors. It is also consistent with industry practice.

Where quoted prices are available in an active market (exchange-traded), the securities are classified as Level 1. It is a market in which transactions occur with sufficient frequency and volume to provide pricing information on an ongoing basis. If quoted market prices are not readily available for a specific financial asset, then value is determined using quoted prices of assets with similar characteristics and is classified as Level 2. Examples of these categories are VHS's investment in high-yield debt securities, collateralized mortgage obligations, and fixed-income prices provided by

Notes to Consolidated Financial Statements (All amounts in Thousands)

a broker-dealer. In cases where there is limited activity and less transparency associated with inputs to the valuation, VHS will designate the investments as Level 3. There were no Level 3 investments at June 30, 2017 and 2016.

Impairment Losses

During the year ended June 30, 2017, VHS recorded (1) \$3,310 of other-than-temporary impairment losses for its equity method investments; (2) \$6,858 of impairment losses for the management contract intangible assets at BASM; and (3) \$3,374 of impairment losses for goodwill at BASM. These represent non-recurring fair value measurement as of June 30, 2017. See Notes 2 and 3 for additional details. The fair value of the respective assets was determined using a discounted cash flow approach and appropriate discounts for lack of control and marketability, as required. Discount rates utilized to determine the business valuations ranged from 13% - 15% depending on the level of risk associated with the business operations. Such fair value measurements represent Level 3 fair value measurements as they utilize significant unobservable inputs.

Guarantee

During the year ended June 30, 2017, VHS recorded a guarantee liability of \$4,760 associated with the guarantee of certain outstanding legal obligations on behalf of the surgery center equity method investees. This represents a non-recurring fair value measurement as of June 30, 2017. See Note 3 for additional details on the terms of the guarantee. The fair value of the guarantee was estimated based on the contingent loss associated with the estimated payments to be made under the guarantee in the event of a default by the surgery centers.

Investment Held in Trust Accounts

VHS is the beneficiary of a split-interest agreement from a donor. The related assets are controlled and invested by an independent third party. VHS records the assets based on the fair value of the underlying investments.

5. Property and Equipment

Property and equipment consists of the following:

June 30,		2017	2016
Land	\$	26,235	\$ 28,970
Land improvements		20,226	20,252
Buildings and service equipment		703,766	705,025
Equipment		543,947	524,828
Construction in progress		24,209	8,139
Total		1,318,383	1,287,214
Less accumulated depreciation	((1,071,341)	(1,042,302)
Property and equipment, net	\$	247,042	\$ 244,912

VHS recorded depreciation expense of \$34,453 and \$48,308 for the years ended June 30, 2017 and 2016, respectively.

Notes to Consolidated Financial Statements (All amounts in Thousands)

6. Other Assets

Other current assets consist of the following:

June 30,	2017	2016
Inventories	\$ 24,032	\$ 21,501
Prepaid expenses	8,377	13,129
Provider fee receivables	35,960	51,761
Other receivables	14,357	5,343
Pledges receivable	4,533	2,968
Deposits	2,782	5,108
Other	5,151	6,463
Total other current assets	\$ 95,192	\$ 106,273
Other long-term assets consist of the following:		

June 30,	2017				
Notes receivable	\$ 3,271	\$	646		
Intangible assets	5,398		-		
Goodwill	3,225		-		
Assets held for sale	2,469		-		
Equity-method investments	5,041		-		
Other	5,681		5,232		
Total other long-term assets	\$ 25,085	\$	5,878		

7. Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consist of the following:

June 30,	2017	2016
Wages and benefits	\$ 64,155	\$ 66,471
Medical claims and IBNR	31,897	31,415
Deferred management fees	46,228	16,108
Current portion of workers' compensation and hospital		
professional and general liability	8,855	9,805
Provider fee payables and advances	55,707	29,361
Other	47,287	64,243
Total accrued expenses and other current liabilities	\$ 254,129	\$ 217,403

Notes to Consolidated Financial Statements (All amounts in Thousands)

8. Pension and Other Postretirement Benefit Plans

VHS maintains single employer defined benefit retirement plans and participates in a multiemployer defined benefit retirement plan. The plans have been frozen for all employees, except members of the California Nurses Association (CNA). Benefits are generally based on age, years of service, and employee compensation. VHS also offers postretirement health care benefits to a limited number of its employees. The postretirement health care benefits are determined based on age and years of service.

The multiemployer defined benefit pension plan is called the Retirement Plan for Hospital Employees (RPHE). The entities that participate in the RPHE are Seton Medical Center, Seton Medical Center Coastside, O'Connor Hospital, Saint Louise Regional Hospital, and Caritas Business Services (however, as noted above, only CNA members at these locations earn new benefits under the plan). Benefits are generally based on years of service and the employee's compensation. Contributions to the plan are based on actuarially determined amounts sufficient to meet the benefits to be paid to plan participants and satisfy IRS funding requirements. VHS recorded benefits expense of \$21,093 and \$17,223 associated with required cash contributions to the RPHE during the fiscal years ended June 30, 2017 and 2016, respectively.

VHS also maintains single-employer defined benefit pension plans (the Retirement Plans). VHS associates at St. Francis Medical Center, St. Vincent Medical Center, O'Connor Hospital, Saint Louise Regional Hospital, and the system office are eligible to participate in this plan (however, as noted above, only CNA members continue to earn new benefits under the plan). VHS contributed \$41,678 and \$12,915 to the Retirement Plans during the fiscal years ended June 30, 2017 and 2016, respectively.

VHS also maintains a retiree health insurance program (the Postretirement Healthcare Plan), which provides medical benefits to retirees from early retirement to age 65 only. VHS employees at O'Connor Hospital, St. Louise Regional Hospital, Seton Medical Center, and Seton Medical Center Coastside are eligible to participate in this plan. The Postretirement Healthcare Plan is an unfunded plan. VHS contributed \$50 and \$58 to the Postretirement Healthcare Plan during the fiscal years ended June 30, 2017 and 2016, respectively.

Defined Contribution Retirement Plans

In addition to the above pension plans, VHS maintains three different defined contribution retirement plans for its employees. One of these defined contribution plans (TSA/403(b)) includes employee voluntary contributions only. A second defined contribution plan (Match Benefit) requires employer contributions and the benefits are based on a percentage of the employees' contributions to the TSA/403(b). A third plan covers all employee groups except members of the CNA and is a fully employer-paid defined contribution plan with benefits based on a percentage of compensation. During the fiscal years ended June 30, 2017 and 2016, the employer's contribution expense for the defined contribution plans was \$18,481 and \$21,749, respectively.

Notes to Consolidated Financial Statements (All amounts in Thousands)

The funded status of the Retirement Plan and the Postretirement Healthcare Plan benefits is as follows:

	June 30, 2017					June	ie 30, 2016			
			Postr	etirement			Postretirement			
	Re	tirement	Hea	althcare	Re	tirement	Healthcare			
		Plans		Plan		Plans	P	lan		
Change in benefit obligation:										
Benefit obligation -										
beginning of year	\$	573,239	\$	1,956	\$	523,435	\$	3,656		
Service cost		1,837		98		2,062		181		
Interest cost		22,929		73		24,614		163		
Actuarial loss (gain)		(887)		(1,205)		47,408		(1,986)		
Plan change		(10,702)		-		=		-		
Benefits paid		(21,528)		(50)		(24,280)		(58)		
Benefit obligation - end of year	\$	564,888	\$	872	\$	573,239	\$	1,956		
Accumulated benefit obligation	\$	564,792	\$	872	\$	563,329	\$	1,956		

	June 30, 2017					June	e 30, 2016			
			Pos	tretirement			Postre	retirement		
	Re	tirement	Н	lealthcare	Re	tirement	Hea	Ithcare		
		Plans		Plan		Plans		Plan		
Change in plan assets:										
Fair value of plan assets -										
beginning of year	\$	270,880	\$	-	\$	275,824	\$	_		
Actual return on plan assets		26,786		-		8,133		_		
Employer contribution		41,678		50		12,915		58		
Benefits paid		(21,528)		(50)		(24,280)		(58)		
Administrative expenses		(6,058)		-		(1,712)		_		
Fair value of plan assets - end of										
year	\$	311,758	\$	-	\$	270,880	\$			
Funded status	\$	(253,130)	\$	(872)	\$	(302,359)	\$	(1,956)		

Amounts that have not yet been recognized as components of net period benefit cost are as follows:

		June	017		June 30, 2016				
	Re	etirement Plans		Postretirement		irement Plans	Postretiremen Healthcare Plan		
Net actuarial loss (gain) Prior service costs	\$	225,849 (10,518)	\$	-	\$	234,717 -	\$	(12,042) 280	
Total amount not recognized	\$	215,331	\$	-	\$	234,717	\$	(11,762)	

Notes to Consolidated Financial Statements (All amounts in Thousands)

The components of net period benefit cost and amounts recognized in the consolidated statements of operations and changes in net assets apart from expenses are as follows:

	Υe	ar Ended	Jun	e 30, 2017	Yε	ear Ended	Ended June 30, 2016			
		tirement Plans		tretirement lealthcare Plan	Re	tirement Plans	Hea	tirement Ithcare Plan		
Components of net periodic benefit										
cost (income): Service cost	\$	1,837	\$	98	\$	2,062	\$	181		
Interest cost	Ф	22,929	Ф	73	Ф	24,614	Ф	163		
Expected return on plan assets		(18,665)		75		(18,611)		103		
Net prior service cost		(10,003)				(10,011)				
amortization		(184)		72		_		72		
Amortization of actuarial loss		(101)		, _				, _		
(gain)		5,918		(1,193)		4,463		(987)		
Immediate recognition of		,		(, ,		•		` ,		
previously deferred cost										
(income)		-		(11,846)						
Cost of special events		-				1,810		_		
Total	\$	11,835	\$	(12,796)	\$	14,338	\$	(571)		
Change in net assets apart from periodic benefit cost:										
Net actuarial loss (gain)	\$	(2,950)	\$	(1,205)	\$	59,598	\$	(1,986)		
Net prior service cost (credit)		(10,702)		=						
Deduct:										
Amortization of prior service										
cost		184		(72)		=		(72)		
Amortization of actuarial		.								
(loss) gain		(5,918)		1,193		(6,273)		987		
Other Adjustments		-		11,846		-		-		
Total	\$	(19,386)	\$	11,762	\$	53,325	\$	(1,071)		

The estimated actuarial loss (gain) and prior service cost for the Retirement Plans that will be amortized into net periodic benefit cost over the next fiscal year is \$6,213 and (\$368), respectively.

During the fiscal year ended June 30, 2017, \$11,846 remaining in net assets associated with prior service cost and net actuarial gains for the Postretirement Healthcare Plan was immediately recognized into net periodic benefit cost as a reduction of expense. During the next fiscal year any prior service cost (credits) and net actuarial losses (gains) will continue to be recognized immediately into net periodic pension cost and will not be amortized in future periods.

Notes to Consolidated Financial Statements (All amounts in Thousands)

Assumptions

The weighted-average assumptions used to determine benefit obligations and net period benefit costs, are as follows:

	June 3	0, 2017	June 30, 2016				
	l	Postretirement		Postretirement			
	Retirement	Healthcare	Retirement	Healthcare			
	Plans	Plan	Plans	Plan			
Weighted-average assumptions used to determine benefit obligations: Discount rate	3.84% - 4.00%	3.70%	4.05%	3.85%			
Rate of compensation increase (rate of 4.00% used for 2019 and later)	5.00%	N/A	2.50%	N/A			
and later)	5.00%	IV/ A	2.50%	IV/ A			
Weighted-average assumptions used to determine net periodic benefit costs:							
Discount rate	3.31% - 3.98%	3.85%	4.80%	4.55%			
Expected return on plan assets	6.75%	N/A	7.00%	N/A			
Rate of compensation increase	5.00%	N/A	2.50%	N/A			

Expected Return on Plan Assets

The Retirement Plan's estimated long-term rate of return on pension assets is driven primarily by historical asset-class returns, an assessment of expected future performance, advice from external actuarial firms, and the incorporation of specific asset-class risk factors. Asset allocations are periodically updated using pension plan asset/liabilities studies, and VHS's estimated long-term rates of return are consistent with these studies.

Discount Rate

The discount rate assumptions used to determine the retirement and postretirement benefit plan obligations and expenses reflect the prevailing rates available on high-quality, fixed-income debt instruments. The rate was based on cash flow analysis that matched estimated future benefit payments to the bond discount yield curve as of June 30, 2017 and 2016. Approximately 98% of VHS's retirement plan liabilities were measured using a discount rate 3.84% as of June 30, 2017.

During the fiscal year ended June 30, 2017, the discount rate was updated from a single equivalent discount rate used to determine the projected benefit obligation and net periodic benefit cost to separate discount rates used for determining the projected benefit obligation, interest on the projected benefit obligation, service cost and interest on service cost. The range of discount rates used to determine the separate components have been included in the table above.

Notes to Consolidated Financial Statements (All amounts in Thousands)

Other Benefit Assumptions

For the measurement of accumulated postretirement benefit obligations at June 30, 2017, the Postretirement Healthcare Plan assumed health care cost trend rates start at 8.00% in 2017 and decrease by 0.25%-0.50% annually, reaching an ultimate rate of 5.50% in fiscal year 2023. A one-percentage-point change in assumed health care cost trend rates would not have a material effect on VHS's consolidated financial statements.

Plan Assets and Investment Strategy

The following information represents VHS's pension plan assets measured at fair value and indicate the fair value hierarchy and valuation techniques utilized to determine such fair value:

	June 30, 2017						
	C			d Prices	Sig	nificant	
				Active	Other		
				ets for		ervable	
				al Assets		nputs	
	Total	Balance	(Le	vel 1)	(Level 2)		
Cash equivalents	\$	7,079	\$	7,079	\$	-	
Fixed-income securities and funds		82,310		-		82,310	
Domestic stocks and funds		39,129		16,132		22,997	
Real estate equity fund investments		16,159		-		16,159	
Foreign stocks		2,200		2,200		-	
Subtotal plan assets		146,877		25,411		121,466	
Investments measured at net asset value:							
Domestic stock funds					\$	66,789	
International stock funds						60,410	
Fixed income funds						37,682	
Total plan assets					\$	311,758	

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Notes to Consolidated Financial Statements (All amounts in Thousands)

	Tota	I Balance	Quot in Mar Identi	30, 2016 ed Prices Active kets for cal Assets evel 1)	Obs I	6,035 70,580 - - - 76,615		
Cash equivalents Common collective trust funds Fixed-income funds Domestic stocks Real estate equity investments	\$	3,852 6,035 70,580 46,765 14,002	\$	3,852 - 46,765 14,002	\$	6,035		
Subtotal plan assets		141,234		64,619		76,615		
Investments measured at net asset value:								
Domestic stock funds International stock funds Fixed income funds					\$	49,734		
Total plan assets					\$	270,880		

As of June 30, 2017, \$1,842 of the plan's cash balance was held in a separate non-interest-bearing cash account for the purpose of claims disbursement by the plan's administrator.

VHS's investment strategy for the assets of the Retirement Plan is designed to preserve principal while earning returns relative to the overall market consistent with a prudent level of risk. The strategy balances the liquidity needs of the Retirement Plan with the long-term return goals necessary to satisfy future obligations. The target asset allocation is diversified across traditional asset classes. Diversification is also achieved through participation in U.S. and non-U.S. markets, investment manager style, philosophy, and capitalization. The complementary investment styles and approaches used by investment managers are aimed at reducing volatility while capturing the equity premium from the capital markets over the long term. Risk tolerance is established through consideration of plan liabilities, plan funded status, and VHS's consolidated financial condition. Consistent with VHS's fiduciary responsibilities, the fixed-income allocation generally provides for security of principal to meet near-term expenses and obligations. Periodic reviews of the market values and corresponding asset allocation percentages are performed to determine whether a rebalancing of the portfolio is necessary.

The following were the target asset allocations as of June 30, 2017, by major asset classification:

Fixed-income	35%
Domestic stocks	29
Foreign stocks	19
Inflation linked	17
Total plan assets	100%

Notes to Consolidated Financial Statements (All amounts in Thousands)

Cash Contributions and Benefit Payments

VHS expects to contribute \$46,048 to the Retirement Plans and \$58 to the Postretirement Healthcare Plan during fiscal year ending June 30, 2018. The expected contributions to the Retirement Plans include an additional expected contribution of approximately \$7,619 resulting from a shortfall in 2017 charity care requirement established by the Attorney General in connection with the Restructuring Agreement.

The benefit payments, which reflect expected future service, as appropriate, expected to be paid in each of the next five years, and in aggregate for the next five years, are as follows:

	Retirement Plan Benefits		Postretirement Healthcare Benefits	
-	 CHCHES		Deficites	
2018	\$ 23,834	\$	58	
2019	25,316		47	
2020	27,251		50	
2021	29,016		55	
2022	30,166		60	
Next five years	161,490		330	

Multiemployer Plan

Certain affiliated entities in Northern California participate in multiemployer defined benefit retirement plans as described below (in thousands):

	Pension Plan Employer Identification Number/Plan	Pension Protection	Funding Improvement/ Rehabilitation Plan Status	
Plan	Number	2017	2016	June 30, 2017
Retirement Plan for Hospital Employees	94-2995676/001	Green	Green	No
Pension Protection Critical Status Seriously Endang Endangered None of the above	•	rom worst to best):		Red Orange Yellow Green

Notes to Consolidated Financial Statements (All amounts in Thousands)

Plan	Pension Plan Employer Identification Number/Plan Number	2018 (Expected)	ontributio	ons	Surcharge Imposed (during 2013)	Collective Bargaining Agreement Expiration Date
Retirement Plan for Hospital Employees	94-2995676/001	\$15.706	\$21,093	\$ 17,223	No	October 31, 2018

Since March 1, 2011, participant benefits were frozen for the non-contractual employees of the two participating affiliates in the Retirement Plan for Hospital Employees. Beginning January 1, 2013, participant benefits were frozen for all Service Employees International Union (SEIU) employees. Certain affiliates will continue to make periodic contributions as needed for eligible participants.

The contributions for the multiemployer plan were approximately 45% and 38% of the total contributions to the plan for June 30, 2017 and 2016, respectively. There are no minimum contributions required for future periods by the collective-bargaining agreements, statutory obligations, or other contractual obligations for both plans.

The risks of participating in multiemployer plans are different from single-employer plans in the following aspects: (i) assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of other participating employers; (ii) if a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers; and (iii) if the affiliates choose to stop participating in the multiemployer plan, the affiliates may be required to pay the plan an amount based on the underfunded status of the plan, referred to as a withdrawal liability.

9. Debt

Long-term debt consists of the following:

June 30,	2017	2016
California Statewide Communities Development Authority Revenue Bonds Series 2005A, payable in varying installments through 2040, fixed interest rates ranging from 5.00% to 5.25%		
per annum	\$ 246,345	\$ 249,850
California Statewide Communities Development Authority Revenue Bonds Series 2005 G and H (St. Francis Medical Center), payable in varying annual installments through 2026,		
fixed interest rates ranging from 5.00% to 5.25% per annum California Public Finance Authority Revenue Notes (Verity Health System), Series 2015 A and B fixed interest only bonds at	19,840	22,740
7.25% per annum. Principal due June 10, 2019	105,000	105,000

Notes to Consolidated Financial Statements (All amounts in Thousands)

June 30,	2017	2016
California Public Finance Authority Revenue Notes (Verity Health System), Series 2015 C (taxable) and D (tax-exempt) fixed interest only bonds at 9.50% and 8.75% per annum,		
respectively. Principal due June 10, 2019 Commercial Property Assessed Clean Energy (C-PACE) Financing, payable in semi-annual installments through 2048, fixed	\$ 55,000	\$ -
interest of 6.40% - 6.45% per annum Notes payable for Health Center One Mortgage, \$6.5 million face value, payable in monthly installments with a lump-sum	40,000	-
payment in May 2018, fixed interest rate of 5.85% per annum Other	5,140 1,411	5,329 53
Total debt obligations Less current portion (including debt issuance costs and bond	472,736	382,972
premiums)	(12,480)	(6,647)
Plus bond premium Less debt issuance costs	460,256 3,672 (4,772)	376,325 4,031 (4,483)
Long-term debt - net of current portion and debt issuance costs	\$ 459,156	\$ 375,873

Obligated Group

Verity Health System of California, Inc. and its five hospitals are collectively referred to as the "Obligated Group" or as "Members," and each individually is sometimes referred to herein as a "Member." The Obligated Group is established pursuant to a Master Indenture of Trust, dated December 1, 2001, as supplemented to date (the Master Indenture), between the Obligated Group and U.S. Bank National Association, as successor master trustee (the Master Trustee). The Obligated Group is jointly and severally liable for obligations issued pursuant to and outstanding under the Master Indenture (Obligations).

Each of the Obligated Group Members has executed one or more deeds of trust pursuant to which the respective Obligated Group Member has granted for the benefit of the Master Trustee, a first lien on, and security interest in, the property of the hospitals and certain other parcels of property owned by such Obligated Group Members, subject to permitted liens, as security for the performance of the Obligated Group Members' obligations under the Master Indenture. Additionally, each of the Obligated Group Members has created a gross revenue fund with its depository bank to further secure its gross revenues for the benefit of the Master Trustee.

The Master Indenture and certain other Obligated Group's financing agreements contain restrictive covenants, including maintenance of a debt ratio, limitations on the amount of any additional borrowings, and limitations on the disposal or transfer of assets to non-obligated group members. Additionally, the financing agreements require that funds are established with, and controlled by, a trustee during the period the bonds remain outstanding. The Obligated Group has complied with such financial covenants and restrictions at June 30, 2017.

Notes to Consolidated Financial Statements (All amounts in Thousands)

For the year ended June 30, 2017, the Obligated Group did not have to comply with a minimum required Annual Debt Service Coverage Ratio per the Master Indenture as there was a covenant holiday. For the year ending June 30, 2018, the minimum required Annual Debt Service Coverage Ratio is 0.7. The minimum required Annual Debt Service Coverage Ratio increases to 1.1 for the year ending June 30, 2019.

Long-Term Debt

Series 2005 Bonds

In March 2005, the California Statewide Communities Development Authority (CSCDA), on behalf of Daughters of Charity Health System (now known as VHS), issued four series of revenue bonds in the aggregate principal amount of \$364,655 (the 2005 Bonds). The 2005 Bonds were comprised of \$259,125 of 2005 Series A bonds, \$39,715 of Series F bonds, \$48,245 of Series G bonds, and \$17,570 of Series H bonds. The issuance of the 2005 Bonds generated original issue premiums of \$12,929. A portion of the proceeds of the 2005 Bonds was used to refinance prior bonds and finance the costs of constructing, improving, renovating, and equipping certain improvements to the facilities of the Obligated Group. The 2005 Series F bonds matured and were paid pursuant to their terms on July 1, 2010. Total interest expense related to the Series 2005 Bonds was \$15,801 and \$17,588 for the years ended June 30, 2017 and 2016, respectively.

The Series 2005 Bonds are a limited obligation of CSCDA and are payable solely from payments made by the Obligated Group. Payment of principal and interest on the Series 2005 Bonds is secured by Obligations issued pursuant to the Master Indenture.

Series 2015 Notes

On December 14, 2015, the California Public Finance Authority issued an aggregate of \$160,000 of Revenue Notes (Verity Health System) Series 2015A, B, C, and D (collectively, the 2015 Notes) for the benefit of VHS. There are four series of 2015 Notes. The Series 2015A, B, and D Notes are tax exempt, and the Series 2015C Notes are taxable. While all of the 2015 Notes were authorized and issued, only the Series 2015A Notes (\$60,000) and the 2015B Notes (\$45,000) were funded as of June 30, 2016. The Series 2015C Notes (\$10,000) and the Series 2015D Notes (\$45,000) were funded on September 19 and October 31, 2016, respectively. A portion of the proceeds of the 2015 Notes was used, together with other funds, to pay the principal of and accrued and unpaid interest on the 2014 Bonds that matured on December 15, 2015. Total interest expense related to the Series 2015 Notes was \$11,013 and \$2,953 for the years ended June 30, 2017 and 2016, respectively.

The 2015 Notes are secured by an Obligation (as defined in the Master Indenture) on parity with other Obligations issued pursuant to the Master Indenture. In addition to their parity lien under the Master Indenture, the 2015 Notes have additional lien rights on the Obligated Group's accounts receivable and in certain properties owned by St. Francis Medical Center and Saint Louise Regional Hospital.

Notes to Consolidated Financial Statements (All amounts in Thousands)

2017 Assessment Bonds (C-PACE bonds)

In May 2017, Verity closed on a Commercial Property Assessed Clean Energy ("C-PACE") funding in the amount of \$40,000 to finance seismic upgrades to the Seton Medical Center campus. CleanFund Commercial PACE Capital, Inc. provided \$20,000 of its own capital and brought in a partner, Petros PACE Finance, to provide an additional \$20,000. The proceeds will be used to make upgrades to the hospital, as required by California's mandatory Hospital Facilities Seismic Safety Act (SB 1953).

C-PACE is long-term, fixed-rate financing, similar to the traditional tax-exempt debt that hospitals often use for infrastructure investments. The C-PACE bonds are exempt from income taxes imposed by the State of California; however are not exempt from federal income tax. To repay the C-PACE financing, Seton will pay property tax assessments at a fixed amount until the C-PACE financing matures in 2047. The assessment payments are secured by a lien against the property at the Seton Medical Center campus. Total interest expense related to the C-PACE bonds was \$323 for the year ended June 30, 2017. Refer to Note 12 for additional information on VHS's seismic requirements.

Scheduled long-term principal debt payments as of June 30, 2017, are as follows:

Years Ending June 30,	Amount
2018	\$ 13,165
2019	167,553
2020	7,982
2021	8,409
2022	8,852
Thereafter	266,775
	\$ 472,736

Fair Values

The fair value of VHS's bond indebtedness is estimated based on the quoted market prices for the same or similar issues or on the current rates offered for debt of the same remaining maturities. The total estimated fair value of VHS's bond and note debt (Series 2005 bonds, Series 2015 Notes and 2017 Assessment Bonds) as of June 30, 2017 and 2016, was \$448,472 and \$336,804, respectively, and such debt was valued using Level 2 inputs. The total carrying value of VHS's bond and note debt as of June 30, 2017 and 2016, was \$466,185 and \$377,590, respectively. The reported fair value of VHS's bond indebtedness instruments excludes the full value of an irrevocable principal prepayment of \$6,405 and \$6,090 made as of June 30, 2017 and June 30, 2016, respectively. The fair values of the remaining mortgage payable and other debt are not materially different from their carrying values as the majority of such amounts are due within the next 12 months. The fair value amounts do not represent the amount that would be required to expend to retire the indebtedness.

Notes to Consolidated Financial Statements (All amounts in Thousands)

10. Functional Classification of Expense

The following is a functional classification of VHS's expenses:

Year Ended June 30,	2017	2016
Health services General and administrative	\$ 1,151,268 363,558	\$ 1,193,112 301,768
	\$ 1,514,826	\$ 1,494,880

11. Temporarily and Permanently Restricted Net Assets

Temporarily and permanently restricted net assets are available for the following purposes:

June 30,	2017	2016
Equipment and expansion	\$ 2,809	\$ 3,522
Research and education	2,581	2,848
Restricted contribution	-	60,367
Charity and other	8,054	6,593
Total temporarily restricted net assets	13,444	73,330
Permanently restricted net assets	8,202	8,137
Total restricted net assets	\$ 21,646	\$ 81,467

Equipment and expansion relate to assets held by VHS, which are restricted by donors or grantors to be used specifically for equipment, capital projects, or other capital needs.

Research and education relate to assets held by VHS, which are restricted by donors or grantors to be used in specific research or education programs.

During the fiscal year ended June 30, 2016, the restricted contribution represented the remaining portion of the contribution recognized at the time of the transaction contemplated by the Restructuring Agreement (see Note 1 "Organization"). The restriction of this contribution was lifted during the fiscal year ended June 30, 2017, pursuant to the terms of the Restructuring Agreement. The release of the restricted funds was recorded as unrestricted contribution revenue for the year ended June 30, 2017.

Charity and other relate mainly to assets held by VHS, which are restricted by donors or grantors to be used in specific health care programs for charity care and other medical and patient services.

Permanently restricted net assets of \$8,202 and \$8,137 at June 30, 2017 and 2016, respectively, are restricted to investments to be held in perpetuity, with the income expendable to support VHS's mission.

Notes to Consolidated Financial Statements (All amounts in Thousands)

Endowments

VHS and five of its consolidated charitable foundations follow the Uniform Prudent Management of Institutional Funds Act (UPMIFA). UPMIFA eliminates the concept of "historic dollar value" and allows an institution to spend or accumulate as the board determines is prudent for the uses, benefits, purposes, and duration of the endowment fund unless the gift instrument states a particular spending rate or formula. California's version of UPMIFA also includes a rebuttable provision that spending greater than 7% of the average fair market value (calculated at least quarterly over a minimal period of three years) is presumed to be imprudent.

In accordance with UPMIFA, VHS considers the following factors when appropriating or accumulating an endowment fund: (i) general economic conditions, (ii) effects of inflation and deflation, (iii) the purposes of the institution and the endowment fund, (iv) expected total return from income and appreciation of investments, (v) VHS's other resources, (vi) the duration and preservation of the endowment fund, and (vii) VHS's investment policies.

From time to time, the fair value of assets associated with individual endowment funds may fall below the level that the donor or UPMIFA requires VHS to retain as a fund of perpetual duration. Deficiencies of this nature that are reported in unrestricted net assets were not material as of June 30, 2017 and 2016. These deficiencies resulted from unfavorable investment market fluctuations.

VHS has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Under these policies, as approved by the boards of trustees of the charitable foundations, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results while assuming a moderate level of investment risk.

To satisfy its long-term rate-of-return objectives, VHS relies on a balanced investment strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). VHS targets a diversified asset allocation that places a great emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

The endowment net asset composition by type of fund consists of the following:

				June 3	0, 2	2017	
			Τe	emporarily	Pe	ermanently	_
	Unrestricted			estricted	I	Restricted	Total
Donor-restricted endowment funds	\$	615	\$	962	\$	8,202	\$ 9,779
Total funds	\$	615	\$	962	\$	8,202	\$ 9,779

Notes to Consolidated Financial Statements (All amounts in Thousands)

				June 3	0, :	2016	
			Te	emporarily	P	ermanently	_
	Unrestricted			Restricted		Restricted	Total
Donor-restricted endowment funds	\$	606	\$	789	\$	8,137	\$ 9,532
Total funds	\$	606	\$	789	\$	8,137	\$ 9,532

The changes in endowment net assets are as follows:

	Unre	stricted	nporarily stricted	nanently stricted	Т	otal
Balance at June 30, 2015 Net gains (losses) - realized and	\$	596	\$ 778	\$ 8,207	\$	9,581
unrealized Other		10 -	11 -	(73) 3		(52) 3
Balance at June 30, 2016 Net gains (losses) - realized and		606	789	8,137		9,532
unrealized Other		9	173 -	65 -		247 -
Balance at June 30, 2017	\$	615	\$ 962	\$ 8,202	\$	9,779

12. Commitments and Contingent Liabilities

Standby Letter of Credit

Marillac, a subsidiary of VHS, pledged \$43,408 of its investments to support a standby letter of credit issued in favor of Old Republic Insurance Company, one of the Parent's insurers, at June 30, 2017.

Litigation, Regulatory and Compliance Matters

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time. These laws and regulations include, but are not necessarily limited to, matters, such as licensure, accreditation, controlled substances, privacy, government health care program participation requirements, reimbursement laws and regulations, anti-referral laws, false claims prohibitions, and in the case of tax-exempt organizations, the requirements of tax exemption. In recent years, government activity has increased with respect to investigations and allegations concerning possible violations of reimbursement, false claims, and anti-referral statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs, as well as imposition of significant fines and penalties and significant repayments for patient services previously reimbursed.

The Health Insurance Portability and Accountability Act (HIPAA) assures health insurance portability, reduces healthcare fraud and abuse, guarantees security and privacy of health information, and enforces standards for health information. The Health Information Technology for Economic and

Notes to Consolidated Financial Statements (All amounts in Thousands)

Clinical Health Act (HITECH Act) expanded upon HIPAA in a number of ways, including establishing notification requirements for certain breaches of protected health information. In addition to these federal rules, California has also developed strict standards for the privacy and security of health information as well as for reporting certain violations and breaches. The Company may be subject to significant fines and penalties if found not to be compliant with these state or federal provisions.

Management assesses the probable outcome of unresolved litigation and investigations and records contingent liabilities reflecting estimated liability exposure. It is the opinion of management, after consulting with legal counsel, that such actions will not have a material effect on VHS's consolidated financial position or results of operations as of June 30, 2017. Therefore, based on the information provided by its legal counsel, VHS has accrued \$1,100 and \$1,240 as of June 30, 2017 and 2016, respectively, which were related to certain of these actions. VHS evaluates recoveries from insurance coverage separately from its liability, and when appropriate, an asset is recorded separately from the associated liability. Following is a discussion of matters of note.

VHS is a named defendant in two related class actions, Jarmaine Johns v. Verity Health System of California and Iris Lara and Tanya Llera v. Verity Health System of California. The complaints allege the plaintiffs were the victims of a data breach where their personal information was obtained and their identities were allegedly used. The breach involved approximately 7,500 employees. The complaints allege the plaintiffs have been harmed and have had to spend time and money addressing identity theft. In the Lara action, plaintiffs specifically allege that they have been harmed by false tax returns that were filed using information released in the data breach. The Lara action is currently stayed by order of the court. VHS intends to contest these actions. At this time, management cannot accurately estimate the amounts of any payments or settlements that might result from these matters.

VHS was previously a named defendant in a breach of contract, unjust enrichment, and declaratory relief complaint filed by Prime Healthcare Services, Inc. and Prime Healthcare Foundation, Inc. and captioned *Prime Healthcare Services, Inc.*, et al., vs. Blue Mountain Management Capital, et al., in the Superior Court of California, County of San Bernardino, and San Bernardino Justice Center. Subsequent to June 30, 2017, a settlement was reached between the parties, which resulted in no loss for VHS.

U.S. Department of Justice and OIG Investigations

VHS and/or its facilities periodically receive notices from governmental agencies, such as U.S. Department of Justice (DOJ) or the Office of Inspector General (OIG), requesting information regarding billing, payment, or other reimbursement matters, or initiating investigations, or indicating the existence of whistleblower litigation. VHS does not anticipate such requests to result in a material impact to the consolidated financial statements.

Within this category, VHS received an informal documentation request from the DOJ related to BASM during the current year (see Note 3 for information on the BASM acquisition transaction). Additionally, during the prior year, VHS filed a self-disclosure with the OIG indicating possible violations of the Stark Law and the Anti-Kickback Statute by Seton Medical Center. The OIG informed VHS that the disclosure was officially accepted into the Self-Disclosure Protocol. At this time, management cannot accurately estimate the amounts of any potential damages or penalties that might result from these matters.

Notes to Consolidated Financial Statements (All amounts in Thousands)

Collective Bargaining

VHS has 6,787 employees as of June 30, 2017, of whom just over 4,149 are full-time employees. Approximately 78% of these employees are represented by collective bargaining units. A majority of the employees are represented by collective bargaining agreements with Service Employees International Union (SEIU) (approximately 40% of employees) and California Nurses Association (CNA) (approximately 23% of employees). Employee strikes or other adverse labor actions may have a material adverse impact on VHS's consolidated financial position or results of operations.

Attorney General Requirements

As part of approving the Restructuring Agreement (see Note 1), the California Attorney General's (AG) office placed certain operational restrictions on VHS and each of its hospitals, which include certain minimum annual targets for charity care, community benefits, and capital expenditures among other requirements. As a result of a shortfall in the fiscal year 2017 charity care requirement for certain hospitals, VHS was required to make an additional contribution to the Retirement Plans of \$7,619 by October 31, 2017 (see Note 8). VHS has complied with such requirements under the AG agreement.

Lease Commitments

Future minimum lease payments under VHS's significant non-cancelable operating leases (with initial or remaining lease terms in excess of one year) as of June 30, 2017, are as follows:

Years Ending June 30,	Amount
2018	\$ 11,840
2019	7,681
2020	5,553
2021	4,468
2022	2,807
Thereafter	996
	\$ 33,345

Rent expense was \$21,601 and \$19,501 for the years ended June 30, 2017 and 2016, respectively.

Seismic Standards

VHS assessed its earthquake retrofit requirements for health care facilities under a state of California law SB 90 that can allow a delay of up to seven years from the January 1, 2013, deadline for Structural Performance Category 1 (SPC-1) retrofits. This affects six buildings at three of VHS's hospitals. The previously reported seventh building, the St. Vincent Medical Center Central Plant, has been upgraded to SPC-2 status. Extensions have been approved by the Office of Statewide Health Planning and Development as follows:

St. Vincent Medical Center Main Hospital must meet SP-2 standards by January 1, 2019. St. Vincent Medical Center Doheny Wing must meet SP-2 standards by July 1, 2019. Management currently estimates that remaining remediation costs required for meeting the standards is approximately \$12,200 based on third-party estimates.

Notes to Consolidated Financial Statements (All amounts in Thousands)

O'Connor Hospital 1953 Building must meet SPC-2 standards by July 1, 2019. O'Connor Hospital 1953 Boiler Plant/Laundry must meet SPC-2 standards by January 1, 2019. Management currently estimates that remaining remediation costs required for meeting the standards is approximately \$13,200 based on third party estimates.

Seton Medical Center Main Tower and Seton Medical Center Front Wing must meet SP-2 standards by July 1, 2019. Management currently estimates that remaining remediation costs required for meeting the standards is approximately \$40,300 based on third party estimates. Seton seismic work will be financed with the funds received from the C-PACE bonds (see Note 9) and grant funds received by the County of San Mateo.

13. Subsequent Events

VHS has evaluated subsequent events and disclosed all material events through November 8, 2017, which is the date these consolidated financial statements of VHS were issued.

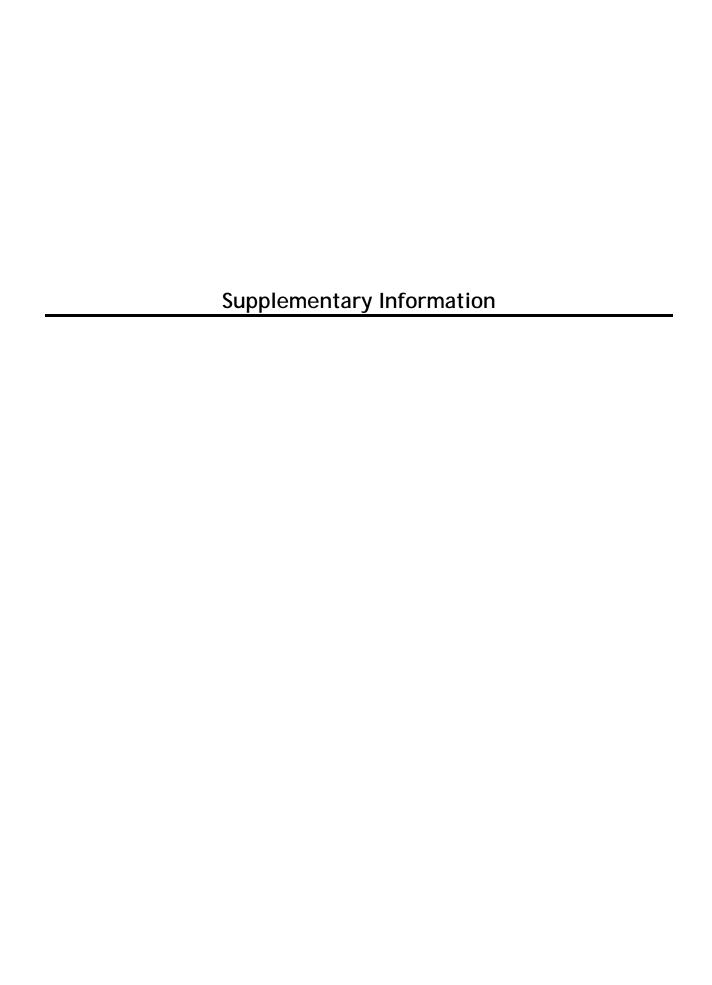
In July 2017, NantWorks LLC (NantWorks), the parent organization for health technology and biotech companies founded by Dr. Patrick Soon-Shiong, acquired a majority stake in VHS's management company, Integrity Healthcare, LLC, from Blue Mountain. There were no significant changes to the terms of the Restructuring Agreement or the California Attorney General requirements as a result of this transaction.

In August 2017, St. Vincent Medical Center Foundation received an unrestricted contribution of \$12,000 as part of a settlement.

In August 2017, VHS completed the sale of certain non-core land and real property located in Los Angeles, CA, for a total purchase price of \$17,950. The net book value of the property was classified as assets held for sale (see Note 6) at June 30, 2017, and VHS expects to recognize a gain on the sale of approximately \$15,500 in the fiscal year ending June 30, 2018.

In September 2017, the California Public Finance Authority issued \$21,000 of tax-exempt notes (the "2017 Notes") for the benefit of VHS. All of the 2017 Notes were purchased by NantWorks. The 2017 Notes are secured pursuant to a certain master trust indenture among the Obligated Group Members and U.S. Bank, National Association. The 2017 Notes bear interest at 7.25% and the principal is due at the maturity date in December 2020.

In October 2017, VHS borrowed \$46,220 (the "MOB Loan") from Verity MOB Financing, LLC. Verity MOB Financing, LLC, is wholly owned by NantWorks. The MOB Loan is secured by Deeds of Trust against four medical office buildings owned by Verity Holdings, LLC. The MOB Loan bears interest at a variable rate that adjusts monthly based on One Month Libor plus a spread and the MOB Loan is interest only for the initial term of 36 months. Principal and any unpaid interest is due at the end of the initial term unless extended. After the initial term, VHS has the option to extend the MOB Loan for two additional twelve month terms.



Consolidating Balance Sheet As of June 30, 2017 (In Thousands)

								O'Connor Hospital		Seton ledical Center	M C	Seton ledical center astside	ı	. Francis Medical Center	R	Saint Louise legional lospital	N	t. Vincent Medical System Center Office			Eliminations		bligated Group Subtotal
Assets																							
Current Assets:																							
Cash and cash equivalents	\$	6,796	\$	7,982	\$	164	\$	27,888	\$	3,500	\$	3,504	\$	263	\$	-	\$ 50,097						
Patient accounts receivable, net	4	44,085		36,629		3,912		87,216		12,937		45,862		-		-	230,641						
Due from government agencies		1,788		3,085		-		5,528		-		5,537		-		-	15,938						
Due from related organizations		8,366		24,828		46		316,476		5,556		17,611	35	51,576	(6	79,951)	44,508						
Other current assets		11,921		7,456		378		36,589		4,548		13,334		5,742		-	79,968						
Total current assets	-	72,956		79,980		4,500		473,697		26,541		85,848	35	57,581	(6	79,951)	421,152						
Assets Limited as to Use:																							
Other investments		-		-		-		-		-		3,039		-		-	3,039						
Under bond indenture agreements		-		38,659		-		-		_		_	2	24,834		-	63,493						
Total assets limited as to use		-		38,659		-		-		-		3,039	2	24,834		-	66,532						
Property and equipment, net	3	30,884		35,311		495		94,973		12,866		45,086		1,921		-	221,536						
Other long-term assets		306		460		3		98		7		13		3,675		-	4,562						
Total Assets	\$ 10	04,146	\$	154,410	\$	4,998	\$	568,768	\$	39,414	\$	133,986	\$ 38	88,011	\$ (6	79,951)	\$ 713,782						

Consolidating Balance Sheet (continued) As of June 30, 2017 (In Thousands)

	Obligated Group Subtotal	Insurance		Verity Medical Foundation		Verity Business Services				All Other Entities		Elimination		VHS Total
Assets														
Current Assets:														
Cash and cash equivalents	\$ 50,097	\$	904	\$	1,767	\$	104	\$	2,735	\$	5,040	\$	_	\$ 60,647
Patient accounts receivable	230,641		-		4,252		-		-		874		-	235,767
Due from government agencies	15,938		-		-		-		-		-		-	15,938
Due from related organizations	44,508		-		104		13,458		5,446		1,312		(64,828)	-
Other current assets	79,968	6	567		2,883		410		3,453		7,765		(5,854)	95,192
Total current assets	421,152	7	471		9,006		13,972		11,634		14,991		(70,682)	407,544
Assets Limited as to Use:														
Other investments	3,039	45	033		-		_		590		12,519		_	61,181
Under bond indenture agreements	63,493		-		-		=		-		-		-	63,493
Total assets limited as to use	66,532	45	033		-		-		590		12,519		-	124,674
Property and equipment, net	221,536		_		2,154		233		22,875		244		_	247,042
Other long-term assets	4,562		-		1,559		4		18,229		987		(256)	25,085
Total Assets	\$ 713,782	\$ 52	504	\$ 1	2,719	\$	14,209	\$	53,328	\$	28,741	\$	(70,938)	\$ 804,345

Consolidating Balance Sheet (continued) As of June 30, 2017 (In Thousands)

	O'Connor Hospital	Seton Medical Center	Seton Medical Center Coastside	N	. Francis Medical Center	Re	t Louise gional ospital	St. Vincent Medical Center	System Office	Eliminations	Obligated Group Subtotal
Liabilities and Net (Deficit) Assets											
Current Liabilities:											
Accounts payable	\$ 12,387	\$ 8,901	\$ 127	\$	11,335	\$	2,621	\$ 13,854	\$ 22,122	\$ -	\$ 71,347
Accrued expenses and other current liabilities	19,512	52,802	1,861		68,202		5,964	22,347	64,858	-	235,546
Current portion of long-term debt, net of debt											
issuance costs	744	912	-		3,800		451	833	(150)	-	6,590
Due to government agencies	975	254	-		2,529		27	1,514	-	-	5,299
Due to related organizations	220,496	116,532	19,235		1,315		66,325	216,877	59,193	(679,951)	20,022
Total current liabilities	254,114	179,401	21,223		87,181		75,388	255,425	146,023	(679,951)	338,804
Pension obligations	53,037	27	27		103,787		6,442	71,180	17,972	1,530	254,002
Long-term portion of workers' compensation and											
hospital professional and general liability	-	-	-		_		-	-	5,404	-	5,404
Other long-term liabilities	192	2,932	-		183		-	2,341	27,559	-	33,207
Long-term debt - net of current portion and debt											
issuance costs	48,410	98,002	-		68,184		29,323	54,192	161,045	-	459,156
Total liabilities	355,753	280,362	21,250		259,335		111,153	383,138	358,003	(678,421)	1,090,573
Net (Deficit) Assets:											
Unrestricted - Verity Health System	(251,607)	(125,952)	(16,252)	١	309,381		(71,739)	(252,418)	30,008	(1,530)	(380,109)
Unrestricted - Noncontrolling	-	-	-		-		-	-	-	-	-
Temporarily restricted	-	-	-		52		-	523	-	-	575
Permanently restricted	-	-	-		-		-	2,743	-	-	2,743
Total net (deficit) assets	(251,607)	(125,952)	(16,252)		309,433		(71,739)	(249,152)	30,008	(1,530)	(376,791)
Total Liabilities and Net (Deficit) Assets	\$ 104,146	\$ 154,410	\$ 4,998	\$	568,768	\$	39,414	\$ 133,986	\$ 388,011	\$ (679,951)	\$ 713,782

Consolidating Balance Sheet (continued) As of June 30, 2017 (In Thousands)

	Obligated Group Subtotal	Marillac Insurance Company, Ltd.	Verity Medical Foundation	Verity Business Services	Verity Holdings, LLC	All Other Entities	Eliminations	VHS Total
Liabilities and Net (Deficit) Assets								
Current Liabilities:								
Accounts payable	\$ 71,347	\$ 35	\$ 1,420	\$ 74	\$ 1,701	\$ -	\$ -	\$ 74,577
Accrued expenses and other current liabilities	235,546	14,730	7,035	1,570	574	775	(6,101)	254,129
Current portion of long-term debt, net of								
debt issuance costs	6,590	-	750	-	5,140	_	-	12,480
Due to government agencies	5,299	-	-	-	-	-	-	5,299
Due to related organizations	20,022	-	126	10,441	499	33,740	(64,828)	-
Total current liabilities	338,804	14,765	9,331	12,085	7,914	34,515	(70,929)	346,485
Pension obligations	254,002	-	-	-	-	-	-	254,002
Long-term portion of workers' compensation and								
hospital professional and general liability	5,404	30,738	-	-	-	-	-	36,142
Other long-term liabilities	33,207	-	-	-	9,308	186	(9)	42,692
Long-term debt - net of current portion and								
debt issuance costs	459,156	-	-	-	-	-	-	459,156
Total liabilities	1,090,573	45,503	9,331	12,085	17,222	34,701	(70,938)	1,138,477
Net (Deficit) Assets:								
Unrestricted - Verity Health System	(380,109	7,001	3,388	2,124	33,740	(24,288)	-	(358,144)
Unrestricted - Noncontrolling	-	-	-	-	2,366	-	-	2,366
Temporarily restricted	575	-	-	-	-	12,869	-	13,444
Permanently restricted	2,743	-		-	-	5,459	-	8,202
Total net (deficit) assets	(376,791	7,001	3,388	2,124	36,106	(5,960)	-	(334,132)
Total Liabilities and Net (Deficit) Assets	\$ 713,782	\$ 52,504	\$ 12,719	\$ 14,209	\$ 53,328	\$ 28,741	\$ (70,938)	\$ 804,345

Consolidating Statement of Operations For the Year Ended June 30, 2017 (In Thousands)

	O'Connor Hospital	Seton Medical Center	Seton Medical Center Coastside	St. Francis Medical Center	Saint Louise Regional Hospital	St. Vincent Medical Center	System Office	Eliminations	Obligated Group Subtotal
Unrestricted Revenues and Other Support:									
Net patient service revenue	\$ 270,032	\$ 230,312	\$ 21,866	\$ 443,825	\$ 88,164	\$ 215,368	\$ -	\$ -	\$ 1,269,567
Provision for doubtful accounts	(6,847)	(3,212)	(314)	(12,742)	(3,099)	(7,104)	-	-	(33,318)
Net patient service revenue less									
provision for doubtful accounts	263,185	227,100	21,552	431,083	85,065	208,264	-	-	1,236,249
Premium revenue	326	-	-	80,039	-	18,312	-	(70)	98,607
Other operating revenue	4,074	3,458	574	1,985	106	1,963	181,675	(181,188)	12,647
Contributions	423	223	-	2,755	51	1,218	-	(382)	4,288
Total unrestricted revenues and other support	268,008	230,781	22,126	515,862	85,222	229,757	181,675	(181,640)	1,351,791
Expenses:									
Salaries and benefits	165,924	136,212	15,951	200,689	51,128	105,754	27,488	-	703,146
Purchased services and other	96,640	82,303	4,132	147,515	30,506	99,643	144,911	(181,188)	424,462
Supplies	40,741	31,451	1,935	38,617	6,457	48,264	(945)	-	166,520
Medical claims	248	-	-	45,508	-	9,848	-	(70)	55,534
Depreciation and amortization	7,992	6,019	161	10,048	1,701	6,037	165	-	32,123
Interest - net	2,821	3,440	(5)	4,284	1,667	3,075	12,359	-	27,641
Goodwill and intangible asset impairment loss	-	-	-	-	-	-	-	-	-
Total expenses	314,366	259,425	22,174	446,661	91,459	272,621	183,978	(181,258)	1,409,426
Operating (loss) income	(46,358)	(28,644)	(48)	69,201	(6,237)	(42,864)	(2,303)	(382)	(57,635)
Investment (loss) income	-	-	-	-	-	-	2,303	-	2,303
(Deficit) excess of revenues over expenses	(46,358)	(28,644)	(48)	69,201	(6,237)	(42,864)	-	(382)	(55,332)
Less (deficit) excess of revenues over expenses attributable to noncontrolling interest	-	-	-	-	-	-	-	-	-
(Deficit) excess of revenues over expenses, net of noncontrolling interest	\$ (46,358)	\$ (28,644)	\$ (48)	\$ 69,201	\$ (6,237)	\$ (42,864)	\$ -	\$ (382)	\$ (55,332)

Consolidating Statement of Operations For the Year Ended June 30, 2017 (In Thousands)

	O'Connor Hospital	Seton Medical Center	Seton Medical Center Coastside	St. Francis Medical Center	Saint Louise Regional Hospital	St. Vincent Medical Center	System Office	Eliminations	Obligated Group Subtotal
Unrestricted Net (Deficit) Assets attributable to Verity Health System: (Deficit) excess of revenues over expenses									
attributable to Verity Health System	\$ (46,358)	\$ (28,644)	\$ (48)	\$ 69,201	\$ (6,237)	\$ (42,864)	\$ -	\$ (382)	\$ (55,332)
Change in funded status of pension and other postretirement benefit plans Net assets released from restrictions used for	(3,461)	(4,800)	(306)	3,833	(1,892)	15,319	504	(1,530)	7,667
purchase of property and equipment	113	63	-	-	327	107	-	-	610
Other	1,829	1,138	-	(741)	(281)	3,776	20,109	382	26,212
Decrease in unrestricted net (deficit) assets attributable to Verity Health System	(47,877)	(32,243)	(354)	72,293	(8,083)	(23,662)	20,613	(1,530)	(20,843)
Unrestricted Net Assets attributable to Noncontrolling Interests:									
(Deficit) excess of revenues over expenses attributable to noncontrolling interests	-	-	-	-	-	-	-	-	-
Noncontrolling interest related to acquisitions and other		-	-	-	-	-	-	-	
Increase in unrestricted net assets attributable to noncontrolling interest	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

Consolidating Statement of Operations (continued) For the Year Ended June 30, 2017 (In Thousands)

	Obligated Group Subtotal	Marillac Insurance Company, Ltd.	Verity Medical Foundation	Verity Business Services	Verity Holdings, LLC	All Other Entities	Eliminations	VHS Total
Unrestricted Revenues and Other Support:								
Net patient service revenue	\$ 1,269,567	\$ -	\$ 26,834	\$ -	\$ -	\$ 4,604	\$ -	\$ 1,301,005
Provision for doubtful accounts	(33,318)	-	(366)	-	-	(86)	-	(33,770)
Net patient service revenue less								
provision for doubtful accounts	1,236,249	-	26,468	-	-	4,518	-	1,267,235
Premium revenue	98,607	-	21,686	-	-	-	-	120,293
Other operating revenue	12,647	12,636	2,703	13,245	16,710	-	(31,637)	26,304
Contributions	4,288	-	-	-	60,368	1,061	-	65,717
Total unrestricted revenues and other support	1,351,791	12,636	50,857	13,245	77,078	5,579	(31,637)	1,479,549
Expenses:								
Salaries and benefits	703,146	-	22,282	9,590	166	3,537	(8,422)	730,299
Purchased services and other	424,462	14,468	44,585	3,424	11,667	1,501	(23,215)	476,892
Supplies	166,520	-	4,424	135	75	1,238	-	172,392
Medical claims	55,534	-	6,425	-	-	-	-	61,959
Depreciation and amortization	32,123	-	821	96	1,848	30	-	34,918
Interest - net	27,641	-	41	-	452	-	-	28,134
Goodwill and intangible asset impairment loss	-	-	-	-	10232	-	-	10,232
Total expenses	1,409,426	14,468	78,578	13,245	24,440	6,306	(31,637)	1,514,826
Operating (loss) income	(57,635)	(1,832)	(27,721)	-	52,638	(727)	-	(35,277)
Investment (loss) income	2,303	11			(6,815)	1,928	-	(2,573)
(Deficit) excess of revenues over expenses	(55,332)	(1,821)	(27,721)	-	45,823	1,201	-	(37,850)
Less (deficit) excess of revenues over expenses attributable to noncontrolling interest	-			-	(5,087)		-	(5,087)
(Deficit) excess of revenues over expenses, net of noncontrolling interest	\$ (55,332)	\$ (1,821)	\$ (27,721)	\$ -	\$ 50,910	\$ 1,201	\$ -	\$ (32,763)

Consolidating Statement of Operations (continued) For the Year Ended June 30, 2017 (In Thousands)

		bligated Group Subtotal	Ins	arillac surance pany, Ltd.	ı	Verity Medical oundation	В	Verity Business Services	Но	Verity Idings, LLC	All Other Entities	Elimina	tions	\$ VHS Total
Unrestricted Net (Deficit) Assets attributable to	Verit	y Health S	ystem	:										
(Deficit) excess of revenues over expenses														
attributable to Verity Health System	\$	(55,332)	\$	(1,821)	\$	(27,721)	\$	-	\$	50,910	\$ 1,201	\$	-	\$ (32,763)
Change in funded status of pension and other														
postretirement benefit plans		7,667		-		-		-		-	-		-	7,667
Net assets released from restrictions used for														
purchase of property and equipment		610		-		-		-		-	-		-	610
Other		26,212		-		26,712		-		(51,192)	(1,395)		-	337
Decrease in unrestricted net (deficit) assets														
attributable to Verity Health System	\$	(20,843)	\$	(1,821)	\$	(1,009)	\$	-	\$	(282)	\$ (194)	\$	-	\$ (24,149)
Unrestricted Net Assets attributable to Noncontrolling Interests:														
(Deficit) excess of revenues over expenses														
attributable to noncontrolling interests		-		-		-		-		(5,087)	-		-	(5,087)
Noncontrolling interest related to acquisitions														
and other		-		-		-		-		7,453	-		-	7,453
Increase in unrestricted net assets attributable			•					•						
to noncontrolling interest	\$	-	\$	-	\$	-	\$	-	\$	2,366	\$ -	\$	-	\$ 2,366